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

Comprehensive Annual Financial Report

Fiscal Year Ended December 31, 2006

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For the Fiscal Year Ended December 31, 2006

Prepared by the Staff of the
Worcester Retirement System

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Introductory Section

Worcester Retirement System

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

Chairman's Letter

May 15, 2007

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, 2006. 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 three 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 but to also diversify those assets to mitigate risks during the inevitable times when certain asset classes experience sub-par returns. No changes were made to the system's asset allocation during the year but there have been some recent changes. Hedge funds of funds have been increased from 5-percent to 6-percent of the portfolio and managers were hired for global REITs (1.5-percent) and global tactical asset allocation mandates (4-percent). Allocations to domestic equities and fixed income securities were reduced to accommodate these changes. WRS now employs 35 investment managers in 41 different strategies.

Each of the last four years has produced investment returns in excess of the WRS actuarial benchmark, which was reduced from 8.5-percent to 8.25-percent in the January 1, 2006 actuarial valuation. In 2006, WRS achieved time-weighted investment returns of 15.08-percent gross and 14.42-percent net of fees.

Last year the WRS unfunded actuarial accrued liability was reduced from $162.9 million to $120.8 million. Because of an experience gain of $41.2 million, due mostly to investment gains, the funding schedule was reduced by 5-years, maturing in 2018 instead of 2023. Future annual funding increases for the 2003 Early Retirement Incentive were reduced from 1.5-percent to level dollar and for the other remaining liabilities from 4.5-perecent to 3.5-percent. Additionally, employer funding was reduced by about $40 thousand from the amount originally planned for in fiscal 2008 and is scheduled to be further reduced from the original plan by about $200 thousand in fiscal 2009 and about $400 thousand in fiscal 2010.

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,

James DelSignore

James DelSignore, CPA
Chairman

Worcester Retirement System

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

May 31, 2007

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, 2006. 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, 2005. This was the third 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 Commonwealth of Massachusetts Commissioner of Insurance, Charles J. Harrington, issued a certificate declaring the establishment of a contributory retirement system on June 12, 1944 after the City Council approved acceptance of Chapter 32 section 31 (I) of the General Laws and the Mayor approved acceptance of sections 26 to 31 (H) inclusive with amendments.

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. The investment market results for 2006 demonstrate the importance of a diversified asset allocation.

WRS's 2006 time-weighted investment return was 14.42%, which exceeds both the actuarial expected rate of return and the Investment policy benchmark. This represents the fourth consecutive calendar year of positive results for the system. Please refer to the Investment Section of this CAFR for more information on investment results.

Major Initiatives

Benefits

In December 2005 the Board accepted section one of Chapter 157 of the Acts of 2005. With acceptance by the Worcester City Council in January 2006 the section became effective. The Act provides an additional benefit to disability retirees that were veterans at the time of retirement. The maximum annual increase allowed by this vote was $300 per retiree.

A cost of living adjustment (COLA) was provided for retirees and survivors effective July 1, 2006. 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.

The Board adopted Chapter 55 of the Acts of 2006 in July 2006. This section increases the child allowance paid to a widow (or widower) receiving an accidental death benefit making it equal to that paid to a retiree receiving an accidental disability benefit. Upon the required acceptance by the Worcester City Council on March 13, 2007 the allowance was increased for all eligible widows (or widowers) prospectively.

Administration

The WRS strives to provide quality service and information to active and retired members and their beneficiaries. To assist in this effort, we have maintained 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. 44 *Economic Condition Reporting: The Statistical Section (an amendment of NCGA Statement 1)*

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, 2006 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, 2006.

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, 2007 the funded ratio of the WRS was calculated at 85.58%, more than a 5.7% increase 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,

Elizabeth A. Early
Executive Secretary

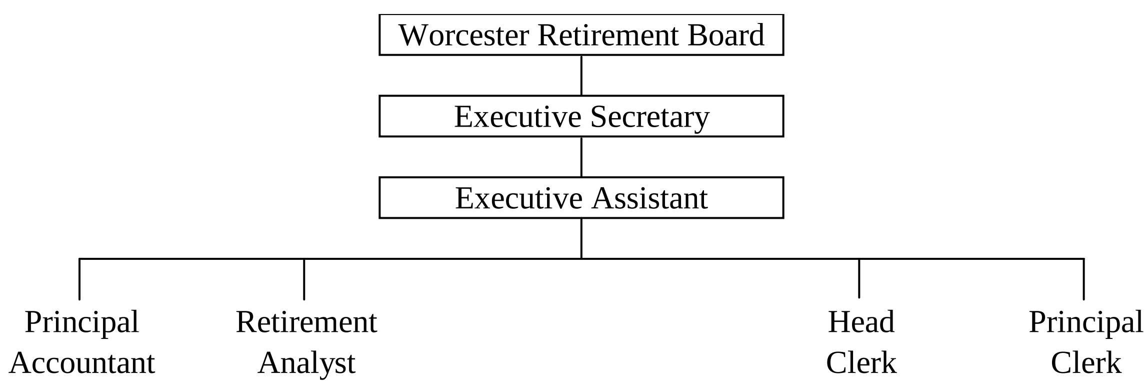
Retirement Board Members

		Terms
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	11/01/2004 - 10/31/2007
Raymond F. McGrath	Elected Member	01/01/2006 - 12/31/2008
Thomas Wade	Appointed Member	01/9/2006 - 01/09/2009

