City of Pontiac General Employees' Retirement System

Financial Report
with Supplemental Information
December 31, 2013

Contents

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Independent Auditor's Report

To the Retirement Board
City of Pontiac General Employees'
Retirement System

We have audited the accompanying statement of plan net position and the related statement of changes in plan net position of the City of Pontiac General Employees' Retirement System (the "System"), a component unit of the City of Pontiac, Michigan, as of and for the year ended December 31, 2013 and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Praxity MEMBER
GLOBAL ALLIANCE OF INDEPENDENT FIRMS

To the Retirement Board
City of Pontiac General Employees'
Retirement System

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net position of the City of Pontiac General Employees' Retirement System as of December 31, 2013 and the changes in plan net position thereof for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplemental Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, and pension system schedules of funding progress and employer contributions, as identified in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplemental information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Plante & Moran, PLLC

June 19, 2014

Using this Annual Report

This annual report consists of three parts: (1) management's discussion and analysis (this section), (2) the basic financial statements, and (3) required supplemental information. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The financial statements are followed by a section of required supplemental information that further explains and supports the information in the financial statements.

Condensed Financial Information

The table below compares key financial information in a condensed format between the current year and the prior year:

	2013	2012
Total assets	$ 491,518,785	$ 424,262,955
Total liabilities	1,045,898	734,166
Net position held in trust for pension benefits	**$ 490,472,887**	**$ 423,528,789**
Net investment income	$ 91,786,846	$ 50,201,824
Net securities lending loss	-	(16,028)
Other - Miscellaneous and litigation revenue	25,795	23,792
Retiree pension and annuity benefits	(23,946,914)	(21,497,123)
General and administrative expenses	(921,629)	(483,269)
Net increase in net position held in trust	**$ 66,944,098**	**$ 28,229,196**

Overall Fund Structure and Objectives

The City of Pontiac General Employees' Retirement System (the "System") exists to pay benefits to its members and retirees. Active members earn service credit that entitles them to receive benefits in the future. Benefits currently being paid are significantly greater than contributions currently being received. The excess of benefits over contributions must be funded through investment income. The public capital markets represent the primary source of investments.

Asset Allocation

The System has established asset allocation policies that are expected to deliver sufficient investment income over a very long period of time to satisfy the obligations to pay the benefits promised to the members of the System. The following is a summary of the adopted asset allocation (excluding the collateral pool) as of December 31, 2013:

Domestic equities	55%
Domestic fixed income	20%
International equities	15%
Basket Clause Category Securities	10%
Cash	0%

Investment Results

In 2012, the U.S. Federal Reserve introduced Quantitative Easing III. This intervention by the central bank provided stability to the capital markets and investors with confidence. Core inflation in the U.S. continued to be below the long-term target at 1.7 percent. The Fed announced on December 18 that they would begin to "taper" their program of quantitative easing in the first quarter of 2014, causing all rates to rise with a full basis point increase for maturities greater than five years. The fixed-income market posted a loss for the year; the Barclay's U.S. Aggregate Index returned (2.02) percent for the year. The Standard & Poor's 500 returned 32.41 percent and the MSCI EAFE Index (a proxy for international stocks) returned 22.8 percent. The total plan returned 22.57 percent for the year.

The total System's return must always be considered in a longer-term context. The fund's investment horizon is long-term, corresponding to the long-term nature of the System's liabilities. Therefore, the board of trustees establishes an asset allocation policy to control risks and generate expected returns that will enable the System to pay the benefits promised to members and retirees. Accordingly, the board of trustees must make investment decisions that it believes will be the most beneficial to the System over many years, not just one or two years.

