

PERAC AUDIT REPORT



Hampden County Regional
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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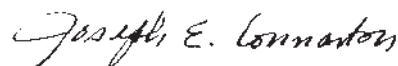
May 12, 2009

The Public Employee Retirement Administration Commission has completed an examination of the Hampden County Regional 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 examiner Robert Madison who conducted this examination, and express appreciation to the Board of Retirement and staff for their courtesy and cooperation.

Sincerely,



Joseph E. Connarton
Executive Director



EXPLANATION OF FINDINGS AND RECOMMENDATIONS

I. Investments

During the review of pooled fund investments, the auditors were unable to confirm the December 31, 2007 asset value of Zero Stage Capital VII, L.P. This asset is classified as a Pooled Alternative Investment on the enclosed financial statements. Starting with an initial investment of \$1,050,000 in 2001, it was found that Zero Stage Capital requested an additional influx of funds of \$1,050,000 three (3) more times for a total value of \$4,200,000. As of June 30, 2007, the reported value of Zero Stage Capital has declined to \$294,529.17. Zero Stage Capital has not responded to multiple requests for an update on current asset values.

Recommendation

The Hampden County Regional Retirement Board and Segal Advisors, the investment consultant, must review this investment to determine the correct current value of this venture capital investment or if it is necessary to write-off the investment. Financial statements produced by the Hampden County Regional Retirement Board must include full disclosure, generally in a footnote to explain the current status of this investment.

Board Response:

Zero Stage – The Board has continued to request accounting updates from the management staff of this investment, unfortunately this company is no longer in an active investment management situation and receiving reports is next to impossible. This system was part of a settlement regarding excessive investment manager fees charged and in October, 2008 we did receive approximately \$181,700.00 from Zero Stage. The Board will consider along with our consultant how best to handle the final accounting of this investment.

2. Membership

A. Membership Contributions

As reported in prior audits, the Board does not always receive adequate information to ascertain the accuracy of members' deductions.

The PERAC auditor obtained copies of payroll deduction reports submitted by all thirty-five (35) Hampden County Regional governmental units. Many unit deduction reports lack fundamental detail as to which pay categories are subject or not subject to retirement deductions. Payroll clerks appear insufficiently trained to determine that contributions are only taken from regular contributions.

The PERAC auditor then sent letters to the treasurers of fourteen governmental units requesting employee payroll registers for twenty employees. Of the fourteen units sampled, five had calculation issues (or, of twenty individuals tested, five members had calculation issues).

EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

Recommendation

Based on the samples noted, it is recommended that the board establish a plan to ensure the governmental units are in compliance with G.L. c. 32 § 22(1)(b); G.L. c. 32 § 22(1)(b1/2); G.L. c. 32 § 22(1)(h), and PERAC Memo #43/1999. PERAC can provide the names of retirement systems that are implementing best practices or internal controls to address calculation issues. It is recognized that, in some cases, governmental units will require computer updates and the costs of these updates prevent immediate reprogramming. However, when short and long-term plans are in place, membership deductions are reported without calculation issues.

B. Payroll Verification

The system does not always verify members' salaries with governmental unit treasurers or payroll disbursing offices. The system does utilize a form requesting salaries for three years; however, department head or supervisor approval of salaries was not always noted in the files sampled.

Recommendation

Actual payroll records should be used when calculating retirement benefits as required under G.L. c. 32, § 5. Best practices suggest that the Board require that department heads review and confirm the payroll records of prospective retirees. Confirming retirement benefits with actual payroll records serves the related purpose of verifying that members' records are maintained accurately on an on-going basis by the Retirement Board. Calculating earnings solely from earnings received monthly may result in differences when compared to the members' annual earnings. We strongly suggest the Board perform a comprehensive review of how retirements are calculated by obtaining the actual payroll salaries from member unit treasurers or the appropriate unit disbursing office.

