

**City of Kalamazoo, Michigan
Perpetual Care Fund**

FINANCIAL STATEMENTS

December 31, 2015

City of Kalamazoo, Michigan
Perpetual Care Fund

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Principals

Dale J. Abraham, CPA
Steven R. Kirinovic, CPA
Aaron M. Stevens, CPA
Eric J. Glashouwer, CPA
Alan D. Panter, CPA
William I. Tucker IV, CPA



3511 Coolidge Road
Suite 100
East Lansing, MI 48823
(517) 351-6836
FAX: (517) 351-6837

INDEPENDENT AUDITOR'S REPORT

Members of the Perpetual Care Investment Committee
and the City Commission of Kalamazoo
Kalamazoo, Michigan

Report on the Financial Statements

We have audited the accompanying financial statements of the Perpetual Care Fund of the City of Kalamazoo, Michigan, (a permanent fund) as of and for the year ended December 31, 2015, and the related notes to the 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 financial statements referred to above present fairly, in all material respects, the respective financial position of the Perpetual Care Fund of the City of Kalamazoo, Michigan, as of December 31, 2015, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of a Matter

As discussed in Note A, the financial statements present only the Perpetual Care Fund and do not purport to, and do not, present fairly the financial position of the City of Kalamazoo, Michigan, as of December 31, 2015, the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, 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, who 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 supplementary 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.

Abraham & Gaffney, P.C.

ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

June 28, 2016

City of Kalamazoo, Michigan
Perpetual Care Fund

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2015

The following is a discussion and analysis of the financial performance and position of the City of Kalamazoo Perpetual Care Fund (PCF). It is intended to provide an overview of PCF's financial activities for the fiscal year ended December 31, 2015. This analysis should be read in conjunction with the *Independent Auditor's Report* and with the financial statements, which follow this section.

Overall Fund Structure and Objectives

PCF is a permanent trust fund which is used to hold and manage funds for the purpose of maintenance and upkeep of cemetery property, inclusive of maintenance of grounds and capital assets, monuments, and infrastructure. To this end, the PCF provides support to the City's Cemetery Fund, which manages the day-to-day operations and maintenance of the City's cemetery system.

Income for the PCF is derived primarily from investments in mutual funds, as well as from ½ of the fee for the sale of each lot.

Condensed Financial Information

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

	2015	2014
Total assets	\$ 3,695,586	\$ 4,187,125
Total liabilities	2,219	2,668
Total fund balance	\$ 3,693,367	\$ 4,184,457
Net investment income	\$ (108,115)	\$ 120,809
Charges for services	29,850	34,433
Total revenue	(78,265)	155,242
Professional fees	21,999	21,851
Transfers to the City of Kalamazoo Cemetery Fund	(390,826)	(188,517)
Net changes in fund balance	(491,090)	(55,126)
Fund balance		
Beginning of Year	4,184,457	4,239,583
End of Year	\$ 3,693,367	\$ 4,184,457

Assets

The assets of the PCF are comprised of cash and investments. Investment assets decreased approximately 13% from the prior year due primarily to unfavorable investment performance and budgeted liquidations ("Transfers out") of \$390,826 for Cemetery operations as reported on the Statement of Revenues, Expenditures, and Changes in Fund Balance.

City of Kalamazoo, Michigan
Perpetual Care Fund

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2015

Asset Allocation

The City Commission has delegated the management of PCF's assets to the Perpetual Care Investment Committee. It is the responsibility of this Committee to determine the allocation of assets among distinct capital markets.

In determining asset allocation, the Committee reviews expected returns of various asset classes, the PCF's future liquidation needs, and the risks associated with alternative asset mix strategies. The Committee has established the following asset allocation:

<u>Asset Class</u>	<u>Target</u>
Large Capitalization Domestic Equity	10%
Large Capitalization Domestic Value Equity	10%
Micro Capitalization Domestic Equity	10%
Small Capitalization Domestic Value Equity	10%
Large Capitalization International Value Equity	10%
Small Capitalization International Equity	5%
Small Capitalization International Value Equity	5%
Emerging Markets Equity	10%
Fixed Income	30%

This asset allocation policy offers the optimal mix for meeting longer term goals at an acceptable risk level. The asset classes stated above shall be further diversified (where possible) as to style and manager type to reduce risk further, while providing the opportunity for enhanced return.

Liabilities

The liabilities of the PCF include accounts and contracts payable for the services of the fund. The decrease is primarily due to the timing of payments for investment management services.

Fund Balance

The fund balance represents the difference between the PCF's assets and liabilities. Note D in the Notes to Financial Statements discusses the various categories of fund balance and definitions.

