STATE OF MINNESOTA

Office of the State Auditor

Rebecca Otto
State Auditor

THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

FOR THE YEAR ENDED DECEMBER 31, 2008

Description of the Office of the State Auditor

The mission of the Office of the State Auditor is to oversee local government finances for Minnesota taxpayers by helping to ensure financial integrity and accountability in local governmental financial activities.

Through financial, compliance, and special audits, the State Auditor oversees and ensures that local government funds are used for the purposes intended by law and that local governments hold themselves to the highest standards of financial accountability.

The State Auditor performs approximately 160 financial and compliance audits per year and has oversight responsibilities for over 3,300 local units of government throughout the state. The office currently maintains five divisions:

Audit Practice - conducts financial and legal compliance audits of local governments;

Government Information - collects and analyzes financial information for cities, towns, counties, and special districts;

Legal/Special Investigations - provides legal analysis and counsel to the Office and responds to outside inquiries about Minnesota local government law; as well as investigates allegations of misfeasance, malfeasance, and nonfeasance in local government;

Pension - monitors investment, financial, and actuarial reporting for approximately 730 public pension funds; and

Tax Increment Financing - promotes compliance and accountability in local governments' use of tax increment financing through financial and compliance audits.

The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employees Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION MINNEAPOLIS, MINNESOTA

For the Year Ended December 31, 2008

Audit Practice Division
Office of the State Auditor
State of Minnesota

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THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

TABLE OF CONTENTS

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Introductory Section

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THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

ORGANIZATION
DECEMBER 31, 2008

	Term of Office	
	From	To
<u>Board of Trustees</u>		
Active Elected Members		
Walter C. Schirmer	December 1986	December 2011
Tim Davison	December 2006	December 2011
Retired Elected Members		
John W. George	December 1991	December 2009
Wallace O. Amundsen	December 1992	December 2010
Joseph D. Quinn	December 1993	December 2011
Dennis Ozment	December 2008	December 2011
Frank Boerboon	December 2002	December 2009
Richard A. Quarnstrom	December 1999	December 2010
Arnold J. Reese	December 2000	December 2009
David R. Pierson	December 2001	December 2010
City of Minneapolis Appointed Representatives		
Jack Qvale	July 2003	December 2010
LeaAnn Stagg	April 2006	December 2010

<u>Officers</u>

Walter C. Schirmer	Executive Secretary
Frank Boerboon	President
Wallace O. Amundsen	Vice President
David R. Pierson	Assistant Executive Secretary
Joseph D. Quinn	Treasurer
Arnold J. Reese	Assistant Treasurer

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Financial Section

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STATE OF MINNESOTA
OFFICE OF THE STATE AUDITOR

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Minneapolis Firefighters' Relief Association

We have audited the basic financial statements of the Minneapolis Firefighters' Relief Association as of and for the year ended December 31, 2008, as listed in the table of contents. These basic financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these basic 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 basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the plan net assets of the Minneapolis Firefighters' Relief Association as of December 31, 2008, and the changes in plan net assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis and other required supplementary information referred to in the table of contents are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures to this information, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

/s/Rebecca Otto	*/s/Greg Hierlinger*
REBECCA OTTO STATE AUDITOR	GREG HIERLINGER, CPA DEPUTY STATE AUDITOR

July 31, 2009

MANAGEMENT’S DISCUSSION AND ANALYSIS

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THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2008
(Unaudited)

This Management's Discussion and Analysis (MD&A) of the Minneapolis Firefighters' Relief Association's (Association) financial performance provides an overview of the Association's financial activities for the fiscal year ended December 31, 2008. Please read it in conjunction with the basic financial statements, which follow this discussion.

FINANCIAL HIGHLIGHTS

The Association's funding objective is to meet benefit obligations through investment income. As of December 31, 2008, the funded ratio was 84.7 percent. Minnesota statutes require full funding of the Association's unfunded accrued liability by December 31 of the year occurring 15 years later.

Due to poor market conditions and payroll requirements, the plan net assets administered by the Association during 2008 decreased by $93.6 million.

Plan asset additions for the year were a negative $70.5 million. The lion's share of these changes consist of net investment losses of $75.4 million, City of Minneapolis contributions of $3.3 million, fire state aid of $204,000, insurance surcharge of $1,209,297, general account receipts of $93,082, and political account receipts of $31,538.

Plan asset deductions decreased from the prior fiscal year from $23.4 million to $23.1 million, or about one percent.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual financial report consists of two financial statements: the Statement of Plan Net Assets (Exhibit A) and the Statement of Changes in Plan Net Assets (Exhibit B). These financial statements report information about the Association as a whole and about its financial condition that should help answer the question: Is the Association, as a whole, better off or worse off as a result of this year's activities? These statements include all assets and liabilities using the accrual basis of accounting. Under the accrual basis of accounting, all revenues and expenses are taken into account regardless of when cash is received or paid.

The Statement of Plan Net Assets presents all of the Association's assets and liabilities, with the difference between the two reported as net assets. Over time, increases and decreases in net assets measure whether the Association's financial condition is improving or deteriorating. The Statement of Changes in Plan Net Assets presents how the Association's net assets changed during the most recent fiscal year. These two statements should be reviewed along with the Schedule of Funding Progress and Schedule of Employer Contributions to determine whether the Association is becoming financially stronger, weaker, or is holding a steady pace of progress and also to understand the reasons for changes to the funded status of the Association over a given period of time.

FINANCIAL ANALYSIS

Association total assets as of December 31, 2008, were $186.3 million and were mostly comprised of cash, investments, and accrued investment income. Total assets decreased $96.1 million, or about 34 percent, from 2007. Of this amount, 20 percent was due to payroll requirements.

Total liabilities as of December 31, 2008, were $3.0 million and were comprised of amounts held in escrow, security purchases payable, and accounts payable. Total liabilities decreased $2.4 million, or about 45 percent, between fiscal years 2007 and 2008.

The Association's assets exceeded its one-year liabilities, not including pension benefits, by $183.4 million at the close of fiscal year 2008. Total net assets held in trust for pension benefits decreased by $93.6 million, or 34 percent, between fiscal years 2007 and 2008.

