MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT

FINANCIAL AUDIT
OF THE

MICHIGAN LEGISLATIVE RETIREMENT SYSTEM

October 1, 2008 through September 30, 2010

THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

900-0140-11

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

Audit report information can be accessed at:
http://audgen.michigan.gov

Michigan
Office of the Auditor General
REPORT SUMMARY

Financial Audit

Michigan Legislative Retirement System

October 1, 2008 through September 30, 2010

Report Number:
900-0140-11

Released:
September 2011

A financial audit determines if the financial statements are fairly presented; considers internal control over financial reporting; and determines compliance with requirements material to the financial statements. This financial audit of the Michigan Legislative Retirement System (MLRS) was conducted as part of the constitutional responsibility of the Office of the Auditor General.

Financial Statements:
Auditor's Report Issued
We issued an unqualified opinion on the MLRS financial statements.

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Internal Control Over Financial Reporting
We identified a significant deficiency in internal control over financial reporting (Finding 1).

MLRS's controls over financial reporting did not ensure the accuracy of the investment classifications on MLRS's statement of pension plan and other postemployment benefits (OPEB) plan net assets. As a result, mutual funds were overstated and alternative investments were understated by $7.8 million as of September 30, 2010. In addition, the amount of equities reported to the Office of Financial Management for inclusion in the *State of Michigan Comprehensive Annual Financial Report* was not properly classified between domestic and international equities.

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Noncompliance and Other Matters Material to the Financial Statements
We did not identify any instances of noncompliance or other matters applicable to the financial statements that are required to be reported under *Government Auditing Standards*.

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Agency Response:
Our audit report includes 1 finding and 1 corresponding recommendation. MLRS's preliminary response indicates that it agrees with the recommendation.

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Background:
MLRS is a single employer, public employee, defined benefit retirement plan and postemployment healthcare plan governed by the State of Michigan. MLRS was created by Act 261, P.A. 1957, as amended, and provides retirement and ancillary benefits to eligible current and former State legislators. MLRS's financial statements

are included as pension and other employee benefit trust funds in the combined financial statements of the State of Michigan.

MLRS operates within the legislative branch of State government. The MLRS Board of Trustees appoints the director who serves as executive secretary to the MLRS Board, with whom the general oversight of MLRS resides. Act 486, P.A. 1996, amended the MLRS enabling statute to mandate that persons elected to the Michigan Legislature after March 30, 1997 participate in a Statewide defined contribution retirement plan administered by the Department of Technology, Management, and Budget. The defined contribution retirement plan operates as a 401(k) plan and is part of the State of Michigan 401K Plan. The State of Michigan 401K Plan annual financial report is issued separately.

A copy of the full report can be obtained by calling 517.334.8050 or by visiting our Web site at: http://audgen.michigan.gov

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Lansing, Michigan 48913

Thomas H. McTavish, C.P.A.
Auditor General

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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

September 30, 2011

The Honorable R. Robert Geake, Chair
Board of Trustees
and
Ms. Christine I. Hammond, Director
Michigan Legislative Retirement System
Cora Anderson Building
Lansing, Michigan

Dear Mr. Geake and Ms. Hammond:

This is our report on the financial audit of the Michigan Legislative Retirement System (MLRS) for the period October 1, 2008 through September 30, 2010.

This report contains our report summary, our independent auditor's report on the financial statements, the MLRS management's discussion and analysis, the MLRS financial statements, and required supplementary information. This report also contains the independent auditor's report on internal control over financial reporting and on compliance and other matters; our finding, recommendation, and agency preliminary response; and a glossary of acronyms and terms. The agency preliminary response was taken from the agency's response subsequent to our audit fieldwork.

We appreciate the courtesy and cooperation extended to us during this audit.

Michigan Auditor General

AUDITOR GENERAL

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INDEPENDENT AUDITOR'S REPORT

STATE OF MICHIGAN
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

Independent Auditor's Report on the Financial Statements

The Honorable R. Robert Geake, Chair
Board of Trustees
and
Ms. Christine I. Hammond, Director
Michigan Legislative Retirement System
Cora Anderson Building
Lansing, Michigan

Dear Mr. Geake and Ms. Hammond:

We have audited the accompanying basic financial statements of the Michigan Legislative Retirement System, as of and for the fiscal years ended September 30, 2010 and September 30, 2009, as identified in the table of contents. These financial statements are the responsibility of the Michigan Legislative Retirement System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 2, the financial statements present only the Michigan Legislative Retirement System and do not purport to, and do not, present fairly the financial position of the State of Michigan or its pension and other employee benefit trust funds as of September 30, 2010 and September 30, 2009 and the changes in financial position thereof for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the plan net assets of the Michigan Legislative Retirement System as of September 30, 2010 and September 30, 2009 and the changes in plan net assets for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 6, the Michigan Legislative Retirement System adopted Governmental Accounting Standards Board Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments.*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 15, 2011 on our consideration of the Michigan Legislative Retirement System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 11 through 15 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, 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.

The accompanying required supplementary information, as identified in the table of contents, is not a required part of the Michigan Legislative Retirement System's financial statements but is supplementary information required by the Governmental Accounting Standards Board. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Michigan Auditor General

AUDITOR GENERAL

September 15, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

The management's discussion and analysis of the Michigan Legislative Retirement System (MLRS) provides an overview of the financial activities and performance for the fiscal years ended September 30, 2010, September 30, 2009, and September 30, 2008. This should be read in conjunction with the financial statements and required supplementary information, which provides information for September 30, 2010 and September 30, 2009.

The statement of pension plan and other postemployment benefits (OPEB) plan net assets presents MLRS's assets and liabilities, with the difference between the two reported as net assets. Over time, increases and decreases in net assets measure whether MLRS's financial position is improving or deteriorating. The statement of changes in pension plan and other postemployment benefits (OPEB) plan net assets presents how MLRS's net assets changed during the fiscal year. These two financial statements should be reviewed along with the schedules of funding progress (page 39) and schedules of employer and other contributions (page 40) to determine whether MLRS is becoming financially stronger or weaker and to understand changes over time in the funded status of MLRS.

Financial Overview

Statement of Pension Plan and Other Postemployment Benefits (OPEB) Plan Net Assets

The statement of plan net assets presents information on MLRS's assets and liabilities using the accrual basis of accounting. Over time, increases or decreases in net assets may serve as a useful indicator of MLRS's financial strength or weakness. MLRS's plan net assets for the fiscal year ended September 30, 2010 **increased** by $4,225,666 or 2.7% due to the increase in market value of MLRS investments. MLRS's plan net assets for September 30, 2009 **decreased** by $5,579,950 or 3.4%, which was primarily due to benefit costs increasing greater than the increase in market value of MLRS investments.

