CITY OF DETROIT
SEWAGE DISPOSAL FUND

Basic Financial Statements

June 30, 2013

(With Independent Auditors' Report Thereon)

CITY OF DETROIT
SEWAGE DISPOSAL FUND

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KPMG LLP
Suite 1900
150 West Jefferson
Detroit, MI 48226

Independent Auditors' Report

Kevyn Orr, Emergency Financial Manager,
the Board of Water Commissioners,
the Honorable Mayor Mike Duggan, and
the Honorable Members of the City Council
City of Detroit, Michigan:

Report on the Financial Statements

We have audited the accompanying financial statements of the Sewage Disposal Fund (the Fund), an enterprise fund of the City of Detroit, Michigan (the City), as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; 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.

Auditors' 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 auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion the basic financial statements referred to above present fairly, in all material respects, the financial position of the Sewage Disposal Fund, as of June 30, 2013, and the changes in its financial position, and its cash flows for the year then ended, in accordance with U.S. generally accepted accounting principles.

Emphasis of Matters

Emphasis of Matter Regarding Uncertainty About Ability to Continue as a Going Concern

The accompanying basic financial statements have been prepared assuming that the City and the Sewage Disposal Fund will continue as a going concern. As discussed in note 16(a) to the basic financial statements, on July 18, 2013, the City, including the Fund, filed a voluntary petition under Chapter 9 of the Bankruptcy Code which raises substantial doubt about the Fund's ability to continue as a going concern. Management's plans in regard to these matters are also described in note 16. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

Emphasis of Matter Regarding Pension Plans

As discussed in note 11(d) and (e) to the basic financial statements, the City and the General Retirement System (GRS) a single-employer defined benefit pension plan which covers substantially all employees of the City, including employees of the Fund, utilized different actuarial assumptions in calculating the unfunded actuarial accrued liability. Our opinion is not modified with respect to this matter.

Emphasis of Matter Regarding Fund Financial Statements

As discussed in note 1, the basic financial statements present only the Sewage Disposal Fund and do not purport to, and do not, present fairly the financial position of the City of Detroit, Michigan, as of June 30, 2013, the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Management has omitted management's discussion and analysis, schedules of employer contributions, and schedules of funding progress that U.S. generally accepted accounting principles require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board 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. Our opinion on the basic financial statements is not affected by this missing information.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Fund's basic financial statements. The other supplemental information is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The other supplemental information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such supplemental information has been subjected to the auditing procedures applied by us in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, based on our audit, the other supplemental information is fairly stated in all material respects in relation to the basic financial statements as a whole.

KPMG LLP

July 25, 2014

CITY OF DETROIT
SEWAGE DISPOSAL FUND

Statement of Fund Net Position

June 30, 2013

Current assets:		
Cash and cash equivalents	$	17,445,997
Investments		32,851,568
Accounts receivable:		
Billed accounts receivable		126,545,085
Unbilled accounts receivable		67,490,396
Other accounts receivable		10,800,510
Allowance for doubtful accounts		(68,548,573)
Total accounts receivable, net		136,287,418
Restricted:		
Cash and cash equivalents		8,602,053
Investments		146,839,849
Due from other funds		14,751,256
Due from fiduciary funds		1,409,855
Inventories		9,762,803
Prepaid expenses		853,192
Total current assets		368,803,991
Noncurrent assets:		
Restricted:		
Cash and cash equivalents		85,061,154
Investments		175,791,347
Other receivables		3,750,000
Net pension asset		86,248,463
Deferred charges		43,193,749
Capital assets:		
Assets not subject to depreciation		225,159,160
Assets subject to depreciation		2,636,097,496
Total noncurrent assets		3,255,301,369
Total assets	$	3,624,105,360

See accompanying notes to basic financial statements.

(Continued)

CITY OF DETROIT
SEWAGE DISPOSAL FUND

Statement of Fund Net Position

June 30, 2013

Current liabilities:	
Accounts and contracts payable	$ 50,488,373
Accrued salaries and wages	602,720
Due to other funds	52,036,220
Revenue bonds and state revolving loans	78,385,000
Pension obligation certificates of participation	3,236,213
Other accrued liabilities	23,327,269
Accrued interest	70,858,984
Accrued compensated absences	717,569
Accrued workers' compensation	551,000
Total current liabilities	280,203,348
Long-term liabilities:	
Revenue bonds and state revolving loans, net	3,112,192,669
Pension obligation certificates of participation, net	86,914,659
Accrued other postemployment benefits	70,445,095
Accrued compensated absences	477,410
Accrued workers' compensation	2,742,000
Claims and judgments	190,000
Derivative instruments – swap liability	18,581,500
Total long-term liabilities	3,291,543,333
Total liabilities	$ 3,571,746,681
Fund net position:	
Net investment in capital assets	$ 248,910,555
Restricted:	
Restricted for debt service	135,156,679
Unrestricted deficit	(331,708,555)
Total fund net position	$ 52,358,679

See accompanying notes to basic financial statements.

CITY OF DETROIT
SEWAGE DISPOSAL FUND

Statement of Revenues, Expenses, and Changes in Fund Net Position

Year ended June 30, 2013

Operating revenues:	
General customers	$ 193,098,413
Suburban customers	238,301,009
City departments	635,188
Sewage surcharge	5,204,732
Miscellaneous	3,623,918
Total operating revenues	440,863,260
Operating expenses:	
Wastewater treatment plant	131,695,533
Pumping stations	8,528,336
Combined sewage overflow control basins	5,319,923
Interceptors	8,638,184
Sewer	8,517,248
Industrial waste control	4,173,167
Meters	142,196
Commercial	6,795,960
Administrative and general	35,974,533
Other items:	
Net OPEB obligation	13,609,015
Nonrecurring capital asset adjustment	36,970,235
Total operating expenses before depreciation	260,364,330
Depreciation	121,464,302
Total operating expenses	381,828,632
Operating income	59,034,628
Nonoperating revenues (expenses):	
Investment losses:	
Losses on investment activity	(1,061,942)
Change in fair value of derivatives	(6,877,343)
Loss on sale of assets	(2,752)
Interest expense, net of capitalized interest	(142,081,167)
Amortization of bond issuance costs	(14,978,455)
Miscellaneous revenues	861,759
Total nonoperating expenses, net	(164,139,900)
Decrease in fund net position	(105,105,272)
Fund net position – beginning of year	157,463,951
Fund net position – end of year	$ 52,358,679

See accompanying notes to basic financial statements.

CITY OF DETROIT
SEWAGE DISPOSAL FUND

Statement of Cash Flows

Year ended June 30, 2013

Cash flows from operating activities:	
Receipts from customers	$ 444,716,374
Internal activity – receipts from other funds	22,740,653
Payments to suppliers	(135,974,669)
Payments to employees	(80,467,547)
Net cash provided by operating activities	251,014,811
Cash flows from noncapital financing activities:	
Interest paid on pension obligation certificates of participation	(4,674,284)
Miscellaneous nonoperating revenue	861,759
Net cash used in noncapital financing activities	(3,812,525)
Cash flow from capital and related financing activities:	
Acquisition and construction of capital assets	(101,431,436)
Principal paid on revenue bonds and state revolving loans	(76,590,000)
Interest paid on revenue bonds and state revolving loans	(127,531,521)
Proceeds from issuance of revenue bonds and state revolving loans	10,070,762
Net cash used in capital and related financing activities	(295,482,195)
Cash flows from investing activities:	
Proceeds from sales and maturities of investments	768,587,656
Purchase of investments	(850,103,038)
Interest received on investments	11,553
Net cash used in investing activities	(81,503,829)
Net decrease in cash and cash equivalents	(129,783,738)
Cash and cash equivalents at beginning of year	240,892,942
Cash and cash equivalents at end of year	$ 111,109,204
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	$ 59,034,628
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	121,464,302
Bad debt expense	39,483,522
Loss on disposal of capital assets	5,134,577
Nonrecurring capital asset adjustment	36,970,235
Changes in assets and liabilities:	
Accounts receivable	(35,630,408)
Due from other funds	10,788,347
Inventories	(878,124)
Prepaid expenses	965,959
Net pension asset	(2,567)
Accounts and contracts payable	(2,652,660)
Accrued salaries and wages	(102,347)
Due to other funds	11,952,306
Due to fiduciary funds	(8,399,139)
Other accrued liabilities, accrued compensated absences, and accrued workers' compensation	947,279
Other postemployment benefits obligation	13,609,014
Claims and judgments payable	(1,329,500)
Pollution remediation obligations	(340,613)
Net cash provided by operating activities	$ 251,014,811
Noncash capital financing activities:	
Fair value of derivatives	$ (9,102,234)
Deferred outflows of resources – investment derivatives	15,979,577

See accompanying notes to basic financial statements.

(1) Reporting Entity

The City of Detroit (the City) Charter established the Detroit Water and Sewerage Department (the DWSD) in the year 1836 to supply water, drainage, and sewage service within and outside the City. The Sewage Disposal Fund (the Fund), an enterprise fund, separately accounts for the Sewage Disposal System (the System), as is required by bond ordinances of the City.

The DWSD is governed by a seven member Board of Water Commissioners (the Board). Pursuant to federal court order issued in February 2011, the Board includes four members appointed by the Mayor of the City of Detroit, and one each nominated by the Wayne County Executive, the Oakland County Water Resources Commissioner, and the Macomb Public Works Commissioner with confirmation by the Mayor of Detroit. All members must have at least seven years of experience in a regulated industry. The Board's governance structure, authority, and level of operational autonomy is established by four standing federal court orders dated September 9, 2011 (Creation of the Root Cause Committee); November 4, 2011 (Adoption of the Root Cause Committee Plan of Action); October 5, 2012 (Clarification of the November 4, 2011 Order) and, December 14, 2012 (Adoption of Root Cause Committee's Plan of Action Clarification).

These court orders were the result of federal court oversight of DWSD for most of the time from May 6, 1977 through March 27, 2013. The nature of this case was alleged violations of the Clean Water Act involving the DWSD's wastewater treatment plant (WWTP) and its National Pollutant Discharge Elimination System (NPDES) permit. On March 15, 2013, DWSD's Director was required to submit the Final Director's report of compliance for federal court review. The report summarized progress made in implementing the changes granted by the four court orders noted above. On March 27, 2013, the federal court judge entered a final order closing the case based upon "tremendous progress" by the empowered Board of Water Commissioners, implementation of human resource functions, and improved procurement policy, the court found that DWSD's compliance record vastly improved. The resulting order was "that the existing ACO [Administrative Consent Order] is a sufficient mechanism to ensure sustained compliance with the DWSD's NPDES permit and the Clean Water Act and this Court shall therefore close this case …." The final court order reiterated that it retains limited jurisdiction for the purpose of enforcement of its orders issued on September 9, 2011, November 4, 2011, October 5, 2012, and December 14, 2012.

Authority granted by the federal court to the DWSD includes operational independence in the areas of law, finance, human resources, and procurement. Specifically these orders enjoin the City from applying any existing or future Charter provisions, ordinances, resolutions, executive orders, city policies, regulations, procedures or similar rules or practices that are inconsistent with the express terms of this court's orders. Further the orders grant DWSD the authority to: purchase its own information technology systems; establish its own subunits and programs within its Finance Division including debt management, accounts payable, accounts receivable, accounting, budget, cash management, asset management, and deferred compensation; independence from City Finance Policies; be exempt from the application of City ordinances, the City's human resources policies and regulations, Civil Service Commission Rules, and City resolutions and orders, pertaining to payroll, employee benefits, and employee and labor relations; establish bank accounts in its own name; establish its own self-insurance fund; and approve the issuance of debt and to refinance debt upon the sole approval of the Board of Water Commissioners (unless the debt contains a full or partial general obligation pledge of the City of Detroit, in which case City Council approval would be required prior to issuance).The basic financial statements of the Fund have been included in the City's Comprehensive Annual Financial Report and reported as an enterprise fund. Copies of these reports, along with other financial information, can be obtained at the Fund's administrative office located at 735 Randolph, Detroit, Michigan 48226 and on its website at www.dwsd.org.

(2) Summary of Significant Accounting Policies

The following is a summary of the more significant accounting policies followed in the preparation of the Fund's basic financial statements. These policies conform to U.S. generally accepted accounting principles (GAAP).

(a) Basis of Accounting

The accounting policies of the Fund conform to GAAP as applicable to governmental entities. The accounts of the Fund, which are organized as an enterprise fund, are used to account for the Fund's activities, which are financed and operated in a manner similar to a private business enterprise. Accordingly, the Fund maintains its records on the accrual basis of accounting. Revenues from operations, investments, and other sources are recorded when earned. Expenses (including depreciation) of providing services to the public are accrued when incurred.

Nonexchange transactions, in which the Fund receives value without directly giving equal value in return, include contributions and grants. On an accrual basis, revenue from contributions and grants is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements and expenditure requirements. Timing requirements specify the year when the resources are required to be used or the fiscal year when use is first permitted. Expenditure requirements specify the year in which the resources are provided to the Fund on a reimbursement basis.

(b) Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

(c) Investments

Investments are reported at fair value based on quoted market prices.

(d) Inventories and Prepaid Items

Inventories consist of operating, maintenance, and repair parts for sewage assets and are valued at the lower of cost or market, with cost being determined on an average-cost method. Inventory is recorded as expenditures when consumed rather than when purchased. Certain payments to vendors reflect costs applicable to future fiscal years and are recorded as prepaid items.

