

Worcester Retirement System
Worcester, Massachusetts
(A Component Unit of the
City of Worcester, Massachusetts)



Comprehensive Annual Financial Report
Fiscal Year Ended December 31, 2008

**Worcester Retirement System
Worcester, Massachusetts
(A Component Unit of the City of Worcester, Massachusetts)**

**Comprehensive Annual Financial Report
For the Fiscal Year Ended December 31, 2008**

**Prepared by the Staff of the
Worcester Retirement System**

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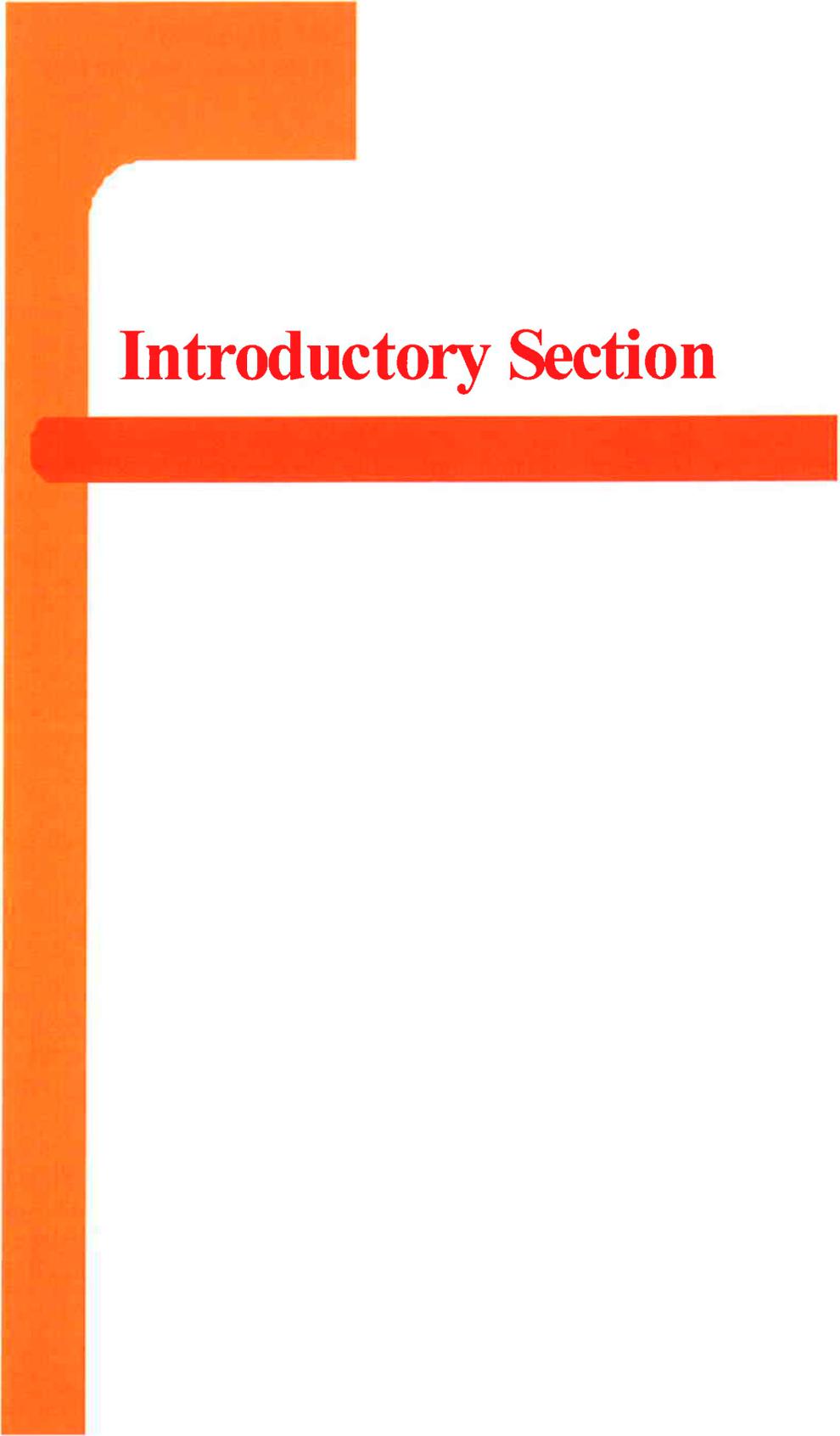
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Introductory Section

Worcester Retirement System

Room 103 City Hall Worcester Massachusetts 01608 Phone (508) 799 1062

Chairman's Letter

July 16, 2009

Dear Members of the Worcester Retirement System:

On behalf of the Worcester Retirement Board (Board), I am pleased to present the Comprehensive Annual Financial Report (CAFR) of the Worcester Retirement System (WRS) for the year ended December 31, 2008. The report is designed to provide a detailed look at the financial, investment and actuarial aspects of the WRS.

A comprehensive report is being issued in the interest of full disclosure to WRS members and to demonstrate the diligent stewardship and internal controls that are in place to protect assets and maintain financial integrity. The last five consecutive CAFRs have been awarded the Certificate of Achievement for Excellence in Financial Reporting making WRS one of only four retirement systems in New England to receive this prestigious award, a fact of which we are all very proud.

The Board typically meets at least twice a month. There is one meeting to discuss benefit issues and at least one other to discuss investment issues and conduct due diligence on those investments. It is the fiduciary responsibility of the Board to insure that current and future pensions will be paid. Therefore, safeguarding the WRS investment portfolio is a top priority. In that regard, the WRS has a policy that incorporates an asset allocation with a 20-year time horizon containing asset classes that involve investment risk to reap the rewards of potential stellar returns and but to also diversify those assets to mitigate risks during the inevitable times when certain asset classes experience sub-par returns.

After having investment returns in excess of our actuarial benchmark for the previous five years, last year proved to be the worst year for investment returns in the history of WRS as net of fee returns were a negative 28.49-percent on a time-weighted and GAAP (GAAP required the recognition of approximately \$1.8 million of unrealized losses in the securities lending collateral pool) basis. The world-wide recession had an extremely negative effect on every asset class during 2008 except for cash and treasury bonds, which only yielded low single-digit returns.

In an attempt to recognize the investment losses of 2008, stay current and stay on a systematic course to fully fund WRS in a reasonable amount of time, the City petitioned the State Legislature to allow it to extend the funding schedule to fund liabilities from, the currently allowed, June 30, 2028 to June 30, 2038. This proposed "home rule" petition was denied by the legislature and in its place was approved legislation that would allow the schedule to be extended to June 30, 2030.

In the hope that the home rule petition would be approved the Board had instructed its actuary to prepare a funding schedule for the 2038 scenario as part of the January 1, 2009 Actuarial Valuation. The fiscal year 2010 amount in the 2038 funding scenario was incorporated into the City's original budget. The 2038 funding schedule requires fiscal year 2010 funding of \$28.5 million and the 2030 funding schedule would require \$32.1 million. The Board has been allowed by PERAC to assess its member units the budgeted amount (per the 2038 scenario) for fiscal year 2010 but will be required to revert to the 2030 funding scenario for the fiscal 2011 assessment. Depending on market conditions it is likely that the City and many other communities will again petition the legislature to extend the funding schedule to a date later than June 30, 2030 before the funding requirement for fiscal year 2011 is determined.

Last year the WRS unfunded actuarial accrued liability increased from \$130.5 million to \$297.7 million on an actuarial basis and to \$403.0 million on a market basis. There was an experience loss of \$278.1 million due, for the most part, to investment losses. There were also actuarial losses due to greater than expected salaries increases and fewer deaths than expected.

I would like to thank the other members of the Board for their diligence on retirement matters and the Board's investment consultant, actuary and independent auditors for their assistance with the preparation of this report and advice on other matters. I would also like to thank the Board's legal representatives for their counsel and the Public Employee Retirement Administration Commission for the oversight of our actions.

Finally, I would like to commend the staff of WRS for their diligent work in preparing this report and their commitment to continually improving administrative operations. I encourage members to carefully review this report as it contains a wealth of information about your retirement system.

Sincerely,

A handwritten signature in cursive script that reads "James DelSignore".

James DelSignore, CPA
Chairman

Worcester Retirement System
Room 103 City Hall Worcester Massachusetts 01608 Phone (508) 799 1062

July 16, 2009

Worcester Retirement Board
City Hall Room 103
455 Main Street
Worcester, MA 01608

Dear Mr. Chairman and Members of the Board:

We are pleased to submit the Comprehensive Annual Financial Report (CAFR) of the Worcester Retirement System (WRS) for the year ended December 31, 2008. The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the WRS for its CAFR for the year ended December 31, 2007. This was the fifth consecutive year that the WRS has achieved this prestigious award. In order to be awarded a Certificate of Achievement, the WRS must publish an easily readable and efficiently organized CAFR. This report must satisfy both accounting principles generally accepted in the United States of America and applicable legal requirements. Management accepts responsibility for the contents of the report.

A Certificate of Achievement is valid for a period of one year only. We believe that our current CAFR continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

GASB Statement No. 34 requires that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to compliment the MD&A and should be read in conjunction with it. The WRS's MD&A can be found immediately following the report of the independent auditor.

History of the WRS

The WRS became operative as of January 1, 1945. The WRS is a contributory defined benefit plan that covers eligible employees of the City of Worcester (except Worcester Public School teachers) and the Worcester Housing Authority (WHA). The WRS is administered by a five member Board consisting of the City Auditor, two representatives elected from the membership, a City Manager representative and a fifth member chosen by the other four who cannot be an employee, retiree or official of the City. One Board member is elected from the group to serve as Chairman.

Investment Results

The WRS has an Investment Policy Statement which establishes investment objectives and policies providing the framework for investments. This Policy is reviewed on an annual basis. A summary of Investment Policy is included in the Investment Section. The System uses a custodian bank to safeguard the assets and ensure proper settlement and recording of transactions.

An integral part of the overall investment policy is the asset allocation policy. This is designed to provide an optimal mix of asset classes to both preserve principal and provide adequate funds to pay pension benefits. Both traditional assets (cash, bonds, domestic stocks, domestic fixed income and mortgages) and nontraditional assets (real estate, international stock and fixed income, venture capital, mezzanine financing, hedge funds, timber and leveraged buyouts) are part of the mix. Typically the investment market results have demonstrated the importance of a diversified asset allocation. However in 2008 the global recession impacted virtually every asset class and traditional diversification provided little protection from significant losses.

WRS' dollar-weighted investment return of -27.1% for 2008 fell short of both the actuarial expected rate of return and the Investment policy benchmark. This loss follows five consecutive calendar years of positive results for the system. Please refer to the Investment Section of this CAFR for more information on investment results.

Major Initiatives

Benefits

A cost of living adjustment (COLA) was provided for retirees and survivors effective July 1, 2008. The 3% COLA was paid on a base of \$12,000 (maximum \$360), the most allowed by law. The WRS has granted the maximum increase every year since enactment of the legislation in 1997.

Chapter 68 of the Acts of 2007, An Act to Reduce The Stress on Local Property Taxes Through Enhanced Pension Fund Investment, was signed into law July 25, 2007. This Act amends MGL chapter 32 section 22 and directs the Public Employee Retirement Administration Commission (PERAC) to conduct an annual analysis of all Massachusetts public pension plans. The assessment includes the investment performance and funded ratio of each system every January 1st in accordance with the established methodology and standard. Systems failing to meet the standard are mandated to transfer ownership and control of the systems assets to the Massachusetts Pension Reserve Investment Management (PRIM) Board. The WRS met these mandated standards for both 2007 and 2008 and currently are not subject to mandatory transfer of system assets.

Administration

The WRS strives to provide quality service and information to active and retired members and their beneficiaries. To assist in this effort, we maintain and continually update our Internet site through the City web page, which includes our CAFR, at www.ci.worcester.ma.us/ret.

Internal and Budgetary Controls

The WRS management is responsible for maintaining a system of internal controls designed to provide reasonable assurance that the financial statements are fairly stated in accordance with accounting principles generally accepted in the United States of America while adequately safeguarding the assets. We believe the current internal controls accomplish this goal.

The WRS budget is presented to and approved by the Board each year. All the expenditures are reviewed by the Board at its monthly meeting.

Accounting

This report has been prepared in accordance with accounting principals generally accepted in the United States of America. The basic financial statements are presented in accordance with the principles of the Government Accounting Standards Board (GASB), including guidelines established by GASB Statements No. 25, *Financial reporting for defined benefit plans*; No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*; No. 37, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments: Omnibus*, No. 38, *Certain Financial Statement Note Disclosures*; No. 40 *Deposit and Investment Risk Disclosures (an amendment of GASB No. 3)* and No. 50 *Pension Disclosures*.

Sullivan, Rogers & Company, LLC, a firm of licensed certified public accountants, performed the audit for the WRS. The goal of the independent audit is to provide reasonable assurance that the financial statements for the year ended December 31, 2008 are free of material misstatements. The report of the independent auditors is included in the Financial Section of this report. Sullivan, Rogers & Company, LLC has issued an unqualified opinion on the WRS’s basic financial statements for the year ended December 31, 2008.

Actuarial Funding

The WRS has retained the services of The Segal Company, an independent actuarial firm, to conduct an annual actuarial valuation of the WRS. The funded ratio is one measure of the financial condition of the WRS. The funded ratio is calculated by dividing the net assets of the WRS by the projected pension liability. The projected pension liability is a measure of the present value of total pension benefits estimated to be payable in the future to both current and future retirees and/or beneficiaries. A higher funding ratio gives the members a greater degree of assurance that their pension benefits are secure. As of January 1, 2009 the funded ratio of the WRS was calculated at 67.98%, a 17.35% decrease from the prior year.

Acknowledgements

The publication of this report represents the combined efforts of the WRS Board, staff, Sullivan, Rogers & Company, LLC and consultants. We are proud to present this report to our members. We feel it is important to provide a CAFR for our members and other interested parties to follow the progress of the WRS.

Respectfully submitted,

A handwritten signature in black ink that reads "Elizabeth A. Early". The signature is written in a cursive, flowing style.

Elizabeth A. Early
Executive Secretary

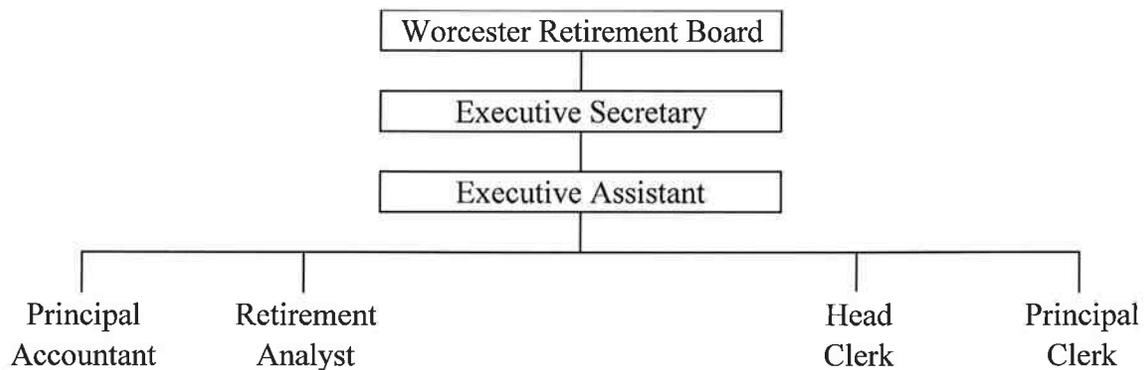
Retirement Board Members

		<u>Terms</u>
James DelSignore	Ex-Officio Member	N/A
Stephen F. Wentzell	City Manager Appointee	At the discretion of the City Manager
Elizabeth A. Early	Elected Member	11/01/2007 - 10/31/2010
Raymond F. McGrath	Elected Member	01/01/2006 - 12/31/2008
Thomas Wade	Appointed Member	01/09/2006 - 01/08/2009

Administrative Staff

Elizabeth A. Early	Executive Secretary
Judith McMillen	Executive Assistant
Donna Tyndall	Principal Accountant
Donna McCaffrey	Retirement Analyst
Barbara Zecco	Head Clerk
Eileen Powers	Principal Clerk

Organizational Chart*



* Does not include investment professionals who provide services to the WRS. A list of these investment professionals is located on the following page.

