# MICHIGAN TOWNSHIP PARTICIPATING PLAN

AUDITED FINANCIAL STATEMENTS

Years ended June 30, 2018 and 2017

# MICHIGAN TOWNSHIP PARTICIPATING PLAN

## TABLE OF CONTENTS

# INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Michigan Township Participating Plan

## Report on the Financial Statements

We have audited the accompanying financial statements of Michigan Township Participating Plan, which comprise the statements of financial position as of June 30, 2018 and 2017, and the related statements of revenue, expenses, and changes in net assets, and cash flows for the years then ended, and the related notes to the financial statements.

## Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

## Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

**Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Michigan Township Participating Plan as of June 30, 2018 and 2017, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

UHY LLP

Farmington Hills, Michigan
October 19, 2018

## MICHIGAN TOWNSHIP PARTICIPATING PLAN
### STATEMENTS OF FINANCIAL POSITION

| | June 30, 2018 | June 30, 2017 |
|---|---|---|
| **ASSETS** | | |
| **CURRENT ASSETS** | | |
| Cash | | |
| Huntington Bank | **$ 186,806** | $ 203,132 |
| Morgan Stanley | **292,477** | 734,864 |
| Total cash | **479,283** | 937,996 |
| Marketable securities | **684,000** | 245,000 |
| Sponsorship fees receivable | **26,089** | 23,185 |
| Other receivables | **35,122** | 34,846 |
| Deposits | **1,000** | 500 |
| Prepaid expenses | **10,635** | 10,000 |
| Total current assets | **1,236,129** | 1,251,527 |
| **MARKETABLE SECURITIES** | **1,524,405** | 1,492,907 |
| Total assets | **$ 2,760,534** | $ 2,744,434 |
| **LIABILITIES** | | |
| **CURRENT LIABILITIES** | | |
| Accounts payable | **$ 355** | $ - |
| Insurance policy holder dividends payable | **5,332** | 7,291 |
| Grants payable | **60,230** | 35,371 |
| Total liabilities | **65,917** | 42,662 |
| **NET ASSETS** | **$ 2,694,617** | $ 2,701,772 |

## MICHIGAN TOWNSHIP PARTICIPATING PLAN
### STATEMENTS OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS

| | Years ended June 30, 2018 | 2017 |
|---|---|---|
| Sponsorship fee revenue | **$ 556,257** | $ 554,191 |
| Operating expenses | | |
| Grants, net of forfeitures | **240,622** | 165,298 |
| Advertising | **183,089** | 178,999 |
| Travel and meetings | **75,364** | 80,667 |
| Newsletter publishing | **11,742** | 11,190 |
| Professional fees | **34,950** | 28,974 |
| Actuarial costs | **29,500** | 29,250 |
| Program enhancement | **6,940** | 7,000 |
| Insurance | **7,863** | 7,739 |
| Office supplies and expense | **1,452** | 1,628 |
| Total operating expenses | **591,522** | 510,745 |
| Operating income (loss) | **(35,265)** | 43,446 |
| Other income (expense) | | |
| Interest income | **28,110** | 24,925 |
| Insurance policy holder dividend income | **582,353** | 1,059,565 |
| Insurance policy holder dividend expense | **(582,353)** | (1,059,565) |
| Total other income, net | **28,110** | 24,925 |
| Change in net assets | **(7,155)** | 68,371 |
| Net assets, beginning | **2,701,772** | 2,633,401 |
| Net assets, ending | **$ 2,694,617** | $ 2,701,772 |

## MICHIGAN TOWNSHIP PARTICIPATING PLAN
### STATEMENTS OF CASH FLOWS

| | Years ended June 30, 2018 | 2017 |
|---|---|---|
| **OPERATING ACTIVITIES** | | |
| Change in net assets | **$ (7,155)** | $ 68,371 |
| Adjustments to reconcile the change in net assets to net cash flows from operating activities | | |
| Changes in | | |
| Sponsorship fees receivable | **(2,904)** | 442 |
| Other receivables | **(276)** | - |
| Deposits | **(500)** | (500) |
| Prepaid expenses | **(635)** | - |
| Accounts payable | **355** | (129) |
| Insurance policy holder dividends payable | **(1,959)** | (3,783) |
| Grants payable | **24,859** | (35,260) |
| Net cash provided by operating activities | **11,785** | 29,141 |
| **INVESTING ACTIVITIES** | | |
| Purchase of marketable securities | **(715,498)** | (984,103) |
| Proceeds from maturity of marketable securities | **245,000** | 1,018,000 |
| Net cash provided by (used in) investing activities | **(470,498)** | 33,897 |
| **NET CHANGE IN CASH** | **(458,713)** | 63,038 |
| **CASH**, Beginning | **937,996** | 874,958 |
| **CASH**, Ending | **$ 479,283** | $ 937,996 |

## NOTE 1 – NATURE OF OPERATIONS

The Michigan Township Participating Plan (the "Plan") was established April 1, 1985, pursuant to laws of the State of Michigan which authorize local units of government to exercise jointly any power, privilege or authority which each might exercise separately. The purpose of the Plan is to jointly exercise powers common to each participating member to establish and administer a risk management program; to prevent or lessen the incidence and severity of casualty losses occurring in the operations of its members; and to defend and protect any member of the authority against liability or loss. The powers, duties and the described activities of the Plan are not intended to constitute the issuance of a policy of insurance. The members intend, in the creation of the Plan, to establish an organization for joint risk management, and have not created any relationship for the debts of or claims between members.