Administrative Staff

Elizabeth A. Early	Executive Secretary
Judith McMillen	Executive Assistant
Donald McLaren	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
The Boston Company Asset Management, LLC
Boston, MA
Columbia Management Advisors, LLC
Hartford, CT
Hutchens Investment Management, Inc.
Concord, NH
Enhanced Investment Technologies, LLC
Palm Beach Gardens, FL
Loomis Sayles & Company, L.P.
Boston, MA
PENN Capital Management Co, Inc
Cherry Hill, NJ
State Street Global Advisors
Boston, MA

DOMESTIC FIXED MANAGERS
OPUS Investment Management, Inc.
Worcester, MA
Loomis Sayles & Company, L.P.
Boston, MA
The Northern Trust Company
Chicago, IL

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
Aetos Alternatives Management, LLC
New York, NY
Ascent Venture Management
Boston, MA
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
INVESCO Private Capital, Inc.
New York, NY
New England Partners Capital L.P.
Boston, MA
Northstar Capital, LLC
Minneapolis, MN
Mass PRIM
Boston, MA
Standard Life Investments Limited
Edinburgh, UK
The Riverside Company
New York, NY

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
L&B Realty Advisors, Inc.
Dallas, TX
RMK Timberland a div. of Regions Bank
Winston-Salem, NC
Mass PRIM
Boston, MA
Apollo Real Estate Advisors
Atlanta, GA

LEGAL ADVISORS
Kirkpatrick & Lockhart Nicholson Graham, LLP
Boston, MA
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
UBS Securities, LLC
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, 2005

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

SULLIVAN ROGERS & COMPANY
Certified Public Accountants

SULLIVAN, ROGERS & COMPANY, LLC
Corporate Place I, Suite 204 • 99 South Bedford Street
Burlington, Massachusetts 01803
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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, 2006, 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, 2006, and the respective changes 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 May 8, 2007, 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 pages 31 through 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.

May 8, 2007

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, 2006. 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, 2006, the funded ratio was 85.58% based on the market value of assets at that date.

Net assets increased during the year by $72.8 million, or 11.3%, because of strong 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 gains were $91.5 million. The dollar-weighted investment rate of return was 14.8% compared with a positive return of 9.7% 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: Assets – Liabilities = 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, 2006. 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, 2006. 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, 2006 were $738.9 million and were primarily comprised of cash and cash equivalents, receivables, and investments. Total assets increased $80.0 million, or 12.1%, from the prior year primarily due to investment gains.

Total liabilities as of December 31, 2006 were $22.1 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 $7.2 million, or 48.6%, over the period.

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 $716.8 million at the close of the fiscal year and are summarized as follows:

Plan Net Assets
(In thousands of dollars)

Assets	2006	2005
Cash	$ 3,600	$ 8,758
Investments	714,874	634,689
Securities lending short-term collateral investment pool	18,179	8,555
Receivables:		
Interest due and accrued	1,210	3,776
Due from Commonwealth of Massachusetts and other systems	352	350
Receivable for securities sold	614	2,088
Other	54	648
Total assets	738,883	658,864
Liabilities		
Accounts payable and accrued expenses	513	673
Due to Commonwealth of Massachusetts and other systems	2,778	2,209
Payable for securities purchased	616	3,411
Collateral held on securities lending transactions	18,179	8,555
Total liabilities	22,086	14,848
Net assets held in trust for pension benefits	$ 716,797	$ 644,016

Management's Discussion & Analysis

Changes in Net Assets

The WRS's total net assets increased by $72.8 million during the current fiscal year and are summarized as follows:

Changes in Net Assets

(in thousands of dollars)

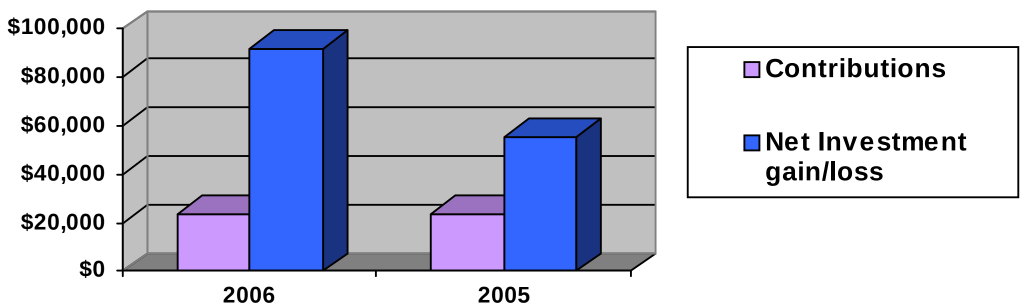
	2006	2005
Additions		
Contributions:		
Employers	$ 23,355	$ 23,580
Plan members	13,448	12,510
Reimbursements from Commonwealth of Massachusetts	2,630	2,665
Reimbursements from other Systems	352	350
Net investment income:		
Interest and dividends	7,331	13,214
Securities lending income	746	510
Net realized and unrealized gains (losses)	88,324	45,725
Less: management fees	(4,183)	(3,506)
Less: borrower rebates & fees	(682)	(472)
Total additions	131,321	94,576
Deductions		
Benefits payments to plan members and beneficiaries	53,350	52,106
Reimbursements to other systems	2,778	2,212
Refunds and transfers of plan member accounts to other systems	1,790	1,785
Administrative expenses	622	557
Total deductions	58,540	56,660
Change in plan net assets	72,781	37,916
Net assets held in trust for pension benefits:		
Beginning of year	644,016	606,100
End of year	$ 716,797	$ 644,016

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 gain for calendar year 2006 resulted in total additions to net assets of $131.3 million. Employers'contributions decreased by $225 thousand in 2006. The WRS had a net investment gain of $91.5 million in 2006 versus a gain of $55.5 million in 2005.