Board Response:

With regards to the reports that this system receives from our member units we have on prior occasions noted to you and your audit staff that until PERAC mandates a particular type of monthly report and provides specifications that must be followed by the member units as to what the report should include and the formatting of said report, this system will continue to receive the reports we currently receive from our member units. The treasurers continue to say that they need a mandated change from the governing authority in order not to be charged by their individual software providers in making changes to the reports currently available to them and their computer programs. This had been noted with prior audits also. In addressing the issue of receiving payroll histories, the staff does send out written forms with the information needed to calculate the three year average salary for a member who is retiring. In 90% of the requests, the treasurer or their designee completes the form in a timely manner and returns it to our office. Occasionally the form is not returned and this office must then go back to the individual monthly reports and the deduction amounts withheld from the pay indicated in order to calculate the retirement allowance.

EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

We would prefer not to use this method but that is what we have to do in some instances to insure that an individual is not unduly harmed by a delay that is through no fault of their own. We will continue to request a timely return of our form to insure that the correct salary amounts are used in calculating an individual's retirement allowance.

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	\$5,698,390	\$4,629,441	\$8,365,074
Fixed Income Securities	0	0	18,917,123
Equities	19,203,824	19,988,038	16,279,386
Pooled Domestic Equity Funds	94,135,721	88,598,763	78,568,782
Pooled International Equity Funds	34,671,022	31,652,785	24,550,273
Pooled Global Fixed Income Funds	45,040,340	42,748,418	30,174,198
Pooled Alternative Investment Funds	13,936,284	11,819,093	4,406,403
Pooled Real Estate Funds	22,055,134	20,248,883	15,909,778
Interest Due and Accrued	11,754	12,722	144,754
Accounts Receivable	605,646	524,645	471,869
Accounts Payable	(122,137)	0	0
Total	<u>\$235,235,977</u>	<u>\$220,222,788</u>	<u>\$197,787,641</u>
Fund Balances:			
Annuity Savings Fund	\$68,131,903	\$63,905,517	\$59,686,723
Annuity Reserve Fund	18,934,566	18,679,220	18,859,413
Pension Fund	0	0	0
Military Service Fund	33,343	27,286	23,014
Expense Fund	0	0	0
Pension Reserve Fund	148,136,166	137,610,765	119,218,492
Total	<u>\$235,235,977</u>	<u>\$220,222,788</u>	<u>\$197,787,641</u>

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)	\$56,562,816	\$18,098,530	\$0	\$13,987	\$0	\$112,090,026	\$186,765,359
Receipts	7,159,377	542,905	13,982,413	15,757	1,582,852	10,633,924	33,917,229
Interfund Transfers	(2,988,731)	2,982,156	3,518,762	(6,731)	0	(3,505,457)	0
Disbursements	(1,046,739)	(2,764,179)	(17,501,175)	0	(1,582,852)	0	(22,894,945)
Ending Balance (2005)	59,686,723	18,859,413	0	23,014	(0)	119,218,492	197,787,641
Receipts	7,712,655	553,314	13,803,190	4,272	1,682,608	23,296,375	47,052,414
Interfund Transfers	(2,088,480)	2,084,397	4,908,184	0	0	(4,904,102)	0
Disbursements	(1,405,381)	(2,817,903)	(18,711,374)	0	(1,682,608)	0	(24,617,267)
Ending Balance (2006)	63,905,517	18,679,220	0	27,286	(0)	137,610,765	220,222,788
Receipts	8,202,894	558,146	17,297,084	6,057	1,968,657	12,425,586	40,458,423
Interfund Transfers	(2,608,570)	2,538,725	1,970,031	0	0	(1,900,186)	0
Disbursements	(1,367,938)	(2,841,525)	(19,267,114)	0	(1,968,657)	0	(25,445,234)
Ending Balance (2007)	<u>\$68,131,903</u>	<u>\$18,934,566</u>	<u>\$0</u>	<u>\$33,343</u>	<u>(\$0)</u>	<u>\$148,136,166</u>	<u>\$235,235,977</u>

