State of Michigan 457 Plan

Financial Report

September 30, 2019

State of Michigan 457 Plan

Table of Contents

INDEPENDENT AUDITOR'S REPORT

OAG
Office of the Auditor General
Doug A. Ringler, CPA, CIA
Auditor General
201 N. Washington Square, Sixth Floor • Lansing, Michigan 48913 • Phone: (517) 334-8050 • audgen.michigan.gov

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

Ms. Tricia L. Foster, Director
Department of Technology, Management, and Budget
and
Ms. Kerrie L. Vanden Bosch, Director
Office of Retirement Services

Dear Ms. Foster and Ms. Vanden Bosch:

Report on the Financial Statements
We have audited the accompanying financial statements of the State of Michigan 457 Plan as of and for the fiscal year ended September 30, 2019 and the related notes to the financial statements, which collectively comprise the Plan's basic financial statements as listed in the table of contents.

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

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Doug A. Ringler, CPA, CIA
Auditor General

Ms. Tricia L. Foster, Director
Ms. Kerrie L. Vanden Bosch, Director
Page 2

Opinion
In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the fiduciary net position of the State of Michigan 457 Plan as of September 30, 2019 and the changes in fiduciary net position for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter
As discussed in Note 2, the financial statements present only the State of Michigan 457 Plan and do not purport to, and do not, present fairly the financial position of the State of Michigan or its pension (and other employee benefit) trust funds as of September 30, 2019 and the changes in financial position for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matter

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

Other Reporting Required by *Government Auditing Standards*
In accordance with *Government Auditing Standards*, we will also issue a report on our consideration of the Plan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Plan's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Plan's internal control over financial reporting and compliance.

Sincerely,

Doug Ringler

Doug Ringler
Auditor General
December 20, 2019

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis

This section presents our discussion and analysis of the State of Michigan 457 Plan's (the Plan's) financial performance and provides an overview of the Plan's financial activities for the fiscal years ended September 30, 2019, and September 30, 2018. This section should be read in conjunction with the Plan's basic financial statements.

Using This Annual Financial Report

This annual financial report consists of two parts: (1) management's discussion and analysis (this section) and (2) the Plan's basic financial statements. The Plan's basic financial statements are comprised of a Statement of Plan Fiduciary Net Position, a Statement of Changes in Plan Fiduciary Net Position, and Notes to the Financial Statements. The Statement of Plan Fiduciary Net Position reports the assets and liabilities of the Plan and the net position that is held on behalf of participants as of the end of the fiscal year. The Statement of Changes in Plan Fiduciary Net Position reports the additions and deductions to the Plan that occurred during the fiscal year. The notes explain some of the information in the financial statements and provide more detailed data.

Condensed Financial Information

The table below compares key financial information in a condensed format between the current and prior year:

	Fiscal Years Ended September 30 (in thousands)	
	2019	2018
Plan Net Position	$ 2,280,016	$ 2,227,552
Net investment gain (loss)	$ 49,545	$ 159,944
Contributions - Employees	178,995	144,116
Contributions - Employers	369	583
Contributions - Transfers from other systems	618	1,209
Benefits paid	(76,792)	(80,516)
Refunds and payments to other systems	(95,489)	(78,098)
Other income and expenses - net	(4,782)	(6,617)
Net Increase (Decrease) in Plan Net Position	$ 52,464	$ 140,622

Overall Fund Structure and Objectives

The Plan was originally established by the State of Michigan in 1974 for the exclusive benefit of eligible State of Michigan employees and their beneficiaries. The Plan has been amended and restated since the Plan's original adoption and retitled as the "State of Michigan 457 Plan". It was last restated in its entirety, effective January 1, 2012, and the restated Plan Document was last amended effective September 1, 2018.