Plan Sponsor Financial Condition/Plan Update

The City of Pontiac (the plan sponsor) is experiencing significant financial difficulty. The City was placed in receivership under Michigan Public Act 436 of 2012. The receivership ended in mid-2013 and an Administrator (overseen by the Transition Advisory Board) was appointed to supervise the City until such time as fiscal authority is returned to the City's elected officials. The effects of the 2013 Mayoral and Council elections on the City's finances should be minimal as a result. The System is currently overfunded and no employer contributions are required at this time. Should a contribution be required in the future, there is uncertainty regarding the City's ability and intent to make contributions to the System.

Contacting the System's Management

This financial report is intended to provide a general overview of the System's finances and investment results in relation to actuarial projections. It shows the System's accountability for the money it receives from employer and employee contributions. If you have questions about this report or need additional information, we welcome you to contact the System's office.

Statement of Plan Net Position
December 31, 2013

Assets	
Cash and cash equivalents (Note 4)	$ 5,218
Investments at fair value (Note 4):	
Money market fund	27,279,777
Government agency notes and debentures	11,845,369
Corporate and other bonds	24,113,642
Equities	315,461,261
Private equity	10,985,579
U.S. government mortgage-backed securities	25,887,608
High-yield bonds	20,922,013
Commercial mortgage pools	6,358,096
Asset-backed securities	9,088,021
Limited partnerships	38,336,949
Receivables:	
Accrued interest receivable	1,231,940
Other receivables	3,312
Total assets	491,518,785
Liabilities - Accounts payable and other	1,045,898
Net Position - Held in trust for pension and other employee benefits	**$ 490,472,887**

The Notes to Financial Statements are an Integral Part of this Statement.

City of Pontiac General Employees' Retirement System

Statement of Changes in Plan Net Position
Year Ended December 31, 2013

Additions	
Investment income:	
Interest and dividends	$ 9,168,565
Net increase in fair value of investments	85,344,964
Less investment advisor fees	(2,726,683)
Net investment income	91,786,846
Miscellaneous and litigation income	25,795
Total additions	91,812,641
Deductions	
Retirees' pension benefits	23,946,914
Administrative expenses	921,629
Total deductions	24,868,543
Net Increase in Net Position Held in Trust	66,944,098
Net Position Held in Trust - Beginning of year	423,528,789
Net Increase in Net Position Held in Trust - End of year	**$ 490,472,887**

The Notes to Financial Statements are an
Integral Part of this Statement.

Note 1 - Summary of Significant Accounting Policies

The City of Pontiac (the "City") sponsors and administers the City of Pontiac General Employees' Retirement System (the "System") (a contributory single-employer retirement plan) that covers substantially all employees of the City, except police and fire employees.

Reporting Entity - The financial statements of the System are also included in the combined financial statements of the City as a pension trust fund. The assets of the pension trust fund include no securities of or loans to the City or any other related party.

Plan Sponsor Financial Condition - The City of Pontiac (the plan sponsor) is experiencing significant financial difficulty. In early 2013, the City was in receivership under Michigan Public Act 436 of 2012. The result was that the State had appointed an Emergency Manager to control the finances of the City. As of the end of fiscal year 2013, the City is no longer under receivership and is now governed by a Transitionary Advisory Board. The System is currently overfunded and no employer contributions are required at this time. Should a contribution be required in the future, there is uncertainty regarding the City's ability and intent to make contributions to the System.

Basis of Accounting - The System's financial statements are prepared using the accrual basis of accounting. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the System.

Methods Used to Value Investments - Investments are reported at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal and interest payments and are discounted at prevailing interest rates for similar instruments. The fair value of real estate investments is based on independent appraisals or audited financial statements. Investments that do not have an established market value are reported at estimated fair value as determined by the System's management. These estimates are determined using financial statements issued by the private equity companies or limited partnerships in which such investments are held, adjusted by management as deemed appropriate based on known circumstances. Approximately 10 percent of the System's assets are not publicly traded, and therefore do not have a readily determinable market value. Because these alternative investments are not readily marketable, their estimated value is subject to uncertainty, and therefore may differ significantly from the values that would have been used had a ready market for these securities existed. The difference could be material.