STATEMENT OF RECEIPTS

	FOR THE PERIOD ENDING DECEMBER 31,		
	2007	2006	2005
Annuity Savings Fund:			
Members Deductions	\$7,094,231	\$6,688,273	\$6,270,677
Transfers from Other Systems	588,455	526,613	449,456
Member Make Up Payments and Re-deposits	150,163	149,470	111,908
Investment Income Credited to Member Accounts	<u>370,045</u>	<u>348,298</u>	<u>327,337</u>
Sub Total	<u>8,202,894</u>	<u>7,712,655</u>	<u>7,159,377</u>
Annuity Reserve Fund:			
Investment Income Credited to the Annuity Reserve Fund	<u>558,146</u>	<u>553,314</u>	<u>542,905</u>
Pension Fund:			
3 (8) (c) Reimbursements from Other Systems Received from Commonwealth for COLA and Survivor Benefits	386,401	354,782	322,527
Pension Fund Appropriation	<u>16,205,013</u>	<u>12,705,243</u>	<u>12,281,004</u>
Sub Total	<u>17,297,084</u>	<u>13,803,190</u>	<u>13,982,413</u>
Military Service Fund:			
Contribution Received from Municipality on Account of Military Service	5,876	4,107	15,513
Investment Income Credited to the Military Service Fund	<u>181</u>	<u>166</u>	<u>244</u>
Sub Total	<u>6,057</u>	<u>4,272</u>	<u>15,757</u>
Expense Fund:			
Investment Income Credited to the Expense Fund	<u>1,968,657</u>	<u>1,682,608</u>	<u>1,582,852</u>
Sub Total	<u>1,968,657</u>	<u>1,682,608</u>	<u>1,582,852</u>
Pension Reserve Fund:			
Federal Grant Reimbursement	0	18,875	73,735
Pension Reserve Appropriation	264,202	267,131	276,745
Interest Not Refunded	12,273	9,278	22,489
Miscellaneous Income	21,935	13,884	35,585
Excess Investment Income	<u>12,127,176</u>	<u>22,987,207</u>	<u>10,225,371</u>
Sub Total	<u>12,425,586</u>	<u>23,296,375</u>	<u>10,633,924</u>
Total Receipts	<u>\$40,458,423</u>	<u>\$47,052,414</u>	<u>\$33,917,229</u>

STATEMENT OF DISBURSEMENTS

	FOR THE PERIOD ENDING DECEMBER 31,		
	2007	2006	2005
Annuity Savings Fund:			
Refunds to Members	\$794,759	\$814,117	\$842,110
Transfers to Other Systems	<u>573,179</u>	<u>591,264</u>	<u>204,629</u>
Sub Total	<u>1,367,938</u>	<u>1,405,381</u>	<u>1,046,739</u>
Annuity Reserve Fund:			
Annuities Paid	2,813,488	2,658,161	2,540,773
Option B Refunds	<u>28,037</u>	<u>159,742</u>	<u>223,406</u>
Sub Total	<u>2,841,525</u>	<u>2,817,903</u>	<u>2,764,179</u>
Pension Fund:			
Pensions Paid:			
Regular Pension Payments	13,334,483	12,830,172	12,379,087
Survivorship Payments	811,254	799,231	754,949
Ordinary Disability Payments	268,949	268,149	280,754
Accidental Disability Payments	2,450,126	2,485,297	2,351,488
Accidental Death Payments	731,831	660,857	611,763
Section 101 Benefits	104,537	102,991	98,235
3 (8) (c) Reimbursements to Other Systems	<u>1,565,934</u>	<u>1,564,677</u>	<u>1,024,899</u>
Sub Total	<u>19,267,114</u>	<u>18,711,374</u>	<u>17,501,175</u>
Expense Fund:			
Board Member Stipend	34,330	31,500	29,000
Salaries	200,360	189,050	180,388
Legal Expenses	43,814	42,759	41,514
Medical Expenses	87	0	65
Travel Expenses	5,624	11,973	10,842
Administrative Expenses	233,737	162,740	165,849
Furniture and Equipment	24,447	1,225	0
Management Fees	1,351,813	1,167,507	1,084,751
Custodial Fees	22,112	27,854	22,443
Consultant Fees	<u>52,333</u>	<u>48,000</u>	<u>48,000</u>
Sub Total	<u>1,968,657</u>	<u>1,682,608</u>	<u>1,582,852</u>
Total Disbursements	<u>\$25,445,234</u>	<u>\$24,617,267</u>	<u>\$22,894,945</u>