Condensed Financial Information From the
Statement of Pension Plan and Other Postemployment Benefits (OPEB) Plan Net Assets
As of September 30
(In Thousands)

	2010	Increase (Decrease) Amount	Increase (Decrease) Percentage	2009	Increase (Decrease) Amount	Increase (Decrease) Percentage	2008
Assets							
Cash	$ 3,252	$ (350)	(9.7%)	$ 3,602	$ (2,967)	(45.2%)	$ 6,569
Receivables	550	(581)	(51.4%)	1,131	128	12.8%	1,003
Investments	157,415	5,109	3.4%	152,307	(3,668)	(2.4%)	155,974
Total assets	$161,218	$ 4,178	2.7%	$157,039	$ (6,506)	(4.0%)	$ 163,546
Liabilities							
Warrants outstanding	$ 25	$ 2	9.2%	$ 23	$ 1	2.6%	$ 23
Accounts payable and other liabilities	625	(49)	(7.3%)	675	(927)	(57.9%)	1,602
Total liabilities	$ 651	$ (47)	(6.8%)	$ 698	$ (926)	(57.0 %)	$ 1,624
Total net assets	$160,567	$ 4,226	2.7%	$156,341	$ (5,580)	(3.4%)	$ 161,921

Statement of Changes in Pension Plan and Other Postemployment Benefits (OPEB) Plan Net Assets

Additions to Plan Net Assets

The reserves needed to finance benefits* provided by MLRS are accumulated through the collection of court fees, member* and other contributions, State appropriations, and through earnings on investments. Contributions, net investment income (loss), and other revenues for fiscal year 2009-10 totaled $21,670,030. Total additions to plan net assets **increased** 91.7% from the prior year due primarily to the fact that the MLRS investments increased. Contributions, net investment income (loss), and other revenues for fiscal year 2008-09 totaled $11,304,136. Total additions to plan net assets in fiscal year 2008-09 **increased** 142.5% from the prior year due primarily to the fact that the MLRS investments increased.

Deductions From Net Plan Assets

The primary deductions include the payment of pension and life insurance benefits to members and beneficiaries; the payments for health, dental, and vision benefits; the refund or transfer of contributions to former members; and the cost of administering

** See glossary at end of report for definition.*

MLRS. Total deductions for fiscal year 2009-10 were $17,444,364, an **increase** of 3.3% over fiscal year 2008-09 deductions. Total deductions for fiscal year 2008-09 were $16,884,086, an **increase** of 8.7% over fiscal year 2007-08 deductions. The increases are primarily due to the increase in retirement and healthcare benefits.

Condensed Financial Information From the
Statement of Changes in Pension Plan and
Other Postemployment Benefits (OPEB) Plan Net Assets
For Fiscal Years Ended September 30
(In Thousands)

	2010	Increase (Decrease) Amount	Increase (Decrease) Percentage	2009	Increase (Decrease) Amount	Increase (Decrease) Percentage	2008
Additions							
Other member contributions	$ 108	$ (7)	(6.0%)	$ 115	$ (8)	(6.3%)	$ 123
DC health premiums	56	15	36.1%	41	19	85.9%	22
Other contributions	3,574	(11)	(0.3%)	3,585	7	0.2%	3,578
Court fees	1,091	(58)	(5.0%)	1,148	(71)	(5.8%)	1,219
Net investment income (loss)	16,588	10,482	171.7%	6,106	37,970	119.2%	(31,864)
Miscellaneous income	252	(56)	(18.2%)	309	(43)	(12.3%)	352
Total additions	$ 21,670	$ 10,366	91.7%	$ 11,304	37,874	142.5%	$ (26,570)
Deductions							
Retirement benefits	$ 11,122	$ 329	3.0%	$ 10,793	$ 529	5.2%	$ 10,264
Healthcare benefits	5,293	138	2.7%	5,155	437	9.3%	4,719
Death benefits	333	(124)	(27.2%)	458	303	196.3%	154
Refunds/qualified rollover	305	197	181.6%	108	99	1,092.5%	9
Administrative expenses	391	21	5.7%	370	(11)	(2.8%)	381
Total deductions	$ 17,444	$ 560	3.3%	$ 16,884	$ 1,357	8.7%	$ 15,527
Changes in net assets	$ 4,226	$ 9,806	175.7%	$ (5,580)	$ 36,517	86.7%	$ (42,097)
Ending net assets	$ 160,567	$ 4,226	2.7%	$ 156,341	$ (5,580)	(3.4%)	$ 161,921

Overall Financial Analysis

One year prior to fiscal year 2008-09, the equity and credit markets were falling rapidly, the government was introducing massive stimulus packages, and many feared we were headed for the second Great Depression. By early 2009, the markets appeared to be forecasting the worst case scenario. Credit investments were priced for default rates not seen since the 1930s, and equities had fallen over 50% from their highs in 2007. As if a switch had been flipped, the markets began to turn in March 2009 with the S&P* 500 Index gaining 18% over the second half of that month. Strong equity performance

** See glossary at end of report for definition.*

continued with returns of over 15% for both the second and third quarters. By the end of MLRS's fiscal year, the S&P 500 Index was up over 50% from its March low, although it was still in negative territory over the one-year period ended September 30, 2009. International stocks, especially emerging markets, performed even better since the March turning point. Credit markets also realized impressive gains during the calendar year 2009, adding to the returns generated the last part of 2008. While the pension fund still must generate significant returns in future years to return to its pre-recession funded status, the MLRS fiduciaries are satisfied with the portfolio's recovery in 2009. Going forward, the MLRS fiduciaries will continue to recommend diversification, especially into strategies that can generate stock-like returns but with low correlations to the traditional stock and bond markets. They regularly examine the markets and the overall asset allocation structure to be certain the best asset allocation is in place.

In fiscal year 2009-10, despite the unfavorable backdrop of continued high unemployment, fears of a double-dip recession, concerns with the European sovereign debt crisis, and a housing market that appeared incapable of improving, the MLRS portfolio ended the fiscal year with strong gains. With the backdrop of a somewhat muted but positive recovery, the MLRS portfolio returned 10.9% on a net-of-fees basis over the fiscal year ended September 30, 2010. MLRS positive return compared favorably to its Balanced Index, which rose 10.3% during the same one-year period. Over the longer term (five-year period), MLRS generated a 4.1% net-of-fees total return, easily out pacing its Balanced Index, which generated 2.8% during the period under review.

The market saw many twists and turns during fiscal year 2009-10 and expects to see more during the remainder of the year and for years to come. In order to smooth the ride, MLRS seeks diversification for the portfolio by continuing to add uncorrelated strategies that provide true diversification, downside protection, and risk mitigation. Many of these strategies require sacrificing liquidity, but because of the long-term time horizon of the portfolio, the MLRS Board of Trustees believes it is acting prudently.

Going forward, it is believed that the U.S. will show good gross domestic product (GDP) growth, albeit less robust than originally hoped for. Although there are signs that the economy is recovering, there are many risks still present that could lead to a double dip recession or simply sluggish growth for the next several years. These factors include massive local, state, and national governmental debt, high interest rates, increased inflation, high unemployment, and lower housing prices.

