

PERAC AUDIT REPORT



Lexington Contributory Retirement System

JAN. 1, 2005 - DEC. 31, 2006



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PERAC

COMMONWEALTH OF MASSACHUSETTS | PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION COMMISSION

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JOSEPH E. CONNARTON, *Executive Director*

October 24, 2007

The Public Employee Retirement Administration Commission has completed an examination of the Lexington Retirement System pursuant to G.L. c. 32, § 21. The examination covered the period from January 1, 2005 to December 31, 2006. 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 Sweeney 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. Checking Account

The only cash account appearing on the general ledger is the System's custodial cash account (general ledger account number 1040) from which some expenses relating to investments are paid directly by the custodian. Deposits for members' deductions, incoming transfers and buybacks, and appropriations are received into that account. A separate checking account at Bank of America is used to pay expenses and retiree allowances. It normally functions with a zero beginning and ending balance each month. A transfer is made from the custodial account to fund each month's payroll and warrant.

Four checks remain outstanding in the Bank of America account from November 2005 through January 2007. One is payable to the estate of a deceased retiree. The remaining three, plus two current checks, are to a single retiree in small amounts totaling approximately \$45. Although the administrator has contacted the retiree, the small dollar amount of each check has evidently contributed to the retiree's failure to cash them in a timely manner.

Recommendation: Although total cash reported on the general ledger appears to be accurate, sound internal financial control practices would dictate that the checking account should be assigned a separate ledger number. This was a finding in a previous audit. Posting transactions to the cash account in which they occur will provide an audit trail for all cash movements and ensure that total cash reported is accurate, should the checking account end the month with something other than a zero balance.

The administrator should continue to research how to return the outstanding check to the deceased member's estate. The other retiree should be contacted to deposit her outstanding checks.

Board Response:

The Board believes the internal controls of the accounting system as it currently exists are sufficiently maintained to account for all transactions processed through the retirement office and to set up a second cash account would be redundant. There is adequate documentation readily available to support all cash flow.

PERAC Response: There is no authoritative source that would sanction the combining of transactions that occur in two separate bank accounts within a single general ledger account. Generally accepted auditing standards and any objective evaluation of internal controls would dictate that accounting entries reflect the source and destination of all cash flows. While the Bank of America monthly statements accurately reflect these transactions, no entries currently appear on the System's general ledger to document them or provide a sufficient audit trail. Published Government Auditing Standards require auditors to comment on reportable conditions relating to internal control.

EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

2. Membership

An examination of members' payroll records showed that a weekly payment for remaining on-call after normal hours was rotated among four Lexington Housing Authority employees. This payment has been erroneously excluded when calculating retirement deductions.

Another member is receiving a small monthly reimbursement toward the cost of using his personal cellular phone. Retirement deductions are being taken from this payment, but it does not qualify as regular compensation as defined in 840 CMR 15.03.

Recommendation: The Housing Authority members' "on-call" compensation is not calculated on an hourly basis for time worked, neither does it depend on actually performing services during the on-call period. These payments are regular and recurring, even though routinely allocated among four members, and they qualify as regular compensation under 840 CMR 15.03.

The second member's contract stipulates that the "Town shall compensate" the member "toward the cost of [his] personal cellular phone," and "payment shall cease immediately" in the event he "accepts a Town-provided cellular phone." The Board must determine whether these payments require submission of proof of cost by the employee and as a result are reimbursements, or whether payments are in a flat amount and, therefore, not a reimbursement but regular compensation.

In order to prevent future errors, the payroll department should notify the Retirement System of new pay codes to allow the Board to determine whether they qualify as regular compensation for retirement purposes.

Board Response:

The Director of the Lexington Housing Authority has been informed that the four members who receive "on call" compensation on a rotating basis should be having this amount included in their regular compensation per the PERAC auditors. The Housing Authority Director's response was that the LHA Board considers this "on call" compensation to be overtime since the member receives no compensation if unable to be on call for his/her designated week.

The member who was receiving the small monthly reimbursement toward the use of his personal cell phone has been informed it is not considered regular compensation for retirement purposes. He has been refunded the amount that was included in his retirement deductions. Human Resource and payroll personnel have been requested to notify the

EXPLANATION OF FINDINGS AND RECOMMENDATIONS

(Continued)

retirement director of any new pay codes and to allow the Board to determine whether they qualify as regular compensation as defined in 840 CMR 15.03.