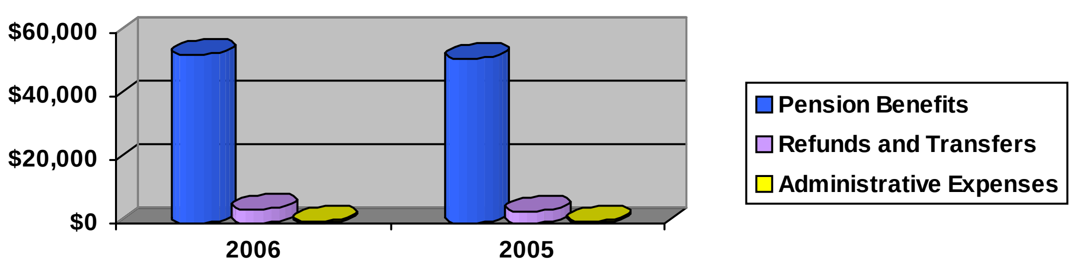
Additions to Plan Net Assets
(in thousands of dollars)



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 2006 were $58.5 million, which represents an increase of 3.2% over deductions of $56.7 million in 2005. The payment of pension benefits increased by $1.2 million, or 2.3%, 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 (2,919 in 2005 versus 2,864 in 2006).

Deductions from Plan Net Assets
(in thousands of dollars)



Management's Discussion & Analysis

Overall Financial Position of WRS

Due to a continuous improvement in the financial markets, the WRS has experienced an increase in its investment portfolio for the fiscal year ending December 31, 2006. 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, 2006

Assets	
Cash & Cash Equivalents	$ 3,600,218
Investments:	
Equities	257,591,082
Fixed Income	100,989,307
Pooled Equities	157,157,017
Pooled Fixed Income	38,574,143
Real Estate	94,113,551
Alternative Investments	66,449,280
Total investments	714,874,380
Securities lending short-term collateral investment pool	18,178,524
Receivables:	
Accrued interest and dividends	1,210,491
Due from Commonwealth of Massachusetts and other systems	351,972
Receivable for securities sold	614,035
Other receivables	53,068
Total receivables	2,229,566
Total plan assets	738,882,688
Liabilities	
Accounts payable and accrued expenses	513,737
Due to Commonwealth of Massachusetts and other systems	2,777,750
Payable for securities purchased	615,907
Collateral held on securities lending transactions	18,178,524
Total plan liabilities	22,085,918
Net assets held in trust for pension benefits (see schedule of funding progress on page 31)	$ 716,796,770

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, 2006

Additions:		
Contributions:		
Employers	$	23,354,603
Plan members		13,448,309
Reimbursements from Commonwealth of Massachusetts		2,630,055
Reimbursements from other systems		351,972
Total contributions		39,784,939
Investment income (loss):		
Interest and dividends		7,331,227
Securities lending income		745,634
Net realized and unrealized gains		88,323,526
Less: management fees		(4,183,485)
Less: borrower rebates and fees under securities lending program		(681,669)
Net investment income		91,535,233
Total additions		131,320,172
Deductions:		
Benefit payments to plan members and beneficiaries		53,350,080
Reimbursements to other systems		2,777,733
Refunds and transfers of plan member accounts to other systems		1,790,445
Administrative expenses		621,648
Total deductions		58,539,906
Change in plan net assets		72,780,266
Net assets held in trust for pension benefits:		
Beginning of year		644,016,504
End of year	$	716,796,770

See accompanying notes to financial statements.

Notes to Financial Statements
December 31, 2006

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) Cash and Investments

Cash is 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

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, because of the inherent uncertainty of valuation, those 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.

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, 2006:

Active employees	3,397
Pensioners and beneficiaries	2,864
Inactive employees	1,072
Total members	7,333
Number of participating employers	2

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 $100,000 of deposits held at each financial institution. As of December 31, 2006, $613,065 of the WRS's bank balance of $690,519 was uninsured and uncollateralized.

Investments Summary

The WRS's investments at December 31, 2006 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
Debt Securities:					
U.S. Treasuries………………	$ 37,186,083	$ -	$ 10,879,868	$ 15,292,935	$ 11,013,280
U.S. Agencies………………	24,790,854	2,368,483	1,418,759	3,373,702	17,629,910
Corporate bonds……………	34,614,283	206,907	11,377,079	7,153,834	15,876,463
Money market mutual funds..	21,150,902	21,150,902	-	-	-
Debt security mutual funds….	42,972,231	42,972,231	-	-	-
Total debt securities……….	160,714,353	$ 66,698,523	$ 23,675,706	$ 25,820,471	$ 44,519,653
Other Investments:					
Equity securities……………	101,653,838				
Equity mutual funds…………	313,094,261				
Real estate investments……...	94,113,551				
Alternative investments……..	66,449,280				
Total other investments…….	575,310,930				
Total investments……………	$ 736,025,283				

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, 2006, 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, 2006, the credit quality ratings of the WRS's debt securities are as follows:

