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City of Detroit Police and Fire  
Retiree Health Care Trust

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**Financial Report  
with Supplemental Information  
December 31, 2018**

# City of Detroit Police and Fire Retiree Health Care Trust

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## **Independent Auditor's Report**

To the Board of Trustees  
City of Detroit Police and Fire Retiree Health Care Trust

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the City of Detroit Police and Fire Retiree Health Care Trust (the "Trust") as of and for the year ended December 31, 2018 and the related notes to the financial statements, which collectively comprise the Trust's basic financial statements, as listed in the table of contents.

#### ***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.

#### ***Opinion***

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the City of Detroit Police and Fire Retiree Health Care Trust as of December 31, 2018 and the changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

#### ***Emphasis of Matter***

As explained in Note 1, the financial statements include investments valued at \$202,748,249 (90.52 percent of net position) at December 31, 2018, whose fair values have been estimated by management in the absence of readily determinable market values. Management's estimates are based on information provided by investment managers and other pricing services. Our opinion is not modified with respect to this matter.

To the Board of Trustees  
City of Detroit Police and Fire Retiree Health Care Trust

***Required Supplemental Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and schedule of changes in the net OPEB liability and related ratios 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.

Management has omitted the schedule of OPEB investment returns that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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. Our opinion on the basic financial statements is not affected by this missing information.

*Plante & Moran, PLLC*

August 26, 2019

# City of Detroit Police and Fire Retiree Health Care Trust

## Management's Discussion and Analysis

### 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.

### Overall Fund Structure and Objectives

The City of Detroit Police and Fire Retiree Health Care Trust (the "Trust") was established on December 10, 2014 (the "Effective Date") under the Plan for the Adjustment of Debts of the City of Detroit (the "Plan of Adjustment") in the matter titled, *In re: City of Detroit, Michigan, Debtor, Chapter 9, Case No. 13-53846*, in the United States Bankruptcy Court for the Eastern District of Michigan. The Trust is newly created as a result of the settlement of certain legal claims made pertinent to that litigation and is established to provide health benefits to existing City of Detroit, Michigan retirees and certain dependents. The Trust is established as a governmental Voluntary Employees Beneficiary Association (VEBA) pursuant to Section 501(c)(9) of the Internal Revenue Code.

The City of Detroit Police and Fire Retiree Health Care Trust is responsible for providing benefits for the welfare of certain police and fire retirees of the City of Detroit, Michigan (the "City"), along with their eligible spouses and dependents, with an effective date of retirement on or before December 31, 2014, and who were eligible to receive retiree healthcare benefits from the City at the time of retirement. Benefits under the Trust will be provided to retirees through the purchase of insurance coverage, or by reimbursement of eligible expenses, in accordance with the Trust and applicable state and federal laws.

### Condensed Financial Information

The table below compares key financial information in a condensed format:

	2018	2017
Total assets	\$ 224,931,671	\$ 214,239,682
Total liabilities	946,707	4,150,302
Trust net position	<u>\$ 223,984,964</u>	<u>\$ 210,089,380</u>
Net investment gain	\$ 22,243,497	\$ 116,696,256
Contributions - Foundation for Detroit's Future	43,750	43,750
Retiree health benefits paid - Net of employee contributions	(7,632,539)	(8,563,612)
General and administrative expenses	<u>(759,124)</u>	<u>(1,058,591)</u>
Net increase in trust net position	<u>\$ 13,895,584</u>	<u>\$ 107,117,803</u>

### Trust Contributions

Contributions to the Trust are established in the Plan of Adjustment and other grant agreements established out of the City's bankruptcy. The Plan of Adjustment required the City to distribute \$253,900,999 of the City's Financial Recovery Bonds, Series 2014B(1) and 2014B(2) on the Effective Date. This contribution represents a complete discharge of the City's OPEB obligation with respect to the Trust's membership, and no additional contributions from the City are required under the Plan of Adjustment. The Trust also received \$1,816,429 from the Foundation for Detroit's Future pursuant to two separate grant agreements during the period ended December 31, 2015. Contributions of \$43,750 will continue to be made annually until 2034 under a grant agreement with the Foundation for Detroit's Future (the "Foundation"). In addition, the Trust received \$3,975,000 from the City of Detroit Employee Benefits Plan during the period ended December 31, 2015, of which \$500,000 was a loan that was forgiven during the year ended December 31, 2016. Member contributions to the Trust are required based on the medical plan selected and serve to offset a portion of the monthly insurance premium paid by the Trust on a member's behalf.

