

**Civilian Employees' Retirement System of the  
Police Department of Kansas City, Missouri**

A Component Unit of the City of Kansas City, Missouri

Auditor's Report and Financial Statements

April 30, 2013



**Civilian Employees' Retirement System of the  
Police Department of Kansas City, Missouri**  
A Component Unit of the City of Kansas City, Missouri  
April 30, 2013

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## Independent Auditor's Report on Financial Statements and Supplementary Information

Retirement Board  
Civilian Employees' Retirement System  
of the Police Department of Kansas City, Missouri  
Kansas City, Missouri

We have audited the accompanying financial statements of the Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri (the Plan), a component unit of the City of Kansas City, Missouri, which comprise the statement of net position as of April 30, 2013, and the related statement of changes in net position for the year then ended, 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.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri as of April 30, 2013, and the changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and pension information listed in the table of contents be presented to supplement the basic financial statements. Such information, although not 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.

***Supplementary Information***

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplemental schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. We previously expressed an unmodified opinion on the 2012, 2011, 2010, 2009 and 2008 financial statements.

***BKD, LLP***

Kansas City, Missouri  
July 30, 2013

**Civilian Employees' Retirement System of the  
Police Department of Kansas City, Missouri**  
A Component Unit of the City of Kansas City, Missouri  
**Management's Discussion and Analysis**  
**April 30, 2013**

This discussion and analysis of the Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri (Civilian Employees' Retirement System or the Plan) financial statements provides an overview of its financial activities during the year ended April 30, 2013. Please read it in conjunction with the more detailed financial statements, notes and required supplementary information which follow this section.

The Civilian Employees' Retirement System is the defined benefit retirement plan for civilian members of the Kansas City, Missouri Police Department. The Plan was established by the Missouri General Assembly in 1965 and is administered by the Retirement Board to provide retirement, disability and survivor benefits to its members.

***Overview of the Financial Statements and Accompanying Information***

- The financial statements presented in this report are the Statement of Plan Net Position as of April 30, 2013, and the Statement of Changes in Plan Net Position for the year ended April 30, 2013. These statements reflect resources available for the payment of benefits as of the year-end, and the sources and use of those funds during the year.
- The notes to the financial statements are an integral part of the financial statements and provide facts and detailed information to assist the reader in understanding the statements. Information in the notes includes a description of the Plan, a summary of significant accounting policies, the method used to value investments, a summary of investments and actuarial methods and assumptions.
- Schedules related to employer contributions and the funding of the Plan are included in the section entitled Required Supplementary Information.
- Other supplementary schedules consist of detailed information supporting administrative and investment expenses and a historical summary of revenues and expenses.

**Civilian Employees' Retirement System of the  
Police Department of Kansas City, Missouri**  
A Component Unit of the City of Kansas City, Missouri  
**Management's Discussion and Analysis**  
**April 30, 2013**

**Plan Net Position**

The following is a summary comparative statement of Plan Net Position for the System:

	<u>April 30, 2013</u>	<u>April 30, 2012</u>	<u>Amount Change</u>
Cash	\$ 32,649	\$ 6,383	\$ 26,266
Receivables	352,355	489,842	(137,487)
Investments	108,694,244	102,004,216	6,690,028
Securities lending collateral	27,317,981	29,102,179	(1,784,198)
Total assets	<u>136,397,229</u>	<u>131,602,620</u>	<u>4,794,609</u>
Accounts and refunds payable	167,877	157,056	10,821
Due to broker for purchases of investments	393,422	1,151,047	(757,625)
Securities lending collateral	27,317,981	29,102,179	(1,784,198)
Total liabilities	<u>27,879,280</u>	<u>30,410,282</u>	<u>(2,531,002)</u>
Net position	<u>\$ 108,517,949</u>	<u>\$ 101,192,338</u>	<u>\$ 7,325,611</u>

**Financial Analysis of Plan Net Position**

The Civilian Employees' Retirement System's benefits are funded through member and employer contributions, and investment income. Net position of the Plan increased to \$108,517,949 as of April 30, 2013 from \$101,192,338 as of April 30, 2012. Plan income is generated through the investment of contributions in stocks, bonds and alternative assets. Members contributed 5% of annual covered salary to the Plan, while employer contributions totaled 13.14% of covered salary. Plan members participate in both Social Security and Medicare.

