

Note I - Summary of Significant Accounting Policies

The accounting policies of the City of Midland, Michigan (the "City") conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The following is a summary of the significant accounting policies used by the City of Midland, Michigan:

Reporting Entity

The City is a municipal corporation governed by an elected five-member City Council (the "Council"), which biannually selects one of its members to serve as mayor. The City operates under a council-manager form of government. The accompanying financial statements present the City and its component units, entities for which the City is considered to be financially accountable. Blended component units, although legally separate entities, are in substance part of the City's operations, and data from these units are therefore combined with data from the primary government.

Blended Component Unit

Midland Downtown Development Authority - The Midland Downtown Development Authority (MDDA) was established in 1987 for the purpose of maintaining and renovating the downtown Midland area. The MDDA is administered by a 13-person board, which is appointed by the City Council. Funding for the MDDA is provided by a two-mill levy on property within the district and by tax increment financing. All projects initiated by the MDDA are considered public improvements to the City's infrastructure, parks, or parking facilities. Since the MDDA is used exclusively as a financing source for City facilities, it has been blended into the financial statements of the City as a Special Revenue Fund. The MDDA has a June 30 year end.

Joint Ventures

Saginaw-Midland Municipal Water Supply Corporation - The Saginaw-Midland Municipal Water Supply Corporation (SMMWSC), located approximately 13.5 miles east of the city of Midland, is an authority incorporated by the cities of Midland and Saginaw, Michigan, under Act 233, Public Acts of Michigan, 1955, as amended. The SMMWSC is administered by a six-member board of trustees, each community appointing three members, and is empowered to prepare, adopt, and submit to the legislative bodies of each municipality an annual budget covering estimated revenues, proposed expenditures, and the necessary funds required from each municipality for the next fiscal year.

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 1 - Summary of Significant Accounting Policies (Continued)

Funding for the acquisition of property and for the development and improvement of the water supply system is provided by sale of SMMWSC negotiable bonds secured by the full faith and credit of each municipality in a ratio based upon predetermined capacity reserves; 20/43rds for the City of Midland and 23/43rds for the City of Saginaw. Funding for operations is provided by sale of water to the two communities on a consumption basis. The City's equity in the SMMWSC is accounted for in the Water Fund, which is included in the business-type activities column of the statement of net assets.

A summary of the financial information for the year ended June 30, 2008 follows:

Total assets	\$ 38,549,606
Total liabilities	20,549,237
Equity - City of Midland	8,372,265
Equity - City of Saginaw	9,628,104
Total revenues	5,101,243
Total expenses	4,203,919
Net income	897,324

At June 30, 2008, total outstanding bonded debt of the SMMWSC was \$20,050,000. The City was obligated for \$9,325,581 of this total.

Midland City/County Joint Building Authority - The City's ownership interest in the Midland City/County Joint Building Authority is accounted for in the governmental activities column of the statement of net assets. The Authority was created as a financing vehicle for the Midland Law Enforcement Center. The Law Enforcement Center is leased from the Joint Building Authority (JBA) by the City of Midland Police Department, the Midland County Sheriff Department, and the Midland County Central Dispatch Authority. The JBA is governed by a three-person board with the City and County each appointing one member and with the third member being mutually appointed. Additional information concerning the Joint Building Authority and its lease with the City is detailed in Note 8 - Leases.

General - Complete financial statements, which are audited for the Saginaw-Midland Municipal Water Supply Corporation and the Midland City/County Joint Building Authority, are available from the city clerk's office.

The City is unaware of any circumstances that would cause an additional benefit or burden to the participating parties in the near future for any of the above organizations.

Note I - Summary of Significant Accounting Policies (Continued)

Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the primary government and its component units. As a general rule, the effect of interfund activity has been removed from these statements. Exceptions to this general rule are charges between the City's water and sewer function and various other functions of the City. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned. Governmental activities, normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual Enterprise Funds are reported as separate columns in the fund financial statements.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Note I - Summary of Significant Accounting Policies (Continued)

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay current period liabilities.

For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, expenditures relating to compensated absences, and claims and judgments are recorded only when payment is due.

Property taxes, franchise fees, licenses, interest, and special assessments are susceptible to accrual. Sales and motor fuel taxes collected and held by the State at fiscal year end on behalf of the City are also recognized as revenue of the current fiscal period. Other receipts become measurable and available when cash is received by the City and are recognized as revenue at that time.

The City reports the following major governmental funds:

- The General Fund is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- The Major Street Fund accounts for state-shared revenues relating to construction activities, repairs, and maintenance of all major streets and trunklines.

The City reports the following major proprietary funds:

- The Water Fund accounts for the operation and maintenance of the City's water supply system, capital additions, and retirement of bonds.
- The Wastewater Fund accounts for the operation and maintenance of the City's sewage disposal system, capital additions and improvements, and retirement of bonds.
- The Landfill Fund accounts for the operation and maintenance of the City's trash and garbage disposal system.
- The Civic Arena Fund accounts for the operations and maintenance of the City's ice arena facility, capital additions, and retirement of debt.

Note I - Summary of Significant Accounting Policies (Continued)

- The Real Estate Rental Fund accounts for the operation and maintenance of the City's various senior housing rental properties.

Additionally, the City reports the following Internal Service Funds:

- The Information Services Fund accounts for the operations of the City's Information Services Department.
- The Geographical Information Systems Fund accounts for operations of the City's geographic information systems.
- The Equipment Revolving Fund accounts for the rental charges of City-owned equipment to other City departments.
- The Municipal Service Center Fund accounts for the operations of the City's Service Center building.
- The Property and Liability Insurance Fund accounts for insurance expenses resulting from property and liability claims.
- The Health Insurance Fund accounts for revenues and expenses of the City's self-insurance program for health insurance along with the contributions toward postemployment healthcare benefits.
- The Special Assessment Revolving Fund accounts for the funding of the City's special assessment projects.
- The Municipal Service Annex Fund accounts for the operations of the City's Municipal Service Annex building.

Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Because these funds represent trust responsibilities of the City, these assets are restricted in purpose and do not represent discretionary assets of the City. The City's only fiduciary fund in the current year is the Police and Fire Retirement Fund. The City's fiduciary activities are reported in separate statements of fiduciary net assets and changes in fiduciary net assets.

Note 1 - Summary of Significant Accounting Policies (Continued)

The Agency Funds account for assets held by the City in a trustee capacity. Agency funds are custodial in nature (assets equal liabilities) and do not involve the measurement of results of operations. The Shopping Area Redevelopment Authority Fund accounts for special assessments charged to property owners within the authority district for promotion of the area. The City acts as an agent for the financial management of this authority. The Tax Collection Fund is used to account for taxes collected on behalf of other governmental units. The DDA Façade Improvements Fund accounts for loans to businesses in the Downtown Development Authority business district. The funding for these loans was provided by a grant from the Rollin M. Gerstacker Foundation.