## City of Detroit Police and Fire Retiree Health Care Trust

### Management's Discussion and Analysis (Continued)

#### **Retiree Health Benefits and Employee Contributions**

As of January 1, 2015, the City has no further responsibility to provide retiree health care or any other retiree welfare benefits to retirees, and such responsibility falls wholly upon the Trust. The board of trustees of the Trust (the "Board") is responsible for designing, adopting, maintaining, and administering retiree healthcare benefits for eligible retirees and beneficiaries. The Board will be under no obligation to design the retiree healthcare plan to assure that the assets of the Trust are sufficient to provide benefits to all potential participants of the plan.

The participant population of the Trust is composed of approximately 7,100 Medicare-eligible retirees and beneficiaries in receipt of one of three Medicare Advantage plans or an HRA. Optional dental and vision benefits were also offered to all eligible retirees and beneficiaries at full cost to the participant. Member contributions to the Trust in the 2018 plan year were required as follows:

Medicare Advantage Plan	Monthly Retiree Contribution One-person Coverage	Monthly Retiree Contribution Two-person Coverage
Aetna	\$29.54	\$59.08
Priority	\$27.00	\$54.00

Retiree contributions for 2018 dental and vision coverage options were as follows:

Plan	Monthly Retiree Contribution One-person Coverage	Monthly Retiree Contribution Two-person Coverage	Monthly Retiree Contribution Family Coverage
Delta Dental HP	\$35.77	\$70.82	\$119.07
Delta Dental LP	\$29.76	\$56.04	\$96.76
VSP Vision	\$13.50	\$13.50	\$13.50

#### **The City's Financial Recovery Bonds**

The B notes owned by the Trust are general unsecured obligations of the City of Detroit, Michigan, with a 30-year maturity date, paying interest at a rate of 4 percent for the first 20 years and 6 percent for years 21 through 30. Interest payments are made twice annually on April 1 and October 1. Amortization of the B notes is interest only for 10 years, with amortization in 20 equal annual installments beginning on the interest payment date nearest to the 11th anniversary from issuance. During fiscal year 2018, the Trust sold 20 million units of the B notes, receiving proceeds of \$16,210,000. Due to the City's recent exit from bankruptcy, its lack of an established credit rating, and other economic factors outside the Board's control, the new B notes owned by the Trust currently have a market value of approximately 86 percent of face value (i.e., \$202,748,249).

#### **Contacting the Trust's Management**

This financial report is intended to provide a general overview of the Trust's finances and investment results in relation to actuarial projections. It shows the Trust'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 Trust's office at 700 Tower Drive, Troy, MI 48098.

## City of Detroit Police and Fire Retiree Health Care Trust

### Statement of Fiduciary Net Position

December 31, 2018

#### Assets

Cash and cash equivalents	\$ 5,902,769
Investments: (Note 2)	
Equities	4,709,205
Bonds	211,921,570
Accrued interest receivable	2,398,127
Total assets	224,931,671

#### Liabilities - Accounts payable

946,707

#### Net Position - Held in trust for retiree health care

\$ 223,984,964

## City of Detroit Police and Fire Retiree Health Care Trust

### Statement of Changes in Fiduciary Net Position

Year Ended December 31, 2018

#### Additions

Investment income:	
Interest and dividends	\$ 9,829,689
Net increase in fair value of investments	12,456,765
Investment related expenses	<u>(42,957)</u>
Net investment income	22,243,497
Contributions - Foundation for Detroit's Future	<u>43,750</u>
Total additions	22,287,247

#### Deductions

Premium payments - Net of employee contributions (Note 1)	4,426,595
Health reimbursement account reimbursements (Note 1)	3,205,944
Administrative expenses	<u>759,124</u>
Total deductions	<u>8,391,663</u>

