

PERAC AUDIT REPORT



Salem Contributory Retirement System

JAN. 1, 2005 - DEC. 31, 2007



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PERAC

COMMONWEALTH OF MASSACHUSETTS | PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION COMMISSION

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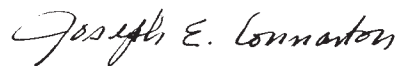
July 3, 2008

The Public Employee Retirement Administration Commission has completed an examination of the Salem Retirement System pursuant to G.L. c. 32, § 21. The examination covered the period from January 1, 2005 to December 31, 2007. This audit was conducted in accordance with the accounting and management standards established by the Public Employee Retirement Administration Commission in regulation 840 CMR 25.00. Additionally, all supplementary regulations approved by PERAC and on file at PERAC are listed in this report.

In our opinion, the financial records are being maintained and the management functions are being performed in conformity with the standards established by the Public Employee Retirement Administration Commission, with the exception of those noted in the findings presented in this report.

In closing, I acknowledge the work of examiners Carol Niemira and James Ryan who conducted this examination, and express appreciation to the Board of Retirement and staff for their courtesies and cooperation.

Sincerely,



Joseph E. Connarton
Executive Director



EXPLANATION OF FINDINGS AND RECOMMENDATIONS

I. **Membership**

The auditor reviewed the city payroll and observed nine employees who worked between 20 and 35 hours during the week sampled and therefore appeared to qualify for Salem Retirement System membership, but who were instead contributing to a deferred compensation plan. An initial sampling of the school payroll also disclosed employees who did not appear to qualify for Massachusetts Teachers' Retirement System membership and did appear to qualify for Salem Retirement System membership, but were contributing to a deferred compensation plan. This appears to be a violation of G. L. c. 32, § 3(2)(a) and § 3(2)(d), and Salem Retirement System supplementary membership regulations approved by PERAC, which define requirements for system membership.

Recommendation:

Employees who qualify under Salem Retirement System supplementary regulations approved by PERAC on February 4, 1986 and July 19, 1990 must become members of the system. A thorough review of payroll records should be conducted to determine which employees have worked the minimum number of hours on a regular basis to qualify for retirement system membership. Those who do qualify must be enrolled, and the payroll department must begin withholding retirement deductions at 9% plus an additional 2% for regular compensation over \$30,000. These new members may purchase creditable service at no interest for all prior service during which they were erroneously excluded from membership, and their deduction rates will be adjusted, if applicable, after such payment. The auditor is aware that the Board has already accepted an application from at least one of these employees, but has been unsuccessful in collecting retirement deductions from her payroll. The Board must be prepared to take all steps necessary to ensure that eligible employees may become members, including legal recourse, if necessary.

Board Response:

The Retirement Board has made the Human Resource department of the City aware of the audit finding and necessity to make sure that all eligible employees are in the retirement system. We are working with the City to correct any errors or omissions in the system.

2. **Expenses Paid**

PERAC auditors reviewed expenses paid over the three year audit period from the cash operating account. During this review it was observed that travel expenses were often charged to the General Ledger (GL) Administrative Expense Account #5589. These charges consisted of airfare, cab-fare, mileage reimbursements, hotel costs, and seminar registrations. In addition, staff and Board member travel expense reports were not consistently prepared and reflective of all travel costs associated with the business trip or educational seminar

EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

Recommendation:

All travel expenses including hotel charges need to be reported on the Board or staff member's related expense report. The travel expenses should always be charged to GL #5719 Travel Expense.

Board Response:

The retirement staff will continue to work to ensure that all expenses are posted to the correct accounts, and that all Board and Staff travel expense reports are consistently prepared in the same manner.

Administrative Observation

In April 2005 the Salem Retirement System purchased an office condominium to house its administrative operation. The purchase cost of approximately \$150,000 was charged to Administrative Expense GL #5589. GASB 34 currently requires governmental units to capitalize real estate structures and equipment as a fixed asset. Along with this requirement would be a yearly depreciation expense outlay. PERAC is finalizing the accounting guidelines for these processes and will require accounting adjustments to reclassify the amounts of buildings and condominiums expensed. At the time these guidelines are finalized, the Salem Retirement System should make appropriate accounting adjustments. The assistance of PERAC's audit unit will be available for any help with these accounting adjustments.

FINAL DETERMINATION:

PERAC Audit staff will follow up in six (6) months to ensure appropriate actions have been taken regarding all findings.