	Investment Type			
Quality Ratings *	Corporate Bonds	Money Market Mutual Funds	Debt Security Mutual Funds	Fair Value
AAA	$ 3,138,495	$ -	$ 2,403,752	$ 5,542,247
AA	304,701	-	-	304,701
AA-	1,364,919	-	-	1,364,919
A	601,852	-	-	601,852
A-	414,309	-	-	414,309
BBB+	2,157,100	-	-	2,157,100
BBB	1,994,724	-	-	1,994,724
BBB-	1,813,619	-	-	1,813,619
BB+	2,309,164	-	-	2,309,164
BB	1,723,025	-	-	1,723,025
BB-	1,498,573	-	-	1,498,573
B+	3,546,949	-	-	3,546,949
B	4,094,526	-	-	4,094,526
B-	1,401,195	-	-	1,401,195
CCC+	1,727,025	-	-	1,727,025
CCC	643,275	-	-	643,275
CCC-	417,862	-	-	417,862
Unrated	5,462,970	21,150,902	40,568,479	67,182,351
Total	$ 34,614,283	$ 21,150,902	$ 42,972,231	$ 98,737,416

* 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, 2006, the WRS's exposure to foreign currency risk is as follows:

Deposit/Investment Type	U.S. Dollar Balances	Currency
U.S. Agencies	$ 1,953,653	Mexican peso
U.S. Agencies	699,900	Singapore dollar
Corporate bonds	636,373	Singapore dollar
Corporate bonds	540,788	Thailand baht
Corporate bonds	429,565	Brazilian real
Corporate bonds	419,266	Indonesian rupiah
Corporate bonds	386,295	British pound sterling
U.S. Agencies	351,048	Argentine peso
U.S. Agencies	268,349	Columbian peso
Corporate bonds	3,517	New Zealand Dollar
Total	$ 5,688,754	

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, 2006, the WRS was not exposed to concentration of credit risk.

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 transaction 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, 2006. 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, 2006, 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, 2006 and 2005 was $18,178,524 and $8,554,774, and $18,090,403 and $18,859,680, respectively. Borrower rebates and fees paid to the broker were $681,669 for the year ended December 31, 2006.

5. Funding Policy

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. Administrative costs are financed from investment income.

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.

6. Legally Required Reserve Accounts

The balances in the WRS' legally required reserves as of December 31, 2006 are as follows:

Description	Amount	Purpose
Annuity Savings Fund	$ 138,456,863	Active members' contribution balance
Annuity Reserve Fund	48,226,093	Retired members' contribution account
Military Service Fund	17,141	Members' contribution account while on military leave
Pension Reserve Fund	451,961,659	Amounts appropriated to fund future retirement
Pension Fund	78,135,014	Remaining net assets
Total	$ 716,796,770	

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

Required Supplementary Information

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 funding status of the WRS.

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
1/1/2002	$ 620,814,307	671,876,943	51,062,636	92.40	$ 148,764,543	34.32
1/1/2003	554,190,090	715,855,564	161,665,474	77.42	142,802,508	113.21
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

Schedule of Employer Contributions

Year Ended December 31	Annual Required Contributions	Percentage of Annual Required Contributed (%)
2001	$ 9,480,000	100
2002	12,956,778	100
2003	18,928,252	100
2004	20,150,377	100
2005	23,579,478	106
2006	23,354,603	100

Notes to Required Supplementary Information
December 31, 2006

Valuation Date	January 1, 2007
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 3.50% increasing payments on the remaining unfunded liability
Remaining amortized period	The remaining effective amortization period is 11 years and the period is closed
Asset valuation method	Market values
	Similar formula used for negative adjustment toward market value if actuarial value exceeds market value.

Actuarial assumptions:

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

Supplementary Information

Schedule of Administrative Expenses

The composition of administrative expenses for the year ended December 31, 2006 is as follows:

Personal Services:		
Staff Salaries	$	327,715
Board Member Compensation		15,000
Insurance		30,990
Total Personal Services		373,705
Professional Services:		
Legal Expenses		105,956
Actuarial Fees		24,500
Audit Fees		20,000
Computer Consultant Fees		450
Medical Fees		1,456
Total Professional Services		152,362
Miscellaneous:		
Travel		5,410
Printing		1,351
Other		88,820
Total Miscellaneous		95,581
Total Administrative Expenses	$	621,648

Schedule of Investment and Consultants' Expenses

Investment Expenses		
Management Fees:		
Domestic & Equity Managers	$	955,905
Venture Capital Funds		863,138
Domestic Fixed Income Managers		356,576
International Investments Managers		651,908
Real Estate Investments Managers		887,107
Consultant Fees		132,000
Custodial Fees		336,851
Total Management Fees		4,183,485
Securities Lending Fees:		
Borrowers Rebates		654,279
Fees		27,390
Total Securities Lending Fees		681,669
Total Investment Expenses	$	4,865,154
Consultant Expenses:		
Independent Audit Fees	$	20,000
Actuarial Fees		24,500
Legal Fees		105,956
Total Consultant Expenses	$	150,456

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 $53.4 million to close to $79.9 million over the next ten years, while cash flows are expected to rise from approximately $39.8 million to $49.5 million (covering normal costs and expenses) over the same period. This pattern results in a net negative cash flow of up to 4% 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	**35**	**30-40**
Domestic Equity: Large Cap	24	19-29
Domestic Equity: Mid Cap	5	3-7
Domestic Equity: Small Cap	6	4-8
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	**8**	**5-11**
Treasury Inflation-Protected Securities (TIPS)	**5**	**5-11**
High yield Bonds / Bank Loans	**7**	**4-10**
Real Estate[1]	**10**	**8-12**
Timber	**3**	**2-4**
Private Equity	**6**	**4-8**
Absolute Return	**6**	**4-8**
Cash[2]	**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 8.6% and an expected annual standard deviation of 13%.

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.

