



SUMMARY ANNUAL FINANCIAL REPORT

for the fiscal year ending

12.31.2019



1134 Municipal Way
Lansing, Michigan 48917

800.767.MERS (6377)
www.mersofmich.com

ABOUT THIS REPORT

This report provides a summary of the MERS Comprehensive Annual Financial Report (CAFR) for the fiscal year which ended December 31, 2019. The CAFR is prepared in accordance with Generally Accepted Accounting Principles (GAAP) and is subject to external audit. This Summary Annual Financial Report is also prepared in accordance with GAAP. The 2019 CAFR contains more detailed information and can be obtained by contacting MERS:

Website:

www.mersofmich.com

By mail:

Municipal Employees' Retirement System of Michigan
1134 Municipal Way
Lansing, MI 48917

By phone:

800.767.MERS (6377)

The financial statements were audited by Plante & Moran, PLLC.

CERTIFICATE OF ACHIEVEMENT FOR EXCELLENCE IN FINANCIAL REPORTING



MERS received the Award for Outstanding Achievement in Popular Annual Financial Reporting from the Government Finance Officers Association for the 2018 Summary Annual Financial Report. This marks the 16th consecutive year MERS has received this honor.

AN INDEPENDENT ELECTED BOARD

MERS is governed by an independent, unpaid board committed to fairness, transparency and accountability for our customers. Our board adheres to strong conflict of interest provisions and best fiscal practices making us a reliable fiduciary agent and a go-to expert for retirement security in Michigan.

Three Officer Members:

Officers of a participating municipality, elected by membership

Three Employee Members:

Non-officers of a participating municipality, elected by membership

Two Expert Members:

With experience in retirement systems or investment management, appointed by the Board

One Retiree Member:

Retiree of the system, appointed by the Board



MERS Retirement Board

is responsible for administration of the system with **fiduciary responsibility** for the investment of assets and oversight.

MERS OFFICERS



Kerrie Vanden Bosch was selected as MERS Chief Executive Officer, effective January 2, 2020



Denise Boucke
Chief Operating Officer



Jeb Burns
Chief Investment Officer



Leon Hank
Chief Financial Officer



Carrie Lombardo
Chief Strategic & External Affairs Officer

MERS RETIREMENT BOARD



Back row (standing left to right): Dale Feldpausch, James Wiersma, Jason Sarata, Michael Brown, Tina Butler
Front row (sitting): Amy Deford, John Ogden, Michael Gilmore, Randy Girard

Officer Members: **Michael Brown** (Chairperson), Barry County; **Randy Girard**, Charter Twp of Marquette; **Dale Feldpausch**, Capital Region Airport Authority

Employee Members: **Tina Butler**, Cass County; **Jason Sarata**, Delta Twp; **Amy Deford**, Saginaw County

Expert Members: **Michael Gilmore**, Red Cedar Investment Mgt, East Lansing; **James R. Wiersma**, Family Investment & Resource Mgt, LLC, Holland;

Retiree Member: **John Ogden**, City of Port Huron (Retired)

LETTER OF TRANSMITTAL, MAY 22, 2020

Dear Board Members:

We are pleased to submit the Summary Annual Financial Report for the Municipal Employees' Retirement System of Michigan (MERS) for the fiscal year ending December 31, 2019.

MERS has laid solid groundwork for goals and measurements by which we evaluate and move toward our vision of delivering superior value to our customers by:

- 1) Achieving a deeper understanding of customer needs and connection with them;
- 2) Proactively partnering with employers by providing options that help meet their unique needs;
- 3) Consistently delivering services through intuitive processes and systems; and
- 4) Significantly increasing resources and awareness that help participants improve financial wellness to be ready for retirement.

To accomplish this, MERS has developed a Balanced Scorecard focusing on four perspectives: Customer, Financial, Process, and Learning & Growth. Specific projects within each perspective drive business efforts and are measured on an ongoing basis, reported on our Balanced Scorecard and driving team work priorities and individual performance company-wide.