Effective July 1, 2011, the Plan entered into an agreement with U.S. Specialty Insurance Company ("USSIC") to sponsor a master insurance policy for the members of the Plan. The Plan earns a sponsorship fee from USSIC which funds operating expenses as well as a risk reduction grant program.

## NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The summary of significant accounting policies is presented to assist in understanding the Plan's financial statements. These accounting policies conform to accounting principles generally accepted in the United States of America as applicable to entities under Section 124.8(2) of the Michigan Compiled Laws, and have been consistently applied in the preparation of the financial statements.

### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

### Revenue Recognition

As discussed above, effective July 1, 2011, the Plan earns a sponsorship fee of 2.6% of net premiums written, up to a maximum of $650,000 per year. The sponsorship fee income is earned at the commencement of the policy. During the years ended June 30, 2018 and 2017, net written premiums were $21,394,501 and $21,315,027, respectively.

## NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Marketable Securities

The Plan classifies all of its investments in marketable securities as held-to-maturity as it has the intent and ability to hold the securities to maturity. Marketable securities classified as held-to-maturity are carried at amortized cost.

### Receivables

At June 30, 2018 and June 30, 2017, there was no allowance for uncollectible receivables.

### Grants Payable

The Plan has established a risk reduction grant program to assist members in reducing specific risk exposures and other efforts of applying effective risk management and loss control techniques. Grant cycles are open twice per fiscal year and grant project submissions require approval by the Plan's Board of Directors. Members must complete the approved grant project, then submit proof of project expenditures for reimbursement. Grants are limited up to $5,000 per member per grant cycle, in accordance with the grant program. Grants payable represent approved grants for which the Plan has not yet received member reimbursement requests. Grants must be completed within six months of the date of the grant agreement. If a member does not complete their grant project within the six month deadline, the grant is forfeited.

### Insurance Policy Holder Dividends

An agreement with USSIC provides for a program which entitles the Plan to receive insurance policy holder dividends if certain ultimate loss ratios are met during an underwriting year. Members of the Plan are the sole beneficiaries of any insurance policy holder dividend which would be allocated in accordance with criteria set forth by the Plan. The ultimate loss ratio cannot be calculated until 24 months after an underwriting year. USSIC has up to 90 days after the fiscal year to remit any dividend earned.

The amount of insurance policy holder dividends to be paid to members is determined annually by USSIC, which utilizes actuarial data provided by Oliver Wyman, the Plan's actuary. Upon receipt of the insurance policy holder dividends from USSIC, the Plan declares and recognizes a liability for insurance policy holder dividends, and subsequently distributes such dividends to members of the Plan.

Should a member leave the Plan after the insurance policy holder dividends have been determined for the year but prior to being paid, their respective portion of the insurance policy holder dividend is forfeited. Forfeited insurance policy holder dividends are paid back to USSIC, or retained by the Plan to offset future insurance policy holder dividends to be received from USSIC.

## NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Concentration of Credit Risk

The Plan, from time to time during the years covered by these financial statements, may have bank balances in excess of insured limits. Management has deemed this to be a normal business risk.

### Income Taxes

The Plan is a municipal entity providing risk management and coverage, operating pursuant to the State of Michigan Public Act 138 of 1982. This law allows local governmental units to provide joint funding for risk management and insurance coverage purposes. The Plan is exempt from taxation under the Internal Revenue Code. Accordingly, no provision for income taxes has been made in the accompanying financial statements.

The benefit of an uncertain tax position is recognized in the financial statements if it meets a minimum recognition threshold. A determination is first made as to whether it is more likely than not that the income tax position will be sustained, based upon technical merits, upon examination by the taxing authorities. If the income tax position is expected to meet the more-likely-than-not criteria, the benefit recorded in the financial statements equals the largest amount that is greater than 50% likely to be realized upon its ultimate settlement. As of June 30, 2018 and 2017, there were no uncertain tax positions for which a reserve or liability is necessary.

### Advertising

Advertising costs are expensed as incurred. Total advertising costs for the years ended June 30, 2018 and 2017, were $183,089 and $178,999, respectively.