Note 2 - Membership Information

At December 31, 2012, the date of the most recent actuarial valuation, membership consisted of the following:

Retirees and beneficiaries currently receiving pension benefits	1,121
Terminated employees entitled to benefits but not yet receiving them	277
Current employees:	
Fully vested	41
Nonvested	16
Total current employees	57

Note 3 - Plan Description and Contribution Information

Plan Description - The System provides retirement benefits, as well as death and disability benefits. Employees may receive cost of living adjustments as a percentage of their base amounts, pursuant to the collective bargaining agreement in effect at their date of retirement. The obligation to contribute to and maintain the System was established by City ordinance and negotiation with the employees' collective bargaining units.

Contributions - Plan members are not required to contribute. The City is required to contribute at an actuarially determined rate. In accordance with the actuary recommendation, the City did not make a contribution to the System in the current year. Administrative costs are financed through investment earnings.

Annual Pension Cost - The annual contribution for the year ended December 31, 2013 was $0. The annual contribution for the plan year was determined as part of actuarial valuations at December 31, 2010 and December 31, 2011 using the entry age actuarial cost method. Significant actuarial assumptions used include (a) a 7.5 percent investment rate of return, (b) projected salary increases of 5.6 - 9.4 percent per year, (c) projected salary increases in (b) include increases of 1.1 percent to 4.9 percent per year based on merit and/or longevity, (d) cost of living adjustments ranging from 2.0 percent to 2.5 percent per year, and (e) inflation of 4.5 percent. Both (a) and (b) are determined by using techniques that smooth the effects of short-term volatility over a five-year period. The unfunded actuarial liability is being amortized as a level of percent of payroll on an open basis. The remaining amortization period is 30 years.

Per the actuarial report dated December 31, 2012, all assumptions have remained consistent.

Note 3 - Plan Description and Contribution Information (Continued)

Funded Status and Funding Progress - As of December 31, 2012, the most recent actuarial valuation date, the System was 149.1 percent funded. The actuarial accrued liability for benefits was $247,968,743 and the actuarial value of assets was $369,621,671, resulting in overfunded actuarial accrued liabilities of $121,652,928. The covered payroll (annual payroll for active employees covered by the System) was $2,742,912 and the ratio for the unfunded AAL to the covered payroll was 0 percent given the funded status.

The schedule of funding progress, presented as required supplemental information following the notes to the financial statements, presents multi-year trend information about whether the actuarial values of plan net assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Three-year trend information as of December 31 is as follows:

	Fiscal Year Ended December 31		
	2010	2012	2012
Annual pension cost (APC)	$ -	$ -	$ -
Percentage of APC contributed	100.0 %	100.0 %	100.0 %
Net pension obligation	-	-	-

Reserves - State law requires employee contributions to be segregated. In addition, amounts must be set aside as determined by the actuary to fund benefits to retirees currently approved to receive benefits. As of December 31, 2013, the System's reserves have been fully funded as follows:

Reserve for employees' contributions	$ 1,316,936
Reserve for retired employees	211,570,137

Note 4 - Deposits and Investments

Michigan Compiled Laws Section 129.91 (Public Act 20 of 1943, as amended) authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The System is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated within the two highest classifications, which matures not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions, which are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

Note 4 - Deposits and Investments (Continued)

The System is also authorized by Michigan Public Act 347 of 2012, as amended, to invest in certain reverse repurchase agreements, stocks, diversified investment companies, annuity investment contracts, real estate leased to public entities, mortgages, real estate (if the System's assets exceed $250 million), debt or equity of certain small businesses, certain state and local government obligations, and certain other specified investment vehicles.

The System has designated one bank for the deposit of its funds. The investment policy adopted by the board in accordance with Public Act 196 of 1997 has authorized investment in all allowable investments under Michigan Public Act 347 of 2012, as amended. The System's deposits and investment policies are in accordance with statutory authority.