STATEMENT OF LEDGER ASSETS AND LIABILITIES

	AS OF DECEMBER 31,		
	2007	2006	2005
Net Assets Available For Benefits:			
Cash	\$6,958,829	\$4,688,313	\$4,860,859
Short Term Investments*	68,070,170	2,322,518	1,914,202
Fixed Income Securities	206,793	10,975,042	10,446,958
Equities	4,104	4,422,579	11,334,087
Pooled Domestic Equity Funds	10,500	43,726,574	35,649,522
Pooled International Equity Funds	0	14,823,794	8,467,297
Pooled Domestic Fixed Income Funds	7,065,720	0	0
Pooled Alternative Investment Funds	7,736,757	3,308,388	3,274,408
Pooled Real Estate Funds	7,339,842	9,195,962	6,257,311
Interest Due and Accrued	142,365	140,796	130,307
Accounts Receivable	3,188,131	187,767	440,617
Accounts Payable	(56,067)	(113,931)	(594,597)
Total	<u>\$100,667,145</u>	<u>\$93,677,802</u>	<u>\$82,180,973</u>
Fund Balances:			
Annuity Savings Fund	\$31,115,446	\$28,877,144	\$27,167,198
Annuity Reserve Fund	8,264,239	8,686,946	8,914,410
Pension Fund	867,735	46,643	151,165
Military Service Fund	743	739	734
Expense Fund	0	0	0
Pension Reserve Fund	60,418,983	56,066,330	45,947,465
Total	<u>\$100,667,145</u>	<u>\$93,677,802</u>	<u>\$82,180,973</u>

*2007 figure includes transitional cash invested in PRIT in January 2008

STATEMENT OF CHANGES IN FUND BALANCES

	Annuity Savings Fund	Annuity Reserve Fund	Pension Fund	Military Service Fund	Expense Fund	Pension Reserve Fund	Total All Funds
Beginning Balance (2005)	\$25,177,803	\$9,512,021	(\$4,048,970)	\$730	\$0	\$48,083,503	\$78,725,088
Receipts	3,025,832	273,658	7,128,822	4	878,198	4,372,767	15,679,282
Interfund Transfers	(536,280)	536,280	6,508,806	0	0	(6,508,806)	0
Disbursements	(500,156)	(1,407,550)	(9,437,493)	0	(878,198)	0	(12,223,397)
Ending Balance (2005)	27,167,198	8,914,410	151,165	734	0	45,947,465	82,180,973
Receipts	3,272,629	261,571	9,025,371	4	1,038,028	10,563,955	24,161,559
Interfund Transfers	(882,355)	894,467	432,978	0	0	(445,090)	0
Disbursements	(680,328)	(1,383,502)	(9,562,871)	0	(1,038,028)	0	(12,664,730)
Ending Balance (2006)	28,877,144	8,686,946	46,643	739	0	56,066,330	93,677,802
Receipts	3,468,329	254,259	9,513,315	4	1,066,496	5,596,408	19,898,811
Interfund Transfers	(765,397)	770,185	1,238,966	0	0	(1,243,755)	0
Disbursements	(464,630)	(1,447,152)	(9,931,190)	0	(1,066,496)	0	(12,909,468)
Ending Balance (2007)	<u>\$31,115,446</u>	<u>\$8,264,239</u>	<u>\$867,735</u>	<u>\$743</u>	<u>\$0</u>	<u>\$60,418,983</u>	<u>\$100,667,145</u>

STATEMENT OF RECEIPTS

	FOR THE PERIOD ENDING DECEMBER 31,		
	2007	2006	2005
Annuity Savings Fund:			
Members Deductions	\$2,797,506	\$2,695,966	\$2,663,354
Transfers from Other Systems	351,767	267,020	140,009
Member Make Up Payments and Re-deposits	132,233	97,731	62,563
Member Payments from Rollovers	17,385	53,447	11,360
Investment Income Credited to Member Accounts	<u>169,437</u>	<u>158,466</u>	<u>148,546</u>
Sub Total	<u>3,468,329</u>	<u>3,272,629</u>	<u>3,025,832</u>
Annuity Reserve Fund:			
Investment Income Credited to the Annuity Reserve Fund	<u>254,259</u>	<u>261,571</u>	<u>273,658</u>
Pension Fund:			
3 (8) (c) Reimbursements from Other Systems Received from Commonwealth for COLA and Survivor Benefits	127,394	125,978	119,503
Pension Fund Appropriation	<u>209,795</u>	<u>431,290</u>	<u>464,330</u>
Sub Total	<u>9,176,126</u>	<u>8,468,103</u>	<u>6,544,989</u>
Military Service Fund:			
Contribution Received from Municipality on Account of Military Service	0	0	0
Investment Income Credited to the Military Service Fund	<u>4</u>	<u>4</u>	<u>4</u>
Sub Total	<u>4</u>	<u>4</u>	<u>4</u>
Expense Fund:			
Expense Fund Appropriation	0	0	0
Investment Income Credited to the Expense Fund	<u>1,066,496</u>	<u>1,038,028</u>	<u>878,198</u>
Sub Total	<u>1,066,496</u>	<u>1,038,028</u>	<u>878,198</u>
Pension Reserve Fund:			
Federal Grant Reimbursement	0	0	30,195
Pension Reserve Appropriation	0	0	1,477,372
Interest Not Refunded	12,243	7,987	3,227
Miscellaneous Income	0	0	0
Excess Investment Income	<u>5,584,165</u>	<u>10,555,968</u>	<u>2,861,974</u>
Sub Total	<u>5,596,408</u>	<u>10,563,955</u>	<u>4,372,767</u>
Total Receipts	<u><u>\$19,898,811</u></u>	<u><u>\$24,161,559</u></u>	<u><u>\$15,679,282</u></u>

