

BOARD OF TRUSTEES LETTER

DEAR ACTIVE MEMBERS & RETIREES:

The Board of Trustees of the Police and Fire Retirement System of the City of Detroit is pleased to submit to you the comprehensive annual financial report for the fiscal year ended June 30, 2006.

FINANCIAL RESULTS

In 1996 the Board of Trustees adopted the policy recommended by its actuary of computing the recognized rate of return by using a “smoothing” formula to average the market value rate of return over three years on a dollar weighted basis. For the current year the recognized rate of return was 10.7% and the market rate of return was 10.1%. The system’s actuarial assumed rate is 7.8%.

ASSET ALLOCATION

The Board’s asset allocation is built upon the foundation that the obligations of the Retirement System to pay the benefits promised to its members and retirants are very

long term obligations. Accordingly, the Board of Trustees must make investment decisions which it believes will be the most beneficial to the Retirement System over many years, not just one or two years. The Board must also balance the desire for long term capital gains with the requirements to pay benefits each month. As of June 30, 2006 the Board’s target asset allocation was as follows:

<i>Equities</i>	56.0%
<i>Fixed Income</i>	27.5%
<i>Real Estate</i>	7.0%
<i>Alternative Investments</i>	8.0%
<i>Cash & Short Term Investments</i>	1.5%

BENEFITS PAID

The Retirement System and its assets exist to pay the benefits which its members have earned. During the fiscal year ended June 30, 2006 the Retirement System paid

\$217,411,446 in benefits to retirants and beneficiaries, plus

\$22,244,391 in lump sum defined contribution plan benefits

OTHER ACCOMPLISHMENTS

In addition to the financial results achieved, other significant accomplishments of the Board of Trustees and staff during this past year included:

The System’s internet web site (www.rscd.org) was enhanced to provide a benefit estimate function which can be accessed by members of the System.

Further enhancements to the System’s state-of-the-art computer systems were implemented to support the System’s internet web site as well as provide electronic access to member files.

The System continued to provide a toll-free telephone number (1-800-339-8344).

CONTENTS OF THE REPORT

This is a consolidated report of the Defined Benefit Plan and the Defined Contribution Plan of the Retirement System. The report consists of six (6) sections:

- I. **INTRODUCTORY SECTION** contains the Board of Trustees letter of transmittal, lists Retirement System Board members, and summarizes the Plan Benefit provisions.
- II. **FINANCIAL SECTION** contains the Independent Auditors report and the financial statements of the System.
- III. **ACTUARIAL & STATISTICAL SECTION** contains the results of the annual valuation and statistical tables which contain significant data pertaining to the Police and Fire Retirement System.
- IV. **INVESTMENT SECTION** summarizes investment activities and identifies the System’s advisors and consultants.
- V. **SPECIAL INFORMATION SECTION** contains the “Safe Harbor Explanation” provided to recipients of distributions from qualified plans in order to satisfy section 402(f) of the Internal Revenue Code.

VI. QUESTION & ANSWER

SECTION contains commonly asked Retirement System related questions.

ACCOUNTING SYSTEM AND REPORTS

These financial statements have been prepared in accordance with generally accepted accounting principles applicable to governmental units in accordance with standards promulgated by the Governmental Accounting Standards Board (GASB).

REVENUES

The reserves needed to fund retirement benefits are accumulated through the collection of employer and employee contributions and from income on investments. Employer contributions for the 2005-2006 fiscal year totaled \$64,986,629 and employee contributions were \$10,007,531. Recognized investment income for the fiscal year was \$397,627,662.

EXPENSES

Benefit payments are the primary disbursements of a Retirement

System. Consequently, recurring benefit payments prescribed by the plan, refunds of contributions from the Defined Contribution Plan and the cost of administering the System comprise the total expenses. Administrative expenses are funded entirely from investment income.