The Plan was established as a means for State employees to save for retirement. Employees of the State of Michigan and judges are eligible to participate in the Plan as of the first day of employment and may voluntarily contribute a portion of their compensation up to the established Internal Revenue Code limits. The Plan was expanded in 2010 and 2012 to benefit eligible Michigan public school employees and their beneficiaries. Then in 2012, the Plan was further expanded to benefit eligible Michigan State Police and their beneficiaries, and to employees of the Education Achievement Authority (EAA) and their beneficiaries.

Effective August 11, 2014, public school employers were provided the option to sign up to offer public school employees a deferred compensation option through the State of Michigan 401K and 457 Plans. Public school employees enrolled in the defined benefit pension plan who were hired prior to July 1, 2010 and also elected to retain their premium subsidy health care are eligible to participate. The deferred compensation option extends the opportunity to invest in the 457 Plan, and it also allows rollovers to the 401K Plan.

On April 25, 2017, the EAA Executive Committee approved a Resolution Authorizing Dissolution of the Education Achievement Authority of Michigan. The EAA ceased to exist as a legal entity on June 30, 2017. No new contributions were made to the plan during the 2019 fiscal year.

On July 13, 2017, the Governor signed Public Act 92 of 2017 into law. The legislation requires public school employers to make a 4% non-matching contribution to the 401(K) Plan effective October 1, 2017 for all Michigan Public School Employees' Retirement System (MPSERS) Defined Contribution participants hired on or after September 4, 2012 and changed the matching contribution formula for all MPSERS Defined Contribution participants hired on or after

September 4, 2012 to a dollar-for-dollar match up to 3% of compensation effective February 1, 2018. Further, the legislation closed the current hybrid plan (Pension Plus) to newly hired employees as of February 1, 2018 and created a new optional revised hybrid plan (Pension Plus 2) with similar plan benefit calculations but containing a 50/50 cost share between the employee and the employer, including the cost of future unfunded liabilities.

On June 3, 2018, the Governor signed Public Act 169 of 2018 into law. The legislation requires public school employers to make a dollar-for-dollar matching contribution to the 401(K) Plan on up to 3% of gross wages deferred to the 457 Plan effective September 1, 2018 for all MPSERS members who had elected to convert to the Defined Contribution plan.

Asset Allocation

The State Treasurer, with the advice of the Department of Technology, Management, and Budget (DTMB), selects mutual funds, pooled funds, separate accounts, or other investment vehicles to pursue the Plan's investment objective, which are then made available by the trustee. Except as required under auto-enrollment in the State of Michigan 457 Plan Document, all participants have the ability to direct the investments of their accounts under the Plan, in accordance with the investment choices made available by the trustee and those policies or procedures determined by the administration from time to time. The Plan has no control over investment decisions made by the participants. Plan assets may be invested and reinvested in various instruments as deemed appropriate by the trustee and Plan management. Several investment tiers have been developed and made available to participants. A summary of the types of investments is listed in Note 3.

Investment Results

During fiscal year 2019, both the Dow Jones Industrial Average (the Dow) and Standard & Poor's 500 Index (S&P 500) outperformed the National Association of Securities Dealers Automated Quotations (NASDAQ) Composite Index. The Dow gained 4.21% and the S&P 500 gained 3.73% while the NASDAQ saw a slight decline of -0.17%.

The global business cycle continues to mature, with the US and most major economies in the late-cycle phase. Sagging trade and industrial activity continued to weigh on global growth, with the share of major countries with expanding manufacturing sectors dropping to its lowest level since 2012. This weakness occurred despite an upturn in Fidelity's diffusion index of China's industrial production. For the first time in the past decade, China's stimulus measures and manufacturing upswing have failed to lift global trade and industrial activity. While China's monetary and fiscal policy easing has helped stabilize industrial activity, high debt levels and US-China trade uncertainty supports the stance that material economic reacceleration remains unlikely.

The US is firmly in the late-cycle phase, but the economy remains supported by consumption, which represents around 70% of Gross Domestic Product (GDP). Historically, consumer spending and employment growth stay positive during the late cycle, typically not falling until the onset of recession. Several leading indicators suggest the labor market is nearing peak levels, including consumers' extremely favorable assessment of the job market, which tends to be most elevated just prior to recession.