STATEMENT OF DISBURSEMENTS

	FOR THE PERIOD ENDING DECEMBER 31,		
	2007	2006	2005
Annuity Savings Fund:			
Refunds to Members	\$278,633	\$415,081	\$270,620
Transfers to Other Systems	<u>185,997</u>	<u>265,247</u>	<u>229,536</u>
Sub Total	<u>464,630</u>	<u>680,328</u>	<u>500,156</u>
Annuity Reserve Fund:			
Annuities Paid	1,425,021	1,383,502	1,355,159
Option B Refunds	<u>22,131</u>	<u>0</u>	<u>52,391</u>
Sub Total	<u>1,447,152</u>	<u>1,383,502</u>	<u>1,407,550</u>
Pension Fund:			
Pensions Paid:			
Regular Pension Payments	6,736,404	6,509,618	6,369,684
Survivorship Payments	443,037	443,552	480,580
Ordinary Disability Payments	101,586	128,096	123,133
Accidental Disability Payments	1,757,609	1,565,494	1,537,994
Accidental Death Payments	563,792	511,104	546,030
Section 101 Benefits	65,155	77,953	60,497
3 (8) (c) Reimbursements to Other Systems	263,607	242,896	234,944
State Reimbursable COLA's Paid	0	84,158	84,633
Chapter 389 Beneficiary Increase Paid	<u>0</u>	<u>0</u>	<u>0</u>
Sub Total	<u>9,931,190</u>	<u>9,562,871</u>	<u>9,437,493</u>
Military Service Fund:			
Return to Municipality for Members Who Withdrew Their Funds	<u>0</u>	<u>0</u>	<u>0</u>
Expense Fund:			
Board Member Stipend	15,910	18,000	18,593
Salaries	167,533	162,654	149,713
Legal Expenses	20,303	10,370	6,393
Medical Expenses	0	0	0
Travel Expenses	3,417	4,569	6,467
Administrative Expenses	116,566	69,882	187,196
Furniture and Equipment	7,949	3,234	3,264
Management Fees	570,711	617,736	387,130
Custodial Fees	51,422	50,938	43,838
Consultant Fees	42,936	56,990	40,000
Rent Expenses	0	0	5,014
Service Contracts	62,187	35,578	23,092
Fiduciary Insurance	<u>7,562</u>	<u>8,079</u>	<u>7,499</u>
Sub Total	<u>1,066,496</u>	<u>1,038,028</u>	<u>878,198</u>
Total Disbursements	<u><u>\$12,909,468</u></u>	<u><u>\$12,664,730</u></u>	<u><u>\$12,223,397</u></u>

INVESTMENT INCOME

	FOR THE PERIOD ENDING DECEMBER 31,		
	2007	2006	2005
Investment Income Received From:			
Cash	\$145,256	\$0	\$80,150
Short Term Investments	103,153	90,678	50,412
Fixed Income	800,231	670,667	726,296
Equities	84,987	147,561	124,804
Pooled or Mutual Funds	1,508,576	1,231,139	182
Commission Recapture	<u>0</u>	<u>0</u>	<u>0</u>
Total Investment Income	<u>2,642,203</u>	<u>2,140,046</u>	<u>981,843</u>
Plus:			
Realized Gains	8,871,492	4,420,734	386,243
Unrealized Gains	7,117,434	9,806,908	9,542,804
Interest Due and Accrued - Current Year	<u>142,365</u>	<u>140,796</u>	<u>130,307</u>
Sub Total	<u>16,131,292</u>	<u>14,368,438</u>	<u>10,059,354</u>
Less:			
Paid Accrued Interest on Fixed Income Securities	(67,497)	(78,922)	(106,279)
Realized Loss	(2,135,762)	(1,072,827)	(426,376)
Unrealized Loss	(9,355,079)	(3,212,389)	(6,186,498)
Interest Due and Accrued - Prior Year	<u>(140,796)</u>	<u>(130,307)</u>	<u>(159,664)</u>
Sub Total	<u>(11,699,134)</u>	<u>(4,494,446)</u>	<u>(6,878,817)</u>
Net Investment Income	<u>7,074,361</u>	<u>12,014,038</u>	<u>4,162,380</u>
Income Required:			
Annuity Savings Fund	169,437	158,466	148,546
Annuity Reserve Fund	254,259	261,571	273,658
Military Service Fund	4	4	4
Expense Fund	<u>1,066,496</u>	<u>1,038,028</u>	<u>878,198</u>
Total Income Required	<u>1,490,196</u>	<u>1,458,070</u>	<u>1,300,407</u>
Net Investment Income	<u>7,074,361</u>	<u>12,014,038</u>	<u>4,162,380</u>
Less: Total Income Required	<u>1,490,196</u>	<u>1,458,070</u>	<u>1,300,407</u>
Excess Income To The Pension Reserve Fund	<u>\$5,584,165</u>	<u>\$10,555,968</u>	<u>\$2,861,974</u>

SCHEDULE OF ALLOCATION OF INVESTMENTS OWNED

(percentages by category)