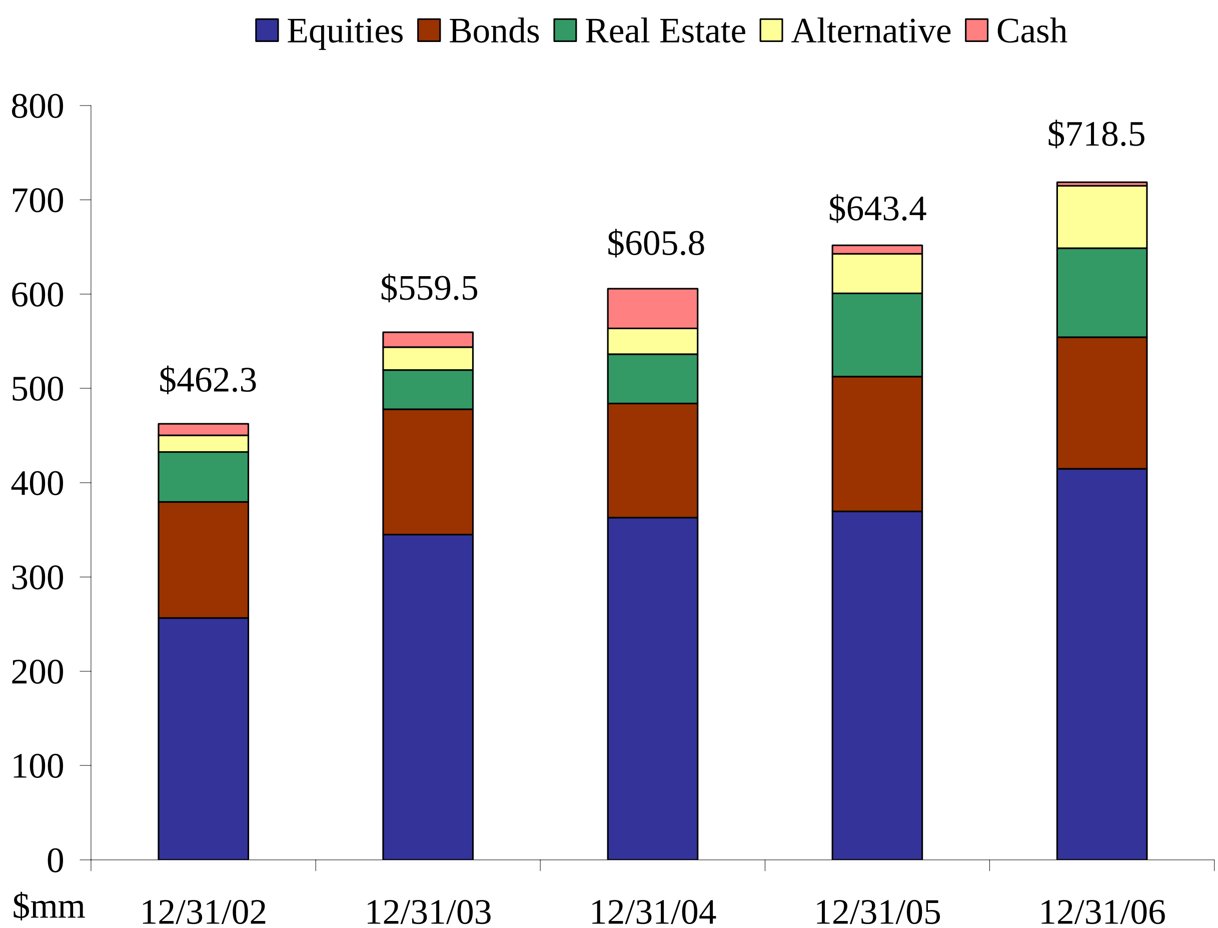
Investment Results*

	4Q06	1 YR	3 YR	5 YR	10 YR	Since Inception	Inception Date
Total System	**6.3**	**14.8**	**12.1**	**9.1**	**9.2**	**9.9**	**10/1/1995**
CPI (inflation)	-0.5	2.5	3.1	2.7	2.4	2.5	
Total Equity	**8.5**	**17.5**	**14.7**	**10.0**	**NA**	**NA**	**10/1/1995**
Russell 3000	7.1	15.7	11.2	7.2	8.6	10.0	
MSCI ACWI Free (ex. U.S.)	11.2	26.7	21.3	16.4	8.3	8.3	
Total Fixed Income	**1.8**	**6.1**	**5.6**	**6.9**	**NA**	**NA**	**10/1/1995**
Lehman Universal	1.5	5.0	4.2	5.6	6.4	6.5	
Total Open-End Real Estate	**4.7**	**17.5**	**15.9**	**11.9**	**NA**	**11.1**	**1/1/1999**
NCREIF Property	4.5	16.6	17.0	13.3	12.7	12.1	
Total Absolute Return **	**4.5**	**11.1**	**NA**	**NA**	**NA**	**12.3**	**7/1/2005**
HFRI Fund of Funds Composite	5.4	10.4	8.2	7.4	7.9	11.3	