MERS exceeded overall metrics in 2019. Highlights include engagement with MERS resources and actions to improve participant financial wellness, positive investment performance, holding operational costs, ongoing measurement of key processes, and a significant increase in employer satisfaction with their voice being heard. Our customer base continued to expand, partnering with 21 new municipalities and cross-enrollment with three-quarters of our member municipalities enrolled in more than one program – more than half enrolling in three or more.

MERS Profile

MERS is a statutory, public corporation that serves members across the state of Michigan. We are one of the largest, most established, and successful shared services stories in Michigan, providing administration, investment expertise, fiduciary responsibility, and oversight for benefit plans. Our approach to efficiently managing retirement and other post-employment plans allows local governments to focus on their core services, leaving day-to-day plan administration and long range management to us. Services we provide include: plan governance, internal auditing, legal counsel, actuarial services, financial management, information technology support, legislative advocacy, administration of benefits, participant education and resources, and investments. The MERS Retirement Board (Board) serves as the fiduciary of the funds and has oversight responsibilities.

Financial Summary

In 2019, MERS had an excellent year, significantly enhancing its financial condition and setting four new records for financial levels. First, MERS continued to enhance investment practices to maximize long-term performance and the stability of the pension portfolio. The MERS Defined Benefit (DB) Portfolio returned 14.02% over the year (net of investment expenses). This investment performance generated \$1.45B. More information regarding our investment management performance, policies and processes are found in the Investments Section of the [2019 Comprehensive Annual Financial Report \(CAFR\)](#).

Second, MERS also grew its net position held for members to a new record level of \$12.4 billion. The most significant factor in that growth was net revenue of \$2.5 billion (\$1.5 billion from investment returns). Strong cost control measures helped MERS hold its administrative costs to \$21.5 million, up slightly from last year, but still comparable with costs back to our 2009 spending level. That long-term trend of modest administrative costs

also has a positive impact on defined benefit plans.

Third, part of the MERS revenue growth included surpassing the \$100 million level of employer and employee contributions to MERS Defined Contribution plan for the first time. Defined contribution, and other participant directed plans, continue to be the fastest growing segment of MERS.

Fourth, as an indicator of how municipalities are more aggressively addressing their other post-employment benefit (OPEB) obligations, MERS experienced its most significant growth in the Retiree Health Funding Vehicle, where net plan assets grew by 24%. The total asset increase for this program in 2019 was over \$97 million.

MERS municipalities also moved to expand access for participants to manage individual supplemental savings accounts with an increase of 14% in municipalities offering MERS 457 programs. More individuals are taking advantage of the MERS IRA opportunities with 127 new accounts funded in the first full year of this program.

One measure of a defined benefit retirement system's financial health is the percentage of its actuarial liabilities owed that is covered by its available actuarial assets. Using this ratio, 59% of MERS' municipalities were funded at 70% or higher (437 municipalities), which is up from the previous year.

We continue to partner with all municipalities in helping them set fiscal goals and exploring options to find the programs and provisions that best fit each municipality's unique needs. There are 841 municipalities within MERS Defined Benefit and Hybrid Plans, which encompass 3,028 divisions with unique benefit designs. There were 131 divisions that increased cost sharing to their employees. In 2019, over half of our employers made voluntary contributions to their plan, contributing an additional \$142 million to help increase funding levels. These efforts helped strengthen the financial condition of all of these plans. In addition, new municipalities joining the MERS system brought in an extra \$16 million.

During 2019 and continuing into early 2020, MERS completed a five-year Experience Study review of its actuarial assumptions. As an outcome of the study, MERS adopted new economic and demographic actuarial assumption rates that will generally increase contribution levels for most defined benefit and hybrid plans, effective with the 2021 and 2022 fiscal years for employers. These changes will further strengthen plans and will help ensure they can meet their future retirement plan obligations.