AS OF DECEMBER 31, 2007			
	MARKET VALUE	PERCENTAGE OF TOTAL ASSETS	PERCENTAGE ALLOWED
Cash	\$6,958,829	7.1%	100%
Short Term*	68,070,170	69.9%	100%
Fixed Income	206,793	0.2%	40-80%
Equities	4,104	0.0%	0-60%
Pooled Domestic Equity Funds	10,500	0.0%	0-60%
Pooled Domestic Fixed Income Funds	7,065,720	7.3%	40-80%
Pooled Alternative Investment Funds	7,736,757	7.9%	10%
Pooled Real Estate Funds	7,339,842	7.5%	2%
Grand Total	<u>\$97,392,716</u>	<u>100.0%</u>	

*Includes transitional cash invested in PRIT in January 2008

For the year ending December 31, 2006, the rate of return for the investments of the Salem Retirement System was 15.03%. For the five-year period ending December 31, 2006, the rate of return for the investments of the Salem Retirement System averaged 7.83%. For the twenty-two-year period ending December 31, 2006, since PERAC began evaluating the returns of the retirement systems, the rate of return on the investments of the Salem Retirement System was 9.78%.

SUPPLEMENTARY INVESTMENT REGULATIONS

The Salem Retirement Board voted as of January 1, 2008 to voluntarily transition its investments into PRIT. Once the transfer of all assets is complete, previously approved investment regulations will effectively be rescinded.

The Salem Retirement System submitted the following supplementary Investment regulations, which were approved by the Public Employee Retirement Administration Commission on:

February 14, 2007

17.03 Notwithstanding the provisions of the Public Employee Retirement Administration Commission regulations, the Salem Retirement Board may invest funds of the Retirement System (the "System") in the fund known as the Institutional Retirement Trust (IRT) Equity Real Estate Securities Trust (the "Fund"), and effective as of the date of the initial investment by the System of any of its assets in the Fund, while the assets of the System are so invested, the activities and investments of the Fund, directly or indirectly, shall be deemed to satisfy the prohibited transaction rules set forth in 840 CMR 16.00 et seq. and 840 CMR 17.03 to the extent such activities satisfy the prohibited transaction rules set forth in Section 406 of the U.S. Employee Retirement Income Security Act of 1974, as amended ("ERISA"), taking into account ERISA section 408(b)(8) as well as other statutory exemptions under ERISA, Prohibited Transaction Class Exemption 84-14, as amended, Prohibited Transaction Class Exemption 91-38, and other available class exemptions.

April 7, 2000

16.08(2) In accordance with PERAC Investment Guideline 99-2, the Salem Retirement Board may invest in the Freedom Capital Equity Style Fund. Proceeds will come from 40% of the Board's current equity account with Freedom Capital Management. The Style Fund has the same investment strategy and invests in the same universe of stocks as the managed account. The difference is that it invests in either of two indexes (the S&P Barra Growth Index or the S&P Barra Value Index) rather than in individual securities. In so doing, management fees and other costs to the Board are reduced.

December 10, 1999

16.08(1) In accordance with PERAC Investment Guideline 99-2, the Salem Retirement Board may amend its domestic fixed income management mandate with Freedom Capital Management Corporation to allow the manager to opportunistically invest up to 15% of its core portfolio in securities rated either Ba by Moody's or BB by Standard and Poor's.

July 11, 1996

20.03(1) Equity investments shall not exceed 60% of the portfolio valued at market, including international equities which shall not exceed 15% of the portfolio valued at market.

June 6, 1996

20.03(2) At least 40% but no more than 80% of the total portfolio valued at market shall consist of fixed income investments with a maturity of more than one year including Yankee Bonds which shall be limited to 10% of the total fixed income portfolio valued at market.

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

January 25, 1996

840 CMR 21.00: Prohibited Investments

(3) Futures Contracts other than as follows:

(a) Forward Currency Contracts may be written against securities in the international portfolio by an investment advisor registered under the Investment Advisors Act of 1940 and who has been granted a waiver from PERAC for international investments.

(b) Forward Currency Contracts may be written against securities in the international portfolio to a maximum of twenty-five percent (25%) of the international portfolios non-dollar holdings at market value. Speculative currency positions unrelated to underlying portfolio holdings are strictly prohibited.

August 4, 1994

20.03(1) Equity investments shall not exceed 50% of the portfolio valued at market, including international equities which shall not exceed 10% of the portfolio valued at market.

20.04(1) United States based corporations and equities of foreign corporations. 20.07(5) Equity investments shall be made only in securities listed on a United States stock exchange, traded over the counter in the United States, or listed and traded on a foreign exchange.

November 17, 1989

20.03(1) Equity investments shall not exceed 50% of the total book value of the portfolio at the time of purchase.