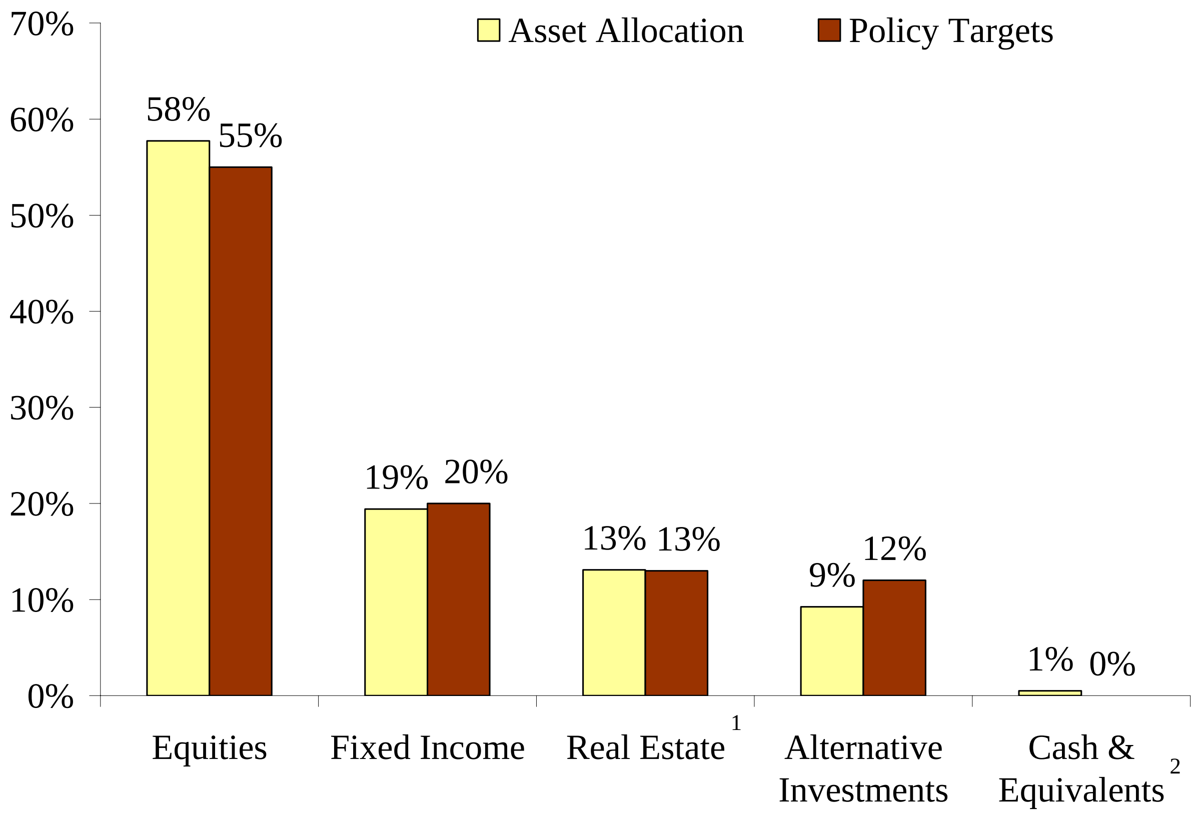
* The WRS's policy is a time weighted average of the representative asset class benchmarks.

** Other alternative investments include private equity 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 appreciated by $7.2 million, including $3.3 million in capital called and $11.2 million in distributions. This appreciation amounts to a dollar-weighted return of approximately 49% for the calendar year period covered in this report.