CONSULTANTS AND PROFESSIONAL SERVICES

DOMESTIC EQUITY MANAGERS

Columbia Management Advisors, LLC
Hartford, CT
Enhanced Investment Technologies, LLC
West Palm Beach, FL
Loomis Sayles & Company, L.P.
Boston, MA
PENN Capital Management Co, Inc
Philadelphia, PA
State Street Global Advisors
Boston, MA

DOMESTIC FIXED MANAGERS

OPUS Investment Management, Inc.
Worcester, MA
Loomis Sayles & Company, L.P.
Boston, MA

INTERNATIONAL EQUITY MANAGERS

Acadian Asset Management
Boston, MA
The Boston Company Asset Management, LLC
Boston, MA
State Street Global Advisors
Boston, MA
Lazard Asset Management
New York, NY

ALTERNATIVE CAPITAL

INVESTMENT MANAGERS
Actos Alternatives Management, LLC
New York, NY
Ascent Venture Management
Boston, MA
Benchmark Plus Management
Tacoma, WA
Blackstone Alternative Asset Management
New York, NY
Boston Capital Ventures
Boston, MA
Boston Millennia Partners
Boston, MA
Charlesbank Capital Partners
Boston, MA
Concord Partners L.P.
Wellesley, MA
Duke Street Capital
London, England
Global Infrastructure Partners
New York, NY
Harvest Partners, LLC
New York, NY
INVESCO Private Capital, Inc.
Atlanta, GA
Mellon Capital Management
San Francisco, CA
New England Partners Capital L.P.
Boston, MA
Newstone Capital Partners, L.P.
Los Angeles, CA
Northstar Capital, LLC
Minneapolis, MN
Mass PRIM
Boston, MA
PIMCO Funds
New York, NY
Standard Life Investments Limited
Edinburgh, UK
The Riverside Company
New York, NY
Vitruvian Partners
London, England

REAL ESTATE MANAGERS

Bailard Fund Services, Inc.
Foster City, CA
Heitman Investment Management
Chicago, IL
Intercontinental Real Estate Corp.
Boston, MA
INVESCO Core Real Estate
New York, NY
RREEF America, LLC
Chicago, IL
RMK Timberland a div. of Regions Bank
Winston-Salem, NC
Mass PRIM
Boston, MA
Apollo Real Estate Advisors
Atlanta, GA
Hancock Timber Resource Group
Boston, MA

LEGAL ADVISORS

The Law Offices of Michael Sacco
Southampton, MA

INDEPENDENT AUDITORS

Sullivan, Rogers & Company, LLC
Burlington, MA

INVESTMENT ADVISORS

Meketa Investment Group
Westwood, MA

ACTUARIAL CONSULTANT

The Segal Company
Boston, MA

CUSTODIAN

State Street Corporation
Boston, MA

COMMISSION RECAPTURE BROKERS

BNY ConvergEx Group
New York, NY

SECURITIES LENDING

State Street Corporation
Boston, MA

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Worcester Retirement System Massachusetts

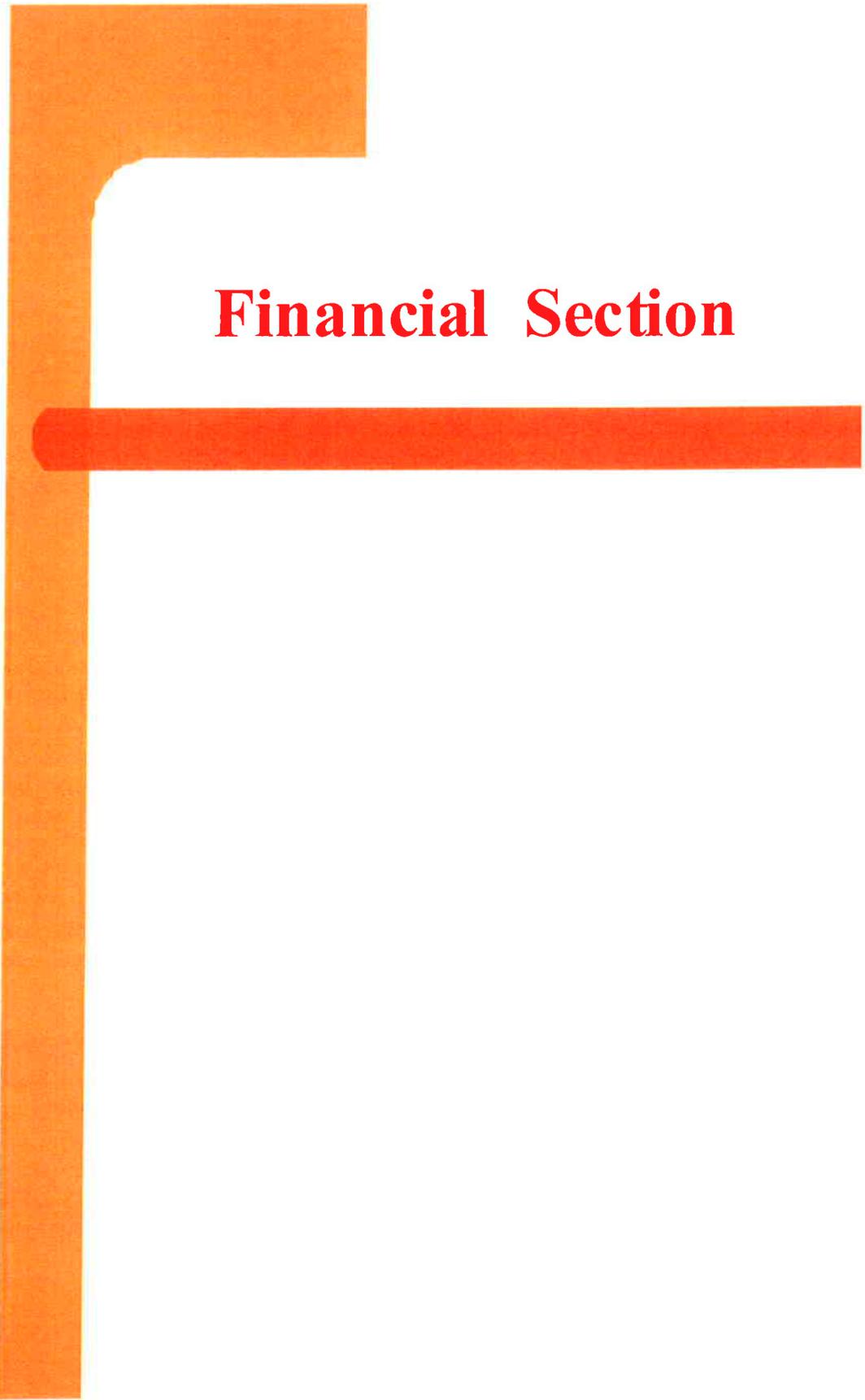
For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
December 31, 2007

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director



Financial Section



Certified Public Accountants

SULLIVAN, ROGERS & COMPANY, LLC
Corporate Place I, Suite 204 • 99 South Bedford Street
Burlington, Massachusetts 01803
P • 781-229-5600 F • 781-229-5610 www.sullivan-rogers.com

Independent Auditors' Report

To the Honorable Retirement Board
Worcester Retirement System

We have audited the accompanying basic financial statements of the Worcester Retirement System (WRS), a component unit of the City of Worcester, Massachusetts, as of and for the year ended December 31, 2008, as listed in the table of contents. These financial statements are the responsibility of the WRS's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the WRS as of December 31, 2008, and the respective change in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated July 16, 2009, on our consideration of the WRS's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in conjunction with this report in considering the results of our audit.

The management's discussion and analysis (located on pages 14 through 19) and historical pension information (located on page 32) are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the WRS's basic financial statements. The supplementary information, introductory section, investment section, actuarial section, and statistical section are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory, investment, actuarial and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

A handwritten signature in cursive script that reads "Sullivan, Ray & Company, LLC".

July 16, 2009

Management's Discussion & Analysis

Our discussion and analysis of the Worcester Retirement System's (WRS) financial performance provides an overview of the WRS's financial activities for the fiscal year ended December 31, 2008. Please read it in conjunction with the transmittal letter in the Introductory Section, at the front of this report, and the basic financial statements that follow this discussion. The Management's Discussion and Analysis (MD&A) is intended to serve as an introduction to the WRS's basic financial statements, as well as to offer readers of the WRS's financial statements a narrative view and analysis of the WRS's financial activities.

Financial Highlights

The WRS's funding objective is to meet long-term benefit obligations through contributions and investment income. As of December 31, 2008, the funded ratio was 67.98% based on the actuarial value of assets at that date.

Net assets decreased during the year by \$233 million, or 30.7%, because of poor investment returns. Net assets are the residual of the WRS's assets in excess of the WRS's liabilities as of the statement date. The WRS's assets are held in trust to meet future benefit payments.

Total investment losses were \$213.7 million. The dollar-weighted investment rate of return was -27.1% compared with a positive return of 9% in the previous year (refer to the "Investment Results" table in the Investment Section).

Overview of the Financial Statements

The basic financial statements are comprised of a Statement of Plan Net Assets, Statement of Changes in Plan Net Assets, Notes to the Financial Statements and Required Supplementary Information.

The *Statement of Plan Net Assets* presents information on the WRS's assets and liabilities and the resulting net assets held in trust for pension benefits. This is calculated using the following formula: $\text{Assets} - \text{Liabilities} = \text{Net Assets held in trust for pension benefits}$. This statement reflects the WRS's investments at fair value, as well as cash, receivables and other assets and liabilities. The Statement of Plan Net Assets reports the financial position of the WRS at December 31, 2008. Over time, the increase or decrease in net assets serves as a useful indicator of the WRS's financial health.

The *Statement of Changes in Plan Net Assets* presents information showing how the WRS's net assets held in trust for pension benefits changed during the year ended December 31, 2008. It reflects contributions by members and participating employers along with deductions for retirement benefits, refunds, withdrawals, and administrative expenses. Investment income during the period is also presented showing income from investing and securities lending activities.

Management's Discussion & Analysis

The *Notes to the Financial Statements* provide additional information that is essential for the reader to gain a full understanding of the data provided in the financial statements.

The *Required Supplementary Information* includes this MD&A and schedules of funding progress and employers' contributions.

Financial Analysis

The WRS's total assets as of December 31, 2008 were \$596.7 million and were primarily comprised of cash and cash equivalents, receivables, and investments. Total assets decreased \$181.3 million, or 23.3%, from the prior year primarily due to investment losses.

Total liabilities as of December 31, 2008 were \$70 million and were primarily comprised of payables for securities purchased as well as payables to other state retirement plans and collateral held under securities lending arrangements. Total liabilities increased by \$51.4 million.

The following tables present current and prior year data on the WRS's financial statements.

Management's Discussion & Analysis

Net Assets

Net assets of the WRS totaled \$526.6 million at the close of the fiscal year and are summarized as follows:

Plan Net Assets (In thousands of dollars)

Assets	2008	2007
Cash and cash equivalents	\$ 4,540	\$ 6,469
Investments	523,221	753,505
Securities lending short-term collateral investment pool	66,281	13,696
Receivables:		
Interest due and accrued	950	1,177
Due from Commonwealth of Massachusetts and other systems	356	1,556
Receivable for securities sold	1,192	1,573
Other	157	9
Total assets	596,697	777,985
Liabilities		
Accounts payable and accrued expenses	263	528
Due to Commonwealth of Massachusetts and other systems	2,421	3,131
Payable for securities purchased	1,154	1,219
Collateral held on securities lending transactions	66,281	13,696
Total liabilities	70,119	18,574
Net assets held in trust for pension benefits	\$ 526,578	\$ 759,411

Management's Discussion & Analysis

Changes in Net Assets

The WRS's total net assets decreased by \$232.8 million during the current fiscal year and are summarized as follows:

Changes in Net Assets

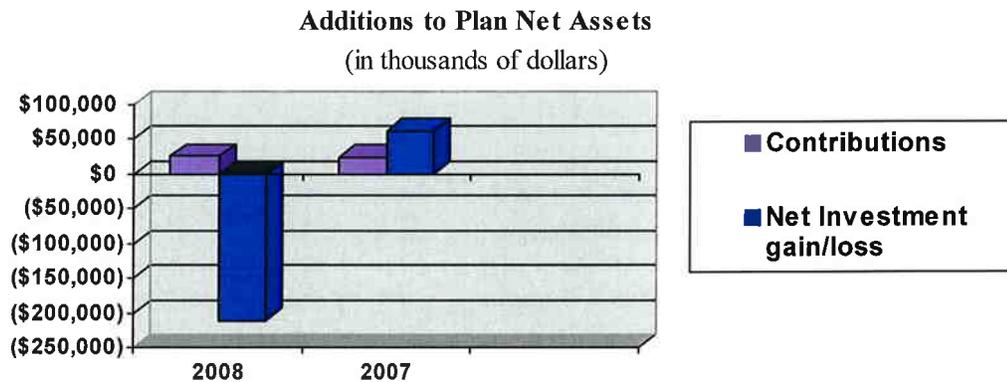
(in thousands of dollars)

	2008	2007
Additions		
Contributions:		
Employers	\$ 24,947	\$ 24,166
Plan members	14,695	13,923
Reimbursements from Commonwealth of Massachusetts	1,198	2,427
Reimbursements from other Systems	356	374
Net investment income:		
Interest and dividends	9,328	13,436
Securities lending income	601	1,061
Net realized and unrealized gains (losses)	(219,967)	52,529
Less: management fees	(3,197)	(4,320)
Less: borrower rebates & fees	(420)	(1,015)
	(172,459)	102,581
Deductions		
Benefits payments to plan members and beneficiaries	56,516	55,033
Reimbursements to other systems	2,002	1,936
Refunds and transfers of plan member accounts to other systems	1,302	2,442
Administrative expenses	554	556
	60,374	59,967
	(232,833)	42,614
Net assets held in trust for pension benefits:		
Beginning of year	759,411	716,797
End of year	\$ 526,578	\$ 759,411

Management's Discussion & Analysis

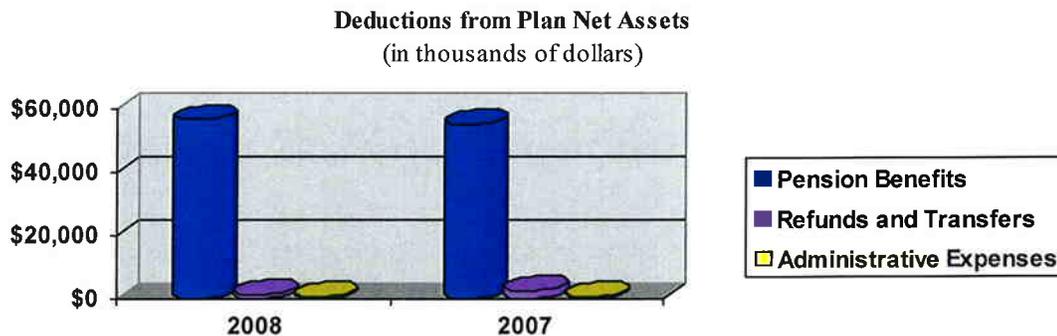
Additions to Plan Net Assets

The amount needed to finance benefits is accumulated through the collection of employers' and employees' contributions, reimbursements from the Commonwealth of Massachusetts for pre-1998 COLA's and through earnings on investments. Contributions and net investment losses for calendar year 2008 resulted in total reductions to net assets of (\$172.5) million. Employers' contributions increased by \$781 thousand in 2008. The WRS had a net investment loss of \$213.7 million in 2008 versus a gain of \$61.7 million in 2007.