Assets – Total assets of the Civilian Employees' Retirement System were \$136.4 million as of April 30, 2013 and included cash, investments and receivables. Total assets increased by \$4.8 million or 3.6% from FY 2012 due to improved investment performance. Investable assets increased during the year by \$6.7 million while securities lending collateral decreased by \$1.8 million.

Liabilities – Total liabilities of the Civilian Employees' Retirement System were \$27.9 million as of April 30, 2013 and included securities lending collateral, payables for money manager fees and amounts due to brokers for purchases of investments. Total liabilities decreased by \$2.5 million during the year mainly due to the \$1.8 million decrease in the offsetting liability for securities lending activity and \$0.8 million decrease in investment purchases payable.

Net Position – Civilian Employees' Retirement System assets exceeded liabilities at April 30, 2013 by \$108.5 million. This was an increase of \$7.3 million or 7.2% from the prior year.

**Civilian Employees' Retirement System of the  
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***Changes in Plan Net Position***

The following is a summary comparative statement of Changes in Plan Net Position for the System:

	<u>April 30, 2013</u>	<u>April 30, 2012</u>	<u>Amount Change</u>
Member contributions	\$ 1,296,963	\$ 1,224,736	\$ 72,227
Employer contributions	3,283,458	3,146,124	137,334
Net investment income (loss)	8,385,124	(613,908)	8,999,032
Total additions	<u>12,965,545</u>	<u>3,756,952</u>	<u>9,208,593</u>
Benefits paid to members	5,249,218	4,786,286	462,932
Refunds of contributions	249,244	183,861	65,383
Administrative expenses	141,472	117,078	24,394
Total deductions	<u>5,639,934</u>	<u>5,087,225</u>	<u>552,709</u>
Net increase (decrease)	7,325,611	(1,330,273)	8,655,884
Net position, beginning of year	<u>101,192,338</u>	<u>102,522,611</u>	<u>(1,330,273)</u>
Net position, end of year	<u>\$ 108,517,949</u>	<u>\$ 101,192,338</u>	<u>\$ 7,325,611</u>

***Financial Analysis of Changes in Plan Net Position***

Revenues – Additions to Plan Net Position – Member contributions, employer contributions and investment income are the sources of revenue for the Civilian Employees' Retirement System. Members contribute 5% of covered salary to the Plan. Employer contributions are 13.14% of covered salary to the Plan. The amount of member and employer contributions and net investment income all increased from FY 2012. Contributions increased due to growth of payroll rather than changes to the contribution rates. The net investment gain of \$8.4 million is the result of positive investment performance. The portfolio's investment rate of return was 8.8% with investment income of \$9.0 million and investment expenses of \$0.6 million. Investments in stocks, bonds, and alternative assets posted gains and investments in commodities posted a loss for the year.

Expenses – Deductions from Plan Net Position – Benefits paid to members, refunds of member contributions and administrative expenses are the sources of expenses for the Civilian Employees' Retirement System. Benefit payments and refunds represent 97.5% of the total deductions. Benefits paid to members increased over the prior year because of new retirements and a cost of living adjustment for retirees. The amount of refunds increased due to longer-term members leaving the Police Department. Administrative expenses increased because of additional actuarial services for pension reform research.

**Civilian Employees' Retirement System of the  
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**April 30, 2013**

For the twelfth consecutive year, employer contributions did not equal the amount and percentage of compensation recommended by the Retirement System actuary. The employer contribution rate was 6.68% below the annual required contribution rate of 19.82%. For the year beginning May 1, 2013, employer contributions are budgeted to remain at 13.14% of covered pay, unless pension reform legislation is signed into law. The annual required contribution rate increases to 20.40%.

The Retirement Board has approved an asset allocation which over time is expected to realize the assumed actuarial rate of investment return of 7.75%. While the asset allocation is structured to provide some control over volatility, investment returns of 8.8% in FY 2013 and (0.1%) in FY 2012 provide an indication of how dramatically the markets can move from year to year. The Retirement Board continues to review investment allocations on a quarterly basis and to make tactical allocations on a more frequent basis with guidance from an independent financial consulting firm.

***Requests for Information***

This financial report is designed to provide members of the Civilian Employees' Retirement System, citizens, investors and creditors of the City of Kansas City, Missouri with a general overview of plan finances and to demonstrate its accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Kansas City Police Employees' Retirement Systems, 9701 Marion Park Drive B, Kansas City, Missouri 64137.