Net Assets
(In Thousands)

	2008	2007
Assets		
Cash	$ 1,950	$ 1,901
Receivables	938	2,245
Investments	183,451	278,224
Total Assets	$ 186,339	$ 282,370
Liabilities		
Accounts payable	$ 190	$ 223
Back-pay payable	-	412
Escrow account for health insurance	2,098	2,657
Security purchases payable	671	2,084
Total Liabilities	$ 2,959	$ 5,376
Total Net Assets	$ 183,380	$ 276,994

Revenues--Additions to Plan Net Assets

The vast majority of reserves needed to finance pension benefits are accumulated primarily through earnings on investments with additional contributions provided by the employer and the State of Minnesota. Total additions for 2008 were negative $70.5 million, which is comprised of investment losses of $75.4 million, City of Minneapolis contributions of $3.3 million, fire state aid of $204,000, insurance surcharge of $1,209,297, general account receipts of $93,082, and political account receipts of $31,538.

Total contributions from the City of Minneapolis and the State of Minnesota increased between fiscal years 2007 and 2008 by $460,000. There were investment losses net of investment fees of $75.4 million for fiscal year 2008, compared to investment income net of investment fees of $29.8 million for fiscal year 2007 due to worsening stock market conditions. The net depreciation in fair value of investments was $82.4 million for the year ended December 31, 2008, compared to net appreciation of $18.8 million for fiscal year 2007. Fiscal year 2008 was a monumentally bad investment year for the entire country and world.

Expenses--Deductions from Plan Net Assets

The primary expenses of the Association include the payment of pension benefits and the cost of administering the plan. Total deductions for fiscal year 2008 were $23.1 million, a decrease of $236,000, or about one percent, from fiscal year 2007 deductions. A decrease of about 15 percent in pension benefit expenses resulted from a 2007 Post Retirement Benefit payment that was not paid in 2008. Administrative expenses increased by $111,000 between fiscal years 2007 and 2008 due to expenses incurred from a lawsuit brought by the City of Minneapolis against the Association.

Changes in Net Assets
(In Thousands)

	2008	2007
Additions		
Contributions	$ 4,750	$ 4,290
Net investment income (loss)	(75,403)	29,764
Other sources	160	156
Total Additions (Losses)	$ (70,493)	$ 34,210
Deductions		
Benefits	$ 22,343	$ 22,713
Administrative expenses	693	582
Other expenses	85	62
Total Deductions	$ 23,121	$ 23,357
Net Increase (Decrease)	$ (93,614)	$ 10,853

THE ASSOCIATION IN GENERAL

The Association's net assets have experienced dramatic losses over the last year. These losses are primarily due to extremely negative world-wide stock market performance.

Unfortunately, the market has not performed up to the levels required to reach the funding level the Association Trustees had hoped for. We do however, have full faith and trust in the ability of the American people to rebound from this temporary, but dramatic plunge in the world economy and we will work hard and diligently to continue our steadfast progress towards the eventual goal of full sufficiency into the future.

The Board of Trustees believe our current financial position will improve greatly over the next couple of years and we will continue to look forward to better times and substantial improvements to our funding level and financial security. The Trustees plan to continue with the prudent investment programs and strategic planning that has made our Association one of the best administered and productive pension plans in the State of Minnesota as well as the entire Country. We will continue to provide the kinds of investment returns required for the Association to meet its goal of total self-reliance sooner than later. It is the Board's feeling that our Association will meet the state's funding requirement of 2018 much sooner than the required time lines currently in place.

At year-end 2008, our Association's funding level was 84.7 percent, down from 92.8 percent on December 31, 2007. According to the Investment Report provided by our investment consultant we finished 2008 with an investment loss of minus 28.6 percent. The Board of Trustees takes its fiduciary responsibility to the Members, City, and State of Minnesota very seriously and we are extremely diligent in the manner in which we administer our pension fund and invest our assets for our current and future retirement needs. We have a very clear and significantly superior record of performance and we are very proud of that record.

We are challenged by our overseers and our adversaries on a regular basis and we welcome such challenges as long as they are provided for the express purpose of assisting the Trustees in making our fund the best it can be, in all respects, while providing our membership with the necessary benefits required to live the remaining years of their lives in the best, most comfortable and peaceful manner possible without any fear of having their future financial security snatched from their grasp by the needs of an ever increasingly less than adequate political, financial, and economical system of governance.

BASIC FINANCIAL STATEMENTS

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THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

EXHIBIT A

STATEMENT OF PLAN NET ASSETS
DECEMBER 31, 2008

Assets		
Cash and deposits		
Cash and deposits in pension account	$	1,836,113
Cash and deposits in general account		107,669
Cash and deposits in political account		6,324
Total cash and deposits	**$**	**1,950,106**
Receivables		
Accrued interest and dividends	$	497,834
Sale of securities		124,921
Contributions		309,350
Other		5,347
Total receivables	**$**	**937,452**
Investments, at fair value		
Certificates of deposit in general account	$	746,188
Corporate obligations		8,987,923
Corporate stock		66,579,408
Corporate stock in general account		118,459
Mutual funds		47,925,890
U.S. government obligations		27,849,623
Investment pools		
Bond market account (State Board of Investment)		4,658,485
Common stock index account (State Board of Investment)		8,501,127
Short-term cash equivalents		9,292,289
Short-term cash equivalents in general account		9,626
Limited liability partnerships		8,782,230
Total investments, at fair value	**$**	**183,451,248**
Total Assets	**$**	**186,338,806**
Liabilities		
Accounts payable	$	190,185
Escrow account for health benefits		2,097,358
Security purchases payable		671,065
Total Liabilities	**$**	**2,958,608**
Net Assets		
Net assets held in trust for pension benefits (a Schedule of Funding Progress is presented on page 26)	$	182,391,932
Net assets restricted for general account		981,942
Net assets restricted for political account		6,324
Total Net Assets	**$**	**183,380,198**

The notes to the financial statements are an integral part of this statement.

THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

EXHIBIT B

STATEMENT OF CHANGES IN PLAN NET ASSETS
FOR THE YEAR ENDED DECEMBER 31, 2008

Additions		
Contributions		
Employer		
City of Minneapolis	$	3,336,852
State of Minnesota		1,413,297
Total contributions	**$**	**4,750,149**
Investment income (loss)		
Net appreciation (depreciation) in fair value of investments	$	(82,401,717)
Interest and dividends		7,845,833
Total investment income (loss)	**$**	**(74,555,884)**
Less: direct investment expense		(847,469)
Net investment income (loss)	**$**	**(75,403,353)**
Other	$	35,222
Receipts to general account		93,082
Receipts to political account		31,538
Total Additions	**$**	**(70,493,362)**
Deductions		
Benefits and refunds paid to participants	$	22,343,316
Administrative expenses		692,982
Other - general account		43,042
Other - political account		41,707
Total Deductions	**$**	**23,121,047**
Net Increase (Decrease)	**$**	**(93,614,409)**
Net Assets - January 1		**276,994,607**
Net Assets - December 31	**$**	**183,380,198**

The notes to the financial statements are an integral part of this statement.

