

Michigan Military Retirement System

A Pension Trust Fund of the State of Michigan

Comprehensive Annual Financial Report for Nine Months Ending September 30, 2016



MMRS

Prepared by:
Financial Services
for
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TABLE OF CONTENTS

INTRODUCTORY SECTION	3
Administrative Organization	4
Retirement Board Members	4
Advisors and Consultants.....	4
Organization Chart	5
FINANCIAL SECTION	7
Independent Auditor's Report.....	8
Management's Discussion and Analysis	10
Basic Financial Statements	13
<i>Statement of Pension Plan Fiduciary Net Position</i>	13
<i>Statement of Changes in Pension Plan Fiduciary Net Position</i>	14
Notes To Basic Financial Statements.....	15
Required Supplementary Information.....	23
Schedule of Changes in Net Pension Liability	23
Schedule Of Net Pension Liability	24
Schedules of Contributions	24
Notes to Required Supplementary Information	25
Supporting Schedules	26
Summary Schedule of Pension Plan Administrative and Other Expenses.....	26
Schedule of Payments for Professional Services.....	26
Detail of Changes in Plan Fiduciary Net Position	27
ACKNOWLEDGMENTS	28

INTRODUCTORY SECTION

Retirement Board Members
Advisors and Consultants
Organization Chart

INTRODUCTORY SECTION

Administrative Organization

RETIREMENT BOARD MEMBERS*

Judge Mark T. Boonstra
General Public
Term Expires Dec. 31, 2019

Anne Marie Storberg
Ex-officio Member Representing
State Treasurer

Matthew Fedorchuk
Active State Employee
Term Expires Dec. 31, 2016

John Gnodke
Ex-officio Member Representing
State Personnel Director

Laurie Hill, Chair
Retired State Employee
Term Expires Dec. 31, 2019

Molly Jason
Ex-officio Member Representing
Attorney General

Craig Murray
Ex-officio Member Representing
Auditor General

Judge David H. Sawyer
Active Judge
Term Expires Dec. 31, 2017

Lt. John Wojcki
Michigan National Guard
Term Expires Dec. 31, 2018

*Statute provides that board members may continue to serve after their term expires until they are replaced or reappointed.

