Michigan State Employees Retirement System

Comprehensive Annual Financial Report for the Year Ended September 30, 1998

A Pension Trust Fund of the State of Michigan
John Engler, Governor

Michigan State Employees' Retirement System

Comprehensive Annual Financial Report for the Fiscal Year Ended September 30, 1998

MSERS

Prepared by:
Office of Retirement Services
Michigan State Employees' Retirement System
7150 Harris Drive
P.O. Box 30171
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INTRODUCTORY SECTION

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The cost of printing this report was $1,499.55 (2.99 each), which was paid for by the retirement system at no cost to taxpayers.

INTRODUCTORY SECTION

Certificate of Achievement

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Michigan State Employees Retirement System

For its Comprehensive Annual Financial Report for the Fiscal Year Ended September 30, 1997

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.

Douglas R Ellsworth
President

Jeffrey L. Esser
Executive Director

Letter of Transmittal

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STATE OF MICHIGAN

JOHN ENGLER, Governor

DEPARTMENT OF MANAGEMENT AND BUDGET

February 16, 1999

The Honorable John Engler
Governor, State of Michigan,

Members of the Legislature
State of Michigan

Retirement Board Members
and
Members, Retirees and Beneficiaries

Ladies and Gentlemen:

We are pleased to present the annual report of the Michigan State Employees' Retirement System (MSERS or System) for fiscal year 1998.

Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the management of the System. To the best of our knowledge and belief, the enclosed data is accurate in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of the System.

The Michigan State Employees' Retirement System was established by legislation under Public Act 240 of 1943 (the State Employees' Retirement Act). The number of active and retired members and beneficiaries of the System is presented in Note 1 of the financial statements in the Financial Section of this report. The services provided by the staff are performed to facilitate benefits to members.

The 1998 annual report is presented in five sections. The Introductory Section contains the transmittal letter, the identification of the administrative organization and professional consultants used by the System. The Financial Section contains the independent auditors' report, the financial statements of the System and certain supplemental schedules. The Investment Section summarizes investment activities. The Actuarial Section contains the independent consulting actuary's certification, an outline of actuarial assumptions and methods, and other actuarial statistics. The Statistical Section contains statistical tables of significant data pertaining to the Retirement System.

Letter of Transmittal (Continued)

MAJOR GOALS ACCOMPLISHED

The Office of Retirement Services (ORS) accomplished several major goals and initiatives in 1998 to improve services to the Michigan State Employee's Retirement System.

» The Office of Retirement Services' Customer Information Center (CIC) initiated toll-free phone service on January 30, 1998 for active and retired members who live outside the Lansing area. The CIC receives approximately 20,000 phone calls per month. In addition, the Outreach Program now makes it possible for employees of all four retirement systems to receive retirement information at four locations - Detroit, Waterford, Holland and Lansing.

» Active and retired members of the State Employees Retirement System were notified in July that the State's pension contribution rate was reduced. Return on the fund's investments was higher than anticipated and various expenditures were less than expected. In the annual actuarial review of the system, the ratio of assets to all estimated current and future retirement benefits was greater than 100%, showing the system to be fully funded. Because of these factors, a lower contribution rate is required to continue the State Employees Retirement System's solid, secure, fully-funded status.

» As mandated by legislation, all State of Michigan new employees hired on or after March 31, 1997, are members of a new Defined Contribution retirement plan as opposed to the Defined Benefit plan. Employees hired before that date were given the option to choose whether to remain in the Defined Benefit plan or transfer to the new Defined Contribution plan. A total of 3,482 applications for transfer to the Defined Contribution plan were received. Of those applicants, 3,224 actually were eligible to transfer. The transfer process went smoothly and was accomplished one and one-half months earlier than projected.

» Changes in the Retirement Act effective August 1, 1998 now allow members of the State Employees Retirement System to purchase up to five years of "universal buy-in" credit toward their Defined Benefit retirement pension without linking the purchase to specific types of service performed outside the system. The change in the Act has generated a 60% increase in the volume of requests for service credit billings.

» In March of 1998 the Office of Retirement Services mailed the first issue of its new Connections newsletter to all retirees, with a second issue going out in October. The objectives for this newsletter are threefold: 1) To establish a direct connection with all retirees; 2) To remind retirees ORS is available to assist them and tell them how to access that assistance, and 3) To give retirees information that will assist them in doing business with the Office of Retirement Services.

» Reengineering has redesigned the process for disability retirement whereas a common application, procedures, policies, tracking and process flow are now used for all four retirement systems. This has laid the groundwork for reducing total processing time by 50%.

» The Office of Retirement Services is diligently working on a year 2000 plan to assure our computer hardware and software will be ready for the new millennium and beyond so that the customers of ORS will receive benefits and information in a timely manner.

» A pension milestone was reached in August 1998 - an annualized $2 billion in combined pension payments for State retirees, Public School retirees, State Police retirees, and retired Judges. The $1 billion mark was reached just eight years ago. This trend reinforces our ranking as the 19th largest public retirement system in the nation based on assets.

Letter of Transmittal (Continued)

CERTIFICATE OF ACHIEVEMENT

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to MSERS for its comprehensive annual financial report (CAFR) for the fiscal year ended September 30, 1997. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government financial reports.

In order to be awarded the Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and are submitting it to the GFOA.

FINANCIAL INFORMATION

Additions to Plan Net Assets

The reserves needed to finance retirement and health benefits are accumulated through the collection of employer contributions and through earnings on investments. Contributions and net investment income for fiscal year 1998 totaled approximately $981 million. Net investment income accounted for 73% and employer contributions accounted for 26% of the total revenue.

Total contributions and net investment income decreased 53.6% from those of the prior year due primarily to decreased investment earnings. Employee contributions decreased 38.3%, employer contributions decreased 36.7% and net investment income decreased 57.8% from the prior year. The Investment Section of this report reviews the results of investment activity for 1998.

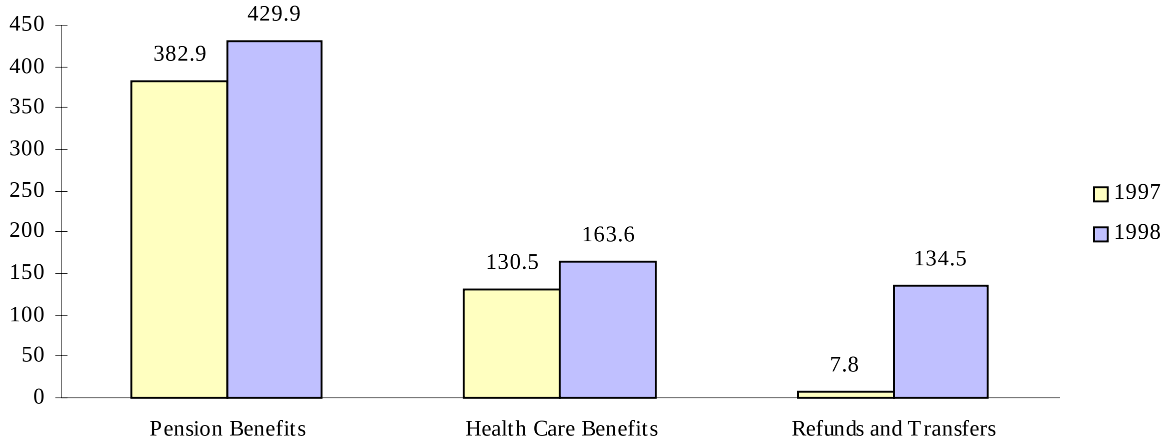
Additions to Plan Net Assets
(In Millions)

Letter of Transmittal (Continued)

Deductions From Plan Net Assets

The primary expenditures of the System include the payment of pension benefits to members and beneficiaries, payments for health, dental and vision benefits, refund of contributions to former members, and cost of administering the System. The growth of health care expenditures continued at a moderate rate during the year. As a result, expenditures for health care increased by $33.1 million from $130.5 million to $163.6 million during the fiscal year. Total deductions for fiscal year 1998 were $732.3 million, an increase of 39.1% over 1997 deductions. In connection with the early retirement plan, members could choose to transfer their retirement benefit to the defined contribution plan. That resulted in an increase of $126.7 million in transfers. Refunds were $18.6 thousand compared to $42.4 thousand in 1997.

Deductions from Plan Net Assets (In Millions)



Internal Control

The management of the System is responsible for maintaining a system of adequate internal accounting control designed to provide reasonable assurance that transactions are executed in accordance with management's general or specific authorization, and are recorded as necessary to maintain accountability for assets and to permit preparation of financial statements in accordance with generally accepted accounting principles. The internal control process is designed to provide reasonable assurance regarding the safekeeping of assets and reliability of all financial records.

INVESTMENT

The State Treasurer is the investment fiduciary and custodian of all investments of the System pursuant to state law. The primary investment objective is to maximize the rate of return on the total investment portfolio, consistent with a high degree of prudence and sufficient diversity to eliminate inordinate risks and to meet the actuarial assumption for the investment return rate. The investment activity for the year produced a total rate of return on the portfolio of 8.2%. For the last five years, the System has experienced an annualized dollar weighted rate of return of 12.9%. A summary of asset allocation and rates of return can be found in the Investment Section of this report.

Letter of Transmittal (Continued)

FUNDING

Funds are derived from the excess of additions to plan net assets over deductions from plan net assets. Funds are accumulated by the System in order to meet future benefit obligations to retirees and beneficiaries. The percentage computed by dividing the actuarial value of assets over the actuarial accrued liability is referred to as the "funded ratio." This ratio provides an indication of the funding status of the System and, generally, the greater this percentage, the stronger the System. As of September 30, 1998, the actuarial value of the assets and actuarial accrued liability of the fund were $9.1 billion and $8.4 billion respectively resulting in a funded ratio of 108.8%. As of September 30, 1997, the amounts were $7.5 billion and $8.2 billion. A historical perspective of funding levels for the System is presented on the Schedule of Funding Progress in the Required Supplementary Information in the Financial Section of this report.

PROFESSIONAL SERVICES

An annual audit of the System was conducted by Andrews, Hooper & Pavlik P.L.C., independent auditors. The auditors' report on the System's financial statements is included in the Financial Section of this report.

Statute requires an annual actuarial valuation be conducted. The purpose of the valuation is to evaluate the mortality, service, compensation and other financial experience of the System and to recommend employer funding rates for the subsequent year. This annual actuarial valuation was completed by the Segal Company for the fiscal years ended September 30, 1998 and 1997. Actuarial certification and supporting statistics are included in the Actuarial Section of this report.

ACKNOWLEDGMENTS

The preparation of this report was accomplished with the dedication and cooperation of many people. It is intended to provide complete and reliable information as a basis for making management decisions, as a means of determining compliance with legal provisions, and as a means for determining responsible stewardship of the funds of the System.

We would, therefore, like to express our appreciation for the assistance given by staff, the advisors and many people who contributed to its preparation. We believe their combined efforts have produced a report that will enable the employer and plan members to better evaluate and understand the Michigan State Employees' Retirement System. Their cooperation contributes significantly to the success of MSERS.

Sincerely,

Janet E. Phipps

Janet E. Phipps, Director
Department of Management and Budget

Christopher M. DeRose

Christopher M. DeRose, Director
Office of Retirement Services

Administrative Organization

Retirement Board Members

R. Douglas Trezise, Chair
Retiree Member
Term Expires July 31, 2000

Janine Winters
Employee Member
Term Expires July 31, 2000

Janet McCelland
Employee Member
Term Expires July 31, 1999

Roy Pentilla
Representing State Treasurer
Statutory Member

George M. Elworth
Representing Attorney General
Statutory Member

D. Daniel McLellan
Representing State Personnel Director
Statutory Member

Dr. James S. Neubecker, C.P.A.
Deputy Auditor General
Statutory Member

John Schoonmaker
Representing State Insurance Commissioner
Statutory Member

Administrative Organization

Department of Management and Budget
Office of Retirement Systems
Third Floor, Wing A, General Office Building
7150 Harris Drive
P.O. Box 30171, Lansing, Michigan 48909-7671
(517) 322-5103
1-800-381-5111

Advisors and Consultants

Actuary
The Segal Company
Michael J. Karlin, F.S.A., M.A.A.A.
New York, New York

Auditors
Thomas H. McTavish, C.P.A.
Auditor General
State of Michigan

Andrews, Hooper & Pavlik P.L.C.
Jeffrey J. Fineis, C.P.A.
Okemos, Michigan

Investment Manager and Custodian
Douglas B. Roberts
State Treasurer
State of Michigan

Legal Advisor
Frank J. Kelley
Attorney General
State of Michigan

Investment Performance Measurement
Capital Resource Advisors
Chicago, Illinois

Administrative Organization

Organization Chart

Department of Management & Budget
Janet E. Phipps, Director

Office of
Retirement Services
Christopher M. DeRose, Director

- **Finance & Administration**
  Deborah A. Gearhart
- **Operations**
  Phillip J. Stoddard
- **Information Technology & Reengineering**
  Ginger Bomar
- **Customer Service**
  Laurie Hill

FINANCIAL SECTION

Independent Auditors' Report
Statements of Plan Net Assets
Statements of Changes in Plan Net Assets
Notes to Financial Statements
Required Supplementary Information
Supporting Schedules

Independent Auditors' Report

ANDREWS HOOPER & PAVLIK P.L.C.