(e) Capital Assets

Capital assets are recorded at historical cost, together with interest capitalized during construction. The Fund's capitalization levels are $5,000 on tangible personal property and for improvements other than buildings, and $50,000 on infrastructure, including sewer lines. All acquisitions of land and land improvements are capitalized regardless of cost. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets as follows:

Land improvements	67 years
Building and structures	40 years
Interceptors and regulators	100 years
Machinery, equipment, and fixtures	3–20 years

The Fund capitalizes qualifying net interest costs of the System on bonds issued for capital construction in accordance with FASB Statement No. 34, *Capitalization of Interest Cost*, as amended. Accordingly, capitalized interest for the year ended June 30, 2013 was $11,400,250.

Construction in progress is related to buildings, improvements or infrastructure, that have not yet been placed in service for the intended use. These costs include contract costs (materials, labor, and overhead) as well as professional fees and interest incurred during the construction period. Upon completion, construction-in-progress costs are transferred to the appropriate capital asset classification. A periodic review of projects included in construction in progress identified projects as suspended or cancelled during the period and resulted in project related operations and maintenance costs being recorded as a nonrecurring capital asset adjustment expense.

(f) Taxes and City Services

The Fund pays no direct federal, state, or local taxes, except local taxes on excess property and federal Social Security taxes. The Fund reimburses the City for most of the direct services furnished by other City departments, including general staff services. Charges are billed for all sewage services provided to City departments.

(g) Shared Costs

Costs related to shared facilities and personnel are allocated to the Fund on a basis that relates costs incurred to the Fund benefited.

(h) Compensated Absences

The liability for compensated absences reported in the basic financial statements consists of unpaid, accumulated vacation, and sick leave balances. Unused vacation pay and banked overtime accumulate up to a maximum level until termination of employment, while there is no vesting of sick pay until an employee reaches age 60 or completes 25 years of service. The liability for compensated absences has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. The liability has been calculated based on the employees' current salary level and includes salary-related costs (e.g., Social Security and Medicare Tax).

(i) Bond Premiums, Discounts, Issuance Costs, and Deferred Amounts on Refunding

Bond premiums, discounts, issuance costs, and deferred amounts on refunding are deferred and amortized over the life of the bonds. Bond premiums and discounts are amortized using the effective interest method, and bond issuance costs and deferred amounts on refunding are amortized using the straight-line method. Bonds payable are reported net of the applicable bond premium, discounts, and deferred amounts on refunding. Bond issuance costs are reported as deferred charges.

(j) Net Position

Fund net position is categorized as follows:

Net Investment in Capital Assets – This consists of capital assets, net of accumulated depreciation, and related debt.

Restricted – The net position has been legally restricted by outside parties or by law through constitutional provisions or enabling legislation. When both restricted and unrestricted resources are available for use, generally it is the Fund's policy to use restricted resources first, and then unrestricted resources when they are needed.

Unrestricted – This consists of assets that do not meet the definition of "restricted" or "net investment in capital assets."

(k) Unbilled Revenue

The Fund records unbilled revenues for services provided prior to year-end by accruing actual revenues billed in the subsequent month.

(l) Interest Expense

Interest expense in the statement of revenues, expenses, and changes in fund net position includes amounts related to the accretion of capital appreciation bonds, amounts paid on interest rate swaps, as well as the amortization of premiums, discounts, and deferred amounts on refunding. Interest expense is reported net of capitalized interest of $11,400,250 for the year ended June 30, 2013.

(m) Classification of Revenues and Expenses

The Fund classifies its revenues and expenses as either operating or nonoperating.

Operating revenues include activities that have the characteristics of exchange transactions, such as revenue from charges for services. Such revenue has been shown net of allowances of $39,483,522.

Nonoperating revenue includes activities that have the characteristics of nonexchange transactions, such as contributions and investment income.

Operating expenses include the costs of operating the sewer utility, administrative expenses, and depreciation on capital assets. All expenses not meeting this definition, including interest expense, are reported as nonoperating expenses.

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(n) Use of Estimates

The preparation of basic financial statements in conformity with 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 basic financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(o) Upcoming Accounting Pronouncements

In March 2012, the Governmental Accounting Standards Board issued GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which is required to be implemented for financial statements for periods beginning after December 15, 2012. Statement No. 65 establishes accounting and financial reporting standards that reclassify, as deferred outflows and inflows of resources, certain items that were previously reported as assets and liabilities. This Statement also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources. The Fund is currently evaluating the impact this standard will have on the financial statements when adopted during the Fund’s fiscal year ending June 30, 2014.

In March 2012, the GASB issued GASB Statement No. 66, *Technical Corrections – an Amendment of GASB Statements No. 10 and No. 62*. This Statement amends or removes certain provisions of GASB Statements No. 10 and No. 62 related to fund-based reporting of a state and local government’s risk financing activities, accounting for operating lease payments, differences between the initial investment and the principal amount of a purchased loan or group of loans, and servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from the current (normal) servicing fee rate. The Fund is currently evaluating the impact this standard will have on the financial statements when adopted during the Fund’s 2014 fiscal year.

In June 2012, the GASB issued GASB Statement No. 67, *Financial Reporting for Pension Plans*. This new standard, which replaces the requirements of GASB Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures*, establishes standards for financial reporting that outline the basic framework for separately issued pension plan financial reports and specifies the required approach to measuring the liability of employer and certain nonemployer contributing entities, about which information is required to be disclosed. GASB Statement No. 67 is required to be adopted for years beginning after June 15, 2013. The Fund is currently evaluating the impact this standard will have on the financial statements when adopted during the Fund’s fiscal year ending June 30, 2014.

In June 2012, the GASB issued GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. Statement No. 68 requires governments providing defined benefit pensions to recognize their unfunded pension benefit obligation as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. This net pension liability that will be recorded on the government-wide, proprietary, and discretely presented component unit statements will be computed differently than the current unfunded actuarial accrued liability, using specific parameters set forth by the GASB. The statement also enhances accountability and transparency through revised and new note disclosures and required supplemental information (RSI). The Fund is currently evaluating the impact this standard will have on the financial statements when adopted during the Fund's fiscal year ending June 30, 2015.

In January 2013, the GASB issued GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*. Statement No. 69 establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in the Statement, the term government combinations includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations. The Statement requires disclosures to be made about government combinations and disposals of government operations to enable financial statement users to evaluate the nature and financial effects of those transactions. The City is currently evaluating the impact this standard will have on the financial statements when adopted during the City's fiscal year ending June 30, 2015.

In November 2013, the GASB issued GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*. The objective of the Statement is to address an issue regarding application of the transition provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions* (see above). The Statement amends paragraph 137 of Statement No. 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. The provisions of this Statement are required to be applied simultaneously with the provisions of Statement No. 68. The City is currently evaluating the impact this standard will have on the financial statements when adopted during the City's fiscal year ending June 30, 2015.

(p) New Accounting Pronouncements

During the year, the Fund adopted GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The statement incorporates deferred outflows of resources and deferred inflows of resources, as defined by GASB Concepts Statement No. 4, into the definitions of the required components of the residual measure of net position, formerly net assets. The statement also provides a new statement of net position format to report all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position. The statement impacted the format and reporting of the balance sheet.

(3) Deposits and Investments

The deposits and investments of the Fund at June 30, 2013 are reported in the financial statements as follows:

		Cash and cash equivalents	Investments
Current unrestricted assets	$	17,445,997	32,851,568
Current restricted assets		8,602,053	146,839,849
Noncurrent restricted assets		85,061,154	175,791,347
Total cash and investments	$	111,109,204	355,482,764

State law authorizes the Fund to make deposits in the accounts of federally insured financial institutions. Cash held by fiscal agents or by trustees is secured in accordance with the requirements of the agency or trust agreement.

The Fund is authorized to invest in obligations of the U.S. government or its agencies; certificates of deposit, savings and depository accounts of insured institutions, commercial paper of certain investment quality, repurchase agreements, banker’s acceptances, mutual funds of certain investment quality, and investment pools as authorized by state law.

(a) Custodial Credit Risk of Bank Deposits

Custodial credit risk is the risk that in the event of bank failure, the Fund’s deposits may not be returned by the bank. The Fund does not have a deposit policy for custodial credit risk. At year end, the Fund had $106,662,315 of bank deposits (certificates of deposit, checking, and savings accounts) that were uninsured and uncollateralized. The Fund believes that due to the dollar amount of cash deposits, and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the Fund evaluates each financial institution it deposits funds with and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

(b) Custodial Credit Risk of Investments

Custodial credit risk is the risk that in the event of failure of the counterparty, the Fund will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Fund does not have a policy for custodial credit risk. As of June 30, 2013, the Fund had no investments subject to custodial credit risk.

(c) Interest Rate Risk

Interest rate risk is the risk that, over time, the value of investments will decrease as a result of an increase in interest rates. The Fund’s investment policy does not specifically restrict investment maturities other than commercial paper, which can only be purchased with a 270-day maturity. The Fund’s policy minimizes interest rate risk by requiring that the Fund attempt to match its investments with anticipated cash flow requirements. Unless related to a specific cash flow, the Fund is generally

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not permitted to directly invest in securities maturing more than 10 years from the original date of purchase. As of June 30, 2013, the maturities for the Fund's fixed income investments were as follows:

			Investment maturities in years	
	Fair value	Less than one year	One to five years	Six to ten years
Investments:				
U.S. government agency securities	$ 125,871,527	—	121,012,327	4,859,200
Commercial paper	4,999,045	4,999,045	—	—
Pooled funds	224,612,192	224,612,192	—	—
Total investments	$ 355,482,764	229,611,237	121,012,327	4,859,200

(d) Credit Risk

Credit risk is the risk that the Fund will not recover its investments due to the inability of the counterparty to fulfill its obligation. The Fund limits its investments in commercial paper, mutual funds, and external investment pools that purchase commercial paper to the top two rating classifications issued by two nationally recognized statistical rating organizations (NRSROs).

As of June 30, 2013, the credit quality ratings for the Fund's fixed income investments were as follows:

		Ratings	
Investments	Fair value	S&P	Moody's
U.S. government agency securities	$ 116,068,927	AA+	Aaa
U.S. government agency securities	4,959,300	AA+	Aa
U.S. government agency securities	4,843,300	AA+	A1
Commercial paper	4,999,045	A1	P1
Pooled funds	224,612,192	AAAm	Aaa
Total investments	$ 355,482,764		

(e) Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the Fund's investment in a single issuer. The Fund's policy specifies a number of limitations to minimize concentration of credit risk, including prohibiting investing more than 5% of the portfolio in securities (other than U.S. government agencies, mutual funds, external investment pools, and other pooled investments) of any one issuer.

More than 5% of the Fund's investments are in Federal Home Loan Bank and Federal National Mortgage Association securities. These investments represented 7% and 22%, respectively, of the Fund's total investments as of June 30, 2013.

(4) Restricted Assets

Restricted assets, principally cash and investments, are available for debt service on revenue bonds and to provide funds for improvements, enlargements, extensions, and construction. In certain instances, minimum levels of assets are required by bond ordinance provisions or by Board of Water Commissioners' decree. These assets are maintained as follows:

(1) With respect to the Bond and Interest Redemption Fund, after provision has been made for expenses of operation and maintenance of the System, a sum proportionately sufficient to provide for payment, when due, of the current principal and interest is set aside. The Bond Reserve Account is part of the Bond and Interest Redemption Fund, and the amounts credited to this account are to be used only to pay principal and interest on the bonds when current revenues are not sufficient.

(2) With respect to the Extraordinary Repair and Replacement Reserve Fund, after meeting the requirements of the foregoing funds, monthly deposits in an amount equal to one-twelfth of 3% of the budgeted operation and maintenance expense of the System for the fiscal year must be set aside until the aggregate amount funded totals at least 15% of that year's budgeted operating and maintenance costs. These deposits are to be used for major unanticipated repairs and replacement to the System with actual or anticipated cost exceeding $1 million. Once this fund is fully funded, deposits required are amounts needed to maintain fully funded status. Borrowings of up to 50% of the balance in this fund on the first day of the related fiscal year are allowed for transfer to and use from the Improvement and Extension Fund. Any such borrowings must be repaid prior to any deposits being made to the Improvement and Extension Fund.

(3) After the above deposits have been made, excess amounts may be deposited in the Improvement and Extension Fund, established for the payment of improvements, enlargements, repairs, extensions, or betterment to the System.

(4) With respect to the Construction Fund, the portion of the proceeds of the sale of bonds for building or improving the System is deposited in this fund. A separate depository account is required for each series of bonds. Proceeds for construction purposes received from federal and state grants and other sources that restrict the use of such proceeds are also deposited into this account.

(Continued)

(5) Capital Assets

Capital asset activity for the year ended June 30, 2013 was as follows:

	Balance, June 30, 2012	**Additions**	**Disposals**	**Balance, June 30, 2013**
Nondepreciable assets:				
Land and land rights	$ 12,110,899	1,258,878	—	13,369,777
Construction in progress	291,377,657	73,102,377	(152,690,651)	211,789,383
Total nondepreciable assets	303,488,556	74,361,255	(152,690,651)	225,159,160
Depreciable assets:				
Land improvements	75,477,901	—	—	75,477,901
Buildings and structures	1,979,578,185	129,017,342	(4,570,671)	2,104,024,856
Interceptors and regulators	207,238,472	22,900	—	207,261,372
Machinery, equipment, and fixtures	1,684,500,977	14,133,804	(1,014,005)	1,697,620,776
Total depreciable assets	3,946,795,535	143,174,046	(5,584,676)	4,084,384,905

	Balance, June 30, 2012	**Additions**	**Disposals**	**Balance, June 30, 2013**
Less accumulated depreciation:				
Land improvements	$ (20,416,642)	(1,033,258)	—	(21,449,900)
Buildings and structures	(571,113,859)	(44,720,497)	—	(615,834,356)
Interceptors and regulators	(66,346,376)	(4,332,563)	—	(70,678,939)
Machinery, equipment, and fixtures	(669,393,578)	(71,377,984)	447,348	(740,324,214)
Total accumulated depreciation	(1,327,270,455)	(121,464,302)	447,348	(1,448,287,409)
Net capital assets	$ 2,923,013,636	96,070,999	(157,827,979)	2,861,256,656

See note 14 for discussion of commitments related to construction activities.