FUNDING AND RESERVES

The trust funds consist of contributions and earnings that are accumulated by the Retirement System in order to meet current and future benefit obligations to retirants and beneficiaries. A higher level of funding and a larger accumulation of assets leads to a greater potential for higher investment income. Continuous improvement in the funding of the System is the primary objective of the Board of Trustees.

As of June 30, 2006, the fund balances of the assets of the Retirement System totaled \$3.98 billion and the actuarial accrued liabilities were \$3.809 billion resulting in a funding surplus (excess of assets over liabilities) of \$171 million.

INVESTMENTS

The Retirement System invests all available funds in order to maximize both current income and long-term appreciation. The primary objective of the System's investment policy is to assure that the System meets its responsibilities for providing all promised retirement benefits. The Board of Trustees invests all available funds in a diversified portfolio of investments with the objective of maximizing the overall long term appreciation of the Retirement System's assets while generating sufficient current income to pay the benefits which the members of the System have earned. The portfolio is diversified to provide the highest possible total return on the System's assets with the least exposure to risk.

ACKNOWLEDGMENTS

The preparation of this report reflects the combined efforts of the Retirement System staff under the direction of the Board of Trustees. It is intended to provide complete and reliable information as a basis for making management decisions, to

disclose compliance with legal provisions, and as a means of disseminating vital and pertinent information to all active and retired members of the Police and Fire Retirement System of the City of Detroit. This report is being distributed to all active members and retirees plus other interested parties.

Respectfully submitted,

Board of Trustees
Police and Fire Retirement System of
the City of Detroit

ELECTED EMPLOYEE MEMBERS:

GEORGE ORZECH

Fire Lieutenant,
Fire Department
Term expires June 30, 2006

PAUL STEWART

Police Officer,
Police Department
Term expires June 30, 2006

FRANK ENGLISH

Fire Captain,
Fire Department
Term expires June 30, 2007

MARTIN BANDEMER

Police Officer,
Police Department
Term expires June 30, 2007

GREG BEST

Fire Captain,
Fire Department
Term expires June 30, 2008

JAMES MOORE

Inspector,
Police Department
Term expires June 30, 2008

EX-OFFICIO MEMBERS:

KWAME M. KILPATRICK
Mayor

ALBERTA TINSLEY-TALABI
Council Designate,
City Council

JEFFREY BEASLEY
Treasurer

ELLA BULLY-CUMMINGS
Chief of Police

TYRONE C. SCOTT
Fire Commissioner

OFFICERS:

WALTER STAMPOR
Executive Secretary

CYNTHIA A. THOMAS
Assistant Secretary

ACTUARY:

GABRIEL, ROEDER,
SMITH & CO.

MEDICAL DIRECTOR:

REGINALD E. O'NEAL, D.O.

PERFORMANCE EVALUATION:

SMITH BARNEY

LEGAL ADVISOR:

RONALD ZAJAC

REAL ESTATE CONSULTANT:

THE TOWNSEND GROUP

MASTER CUSTODIAN:

BANK OF NEW YORK

FULL SERVICE CONSULTANT:

NORTH POINT ADVISORS

SUMMARY OF PLAN BENEFIT PROVISIONS

AGE AND SERVICE RETIREMENT

ELIGIBILITY – 25 years of service regardless of age.

ANNUAL AMOUNT – An annuity equal to the actuarial equivalent of the member’s accumulated contribution account plus a defined benefit, which, when added to the annuity, will provide the following:

- **Pre-1969 Members** 2.5% of AFC times the first 25 years of service, with a maximum allowance of 15/22 of a police officer’s or firefighter’s annual rate of compensation.
- **1969 Plan Members** 2.5% of AFC times the first 25 years of service plus 2.1% of AFC times each of the next 10 years of service.

Members may elect to receive their accumulated contribution account in a lump sum after 25 years of service. The defined benefit at retirement is then reduced by the actuarial equivalent of the amount of principal withdrawn. No reduction is made with regard to the interest portion of the withdrawal.