4295 Okemos Road, Suite 200 • Okemos, Michigan 48864

Ms. Janet Phipps, Director
Department of Management and Budget
Mr. Thomas H. McTavish, CPA
Auditor General
Michigan State Employees
Retirement System Board:

We have audited the accompanying statements of pension plan and postemployment healthcare plan net assets of the Michigan State Employees Retirement System, as of September 30, 1998 and 1997, and the related statements of changes in pension plan and post-employment healthcare plan net assets for the years then ended. These financial statements are the responsibility of the management of the Michigan State Employees Retirement System. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and *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 significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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 State Employees Retirement System, as of September 30, 1998 and 1997, and the changes in plan net assets for the years then ended in conformity with generally accepted accounting principles.

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The required supplementary information and supporting schedules listed in the table of contents are presented for the purpose of additional analysis and are not a required part of the basic financial statements. The required supplementary information and supporting schedules are the responsibility of the System's management. The Schedules of Funding Progress and Employer Contributions and related notes on pages 26 to 28 and the supporting schedules on pages 30 and 31 have been subjected to the auditing procedures applied in our audits of the basic financial statements and, in our opinion, are fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole. The Year 2000 information on page 29 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 supplementary information. However, we did not audit the information and do not express an opinion on it. In addition, we do not provide assurance that Michigan State Employees Retirement System is or will become year 2000 compliant, that Michigan State Employees Retirement System year 2000 remediation efforts will be successful in whole or in part, or that parties with which Michigan State Employees Retirement System does business are or will become year 2000 compliant.

In accordance with *Government Auditing Standards*, we have also issued a report dated February 4, 1999 on our consideration of the Michigan State Employees Retirement System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts.

Andrews Hooper & Pavlik P.L.C.

February 4, 1999

Okemos 517 487-5000 • Fax 517 487-9535 / Saginaw 517 497-5300 • Fax 517 497-5353

Statements of Pension Plan and Postemployment Healthcare Plan Net Assets

	As of September 30, 1998			As of September 30, 1997		
	Pension Plan	Health Plan	Total	Pension Plan	Health Plan	Total
Assets:						
Cash	$ 22,580,235	$ 187,946	$ 22,768,181	$ 15,186,520	$ 195,692	$ 15,382,212
Receivables:						
Amounts due from employees				1,063	14	1,077
Amounts due from employers	12,871,636	107,137	12,978,773	26,516,832	341,693	26,858,525
Interest and dividends	37,348,476	310,870	37,659,346	41,454,637	534,180	41,988,817
Sale of investments	6,379,151	53,097	6,432,248	9,340,952	120,367	9,461,319
Total receivables	56,599,263	471,104	57,070,367	77,313,484	996,254	78,309,738
Investments:						
Short-term investments	354,151,709	2,947,779	357,099,488	832,135,795	10,722,823	842,858,618
Bonds, notes, mortgages and preferred stock	2,259,065,931	18,803,318	2,277,869,249	2,222,674,424	28,641,171	2,251,315,595
Common stock	4,474,637,606	37,244,613	4,511,882,219	4,096,762,785	52,790,495	4,149,553,280
Real estate	751,798,004	6,257,585	758,055,589	561,888,399	7,240,440	569,128,839
Alternative investments	809,358,964	6,736,693	816,095,657	571,677,636	7,366,584	579,044,220
International investments	372,719,070	3,102,324	375,821,394	462,070,902	5,954,202	468,025,104
Collateral on loaned securities	377,603,702	3,142,982	380,746,684	318,778,742	4,107,752	322,886,494
Total investments	9,399,334,986	78,235,294	9,477,570,280	9,065,988,683	116,823,467	9,182,812,150
Equipment (net of depreciation)	0	0	0	578	7	585
Total assets	9,478,514,484	78,894,344	9,557,408,828	9,158,489,265	118,015,420	9,276,504,685
Liabilities:						
Warrants outstanding	(2,914,772)	(24,261)	(2,939,033)	(3,413,655)	(43,989)	(3,457,644)
Accounts payable and and accrued liabilities	(14,339,268)	(119,353)	(14,458,621)	(38,746,007)	(499,278)	(39,245,285)
Obligations under securties lending	(377,603,702)	(3,142,982)	(380,746,684)	(318,778,742)	(4,107,752)	(322,886,494)
Total liabilities	(394,857,742)	(3,286,596)	(398,144,338)	(360,938,404)	(4,651,019)	(365,589,423)
Net Assets Held in Pension and Health Benefits*	$9,083,656,742	$ 75,607,748	$9,159,264,490	$8,797,550,861	$ 113,364,401	$8,910,915,262

*A schedule of funding progress is presented in the Required Supplementary Information in the Financial Section.

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

Statements of Changes in Pension Plan and Postemployment Healthcare Plan Net Assets

For Years Ended September 30, 1998 and 1997

	For year ended September 30, 1998			For year ended September 30, 1997		
	Pension Plan	Health Plan	Total	Pension Plan	Health Plan	Total
Additions:						
Members contributions:						
Other	$ 3,735,468	$ 4,619,101	$ 8,354,569	$ 7,229,118	$ 3,714,213	$ 10,943,331
Military	1,423,276		1,423,276	4,915,035		4,915,035
Employer contributions	147,599,551	112,199,628	259,799,179	288,590,215	121,641,412	410,231,627
Investment income:						
Investment income	708,481,812		708,481,812	1,679,743,639		1,679,743,639
Securitites lending income	16,584,243		16,584,243	11,803,417		11,803,417
Real estate operating expenses	(646,133)		(646,133)	(311,903)		(311,903)
Securities lending expenses	(16,053,905)		(16,053,905)	(11,412,796)		(11,412,796)
Other investment expenses	(6,308,082)		(6,308,082)	(2,042,558)		(2,042,558)
Interest income		8,998,673	8,998,673		7,546,437	7,546,437
Miscellaneous income	381		381	272		272
Total additions	854,816,611	125,817,402	980,634,013	1,978,514,439	132,902,062	2,111,416,501
Deductions:						
Retirement allowances	429,879,875		429,879,875	382,866,379		382,866,379
Employer share of health insurance		148,458,180	148,458,180		115,670,352	115,670,352
Employer share of dental/vision insurance		15,115,875	15,115,875		14,822,508	14,822,508
Refunds of member contributions	18,555		18,555	42,388		42,388
Transfers to other systems	134,515,208		134,515,208	7,806,261		7,806,261
Administrative	4,297,092		4,297,092	5,247,943		5,247,943
Total deductions	568,710,730	163,574,055	732,284,785	395,962,971	130,492,860	526,455,831
Net Increase (Decrease)	286,105,881	(37,756,653)	248,349,228	1,582,551,468	2,409,202	1,584,960,670
Net Assets Held in Trust for Pension and Healthcare Benefits:						
Beginning of Year	8,797,550,861	113,364,401	8,910,915,262	7,214,999,393	110,955,199	7,325,954,592
End of Year*	$9,083,656,742	$ 75,607,748	$9,159,264,490	$8,797,550,861	$ 113,364,401	$8,910,915,262

* A schedule of funding progress is presented in the required supplementary information in the Financial Section.
The accompanying notes are an integral part of these financial statements.

Notes to General Purpose Financial Statements

NOTE 1 - PLAN DESCRIPTION

ORGANIZATION

The Michigan State Employees' Retirement System (MSERS) is a multiple employer, state-wide, defined benefit public employee retirement plan governed by the State of Michigan (State) and created under Public Act 240 of 1943, as amended. MSERS was established by the State to provide retirement, survivor and disability benefits to the State's government employees. MSERS is a qualified trust fund under section 401(a) of the Internal Revenue Code. By statute, employees of the following employers are also covered by this plan: American Legion, American Veterans, Disabled American Veterans, Probate Judges, Mackinac Island State Park, Marine Corps League, Michigan Bar Association, Michigan Veterans Trust Fund, Military Order of the Purple Heart, Commission for Independent Vendors, Third Circuit Court, Recorders Court and 36th District Court. Michigan judges and elected officials, legislators, national guard and state police officers are covered by separate retirement plans.

MSERS' financial statements are included as a pension trust fund in the combined financial statements of the State of Michigan.

MSERS operates within the Michigan Department of Management and Budget, Office of Retirement Services. The Department Director appoints the Office Director who serves as Executive Secretary to the MSERS' Board, with whom the general oversight of the System resides. The State Treasurer serves as the investment officer and custodian for the System.

MEMBERSHIP

At September 30, 1998 and 1997, the System's membership consisted of the following:

Retirees and beneficiaries currently receiving benefits:	1998	1997
Regular benefits	28,480	28,648
Survivor benefits	4,928	4,739
Disability benefits	2,777	2,736
Total	36,185	36,123
Current employees:		
Vested	35,235	33,925
Non-vested	14,482	21,509
Total	49,717	55,434
Inactive employees entitled to benefits and not yet receiving them	8,021	7,656
Total All Members	93,923	99,213

Enrollment in the health care fund is voluntary. The number of participants is as follows:

Health/Dental/Vision Plan	1998	1997
Eligible participants	36,185	36,123
Participants receiving benefits:		
Health	33,384	33,299
Dental	32,468	32,300
Vision	32,654	32,494

Notes to General Purpose Financial Statements

BENEFIT PROVISIONS

Introduction

Benefit provisions of the defined benefit pension plan are established by state statute, which may be amended. Public Act 240 of 1943, State Employees' Retirement Act, as amended, establishes eligibility and benefit provisions for the defined benefit pension plan. Retirement benefits are determined by final average compensation and years of service. Members are eligible to receive a monthly benefit when they meet certain age and service requirements. MSERS also provides duty disability, non-duty disability and survivor benefits.

Members who separated from employment may request a refund of his or her member contribution account. (MSERS is currently non-contributory.) A refund cancels a former member’s rights to future benefits. Former members who return to employment and who previously received a refund of their contributions may reinstate their service through repayment of the refund upon satisfaction of certain requirements.

Effective March 31, 1997, Public Act 487 of 1996 closed the plan to new entrants. All new employees become members of the defined contribution plan. The Public Act allows returning employees and members who left state employment on or before March 31, 1997, to elect the defined benefit plan instead of the defined contribution plan.

Regular Retirement

The retirement benefit is based on a member’s years of credited service (employment), age, and final average compensation. The normal benefit equals 1.5% of a member’s final average compensation multiplied by the years of credited service and is payable monthly over the member's lifetime.

Final average compensation is the average of a member’s monthly pay during 36 consecutive months of credited service. The 36 consecutive month period producing the highest monthly average is used. For most members, this is the last three years of employment.

A member may retire and receive a monthly benefit after attaining:

1. age 60 with 10 or more years of credited service; or
2. age 55 with 30 or more years of credited service; or
3. age 55 with at least 15 but less than 30 years of credited service. The benefit allowance is permanently reduced 0.5% for each month from the member’s age on the effective date of retirement to the date the member will attain age 60.

Employees in covered positions are eligible for supplemental benefits and may retire after attaining:

1. age 51 with 25 or more years in a covered position; or
2. age 56 with 10 or more years in a covered position.

In either case, the three years immediately preceding retirement must have been in a covered position. Employees in covered positions are responsible for the custody and supervision of inmates.

Employees of closing Department of Community Health facilities are eligible for retirement under one of the following conditions:

1. age 51 with 25 years of service, the last 5 of which were rendered in the closing facility;
2. age 56 with 10 years of service, the last 5 of which were rendered in the closing facility; or
3. 25 years of service at the closing facility regardless of age.

Notes to General Purpose Financial Statements

Employees of the State Accident Fund, Michigan Biologic Products or Liquor Control Commission who were terminated as the result of privatization may retire if the member's age and length of service was equal to or greater than 70 on the date of transfer or termination.

Conservation Officers (CO) with a hire date on or before April 1, 1991, are eligible to retire after 25 years of service, 20 of which must have been rendered as a CO. CO's hired after April 1, 1991 and before March 31, 1997, must have 23 years of service as a CO to be eligible for a full retirement with only 25 years of service. In either case, 2 years immediately preceeding retirement must be as a CO.

Deferred Retirement

Any member with 10 or more years of credited service who terminates employment but has not reached the age of 60 is a deferred member and is entitled to receive a monthly pension upon reaching age 60, provided the member's accumulated contributions have not been refunded. Deferred retirement is available after 5 years of service for State employees occupying unclassified positions in the executive and legislative branches and certain Department of Community Health employees subject to reduction in force lay-offs by reason of deinstitutionalization.

Non-Duty Disability Benefit

A member with 10 or more years of credited service who becomes totally and permanently disabled not due to performing duties as a state employee is eligible for a non-duty disability pension. The non-duty disability benefit is computed in the same manner as an age and service allowance based upon service and salary at the time of disability.

Duty Disability Benefit

A member who becomes totally and permanently disabled from performing duties as a state employee as a direct result of state employment and who has not met the age and service requirement for a regular pension, is eligible for a duty disability pension. If the member is under age 60, the duty disability allowance is a maximum payment of $6,000 payable annually. At age 60 the benefit is recomputed under service retirement.

Survivor Benefit

Upon the death of a member who was vested, the surviving spouse shall receive a benefit calculated as if the member had retired the day before the date of death and selected Option A (see below). Certain designated beneficiaries can be named to receive a survivor benefit.

Pension Payment Options

When applying for retirement, an employee may name a person other than his or her spouse as a beneficiary if the spouse waives this right. If a beneficiary is named, the employee must choose whether the beneficiary will receive 100% or 50% of the retiree's pension benefit after the retiree's death. The decision is irrevocable. A description of the options follows.

<u>Regular Pension</u> — The pension benefit is computed with no beneficiary rights. If the retiree made contributions while an employee and has not received the total accumulated contributions before death, a refund of the balance of the contributions is made to the beneficiary of record. If the retiree did not make any contributions, there will not be payments to beneficiaries.