August 16, 1989

16.02(3) A board may incur expenses for consultant services, which shall be limited to setting of investment objectives, selection and on-going review of qualified investment advisors and performance evaluation, and investment advice or management of the funds of the system by a qualified investment advisor and may charge such expenses against earned income from investments provided that such expenses shall not exceed in any one year:

(a) 1% of the value of the fund for the first \$5 million, and

(b) 0.5% of the value of the fund in excess of \$5 million 16.02(4) The employment of a consultant must take place by a written contract, negotiated between the consultant and the board. Such contract shall state the terms and conditions of the agreement, including but not limited to, termination provisions, length and fees. All such contracts must be forwarded to PERAC.

November 17, 1988

(1) Real estate investments shall not exceed 2% of the total book value of the portfolio at the time of purchase and shall consist of real estate trusts and partnerships, provided that:

(a) trust participants or limited partners do not participate in the selection of the trustees or general partners and should a limited partner be required to participate in the selection of a general partner, prior to any participation by the board, the board shall consult with PERA to determine the appropriate course of action, and (b) such trustees or general partners retain authority in the decision making process, and (c) should an investment in a trust or limited partnership result in the direct ownership of real estate or mortgage indebtedness, such shall be permitted only until such time as divestiture of said trust or limited partnership is prudent.

NOTES TO FINANCIAL STATEMENTS

NOTE I – SUMMARY OF PLAN PROVISIONS

The plan is a contributory defined benefit plan covering all Salem Retirement System member unit employees deemed eligible by the retirement board, with the exception of school department employees who serve in a teaching capacity. The Teachers' Retirement Board administers the pensions of such school employees.

ADMINISTRATION

There are 106 contributory Retirement Systems for public employees in Massachusetts. Each system is governed by a retirement board, and all boards, although operating independently, are governed by Chapter 32 of the Massachusetts General Laws. This law in general provides uniform benefits, uniform contribution requirements, and a uniform accounting and funds structure for all systems.

PARTICIPATION

Participation is mandatory for all full-time employees. Eligibility with respect to part-time, provisional, temporary, seasonal, or intermittent employment is governed by regulations promulgated by the retirement board, and approved by PERAC. Membership is optional for certain elected officials.

There are 3 classes of membership in the Retirement System:

Group 1:

General employees, including clerical, administrative, technical, and all other employees not otherwise classified.

Group 2:

Certain specified hazardous duty positions.

Group 4:

Police officers, firefighters, and other specified hazardous positions.

NOTES TO FINANCIAL STATEMENTS (Continued)

MEMBER CONTRIBUTIONS

Member contributions vary depending on the most recent date of membership:

Prior to 1975:	5% of regular compensation
1975 - 1983:	7% of regular compensation
1984 to 6/30/96:	8% of regular compensation
7/1/96 to present:	9% of regular compensation
1979 to present:	an additional 2% of regular compensation in excess of \$30,000.

RATE OF INTEREST

Interest on regular deductions made after January 1, 1984 is a rate established by PERAC in consultation with the Commissioner of Banks. The rate is obtained from the average rates paid on individual savings accounts by a representative sample of at least 10 financial institutions.

RETIREMENT AGE

The mandatory retirement age for some Group 2 and Group 4 employees is age 65. Most Group 2 and Group 4 members may remain in service after reaching age 65. Group 4 members who are employed in certain public safety positions are required to retire no later than the end of month they attain age 65. There is no mandatory retirement age for employees in Group 1.

SUPERANNUATION RETIREMENT

A member is eligible for a superannuation retirement allowance (service retirement) upon meeting the following conditions:

- completion of 20 years of service, or
- attainment of age 55 if hired prior to 1978, or if classified in Group 4, or
- attainment of age 55 with 10 years of service, if hired after 1978, and if classified in Group 1 or 2

NOTES TO FINANCIAL STATEMENTS (Continued)

AMOUNT OF BENEFIT

A member's annual allowance is determined by multiplying average salary by a benefit rate related to the member's age and job classification at retirement, and the resulting product by his creditable service. The amount determined by the benefit formula cannot exceed 80% of the member's highest three year average salary. For veterans as defined in G.L. c. 32, § 1, there is an additional benefit of \$15 per year for each year of creditable service, up to a maximum of \$300.

- Salary is defined as gross regular compensation.
- Average Salary is the average annual rate of regular compensation received during the 3 consecutive years that produce the highest average, or, if greater, during the last three years (whether or not consecutive) preceding retirement.
- The Benefit Rate varies with the member's retirement age, but the highest rate of 2.5% applies to Group 1 employees who retire at or after age 65, Group 2 employees who retire at or after age 60, and to Group 4 employees who retire at or after age 55. A .1% reduction is applied for each year of age under the maximum age for the member's group. For Group 2 employees who terminate from service under age 55, the benefit rate for a Group 1 employee shall be used.

DEFERRED VESTED BENEFIT

A participant who has completed 10 or more years of creditable service is eligible for a deferred vested retirement benefit. Elected officials and others who were hired prior to 1978 may be vested after 6 years in accordance with G.L. c. 32, § 10.

The participant's accrued benefit is payable commencing at age 55, or the completion of 20 years, or may be deferred until later at the participant's option.