(6) Long-Term Obligations

Changes in long-term obligations for the year ended June 30, 2013 were as follows:

	Balance, June 30, 2012	Increase	Decrease	Balance, June 30, 2013	Amount due within one year
Revenue bonds	$ 2,793,925,000	—	(30,860,000)	2,763,065,000	34,755,000
Capital appreciation bonds	90,545,000	—	(10,295,000)	80,250,000	7,700,000
Discount on capital appreciation bonds	(20,613,925)	—	1,793,241	(18,820,684)	—
State revolving loans	508,236,265	10,070,762	(35,435,000)	482,872,027	35,930,000
Total revenue bonds	3,372,092,340	10,070,762	(74,796,759)	3,307,366,343	78,385,000
Add unamortized premiums	118,338,751	—	(7,825,286)	110,513,465	—
Less :					
Unamortized discounts	(2,848,046)	—	268,075	(2,579,971)	—
Deferred amounts on refunding	(237,578,258)	—	12,856,090	(224,722,168)	—
Total revenue bonds, net	3,250,004,787	10,070,762	(69,497,880)	3,190,577,669	78,385,000
Pension obligation certificates 2006 series	58,040,761	—	—	58,040,761	—
Plus deferred amounts on refunding	1,074,459	—	(3,230)	1,071,229	—
Total pension obligation certificates, net	90,154,102	—	(3,230)	90,150,872	3,236,213
Other long-term liabilities:					
Capital lease	—	—	—	—	—
Accrued compensated absences	5,502,481	1,480,942	(5,788,444)	1,194,979	717,569
Accrued workers' compensation	3,554,000	1,158,863	(1,419,863)	3,293,000	551,000
Claims and judgments	1,519,500	846,227	(2,175,727)	190,000	—
Pollution remediation obligation	340,613	—	(340,613)	—	—
Accrued other postemployment benefits:	56,836,081	24,830,446	(11,221,432)	70,445,095	—
Total other long-term liabilities	67,752,675	28,316,478	(20,946,079)	75,123,074	1,268,569
Total	$ 3,407,911,564	38,387,240	(90,447,189)	3,355,851,615	82,889,782

(7) Revenue Bonds Payable (Including State Revolving Loans)

Revenue bonds payable were $3,307,366,343 at June 30, 2013. Net revenues of the Fund are pledged to repayment of bonds. The following is a schedule of the revenue bonds payable at June 30, 2013:

Issue	Bond date	Amount issued	Range of interest rates	Maturity date	Outstanding balance at June 30, 2013	
Series 1998-A	39,065	$ 18,540,000	5.50%	07/01/13–17	$ 16,435,000	
Series 1998-A	39,065	49,075,000	5.25	07/01/18–23	49,075,000	c
Series 1998-B	39,065	18,750,000	5.50	07/01/13–17	16,505,000	
Series 1998-B	39,065	48,770,000	5.25	07/01/18–23	48,770,000	c
Series 1999-A **	36,495	33,510,118	—	07/01/13–21	61,429,316	
Series 2001-B	37,149	110,550,000	5.50	07/01/23–29	110,550,000	
Series 2001-C-1	39,981	6,360,000	5.25	07/01/13–19	4,410,000	
Series 2001-C-1	39,981	148,510,000	6.50 – 7.00	07/01/24–27	148,510,000	c
Series 2001-C-2	39,576	3,275,000	3.50 – 4.00	07/01/13–18	2,020,000	
Series 2001-C-2	39,576	119,630,000	4.00 – 5.25	07/01/19–29	119,630,000	c
Series 2001-D	37,187	92,450,000	Variable (*)	07/01/32	21,300,000	c
Series 2001-E	39,575	136,150,000	5.75	07/01/31	136,150,000	c
Series 2003-A	37,763	158,000,000	3.30 – 5.00	07/01/13	70,450,000	
Series 2003-A	37,763	441,380,000	3.50 – 5.50	07/01/14–32	128,940,000	c
Series 2003-B	39,981	150,000,000	7.50	07/01/33	150,000,000	c
Series 2004-A	38,029	101,435,000	5.00 – 5.25	07/01/13–24	67,755,000	
Series 2005-A	38,428	3,765,000	3.40 – 3.70	07/01/13–15	1,820,000	
Series 2005-A	38,428	269,590,000	3.75 – 5.125	07/01/16–35	236,770,000	c
Series 2005-B	38,428	40,215,000	3.40 – 5.50	07/01/13–22	37,195,000	
Series 2005-C	38,447	22,065,000	5.00	07/01/13–15	12,425,000	
Series 2005-C	38,447	41,095,000	5.00	07/01/16–25	41,095,000	c
Series 2006-A	39,575	123,655,000	5.50	07/01/34–36	123,655,000	
Series 2006-B	38,939	11,850,000	4.00 – 5.00	07/01/13–16	6,335,000	
Series 2006-B	38,939	238,150,000	4.25 – 5.00	07/01/17–36	238,150,000	c
Series 2006-C	38,939	8,495,000	5.25	07/01/16	8,495,000	
Series 2006-C	38,939	18,065,000	5.00	07/01/17–18	18,065,000	c
Series 2006-D	39,065	370,000,000	Variable (*)	07/01/26–32	288,780,000	c
Series 2012-A	41,086	95,445,000	5.00	07/01/14–22	95,445,000	
Series 2012-A	41,086	564,335,000	5.00 – 5.50	07/01/23–39	564,335,000	c
Total revenue bonds payable					$ 2,824,494,316	

* Interest rates are reset periodically at the stated current market interest rate.

** Bonds are capital appreciation bonds. The outstanding balance represents the discounted present value.

c Indicates bonds are callable under terms specified in the indenture, all other bonds are noncallable.

The following is a schedule of the state revolving loans payable at June 30, 2013:

Issue	Bond date		Amount issued	Range of interest rates	Maturity date		Outstanding balance at June 30, 2013
Series 1992-B-SRF	09/24/92	$	1,915,000	2.000%	10/1/2013	$	115,000
Series 1993-B-SRF	09/30/93		6,603,996	2.000	10/01/13–14		775,000
Series 1997-B-SRF	09/30/97		5,430,174	2.250	10/01/13–18		1,870,000
Series 1999-SRF-1	06/24/99		21,475,000	2.500	04/01/14–20		8,750,000
Series 1999-SRF-2	09/30/99		46,000,000	2.500	10/01/13–22		25,860,000
Series 1999-SRF-3	09/30/99		31,030,000	2.500	10/01/13–20		14,295,000
Series 1999-SRF-4	09/30/99		40,655,000	2.500	10/01/13–20		18,725,000
Series 2000-SRF-1	03/30/00		44,197,995	2.500	10/01/13–22		21,947,995
Series 2000-SRF-2	09/28/00		64,401,066	2.500	10/01/13–22		36,051,066
Series 2001-SRF-1	06/28/01		82,200,000	2.500	10/01/13–24		54,145,000
Series 2001-SRF-2	12/20/01		59,850,000	2.500	10/01/13–24		39,430,000
Series 2002 SRF-1	06/27/02		18,985,000	2.500	04/01/14–23		10,660,000
Series 2002-SRF-2	06/27/02		1,545,369	2.500	04/01/14–23		865,369
Series 2002-SRF-3	12/19/02		31,549,466	2.500	10/01/13–24		19,189,466
Series 2003-SRF-1	06/28/03		48,520,000	2.500	10/01/13–25		34,215,000
Series 2003-SRF-2	09/25/03		25,055,370	2.500	04/01/14–25		16,390,370
Series 2004 SRF-1	06/24/04		2,910,000	2.125	10/01/13–24		1,890,000
Series 2004 SRF-2	06/24/04		18,353,459	2.125	04/01/14–25		11,888,459
Series 2004 SRF-3	06/24/04		12,722,575	2.125	04/01/14–25		8,232,575
Series 2007 SRF-1	09/20/07		167,565,000	1.625	10/01/13–29		140,109,096
Series 2009 SRF-1	04/17/09		16,785,000	2.500	04/01/14–30		9,806,301
Series 2010 SRF-1	01/22/10		4,899,000	2.500	04/01/14–31		3,358,917
Series 2012 SRF-1	08/30/12		14,950,000	2.500	10/01/15–34		4,302,413
Total state revolving loans payable						$	482,872,027

The state revolving loans are issued as part of the State of Michigan's Revolving Fund Loan Program. As the System draws additional amount from time to time hereafter, the outstanding principal amounts of such bonds will correspondingly increase. All loans are callable under terms specified in the loan agreements.

As of June 30, 2013, aggregate debt service requirements of the Fund's debt (fixed-rate and variable-rate) instruments were as follows, to the extent not otherwise adjusted and/or discharged pursuant to a plan of adjustment confirmed in the Bankruptcy Case. These amounts assume that current interest rates on variable-rate bonds will remain the same for their term. As these rates vary, interest payments on variable-rate bonds will vary.

	Principal*	Interest	Total requirements
Year(s) ending June 30:			
2014	$ 78,385,000	145,938,248	224,323,248
2015	86,655,000	142,911,115	229,566,115
2016	89,860,000	140,009,862	229,869,862
2017	92,180,000	136,873,443	229,053,443
2018	95,425,000	133,639,587	229,064,587
2019 – 2023	523,491,843	615,395,483	1,138,887,326
2024 – 2028	611,991,088	500,694,196	1,112,685,284
2029 – 2033	744,584,096	358,892,594	1,103,476,690
2034 – 2038	772,230,000	178,028,565	950,258,565
2039 – 2040	231,385,000	18,246,563	249,631,563
	$ 3,326,187,027	2,370,629,656	5,696,816,683

* The future principal payments exceed the bonds payable balance by $18,820,684 at June 30, 2013 because the future principal payments on capital appreciation bonds are greater than the carrying value of those bonds. The balance of the capital appreciation bonds will increase each year, until maturity, through accretion.

(a) Issuance of State Revolving Loans

The City received loans from the State of Michigan Revolving Loan Fund totaling $10,070,762 during the year ended June 30, 2013. The proceeds of the loans were used to pay costs of acquiring, constructing extensions, and making certain repairs and improvements to the System. At June 30, 2013, $22,418,273 in bonds was authorized and unissued.

(b) Defeased Debt

In previous years, the Fund defeased certain revenue bonds by placing the proceeds of new revenue bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Fund's financial statements. At June 30, 2013, $259,545,000 of bonds outstanding are considered defeased.

(c) Pledges of Future Revenue

The Sewage Disposal Fund has pledged specific revenue streams to secure the repayment of the revenue bonds and State of Michigan Revolving Fund Loans. The bonds and loans are paid solely from the net revenues of the System. A summary of the pledged revenue and the applicable debt as of June 30, 2013 is as follows:

Debt	Type of revenue pledged	General purpose for debt	Term of pledged commitment	Remaining principal and interest requirement	Principal and interest	Pledged Revenue recognized for the year ended June 30, 2013	Proportion of pledged revenue collected
Revenue Bonds and State of Michigan Revolving Fund Loans	All Sewage Disposal Fund operating revenue	Funding of various waste water treatment and collection capital improvements, refund certain sewage disposal revenue bonds, pay termination amounts for interest rate swap agreements, and funding reserve requirements	Thru 2040	$ 5,696,816,683	225,222,903	230,875,249	102.5%

The fund has approximately $416 million in restricted cash and investments related to various bond indentures as of June 30, 2013.

(d) Debt Ratings

In November 2012, Moody’s downgraded the ratings of the Funds Senior and Second Lien Bonds from “Baa2/Baa3” to “Baa3/Ba1.” In June 2013, Moody’s further downgraded the ratings from “Baa3/Ba1” to “Ba1/Ba2” and then to “B1/B2.” In April 2013, Fitch downgraded the ratings of the Senior and Second Lien Bonds as well, from “A/A-” to “BBB+/BBB”. See additional disclosure in note 17(c).

(8) Pension Obligation Certificates (POCs)

The Detroit Retirement Systems Funding Trust issued POCs for the purpose of funding certain unfunded accrued actuarial liabilities (UAAL) of the two retirement systems of the City, which include the General Retirement System (GRS) and the Police and Fire Retirement System (PFRS). The GRS includes employees and retirees of certain governmental funds, proprietary funds (Transportation Fund, Sewage Disposal Fund, and Water Fund) and the Detroit Public Library, a discretely presented component unit of the City.

A trust was created by the General Retirement System Service Corporation (GRSSC) and the Police and Fire Retirement System Service Corporation (PFRSSC), both blended component units of the City. The City entered into service contracts with the GRSSC and PFRSSC to facilitate the transaction.

The POCs were allocated to the governmental activities and the Transportation Fund, Sewage Disposal Fund, and Water Fund based on those funds portion of the overall UAAL liquidated by the use of the

POCs net proceeds. Since the Detroit Public Library is a discretely presented component unit of the City, its prorated portion of the POCs liability assumed was included in the balance of the POCs obligation recorded in the governmental activities.

As of June 30, 2013, the Fund did not remit the required principal payments on the POCs totaling $1,417,492. This payment is considered callable and has been reflected as a current obligation as of June 30, 2013.

In June 2013, Fitch downgraded the rating of the POCs from “CC” to “C” and then again from “C” to “D.” Moody’s downgraded the POC rating in November 2012 from “B3” to “Caa1.” Moody’s further downgraded the POC rating in June 2013 from “Caa1” to Caa3” and then again from “Caa3” to “Ca.” In June 2013, Standard & Poor’s lowered its rating of the POC from “B” to “CCC-”, from “CCC – to “CC” and then further from “CC” to “D.”