<u>Option A (100% survivor)</u> — Under this option, after the retiree's death, the beneficiary will receive 100% of the pension for the remainder of the beneficiary's lifetime. If this option is elected, the normal retirement benefit is reduced by a factor based upon the ages of the retiree and of the beneficiary. If the beneficiary predeceases the retiree, the pension "pops-up" to the regular pension amount; another beneficiary cannot be named.

Notes to General Purpose Financial Statements

Option B (50% survivor) — Under this option, after the retiree's death, the beneficiary will receive 50% of the pension for the remainder of the beneficiary's lifetime. If this option is elected, the normal retirement benefit is reduced by a factor based upon the ages of the retiree and of the beneficiary. The reduction factor is lower than the factor used in Option A above. If the beneficiary predeceases the retiree, the pension "pops-up" to the regular pension amount; another beneficiary cannot be named.

Equated Pension — An equated pension may be chosen by any member under age 65 except a disability retiree and an early supplemental retiree. Equated pensions provide an additional amount until age 65 and may be combined with Regular, Option A or B. At age 65 the monthly amount is permanently reduced. The initial and reduced amounts are based on an estimate of social security benefits at age 65. Social security benefits are estimated by using age, final salary average, and State service. The actual amount received from social security may vary from the estimate.

Post Retirement Adjustments

One time upward benefit adjustments were made in 1972, 1974, 1976, 1977 and 1987. Beginning October 1, 1988, a 3% non-compounding increase, up to a maximum of $25 monthly, is paid each October to recipients who have been retired 12 full months. Beginning in 1983, eligible benefit recipients share in a distribution of investment income earned in excess of 8% annually. This distribution is known as the supplemental payment. The supplemental payment is offset by one year's cumulative increases received after the implementation of the annual 3% increase in benefits. These adjustment payments were not issued during fiscal years 1991 through 1994. Members who retired on or after October 1, 1987, are not eligible for the supplemental payment.

Contributions

Member Contributions — Members currently participate in MSERS on a noncontributory basis. Under certain circumstances, members may contribute to the System for the purchase of creditable service, such as military service or maternity leave. If a member terminates MSERS covered employment before a retirement benefit is payable, the member's contribution and interest on deposit may be refunded. If the member dies before being vested, the member's contribution and interest are refunded to the designated beneficiaries.

Employer contributions — The statute requires the employer to contribute to finance the benefits of plan members. These employer contributions are determined annually by the System's actuary and are based upon level-percent-of-payroll funding principles so the contribution rates do not have to increase over time.

Early Retirement

Public Act 487 of 1996 provided an opportunity for employees to retire early if they met certain age and years of service requirements. To take advantage of the early retirement plan, an employee had to apply on or after March 1, 1997, but no later than April 30, 1997. The effective date of retirement had to be on or after April 1, 1997, but no later than June 1, 1997. Under certain circumstances, the effective date of retirement could be between June 1, 1997 and December 31, 1998. The plan included an incentive in the benefit calculation. The benefit was calculated by multiplying the final average compensation by 1.75% (instead of 1.5%) and the years of service. State employees may work until June 1, 1998 and legislative employees may work until December 31, 1998.

Transfers to Defined Contribution Plan

During fiscal year 1998, the MSERS Retirement Act provided members an opportunity to transfer to the defined contribution plan. This was a one-time opportunity and the decision is irrevocable. The transfer was completed by September 30, 1998. A total of 1,469 vested individuals with funds totaling $133,940,854 were transferred. In addition 1,927 non vested individuals with no funds were transferred. With the passage of the legislation permitting the transfer, the System also became a closed system. All new employees are members of the defined contribution plan.

Notes to General Purpose Financial Statements

Other Post Employment Benefits

Under the State Employees Retirement Act, all retirees have the option of receiving health, prescription, dental and vision coverage. The employer funds health benefits on a pay-as-you-go basis. Retirees with this coverage contribute 5% and 10% of the monthly premium amount for the health, dental and vision coverage, respectively. The employer's payroll contribution rate to provide this benefit was 5.0% and 4.8% for fiscal years 1998 and 1997 respectively.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting and Presentation

MSERS' financial statements are prepared using the accrual basis of accounting. Contributions from the State are recognized as revenue in the period in which employees provide service. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Reserves

Public Act 240 of 1943, as amended, created the employees' savings reserve, employer's accumulation reserve, pension reserve, income account, expense account, and health insurance reserve. The financial transactions of the plan are recorded in these accounts as required by Public Act 240 of 1943, as amended.

<u>Employees' Savings Reserve</u> — Members no longer contribute to this fund except to purchase eligible service credit or repay previously refunded contributions. This fund represents active member contributions and interest less amounts transferred to the Pension Reserve for regular and disability retirement, amounts refunded to terminated members and unclaimed amounts transferred to the income account. At September 30, 1998, and 1997, the balance in this account was $2.1 million and $3.3 million respectively.

<u>Pension Reserve</u> — This represents the reserves for payment of future retirement benefits to current retirees. At retirement, a member's accumulated contributions plus interest are transferred into this reserve from the Employee's Savings Reserve. 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 Employer Accumulation Reserve to this reserve to bring the balance into balance with the actuarial present value of retirement allowances. At September 30, 1998 and 1997, the balance in this account was $4.2 billion and $3.3 billion respectively.

<u>Employer Accumulation Reserve</u> — All employer contributions are credited to this reserve. Interest from the income account is credited annually. Amounts are transferred annually from this reserve to the Pension Reserve to fund that reserve. At September 30, 1998 and 1997, the balance in this account was $3.0 billion and $3.7 billion respectively.

<u>Income Account and Expense Account</u> — The income account is credited with all investment earnings. Interest is transferred annually to the reserves. Administrative expenses are paid from the expense account. The legislature appropriates the funds necessary to defray and cover the administrative expense of the plan. At September 30, 1998 and 1997, the net balance of these accounts was $1.9 billion and $1.8 billion respectively.

<u>Health Insurance Reserve</u> — This fund is credited with employee and employer contributions for retirees' health, dental and vision benefits. Premiums for health, dental and vision benefits are paid from this fund. At September 30, 1998 and 1997, the balance in this account was $75.6 million and $113.4 million respectively.

Fair Value of Investments

Plan investments are reported at fair value, except for short-term investments. Short-term investments are carried at cost, which approximates fair value. Securities traded on a national or international 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. Real estate debt is valued on the basis of future

Notes to General Purpose Financial Statements

principal and interest payments, and is discounted at prevailing interest rates for similar instruments. The fair value of real estate investments is based on independent appraisals. Other investments not having an established market are recorded at estimated fair value.

Reporting Entity

MSERS is a pension trust fund of the State of Michigan. As such, MSERS is considered part of the State and is included in the State's comprehensive annual financial report as a pension trust fund. MSERS and the MSERS' board are not financially accountable for any other entities or other organizations. Accordingly, MSERS is the only entity included in this financial report.

Investment Income

Dividend income is recognized based 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 (the date upon which the transaction is initiated), except for purchase and sale of mortgages, real estate, and alternative investments which are recorded as of the settlement date (the date upon which the transaction is ultimately completed). The effect of recording such transactions as of the settlement date does not materially affect the financial statements.

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 and Postemployment Heathcare Plan Net Assets. Such assets are depreciated on a straight line basis over 10 years. As of September 30, 1998, all capitalized equipment was fully depreciated.

Related Party Transactions

Leases and services — The Retirement System leases operating space and purchases certain administrative, data processing, legal and investment services from the State. The space and services are not otherwise available by competitive bid. The following summarizes costs incurred by MSERS for such services.

	1998	1997
Building rentals	$ 92,750	$ 117,071
Data processing services	1,061,241	1,197,252
Legal	270,300	158,410
Investment	1,408,508	1,745,236

Common Cash — The cash account includes $22,768,181 and $15,382,212, on September 30, 1998, and 1997, 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 $2,274,104 and $2,931,025 for the years ended September 30, 1998 and 1997, respectively.

Reclassification of Prior Year Amounts

Certain prior year amounts have been reclassified or restated to conform with the current year presentation.

Notes to General Purpose Financial Statements

NOTE 3 - CONTRIBUTIONS

Members currently participate in MSERS on a non-contributory basis. Under certain circumstances, members may contribute to the System for the purchase of creditable service such as military service or maternity leave. Effective August 1, 1998, the retirement act was amended to permit a "universal buy-in". With a universal buy-in, a member may elect to purchase no more than 5 years of service credit (less other service credit purchased). The State is required by Public Act 240 of 1943, as amended, to contribute amounts necessary to finance the benefits of its employees. Contribution provisions are specified by state statute and may be amended only by action of the state legislature.

Periodic employer contributions to MSERS 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 unfunded actuarial accrued liability is funded over a 38-year period (remaining) for the 1997-98 fiscal year.

Actual employer contributions paid for retirement benefits for the year were $147,599,551 and $288,590,215, representing 7.0% and 12.7% of annual covered payroll, for the years ended September 30, 1998, and 1997, respectively. Required employer contributions for pensions included:

1. $185,845,073 and $229,502,829 for fiscal years 1998 and 1997, respectively, for normal cost of pensions representing 8.2% and 9.1% (before reconciliation), respectively, of annual covered payroll.

2. ($59,448,893) and $20,295,693 for fiscal years 1998 and 1997, respectively, for amortization of (overfunded)unfunded actuarial liability, representing (2.62%) and 0.8% (before reconciliation), respectively, of annual covered payroll.

The fund is required to reconcile actuarial requirements annually. Any funding excess or deficiency is included in the subsequent years appropriation request, and is not recognized as a payable or receivable in the accounting records. Based on this reconciliation and other adjustments, the differences are smoothed over 5 years.

NOTE 4 - INVESTMENTS

Investment Authority

Under Public Act 380 of 1965, as amended, the authority for the purchase and the sale of investments resides with the State Treasurer. Investments are made subject to the Michigan Public Pension Investment Act, Public Act 314 of 1965, as amended. The Michigan Public Pension Investment Act authorizes, with certain restrictions, the investment of pension fund assets in stock, corporate and government bonds and notes, mortgages, real estate, and certain short-term and alternative investments. Investments must be made for the exclusive purposes of providing benefits to active members, retired members and beneficiaries, and of defraying the expenses of investing the assets.

Under Public Act 314 of 1965 up to 5% of the System’s assets may be invested in alternative investments and up to 15% of the System’s assets may be invested in investments not otherwise qualified under the act. Alternative investments include limited partnerships and distributions from these partnerships in the form of bonds, common stock and preferred stock.

Derivatives

The State Treasurer does not employ the use of derivatives in the investment of Common Cash or the investment of trust funds other than the pension trust funds.

Notes to General Purpose Financial Statements

Derivatives are used for a small amount of the pension trust fund portfolios. However, derivatives are not used for speculation and they are not used to leverage the investment portfolios. Less than 6% of the total pension trust fund's portfolio has been invested from time to time in future contracts, collateralized mortgages and swap agreements. Swap agreements represent the largest category of derivatives used, and represented 4.1% of the total portfolio at market values.

To further diversify the pension fund's portfolio into international equities, the State Treasurer has entered into swap agreements with investment grade counterparties which are tied to stock market indices in eighteen foreign countries. The notional amounts of the swap agreements at September 30, 1998 and 1997, were $383.3 million and $389.1 million, respectively. One half of the notional amount is hedged against foreign currency fluctuations. The swap agreements provide that the retirement systems will pay quarterly, over the term of the swap agreements, interest indexed to the three month London Inter Bank Offer Rate (LIBOR), adjusted for an interest rate spread, on the notional amount stated in the agreements. At the maturity of the swap agreements the pension fund will either receive the increase in the value of the international equity indices from the level of the indices at the inception of the agreements, or pay the decrease in the value of the indices. Swap agreement maturities range from October, 1998 to December, 2001.

U.S. domestic LIBOR based floating rate notes were purchased in the open market to correspond with the notional amount of the swap agreements. The State Treasurer maintains custody and control of these notes.

The value of these synthetic equity structures is a combination of the value of the swap agreements and the value of the notes. The book value represents the cost of the notes. The current value represents the current value of the notes and the change in value of the underlying indices from the inception of the swap agreements. The current value is used as a representation of the fair value based upon the intention to hold all swap agreements until maturity. Since the inception of the international equity investment program, over $109.2 million of gains on international equity exposure and excess interest received have been realized. The unrealized loss of $15.2 million at September 30, 1998 reflects the decrease in international indices and higher notional cost levels following realization of gains in the months prior to September.

The respective September 30, 1998 and 1997 values are as follows:

	Notional Value	Book Value	Current Value
9/30/98 (dollars in millions)	$383.3	$391.0	$375.8
9/30/97 (dollars in millions)	389.1	385.3	468.0

Investments Exceeding 5% of Plan Net Assets

MSERS did not hold an individual investment (other than U.S. Government securities) that exceeded 5% of net assets available for benefits at September 30, 1998 or 1997.

Securities Lending

State statutes do not prohibit the retirement system from participating in securities lending transactions, and the retirement system has, via a Securities Lending Authorization Agreement, authorized the agent bank to lend its securities to broker-dealers and banks pursuant to a form of loan agreement.

Notes to General Purpose Financial Statements

During the fiscal year, the agent bank lent, at the direction of the retirement system, the retirement system's securities and received cash (United States and foreign currency), securities issued or guaranteed by the United States government, sovereign debt rated A or better, convertible bonds, and irrevocable bank letters of credit issued by a person other than the borrower or an affiliate of the borrower as collateral. The agent bank did not have the ability to pledge or sell collateral securities delivered absent a borrower default. Borrowers were required to deliver collateral for each loan equal to: (i) in the case of loaned securities denominated in United States dollars or whose primary trading market was located in the United States or sovereign debt issued by foreign governments, 102% of the market value of the loaned securities; and (ii) in the case of loaned securities not denominated in United States dollars or whose primary trading market was not located in the United States, 105% of the market value of the loaned securities.