PERAC Response: With all due respect, the Director of the Lexington Housing Authority and that Board has no authority to interpret Chapter 32 or to contradict the regulations relating to retirement practices. It is the Lexington Retirement Board's responsibility to determine what is regular compensation subject to retirement deductions. It has been established that this type of compensation is “reasonable and recurring” and related to their regular job responsibilities. This has been sufficient in many other systems to include this type of compensation as qualifying for retirement contributions. The fact that no compensation is paid if a person cannot fulfill the “on-call” requirements does not change this interpretation.

3. Contracts

Only one of three executed vendor contracts requested for review could be located by the staff.

Recommendation: The Board must comply with 840 CMR 16.02(5) which states in part “A copy of every contract shall be retained by the board and be subject to audit by the commission.” A total review of all vendor contracts should be made to confirm that fully executed contracts exist and are on file with the Board.

Board Response:

The Lexington Retirement System is participating in vehicles that are registered mutual funds. The Board’s statement reflects the acknowledgement between the Board and the investment managers that they are invested in these funds. On file there were documents that were signed by the Lexington Retirement System but lacked the necessary signature of an agent of a few investment companies. These representatives have been asked to forward copies of signed documents to maintain compliance with 840 CMR 16.02 (5).

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,	
	2006	2005
Assets:		
Cash	\$2,494	\$0
Short Term Investments	579,193	1,197,342
Equities	6,750,192	5,943,121
Pooled Domestic Equity Funds	7,342,576	6,296,673
Pooled International Equity Funds	31,012,070	25,769,494
Pooled Domestic Fixed Income Funds	13,353,655	12,647,585
Pooled Domestic Balanced Funds	50,020,396	45,135,052
PRIT Cash Fund	0	0
PRIT Core Fund	0	0
Interest Due and Accrued	4,886	4,899
Accounts Receivable	1,915,975	1,857,277
Accounts Payable	(159,245)	(92,183)
Total	<u>\$110,822,191</u>	<u>\$98,759,260</u>
Fund Balances:		
Annuity Savings Fund	\$20,996,103	\$19,274,033
Annuity Reserve Fund	6,443,296	6,840,732
Pension Fund	845,501	3,173,897
Military Service Fund	5,324	5,292
Expense Fund	0	0
Pension Reserve Fund	82,531,966	69,465,305
Total	<u>\$110,822,191</u>	<u>\$98,759,260</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
Ending Balance (2005)	18,245,826	6,693,484	6,806,758	5,261	0	61,054,029	92,805,359
Receipts	2,668,039	199,180	2,210,068	32	456,062	8,417,521	13,950,902
Inter Fund Transfers	(859,905)	866,150	0	0	0	(6,245)	0
Disbursements	<u>(779,927)</u>	<u>(918,082)</u>	<u>(5,842,930)</u>	0	<u>(456,062)</u>	0	<u>(7,997,001)</u>
Ending Balance (2005)	19,274,033	6,840,732	3,173,897	5,293	0	69,465,305	98,759,260
Receipts	2,608,285	195,852	3,691,789	32	615,587	13,057,321	20,168,866
Inter Fund Transfers	(359,579)	350,239	0	0	0	9,340	0
Disbursements	<u>(526,636)</u>	<u>(943,526)</u>	<u>(6,020,185)</u>	0	<u>(615,587)</u>	0	<u>(8,105,935)</u>
Ending Balance (2006)	<u>\$20,996,103</u>	<u>\$6,443,296</u>	<u>\$845,501</u>	<u>\$5,324</u>	<u>\$0</u>	<u>\$82,531,966</u>	<u>\$110,822,191</u>