Financial Questions or Requests

This financial report is designed to provide a general overview of MLRS's financial position. Requests for additional information or questions about this report should be addressed to: Michigan Legislative Retirement System, P.O. Box 30014, Lansing, MI 48909.

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FINANCIAL STATEMENTS

MICHIGAN LEGISLATIVE RETIREMENT SYSTEM
Statement of Pension Plan and Other Postemployment Benefits (OPEB) Plan Net Assets
As of September 30

	2010			2009		
	Pension Plan	OPEB Plan	Total	Pension Plan	OPEB Plan	Total
ASSETS						
Cash	$ 2,930,422	$ 321,758	$ 3,252,180	$ 3,265,639	$ 336,060	$ 3,601,699
Receivables:						
Employer	$ 226,588	$ 24,879	$ 251,467	$ 245,631	$ 25,277	$ 270,908
Interest and dividends	53,861	5,914	59,775	51,398	5,289	56,687
Sale of investments	215,340	23,644	238,984	728,605	74,979	803,584
Total receivables	$ 495,789	$ 54,437	$ 550,226	$ 1,025,634	$ 105,545	$ 1,131,179
Investments:						
Equities	$ 59,766,819	$ 6,562,348	$ 66,329,167	$ 59,445,668	$ 6,117,426	$ 65,563,094
Mutual funds	81,938,980	8,996,832	90,935,812	78,649,772	8,093,679	86,743,451
Alternative investments	135,526	14,881	150,407			
Total investments	$ 141,841,325	$ 15,574,061	$ 157,415,386	$ 138,095,440	$ 14,211,105	$ 152,306,545
Total assets	$ 145,267,536	$ 15,950,256	$ 161,217,792	$ 142,386,713	$ 14,652,710	$ 157,039,423
LIABILITIES						
Warrants outstanding	$ 22,823	$ 2,506	$ 25,329	$ 21,033	$ 2,165	$ 23,198
Accounts payable and other liabilities	563,502	61,872	625,374	611,839	62,963	674,802
Total liabilities	$ 586,325	$ 64,378	$ 650,703	$ 632,872	$ 65,128	$ 698,000
Net assets held in trust for pension and OPEB benefits	$ 144,681,211	$ 15,885,878	$ 160,567,089	$ 141,753,841	$ 14,587,582	$ 156,341,423

Schedules of funding progress are presented as required supplementary information.

The accompanying notes are an integral part of these financial statements.

MICHIGAN LEGISLATIVE RETIREMENT SYSTEM
Statement of Changes in Pension Plan and Other Postemployment Benefits (OPEB) Plan Net Assets
For Fiscal Years Ended September 30

	2010			2009		
	Pension Plan	OPEB Plan	Total	Pension Plan	OPEB Plan	Total
ADDITIONS						
Member contributions:						
Other member contributions	$ 11,044	$ 97,264	$ 108,308	$ 11,581	$ 103,589	$ 115,170
DC health premiums		56,103	56,103		41,215	41,215
Employer contributions		3,424,100	3,424,100		3,424,100	3,424,100
Other governmental contributions		150,113	150,113		160,758	160,758
Court fees		1,090,565	1,090,565	269,944	878,254	1,148,198
Total contributions	$ 11,044	$ 4,818,145	$ 4,829,189	$ 281,525	$ 4,607,916	$ 4,889,441
Investment income (loss):						
Net appreciation (depreciation) in fair value of investments	$ 13,693,358	$ 1,295,287	$ 14,988,645	$ 118,618	$ 9,859	$ 128,477
Interest, dividends and other	1,876,104	316,909	2,193,013	5,897,282	577,862	6,475,144
Total investment income (loss)	$ 15,569,462	$ 1,612,196	$ 17,181,658	$ 6,015,900	$ 587,721	$ 6,603,621
Less investment expenses	(537,869)	(55,351)	(593,220)	(451,219)	(46,434)	(497,653)
Net investment income (loss)	$ 15,031,593	$ 1,556,845	$ 16,588,438	$ 5,564,681	$ 541,287	$ 6,105,968
Miscellaneous income	$	$ 252,403	$ 252,403	$	$ 308,727	$ 308,727
Total additions	$ 15,042,637	$ 6,627,393	$ 21,670,030	$ 5,846,206	$ 5,457,930	$ 11,304,136
DEDUCTIONS						
Benefits and refunds paid to plan members and beneficiaries:						
Retirement benefits	$ 11,121,971	$	$ 11,121,971	$ 10,793,318	$	$ 10,793,318
Health benefits		4,866,041	4,866,041		4,760,057	4,760,057
Dental benefits		426,560	426,560		394,566	394,566
Death benefits	333,172		333,172	457,500		457,500
Refund of contribution and interest	17,506		17,506	14,638		14,638
Qualified rollover	287,969		287,969	93,823		93,823
Administrative expenses	354,649	36,496	391,145	335,644	34,540	370,184
Total deductions	$ 12,115,267	$ 5,329,097	$ 17,444,364	$ 11,694,923	$ 5,189,163	$ 16,884,086
Net increase (decrease)	$ 2,927,370	$ 1,298,296	$ 4,225,666	$ (5,848,717)	$ 268,767	$ (5,579,950)
Net assets held in trust for pension and OPEB benefits:						
Beginning of year	141,753,841	14,587,582	156,341,423	147,602,558	14,318,815	161,921,373
End of year	$ 144,681,211	$ 15,885,878	$ 160,567,089	$ 141,753,841	$ 14,587,582	$ 156,341,423

Schedules of funding progress are presented as required supplementary information.

The accompanying notes are an integral part of these financial statements.

Note 1 Plan Description

a. Organization

The Michigan Legislative Retirement System (MLRS) is a single employer, public employee, defined benefit retirement plan and postemployment healthcare plan governed by the State of Michigan. MLRS was created by Act 261, P.A. 1957, as amended, and provides retirement and ancillary benefits to eligible current and former State legislators. MLRS's pension plan was established by the State to provide retirement, survivor, and disability benefits to the Michigan Legislature, elected for the first time before March 31, 1997. In addition, MLRS's health plan provides to eligible vested members the option of receiving health, prescription, dental, and vision coverage under the Michigan Legislative Retirement Act.