There are no other currently known facts, conditions or decisions that are expected to have a significant effect on the financial position or results of operations of the Civilian Employees' Retirement System.



# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

A Component Unit of the City of Kansas City, Missouri  
Statement of Plan Net Position

April 30, 2013

## Assets

### Investments

U.S. government securities	\$ 13,580,088
Corporate bonds and notes	13,689,447
Common and preferred stock	18,923,186
Equity exchange-traded-funds	11,800,001
Fixed income exchange-traded-funds	664,513
Government mortgage-backed securities	2,287,338
Real estate funds	4,248,403
Partnerships - equity	2,747,498
Partnerships - fixed income	8,492,374
Short-term investment funds	3,880,663
Emerging markets equities	5,679,523
Commodities funds	4,871,795
Hedge fund of funds	10,539,206
Foreign equities	7,290,209

Total investments 108,694,244

### Securities Lending Collateral

27,317,981

### Receivables

Member insurance premiums	46,487
Accrued interest and dividends	257,182
Member contributions	48,686

Total receivables 352,355

### Cash

32,649

Total assets 136,397,229

## Liabilities

Accounts and refunds payable	167,877
Due to broker for purchases of investments	393,422
Securities lending collateral	27,317,981

Total liabilities 27,879,280

### Net Position Restricted for Pensions

\$ 108,517,949

**Civilian Employees' Retirement System of the  
Police Department of Kansas City, Missouri**  
A Component Unit of the City of Kansas City, Missouri  
**Statement of Changes in Plan Net Position**  
**Year Ended April 30, 2013**

**Additions**

**Investment Income**

Net appreciation in fair value of investments	\$ 6,979,496
Interest and dividends	1,989,414
Investment expense	<u>(637,468)</u>
Net investment income	<u>8,331,442</u>

**Securities Lending Income**

Securities lending gross income	<u>93,030</u>
Securities lending expenses	
Borrower rebates	(16,468)
Management fees	<u>(22,880)</u>
Total securities lending expenses	<u>(39,348)</u>
Net securities lending income	<u>53,682</u>
Total net investment income	<u>8,385,124</u>

**Contributions**

City	3,283,458
Members	<u>1,296,963</u>
Total contributions	<u>4,580,421</u>
Total additions	<u>12,965,545</u>

**Deductions**

**Benefits Paid**

Retired members	4,602,158
Spouses	212,112
Disabled members	225,046
Partial lump sum option	205,902
Death benefits	<u>4,000</u>
Total benefits paid	<u>5,249,218</u>

**Other Deductions**

Refunds of contributions	249,244
Administrative expenses	<u>141,472</u>
Total other deductions	<u>390,716</u>
Total deductions	<u>5,639,934</u>

**Net Increase** 7,325,611

**Net Position Restricted for Pensions, Beginning of Year** 101,192,338

**Net Position Restricted for Pensions, End of Year** \$ 108,517,949

# **Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri**

**A Component Unit of the City of Kansas City, Missouri  
Notes to Financial Statements**

**April 30, 2013**

## **Note 1: Summary of Significant Accounting Policies**

### ***Reporting Entity***

The Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri (the Plan) is considered a component unit of the City of Kansas City, Missouri financial reporting entity and included in the City's financial reports as a pension trust fund due to the nature of the Plan's reliance on funding from the City of Kansas City, Missouri. Accounting principles generally accepted in the United States of America require that the financial reporting entity include the primary government, organizations for which the primary government is financially accountable and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. Based on these criteria, there are no other organizations or agencies whose financial statements should be combined and presented with these basic financial statements.

### ***Measurement Focus and Basis of Accounting***

The Plan uses a fund to report on its financial position and the results of its operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. The Plan's fund is classified as a pension trust fund of fiduciary fund type. Pension trust funds account for assets held by the Plan in a trustee capacity, or as an agent on behalf of others and are accounted for on the flow of economic resources measurement focus and the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to the Plan are recognized when due and the employer has made a formal commitment to provide the contributions. Interest and dividend income are recorded when earned. Expenses are recorded when the corresponding liabilities are incurred. Realized gains and losses on security transactions are based on the difference between sales proceeds and carrying value of the securities, and are recognized on the transaction date. Benefits and refunds are recognized when due and payable in accordance with the terms of the Plan.