10-year US Treasury yields dropped due to a decline in both inflation expectations and real interest rates, with both measures decreasing to near multi-year lows. Yields on 10-year Treasuries remained below 3-month Treasuries, keeping the yield curve inverted. Curve inversions have preceded the past 7 recessions and may be interpreted as the market signaling weaker expectations relative to current conditions.

Core inflation has been generally stable at about 2% in recent years, but tariff hikes have lately pushed goods prices upward, helping boost core Consumer Price Index (CPI) to a multi-year high. Tariffs also have negatively impacted demand—for example, last year's tariffs on washing machines both boosted prices and lowered consumption. The near-term inflation outlook remains balanced amid uncertain trade policy and downside economic risk.

Global central banks lowered interest rates during the 3rd quarter, and the Federal Reserve (the Fed) ended its balance-sheet drawdown while the European Central Bank (ECB) reinitiated quantitative easing.

However, the global liquidity backdrop is much less favorable than it was in 2016–2017, with US Treasury increases of cash held at the Fed offsetting recent central-bank accommodation. Monetary policy may be showing its limitations, with a number of challenges blunting the effects of easing.

Honors

Plan Sponsor Council of America (PSCA) Signature Award – For the second year in a row, the Office of Retirement Services (ORS) won a PSCA Signature Award. The 2019 award, which was presented during PSCA's 72nd annual National Conference in Tampa, Florida, was for the MPSERS Outreach campaign in the "Overcoming Obstacles" category. The Signature Award recognizes excellence in retirement plan communications.

The goal of the MPSERS Outreach campaign was to engage with MPSERS participants in the State of Michigan 401(k) and 457 Plans, many of whom were confused about the retirement changes that occurred in 2012, especially those participants that had to make an election to remain in their current plan or move to a new one. Because communication efforts did not focus on this group in the past, ORS wanted to offer seminars and 1-on-1 appointments presented by Voya Financials' local education office to these participants and to encourage them to engage with their accounts and the tools available to them online.

Contacting Management

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

BASIC FINANCIAL STATEMENTS

Statement of Plan Fiduciary Net Position (in thousands)

As of September 30, 2019

	State of Michigan Deferred Compensation Fund	Public School Deferred Compensation Fund	Education Achievement Authority - Deferred Compensation Fund	Total
Assets				
Equity in Common Cash	$ 200	$ 3,073	$ 24	$ 3,297
Participant-directed investments,				
at fair value/contract value (Note 3):				
Mutual funds	145,586	5,218	35	150,839
Common trust funds	811,226	464,465	5,454	1,281,146
Tier III investments	44,984	798	11	45,793
Stable Value Fund	533,044	1,511	44	534,599
Voya Small Cap Growth Strategy Fund	26,821	809		27,630
Jennison Large Cap Growth Equity Fund	77,782	2,581	2	80,365
Artisan U.S. Mid Cap Growth Stragety Fund	25,689	1,058	4	26,752
Dodge & Cox Stock Portfolio	117,365	2,240		119,605
Participant loans	6,757	3,031	18	9,806
Other receivable	47	3,515	1	3,563
Total assets	$ 1,789,502	$ 488,298	$ 5,594	$ 2,283,393
Liabilities				
Accounts Payable	$ 528	$ 2,238		$ 2,766
Unearned Revenue		611		611
Total liabilities	$ 528	$ 2,849		$ 3,377
Plan Net Position	$ 1,788,973	$ 485,449	$ 5,594	$ 2,280,016

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

Statement of Changes in Plan Fiduciary Net Position (in thousands)