STATEMENT OF RECEIPTS

	FOR THE PERIOD ENDING DECEMBER 31,	
	2006	2005
Annuity Savings Fund:		
Members Deductions	\$2,043,939	\$1,893,034
Transfers from Other Systems	398,275	606,548
Member Make Up Payments and Re-deposits	36,726	53,817
Member Payments from Rollovers	15,147	7,731
Investment Income Credited to Member Accounts	<u>114,200</u>	<u>106,908</u>
Sub Total	<u>2,608,285</u>	<u>2,668,039</u>
Annuity Reserve Fund:		
Investment Income Credited to the Annuity Reserve Fund	<u>195,852</u>	<u>199,180</u>
Pension Fund:		
3 (8) (c) Reimbursements from Other Systems	105,939	94,255
Received from Commonwealth for COLA and Survivor Benefits	243,519	241,598
Pension Fund Appropriation	<u>3,342,331</u>	<u>1,874,215</u>
Sub Total	<u>3,691,789</u>	<u>2,210,068</u>
Military Service Fund:		
Contribution Received from Municipality on Account of Military Service	0	0
Investment Income Credited to the Military Service Fund	<u>32</u>	<u>32</u>
Sub Total	<u>32</u>	<u>32</u>
Expense Fund:		
Expense Fund Appropriation	0	0
Investment Income Credited to the Expense Fund	<u>615,587</u>	<u>456,062</u>
Sub Total	<u>615,587</u>	<u>456,062</u>
Pension Reserve Fund:		
Federal Grant Reimbursement	0	0
Pension Reserve Appropriation	0	0
Interest Not Refunded	5,556	3,417
Miscellaneous Income	659	3,854
Excess Investment Income	<u>13,051,105</u>	<u>8,410,250</u>
Sub Total	<u>13,057,321</u>	<u>8,417,521</u>
Total Receipts	<u>\$20,168,866</u>	<u>\$13,950,902</u>

STATEMENT OF DISBURSEMENTS

	FOR THE PERIOD ENDING DECEMBER 31,	
	2006	2005
Annuity Savings Fund:		
Refunds to Members	\$193,916	\$279,461
Transfers to Other Systems	<u>332,720</u>	<u>500,466</u>
Sub Total	<u>526,636</u>	<u>779,927</u>
Annuity Reserve Fund:		
Annuities Paid	917,799	892,847
Option B Refunds	<u>25,727</u>	<u>25,235</u>
Sub Total	<u>943,526</u>	<u>918,082</u>
Pension Fund:		
Pensions Paid:		
Regular Pension Payments	4,443,071	4,396,424
Survivorship Payments	233,954	219,574
Ordinary Disability Payments	45,149	44,069
Accidental Disability Payments	767,849	678,947
Accidental Death Payments	180,311	164,856
Section 101 Benefits	4,850	0
3 (8) (c) Reimbursements to Other Systems	345,000	339,061
State Reimbursable COLA's Paid	0	0
Chapter 389 Beneficiary Increase Paid	<u>0</u>	<u>0</u>
Sub Total	<u>6,020,185</u>	<u>5,842,930</u>
Military Service Fund:		
Return to Municipality for Members Who Withdrew Their Funds	<u>0</u>	<u>0</u>
Expense Fund:		
Board Member Stipend	0	0
Salaries	65,515	60,000
Legal Expenses	3,881	8,670
Medical Expenses	0	50
Travel Expenses	4,186	3,171
Administrative Expenses	22,096	2,406
Furniture and Equipment	0	0
Management Fees	412,222	281,043
Custodial Fees	27,747	42,675
Consultant Fees	58,750	50,000
Rent Expenses	0	0
Service Contracts	16,425	8,047
Fiduciary Insurance	<u>4,765</u>	<u>0</u>
Sub Total	<u>615,587</u>	<u>456,062</u>
Total Disbursements	<u>\$8,105,935</u>	<u>\$7,997,001</u>