INVESTMENT INCOME

	FOR THE PERIOD ENDING DECEMBER 31,		
	2007	2006	2005
Investment Income Received From:			
Cash	\$231,396	\$253,808	\$138,146
Short Term Investments	0	47,791	21,149
Fixed Income	0	940,132	1,041,828
Equities	161,216	92,092	31,230
Pooled or Mutual Funds	5,771,760	5,048,663	3,969,633
Commission Recapture	<u>1,348</u>	<u>2,568</u>	<u>14,040</u>
Total Investment Income	<u>6,165,720</u>	<u>6,385,054</u>	<u>5,216,026</u>
Plus:			
Realized Gains	24,202,298	11,945,945	9,445,386
Unrealized Gains	20,785,672	23,043,228	20,598,098
Interest Due and Accrued - Current Year	<u>11,754</u>	<u>12,722</u>	<u>144,754</u>
Sub Total	<u>44,999,725</u>	<u>35,001,895</u>	<u>30,188,238</u>
Less:			
Paid Accrued Interest on Fixed Income Securities	0	(106,983)	(98,508)
Realized Loss	(1,367,412)	(2,266,266)	(1,299,268)
Unrealized Loss	(34,761,108)	(13,297,351)	(21,174,703)
Interest Due and Accrued - Prior Year	<u>(12,722)</u>	<u>(144,754)</u>	<u>(153,077)</u>
Sub Total	<u>(36,141,241)</u>	<u>(15,815,355)</u>	<u>(22,725,556)</u>
Net Investment Income	<u>15,024,204</u>	<u>25,571,593</u>	<u>12,678,708</u>
Income Required:			
Annuity Savings Fund	370,045	348,298	327,337
Annuity Reserve Fund	558,146	553,314	542,905
Military Service Fund	181	166	244
Expense Fund	<u>1,968,657</u>	<u>1,682,608</u>	<u>1,582,852</u>
Total Income Required	<u>2,897,028</u>	<u>2,584,386</u>	<u>2,453,338</u>
Net Investment Income	<u>15,024,204</u>	<u>25,571,593</u>	<u>12,678,708</u>
Less: Total Income Required	<u>2,897,028</u>	<u>2,584,386</u>	<u>2,453,338</u>
Excess Income To The Pension Reserve Fund	<u>\$12,127,176</u>	<u>\$22,987,207</u>	<u>\$10,225,371</u>

SCHEDULE OF ALLOCATION OF INVESTMENTS OWNED

(percentages by category)

AS OF DECEMBER 31, 2007			
	MARKET VALUE	PERCENTAGE OF TOTAL ASSETS	PERCENTAGE ALLOWED
Cash	\$5,698,390	2.4%	100%
Equities	19,203,824	8.2%	100%
Pooled Domestic Equity Funds	94,135,721	40.1%	100%
Pooled International Equity Funds	34,671,022	14.8%	100%
Pooled Global Fixed Income Funds	45,040,340	19.2%	100%
Pooled Alternative Investment Funds	13,936,284	5.9%	10%
Pooled Real Estate Funds	<u>22,055,134</u>	<u>9.4%</u>	<u>10%</u>
Grand Total	<u>\$234,740,715</u>	<u>100.0%</u>	100%

For the year ending December 31, 2007, the rate of return for the investments of the Hampden County Retirement System was 6.59%. For the five-year period ending December 31, 2007, the rate of return for the investments of the Hampden County Retirement System averaged 11.23%. For the 23-year period ending December 31, 2007, since PERAC began evaluating the returns of the retirement systems, the rate of return on the investments of the Hampden County Retirement System was 10.05%.

SUPPLEMENTARY INVESTMENT REGULATIONS

The Hampden County Regional Retirement System submitted the following supplementary investment regulations, which were approved by the Public Employee Retirement Administration Commission on:

December 11, 2007

17.03. Notwithstanding the provisions of the Public Employee Retirement Administration Commission regulations, the Hampden County Regional Retirement Board may invest funds of the Retirement System (the "System") in the fund known as the INVESCO Non-US Partnership Fund III, LP (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 statutory exemptions under ERISA, and Prohibited Transaction Class Exemption 84-14, as amended, and other available class exemptions.