### Reclassifications

Certain reclassifications have been made to the financial statements for the year ended June 30, 2017 to conform to the presentation for the year ended June 30, 2018. These reclassifications did not affect net assets or the change in net assets.

### Subsequent Events

Plan management has performed a review of events subsequent to June 30, 2018 through October 19, 2018, the date the financial statements were available to be issued.

## NOTE 3 – SELF-RETENTION AND INSURANCE

The Plan, while it operates under the Michigan Legislation of Public Act 138, does not operate as a risk pool due to the transfer of risk to USSIC. The Plan now sponsors a master policy under which USSIC insures the members under a master policy for the period July 1, 2011 to July 1, 2019. Due to this master policy purchase, there is no pooling of risk between members. For policies with an effective date before July 1, 2011, the Plan transferred the risk to reinsurance companies. Further, the Plan has protected itself in the event that amounts due from a reinsurance company become uncollectible by purchasing a contingency policy for uncollectible reinsurers (see Note 4). However, the Plan holds $170,000 of self-retention on this policy. Additionally, the Plan maintains a self-insured director and officer excess policy to cover up to $1 million in losses with an effective date of January 2, 2013 which is renewed annually.

Prior to July 1, 2011, the Plan chose to adopt the forms and endorsements of conventional insurance protection and to reinsure these coverages 100%, rather than utilize a risk pool of member funds to pay individual and collective losses up to a given retention, and then have reinsurance above that retention amount. The individual members were responsible for their self-retention amount, which varies from member to member. These policies and coverage remain in effect until all claims have been settled. The Plan projects that it will take seven to ten years for all claims to be made and settled. The liability for these claims remains with the reinsurers.

## NOTE 4 – CONTINGENCY COMMUTATION RECOVERY

As discussed in Note 3, prior to July 1, 2011 the Plan chose to adopt the forms and endorsements of conventional insurance protection and to reinsure these coverage's 100%. The Plan had entered into an unrecoverable reinsurance agreement on June 30, 2003 with Motors Insurance Corporation to provide protection to the plan members in the event that the Plan had difficulties in the collection of claim recoverables from one or more of the reinsurers. The agreement allowed the Plan the option to increase the limit of protection through additional premium payments. Effective April 13, 2012, the Plan entered into a commutation agreement with Maiden Re Insurance Services, LLC, successor to Motors Insurance Corporation. As a result of the commutation agreement, premiums in the amount of $3,035,826 were returned to the Plan during the year ended June 30, 2013.

In connection with the commutation agreement above, the Plan entered into an insurance contract with Houston Casualty Company ("HCC") to cover up to $5 million in losses to the Plan if a prior reinsurer is unable or unwilling to make some or all payments under its reinsurance agreements. Proceeds from the commutation of the unrecoverable reinsurance agreement were used for payment of the $512,500 premium to HCC during the year ended June 30, 2013. The premium was planned to be expensed over the ten year policy period from April 13, 2012 to March 31, 2022. However, during the Michigan Department of Insurance and Financial Services ("DFIS") examination of the Plan for the year ended June 30, 2015, they noted that the Plan had a prepaid asset (prepaid insurance) of an amount in excess of 10% of net assets.

## NOTE 4 – CONTINGENCY COMMUTATION RECOVERY (Continued)

Section 124.8(2) of the Michigan Compiled Laws states that pools can only include a prepaid expense as an asset if it is an immaterial asset as defined by the Commissioner of the DFIS. As of June 30, 2015, this prepaid asset exceeded 10% of net assets, and, therefore, the Plan's board concluded that the remaining balance of the prepaid insurance would be expensed. The policy remains in force through March 31, 2022.

## NOTE 5 – MARKETABLE SECURITIES

The Plan invests in marketable securities that are classified as held-to-maturity according to management's intent and are carried at amortized cost. Held-to-maturity securities, by security type, consist of the following:

| | June 30, 2018 | | |
|---|---|---|---|
| | Amortized Cost | Gross Unrealized Losses | Fair Value |
| Held-to-maturity | | | |
| Certificates of deposit | $ 976,000 | $ (10,123) | $ 965,877 |
| Government bonds | 1,232,405 | (36,004) | 1,196,401 |
| | $ 2,208,405 | $ (46,127) | $ 2,162,278 |

| | June 30, 2017 | | |
|---|---|---|---|
| | Amortized Cost | Gross Unrealized Losses | Fair Value |
| Held-to-maturity | | | |
| Certificates of deposit | $ 979,000 | $ (4,647) | $ 974,353 |
| Government bonds | 758,907 | (20,469) | 738,438 |
| | $ 1,737,907 | $ (25,116) | $ 1,712,791 |

The marketable securities are classified as short-term or long-term on the statement of financial position according to their maturity dates. As of June 30, 2018, $684,000 and $1,524,405 of marketable securities are classified as short-term and long-term, respectively. As of June 30, 2017, $245,000 and $1,492,907 of marketable securities are classified as short-term and long-term, respectively. Certificates of deposit mature at various dates through November 2019. Government bonds mature at various dates through June 2022.