ADVISORS AND CONSULTANTS

Actuaries

Gabriel Roeder Smith & Co.
Mita D. Drazilov
Southfield, Michigan

Independent Auditors

Doug A. Ringler, C.P.A., C.I.A.
Auditor General
State of Michigan

Investment Manager and Custodian

Nick A. Khouri
State Treasurer
State of Michigan

Legal Advisor

Bill Schuette
Attorney General
State of Michigan

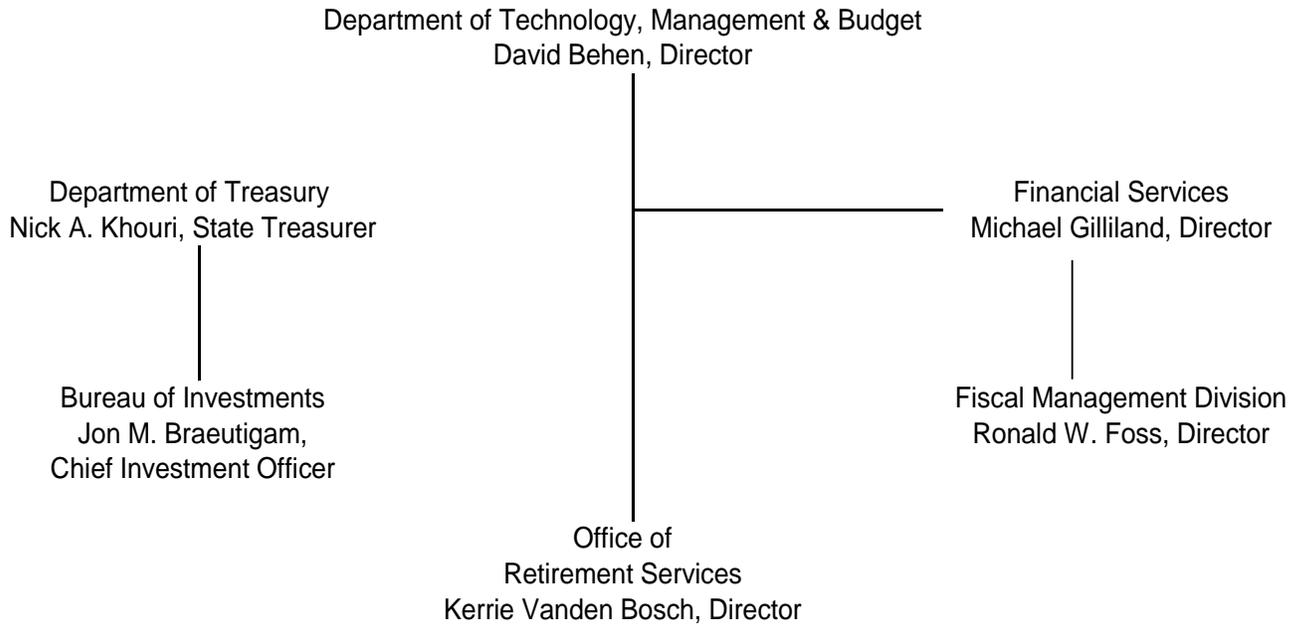
Investment Performance Measurement

State Street Corporation
State Street Investment Analytics
Boston, MA

INTRODUCTORY SECTION

Administrative Organization (continued)

Organization Chart



INTRODUCTORY SECTION

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FINANCIAL SECTION

Independent Auditor's Report
Management's Discussion and Analysis
Basic Financial Statements
Notes to Basic Financial Statements
Required Supplementary Information
Note to Required Supplementary Information
Supporting Schedules



OAG

Office of the Auditor General

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Doug A. Ringler, CPA, CIA
Auditor General

Independent Auditor's Report on the Financial Statements
and Other Reporting Required by *Government Auditing Standards*

Ms. Laurie Hill, Chair
State of Michigan Retirement Board
and
Mr. David B. Behen, Director
Department of Technology, Management, and Budget
and
Ms. Kerrie L. Vanden Bosch, Director
Office of Retirement Services

Dear Ms. Hill, Mr. Behen, and Ms. Vanden Bosch:

Report on the Financial Statements

We have audited the accompanying financial statements of the Michigan Military Retirement System as of and for the nine months ending September 30, 2016 and the related notes to the financial statements, which collectively comprise the System's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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 from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the fiduciary net position of the Michigan Military Retirement System as of September 30, 2016 and the changes in fiduciary net position for the nine months ending September 30, 2016 in accordance with accounting principles generally accepted in the United States of America.



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Office of the Auditor General

Doug A. Ringler, CPA, CIA
Auditor General

Ms. Laurie Hill, Chair
Mr. David B. Behen, Director
Ms. Kerrie L. Vanden Bosch, Director
Page 2

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, schedule of changes in net pension liability, schedule of net pension liability, schedules of contributions, and related notes, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the System's basic financial statements. The supporting schedules and the introductory section are presented for purposes of additional analysis and are not a required part of the basic financial statements.

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

The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we will also issue a report on our consideration of the 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control over financial reporting and compliance.

Sincerely,

Doug Ringler
Auditor General
January 30, 2017

FINANCIAL SECTION

Management's Discussion and Analysis

Effective January 1, 2016, in accordance with Executive Order 2015-13, the System became a qualified pension plan created in trust under Section 401 of the Internal Revenue Code. The System will be administered in accordance with the State Employees' Retirement Act and all plan documents relating the governance of the same. The accompanying financial statements, highlights, analysis and schedules represent nine (9) months of financial activity for the nine months ending September 30, 2016. Our discussion and analysis of the Michigan Military Retirement System's (System) financial performance provides an overview of the System's financial activities. Please read it in conjunction with the basic financial statements, which follow this discussion.

FINANCIAL HIGHLIGHTS

System assets exceeded liabilities at the close of fiscal year 2016 by \$3.6 million (reported as *net position*). Net position is restricted for pension benefits to meet future benefit payments.

Additions for the year were \$6.8 million, which are comprised primarily of employer contributions.

Deductions for the year were \$3.2 million, which are comprised primarily of retirement benefits paid.