**Net Increase in Net Position Held in Trust** 13,895,584

**Net Position Held in Trust - Beginning of year** 210,089,380

**Net Position Held in Trust - End of year** \$ 223,984,964

December 31, 2018

### Note 1 - Significant Accounting Policies

#### ***Accounting and Reporting Principles***

The City of Detroit Police and Fire Retiree Health Care Trust follows accounting principles generally accepted in the United States of America (GAAP), as applicable to governmental units. Accounting and financial reporting pronouncements are promulgated by the Governmental Accounting Standards Board. The following is a summary of the significant accounting policies used by the Trust:

#### ***Reporting Entity***

The City of Detroit Police and Fire Retiree Health Care Trust (the "Trust") is governed by a seven-member board of trustees and, for the first four years, one additional nonvoting, ex officio member. The Trust was established under the Plan for the Adjustment of Debts of the City of Detroit (the "Plan of Adjustment") related to the City of Detroit, Michigan's (the "City") Chapter 9 bankruptcy on December 10, 2014. The Plan of Adjustment provides for the establishment of the Trust as a governmental Voluntary Employees Beneficiary Association (VEBA) pursuant to Section 501(c)(9) of the Internal Revenue Code of 1986, as amended.

The Trust is responsible for providing benefits for the welfare of certain police and fire retirees of the City of Detroit, Michigan, along with their eligible spouses and dependents, with an effective date of retirement on or before December 31, 2014, and who were eligible to receive retiree healthcare benefits from the City at the time of retirement. Benefits under the Trust will be provided to retirees through the purchase insurance coverage, or by reimbursement of eligible expenses, in accordance with the Trust and applicable state and federal laws. Benefit expense for the year ended December 31, 2018 was \$7,632,539, which is net of \$4,976,696 in employee contributions toward premiums and also net of \$778,311 expense credit resulting from the settlement of a previous premium liability.

The Trust was established on December 10, 2014 under the Plan of Adjustment, at which point the Trust was distributed approximately \$253.9 million of the City's Financial Recovery Bonds, Series 2014B(1) and 2014B(2) (the "bonds"). During fiscal year 2018, the Trust sold a portion of these bonds with a face value of \$20,000,000. As of December 31, 2018, the remaining bonds held by the Trust had a market value of \$202,748,249. These bonds represent the entire funding responsibility of the City.

The Trust will provide future benefits only to the extent that plan assets are available to pay them. The Trust is under no obligation to design the retiree healthcare benefits plan to assure that the assets of the Trust are sufficient to provide benefits to all potential participants in the plan for any particular period.

The Trust will sponsor a health reimbursement account (HRA) benefit for non-Medicare-eligible retirees and spouses. This benefit will also be offered to Medicare-eligible retirees electing to opt out of coverage under the Trust's Medicare program. Upon enrollment, eligible retirees receive a monthly HRA benefit.

#### ***Basis of Accounting***

The Trust's financial statements are prepared using the accrual basis of accounting. Revenue is recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Contributions are recognized when due pursuant to legal requirements. Benefits and refunds are recognized when due and payable in accordance with the terms of the Trust.

#### ***Specific Balances and Transactions***

##### **Cash and Cash Equivalents**

Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with a maturity of three months or less when acquired.

##### **Investments**

Investments are reported at fair value or estimated fair value. Investments that do not have an established market value are reported at estimated fair value, as determined by the Trust's management.

# City of Detroit Police and Fire Retiree Health Care Trust

## Notes to Financial Statements

December 31, 2018

### Note 1 - Significant Accounting Policies (Continued)

As of December 31, 2018, the Trust holds City of Detroit Financial Recovery Bonds Series 2014B(1) and 2014B(2) with a face value of \$233,900,999 and an estimated market value of \$202,748,249. The bonds do not have a readily determinable market value given the illiquidity and limited trading of these bonds. Management's estimates of these values are based on information provided by investment custodians and other pricing services. Because they 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 bonds mature in 2044 and carry an interest rate of 4.0 percent for the first 20 years and a 6.0 percent interest rate thereafter. For the first 10 years, semiannual interest-only payments will be made on the bonds. Beginning on the 11th anniversary of the issuance, 20 equal installments will be made annually.

#### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

#### **Federal Income Taxes**

The Trust is tax exempt under Section 501(c)(9) of the Internal Revenue Code.

### Note 2 - Deposits and Investments

The Trust is not limited in the types of investments held by any legal or contractual provisions. The Trust has designated three banks for the deposit of its funds. Under the Plan of Adjustment, the City was required to distribute the bonds to provide initial funding for the Trust. The bonds were the primary investment held by the Trust, but the Trust has sold a portion of the bonds to diversify its portfolio.

The Trust'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 Trust's deposits may not be returned to it. The Trust does not have a deposit policy for custodial credit risk. At year end, the Trust had \$531,777 of bank deposits that were uninsured and uncollateralized. The Trust believes that, due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the Trust evaluates 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.

At year end, the Trust had the following investments and maturities:

Fiduciary Funds	Fair Value	Less Than 1 Year	1-5 Years	6-10 Years	More Than 10 Years
Municipal bonds	\$ 202,748,249	\$ -	\$ -	\$ -	\$ 202,748,249
Corporate bonds	9,173,321	1,480,389	7,692,932	-	-
Total	<u>\$ 211,921,570</u>	<u>\$ 1,480,389</u>	<u>\$ 7,692,932</u>	<u>\$ -</u>	<u>\$ 202,748,249</u>

# City of Detroit Police and Fire Retiree Health Care Trust

## Notes to Financial Statements

December 31, 2018

### Note 2 - Deposits and Investments (Continued)

#### **Credit Risk**

As of year end, the credit quality ratings of debt securities per Standard & Poor's (other than the U.S. government) are as follows:

Investment	AAA	AA+	AA	AA-	A+	A and Below	Not Rated
Municipal bonds	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$202,748,249
Corporate bonds	247,513	495,268	991,072	1,235,745	1,987,614	4,216,109	-
Total	<u>\$ 247,513</u>	<u>\$ 495,268</u>	<u>\$ 991,072</u>	<u>\$ 1,235,745</u>	<u>\$ 1,987,614</u>	<u>\$ 4,216,109</u>	<u>\$202,748,249</u>

#### **Concentration of Credit Risk**

The Trust places no limit on the amount it may invest in any one issuer. More than 5 percent of the Trust's investments are in the City of Detroit Financial Recovery Bonds, Series 2014B(1) and 2014B(2); these investments are 94 percent of the Trust's total investments.

#### **Fair Value Measurements**

The Trust categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. Investments that are measured at fair value using the net asset value per share (or its equivalent) as a practical expedient are not classified in the fair value hierarchy below.

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Trust's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

As of December 31, 2018, the Trust has the following recurring fair value measurements:

- Equities of \$4,709,205 are valued using quoted marketed prices (Level 1 inputs).
- Bonds of \$211,921,570 are valued using a matrix pricing model (Level 2 inputs).

In addition, the Trust has an investment reported at amortized cost in accordance with GASB Statement No. 79. This investment is not subject to any limitations or restrictions on withdrawals.

### Note 3 - Other Postemployment Benefit Plan

#### **Plan Description**

The Trust provides healthcare benefits to retirees, and their eligible spouses and dependents, with an effective date of retirement on or before December 31, 2014 and who were eligible to receive retiree healthcare benefits from the City of Detroit, Michigan at the time of retirement. This is a single-employer benefit plan administered by the Trust. As of December 31, 2018, there were 7,099 participants in the plan.

Management of the Trust is vested with the board of trustees, which consists of seven members.

December 31, 2018

#### **Note 3 - Other Postemployment Benefit Plan (Continued)**

##### ***Benefits Provided***

The Trust provides healthcare and vision benefits for certain police and fire retirees of the City of Detroit, Michigan, along with their eligible spouses and dependents, with an effective date of retirement on or before December 31, 2014 and who were eligible to receive retiree healthcare benefits from the City at the time of retirement. Benefits are provided through third-party insurers, or by reimbursement of eligible expenses, in accordance with the Trust and applicable state and federal laws.