December 11, 2007

17.03. Notwithstanding the provisions of the Public Employee Retirement Administration Commission regulations, the Hampden County Regional Retirement Board may invest funds of the Retirement System (the "System") in the fund known as the INVESCO Venture Partnership Fund III, LP (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, and the underlying funds in which the Fund may invest, 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 statutory exemptions under ERISA, and Prohibited Transaction Class Exemption

May 7, 2007

19.01(6). Notwithstanding the provisions of the Public Employee Retirement Administration Commission regulations, the Hampden County Regional Retirement Board may invest funds of the Hampden County Regional Retirement System (the "System") in the fund known as Fidelity Real Estate Growth Fund III, L.P. ("the Fund"), and effective as of the date of the initial investment by the System of any of its assets in the Fund.

(1) while the assets of the System are so invested, the assets of the System shall be deemed to include, for purposes of applying the rules set forth in 840 CMR 16.00 et seq. and 17.00 et seq.; the System's interest in the Fund but not any of the underlying assets of the Fund; provided that, at all times, the Fund qualifies as a "venture capital operating company" within the meaning of the Employee Retirement Income Security Act of 1974, as amended, and the regulations promulgated thereunder. As such, the limitations of 840 CMR Sections 16.00 et seq. and 17.00 et seq. shall not apply.

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

(2) the limitations and restrictions of 840 CMR Section 19.01(6) shall not apply to the Fund for the two-year period commencing on the date of the Fund's initial investment.

March 5, 2007

21.01(2). The State Street Global Advisors Index Plus Edge Strategy is allowed to sell short equities held within the S&P 500 Index. This is to allow the manager to underweight any stock in the index by 0.50% relative to its weight in the benchmark. For every short position taken, a levered long position will be taken so that overall portfolio beta will be maintained at 1.0. Aggregate net equity exposure will not exceed total portfolio assets.

The Board and its consultant understand that shorting stocks can be risky and they are comfortable with the manager's ability to control those risks in this product.

March 2, 2007

16.08. The Hampden County Regional Retirement Board is authorized to invest in the Fidelity Real Estate Growth Fund III, now run under the umbrella of Pyramis Global Advisors Trust Company. The Board has been a satisfied investor in a predecessor Fidelity Real Estate Growth Fund, and the strategy and the portfolio management team are essentially the same. The Board has received over 100% of its original investment back from Fidelity (Pyramis) and is pursuing this investment in order to maintain its allocation to real estate. The manager has submitted the required regulatory documents.

October 8, 2002

In accordance with PERAC Investment Guideline 99-2, the Hampden County Regional Retirement Board is authorized to make some minor modifications to its large cap equity mandate with Freedom Capital Management.

First, as part of its portfolio rebalancing, the Board will initiate an investment in Freedom's "Style-Weighted Concentrated Fund". Run by the same portfolio management team as the board's existing accounts, this new fund is a "best ideas" fund that operates in the same investment universe as the large cap growth, large cap value, and equity style products in which the board currently invests.

Second, the Board's large cap growth and large cap value accounts will be changed from separate accounts to commingled funds. With no change in strategy or in the portfolio management team, the Board expects to achieve administrative efficiencies from these changes.

July 10, 2001

- I. Exemption of the Board and INVESCO from the second sentence of 840 CMR 17.04(1)(c) – This Regulation deals with the use of non-public information by managers and consultants. PERAC recognizes that, in making the investments contemplated by the INVESCO Funds delineated above, that sentence, which prohibits action until information is publicly disseminated, represents an undue burden on the ability

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

of the Partnerships to operate. Consequently, the Hampden County Retirement Board's request as it applies to 840 CMR 17.04(1)(c) is approved.