THE STATEMENT OF PLAN FIDUCIARY NET POSITION AND THE STATEMENT OF CHANGES IN PLAN FIDUCIARY NET POSITION

This Comprehensive Annual Financial Report (CAFR) consists of two financial statements; *The Statement of Pension Plan Fiduciary Net Position* (page 13) and *The Statement of Changes in Pension Plan Fiduciary Net Position* (page 14). These financial statements report information about the System, as a whole, and about its financial condition that should help answer the question: Is the System, 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 economic resources measurement focus and 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 Pension Plan Fiduciary Net Position presents all of the System's assets and liabilities, with the difference between the two reported as fiduciary net position. Over time, increases and decreases in fiduciary net position measure whether the System's financial position is improving or deteriorating. *The Statement of Changes in Pension Plan Fiduciary Net Position* presents how the System's fiduciary net position changed during the most recent fiscal year. These two financial statements should be reviewed along with the Schedule of Net Pension Liability (page 24) and Schedules of Contributions (page 24) to determine whether the System is becoming financially stronger or weaker.

FINANCIAL ANALYSIS

System total assets as of September 30, 2016, were \$3.8 million and were mostly comprised of cash.

Total liabilities as of September 30, 2016, were \$189.0 thousand and were comprised of warrants outstanding and accounts payable.

FINANCIAL SECTION

Management's Discussion and Analysis (Continued)

Plan Fiduciary Net Position (in thousands)

	<u>2016</u>
Assets	
Equity in common cash	\$ 3,718
Receivables	<u>62</u>
Total Assets	<u>3,780</u>
Liabilities	
Accounts payable and other accrued liabilities	<u>189</u>
Total Liabilities	<u>189</u>
Net Position Restricted for Pension Benefits	<u>\$ 3,591</u>

ADDITIONS TO PLAN FIDUCIARY NET POSITION

The reserves needed to finance pension are accumulated through the employer contributions from the State of Michigan General Fund. Contributions and net investment income for nine months ending September 30, 2016 totaled \$6.8 million.

DEDUCTIONS FROM PLAN FIDUCIARY NET POSITION

The primary deductions of the System include the payment of pension benefits to members and beneficiaries, and the cost of administering the System. Total deductions for nine months ending September 30, 2016 were \$3.2 million.

FINANCIAL SECTION

Management's Discussion and Analysis (Continued)

Changes in Plan Fiduciary Net Position (in thousands)

	<u>2016</u>
Additions	
Employer contributions	\$ 6,790
Net investment income (loss)	11
Miscellaneous income	1
Total additions	<u>6,802</u>
Deductions	
Pension benefits	2,961
Administrative and other expenses	250
Total deductions	<u>3,211</u>
Net Increase (Decrease) in Net Position	3,591
Net Position Restricted for Pension Benefits:	
Beginning of Year	
End of Year	<u>\$ 3,591</u>

RETIREMENT SYSTEM AS A WHOLE

Management believes that the System is financially sound and positioned to meet its ongoing benefit obligations due, in part, to prudent cost controls, and strategic planning.

CONTACTING SYSTEM FINANCIAL MANAGEMENT

This financial report is designed to provide the Retirement Board, our membership, taxpayers, investors, and creditors with a general overview of the System's finances and to demonstrate the System's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the Office of Retirement Services, P.O. Box 30171, Lansing, MI 48909-7671.

FINANCIAL SECTION

Basic Financial Statements

STATEMENT OF PENSION PLAN FIDUCIARY NET POSITION As of September 30, 2016 (in thousands)

	<u>Pension Plan</u>
Assets:	
Equity in common cash	<u>\$ 3,718</u>
Receivables:	
Amounts due from members	3
Amounts due from other	59
Total Receivables	<u>62</u>
Total assets	<u>3,780</u>
Liabilities:	
Accounts payable and other accrued liabilities	189
Total liabilities	<u>189</u>
Net Position Restricted for Pension Benefits:	<u>\$ 3,591</u>

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

FINANCIAL SECTION

Basic Financial Statements (Continued)

STATEMENT OF CHANGES IN PENSION PLAN FIDUCIARY NET POSITION

For Nine Months Ending September 30, 2016 (in thousands)