Private sector standards of accounting issued prior to December 1, 1989 are generally followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with the standards of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private sector guidance for their business-type activities and Enterprise Funds, subject to this same limitation. The City has elected not to follow subsequent private sector guidance.

Amounts reported as program revenue include (1) charges to customers or applicants for goods, services, or privileges provided; (2) operating grants and contributions; and (3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenue rather than as program revenue. Likewise, general revenue includes all taxes.

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's proprietary funds are charges to customers for sales and services. The City also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. The portion intended to recover the cost of infrastructure is recognized as nonoperating revenue. Operating expenses for the proprietary funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenue and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Note I - Summary of Significant Accounting Policies (Continued)

Assets, Liabilities, and Net Assets or Equity

Bank Deposits and Investments - The City's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. Investments for the City, as well as for its component unit, are reported at fair value.

Receivables and Payables - Transactions between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "interfund receivable/payables" or "advances to/from other funds." All other outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances."

Property tax receivables are shown net of an allowance for uncollectible amounts totaling \$14,300. The property tax receivable allowance at June 30, 2008 equals 100 percent of outstanding property taxes over two years old, 50 percent of outstanding property taxes two years old, and 10 percent of outstanding property taxes one year old.

Properties are assessed annually as of December 31, and property taxes are billed and become a lien on July 1 of the following year. These taxes are due on September 15 with a final collection date of February 28 before they are added to the county tax roll. The City also bills and collects an amount each December, primarily for schools, county, and college. Also included in the December billing is a tax administration fee, which is revenue to the City. The December billing is due on February 14 with a final collection date of February 28. Penalties and interest are assessed on payments received after the due date.

The 2007 taxable valuation of the City totaled \$2,525,202,300, on which ad valorem taxes levied consisted of 11.0 mills for the City's operating purposes, 1.0 mills for Library services, and .24 mills for debt levies. This resulted in \$27,434,804 for operating, \$2,545,106 for the Library, and \$602,075 for debt service. The ad valorem taxes levied are recognized in the respective General, Special Revenue, and Water and Sewer Funds financial statements as taxes receivable - current or as tax revenue.

Inventories and Prepaid Items - Inventories are valued at cost on an average cost method. The costs of governmental fund-type inventories are recorded as expenditures when consumed rather than when purchased.

Note I - Summary of Significant Accounting Policies (Continued)

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements.

Restricted Assets - Certain resources set aside for debt service on the City's Enterprise Fund revenue bonds are classified as restricted assets on the balance sheet because their use is limited by applicable bond covenants. Additionally, certain resources set aside for closure and postclosure costs for the enterprise landfill operation are classified as restricted assets because their use is limited by applicable state regulations.

Capital Assets - Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items) are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the City as assets with an initial individual cost of more than \$1,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Projects with total costs of less than \$10,000 are considered repairs and are expensed in the year incurred. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Property, plant, and equipment are depreciated using the straight-line method over the following estimated useful lives:

Buildings	50 years
Building improvements	20 years
Land improvements	50 years
Roads and sidewalks	20-30 years
Water and sewer distribution systems	50 years
Vehicles	3-10 years
Equipment	10 years
Library circulation material	5 years
Computer equipment	4 years

Note I - Summary of Significant Accounting Policies (Continued)

Compensated Absences - It is the City's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. Vacation pay is fully vested when earned, and sick pay is conditionally vested upon completion of 10 years of service. Upon retirement, employees are paid accumulated vacation and one-half of unused sick days at their hourly rate as of their retirement date.

All sick and vacation pay is accrued when incurred in the government-wide and proprietary fund financial statements. A liability for the entire amount, current and long-term, is accrued in the government-wide and proprietary financial statements. A liability for these amounts is reported in governmental funds only for employee terminations as of year end.

Long-term Obligations - In the government-wide financial statements and the proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund-type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts are reported as other financing uses. Issuance costs are reported as debt service expenditures.

Fund Equity - In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

When an expense has been incurred for purposes for which both restricted and unrestricted net assets are available, it is the City's policy to first apply restricted resources.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) 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 these estimates.

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 2 - Stewardship, Compliance, and Accountability

State Construction Code Act - The City oversees building construction, in accordance with the State's Construction Code Act, including inspection on building construction renovation to ensure compliance with the building codes. The City charges fees for these services. Beginning January 1, 2000, the law requires that collection of these fees be used only for construction code costs, including an allocation of estimated overhead costs. A summary of the current year activity and the cumulative shortfall generated since January 1, 2000 follows:

Shortfall at July 1, 2007		\$	(403,107)
Current year building permit revenue			435,298
Related expenses:			
Direct costs	\$	384,075	
Estimated indirect costs		<u>23,045</u>	
Total construction code expenses			<u>407,120</u>
Cumulative shortfall at June 30, 2008		\$	<u>(374,929)</u>

Note 3 - Deposits and Investments

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

Note 3 - Deposits and Investments (Continued)

The City Council has designated nine financial institutions for the deposit of local unit funds. The investment policy adopted by the City in accordance with Public Act 20 of 1943 (as amended) authorizes investments in U.S. Treasuries, U.S. agencies and instrumentalities, certificates of deposit, commercial paper (meeting certain rating and maturity requirements), repurchase agreements, investment pools, bankers' acceptances of U.S. banks, and mutual funds. Repurchase agreements must be signed with the bank or dealer and must contain provisions comparable to those outlined in the Public Security Association's model Master Repurchase Agreement. The treasurer may invest in investment pools organized under the Surplus Funds Investment Pool Act of 1982 and under the Urban Cooperation Act of 1967.

For mutual funds, the treasurer may invest in funds registered under the Investment Company Act of 1940. This authorization is limited to securities whose intention is to maintain a net asset value of \$1.00 per share and investment vehicles that are legal for direct investment by a public corporation.

The above-mentioned City investment policy applies to all financial assets of the City except for its Post Retirement Health Care and the Police and Fire Retirement System Fund, which are organized and administered separately. Investments are made pursuant to provisions of the Public Employee Retirement System Investment Act of 1965. Michigan Public Act 314 of 1965 and Michigan Public Act 149 of 1999, as amended, authorize investments in certain reverse repurchase agreements, stocks, diversified investment companies, annuity investment contracts, real estate leased to public entities, mortgages, real estate (if the trust fund's assets exceed \$250 million), debt or equity of certain small businesses, certain state and local government obligations, and certain other specified investment vehicles.