2. Exemption of the Board and INVESCO from 840 CMR 17.04(6), except as otherwise provided for in the Partnership Agreement and/or as disclosed in INVESCO's Form ADV – This Regulation deals with the Priority of Transactions and an investment manager's obligation to prioritize board transactions and provide the board with the opportunity to act prior to the manager acting, if applicable. PERAC recognizes that this Regulation may impede the ability of partnerships such as INVESCO's to operate. Upon receipt of a copy of the provisions of the Partnership Agreement and/or disclosures in the INVESCO Form ADV, the Commission will approve the Hampden County Retirement Board's request as it applies to 840 CMR 17.04(6).
3. Exemption of the Board and INVESCO from 840 CMR 19.01(7)(a)(6) with respect to the management fees and the General Partner's Carried Interest to be received by the manager or the General Partner pursuant to the (a) Subscription Agreement, (b) Agreement as defined in the side letter, and/or (c) Manager's Investment Advisory Agreement with respect to the Board's commitments to the Partnerships – PERAC recognizes the fact that the market, at the present time, is such that fee limitations, as outlined in these Regulations, result in limiting the number of partnerships available to the retirement boards. Consequently, the Hampden County Retirement Board's request, as it applies to 840 CMR 19.01(7)(a)(6), is approved.
4. Exemption of the Board and INVESCO from 840 CMR 21.01(2), 21.01(3)(a), 21.01(4), and 21.01(5) to the extent as otherwise permitted under the applicable agreement – These Regulations prohibit certain transactions as follows: 21.01(2) prohibits the sale of securities not owned by the system at the time of the sale (short sales); 21.01(3)(a) permits the use of forward currency contracts in limited circumstances; 21.01(4) prohibits the use of call options; 21.01(5) prohibits the purchase of options other than as required to close out option positions. PERAC has received a letter dated August 22, 2000 from INVESCO that clarifies the possible use of options, futures, or other derivatives. In pertinent part, the letter states as follows:

“Although the above referenced funds do not expect to use options, futures, or other derivatives other than infrequently, if at all, futures and/or options would be used only for nonspeculative true hedging purposes. In general, we would anticipate their use, if at all, for among other reasons to protect downside risk on public securities of companies distributed to the funds by the underlying portfolio funds we invest in and where a commitment to a fund was made in a non US currency to limit currency risk of the funds.”

PERAC approves the exemption of the Board and INVESCO from 840 CMR 21.01(2), 21.01(3)(a), 21.01(4), and 21.01(5) for the limited purpose of protecting downside risk on public securities of companies distributed to the funds by underlying portfolio funds and to

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

limit currency risk of the funds where a commitment to a fund was made in a non US currency.

Please be advised that this Supplemental Regulation as it exempts the Hampden County Retirement Board from PERAC Regulations, only does so in relation to the INVESCO Funds that are the subject of the Supplementary Regulation. In all other circumstances, these Regulations apply to the Hampden County Retirement Board.

The Supplementary Regulations approved herein are applicable only to the Hampden County Retirement System's investment in the INVESCO Venture Partnership Fund III, L.P. Exemption from the regulations pertaining to prohibited investments is limited to the purpose of protecting downside risk on public securities of companies distributed to the funds by underlying portfolio funds and to limiting currency risk of the funds where a commitment to a fund was made in a non-U.S. currency.

NOTES TO FINANCIAL STATEMENTS

NOTE I – SUMMARY OF PLAN PROVISIONS

The plan is a contributory defined benefit plan covering all Hampden County Regional 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 \$687.96 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 Hampden County Retirement System submitted the following supplementary membership regulations, which were approved by the Public Employee Retirement Administration Commission on:

January 28, 2002

Durable Power of Attorney for Retirement Board Purposes:

The Retirement Board has prepared for its members, retirees and beneficiaries use, a Durable Power of Attorney form which the Board strongly urges all persons contemplating the need for such form to complete and forward to the Retirement Board. The purpose of this regulation is to encourage uniformity in the use of these documents and to reduce the opportunity for misfeasance and/or fraud.

September 25, 2000

Signature on the Disability Transmittal

The board authorizes, after approval of an application for disability retirement by the Retirement Board at a formal meeting, the Executive Director or in his absence the Assistant Director to sign the PERAC transmittal form regarding that disability.