## NOTE 6 – FAIR VALUE MEASUREMENTS

The Accounting Standards Codification regarding fair value enhances existing guidance for measuring assets and liabilities using fair value. The standard provides a single definition of fair value, together with a framework for measuring it, and requires additional disclosure about the use of fair value to measure assets and liabilities. The standard also emphasizes that fair value is a market-based measurement, not an entity specific measurement, and sets out a fair value hierarchy with the highest priority being quoted prices in active markets. Under the standard, fair value measurements are disclosed by level within that hierarchy.

Determining which hierarchical level an asset or liability falls within requires significant judgment. The Plan's management evaluates its hierarchy disclosures. Hierarchical levels, as defined by the standard and directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities are as follows.

> Level 1: Quoted prices in active markets for identical assets or liabilities.
>
> Level 2: Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
>
> Level 3: Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities.

Because valuation methodologies require the use of subjective assumptions, changes in these assumptions can materially affect fair value. A description of the valuation methodologies used by the Plan for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. There were no changes in the valuation techniques in determining the fair value of assets and liabilities during the years ended June 30, 2018 and 2017.

*Certificates of deposit:* Valued at the quoted market price which is considered a Level 1 approach.

*Government securities:* Valued using quoted prices for similar assets which is considered a Level 2 measurement approach.

## NOTE 6 – FAIR VALUE MEASUREMENTS (Continued)

The Plan had no assets or liabilities measured at fair value on a recurring or nonrecurring basis. However, the following tables summarize financial instruments for which fair value is disclosed in the financial statements as of June 30, 2018 and 2017, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

| | June 30, 2018 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Marketable securities | | | | |
| Certificates of deposit | $ 965,877 | $ - | $ - | $ 965,877 |
| Government bonds | - | 1,196,401 | - | 1,196,401 |
| Total marketable securities | $ 965,877 | $ 1,196,401 | $ - | $ 2,162,278 |

| | June 30, 2017 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Marketable securities | | | | |
| Certificates of deposit | $ 974,353 | $ - | $ - | $ 974,353 |
| Government bonds | - | 738,438 | - | 738,438 |
| Total marketable securities | $ 974,353 | $ 738,438 | $ - | $ 1,712,791 |

## NOTE 7 – GRANT PROGRAM

The Plan has established a risk reduction grant program to assist members in reducing specific risk exposures and other efforts of applying effective risk management and loss control techniques. Grants totaling $249,530 and $185,529 were awarded during the years ended June 30, 2018 and 2017, respectively. Grants totaling $8,908 and $20,231 were forfeited during the years ended June 30, 2018 and 2017, respectively. Grants of $60,230 and $35,371 were unpaid and are reflected as current liabilities on the statements of financial position as of June 30, 2018 and 2017, respectively.

## NOTE 8 – INSURANCE POLICY HOLDER DIVIDEND PROGRAM

An agreement with USSIC provides for a program which entitles the Plan to receive insurance policy holder dividends if certain ultimate loss ratios are met during an underwriting year. Members of the Plan are the sole beneficiaries of any insurance policy holder dividend which would be allocated in accordance with criteria set forth by the Plan. The ultimate loss ratio cannot be calculated until 24 months after an underwriting year. USSIC has up to 90 days after the fiscal year to remit any dividend earned.

During the years ended June 30, 2018 and 2017, the Plan received insurance policy holder dividends totaling $582,353 and $1,059,565, respectively, of which $582,353 and $1,059,565, respectively, was distributed to the members of the Plan.

Should a member leave the Plan after the insurance policy holder dividends have been determined for the year but prior to being paid, their respective portion of the insurance policy holder dividend is forfeited. Forfeited insurance policy holder dividends are paid back to USSIC, or retained by the Plan to offset future insurance policy holder dividends to be received from USSIC. As of June 30, 2018 and 2017, forfeited insurance policy holder dividends payable totaled $5,332 and $7,291, respectively.

## NOTE 9 – PLAN TERMINATION

While the board is not presently considering Plan termination, the Plan may cease its activities upon a three-fourths vote of the members to such effect. The Plan shall be administered by the Board of Directors holding office on the effective date of the termination until all of the Plan's affairs are completed. Upon termination, net assets of the Plan remaining after payment of debts and liabilities will be distributed to its members.

## NOTE 10 – NET RESERVES FOR LOSSES

Effective July 1, 2011, the Plan retains no risk due to the agreement with USSIC (see Note 3) and therefore has no liability for loss reserves. For claims prior to July 1, 2011, the Plan has reinsured one hundred percent of its loss reserves. Consequently, the Plan has not reflected a liability for loss reserves in its statements of financial position.