More detail on these financial metrics is included in the Management Discussion & Analysis section of the [2019 Comprehensive Annual Financial Report \(CAFR\)](#). A complete copy of the CAFR is provided to the Governor, the members of both the State House and Senate, and the Office of the State Treasurer, as required by law. The CAFR and Summary Report are available on our website, www.mersofmich.com.

Respectfully submitted,



Kerrie Vanden Bosch
Chief Executive Officer



Leon E. Hank, CPA
Chief Financial Officer

FINANCIAL HIGHLIGHTS

The following financial highlights occurred during the year ended December 31, 2019:

- Total fiduciary net position for the Defined Benefit Plan, Defined Contribution Plan, Health Care Savings Program, Retiree Health Funding Vehicle, 457 Program, Investment Services Program, and Individual Retirement Account Program increased by nearly 14%, primarily due to market increases for the year. MERS finished the year with \$12.4 billion in net fiduciary position, which is the highest in MERS history.
- The portfolio investment returns saw a gain of 14.02% net of investment expenses for the year. The 10-year return was 7.97% net of investment expenses, which is above the long-term target of MERS' expected investment rate of return of 7.75%. The portfolio investment income returned \$1.5 billion in 2019, the highest amount in MERS history.
- Contribution revenue declined by 2% in 2019, which is attributed to fewer bonding proceeds coming into the Defined Benefit Plan. Defined Contributions revenues topped \$100 million in 2019.

Comparison Statement of Fiduciary Net Position (Dollars in Thousands)

	December 31, 2019	December 31, 2018	\$ Increase (Decrease)	% Increase (Decrease)
Assets				
Cash and Short-Term Investments	\$39,669	\$17,538	\$22,131	126%
Receivables	66,285	478,177	(411,892)	-86%
Interfund Receivables	125	127	(2)	-1%
Loans	6,099	6,161	(62)	-1%
Investments, at fair value	12,298,251	10,833,075	1,465,176	14%
Invested Securities Lending Collateral	164	573,927	(573,763)	-100%
Prepays/Other Assets	1,164	4,320	(3,156)	-73%
Net Capital Assets	19,919	18,246	1,673	9%
Total Assets	12,431,676	11,931,570	500,106	4%
Deferred Outflow of Resources				
Outflows Related to Pension	5,801	3,571	2,230	62%
Liabilities				
Purchase of Investments	32,590	438,629	(406,039)	-93%
Securities Lending Collateral	164	573,997	(573,833)	-100%
Administrative/Investment Costs/Reserves	7,414	10,359	(2,945)	-28%
Interfund Payables	125	127	(2)	-2%
Total Liabilities	40,293	1,023,112	(982,819)	-96%
Deferred Inflow of Resources				
Inflows Related to Pension		717	(717)	-100%
Net Position - Restricted for:				
Pensions	9,917,856	8,967,305	950,551	11%
Postemployment benefits other than pensions	2,432,345	1,883,832	548,513	29%
Pool participants	49,894	60,175	(10,281)	-17%
	\$12,397,184	\$10,911,312	\$1,485,872	14%

The Statement of Fiduciary Net Position summarizes what MERS owns and owes as of the end of the fiscal year.

- Total annual benefits, transfers, and withdrawals increased by \$34 million for a total of \$1 billion up from \$987 million in 2018. This is the first time in MERS history that benefit payments exceeded \$1 billion.
- Administrative expenses increased in 2019 to \$21.5 million. This increase is attributed to investment in staffing as well as systems enhancements and security.
- Investment expenses declined slightly due to lower investment manager fees. The decrease in investment manager expense was partly due to bringing in additional assets to be managed in-house by MERS Office of Investments at a lower cost.
- The most recent MERS actuarial valuation, dated December 31, 2018, showed 437 of 745 Defined Benefit municipalities are funded 70% or better, with 76 municipalities over 100% funded.
- The difference between the MERS actuarial and fair value assets declined from last year, as the actuarial calculation for 2018 is 109.3% of the fair value of assets as calculated by the actuaries (the ratio was 101.1% as of December 31, 2017). Total Defined Benefit Plan actuarial assets and fair value of assets were valued at \$9.8 billion and \$9.0 billion respectively at December 31, 2018.
- As part of the MERS 2019 Strategic Plan, MERS invested \$4.6 million in capital assets. This includes \$3.9 million for key projects to upgrade the pension administration and actuarial valuation software. The MERS investment in all capital assets is \$19.9 million, net of accumulated depreciation.