May 5, 2000

Public Officials Regulations

X. Public Officials Regulation

A person appointed by the Mayor, Board of Selectmen, Town Council or Retirement Board, to serve as a member of a public Board or Commission or as public official in a member unit of the Hampden County Regional Retirement System including but not limited to member of the Retirement Board, Planning Board, Board of Public Health, Town Counsel, Assessor, Legal Counsel, Police Chief or Fire Chief, shall be entitled to membership in the Hampden County Regional Retirement System provided that the person earns at least two hundred dollars in a calendar year, and regardless of whether the person is employed more than twenty hours per week. Credit for such service shall be calculated by using a fraction in which the denominator is 1000 and the numerator is the actual hours employed in a calendar year by the person. If the numerator equals or exceeds the denominator then the person shall be entitled to one year of creditable service per calendar year of actual service. If the numerator is less than the denominator then that fraction shall be multiplied by 12 to determine the number of full months of the creditable service the person is entitled to. If the person receives a stipend or annual payment or compensation without a requirement of hours to be worked, then creditable service shall be determined by using a fraction in which the denominator is

NOTES TO FINANCIAL STATEMENTS (Continued)

2400 and the numerator is the amount of stipend paid or compensation received by the person in a calendar year. If the numerator equals or exceeds the denominator then the person shall be entitled to six months of creditable service.

January 19, 1999

The Hampden County Board of Retirement may designate a hearing officer for the purpose of conducting preliminary hearings regarding all ordinary and accidental disability claims, accidental death claims and retirement forfeiture issues.

September 11, 1996

I. MINIMUM EARNINGS REQUIRED FOR MEMBERSHIP

All employees including elected or appointed officials must earn more than two hundred dollars in a calendar year for at least one year in order to be eligible for membership in the retirement system. Once this requirement is met, the individual remains a member of the retirement system even if he or she earns less than two hundred dollars in a calendar year thereafter.

II. REQUIREMENTS FOR MEMBERSHIP

A. A permanent full-time employee of any member unit of the Hampden County Retirement System shall become a member of the Hampden County Retirement System on the first day of employment.

B. A part-time permanent employee who normally works more than twenty hours per week shall become a member of the Hampden County Retirement System on the first day of employment.

C. A seasonal employee who normally works more than twenty hours per week for five months or more in a year shall become a member of the Hampden County Retirement System on the first day of employment.

D. Part-time employees whose normal work week is twenty hours or less and seasonal employees whose normal work week is less than twenty hours or who are employed less than five months in a year, temporary or provisional employees shall not become members of the Hampden County Retirement System until they meet one of the requirements set out in Regulation II. A, B or C above.

E. Elected officials shall continue to have the option of joining the Hampden County Retirement System in accordance with General Laws Chapter 32 section 3 (2) (a) (vi) provided the official meets the requirements of Regulation I above.

III. CREDITABLE SERVICE FOR LESS THAN PERMANENT FULL-TIME EMPLOYMENT

A. All employees who are members of the Hampden County Retirement System who are full time permanent, part time, temporary, provisional or seasonal employees shall receive full creditable service for service rendered during his or her period of membership in the retirement system or for any period of creditable service purchased as prior service pursuant to regulation IV.

NOTES TO FINANCIAL STATEMENTS (Continued)

IV. BUY BACK OF CREDITABLE SERVICE

A. For any employee who is not a member of the Hampden County Retirement System on the first day of employment, that employee shall be allowed to buy back their service with a member unit as a non-member regardless if the employee made contributions to social security. However, an employee who is a member of the Hampden County Retirement System shall not be eligible to buy-back service credit for service rendered as a non-member if the employee did not earn at least one thousand five hundred dollars in a calendar year for the year the buy back is being requested.

V. CREDITABLE SERVICE FOR CALL FIREFIGHTERS AND PERMANENT INTERMITTENT OR RESERVE POLICE OFFICERS

A. The Board shall credit as full-time service not to exceed a maximum of five years that period of time during which a reserve or permanent-intermittent police officer or a reserve, permanent-intermittent or call firefighter was on his respective list and was eligible for assignment of duty subsequent to his appointment, and provided that such service as a reserve or permanent-intermittent police officer or call firefighter was later appointed as a permanent member of the fire department or police department.

B. Creditable service for a call firefighter or reserve or permanent-intermittent police officer shall be credited with one year of full creditable service for every two full years of service as a reserve or permanent-intermittent police officer or call firefighter, as consistent in Section 4 (2)(b) of Chapter 32.

C. A call firefighter who is elected in a manner prescribed by the General Laws shall be credited with one year of creditable service for each year as an elected firefighter.