The Fund’s regularly scheduled future principal and interest amounts payable would be as follows, to the extent not otherwise adjusted and/or discharged pursuant to a plan of adjustment confirmed in the Bankruptcy case. See note 17(a).

	Principal	Interest	Investment derivatives, net	Total
Year(s) ending June 30:				
2014	$ 3,236,213	3,366,076	2,817,401	9,419,690
2015	2,041,421	2,186,523	2,817,401	7,045,345
2016	2,266,883	2,092,352	2,817,401	7,176,636
2017	2,513,203	1,983,247	2,817,401	7,313,851
2018	2,777,315	1,862,286	2,817,401	7,457,002
2019 – 2023	15,557,194	7,569,421	13,602,639	36,729,254
2024 – 2028	20,166,297	4,482,686	12,053,679	36,702,662
2029 – 2033	27,138,356	3,382,512	6,082,700	36,603,568
2034 – 2035	13,382,761	984,637	244,632	14,612,030
Total	$ 89,079,643	27,909,740	46,070,655	163,060,038

(9) Risk Management

The Fund is exposed to various types of risk of loss including torts; theft of, damage to, or destruction of assets; errors or omissions; job-related illnesses or injuries to employees; natural disasters; and environmental occurrences. The Fund is self-insured for losses such as workers’ compensation, legal, disability benefits, and vehicular liabilities. Also included are risk of loss associated with providing health, dental, and life insurance benefits to employees and retirees.

The Fund, through the City, provides health and dental insurance benefits to employees and retirees through self-insured health plans that are administered by third-party administrators. The Fund does not purchase excess or stop-loss insurance for its self-insured health plans.

The Fund purchases public official liability insurance, property insurance for certain properties, and general liability insurance for accidents occurring at certain properties. The Fund assumes a $250,000 self-insured retention for any one loss or occurrence under its self-insured public official liability program. The Fund purchases excess liability insurance for its general liability for certain properties that provides per occurrence and aggregate protection. The Fund is fully self-insured for environmental-related liabilities and purchases no excess environmental liability insurance.

There were no significant changes in the insurance coverage from coverage provided in the prior year for any of the above-described risks.

A liability for claims is reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Claim liabilities are calculated considering the effects of recent claim settlement trends including frequency and amount of payouts and other economic and social factors. The claim liabilities also include estimated costs for claim administration fees and outside legal and medical assistance costs.

Changes in the balance of claim liabilities for the years ended June 30, 2013 and 2012 are as follows:

		2013	2012
Balance at beginning of year	$	5,073,500	5,042,000
Current year claims and changes in estimates		2,005,090	1,138,018
Claims payments		(3,595,590)	(1,106,518)
Balance at end of year	$	3,483,000	5,073,500

(10) Derivative Instruments

The table below summarizes derivative instrument activity during the reporting period and balances at the end of the period:

	Changes in fair value			Fair value at June 30, 2013			Notional
	Classification		Amount	Classification		Amount	amount
Investment derivatives:							
Pay-fixed interest rate swaps	Interest and investment earnings	$	9,102,234	Long-term liabilities	$	(18,581,500)	48,951,660

As of June 30, 2013, the Fund determined that the pay-fixed interest rate swaps listed as investment derivative instruments no longer met the criteria for effectiveness. Accordingly, the change in fair value of the swaps noted in the above table, and previously deferred amounts totaling $15,979,577 were reported within investment revenue for the year ended June 30, 2013.

The fair values of the interest rate swaps were estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swaps.

(a) Objectives

In order to better manage its interest rate exposure and to reduce the overall costs of its financings, the Fund has been allocated a portion of the City's four separate pay-fixed, receive-variable interest rate swaps related to the POCs and the GRS.

(b) Terms

Certain key terms and fair values relating to the outstanding investment derivative instruments are presented below:

Associated financing issue	Notional amount (1)	Effective date	Rate paid	Rate received	Fair value	Swap termination date	Final maturity of bonds
Investment derivatives:							
Pension obligation certificates:							
Taxable certificate of participation SBSFPC-0009 (2)	$ 16,668,987	06/12/2006	6.36%	3-MTH LIBOR + 0.34%	$ (6,567,466)	06/15/2034	06/15/2034
Taxable certificate of participation SBSFPC-0012 (2)	7,806,843	06/12/2006	6.32	3-MTH LIBOR + 0.30%	(2,726,783)	06/15/2029	06/15/2029
Taxable certificate of participation 37380341 (2)	16,668,987	06/12/2006	6.36	3-MTH LIBOR + 0.34%	(6,563,011)	06/15/2034	06/15/2034
Taxable certificate of participation 37380351 (2)	7,806,843	06/12/2006	6.32	3-MTH LIBOR + 0.30%	(2,724,240)	06/15/2029	06/15/2029
Total	$ 48,951,660				$ (18,581,500)		

(1) Notional amount balance as of June 30, 2013.

(2) Denotes the System's allocation of the associated notional amount.

(c) Credit Risk

Credit risk can be measured by actual market value exposure or theoretical exposure. When the fair value of any swap has a positive market value, then the Fund is exposed to the actual risk that the counterparty will not fulfill its obligations. As of June 30, 2013, the Fund had no net exposure to actual credit risk on its investment derivatives (without regard to collateral or other security arrangements) for any of its counterparties. The table below shows the credit quality ratings of the counterparties to each swap. The Fund uses two different counterparties, as one way of diversifying its credit risk. In addition, the swap agreements contain varying collateral agreements with the counterparties. The swaps require full collateralization of the fair value of the swap should the counterparty's credit rating fall below certain rating levels by Fitch Ratings, Standard & Poor's (S&P), and/or Moody's Investors Service (Moody's). Collateral on all swaps is to be in the form of cash or U.S. government securities held by a third-party custodian. The Fund has not calculated theoretical credit exposure.

Counterparty	S&P	Moody's
SBS Financial Products Company, LLC		
Credit Support provided by Merrill Lynch Capital		
Services, Inc. and guaranteed by Merrill Lynch & Co.	A-	Baa2
UBS, AG	A	A2

(d) Interest Rate Risk

All investment derivatives are pay-fixed, receive-variable interest rate swaps. The Fund believes it has significantly reduced interest rate risk by entering into interest rate swaps, subject to the settlement with the swap counterparties described in note 10 (f) and the potential adjustment of the related POCs pursuant to a plan of adjustment confirmed by the Bankruptcy Case, or the invalidation thereof pursuant to the lawsuit commenced by the City on January 31, 2014 described in note (17).

(e) Basis Risk

The Fund is exposed to basis risk when the variable interest received on a swap is based on a different index than the variable interest rate to be paid on the associated variable rate debt obligation. At June 30, 2013, the associated debt used the same index for the POCs (based on LIBOR) in the table above. As a result, there was no significant exposure to basis risk as of June 30, 2013.

(f) Termination Risk

The Fund or counterparty may terminate any of the swaps if the other party fails to perform under the terms of the contract. In such cases, the Fund may owe or be due a termination payment depending on the fair value of the swap at that time. The termination payment due to a counterparty may not be equal to the fair value. If any of the swaps were terminated, the associated variable rate financings would no longer carry synthetic interest rates.

On January 8, 2009, the City received formal notice from the Swap Counterparty to four of the eight Swap Agreements stating that an event had occurred, which, if not cured by the City, would constitute an Additional Termination Event. On January 14, 2009, the City also received formal notice from the Swap Counterparty to the four remaining Swap Agreements, stating that the applicable Swap Insurers had been downgraded below the thresholds set forth in the Swap Agreements. Under the Swap Agreements, such Swap Insurer downgrades, coupled with the downgrades of the POCs, if not cured by the City, constitute an Additional Termination Event. In June 2009, the City and the Counterparties agreed to an amendment to the Swap Agreements, and thereby eliminating the Additional Termination Event and the potential for an immediate demand for payment to the Swap Counterparties. As part of the amended Swap Agreements, the Counterparties waived their right to termination payments. Additionally, the City now directs its Wagering Tax revenues to a Trust as collateral for the quarterly payment to the Counterparties, increased the Swap rate by 10 basis points effective July 1, 2010, and agreed to other new termination events. The termination events under the amended Swap Agreement includes a provision granting the Counterparties the right to terminate the amended Swap Agreement if certain coverage levels of the Wagering Taxes over the required quarterly payment are not met or if POCs ratings are withdrawn, suspended, or downgraded below “Ba3” (or equivalent). In March 2012, the POCs received a credit downgrade below “Ba3.” In light of the debt rating declines of the City, a risk of a Swap Agreement Termination exists.

In December 2013, the City had negotiated an agreement with the counterparties to terminate the swaps, but the Bankruptcy Court rejected the agreement and the agreement was subsequently terminated. After the termination of this agreement, the City continued to negotiate with the swap counterparties in an effort to reduce the City’s obligation under the swap agreements. These negotiations resulted in the parties’ agreement on the principal terms of a settlement and plan support agreement pursuant to which, among other things, the City will pay, overtime, the aggregate sum of $85 million in full satisfaction of the claims between the parties (the Plan Support Agreement). On March 3, 2014, the City filed a motion seeking Bankruptcy Court’s approval of the Plan Support Agreement pursuant to section 105(a) of the Bankruptcy Code and Rule 9019 of the Federal Rules of Bankruptcy Procedure (the Renewed Settlement Motion). On April 15, 2014, the Bankruptcy Court entered an order approving the renewed settlement motion.

(g) Rollover Risk

The Fund is exposed to rollover risk on swaps that mature or may be terminated prior to the maturity of the associated financings. When these swaps terminate, or in the case of the termination option, if the counterparty exercises its option, the Fund will not realize the synthetic rate offered by the swaps on the underlying issues. The Fund is exposed to rollover risk on the GRS swaps should they be terminated prior to the maturity of the associated financings (POCs).

(h) Foreign Currency Risk

All derivatives are denominated in U.S. dollars, and therefore, the Fund is not exposed to foreign currency risk.

(i) Market Access Risk

The Fund is exposed to market access risk on swaps in the event it will not be able to enter credit markets or in the event the credit will become more costly.

(11) Pension Plan

The City’s proposed plan of adjustment (see note 17(a)) proposes significant changes to its pension plans. Confirmation of a plan of adjustment may materially restructure benefits available under such plans.

Substantially all employees of the City, including employees of the Fund, are covered by a single-employer plan composed of a defined benefit with an optional employee-contributed annuity through the GRS. The GRS pays a monthly pension to qualified individuals upon retirement. The amount is based upon a combination of years of service and annual salary.

(a) Plan Description

The GRS is administered in accordance with the City of Detroit Charter and union contracts, which assign the authority to establish and amend contributions and benefit provisions to the GRS board of trustees. The GRS issues separate, stand-alone financial statements annually. A copy of these financial statements can be obtained at the Coleman A. Young Municipal Center, 2 Woodward Avenue, Room 908, Detroit, Michigan 48226.

(b) Funding Policy

The GRS 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. The contribution requirements are established and may be amended by the GRS board of trustees based on information provided by the GRS consulting actuary. The City’s contribution is set by the City Council in conjunction with its approval of the City’s annual budget based on information provided by the GRS consulting actuary.

The recommended contribution rate is determined by the GRS’ consulting actuary using the entry age normal actuarial cost-funding method. Significant actuarial assumptions used to compute contribution requirements are the same as those used to compute the actuarial accrued liability.

Based upon the June 30, 2011 actuarial valuation, the actuarial required contribution rate for the Fund was 28.32% of covered payroll for the year ended June 30, 2013. Contributions for the Fund were $10,767,650 for the year ended June 30, 2013.

Employees may also elect to contribute (a) 0%, (b) 3% of annual compensation up to the Social Security wage base and 5% of any excess over that, (c) 5%, or (d) 7% toward annuity savings. Contributions are voluntary for all union and nonunion employees. Contributions received from Fund employees were $2,325,357 during the year ended June 30, 2013.

The contribution requirements of plan members and the City are established and may be amended by the board of trustees in accordance with the City Charter, union contracts, and plan provisions. Members may retire with full benefits after attaining 30 years of service; age 55 with 30 years of

(Continued)

service if hired after January 1, 1996; age 60 with 10 years of service; or age 65 with 8 years of service. Employees may retire after 25 years of service and collect an actuarially reduced retirement benefit. Monthly pension benefits, which are subject to certain minimum and maximum amounts, are determined according to fixed rates per year of credited service. Members of the GRS who separated prior to July 1, 1981, met the age and service requirements, and who did not withdraw their accumulated annuity contributions are generally eligible for a pension at the time they would have been eligible had they continued in City employment. Members who separate after July 1, 1981 are not required to leave their accumulated annuity contributions in the System. Pension benefits for all members of the GRS are increased annually by 2.25% of the original pension.

The annual pension cost and the change in net pension asset allocated to the Fund for the year ended June 30, 2013 were as follows:

Annual required contributions	$	12,681,196
Interest on net pension asset		(6,774,250)
Adjustment to annual required contribution		4,858,137
Annual pension cost		10,765,083
Contributions made (employer)		10,767,650
Change in net pension asset		2,567
Net pension asset, beginning of year		86,245,896
Net pension asset, end of year	$	86,248,463

The actuarial methods and significant assumptions used to determine the annual required contributions (ARCs) for the year ended June 30, 2013 were as follows:

Valuation date	June 30, 2011
Actuarial cost method	Entry age
Amortization method	Level percent
Remaining amortization period for unfunded accrued liabilities	30 years, open
Asset valuation method	7-year smoothed market
Actuarial assumptions:	
Investment rate of return	7.90%
Projected salary increases*	4.00% – 8.90%
Cost-of-living adjustments	2.25%

* Includes inflation rate of 4.00%.