1. Financial Reporting Entity

The Minneapolis Firefighters' Relief Association was incorporated on November 24, 1886, to provide financing for and the payment of service, disability, or dependency pensions to its eligible members and dependents. The Association is governed by a Board of Trustees consisting of 12 persons. Ten trustees are elected by the members, and two are appointed by the City of Minneapolis. The Board bi-annually elects a president, vice president, executive secretary, assistant secretary, treasurer, and assistant treasurer.

The Association is not a component unit of the City of Minneapolis (employer), and its financial statements are not included with the City's financial statements because the City does not appoint a voting majority of the Board, and the Association is legally a separate entity and fiscally independent of the City.

2. Plan Description

A. Membership Information

Firefighters of the City of Minneapolis are members of the Minneapolis Firefighters' Relief Association. The Association is the administrator of a single-employer, defined benefit pension plan available to firefighters hired prior to June 15, 1980, and operated under the provisions of its bylaws and Minnesota State Law. Firefighters hired after June 15, 1980, are members of the Minnesota Public Employees Retirement Association Police and Fire Fund.

At December 31, 2008, the membership of the Minneapolis Firefighters' Relief Association consisted of:

Retirees and beneficiaries currently receiving benefits	563
Terminated employees entitled to benefits but not yet receiving them	-
Active plan participants - vested	27
Total	590

2. Plan Description (Continued)

B. Pension Benefits

Authority for payment of pension benefits is established in Minn. Stat. § 69.77 and ch. 423C, and may be amended only by the Minnesota State Legislature.

Normal Service Pensions

Each member who is at least 50 years of age and has five years of service with the Minneapolis Fire Department is eligible to receive a service pension, monthly, for the remainder of the member's life. All benefits are based on a plan of a number of units. A unit is 1/80th of the maximum current monthly salary of a first grade firefighter. Pensions are based on current fire department payroll and are fully escalated for all persons receiving a pension benefit. Each vested member also receives a lump sum amount, at the time of separation, from the General Fund based on the number of years the member has belonged to the Association. Units paid per month are based on the percentage that the actuarial value of assets of the special fund equal the actuarial accrued liabilities of the special fund according to the most recent annual actuarial valuation of the relief association prepared in accordance with Minn. Stat. §§ 356.215 and 356.216 and the number of years of service on the Minneapolis Fire Department. The service pension schedules in terms of units is identified in Minn. Stat. § 423C.05, subd. 2(b).

Retirement Benefit Options and Survivor Spouse Pensions

The surviving spouse of a service pensioner, who was married to the service pensioner for at least one year at the date of retirement or who has been married to the pensioner for at least two years after retirement, is entitled to a survivor spouse pension.

2. Plan Description

B. Pension Benefits

Retirement Benefit Options and Survivor Spouse Pensions (Continued)

The surviving spouse of an active plan member is entitled to an Option 1 - 100 percent Joint and Survivor Spouse Annuity survivor spouse pension, as described below.

During 1997, the Association amended the plan provisions to include several annuity options available to retiring, married members.

- Normal Retirement Benefit

  Described in detail for normal service pensioners previously, a surviving spouse receives a pension of 22 units per month for life.

- Option 1 - 100% Joint and Surviving Spouse Annuity

  This option pays the retiree a reduced monthly benefit and, upon death, continues to pay a like amount for the life of the surviving spouse.

- Option 2 - 75% Joint and Surviving Spouse Annuity

  This option is similar to Option 1, except upon death of the retiree, the surviving spouse pension is reduced to 75 percent of the previous benefit level.

- Option 3 - 50% Joint and Surviving Spouse Annuity

  This option is similar to Options 1 and 2, except upon the death of the retiree, the monthly benefit payable to the surviving spouse is reduced by 50 percent.

- Option 4 - Options 1, 2, or 3 with Bounce-Back Provision

  Options 1, 2, or 3 can be chosen with a "bounce-back" provision. This option would further reduce the monthly benefit but, should the retiree's spouse die first, the monthly benefit amount would increase or "bounce-back" to what the amount would have been had the Normal Retirement Benefit option been chosen at retirement.

2. Plan Description

B. Pension Benefits

Retirement Benefit Options and Survivor Spouse Pensions (Continued)

During 2002, the Association amended the plan provisions to include an annuity option available to retiring, unmarried members.

- Option 5

  This option allows for an offset to the married members whose surviving spouse receives a survivor spouse benefit upon their death since the surviving spouse benefit has an actuarial impact to the fund and its remaining members. This option provides that a member submitting an application for a service pension who was not legally married on September 1, 1997, and remained unmarried on October 25, 2001, may, if the member had obtained 25 years of service credit on or before October 25, 2001, select a service pension of 42.3 units in lieu of a regular 42-unit service pension. This additional fraction of a unit helps to blend out the cost of the surviving spouse benefit and provides for a more equal distribution of pension benefits to all members.

Survivor Children Pensions

The dependent children of a deceased active member or service pensioner each receive a pension of eight units until age 18, or until age 22 if they are a full-time student. The combined pension benefits for one member's surviving spouse and children may not exceed 42 units.

Disability Pensions

Whenever an active member becomes temporarily disabled because of sickness or injury, on or off the job, the member will receive a temporary disability pension of 40 units, provided the member has expired all leaves of absence.

Whenever an active member becomes permanently disabled because of sickness or injury, the member will be entitled to a permanent disability pension of 41 units. Disability arising from employment other than the Minneapolis Fire Department will cause a member to forfeit entitlement to a disability pension.

2. Plan Description

B. Pension Benefits (Continued)

Post-Retirement Benefit

On or about June 1 annually following a year in which the Association's average time weighted total rate of return earned in the most recent five years exceeds by two percent the average percentage increase in the current monthly salary of a top grade firefighter in the most recent five years, the Association pays a post-retirement benefit to eligible pensioners. The amount of the post-retirement distribution is equal to the excess investment income earned in the previous year. Excess investment income is defined as the amount by which the average time weighted total rate of return in the most recent five years exceeds the average percentage increase in the current monthly salary of a top grade firefighter in the most recent five years plus two percent. Excess investment income may not exceed one-half of one percent of the total assets of the Association. Payment to each eligible member is calculated by dividing the total number of pension units paid to the member during the previous year by the excess investment income available for distribution; however, each payment may not exceed the monthly pension amount received by the member in the prior year.