The City'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 City's deposits may not be returned to it. The City does not have a deposit policy for custodial credit risk. At year end, the City had \$45,441,703 of bank deposits (certificates of deposit, checking, and savings accounts) that were uninsured and uncollateralized. The City 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 City evaluates each financial institution with which it deposits its funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Note 3 - Deposits and Investments (Continued)

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's investment policy does not restrict investment maturities, other than commercial paper which can only be purchased with a 270-day maturity. At year end, the average maturities of investments are as follows:

Investment	Fair Value	Weighted Average Maturity (Years)
Commercial paper	\$ 10,424,134	0.159
Government bonds	1,545,915	3.567
Corporate bonds	7,591,831	18.150
International bonds	622,519	16.965

Credit Risk

State law limits investments in commercial paper to the top two ratings issued by nationally recognized statistical rating organizations. The City's investment policy does not further limit its investment choices. As of year end, the credit quality ratings of debt securities (other than the U.S. government) are as follows:

Investment	Fair Value	Rating	Organization
Interlocal Agreement Fund	\$ 256,347	AAA- VI+	Fitch
Bank Investment Pooled Funds	409,872	Not Rated	N/A
Commercial paper	2,250,413	A1	S & P
Commercial paper	8,173,721	A1 +	S & P
Money market funds	1,247,502	AAA	S & P
Money market funds	9,136,523	Not Rated	N/A
Mutual funds	2,623,525	Not Rated	N/A
Corporate bonds	93,975	AAA	S & P
Corporate bonds	415,063	AA-	S & P
Corporate bonds	716,353	A+	S & P
Corporate bonds	592,175	A	S & P
Corporate bonds	1,736,815	A-	S & P
Corporate bonds	1,654,044	BBB+	S & P
Corporate bonds	949,288	BBB	S & P
Corporate bonds	591,344	BBB-	S & P
Corporate bonds	520,650	BB+	S & P
Corporate bonds	212,519	BB	S & P
Corporate bonds	109,606	Not Rated	N/A
International bonds	205,800	BBB	S & P
International bonds	416,719	BBB-	S & P

Note 3 - Deposits and Investments (Continued)

Declines in Investment Values

Subsequent to year end, the City's investment portfolio for its Police and Fire Retirement Fund has incurred a significant decline in the market value of the plan's assets, consistent with the general decline in financial markets. As of October 31, 2008, the latest valuation date available, the plan's portfolio had lost approximately \$12,800,000 or 24 percent of the net asset balance as of June 30, 2008. However, because the values of individual investments fluctuate with market conditions, the amount that will ultimately be recognized in future periods cannot be determined.

Note 4 - Interfund Transfers, Receivables, and Payables

Interfund transfers reported in the fund statements for the year ended June 30, 2008 were as follows:

	Transfers Out					
	General Fund	Major Street Fund	Local Street Fund	Storm Water Mgmt. Fund	Community Develop Block Grant	Downtown Develop. Auth. Fund
Transfers in:						
General Fund	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Local Street Fund	-	1,203,000	-	-	198,126	-
Storm Water Mgmt. Fund	429,531	87,766	103,586	-	-	-
Grace A. Dow Library Fund	543,961	-	-	-	-	-
Midland Community Television Fund	15,000	-	-	-	-	-
Dial-A-Ride Fund	562,459	-	-	-	-	-
Downtown Develop. Auth. Fund	-	-	-	-	-	-
Debt Fund	201,881	-	-	-	-	103,025
Capital Projects Fund	307,299	-	-	15,000	-	3,300
Parking Fund	-	-	-	-	-	45,000
Wastewater Fund	-	101,905	-	-	40,578	-
Water Fund	-	59,997	-	-	-	-
Civic Arena	200,000	-	-	-	-	-
Golf Course Fund	20,263	-	-	-	-	-
Geographic Info Sys Fund	177,500	31,250	31,250	-	-	-
Equipment Revolving Fund	-	-	-	-	-	-
Municipal Services Annex Fund	40,051	-	-	-	-	-
Midland Housing Fund	77,138	-	-	-	30,174	-
Total	\$ 2,575,083	\$ 1,483,918	\$ 134,836	\$ 15,000	\$ 268,878	\$ 151,325

Note 4 - Interfund Transfers, Receivables, and Payables (Continued)

The transfers from the General Fund to the Grace A. Dow Memorial Library Fund, the Midland Community Television Fund, the Dial-A-Ride Fund, the Civic Arena Fund, and the Geographical Information Systems Fund represent the use of unrestricted resources to finance these programs, in accordance with budgetary authorizations. The transfer from the General Fund to the Capital Projects Fund represents funding of construction projects from unrestricted resources, in accordance with budgetary authorizations. The transfer from the Major Street Fund to the Local Street Fund represents the sharing of gas and weight tax revenues, in accordance with Act 51. The transfer from the Debt Fund to the Wastewater Fund is necessary to transfer an additional millage for debt retirement to the Wastewater Fund, which is the fund that accounts for the related debt. The transfers from the Community Development Block Grant Fund to the Local Street Fund, the Wastewater Fund, and the Housing Fund represent the use of grant funds for construction related projects, in accordance with budgetary authorizations.

Transfers Out					
Debt Fund	Capital Projects Fund	Wastewater Fund	Water Fund	Golf Course Fund	Total
\$ -	\$ 54,414	\$ -	\$ -	\$ -	\$ 54,414
-	-	-	-	-	1,401,126
-	-	-	-	-	620,883
-	-	-	-	-	543,961
-	-	-	-	-	15,000
-	-	-	-	-	562,459
-	54,917	-	-	-	54,917
-	-	-	-	-	304,906
-	-	-	-	-	325,599
-	-	-	-	-	45,000
829,687	-	-	-	-	972,170
-	-	-	-	-	59,997
-	-	-	-	-	200,000
-	-	3,960	-	-	24,223
-	-	70,000	120,000	-	430,000
-	-	-	-	49,800	49,800
-	-	-	70,000	-	110,051
-	-	-	-	-	107,312
<u>\$ 829,687</u>	<u>\$ 109,331</u>	<u>\$ 73,960</u>	<u>\$ 190,000</u>	<u>\$ 49,800</u>	<u>\$ 5,881,818</u>

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 4 - Interfund Transfers, Receivables, and Payables (Continued)

The composition of interfund balances as of June 30, 2008 was as follows:

Receivable Fund	Payable Fund	Amount
General	Community Development Block Grant	\$ 95,243
General	Currie Municipal Golf Course	652,950
General	Dial-A-Ride	24,079
General	Civic Arena	21,920
Community Development Block Grant	Midland Housing	137,809
Landfill	Civic Arena	1,047,656
Total		<u>\$ 1,979,657</u>

The balance owing from the Midland Housing Fund to the Community Development Block Grant (CDBG) Fund represents remaining balances on mortgages subsidized by the CDBG Fund. The remaining interfund balances resulted from loans made for working capital purposes.