The retirement system did not impose any restrictions during the fiscal year on the amount of the loans the agent bank made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during the fiscal year. Moreover, there were no losses during the fiscal year resulting from a default of the borrowers or the agent bank.

During the fiscal year, the retirement system and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified tax-exempt plan lenders, in a collective investment pool. As of September 30, 1998, such investment pool had an average duration of 64 days and an average weighted maturity of 504 days. Because the loans were terminable at will, their duration did not generally match the duration of the investments made with cash collateral. On September 30, 1998, the retirement system had no credit risk exposure to borrowers. The collateral held and the market value of securities on loan for the retirement system as of September 30, 1998, were $393,881,586 and $378,778,528 repectively. Gross income from security lending for the fiscal year was $16,584,243. Expenses associated with this income amounted to $15,877,085 for the borrower's rebate and $176,820 for fees paid to the agent.

Categories of Investment Risk

Investments made by the fund, including repurchase agreements and information concerning reverse repurchase agreements, are summarized below. The investments represented by specific identifiable investment securities are classified as to credit risk in three categories.

Category 1 includes investments insured, registered, or held by MSERS or its agent in MSERS' name. Category 2 includes uninsured and unregistered investments held by the counterparty's trust department or agent in MSERS' name. Category 3 includes uninsured and unregistered investments held by the counterparty, its trust department, or agent, but not in MSERS' name.

At September 30, 1998, all investments of the pension trust fund were classified as Category 1, except for certain investments not categorized.

Notes to General Purpose Financial Statements

The following table summarizes the investments:

Category 1	1998	1997
Prime Commercial Paper	$ 238,323,470	$ 689,794,068
Short Term Note	118,776,018	153,064,550
Government Securities	983,355,193	1,148,962,267
Corporate Bonds & Notes	936,961,950	845,339,668
Convertible Bonds	0	4,183,670
Preferred Stock	255,930	120,928
Equities	4,370,500,542	4,004,306,139
Real Estate	68,418,133	62,319,556
Alternative Investments	30,398,933	28,438,453
Derivatives (International)	375,821,394	468,025,104
Total Category 1	**$** 7,122,811,563	$ 7,404,554,403
Non-Categorized		
Private Placements	$ 98,098,045	$ 36,803,001
Mortgages	34,617,940	47,294,284
Real Estate	689,637,456	506,809,283
Alternative Investments	785,696,724	550,605,767
Cash Collateral	380,746,684	322,886,494
Securities on Loan:		
U.S. Government Securities	205,666,662	167,459,252
Corporate Bonds and Notes	18,913,533	1,152,525
Equities	141,381,677	145,247,141
Total Non-Categorized	**$** 2,354,758,717	$ 1,778,257,747
Grand Total	$ 9,477,570,280	$ 9,182,812,150

NOTE 5 - 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. 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.

Required Supplementary Information

Schedule of Funding Progress
(Amounts in Millions)

Expressing the net assets available for benefits as a percentage of the actuarial accrued liability provides one indication of MSERS' funding status. 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 or overfunded actuarial accrued liability as a percentage of annual covered payroll approximately adjusts for the effects of inflation and aids analysis of progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the system.

Retirement Benefits ($ in Millions)

Valuation Date Sept 30	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)[1] (b)	Unfunded (Overfunded) Accrued Liability (UAAL) (b-a)	Funded Ratio AAL (a/b)	Covered Payroll (c)	UAAL as a % of Covered Payroll ((b-a)/c)
1989	3,928	3,967	39	99.0	2,066	1.9
1990[#]	4,106	4,464	358	92.0	2,306	15.5
1991	4,347	4,939	592	88.0	2,315	25.6
1992	4,534	5,480	946	82.7	2,266	41.8
1993[+]	5,043	6,172	1,129	81.7	2,261	49.9
1994	5,476	6,560	1,084	83.5	2,351	46.1
1995	6,090	6,861	771	88.8	2,431	31.7
1996	6,678	7,147	469	93.4	2,515	18.6
1997	7,515	8,213	698	91.5	2,273	30.7
1997#	8,834	8,100	(734)	109.1	2,273	(32.3)
1998	9,109	8,374	(735)	108.8	2,108	(34.9)

(1) Based on entry age normal actuarial method.
Benefits amended.
+ Revised asset valuation method.
# Revised actuarial assumptions and revised asset valuation method.

Required Supplementary Information (Continued)

Schedule of Employer Contributions

Fiscal Year Ending Sept. 30	Annual Required Contribution (ARC)	Actual Contribution	Percentage Contributed
1989	$ 141,862,851	$ 113,348,418	79.9 %
1990	160,367,963	123,964,435	77.3
1991	195,590,162	154,125,048	78.8
1992	215,470,500	187,028,394	86.8
1993	219,912,052	246,961,234	112.3
1994	230,231,706	263,845,535	114.6
1995	260,769,716	306,404,416	117.5
1996	262,682,020	286,060,720	108.9
1997	229,502,829	288,590,215	125.7
1998	185,845,073	147,599,551	79.4

Notes to Required Supplemental Information

NOTE A - DESCRIPTION

Ten year historical trend information designed to provide information about MSERS' progress made in accumulating sufficient assets to pay benefits when due is presented in the preceding schedules. Other ten year historical trend information related to the pension plan is presented in the Statistical and Actuarial Sections of the report. This information is presented to enable the reader to assess the progress made by MSERS 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 obligation as a factor.

The Schedule of Funding Progress and Schedule of Employer Contributions are reported as historical trend information. The Schedule of Funding Progress is presented to measure the progress being made to accumulate sufficient assets to pay benefits when due. The Schedule of Employer Contributions is presented to show the responsibility of the Employer in meeting the actuarial requirements to maintain the System on a sound financial basis.

NOTE B - SUMMARY OF ACTUARIAL ASSUMPTIONS

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.

Valuation Date	09/30/98
Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Percent of Payroll, Closed
Remaining Amortization Period	38 Years
Asset Valuation Method	5-Year Smoothed Market
Actuarial Assumptions:	
Inflation Rate	3% next year, then 4%
Investment Rate of Return	8%
Projected Salary Increases	3% - 10.5%
Cost-of-Living Adjustments	3% Annual Non-Compounded with Maximum Annual Increase of $300 for those Eligible

Required Supplementary Information (Continued)

YEAR 2000

In October 1998, the Governmental Accounting Standards Board (GASB) issued Technical Bulletin 98-1, entitled *Disclosures about Year 2000 Issues.* The provisions of the GASB technical bulletin, as amended by Technical Bulletin 99-1, require the System to make disclosures about its readiness in addressing year 2000 issues for its computer systems and other electronic equipment.

The year 2000 issue is the result of shortcomings in the manner in which "year" information is stored and interpreted by many electronic data processing systems and other electronic equipment. Operations may be adversely affected if critical systems and equipment are not made year 2000 compliant. The year 2000 issue will impact not only internal operations, but also interactions with external parties such as other governmental entities and critical vendors. To address the year 2000 issues, the State established the Year 2000 Project Office within the Department of Management and Budget (DMB). The Year 2000 Project Office's mission is to lead, support, and facilitate achievement of year 2000 compliance throughout the state's executive branch to ensure uninterrupted service to Michigan's citizens. The Year 2000 Project Office is monitoring year 2000 compliance efforts at the various agencies and is providing assistance and assigning resources to accelerate compliance for all mission critical systems and equipment. Additional disclosure regarding the status of statewide systems year 2000 compliance efforts upon which MSERS is dependent can be found in the State of Michigan's Comprehensive Annual Financial Report.
MSERS' in conjunction with the Year 2000 Project Office, DMB, is subjecting those systems and equipment to the following stages of work to address year 2000 issues:

Awareness stage — Establishing a budget and project plan for dealing with the year 2000 issue.
Assessment stage — Identifying the systems and components for year 2000 compliance.
Remediation stage — Making changes to systems and equipment.
Validation/testing stage — Validating and testing the changes that were made during the remediation stage.

MSERS has identified the computer systems and electronic equipment that are critical to its operations, and the following is a summary of progress towards achieving year 2000 compliance:

Internal Systems:
Common Pension Payroll and TRKSERS -- MSERS has completed the assessment, remediation, validation and testing stages of these systems. In addition, in 1999 there will be additional testing of these systems and on other non-critical systems.

As of year-end, MSERS has a commitment to spend approximately $532 thousand to make critical computer systems and equipment year 2000 compliant.

External Factors:
There can be no assurance that organizations and governmental agencies with which MSERS interacts, including banks, vendors, customers, state and federal governments will be year 2000 compliant. With regard to these external organizations, MSERS is currently in the process of obtaining assurances that their systems will be ready for the year 2000. If issues are identified, action plans will be instituted as necessary. However, even if the systems of both are compliant in a timely manner, problems could arise with communications between systems if compliance is achieved through inconsistent approaches or methodologies.

Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that MSERS is or will be year 2000 ready, or that MSERS' remediation efforts have been successful in whole or in part. However, management believes that it has instituted a plan to minimize the impact that the year 2000 issue may have on critical operations.

Supporting Schedules

Comparative Summary Schedule of Pension Plan Administrative Expenses for the Years Ended September 30, 1998 and 1997

	1998	1997
Personnel Service:		
Staff salaries	$ 961,902	$1,081,072
Retirement and social security	173,691	223,825
Other fringe benefits	129,782	167,433
Total	1,265,375	1,472,330
Professional Services:		
Actuarial	138,202	62,315
Accounting, records management and mail	331,441	237,873
Data processing	1,061,241	1,197,252
Legal	270,300	158,410
Audit	34,745	30,438
Medical	157,884	195,289
Total	1,993,813	1,881,577
Building and Equipment:		
Building rentals	92,750	117,071
Equipment purchase, maintenance and rentals	26,576	156,221
Depreciation	586	586
Total	119,912	273,878
Miscellaneous:		
Customer Information Center	31,783	20,796
Office administrative support	59,474	59,030
Department administrative support	16,639	203,168
Travel and board meetings	4,660	13,544
Postage, telephone and other	805,436	1,323,620
Total	917,992	1,620,158
Total Administrative Expenses	$4,297,092	$5,247,943

Supporting Schedules (Continued)

Schedule of Investment Expenses

	1998	1997
Real Estate	$ 646,133	$ 311,903
Securities Lending Expense	16,053,905	11,412,796
Other	6,308,082	2,042,558
Total Investment Expenses	$23,008,120	$13,767,257

Schedule of Payments to Consultants

	1998	1997
Independent Auditors	$ 34,745	$ 30,438
Legal	270,300	158,410
Actuary	138,202	62,315
Total Payments	$ 443,247	$ 251,163

Supporting Schedules (continued)

Detail of Changes in Plan Net Assets (Pension and Postemployment Healthcare Benefits)

	For the Year Ended September 30, 1998					
	Employee Savings	Pension Reserve	Employer Accumulation	Income	Health Insurances	Total
Additions:						
Members contributions:						
Other	$ 3,735,468				$ 4,619,101	$ 8,354,569
Military	1,423,276					1,423,276
Employer contributions			$ 147,599,551		112,199,628	259,799,179
Investment income:						
Investment income				$ 708,481,812		708,481,812
Securitites lending income				16,584,243		16,584,243
Real estate operating expenses				(646,133)		(646,133)
Securities lending expenses				(16,053,905)		(16,053,905)
Other investment expenses				(6,308,082)		(6,308,082)
Interest income					8,998,673	8,998,673
Miscellaneous income				381		381
Total additions	5,158,744		147,599,551	702,058,316	125,817,402	980,634,013
Deductions:						
Benefits paid to plan members and beneficiaries:						
Retirement allowances		$ 429,879,875				429,879,875
Employer share of health insurance					148,458,180	148,458,180
Employer share of dental/vision insurance					15,115,875	15,115,875
Refunds of member contributions	18,003			552		18,555
Transfers to other systems	3,025,208		131,490,000			134,515,208
Administrative				4,297,092		4,297,092
Total deductions	3,043,211	429,879,875	131,490,000	4,297,644	163,574,055	732,284,785
Net Increase (Decrease)	2,115,533	(429,879,875)	16,109,551	697,760,672	(37,756,653)	248,349,228
Other Changes in Net Assets:						
Interest allocation	1,234,240	356,673,025	318,156,315	(676,063,580)		
Transfers upon retirements	(4,539,047)	4,539,047				
Transfers of inactive balances	(149)			149		
Transfers of employer shares		1,054,676,296	(1,054,676,296)			
Total other changes in net assets	(3,304,956)	1,415,888,368	(736,519,981)	(676,063,430)		
Net Increase (Decrease) After Other Changes	(1,189,423)	986,008,493	(720,410,430)	21,697,241	(37,756,653)	248,349,228
Net Assets Held in Trust for Pension and Healthcare Benefits:						
Beginning of Year	3,281,893	3,252,062,516	3,700,846,519	1,841,359,933	113,364,401	8,910,915,262
End of Year	$ 2,092,470	$4,238,071,009	$2,980,436,089	$1,863,057,174	$ 75,607,748	$9,159,264,490

Supporting Schedules (continued)

Detail of Changes in Plan Net Assets (Pension and Postemployment Healthcare Benefits)