### ***Contributions***

Contributions totaling \$4,580,421 (\$3,283,458 employer and \$1,296,963 employee) were made during the Plan year. The annual required contribution rate (ARC) was determined through an actuarial valuation performed at April 30, 2012. As a percentage of payroll, the amount contributed did not equal the ARC. Significant actuarial assumptions used include (a) rate of return on the investment of present and future assets of 7.75% per year compounded annually, (b) projected salary increases based on years of service and (c) post-retirement benefit increase of 3% per year of the original base pension granted annually.

# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

A Component Unit of the City of Kansas City, Missouri

## Notes to Financial Statements

April 30, 2013

As a condition of participation in the Plan, members are required to contribute 5% of their salary to the Plan. The computed City contribution rate of 19.82% was the balance required to pay pensions and maintain the Plan on an actuarially sound basis and was expected to fund the normal cost and amortize the net unfunded actuarial accrued liability. For the year ended April 30, 2013, the City contributed at a rate of 13.14% of members' salaries.

The actual contributions by the City have been less than the rates recommended by the actuary for the past twelve years. The Plan is dependent upon the relationship of actual plan experience with the underlying actuarial assumptions and sufficient funding by the City to meet future cash flow needs.

The Plan's funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are sufficient to accumulate sufficient assets to pay benefits when due.

### Funded Status and Funding Progress

The funded status of the Plan as of April 30, 2012, the most recent actuarial valuation date, is as follows:

Actuarial Valuation Date	(a) Actuarial Value of Assets	(b) Actuarial Accrued Liability (AAL) Entry Age	(b - a) Unfunded AAL (UAAL)	(a/b) Funded Ratio	(c) Active Member Covered Payroll	[(b - a)/c] UAAL as a Percentage of Covered Payroll
4/30/2012	\$ 108,018,073	\$ 142,907,530	\$34,889,457	76%	\$ 25,255,423	138%

The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

### **Valuation of Investments and Income Recognition**

Marketable securities, including mutual funds, are stated at fair value. Securities traded on a national securities exchange are valued at the last reported sales price on the last business day of the Plan year; investments traded in the over-the-counter market and listed securities for which no sale was reported on that date are valued at the average of the last reported bid and ask prices.

For certain investments consisting of corporate bonds and notes that do not have an established fair value, the Plan has established a fair value based on yields currently available on comparable securities of issuers with similar credit ratings and quotations are obtained from brokerage firms or national pricing services.

# **Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri**

**A Component Unit of the City of Kansas City, Missouri**

## **Notes to Financial Statements**

**April 30, 2013**

The hedge fund of funds are invested in a non-marketable limited liability company which operates as a commodity pool, with the fund investing a majority of its assets in related commodity pools. The private equity partnerships and real estate funds consist primarily of non-marketable investments in various venture capital, corporate finance funds and private partnerships. These funds are primarily invested in the technology, communications, energy, commodities and real estate markets. A portion of these funds is also invested in foreign operations under certain partnership agreements. The Plan is obligated to pay certain capital commitments to the partnerships. These outstanding commitments totaled \$2,004,343 at April 30, 2013. The fair value of these investments is estimated based on the estimated fair values of the underlying securities. These estimates could change materially in the near term.

Securities, which are not traded on a national security exchange, are valued by the respective investment manager or other third parties based on similar sales.

Mortgages have been valued on the basis of their future principal and interest payments discounted at prevailing interest rates for similar instruments.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

### ***Administrative Expenses***

Actuarial, investment management and bank trustee fees and expenses are included in the Plan's expenses when incurred. These expenses are financed through investment income. The Kansas City, Missouri Police Department provides office space without any direct cost to the Plan.

### ***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 changes therein, disclosure of contingent assets and liabilities and the actuarial present value of accumulated plan benefits at the date of the financial statements. Actual results could differ from those estimates.

### ***Plan Tax Status***

The Plan obtained its most recent determination letter on November 18, 2010, in which the Internal Revenue Service stated that the Plan, as designed, was in compliance with the applicable requirements of the Internal Revenue Code and, therefore, not subject to tax.

# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

A Component Unit of the City of Kansas City, Missouri

## Notes to Financial Statements

April 30, 2013

### Note 2: Plan Description

The following description of the Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri provides only general information. Participants should refer to the Plan Statutes (Sections 86.1310 to 86.1640 RSMo) for a more complete description of the Plan's provisions.

The Plan is a single-employer, contributory, defined benefit plan established by the State of Missouri's General Assembly and administered by the Retirement Board of the Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri.

The Plan covers the regularly appointed full-time civilian employees of the Police Department of Kansas City, Missouri whose eligibility is effective on their hire date.