	<u>Pension Plan</u>
Additions:	
Contributions:	
Employer contributions:	<u>\$ 6,790</u>
Investment income (loss):	
Interest, dividends, and other	<u>11</u>
Miscellaneous income	<u>1</u>
Total additions	<u>6,802</u>
Deductions:	
Benefits paid to plan members and beneficiaries:	
- Retirement benefits	2,961
Administrative and other expenses	<u>250</u>
Total deductions	<u>3,211</u>
Net Increase (Decrease) in Net Position	3,591
Net Position Restricted for Pension Benefits:	
Beginning of Year	<u> </u>
End of Year	<u>\$ 3,591</u>

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

NOTES TO BASIC FINANCIAL STATEMENTS

September 30, 2016

NOTE 1- PLAN DESCRIPTION

ORGANIZATION

The Michigan Military Retirement System (System) is a single employer, state-wide, defined benefit public employee retirement plan governed by the State of Michigan (State), created under Public Act 150 of 1967, as amended. Effective January 1, 2016, Executive Order 2015-13 signed by the Governor on October 27, 2015 established the State of Michigan Retirement Board. The executive order establishes the board's authority to promulgate or amend the provision of the System. The board shall administer the System in accordance with the State Employees' Retirement Act and all plan documents relating to the governance of the same. The board consists of nine members:

- The Attorney General
- The State Treasurer
- The Legislative Auditor General
- The State Personnel Director
- One member or retirant of the State Employees' Retirement System appointed by the Governor
- One member of the Judges Retirement System appointed by the Governor
- One current or former officer or enlisted person in the Michigan military Establishment who is a member or retirant under the Military Retirement Provisions appointed by the Governor
- One retirant member of the State Employees' Retirement System appointed by the Governor.
- One member of the general public appointed by the Governor.

The System's pension plan was established by the State to provide retirement, survivor and disability benefits to the State's National Guard members. The System is contained in a qualified pension trust fund under section 401(a) of the Internal Revenue Code.

The System is administered by the Office of Retirement Services within the Michigan Department of Technology, Management & Budget. The Department Director appoints the Office Director, with whom the general oversight of the System resides. The State Treasurer serves as the investment officer and custodian for the system.

FINANCIAL SECTION

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

MEMBERSHIP

At September 30, 2015, the System's membership consisted of the following:

Inactive plan members or their beneficiaries currently receiving benefits:	<u>4,248</u>
Inactive plan members entitled to but not yet receiving benefits:	<u>457</u>
Active plan members:	<u>10,047</u>
Total plan members	<u><u>14,752</u></u>

BENEFIT PROVISIONS

Introduction

Benefit provisions of the defined benefit pension plan are established by State statute, which may be amended. Public Act 150 of 1967, Michigan Military Act establishes eligibility and benefit provisions for the defined benefit pension plan.

Members are eligible to receive a monthly benefit when they meet certain age and service requirements. The System also provides duty disability, non-duty disability and survivor benefits.

There are two kinds of benefits paid to the system's membership depending on classification:

- 1) State of Michigan Military Officers: This group includes the adjutant general, assistant adjutant general(s) and special duty Officer(s) who are employees of the State of Michigan.
- 2) Former members of the Michigan National Guard (Army or Air Force) who have served in the State Defense Force and Michigan National Guard who are not State of Michigan Military Officers.

Eligibility

State of Michigan Military Officers can retire at age 55 with at least 20 years of services. The adjutant general and the assistant adjutant general(s) must serve four consecutive years of service as an adjutant general or assistant adjutant general. This requirement is waived if the service member is relieved due to a new governor assuming office. State of Michigan Military Officers may qualify for health benefits that are paid out of the Michigan State Employees Retirement System (MSERS).

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

Members of the Michigan National Guard who are not Michigan Military Officers can retire at age 60 with at least 20 years of service for members who began active service before June 30, 1967. Members who began active service after June 30, 1967, can retire at age 62 with at least 20 years of service.