If the Association had excess investment income in the previous year *and* the actuarial value of the Association's assets according to the most recent annual actuarial valuation is greater than 102 percent of its actuarial accrued liabilities, then excess investment income may not exceed one and one-half percent of the total assets of the Association. When this occurs, payment to each eligible member is calculated by dividing the total number of pension units paid to the member during the previous year by one and one-half percent of the total assets of the Association.

When the special fund's actuarial funding level exceeds 110 percent, up to 20 percent of the assets greater than 110 percent will be distributed to eligible pensioners based on a proportionate number of units each member received in the prior year compared to the total number of units received.

3. Summary of Significant Accounting Policies

A. Basis of Presentation

The accompanying financial statements are presented in accordance with Governmental Accounting Standards Board (GASB) Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*; Statement No. 34, *Basic Financial Statements--and Management's Discussion and Analysis--for State and Local Governments*, as amended; and Statement No. 50, *Pension Disclosures*.

B. Basis of Accounting

The basis of accounting is the method by which additions and deductions to plan net assets are recognized in the accounts and reported in the financial statements. The Association uses the accrual basis of accounting. Under the accrual basis of accounting, additions are recognized when they are earned, and deductions are recognized when the liability is incurred. Resources are derived from investment earnings and contributions from the City of Minneapolis, the Association's active membership, and the State of Minnesota. Benefits are recognized when they are due and payable in accordance with the terms of the plan.

C. Net Assets

Net assets consist of the following:

- Net Assets Held in Trust for Pension Benefits represent the portion of net assets to be used to provide benefits for retirement, death, and disability payments of appropriate amounts and at appropriate times in the future.

- Net Assets Restricted for General Account represent the portion of net assets derived from membership contributions and certain investment income to be used for the good and benefit of the Association as determined by Association bylaws.

- Net Assets Restricted for Political Account represent the portion of net assets derived from membership contributions to be used for contributions to political candidates.

3. Summary of Significant Accounting Policies (Continued)

D. Investments

Investments are reported at fair value. Short-term investments are reported at cost, which approximates fair value. Investments that are regularly traded in the market are valued at last reported sales price at the current exchange rates. Investments that do not have an established market are reported at estimated fair value.

Net appreciation (depreciation) in fair value of investments includes net unrealized and realized gains and losses. Purchases and sales of securities are recorded on a trade-date basis.

Interest and dividends are recorded when earned.

E. Capital Assets

The Association follows a policy of expensing capital assets at the time of purchase. At December 31, 2008, the Association owned capital assets costing $45,727. This amount is not shown in the accompanying Statement of Plan Net Assets (Exhibit A).

F. Liabilities

The escrow account for health benefits represents amounts contributed and earnings thereon of active plan members with over 25 years of service on the City of Minneapolis Fire Department. The Association holds the funds in escrow until retirement when members will receive periodic distributions from their accounts to offset health insurance costs. The escrow account for health benefits is not available for the payment of pension benefits.

4. Deposits and Investments

A. Deposits

Authority

Minn. Stat. § 356A.06, subd. 8a, authorizes the Association to deposit cash and to invest in certificates of deposit in financial institutions designated by the Board of Trustees. Minnesota statutes require that all pension plan deposits be covered by deposit insurance, surety bond, or pledged collateral. The market value of collateral pledged shall be at least ten percent more than the amount on deposit at the close of the financial institution's banking day, not covered by insurance or bonds.

Authorized collateral includes treasury bills, notes and bonds; issues of U.S. government agencies; general obligations rated "A" or better, revenue obligations rated "AA" or better; irrevocable standby letters of credit issued by the Federal Home Loan Bank; and certificates of deposit. Minnesota statutes require that securities pledged as collateral be held in safekeeping in a restricted account at the Federal Reserve Bank or in an account at a trust department of a commercial bank or other financial institution not owned or controlled by the financial institution furnishing the collateral.

Custodial Credit Risk for Deposits

Custodial credit risk is the risk that in the event of a financial institution failure, the Association's deposits may not be returned to it. The Association's policy for custodial credit risk is to maintain compliance with Minnesota statutes that require the Association's deposits be protected by insurance, surety bond, or pledged collateral. The Association's deposits at December 31, 2008, are completely protected and therefore, there is no custodial credit risk for deposits.

4. Deposits and Investments (Continued)

B. Investments

Authority

Minn. Stat. §§ 356A.06, subds. 6 and 7, and 69.77, subd. 9, authorize the types of, and restrictions on, securities available to the Association for investment. The Association is authorized to invest its funds in the following:

(a) Government obligations provided the issue is backed by the full faith and credit of the issuer or is rated among the top four quality rating categories by a nationally recognized rating agency. Such obligations may include: (1) guaranteed or insured issues of the United States or its agencies, instrumentalities, or organizations created and regulated by an act of Congress; (2) guaranteed or insured issues of Canada and its provinces; or (3) guaranteed or insured issues of states and their municipalities, political subdivisions, agencies, or instrumentalities.

(b) Corporate obligations issued or guaranteed by a corporation organized under the laws of the United States or any state thereof, or the Dominion of Canada or any province thereof, provided they are rated among the top four quality categories by a nationally recognized rating agency.

(c) Corporate stock or convertible issues of any corporation organized under the laws of the United States or states thereof, the Dominion of Canada or its provinces, or any corporation listed on the New York Stock Exchange or the American Stock Exchange under specified conditions.

(d) TBA or "to-be-announced" mortgage-backed securities transactions. These are a basic mechanism for trading federal agency mortgage pass-through securities on a delayed delivery and settlement basis. They do not represent a separate type or class of mortgage-backed securities. A TBA transaction is a purchase or sale of mortgage pass-through securities with settlement agreed upon for some future date. The purchase of pass-throughs on a TBA basis creates a long position in the underlying security on the trade date with associated market risk in the position. The securities to be delivered are described in general detail at the time of trade but are not specifically identified until shortly prior to settlement. TBA transactions may involve newly-issued or existing agency mortgage pass-throughs.