At April 30, 2013, the Plan's membership consisted of the following:

Retirees and beneficiaries currently receiving benefits	211
Terminated members entitled to but not yet receiving benefits	21
Active members	
Vested	440
Non-vested	118
	<hr/>
Total	790
	<hr/> <hr/>

The Plan provides retirement benefits and disability benefits. All benefits vest after five years of creditable service for those employees. A member is then entitled to an annual pension beginning at the latter of age 65, or 10<sup>th</sup> anniversary of employment, equal to 2% of final average compensation multiplied by the number of years of creditable service. A married member may elect an optional 100% joint and survivor annuity equivalent to the actuarial value of the normal pension for such member at the date of retirement.

The Plan provides active members three early retirement options:

- (A) Employee's total of age and years of service equals or exceeds 80 years.
- (B) Employee's age equals or exceeds 55 and years of service equals or exceeds 10 years.
- (C) Employee's age equals or exceeds 60 and years of service equals or exceeds five years but is not greater than 10 years.

Early retirement monetary reductions may be applicable to items (B) and (C) above.

# **Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri**

**A Component Unit of the City of Kansas City, Missouri**

## **Notes to Financial Statements**

**April 30, 2013**

When a member terminates employment prior to retirement, accumulated contributions of the member are refundable with interest. Such refunds result in forfeiture of all other benefits under the Plan. Members with five or more years of creditable service who terminate employment prior to retirement may choose to leave their accumulated contributions in the Retirement System fund and receive a pension upon the member's normal retirement date or upon the member's early retirement date subject to any applicable adjustment.

The Plan provides for duty disability pension based on 50% of the member's final average compensation for the remainder of his or her life or so long as the disability continues. The Plan also provides for non-duty disability benefits calculated at a minimum of 30% of the member's final average compensation for the remainder of his or her life or so long as the disability continues.

Upon the death of a member in service with less than five years of service, the Plan provides for refunding the accumulated member contributions plus interest to the member's surviving spouse. If a member dies in service and has at least five but less than twenty years of service, the member's surviving spouse may elect either the lump-sum payment of accumulated contributions above or a pension payable for life equal to 50% of the member's accrued pension at the date of death calculated for normal retirement. The surviving spouse's pension may be deferred until what would have been the member's earliest possible retirement date. If a member dies in service and has at least 20 years of service, the member's surviving spouse may elect either the lump-sum payment of accumulated contributions or, the larger of the 50% pension calculated for normal retirement or a pension determined on a joint and survivor's basis from the actuarial value of the member's accrued pension at the date of death. If there is no surviving spouse, the accumulated member contributions plus interest will be paid to the member's designated beneficiary.

An annual cost of living adjustment, not to exceed 3%, may be provided for members receiving benefits.

The Plan also provided a \$160 monthly supplemental retirement benefit to all retirees, disability recipients and eligible surviving spouses for the year ended April 30, 2013. Members and their surviving spouses were eligible if the member retired after August 28, 2007 and had 15 years of creditable service. Prior to August 28, 2007, all retirees, disability recipients and eligible surviving spouses were eligible for the supplemental retirement benefit.

The Plan is permitted by state statute to withhold amounts on behalf of members receiving benefits, including amounts for health and life insurance premiums. The Plan does not contract with insurance carriers on behalf of its members; instead, all insurance premiums are remitted through the Kansas City Police Department.

# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

A Component Unit of the City of Kansas City, Missouri

## Notes to Financial Statements

April 30, 2013

### Note 3: Deposits, Investments and Investment Income

#### *Deposits*

Custodial credit risk is the risk that, in the event of a bank failure, a government's deposits may not be returned to it. The Plan's deposit policy for custodial credit risk requires compliance with the provisions of state law.

State law requires collateralization of all deposits with federal depository insurance; bonds and other obligations of the U.S. Treasury, U.S. agencies or instrumentalities or the state of Missouri; bonds of any city, county, school district or special road district of the state of Missouri; bonds of any state; or a surety bond having an aggregate value at least equal to the amount of the deposits.

The Plan had no bank balances exposed to custodial credit risk at April 30, 2013.

#### *Investments*

For the year ended April 30, 2013, Northern Trust was the master custodian for substantially all of the securities of the Plan. The investments held by the Plan are managed by thirteen Board-appointed money managers. Each of the money managers has a different asset allocation based on Board-approved policy. The Plan may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities, real estate, partnerships, corporate bonds, commodities and equity securities.