The System's cash and investments are subject to several types of risk, which are examined in more detail below:

Custodial Credit Risk of Bank Deposits - Custodial credit risk is the risk that in the event of a bank failure, the System's deposits may not be returned to it. The System does not have a deposit policy for custodial credit risk. At year end, the System had no bank deposits (certificates of deposit, checking, and savings accounts) that were uninsured and uncollateralized. The System continues to evaluate each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Interest Rate Risk - Interest rate risk is the risk that the value of investments will decrease as a result of a rise in interest rates. The System's investment policy does not restrict investment maturities.

At year end, the average maturities of investments are as follows:

Investment	Fair Value	Effective Duration
Asset-backed securities	$ 9,088,021	1.91 years
Commercial mortgage pools	6,358,096	2.6 years
Corporate and other bonds	45,035,655	4.44 years
Government agency notes and debentures	11,845,366	21.54 years
U.S. governmental issued commercial mortgage-backed securities	345,916	2.16 years
U.S. governmental mortgage-backed securities	25,541,692	3.93 years
Nongovernment-backed CMOs	147,134	1.26 years
Short-term investment funds	24,873,751	Unavailable

Note 4 - Deposits and Investments (Continued)

Credit Risk - State law limits investments in commercial paper to the top two ratings issued by nationally recognized statistical rating organizations. The System's investment policy limits investments in domestic fixed-income securities to not less than a CCC rating for an overall average quality of each high-yield portfolio; the overall quality rating of each high-grade portfolio must be AA or an equivalent rating; for domestic equity investments, the securities must be the equivalent of Standard & Poor's A1 or Moody's P-1. As of year end, the credit quality ratings of debt securities are as follows:

Investment	Fair Value	Moody's
Asset-backed securities	$ 3,087,761	Aaa
Asset-backed securities	1,376,533	Aa
Asset-backed securities	585,364	A
Asset-backed securities	4,038,363	Unrated
Commercial mortgage-backed securities	5,050,898	Aaa
Commercial mortgage-backed securities	585,434	Aa
Commercial mortgage-backed securities	186,839	Baa
Commercial mortgage-backed securities	534,925	Unrated
Corporate bonds	1,388,515	Aa
Corporate bonds	7,143,967	A
Corporate bonds	15,198,227	Baa
Corporate bonds	753,775	Ba
Corporate bonds	10,795,303	B
Corporate bonds	8,981,838	Caa
Corporate bonds	774,032	Unrated
Government agency notes and debentures	9,571,014	Aaa
Government agency notes and debentures	2,274,356	Aa
U.S. governmental agency mortgage-backed securities	29,951	Unrated
Nongovernment-backed CMOs	12,973	A
Nongovernment-backed CMOs	134,161	Unrated
Short-term investment funds	24,873,751	Unrated

Foreign Currency Risk - Foreign currency risk is the risk that an investment denominated in the currency of a foreign country could reduce its U.S. dollar value, as a result of changes in foreign currency exchange rates. The pension system restricts the amount of investments in foreign currency-denominated investments to 15 percent of total pension system investments. At year end December 31, 2013, the only type of investments which were subject to foreign currency risk were equity investments. The total amount of equity investments which were subject to foreign currency risk at year end was $17,586,715. At year end, the City of Pontiac General Employees' Retirement System had a total foreign currency translation gain of $214,179 related to equity investments.

Note 5 - Upcoming Accounting Pronouncements

In June 2012, GASB Statement No. 67, *Financial Reporting for Pension Plans*, was issued by the Governmental Accounting Standards Board. This new standard, which replaces the requirements of GASB Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans,* and No. 50, *Pension Disclosures*, establishes standards for financial reporting that outline the basic framework for separately issued pension plan financial reports and specifies the required approach to measuring the liability of employer(s) and certain nonemployer contributing entities, about which information is required to be disclosed. GASB Statement No. 67 is required to be adopted for years beginning after June 15, 2013. For the City of Pontiac General Employees' Retirement System, this standard will be adopted for the year ending December 31, 2014.