4. Deposits and Investments

B. Investments

Authority (Continued)

(e) Venture capital investment businesses through participation in limited partnerships and corporations, subject to limitations.

(f) Regional and mutual funds through bank-sponsored collective funds and open-end investment companies registered under the Federal Investment Company Act of 1940, subject to limitations.

(g) Real estate ownership interests or loans secured by mortgages or deeds of trust through investment in limited partnerships, bank-sponsored collective funds, trusts, and insurance company commingled accounts, including separate accounts, subject to limitations.

(h) Resource investments through limited partnerships, private placements, and corporations, subject to limitations.

(i) Bankers' acceptances, certificates of deposit, deposit notes, commercial paper, mortgage participation certificates and pools, asset-backed securities, repurchase agreements and reverse repurchase agreements, guaranteed investment contracts, savings accounts, and guaranty fund certificates, surplus notes, or debentures of domestic mutual insurance companies, if they conform to specified provisions.

Custodial Credit Risk for Investments

The custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the Association will not be able to recover the value of the investment or the collateral securities in the possession of an outside party.

A third-party safekeeping agent appointed as custodian holds 99.6 percent of the securities purchased by the Association.

The Association has no custodial credit risk for investments at December 31, 2008.

4. Deposits and Investments

B. Investments (Continued)

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Duration is a measure of a debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows weighted for those cash flows as a percentage of the investment's full price.

The Association manages its exposure to fair value of loss arising from changing interest rates by having fixed income investments managed by external money managers. The Association employs three managers who invest in fixed income investments. The investment guidelines for each manager require that the manager be responsible for determining the maturities for all fixed income securities within their portfolio.

For these asset managers, the duration of the overall portfolio must be managed to have a targeted duration around the duration of the Barclay's Capital Aggregate Bond Index of 3.80 years, as this is the benchmark for all these portfolios. All managers were in compliance with the duration guidelines for the year ended December 31, 2008.

The following table shows the interest rate risk by manager.

Bond Manager	Fair Value of Fixed Income Securities Managed	Account Duration (in Years)
FAF Advisors	$ 4,677,190	3.9
RiverSource Investments, LLC	15,185,934	4.2
Mairs and Power, Inc.	13,918,514	8.8

The Association has $4,658,485 in the Minnesota State Board of Investment (SBI) Supplemental Investment Fund Bond Market Account. This account invests the large majority of its assets in high quality government and corporate bonds and mortgage securities that have intermediate to long-term maturities, usually 3 to 20 years. The managers of this account also may attempt to earn returns by anticipating changes in

4. Deposits and Investments

B. Investments

Interest Rate Risk (Continued)

interest rates and adjusting holdings accordingly. This account is invested entirely in fixed income securities. In addition, the Association has $3,055,908 in a U.S. Treasury bill which matures on February 12, 2009, and is managed by Leuthold Weeden Capital Management.

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. Minnesota statutes provide for the types of fixed income investments that a pension plan can make. In addition, the Association establishes other restrictions that are set forth in the investment guidelines for the management of the Association's fixed income assets.

This risk is measured by the assignment of a rating by a nationally recognized statistical rating organization.

The following table shows the Association's investments by type and credit quality rating at December 31, 2008.

		Standard and Poor's Quality Ratings				
Investment Type	Fair Value	AAA	AA	A	BBB	Unrated
Corporate Obligations	$ 7,839,072	$ -	$ 73,628	$ 727,435	$ 989,755	$ 6,048,254
Foreign Obligations	266,776	-	-	-	-	266,776
Mortgage-Backed Securities	3,028,406	-	-	-	-	3,028,406
SBI Bond Market Account	4,658,485	-	-	-	-	4,658,485
U.S. Government Agencies	19,707,890	1,255,196	-	-	-	18,452,694
U.S. Treasury Obligations	5,995,402	-	-	-	-	5,995,402*
Totals	$ 41,496,031	$ 1,255,196	$ 73,628	$ 727,435	$ 989,755	$ 38,450,017

*Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality.

4. Deposits and Investments

B. Investments (Continued)

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates of foreign currencies relative to the U.S. dollar adversely affect the fair value of an investment or a deposit. The Association limits this risk in several ways. Minnesota statutes limit certain investments to a total portfolio limit of no more than 35 percent of the market value of the portfolio. Both international equities and international bonds are in this category. Other items include venture capital, real estate, and partnerships.

The Association's investments managed by several of its managers include either equities or debt securities or combination of equities and debt securities exposed to foreign currency risk.

Risk of loss arises from changes in currency exchange rates. The Association's exposure to foreign currency risk at December 31, 2008, is presented in the following table.

Currency	Total	Fixed Income Security	Stocks in ADR	Stocks
Bermudian Dollar	$ 132,099	$ -	$ 132,099	$ -
Brazilian Real	221,968	-	221,968	-
British Pound	516,593	20,092	496,501	-
Canadian Dollar	712,800	222,989	489,811	-
Caymanian Dollar	36,250	-	36,250	-
Chinese Yuan Renminbi	78,390	-	78,390	-
Euro	490,402	13,695	476,707	-
Israeli Shekel	794,101	-	794,101	-
Mexican Peso	10,000	10,000	-	-
Swiss Franc	420,883	-	342,878	78,005
Totals	$ 3,413,486	$ 266,776	$ 3,068,705	$ 78,005

4. Deposits and Investments

B. Investments

Foreign Currency Risk (Continued)

In addition, of the Association's holdings in mutual funds totaling $47,925,890, the following are international equity and bond mutual funds:

Mutual Fund	Fair Value
Dodge and Cox International Stock	$ 10,727,881
Ivy Global Funds	4,861,931
Leuthold Weeden Capital Management (various funds within account)	4,099,237
Manning & Napier	17,060,323
Total	$ 36,749,372

Concentration of Credit Risk

The Association's investment policy limits investments in any one issuer to not more than five percent, unless the manager has received prior approval, or the increase is a result of market price increase. U.S. Treasuries and agencies are exempted. The Association's investments as of December 31, 2008, were below these limits.

5. Contributions

Authority for contributions to the pension plan is established by Minn. Stat. § 69.77 and may be amended only by the Minnesota State Legislature.