Comparison Statement of Changes in Fiduciary Net Position (Dollars in Thousands)

	December 31, 2019	December 31, 2018	\$ Increase (Decrease)	% Increase (Decrease)
Additions				
Contributions/Transfers in	\$1,003,170	\$1,024,586	\$(21,416)	-2%
Investment Net Income (Loss) Investing Activities	1,523,215	(498,201)	2,021,416	406%
Investment Net Income-Securities Lending	2,159	3,152	(993)	-32%
Miscellaneous Income	20	221	(201)	-91%
Total Additions	2,528,564	529,758	1,998,806	377%
Deductions				
Benefits/Transfers and Withdrawals	1,021,166	987,449	33,717	3%
Forfeitures, Miscellaneous	4	6	(2)	100%
Administrative Expense	21,522	19,065	2,457	13%
Total Distributions	1,042,692	1,006,520	36,172	4%
Net Increase/Decrease	1,485,872	(476,762)	1,962,634	412%
Net Position - Beginning of Fiscal Period	10,911,312	11,388,074	(476,762)	-4%
Net Position - End of Fiscal Period	\$12,397,184	\$10,911,312	\$1,485,872	14%

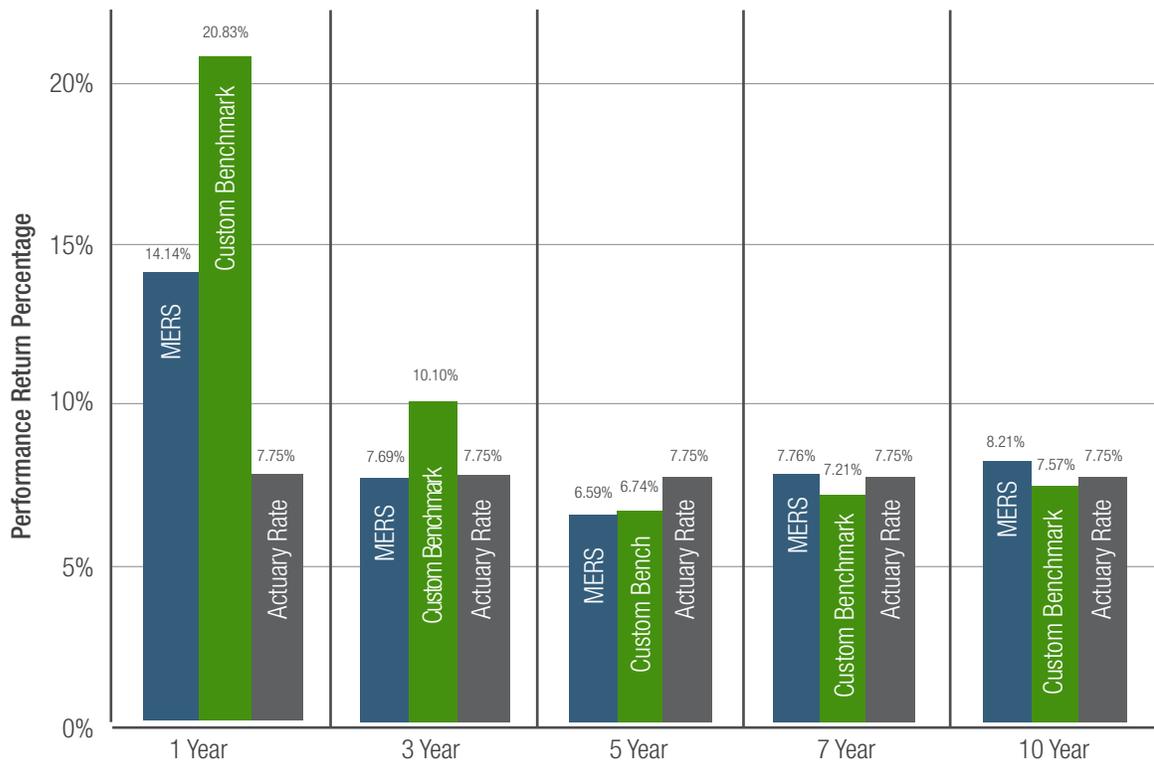
The Statement of Changes in Fiduciary Net Position summarizes the flow of money in and out of the fund throughout the fiscal year. The primary uses of MERS assets are the payments of benefits to participants and their beneficiaries, refunds to terminated participants, and the cost of administering the system.