	For the Year Ended September 30, 1997					
	Employee Savings	Pension Reserve	Employer Accumulation	Income	Health Insurances	Total
Additions:						
Members contributions:						
Other	$ 7,229,118				$ 3,714,213	$ 10,943,331
Military	4,915,035					4,915,035
Employer contributions			$ 288,590,215		121,641,412	410,231,627
Investment income:						
Investment income				$1,679,743,639		1,679,743,639
Securitites lending income				11,803,417		11,803,417
Real estate operating expenses				(311,903)		(311,903)
Securities lending expenses				(11,412,796)		(11,412,796)
Other investment expenses				(2,042,558)		(2,042,558)
Interest income					7,546,437	7,546,437
Miscellaneous income				272		272
Total additions	12,144,153		288,590,215	1,677,780,071	132,902,062	2,111,416,501
Deductions:						
Benefits paid to plan members and beneficiaries:						
Retirement allowances		$ 382,866,379				382,866,379
Employer share of health insurance					115,670,352	115,670,352
Employer share of dental/vision insurance					14,822,508	14,822,508
Refunds of member contributions	42,388					42,388
Transfers to other systems	312,680		7,493,581			7,806,261
Administrative				5,247,943		5,247,943
Total deductions	355,068	382,866,379	7,493,581	5,247,943	130,492,860	526,455,831
Net Increase (Decrease)	11,789,085	(382,866,379)	281,096,634	1,672,532,128	2,409,202	1,584,960,670
Other Changes in Net Assets:						
Interest allocation	1,898,501	214,919,479	228,528,776	(445,346,756)		
Transfers upon retirements	(64,964,806)	64,964,806				
Transfers of inactive balances	231			(231)		
Transfers of employer shares		182,720,864	(182,720,864)			
Total other changes in net assets	(63,066,074)	462,605,149	45,807,912	(445,346,987)		
Net Increase (Decrease) After Other Changes	(51,276,989)	79,738,770	326,904,546	1,227,185,141	2,409,202	1,584,960,670
Net Assets Held in Trust for Pension and Healthcare Benefits:						
Beginning of Year	54,558,882	3,172,323,746	3,373,941,973	614,174,792	110,955,199	7,325,954,592
End of Year	$ 3,281,893	$3,252,062,516	$3,700,846,519	$1,841,359,933	$ 113,364,401	$8,910,915,262

INVESTMENT SECTION

Report on Investment Activity

INTRODUCTION

The State Treasurer reports quarterly the investment activity to the Investment Advisory Committee ("IAC") which reviews the investments, goals and objectives of the retirement funds and may submit recommendations regarding them to the State Treasurer. The IAC may also, by a majority vote, direct the state Treasurer to dispose of any holdings which, in the committee's judgement, are not suitable for the funds involved, and may, by unanimous vote, direct the State Treasurer to make specific investments.

The IAC was created by Act 380 of the Public Acts of 1965. The three public members of the five-member committee are appointed by the Governor with the advice and consent of the Senate for three-year terms. The Director of the Department of Consumer and Industry Services and the Director of the Department of Management and Budget are ex-officio members. The members of the IAC are as follows: Mr. Samuel Valenti III (public member), Farris W. Womack (public member), Jerry L. Tubergen (public member), Kathleen M. Wilbur (ex-officio member), and Janet E. Phipps (ex-officio member). The public members serve without pay, but are paid actual and necessary travel and other expenses.

INVESTMENT POLICY & GOAL

The primary function of the MSERS is to provide retirement, survivor and disability benefits to its members. The State Treasurer is the sole investment fiduciary and custodian of the System's investment pursuant to state law. The primary investment objective is to maximize the rate of return on the total investment portfolio, consistent with a high degree of prudence and sufficient diversity to eliminate inordinate risks and to meet the actuarial assumption for the investment rate of return, at a reasonable cost achieved by cultivating a motivated team of dedicated professionals. The goals of the fund are:

1. To outperform the actuarial assumption over the long-term.
2. To produce competitive results at a low cost.
3. To achieve a delicate balance between risk and return.
4. To perform in the top half of the Capital Resource Advisors public plan universe.
5. To exceed individual asset class benchmarks over the long-term.

The strategy for achieving these goals is carried out by investing the assets of the system according to a five-year asset allocation model which currently has seven different asset classes which provides for a well diversified portfolio.

	Asset Allocation	
Investment Category	**As of 9/30/98 Actual %**	**Target %**
Mortgages	0.4%	0.0%
International Equity	4.1%	7.5%
Real Estate	8.3%	8.5%
Alternative Investments	8.9%	7.5%
Short Term Investments	4.2%	1.5%
Fixed Income	24.6%	25.5%
Domestic Equity	49.5%	49.5%
TOTAL	100.0%	100.0%

Report on Investment Activity

STATE LAW

Pursuant to State Law (Section 91 of Act No. 380 of the Public Acts of 1965, as amended), the State Treasurer, State of Michigan, is the investment fiduciary for the following four State sponsored retirement systems: Michigan Public School Employees' Retirement System; Michigan State Employees' Retirement System; Michigan State Police Retirement System; and Judges' Retirement System.

Act No. 314 of the Public Act of 1965, as amended, authorizes the investment of assets of public employee retirement systems or plans created and established by the state or any political subdivision.

PROXY VOTING POLICY

MSERS' Proxy Voting Policy sets forth directives on the following issues: Board of Directors, Corporate Governance, Social Issues, corporate restructurings and defenses. All proxies are reviewed and voted in accordance with the above mentioned items.

INVESTMENT RESULTS

Total Portfolio Result

For the fiscal year ended September 30, 1998, the total portfolio returned 8.2%, compared to the median of 6.6% of state plans, including MSERS, as compiled by Capital Resource Advisors. For the three-year period the fund returned 15.3%, and for the five-year period the fund returned 12.9%. This compares with the median fund return of 12.9% for the three-year period and 11.9% for the five-year period.

During the fiscal year ending September 30, 1998, the nation's economy was characterized by full employment, low inflation, declining interest rates, and moderate economic growth. The equity markets experienced a significant correction in the quarter ending September 30, 1998. The S&P 500 was off 9.9% while the Dow Jones Industrial Average fell 12.0% during this time frame. This tended to reduce the one-year return on the S&P 500 to 9.1%, with the Dow Jones Industrial Average returning 0.5%. Because of declining interest rates, the Lehman Brothers Government/Corporate Bond Index experienced a return of 12.8% for the year ending September 30, 1998, and the Salomon Brothers Broad Grade Index experienced a return of 11.5%.

The returns were calculated using a time weighted rate of return in accordance with Standards of the Association for Investment Management and Research (AIMR), unless a modification is described in the discussion of the return.

The MSERS is well diversified among asset classes. As of September 30, 1998, the portfolio consisted of 49.5% domestic equities, 25.0% fixed income (includes 0.4% in mortgages), 8.9% alternative investments, 8.3% real estate, 4.2% short-term investments, and 4.1% international equities.

Domestic Stocks - Active

The objective of the actively-managed domestic stock division is long-term capital appreciation by investing primarily in publicly-traded stocks of U.S.-based companies.

Fiscal year 1998 witnessed considerable volatility in the equity markets as competing factors pulled in different directions. On the positive side, low inflation, declining interest rates, low unemployment, and moderate growth in the U.S. economy helped the markets achieve new highs. On the negative side, concerns about corporate earnings growth, deflation fears, questions about presidential integrity, and worries about the health of a number of international economies and financial markets caused some temporary market declines.

Report on Investment Activity

Domestic stock returns closed the fiscal year with a 5.1% increase compared with a 9.1% increase for the S&P 500 Index, and a 0.5% increase for the Dow Jones Industrial Average. This compared with a median return of 3.7% for state plans, including MSERS, as compiled by Capital Resource Advisors. The markets were led by a 44.0% gain for communication stocks, followed by 38.3% for health care, and 31.0% for utilities. Three-year and five-year results for the actively-managed domestic stock portfolio were 20.6% and 17.4%, respectively, on an annualized basis. This compared with 22.6% and 19.9% for the S&P 500, and 12.9% and 11.9% for the median of state plans.

At the end of the fiscal year, actively-managed domestic stocks represented 37.5% of total assets, compared with 36.4% at the end of 1997, and 34.5% at the close of 1996.

Domestic Stocks - Passive

The objective of the enhanced S&P 500 and S&P MidCap Index Funds is to closely match the return performance of their benchmarks. The S&P 500 Index return for the fiscal year was 10.1% versus the benchmark's 9.1%. The S&P MidCap Index Fund return for the fiscal year was a negative 4.3% versus its benchmark of a negative 6.3%. The enhancements to the returns were the result of strategic allocations of additional funds to passive equity investments during market corrections and the opportunistic use of derivative programs. At the end of the fiscal year, passive domestic stock portfolios represented 11.9% of total assets, with the S&P 500 Index Fund accounting for 11.0% and the S&P MidCap Index Fund accounting for 0.9%. Indexed stock portfolios represented 10.5% of total assets at the end of the prior fiscal year.

International Equities

Passive exposure to international equity returns is achieved by investing in a combination of fixed income notes and equity swap agreements on foreign stock indices in developed markets. Interest on the dedicated notes is exchanged for international stock index returns, and the notional amount of the swap agreements is held in the approximate proportions of the Salomon Smith Barney Broad Market Index (BMI) Europe and Pacific Composite (EPAC) country weightings for the larger component countries. The passive investment program using swap agreements was established in 1993. During fiscal year 1998, $63 million of exposure was withdrawn from the combination structure, bringing international equity investments to 4.1% of total assets.

The benchmark used to evaluate international equity returns is a custom version of the Salomon Smith Barney BMI-EPAC adjusted for net dividends. Fifty percent of the benchmark is hedged to the U.S. dollar and the other 50% is impacted by local currency exchange rate changes. The composite international equity return of a negative 4.7% in fiscal year 1998 compared favorably with the Salomon Smith Barney BMI-EPAC return of a negative 8.1%. The composite international equity return of 8.4% for 3 years compared well with the benchmark's return of 6.6% over the same period.

The international equity exposure through the combination of fixed income LIBOR notes and equity swap agreements was valued at $376 million on September 30, 1998. That valuation included a net unrealized loss on equity index exposures of $10.7 million and an unrealized loss of $4.4 million on LIBOR note investments held. Unrealized equity losses reflect both the decline of several targeted international equity indices later in the year and the increase in index exposure cost levels throughout the year. As older swap agreements matured, equity gains were realized and new replacement swap exposures were established at higher index levels. At the end of September, total realized gains and net interest received in excess of counterparty obligations reached a record $109.2 million since the program began. During fiscal year 1998, $68.9 million of gains on equity exposures were realized, and $12.4 million of interest in excess of obligations on completed swaps was also recognized.

Fixed Income (Excluding Mortgages)

For the fiscal year ending September 30, 1998, the fixed income portfolio returned 10.0% compared to the median of 10.9% for the state plans, including MSERS, as compiled by Capital Resource Advisors evaluations. For the three-year period, the portfolio returned 8.7%, and for the five-year period the portfolio returned 7.8%. This compares with the median portfolio return of 8.7% for the three-year period and 7.2% for the five-year period.

Report on Investment Activity

As the year progressed, rates declined and quality spreads widened as investors purchased the long-term treasury issues in a flight to quality. The fixed income market, therefore, rewarded higher grade, longer-term issues. MSERS' fixed income portfolio had a shorter duration than the Lehman Government and Corporate Index. As a result, the fund under-performed the Lehman Index for the one-year period, 10.0% versus 12.8%, but was still in line for the three-year period, 8.7% versus 8.9%, and out-performed the index for the five-year period, 7.8% versus 7.2%. Relative to the Salomon Brothers Broad Grade Index, MSERS' fixed income portfolio under-performed in the one-year time horizon, 10.0% to 11.5%, matched in the three year period, 8.7% to 8.7%, and was ahead in the five-year period 7.8% to 7.2%.

Fixed Income represented 24.6% of the total portfolio compared with 24.8% last year. The corporate sector represented 47% of fixed income securities with government securities representing 53%. Last year, corporates represented 40% of the total with governments representing 60%. The high level of corporates was due to a concerted strategy to acquire investment grade issues where spreads had widened significantly. The lower holding of governments can be attributed to a substantial increase in the number of issues called, particularly government sponsored enterprises.

Real Estate Equity

As of the fiscal year ending September 30, 1998, 8.3% of the total portfolio was invested in equity real estate. This compares to 6.4% and 6.4% for the fiscal years ending September 30, 1997 and 1996, respectively. The asset allocation for equity real estate investment was increased to 8.5% of the total portfolio from 7.5% for fiscal year ending September 30, 1997.

The one-year, three-year and five-year total equity real estate net returns for the fiscal year ending September 30, 1998, were 10.6%, 11.6% and 8.1%, respectively, as quoted by Capital Resource Advisors. This compares to the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index returns of 17.3%, 12.5% and 9.9% relating to the same time periods. The NCREIF portfolio of properties is heavily weighted in the office sector, 41.3% versus the MSERS portfolio at 28.9%. However, the historical volatility of the office sector returns makes it a more risky asset class. This variation in portfolio weighting gives the NCREIF portfolio a much higher level of risk than MSERS has chosen to assume. In addition, the NCREIF Index does not account for fees/overhead, while MSERS' returns quoted above are after fees/overhead.

The real estate investments are broadly diversified geographically, across the country, by type of property, and by class of property, to reduce risk. Major property types include the following: Central Business District (CBD) office, suburban office, regional malls, neighborhood and community shopping centers, industrial/warehouse buildings and apartments. The MSERS, through its advisors and private real estate operating companies it controls, acquires, develops, redevelops and disposes of real estate with the goal of maximizing returns while maintaining an ***acceptable*** level of risk. The properties are held in various investment vehicles: Partnerships, LLC's, Trusts, Commingled funds, and REIT stock. These legal entities allow MSERS to enjoy the benefits of real estate ownership while limiting the liability associated with this asset class. In all new investments, MSERS retains approval rights over critical decisions. The properties are regularly valued by independent appraisers to establish market values. The market values established by the appraisers are utilized in computing the real estate portfolio appreciation return. The appreciation return coupled with the income return produced from the real estate holdings are utilized to derive the equity real estate portfolio total return.