For Fiscal Year Ended September 30, 2019

Additions to Net Position	State of Michigan Deferred Compensation Fund	Public School Deferred Compensation Fund	Education Achievement Authority - Deferred Compensation Fund	Total
Investment income (loss):				
Interest and Dividends	$ 16,779	$ 201	$ 2	$ 16,982
Net increase (decrease) in fair value of investments	15,414	16,984	164	32,563
Total investment income (loss)	$ 32,193	$ 17,185	$ 166	$ 49,545
Contributions:				
Employees	$ 46,294	$ 132,701		$ 178,995
Employers	369			369
Transfers from other systems	353	265		618
Total contributions	$ 47,016	$ 132,966		$ 179,982
Miscellaneous income	$ 1,293	$ 710	$ 6	$ 2,010
Total additions	$ 80,502	$ 150,862	$ 173	$ 231,536
Deductions from Net Position				
Benefits paid to participants	$ 68,423	$ 8,104	$ 266	$ 76,792
Administrative and investment expenses	3,196	3,573	22	6,791
Refunds and payments to other systems	91,256	4,058	175	95,489
Total deductions	$ 162,875	$ 15,735	$ 463	$ 179,072
Net increase (Decrease) in Net Position	$ (82,373)	$ 135,127	$ (290)	$ 52,464
Plan Net Position				
Beginning of fiscal year	$ 1,871,346	$ 350,322	$ 5,884	$ 2,227,552
End of fiscal year	$ 1,788,973	$ 485,449	$ 5,594	$ 2,280,016

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

NOTE 1 – GENERAL DESCRIPTION OF THE PLAN

The State of Michigan 457 Plan (the Plan) is a deferred compensation plan sponsored by the State of Michigan. The Plan is considered part of the State reporting entity and is included in the *State of Michigan Comprehensive Annual Financial Report* as a pension (and other employee benefit) trust fund. The Office of Retirement Services administers the Plan and the plan administrator has the authority to amend the Plan.

The following description provides only general information. Participants should refer to the Plan Document for a more complete description of the Plan's provisions. The Plan Document is available on the State of Michigan 401K and 457 plan website.

General

The Plan was established by the Civil Service Commission in 1974. The first enrollment was on April 17, 1975, with contributions starting in May 1975. The Plan Document was last restated effective January 1, 2012 to incorporate all amendments, update changes required by law, and add new sections for changes in provisions made since the previous restatement. The restated Plan Document was last amended effective September 1, 2018. As of September 30, 2019, the Plan included 23,660 State of Michigan participants, 106,262 Michigan public school participants (660 participating employers), and 561 participants of the former Educational Achievement Authority (EAA).

Eligibility

The following employees are eligible to participate in the Plan on the first day of employment:

- State of Michigan employees,
- Judges,
- Michigan State Police,
- Public school employees, and
- Former Education Achievement Authority employees (no new contributions).

Contributions

In accordance with Section 457 of the Internal Revenue Code, the Plan limits the amount of an individual's annual contribution, including additional catch-up contributions for those participants age 50 or older. Plan limits are adjusted each year by the Internal Revenue Service (IRS) based on increases in the Consumer Price Index (CPI).

The Plan provides for the Personal Healthcare Fund (PHF) for State of Michigan employees hired on or after January 1, 2012, public school employees hired on or after September 4, 2012 and Michigan State Police hired after June 10, 2012 to account for employee contributions and an employer match on up to 2% of compensation. State employees hired after March 31, 1997 but prior to January 1, 2012 and who opted out of the graded premium receive an employer match on up to 2% of compensation plus a monetized amount for existing years of service upon terminating employment. Public school employees hired prior to September 4, 2012 and who opted out of the graded premium also receive an employer match on up to 2% of compensation.

The EAA was dissolved effective June 30, 2017 and the plan no longer receives new EAA contributions; however, the plan will remain open as long as former EAA employee balances remain in the plan.

Contributions from Other Systems

Active employees or former employees during the first twelve (12) months following the retirement or other severance from employment, may roll over money from another governmental 457 plan into their State of Michigan 457 Plan account. Participants may withdraw funds rolled into the Plan at any time.