Note 5 - Capital Assets

Capital asset activity for the year ended June 30, 2008 was as follows:

Governmental Activities	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets not being depreciated:				
Land	\$ 5,075,219	\$ 295,475	\$ -	\$ 5,370,694
Construction in progress	4,136,272	2,416,199	3,196,899	3,355,572
Total capital assets not being depreciated	9,211,491	2,711,674	3,196,899	8,726,266
Capital assets being depreciated:				
Major and local roads	49,833,434	4,773,099	-	54,606,533
Sidewalks	3,207,583	797,011	-	4,004,594
Buildings	24,668,269	190,835	-	24,859,104
Land improvements	21,633,431	179,931	-	21,813,362
Library circulation materials	6,725,554	488,912	1,275,113	5,939,353
Equipment	8,610,151	419,768	25,005	9,004,914
Vehicles	14,682,938	1,661,738	340,436	16,004,240
Total capital assets being depreciated	129,361,360	8,511,294	1,640,554	136,232,100
Total capital assets before depreciation	138,572,851	11,222,968	4,837,453	144,958,366
Less accumulated depreciation:				
Major and local roads	20,438,038	2,175,843	-	22,613,881
Sidewalks	1,851,204	159,584	-	2,010,788
Buildings	9,688,675	509,722	-	10,198,397
Land improvements	4,759,511	437,847	-	5,197,358
Library circulation materials	5,473,359	528,125	1,275,113	4,726,371
Equipment	6,430,367	522,381	18,116	6,934,632
Vehicles	8,307,119	1,387,920	326,418	9,368,621
Subtotal	56,948,273	5,721,422	1,619,647	61,050,048
Net capital assets being depreciated	72,413,087	2,789,872	20,907	75,182,052
Net governmental activities capital assets	\$ 81,624,578	\$ 5,501,546	\$ 3,217,806	\$ 83,908,318

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 5 - Capital Assets (Continued)

Business-type Activities	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets not being depreciated:				
Land	\$ 2,378,954	\$ 128,960	\$ -	\$ 2,507,914
Construction in progress	<u>2,382,931</u>	<u>1,532,216</u>	<u>2,192,203</u>	<u>1,722,944</u>
Total capital assets not being depreciated	4,761,885	1,661,176	2,192,203	4,230,858
Capital assets being depreciated:				
Water and sewer lines	76,861,263	1,833,575	-	78,694,838
Buildings and building improvements	79,073,983	591,834	-	79,665,817
Land improvements	6,550,021	244,605	-	6,794,626
Landfill improvements	9,894,017	2,693,715	-	12,587,732
Equipment	5,544,647	557,678	21,232	6,081,093
Vehicles	<u>731,511</u>	<u>7,500</u>	<u>-</u>	<u>739,011</u>
Total capital assets being depreciated	178,655,442	5,928,907	21,232	184,563,117
Less accumulated depreciation:				
Water and sewer lines	26,531,400	1,546,680	-	28,078,080
Buildings and building improvements	30,812,183	1,606,589	-	32,418,772
Land improvements	1,264,196	134,112	-	1,398,308
Landfill improvements	7,242,980	302,620	-	7,545,600
Equipment	3,329,850	428,068	12,333	3,745,585
Vehicles	<u>424,120</u>	<u>47,329</u>	<u>-</u>	<u>471,449</u>
Total accumulated depreciation	69,604,729	4,065,398	12,333	73,657,794
Net capital assets being depreciated	<u>109,050,713</u>	<u>1,863,509</u>	<u>8,899</u>	<u>110,905,323</u>
Net business-type activities capital assets	<u>\$ 113,812,598</u>	<u>\$ 3,524,685</u>	<u>\$ 2,201,102</u>	<u>\$ 115,136,181</u>

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 5 - Capital Assets (Continued)

Depreciation expense charged to programs of the government follows:

Governmental activities:

General government	\$ 387,051
Public safety	437,853
Public works	3,374,548
Sanitation	44,794
Parks and recreation	460,301
Library	748,335
Airport	44,414
Transportation	201,318
Other functions	<u>22,808</u>
Total governmental activities	<u>\$ 5,721,422</u>

Business-type activities:

Civic Arena	\$ 328,094
Landfill	424,722
Real estate rental	452,214
Currie municipal golf course	130,171
Parking	38,383
Wastewater	1,475,472
Water	<u>1,216,342</u>
Total business-type activities	<u>\$ 4,065,398</u>

Construction Commitments - The City has active construction projects as of June 30, 2008. The projects include sidewalk, street, and water system projects. At year end, the City's commitments with contractors are as follows:

	<u>Spent to Date</u>	<u>Remaining Commitment</u>
Sidewalk projects	\$ 74,522	\$ 52,111
Street projects	454,164	923,611
Water system projects	<u>289,766</u>	<u>50,403</u>
Total	<u>\$ 818,452</u>	<u>\$ 1,026,125</u>

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 6 - Restricted Assets

Enterprise Funds - Cash and cash equivalents are restricted within the Water and Wastewater Funds for future debt service obligations in the amounts of \$1,244,084 and \$952,085, respectively. Within each of these funds, an offsetting liability “payable from restricted assets” designates the separation of these assets from unreserved assets. In addition, the Landfill Fund has \$1,794,332 of restricted assets that are for closure and postclosure costs.

Note 7 - Deferred Revenue

Governmental funds report deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received but not yet earned. As of June 30, 2008, the various components of deferred revenue are as follows:

	<u>Unavailable</u>	<u>Unearned</u>
Grant money earned but not received -		
Transportation Fund	\$ 84,883	\$ 806
Trust deeds	<u>-</u>	<u>1,309,044</u>
Total deferred/unearned for governmental funds	<u>\$ 84,883</u>	<u>\$ 1,309,850</u>

Note 8 - Leases

Operating Leases

The City leases its police administration facility and landfill equipment under non-cancelable operating leases. Total costs for such leases were \$490,590 for the year ended June 30, 2008. According to the terms of its lease with the Midland City/County Joint Building Authority, the City’s obligation for operating leases amounts to 64.8 percent of total operating expenses of the police administration facility.

Note 8 - Leases (Continued)

The future minimum lease payments for these leases, including estimates of obligations under the police administration facility lease areas, are as follows:

Years Ending June 30	Amount
2009	\$ 441,002
2010	446,911
2011	245,647
2012	215,220
2013	221,677
2014-2018	<u>1,212,219</u>
Total	<u>\$ 2,782,676</u>

Capital Leases

The City has entered into a lease agreement with the Midland City/County Joint Building Authority as lessee for financing the construction of police administration facilities. This lease qualifies as a capital lease for accounting purposes and, therefore, has been recorded at the present value of the future minimum lease payments as of the inception date. The gross amount of the capital lease, \$2,985,679, has been capitalized as a building. The total cost of this lease was \$215,495 for the year ended June 30, 2008. Payments under this lease agreement for the year ended June 30, 2008 totaled \$215,495, including \$34,923 of interest charges.