#### *Securities Lending Transactions*

State statutes and the Plan's Board policies permit the Plan to use investments of the Plan to enter into securities lending transactions – loans of securities to broker-dealers and other entities for collateral with a simultaneous agreement to return the collateral for the same securities in the future.

The Plan has contracted with Northern Trust as its third-party lending agent to lend domestic equity and debt securities for cash collateral of not less than 102% of the market value and international debt and equity securities of not less than 105% of the market value. Contracts with the lending agent require it to indemnify the Plan if borrowers fail to return the securities, if the collateral is inadequate to replace the securities lent or if the borrowers fail to pay the Plan for income distributions by the securities' issuers while the securities are on loan; therefore, non-cash collateral is not recorded as an asset or liability on the financial statements.

Market value of securities loaned	\$ 26,760,995
Market value of cash collateral received from borrowers	\$ 27,317,981
Market value of non-cash collateral received from borrowers	-
Total market value of collateral	\$ 27,317,981



# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

A Component Unit of the City of Kansas City, Missouri

## Notes to Financial Statements

April 30, 2013

All securities loans can be terminated on demand by either the Plan or the borrower. The cash collateral received on each security loan was invested, in accordance with the Plan investment guidelines, in short-term funds. The maturities of the resulting investments generally match the maturities of the securities lending arrangement themselves. The Plan is not permitted to pledge or sell collateral received unless the borrower defaults.

At April 30, 2013, the Plan had the following investments and maturities:

Type	Fair Value	Maturities in Years				Loaned Under Securities Lending Agreements
		Less than 1	1 - 5	6 - 10	More than 10	
U.S. Treasury obligations	\$ 12,750,859	\$ 1,491,871	\$ 6,018,535	\$ 3,611,243	\$ 1,629,210	\$ 12,750,859
U.S. Agencies obligations	829,229	-	-	224,453	604,776	-
Corporate bonds	13,689,447	416,285	4,925,430	6,263,704	2,084,028	3,239,786
Government mortgage-backed securities	2,287,338	-	-	117,423	2,169,915	-
Money market mutual funds	3,880,663	3,880,663	-	-	-	-
Fixed income exchange-traded-funds	664,513	664,513	-	-	-	-
		<u>\$ 6,453,332</u>	<u>\$ 10,943,965</u>	<u>\$ 10,216,823</u>	<u>\$ 6,487,929</u>	
Common and preferred stocks	18,923,186					10,615,233
Equity exchange-traded-funds	11,800,001					139,929
Real estate funds	4,248,403					-
Partnerships - equity	2,747,498					-
Partnerships - fixed income	8,492,374					-
Emerging market equities	5,679,523					-
Commodities funds	4,871,795					-
Hedge fund of funds	10,539,206					-
Foreign equities	7,290,209					15,188
	<u>\$ 108,694,244</u>					<u>\$ 26,760,995</u>

**Interest Rate Risk** - The money market mutual funds and fixed income exchange-traded-funds are presented as an investment with a maturity of less than one year because they are redeemable in full immediately. The debt securities are presented in their respective category based on final maturity date. The Plan's investment policy does not specifically address exposure to fair value losses arising from rising interest rates.

# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

A Component Unit of the City of Kansas City, Missouri

## Notes to Financial Statements

April 30, 2013

**Credit Risk** - Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. It is the Plan's policy to limit its investments in corporate bonds to those that are rated BBB or better by credit rating agencies. The Plan's portfolio must have an average rating of A or better in the aggregate as measured by at least one credit rating agency. At April 30, 2013, the Plan's investments in corporate bonds were rated BBB+ or better by *Standard & Poor's*. At the same date, the Plan's investments in U.S. agencies obligations not directly guaranteed by the U.S. Government (including Federal National Mortgage Association, Federal Home Loan Banks & Federal Home Loan Mortgage Corporation) and in government mortgage-backed securities were rated A or better by *Standard & Poor's*. U.S. Treasury obligations were explicitly guaranteed by the U.S. Government. The Plan's investments in money market mutual funds and fixed income exchange-traded-funds were not rated by *Standard & Poor's*. These bond rating requirements do not apply to the high yield portion of the fixed income portfolio. The following table summarizes the Plan's fixed income portfolio exposure level and credit qualities at April 30, 2013:

Fixed Income Security Type	Fair Value April 30, 2013	S&P Weighted Average Credit Quality
U.S. Agencies obligations	\$ 829,229	AA+
Corporate bonds	13,689,447	A
Government mortgage-backed securities	2,287,338	AA+
Money market mutual funds	3,880,663	Not rated
Fixed income exchange-traded-funds	664,513	Not rated

**Custodial Credit Risk** - For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Plan will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. Consistent with the Plan's securities lending policy, \$26,760,995 was held by the counterparty that was acting as the Plan's agent in securities lending transactions.