Members who are age 55 and who have completed not less than 20 years of active service with the National Guard or State Defense Force, or both, may retire and receive retirement benefits under one or more of the following circumstances:

- Ineligibility, because of federal law or regulation, for further federal recognition in the person's current grade because of age or length of service, and termination of the person's commission or enlistment in the national guard of the United States
- Withdrawal of the person's federal recognition and termination of the person's commission or enlistment in the National Guard of the United States because of physical disqualification from further service.
- Separation from the National Guard or State Defense Force under an honorable circumstance.

Benefit Calculations

State of Michigan Military Officers receive an annual benefit of 2.5% of final compensation times total years of service. Final compensation is equal to the pay that an officer of like grade and total years of service would receive as indicated in appropriate federal regulations when they are retired or honorably relieved. The maximum annual benefit is 75% of final compensation. Retirement benefits will start on the date of retirement or honorable relief from duty. The spouse of a Michigan Military Officer who dies prior to retirement but after earning 15 years of special duty shall be paid a lifetime monthly benefit equal to 67% of the retired pay to which the member would have been authorized had the member retired on the day before death. Michigan Military Officers and their survivors receive annual benefit adjustments equal to the percentage by which federal military service benefits are increased.

Members of the Michigan National Guard who are not Michigan Military Officers receive \$600 per year. The benefit is payable for life. The surviving spouse of a member who dies after retiring or before becoming eligible for retirement shall receive a lifetime monthly benefit equal to a portion of the deceased person's benefit. If the member was active with at least 20 years of service before death, the spouse receives \$500 per year.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting and Presentation

The System became a qualified pension plan under trust effective January 1, 2016 in accordance with Executive Order 2015-13 and accordingly the accompanying financial statements and supporting schedules represent nine (9) months of financial activity for the fiscal year ended September 30, 2016. The first three (3) months of financial activity for the fiscal year ended September 30, 2016 is reported within the State of Michigan General Fund. The System's financial statements are prepared using the accrual basis of accounting. Contributions from the State are recognized as revenue when due and payable. Benefits and refunds are recognized when due and payable in accordance with the terms of the System.

Governmental Accounting Standards Board (GASB) Statement No. 67 which was adopted during the year ended September 30, 2014, addresses accounting and financial reporting requirements for pension plans. The requirements for GASB Statement No. 67 require changes in presentation of the financial statements, notes to the financial statements, and required supplementary information. Significant changes include an actuarial calculation of total and net pension liability. It also includes comprehensive footnote disclosure regarding the pension liability, the sensitivity of the net pension liability to the discount rate, and increased investment activity disclosures. The implementation of GASB Statement No. 67 did not significantly impact the accounting for accounts receivable and investment balances. The total pension liability, determined in

FINANCIAL SECTION

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

accordance with GASB Statement No. 67, is presented in Note 4 and in the Required Supplementary Information on page 23.

Reserves

Reserve for Employer Contributions – All employer contributions are credited to this reserve. At September 30, 2016, the balance in this reserve was \$6.8 million.

Reserve for Retired Benefit Payments – This represents the reserves for payment of future retirement benefits to current retirees. Monthly benefits, which are paid to the retiree, reduce the reserve. At the end of each fiscal year, an amount determined by an annual actuarial valuation is transferred from the Reserve for Employer Contributions to this reserve to bring the reserve into balance with the actuarial present value of retirement allowances. At September 30, 2016, the balance in this reserve was \$(3.0) million.

Reserve for Undistributed Investment Income – The net investment earnings (losses) are recorded in this reserve. Interest as authorized by the board is transferred annually to the other reserves. Administrative expenses are paid from this reserve. At September 30, 2016, the balance in this reserve was \$(239.0) thousand.

Reporting Entity

The System is a pension trust fund of the State. As such, the System is considered part of the State and is included in the State's Comprehensive Annual Financial Report as a pension trust fund. The System and its Board are not financially accountable for any other entities or other organizations. Accordingly, the System is the only entity included in this financial report.

Benefit Protection

Public Act 100 of 2002 was passed by the Michigan Legislature to protect pension benefits of public employees from alienation (being transferred). Alienation is attachment, garnishment, levy, execution, bankruptcy or other legal process except for divorce orders or eligible domestic relation orders. The statutes governing the System contained an "anti-alienation" clause to provide for this protection; however, many smaller public pension systems did not have the benefit of this protection. Therefore, Public Act 100 of 2002 was passed to establish legal protection of pension assets that encompasses all public employees.