In April 2013, the Governmental Accounting Standards Board issued GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*. The requirements of this statement will enhance comparability of financial statements among governments by requiring consistent reporting by those governments that extend nonexchange financial guarantees and by those governments that receive nonexchange financial guarantees. This statement also will enhance the information disclosed about a government's obligations and risk exposure from extending nonexchange financial guarantees. This statement also will augment the ability of financial statement users to assess the probability that governments will repay obligation holders by requiring disclosures about obligations that are issued with this type of financial guarantee. GASB Statement No. 70 is required to be adopted for years beginning after June 15, 2013. The City of Pontiac General Employees' Retirement System is currently evaluating the impact this standard will have on the financial statements when adopted, during the City of Pontiac General Employees' System's 2014 fiscal year.

Required Supplemental Information

Required Supplemental Information
Schedules of Funding Progress and Employer Contributions
Year Ended December 31, 2013

The schedule of funding progress is as follows:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (Percent) (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll
12/31/07	$433,028,186	$257,940,349	$ (175,087,837)	167.9	$ 13,559,473	-
12/31/08	416,678,512	261,497,756	(155,180,756)	159.3	14,414,481	-
12/31/09	405,193,572	255,720,207	(149,473,365)	158.5	12,553,146	-
12/31/10	399,573,669	253,866,554	(145,707,115)	157.4	9,493,229	-
12/31/11	383,349,729	249,739,988	(133,609,741)	153.5	3,968,743	-
12/31/12	369,621,671	247,968,743	(121,652,928)	149.1	2,742,912	-

The schedule of employer contributions is as follows:

Year Ended	Annual Required Contribution	Percentage Contributed
12/31/08	$ -	100.0
12/31/09	-	100.0
12/31/10	-	100.0
12/31/11	-	100.0
12/31/12	-	100.0
12/31/13	-	100.0
	-	100.0

The information presented above was determined as part of the actuarial valuations at the dates indicated. Additional information as of December 31, 2012, the latest actuarial valuation, follows:

Asset valuation method	Market value with five-year smoothing of gains and losses
Actuarial assumptions:	
Investment rate of return*	7.5%
Projected salary increases*	5.6% - 9.4%
Cost of living adjustments	2.0 - 2.5 percent (2.5 percent Court/MAPE) of original amount, subject to a maximum that varies by group

*Includes inflation at 4.5%

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June 19, 2014

To the Members of the Board
City of Pontiac General Employees'
Retirement System

We have audited the financial statements of the City of Pontiac General Employees' Retirement System (the "System") as of and for the year ended December 31, 2013 and have issued our report thereon dated June 19, 2014. Professional standards require that we provide you with the following information related to our audit which is divided into the following sections:

Section I - Required Communications with Those Charged with Governance

Section II - Other Recommendations and Related Information

Section III - Informational Item

Section I includes information that current auditing standards require independent auditors to communicate to those individuals charged with governance. We will report this information annually to the board of the City of Pontiac General Employees' Retirement System.

Section II presents recommendations related to internal control, procedures, and other matters noted during our current year audit. These comments are offered in the interest of helping the System in its efforts toward continuous improvement, not just in the areas of internal control and accounting procedures, but also in operational or administrative efficiency and effectiveness.

Section III contains an updated informational item that we believe will be of interest to you.

We would like to take this opportunity to thank the System's staff for the cooperation and courtesy extended to us during our audit. Their assistance and professionalism are invaluable.

This report is intended solely for the use of the board and management of the City of Pontiac General Employees' Retirement System and is not intended to be and should not be used by anyone other than these specified parties.