Nonspendable fund balance

The nonspendable fund balance of the PCF represents the assets that are legally required to be maintained as the corpus of the permanent fund.

Restricted for cemetery care

The portion of the fund balance that is not restricted is required to be used for the care of the City's cemeteries.

Revenues

Revenues are composed of:

Charges for Services

The PCF receives a portion of the sale of each cemetery lot for the long term care of the lot. Charges for services decreased by \$4,583 as demand decreased in 2015 compared to the prior year.

City of Kalamazoo, Michigan
Perpetual Care Fund

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2015

Interest and dividends

Interest and dividends earned on investments and cash balances increased approximately 77% in 2015 due primarily to an increase in market interest rates.

Net increase (decrease) in fair value of investments

As discussed in Note A in the Notes to Financial Statements, the mutual funds of the PCF are reported at fair value. Increases (decreases) to the value of investments are reported on the Statement of Revenues, Expenditures, and Changes in Fund Balance. The decrease of \$293,359 in 2015 is primarily due to a significantly unfavorable performance of the PCF's mutual funds, and is much lower than the \$16,335 increase experienced in 2014. See Economic Factors, Investment Returns, and Other Important Matters below for further discussion.

Expenditures

The expenditures of the PCF are composed of contractual services. The expenditures of the fund were consistent in 2015 and 2014.

Other Financing Uses

The PCF transfers funds to the City of Kalamazoo Cemeteries Fund to support operations and capital outlay for the City's cemeteries. The 107% increase in 2015 is due to an increase in capital outlay in the Cemeteries fund as projects that were put on hold in 2014 were completed in 2015.

Economic Factors, Investment Returns, and Other Important Matters

The purpose of this fund is to preserve and manage the assets of the cemetery system. The returns on investment realized in any particular period are not reflective of the overall objective of the investment strategy. The investment strategy is focused on total long-term returns, which will align expected revenue with the fund's long-term objectives.

At December 31, 2015, the PCF's investments represented 95% of the fund's assets. The market value of PCF investments decreased over the past year. PCF investments decreased (net of interest, dividends, and depreciation of fair market value) by \$501,293 in 2015, after increasing by \$120,809 in 2014. Since the transfer on December 5, 2006, from Dimensional Fund Advisors to Schwab Investments, the assets have had a nominal net return of 5.8% and an inflation-adjusted or real return of 3.9%.

Contacting the System's Financial Management

This financial report is designed to provide the public, citizens, and other interested parties with a general overview of PCF's financial position. If you have questions about this report or need additional financial information, contact Thomas C. Skrobola, Director of Management Services/CFO, City of Kalamazoo, 241 W. South Street, Kalamazoo, MI 49007, (269) 337-8468.

FUND FINANCIAL STATEMENTS

City of Kalamazoo, Michigan
Perpetual Care Fund

BALANCE SHEET

December 31, 2015

ASSETS	
Cash	\$ 203,934
Investments	<u>3,491,652</u>
TOTAL ASSETS	<u>\$ 3,695,586</u>
LIABILITIES	
Contract payable	\$ 2,219
FUND BALANCE	
Nonspendable	1,735,160
Restricted for cemetery care	<u>1,958,207</u>
TOTAL FUND BALANCE	<u>3,693,367</u>
TOTAL LIABILITIES AND FUND BALANCE	<u>\$ 3,695,586</u>

See accompanying notes to financial statements.

City of Kalamazoo, Michigan
Perpetual Care Fund

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE

Year Ended December 31, 2015

REVENUES	
Charges for services	\$ 29,850
Interest and dividends	185,244
Net (decrease) in fair value of investments	<u>(293,359)</u>
TOTAL REVENUES	(78,265)
EXPENDITURES	
Current	
General government	
Contracted services	<u>21,999</u>
EXCESS OF EXPENDITURES (UNDER) REVENUES	(100,264)
OTHER FINANCING USES	
Transfers out	<u>(390,826)</u>
NET CHANGE IN FUND BALANCE	(491,090)
Fund balance, beginning of year	<u>4,184,457</u>
Fund balance, end of year	<u><u>\$ 3,693,367</u></u>

See accompanying notes to financial statements.

City of Kalamazoo, Michigan
Perpetual Care Fund

NOTES TO FINANCIAL STATEMENTS

December 31, 2015

NOTE A: DESCRIPTION OF THE FUND AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Perpetual Care Fund (the Fund) was established to hold and manage funds for the purpose of financing the annual maintenance of the City of Kalamazoo's cemeteries, in perpetuity. Management of the Fund's assets has been delegated to the Perpetual Care Investment Committee by the City Commission. The investment committee currently contracts with Merion Capital, LLC to provide investment advisory services for the Fund's assets.