Real Estate Debt (Mortgages)

As of the fiscal year ending September 30, 1998, 0.4% of the total portfolio was invested in mortgages. This compares to 0.5% and 2.2% for the fiscal years ending September 30, 1997 and 1996, respectively. The asset allocation objective is to reduce mortgage holdings to 0% over time. In the current interest rate environment, MSERS cannot meet actuarial return requirements in new mortgage loans.

The one-year, three-year and five-year total returns for the mortgage portfolio, for the fiscal year ending September 30, 1998, were 8.7%, 8.1% and 7.6%, respectively. This compares to Salomon Brothers Broad Grade Index returns of 11.5%,

Report on Investment Activity

8.7% and 7.2% relating to the same time periods. Since the majority of the mortgage portfolio is federally insured mortgages, and therefore less risky, the returns generated by the mortgage portfolio would normally be less than the index.

During the previous year, the majority of the mortgage portfolio was sold to take advantage of the favorable low interest rate environment. The low interest rates, existing in the overall economy, resulted in premium prices being paid for the mortgages sold. The sale of the mortgages resulted in realized gains to the portfolio. On average, MSERS received sale prices between 101% and 105% of the unpaid principal balance of the notes compared to purchase prices of between 55% and 60% of face value for these same loans when purchased back in the late 1970's and early 1980's. The remaining mortgage holdings are mainly comprised of federally insured multifamily mortgages and a few multi-tenant commercial office buildings. The mortgage portfolio is concentrated in Michigan and the Midwest.

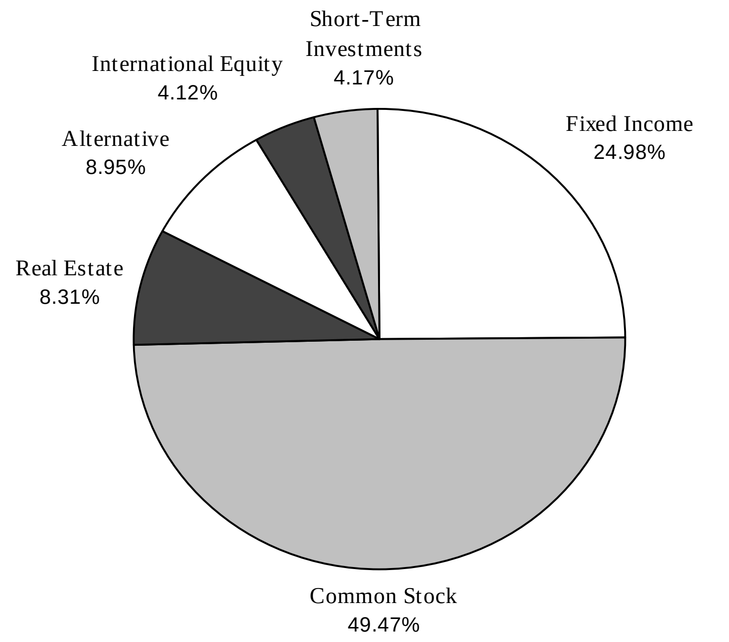
Alternative Investments

Alternative Investments are investments in the private equity market, either directly in companies or indirectly through limited partnerships. Through September 30, 1998, approximately 90% of Alternative investments were made through limited partnerships. Of the investments in limited partnerships, approximately 8% were in partnerships investing internationally. The remaining 10% were direct private equity investments and public stock distributions received from the limited partnerships. The percentage of assets in alternative investments has consistently increased from 4.6% as of September 30, 1993, to 8.9% as of September 30, 1998. The asset allocation for alternative investments is 8.9% while the long-term target asset allocation is 7.5%.

The one-year, three-year and five-year total alternative investment returns for the fiscal year ending September 30, 1998, were 26.4%, 25.7% and 21.9%, respectively.

Report on Investment Activity

Asset Allocation



Investment Results Periods Ending September 30, 1998

Investment Category	Current Year	Annualized Rate of Return 3 Years	5 Years	10 Years
Total Portfolio	8.2 %	15.3 %	12.9 %	11.4 %
Median	6.6	12.9	11.9	11.4
Domestic Equities Stock - Active	5.1	20.6	17.4	13.6
Domestic Equities Stock - Passive*	8.4	22.4	19.2	17.7
Standard & Poor's (S&P 500)	9.1	22.6	19.9	17.3
International Equities	(4.7)	8.4	6.6	N/A
Net Salomon Brothers BMI - EPAC 50/50	(8.1)	6.6	6.0	N/A
Fixed Income Bonds (U.S. Corp and Govt)	10.0	8.7	7.8	9.6
Salomon Brothers Broad Grade Index	11.5	8.7	7.2	9.3
Real Estate - Debt	8.7	8.1	7.6	N/A
Salomon Brothers Broad Grade Index	11.5	8.7	7.2	9.3
Real Estate - Equity	10.6	11.6	8.1	N/A
NCREIF	17.3	12.5	9.9	5.3
Alternative Investments	26.4	25.7	21.9	16.0

* Passive portfolio consists of a S&P 500 fund and a S&P MidCap fund. The return is a weighted average of the two funds.

Report on Investment Activity

Largest Assets Held

Largest Stock Holdings (By Market Value)
September 30, 1998

Rank	Shares	Stocks	Market Value
1	1,549,458	Microsoft Corporation	$ 170,537,221
2	1,945,019	General Electric Corporation	154,750,574
3	1,697,715	Warner-Lambert Company	128,177,483
4	1,143,091	Pfizer Incorporated	120,881,873
5	1,664,718	Amoco Corporation	89,686,682
6	1,476,191	McDonald's Corporation	88,110,150
7	1,780,378	Chrysler Corporation	85,235,597
8	1,130,983	Federal National Mortgage Association	72,665,658
9	2,244,899	Compaq Computer Corporation	70,994,931
10	1,274,197	Wal-Mart Stores Incorporated	69,603,011

Largest Bond Holdings (By Market Value)
September 30, 1998

Rank	Par Amount	Bonds & Notes	Market Value
1	$ 85,815,000	U.S. Treasury Bonds at 9.125% Due 5-15-2009	$ 104,922,568
2	69,781,800	U.S. Treasury 0% Callable Principal Due 5-15-2011	49,412,493
3	59,950,000	U.S. Treasury 0% Coupon Strips Due 8-15-2003	48,552,306
4	43,600,000	Morgan, J.P. FRN Due 3-13-2000	43,382,000
5	49,486,000	U.S. Treasury 0% Callable Principal Due 11-15-2011	34,188,888
6	32,700,000	FHLMC Debenture 6.70% Due 7-23-2008	33,115,290
7	34,777,000	U.S. Treasury Tiger 14 0% Due 8-15-2004	26,815,154
8	24,797,500	FHLMC Debenture 6.51% Due 8-18-2008	25,057,130
9	21,992,930	First Chicago FRN Due 7-28-2003	22,294,673
10	21,800,000	FHLMC - Global 6.55% Due 11-13-2001	21,840,766

A complete list of stock and bond holdings is available from the Michigan Department of Treasury.

Schedule of Investment Fees

The State Treasurer is the investment fiduciary and custodian of the System's funds pursuant to state law. Outside advisors are utilized to augment the State Treasurer's internal staff in the real estate and alternative investment markets. Only 8.6% of the total investment portfolio is managed by fully discretionary outside advisors. Outside advisor's fees are netted against the partnership or trust fund income. The Michigan Department of Treasury's cost of operations applicable to the System for the fiscal year amounted to $1.4 million or less than two basis points (.02%) of the market value of the portfolio.

Schedule of Investment Fees

Investment Managers' Fees:

	Assets under Management (in thousands)	Fees (in thousands)	Basis Points*
State Treasurer	$8,330,632.4	1,408.5	1.7
Outside Advisors - Alternative	746,015.1	4,952.7	66.4
Real Estate	42,944.3	-	-
Total	$9,119,591.8		

Other Investment Services Fees:

	Assets in Custody**	
Custody Fees	$6,567,594.4	30.7
Security Lending Fees	378,778.5	16,305.9

* Outside Advisors Fees are netted against the income of the partnership and trust income. The partnership agreements define the management fees, which range from 150 to 250 basis points of the committed capital, in most cases the fees are netted against income. For Real Estate the asset management fee ranges from 25 to 90 basis points and is netted against current year's income.

** Other investment service fees are charged on assets managed by the State Treasurer held at its custodial bank in the amount of $6,567.6 million; $378.8 million of the assets were on loan at fiscal year end.

Report on Investment Activity

Schedule of Investment Commissions

	Number of Shares Traded	Commissions Paid (1)	Average Commission Rate per Share
	Fiscal Year Ended 9-30-98		
Investment Performance Measurement Consultant:			
Capital Resource Advisors			
(Directed brokerage included below)	378,760	$ 22,726	0.06
Investment Brokerage Firms:			
Merrill Lynch & Company	2,548,925	$ 146,303	0.06
Salomon Smith Barney, Inc.	1,929,017	115,741	0.06
Paine Webber, Inc.	1,755,032	105,302	0.06
Bear Stearns & Company	1,543,393	87,951	0.06
Donaldson, Lufkin & Jenrette Securities Corp.	1,220,865	73,252	0.06
Bridge Trading Company	1,092,725	65,564	0.06
Schroder & Company	1,080,691	63,599	0.06
Sanford C. Bernstein & Company	885,930	53,156	0.06
C.S. First Boston Corporation	785,925	47,156	0.06
Prudential Securities Inc.	690,103	41,406	0.06
Goldman, Sachs & Company	692,634	40,414	0.06
Lehman Brothers, Inc.	680,116	39,717	0.06
Morgan Stanley & Company	611,141	36,534	0.06
Oppenheimer & Company	601,200	34,982	0.06
J.P. Morgan Securities, Inc.	568,086	34,085	0.06
Capital Inst. Services	477,878	28,673	0.06
S.G. Cowen & Company	429,286	25,757	0.06
Charles Schwab & Company, Inc.	415,791	24,947	0.06
The Citation Group	354,773	20,850	0.06
Wilshire Associates	339,688	20,381	0.06
Everen Securities	327,065	19,624	0.06
Standard & Poor's Securities	325,103	19,506	0.06
Montgomery Securities	229,227	13,754	0.06
Deutsche/Morgan/Grenfell	208,277	12,497	0.06
SoundView Financial Group	143,815	8,629	0.06
Subtotal (25 highest)	19,936,686	$ 1,179,780	0.06(2)
All Other Brokerage Firms	262,690	15,761	0.06(3)
Total	20,199,376	$ 1,195,541	0.06(4)

(1) These amounts are included in purchase and sale prices of investments.
(2) The average commission rate per share for the top 25 brokerage firms.
(3) The average commission rate per share for all other brokerage firms, excluding the top 25 brokerage firms.
(4) The average commission rate per share for all brokerage firms.

Report on Investment Activity

Investment Summary

	1998		1997	
	Market Value*	Percent of Total Market Value	Market Value*	Percent of Total Market Value
Fixed Income:				
Government Bonds	$ 1,189,021,855	13.04 %	$ 1,316,421,519	14.83 %
Corporate Bonds & Preferred Stocks	1,054,229,454	11.56	883,416,122	9.96
Convertible Bonds	0	0	4,183,670	0.05
Mortgages	34,617,940	0.38	47,294,284	0.53
Total Fixed Income	$ 2,277,869,249	24.98 %	$ 2,251,315,595	25.37 %
Common Stock	4,511,882,219	49.47	4,149,553,280	46.76
Real Estate	758,055,589	8.31	569,128,839	6.41
Alternative	816,095,657	8.95	579,044,220	6.52
International Equity	375,821,394	4.12	468,025,104	5.27
Short-Term Investments**	379,867,669	4.17	858,240,830	9.67
Total	$ 9,119,591,777	100.00 %	$ 8,875,307,868	100.00 %

* Short-term investments are at cost, which approximates market.

** Includes equity in the State Treasurer's Common Cash Fund, but excludes amounts payable and receivable for sales and purchases of securities with a settlement date after September 30 for each fiscal year. Amount also excludes $380,746,684 and $322,886,494 in cash collateral for security lending for fiscal years 1998 and 1997, respectively.

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ACTUARIAL SECTION

Actuary's Certification

THE SEGAL COMPANY

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Michael J. Karlin, F.S.A., M.A.A.A.
Senior Vice President & Actuary

January 22, 1999

Ms. Janet E. Phipps
Director
Department of Management and Budget
and
Retirement Board
Michigan State Employees Retirement System
P.O. Box 30176
Lansing, Michigan 48909

Ladies and Gentlemen:

The Michigan State Employees Retirement System (MSERS) is funded on an actuarial reserve basis. The basic financial objective of MSERS is to establish and receive contributions that remain approximately level as a percentage of active member payroll over a long period of years.

Actuarial valuations are prepared annually to determine MSERS's actuarial liabilities and the employer contributions required to fund the System in accordance with the actuarial reserve funding provisions of the governing State Statute. The most recent actuarial valuation as of September 30, 1998 included a total of 93,923 members of MSERS. The actuarial value of MSERS's assets amounted to approximately $9.11 billion on September 30, 1998.