Investment Income

Interest income is recognized on the accrual basis. Fair value changes are recorded as investment income or loss.

Costs of Administering the System

Each year a restricted general fund appropriation is requested to fund the ongoing business operations of the System. These administrative costs are ultimately funded by the System through the regular transfer of funds from the System to the State's general fund based on either a direct cost or allocation basis depending on the nature of the expense. Costs of administering the System are financed by undistributed investment income of the System.

Property and Equipment

Office space is leased from the State on a year-to-year basis. Office equipment is capitalized if the value exceeds \$5,000. These assets are recorded at cost and are reported net of depreciation in the *Statement of Pension Plan Fiduciary Net Position*. Such assets are depreciated on a straight-line basis over 10 years. The System does not have equipment that falls within these parameters.

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

Related Party Transactions

Leases and Services – The System leases operating space and purchases certain administrative, data processing, and legal services from the State. The space and services are not otherwise available by competitive bid. The schedule below summarizes costs incurred by the System for such services.

	<u>2016</u>
Attorney General	\$ 10,322
Personnel Services	156,266

Cash – At September 30, 2016, the System had \$3.7 million 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.

NOTE 3 – CONTRIBUTIONS AND FUNDED STATUS

Contributions

The State contributes annually to the System, based on the actuarial required contributions to support retirement benefits, through appropriation from the state's general fund.

Employer contributions to the System are determined on an actuarial basis using the entry age normal actuarial cost method. Under this method, the actuarial present value of the projected benefits of each individual included in the actuarial valuation is allocated on a level basis over the service of the individual between entry age and assumed exit age. The portion of this cost allocated to the current valuation year is called the normal cost. The remainder is called the actuarial accrued liability. Normal cost is funded on a current basis.

The system is required to reconcile with actuarial requirements annually. Any funding excess or deficiency for pension benefits is smoothed over 5 years. One fifth (20%) of the funding excess or deficiency is included in each of the subsequent years' contribution, and is not recognized as a payable or receivable in the accounting records.

NOTE 4 – NET PENSION LIABILITY

Measurement of the Net Pension Liability

The net pension liability is to be measured as the total pension liability, less the amount of the pension plan's fiduciary net position. In actuarial terms, this will be the accrued liability less the fair value of assets (not the smoothed actuarial value of assets that is often encountered in actuarial valuations performed to determine the employer's contribution requirement).

FINANCIAL SECTION

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

Net Pension Liability

Total Pension Liability	\$	47,106,532
Plan Fiduciary Net Position		3,591,109
Net Pension Liability	\$	<u>43,515,423</u>
Plan Fiduciary Net Position as a Percentage of Total Pension Liability		7.62%
Net Pension Liability as a percentage of Covered Payroll		9269%
Total Covered Payroll	\$	469,456

Discount Rate

A discount rate of 8.0% was used to measure the total pension liability. This discount rate was based on the long term expected rate of return on pension plan investments of 8.0%. The projection of cash flows used to determine this discount rate assumed that employer contributions will be made at rates equal to the actuarially determined contribution rates. Based on these assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

As required by GASB Statement No. 67, the following presents the plan's net pension liability, calculated using a single discount rate of 8.0%, as well as what the plan's net pension liability would be if it were calculated using a single discount rate that is 1-percentage-point lower or 1-percentage-point higher:

1% Decrease 7.0%	Current Discount Rate Assumption 8.0%	1% Increase 9.0%
\$48,462,878	\$43,515,423	\$39,375,853

Timing of the Valuation

An actuarial valuation to determine the total pension liability is required to be performed at least every two years. If the actuarial valuation is not calculated as of the plan's fiscal year end, the total pension liability is required to be rolled forward from the actuarial valuation date to the pension plan's fiscal year end.

The total pension liability as of September 30, 2016, is based on the results of an actuarial valuation date of September 30, 2015, and rolled-forward using generally accepted actuarial procedures.