Asset Allocation

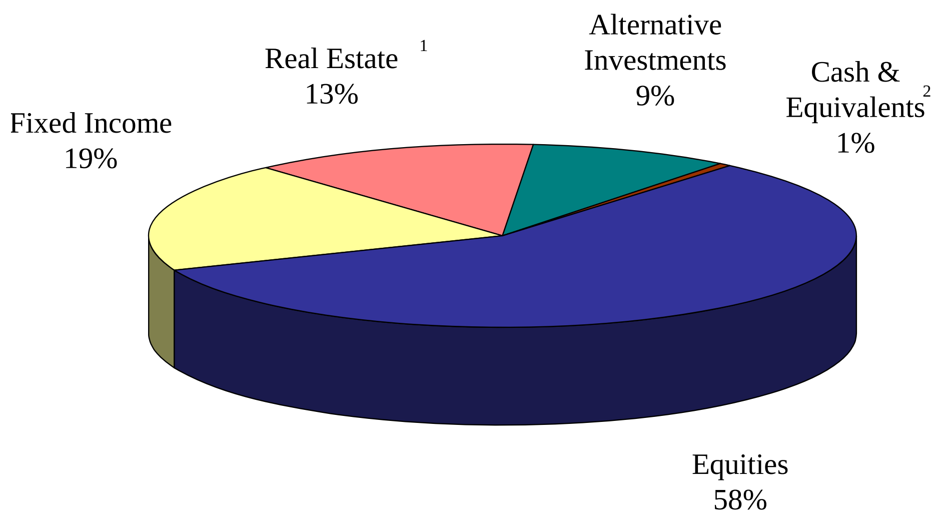


Aggregate Asset Allocation vs. Policy Targets

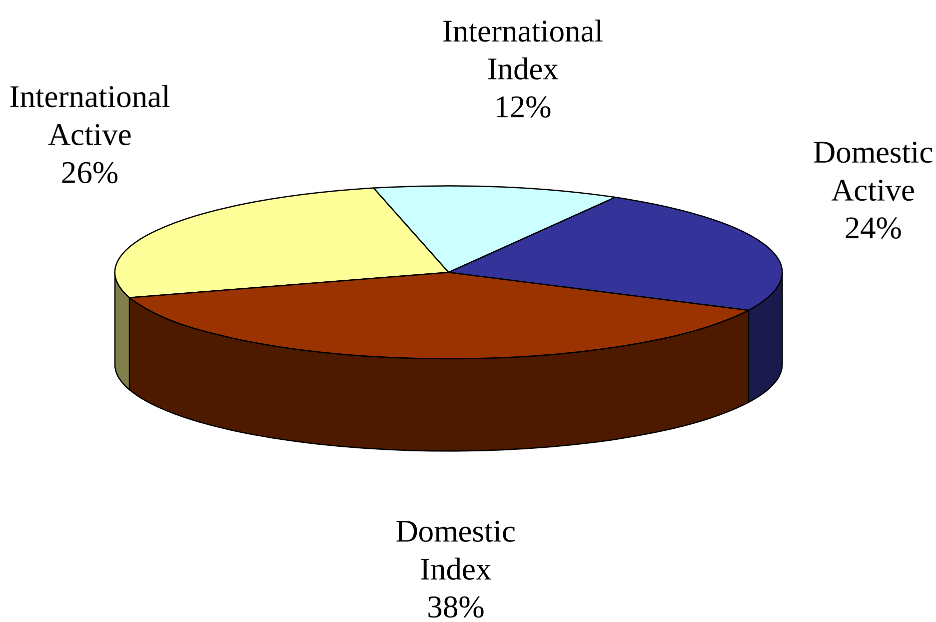


[1] The Real Estate policy target includes a strategic allocation to Timber of 3%.
[2] Includes investment in cash held by managers within separate accounts. Less than 1% of assets were held directly in money market funds on December 31, 2006.

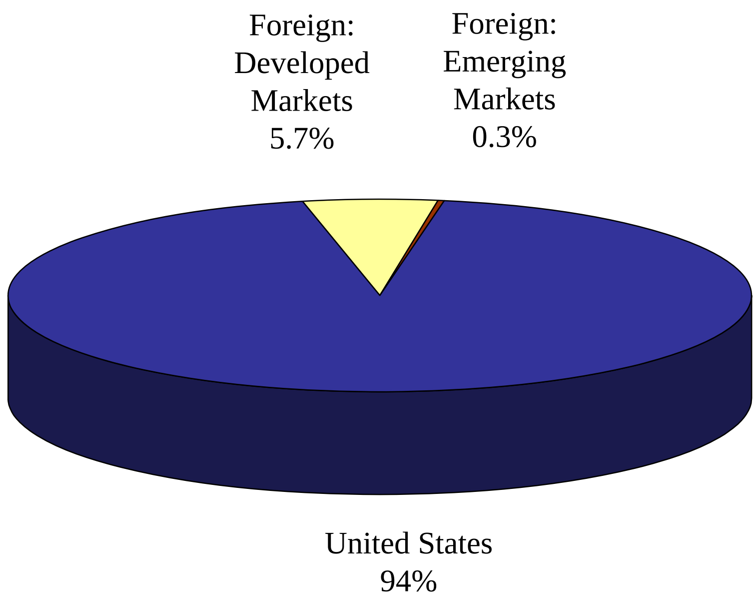
Aggregated Asset Allocation



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	74,084	5.68	2.2%	Energy
2.	General Electric	130,172	4.84	1.9%	Capital Goods
3.	Citigroup	61,480	3.42	1.3%	Diversified Financials
4.	Procter & Gamble	52,614	3.38	1.3%	Household & Personal Products
5.	Bank of America	56,378	3.01	1.2%	Diversified Financials
6.	Pfizer	90,462	2.34	0.9%	Pharmaceuticals Biotechnology & Life Sciences
7.	Microsoft	73,798	2.20	0.9%	Software & Services
8.	American International Group	30,272	2.17	0.8%	Insurance
9.	JPMorgan Chase	43,243	2.09	0.8%	Diversified Financials
10.	Chevron	27,396	2.01	0.8%	Energy

Ten Largest Fixed Income Holdings by Fair Value

	Security	Coupon (%)	Maturity Date	Number of Shares	Market Value ($mm)	% of Bonds
1.	TIPS	3.9	4/15/2029	2,148,580	2.7	1.9
2.	TIPS	0.9	4/15/2010	2,615,557	2.5	1.7
3.	TIPS	2.4	1/15/2025	2,398,502	2.4	1.7
4.	TIPS	3.0	7/15/2012	2,290,022	2.4	1.6
5.	TIPS	3.6	4/15/2028	1,871,850	2.3	1.6
6.	TIPS	2.0	1/15/2014	1,998,982	1.9	1.3
7.	TIPS	1.9	7/15/2013	1,928,640	1.9	1.3
8.	TIPS	3.6	1/15/2008	1,780,295	1.8	1.2
9.	TIPS	2.0	7/15/2014	1,852,415	1.8	1.2
10.	TIPS	3.9	1/15/2009	1,716,827	1.8	1.2

A complete portfolio is available upon request.

