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payments over two decades to retirees and active employees' retirement accounts instead of reinvesting the extra earnings for the future, according to a Free Press review of city records.

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One of Detroit’s two pension funds handed out nearly $1 billion in bonus cash payments over two decades to retirees and active employees’ retirement accounts instead of reinvesting the extra earnings for the future, according to a Free Press review of city records.

The payments, often referred to as a “13th check,” contributed to Detroit’s financial crisis and its historic Chapter 9 bankruptcy filing by increasing the amount the city needed to contribute each year to keep the pension fund solvent.

Had the city’s General Retirement System held on to the excess cash, the city might not have felt the need to borrow $1.44 billion in 2005 to plug the city’s unfunded pension liabilities gap, the Free Press found. That debt has ballooned to nearly one-fifth of the city’s total debt today and played a role in pushing the city into filing the largest municipal bankruptcy in the nation’s history in July.

— Full coverage: Detroit’s financial crisis

“If it had been reinvested, maybe it’s worth a billion and a half today,” said Ed Rago, who served as budget director for Mayor Coleman Young for several years and then as budget director for Mayor Dennis Archer for one year. “It’s always been a bug in my ass. Always angry about that.”

It’s unclear exactly how much extra money was distributed from the city’s other pension fund that covers police and fire service employees. Officials, however, have told the Free Press it was a much less frequent practice and that it happened in earnest for only a few years. An unofficial tabulation by Rago puts the bonus figure



"Things were always bad for employees," she said. "It was a way to make up for lots of the years that there were no pension increases."

Annual pensions for the vast majority of retired city employees are modest. The average annual pension for retired Detroit police officers and firefighters is about $34,000, and for retirees from Detroit's general city pension fund the average is less than $20,000.

How payments add up

No one is getting wealthy off of 13th checks, but the cumulative effect of distributing the bonuses to about 20,000 retirees and also as annuity bonuses for active employees over time has destabilized the funds and the city's budget, Detroit emergency manager Kevyn Orr and others contend.

By the time the practice was outlawed, the General Retirement System board, which represents nonuniform employees, had already distributed $951 million in excess earnings from 1985 to 2008, according to an actuarial report performed for the council in 2011 by independent statistician Joseph Esuchanko.

He estimated that the total accumulated cost to the city of not leaving the excess payments in the funds to grow with interest would be $1.9 billion as of June 30, 2008, a figure that would likely have grown even higher by today.

The 13th checks were distributed when the pension fund's investments outperformed annual expectations. The extra bucks were given to active workers' annuity accounts and to retirees usually as an extra monthly payment.

The excess payments, coupled with then-Mayor Kwame Kilpatrick's decision to borrow $1.44 billion to plug a hole in the pension funds, amplified the city's financial crisis.

Even after the city used borrowed cash to fund the pensions, pension trustees



The city is expected to release the results of a 60-day internal investigation and audit into the pension funds' practices as soon as this week, potentially giving more ammunition for Orr to remove current trustees.

Checks called justified

The practice of distributing 13th checks and annuity bonuses dates back at least to the mid-1980s. The funds also raised benefits year after year for decades through a cost-of-living allowance and through higher benefits negotiated by city unions. Unions have been allowed to represent public employees since the 1970s. The total payments are difficult to find in pension and city records because they are often hidden among cost-of-living adjustments and other types of payouts.

Michael VanOverbeke, an attorney representing the General Retirement System, said the 13th checks were justified by double-digit returns on pension investments over many years. He blamed the funds' current stress on the Great Recession and the collapse of the stock market in 2008 and 2009, which devastated pension funds around the nation.

Studzinski said that during her tenure, the excess funds were distributed equally among retirees, active employees and the city's pension funds. But years later, the GRS board tweaked the percentages, giving more to workers, she said.

It's unclear from existing records exactly how much of the extra earnings in good years was left in the funds and how much was given out as 13th checks to retirees and annuity bonuses to active employees.

An 'abuse of discretion'

On one of his first days in office in January 1994, Mayor Archer met with Rago and



opposition.

"I tried to get rid of the 13th check," he told the Free Press last week. "That's a whole lot of money that if it was in the pension fund today, that may have made a difference in terms of where the pension fund stands."

John Riehl, the current vice chairman of the GRS, who declined to comment through a spokeswoman, has defended the practice in the past.

"Many retirees relied on that check to pay their increased utility bills during the winter," he wrote in a trustees report Dec. 4, 2011. "Also remember that the money would go directly into the local economy."

An audit report from Conway MacKenzie, filed by Orr's team in bankruptcy court on July 18, highlighted a move by the GRS in 2009 that increased active employees' pension annuity accounts by 7.5%, even though the overall pension fund lost 24.1% of its value that same year. The report called it a particularly "egregious" move and an "abuse of discretion."

"And they did so by taking GRS assets attributable to city contributions to fund defined benefit pensions, and reallocating those assets to the annuity savings plan, thus effectively robbing GRS of precious funds necessary to support the traditional pensions the city had promised," wrote Conway MacKenzie consultant Charles Moore, who prepared the report.

"Hundreds of millions of dollars of plan assets intended to support the city's traditional defined benefit pension arrangements were converted by GRS trustees to provide a windfall to the annuity savings accounts of active employees outside of the defined benefit pension plan."

Optimistic projections

Debate is swirling over the health of the city's pension funds, a critical question in



have been too optimistic at 7.9% and 8%, and that 6.3% to 6.7% is a safer, more responsible assumed rate of return.

The pension fund boards disagree and say that 8% expected annual returns are realistic and reflect historic market performance. They say as a result the funds are actually healthy, and Orr is overreacting.

Pension fund trustees and other officials also say any unfunded liabilities can be blamed on the global financial crisis and past trustees' poor investment decisions.

"The investment world changed when the economy collapsed in 2008. The Detroit General Retirement System experienced the same economic difficulties experienced by everyone else throughout the country due to the worst economic crisis since the Great Depression," GRS spokeswoman Tina Bassett said in a statement after a phone call with the Free Press and e-mail exchanges for this story.

"The Detroit General Retirement System today is well managed, transparent, responsible and accountable. The last two years have been profitable and stable under the direction of the current Board. Our internal reviews continue to show that the funds are on sound footings. The Board of Detroit General Retirement System is totally focused on looking out for the best interests of its members and beneficiaries."

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