Praxity MEMBER
GLOBAL ALLIANCE OF INDEPENDENT FIRMS

To Members of the Board
City of Pontiac General Employees'
Retirement System

June 19, 2014

We welcome any questions you may have regarding the following communications and we would be willing to discuss any of these or other questions that you might have at your convenience.

Very truly yours,

Plante & Moran, PLLC

Beth Bialy

Beth Bialy

Manju P

Manju Patnaik

To Members of the Board
City of Pontiac General Employees'
Retirement System

June 19, 2014

Section I - Required Communications with Those Charged with Governance

<u>Our Responsibility Under U.S. Generally Accepted Auditing Standards</u>

As stated in our engagement letter dated February 27, 2014, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities. Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

As part of our audit, we considered the internal control of the City of Pontiac General Employees' Retirement System. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

<u>Planned Scope and Timing of the Audit</u>

We performed the audit according to the planned scope and timing previously communicated to you in our letter about planning matters dated March 6, 2014.

<u>Significant Audit Findings</u>

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the City of Pontiac General Employees' Retirement System are described in Note 1 to the financial statements.

No new accounting policies were adopted and the application of existing policies was not changed during 2013.

We noted no transactions entered into by the System during the year for which there is a lack of authoritative guidance or consensus.

There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected.

The most sensitive estimates affecting the financial statements relate to the following:

- The valuation of alternative investments constitutes a sensitive estimate affecting the financial statements. The valuation for certain alternative investments is based on audited financial statements or other valuation methods in use by the board.

- Significant estimates also result from the selection of certain assumptions used in the actuarial valuation, which would have an impact on the actuarial accrued liability and resulting funded position.

We evaluated the key factors and assumptions used to develop these estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

The disclosures in the financial statements are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Disagreements with Management

For the purpose of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

We did not detect any misstatements as a result of audit procedures.

Significant Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the System, and business plans and strategies that may affect the risks of material misstatement with management each year prior to retention as the System's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition of our retention.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated June 19, 2014.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the System's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Section II - Other Recommendations and Related Information

During our audit, we noted areas where we believe there are opportunities for the System to further strengthen internal control or to increase operating efficiencies. Our observations on those areas are presented for your consideration below:

Compliance with Investment Policy

During the year, we noted that certain investments were over the 5 percent threshold indicated in the System's investment policy. Typically, market value fluctuations impact the holdings mix. The System meets twice a year to monitor the limits and attempts to meet policy requirements during these meetings. The System should continue to ensure that the overall allocation of investments complies with the System's investment policy.

Segregation of Duties

Subsequent to year end, there have been some changes in staffing and resulting duties. The System management was very pro-active in assessing the internal control implications of the staffing changes. As the year unfolds, we encourage the System to continue evaluating existing controls and processes to ensure proper segregation of duties in view of the current staffing mix.

Section III - Informational Item

New Pension Standards

Beginning with the System's December 31, 2014 year end, GASB Statement No. 67, *Financial Reporting for Pension Plans,* will be effective. GASB Statement No. 68, *Accounting and Financial Reporting for Pensions,* will be effective for the City for their year ending June 30, 2015. These new pronouncements significantly revise the current accounting and reporting requirements for pensions, both from an employer perspective as well as from a plan perspective. As noted, GASB No. 67 will significantly impact the financial statements of the System, whereas GASB No. 68 will impact the City's reporting.

Employers providing defined benefit pensions to its employees must now recognize their unfunded pension benefit obligation as a liability for the first time, and must more comprehensively and comparably measure the annual costs of pension benefits. The Statements also enhance accountability and transparency through revised and expanded note disclosures and required supplementary information (RSI).

Significant coordination between the System, the actuary, and Plante & Moran, PLLC will be required in order to implement these pronouncements effectively. Statement No. 67 is required to be adopted for the System's December 31, 2014 year end. We are happy to work with the System over the next two years to ensure smooth implementation of the new standard. We would also encourage System personnel to view the free webinars available on Plante & Moran, PLLC's website, if you have not already done so.