(c) *Three-Year Trend Information*

	Fiscal year ended	Annual pension cost (APC)	Percentage of APC contributed	Net pension asset
General Retirement System	June 30, 2013	$ 10,765,083	100%	$ 86,248,463
	June 30, 2012	4,899,740	87	86,245,896
	June 30, 2011	9,264,926	83	86,874,832

(d) *Funded Status and Funding Progress Based on Actuarial Assumptions of GRS*

The funded status of the GRS plan as of June 30, 2012 (the most recent actuarial valuations available) based on actuarial assumptions of GRS is as follows:

Actuarial value of assets	$ 2,806,489,202
Actuarial accrued liability	$ 3,644,172,577
Unfunded (overfunded) AAL	$ 837,683,375
Funded ratio	77.0%
Covered payroll	$ 257,992,420
Ratio of UAAL/covered payroll	324.7%

Significant actuarial assumptions used by GRS to determine the funded status for the year ended June 30, 2012 are as follows:

Valuation Date	June 30, 2012
Actuarial Cost Method	Entry Age
Asset Valuation Method	7-year Smoothed Market
Actuarial Assumptions:	
Investment Rate of Return	7.9%
Projected Salary Increases	4.0% – 8.9%
Includes Inflation at	4.0%
Cost-of-Living Adjustments	2.25%

(e) Funded Status and Funding Progress Based on Actuarial Assumptions of the City

As discussed further in note 17, and in connection with the City's filing of a voluntary petition under Chapter 9 of the Bankruptcy Code, the City utilized different actuarial assumptions than GRS to determine the funded status of the plan. Specifically, the City believes that an investment rate of return of 7.0%, instead of 7.9% used by GRS is more achievable. Additionally, the City believes the actual market value of plan assets instead of a 7-year smoothed market value is more appropriate in measuring the funded status of the plan. The funded status of the plan as of June 30, 2012 (the most recent actuarial valuations available) based on the City's actuarial assumptions, is as follows:

Actuarial value of assets	$ 2,159,000,000
Actuarial accrued liability	$ 4,085,000,000
Unfunded (overfunded) AAL	$ 1,926,000,000
Funded ratio	52.9%
Covered payroll	$ 257,992,420
Ratio of UAAL/covered payroll	746.5%

Significant actuarial assumptions used by the City to determine the funded status for the year ended June 30, 2012 are as follows:

Actuarial Cost Method	Entry Age
Asset Valuation Method	Actual Market Value
Actuarial Assumptions:	
Investment Rate of Return	7.0%
Projected Salary Increases	4.0% – 8.9%
Includes Inflation at	4.0%
Cost-of-Living Adjustments	2.25%

(f) Administrative Expenses

Actuarial investment management and bank trustee fees and expenses are included in the GRS plan's administrative expenses when incurred. In addition, the GRS plan's administrative salary, rent, accounting services, duplicating, telecommunications, and travel expenses are included in the GRS plan's administrative expenses when incurred.

(12) Other Postemployment Benefits

(a) Plan Description

The employees of the Fund participate in the Employee Health and Life Insurance Benefit Plan (Benefit Plan), which is a single-employer defined benefit plan administered by the City and City's Retirement Systems. The Benefit Plan provides hospitalization, dental care, vision care, and life insurance to all officers and employees of the City who were employed on the day preceding the effective date of the Benefit Plan and who continue in the employ of the City on and after the effective date of the Benefit Plan. Retirees are allowed to enroll in any of the group plans offered by the City to active employees. The City provides healthcare coverage for substantially all retirees in accordance with terms set forth in union contracts or provisions found in Section 13, Article 8 of the Code of Ordinances.

The healthcare benefit eligibility conditions for Fund employees hired before 1995 are 30 years of creditable service or age 60 and 10 years of creditable service or age 65 and 8 years of creditable service. The healthcare benefit eligibility conditions for Fund employees hired on after 1995 are age 55 and 30 years of creditable services, or age 60 and 10 years of creditable service or age 65 and 8 years of creditable service. The City provides full healthcare coverage to Fund employees who retired prior to January 1, 1984, except for the Master Medical benefit that was added on to the coverage after that date. The Fund pays up to 90 percent of healthcare coverage if retired after January 1, 1984; however, for Fund employees who retired between January 1, 1984 and June 30, 1994, the retiree share has been reduced by 50% by appropriations from City Council. The Fund also pays healthcare coverage for the spouse, under the same formulas noted above, as long as the spouse continues to receive a pension. The Fund does not pay healthcare coverage for a new non-City retiree spouse. Dental and vision coverage is provided for the retiree and the spouse.

The City does provide healthcare coverage to Fund employees that opt for early retirement. For Fund employees hired before 1995, the healthcare benefit eligibility conditions are 25 years of creditable service and employees hired after 1995 is age 55 and 25 years of creditable service. The coverage begins when the retiree would have been eligible for normal retirement. The Fund pays up to 90% of healthcare coverage for the retiree and the spouse. The Fund pays up to 90% of healthcare coverage for the spouse as long as the spouse continues to receive a pension. The City does not pay for healthcare coverage for a new non-City retiree spouse. Dental and vision coverage is provided for the retiree and the spouse.

The City also provides healthcare coverage to Fund employees who meet certain healthcare benefit eligibility conditions at reduced rates for those that retire under the Deferred Retirement Benefits (Vested), the Death-in-Service Retirement Benefits Duty and Non-Duty Related, and the Disability Retirement Benefits Duty and Non-Duty Related. Complementary healthcare coverage is provided by the City for those Fund retirees that are Medicare-Eligible. Fund retirees who opt out of the retiree healthcare coverage may obtain coverage at a later date.

In addition to healthcare coverage, the City allows Fund retirees to continue life insurance coverage under the Group Insurance Protection Plan offered to active employees in accordance with Section 13, Article 9 of the Code of Ordinances. The basic life insurance coverage for Fund employees is based on the employee's basic annual earnings to the next higher thousand dollars. The life insurance benefit amounts range from $3,750 to $12,500.

The Supplemental Death Benefit Plan (Supplemental Plan) is a pre-funded single-employer defined benefit plan administered by the Employee Benefits Board of Trustees. The money is held in the City of Detroit Employee Benefit Trust and the City uses the trust fund to account for the Supplemental Plan. In accordance with Section 13, Article 8 of the Code of Ordinances, effective July 1, 1999 and prior to the member's retirement from the City, a death benefit of $10,000 will be paid. After retirement of the member from the City, the amount of death benefits paid is based upon the retiree's years of City service ranging from $1,860 (for 8 to 10 years of service) to $3,720 (for 30 years of service). For years of service beyond 30 years, $93.00 will be added per year for each additional year of service.

There were 894 retirees eligible for benefits, as of June 30 2013. These plans do not issue separate financial statements.

Under the City's proposed plan of adjustment in the Bankruptcy Case (see note 17(a)), the City intends to establish voluntary employees' beneficiary association trust that provide life, sickness, accident, and other similar benefits to current and future retirees of the City and certain of their dependents who are eligible for benefits. Upon the effectiveness of such plan, if such plan is confirmed, the City would have no further responsibility to provide life insurance or death benefits to retirees.

(b) Funding Policy

Employee Health and Life Insurance Benefit Plan – The cost of benefits for the Benefit Plan, which is financed on a pay-as-you-go basis, for the year ended June 30, 2013 for the Fund retiree's was as follows:

Benefits		Fund cost	Retiree cost	Total cost
Hospitalization	$	10,628,280	1,378,604	12,006,884
Dental		485,567	40,792	526,359
Vision		86,081	6,653	92,734
Life insurance		11,518	978	12,496
	$	11,211,446	1,427,027	12,638,473

Supplemental Death Benefit Plan – The cost of benefits for the Supplemental Plan, which is a pre-funded plan, with the funds held in the City of Detroit Employee Benefit Trust, for the year ended June 30, 2013 for the Fund retiree's was as follows:

Benefit		Fund cost	Retiree cost	Total cost
Supplemental death benefit plan	$	9,986	1,283	11,269

The City of Detroit Employee Benefit Trust paid death benefits in the amount of $80,470 for the Fund retirees for the year ended June 30, 2013.

(c) *Annual OPEB Costs and Net OPEB Obligation*

The Fund's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pension*. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial accrued liabilities (or funding excess) over a period not to exceed 30 years.

The following table shows the components of the Fund's annual OPEB cost for the year ended June 30, 2013, the amount actually contributed to the plans, and changes in the Fund's OPEB obligation for the retirees of the Fund:

		Employee health and life insurance benefit plan	Supplemental death benefit plan	Total
Annual required contribution (ARC)	$	24,370,834	78,984	24,449,818
Interest on net OPEB obligation		2,266,556	8,608	2,275,164
Adjustment to ARC		(1,888,797)	(5,739)	(1,894,536)
Annual OPEB cost (expense)		24,748,593	81,853	24,830,446
Contributions made		(11,211,446)	(9,986)	(11,221,432)
Changes in net OPEB obligation		13,537,147	71,867	13,609,014
Net OPEB obligation, beginning of year		56,663,918	172,163	56,836,081
Net OPEB obligation, end of year	$	70,201,065	244,030	70,445,095

(Continued)

The annual OPEB cost, the percentage of annual OPEB cost contributed to each plan, and the net OPEB obligation for the three most recent fiscal years ended June 30 for the retirees of the Fund were as follows:

	Year ended	Annual OPEB cost	Actual contributions	Percentage of annual OPEB cost contributed	Net OPEB obligation
Employee Health and Life Insurance Benefit Plan	June 30, 2013	$ 24,748,593	$ 11,211,446	45.3%	$ 70,201,065
	June 30, 2012	23,677,318	10,102,647	42.7	56,663,918
	June 30, 2011	22,427,487	9,754,558	43.5	43,089,247
Supplemental Death Benefit Plan	June 30, 2013	81,853	9,986	12.2%	244,030
	June 30, 2012	80,747	23,176	28.7	172,163
	June 30, 2011	91,481	12,611	13.8	114,592

(d) Funded Status and Funding Progress

Employee Health and Life Insurance Benefit Plan (Benefit Plan) – As of June 30, 2011, the most recent actuarial valuation date for the Benefit Plan, the actuarial accrued liability for benefits related to all current and former City employees was $5,718,286,228, and the actuarial value of assets was zero, resulting in an unfunded actuarial accrued liability (UAAL) of $5,718,286,228. The covered payroll (annual payroll of all active City employees covered by the plan) was $444,358,728 and the ratio of the UAAL to the covered payroll was 1,287%. The funded status related to the retirees of the Fund was not available.

Supplemental Death Benefit Plan (Supplemental Plan) – As of June 30, 2011, the most recent actuarial valuation date for the Supplemental Plan, the actuarial accrued liability for benefits related to all current and former City employees was $34,564,960 and the actuarial value of assets was $25,681,765, resulting in an unfunded actuarial accrued liability (UAAL) of $8,883,195. The covered payroll (annual payroll of all active City employees covered by the plan) was $444,358,728 and the ratio of the UAAL to the covered payroll was 2.0%. The funded status related to the retirees of the Fund was not available.

Actuarial valuations of the ongoing plans involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

A schedule of funding progress, which presents multiyear trend information about whether the actuarial value of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits, is included in the City's Comprehensive Annual Financial Report.

(Continued)

(e) Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and the plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

The actuarial methods and significant assumptions used to determine the annual required contributions for the year ended June 30, 2013 were as follows:

	Employee health and life insurance benefit plan	**Supplemental death benefit plan**
Valuation date	June 30, 2011	June 30, 2011
Actuarial cost method	Individual entry-age	Individual entry-age
Amortization method	Level percent	Level dollar
Amortization period for		
unfunded actuarial accrued liabilities	30 years, open	30 years, open
Asset valuation method	N/A	3 year smoothed market
Actuarial assumptions:		
Investment rate of return	4.0%	5.0%
Projected salary increases*	4.0%	N/A
Healthcare cost trend rate	8.5% for 2013, grading down to 4.5% in 2021 and 4.0% in 2022 and beyond	N/A

* Includes inflation rate of 4.0%.

In the June 30, 2011 actuarial valuation for the Employee Health and Life Insurance Benefit Plan, the mortality tables used by the City's plan to evaluate death benefits to be paid for retirees was 110% of the RP 2000 Combined Male and 110% of the RP 2000 Combined Female table setback two years. The City's plan used an annual rate of retirement of 50%, initially, reduced to an ultimate rate of 20% after age 70 for General City.

In the June 30, 2011 actuarial valuation for the Supplemental Death Benefit Plan, the mortality tables used by the City's plan to evaluate death benefits to be paid for Fund retirees was 120% of the RP 2000 Combined Male and 120% of the RP 2000 Combined Female table setback two years. The City's plan used an annual rate of retirement of 50%, initially, reduced to an ultimate rate of 20% after age 70 for General City.

(13) Due from (to) Other Funds

During the course of operations, numerous transactions occur between individual funds and other City funds for goods provided or services rendered. Related receivables and payables are classified as "due from other funds" or "due to other funds," respectively, on the statement of fund net assets, will be settled within one year, and are summarized as follows as of June 30, 2013:

Due from other funds:		
General Fund	$	14,718,135
General Retirement System Service Corporation		33,121
Fiduciary Fund		1,409,855
Total due from other funds	$	16,161,111
Due to other funds:		
General Fund	$	6,257,680
Other governmental funds		3,512,108
Water Fund		42,266,431
Total due to other funds	$	52,036,219

(14) Capital Improvement Program

The Fund is engaged in a variety of projects that are a part of its five-year Capital Improvement Program (the Program). The total cost of this Program is anticipated to be approximately $594 million through fiscal year 2018. The Program is being financed primarily from revenues of the Fund and proceeds from the issuance of revenue bonds.