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 8 - Leases (Continued)

The future minimum lease obligation and net present value as of June 30, 2008 are as follows:

Years Ending <u>June 30</u>	<u>Amount</u>
2009	\$ 207,530
2010	215,703
2011	223,005
2012	212,621
2013	<u>215,457</u>
Total minimum lease payments	1,074,316
Less amount representing interest	<u>90,665</u>
Present value of minimum lease payments	<u><u>\$ 983,651</u></u>

Note 9 - Long-term Debt

The City issues bonds to provide for the acquisition and construction of major capital facilities. General obligation bonds, which are direct obligations and pledge the full faith and credit of the City, have been issued for both governmental and business-type activities. Revenue bonds involve a pledge of specific income derived from the acquired or constructed asset to pay debt service and have been issued for business-type activities. Also, for the governmental activities, compensated absences are generally liquidated by the General Fund.

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 9 - Long-term Debt (Continued)

Long-term obligation activity can be summarized as follows:

	Interest Rate Ranges	Principal Maturity Ranges	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental Activities							
<u>General obligation bonds</u>							
1992 Downtown Development Amount of issue: \$600,000 Matured in September 2007	5.65% - 6.05%	\$50,000 - \$100,000	\$ 100,000	\$ -	\$ (100,000)	\$ -	\$ -
Capital lease (Note 8)			1,164,223	-	(180,572)	983,651	178,018
Total bond and capital lease			1,264,223	-	(280,572)	983,651	178,018
<u>Other long-term obligations</u>							
Compensated absences			3,821,560	119,207	(317,534)	3,623,233	1,897,569
Property tax refund liability (Note 17)			29,830,685	20,163,841	(13,692,799)	36,301,727	36,301,727
Total other long-term obligations			33,652,245	20,283,048	(14,010,333)	39,924,960	38,199,296
Total governmental activities			34,916,468	20,283,048	(14,290,905)	40,908,611	38,377,314
Business-type Activities							
<u>General obligation bonds</u>							
2001 Sewer Construction: Amount of issue: \$13,600,000 Maturing through May 2021	4.50% - 5.25%	\$375,000 - \$1,100,000	2,275,000	-	(525,000)	1,750,000	550,000
2001 Sewer Construction - State Revolving Fund: Amount of issue: \$5,130,000 Borrowed as of 6/30/03: \$4,688,961 Maturing through April 2022	2.50%	\$205,000 - \$320,000	3,924,063	-	(230,000)	3,694,063	235,000
2004 Civic Arena Amount of issue: \$6,500,000 Maturing through May 2030	2.50% - 4.75%	\$135,000 - \$490,000	5,585,000	-	(490,000)	5,095,000	135,000
Less deferred charge on defeasance			(576,349)	-	(41,168)	(535,181)	-
2005 Sewer Refunding Bonds Amount of issue: \$9,480,000 Maturing through May 2021	2.95% - 4.15%	\$135,000 - \$490,000	9,420,000	-	(60,000)	9,360,000	70,000
<u>Revenue bonds</u>							
2000 Water Rev Refunding: Amount of issue: \$12,190,000 Maturing through April 2010	4.80% - 5.30%	\$1,155,000 - \$1,390,000	3,465,000	-	(1,155,000)	2,310,000	1,155,000
Total bonds obligations			24,092,714	-	(2,501,168)	21,673,882	2,145,000
<u>Other long-term obligations</u>							
Compensated absences			784,615	134,573	(61,532)	857,656	399,117
Landfill closure and postclosure (Note 10)			3,018,000	72,000	-	3,090,000	-
Total other long-term obligations			3,802,615	206,573	(61,532)	3,947,656	399,117
Less current portion payable from restricted assets (Note 6)			1,970,000	40,000	-	2,010,000	2,010,000
Total business-type activities			25,925,329	166,573	(2,562,700)	23,611,538	534,117
Total governmental and business-type activities			<u>\$ 60,841,797</u>	<u>\$ 20,449,621</u>	<u>\$ (16,853,605)</u>	<u>\$ 64,520,149</u>	<u>\$ 38,911,431</u>

Note 9 - Long-term Debt (Continued)

The 1992 Downtown Development Bonds were issued pursuant to a tax increment financing plan and development plan for the Midland Downtown Development Area, under authority of Act 197, Public Act of Michigan, 1975, as amended. The bonds were used to finance a portion of the Downtown Streetscape Project, and were paid in full in September 2007.

The 2001 Sewer Construction Bonds were approved by the voters in a general election held on February 22, 2000. The City Council has approved a resolution to levy a millage to pay approximately 60 percent of the principal and interest cost of these bonds. The 40 percent balance of the obligation is to be repaid by fees from the users of the municipal sanitary sewage collection and treatment system. The proceeds are being used for construction of sewer facilities recorded as construction in progress in the Wastewater Fund. On September 12, 2005, General Obligation Unlimited Tax Bonds were issued to refund \$9,025,000 of the outstanding bond.

On December 3, 2001, the City Council authorized issuance of general obligation limited tax bonds, series 2001, in the principal sum not to exceed \$5,130,000. The purpose of this issuance is to fund the construction of a storm water retention basin at the wastewater treatment plant. User fees will fund 40 percent of the principal and interest on these bonds, and the remaining 60 percent will be funded by a millage that the City will levy. The full faith and credit and the limited taxing power of the City are pledged for payment of the principal and interest thereon.

On August 9, 2004, the City Council approved the sale of \$6.5 million in limited tax general obligation bonds for the construction of a new civic arena. Annual principal payments range from \$135,000 to \$490,000, while annual interest payments range from 2.50 percent to 4.75 percent. The final payment will be made in the year 2030. The total cost of the civic arena project was approximately \$10.3 million, with the balance of the funding coming primarily from area foundations. The project was completed in the fall of 2005.

On September 13, 2005, the City issued \$9,480,000 of General Obligation Unlimited Tax Refund Bonds. The bonds were issued pursuant to resolutions adopted by the City Council on July 11, 2005 and August 22, 2005, and provide for an average interest rate of 3.95 percent. The proceeds of these bonds were used to advance refund \$9,025,000 of outstanding 2001 General Obligation Unlimited Bonds with an average interest rate of 5.07 percent.

The City has pledged its full faith and credit on the bonded indebtedness of the Saginaw-Midland Municipal Water Supply Corporation, a jointly owned raw water system described in Note 1 - Summary of Significant Accounting Policies.

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 9 - Long-term Debt (Continued)

On May 19, 2008, the City Council authorized the issuance of \$17,890,000 limited tax general obligation judgment bonds for the purpose of paying a part of a tax refund to The Midland Cogeneration Venture (MCV), as ordered by the Michigan Tax Tribunal's Consent Judgment, dated April 18, 2008. Additional discussion on the tax refund is included in Note 17 - Property Tax Appeals Contingency. The sale of the bonds occurred on June 17, 2008, with the City taking possession of the proceeds on July 10, 2008, and issuing the refund to MCV on July 17, 2008.

The term of the bonds is 15 years (through May 2023) and provides for annual principal payments of between \$930,000 and \$1,545,000, with interest rates ranging between 3.625 percent and 4.375 percent, generating a true interest cost of 4.32 percent. Future funding for this bond's debt service will come from the General Fund.