MLRS operates within the legislative branch of State government. The MLRS Board of Trustees appoints the director who serves as executive secretary to the MLRS Board, with whom the general oversight of MLRS resides. Act 486, P.A. 1996, amended the MLRS enabling statute to mandate that persons elected to the Michigan Legislature after March 30, 1997 participate in a Statewide defined contribution retirement plan administered by the Department of Technology, Management, and Budget. Thus, the defined benefit retirement plan is a closed plan. The defined contribution retirement plan operates as a 401(k) plan and is part of the State of Michigan 401K Plan. The State of Michigan 401K Plan annual financial report is issued separately.

b. Membership

At September 30, 2010 and September 30, 2009, MLRS's membership consisted of the following:

	2010	2009
Retirees and beneficiaries currently receiving benefits:		
Regular benefits	223	224
Survivor benefits	65	64
Disability benefits	0	0
Total	288 *	288 *
Current members:		
Vested	14	14
Nonvested	0	0
Total	14	14
Inactive members entitled to benefits and not yet receiving them	28	33
Total members	330	335

* Includes 11 domestic relations orders* alternate payees for 2010 and 2009.

MLRS provides other postemployment benefits (OPEB) which include health, dental, and life insurance benefits. The number of plan participants at September 30, 2010 and September 30, 2009 was as follows:

	2010	2009
Health and Dental Plans:		
Eligible participants	373 **	370 **
Participants receiving benefits	348 **	353 **
Life Insurance Plan:		
Participants receiving benefits	293	298

** Includes 57 defined contribution (DC) plan participants for 2010 and 50 DC plan participants for 2009 who are receiving healthcare insurance through MLRS in accordance with State statute. There were 15 DC plan participants in 2010 and 14 DC plan participants in 2009 who were eligible for healthcare insurance and declined to receive the benefits.

c. Benefit Provisions

(1) Introduction:

Act 261, P.A. 1957, as amended (the Michigan Legislative Retirement System Act), establishes eligibility and benefit provisions for this defined benefit retirement plan.

Michigan's constitutional term-limit amendment limits members of the House of Representatives to six years in office and members of the Senate to eight years in office. Effective March 31, 1997, Act 486, P.A. 1996, closed MLRS to new legislators. The Act provides certain re-elected former legislators the option to rejoin MLRS. All legislators who first take office after March 1997 are automatically enrolled in the State's defined contribution retirement plan.

Benefit provisions of the postemployment healthcare (OPEB) plan are established by State statute, which may be amended. Act 261, P.A. 1957, as amended, establishes eligibility and benefit provisions for the health plan. Eligible members may receive health, prescription, dental, and vision benefits.

(2) Regular Retirement:

A member may retire and receive retirement benefits based on age and service after: (1) attaining age 50, if age and years of credited service combined are equal to or greater than 70; or (2) attaining age 55 with 5 or more years of credited service if elected, qualified, and seated not less than (a) 3 full or partial terms in the House of Representatives, (b) 2 full or partial terms in the Senate, or (c) 1 term in the House of Representatives and 1 term in the Senate.

A member's retirement benefit is computed using a benefit formula prescribed by the enabling statute and described in the next two paragraphs. The benefit is paid on a monthly basis.

For those legislators who first became members on or before January 1, 1995, the retirement benefit is calculated by multiplying

20% of the highest salary earned for the first 5 years of service, plus 4% of the highest salary for each of the next 11 years of service, plus 1% of the highest salary for each additional year.

For those legislators who first became members after January 1, 1995, the retirement benefit is calculated by multiplying 3% of the highest salary for each year of service.

(3) Post Retirement Benefit Adjustment:
For those legislators who first became members on or before January 1, 1995, the annual retirement benefit payable to a retiree and/or his/her survivor is increased by 4% compounded annually. The adjustment is effective each January.

For those legislators who first became members after January 1, 1995, the annual retirement benefit payable to a retiree and/or his/her survivor is increased by 4%, but it is not compounded annually. The adjustment is effective each January.

(4) Other Postemployment Benefits (OPEB):
Under Sections 50a and 50b of the Michigan Legislative Retirement System Act, all retirees and their dependents and survivors receive health and dental insurance coverage. MLRS also provides health and dental insurance coverage for deferred vested members* who were members on or before January 1, 1995 and for their survivors and dependents. In addition, in accordance with State law, MLRS provides health insurance coverage to eligible former legislators (and their dependents) who meet certain vesting requirements established by statute and who belong to the State's defined contribution retirement plan. Member enrollment in the MLRS health plan is voluntary. MLRS pays for health and dental benefits on a modified pay-as-you-go basis*; however, the State has begun to advance funds for future MLRS health insurance costs.

** See glossary at end of report for definition.*

MLRS provides $150,000 in life insurance coverage to active members. Deferred vested members are covered by varying amounts of life insurance, ranging from $5,000 to $150,000, depending on the member's date of deferral and, in some instances, the payment of an annual premium. Retirees are covered by varying amounts of life insurance, ranging from $2,500 to $75,000, depending on their retirement dates and, in some instances, the payment of an annual premium. MLRS prefunds life insurance benefits using the entry age actuarial cost method*. The life insurance plan and the pension plan use the actuarial assumptions stated in Note 4.

(5) Disability Benefit:
A member or deferred vested member who becomes disabled as determined by at least two licensed physicians appointed by the MLRS Board of Trustees is eligible for a disability benefit computed in the same manner described under "Regular Retirement."

(6) Survivor Benefit:
Upon the death of a vested member or deferred vested member who meets the service but not the age requirement for regular retirement (see "Regular Retirement"), or upon the death of a retiree, a surviving spouse shall be entitled to a benefit equal to 66.67% of the benefit the member would have received or was receiving at the time of death. Special provisions apply to surviving minor children and surviving spouses with minor children.

(7) Refunds:
A member who leaves legislative service may request a refund of his/her contributions from the Members' Savings Fund. A member who receives a refund of contributions forfeits all rights to any future MLRS benefits. Members who return to legislative service and who previously received a refund of their contributions may reinstate their service through repayment of the refund plus interest in accordance with the statute.

** See glossary at end of report for definition.*

Note 2 Summary of Significant Accounting Policies

a. Measurement Focus, Basis of Accounting, and Presentation

The MLRS financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting, as provided by accounting principles generally accepted in the United States of America. Contributions are recognized as revenue in the period in which service is provided, and expenses are recorded when incurred regardless of when payment is made. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

b. Contributions and Reserves

The Michigan Legislative Retirement System Act provides for several reserves or funds. These funds and the contributions and other monies allocated to them are described below:

(1) Members' Savings Fund (MSF) - Members who first became members on or before January 1, 1995, with less than 20 years of service, contributed approximately 7% of salary to MSF. Members who first became members after January 1, 1995 contributed 5% of salary to MSF. Beginning January 1, 1999, there were no member contributions allocated to MSF except for approximately 4% of salary for the period beginning on January 1, 1999 and ending on December 31, 2000, for members who first became members after December 1, 1994 and on or before January 1, 1995 in accordance with legislation. Eligible members may make other contributions to MSF to purchase special service credit or to repay previously refunded contributions. MSF represents active member contributions (and interest credited from the Income Fund) less amounts transferred to reserves for retirement and amounts refunded to terminated members. At September 30, 2010 and September 30, 2009, the balance in this account was $1.3 million and $1.5 million, respectively.