Participant Account

Each participant's account is credited with his or her contributions and an allocation of the Plan's earnings. Allocations are based on the participant's account balance to reflect the effect of income or losses from the particular investments. The benefit to which a participant is entitled is limited to the benefit that can be provided from the participant's account.

Vesting

Participants are 100% vested in their contributions and related earnings or losses at all times.

Loans to Participants

Participants of the plan may borrow from their account balances of the Plan in accordance with the loan policy statement. Loan amounts can range from a minimum of $1,000 to a maximum of $50,000. Loans must be repaid within five years, with the exception of residential loans, which may be extended up to thirty years. The interest rate on loans reflects a rate equal to the prime interest rate on the first day of the prior month.

Loans to Participants – Defaulted

Defaulted loans are loans resulting from the failure of a participant to make the required loan repayments on an outstanding loan. These loans are considered a distribution to the participant for which a federal 1099 tax form is issued. During fiscal year 2019 defaulted loans totaled $582.5 thousand for participants in the State of Michigan Deferred Compensation Retirement Fund, $398.1 thousand in the Public School Deferred Compensation Fund and $31.4 thousand in the EAA Deferred Compensation Fund.

Payment of Benefits

Participants may withdraw their funds upon leaving employment. Withdrawal of participant funds may be by lump sum, monthly payments, annual payments, or rollovers to other qualified plans or an Individual Retirement Account (IRA). Payments may occur over a period not to exceed life expectancy from the date that the payments begin. In-service benefit payments are permitted for various reasons as outlined in the Plan Document.

Refunds and Payments to Other Systems

Upon leaving employment, participants may, but are not required to, roll over all or a portion of their account balances to other qualified plans or an IRA, or they may use all or a portion of their account balances to purchase preapproved service credit in the State of Michigan's pension trust funds, if applicable.

Forfeited Accounts

Forfeited accounts totaled $44.6 thousand at September 30, 2019. As specified in the Plan Document, these accounts are to be used to restore forfeited assets when applicable, offset future employer contributions, and pay administrative expenses of the Plan.

Other Postemployment Benefits (OPEB)

The Plan's financial statements reflect the PHF activity for State employees, Michigan State Police, and public school employees participating in the PHF that are not eligible for subsidized health care benefits. The State employees eligible for subsidized health care benefits are included in the OPEB actuarial valuation provided for Michigan State Employees' Retirement System (MSERS) and reported in the MSERS financial statements. The public school employees eligible for subsidized health care are included in the OPEB actuarial valuation provided for the

Michigan Public School Employees' Retirement System (MPSERS) and reported in the MPSERS financial statements. The Michigan State Police eligible for subsidized health care are included in the OPEB actuarial valuation provided for the Michigan State Police Retirement System (MSPRS) and reported in the MSPRS financial statements. For more information regarding these OPEB, please refer to the separately issued retirement system comprehensive annual financial reports.

Tax Status

The U.S. Department of Treasury made its most recent issuance of a Private Letter Ruling on February 19, 2010, that the Plan constitutes an eligible deferred compensation plan as defined in section 457(b) of the Code and the trust associated with the Plan satisfies all applicable requirements of section 457(g), and will be treated as and is, therefore, exempt from federal income tax under section 501(a). Although the Plan may be subsequently amended and restated, management believes that the Plan will continue to operate as an eligible deferred compensation plan and trust.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). The accompanying financial statements present only the State of Michigan 457 Plan. Accordingly, they do not purport to, and do not, present fairly the financial position and the changes in financial position of the State of Michigan as a whole or its pension (and other employee benefit) trust funds in conformity with accounting principles generally accepted in the United States of America.

Measurement Focus and Basis of Accounting

The Plan uses the economic resources measurement focus and the accrual basis of accounting. Employee contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions.