By statute, the City's general obligation debt is restricted to 10 percent of the equalized value of all property in the City. Certain obligations, such as water revenue refunding bonds, are not subject to this limitation. At June 30, 2008, the City's general obligation debt statutory and legal debt limit amounted to \$281,422,420 and the indebtedness subject to the limitation aggregated \$19,363,882.

Annual requirements to pay principal and interest on the long-term bonds and capital leases outstanding at June 30, 2008 are as follows:

Fiscal Year	Governmental Activities			Business-type Activities		
	Principal	Interest	Total	Principal	Interest	Total
2009	\$ 178,018	\$ 29,512	\$ 207,530	\$ 2,145,000	\$ 876,189	\$ 3,021,189
2010	191,537	24,166	215,703	2,200,000	778,202	2,978,202
2011	204,573	18,432	223,005	1,095,000	676,828	1,771,828
2012	200,336	12,285	212,621	1,155,000	634,364	1,789,364
2013	209,187	6,270	215,457	1,205,000	595,666	1,800,666
2014-2018	-	-	-	6,805,000	2,305,622	9,110,622
2019-2023	-	-	-	5,404,063	996,603	6,400,666
2024-2028	-	-	-	1,500,000	382,879	1,882,879
2029-2033	-	-	-	700,000	50,350	750,350
Total	<u>\$ 983,651</u>	<u>\$ 90,665</u>	<u>\$ 1,074,316</u>	<u>\$ 22,209,063</u>	<u>\$ 7,296,703</u>	<u>\$ 29,505,766</u>

Future Revenues Pledged for Debt Payment - The City has pledged substantially all revenue of the Water and Sewer Fund, net of operating expenses, to repay the 2000 Water Supply System Refunding Revenue Bonds, Series 2000. Proceeds from the bonds provided financing for refunding the City of Midland's Water Supply System Revenue Refunding Bonds, Series 1991.

Note 9 - Long-term Debt (Continued)

The bonds are payable solely from the net revenues of the water and sewer system. The remaining principal and interest to be paid on the bonds total \$2,492,490. During the current year, net revenues of the water system were \$869,540 compared to the annual debt requirements of \$1,155,000.

Note 10 - Landfill Closure and Postclosure Care Cost

State and federal laws and regulations require the City to place a final cover on its sanitary landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. Although closure and postclosure care costs will be paid only near or after the date that the landfill stops accepting waste, the City reports a portion of these closure and postclosure care costs as an operating expense in each period based on landfill capacity used as of each balance sheet date. The \$3,090,000 reported as landfill closure and postclosure care liability at June 30, 2008 represents the cumulative amount reported to date based on the use of 100 percent of the capacity of Area A (32 acres closed in 1993) and cells 1 through 13 (40.2 acres closed in 2005), cell 14 (12.6 acres), and 53 percent of the estimated capacity of cell 15.

The City will recognize the remaining estimated cost of closure and postclosure care of \$453,126 as the remaining capacity of cell 15 is filled.

These amounts are based on what it would cost to perform all closure and postclosure care in current dollars. The City expects to reach 100 percent capacity in cell 15 during the fiscal year ending June 2012. The actual cost may be higher due to inflation, changes in technology, or changes in regulations.

Cell 16 was opened during the current year. Since 100 percent of capacity is available, no closure or postclosure care costs were reported.

The City is required by state and federal laws and regulations to make contributions to a trust to finance closure and postclosure care. The City is in compliance with these requirements, and at June 30, 2008, cash and cash equivalents in the amount of \$1,794,332 were held for these purposes, reported as restricted assets on the balance sheet. The City expects that future inflation costs will be paid from interest earnings on these contributions. However, if interest earnings are inadequate or additional postclosure care requirements are determined (due to changes in technology or applicable laws or regulations, for example), these costs may need to be covered by charges to future landfill users or from future tax revenue.

Note 10 - Landfill Closure and Postclosure Care Cost (Continued)

The City has also entered into an agreement to provide a letter of credit in favor of the State of Michigan to fulfill certain bonding requirements imposed upon the City, by Michigan law.

Note 11 - Pension Funds

Police and Fire Pension System

Plan Description - The Police and Fire Pension System is a single-employer defined benefit pension plan that is administered by the City of Midland Police and Fire Employees Retirement System. This plan covers all police and fire employees of the City. The system provides retirement, disability, and death benefits to plan members and their beneficiaries. At December 31, 2007, the date of the most recent actuarial valuation, membership consisted of 110 retirees and beneficiaries currently receiving benefits, terminated employees entitled to benefits but not yet receiving them, and 91 current active employees. The plan does not issue a separate financial report.

Funding Policy - The obligation to contribute to and maintain the system for those employees was established by negotiation with the City's collective bargaining units and requires a contribution from the employees of 8 percent of gross wages from all employees.

The City's funding policy provides for biweekly employee contributions and monthly employer contributions at actuarially determined rates. Administrative costs of the plan are financed through investment earnings.

The required schedule of funding progress immediately 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 liability for benefits.

Contributions - 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. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. Please refer to Note 1 for further significant accounting policies.

Note 11 - Pension Funds (Continued)

Annual Pension Cost - For the year ended June 30, 2008, the City's annual pension cost was \$1,582,533, which was equal to the City's required and actual contribution. The required employer contributions were determined as part of an actuarial valuation at December 31, 2006, using the entry age actuarial funding method. Significant actuarial assumptions used include (a) a 7 percent investment rate of return, (b) projected salary increases of 4.5 percent per year, compounded annually, (c) additional projected salary increases of up to 5.2 percent per year, attributable to seniority/merits, and (d) no postretirement benefit increases other than 5 percent increases for Police Command members with 25 or more years at 5, 10, 15, and 20 years after retirement. Both (a) and (b) include an inflation component of 4.5 percent. The actuarial value of assets was determined using techniques that smooth the effects of short-term volatility over a four-year period. The unfunded actuarial accrued liability is being amortized as a level (principal and interest) percentage of payroll contributions over 19 years.

Reserves - As of June 30, 2008, the plan's legally required reserves have been fully funded as follows:

Reserve for employees' contributions	\$5,262,493
Reserve for employer contributions	13,638,308
Reserve for retired benefit payment	33,871,078

Three-year Trend Information

Year Ended <u>June 30</u>	Annual Pension Cost (APC)	Percentage of APC Contribution	Net Pension Obligation
2006	\$ 1,290,917	100	None
2007	1,477,650	100	None
2008	1,582,533	100	None

Note 11 - Pension Funds (Continued)

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liabilities (AAL)	Unfunded (Overfunded) AAL (UAAL)	Funded Ratio (Percent)	Covered Payroll	UAAL as a Percent of Covered Payroll
12/31/05	\$ 50,186,088	\$ 54,310,758	\$ 4,124,670	92	\$ 5,665,317	72.8
12/31/06	52,563,758	57,395,444	4,831,686	92	5,960,007	81.1
12/31/07	55,699,201	60,025,641	4,326,440	93	6,075,182	71.2

Municipal Employees' Retirement System of Michigan - Defined Benefit Retirement Plan

Plan Description - The City of Midland participates in the Municipal Employees' Retirement System of Michigan (MERS), an agent multiple-employer, defined-benefit pension plan that covers substantially all employees of the City other than police and fire employees and employees hired on or after July 1, 2005. The system provides retirement, disability, and death benefits to plan members and their beneficiaries. The MERS issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to MERS at 1134 Municipal Way, Lansing, MI 48917.