The total amount of construction contract commitments outstanding at June 30, 2013 was approximately $808.3 million.

(15) Contingencies

The City is subject to various government environmental laws and regulations. GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, established accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remedial activities such as site assessments and cleanups. The standard excludes pollution prevention or control obligations with respect to current operations, and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and postclosure care. The Fund determined that there were no estimated pollution remediation obligations to be recorded at June 30, 2013.

The operation of the Fund's Waste Water Treatment Plant (WWTP) is subject to regulation pursuant to the Federal Water Pollution Control Act, as amended by the Clean Water Act of 1977 and the Water Quality Act of 1987 (collectively, the Clean Water Act). Included in the regulatory framework established by the Clean Water Act is the National Pollutant Discharge Elimination System (NPDES) permit program, which requires operation of wastewater treatment facilities according to discharge limitations and other requirements as set forth in permits issued to each facility. The EPA has authorized the State of Michigan Department of Environmental Quality (MDEQ) to implement and enforce the federal NPDES permit program.

The Fund operates the WWTP pursuant to an NPDES permit that was renewed through October 1, 2017.

The Fund is also a defendant in numerous alleged claims, lawsuits, billing disputes, and other stated and pending demands. The Fund and the City's Legal Department have estimated a reserve, which is included in the accompanying financial statements, for the potential outcome of such claims or the amount of potential damages in the event of an unfavorable outcome for each of the above contingencies. The Fund's management and the City's Legal Department believe that any differences in reserved amounts and final settlement, after consideration of claims covered by insurance, resulting from such litigation will not materially impact the Fund's financial position or results of operations.

The City holds various commercial insurance policies to cover other potential loss exposures.

(16) Compliance with Finance-Related Legal and Contractual Provisions

Bond ordinances require amounts to be held on deposit in a Bond and Interest Redemption Fund such that the aggregate balance is sufficient to provide for payment, when due, of the current principal and interest.

During the fiscal year ended June 30, 2013, the balance in the Bond and Interest Redemption Fund was not in compliance with these ordinances. However, the Fund transferred the required amounts on July 1, 2013 and made the principal and interest payments on a timely basis.

(17) Bankruptcy and Subsequent Events

(a) Bankruptcy

The City of Detroit was insolvent on June 30, 2013 as the General Fund liabilities exceeded its assets by $73.0 million and cash and investments on hand totaling $102.2 million were insufficient to meet obligations due. The City's accumulated unassigned General Fund deficit was $132.6 million on June 30, 2013. On June 15, 2013, due to liquidity constraints, the City did not make a principal and interest payment totaling $41.0 million ($33.3 million due from the General Fund) due on its pension obligation certificates of participation (POCs). In addition, as of June 30, 2013, the City did not make a payment of $105.6 million ($96.9 million General Fund) of pension contributions due to the General Retirement and Police and Fire Retirement systems. Also, the City's General Fund owed the Other Post Employment Benefits Fund $44.4 million on June 30, 2013. Furthermore, as of June 30, 2013, the City's General Fund has utilized restricted funds of $69.6 million from the Risk management and Motor Vehicle accounts and the Solid Waste Fund to cover other obligations.

Over the past several decades, the City has experienced significant economic and social challenges that have negatively impacted employment, business conditions and quality of life. Three of the City's largest revenue streams – distributable state aid, property taxes, and municipal income taxes – are especially susceptible during times of major economic downturns and have declined in recent years due to high levels of unemployment. Population decline and home foreclosures have adversely impacted City property valuations and property and income tax collections. Further stressing the City's liquidity are legacy costs such as retiree health care and debt service. As the City's tax base and revenues decline, the legacy costs become an increasing percentage of the General Fund budget reducing funding available for essential services such as police and fire.

In February 2013, a financial review team appointed by the Governor of the State of Michigan determined that a local government financial emergency existed in the City. On March 14, 2013, the Local Emergency Financial Assistance Loan Board appointed Kevyn Orr as the emergency financial manager of the City in accordance with Public Act 72 of 1990, the Local Government and School District Fiscal Responsibility Act. On March 28, 2013, Public Act 436 of 2012, the Local Financial Stability and Choice Act, took effect which replaced Public Act 72. Public Act 436 specified that an emergency financial manger appointed under Public Act 72 of 1990 and serving on the effective date of Public Act 436 of 2012 would continue to serve under the new act. Public Act 436 changed the title of the emergency financial manager to emergency manager and expanded the powers of the emergency manager to include the ability to recommend to the Governor that the City file a petition for relief under chapter 9 of title 11 of the United State Code (the "Bankruptcy Code").

On July 18, 2013, the Governor delivered the Authorization Letter to the emergency manager and the State treasurer authorizing the City to commence a bankruptcy case under Chapter 9 of the Bankruptcy Code. In the Authorization Letter, the Governor agreed with the emergency manager that chapter 9 offers the only feasible alternative to fix the City's finances and to complete a sustainable restructuring for the benefit of Detroit's approximately 700,000 residents. Based on the emergency manager's Recommendation Letter, the Governor determined that: (a) the City cannot meet its obligations to its citizens; (b) the City cannot meet its basic obligations to its creditors; (c) the City's failure to meet its obligations to its citizens is the primary cause of its inability to meet its obligations to its creditors; and (d) the only feasible path to ensuring the City will be able to meet obligations in the future is to have a successful restructuring under the federal bankruptcy process.

Upon receiving the Authorization Letter, the emergency manager issued an order directing the commencement of the City's chapter 9 bankruptcy case. Consistent with these approvals, on July 18, 2013, the City filed a voluntary petition under chapter 9 of the Bankruptcy Code in the Bankruptcy Court, which case is captioned In re City of Detroit, Michigan, Case No. 13-53846 (Bankr. E.D. Mich.).

On July 19, 2013, Bankruptcy Judge Steven W. Rhodes was assigned to the Bankruptcy Case by the Chief Judge of the United States Court of Appeals for the Sixth Circuit.

On December 5, 2013, the Bankruptcy Court entered (a) the Eligibility Order stating that the City is eligible to be a debtor under chapter 9 of the Bankruptcy Code and (b) the Order for Relief entitling the City to proceed under chapter 9.

Notices of appeal of the Eligibility Order were filed by a number of entities, all of whom also filed petitions for permission to appeal the Eligibility Order directly to the United States Court of Appeals for the Sixth Circuit (the Sixth Circuit). The Sixth Circuit granted these parties' petitions on February 21, 2014, and a briefing schedule has been established. All appeals of the Eligibility Order pending in the District Court have been stayed pending the Sixth Circuit's disposition of the various appeals pending before it. By law, the Bankruptcy Case is not stayed pending the resolution of the various appeals of the Eligibility Order.

Under chapter 9 of the Bankruptcy Code, actions by creditors to collect indebtedness the City owed prior to the Petition Date were stayed, and certain other pre-petition contractual obligations may not be enforced against the City. The chapter 9 filing has enabled the City to continue to operate and provide services to its residents by freezing certain pre-petition debts until a plan of adjustment can be approved. The City has been paying certain pre-petition liabilities, including certain employee salaries, wages, benefits, and other obligations, during the Bankruptcy Case. Other unsecured obligations owed by the City at July 18, 2013 are subject to compromise in the bankruptcy process. The City has stopped making payments related to unsecured funded debt and legacy liabilities, with the exception of retiree healthcare benefits and certain vendors providing essential goods and services.

Since filing the Bankruptcy Case, the emergency manager has coordinated the City's legal strategy related to bankruptcy with his professional advisors. Certain of the primary activities to date in the Bankruptcy Case are summarized below:

Administrative Matters

Since the Petition Date, the emergency manager has taken steps to preserve the benefits and protections afforded by the automatic stay imposed by sections 362 and 922 of the Bankruptcy Code (the Chapter 9 Stay). For example, at the outset of the Bankruptcy Case, the City obtained orders of the Bankruptcy Court (a) confirming the application of the Chapter 9 Stay to the City and its officers and inhabitants and (b) extending the protections of the Chapter 9 Stay to, among others, nondirector City employees and certain State officials.

Upon a motion filed by the City, the Bankruptcy Court entered an order on November 21, 2013 establishing certain bar dates for the filing of proof of claims. Also upon a motion of the City, the Bankruptcy Court entered an order on December 24, 2013, approving certain alternative dispute resolution procedures to facilitate the resolution of certain contingent, unliquidated and/or disputed claims against the City that arose prior to the Petition Date. The City's proposed plan of adjustment establishes a claims resolution process that will enable the City to resolve the claims that will be addressed pursuant to such plan.

Retiree Committee

Since the Petition Date, the emergency manager has continued to participate in negotiations with the City's creditors and other interested parties with the goal of reaching consensus, to the fullest extent possible, on the terms of a plan of adjustment. In support of these discussions, at the outset of the Bankruptcy Case, the City requested the appointment of an official committee of retired employees (the Retiree Committee) to represent the interests of retirees in these negotiations. Prior to the commencement of the Bankruptcy Case, no single party was empowered to represent all of the City's retirees, who hold billions of dollars of legacy claims that must be addressed in any restructuring. On August 2, 2013, the Bankruptcy Court entered an order directing the appointment of the Retiree Committee, which was formed on August 22, 2013. Since that time, the City has conducted discussions with the Retiree Committee and its advisors regarding the City's restructuring and the treatment of retirees' claims, which discussions have resulted in an agreement with respect to retiree claims for pension and medical benefits under the plan of adjustment.

Swap Settlement

Prior to the Petition Date, the emergency manager reached a consensual resolution with the counterparties to the City's interest rate swap agreements (the Swap Counterparties) that would, among other things, allow the City to terminate its obligations under the swap agreements in exchange for approximately $235.0 million (the Settlement Payment). This agreement was memorialized in a Forbearance and Optional Termination Agreement (the FOTA) between the City and the Swap Counterparties. On the Petition Date, the City filed a motion with the Bankruptcy Court to assume the FOTA under section 365 of the Bankruptcy Code and approve the parties' settlement under Rule 9019 of the Federal Rules of Bankruptcy Procedure (the Settlement Motion). There was significant opposition to the Settlement Motion, which resulted in litigation regarding, among other things, the appropriateness of the compromises in the FOTA, the Swap Counterparties' ability to consummate the FOTA and the City's ability to make the Settlement Payment. An evidentiary hearing on the Settlement Motion commenced on December 17, 2013. On December 18, 2013, the Bankruptcy Court ordered the City and the Swap Counterparties back to mediation to discuss a reduction of the Settlement Payment. On December 24, 2013, the parties agreed to fix the Settlement Payment at the reduced amount of $165 million. The hearing on the Settlement Motion was concluded on January 13, 2014, and, on January 17, 2014, the Bankruptcy Court issued an order denying the Settlement Motion. On February 6, 2014, the City filed a notice of termination of the FOTA.

After the termination of the FOTA, the City continued to negotiate with the Swap Counterparties in an effort to reduce the City's obligations under the swap agreements. These negotiations resulted in the parties' agreement on the principal terms of a settlement and plan support agreement pursuant to which, among other things, the City will pay, over time, the aggregate sum of $85 million in full satisfaction of the claims between the parties (the Plan Support Agreement). On March 3, 2014, the City filed a motion seeking the Bankruptcy Court's approval of the Plan Support Agreement pursuant to section 105(a) of the Bankruptcy Code and Rule 9019 of the Federal Rules of Bankruptcy Procedure (the Renewed Settlement Motion). On April 15, 2014, the Bankruptcy Court entered an order approving the Renewed Settlement Motion, which order was subsequently appealed by certain parties in interest.

Mediation

The Bankruptcy Court established a mediation program to facilitate the negotiation of restructuring issues. In particular, Judge Rhodes appointed Judge Gerald E. Rosen, Chief Judge for the United States District Court for the Eastern District of Michigan, as the lead mediator for the City's Bankruptcy Case. In turn, Judge Rosen appointed six additional mediators, each focusing on different elements of the City's restructuring and reorganization activities. To date there have been multiple mediation sessions and numerous written submissions related to, among other things, the City's core restructuring initiatives outlined in the City of Detroit Proposal for Creditors, dated June 14, 2013; issues arising in connection with the City's general obligation debt; labor and pension matters; and matters related to the future of the DWSD.

POC Litigation

On January 31, 2014, the City commenced an adversary proceeding in the Bankruptcy Court by filing a complaint against the Service Corporations and the funding trusts (the Funding Trusts) that issued the POCs, alleging that the 2005 and 2006 transactions and agreements resulting in the sale of the POCs to the public was invalid, illegal and unenforceable because the $1.5 billion of debt incurred by the City exceeded the City's statutory debt limit and was not incurred in conformity with other state laws. The complaint seeks (a) a declaratory judgment that the POC transactions are illegal, void and of no effect whatsoever; (b) a declaratory judgment that any Claims based on the City's obligations under the Service Contracts on account of the POCs should be disallowed pursuant to 11 U.S.C. § 502(b)(1); and (c) an injunction prohibiting the defendants from taking any action to require the City to make payments or provide distributions under a plan of adjustment on account of the POCs.

The Funding Trusts answered the complaint on March 17, 2014, (a) denying the City's allegations that the POC transactions caused the City to exceed its statutory debt limit and created debt not in conformity with other state laws, (b) raising several affirmative defenses and (c) asserting several counterclaims against the City. On April 10, 2014, the City moved to dismiss substantially all of the counterclaims brought by the Funding Trusts. Also on March 17, 2014, motions to intervene in the adversary proceeding were filed by Financial Guarantee Insurance Company, an insurer of the POCs, and several POC holders. On April 10, 2014, the Service Corporations moved to dismiss the complaint as to them, arguing primarily that the City lacked standing to bring suit against the Service Corporations. A hearing was held on the motions to intervene and the Service Corporations' motion to dismiss on May 15, 2014. On June 30, 2014, the Bankruptcy Court entered an order denying the Service Corporations' motion to dismiss and granting the motions to intervene for the limited purpose of defending against the City's claims in the complaint.