Deductions from Plan Net Assets

The primary deductions of the WRS include the payment of pension benefits to participants and beneficiaries, refunds of contributions, and the costs of administering the WRS. Total deductions from net assets for 2008 were \$60.4 million, which represents an increase of 0.7% over deductions of \$60.0 million in 2007. The payment of pension benefits increased by \$1.5 million, or 2.7%, over the previous year. The increase in these expenses resulted from an increase in benefit payments to newer retirees with higher average compensation offset by a small decrease in the number of pensioners and beneficiaries.



Management's Discussion & Analysis

Overall Financial Position of WRS

Due to a decline in the financial markets, the WRS has experienced a decrease in its investment portfolio for the fiscal year ending December 31, 2008. However, management believes the WRS is in a solid financial position and will be able to meet its obligations.

Contacting WRS's Financial Management

This financial report is designed to provide the Board, our membership, taxpayers, investors, and creditors with a general overview of the WRS's financial results and to demonstrate WRS's accountability for the funding it receives. If you have any questions about this report or need additional financial information, contact the Worcester Retirement System, City Hall Room 103, 455 Main Street, Worcester, Massachusetts 01608.

WORCESTER RETIREMENT SYSTEM
 (A Component Unit of the City of Worcester, Massachusetts)
Statement of Plan Net Assets
 December 31, 2008

Assets	
Cash & Cash Equivalents	\$ <u>4,540,494</u>
Investments:	
Equities	148,374,974
Fixed Income	83,330,738
Pooled Equities	81,595,791
Pooled Fixed Income	20,455,943
Real Estate	78,233,713
Alternative Investments	<u>111,229,908</u>
Total investments	<u>523,221,067</u>
Securities lending short-term collateral investment pool	<u>66,280,770</u>
Receivables:	
Accrued interest and dividends	949,626
Due from Commonwealth of Massachusetts and other systems	355,936
Receivable for securities sold	1,192,201
Other	<u>156,566</u>
Total receivables	<u>2,654,329</u>
Total plan assets	<u>596,696,660</u>
Liabilities	
Accounts payable and accrued expenses	263,065
Due to Commonwealth of Massachusetts and other systems	2,420,920
Payable for securities purchased	1,153,646
Collateral held on securities lending transactions	<u>66,280,770</u>
Total plan liabilities	<u>70,118,401</u>
Net assets held in trust for pension benefits (see schedules of funding progress on pages 30 and 32)	<u>\$ <u>526,578,259</u></u>

See accompanying notes to financial statements.

WORCESTER RETIREMENT SYSTEM
(A Component Unit of the City of Worcester, Massachusetts)
Statement of Changes in Plan Net Assets
Year ended December 31, 2008

Additions:

Contributions:

Employers	\$ 24,947,158
Plan members	14,695,126
Reimbursements from Commonwealth of Massachusetts	1,198,044
Reimbursements from other systems	<u>355,936</u>
Total contributions	<u>41,196,264</u>

Investment income (loss):

Interest and dividends	9,328,423
Securities lending income	601,676
Net realized and unrealized gains (losses)	(219,966,280)
Less: management fees	(3,197,422)
Less: borrower rebates and fees under securities lending program	<u>(420,300)</u>
Net investment income	<u>(213,653,903)</u>

Total additions	<u>(172,457,639)</u>
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Deductions:

Benefit payments to plan members and beneficiaries	56,516,348
Reimbursements to other systems	2,002,234
Refunds and transfers of plan member accounts to other systems	1,301,576
Administrative expenses	<u>554,276</u>
Total deductions	<u>60,374,434</u>

Change in plan net assets	(232,832,073)
---------------------------	---------------

Net assets held in trust for pension benefits:

Beginning of year	<u>759,410,332</u>
End of year	\$ <u><u>526,578,259</u></u>

See accompanying notes to financial statements.

**Notes to Financial Statements
December 31, 2008**

1. Summary of Significant Accounting Policies

(a) Financial Reporting Entity

Because of the significance of its operational and financial relationship with the City of Worcester, Massachusetts (City), the Worcester Retirement System (WRS) is included as a blended component unit in the City's financial statements.

(b) Basis of Accounting

The accompanying financial statements are presented on the accrual basis of accounting.

(c) Revenue Recognition

Contributions are recognized as additions in the period when they become due pursuant to formal commitments, statutory or contractual requirements. Investment income is recognized when earned.

(d) Benefits and Refunds

Benefits and refunds to WRS members and beneficiaries are recognized as deductions when due and payable in accordance with the terms of the WRS.

(e) Deposits and Investments

Cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with an original maturity of three months or less from the date of acquisition.

Investments are reported at fair value. Fair values of investments are based on quotations from a national securities exchange except for pooled funds, venture capital and real estate, for which fair values are estimated as detailed below.

Pooled Funds

The fair value of shares in managed investment pools is based on unit values reported by the funds.

Venture Capital and Alternative Investments

Venture capital investments are recorded at fair value as determined in good faith by the general partners of the venture capital firms after consideration of pertinent information, including current financial position and operating results, price-earnings multiples and available market prices of similar companies' securities, the nature of securities, marketability, restrictions on disposition and other appropriation and do not necessarily represent amounts which might ultimately be realized, since such amounts depend on future circumstances and cannot reasonably be determined until individual securities are liquidated.

Real Estate

The fair value of real estate funds is based on independent third-party appraisals. The investment managers of the funds are responsible for the reported value of those investments. However, the structure, risk profile, return potential and marketability of those investments differ from traditional equity and fixed income investments. Determination of the value of these investments involves subjective judgment because the actual market value can be determined only by negotiation between the parties to a sales transaction. As a result, the estimated values may differ significantly from the values that would have been used had a ready market for the real estate existed, and the differences could be material.

(f) Basis of Investment Transactions

Purchases and sales of investments are recorded on the trade date. Transactions remaining unsettled as of year-end are recorded as payables for securities purchased and as a receivable for securities sold.

(g) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of additions and deductions during the reporting period. Fair values of real estate funds and venture capital funds have been estimated in the absence of readily available market values, and these estimates may be materially different than values that would have been used had a ready market existed.

(h) Administrative Expenses

Administrative expenses are financed by investment income.

2. Plan Description

(a) General

The WRS is a cost-sharing multiple-employer public employee retirement system established by the City on June 12, 1944, under Massachusetts General Laws (MGL), Chapter 32, and is regulated by the Massachusetts Public Employee Retirement Administration Commission (PERAC). The WRS is a defined benefit pension plan that covers certain eligible employees of the City and the Worcester Housing Authority. For the year ended December 31, 2008, the City's payroll for employees covered by WRS was approximately \$166,000,000; the City's total payroll was approximately \$320,000,000.

Membership in the WRS is mandatory immediately upon the commencement of employment for all permanent full-time employees working at least 20 hours weekly, except for City school teachers, who participate in the Massachusetts Teachers' Retirement System.

Membership in the WRS was as follows at December 31, 2008:

Active employees	3,352
Pensioners and beneficiaries	2,792
Inactive employees	<u>910</u>
 Total members	 <u><u>7,054</u></u>
 Number of participating employers	 <u><u>2</u></u>

The WRS is administered by a five-person Retirement Board (the Board) consisting of the City Auditor, who serves *ex-officio*; two members who are elected by the participants in or retired from the service of the WRS; a fourth member appointed by the City Manager; and a fifth member appointed by the other members.

(b) Significant Plan Provisions and Requirements

Benefit provisions and state law establishes contribution requirements of the WRS. Members of the WRS become vested after 10 years of creditable service. Normal retirement occurs at age 65 except for employees of the City's Police and Fire departments, whose normal retirement age is 55. Retired employees receive an allowance based upon the average of their three highest average salary years of service multiplied by (1) the number of years and full months of creditable service at the time of retirement and (2) a percentage based on age at retirement in accordance with a schedule provided by state law.

Assuming normal retirement at age 65, this percentage is 2.5%, which is reduced for individuals who retire prior to age 65 to reflect the longer pay out period.

Employees may elect early retirement after 20 years of service or at any time after attaining age 55 with 10 years of eligible service. Plan members who become permanently and totally disabled may be eligible to receive a disability retirement allowance. The amount of benefits to be received depends on several factors, including the member's age, compensation, veteran status, years of service and whether or not the disability is work-related. In addition, certain death benefits exist for beneficiaries of employees who die in active service.

Under MGL, c.32 Section 3(8)(c), for members leaving the City's employment to work for other Massachusetts governmental units, the WRS transfers their accumulated account balances and creditable service to the retirement system of their new employer. Other such retirement systems are in turn required to make comparable transfers to the WRS for employees coming to work for the City or the Worcester Housing Authority. Liability for the service transfer is not calculated until the member's actual retirement date. Per statute, the PERAC actuary shall consider length of service as well as acceptance of military service credit and salary cap provisions if applicable in calculating the liability.

3. Deposits and Investments

Deposits and investments made by the WRS are governed by the MGL c.32. The WRS has the ability to invest in equity securities, corporate bonds, annuities and other specified investments in accordance with state laws and regulations.

Deposits - Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of a bank failure, the WRS's deposits may not be recovered. The WRS's policy for custodial credit risk of deposits is to rely on FDIC insurance coverage for the first \$250,000 of deposits held at each financial institution. As of December 31, 2008, the WRS's bank balance of \$1,388,955 was not exposed to custodial credit risk.

Investments Summary

The WRS's investments at December 31, 2008 are presented below. All investments are presented by investment type, with debt securities presented by maturity.

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 - 5	6 - 10	More Than 10
<u>Debt Securities:</u>					
U.S. Treasuries.....	\$ 53,629,656	\$ 24,717,709	\$ 10,679,427	\$ 9,792,414	\$ 8,440,106
U.S. Agencies.....	25,084,183	1,612,705	2,500,232	1,112,911	19,858,335
Corporate bonds.....	29,779,722	6,416,726	6,684,343	10,695,938	5,982,715
Money market mutual funds..	3,593,454	3,593,454	-	-	-
Debt security mutual funds....	25,543,602	20,925,463	-	-	4,618,139
Total debt securities.....	<u>137,630,617</u>	<u>\$ 57,266,057</u>	<u>\$ 19,864,002</u>	<u>\$ 21,601,263</u>	<u>\$ 38,899,295</u>
<u>Other Investments:</u>					
Equity securities.....	93,620,340				
Equity mutual funds.....	172,380,715				
Real estate investments.....	78,233,713				
Alternative investments.....	<u>111,229,908</u>				
Total other investments.....	<u>455,464,677</u>				
Total investments.....	<u>\$ 593,095,294</u>				

Investments - Interest Rate Risk of Debt Securities

Interest rate risk for debt securities is the risk that changes in interest rates of debt securities will adversely affect the fair value of an investment. The WRS's policies for interest rate risk intend that the average duration of investments remain fairly stable over time and be focused in the intermediate range. The WRS's debt security managers are not permitted to make large-scale changes in portfolio duration in an attempt to anticipate interest rate changes. However, they are permitted to shift portfolio duration within a limited range (defined by their guidelines) in an effort to enhance performance.

Investments - Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, the WRS will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The WRS's policy for custodial credit risk of investments intends that all investments are either insured and/or registered in the name of the WRS. As of December 31, 2008, the WRS was not exposed to custodial credit risk.

Investments - Credit Risk of Debt Securities

Credit risk for debt securities is the risk that an issuer or other counterparty to a debt security will not fulfill its obligations. The WRS's policies for credit risk of debt securities sets minimum average quality requirements for investment strategies employed, among other limitations. In monitoring credit risk, the WRS relies on credit ratings assigned by Moody's and Standard & Poor's. As of December 31, 2008, the credit quality ratings of the WRS's debt securities are as follows:

Quality Ratings *	Investment Type			Fair Value
	Corporate Bonds	Money Market Mutual Funds	Debt Security Mutual Funds	
AAA.....	\$ 2,799,149	\$ -	\$ 2,989,769	\$ 5,788,918
AA.....	420,053	-	-	420,053
AA-.....	1,032,892	-	-	1,032,892
A+.....	785,510	-	-	785,510
A.....	2,193,023	-	107,394	2,300,417
A-.....	2,345,875	-	-	2,345,875
BBB+.....	2,494,993	-	-	2,494,993
BBB.....	1,688,771	-	396,101	2,084,872
BBB-.....	1,808,358	-	-	1,808,358
BB+.....	780,490	-	-	780,490
BB.....	1,216,375	-	-	1,216,375
BB-.....	1,281,791	-	-	1,281,791
B+.....	2,310,850	-	94,013	2,404,863
B.....	944,425	-	-	944,425
B-.....	449,244	-	-	449,244
CCC+.....	902,020	-	-	902,020
CCC.....	648,138	-	-	648,138
CCC-.....	37,200	-	-	37,200
CC.....	51,400	-	-	51,400
D.....	277,734	-	-	277,734
Unrated.....	5,311,431	3,593,454	21,956,325	30,861,210
Total.....	\$ <u>29,779,722</u>	\$ <u>3,593,454</u>	\$ <u>25,543,602</u>	\$ <u>58,916,778</u>

* Per the rating scale of Standard & Poors, a national credit rating organization

Deposits and Investments – Foreign Currency Risk

Foreign currency risk is the risk that fluctuations in exchange rates will adversely affect the fair value of an investment or a deposit. The WRS’s policy is to limit investments in non-U.S. dollar-denominated securities to not exceed 10% of the total market value of investments at all times. As of December 31, 2008, the WRS’s exposure to foreign currency risk is as follows:

<u>Deposit/Investment Type</u>	<u>U.S. Dollar Balances</u>	<u>Currency</u>
Corporate bonds.....	\$ 662,169	South Korean won
U.S. Agencies.....	537,052	Mexican peso
Corporate bonds.....	504,711	Singapore dollar
Corporate bonds.....	306,144	Indonesian rupiah
U.S. Agencies.....	170,829	Canadian dollar
U.S. Agencies.....	160,765	Australian dollar
Corporate bonds.....	42,027	Canadian dollar
Corporate bonds.....	<u>34,497</u>	Australian dollar
Total.....	<u>\$ 2,418,194</u>	

Investments – Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the WRS’s investment in a single issuer. The WRS’s policy for concentration of credit risk instructs investment managers not to invest more than 5% of their portfolio at market value in a single security, or in the securities of a single issuer or its subsidiaries. U.S. Treasury, U.S. government agency, mutual fund and pooled fund investments are exempted from this restriction. As of December 31, 2008, the WRS was not exposed to concentration of credit risk.