The Association's funding policy provides for contributions from the City of Minneapolis, the State of Minnesota, and active plan members. City contributions are actuarially determined pursuant to Minn. Stat. § 69.77, subd. 4, and ch. 423C. Minn. Stat. § 423C.15, subd. 3, requires full funding of the Association's unfunded accrued liability by December 31 of the year occurring 15 years later. Active plan members contribute annually an amount equal to eight percent of the maximum first grade firefighter's salary from which pension benefits are determined. The State of Minnesota annually contributes fire state aid pursuant to Minn. Stat. §§ 69.021 and 297I.10. The City of Minneapolis and the State of Minnesota provided statutory contributions in 2008. Since all active plan members have achieved 25 years of service, active member contributions are no longer required.

6. Risk Management

The Association is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and injuries to employees. The Association manages its risk of loss through the purchase of commercial insurance. There were no significant reductions in insurance from the previous year, nor have there been any settlements in excess of insurance coverage for any of the past three years.

7. Contingencies

In connection with the normal conduct of its affairs, the Association is involved in various claims, litigation, and judgments. It is expected that the final settlement of these matters will not materially affect the financial statements of the Association.

8. Funded Status and Funding Progress

Effective December 31, 2008, the Association implemented the provisions of GASB Statement No. 50, *Pension Disclosures*. The disclosures are amendments to GASB Statement 25 and present the disclosures of the actuarial methods, assumptions, and funded status of the plan in the financial notes. The funded status as of December 31, 2008, the most recent actuarial date, is as follows:

Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b) (%)	Annual Covered Payroll (Previous Fiscal Year) (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c) (%)
$ 237,401,000	$ 280,312,000	$ 42,911,000	84.7%	$ 2,325,000	1845.6%

The net funded ratio decreased 8.1 percent. The Schedule of Funding Progress, presented as required supplementary information (RSI) following the notes to the financial statements, presents similar information but uses a multi-year format to show trend information. These trends indicate whether the actuarial values of plan assets are increasing or decreasing over time relative to the Actuarial Accrued Liability for benefits. The trend information was obtained from the Association's independent actuary's annual valuation report.

8. Funded Status and Funding Progress (Continued)

Additional information as of the latest valuation follows:

- the most recent actuarial valuation date is December 31, 2008;
- actuarial cost is determined using the Entry Age Normal Cost Method;
- the amortization method is determined using the level annual dollar approach;
- the actuarial value of assets is book value plus the average unrealized gain for the last three years minus excess investment income as defined by state law; and
- the unfunded accrued liability is amortized using a 15-year period.
- Significant actuarial assumptions are as follows:
  - investment rate of return is six percent per annum;
  - projected salary increase is four percent annually, adjusted by the terms of a collective bargaining agreement;
  - post-retirement benefit increases are not projected;
  - there is no inflation rate assumption; and
  - mortality assumptions use the 1983 GAM Mortality Table set forward two years for females.

REQUIRED SUPPLEMENTARY INFORMATION

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THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

Schedule 1

SCHEDULE OF FUNDING PROGRESS

Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b) (%)	Annual Covered Payroll (Previous Fiscal Year) (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c) (%)
2003	$ 236,991,000	$ 293,955,000	$ 56,964,000	80.6	$ 4,397,000	1295.5
2004	248,546,000	275,513,000	26,967,000	90.2	3,142,000	858.3
2005	269,426,000	312,563,000	43,137,000	86.2	2,933,000	1470.7
2006	263,276,000	300,926,000	37,650,000	87.5	2,489,000	1512.7
2007	270,096,000	291,078,000	20,982,000	92.8	2,236,000	938.4
2008	237,401,000	280,312,000	42,911,000	84.7	2,325,000	1845.6

THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

Schedule 2

SCHEDULE OF CONTRIBUTIONS FROM THE PLAN SPONSOR AND OTHER CONTRIBUTING ENTITIES

Fiscal Year	Annual Required Contributions	City Contributions	City Percentage Contributed (%)	State Contribution	State Percentage Contributed (%)
2003	$ 1,333,171	$ 4,270	0.32	$ 1,328,901	99.68
2004	1,950,098	2,670	0.14	2,146,934	110.09
2005	6,651,403	4,737,705	71.23	1,913,951	28.78
2006	2,570,016	1,348,855	52.48	1,221,161	47.52
2007	4,290,278	3,030,347	70.63	1,259,931	29.37
2008	4,750,149	3,336,852	70.25	1,413,297	29.75

Note:
The annual required contributions are actuarially determined. The City and State are required by statute to make contributions, all of which have been made.

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NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULES 1 AND 2
FOR THE YEAR ENDED DECEMBER 31, 2008

Actuarial Methods and Assumptions

The actuarial accrued liability is determined as part of an annual actuarial valuation on December 31, 2008. Significant methods are as follows:

- The most recent actuarial valuation date is December 31, 2008.
- Actuarial cost is determined using the Entry Age Normal Cost Method.
- The amortization method is determined using the level annual dollar approach.
- The actuarial value of assets is book value plus the average unrealized gain for the last three years minus excess investment income as defined by state law.
- The unfunded accrued liability is amortized over a 15-year period.

Significant actuarial assumptions are as follows:

- Investment rate of return is six percent per annum.
- Projected salary increase is four percent annually, adjusted by the terms of a collective bargaining agreement.
- Post-retirement benefit increases are not projected.
- There is no inflation rate assumption.
- Mortality assumptions use the 1983 GAM Mortality Table set forward two years for females.

There have been no significant changes to plan provisions and actuarial methods and assumptions in the last six years, except the following:

- The salary scale, which has been adjusted to reflect new collective bargaining agreements.

In addition:

In 2005, the mortality assumptions changed from using the UP-1984 Mortality Table set forward two years for males and set back three years for females to the 1983 GAM Mortality Table set forward two years for females.

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Management and Compliance Section

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THE MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION
MINNEAPOLIS, MINNESOTA

Schedule 3

SCHEDULE OF FINDINGS AND RECOMMENDATIONS
FOR THE YEAR ENDED DECEMBER 31, 2008

I. INTERNAL CONTROL OVER FINANCIAL REPORTING

PREVIOULY REPORTED ITEM NOT RESOLVED

06-1 Internal Control/Segregation of Duties/Preparation of Financial Statements

Management is responsible for establishing and maintaining internal control. This responsibility includes the internal control over the various accounting cycles, the fair presentation of the financial statements and related notes, and the accuracy and completeness of all financial records and related information. Adequate segregation of duties is a key internal control in an organization's accounting system. The size of the Minneapolis Firefighters' Relief Association and its staffing limits the internal control that management can design and implement into the organization. This situation is not unusual in operations the size of the Association, but the Board of Trustees should constantly be aware of this condition and realize that the concentration of duties and responsibilities in a limited number of individuals is not desirable from an internal control and accounting point of view.