October 18, 2002

The Board adopted Travel Supplemental Regulations under the provisions of G.L. c.7, § 50 and G.L. c. 32, § 21(4). This regulation established rules for membership of less than full time, appointed officials and is consistent with the provisions of G.L. c. 32. (Regulation available upon 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 Chairman/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 M. Theroux

Appointed Member: Karl J. Schmaelzle Term Expires: 12/31/08

Elected Member: Patricia C. Donovan Term Expires: 12/31/10

Elected Member: Laurel A. Plazek Term Expires: 01/01/10

Appointed Member: Patrick E. O'Neil Term Expires: 12/02/09

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:)	
Ex-officio Member:)	\$50,000,000 Fiduciary,
Elected Member:)	\$1,000,000 Fidelity
Appointed Member:)	MACRS Master 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 Buck Consultants as of January 1, 2007.

The actuarial liability for active members was	\$182,187,074
The actuarial liability for retired members was	169,574,665
The actuarial liability for non-vested terminated members was	<u>2,773,641</u>
The total actuarial liability was	354,535,380
System assets as of that date were	<u>218,738,644</u>
The unfunded actuarial liability was	<u>\$135,796,736</u>
The ratio of system's assets to total actuarial liability was	61.7%
As of that date the total covered employee payroll was	\$81,740,364

The normal cost for employees on that date was	8.00% of payroll
The normal cost for the employer was	6.20% of payroll

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

Investment Return:	8.50% per annum
Rate of Salary Increase:	5.50% per annum

GASB STATEMENT NO. 25, DISCLOSURE INFORMATION AS OF JANUARY 1, 2007

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)
1/1/2007	\$218,738,644	\$354,535,380	\$135,796,736	61.7%	\$81,740,364	166.1%
1/1/2006	\$200,497,347	\$332,139,489	\$131,642,142	60.4%	\$77,836,219	169.1%
1/1/2005	\$191,979,825	\$317,047,443	\$125,067,618	60.6%	\$74,555,992	167.7%
1/1/2004	\$187,556,932	\$294,799,663	\$107,242,731	63.6%	\$69,403,424	154.5%
1/1/2003	\$175,587,680	\$281,630,496	\$106,042,816	62.3%	\$68,912,960	153.9%
1/1/2002	\$168,722,805	\$268,661,316	\$99,938,511	62.8%	\$69,512,256	143.8%

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 6 - MEMBERSHIP EXHIBIT

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Retirement in Past Years										
Superannuation	59	56	43	54	45	71	63	63	52	45
Ordinary Disability	4	1	1	1	2	0	0	1	1	1
Accidental Disability	5	5	4	5	3	3	2	4	3	6
Total Retirements	68	62	48	60	50	74	65	68	56	52
Total Retirees, Beneficiaries and Survivors	1,412	1,423	1,426	1,418	1,419	1,422	1,423	1,476	1,474	1,475
Total Active Members	2,403	2,436	2,557	2,600	2,585	2,547	2,500	2,520	2,544	2,618
Pension Payments										
Superannuation	\$7,612,885	\$8,148,501	\$8,786,162	\$9,244,607	\$9,715,087	\$10,691,474	\$11,594,197	\$12,379,087	\$12,830,172	\$13,334,483
Survivor/Beneficiary Payments	655,725	656,658	660,699	741,041	665,289	690,571	706,330	754,949	799,231	811,254
Ordinary Disability	242,209	268,801	295,707	291,615	309,022	324,966	307,352	280,754	268,149	268,949
Accidental Disability	1,738,780	1,845,736	1,984,835	2,070,011	2,189,654	2,276,812	2,191,743	2,351,488	2,485,297	2,450,127
Other	1,610,278	564,370	573,255	541,486	2,633,502	2,125,601	2,499,811	1,734,897	2,328,525	2,402,302
Total Payments for Year	<u>\$11,859,877</u>	<u>\$11,484,066</u>	<u>\$12,300,658</u>	<u>\$12,888,760</u>	<u>\$15,512,554</u>	<u>\$16,109,424</u>	<u>\$17,299,433</u>	<u>\$17,501,175</u>	<u>\$18,711,374</u>	<u>\$19,267,115</u>

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