INVESTMENT OBJECTIVES AND ACTIVITY

In compliance with state laws, the primary goal of MERS' investment program is to grow assets at a rate which, when coupled with employer and employee contributions, will sustain promised benefits to MERS' retirees and beneficiaries. To achieve this objective, MERS prudently allocates the trust assets by:

- Identifying investments that meet or beat the annual actuarial investment assumption of 7.75% on a long-term basis.
- Maintaining adequate liquidity to pay promised benefits.
- Adopting a strategic asset allocation plan that reflects current and future liabilities, minimizes volatility, and seeks to exceed the annual actuarial investment assumption.
- Minimizing the costs associated with the implementation of the asset allocation through the efficient use of internal and external resources.
- Maintaining above median peer rankings for the 10-year time period.
- Making investments that will meet or beat the return of the Portfolio's Policy Benchmark. The Policy Benchmark currently consists of 45% Russell 3000, 25% Bloomberg Barclays Global Aggregate Bond Index, 20% MSCI ACWI IMIex-US, and 10% Bloomberg Barclays Global Aggregate ex US.

Performance Versus Custom Benchmarks as of December 31, 2019 (gross of fees)



MERS INVESTMENT HIGHLIGHTS

- MERS Defined Benefit Portfolio returned 14.14% gross of fees for the year, underperforming its policy benchmark by 6.69%. The five-year return of 6.59% underperformed the policy benchmark by 0.15% on an annualized basis. The Portfolio returned 8.21% at the ten-year mark and outperformed the policy benchmark by 0.64%.
- The Office of Investments initiated work on a Valuation Based Allocation approach to its investment program.
- The base asset allocation breakdown is shown below:

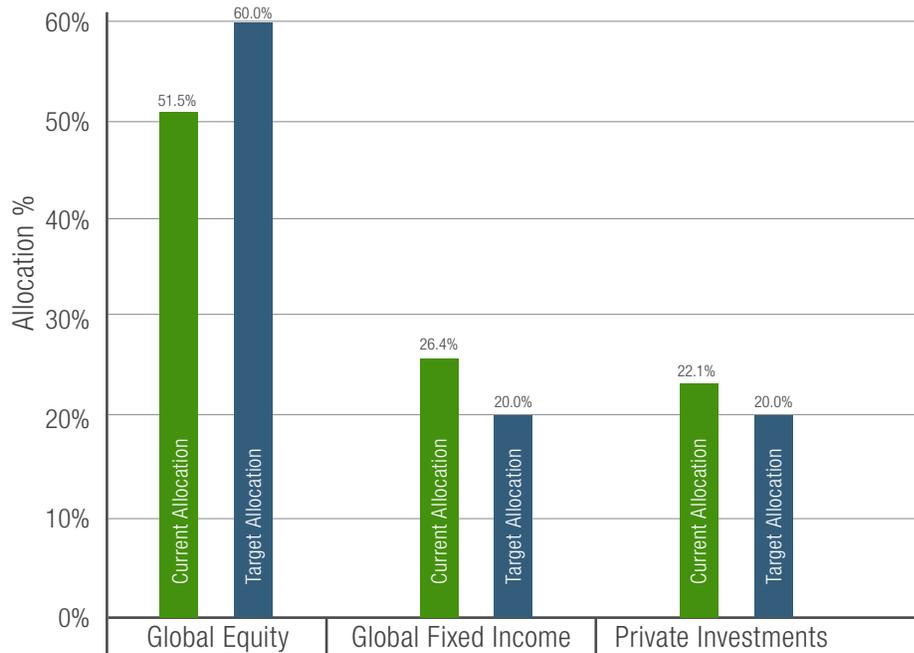
Global Equity	60.00%
Global Fixed Income	20.00%
Private Investments	20.00%