The actuarial assumptions used in the 1998 valuation are the same as those used in the previous annual actuarial valuation. These assumptions produce valuation results which we consider to be reasonably indicative of the plan's underlying cost. Also, in our opinion, the actuarial assumptions and methods used for funding purposes meet the parameters for the disclosures presented in the financial section by GASB Statement No. 25.

Our actuarial valuation of MSERS as of September 30, 1998 was performed by qualified actuaries in accordance with accepted actuarial procedures. In our opinion, the calculated contribution rate meets the fundamental objectives of State law. Based on the 1998 valuation results, it is also our opinion that the Michigan State Employees Retirement System continues in sound condition, in accordance with actuarial principles of level cost financing.

Most of the information used in the supporting schedules in the Actuarial and Statistical Sections, as well as the Schedules of Funding Progress and the employer contributions shown in the Schedules of Employer Contributions in the Financial Section of this report were provided by our firm.

Sincerely,

Michael Karlin

Michael Karlin, F.S.A., M.A.A.A.
Senior Vice President & Actuary

Summary of Actuarial Assumptions and Methods

1. The investment return rate used in making the valuations was 8% per year, compounded annually. This rate of return is not the assumed real rate of return. The real rate of return is the rate of investment return in excess of the inflation rate. Considering other financial assumptions, this investment return rate translates to an assumed long term real rate of return of 3% for 5 years, beginning October 1, 1994 and 5% thereafter. Adopted 1994.

2. The mortality table used in evaluating allowances to be paid was the 1983 Group Annuity Mortality Table, set forward one year for men and 2 years for women. Adopted 1994.

3. Sample probabilities of retirement with an age and service allowance are shown in Schedule 1 on the next page. Adopted 1994.

4. Sample probabililties of withdrawal from service and disability, together with individual pay increase assumptions, are shown in Schedule 2 on the next page of this report. Adopted 1994.

5. Total active member payroll is assumed to increase 3% per year for the next 5 years, beginning October 1, 1994 and 5% thereafter. This represents the portion of the individual pay increase assumptions attributable to inflation. In effect, this assumes no change in the number of active members. Adopted 1994.

6. An individual entry age actuarial cost method of valuation was used in determining age and service allowance actuarial liabilities and normal cost. Adopted 1975. Unfunded actuarial accrued liabilities are financed over a period of 50 years and over a declining 40 year period for years beginning October 1, 1996. Adopted 1996.

7. During 1998, the Department of Management and Budget approved the use of market value of assets as of September 30, 1997 for valuation purposes. For investment gains and losses that occur after that date, a 5-year smoothing technique will be used. Specifically, the excess (shortfall) of actual investment income (including interest, dividends, realized and unrealized gains or losses) over the imputed income at the valuation interest rate is considered the gain (loss), which is spread over five years. .

8. The data about persons now covered and about present assets was furnished by the System's administrative staff. Although examined for general reasonableness, the data was not audited by the actuary.

9. The actuarial valuation computations were made by or under the supervision of a Member of the American Academy of Actuaries (MAAA). The assumptions used in the actuarial valuations were adopted by the System's board after consulting with the actuary.

Summary of Actuarial Assumptions and Methods (Continued)

SCHEDULE 1

Percent of Eligible Active Members Retiring Within Next Year

Retirement Ages	Correction Officers	Conservation Officers	Other Members
45		20 %	
48		20	
51	20 %	20	
55	25	25	23 %
58	15	15	18
61	20	20	20
64	15	15	28
67	40	100	35
70	100	100	50

SCHEDULE 2

Separation From Active Employment Before
Age & Service Retirement & Individual Pay Increase Assumptions

Sample Ages	Years Service	Percent of Active Members Withdrawing Within Next Year (Men and Women)	Percent of Active Members Becoming Disabled Within Next Year	Percent Increase In Pay During Next Year
All	0	16.50 %		
	1	12.50		
	2	7.50		
	3	5.50		
	4	4.50		
25	5 & Over	3.40	0.01 %	9.50 %
35		2.08	0.04	4.70
45		1.42	0.26	3.75
55		1.36	0.65	3.24
65		1.36	1.15	3.00

Actuarial Valuation Data

Schedule of Active Member Valuation Data

Valuation Date Sept. 30	Number	Reported Annual Payroll*	Average Annual Pay	% Increase	Average Age	Average Service
1989	66,388	$1,996,039	$30,066	2.6 %	40.9	10.7 years
1990	69,558	2,227,755	32,027	6.5	41.2	10.9
1991	65,595	2,236,336	34,093	6.5	42.1	11.9
1992	64,248	2,189,752	34,083		42.2	11.9
1993	63,906	2,184,972	34,190	0.3	42.6	12.1
1994	64,923	2,271,304	34,985	2.3	43.0	12.5
1995	65,133	2,348,534	36,058	3.1	43.2	12.7
1996	63,807	2,515,420	39,422	9.3	43.8	13.0
1997	55,434	2,273,203	41,007	4.0	43.7	13.1
1998	49,717	2,107,996	42,400	3.4	44.8	14.8

* In thousands of dollars. Base pay only excluding 3 1/2% for overtime and shift differentials through 1995. Greater of base pay or prior year actual earnings beginning in 1996.

Schedule of Changes in the Retirement Rolls

Year Ended Sept. 30	Added to Rolls		Removed from Rolls		Rolls–End of Year		% Increase in Annual Allowances	Average Annual Allowances
	No.	Annual Allowances*	No.	Annual Allowances*	No.	Annual Allowances*		
1989	1,944	$ 24,625	765	$ 5,067	24,187	$168,795	13.1 %	$ 6,979
1990	1,449	17,453	773	5,552	24,863	180,696	7.1	7,268
1991	1,493	20,168	790	5,936	25,566	194,928	7.9	7,624
1992	4,177	55,336	887	6,652	28,856	243,612	25.0	8,442
1993	1,105	18,468	786	4,887	29,175	257,193	5.6	8,816
1994	1,888	22,636	1,101	6,442	29,962	273,387	6.3	9,124
1995	1,566	23,575	966	6,268	30,562	290,694	6.3	9,512
1996	1,595	24,527	1,064	7,288	31,093	307,933	5.9	9,904
1997	6,098	121,005	1,068	7,878	36,123	421,060	36.7	11,656
1998	1,279	21,085	1,217	9,689	36,185	432,456	2.7	11,951

* In thousands of dollars

Prioritized Solvency Test

MSERS' funding objective is to meet long term benefit promises through contributions that remain approximately level from year to year as a percent of member payroll. If the contributions to the System are level in concept and soundly executed, the System will pay all promised benefits when due -- the ultimate test of financial soundness. Testing for level contribution rates is the long term solvency test.

A prioritized solvency test is another means of checking a system's progress under its funding program. In a short condition test, the plan's present assets (cash and investments) are compared with: (1) active member contributions on deposit; (2) the liabilities for future benefits to present retired lives; and (3) the liabilities for service already rendered by active members. In a system following the discipline of level percent of payroll financing, the liabilities for active member contributions on deposit (liability 1) and the liabilities for future benefits to present retired lives (liability 2) will be fully covered by present assets (except in rare circumstances). In addition, the liabilities for service already rendered by active members (liability 3) is normally partially covered by the remainder of present assets. Generally, if the System has been using level-cost financing, the funded portion of liability 3 will increase over time. Liability 3 being fully funded is not necessarily a byproduct of level percent of payroll funding methods.

The schedule below illustrates the history of the liabilities of the System and is indicative of MSERS' policy of following the discipline of level percent of payroll financing.

	Actuarial Present Value of Accrued Liabilities ($ in Millions)				Portion of Present Value Covered by Assets			
	(1)	(2)	(3)					
Valuation Date Sept. 30	Active Member Contributions	Retirants and Beneficiaries	Active Members (Employer Financed Portion)	Valuation Assets	(1)	(2)	(3)	(4)***
1989	$ 83	$ 1,551	$ 2,333	$ 3,928	100 %	100 %	98.3 %	99.0 %
1990#	83	1,715	2,668	4,106	100	100	86.6	92.0
1991#	82	1,870	2,987	4,347	100	100	80.2	88.0
1992	83	2,413	2,984	4,533	100	100	68.3	82.7
1993+	72	2,561	3,539	5,043	100	100	68.1	81.7
1994@	73	2,778	3,709	5,476	100	100	70.8	83.5
1995	72	2,751	4,038	6,090	100	100	80.9	88.8
1996	55	2,844	4,248	6,678	100	100	88.9	93.4
1997	3	4,300	3,910	7,516	100	100	82.2	91.5
1998	27	4,360	3,987	9,109	100	100	118.4	108.8

@ Revised actuarial assumptions.
# Benefits amended.
\+ Revised asset valuation method.
*** Percents funded on a total valuation asset and total actuarial accrued liability basis.

Summary Of Plan Provisions

Our actuarial valuation of MSERS as of September 30, 1998 is based on the present provisions of the State Employees' Retirement Act, which are summarized in this section.

Regular Retirement (no reduction factor for age)

Eligibility — Age 55 with 30 years service, or age 60 with 10 or more years service. Corrections Officers may retire at age 51 with 25 or more years service, or age 56 with 10 or more years service. Conservation Officers may retire after 25 years of service regardless of age.

Final Average Compensation — Regular retirement benefit is based on final average compensation (FAC), which is the average of highest 3 consecutive years (2 years for Conservation Officers).

Annual Amount — Total service times 1.5% of FAC. For members with 20 or more years of service, a $3,000 minimum annual benefit is payable. Corrrections Officers receive an additional temporary supplement to age 62 equal to the product of supplemental service times 0.5% of FAC. Conservation Officers retiring after 25 years receive a benefit equal to 60% of FAC.

Early Retirement (age reduction factor used)

Eligibility — Age 55 with 15 or more years service.

Annual Amount — Computed as regular retirement benefit but reduced by 0.5% for each month under age 60.

Deferred Retirement (vested benefit)

Eligibility — 10 years of service (5 years for unclassified persons in the executive or legislative branch). Benefit commences at age 60.

Annual Amount — Computed as regular retirement benefit based on service and FAC at termination.

Duty Disability Retirement:

Eligibility — No age or service requirement.

Annual Amount — Disability after age 60: Computed as regular retirement benefit with minimum benefit based on 10 years service. Disability prior to age 60: To age 60, benefit is two-thirds of FAC but limited to $6,000 per year. Additional limitation such that benefit plus workers' compensation does not exceed final compensation. After age 60, benefit is recomputed as a regular retirement benefit with service granted for period in receipt of disability benefit before age 60 (benefit not reduced after age 60).

Non-Duty Disability Retirement:

Eligibility — 10 years of service.

Annual Amount — Computed as regular retirement benefit based on service and FAC at time of disability. Minimum annual benefit is $600.

Summary Of Plan Provisions (continued)

Duty Death Before Retirement

Eligibility — No age or service requirement. Also applies to duty disability retirant who dies within 3 years of disability and before age 60.

Annual Amount — Accumulated employee contributions are refunded. Surviving spouse receives annual benefit of one-third of final compensation until death. Unmarried children under age 18 each receive an equal share of one-fourth of final compensation (if no spouse each child receives one-fourth, to a maximum of one-half for all children). If no spouse or eligible children, each dependent parent receives one-sixth of final compensation. Total benefits payable are limited to $2,400 per year. Additional limitation such that benefits plus workers' compensation does not exceed final compensation.

Non Duty Death Before Retirement

Eligibility — 10 years of service. In the case of a deceased vested former member, the survivor benefit commences when the deceased former member would have attained age 60.

Annual Amount — Computed as regular retirement benefit but reduced in accordance with a 100% joint and survivor election.

Post-Retirement Cost-of-Living Adjustments

One-time upward adjustments have been made in 1972, 1974, 1976, 1977 and 1987. Beginning in 1983, some benefit recipients share in a distribution of a portion of investment income earned in excess of 8% annually (supplemental payment). Beginning in 1988 all benefit recipients are eligible for automatic 3% annual (non-compounded) benefit increases, with a maximum $300 annual increase. Eligibility for the above benefits:

Retired before October 1, 1987	Greater of supplemental payment or the combination of the 1987 one-time adjustment and the automatic increases.
Retired on or after October 1, 1987	Automatic increases only.

Post-Retirement Health Insurance Coverage

Persons in receipt of retirement allowance (including members who did not retire directly from the System, but come from a vested deferred status), and their dependents, are eligible for 95% State-paid health insurance coverage and 90% State-paid dental and vision insurance

Member Contributions

None

Defined Contribution

New employees hired on or after March 31, 1997, become participants in Tier 2 (i.e., a defined contribution plan) rather than Tier 1 (i.e., the above described defined benefit plan).

Active members on March 30, 1997, had an opportunity to irrevocably elect to terminate membership in Tier 1 and become participants in Tier 2. Elections were in writing and submitted between January 2, 1998 and April 30, 1998. Such members became Tier 2 participants on June 1, 1998, and had the actuarial present value of their Tier 1 accrued benefit transferred into Tier 2 by September 30, 1998.