Subsequent Events

Subsequent to year end, the financial markets have experienced significant levels of volatility that caused a decline in the value of certain investments held at year end. While such declines may be temporary, investment values are subject to market fluctuations, and the timing of any such recovery is unknown at the present time.

4. Securities Lending Transactions

PERAC has issued supplemental regulations that permit the WRS to engage in securities lending transactions. These transactions are conducted by the WRS’s custodian, who lends certain securities owned by the WRS to other broker-dealers and banks pursuant to a form of loan agreement. The WRS and the borrowers maintain the right to terminate all securities lending transactions on demand.

The custodian lends, at the direction of the lending agent, the WRS's securities and cash received (including both U.S. and foreign currency), U.S. government securities, sovereign debt of foreign countries, and irrevocable bank letters of credit as collateral. The custodian does not have the ability to pledge or sell collateral unless the borrower defaults. Borrowers are required to deliver cash collateral in amounts equal to not less than 105% of the market value of foreign securities on loan and 102% of the market value of domestic securities on loan (Required Collateral Level). If at any time the market value of the collateral for any loan decreases to 100% or less of the market value of the loaned securities, borrowers are required to provide additional collateral sufficient to increase the market value of the collateral to at least the Required Collateral Level.

The WRS does not impose any restrictions on the amount of securities lent on its behalf by the custodian. There were no failures by any borrowers to return loaned securities or pay distributions thereon, nor were there any losses from default of the borrowers or the custodian for the year ended December 31, 2008. The cash collateral received on each loan was invested; together with the cash collateral of other qualified tax-exempt plan lenders, in a collective investment pool. The relationship between the average maturities of the investment pool and loans was affected by the maturities of the loans made by other plans that invested cash collateral in the collective investment pool, which the WRS could not determine. At December 31, 2008, the WRS had no credit risk exposure to borrowers because the amounts the WRS owed the borrowers exceeded the amounts owed the WRS. The cash collateral held and the fair value of the securities on loan for the WRS at December 31, 2008 and 2007 was \$66,280,770 and \$13,696,321 and \$66,105,108 and \$13,598,567, respectively. Borrower rebates and fees paid to the broker were \$420,300 for the year ended December 31, 2008.

5. Funding Policy

Chapter 32 of MGL governs the contributions of plan members and the City. Depending on their employment date, active System members must contribute 5%, 7%, 8% or 9% of their gross regular compensation. Members hired after December 31, 1978 must contribute an additional 2% of regular compensation in excess of \$30,000. These deductions earn interest at a rate determined by PERAC that vests based upon years of service. Employers are required to pay into the WRS its share of the system-wide actuarial determined contribution that is apportioned among the employers based on annual covered payroll.

Contributions are recognized as additions in the period when they become due pursuant to formal commitments, statutory or contractual requirements. Benefits and refunds are recognized as deductions when incurred and administrative expenses are funded through investment earnings.

Except for a portion of benefits owed due to cost-of-living adjustments granted through June 30, 1998, member employers are required to contribute the remaining amounts necessary to finance benefits. Member employer contributions are determined by the annual actuarial valuation.

COLA's granted through June 30, 1998 are reimbursed by the Commonwealth of Massachusetts (the Commonwealth). COLA's granted subsequent to June 30, 1998 must be granted by the Board and are the responsibility of the WRS. COLA may be approved in excess of the Consumer Price Index but not to exceed 3% on the first \$12,000 of a retirement allowance. The WRS has granted the maximum increase every year since June 30, 1998.

The funded status of the WRS at January 1, 2009, the most recent actuarial valuation date, is as follows:

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (b)	Unfunded Actuarial Accrued Liability (b - a)	Funded Ratio (%) (a/b)	Covered Payroll (c)	UAAL as a Percent of Covered Payroll (%) (b - a)/c
1/1/2009	\$ 631,893,995	929,569,464	297,675,469	67.98	\$ 166,050,095	179.27

The schedules of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, present multi-year trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the AAL for benefits.

The significant methods and assumptions of the latest actuarial valuation are as follows:

Valuation Date	January 1, 2009
Actuarial cost method	Entry Age Normal Cost Method
Amortization method	Level payments on the 2002 and 2003 ERI liability and the Section 90 ACD liability and 4.5% increasing payments on the remaining unfunded liability
Remaining amortized period	9 years for the 2002 ERI liability 3 years for the 2003 ERI liability 5 years for the Section 90 ACD liability and 21 years for the remaining unfunded liability (period closed)
Asset valuation method	The difference between the expected return and the actual investment return on a market value basis is recognized over a five-year period

Actuarial assumptions:

Investment rate of return	8.25%
Projected salary increases	3.00% for the next 2 years; 5.00% thereafter
Rate of inflation	4.00%
Cost of living adjustments	3.00% of first \$12,000 of retirement income

6. Legally Required Reserve Accounts

The balances in the WRS' legally required reserves as of December 31, 2008 are as follows:

Description	Amount	Purpose
Annuity Savings Fund	\$ 152,780,052	Active members' contribution balance
Annuity Reserve Fund	49,266,003	Retired members' contribution account
Military Service Fund	15,595	Members' contribution account while on military leave
Pension Reserve Fund	296,433,205	Amounts appropriated to fund future retirement
Pension Fund	28,083,404	Remaining net assets
Total	\$ 526,578,259	

All reserve accounts are funded at levels required by state law.

7. Implementation of GASB Pronouncements

During fiscal year 2008, the WRS implemented the following GASB pronouncements:

- Statement #49, Accounting and Financial Reporting for Pollution Remediation Obligations. This statement had no impact on the financial statements.
- Statement #50, Pension Disclosures. This Statement enhances pension disclosures in the notes to financial statements and RSI.

**Required Supplementary Information
December 31, 2008**

The following reflects the Schedule of Funding Progress under the Entry-Age-Normal Actuarial Cost Method, which is the required method for all retirement systems governed by MGL, c.32. The WRS believes that this method of valuation more clearly reflects the actual funded status of the WRS.

Schedule of Funding Progress

Actuarial Valuation <u>Date</u>	Actuarial Value of Plan <u>Assets *</u> (a)	Actuarial Accrued <u>Liability</u> (b)	Unfunded Actuarial Accrued <u>Liability</u> (b - a)	Funded <u>Ratio (%)</u> (a/b)	Covered <u>Payroll</u> (c)	UAAL as a Percent of Covered <u>Payroll (%)</u> (b - a)/c
1/1/2004	\$ 577,123,067	743,570,440	166,447,373	77.62	\$ 138,796,895	119.92
1/1/2005	606,099,616	771,948,311	165,848,695	78.52	147,126,606	112.73
1/1/2006	644,016,504	806,957,464	162,940,960	79.81	145,830,593	111.73
1/1/2007	716,796,770	837,608,233	120,811,463	85.58	152,838,201	79.05
1/1/2008	759,410,332	889,924,310	130,513,978	85.33	156,585,326	83.35
1/1/2009	631,893,995	929,569,464	297,675,469	67.98	166,050,095	179.27

* The 1/1/2005 through 1/1/2008 actuarial valuations valued plan assets at market value. The 1/1/2004 and 1/1/2009 actuarial valuations valued plan assets at the difference between the expected return and the actual investment return on a market value basis, recognized over a five-year period

Schedule of Employer Contributions

<u>Year Ended</u> <u>December 31</u>	<u>Annual Required</u> <u>Contributions</u>	<u>Percentage of Annual</u> <u>Required Contributed (%)</u>
2003	\$ 18,928,252	100
2004	20,150,377	100
2005	23,579,478	106
2006	23,354,603	100
2007	24,166,318	100
2008	24,947,158	100

**Supplementary Information
December 31, 2008**

Schedule of Administrative Expenses

The composition of administrative expenses for the year ended December 31, 2008 is as follows:

Personal Services:	
Staff Salaries	\$ 336,099
Board Member Compensation	15,000
Insurance	35,085
Total Personal Services	<u>386,184</u>
Professional Services:	
Legal Expenses	90,620
Actuarial Fees	26,500
Audit Fees	20,000
Medical Fees	690
Total Professional Services	<u>137,810</u>
Miscellaneous:	
Travel	4,738
Printing	729
Other	24,815
Total Miscellaneous	<u>30,282</u>
Total Administrative Expenses	<u><u>\$ 554,276</u></u>

Schedule of Investment and Consultants' Expenses**Investment Expenses**

Management Fees:

Domestic & Equity Managers	\$	503,372
Venture Capital Funds		1,093,529
Domestic Fixed Income Managers		301,732
International Investments Managers		516,838
Real Estate Investments Managers		370,531
Consultant Fees		170,000
Custodial Fees		241,420
Total Management Fees		<u>3,197,422</u>

Securities Lending Fees:

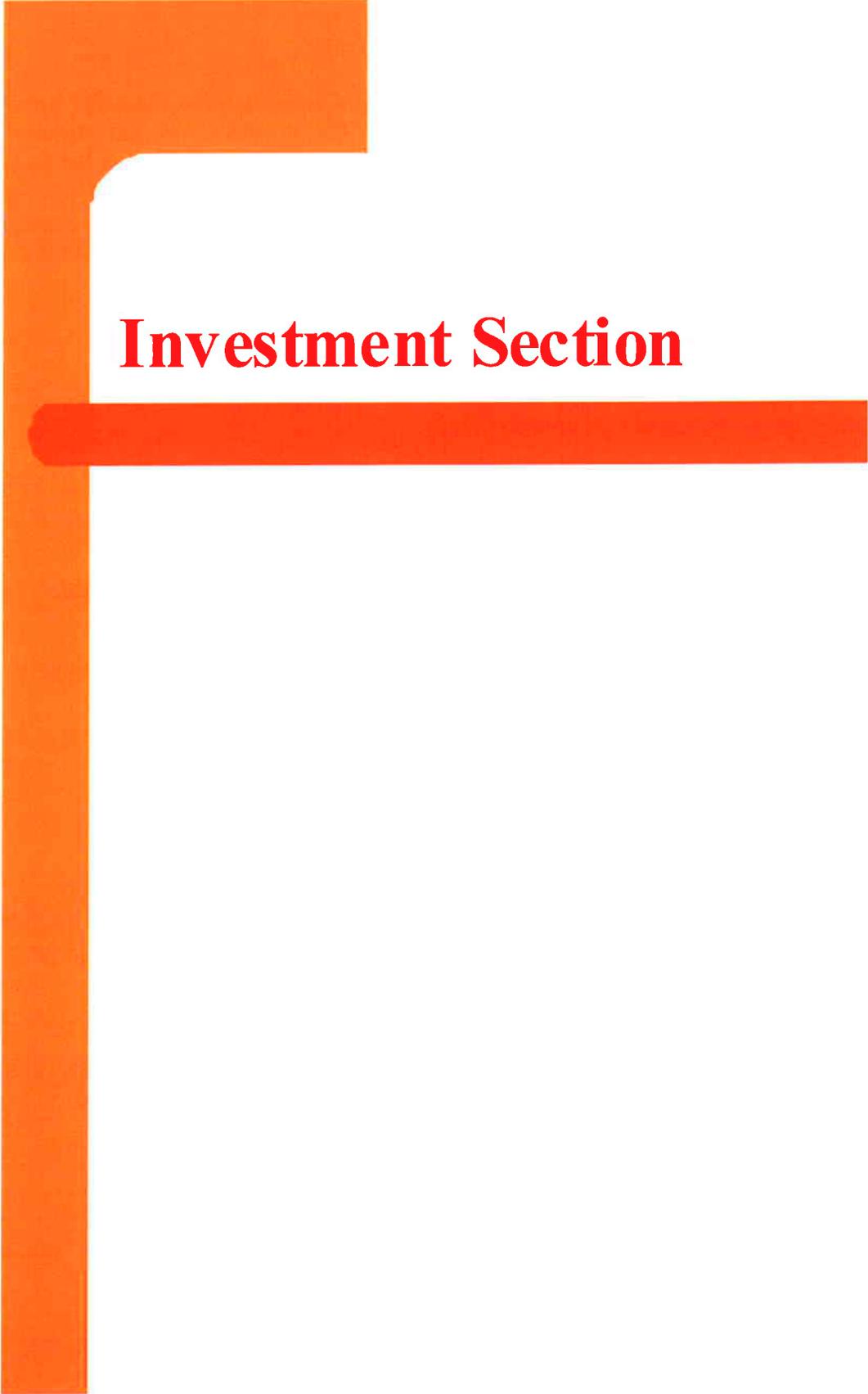
Borrowers Rebates		342,532
Fees		77,768
Total Securities Lending Fees		<u>420,300</u>

Total Investment Expenses \$ 3,617,722

Consultant Expenses:

Independent Audit Fees	\$	20,000
Actuarial Fees		26,500
Legal Fees		<u>90,620</u>

Total Consultant Expenses \$ 137,120



Investment Section

REPORT ON INVESTMENT ACTIVITY

The information contained in the Investment Section of the Comprehensive Annual Financial Report (CAFR) has been prepared by Meketa Investment Group, acting as the investment consultant for the Worcester Retirement System (WRS). All investment information herein has been reconciled between the WRS, the investment managers hired by the WRS, and Meketa Investment Group. The investment returns presented herein were calculated in a manner consistent with that specified in the Global Investment Performance Standards (GIPS®), as developed by the CFA Institute.

OUTLINE OF INVESTMENT POLICIES

The purpose of this document is to set forth the goals and objectives of the WRS, and to establish guidelines for the implementation of investment strategy.

The Board of the WRS recognizes that a stable, well-articulated investment policy is crucial to the long-term success of the WRS. As such, the Board has developed this Investment Policy Statement with the following goals in mind:

- To clearly and explicitly establish the objectives and constraints that govern the investment of the WRS's assets,
- To establish a long-term target asset allocation with a high likelihood of meeting the WRS's objectives given the explicit constraints, and
- To protect the financial health of the WRS through the implementation of this stable long-term investment policy.

I. Worcester Retirement System Goals

The WRS was established to provide retirement income for the City of Worcester and WHA employees and their families. The WRS's assets are structured to provide real growth from capital gains and income, while maintaining sufficient liquidity to meet the WRS's benefit payments.

II. Investment Objectives

The investment strategy of the WRS is designed to ensure the prudent investment of funds in such a manner as to provide real growth of assets over time while protecting the value of the assets from undue volatility or risk of loss.

Risk Objectives

- To accept a level of market risk consistent with moderate interim volatility without sacrificing the potential for long-term real growth of assets.
- To use extensive diversification to minimize or eliminate completely exposure to company and industry-specific risks in the aggregate investment portfolio.

- To avoid extreme levels of volatility that could adversely affect WRS's portfolio.
- To limit the likelihood of investment return patterns that could negatively impact the funded status of the WRS.

Return objective

- Within the risk constraints outlined above, to achieve the highest real return possible.
- To achieve, over long time periods, investment returns consistent with the actuarial return on assets of 8.25%.