- At the broad asset class level, absolute returns gross of investment fees for the year were as follows:

Global Equity	19.81%
Global Fixed Income	9.37%
Private Investments	
Private Equity	11.00%
Real Assets	13.54%
Diversifying Strategies	7.48%

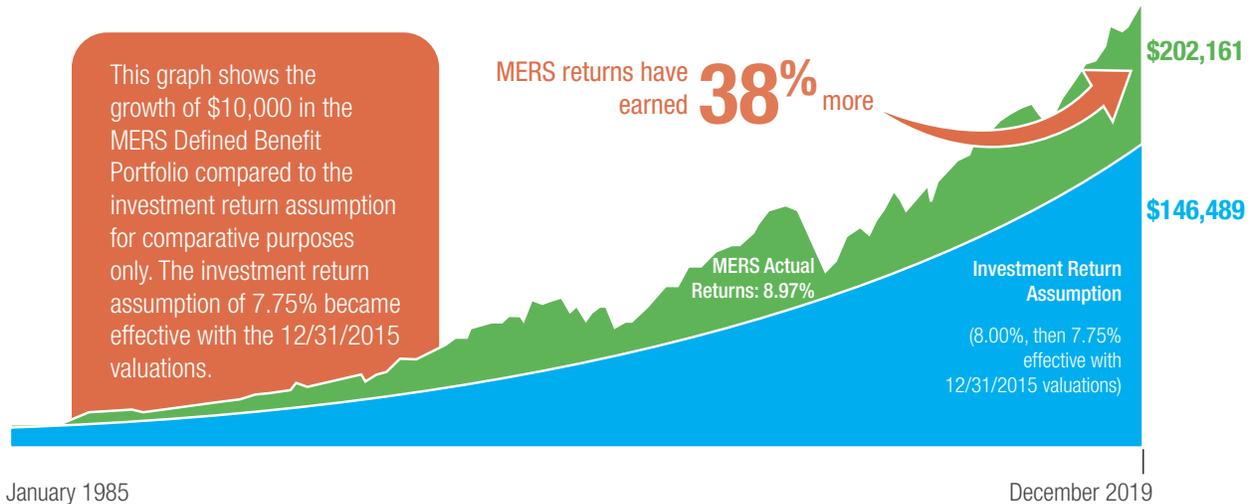
The MERS Retirement Board's support of the Office of Investments in their roles as the fiduciaries of the MERS Plan with its functional checks and balances allows the investment program to be successful for our members. This relationship makes for an efficient decision-making process, benefiting our membership through stronger risk-adjusted returns.

Current Asset Allocation versus Base Allocation as of December 31, 2019



A TRACK RECORD OF SUCCESS

As retirement plans operate over long-term time horizons, it's important to focus on long-term rates rather than any single year. The investment return assumption of 7.75% is projected over the lifetime of the participants covered in the plan, typically more than 30 years. For municipalities that wish to project a more conservative approach, MERS provides tools to do so within our annual valuation reports.