WITHDRAWAL OF CONTRIBUTIONS

Member contributions may be withdrawn upon termination of employment. Employees who first become members on or after January 1, 1984, may receive only limited interest on their contributions if they voluntarily terminate their service. Those who leave service with less than 5 years receive no interest; those who leave service with greater than 5 but less than 10 years receive 50% of the interest credited.

NOTES TO FINANCIAL STATEMENTS (Continued)

DISABILITY RETIREMENT

The Massachusetts Retirement Plan provides 2 types of disability retirement benefits:

ORDINARY DISABILITY

Eligibility: Non-veterans who become totally and permanently disabled by reason of a non-job related condition with at least 10 years of creditable service (or 15 years creditable service in systems in which the local option contained in G.L. c. 32, § 6(1) has not been adopted).

Veterans with ten years of creditable service who become totally and permanently disabled by reason of a non-job related condition prior to reaching “maximum age”.

Retirement Allowance: Equal to the accrued superannuation retirement benefit as if the member was age 55. If the member is a veteran, the benefit is 50% of the member’s final rate of salary during the preceding 12 months, plus an annuity based upon accumulated member contributions plus credited interest. If the member is over age 55, he or she will receive not less than the superannuation allowance to which he or she is entitled.

ACCIDENTAL DISABILITY

Eligibility: Applies to members who become permanently and totally unable to perform the essential duties of the position as a result of a personal injury sustained or hazard undergone while in the performance of duties. There are no minimum age or service requirements.

Retirement Allowance: 72% of salary plus an annuity based on accumulated member contributions, with interest. This amount is not to exceed 100% of pay. For those who became members in service after January 1, 1988 or who have not been members in service continually since that date, the amount is limited to 75% of pay. There is an additional pension of \$667.92 per year (or \$312.00 per year in systems in which the local option contained in G.L. c. 32, § 7(2)(a)(iii) has not been adopted), per child who is under 18 at the time of the member’s retirement, with no age limitation if the child is mentally or physically incapacitated from earning. The additional pension may continue up to age 22 for any child who is a full time student at an accredited educational institution.

NOTES TO FINANCIAL STATEMENTS (Continued)

ACCIDENTAL DEATH

Eligibility: Applies to members who die as a result of a work-related injury or if the member was retired for accidental disability and the death was the natural and proximate result of the injury or hazard undergone on account of which such member was retired.

Allowance: An immediate payment to a named beneficiary equal to the accumulated deductions at the time of death, plus a pension equal to 72% of current salary and payable to the surviving spouse, dependent children or the dependent parent, plus a supplement of \$312 per year, per child, payable to the spouse or legal guardian until all dependent children reach age 18 or 22 if a full time student, unless mentally or physically incapacitated.

The surviving spouse of a member of a police or fire department or any corrections officer who, under specific and limited circumstances detailed in the statute, suffers an accident and is killed or sustains injuries resulting in his death, may receive a pension equal to the maximum salary for the position held by the member upon his death.

In addition, an eligible family member may receive a one time payment of \$100,000 from the State Retirement Board.

DEATH AFTER ACCIDENTAL DISABILITY RETIREMENT

Effective November 7, 1996, Accidental Disability retirees were allowed to select Option C at retirement and provide a benefit for an eligible survivor. For Accidental Disability retirees prior to November 7, 1996, who could not select Option C, if the member's death is from a cause unrelated to the condition for which the member received accidental disability benefits, a surviving spouse will receive an annual allowance of \$6,000.

DEATH IN ACTIVE SERVICE

Allowance: An immediate allowance equal to that which would have been payable had the member retired and elected Option C on the day before his or her death. For death occurring prior to the member's superannuation retirement age, the age 55 benefit rate is used. The minimum annual allowance payable to the surviving spouse of a member in service who dies with at least two years of creditable service is \$3,000, provided that the member and the spouse were married for at least one year and living together on the member's date of death.

The surviving spouse of such a member in service receives an additional allowance equal to the sum of \$1,440 per year for the first child, and \$1,080 per year for each additional child until all dependent children reach age 18 or 22 if a full time student, unless mentally or physically incapacitated.

NOTES TO FINANCIAL STATEMENTS (Continued)

COST OF LIVING

If a system has accepted Chapter 17 of the Acts of 1997, and the Retirement Board votes to pay a cost of living increase for that year, the percentage is determined based on the increase in the Consumer Price Index used for indexing Social Security benefits, but cannot exceed 3.0%. Section 51 of Chapter 127 of the Acts of 1999, if accepted, allows boards to grant COLA increases greater than that determined by CPI but not to exceed 3.0%. The first \$12,000 of a retiree's total allowance is subject to a cost-of-living adjustment. The total Cost-of-Living adjustment for periods from 1981 through 1996 is paid for by the Commonwealth of Massachusetts.

METHODS OF PAYMENT

A member may elect to receive his or her retirement allowance in one of 3 forms of payment.

Option A: Total annual allowance, payable in monthly installments, commencing at retirement and terminating at the member's death.

Option B: A reduced annual allowance, payable in monthly installments, commencing at retirement and terminating at the death of the member, provided, however, that if the total amount of the annuity portion received by the member is less than the amount of his or her accumulated deductions, including interest, the difference or balance of his accumulated deductions will be paid in a lump sum to the retiree's beneficiary or beneficiaries of choice.