Generally, segregation of duties can be attained with the hiring of additional personnel; however, this becomes a significant cost consideration to entities such as the Association. Under the above conditions, the most effective system of control lies in the knowledge of the Board of Trustees regarding the Association's operations and the periodic review of those operations.

Management is also responsible for controls over the period-end financial reporting process, including controls over procedures used to enter transaction totals into the general ledger; initiate, authorize, record, and process journal entries into the general ledger; and record recurring and nonrecurring adjustments to the financial statements. The Association has established controls and procedures for recording, processing, and summarizing its accounting data used in the preparation of its basic financial statements.

As is the case with many small and medium-sized entities, however, the Association has requested its independent external auditors to assist in the preparation of the basic financial statements, including notes to the financial statements, and relied on us to format information from the Association's financial records to the financial statements as reported as part of the external financial reporting process. This decision was based on the availability of the Association's staff and the cost benefit of using our expertise.

Accordingly, the Association's ability to prepare financial statements in accordance with generally accepted accounting principles (GAAP) is based, at least in part, on its reliance on its external auditors who cannot, by definition, be considered part of the Association's internal control.

We recommend the Board of Trustees be mindful that limited staffing causes inherent risks in safeguarding the Association's assets and the proper reporting of its financial activity. The Board of Trustees should continue to implement oversight procedures and monitor those procedures to determine if they are still effective internal controls. If the Association still intends to have staff from the Office of the State Auditor assist in the preparation of its annual financial statements in accordance with GAAP then, at a minimum, it must retain individuals with the expertise that can sufficiently review, understand, and approve the financial statements, including notes. As an alternative, the Association could consider hiring an outside consultant to assist in preparing its basic financial statements.

Client's Response:

In response to the Auditor's concerns over internal control over financial reporting, the MFRA has hired another person to aid in providing additional assistance with the duties of internal control, segregation of duties and preparation of financial statements.

II. COMPLIANCE

PREVIOUSLY REPORTED ITEM NOT RESOLVED

03-1 Components of Unit Value

Pension benefits for the Minneapolis Firefighters' Relief Association are based on a unit value. Minn. Stat. § 423C.01, subd. 28, and the Association's bylaws define a unit as 1/80th of the maximum monthly salary of a first grade firefighter on the first day of the month in which pension benefits are paid.

Schedule 3
(Continued)

Following is a schedule of the calculation of per unit value used at December 31, 2008:

Component	Hourly Rate	Number of Hours	Annually	Monthly	Per Unit
Base wages	$ 21.85	2,848	$ 62,285.84	$ 5,190.49	$ 64.88
Selection premium	.77	2,848	2,195.95	183.00	2.29
Longevity	2.65	2,848	7,542.16	628.51	7.86
Health club dues	-	-	392.97	32.75	0.41
Sick leave buy back	25.27	144	3,639.10	303.26	3.79
Vacation cash out	25.27	48	1,213.03	101.09	1.26
FLSA overtime	12.64	84.46	1,068.17	89.01	1.11
Overtime (@1.5)	37.91	136	5,155.39	429.62	5.37
Work out of grade	-	-	904.87	75.41	0.94
Holiday pay	12.64	35.59	449.75	37.48	0.47
Total			$ 84,847.23	$ 7,070.60	$ 88.38

The sum of the hourly rate for base wages, selection premium, and longevity is the rate used to calculate the unit value for hours of sick leave buy back, vacation cash out, FLSA overtime, holiday pay, and overtime components. Work out of grade refers to compensation firefighters are eligible to receive when they perform the duties of a higher job classification, and it is calculated by taking the pay differential between a firefighter's regular rate of pay and the hourly rate payable if he or she had been permanently promoted to the higher rank with at least a five percent increase in this differential.

The Association's bylaws identify that the components of salary be included to the extent they are payable under a collective bargaining agreement. Those salary components added after the 1995 Settlement Agreement between the Association and the City of Minneapolis should be included at the average amount paid to those first grade firefighters who received the compensation item. Therefore, actual payroll practices of the City of Minneapolis have been reviewed to determine that the salary components used by the Association in the unit value calculation were not inconsistent with payments to active firefighters.

The actual payroll practice of the City of Minneapolis, for work out of grade, 48 hours of vacation cash out, 144 hours of sick leave buy back, and 35.59 hours of holiday pay, is that these components of pay are not paid at a rate which includes selection premium. The City's practice is consistent with the terms of the collective bargaining agreement in that selection premium is paid only on hours worked as a firefighter. Therefore, the unit value calculation for the Association should not include selection premium in those components because they do not represent hours worked. The unit value is overstated by approximately $0.17/unit, or $85.68 per year per beneficiary at the maximum 42 units.

The 1995 Settlement Agreement states that salary includes "an average of overtime actually worked in excess of FLSA overtime amounts by firefighters with 25 years or more of service, up to a maximum of 136 hours, in the immediately preceding year." The Association uses the maximum 136 hours of overtime in its unit value calculation. However, there is no indication that any actual average overtime amounts of eligible firefighters paid by the City are reflected in this amount. The Association maintains that 136 hours of overtime was intended to be the agreed-upon amount to remain unchanged as negotiated during the 1995 Settlement Agreement. This is not what the express language of that agreement reflects. The actual City of Minneapolis payroll records indicate the following:

- For 2003, only four firefighters were at Step 7 with more than 25 years of service. Two of these four firefighters worked 12 hours of overtime each. The average overtime worked for the four qualifying firefighters is 6 hours.

- For 2005, there were five firefighters at Step 7 with more than 25 years of service. Two of these worked one hour of overtime each, and two firefighters worked three hours each. The average overtime worked for the five qualifying firefighters is 1.6 hours.

- For 2006, there were two firefighters at Step 7 with more than 25 years of service. These two firefighters worked 64 and 110 hours of overtime. The average overtime worked for the two qualifying firefighters is 87 hours.

- For 2007, there were five firefighters at Step 7 with more than 25 years of service. All five firefighters worked overtime for a total of overtime hours worked of 84.25. The average overtime worked for the five qualifying firefighters is 16.85 hours.

- For 2008, there were five firefighters at Step 7 with more than 25 years of service, two of which retired in the first three months of the year. Of the three remaining firefighters, two of them worked 117.5 and 12 hours of overtime. The average overtime worked for the three remaining qualifying firefighters is 43.17 hours.