Actuarial Valuations and Assumptions

Actuarial valuations for the pension plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

employment and mortality trends. Amounts determined regarding the funded status of the plan and the annual required contributions (ARC) are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

The Schedules of Contributions in Required Supplementary Information present trend information about the amounts contributed to the plan by employers in comparison to the ARC, an amount that is actuarially determined in accordance with the parameters of GASB Statement No. 67 for pension contributions.

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

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Summary of Actuarial Assumptions

Valuation Date	September 30, 2015
Actuarial Cost Method	Entry Age, Normal
Amortization Method	Level Dollar, Closed
Remaining Amortization Period	21 years
Asset Valuation Method	N/A
Actuarial Assumptions:	
Inflation Rate	2.5%
Investment Rate of Return	8.0%
Projected Salary Increases	3.5%
Mortality:	RP-2000 Combined Healthy Life Mortality Table, adjusted for mortality improvements to 2030 using projection scale BB for males and adjusted for mortality improvements to 2015 using projection scale BB for females.
Notes:	Assumption changes as a result of an experience study for the periods 2007 through 2012 have been adopted by the System for use in the annual pension valuations beginning with the September 30, 2015 valuation.

NOTE 5 – NEW ACCOUNTING PRONOUNCEMENTS

GASB issued Statement No. 82, *Pension Issues—an amendment of GASB Statements No. 67, No. 68 and No. 73*. This statement addresses issues regarding: 1) the presentation of payroll-related measures in required supplementary information; 2) the selection of assumptions and the treatment of deviations from the guidance in an actuarial standard of practice for financial reporting purposes; and 3) the classification of payments made by employers to satisfy employee (member) contribution requirements. This Statement is effective for financial statements for fiscal years beginning after June 15, 2016.

NOTE 6 – COMMITMENTS AND CONTINGENCIES

Under the Administrative Procedures Act, members may appeal a decision made by the Board. Once the administrative procedure has been exhausted, the decision may be appealed in Michigan's court system.

FINANCIAL SECTION

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

Various cases that have exhausted the administrative procedures have been appealed in the court system. These cases are in the normal course of business and the System does not anticipate any material loss as a result of the contingent liabilities.

FINANCIAL SECTION

Required Supplementary Information

SCHEDULE OF CHANGES IN NET PENSION LIABILITY (in thousands)

	Fiscal Year	
	2016	2015
Total Pension Liability		
Service Cost	\$ 403	\$ 357
Interest	2,829	3,564
Changes of benefit terms		
Differences between expected and actual experience		(17,548)
Changes of assumptions	(30,216)	7,086
Benefit payments, including refunds of member contributions	(3,950)	(3,923)
Net Change in Total Pension Liability	(30,933)	(10,463)
Total Pension Liability - Beginning	78,040	88,503
Total Pension Liability - Ending (a)	\$ 47,107	\$ 78,040
Plan Fiduciary Net Position		
Contributions - Employer	\$ 7,780	\$ 4,267
Contributions - Member		
Net Investment Income	12	
Benefit payments, including refunds of member contributions	(3,950)	(3,923)
Administrative and Other Expenses	(251)	(344)
Net Change in Plan Fiduciary Net Position	3,591	
Plan Fiduciary Net Position - Beginning		
Plan Fiduciary Net Position - Ending (b)	\$ 3,591	
Net Pension Liability - Ending (a) - (b)	\$ 43,515	\$ 78,040
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	7.62%	0.00%
Covered Employee Payroll¹	\$ 469	\$ 484
Net Pension Liability as a Percentage of Covered Employee Payroll	9,269 %	16,110 %

¹For special duty officers only

FINANCIAL SECTION

Required Supplementary Information (continued)

SCHEDULE OF NET PENSION LIABILITY (in thousands)

<u>Fiscal Year Ended Sept. 30</u>	<u>Total Pension Liability</u>	<u>Plan Net Position</u>	<u>Net Pension Liability</u>	<u>Plan Net Position as % of Total Pension Liability</u>	<u>Covered Payroll</u>	<u>Net Pension Liability as % of Covered Payroll</u>
2015	\$ 78,040		\$ 78,040	0.00 %	\$ 484	16,110 %
2016	47,107	\$ 3,591	43,515	7.62	469	9,269

SCHEDULES OF CONTRIBUTIONS

Pension Benefits (in thousands)