(2) Members' Retirement Fund (MRF) - MRF represents the reserves for payment of retirement benefits. At retirement, a member's accumulated contributions (with interest) are transferred to MRF (from MSF). Interest is credited to MRF (from the Income Fund) and monthly allowances are debited. At each fiscal year-end, an actuarial valuation determines the 100% funding requirements for MRF. Any amounts required to 100% fund MRF are transferred in the next fiscal year. At September 30, 2010 and September 30, 2009, the balance in this account was $73.4 million and $75.0 million, respectively.

(3) Survivors' Retirement Fund (SRF) - On and before January 1, 1999, all members with less than 20 years of service contributed 0.5% of salary to SRF. After January 1, 1999, there were no member contributions allocated to SRF. Interest is credited annually to SRF (from the Income Fund), member savings are transferred to SRF from MSF upon the death of a vested member, and additional State contributions may be made in order to make SRF 100% funded. Survivors' monthly retirement allowances are paid from SRF upon the death of vested members, deferred vested members, and retirants. At September 30, 2010 and September 30, 2009, the balance in this account was $52.6 million and $49.2 million, respectively.

(4) Insurance Revolving Fund (IRF) - On and before January 1, 1999, all members contributed 0.5% of salary to IRF. After January 1, 1999, there were no member contributions allocated to IRF. State contributions, if any, member premiums, and interest from the Income Fund are credited to IRF. Life insurance benefits are paid from IRF to beneficiaries of members, retirants, and deferred vested members. At September 30, 2010 and September 30, 2009, the balance in this account was $17.4 million and $16.1 million, respectively.

(5) Health Insurance Fund (HIF) - On and before January 1, 1999, all members contributed 1% of salary to HIF. After January 1, 1999, member contributions are made as follows: (1) members who first became members on or before January 1, 1995 contribute 9% to HIF; (2) members who first became members after January 1, 1995

contribute 7% to HIF. HIF is also credited with employer contributions, court fees, other governmental contributions, and interest income. Funds from this reserve are used to pay healthcare expenses and are accumulated to fully fund the future health insurance liabilities for MLRS. At September 30, 2010 and September 30, 2009, the balance in this account was $15.9 million and $14.6 million, respectively.

(6) Income Fund (IF) - IF is credited with all investment earnings and other miscellaneous income. Interest transfers are made annually to the other reserves, based on beginning balance. IF also accounts for investment and administrative expenses and interest on refunds and transfers.

c. Fair Value of Investments

Plan investments are presented at fair value. Securities traded on a national exchange are valued at the last reported sales price at current exchange rates. Corporate bonds not traded on a national or international exchange are based on equivalent values of comparable securities with similar yield and risk. Other investments that do not have an established market are recorded at estimated fair value. Short-term investments are carried at cost, which approximates fair value.

d. Reporting Entity

MLRS has pension and other employee benefit trust funds. MLRS is considered part of the State and is included in the *State of Michigan Comprehensive Annual Financial Report.* MLRS and the MLRS Board of Trustees are not financially accountable for any other entities. Accordingly, MLRS is the only entity included in this financial report.

e. Investment Income

Dividend income is recognized on the ex-dividend date, and interest income is recognized on the accrual basis as earned. Fair value changes are recorded as investment income or loss. Purchases and sales of investments are recorded as of the trade date.

f. Related Party Transactions

The cash account included $3,252,180 and $3,601,699 on September 30, 2010 and September 30, 2009, respectively, which represents funds deposited in a common cash investment pool maintained for various State operating funds. The participating funds in the common cash pool earn interest at various rates depending upon prevailing short-term interest rates. Earnings from these activities amounted to $6,844 and $33,851 for the fiscal years ended September 30, 2010 and September 30, 2009, respectively.

g. Fixed Assets

MLRS does not own any fixed assets. Equipment expenses are immaterial in amount and are expensed annually.

h. Excess Benefits

Section 415 of the Internal Revenue Code requires that, for individuals who receive retirement benefits in excess of established limits, these benefits are recorded and reported outside of the pension fund in order to keep the qualified status of the plan. This includes coordination of benefits issued where a retiree participates in more than one qualified plan. MLRS provided excess benefits to three retirees, for a total amount of $47,082 as of September 30, 2010 and $38,046 as of September 30, 2009.

Note 3 Contributions

a. Member Contributions

On or before January 1, 1999, the following contributions were made by members of MLRS:

Members who first became members on or before January 1, 1995 contributed 9% of their salaries to MLRS. The contributions were placed in the following reserves created by the enabling statute: 7% to MSF for the first 20 years of service; 0.5% to IRF; 0.5% to SRF for the first 20 years of service; and 1% to HIF.

Members who first became members on or after January 1, 1995 contributed 7% of their salaries to MLRS. The contributions were placed in the following reserves created by the enabling statute: 5% to MSF; 0.5% to IRF; 0.5% to SRF; and 1% to HIF.

After January 1, 1999, the following contributions are made by the members of MLRS:

Members who first became members on or before December 1, 1994 contribute 9% of their salaries to MLRS. The contributions are placed in accordance with the enabling statute to HIF.

Members who first became members after December 1, 1994 and on or before January 1, 1995 contributed 13% of their salaries to MLRS. The contributions were placed in the following reserves in accordance with the enabling statute: 9% to HIF and 4% to MSF beginning on January 1, 1999 and ending on December 31, 2000. After December 31, 2000, these members contribute 9% of their salaries to MLRS. The contributions are placed in HIF in accordance with the enabling statute: 9% to HIF.

Members who first became members after January 1, 1995, contribute 7% of their salaries to MLRS. The contributions are placed in HIF in accordance with the enabling statute: 7% to HIF.

Member contributions are tax-deferred through the provisions of Section 414(h)(2) of the Internal Revenue Code.

b. <u>State Contributions</u>

State contributions are made on the basis of actuarial requirements as determined by the MLRS actuary and approved by the MLRS Board of Trustees. Through the annual State budgetary process, the Legislature annually appropriates, and the Governor approves, the State contributions along with certain court fee revenues, which are paid to MLRS pursuant to State statute. A chart showing State contributions is presented as required supplementary information.

Note 4 Funded Status

a. Pension Plan

State contributions are determined based on a statutorily required annual actuarial valuation. The annual required employer contribution and the actual contribution for the pension plan were $774,898 and $0, respectively, for fiscal year 2009-10 and $269,944 and $269,944, respectively, for fiscal year 2008-09.

As of September 30, 2010, the actuarial value of assets* and actuarial accrued liability* (AAL) of the plan were $159.0 million and $172.7 million, respectively, resulting in a funded ratio of 92.0%. As of September 30, 2009, the amounts were $165.8 million and $171.4 million, respectively, resulting in a funded ratio of 96.7%. A historical perspective of funding levels for MLRS is presented in the required supplementary information section of this report.

b. Postemployment Health (OPEB) Plan

Legislation does not appropriate State contributions for prefunding OPEB costs. The required employer contribution for OPEB was $10.8 million and $8.0 million for fiscal years 2009-10 and 2008-09, respectively, while the actual contributions were $4.5 million and $4.3 million.