Option C: A reduced annual allowance, payable in monthly installments, commencing at retirement. At the death of the retired employee, 2/3 of the allowance is payable to the member's designated beneficiary (who may be the spouse, or former spouse who remains unmarried for a member whose retirement becomes effective on or after February 2, 1992, child, parent, sister, or brother of the employee) for the life of the beneficiary. For members who retired on or after January 12, 1988, if the beneficiary pre-deceases the retiree, the benefit payable increases (or "pops up") based on the factor used to determine the Option C benefit at retirement. For members who retired prior to January 12, 1988, if the System has accepted Section 288 of Chapter 194 of the Acts of 1998 and the beneficiary pre-deceases the retiree, the benefit payable "pops up" in the same fashion. The Option C became available to accidental disability retirees on November 7, 1996.

NOTES TO FINANCIAL STATEMENTS (Continued)

ALLOCATION OF PENSION COSTS

If a member's total creditable service was partly earned by employment in more than one retirement system, the cost of the "pension portion" is allocated between the different systems pro rata based on the member's service within each retirement system.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The accounting records of the System are maintained on a calendar year basis in accordance with the standards and procedures established by the Public Employee Retirement Administration Commission.

The Annuity Savings Fund is the fund in which members' contributions are deposited. Voluntary contributions, re-deposits, and transfers to and from other systems, are also accounted for in this fund. Members' contributions to the fund earn interest at a rate determined by PERAC. Interest for some members who withdraw with less than ten years of service is transferred to the Pension Reserve Fund. Upon retirement, members' contributions and interest are transferred to the Annuity Reserve Fund. Dormant account balances must be transferred to the Pension Reserve Fund after a period of ten years of inactivity.

The Annuity Reserve Fund is the fund to which a member's account is transferred upon retirement from the Annuity Savings Fund and Special Military Service Credit Fund. The annuity portion of the retirement allowance is paid from this fund. Interest is credited monthly to this fund at the rate of 3% annually on the previous month's balance.

The Special Military Service Credit Fund contains contributions and interest for members while on a military leave for service in the Armed Forces who will receive creditable service for the period of that leave.

The Expense Fund contains amounts transferred from investment income for the purposes of administering the retirement system.

The Pension Fund contains the amounts appropriated by the governmental units as established by PERAC to pay the pension portion of each retirement allowance.

The Pension Reserve Fund contains amounts appropriated by the governmental units for the purposes of funding future retirement benefits. Any profit or loss realized on the sale or maturity of any investment or on the unrealized gain of a market valued investment as of the valuation date is credited to the Pension Reserve Fund. Additionally, any investment income in excess of the amount required to credit interest to the Annuity Savings Fund, Annuity Reserve Fund, and Special Military Service Credit Fund is credited to this Reserve account.

The Investment Income Account is credited with all income derived from interest and dividends of invested funds. At year-end the interest credited to the Annuity Savings Fund, Annuity Reserve Fund, Expense Fund, and Special Military Service Credit Fund is distributed from this account and the remaining balance is transferred to the Pension Reserve Fund.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

NOTE 3 - SUPPLEMENTARY MEMBERSHIP REGULATIONS

The Salem Retirement System submitted the following supplementary membership regulations, which were approved by the Public Employee Retirement Administration Commission on:

August 23, 2007

BUYBACK POLICIES

The policy of the Salem Contributory Retirement Board in regards to buybacks, make-ups, and veteran's buyback is as follows:

BUYBACK FOR MILITARY CREDIT

This payment is made, when necessary, as a lump sum payment before retirement by either a cash payment or from a deferred comp plan. (members are encouraged to make deductions to a deferred comp plan so that if and when payment is made, the payments are pretax)

BUYBACK of PREVIOUS REFUNDS

Lump sum payment at any time

MAKEUP FOR PREVIOUS SERVICE

- Lump sum payment at any time
- Three equal installments over a year
- Over \$3,000 owed, two payments a year up to three years to complete

All members are encouraged to make deductions to a deferred compensation plan so that their payments will be pretax.

July 19, 1990

School employees must work a minimum of 25 hours per week to be eligible for membership. Full time school employees who are members will be given 1 year of creditable service for 10 months employment.

February 4, 1986

MEMBERSHIP

City of Salem; Salem Redevelopment Authority; Salem Housing Authority, North Shore Regional Vocational School District; Salem-Beverly Water Board; South Essex Sewerage employees shall become members of the system when hired as directed by Chapter 32, section 3.

Part-time employees shall become members by meeting qualification of Chapter 32 and rules of retirement board as follows: 20 hrs. per week, 39 weeks per year give 1/2 yr. creditable service.

Employees of temporary nature found to be ineligible for membership in system upon becoming permanent employee shall have privilege of purchasing past service, so allowed by board.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 3 - SUPPLEMENTARY MEMBERSHIP REGULATIONS (Continued)

January 30, 2004

The Salem Retirement System has adopted Supplemental Travel Regulations pursuant to PERAC guidelines and approved by PERAC under the provisions of G.L. c. 7, § 50 and G.L. c. 32, § 21(4). (Regulations are available upon written request.)