Substituting 43.17 hours of overtime for 136 hours, an $88.38 unit value is overstated by approximately $3.67/unit, or $1,847 per year per beneficiary at the maximum 42 units.

In the 2003 audit, we recommended the Association review and analyze components of unit value. The Association and its legal counsel have reviewed its methods and calculations of monthly salary used to calculate unit value and have concluded they are proper and reasonable. They obtained payroll data from the City of Minneapolis and formulated a methodology for accumulating averages, which were then used to calculate average hours for certain components of pay, including vacation cash out, work out of grade, and holiday pay. The Association has included those amounts in its subsequent unit value calculations.

We recommend the unit value reflect compliance with the terms of the 1995 Settlement Agreement and the collective bargaining agreement. The City of Minneapolis and the Association should agree on the methodology for determining relevant averages for the components of pay to be included in the unit value calculation. The actual payroll practice of the City of Minneapolis should be followed for the components of salary that are used by the Association as the basis for calculating the unit value for pension benefits to ensure consistency. This matter is in litigation.

<u>Client's Response</u>:

It is and always has been the MFRA Board of Trustees belief that the components of the unit value are correctly applied. This matter is currently in the hands of the District Court System for an independent determination.

<u>ITEM ARISING THIS YEAR</u>

08-1 <u>Investment in Post Total Return Offshore Fund</u>

In 2008, the Association invested in shares of the Post Total Return Offshore Fund (Post Total), a Cayman Island exempt company. This company, in turn, invests in a limited partnership called the Post Total Master Fund L.P. We have not identified any statutory authority under which this investment would be permitted.

We requested information on this investment and were provided with a copy of the Subscription Booklet that the Association used to purchase the shares of Post Total. This Booklet indicates that investors should read the Confidential Private Placement Memorandum and Articles of Association of the Fund, which are distributed separately to investors. We requested copies of the Fund Documents including the Confidential Private Placement Memorandum and Articles of Association of the Fund, all referred to in the Subscription Booklet. In June 2009, we were provided with a copy of the Confidential Private Placement Memorandum dated January 1, 2008.

We also obtained a copy of the Financial Statements of Post Total and Post Total Return Master Fund for year ended December 31, 2008. The Post Total Fund Placement Memorandum and Financial Statements reveal that the Limited Partnership invests in the following highly speculative investments:

- short sales of debt and equity,
- credit fault swaps, and
- uncovered options.

We can find no authority for the Association to invest in the shares of a Cayman Island exempt company. Besides U.S. and Canadian corporate stock, exchange traded funds, and shares in mutual funds, the Association is authorized to purchase shares of only emerging market equities and venture capital businesses. (Minn. Stat. § 356A.06, subd. 7.) The shares of Post Total do not qualify under any of these permissible investment types. Our inquiries of the Post Total Fund management confirmed that Post Total is not a venture capital investment, nor does it qualify as domestic government or corporate debt under Minn. Stat. § 69.77, subd. 9.

Additionally, we question whether indirect investment in highly speculative investments such as those identified above is consistent with the role of a public pension plan fiduciary. On page 26 of the Private Placement Memorandum (2008), the "Investment Philosophy" of the Fund is summarized in bold lettering. It begins:

> The investment program of the Fund is <u>speculative</u> and may entail substantial risk. (emphasis added)

Minn. Stat. § 356A.04 defines the "prudent person standard" for public pension plan fiduciaries as follows:

> A fiduciary . . . shall exercise that degree of judgment and care, under the circumstances then prevailing, that persons of prudence, discretion, and intelligence would exercise in the management of their own affairs, not for speculation, considering the probable safety of the plan capital as well as the probable investment return. . . . (emphasis added)

The plain language of the statute setting forth the plan's fiduciary duty is at odds with the bold-letter risk warning of Post Total's investment strategy.

We recommend that in the future the Association invest only in securities authorized by statute and avoid indirect investment in highly speculative securities. Further, we recommend that the Association obtain and retain in its files the Offering Memorandum or other investor information documents that set forth the objectives, risks, limitations and structure of investments it is making.

Client's Response:

The Executive Secretary and the MFRA General Counsel have engaged in numerous discussions with the State Auditor's Office and their Legal Counsel over this matter. It is the MFRA's belief that this investment was entered into with the full and sincere belief that this investment vehicle was legal and proper for the use of the MFRA in their investment strategy. The vehicle has performed exceptionally well for the MFRA and it is with great regret that we will place this item before the MFRA Board of Trustees at the August 14, 2009, Board Meeting for a discussion of the Auditor's concerns and their suggestion that the MFRA discontinue the use of this investment vehicle based on their belief that Minnesota State Laws do not allow the MFRA to participate in this type of investment vehicle.

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND MINNESOTA LEGAL COMPLIANCE

Board of Trustees
Minneapolis Firefighters' Relief Association

Internal Control Over Financial Reporting

In planning and performing our audit of the basic financial statements of the Minneapolis Firefighters' Relief Association as of and for the year ended December, 31, 2008, in accordance with auditing standards generally accepted in the United States of America, we considered the Association's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Association's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Association's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Association's financial statements that is more than inconsequential will not be prevented or detected by the Association's internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Association's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified the deficiency described in the accompanying Schedule of Findings and Recommendations as item 06-1 to be a significant deficiency in internal control over financial reporting.

Minnesota Legal Compliance

We have audited the basic financial statements of the Association as of and for the year ended December 31, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the provisions of the *Minnesota Legal Compliance Audit Guide for Local Government*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65. Accordingly, the audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The *Minnesota Legal Compliance Audit Guide for Local Government* covers three categories of compliance to be tested in audits of relief associations: deposits and investments, conflicts of interest, and relief associations. Our study included all of the listed categories.

The results of our tests indicate that, for the items tested, the Association complied with the material terms and conditions of applicable legal provisions, except as described in the Schedule of Findings and Recommendations as items 03-1 and 08-1.

The Association’s written responses to the significant deficiency and compliance findings identified in our audit have been included in the Schedule of Findings and Recommendations. We did not audit the Association’s responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Board of Trustees, management, and others within the Association and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Rebecca Otto	*/s/Greg Hierlinger*
REBECCA OTTO STATE AUDITOR	GREG HIERLINGER, CPA DEPUTY STATE AUDITOR

July 31, 2009