##### ***Contributions***

Contributions are established in the Plan of Adjustment and other grant agreements. The Plan of Adjustment required the City to distribute \$253,900,999 of the City's Financial Recovery Bonds, Series 2014B(1) and 2014B(2) on the effective date (December 10, 2014). The City of Detroit, Michigan no longer has any responsibility to provide retiree healthcare or any other retiree welfare benefits. Contributions of \$43,750 will continue to be made annually until 2034 under a grant agreement with the Foundation for Detroit's Future (the "Foundation"). Plan members are required to contribute based on the medical plan selected.

##### ***Total OPEB Liability***

The Trust will provide future benefits only to the extent that plan assets are available to pay them. After the contribution of the bonds, no further employer contributions will be made to the Trust. Future contributions will be composed of \$43,750 annually until 2034 under a city grant agreement with the Foundation. As such, the total OPEB liability as of December 31, 2018 is equal to the plan net position of \$223,984,964.

The majority of net position of the Trust is the City of Detroit Financial Recovery Bonds. Valuation of these bonds is at current market value, which is heavily discounted from the face or principal value of the bonds and represents less than the expected future cash flows if the City fulfills all of its obligations under the notes. Therefore, if the City ultimately does pay 100 percent of the interest and principal of the bonds, the benefits the Trust are able to provide will be higher than what is currently projected.

##### ***Investment Policy***

As of December 31, 2018, the Trust has not adopted a policy in regard to the allocation of invested assets given majority of all the investments held are the bonds. As the Trust begins selling additional bonds, the Trust will formalize an investment strategy that manages risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes.

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## Required Supplemental Information

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## City of Detroit Police and Fire Retiree Health Care Trust

### Required Supplemental Information Schedule of Changes in the Net OPEB Liability and Related Ratios

	Last Three Fiscal Years		
	2018	2017	2016
<b>Total OPEB Liability -</b>			
Increase (decrease) in total OPEB liability due to availability of assets	\$ 13,895,584	\$ 107,117,803	\$ (15,656,501)
<b>Total OPEB Liability - Beginning of year</b>	<u>210,089,380</u>	<u>102,971,577</u>	<u>118,628,078</u>
<b>Total OPEB Liability - End of year</b>	<u><b>\$ 223,984,964</b></u>	<u><b>\$ 210,089,380</b></u>	<u><b>\$ 102,971,577</b></u>
<b>Plan Fiduciary Net Position</b>			
Contributions - Foundation for Detroit's Future	\$ 43,744	\$ 43,750	\$ -
Net investment income (loss)	22,243,497	116,696,256	(6,355,018)
Administrative expenses	(759,118)	(1,058,591)	(1,186,906)
Benefit payments - Net of employee contributions	(7,632,539)	(8,563,612)	(8,614,577)
Other income	-	-	500,000
<b>Net Change in Plan Fiduciary Net Position</b>	<u>13,895,584</u>	<u>107,117,803</u>	<u>(15,656,501)</u>
<b>Plan Fiduciary Net Position - Beginning of year</b>	<u>210,089,380</u>	<u>102,971,577</u>	<u>118,628,078</u>
<b>Plan Fiduciary Net Position - End of year</b>	<u><b>\$ 223,984,964</b></u>	<u><b>\$ 210,089,380</b></u>	<u><b>\$ 102,971,577</b></u>
<b>Net OPEB Liability - Ending</b>	<u><b>\$ -</b></u>	<u><b>\$ -</b></u>	<u><b>\$ -</b></u>
<b>Plan Fiduciary Net Position as a Percentage of Total OPEB Liability</b>	100.0 %	100.0 %	100.0 %

As the Trust will provide future benefits only to the extent that plan assets are available to pay them, the total OPEB liability is either the present value of future benefits based on current benefit levels or the Trust's ending net position plus the present value of future assets, whichever is lower. For December 31, 2018, the Trust's total OPEB liability is the ending net position, as this is currently lower than the present value of future benefits.

There is no applicable payroll; therefore, no covered payroll is presented