Investments

Investments in the mutual funds, common trust funds, Voya Small Cap Growth Strategy Fund, Jennison Large Cap Growth Equity Fund, Artisan U.S. Mid Cap Growth Strategy Fund, Dodge & Cox Stock Portfolio, and Tier III investments are stated at fair value based on quoted market prices. The Stable Value Fund is stated at contract value (see Note 3 for additional information). The mutual funds are registered with the Securities and Exchange Commission, and guaranteed investment contracts (GICs) are regulated by state insurance departments. Investments in common trust funds are managed by State Street Global Advisors (SSgA), BlackRock, and the Prudential Trust Company. Common trust funds are similar to mutual funds though not registered like mutual funds are. The value of the Plan's position in the common cash fund is equivalent to the fair value of the common cash fund shares.

Investments measured at fair value are determined based on the market approach, which utilizes prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. The fair value of publicly traded fixed income and equity securities is based upon quoted market prices and exchange rates, when applicable.

Participant Loans

Participant loans are stated at the outstanding principal amount.

NOTE 3 – INVESTMENTS

The State Treasurer, with the advice of the Department of Technology, Management, and Budget (DTMB), selects mutual funds, pooled funds, separate accounts, or other investment vehicles to pursue the Plan's investment objective, which are then made available to participants by the trustee. Except as required under auto-enrollment in the State of Michigan 457 Plan document, all participants have the ability to direct the investments of their accounts under the Plan, in accordance with the investment choices made available by the trustee and those policies or procedures determined by the administration from time to time.

Three investment tiers have been developed to classify the investments available to participants, based upon the general investment strategy. Tier I contains funds that have a passive investment strategy. These investments are managed to mirror investment performance of an established index. Tier II contains funds that have an active investment strategy. These investments are managed actively by an investment advisor using a specific fund investment objective. Tier III contains accounts with investments that are self-directed by the participant. These are not managed passively or actively by anyone other than the participant. A brief summary of the types of investments included in each tier follows:

Tier I - Common trust funds include BlackRock Government Short-Term Investment Fund, State Street U.S. Bond Index Fund, State Street S&P 500 Index Fund, State Street S&P Mid Cap Index Fund, BlackRock S&P Small Cap 600 Equity Index Fund, State Street Global All Cap Equity ex-U.S. Index Fund, BlackRock Emerging Markets Index Fund, State Street Target Retirement Income Fund, and State Street Target Retirement Funds ranging in retirement dates from 2015 through 2060. All of the BlackRock funds employ the unitized accounting method.

Tier II - Two of the Tier II funds (PIMCO Total Return Fund and American Funds EuroPacific Growth Fund R6) are mutual funds that employ the traditional share accounting method in which dividends are directly applied to participant accounts. The Prudential High Yield Fund is a common trust fund that also employs the traditional share accounting method. Three of the Tier II funds (Oakmark Equity and Income Fund, T. Rowe Price Mid-Cap Value Fund, and

Virtus Ceredex Small-Cap Value Equity Fund) are mutual funds that employ a unitized accounting method in which dividends are applied to the pooled investment account. Other Tier II investments that include the Stable Value Fund, Voya Small Cap Growth Strategy Fund, Jennison Large Cap Growth Equity Fund, Artisan U.S. Mid-Cap Growth Strategy Fund, and Dodge & Cox Stock Portfolio, all employ the unitized accounting method and are designed for the exclusive use and benefit of State of Michigan 401K Plan and 457 Plan participants. The funds are unitized to eliminate the impact of revenue sharing on pricing. Unitization also allows the cash holding percentage of each unitized fund to be established between the plan sponsor and the trustee, which reduces the need to trade underlining securities of the investment option on a daily basis and, therefore, the commission cost of trading those securities can be minimized.

Tier III - Individual stocks and bonds and thousands of mutual funds (load, no-load, and no-fee/no-load) from a multitude of fund families are available through the Plan's third party administrator. The various types of investments within Tier III are self-managed by the participants and are not separately classified by type of investment by the Plan's third party administrator. These self-managed stocks, bonds, mutual funds, covered call options and Exchange Traded Funds are presented on the statement of plan net position within the Tier III investments.