Funding Policy - The obligation to contribute to and maintain the system for these employees was established primarily by negotiation with the City's collective bargaining units and requires a contribution from the employees ranging from 0 percent to 5 percent of gross wages. The City's funding policy provides for quarterly employee and employer contributions at actuarially determined rates.

Annual Pension Cost - For the year ended June 30, 2008, the City's annual pension cost of \$2,891,256 for the plan was equal to the required and actual contribution. The annual required contribution was determined as part of an actuarial valuation at December 31, 2005 using the entry age actuarial funding method. Significant actuarial assumptions used include (a) an 8 percent investment rate of return, (b) projected salary increases of 4.5 percent per year, compounded annually, (c) additional projected salary increases of 0 percent to 4.16 percent per year, attributable to seniority/merit, and (d) the assumption that benefits will increase after retirement by 2.5 percent annually, non-compounded. Both (a) and (b) include an inflation component of 4.5 percent. The actuarial value of assets was determined using techniques that smooth the effects of short-term volatility over a 10-year period. The unfunded actuarial liability is being amortized as a level percentage of payroll on a closed basis. The remaining amortization period is 30 years.

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 11 - Pension Funds (Continued)

Three-year Trend Information

Year Ended June 30	Annual Pension Cost (APC)	Percentage of APC Contribution	Net Pension Obligation
2006	\$ 2,332,776	100	None
2007	2,495,316	100	None
2008	2,891,256	100	None

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liabilities (AAL)	Unfunded (Overfunded) AAL (UAAL)	Funded Ratio (Percent)	Covered Payroll	UAAL as a Percent of Covered Payroll
12/31/05	\$ 72,701,562	\$ 95,809,652	\$ 23,108,090	76	\$ 12,935,257	178.6
12/31/06	76,147,020	101,188,678	25,041,658	75	12,537,515	199.7
12/31/07	79,669,492	107,392,597	27,723,105	74	12,173,842	227.7

Municipal Employees' Retirement System of Michigan - Defined Contribution Retirement Plan

The City of Midland participates in the Municipal Employees' Retirement System of Michigan (MERS) defined contribution plan which is administered by ICMA for all employees hired on or after July 1, 2005, with the exception of police and fire employees. In the defined contribution plan, benefits depend solely on the amounts contributed to the plan plus investment earnings. Employees are eligible to participate from the date of employment. As established by City Council resolution, the City contributes 5 percent of the employee's gross earnings in the plan. The employee is fully vested after five years of service or at age 65.

The City's total payroll during the current year was \$23,954,263. The current year contribution was calculated based on covered payroll of \$1,891,265, resulting in an employer contribution of \$94,564.

Note 11 - Pension Funds (Continued)

International City/County Management Association (ICMA) - RC 457 - Deferred Compensation Plan

The City also participates in an ICMA-RC 457 deferred compensation plan for all employees hired on or after July 1, 2005, with the exception of police and fire employees. In the deferred compensation plan, benefits depend solely on the amounts contributed to the plan plus investment earnings. Employees are eligible to participate from the date of employment. As established by City Council resolution, the City will contribute up to 7 percent of the employee's wages with 100 percent matching of the employee wage contributions, in 1 percent increments.

The City's total payroll during the current year was \$23,954,263. The current year contribution was calculated based on covered payroll of \$1,891,265, resulting in an employer contribution of \$75,448 and employee contributions of \$75,448.

Note 12 - Postemployment Benefits

The City of Midland provides postemployment healthcare coverage under a traditional insured plan to retired employees and their qualified spouses and other dependents, as mandated by collective bargaining agreements. Each agreement contains variations of the following general guidelines. Most employees fall into one of the following general groups:

The first group of employees will be enrolled in the comprehensive master medical plan available at the time of retirement. The City will pay 100 percent of the premium for retiree, spouse, and family.

The second group of employees will be eligible for continued medical coverage when they retire from the City, providing they pay 50 percent of the premium. The City will pay the other 50 percent.

The third group, employees hired on or after July 1, 2005, excluding police and fire employees, will not be eligible to be included in the City's group health insurance plan. For those employees, the City will contribute 2 percent of the employee's wages into a healthcare savings program.

City of Midland, Michigan

Notes to Financial Statements June 30, 2008

Note 12 - Postemployment Benefits (Continued)

The City funds the retiree health insurance on a “pay as you go” basis. The net cost to the City of providing postemployment health care coverage follows:

<u>Year</u>	<u>Number of Retirees</u>	<u>Amount</u>
2008	322	\$ 3,677,142
2007	317	5,083,814
2006	300	4,636,377

For the fiscal year, the City of Midland transferred \$2,015,707 to Municipal Employees’ Retirement System of Michigan (MERS) Retiree Health Funding Vehicle. MERS acts as a fiduciary, investing and managing funds for the future payment of postemployment healthcare coverage for the City of Midland.

Municipal Employees’ Retirement System of Michigan - Health Care Savings Program

The City of Midland participates in the Municipal Employees’ Retirement System of Michigan (MERS) healthcare savings program for all employees hired on or after July 1, 2005, with the exception of police and fire employees. In the healthcare savings program, benefits depend solely on the amounts contributed to the plan plus investment earnings. Employees are eligible to participate from the date of employment. As established by City Council resolution, the City contributes 2 percent of the employee’s gross earnings in the program. The employee is fully vested after three years of service.

The City’s total payroll during the current year was \$23,954,263. The current year contribution was calculated based on covered payroll of \$1,891,265, resulting in an employer contribution of \$37,825.

Upcoming Reporting Change - The Governmental Accounting Standards Board has recently released Statement Number 45, *Accounting and Reporting by Employers for Postemployment Benefits Other Than Pensions*. The new pronouncement provides guidance for local units of government in recognizing the cost of retiree health care, as well as any “other” postemployment benefits (other than pensions). The new rules will cause the government-wide financial statements to recognize the cost of providing retiree healthcare coverage over the working life of the employee, rather than at the time the healthcare premiums are paid. The new pronouncement is effective for the year ending June 30, 2009.

Note 13 - Claims, Litigation, and Other Contingencies

In the normal course of its activities, the City becomes a party in various legal actions. Although some actions have been brought for large amounts, the City has not generally experienced significant losses or cost. City management is of the opinion that the outcome of such actions will not have a material effect on the financial position of the City.