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 4 - ADMINISTRATION OF THE SYSTEM

The System is administered by a five-person Board of Retirement consisting of the Treasurer who shall be a member ex-officio, a second member appointed by the governing authority, a third and fourth member who shall be elected by the members in or retired from the service of such system, and a fifth member appointed by the other four board members.

Ex-officio Member: Richard Viscay

Appointed Member: Kimberley Driscoll Term Expires: Indefinite

Elected Member: John H. Burke Jr. Term Expires: 12/05/08

Elected Member: John O'Leary Term Expires: 06/03/10

Appointed Member: Katherine O'Leary, Chairman Term Expires: 11/03/09

The Board members are required to meet at least once a month. The Board must keep a record of all of its proceedings. The Board must annually submit to the appropriate authority an estimate of the expenses of administration and cost of operation of the system. The board must annually file a financial statement of condition for the system with the Executive Director of PERAC.

The investment of the system's funds is the responsibility of the Board. All retirement allowances must be approved by the Retirement Board and are then submitted to the PERAC Actuary for verification prior to payment. All expenses incurred by the System must be approved by a majority vote of the Board. Payments shall be made only upon vouchers signed by two persons designated by the Board.

The following retirement board members and employees are bonded by an authorized agent representing a company licensed to do business in Massachusetts as follows:

Treasurer - Custodian:)	\$1,000,000 Commercial Crime &
Ex-officio Member:)	\$50,000,000 Fiduciary with Travelers
Elected Member:)	Insurance Company (MACRS blanket
Appointed Member:)	policy)
Staff Employee:)	

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 5 - ACTUARIAL VALUATION AND ASSUMPTIONS

The most recent actuarial valuation of the System was prepared by The Segal Group, Inc. as of January 1, 2006.

The actuarial liability for active members was	\$78,053,840
The actuarial liability for terminated members was	1,655,022
The actuarial liability for retired members was	<u>87,249,744</u>
The total actuarial liability was	166,958,606
System assets as of that date were	<u>84,796,044</u>
The unfunded actuarial liability was	<u>\$82,162,562</u>
The ratio of system's assets to total actuarial liability was	50.8%
As of that date the total covered employee payroll was	\$32,824,144

The normal cost for employees on that date was 8.78% of payroll

The normal cost for the employer was 7.10% of payroll

The principal actuarial assumptions used in the valuation are as follows:

Investment Return: 8.25% per annum

Rate of Salary Increase: 5.50% per annum

GASB STATEMENT NO. 25, DISCLOSURE INFORMATION AS OF JANUARY 1, 2006

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a % of Cov. Payroll ((b-a)/c)
1/1/2006	\$84,796,044	\$166,958,606	\$82,162,562	50.8%	\$32,824,144	250.3%
1/1/2005	\$81,801,377	\$156,479,479	\$74,678,102	52.3%	\$31,328,083	238.4%
1/1/2004	\$80,659,012	\$142,499,185	\$61,840,173	56.6%	\$29,355,291	210.7%
1/1/2003	\$76,438,885	\$137,111,559	\$60,672,674	55.7%	\$31,089,195	195.2%
1/1/2001	\$73,727,923	\$117,334,727	\$43,606,804	62.8%	\$29,072,187	150.0%

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 6 - MEMBERSHIP EXHIBIT

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Retirement in Past Years										
Superannuation	19	16	2	2	15	54	21	5	14	15
Ordinary Disability	1	0	0	0	0	0	2	0	0	0
Accidental Disability	0	0	1	0	3	3	3	1	1	3
Total Retirements	20	16	3	2	18	57	26	6	15	18
Total Retirees, Beneficiaries and Survivors	652	647	611	599	589	646	640	619	633	625
Total Active Members	811	865	895	909	924	839	883	840	834	867
Pension Payments										
Superannuation	\$4,251,808	\$4,454,116	\$4,459,386	\$4,682,268	\$4,819,607	\$5,532,260	\$6,272,261	\$6,369,684	\$6,509,618	\$6,736,404
Survivor/Beneficiary Payments	703,038	632,453	600,831	472,011	486,663	467,567	464,813	480,580	443,552	443,037
Ordinary Disability	157,768	139,292	166,773	143,724	132,273	125,572	129,197	123,133	128,096	101,586
Accidental Disability	1,156,306	1,143,576	1,283,437	1,272,186	1,334,265	1,438,846	1,488,077	1,537,994	1,565,494	1,757,609
Other	488,918	541,339	576,310	736,371	846,862	741,454	818,390	926,104	916,111	892,554
Total Payments for Year	<u>\$6,757,838</u>	<u>\$6,910,776</u>	<u>\$7,086,737</u>	<u>\$7,306,560</u>	<u>\$7,619,670</u>	<u>\$8,305,699</u>	<u>\$9,172,737</u>	<u>\$9,437,493</u>	<u>\$9,562,871</u>	<u>\$9,931,190</u>

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