Plan of Adjustment

The Bankruptcy Court set a deadline of March 1, 2014 for the City to file a plan of adjustment in the Bankruptcy Case. On February 21, 2014, the City filed its plan of adjustment and a related disclosure statement. On March 31, 2014, the City filed its amended plan of adjustment and amended disclosure statement. On April 16, 2014, the City filed its second amended plan of adjustment and second amended disclosure statement. On April 25, 2014, the City filed its third amended plan of adjustment and third amended disclosure statement. On May 5, 2014, the City filed its fourth amended plan of adjustment and fourth amended disclosure statement. Also on May 5, 2014, the Bankruptcy Court entered an order approving the disclosure statement and the mailing of the disclosure statement and plan of adjustment to creditors to vote on. The plan of adjustment (as it has been and may be further amended, modified, or supplemented, the "Plan) is subject to further change.

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On July 21, 2014, Kurtzman Carson Consultants LLC filed a declaration regarding the solicitation and tabulation of votes on, and the results of voting with respect to, the fourth amended plan of adjustment. Those impaired classes that voted to accept the Plan included the PFRS pension claims, GRS pension claims, OPEB claims, COP Swap claims and Unlimited Tax General Obligation Bond claims. Those impaired classes that voted to reject the Plan included the COP claims and certain classes of DWSD debt. A hearing to consider confirmation of the Plan is scheduled to commence on August 14, 2014. The Plan is subject to challenge by creditors or to modification made as the result of issues that may be raised by the Bankruptcy Court. Copies of the Plan and the related disclosure statement can be found on the City's website at:
http://www.detroitmi.gov/EmergencyManager/BankruptcyChapter9.aspx.

The Plan provides a framework to restructure the City's long-term obligations such that the City can exit bankruptcy and return to fiscal stability. It provides for the adjustment of secured and unsecured debt and outlines proposed reinvestment initiatives. The Plan proposes that unsecured Nonretiree creditors with whom the City has not reached a settlement generally will receive an approximately 10%-13% recovery on their claims. The Plan also proposes for the City to invest approximately $1.4 billion over 10 years to, among other things: (1) comprehensively address and remediate residential urban blight, (2) improve the operating performance and infrastructure of its police, fire, EMS and transportation departments (among other departments), (3) modernize its information technology systems on a City-wide basis and (4) improve services at all levels to Detroit's citizens.

The Plan includes settlements that the City believes will inure to the benefit of the City's creditors and its residents. The City settled controversial and sensitive issues relating to the Detroit Institute of Arts, which settlement is expected to yield at least $466 million to provide a source of recovery for the approximately 33,000 individuals who participate in the City's two Retirement Systems. The State of Michigan is also participating in this settlement and will contribute the value of $350 million to the City's two retirement systems in exchange for, among other things, the receipt of releases from pension claimants.

The Plan also proposes a reduction in health care benefits for retirees. The Plan provides for the establishment of two VEBAs (Voluntary Employees Beneficiary Association) in accordance with section 501(c)(9) of the Internal Revenue Code of 1986, as amended, that would provide health care, life and other benefits to beneficiaries and certain of their dependents. The "Detroit Police and Fire VEBA" would be established for retired police and fire uniform employees and the "Detroit General VEBA" would be established for the retirees in the General Retirement System. The two VEBAs will each be governed by a board of trustees who will be responsible for management of the assets held by the VEBA, administration, and determination of the level of distribution of benefits to the beneficiaries. The Plan contemplates that the City will distribute to both VEBAs an appropriate share of New B Notes, which will be issued pursuant to the Plan. Under the Plan, the City will have no responsibility following the effectiveness thereof to provide life insurance or death benefits to current or former employees.

The total gain expected to occur by adjusting the City's debts pursuant to the proposed Plan is not reasonably measured or estimated, given that settlements with all creditors have not been reached and the Plan has not been confirmed by the Bankruptcy Court as of the date of this report. The Plan does not contemplate termination of services, discontinuance of operations, or termination of the City.

UTGO Settlement

On April 9, 2014, the City and three bond insurers agreed to a settlement in principle regarding the unlimited tax general obligation bonds (UTGO) that they insure, which UTGO bonds had a total principal value of $369.1 million at June 30, 2013. The settlement, which is subject to Bankruptcy Court approval pursuant to Bankruptcy Rule 9019, would resolve, among other disputes, certain litigation pending in the Bankruptcy Court regarding the UTGO bonds. Pursuant to the settlement, holders of UTGO bonds will transfer a portion of such bonds having a principal amount of $287.5 million in consideration for $279.6 million of new UTGO bonds issued by the Michigan Finance Authority. The insurers of the prior UTGO bonds will receive $7.9 million of the new UTGO bonds which will aggregate $287.5 million in principal amount. The new bonds will be secured by the City's pledge of UTGO bond ad valorem tax levy and the distributable state aid (DSA) that the City is entitled to receive. The City's plan of adjustment, if approved, will provide that the proceeds of ad valorem taxes pledged and collected to pay the remaining principal and related interest of the original UTGO bonds — which will remain outstanding and not be exchanged for new bonds — will be assigned by the Plan to support the City's two pension plans primarily for additional distributions to those retirees who meet certain income eligibility criteria.

Pension Settlements

The Plan provides that, on the effective date of the Plan, the City will assume the obligations related to the already accrued benefits under the GRS pension plan and the PFRS pension plan as those benefits will have been modified in the Plan. This means that the City will not seek to terminate the GRS or the PFRS, although their respective pension plans will be closed to new participants, and vested active employees will not continue to accrue additional pension benefits under the terms and conditions of the current plans, i.e., the two plans will be "frozen." The City will continue to retain the responsibility to fund all amounts necessary to provide the adjusted (reduced) pension benefits to its employees and retirees who will have accrued benefits in either of the GRS or PFRS pension plans as of the effective date of the Plan, although the City's contributions will be fixed during the period ending June 30, 2023. Thereafter, the City will be required to contribute all amounts necessary to fund the modified accrued pensions regardless of the actual future investment performance of the pension plan assets. Although, pursuant to the Plan, the City will provide necessary funding to support the reduced pension benefit levels, the level of funding necessary to support those reduced pension benefits will depend upon, among other things, future actuarial assumptions, changes in retiree mortality and investment returns. Using the assumptions adopted by the City in proposing the Plan, between 2024 and 2053, the City will contribute approximately $2.816 billion, the present value of which is approximately $1.038 billion.

To reduce the risk that the City has experienced from the past investment and discretionary benefit allowance practices of the GRS and PFRS pension funds, which contributed to the current underfunding in each of the pension funds, and to ensure that pension funding obligations do not impair the Plan objective of assuring that the City will have sufficient funds to operate and to improve infrastructure and public safety, the City has developed the following pension restructuring approach: (a) the City has set a goal of achieving a 70% and 75% funded status for GRS and PFRS, respectively, based upon an assumed investment rate of return of 6.75%, by June 30, 2023 and based further on the market value of assets, not a smoothed value of assets; and (b) the City has determined the cash contributions it can reasonably afford to make to each pension plan during the period ending June 30, 2023. Based on these parameters, which were chosen to achieve predictable pension contributions over the long term and sufficient pension funding to provide benefits as modified, and to align the City's required future cash contributions to the plans with its reasonably projected revenues, the City has determined what pension benefit cuts are necessary from the participants in each pension plan.

Under the Plan, claims against the City are divided into different classes. Claims related to PFRS pensions are in Class 10. Claims related to GRS pensions are in Class 11. Specifically, the calculation of the amounts of the allowed PFRS pension claims in Class 10 and the allowed GRS pension claims in Class 11 utilizes among, other assumptions, a 6.75% discount rate to value liabilities and a 6.75% investment return rate for future growth rate of assets. This investment return rate is less than (a) the net 8% investment return rate historically utilized by PFRS in calculating the actual underfunding of the PFRS pension plan and (b) the net 7.9% investment return rate historically utilized by GRS in calculating the actuarial underfunding of the GRS pension plan. In both cases the City has utilized the lower rate as a measure to ensure that both GRS and PFRS utilize prudent and conservative investment policies going forward to protect the assets in both pension plans from unnecessary and imprudent risk of depletion to the detriment of the plan beneficiaries and also to insulate the City — given its limited cash resources — from unforeseen and unbudgeted increases in required future contributions to the pension plans that could cause the City to experience budget deficits in the future.

With respect to PFRS pension claims, the Plan provides for two alternatives for pension benefits. The Plan will not reduce monthly pension payments for holders of PFRS pension claims, but it will either reduce annual cost of-living adjustments (COLAs or escalators) by 55% or eliminate them entirely, depending upon whether certain outside funding is received from the settlement with the State (the State Settlement) and the settlement regarding the Detroit Institute of Arts (the DIA Settlement). The State Settlement and the DIA Settlement are subject to a number of conditions precedent, including, but not limited to, the retirees of both pension systems voting to accept the Plan. As noted above, holders of PFRS pension claims voted to accept the Plan.

Similarly, with respect to GRS pension claims, the Plan provides for two alternatives for pension benefits. If the outside funding is received from the State Settlement and the DIA Settlement, monthly GRS pension benefits will be reduced by 4.5% and COLAs will be eliminated. If the outside funding from the State Settlement and the DIA Settlement is not received, monthly GRS pension benefits will be reduced by 27% and COLAs will be eliminated. In either case, holders of GRS pension claims who participated in the Annuity Savings Fund during the period July 1, 2003 to

(Continued)

June 30, 2013, also will be subject to the recoupment by the City of excess interest credited to Annuity Savings Funds accounts during that period. As noted above, holders of GRS pension claims voted to accept the Plan. The State Settlement and DIA Settlement remain subject to a number of other conditions precedent.

Pursuant to the DIA Settlement, (a) certain charitable foundations and funders of the Nonprofit corporation (DIA Corp.) that operates the Detroit Institute of Arts (collectively with DIA Corp., the "DIA Funding Parties) have committed to assist in the funding of the City's restructured legacy pension obligations and (b) the City has agreed to enter into certain transactions that will cause the DIA assets to remain in the City in perpetuity and to otherwise make the DIA assets available for the benefit of the residents on the City and State of Michigan. The DIA Settlement will be funded as follows: (a) an irrevocable commitment of at least $366 million by the charitable foundations; and (b) in addition to its continuing commitments outside of the DIA Settlement, an irrevocable commitment from DIA Corp. to raise at least $100 million from its donors, the payment of which $100 million will be guaranteed by DIA Corp. Upon the closing of the DIA Settlement transaction, the City shall irrevocably transfer the DIA assets to the DIA Corp., as trustee, to be held in perpetual charitable trust, and within the City limits, for the primary benefit of the residents of the City and citizens of the State.

On the effective date of the Plan, if the conditions precedent to the State Settlement are satisfied or otherwise addressed, the City and the State will consummate the State Settlement. On the later of (a) the date on which the conditions precedent set forth in the definitive documents governing the State Settlement have been satisfied or (b) 60 days after the effective date of the Plan, the State or the State's authorized agent will contribute the net present value of $350 million using a discount rate of 6.75% to GRS and PFRS for the benefit of the holders of pension claims. The State Settlement requires that the Plan provide for the release of the State and certain related entities by each holder of a pension claim from all liabilities arising from or related to the City and the Bankruptcy Case.

The consummation of both the DIA Settlement and the State Settlement are subject to a number of conditions, as set forth in the Plan. If the DIA Settlement or State Settlement is not consummated, the treatment of pension claims in Classes 10 and 11 under the Plan will reflect larger cuts to pension benefits

Actuarial Assumptions of the City versus the Retirement Systems for the Actuarial Calculation of the UAAL

The unfunded actuarial accrued liability (UAAL) with respect to the GRS plan and PFRS plans is based on the Retirement Systems' actuarial valuations. The City believes that the UAAL amounts reported by the Retirement Systems were based on various actuarial assumptions and methods that were favorable to reducing the City's required contributions to the Systems. The assumptions are further discussed in Note 11 (d) and (e) and included: (1) annual rates of return on investments (GRS – 7.9%; PFRS – 8.0%) that were overly optimistic in light of the Retirement Systems' diverse mix of assets/investments and the inability of the City to budget for and fund pension investment loss in the event that investment returns were not achieved; (2) the "smoothing" (reallocation over a period of years) of asset gains and losses over a seven-year period, which masks the funding shortfall; and (3) the use of 29-year (PFRS) and 30-year (GRS) amortization periods for funding UAAL – which is applied anew each year to the full amount of unfunded liability – that allows unfunded liabilities to continue to grow rapidly as a result of the compounding effect.

As set forth in the City's disclosure statement with respect to its proposed plan of adjustment, the City estimated that the combined UAAL for the Retirement Systems was $3.474 billion as of June 30, 2013, consisting of $2.037 billion in UAAL for GRS and $1.437 billion in UAAL for PFRS. The City's actuary, Milliman Inc., calculated this UAAL using the June 30, 2012 actuarial valuations performed by the Retirement Systems, rolling forward the actuarial accrued liability to June 30, 2013 using the City's actuarial assumptions discussed in the previous paragraph, and using the actual market fair value of the Retirement Systems' assets as of June 30, 2013.