The financial statements of the Fund have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) as applied to governments. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Fund's more significant accounting policies are described below.

1. Reporting Entity

The Fund is considered a permanent trust fund of the City of Kalamazoo, Michigan (the City). As a result, industry standards require the City to include the financial activities of the fund in the City's annual financial report. The City of Kalamazoo's annual financial report may be obtained from the City's management.

The accompanying financial statements are exclusive presentations of the financial condition and results of operations of the Perpetual Care Fund, and do not purport to, and do not, present fairly the financial position of the City of Kalamazoo, Michigan, as of December 31, 2015, or the results of its operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

2. Basis of Presentation

The Fund is considered a separate accounting entity. The operation of the Fund is accounted for with a separate set of self-balancing accounts that comprise its assets, deferred outflows of resources, liabilities, deferred inflows of resources, fund balance, revenues, and expenditures. Fund resources are accounted for based upon the purpose for which they are to be spent and the means by which spending activities are controlled.

The Perpetual Care Fund is a permanent trust (governmental) fund of the City and is used to account for the financial resources endowed to the City's cemeteries. The resources of the Fund are legally restricted by the terms of the trust agreement.

3. Measurement Focus

All governmental funds are presented using the current financial resources measurement focus. With this measurement focus, only current assets, deferred outflows of resources, current liabilities, and deferred inflows of resources generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in fund balance.

4. Basis of Accounting

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

All governmental funds are accounted for using the modified accrual basis of accounting. Under this method, revenues are recognized when they become susceptible to accrual (when they become both "measurable" and "available to finance expenditures of the current period"). The length of time used for "available" for purposes of revenue recognition in the governmental fund financial statements is sixty (60) days. Expenditures are generally recognized under the modified accrual basis of accounting when the related fund liability is incurred.

City of Kalamazoo, Michigan
Perpetual Care Fund

NOTES TO FINANCIAL STATEMENTS

December 31, 2015

NOTE A: DESCRIPTION OF THE FUND AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

4. Basis of Accounting - continued

If/when both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

5. Cash and Investments

The Fund's cash consists of demand deposits. Investments consist of mutual funds and are reported at fair value, based on quoted market prices.

6. Deferred Outflows/Inflows of Resources

In addition to assets, the balance sheet will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of fund balance that applies to future period(s) and so will not be recognized as an outflow of resources (expenditure) until then.

In addition to liabilities, the balance sheet will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of fund balance that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time.

Currently, the Fund does not have any items that meet the recognition criteria for classification as deferred outflows of resources or deferred inflows of resources.

NOTE B: CASH AND INVESTMENTS

In accordance with the Uniform Prudent Management of Institutional Funds Act, Public Act 87 of 2009, in addition to an investment otherwise authorized by law or by the trust agreement, the City of Kalamazoo, subject to specific limitations set forth in the trust agreement, may:

1. Invest and reinvest the Fund in real or personal property deemed advisable by the governing board, whether or not it produces a current return, including mortgages, stocks, bonds, debentures, and other securities of profit or nonprofit corporations, shares in or obligations of associations, partnerships, or individuals, and obligations of any government, or subdivision, or instrumentality thereof.
2. Retain property contributed by a donor to the Fund for as long as the governing board deems advisable.
3. Include all or any part of the Fund in a pooled or common fund maintained by the institution.
4. Invest all or any part of the Fund in any other pooled or common fund available for investment, including shares or interest in regulated investment companies, mutual funds, common trust funds, investment partnerships, real estate investment trusts, or similar organizations in which funds are commingled and investment determinations are made by persons other than the governing board.

City of Kalamazoo, Michigan
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NOTES TO FINANCIAL STATEMENTS

December 31, 2015

NOTE B: CASH AND INVESTMENTS - CONTINUED

Investments

As of December 31, 2015, the carrying amounts and market values for the investments are as follows:

	<u>Carrying Amount</u>	<u>Market Value</u>	<u>Rating</u>	<u>Weighted Average Maturity</u>
Uncategorized Pooled Investments Mutual Funds	\$ 3,491,652	\$ 3,491,652	N/A	N/A

The Fund'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 Fund's deposits may not be returned to it. The Fund's banking and investment policy does not specifically address this risk, although management believes that due to the dollar amounts of cash deposits and the limits of insurance provided through the Federal Deposit Insurance Corporation (FDIC), it is impractical to insure all bank deposits. As a result, management 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 level risk level are used as depositories. As of December 31, 2015, the carrying amount of the Fund's deposits (which includes a portion of the City of Kalamazoo's pooled checking account) was \$203,934; however, as the City's pooled checking account was not fully insured by the FDIC, the amount of Perpetual Care coverage is undeterminable.