**Concentration of Credit Risk** - The Plan limits the amount that may be invested in any one security at 5% to 15% of total plan assets.

**Foreign Currency Risk** - This risk relates to adverse effects on the fair value of an investment from changes in exchange rates. The Plan's investment policy permits investments in international equities, American Depository Receipts (ADRs), warrants, rights, 144A securities, convertible bonds and U.S. registered securities whose principal markets are outside of the United States. All foreign equities and emerging market equities held are denominated in U.S. dollars.

# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

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## Notes to Financial Statements

April 30, 2013

### **Investment Income**

Investment income for the year ended April 30, 2013 consisted of:

Interest and dividend income	\$ 1,989,414
Net increase in fair value of investments	6,979,496
	8,968,910
Less investment expense	637,468
	\$ 8,331,442

### **Note 4: Actuarial Methods and Assumptions**

An actuary from Cavanaugh Macdonald Consulting, LLC determines the actuarial present value of accumulated plan benefits, which is the amount that results from applying actuarial assumptions to adjust the accumulated plan benefits to reflect the time value of money (through discounts for interest) and the probability of payment (by means of decrements such as for death, disability, withdrawal or retirement) between the valuation date and the expected date of payment.

The information presented in the required supplemental schedules was determined as part of the actuarial valuations as of the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation date	April 30, 2012
Actuarial cost method	Individual entry age
Amortization method	Level percent closed
Equivalent single amortization period	15 years

#### Actuarial Assumptions

Investment rate of return	7.75% per annum
Inflation rate	3.00% per annum
Cost of living adjustments	3.00%, simple

# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

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## Notes to Financial Statements

April 30, 2013

Projected salary increases based on years of service as follows:

Years of Service	General Wage Growth	Merit and Longevity	Total
0	4.00%	5.75%	9.75%
1	4.00%	4.75%	8.75%
2	4.00%	3.75%	7.75%
3	4.00%	2.75%	6.75%
4	4.00%	2.25%	6.25%
5	4.00%	2.10%	6.10%
10	4.00%	1.60%	5.60%
15	4.00%	1.00%	5.00%
20	4.00%	0.55%	4.55%
25	4.00%	0.25%	4.25%

Actuarial accrued liability as of April 30, 2012:

Active employees accruing benefits	
Present value of future benefits	\$ 110,385,944
Present value of future normal costs	26,079,413
Total active employees accruing benefits	<u>84,306,531</u>
Retired and inactive members	
Members with deferred benefits	1,622,700
Members receiving benefits	53,595,142
Retired member supplemental benefits	3,383,157
Total retired and inactive members	<u>58,600,999</u>
Total actuarial accrued liability	142,907,530
Assets, at actuarial value	<u>108,018,073</u>
Unfunded actuarial accrued liability	<u>\$ 34,889,457</u>

The actuarial value of assets is calculated using an asset smoothing method. The difference between the actual and assumed investment returns on the market value of assets is recognized evenly over a five-year period.

# **Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri**

**A Component Unit of the City of Kansas City, Missouri**

## **Notes to Financial Statements**

**April 30, 2013**

### **Note 5: Risks and Uncertainties**

The Plan invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the statement of net position.

Plan contributions are made and the actuarial present value of accumulated plan benefits are reported based on certain assumptions pertaining to interest rates, inflation rates and employee demographics, all of which are subject to change. Due to uncertainties inherent in the estimation and assumption process, it is at least reasonably possible that changes in these estimates and assumptions in the near term would be material to the financial statements.

### **Note 6: Litigation**

The Plan is subject to claims and lawsuits that arise primarily in the ordinary course of operating a retirement system. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the net position of the Plan.

### **Note 7: Retirement Plan**

The Retirement System has a 408(k) SEP retirement plan covering its employees that meet certain eligibility requirements. The Retirement System's contributions to its employees' SEP are determined by the Retirement Board. Contributions to the SEP were \$8,411 for fiscal year 2013.