As of September 30, 2010, the actuarial value of the assets and AAL of the fund were $15.9 million and $155.3 million, respectively, resulting in an UAAL of $139.4 million and a funded ratio of 10.2%. As of September 30, 2009, the actuarial value of the assets and AAL were $14.6 million and $136.9 million, respectively, resulting in a UAAL of $122.3 million and a funded ratio of 10.7%. The covered payroll (annual payroll of active members covered by the plan) was $11.6 million and the ratio of UAAL to covered payroll was 1,201.7% as of September 30, 2010. The covered payroll was $11.7 million and the ratio of UAAL to covered payroll was 1,043.6% as of September 30, 2009.

** See glossary at end of report for definition.*

c. Actuarial Valuations and Assumptions

Actuarial valuations for both the pension and OPEB plans involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. Examples include assumptions about future employment, mortality, and trends. The actuarial methods and assumptions used are designed to reduce the effects of short-term volatility. The schedules of funding progress, presented as required supplementary information following the notes to the financial statements, present multi-year trend information about whether the actuarial value of plan assets for both pension and OPEB plans is increasing or decreasing over time relative to the AAL for benefits.

Calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation and on the historical pattern of sharing of costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

Pension Plan

Valuation Date	September 30, 2010
Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Dollar
Amortization Period	10 years open
Asset Valuation Method	5-Year Smoothed Market
Actuarial Assumptions:	
Investment Rate of Return	7.0%
Projected Salary Increases	4.0%
Cost-of-Living Adjustments	4.0% Annual compounded (non-compounded for legislators who first became members after January 1, 1995)

OPEB Plan

Valuation Date	September 30, 2010
Actuarial Cost Method	Project Unit Credit
Amortization Method	Level Percent Open
Amortization Period	30 Year Open
Asset Valuation Method	Market Value
Actuarial Assumptions:	
Discount Rate	4.5% Per Year
Projected Salary Increases	4.0%
Valuation Healthcare Cost Trend Rate	8.75% in 2011, grading to 4.0% in 2020

Note 5 Deposits and Investments

Investment Authority

All investments made are subject to approval by the MLRS Board of Trustees, which has investment authority under the Michigan Legislative Retirement System Act. Investments made are subject to statutory regulations imposed under the Public Employee Retirement System Investment Act (Act 314, P.A. 1965, as amended). The Act authorizes, with certain restrictions, the investment of pension fund assets in stocks, corporate and governmental bonds and notes, mortgages, real estate, and certain short-term and alternative investments. MLRS also contracts with independent investment advisors.

a. Derivatives and Securities Lending

State investment statutes limit total derivative exposure to 15% of a fund's total asset value, and restricts uses to replication of returns and hedging of assets. MLRS Investment Policy Statement (IPS) has a target asset allocation of 5% for hedge funds, which may include derivatives. MLRS's investment in hedge funds has an exposure to derivatives of approximately 15-20%. The hedge funds use these instruments as part of their overall investment strategies and also utilize derivatives for hedging and portfolio protection purposes. As of September 30, 2010 and

September 30, 2009, total investments in hedge funds were 4.9% and 0%, respectively. The market value of the hedge funds at September 30, 2010 was $7,950,407.

The MLRS did not participate in any securities lending activities.

b. Deposit and Investment Risk

In accordance with Governmental Accounting Standards Board* (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures (an amendment to GASB Statement No. 3),* deposits and investments require certain disclosure regarding policies and the risks associated with them. The custodial credit risk, credit risk, interest rate risk, and foreign currency risk are discussed in the following paragraphs:

(1) Custodial credit risk associated with common cash deposits:

The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, MLRS deposits may not be recovered. Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are: (a) uncollateralized, (b) collateralized with securities held by the pledging financial institution, or (c) collateralized with securities held by the pledging financial institution's trust department or agent but not in the depositor-government's name. At September 30, 2010 and September 30, 2009, all MLRS common cash deposits were covered by depository insurance or collateralized with securities held by the State's agent in the State's name.

To lessen the custodial credit risk associated with common cash deposits, the State Treasurer's policy requires all financial institutions holding the State's money to pledge collateral equal to the amount of the account balance for all demand and time deposits to secure the State funds. A bank, savings and loan association, or credit union holding State funds must be organized under the law of Michigan or federal law and maintain a principal office or branch office in the State of Michigan. No deposit in any financial organization may be in excess of 50% of the net worth of the organization.

(2) Foreign currency risk associated with common cash deposits:

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of deposits. Act 35, P.A. 1997, requires State deposits be held in a financial institution that maintains a principal office or branch office located in the State of Michigan. MLRS had no common cash deposits subject to foreign currency risk at September 30, 2010 or September 30, 2009.

(3) Custodial credit risk associated with investments:

The custodial credit risk for investments is the risk that, in the event of a failure of the counterparty, MLRS will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government, and are held by either: (a) the counterparty or (b) the counterparty's trust department or agent but are not in the government's name. The State Treasurer does not have an investment policy for managing custodial credit risk. At September 30, 2010 or September 30, 2009, MLRS investments were not exposed to custodial credit risk as they were all registered in MLRS's name.

(4) Credit risk for investments:

Credit risk is the risk that an issuer will not fulfill its obligations. MLRS has a policy to maintain an overall weighted average of "Aa" or better by Moody's Investors Service* "AA" or better by Standards & Poor's. GASB Statement No. 40 states that governments should disclose the credit quality ratings of external investment pools, money market funds, bond mutual funds, and other pooled investments of fixed

** See glossary at end of report for definition.*

income securities in which they invest. The following investments are subject to credit risk:

Debt Securities
As of September 30

	2010			2009		
		Rating			Rating	
Investment Type	Fair Value	Standard & Poor's	Moody's Investors Service	Fair Value	Standard & Poor's	Moody's Investors Service
Mutual funds*	$28,486,964	AA	Aa	$23,149,841	AA	Aa
				8,128,252	BB	Ba
	$28,486,964			$31,278,093		

* Average Quality Rating

(5) Concentration of credit risk:
Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer.

MLRS is prohibited by Act 314, P.A. 1965, as amended, from investing in more than 5% of the outstanding stock or obligations of any one issuer or investing more than 5% of its assets in the stock or obligations of any one issuer.

As of September 30, 2010 and September 30, 2009, there were no investments in any one issuer that accounted for more than 5% of MLRS's assets nor were there any investments totaling more than 5% of the stock or obligations of any one issuer.