Liabilities Subject to Compromise

Unsecured obligations owed by the City at July 18, 2013 are subject to compromise in the bankruptcy process. Liabilities subject to compromise at June 30, 2013 include the following:

		Business-type Activities					
	Total Governmental Activities	Sewage Disposal Fund	Transportation Fund	Water Fund	Automobile Parking Fund	Non-Major Proprietary Fund	Total Primary Government (a)
Long-term obligations							
Subject to compromise:							
Unfunded Actuarial Accrued Liability (Note 11 (d))	$ 341,752,000	163,542,720	140,583,000	157,129,280	—	—	803,007,000
Unfunded Actuarial Accrued Liability PFRS	147,216,398	—	—	—	—	—	147,216,398
OPEB Employee Health and Life Insurance Benefit Plan (Note 12 [d])	4,435,014,878	394,762,645	426,621,672	446,879,462	13,158,072	1,849,499	5,718,286,228
OPEB Supplemental Death Benefit Plan (Note 12 [d])	5,034,167	1,184,046	1,279,604	1,340,365	39,466	5,547	8,883,195
General Obligation Bonds Unlimited Tax	369,115,000	—	—	—	—	—	369,115,000
General Obligation Bonds Limited Tax	155,511,968	—	5,458,032	—	—	—	160,970,000
Revenue Bonds (Note 7)	—	2,824,494,316	—	2,524,775,000	—	—	5,349,269,316
POC (Note 8)	1,180,285,236	89,079,643	103,935,832	78,604,289	—	—	1,451,905,000
Notes & Loans Payable	33,600,000	—	—	—	—	—	33,600,000

	Total Governmental Activities	Business-type Activities: Sewage Disposal Fund	Transportation Fund	Water Fund	Automobile Parking Fund	Non-Major Proprietary Fund	Total Primary Government (a)
Accrued Compensated Absences (Note 6)	$ 66,500,292	1,194,979	3,436,935	10,622,865	179,633	17,349	81,952,053
Accrued Workers Compensation (Note 6)	61,849,000	3,293,000	4,302,693	9,590,000	597,000	81,000	79,712,693
Capital Leases Payable	54,499,463	—	8,243,938	—	—	—	62,743,401
Claims and Judgments (Note 6)	—	190,000	—	243,986	113,997	2,000	549,983
Accrued Pollution Remediation	156,765	—	—	—	—	—	156,765
Total long-term obligations subject to compromise	$ 6,850,535,167	3,477,741,349	693,861,706	3,229,185,247	14,088,168	1,955,395	14,267,367,032
Current obligations subject to Compromise:							
Accounts Payable	$ 50,176,837	50,488,376	9,010,130	23,947,479	349,573	102,394	134,074,789
Accrued Liabilities	53,467,821	—	—	—	—	—	53,467,821
Accrued Interest Payable	30,143,758	70,858,984	1,737,106	66,454,704	237,550	—	169,432,102
Due to Other Governmental Agencies	130,821,685	—	—	—	—	2,234	130,823,919
Due to Fiduciary Funds	141,316,438	—	13,631,878	25,278	621,640	503,834	156,099,068
Due to Component Units	9,125,372	—	—	—	—	—	9,125,372
Deposits and Refunds	14,172,507	—	—	—	—	—	14,172,507
Swap Liability	239,677,971	18,581,500	21,739,808	16,489,465	—	—	296,488,744
Other Liabilities	15,660,102	23,327,269	—	13,592,704	658,573	2,054,629	55,293,277
Total current obligations subject to compromise	$ 684,562,491	163,256,129	46,118,922	120,509,630	1,867,336	2,663,091	1,018,977,599

(a) Liabilities related to component units have been excluded from this table

Amounts that the City recorded as liabilities subject to compromise are in many instances different from amounts filed by the creditors. Differences between amounts scheduled by the City and claims filed by the creditors are being investigated and will be resolved in connection with the claims reconciliation process. Until the process is complete, the ultimate number and amount of allowable claims cannot be ascertained. In this regard, it should be noted that the claims reconciliation process may result in adjustments to current estimates of allowable claims. Although the City currently believes the liability amounts are fairly represented, the ultimate resolution of these claims will be based upon the final plan of adjustment confirmed by the Bankruptcy Court.

Bonds Subject to Compromise

Listed below are the General Obligation Unlimited Tax, General Obligation Limited Tax and Revenue bonds that are subject to compromise.

	Balance June 30, 2013
Governmental Activities :	
General obligation bonds -	
Unlimited tax:	
Series 1999-A	18,470,000
Series 2001-A(1)	77,600,000
Series 2001-B	4,000,000
Series 2002	6,645,000
Series 2003-A	—
Series 2003-A	34,380,000
Series 2004-A(1)	39,270,000
Series 2004-B(1)	8,275,000
Series 2004-B(1)	29,365,000
Series 2004-B(2)	725,000
Series 2005-B	6,875,000
Series 2005-B	37,920,000
Series 2005-C	7,605,000
Series 2005-C	10,795,000
Series 2008-A	15,120,000
Series 2008-A	43,510,000
Series 2008-B(1)	28,560,000
	369,115,000

	Balance June 30, 2013
General obligation bonds -	
Unlimited tax:	
Self-insurance bonds:	
Series 2004	13,000,000
General obligation:	
Series 2005-A(1)	7,720,000
Series 2005-A(1)	52,175,000
Series 2005-A(2)	1,460,000
Series 2005-A(2)	9,475,000
Series 2005-B	1,935,000
Series 2005-B	6,940,000
Series 2008-A(1)	37,806,968
Series 2008-A(2)	25,000,000
	155,511,968

(Continued)

Business-type Activities:			
Transportation Fund:		Water Fund:	
General obligation bonds - Limited tax:		Water supply system revenue bonds:	
Series 2008-A(1)	5,458,032	Series 1993	24,725,000
Sewage Disposal Fund:		Series 1997-A	13,430,000
Sewage disposal system revenue		Series 1999-A	—
bonds (note7):		Series 2001-A	73,790,000
Series 1998-A	16,435,000	Series 2001-C	2,240,000
Series 1998-A	49,075,000	Series 2001-C	186,350,000
Series 1998-B	16,505,000	Series 2003-A	178,785,000
Series 1998-B	48,770,000	Series 2003-B	41,770,000
Series 1999-A		Series 2003-C	4,335,000
Series 1999-A	61,429,316	Series 2003-C	25,325,000
Series 2001-B	110,550,000	Series 2003-D	1,320,000
Series 2001-C (1)	4,410,000	Series 2003-D	139,575,000
Series 2001-C (1)	148,510,000	Series 2004-A	17,520,000
Series 2001-C (2)	2,020,000	Series 2004-A	55,165,000
Series 2001-C (2)	119,630,000	Series 2004-B	29,975,000
Series 2001-D	21,300,000	Series 2004-B	100,990,000
Series 2001-E	136,150,000	Series 2005-A	6,375,000
Series 2003-A	70,450,000	Series 2005-A	84,035,000
Series 2003-A	128,940,000	Series 2005-B	13,525,000
Series 2003-B	150,000,000	Series 2005-B	175,830,000
Series 2004-A	67,755,000	Series 2005-C	21,090,000
Series 2005-A	1,820,000	Series 2005-C	90,200,000
Series 2005-A	236,770,000	Series 2006-A	26,900,000
Series 2005-B	37,195,000	Series 2006-A	237,205,000
Series 2005-C	12,425,000	Series 2006-B	700,000
Series 2005-C	41,095,000	Series 2006-B	119,100,000
Series 2006-A	123,655,000	Series 2006-C	9,655,000
Series 2006-B	6,335,000	Series 2006-C	208,060,000
Series 2006-B	238,150,000	Series 2006-D	1,760,000
Series 2006-C	8,495,000	Series 2006-D	142,160,000
Series 2006-C	18,065,000	Series 2011-A	32,380,000
Series 2006-D	288,780,000	Series 2011-A	341,710,000
Series 2012-A	95,445,000	Series 2011-B	6,390,000
Series 2012-A	564,335,000	Series 2011-B	9,740,000
	2,824,494,316	Series 2011-C	2,700,000
		Series 2011-C	99,965,000
			2,524,775,000

(b) Legal Matters

For more than 35 years, the Detroit Water and Sewerage Department (DWSD) was a defendant in a lawsuit initiated by the United States Environmental Protection Agency (the EPA). In 1977, the EPA sued the City and the DWSD, alleging violations of the federal Clean Water Act (the CWA). The case was pending in the United States District Court for the Eastern District of Michigan (the District Court) – and the DWSD operated under federal court oversight – until March of 2013 due to "a recurring cycle" of compliance failures with regard to the CWA and National Pollutant Discharge Elimination System (NPDES) permits required by the Michigan Department of Environmental Quality (the MDEQ). Pursuant to an Administrative Consent Order (the ACO) with the MDEQ, in July 2011 the DWSD agreed to undertake certain remedial measures to address what the District Court had identified as areas of persistent dysfunction, including deficiencies in maintenance, capital expenditures, planning, staffing, and procurement. As of the Petition Date, the ACO remained effective, allowing the MDEQ to continue its oversight of the DWSD.

Determining that the ACO, standing alone, was insufficient to guarantee the DWSD's long-term compliance with the CWA and NPDES standards, in 2011 the District Court ordered a "Root Cause Committee" comprised of City and DWSD officials to formulate a plan to address the root causes of the DWSD's persistent noncompliance. The Root Cause Committee drafted—and the District Court adopted—a "Plan of Action," which proposed to restructure the DWSD to address systemic dysfunction and achieve long-term compliance with federal and state environmental standards. In March 2013, the Root Cause Committee submitted a plan to the District Court recommending the creation of an autonomous DWSD. On March 27, 2013, the District Court issued an order closing the case and declining to address the Root Cause Committee's recommendation for further restructuring the DWSD. In its order dismissing the case, the District Court stated that it was satisfied that the court's orders "have been substantially implemented."

On April 8, 2013, the Sixth Circuit Court of Appeals issued a ruling in favor of certain unions that had sought to intervene in the case prior to the dismissal, reversing the District Court's denial of certain motions to intervene and remanding for a limited grant of intervention.

On June 5, 2013, the District Court issued an order to show cause regarding the question of whether the District Court is divested of jurisdiction to address the remanded issues as a result of the order of dismissal. The City also has commenced an appeal in this case. On July 30, 2013, the Sixth Circuit Court of Appeals stayed the City's appeal pending resolution of the City's chapter 9 bankruptcy case.

(c) Debt Ratings

On July 3, 2013, Standard & Poor's downgraded the rating on the Sewage Disposal Fund on the senior lien and second lien revenue bonds to "BB-" and then again lowered the rating on March 25, 2014, to a "CCC." On February 28, 2014, Fitch downgraded the Sewage Disposal Fund revenue bonds. Sewage Disposal Fund senior lien revenue bonds were downgraded to "BB+" from "BBB+." Sewage Disposal Fund second lien revenue bonds were downgraded to "BB" from "BBB."

(d) Sale of Bonds

On January 21, 2014, the BOWC adopted a resolution authorizing the publication of a notice of intent to issue revenue bonds in an amount up to $350,000,000 of Sewage Disposal System Revenue Bonds for the purpose of paying all or part of the cost of acquiring and constructing facilities, replacements, extensions, improvements, and repairs to the Sewage Disposal System. Management's intent is to issue approximately $150,000,000 in revenue bonds in early fiscal year 2015 to fund the capital improvement program consistent with the DWSD's five-year capital improvement and finance plan.

(e) Other Matters

On November 14, 2012, the Detroit Water and Sewerage Department's Board of Water Commissioners approved a $2 million contract with a consultant, EMA, for job redesign and organizational optimization services with a term that ended June 30, 2013. On June 26 and July 24, 2013, three additional contracts were awarded continue the entity wide organizational optimization. First, the Phase II Amendment Project ($1,999,760) is implementing the Job Design and new Business Processes at the Water Plants, System Control Center, Wastewater Plant, and Field Service Yards. Second, the Phase IV Information Technology (IT) Project ($1,550,000) is developing the requirements and documentation for the Enterprise Resource Planning/Financial System, producing an IT and Geographic Information System Roadmap, developing the Network Requirements, and other related systems, governance, and planning matters. Third, the Phase V Asset Management Program ($1,996,540) is developing and implementing specific requirements for asset management activities to meet the regulatory requirements. These projects will be completed in phases over a 12 to 30 month time period.

CITY OF DETROIT
SEWAGE DISPOSAL FUND

Other Supplemental Information

June 30, 2013

Other Supplemental Information

As discussed in note 4, City of Detroit bond ordinance requires minimum levels of assets held in reserve for debt service on revenue bonds and to provide funds for improvements, enlargements, extensions, and construction. The Sewage Disposal Fund's reserves consist of the following cash and investments classified on the statement of net position as either restricted or unrestricted as follows:

		Funded from revenues		Funded from debt issuance	
		Unrestricted	**Restricted**	**Restricted**	**Total**
Flow of funds (per ordinance):					
Receiving fund	$	—	—	—	—
Operations and maintenance		18,124,466	—	—	18,124,466
Senior lien debt service		—	83,850,466	—	83,850,466
Senior lien bond reserve		—	—	152,787,913	152,787,913
Second lien debt service		—	51,306,214	—	51,306,214
Second lien bond reserve		—	—	79,885,219	79,885,219
Extraordinary repair and replacement		32,624,038	—	—	32,624,038
Improvement and extension		—	—	—	—
Subtotal – reserves defined by ordinance		50,748,504	135,156,680	232,673,132	418,578,316
Less funded by surety		—	—	(128,925,360)	(128,925,360)
Total – reserves defined by ordinance (net of Surety coverage)		50,748,504	135,156,680	103,747,772	289,652,956
Unspent construction bond proceeds		—	—	177,389,951	177,389,951
Variance from ordinance requirement		(450,938)	—	—	(450,938)
Total cash, cash equivalents and investments	$	50,297,566	135,156,680	281,137,723	466,591,969

Note: Surety coverage includes series specific policies; therefore, represents the lesser of the maximum amount of the policy, or amount of reserve requirement allocated to the specific series covered by such policy.

See accompanying independent auditor's report