Pre-1969 plan members may elect 1969 plan benefits at the time of retirement.

TYPE OF AVERAGE FINAL COMPENSATION (AFC) – Average of the current compensation for the ranks held in each of the last five years (last three years for DPCOA, Executive members and their Fire equivalents) plus longevity. Pension benefits for nonunion employees may not be diminished due to a reduction in compensation because of fiscal emergency. AFC includes prior longevity distributions during the averaging period in accordance with the following schedule: 1% of compensation after 5 years of service, 2% after 11 years, 3% after 16 years and 4% after 21 years.

DEFERRED RETIREMENT VESTED BENEFIT

ELIGIBILITY – Age 40 with 8 years of service, or if a DPOA Member or their Fire equivalents who terminate employment on or after August 29, 2003 with ten years of credited service regardless of age.

ANNUAL AMOUNT – Same as regular retirement but based on average final compensation and credited service at the time of termination.

BENEFIT COMMENCEMENT – **Members hired prior to 7/1/85:** Unreduced benefit begins at the age when the member would have first been eligible for regular retirement had the member continued in City service. **DPOA Members and their Fire equivalents hired after 6/30/85:** Unreduced benefit begins at age 62. All members may elect a reduced benefit payable immediately.

DUTY DISABILITY RETIREMENT

ELIGIBILITY – No age or service requirements.

ANNUAL AMOUNT – A basic benefit of 50% of final compensation and a supplemental benefit of 16 2/3% of final compensation. After 24 months, members disabled from any occupation continue to receive both benefits, otherwise, members receive only the 50% benefit. Upon attaining 25 years of service, members receive only the basic benefit of 50%. Members convert to regular retirement at age 65. Workers Compensation payments are offset.

Members who filed for duty disability retirement prior to July 1, 1995, for DPOA members and fire equivalents or prior to June 30, 1998, for all others receive 66 2/3% of final compensation payable to the eligibility date for regular retirement. After the eligibility date for regular retirement, benefit is computed as a regular retirement benefit. Workers Compensation payments are offset.

SUMMARY OF PLAN BENEFIT PROVISIONS CON'T

NON-DUTY DISABILITY RETIREMENT

ELIGIBILITY – 5 years of service.

ANNUAL AMOUNT – Computed as a regular retirement benefit, but based on average final compensation and credited service at the time of disability. Minimum benefit is 20% of average final compensation.

DUTY DEATH BEFORE RETIREMENT

ELIGIBILITY – No age or service requirement.

ANNUAL AMOUNT – Widow receives 5/11 of a patrolman's or fireman's compensation and each child under age 18 receives 1/10 of such compensation with a maximum total of 7/33 of such compensation. If there is no widow, each child receives 1/4 of such compensation with a maximum total of 1/2 of such compensation. If there is no widow or children, each dependent parent receives 1/6 of such compensation. Worker's compensation payments are offset.

NON-DUTY DEATH BEFORE RETIREMENT

ELIGIBILITY – No age or service requirement.

ANNUAL AMOUNT – Same as regular retirement benefit to a widow or dependent widower, but reduced in accordance with a 100% joint and survivor option election. Minimum benefit is 20% of average final compensation. Each child under 18 receives 1/7 of a patrolman's or fireman's compensation with a maximum total of 2/7 of such compensation. If there is no spouse or children, each dependent parent receives 1/7 of such compensation.

POST RETIREMENT COST-OF-LIVING ADJUSTMENTS

PRE-1969 PLAN MEMBERS: Allowances increase in proportion to active member compensation for the corresponding rank.

POST-1969 PLAN MEMBERS: Pensions increase by 2.25% of the **original** pension amount.

LSA and DPCOA members, and their Fire equivalents, who retire July 1, 1998 or later and DPOA members and their Fire equivalents, who retire July 1, 2001 or later the 2.25% annual increase shall be compounded.

MEMBER CONTRIBUTIONS

5% of covered compensation payable until first eligible for regular retirement.