STATISTICAL SECTION

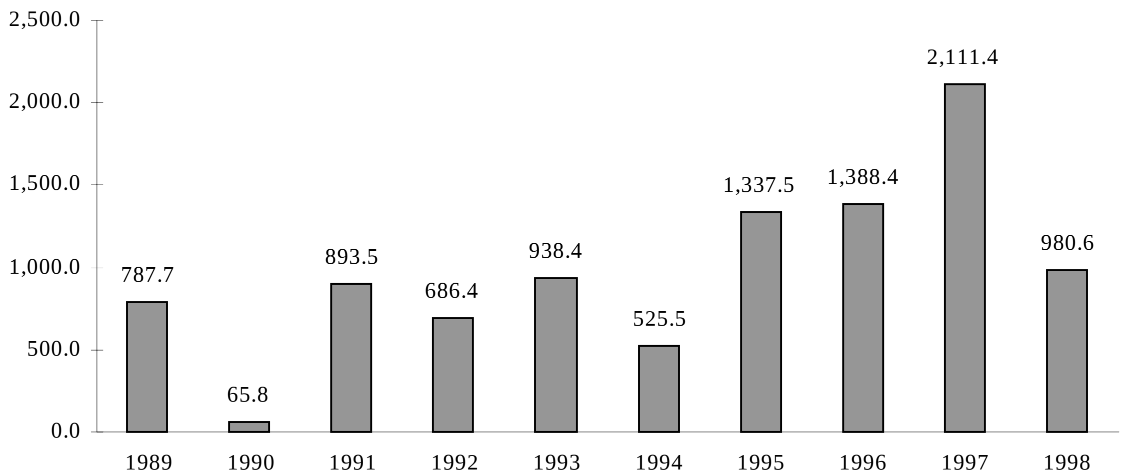
Schedule of Revenues by Source

Fiscal Year Ended Sept. 30	Member Contributions	Employer Contributions Dollars*	Employer Contributions % of Annual Covered Payroll	Net Investment & Other Income	Total
1989	$ 3,065,894	$ 162,046,886	8.12 %	$ 622,558,381	$ 787,671,161
1990	2,733,598	188,863,034	8.48	(125,829,294)	65,767,338
1991	4,416,336	227,348,243	10.17	661,760,771	893,525,350
1992	4,810,700	285,424,393	13.03	396,188,599	686,423,692
1993	4,068,696	371,902,232	17.02	562,436,683	938,407,611
1994	2,257,216	389,728,590	17.16	133,510,369	525,496,175
1995	2,260,510	422,294,609	17.98	912,938,131	1,337,493,250
1996	2,619,067	431,094,371	17.14	954,696,384	1,388,409,822
1997	15,858,366**	410,231,627	18.05	1,685,326,508	2,111,416,501
1998	9,777,845	259,799,179	12.32	711,056,989	980,634,013

* Includes financing for early retirement pensions

** Increase is attributable to purchase of service credit in connection with "early out" retirement.

Total Revenues
(In Millions)

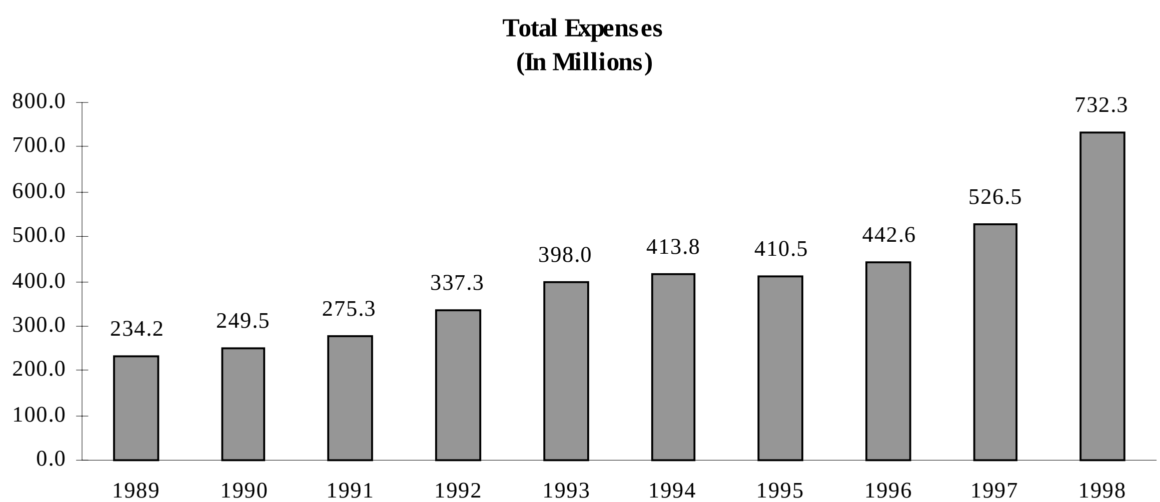


Schedule of Expenses by Type

Fiscal Year Ended Sept. 30	Benefit Payments*	Refunds and Transfers	Administrative Expenses	Total
1989	$ 231,499,226	$ 204,889	$ 2,461,919	$ 234,166,034
1990	246,339,702	125,828	2,993,159	249,458,689
1991	271,569,768	126,406	3,607,115	275,303,289
1992	333,082,770	123,792	4,047,661	337,254,223
1993	394,557,537	99,369	3,412,142	398,069,048
1994	409,975,308	92,153	3,777,812	413,845,273
1995	406,140,322	80,453	4,268,833	410,489,608
1996	439,056,397	30,082	3,489,761	442,576,240
1997	513,359,239	7,848,649**	5,247,943	526,455,831
1998	593,453,930	134,533,763**	4,297,092	732,284,785

* Includes health benefits.

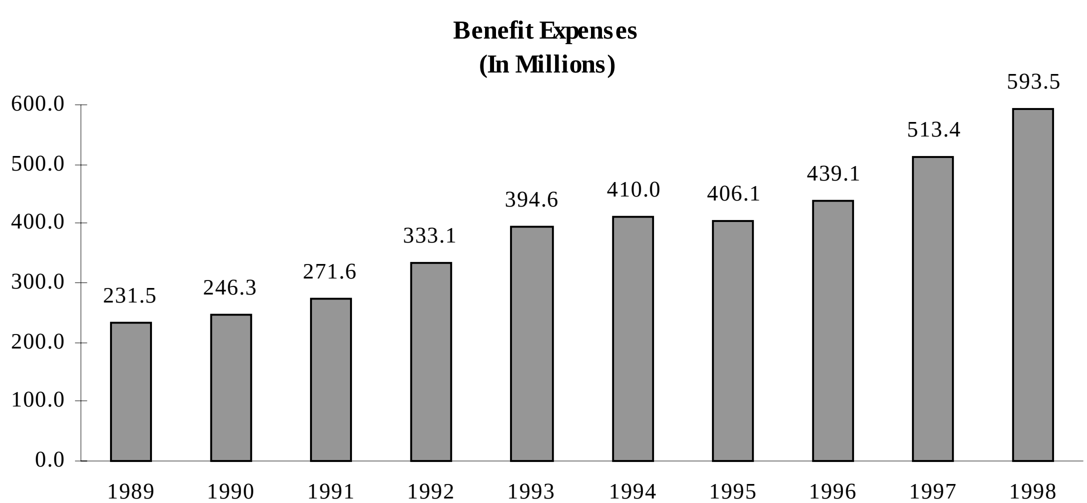
** Includes transfers to defined contribution plan in connection with the "early out" retirement.



Schedule of Benefit Expenses by Type

Fiscal Year Ended Sept. 30	Regular Benefits	Disability Benefits	Supplemental Check	Health Benefits**	Total
1989	$ 153,243,799	$ 9,928,141	$ 15,488,627*	$ 52,838,659	$ 231,499,226
1990	164,701,113	12,231,653		69,406,936	246,339,702
1991	178,896,021	11,827,319		80,846,428	271,569,768
1992	212,280,362	13,850,266		106,952,142	333,082,770
1993	245,615,207	14,725,503		134,216,826	394,557,536
1994	256,660,402	16,672,201		136,642,705	409,975,308
1995	269,206,552	20,494,647		116,439,123	406,140,322
1996	284,061,320	22,017,877	15,234,884	117,742,316	439,056,397
1997	331,964,200	26,069,505	24,832,674	130,492,860	513,359,239
1998	401,855,102	28,024,773		163,574,055	593,453,930

* Includes $88,674 paid in March 1989 and an estimated $15,399,953 paid in March 1990.
** Includes vision and dental benefits.



Schedule of Retired Members by Type of Benefit
September 30, 1998

Amount Monthly Benefit	Number of Retirees	Type of Retirement *								Selected Option**					
		1	2	3	4	5	6	7	8	Reg.	Opt. A	Opt. B	Opt. E	Opt. E1	Opt. E2
$ 1 - 200	1,491	772	455	9	179	35	22	1	18	520	432	358	151	18	12
201 - 400	5,303	3,401	906	31	724		176	1	64	2,384	1,458	979	363	57	62
401 - 600	5,901	3,583	573	380	878		285	7	195	2,959	1,577	947	328	45	45
601 - 800	4,620	3,122	343		581		242	17	315	2,073	1,283	918	244	40	62
801 - 1,000	3,992	2,729	216		377		154	42	474	1,781	1,157	773	173	47	61
1,001 - 1,200	3,677	2,620	186		183		112	32	544	1,514	1,095	742	204	54	68
1,201 - 1,400	2,857	2,187	109		70		70	35	386	1,004	870	656	211	45	71
1,401 - 1,600	2,175	1,758	65		47		40	49	216	755	676	452	182	52	58
1,601 - 1,800	1,682	1,455	32		14		28	60	93	468	575	334	176	48	81
1,801 - 2,000	1,302	1,152	22		5		14	63	46	326	445	265	152	53	61
Over 2,000	3,185	2,951	37		5		30	115	47	809	958	736	320	156	206
Totals	36,185	25,730	2,944	420	3,063	35	1,173	422	2,398	14,593	10,526	7,160	2,504	615	787

* Type of Retirement

1 - Normal retirement for age & service
2 - Survivor payment - normal or early retirement
3 - Duty disability retirement (incl. survivors)
4 - Non-duty disability retirement (incl. survivors)
5 - Survivor payment - duty death in service
6 - Survivor payment - non-duty death in service
7 - Retirees with supplemental benefits for early retirement incentive factors
8 - Retirees with reduced benefits for early retirement reduction factors

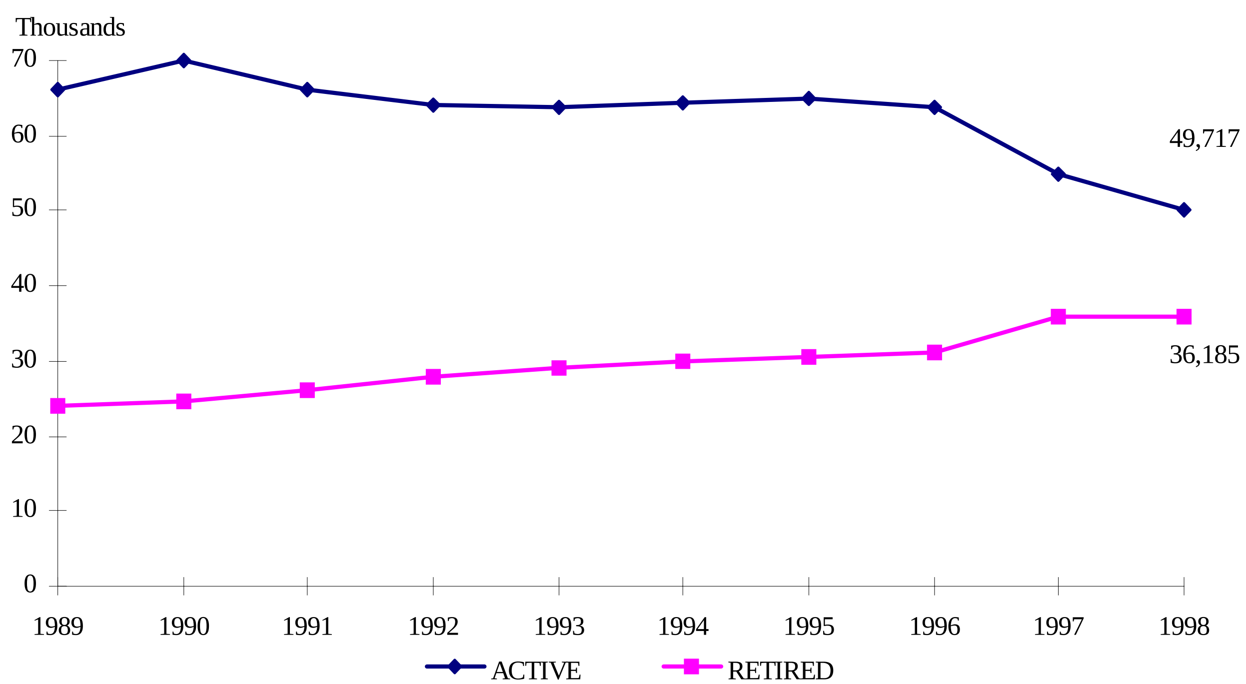
**Selected Option

Reg. - Straight life allowance
Opt. A - 100% survivor option
Opt. B - 50% survivor option
Opt. E - Social Security equated
Opt. E1 - Social Security equated w/100% survivor
Opt. E2 - Social Security equated w/50% survivor option

Schedule of Average Benefit Payments

Retirement Effective Dates	Average Yearly Benefit	Number of Active Retirants
Period 10/01/91 to 09/30/92	$ 8,442	28,856
Period 10/10/92 to 09/30/93	8,816	29,175
Period 10/01/93 to 09/30/94	9,124	29,962
Period 10/01/94 to 09/30/95	9,512	30,562
Period 10/01/95 to 09/30/96	9,904	31,093
Period 10/01/96 to 09/30/97	11,656	36,123
Period 10/01/97 to 09/30/98	11,952	36,185

10 Year History of Membership Fiscal Years Ended September 30



ACKNOWLEDGMENTS

The Michigan State Employees' Retirement System's Comprehensive Annual Financial Report is prepared by the Office of Retirement Services, Finance and Administration Division. Finance staff of the division for the fiscal year 1997-1998 report included:

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