<u>Fiscal Year Ended Sept. 30</u>	<u>Annual Required Contribution (ARC)</u>	<u>Actual Employer Contribution</u>	<u>Contribution Deficiency (Excess)</u>	<u>Covered Payroll</u>	<u>Actual Contribution as a % of Covered Payroll</u>
2015	\$ 6,293	\$ 4,267	\$ 2,026	\$ 484	881 %
2016	5,200	7,780	(2,580)	469	1,657

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

NOTE A – DESCRIPTION

Historical trend information designed to provide information about the System's progress made in accumulating sufficient assets to pay benefits when due is presented in the preceding schedules. This information is presented to enable the reader to assess the progress made by the System in accumulating sufficient assets to pay pension benefits as they become due.

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 obligations as a factor.

The Schedule of Contributions are reported as historical trend information. The Schedule of Contributions are presented to show the responsibility of the Employer in meeting the actuarial requirements to maintain the System on a sound financial basis.

The Schedule of Changes in Net Pension Liability, Schedule of Net Pension Liability, and Schedule of Contributions are schedules that are required in implementing GASB Statement No. 67. These schedules are required to show information for ten years; additional years will be displayed as it becomes available. The two schedules of the Net Pension Liability represents in actuarial terms, the accrued liability less the fair value of assets. The Schedule of Contributions is a comparison of the employer's contributions to the actuarially determined contributions.

The information presented in the Schedule of Contributions was used in the actuarial valuation for purposes of determining actuarially determined contribution rate. Additional information as of the latest actuarial valuation for the pension plan follows.

Valuation:

Actuarially determined contribution amounts for fiscal year 2016 were calculated based upon the results of the September 30, 2013 actuarial valuation.

Methods and Assumptions Used to Determine Contributions for Fiscal Year 2016:

Actuarial Cost Method	Entry Age, Normal
Amortization Method	Level Dollar, Closed
Remaining Amortization Period	21 Years
Asset Valuation Method	N/A
Inflation	2.5%
Salary Increases	3.5% for Special Duty officers
Investment Rate of Return	8% net of investment and administrative expenses
Retirement Age	Experience-based table of rates that are specific to the type of eligibility conditions.
Mortality	RP-2000 Combined Healthy Life Mortality Table, adjusted for mortality improvements to 2020 using projection scale AA.

FINANCIAL SECTION

Supporting Schedules

SUMMARY SCHEDULE OF PENSION PLAN ADMINISTRATIVE AND OTHER EXPENSES

For Nine Months Ending September 30, 2016

Personnel Services:

Staff Salaries	\$ 156,266
Total	<u>156,266</u>

Professional Services:

Actuarial	427
Attorney General	10,322
Consulting	256
Total	<u>\$ 11,005</u>

SCHEDULE OF PAYMENTS FOR PROFESSIONAL SERVICES

For Nine Months Ending September 30, 2016

Actuary	\$ 427
Attorney General	10,322
Consulting	<u>256</u>
Total Payments	<u>\$ 11,005</u>

FINANCIAL SECTION

Supporting Schedules (continued)

DETAIL OF CHANGES IN PLAN FIDUCIARY NET POSITION For Nine Months Ending September 30, 2016 (in thousands)

	Employer Contributions	Retired Benefit Payments	Undistributed Investment Income	Total
Additions:				
Contributions:				
Employer contributions:	\$ 6,790			\$ 6,790
Investment income (loss):				
Interest, dividends, and other			\$ 11	11
Miscellaneous income		\$ 1		1
Total additions	<u>6,790</u>	<u>1</u>	<u>11</u>	<u>6,802</u>
Deductions:				
Benefits paid to plan members and beneficiaries:				
Retirement benefits		2,961		2,961
Administrative and other expenses			250	250
Total deductions		<u>2,961</u>	<u>250</u>	<u>3,211</u>
Net Increase (Decrease) in Net Position	6,790	(2,960)	(239)	3,591
Net Position Restricted for Pension Benefits:				
Beginning of Year				
End of Year	<u>\$ 6,790</u>	<u>\$ (2,960)</u>	<u>\$ (239)</u>	<u>\$ 3,591</u>

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This report may be viewed online at: www.michigan.gov/ors