(6) Interest rate risk associated with investments:
Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of those investments. MLRS has a 25.0% target allocation of fixed income securities, which is affected by interest rates because these securities are a debt investment. As of September 30, 2010 and September 30, 2009, the

fair value was $28,486,964 and $31,278,093, respectively, with the investment activity for the year producing a total rate of return of 10.9% and 15.9% and a rate of return since inception of 8.9% and 6.5%. The projected duration is 4.7 and 3.5 years, respectively. MLRS does not have a policy for controlling interest rate risk.

(7) Foreign currency risk associated with investments:
Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of investments. MLRS invests in various foreign investments (including, but not limited to, equities, fixed income, and mutual funds), which are subject to various limitations in accordance with the MLRS Investment Policy Statement (which incorporates the provision of the Public Employee Retirement System Investment Act, Act 314, P.A. 1965, as amended). Foreign investment restrictions per this policy include a 20% limitation on the total assets of MLRS and, additionally, a 5% limitation on the outstanding foreign securities of a single issuer (allowances are made for the daily market pricing fluctuations of an investment). New investments in countries that have been identified by the U.S. Department of State as engaging in or sponsoring terrorism are prohibited, and existing investments in any such newly-identified country shall be quickly divested in accordance with the Act.

As of September 30, 2010 and September 30, 2009, MLRS held the following investments subject to foreign currency risk:

Foreign Currency Risk

		Value in U.S. Dollars As of September 30							
		2010					2009		
Country	Currency	Alternative Investments	Mutual Funds	Equities	International Equities	Total	Mutual Funds	International Equities	Total
Americas									
Brazil	Real	$	$	$	$ 231,838	$ 231,838	$	$ 330,249	$ 330,249
Canada	Dollar			627,666		627,666			
Europe									
European Union	Euro			673,793	650,192	1,323,985		1,023,589	1,023,589
Switzerland	Franc			121,424		121,424		189,779	189,779
Netherlands Antilles	Guilder (Florin)			382,598		382,598			
United Kingdom	Sterling				556,371	556,371		342,142	342,142
Pacific/Asia									
Australia	Dollar				196,906	196,906		220,473	220,473
Singapore	Dollar			213,006		213,006			
Middle East									
Israel	Shekel				154,558	154,558		257,856	257,856
Mutual Funds									
Various		7,950,407	41,314,165			49,264,572	42,991,934		42,991,934
Total		$7,950,407	$41,314,165	$2,018,487	$1,789,865	$53,072,924	$42,991,934	$2,364,088	$45,356,022

Note 6 Accounting Change

During fiscal year 2009-10, MLRS implemented GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This Statement addresses the recognition, measurement, and disclosure of information regarding derivative instruments. Note 5 includes disclosure regarding derivative investments of MLRS.

REQUIRED SUPPLEMENTARY INFORMATION

Schedules of Funding Progress

Each time a higher level of benefit is adopted, unfunded obligations are created. The law governing the Michigan Legislative Retirement System (MLRS) requires that these additional obligations be financed systematically over a period of future years.

Analysis of the dollar amounts of actuarial value of assets, actuarial accrued liability, or unfunded actuarial accrued liability in isolation can be misleading. Expressing the actuarial value of assets as a percentage of the actuarial accrued liability provides one indication of the MLRS funding status on a going-concern basis. Analysis of this percentage over time indicates whether the system is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the system. Trends in unfunded actuarial accrued liability and annual covered payroll are both affected by inflation. Expressing the unfunded actuarial accrued liability as a percentage of annual covered payroll approximately adjusts for the effects of inflation and aids analysis of MLRS progress in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the system.

Schedules of Employer and Other Contributions

Pension Benefits
(In Thousands)

Valuation Date September 30	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded (Overfunded) Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio AAL (a/b)	Covered Payroll (1) (c)	UAAL as a Percentage of Covered Payroll (2) ((b-a)/c)
2001	$168,399	$138,621	$(29,778)	121.5%	$4,284	N/A
2002	167,158	143,858	(23,300)	116.2%	4,331	N/A
2003	164,950	147,431	(17,519)	111.9%	2,016	N/A
2004	161,905	151,938	(9,967)	106.6%	2,016	N/A
2005	157,456	154,650	(2,806)	101.8%	2,016	N/A
2006	159,347	158,407	(940)	100.6%	2,016	N/A
2007	167,750	163,313	(4,437)	102.7%	1,332	N/A
2008	169,986	169,396	(590)	100.3%	1,332	N/A
2009	165,810	171,441	5,631	96.7%	1,151	N/A
2010	158,952	172,694	13,741	92.0%	1,173	N/A

(1) October based payrolls.

(2) Because the MLRS plan is a closed plan, the UAAL as a percentage of covered payroll is not applicable (N/A).

Other Postemployment Benefits (1)
(In Thousands)

Valuation Date September 30	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded (Overfunded) Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio AAL (a/b)	Covered Payroll (2) (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2005	$11,929	$111,393	$ 99,464	10.7%	$11,875	837.6%
2008	14,319	132,628	118,309	10.8%	11,859	997.6%
2009	14,588	136,870	122,282	10.7%	11,718	1,043.6%
2010	15,886	155,259	139,373	10.2%	11,598	1,201.7%

(1) Includes members in both the defined benefit plan and the defined contribution plan.

(2) October based payrolls.

Pension Benefits

Fiscal Year Ended September 30	Valuation Date September 30	Annual Required Contribution (ARC)	Actual Contributions	Percent Contributed (1)
2001	2000	$ 0	$ 0	N/A
2002	2001	0	0	N/A
2003	2002	0	0	N/A
2004	2003	0	0	N/A
2005	2004	0	0	N/A
2006	2005	0	0	N/A
2007	2006	394,957	394,957	100.0%
2008	2007	0	0	N/A
2009	2008	269,944	269,944	100.0%
2010	2009	774,898	0	0.0%

Other Postemployment Benefits (2)

Fiscal Year Ended September 30	Valuation Date September 30	Annual Required Contribution (ARC)	Actual Contributions	Other Governmental Contributions	Percent Contributed
2008	2005	$ 7,965,791	$4,643,427	$153,982	60.2%
2009	2005	7,978,764	4,302,354	160,758	55.9%
2010	2009	10,842,010	4,514,665	150,113	43.0%

(1) N/A indicates no annual required contributions.

(2) Includes members in both the defined benefit plan and the defined contribution plan.

Note A Description

Ten-year historical trend information designed to provide information about the Michigan Legislative Retirement System's (MLRS's) progress in accumulating sufficient assets to pay benefits when due is presented in the preceding schedules. This information is presented to enable the interested parties to assess the progress made by MLRS in accumulating sufficient assets to pay pension and other postemployment benefits as they become due. Because this is the second two-year period that MLRS is reporting other postemployment benefits in accordance with GASB Statement No. 43, only four years of historical trend information is provided.

The comparability of trend information is affected by changes in actuarial assumptions, benefit provisions, actuarial funding methods, accounting policies, and other changes. Those changes usually affect trends in contribution requirements and in ratios that use the pension benefit obligation as a factor.