INVESTMENT INCOME

	FOR THE PERIOD ENDING DECEMBER 31,	
	2006	2005
Investment Income Received From:		
Cash	\$0	\$0
Short Term Investments	68,795	57,769
Fixed Income	0	0
Equities	101,241	14,737
Pooled or Mutual Funds	5,005,970	3,226,325
Commission Recapture	<u>0</u>	<u>0</u>
Total Investment Income	<u>5,176,006</u>	<u>3,298,831</u>
Plus:		
Realized Gains	122,520	524,647
Unrealized Gains	12,638,262	8,930,653
Interest Due and Accrued on Fixed Income Securities - Current Year	<u>4,886</u>	<u>4,899</u>
Sub Total	<u>12,765,668</u>	<u>9,460,199</u>
Less:		
Paid Accrued Interest on Fixed Income Securities	0	0
Realized Loss	(1,166)	(471,366)
Unrealized Loss	(3,958,834)	(3,113,962)
Interest Due and Accrued on Fixed Income Securities - Prior Year	<u>(4,899)</u>	<u>(1,271)</u>
Sub Total	<u>(3,964,899)</u>	<u>(3,586,599)</u>
Net Investment Income	<u>13,976,775</u>	<u>9,172,432</u>
Income Required:		
Annuity Savings Fund	114,200	106,908
Annuity Reserve Fund	195,852	199,180
Military Service Fund	32	32
Expense Fund	<u>615,587</u>	<u>456,062</u>
Total Income Required	<u>925,670</u>	<u>762,181</u>
Net Investment Income	<u>13,976,775</u>	<u>9,172,432</u>
Less: Total Income Required	<u>925,670</u>	<u>762,181</u>
Excess Income To The Pension Reserve Fund	<u>\$13,051,105</u>	<u>\$8,410,250</u>

SCHEDULE OF ALLOCATION OF INVESTMENTS OWNED

(percentages by category)

AS OF DECEMBER 31, 2006			
	MARKET VALUE	PERCENTAGE OF TOTAL ASSETS	PERCENTAGE ALLOWED
Cash	\$2,494	0.0%	100%
Short Term	579,193	0.5%	40-80%
Equities	6,750,192	6.2%	70%
Pooled Domestic Equity Funds	7,342,576	6.7%	
Pooled International Equity Funds	31,012,070	28.4%	20%
Pooled Domestic Fixed Income Funds	13,353,655	12.2%	
Pooled Domestic Balanced Funds	50,020,396	45.9%	
PRIT Cash Fund	0	0.0%	
PRIT Core Fund	0	0.0%	
Grand Total	<u>\$109,060,575</u>	<u>100.0%</u>	

For the year ending December 31, 2006, the rate of return for the investments of the Lexington Retirement System was 14.50%. For the five-year period ending December 31, 2006, the rate of return for the investments of the Lexington Retirement System averaged 9.74%. 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 Lexington Retirement System was 10.59%.

SUPPLEMENTARY INVESTMENT REGULATIONS

The Lexington Retirement System submitted the following supplementary investment regulations, which were approved by PERAC on:

June 27, 2007

16.08

In accordance with Investment Guideline 99-2, the Lexington Retirement Board is authorized to modify its international equity management mandate with Wellington Management Company. Assets currently in Wellington's Pacific Basin portfolio (which is being closed) will be transferred to the Asia Pacific ex-Japan portfolio. The two funds are very similar in strategy and style except that the new fund does not invest in Japan. This difference is acceptable to the Board since it has exposure to Japan in two separate international equity portfolios.

October 26, 2004

21.01 (2) (3)

In order to expand the range of investment opportunities and to better manage risk, Wellington Management Company's Opportunistic Investment Approach is authorized to utilize long and short positions in certain derivative instruments. These positions would be used to implement pair-wise relative value trades involving various asset classes and subclasses, regions, currencies, and other market segments. The instruments used will be highly liquid, no net leverage will be employed, and there will be no individual stocks sold short. The notational value of such instruments will be limited to 15% of the total market value of the portfolio.

July 28, 2004

16.08

In accordance with PERAC Investment Guideline 99-2, the Lexington Retirement Board is authorized to modify its international equity mandate with Wellington Management Company. The Board wishes to increase its exposure to the Pacific Rim, and intends to do so by investing in a new commingled fund, the Wellington Pacific Basin Investment Approach. Pacific Rim stocks already constitute about one quarter of the investment universe in which Wellington currently invests for the Board. Lexington has had a very satisfactory relationship with Wellington for international equity management for over ten years and, based on the depth of the firm's international equity portfolio management and research staff and the excellent performance record of the Pacific Basin product, it feels that this is the most effective and efficient way to achieve greater exposure to that area. The investment team that manages the Pacific Basin product is part of the team that manages the EAFE product in which the Board currently invests, and the investment process and strategy are the same.