III. Investment Constraints

Legal and Regulatory

The WRS is a qualified defined benefit pension plan governed by the Massachusetts General Laws, Chapter 32. Investment procedures and restrictions stipulated under these regulations must be followed.

The Board intends to manage the assets of the WRS at all times in accordance with the provisions of the Public Employee Retirement Administration Commission (PERAC) and the Massachusetts General Laws, Chapter 32. The Board will retain legal counsel when appropriate to review contracts and provide advice with respect to applicable statutes and regulations.

Time Horizon

The WRS will be managed on a going-concern basis. The assets of the WRS will be invested with long-term time horizon (twenty years or more), consistent with the participant demographics and the purpose of the WRS.

Liquidity

The WRS exhibits a moderate need for interim liquidity. Cash outflows for benefit payments are expected to grow from approximately \$56.5 million to close to \$90.5 million over the next ten years, while cash flows are expected to rise from approximately \$41.2 million to \$65.2 million (covering normal costs and expenses) over the same period. This pattern results in a net negative cash flow of up to 4.7% of WRS assets, based on the WRS's year-end asset value and the actuarial assumed rate of return of 8.25% per year.

Tax Considerations

The WRS is a tax-exempt entity. Therefore, investments and strategies will be evaluated only on the basis of expected risks and potential returns.

IV. Risk and Return Considerations

The WRS's Board recognizes that a persistent positive relationship exists between risk and return, whether risk is described as possibility of loss or as interim volatility. The Board also recognizes that investors are rarely compensated for risks that can be eliminated through diversification. Within the risk and return parameters discussed above, the Board accepts the risks associated with investing in the capital markets (market risks), but will minimize wherever possible those risks for which the WRS is unlikely to be compensated (non-market or diversifiable risks).

V. Diversification

The WRS's Board recognizes that a primary element of risk control is diversification. Therefore, investments will be allocated across multiple classes of assets, chosen in part for their low correlation of returns. Within each asset type, investments will be distributed across many individual holdings, thus further reducing volatility. In addition, each investment manager's guidelines will specify the largest permissible investment in any one asset, and the largest permissible investment in any group of related assets.

The WRS's aggregate equity portfolio will be diversified by individual issue, capitalization, and industry (international equity portfolios will also be diversified by country). The WRS's aggregate fixed income portfolio will, at a minimum, be diversified by individual issue, by issuer, by maturity, and by industry. Residual cash will be swept by the custody bank into a short-term fixed income investment pool that is broadly diversified across individual issue and issuer. The WRS's aggregate real estate portfolio will be invested across a spectrum of geographic regions and property types.

The specific degrees of diversification within the above asset classes will be addressed in each manager's investment guidelines.

VI. Asset Allocation

The Board recognizes that the allocation of monies to various asset classes will be the major determinant of the WRS return and risk experience over time. Therefore, the WRS will allocate investments across those asset classes that, based on historical and expected returns and risks, provide the highest likelihood of meeting the WRS's investment objectives.

A. Permissible Asset Classes

Because investment in any particular asset class may or may not be consistent with the objectives of the WRS, the Board has specifically indicated those asset classes that may be utilized when investing the WRS's assets, and are summarized as follows:

Asset Type	Asset Class	Purpose
Equity	U.S. Common Stocks	Total Return Potential
Equity	Non-U.S. Common Stocks	Total Return Potential Diversification
Equity	Private Markets	Total Return Potential Diversification
Fixed Income	Investment Grade Bonds	Return Stability Income
Fixed Income	TIPS	Return Stability Income
Fixed Income	High Yield Bonds	Total Return Potential Diversification Income
Fixed Income	Bank Loans	Total Return Potential Diversification Income
Real Estate	Real Estate	Total Return Potential Diversification Income
Real Estate	Timber	Total Return Potential Diversification Income
Hedge Funds	Absolute Return Strategies	Return Stability Diversification
Cash	Cash Equivalents	Liquidity Return Stability

B. Expected Returns, Risks, and Correlations for Permissible Asset Classes

The risk and return behavior of the WRS will be driven primarily by the allocation of investments across asset classes. In determining the appropriate allocation, the expected return and risk behavior of each asset class and the likely interaction of various asset classes in a portfolio must be examined.

C. Long-Term Target Allocations

Based on the investment objectives and constraints of the WRS, and on the expected behavior of the permissible asset classes, the Board will specify a long-term target allocation for each class of permissible assets. These targets will be expressed as a percentage of the WRS's overall market value, surrounded by a band of permissible variation resulting from market forces.

The long-term target allocations are intended as strategic goals, not short-term imperatives. Thus, it is permissible for the overall System's asset allocation to deviate from the long-term target, as would likely occur during manager transitions, asset class restructurings, and other temporary changes in the WRS. Deviations from targets that occur due to capital market changes are discussed below:

ASSET ALLOCATION TARGETS

	Target (%)	Range (%)
Domestic Equity	31%	26-36%
Domestic Equity: Large Cap	21%	16%-26%
Domestic Equity: Mid Cap	3%	1%-5%
Domestic Equity: Small Cap	5%	3%-7%
Portable Alpha: Large Cap	2%	1%-3%
Foreign Equity	20%	15-25%
Developed: Large Cap	14%	11%-17%
Developed: Small Cap	3%	2%-4%
Emerging Markets	3%	2%-4%
Investment Grade Bonds	7%	5-9%
Treasury Inflation-Protected Securities (TIPS)	4%	3-5%
High yield Bonds / Bank Loans	7%	5-9%
Real Estate¹	10%	7-13%
Timber	3%	2-4%
Private Equity¹	6%	4-8%
Absolute Return¹	6%	4-8%
Total Global Tactical Asset Allocation Assets	4%	3-5%
Infrastructure Assets	2%	1-3
Cash²	0%	<5%

¹ The Retirement System is restricted by PERAC to target allocations of 10% for real estate, and 10% for private equity, and 7.5% for absolute return strategies. The System will make reasonable attempts to maintain those allocations, recognizing that market fluctuations and the funding requirements of alternative investments may result in short-term deviations from the targets.

² The cash target of zero defines the System's objective of keeping cash balances as low as possible, at least below 5% at all times. The Retirement Board is aware, however, that a certain cash balance is needed for the efficient operation of the System and its various portfolios.

Based upon the expected asset returns, risks, and correlations determined by Meketa Investment Group, this target allocation exhibits an expected annual return of 9.0% and an expected annual standard deviation of 12.0%.

D. Rebalancing

In general, cash flows to and from the WRS will be allocated in such a manner as to move each asset class toward its target allocation.

The Board recognizes that, periodically, market forces may move the WRS's allocations outside the target ranges. The Board also recognizes that failing to rebalance the allocations would unintentionally change the WRS's structure and risk posture. However, the Board understands that constant rebalancing would result in a significant increase in explicit and implicit trading costs to the WRS. Consequently, the Board has established a process to rebalance the allocations periodically.

On at least an annual basis, if any strategic allocation is outside the specified target range, assets will be shifted to return the strategy to the target range. The specific plan for rebalancing will identify those assets that can be shifted at the lowest possible risk and cost, if the rebalancing cannot be accomplished solely by allocating contributions and withdrawals.

E. Changes to Asset Allocation

Once established, permanent changes in the WRS's target asset allocation will take place only in response to significant changes in the objectives and constraints of the WRS, or in response to material changes in the fundamental nature or appropriateness of the asset classes themselves.

VII. Review of Investment Policy, Asset Allocation, and Performance

The Investment Policy Statement will be reviewed at least annually, and specifically upon each actuarial valuation, to ensure that the objectives and constraints remain relevant. However, the Board recognizes the need for a stable long-term policy for the WRS, and major changes to this policy statement will be made only when significant developments in the circumstances of the WRS occur. The Board will notify PERAC of any changes to this document within ten days of the effective date of those changes.

The asset allocation of the WRS will be reviewed on an on-going basis, and at least annually. When necessary, such reviews may result in a rebalancing of asset allocations. In general, the Board intends that the WRS will adhere to its long-term target allocations, and that major changes to these targets will be made rarely and only in response to significant developments in the circumstances of the WRS.

The Board will specifically evaluate the performance of the WRS relative to its objectives and to the returns available from the capital markets during the period under review. In general, the Board will utilize relative, rather than absolute, benchmarks in evaluating performance.

VIII. Trading and Proxy Voting by Investment Managers

In accordance with the fiduciary and other obligations imposed on investment managers by their agreements with the Board, all trades executed by managers must be for the exclusive benefit of the WRS's participants and beneficiaries. Managers are expected to seek best execution on all trades. This is addressed in the individual manager guidelines.

The Board recognizes that the right to vote proxies for securities held represents an asset of the WRS.

As such, the Board has specifically delegated the responsibility for voting all security proxies to the individual managers. The Board believes that the voting of proxies constitutes an investment decision by the managers, and that prudent voting of proxies is important to the overall performance of the WRS. Investment managers are expected to execute all proxy votes in a timely fashion and to provide a full written accounting of proxy votes on an annual basis.

IX. Management Structure

To diversify the WRS's assets so as to minimize the risk associated with dependence on the success of one enterprise, the Board Members have decided to employ a multi-manager team approach to investing System assets.

A consultant will be employed whose responsibilities will be to: 1) provide risk and return assumptions for various asset classes, 2) to diversify WRS so as to minimize risk, while enhancing the probability of achieving the WRS's return objectives, and 3) to evaluate the performance and compliance of investment managers.

Investment managers will be employed to utilize individual expertise within their assigned area of responsibility. Each manager will be governed by individual investment guidelines.

X. Implementation

All monies invested for the WRS after the adoption of this investment policy statement shall conform to this statement.

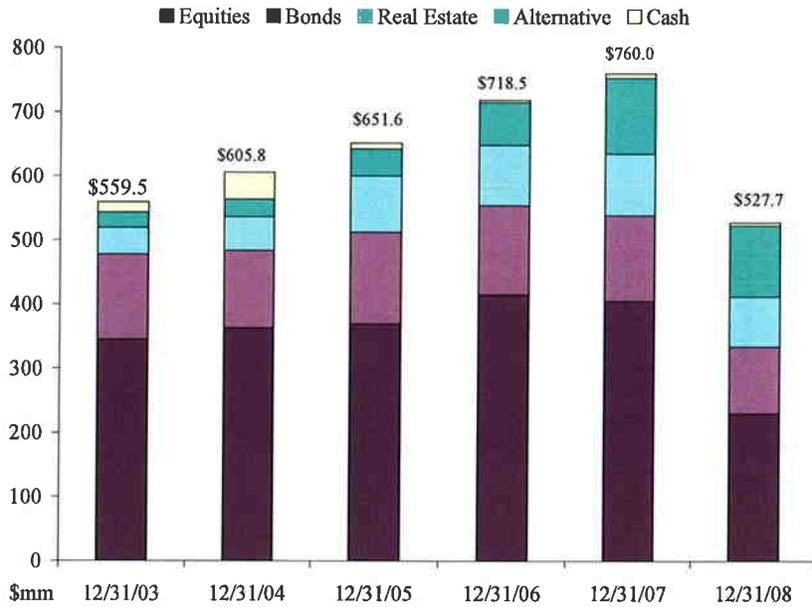
Investment Results*

	4Q08	1 YR	3 YR	5 YR	10 YR	Since Inception	Inception Date
Total System	-15.5	-27.1	-3.0	2.3	3.6	6.5	10/1/1995
CPI (inflation)	-3.9	0.1	2.2	2.7	2.5	2.4	
Total Equity	-10.8	-42.3	-14.9	-3.8	-0.1	0.7	
Russell 3000	-10.8	-38.2	-13.6	-4.6	-2.3	-0.9	
MSCI ACWI Free (ex. U.S.)	-10.7	-46.5	-13.1	-0.7	0.6	0.8	
Total Fixed Income	-6.0	-8.8	0.6	2.5	4.7	4.8	1/1/1998
Lehman Universal	2.7	2.4	4.6	4.3	5.6	5.7	
Total Open-End Real Estate	-12.6	-14.5	2.8	7.6	7.9	7.9	1/1/1999
NCREIF ODCE(was NCREIF Property)	-11.0	-10.0	6.7	10.7	10.1	10.1	
Total Absolute Return **	-8.6	-17.5	0.2	NA	NA	2.1	8/1/2007
HFRI Fund of Funds Composite	-9.3	-20.7	-1.2	2.1	5.4	0.8	

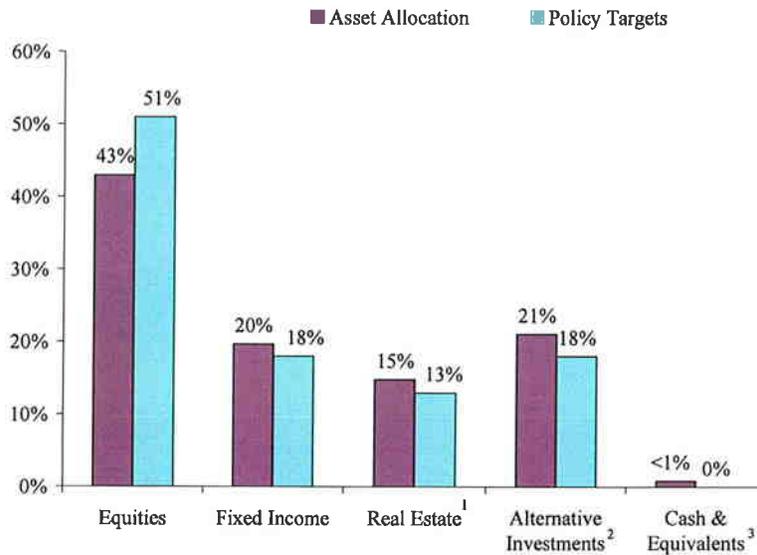
* The WRS's policy is a time weighted average of the representative asset class benchmarks. Manager returns include the effects on cash and equivalents; returns for all periods greater than one year are annualized. For pooled investments, returns are reported by the manager. Throughout this report, numbers may not sum due to rounding.

** Other alternative investments include private equity and infrastructure limited partnerships that are measured by dollar-weighted, rather than time-weighted returns. For the calendar year period covered by this report, the WRS's private equity investments declined by \$2.7 million, including \$8.8 million in capital called and \$7.3 million in distributions. This WRS's private infrastructure investments declined by \$0.4 million, including \$3.1 million in capital called during the period.

Asset Allocation



Aggregate Asset Allocation vs. Policy Targets

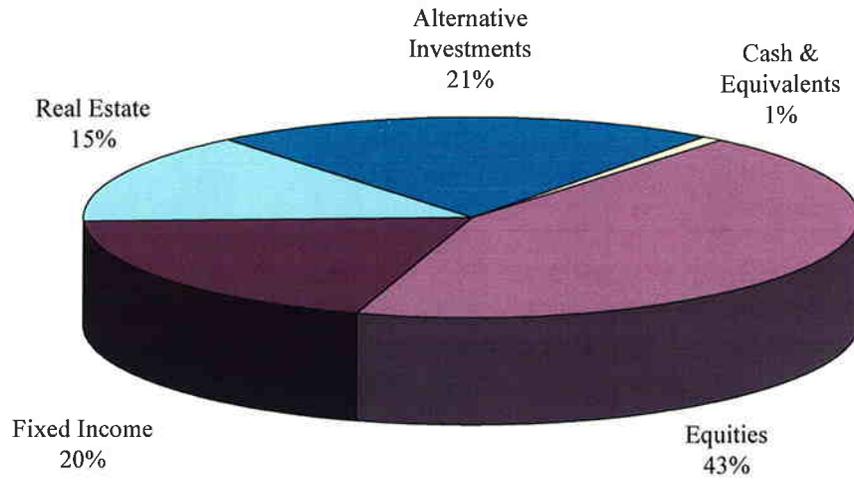


¹ The Real Estate policy target includes a strategic allocation to Timber of 3%.