Investment Risk:

The Plan's investments are subject to several types of risk. As of September 30, 2019, the Plan did not have any investments subject to custodial credit risk or concentration of credit risk. Other types of risk are examined in more detail on the following page:

a. Interest Rate Risk

Interest rate risk is the risk that the value of investments will decrease as a result of a rise in interest rates. The Plan's investment policy does not restrict investment maturities. As of September 30, 2019 the weighted average maturities of investments subject to interest rate risk are shown below (in thousands):

Investment Type	Fair Value/ Contract Value		Weighted Average Maturity (Years)
Stable Value Fund:			
Synthetic contracts*	$	534,599	3.83
Common trust funds:			
State Street U.S. Bond Index Fund	$	186,760	7.91
BlackRock Government Short-Term Investment Fund	$	29,062	0.08
Prudential High Yield Fund	$	7,718	4.73
Mutual Funds:			
PIMCO Total Return Fund	$	27,997	7.65
Oakmark Equity and Income Fund	$	21,959	2.90

*These investments are reported at contract value as disclosed in Note 2.

b. Credit Risk

Credit risk is the risk that an issuer or another counterparty to an investment will not fulfill its obligation. The Plan has an investment policy that limits its investment choices. The investment choices offered to participants are defined by tiers as described in the preceding paragraphs. As of September 30, 2019 the credit quality ratings of debt securities subject to credit risk (other than U.S. government securities) are shown on the following page (in thousands):

Investment Type	Fair Value/ Contract Value	Duration	Rating	Rating Organization
Stable Value Fund:				
Synthetic contracts*	$ 534,599	Long-term	A to AAA	S&P
Common trust funds:				
State Street U.S. Bond Index Fund	$ 186,760	Long-term	Baa to Aaa	Moody's
BlackRock Government Short-Term Investment Fund	$ 29,062	Short-term	A-1+	S&P
Prudential High Yield Fund	$ 7,718	Long-term	CCC to AAA	S&P
Mutual Funds:				
PIMCO Total Return Fund	$ 27,997	Short-term	B to A1+	S&P
		Long-term	Below B to AAA	S&P
Oakmark Equity and Income Fund**	$ 21,959		Not Rated	

*These investments are reported at contract value as disclosed in Note 2.

** This is a composite fund which is not rated separately by the rating agencies.

c. Foreign Currency Risk

Foreign currency risk is the risk that investments in securities traded in foreign currencies or more directly in foreign currencies may decline in value relative to the U.S. dollar, which may reduce the value of the portfolio. The Plan does not have an investment policy addressing foreign currency risk. As of September 30, 2019 the following investments (other than U.S. government securities) shown on the following page were subject to foreign currency risk (in thousands):

Investment Type	Foreign Currency	Fair Value
Mutual funds:		
American Funds EuroPacific Growth Fund R6	Various	$ 61,360
Oakmark Equity and Income Fund	Various	$ 21,959
T. Rowe Price Mid-Cap Value Fund	Various	$ 23,539
PIMCO Total Return Fund	Various	$ 27,997
Virtus Ceredex Small-Cap Value Equity Fund	Various	$ 15,983
Common Trust funds:		
State Street Global All Cap Equity ex-U.S. Index Fund	Various	$ 110,478
Prudential High Yield Fund	Various	$ 7,718
BlackRock Emerging Markets Index Fund	Various	$ 23,579
Separate accounts:		
Jennison Large Cap Growth Equity Fund	Various	$ 80,365
Dodge & Cox Stock Portfolio	Various	$ 119,605

Fully Benefit Responsive Synthetic Guaranteed Investment Contract (SGIC):

As part of the Stable Value Fund, the Plan uses SGIC investment derivatives that invest in a portfolio of underlying securities and a benefit response wrap contract. The wrap contract produces a floating rate of return that is adjusted periodically, but not below zero, to reflect the underlying investment portfolio and generally provides for participant withdrawals at contract value (principal plus accrued interest). As of September 30, 2019, the fair values of SGIC are shown below (in thousands):

	Fair Value
SGIC Components:	
Underlying investments	$ 553,129
Wrap contract	*
Total	$ 553,129

* The market value of the SGIC's underlying investments was higher than the SGIC's contract value; therefore, the wrap contract does not have a value.