The schedules of funding progress and the schedules of employer and other contributions are reported as historical trend information. The schedules of funding progress are presented to measure the progress being made to accumulate sufficient assets to pay benefits when due. The schedules of employer and other contributions are presented to show the responsibility of the State in meeting the actuarial requirements to maintain MLRS on a sound financial basis.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL AND COMPLIANCE

STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
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(517) 334-8050
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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

Independent Auditor's Report on Internal Control Over
Financial Reporting and on Compliance and Other Matters

The Honorable R. Robert Geake, Chair
Board of Trustees
and
Ms. Christine I. Hammond, Director
Michigan Legislative Retirement System
Cora Anderson Building
Lansing, Michigan

Dear Mr. Geake and Ms. Hammond:

We have audited the financial statements of the Michigan Legislative Retirement System as of and for the fiscal years ended September 30, 2010 and September 30, 2009, which collectively comprise the System's basic financial statements as identified in the table of contents, and have issued our report thereon dated September 15, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting
In planning and performing our audit, we considered the Michigan Legislative Retirement System'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 System's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the System's internal control over financial reporting.

A deficiency in internal control 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 and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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 in the preceding paragraph. However, we identified a deficiency in internal control over financial reporting, as described in Finding 1, that we consider to be a significant deficiency in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The System's preliminary response to the finding identified in our audit is included in the body of the report. We did not audit the System's preliminary response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Michigan Legislative Retirement System Board of Trustees, the Michigan Legislative Retirement System management, and the Legislature and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Michigan Auditor General

AUDITOR GENERAL

September 15, 2011

FINDING, RECOMMENDATION, AND AGENCY PRELIMINARY RESPONSE

FINDING

1. Controls Over Financial Reporting

   The Michigan Legislative Retirement System's (MLRS's) controls over financial reporting did not ensure the accuracy of the investment classifications on MLRS's statement of pension plan and other postemployment benefits (OPEB) plan net assets. As a result, mutual funds were overstated and alternative investments were understated by $7.8 million as of September 30, 2010 in the MLRS financial statements and *State of Michigan Comprehensive Annual Financial Report*. In addition, the amount of equities reported to the Office of Financial Management for inclusion in the *State of Michigan Comprehensive Annual Financial Report* was not properly classified between domestic and international equities and was reported as all domestic equities.

   In fiscal year 2009-10, MLRS invested in hedge funds, which use derivative instruments for hedging and portfolio protection as part of its overall investment strategy. These hedge funds were properly classified as alternative investments in the State's accounting system. However, MLRS's controls over financial reporting did not ensure that its statement preparation process properly accounted for the initial investment of $7.8 million as an alternative investment. As a result, the hedge funds of $7.8 million are reflected as mutual funds on MLRS's statement of pension plan and OPEB plan net assets as of September 30, 2010.

   MLRS invests in both domestic and international equities as part of its investment portfolio. We noted that MLRS reported to the Office of Financial Management the entire amount of equities held in its portfolio as domestic equities. However, we determined that $1.8 million of the $66.3 million of equities in fiscal year 2009-10 and $2.4 million of the $65.6 million of equities in fiscal year 2008-09 were international equities held by the investment portfolio.

RECOMMENDATION

We recommend that MLRS implement sufficient controls over financial reporting to ensure the accuracy of the investment classifications on MLRS's statement of pension plan and OPEB plan net assets.

AGENCY PRELIMINARY RESPONSE

MLRS agrees with the recommendation and informed us that it will implement steps to make certain that there are proper controls over financial reporting to ensure the accuracy of the investment classifications on MLRS's statement of pension plan and OPEB plan net assets. These steps will include, but are not limited to, communicating more effectively with the MLRS custodian on the investment classifications that it uses for accounting purposes and comparing them to classifications accepted by the Governmental Accounting Standards Board (GASB).

GLOSSARY

actuarial accrued liability (AAL)	The difference between the actuarial present value of pension plan benefits and the actuarial present value of future normal costs; also referred to as "past service liability."
actuarial value of assets	The value placed at any particular date on the assets and liabilities of a retirement fund by the actuary responsible for the valuation of the assets and liabilities.
benefits	Payments to which participants may be entitled under the pension plan, including pension benefits, death benefits, and benefits due on termination of office.
DC	defined contribution.
deferred vested member	A member who leaves office and meets the service requirement but not the age requirement or a member who defers receipt of a retirement allowance until a future date.
deficiency in internal control over financial reporting	The design or operation of a control that does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.
domestic relations order	A judgment, decree, or order of the court made pursuant to the domestic relations law of the State and relating to the provision of alimony payments, child support, or marital property rights to a spouse of a participant under a judgment of separate maintenance or to a former spouse, child, or dependent of a participant.
entry age actuarial cost method	A method under which the actuarial present value of the projected benefits of each individual included in an actuarial

	valuation is allocated on a level basis over the earnings or services of the individual between entry age and assumed exit age.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules and/or financial statements of an audited entity are presented fairly in all material respects in conformity with the disclosed basis of accounting.
Governmental Accounting Standards Board (GASB)	An arm of the Financial Accounting Foundation established to promulgate standards of financial accounting and reporting with respect to activities and transactions of state and local governmental entities.
HIF	Health Insurance Fund.
IF	Income Fund.
internal control	A process, effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance about the achievement of the entity's objectives with regard to the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
IRF	Insurance Revolving Fund.
material misstatement	A misstatement in the financial schedules and/or financial statements that causes the schedules and/or statements to not present fairly the financial position or the changes in financial position or cash flows in conformity with the disclosed basis of accounting.

material weakness in internal control over financial reporting	A deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial schedules and/or financial statements will not be prevented, or detected and corrected, on a timely basis.
member	A person elected to the Michigan House of Representatives or the Michigan Senate.
MLRS	Michigan Legislative Retirement System.
Moody's Investors Service	A credit rating agency that, among other things, provides credit ratings for issuers of certain debt obligations or debt instruments.
MRF	Members' Retirement Fund.
MSF	Members' Savings Fund.
OPEB	other postemployment benefits.
pay-as-you-go basis	A method of financing a pension plan under which the contributions to the plan are generally made at about the same time and in about the same amount as benefit payments and expenses becoming due.
significant deficiency in internal control over financial reporting	A deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.
S&P	Standard & Poor's. A credit rating agency that, among other things, provides credit ratings for issuers of certain debt obligations or debt instruments.
SRF	Survivors' Retirement Fund.

unfunded actuarial accrued liability (UAAL)	The difference between the actuarial accrued liability and the actuarial value of assets.
unqualified opinion	An auditor's opinion in which the auditor states that the financial schedules and/or financial statements presenting the basic financial information of the audited agency are fairly presented in conformity with the disclosed basis of accounting.

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