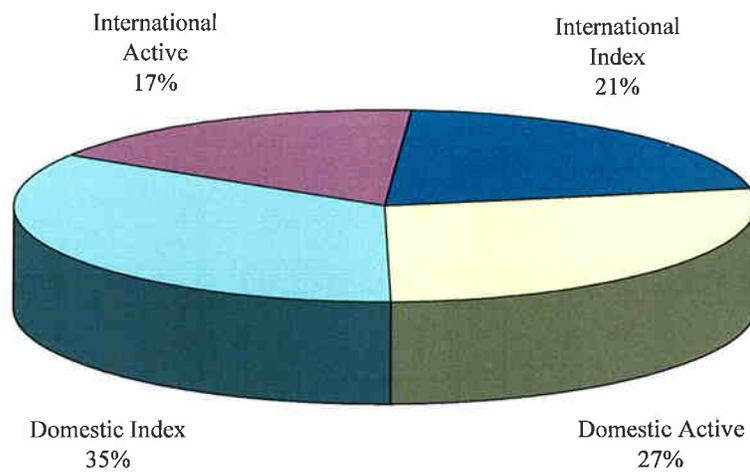
² The Alternative Investments allocation includes Private Equity, Absolute Return, Global Tactical Asset Allocation, and Infrastructure assets.

³ Includes cash and cash held by managers within separate accounts.

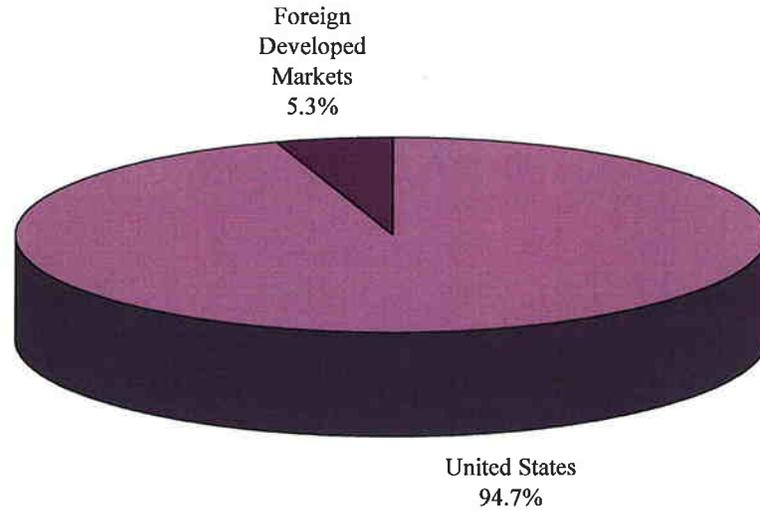
Aggregated Asset Allocation



Equity Allocation



Fixed Income Allocation



Ten Largest Stock Holdings by Fair Value

Company	Number of Shares	Fair Value (\$mm)	% of Domestic Stock	Industry
1. Exxon Mobil Corp	59,393	4.74	3.4%	Energy
2. Procter & Gamble Co	39,165	2.42	1.7%	Household & Personal Products
3. Microsoft Corp	103,468	2.01	1.4%	Software & Services
4. General Electric Co	118,966	1.93	1.4%	Capital Goods
5. AT&T Inc	66,959	1.91	1.4%	Telecommunication Services
6. Intl Business Machines Corp	22,478	1.89	1.4%	Technology Hardware & Equipment
7. Johnson & Johnson	31,093	1.86	1.3%	Pharmaceuticals Biotechnology & Life Sciences
8. Chevron Corp	23,240	1.72	1.2%	Energy
9. Coca-Cola Co	34,502	1.56	1.1%	Food Beverage & Tobacco
10. Wal-Mart Stores Inc	24,987	1.40	1.0%	Food & Staples Retailing

A complete portfolio is available upon request.

Ten Largest Fixed Income Holdings by Fair Value

Security	Coupon (%)	Maturity Date	Number of Shares	Market Value (\$mm)	% of Bonds
1. TIPS	3.9%	04/15/29	1,344,197	1.7	1.6
2. TIPS	2.4%	01/15/25	1,660,782	1.6	1.5
3. TIPS	0.9%	04/15/10	1,652,459	1.6	1.5
4. TIPS	3.0%	07/15/12	1,415,781	1.4	1.3
5. TIPS	3.6%	04/15/28	1,151,936	1.4	1.3
6. TIPS	2.0%	01/15/14	1,313,178	1.2	1.2
7. TIPS	2.4%	04/15/11	1,173,341	1.1	1.1
8. TIPS	1.9%	07/15/13	1,209,059	1.1	1.1
9. TIPS	2.5%	07/15/16	1,115,660	1.1	1.0
10. TIPS	2.0%	01/15/26	1,118,818	1.1	1.0

A complete portfolio is available upon request.

Schedule of Fees & Commissions

Investment Fees December 31, 2008	
Acadian Asset Management	\$ 162,469
Aetos Alternative	140,671
Ascent Venture Management Inc IV	142,106
Ascent Venture Management, Inc. II	3,411
Ascent Venture Management, Inc. III	(2,998)
Ascent Venture Management, Inc. V	12,448
Bailard	199,035
BOI	28,255
Boston Co EAFE	149,117
Boston Millennium Partners	59,845
BPIF Blackstone	180,591
Charlesbank Capital Partners V	40,016
Charlesbank Capital Partners VI	56,594
Columbia	154,309
Concord Partners III	964
Global Infrastructure	33,286
Hancock	67,774
Heitman Investment Management	(169,906)
Intech	249,029
Intercontinental Real Estate Corp.	37,500
Invesco	27,795
Lazard	171,873
Loomis Sayles	228,714
Mellon	94,715
New England Partners Capital I	37
New England Partners Capital II	3,554
Newstone	44,977
Northstar V	103,019
OPUS	46,462
OPUS TIPS	26,557
Penn	91,370
PRIT Hedge Fund	129,011
PRIT Core Real Estate	26,363
Riverside 2003	898
RMK Balanced B Fund	63,433
RMK Fund I	31,152
RMK Select Timberland Fund	24,724
RREEF	66,302
SSgA Daily EAFE	5,124
SSgA Flagship	4,865
SSgA Russell	3,799
Standard Life Investments Limited	22,588
VEF Advisors II	10,279
VEF Advisors IV	13,875
Total Investment Managers Fees	<u>2,786,002</u>
State Street Bank (Custodian Bank Fee)	241,420
Meketa Investment Group (Consultant Fee)	170,000
Security Lending Fees	420,300
Total Other Fees	<u>831,720</u>
Total Investment Fees	<u>\$ 3,617,722</u>

Commissions to Brokers

Broker	Total Commissions (\$)	Total Shares	Commission Per Share (\$)
AMERICAN TECHNOLOGY RESEARCH INC	291	7,280	0.04
AVONDALE PARTNERS LLC	575	16,460	0.03
BAIRD, ROBERT W. & COMPANY INCORPORATED	242	7,255	0.03
BANC OF AMERICA SECURITIES LLC	336	8,410	0.04
BARCLAY'S CAPITAL INC	181	5,735	0.03
BEAR STEARNS + CO INC	640	16,185	0.04
BEAR STEARNS SECURITIES CORP	3,206	88,939	0.04
BNY BROKERAGE INC	1,196	33,133	0.04
BNY CONVERGEX LJR	1,276	46,350	0.03
BREAN MURRAY	89	2,235	0.04
BUCKINGHAM RESEARCH GROUP INC	5	1,115	0.00
CANACCORDADAMS INC.	608	15,445	0.04
CANTOR FITZGERALD + CO	200	9,204	0.02
CAPITAL INSTITUTIONAL SVCS INC EQUITIES	2,102	113,800	0.02
CIBC WORLD MARKETS CORP	162	5,400	0.03
CITATION GROUP	160	5,349	0.03
CITIGROUPGLOBAL MARKETS INC	654	16,792	0.04
COWEN + CO., LLC	1,524	49,291	0.03
COKER, PALMER, PHILLIPS + MULLER INC	266	6,660	0.04
CREDIT SUISSE SECURITIES (USA) LLC	7,912	391,698	0.02
DAHLMAN ROSE + COMPANY LLC	139	3,975	0.04
DAVENPORT& CO. OF VIRGINIA, INC.	177	4,435	0.04
DAVIDSON D.A. + COMPANY INC	139	4,719	0.03
DEUTSCHE BANK SECURITIES INC	5,778	284,655	0.02
DOUGHERTY COMPANY	123	3,128	0.04
FERRIS BAKER WATTS INC	62	1,545	0.04
FIRST CLEARING, LLC	167	4,175	0.04
FOX PITT KELTON INC	185	4,630	0.04
FRANK RUSSELL SEC/BROADCORT CAP CLEARING	1	51	0.02
FRIEDMAN BILLINGS + RAMSEY	371	10,639	0.03
GARDNER RICH + CO	23	570	0.04
GOLDMAN SACHS + CO	6,665	1,045,432	0.01
GOLDMAN SACHS INTERNATIONAL	353	8,830	0.04
GOLDMAN SACHS EXECUTION + CLEARING	124	4,610	0.03
GUZMAN + CO	4,767	258,800	0.02
HARRIS NESBITT CORP. BONDS	72	2,387	0.03
HIBERNIA SOUTCOAST CAPITAL INC	285	7,130	0.04
HOWARD WEIL DIVISION LEGG MASON	521	13,015	0.04
IMPERIAL CAPITAL	34	860	0.04
INSTINET	5,354	296,886	0.02
INSTINET LLC	340	9,610	0.04
ISI GROUPINC	91	2,270	0.04
J P MORGAN SECURITIES INC	2,399	74,643	0.03
J P MORGAN CLEARING CORP.	616	15,405	0.04
JANNEY MONTGOMERY, SCOTT INC	222	5,555	0.04
JEFFERIES+ COMPANY INC	9,836	455,934	0.02
JMP SECURITIES	36	1,190	0.03
JNK SECURITIES INC	284	7,095	0.04
JOHNSON RICE + CO	387	9,665	0.04

Worcester Retirement System

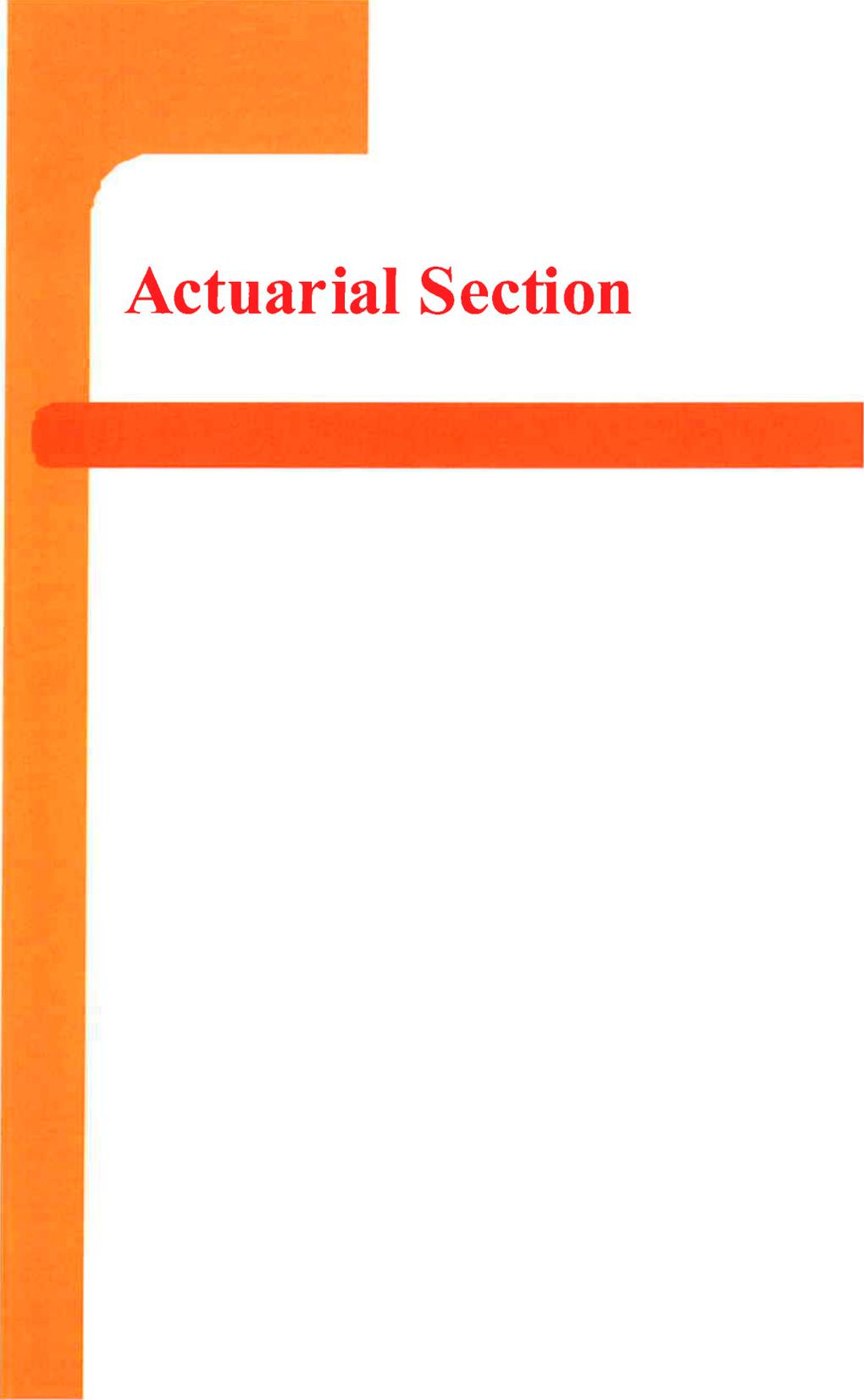
Broker	Total Commissions (\$)	Total Shares	Commission Per Share (\$)
JONESTRADING INSTITUTIONAL SERVICES LLC	9,276	261,290	0.04
KEEFE BRUYETTE + WOODS INC	425	19,794	0.02
KEYBANC CAPITAL MARKETS INC	933	27,371	0.03
KING, CL,& ASSOCIATES, INC	72	1,800	0.04
KNIGHT SECURITIES	2,525	99,070	0.03
LAZARD CAPITAL MARKETS LLC	409	9,787	0.04
LEHMAN BROTHERS INC	2,696	90,895	0.03
LYNCH JONES AND RYAN INC	438	28,900	0.02
MACQUARIESECURITIES (USA) INC	35	865	0.04
MERRILL LYNCH PROFESSIONAL CLEARING CORP	537	14,615	0.04
MERRILL LYNCH,PIERCE,FENNER + SMITH, INC	4,773	464,176	0.01
MERRIMAN CURHAN FORD + CO	104	2,605	0.04
MIDWEST RESEARCH SECURITIES	44	1,474	0.03
MORGAN KEEGAN & CO INC	809	21,433	0.04
MORGAN STANLEY CO INCORPORATED	194	1,035,523	0.00
MORGAN STANLEY CO INCORPORATED/RETAIL	159	5,252	0.03
NATIONAL FINANCIAL SERVICES CORP.	536	13,405	0.04
OPPENHEIMER & CO. INC.	320	10,130	0.03
PALI CAPITAL INC	640	32,015	0.02
PAYSON H.M. + CO	76	1,910	0.04
PERSHING LLC	8,830	241,168	0.04
PICKERING ENERGY PARTNERS INC	67	1,670	0.04
PIPELINE TRADING SYSTEMS LLC	57	2,843	0.02
PIPER JAFFRAY	348	11,600	0.03
PRITCHARDCAPITAL PARTNERS LLC	23	858	0.03
RAYMOND JAMES AND ASSOCIATES INC	2,741	72,160	0.04
RAYMOND JAMES/FI	7	243	0.03
RBC CAPITAL MARKETS	425	12,978	0.03
RBC DAIN RAUSCHER INC	46	1,140	0.04
ROSENBLATT SECURITIES INC	8,891	443,358	0.02
ROTH CAPITAL PARTNERS LLC	322	8,040	0.04
ROUSTON RESEARCH CORP	31	775	0.04
SANDERS MORRIS MUNDY	437	21,866	0.02
SANDLER ONEILL + PART LP	98	2,440	0.04
SANFORD CBERNSTEIN CO LLC	281	7,947	0.04
SCOTT & STRINGFELLOW, INC	240	7,725	0.03
SIMMONS + COMPANY INTERNATIONAL	552	13,815	0.04
SOLEIL SECURITIES	151	5,225	0.03
STEPHENS, INC.	135	3,385	0.04
STERNE, AGEE & LEACH, INC	133	3,325	0.04
STIFEL NICOLAUS + CO INC	1,509	42,883	0.04
SUNTRUST CAPITAL MARKETS INC.	689	17,222	0.04
TRISTONE CAPITAL MARKETS, INC.	47	1,170	0.04
UBS SECURITIES LLC	2,306	86,950	0.03
WACHOVIA SECURITIES, LLC	458	14,000	0.03
WACHOVIACAPITAL MARKETS, LLC	457	14,020	0.03
WDR WARBURG DILLION READ	1,161	45,993	0.03
WEDBUSH MORGAN SECURITIES INC	524	13,095	0.04
WEEDEN + CO	3,157	124,147	0.03
WILLIAM BLAIR & COMPANY L.L.C	43	1,554	0.03
TOTALS	120,347	6,754,480	0.02