### **Note 8: Subsequent Events**

On June 28, 2013, House Bill 418 was signed into law by the Governor of Missouri. This bill which becomes effective August 28, 2013, creates a Tier II retirement plan for new employees and a Tier I retirement plan for current employees and retirees.

Civilian Employees' Retirees and Surviving Spouses (Tier I) – No change in current retirement benefits

Civilian Employees' Currently Active Members (Tier I) – No change in current retirement benefits

Civilian Employees' New Members (Tier II) – Retirement benefit formula remains at 2.0% of the final average salary multiplied by the years of creditable service. Final average salary is calculated over highest 3 years. Members are first eligible to retire with full benefits at age 67 with 5 years of service, age 62 with 20 years of service, or when age and service equals 85.

## **Required Supplementary Information**

# Civilian Employees' Retirement System of the Police Department of Kansas City, Missouri

A Component Unit of the City of Kansas City, Missouri  
Required Supplementary Information

## Schedule of Funding Progress

April 30, 2013

Actuarial Valuation Date	(a) Actuarial Value of Assets	(b) Actuarial Accrued Liability (AAL) Entry Age	(b - a) Unfunded AAL (UAAL)	(a/b) Funded Ratio	(c) Active Member Covered Payroll	[(b - a)/c] UAAL as a Percentage of Covered Payroll
4/30/2007	\$ 89,110,860	\$ 110,394,115	\$ 21,283,255	81%	\$ 25,472,341	84%
4/30/2008	97,989,985	117,626,995	19,637,010	83%	27,045,762	73%
4/30/2009	86,332,962	124,990,468	38,657,506	69%	27,580,796	140%
4/30/2010	100,515,970	131,222,564	30,706,594	77%	26,136,353	117%
4/30/2011	102,522,611	137,040,461	34,517,850	75%	25,238,690	137%
4/30/2012	108,018,073	142,907,530	34,889,457	76%	25,255,423	138%

## Schedule of Employer Contributions

Year Ended April 30	Annual Required Contributions	Percentage Contributed
2008	\$ 4,202,987	80%
2009	4,322,860	80%
2010	4,013,807	83%
2011	5,412,676	59%
2012	4,944,371	64%
2013	5,202,401	63%

## **Supplementary Information**



**Civilian Employees' Retirement System of the  
Police Department of Kansas City, Missouri**

A Component Unit of the City of Kansas City, Missouri

**Supplementary Information**

**Schedule of Expenses**

**Year Ended April 30, 2013**

**Investment Expenses**

Bank custodial fees and expenses	\$	80,459
Financial management expenses		538,336
Financial consultation		18,673
		<hr/>
Total	\$	637,468
		<hr/> <hr/>

**Administrative Expenses**

Salaries and payroll taxes	\$	53,685
Legal		13,835
Audit		10,772
Actuarial fees		53,521
Printing and office expense		3,567
Postage		104
Legislative consultation		4,015
Board meeting		152
Board election		929
Other		892
		<hr/>
Total	\$	141,472
		<hr/> <hr/>

**Civilian Employees' Retirement System of the  
Police Department of Kansas City, Missouri**

A Component Unit of the City of Kansas City, Missouri  
Supplementary Information

**Schedule of Revenues by Source and Expenses by Type  
Years Ended April 30, 2008 through 2013**

Fiscal Year Ended	Revenues by Source			Total
	Employee Contributions	Employer Contributions	Investment Income (Loss)	
2008	\$ 1,285,869	\$ 3,372,411	\$ (63,658)	\$ 4,594,622
2009	1,338,180	3,470,682	(25,282,608)	(20,473,746)
2010	1,311,963	3,329,727	19,545,133	24,186,823
2011	1,383,479	3,185,041	11,852,884	16,421,404
2012	1,224,736	3,146,124	(613,908)	3,756,952
2013	1,296,963	3,283,458	8,385,124	12,965,545

Fiscal Year Ended	Expenses by Type			Total
	Benefits	Administrative Expenses		
		General	Refunds	
2008	\$ 3,431,959	\$ 111,993	\$ 218,281	\$ 3,762,233
2009	3,716,269	123,561	381,590	4,221,420
2010	4,519,593	117,579	269,586	4,906,758
2011	4,875,154	116,767	131,072	5,122,993
2012	4,786,286	117,078	183,861	5,087,225
2013	5,249,218	141,472	249,244	5,639,934