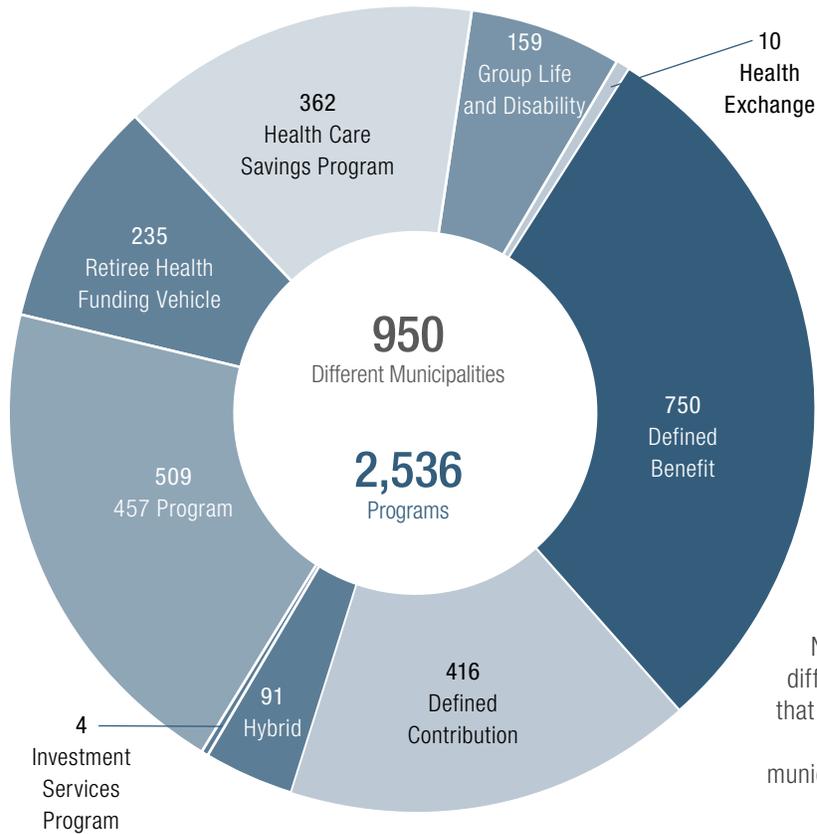
Year-by-Year Returns (35 years: 1985-2019)

Year	Rate of Return	Year	Rate of Return	Year	Rate of Return
2019	14.14%	2007	8.58%	1995	23.95%
2018	-3.51	2006	13.61	1994	0.52
2017	13.40	2005	6.78	1993	9.67
2016	11.10	2004	14.90	1992	8.05
2015	-0.85	2003	24.72	1991	22.14
2014	6.68	2002	-8.34	1990	2.94
2013	15.00	2001	-1.91	1989	19.10
2012	11.39	2000	-2.76	1988	11.20
2011	2.30	1999	17.01	1987	5.51
2010	14.43	1998	14.20	1986	13.55
2009	17.31	1997	14.43	1985	24.33
2008	-24.79	1996	12.68		

Annualized 35-year rate of return for MERS Defined Benefit: 8.97%

Performance numbers on this page are gross of fees.

MERS Participating Municipalities as of December 31, 2019



MERS Participants as of December 31, 2019

	Defined Benefit	Defined Contribution	Hybrid	Health Care Savings Program	457	Health Exchange	IRA
Active	30,263	14,911	3,626	19,250	6,600	340	133
Deferred	9,319	NA	301	NA	NA	NA	NA
Retired	42,111	NA	119	NA	NA	NA	NA
Contributions not Vested	13,833	NA	8	NA	NA	NA	NA
Terminated	NA	6,582	NA	7,424	1,165	NA	NA
Product Totals	95,526	21,493	4,054	26,674	7,765	340	133
Total MERS Accounts*							155,985

* Total MERS Accounts represents the total number of accounts within MERS; individuals may be represented multiple times across categories.



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This publication contains a summary description of MERS benefits, policies or procedures. MERS has made every effort to ensure that the information provided is accurate and up to date (as of the date of publication 06/16/2020). If this publication conflicts with the relevant provisions of the Plan Document, the Plan Document Controls. MERS, as a governmental plan, is exempted by state and federal law from registration with the SEC. However, it employs registered investment advisors to manage the trust fund in compliance with Michigan Public Employee Retirement System Investment Act. Past Performance is not a guarantee of future returns. Please make independent investment decisions carefully and seek the assistance of independent experts when appropriate.