INVESTMENT SUMMARY

	Assets (mm)	% of Aggregate	% of System
Total System	\$527.7	100%	100%
Total Domestic Equities	\$139.2	100%	27%
Information Technology	22.3	16%	4%
Financials	18.1	13%	3%
Health Care	19.5	14%	4%
Consumer Discretionary	13.9	10%	3%
Industrials	19.5	14%	4%
Energy	16.7	12%	3%
Consumer Staples	13.9	10%	3%
Materials	5.6	4%	1%
Utilities	5.6	4%	1%
Telecommunications Services	4.2	3%	1%
Total Fixed Income	\$103.8	100%	20%
Credit	43.9	42%	8%
U.S. Treasury	28.9	28%	6%
Mortgage Backed	21.4	21%	4%
U.S. Agency	4.3	4%	1%
Commercial Mortgage Backed	3.2	3%	1%
Asset Backed	2.1	2%	0%
Total International Equities	\$90.8	100%	16%
Europe - Developed	48.9	54%	9%
Pacific Rim/Australasia - Developed	28.6	32%	5%
Emerging Markets	12.8	14%	2%
Other (Non-EAFE)	0.5	1%	0%
Total Alternative Investments	\$189.4	100%	36%
Real Estate	78.2	41%	15%
Private Markets	50.2	27%	10%
Absolute Return	38.3	20%	7%
Global Tactical Assets	22.7	12%	4%
Cash & Equivalents	\$4.5	100%	1%

LIQUIDITY PROFILE

Benefits payments totaled approximately \$56.5 million during the year and along with other payments of \$3.9 million resulted in total cash outflows of \$60.4 million in 2008. These payments were partially offset by a contribution of approximately \$24.9 million from employers and other cash receipts of \$16.2 million for a total of \$41.1 million in 2008. This resulted in a negative cash flow of approximately \$19.3 million for the fiscal year. Note that these figures do not incorporate expected income and asset gains from the WRS's investments. The WRS's portfolio is structured with a long-term expected return of 8.25%.



Actuarial Section

THE SEGAL COMPANY

116 Huntington Avenue, 8th Floor Boston, MA 02116
T 617.424.7336 F 617.424.7390 www.segalco.com

Kathleen A. Riley, FSA, MAAA, EA
Senior Vice President & Actuary
kriley@Segalco.com

June 3, 2009

City of Worcester Retirement Board
City Hall, Room 103
455 Main Street
Worcester, MA 01608

Dear Board Members:

The Segal Company has performed a January 1, 2009 actuarial valuation of the City of Worcester Retirement System. This actuarial valuation has been completed in accordance with generally accepted actuarial principles and practices. To the best of our knowledge, the information supplied in this actuarial valuation is complete and accurate. Further, in our opinion, the assumptions as approved by the Retirement Board are reasonably related to the experience of and the expectations for the Plan.

As part of performing the valuation, The Segal Company was furnished member data by the City of Worcester Retirement System's administrative staff. Although examined for general reasonableness, the data was not audited by the actuary. In addition, the administrative staff furnished financial statements that were not audited by the actuary.

The funding objective of the plan is to provide for the current cost of benefits (*i.e.*, normal cost) and to reduce the unfunded liability to zero by June 30, 2030. The normal cost is expected to remain at a level percentage of payroll. The remaining liability of the 2002 ERI is amortized over a 9-year period (by June 30, 2018) with level payments. The 2003 ERI liability is amortized over a 3-year period (by June 30, 2012) with level payments. The Section 90 ACD liability is amortized over a 5-year period (by June 30, 2014) with level payments. The remaining unfunded liability is amortized over a 21-year period with payments increasing at the rate of 4.5% per year. The fiscal year 2010 appropriation has been budgeted at \$28,505,066, which is a 9.22% increase over the fiscal year 2010 appropriation shown in the prior valuation report. The contribution will increase by 4.0% - 4.5% per year, except for years when the ERI and Section 90 ACD liabilities are fully amortized. In the prior valuation, the remaining unfunded liability was being amortized over a period ending June 30, 2019 with payments increasing at the rate of 4.0% per year.

Actuarial valuations have been performed annually. This is consistent with the guidelines promulgated by PERAC and GASB. The last valuation was performed as of January 1, 2009.

The assumptions and methods used for funding purposes met the parameters set for the disclosures presented in the financial section by GASB Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*.

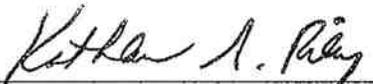
The Segal Company has prepared, and included as part of this report, all of the supporting schedules for the Actuarial Section and Statistical Section of the CAFR. In addition, we have prepared the Schedules of Funding Progress and the Schedule of Employer Contributions found in the Financial Section of the CAFR.

Please let us know if you have any questions on this material.

Sincerely,

THE SEGAL COMPANY

By:


Kathleen A. Riley, FSA, MAAA
Senior Vice President and Actuary

I. Summary of Actuarial Assumptions and Actuarial Cost Method

The actuarial assumptions, as set forth in the accompanying supporting schedules, were selected by the Worcester Retirement Board and actuary. Unless stated otherwise, the actuarial assumptions are based upon the actuarial valuation as of January 1, 2009, which was adopted by the WRS on July 16, 2009.

Mortality Rates

<i>Healthy</i>	1994 Group Annuity Mortality Table
<i>Disabled</i>	1994 Group Annuity Mortality Table set forward 10 years

Termination Rates before Retirement

Age	Rate (%)			
	Mortality		Group 1 and 2	
	Male	Female	Disability	Withdrawal
20	0.05	0.03	0.02	12.00
25	0.07	0.03	0.03	8.78
30	0.08	0.04	0.04	5.55
35	0.09	0.05	0.05	3.93
40	0.11	0.07	0.07	2.31
45	0.16	0.10	0.13	1.89
50	0.26	0.14	0.19	1.46
55	0.44	0.23	0.29	0.00
60	0.80	0.44	0.38	0.00

*Notes: 55% of the disability rates shown represent accidental disability.
20% of the accidental disabilities will die from the same cause as the disability.
55% of the death rates shown represent accidental death.*

Age	Rate (%)			
	Mortality		Group 4	
	Male	Female	Disability	Withdrawal
20	0.05	0.03	0.08	2.10
25	0.07	0.03	0.12	1.88
30	0.08	0.04	0.17	1.65
35	0.09	0.05	0.41	1.11
40	0.11	0.07	0.65	0.56
45	0.16	0.10	0.89	0.28
50	0.26	0.14	1.13	0.00
55	0.44	0.23	1.33	0.00
60	0.80	0.44	1.53	0.00

*Notes: 90% of the disability rates shown represent accidental disability.
60% of the accidental disabilities will die from the same cause as the disability.
90% of the death rates shown represent accidental death.*

Retirement Rates

Age	Rate (%)		Age	Group 4
	Groups 1 and 2			
55	12.55		50	32.00
56	3.21		51	7.21
57	3.10		52	5.90
58	3.34		53	8.00
59	3.48		54	7.71
60	7.84		55	15.51
61	6.92		56	9.11
62	15.11		57	9.09
63	10.71		58	11.90
64	10.37		59	11.42
65	35.68		60	23.95
66	22.14		61	13.60
67	21.59		62	19.50
68	21.64		63	12.53
69	25.36		64	18.73
70	100.00		65	100.00

Unknown Data for Participants

Same as those exhibited by participants with similar known characteristics.

Age of Spouse

Females 3 years younger than their spouses.

Percent-Married

80%

Net Investment Return

8.25%

Salary Increases

Age	Present salary as a percent of salary at 65 (%)	Annual increase rate (%)
20	11.13	5.00
25	14.20	5.00
30	18.13	5.00
35	23.14	5.00
40	29.53	5.00
45	37.69	5.00
50	48.10	5.00
55	61.39	5.00
60	78.35	5.00

Includes allowance for inflation of 4.00%.

Administrative Expenses

\$625,000 for calendar 2009.

Actuarial Value of Assets

The difference between the expected return and the actual investment return on a market value basis is recognized over a five-year period.

2008 Salary

2008 salary equal to salaries provided in the data, except for new hires where salaries were calculated from annualized contributions divided by the contribution rate(s) reported. The salaries of police officials were adjusted for retroactive pay amounts.

Total Service

Total creditable service based on adjusted date of hire.

Actuarial Cost Method

Entry Age Normal Actuarial Cost Method. Entry Age is the age of the participant at the Date of Hire. Normal Cost and Actuarial Accrued Liability are calculated on an individual basis and are allocated by salary.

Recent Changes

The investment return assumption was lowered from 8.50% to 8.25% as of January 1, 2006.

The salary increase assumption was lowered January 1, 2003 from 5.50% to 5.00%.

An asset smoothing method was first applied with the January 1, 2000 valuation and modified as of January 1, 2004. As of December 31, 2004, the actuarial value of assets was set equal to market value. As of January 1, 2009, the actuarial value of assets were changed from the market value of assets to a five-year smoothing method.

II. Schedule of Active Member Valuation Data

<u>Valuation date</u>	<u>Number</u>	<u>Projected annual payroll (\$)</u>	<u>Annual average pay (\$)</u>	<u>% Increase in average pay</u>
1/1/2004	3,409	138,796,895	40,715	4.89
1/1/2005	3,498	147,126,606	42,060	3.30
1/1/2006	3,430	145,830,593	42,516	1.08
1/1/2007	3,397	152,838,201	44,992	5.82
1/1/2008	3,299	156,585,326	47,464	5.49
1/1/2009	3,352	166,050,095	49,538	4.37

III. Schedule of Retirants and Beneficiaries Added to and Removed from Rolls

<u>Year ended</u>	<u>Added to Rolls</u>		<u>Removed from Rolls</u>		<u>Rolls - end of year</u>		<u>% Increase in annual allowances</u>	<u>Average annual allowances</u>
	<u>Number</u>	<u>Annual allowances¹</u>	<u>Number</u>	<u>Annual allowances</u>	<u>Number</u>	<u>Annual allowances¹</u>		
2003	115	3,212,097	120	1,357,111	2,996	49,606,369	5.16	16,558
2004	77	2,031,304	106	1,186,904	2,967	51,566,334	3.95	17,380
2005	76	1,890,735	124	1,544,809	2,919	52,623,545	2.05	18,028
2006	78	1,891,430	133	1,760,235	2,864	53,571,242	1.80	18,705
2007	105	2,719,667	120	1,728,323	2,849	55,329,380	3.28	19,421
2008	93	2,867,851	150	2,034,502	2,792	56,905,570	2.85	20,382

¹ Annual allowances are shown for retirees in pay status at the end of the year.

IV. Solvency Test

Valuation Date	Actuarial Accrued Liability				Portion of Actuarial Accrued Liability Covered by Assets		
	(1)	(2)	(3)	Actuarial value of assets	(1)	(2)	(3)
	Active member contributions	Retirees and beneficiaries	Active/Inactive members (Employer financed)				
1/1/2004	\$ 115,779,891	418,037,422	209,753,127	577,123,067	100	100	21
1/1/2005	122,748,771	425,655,839	223,543,701	606,099,616	100	100	26
1/1/2006	130,292,926	438,740,267	237,924,271	644,016,504	100	100	32
1/1/2007	138,456,863	444,678,593	254,472,777	716,796,770	100	100	53
1/1/2008	144,175,273	476,412,539	269,336,498	759,410,332	100	100	52
1/1/2009	152,780,052	488,818,808	287,970,604	631,893,995	100	98	0

V. Analysis of Financial Experience

	Year Ended December 31,				
	2008	2007	2006	2005	2004
1. Unfunded actuarial accrued liability as of January 1	\$ 130,513,978	\$ 120,811,463	\$ 162,940,960	\$ 165,848,695	\$ 166,447,373
2. Normal cost as of January 1	22,574,842	22,122,545	21,159,434	20,362,054	19,170,321
3. Employer and employee contributions during year	(39,375,618)	(36,995,766)	(35,961,906)	(35,484,556)	(31,843,173)
4. Interest					
(a) For whole year on (1)+(2)	12,629,827	11,792,055	15,188,283	15,827,913	15,777,504
(b) For half year on (3)	(1,467,582)	(1,378,882)	(1,340,348)	(1,362,059)	(1,222,286)
(c) Total interest	11,162,245	10,413,173	13,847,935	14,465,854	14,555,218
5. Expected unfunded actuarial liability	124,875,447	116,351,415	161,986,423	165,192,047	168,329,739
6. Actual unfunded actuarial accrued liability	297,675,469	130,513,978	120,811,463	162,940,960	165,848,695
7. (Gain) or loss for the year: (6)-(5)	\$ 172,800,022	\$ 14,162,563	\$ (41,174,960)	\$ (2,251,087)	\$ (2,481,044)
8. Investment (gain) or loss	\$ 275,514,085	\$ (3,341,587)	\$ (39,177,515)	\$ (4,698,351)	\$ 405,058
9. (Gains) or losses from sources other than investments	2,601,602	1,694,376	(1,997,445)	(14,912,389)	(5,367,076)
10. Plan changes	-	-	-	370,567	2,480,974
11. Assumption changes	(105,315,665)	15,809,774	-	16,989,086	-

VI. Summary of Plan Provisions

The following summarizes the major provisions of Chapter 32 of the Massachusetts General Laws.