September 12, 1996

20.06(10)

Private Placement securities falling under the governance of Rule 144A may be purchased up to 5% of the market value of the fixed income portfolio at the time of purchase. These Rule 144A Private Placements shall be considered to be corporate bonds and, as such, governed by guideline

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

constraints pertaining to corporate bonds including those stated in the Statement of Objectives (Form 18-1) and PERA Regulations 840 CMR.

20.03(1)

Equity investments shall not exceed 70% of the portfolio valued at market, including international equities, which shall not exceed 20% of the portfolio valued at market.

May 22, 1992

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.

August 1, 1991

16.02(4)

The board may charge custodian bank expenses against earned income from investments in an amount not to exceed .08% of the market value of the assets of the system on an annual basis.

September 14, 1989

20.04(6) American Depository Receipts listed on a United States stock exchange or traded over the counter in the United States, provided that all such investments not exceed 6% of the total market value of the portfolio.

NOTES TO FINANCIAL STATEMENTS

NOTE I – SUMMARY OF PLAN PROVISIONS

The plan is a contributory defined benefit plan covering all Lexington 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 at 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 \$667.92 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 \$100,000.00 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 Lexington Retirement System submitted the following supplementary membership regulations, which were approved by PERAC on:

February 19, 1992

Membership

A minimum workweek of eighteen (18) hours shall be required for membership in the System.

February 13, 1991

Creditable Service

Permanent part-time employees working at least 18 hours per week are granted full time creditable service.

June 6, 1990

Creditable Service

For school employees, nine (9) months served shall be equal to 12 months creditable service.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 5 - ACTUARIAL VALUATION AND ASSUMPTIONS

The most recent actuarial valuation of the System was prepared by Buck Consultants, LLC as of January 1, 2006.

The actuarial liability for active members was	\$51,210,453
The actuarial liability for retired members was	<u>60,513,521</u>
The total actuarial liability was	111,723,974
System assets as of that date were	<u>98,759,260</u>
The unfunded actuarial liability was	<u>\$12,964,714</u>
The ratio of system's assets to total actuarial liability was	88.4%
As of that date the total covered employee payroll was	\$22,149,964

The normal cost for employees on that date was 8.02% of payroll
 The normal cost for the employer was 5.65% of payroll

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

Investment Return: 8.00% per annum
 Rate of Salary Increase: Varies by Service

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	\$98,759,000	\$111,724,000	\$12,965,000	88.4%	\$22,150,000	58.5%
1/1/2004	\$83,050,000	\$98,031,000	\$14,981,000	84.7%	\$20,464,000	73.2%
1/1/2002	\$77,015,000	\$86,500,000	\$9,485,000	89.0%	\$20,803,000	45.6%
1/1/1999	\$71,069,000	\$74,362,000	\$3,293,000	95.6%	\$18,631,000	17.7%

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 6 - MEMBERSHIP EXHIBIT

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Retirement in Past Years										
Superannuation	8	13	14	14	21	7	42	8	12	9
Ordinary Disability	0	1	0	0	0	0	0	0	0	0
Accidental Disability	0	1	0	1	0	0	1	0	4	0
Total Retirements	8	15	14	15	21	7	43	8	16	9
Total Retirees, Beneficiaries and Survivors	353	351	353	351	360	361	389	385	403	381
Total Active Members	667	670	664	670	690	692	652	584	614	619
Pension Payments										
Superannuation	\$3,170,917	\$2,409,881	\$2,525,620	\$2,685,347	\$2,981,963	\$3,238,169	\$3,336,345	\$4,281,068	\$4,396,424	\$4,443,071
Survivor/Beneficiary Payments	*	187,976	192,657	193,365	216,132	235,102	226,138	222,283	219,574	233,954
Ordinary Disability	*	46,108	46,857	47,523	49,250	50,618	45,071	42,989	44,069	45,149
Accidental Disability	*	582,100	583,711	578,716	577,167	573,842	602,568	627,593	678,947	767,849
Other	*	128,271	101,598	256,869	288,754	270,532	300,137	369,004	503,916	530,161
Total Payments for Year	\$3,170,917	\$3,354,336	\$3,450,443	\$3,761,820	\$4,113,267	\$4,368,262	\$4,510,259	\$5,542,938	\$5,842,930	\$6,020,185

* Information unavailable, during this time frame the Board was not differentiating the types of pension payments.

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