Fair Value of Investments

Investments are recorded at fair value in accordance with GASB Statement No. 72, *Fair Value Measurement and Application*, which establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Observable inputs reflect market data obtained from sources independent of the reporting entity. Unobservable inputs reflect the entity's own assumptions about how market participants would value an asset or liability based on the best information available. Valuation techniques used to measure fair value maximize the use of observable inputs and minimize the use of unobservable inputs. Accordingly, the change in fair value of investments is recognized as an increase or decrease to investment assets and investment income.

The Plan categorizes fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset.

a. Level 1 debt and equity securities are valued using quoted prices in active markets for the actual or identical securities. Market price data is generally obtained from relevant exchanges or dealer markets.

b. Level 2 securities are valued using significant other observable securities.

c. Level 3 securities are valued using significant unobservable inputs.

The Plan has the following recurring fair value measurements as of September 30, 2019 shown below (in thousands):

		Fair Value Measurements Using		
	9/30/2019	Quoted Prices In Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level				
Mutual Funds	$ 150,839	$ 150,839		
Common trust funds	1,281,146	895,398	$ 385,748	
Tier III Investments*	38,588		38,588	
Stable Value Fund	534,599		534,599	
Voya Small Cap Growth Strategy Fund	27,630		27,630	
Jennison Large Cap Growth Equity Fund	80,365	80,365		
Artisan U.S. Mid Cap Growth Strategy Fund	26,752		26,752	
Dodge & Cox Stock Portfolio	119,605		119,605	
Total Investments by fair value	$ 2,259,523	$ 1,126,602	$ 1,132,921	$ -

*Tier III investments exclude cash held in participant accounts totaling approximately $7.2 million.

The fair value of debt and equity securities classified in Level 1 at September 30, 2019 were valued using prices quoted in active markets for those securities. The fair value of debt securities classified in Level 2 at September 30, 2019 was based on the value of their underlying investments, which include, but are not limited to, treasury bills, government and corporate bonds, mortgage backed securities, and asset backed securities.

The State Street S&P 500 Index Fund, State Street S&P Mid Cap Index Fund, State Street Target Retirement Income Fund, and State Street Target Retirement Funds, within the common trust funds, are classified as Level 1. All other common trust funds, which are similar to mutual funds though not registered like mutual funds, are Level 2 because their fair value is determined by the fund manager based on the value of each underlying investment within their respective pooled investment account. The fair value of the State Street Target Retirement Income Fund and State Street Target Retirement Funds, within the common trust funds, was based on the units of the underlying funds that make up each Target Retirement fund, which may include, but are not limited to, the State Street S&P 500 Index Fund, State Street Russel Small/Mid Cap Index Fund, State Street Global All Cap Equity ex-U.S. Index Fund, State Street Bloomberg Roll Select Commodity Index Fund, and State Street government and corporate bond funds. The value of the

Stable Value Fund was also based on the value of its underlying investments, which include a Synthetic GIC issued by Voya Retirement Insurance and Annuity Company. The Jennison Large Cap Growth Equity Fund is classified as Level 1 and the Voya Small Cap Growth Strategy Fund, Artisan U.S. Mid Cap Growth Strategy Fund, and Dodge & Cox Stock Portfolio are all classified as Level 2 because a portion of their value was based on assets held within State Street's Short-Term Investment Fund (STIF) for liquidity purposes. The Tier III investments are classified as Level 2 based on the value of its underlying investments, a portion of which are classified as Level 2.

The Plan does not contain any debt or equity securities classified in Level 3.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Plan's assessment of the significance of particular inputs to these fair value measurements requires judgement and considers factors specific to each asset or liability.