Plan Year

January 1 – December 31

Retirement Benefit

Employees covered by the Contributory Retirement Law are classified into one of four groups depending on job classification. Group 1 comprises most positions in state and local government. It is the general category of public employees. Group 4 comprises mainly police and firefighters. Group 2 is for other specified hazardous occupations. (Officers and inspectors of the State Police are classified as Group 3.)

The annual amount of the retirement allowance is based on the member's final three-year average salary multiplied by the number of years and full months of creditable service at the time of retirement and multiplied by a percentage according to the following table based on the age of the member at retirement.

Age Last Birthday at Date of Retirement

Percent	Group 1	Group 2	Group 4
2.5	65 or over	60 or over	55 or over
2.4	64	59	54
2.3	63	58	53
2.2	62	57	52
2.1	61	56	51
2.0	60	55	50
1.9	59	--	49
1.8	58	--	48
1.7	57	--	47
1.6	56	--	46
1.5	55	--	45

A member's final three-year average salary is defined as the greater of the highest consecutive three-year average annual rate of regular compensation and the average annual rate of regular compensation received during the last three years of creditable service prior to retirement. The \$30,000 cap on salary used in a benefit determination for any employee hired after January 1, 1979 has been removed.

The maximum annual amount of the retirement allowance is 80 percent of the member's final three-year average salary. Any member who is a veteran also receives an additional yearly retirement allowance of \$15 per year of creditable service, not exceeding \$300. The veteran allowance is paid in addition to the 80 percent maximum.

Employee Contributions

Employees hired before January 1, 1975 contribute 5 percent of their salary; employees hired after December 31, 1983 and before January 1, 1975 contribute 7 percent; employees hired after January 1, 1984 and before June 30, 1996 contribute 8 percent; employees hired after July 1, 1996 contribute 9 percent.

In addition, employees hired after December 31, 1978 contribute an additional 2 percent of salary in excess of \$30,000.

Employees hired after 1983 who leave with less than five years of credited service receive no interest on their contributions, and employees who leave with five but less than ten years receive one-half the rate of regular interest otherwise payable.

Retirement Benefits (Superannuation)

Members of Group 1, 2 or 4 may retire upon the attainment of age 55. For retirement at ages below 55, twenty years of creditable service is required.

Members who terminate before age 55 with ten or more years of creditable service are eligible for a retirement allowance upon the attainment of age 55 (provided they have not withdrawn their accumulated deductions from the Annuity Savings Fund of the System).

Ordinary Disability Benefits

A member who is unable to perform his job due to a non-occupational disability will receive a retirement allowance if he has ten or more years of creditable service and has not reached age 55. The annual amount of such allowance shall be determined as if the member retired for superannuation at age 55, based on the amount of creditable service at the date of disability. For veterans, there is a minimum benefit of 50 percent of the member's most recent year's pay plus an annuity based on his own contributions.

Accidental Disability Benefit

For a job-connected disability the benefit is 72 percent of the member's most recent annual pay plus an annuity based on his own contributions, plus additional amounts for surviving children. Benefits are capped at 75 percent of annual rate of regular compensation for employees who become members after January 1, 1988.

Death Benefits

In general, the beneficiary of an employee who dies in active service will receive a refund of the employee's own contributions. Alternatively, if the employee were eligible to retire on the date of his death, a spouse's benefit will be paid equal to the amount the employee would have received under Option C. The surviving spouse of a member who dies with two or more years of credited service has the option of a refund of the employee's contributions or a monthly benefit regardless of eligibility to retire, if they were married for at least one year. There is also a minimum widow's pension of \$500 per month, and there are additional amounts for surviving children.

If an employee's death is job-connected, the spouse will receive 72 percent of the member's most recent annual pay in addition to a refund of the member's accumulated deductions, plus additional amounts for surviving children. However, in accordance with Section 100 of Chapter 32, the surviving spouse of a police officer, firefighter or corrections officer killed in the line of duty will be eligible to receive an annual benefit equal to the maximum salary held by the member at the time of death, and will be eligible for pay increases that would have been awarded to the officer if they were still living.

"Heart and Lung Law" and Cancer Presumption

Any case of hypertension or heart disease resulting in total or partial disability or death to a uniformed fireman, permanent member of a police department, or certain employees of a county correctional facility is presumed to have been suffered in the line of duty, unless the contrary is shown by competent evidence. Any case of disease of the lungs or respiratory tract resulting in total disability or death to a uniformed fireman is presumed to have been suffered in the line of duty, unless the contrary is shown by competent evidence. There is an additional presumption for uniformed firemen that certain types of cancer are job-related if onset occurs while actively employed or within five years of retirement.

Options

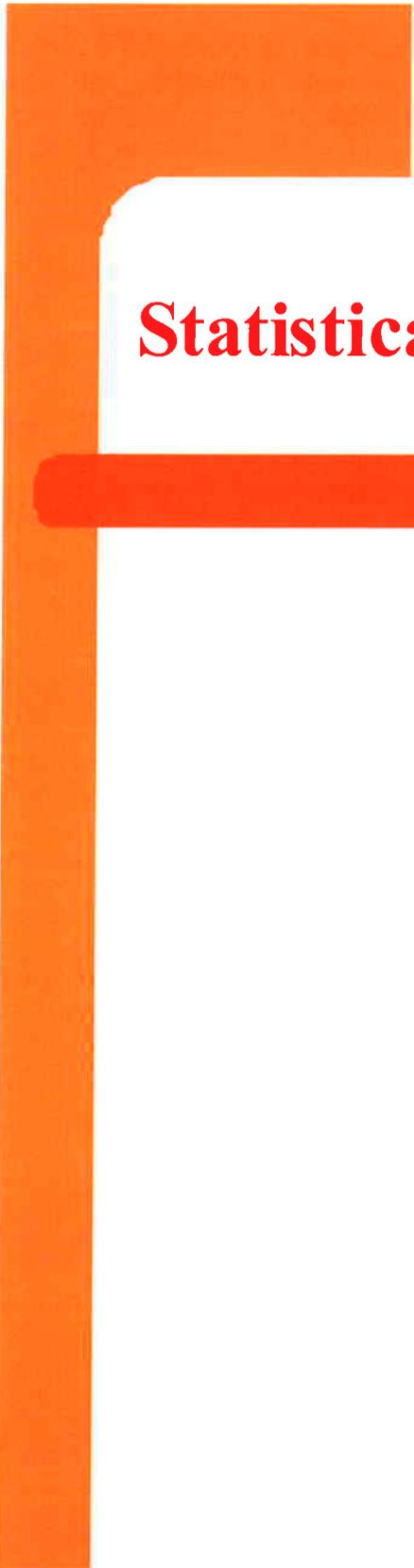
Members may elect to receive a full retirement allowance payable for life under Option A. Under Option B a member may elect to receive a lower monthly allowance in exchange for a guarantee that at his death any of his contributions not expended for annuity payments will be refunded to his beneficiary. Option C allows the member to take a lesser retirement allowance in exchange for providing his survivor with two-thirds of the lesser amount. Option C pensioners will have their benefits converted from a reduced to a full retirement if the beneficiary predeceases the retiree.

Post-Retirement Benefits

The Board has adopted the provisions of Section 51 Chapter 127 of the Acts of 1999, which provide that the Retirement Board may approve an annual COLA in excess of the Consumer Price Index but not to exceed a 3% COLA on the first \$12,000 of a retirement allowance. Cost-of-living increases granted prior to July 1, 1998 are reimbursed by the Commonwealth and are not reflected in this report.

Changes in Plan Provisions

There have been no changes in plan provisions since the last valuation.



Statistical Section



STATISTICAL SECTION

This part of the WRS' Comprehensive Annual Financial Report presents information as a context for understanding what the information in the financial statements, note disclosures, and required supplementary information says about the WRS' overall financial health.

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<p>These schedules contain trend information to help the reader understand how the WRS' financial performance and well-being have changed over time.</p>	
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<p>This schedule presents trend data about retired members by type of benefit.</p>	
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<p>This schedule presents trend data about average benefit payments.</p>	
Schedule of Participating Employers	70
<p>This schedule shows each participating employer's number of covered employees and percentage of total covered employees.</p>	

Schedule of Additions to Plan Net Assets by Source

<u>Fiscal Year</u>	<u>Plan Member Contributions</u>	<u>Employer Contributions</u>	<u>Employer Contributions as % of Covered Payroll</u>	<u>Investment Income(a)</u>	<u>Other(b)</u>	<u>Total</u>
1999	\$ 9,991,998	8,606,751	7.44	\$ 101,675,377	3,008,009	123,282,135
2000	10,641,408	8,343,309	6.70	3,874,421	4,517,210	27,376,348
2001	11,875,466	9,480,000	6.52	(29,629,122)	3,442,841	(4,830,815)
2002	12,393,094	12,956,778	8.71	(67,805,128)	3,615,546	(38,839,710)
2003	11,691,887	18,928,252	13.25	115,602,944	2,783,268	149,006,351
2004	12,187,208	20,150,377	14.52	66,454,940	3,530,693	102,323,218
2005	12,509,613	23,579,478	16.03	55,470,779	3,015,645	94,575,515
2006	13,448,309	23,354,603	16.01	91,535,233	2,982,027	131,320,172
2007	13,922,938	24,166,318	15.81	61,690,401	2,800,696	102,580,353
2008	14,695,126	24,947,158	15.93	(213,653,903)	1,553,980	(172,457,639)

(a) Net of Investment expenses

(b) Includes state pension reimbursements and transfer of employees' contributions from other public pension plans as defined by Massachusetts General Law, Chapter 32.

Schedule of Deductions from Plan Net Assets by Type

<u>Fiscal Year</u>	<u>Benefits</u>	<u>Administrative Expenses</u>	<u>Withdrawals(a)</u>	<u>Total</u>
1999	\$ 36,868,926	\$ 1,131,072	\$ 2,716,627	\$ 40,716,625
2000	39,696,596	1,428,037	2,659,748	43,784,381
2001	41,095,678	811,315	3,129,455	45,036,448
2002	43,540,572	561,697	3,802,339	47,904,608
2003	47,848,502	440,294	3,866,838	52,155,634
2004	50,517,094	518,078	3,704,908	54,740,080
2005	52,105,583	556,781	3,996,263	56,658,627
2006	53,350,080	621,648	4,568,178	58,539,906
2007	55,033,466	555,774	4,377,551	59,966,791
2008	56,516,348	554,276	3,303,810	60,374,434

(a) Includes amounts for employee withdrawals and employee transfers to other governmental units.

Schedule of Total Change in Net Assets

<u>Fiscal Year</u>	<u>Total Change in Net Assets</u>
1999	\$ 82,565,510
2000	(16,408,033)
2001	(49,867,263)
2002	(86,744,318)
2003	96,862,717
2004	47,583,138
2005	37,916,888
2006	72,780,266
2007	42,613,562
2008	(232,832,073)

Schedule of Benefit Expenses by Type

<u>Year ended December 31</u>	<u>Regular</u>	<u>Disability</u>	<u>Beneficiary</u>	<u>COLA</u>	<u>Annuities</u>	<u>Total</u>
2000	\$ 16,423,542	7,785,392	4,621,538	6,217,596	4,648,528	39,696,596
2001	17,082,481	7,872,843	4,737,758	6,771,240	4,631,355	41,095,677
2002	18,332,032	8,532,815	4,771,934	7,056,425	4,847,366	43,540,572
2003	21,186,242	8,706,365	5,105,775	7,422,192	5,427,928	47,848,502
2004	22,505,296	9,192,940	5,145,320	7,795,981	5,877,557	50,517,094
2005	22,855,516	9,796,237	4,830,540	8,581,377	6,041,913	52,105,583
2006	23,016,975	10,282,032	4,999,986	8,846,248	6,204,839	53,350,080
2007	23,437,804	10,890,179	5,081,340	9,147,566	6,476,577	55,033,466
2008	23,937,559	11,123,001	5,285,744	9,355,548	6,814,496	56,516,348

Schedule of Retired Members by Type of Benefit

	12/31/2008	12/31/2007	12/31/2006	12/31/2005	12/31/2004	12/31/2003	12/31/2002	12/31/2001	12/31/2000
Superannuation									
Group 1	1,493	1,545	1,560	1,577	1,622	1,653	1,653	1,589	1,621
Group 2&4	276	270	263	269	270	262	254	220	224
Total	1,769	1,815	1,823	1,846	1,892	1,915	1,907	1,809	1,845
Ordinary Disability									
Group 1	39	43	42	44	41	42	42	41	46
Group 2&4	6	7	7	6	5	7	6	6	6
Total	45	50	49	50	46	49	48	47	52
Accidental Disability									
Group 1	130	128	125	139	139	140	147	147	152
Group 2&4	317	319	318	323	321	315	319	316	313
Total	447	447	443	462	460	455	466	463	465
Beneficiaries									
Group 1	349	361	373	389	395	408	417	427	438
Group 2&4	182	176	176	172	174	169	163	159	150
Total	531	537	549	561	569	577	580	586	588
Total Retired Members									
Group 1	2,011	2,077	2,100	2,149	2,197	2,243	2,259	2,204	2,257
Group 2&4	781	772	764	770	770	753	742	701	693
Total	2,792	2,849	2,864	2,919	2,967	2,996	3,001	2,905	2,950

Source: Actuarial valuation as of January 1, 2009

Schedule of Average Benefit Payments

<u>Year ended December 31</u>	<u>Number</u>	<u>Annual benefits (\$)</u>	<u>Monthly average (\$)</u>	<u>Annual average (\$)</u>	<u>% Increase</u>
2000	2,950	39,696,596	1,121	13,456	8.47
2001	2,905	41,095,677	1,179	14,147	5.14
2002	3,001	43,540,572	1,209	14,509	2.56
2003	2,996	47,848,502	1,331	15,971	10.08
2004	2,967	50,517,094	1,419	17,026	6.61
2005	2,919	52,105,583	1,488	17,850	4.84
2006	2,864	53,350,080	1,552	18,628	4.36
2007	2,849	55,033,466	1,610	19,317	3.70
2008	2,792	56,516,348	1,687	20,242	4.79

Note: Data is being accumulated beginning in fiscal year 2000. The System believes that this provides an adequate amount of data for trend analysis related to average benefit payments.

Schedule of Participating Employers

<u>Fiscal Year</u>	<u>Employer Name</u>	<u>Number of Covered Employees</u>	<u>Percentage of Total Covered Employees</u>
1999	City of Worcester	3,342	93.6%
1999	Worcester Housing Authority	227	6.4%
2008	City of Worcester	3,178	94.8%
2008	Worcester Housing Authority	174	5.2%

Source: The WRS administrative staff