Custodial Credit Risk of Investments

As of December 31, 2015, the Fund's investments in the amount of \$3,491,652 were comprised of bond and equity mutual funds. For investments, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Fund will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Fund's investment policy requires that investment securities be held in third-party safekeeping by a designated institution and that the safekeeping agent follow the procedure of delivery vs. payment. As of December 31, 2015, none of the Fund's investments were exposed to risk since the securities are held in the Fund's name by the counterparty.

Investments, managed by Merion Capital, LLC, consist of a variety of bond and equity mutual funds. The investments are designed to comply with the requirements and restrictions of Act 177 of the Public Acts of 1937, as amended, dealing with the investment of trust funds and the investment philosophy of the Fund's investment committee.

The Act provides for the investment of funds in, but not limited to, bond and equity securities and various interest-bearing instruments.

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 City of Kalamazoo, as administrator for the Fund, will minimize interest rate risk by designating its investment portfolio with the objective of obtaining a rate of return through the economic cycles considering risk constraints and cash flow characteristics. The City's policy provides that the maximum weighted average maturity will be limited to eighteen (18) months.

City of Kalamazoo, Michigan
Perpetual Care Fund

NOTES TO FINANCIAL STATEMENTS

December 31, 2015

NOTE B: CASH AND INVESTMENTS - CONTINUED

Credit Risk

The Uniform Prudent Management of Institutional Funds Act does not limit investments of the Fund to certain credit ratings issued by nationally recognized statistical rating organizations. Similarly, the City of Kalamazoo has no investment policy that limits its investment choices. The Fund's investments in bond and equity mutual funds are not rated.

NOTE C: RISK MANAGEMENT

The Perpetual Care Fund is exposed to various risks of loss related to torts, errors, and omissions. The Perpetual Care Fund participates in the City of Kalamazoo's risk management program for all of these exposures. The City's risk management program is a primarily self-insured program with reinsurance for amounts in excess of aggregate loss funds. The City estimates the liability for unpaid claims (including claims incurred but not reported) and allocates cost to all appropriate entities and funds. There is no further exposure to the Perpetual Care Fund that would require a liability to be recorded in the financial statements.

NOTE D: DETAILS OF FUND BALANCE CLASSIFICATIONS

GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, established fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds. The following are the five classifications of fund balance under this standard:

Nonspendable - assets that are not available in a spendable form such as inventory, prepaid expenditures, and long-term receivables not expected to be converted to cash in the near term. It also includes funds that are legally or contractually required to be maintained intact such as the corpus of a permanent fund or foundation.

Restricted - amounts that are required by external parties to be used for a specific purpose. Constraints are externally imposed by creditors, grantors, contributors or laws, regulations or enabling legislation.

Committed - amounts constrained on use imposed by formal action of the government's highest level of decision making authority (i.e., Board, Council, etc.).

Assigned - amounts intended to be used for specific purposes. This is determined by the governing body, the budget or finance committee or a delegated municipality official.

Unassigned - all other resources; the remaining fund balance after non-spendable, restrictions, commitments, and assignments. This class only occurs in the General Fund, except for cases of negative fund balances. Negative fund balances are always reported as unassigned, no matter which fund the deficit occurs in.

Fund Balance Classification Policies and Procedures

For committed fund balance, the City of Kalamazoo's highest level of decision-making authority is the City Commission. Formal action that is required to be taken to establish a fund balance commitment is a resolution of the City Commission.

For assigned fund balance, the City Commission has not approved a policy indicating who is authorized to assign amount to a specific purpose. As a result, this authority is retained by the City Commission.

City of Kalamazoo, Michigan
Perpetual Care Fund

NOTES TO FINANCIAL STATEMENTS

December 31, 2015

NOTE D: DETAILS OF FUND BALANCE CLASSIFICATIONS - CONTINUED

The City of Kalamazoo has not formally adopted a policy that defines the order of usage for fund balance amounts classified as restricted, committed, assigned, or unassigned. Therefore, restricted resources will be used first, then unrestricted resources as they are needed.

NOTE E: UPCOMING ACCOUNTING PRONOUNCEMENTS

In March 2015, the GASB issued Statement No. 72, *Fair Value Measurement and Application*. This statement addresses accounting and financial reporting issues related to fair value measurements. The definition of fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This statement provides guidance for determining a fair value measurement for financial reporting purposes. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The City is currently evaluating the impact this standard will have on the financial statements when adopted for the 2016 fiscal year.