The City has received several federal and state grants for specific purposes that are subject to review and audit by the grantor agencies. Such audits could lead to requests for reimbursement to the grantor agency for expenditures disallowed under the terms of the grant. City management believes such disallowances, if any, will be immaterial.

Note 14 - Enterprise Fund Contractual Revenue

The City supplies large quantities of water to Dow Chemical Company and Dow Corning Corporation under contractual arrangements with each company. Under the Dow Chemical Supplemental Agreement dated March 1, 1979, and the Dow Corning Agreement dated July 15, 1985, the companies agree to pay for the variable cost of industrial grade water. In addition, the companies agree to pay a percentage of certain fixed costs, including the principal and interest costs on debt incurred by the City related to plant expansions necessary to meeting the companies' special requirements. These fixed cost payments are due in monthly installments until the bonds are paid in full.

The payment percentage is based upon the cost of the facilities required to meet the companies' exact capacity requirements relative to the total cost of the City's initial capacity requirements.

The percentage of the bond principal and interest payments reimbursed by each company follows:

	Percentage	
	Dow Chemical Company	Dow Corning Corporation
1998 Saginaw-Midland - Water Revenue Refinancing Bonds	34.00	4.20
2000 Water Revenue Refinancing Bonds	37.976	4.667
2002 Saginaw-Midland - Water Revenue Refinancing Bond	34.00	4.20
2006 Saginaw-Midland - Water Revenue Bonds	34.00	4.20

Note 14 - Enterprise Fund Contractual Revenue (Continued)

Total payments received under these agreements during the fiscal year were \$1,028,027, consisting of principal and interest of \$790,725 and \$237,302, respectively. These payments have been recorded as nonoperating revenue in the City's Enterprise Funds. Under the terms of these agreements, no equity accrues to either company.

Under the terms of the agreement with Dow Chemical Company, the Water Fund shall retain in a Dow Chemical Emergency Repair and Maintenance Fund, \$25,000 to fund Dow's share of non-budgeted repair, replacement, or improvements.

Note 15 - Urban Cooperation Act Agreement

Effective December 30, 1992, the City entered into a 30-year interlocal public agency agreement with the Township of Midland, as authorized by the provisions of Public Act 7 of the Public Acts of the State of Michigan of 1967 (Ex Sess) [MSA 5.4088(1) et seq; MCLA 124.501 et seq].

The agreement provides for (1) the orderly and uncontested annexation to the City of certain property then located in the Township; (2) future sharing, through the year 2022, of revenues derived from the City's levy of property taxes on certain property to be annexed under the agreement; (3) beginning in September 1993, and continuing through the year 2012, the sharing of revenues derived from the City's levy of property taxes on certain commercial and industrial property already located within the City; and (4) extension, at City cost, of water and sewer services by the City to the Township boundary.

The City's obligation under provision 3 above, shall cease if and when total cumulative payments thereunder reach \$15,000,000. The amount of revenue sharing due to the Township by the City under this agreement during the year ended June 30, 2008 was \$369,817. The total cumulative payments from the City through June 30, 2007 were \$3,178,140.

Note 16 - Risk Management

The City is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The City has purchased commercial insurance for liability and property claims, airport liability, and pension fiduciary liability claims; it participates in the Michigan Municipal Workers' Compensation Pool for employee injury claims.

Note 16 - Risk Management (Continued)

The Michigan Municipal League risk pool programs operate as common risk-sharing/management programs for local units of government in Michigan. Member premiums are used to purchase commercial excess insurance coverage and to pay member claims in excess of deductible amounts.

Beginning July 1, 2007, the City started a self-insurance program for health insurance, which is accounted for in the Health Insurance Fund (Internal Service Fund). An independent administrator (BCBS) processes the daily claims. Through June 30, 2008, the City had a \$25,000 stop-loss, per contract. There were no reductions to insurance coverage from the prior year.

The cost for health care is charged out to other City funds through its payroll system based upon illustrative rates generated by BCBS. These charges, together with employee withholdings, are the source of revenue to the Health Insurance Fund. Settled claims for the past three years, including the current year, as well as the prior two years relating to the commercial health insurance, have not exceeded the amount of insurance coverage.

The City estimates the liability for healthcare claims that have been incurred through the end of the fiscal year, including claims that have been reported as well as those that have not yet been reported.

The estimated liability for the past fiscal year is as follows:

Unpaid claims - Beginning of year	\$ -
Incurred claims, including claims incurred but not reported	7,921,304
Claims paid	<u>(6,960,082)</u>
Unpaid claims - End of year	<u>\$ 961,222</u>

Note 17 - Property Tax Appeals Contingency

In 1997, the City was presented with tax appeals from its three largest taxpayers: Midland Cogeneration Venture, the Dow Chemical Company, and the Dow Corning Corporation. Each year, since 1997, a significant portion of the City's budget process has been dedicated to providing funding to maintain reserves in both the General Fund and the Major Street Fund for possible tax refunds related to settlements of these cases.

Note 17 - Property Tax Appeals Contingency (Continued)

In October 2004, the City and the Dow Corning Corporation reached a settlement that was approved by the Michigan Tax Tribunal (MTT), resolving all appealed issues between the two parties. Similarly, in December 2006, the City and the Dow Chemical Company also reached a settlement that was approved by the MTT, bring closure to all appealed issues. On June 12, 2007, the City received a final settlement from the MTT for the tax years 1997 through 2000 of the appeal with the Michigan Cogeneration Venture (MCV). The final settlement included an order to issue a refund based upon the final taxable values as determined by the MTT. On September 10, 2007, the City issued a refund which included approximately \$13.7 million from the General Fund and \$1.1 million from the Major Street Fund. Tax years subsequent to 2000 were processed under a separate appeal and were not part of this settlement. All of these refunds were paid using accumulated reserves earmarked for tax appeal refunds.

On April 18, 2008, the MTT issued a consent judgment ratifying an agreement that the City and MCV had entered into on February 14, 2008. This agreement included reductions to taxable values based upon an independent appraisal. The judgment ordered a 64 percent reduction to MCV's taxable values, caused by final resolution of factors contained in the first MCV appeal, and the volatility of the natural gas market. The agreement provided 90 days for the City to pay the resulting tax refund to MCV. On July 17, 2008, the City refunded \$36,301,727 to MCV in full settlement of the appeals for the tax years 2001 through 2007.

Funding sources for this refund as of June 30, 2008 are as follows:

Fund balances reserved for tax appeals:

General Fund	\$ 14,999,179
Major Street Fund	<u>2,162,500</u>
Total reserved fund balance	17,161,679

Unreserved fund balances:

General Fund	1,571,807
Judgment bond issue proceeds	<u>17,568,241</u>
Total unreserved fund balance	<u>19,140,048</u>
Total refund	<u>\$ 36,301,727</u>

Note 17 - Property Tax Appeals Contingency (Continued)

A separate discussion on the judgment bond issuance is included in Note 9 - Long-term Debt.

The pending refund to MCV is reported in the government-wide financial statements as being due within one year.