Schedule of Fees & Commissions

Investment Fees December 31, 2006	
Acadian Asset Management	$ 169,708
Ascent Venture Management Inc IV	103,748
Ascent Venture Management, Inc. II	29,673
Ascent Venture Management, Inc. III	92,042
Bailard Real Estate Investment Trust I	252,137
Boston Company Asset Mgt (EAFE)	179,899
Boston Company Asset Mgt. (Premier)	195,158
Boston Company Asset Mgt.(ACWI)	197,705
Boston Millennium Partners	67,139
BPIF Blackstone	96,931
Charlesbank Capital Partners V	20,935
Charlesbank Capital Partners VI	57,506
Columbia Management Adv. Inc.	226,692
Concord Partners LP	619
Duke Street Capital	6,175
Enhancement Investment Tech. LLC	265,755
Hancock	56,678
Heitman Investment Management	210,931
Hutchens Investment Mgt. Inc.	85,831
Intercontinental Real Estate Corp.	37,500
INVESCO Private Capital, Inc.	37,500
L&B Realty Advisors Inc.	288
Lazard	91,668
Loomis Sayles & Company, L.P.	279,768
New England Partners Capital II	1,041
Northern Trust Company	11,768
Northstar Capital LLC IV	86,429
OPUS Investment Mgt. Inc.	33,791
OPUS Investment Mgt. Inc. (Tips)	31,248
PENN Capital Management	126,695
PRIT Absolute Return	169,769
PRIT Core Real Estate	220,033
Riverside Company 2000	23,046
Riverside Company 2003	19,434
RMK Balanced B Fund	60,803
RMK Fund I	19,466
Standard Life Investments Limited	51,151
State Street Global Advisors EAFE Index	12,929
State Street Global Advisors S&P 500 Flagship	29,728
State Street Global Advisors Russell 1000 Value	19,272
State Street Global Advisors S & P Midcap	6,773
VEF Advisors II	11,121
VEF Advisors III	218
VEF Advisors IV	17,933
Total Investment Managers Fees	**3,714,634**
State Street Bank (Custodian Bank Fee)	336,851
Meketa Investment Consultant Fee	132,000
Security Lending Fees	681,669
Total Other Fees	**1,150,520**
Total Investment Fees	$ **4,865,154**

Commissions to Brokers

Broker	Total Commission ($)	Total Shares	Commission Per Share ($)
ADP CLEARING + OUTSOURCING SERVICES, INC	2,572	71,955	0.04
AVONDALE PARTNERS LLC	414	10,586	0.04
BAIRD, ROBERT W. & COMPANY INCORPORATED	1,063	34,706	0.03
BANC/AMERICA SECUR.LLC MONTGOMERY DIV	962	19,575	0.05
BEAR STEARNS + CO INC	4,334	99,231	0.04
BEAR STEARNS SECURITIES CORP	17,155	436,632	0.04
BNY BROKERAGE INC	7,529	185,785	0.04
BOENNING + SCATTERGOOD INC	124	3,100	0.04
BREAN MURRAY	334	7,530	0.04
CANACCORDADAMS INC.	436	9,140	0.05
CANTOR FITZGERALD + CO	497	19,368	0.03
CAPITAL INSTITUTIONAL SVCS INC EQUITIES	6,549	327,187	0.02
CIBC WORLD MARKETS CORP	22	550	0.04
CITIGROUPGLOBAL MARKETS INC	1,715	43,324	0.04
CJS SECURITIES	155	5,158	0.03
COWEN + CO., LLC	73	1,828	0.04
CREDIT RESEARCH + TRADING LLC	79	1,975	0.04
CREDIT SUISSE FIRST BOSTON CORPORATION	1,709	76,721	0.02
CREDIT SUISSE SECURITIES (USA) LLC	6,595	314,352	0.02
DAVENPORT& CO. OF VIRGINIA, INC.	961	24,645	0.04
DAVIDSON D.A. + COMPANY INC.	27	907	0.03
DEUTSCHE BANC ALEX. BROWN INSTIT FIX INC	186	4,278	0.04
DEUTSCHE BANK SECURITIES INC	3,789	167,225	0.02
E TRADE SECURITIES, INC	13	665	0.02
EDWARDS AG SONS INC	160	4,000	0.04
FIRST ALBANY CAPITAL INC.	25	500	0.05
FIRST ANALYSIS SECURITIES CORP	108	2,690	0.04
FIRST CLEARING, LLC	24,474	489,480	0.05
FRIEDMAN BILLINGS + RAMSEY	630	16,560	0.04
GOLDMAN SACHS + CO	5,184	247,381	0.02
GOLDMAN SACHS EXECUTION + CLEARING	2,136	92,815	0.02
GRAIG - HALLUM	134	5,102	0.03
GRIFFITHSMCBURNEY + PARTNERS	1,107	55,345	0.02
GUZMAN + CO	1,849	88,520	0.02
INSTINET	9,309	445,592	0.02
INVESTMENT TECHNOLOGY GROUP INC.	9,369	466,860	0.02
J P MORGAN SECURITIES INC	605	18,723	0.03
JEFFERIES+ CO. - BOND DIVISION	9	228	0.04
JEFFERIES+ COMPANY INC	10,067	622,742	0.02
JMP SECURITIES	51	1,250	0.04
JOHNSON RICE + CO	36	715	0.05
JONES & ASSOCIATES INC	474	11,266	0.04
KEEFE BRUYETTE + WOODS INC	793	22,962	0.03
KING, CL,& ASSOCIATES, INC	690	16,769	0.04
KNIGHT SECURITIES	51	1,491	0.03

(continued)

Broker	Total Commissions ($)	Total Shares	$/share
LEGG MASON WOOD WALKER INC	44	875	0.05
LEHMAN BROTHERS INC	3,747	116,516	0.03
LIQUIDNETINC	2	100	0.02
LYNCH JONES AND RYAN INC	18,931	592,349	0.03
MCDONALD AND COMPANY SECURITIES, INC.	234	9,156	0.03
MERRILL LYNCH PROFESSIONAL CLEARING CORP	825	18,075	0.05
MERRILL LYNCH,PIERCE,FENNER + SMITH, INC	5,979	384,678	0.02
MERRILL PROFESSIONAL	214	7,137	0.03
MIDWEST RESEARCH SECURITIES	173	4,320	0.04
MIDWOOD SECURITIES INC	23,544	470,875	0.05
MORGAN KEEGAN & CO INC	1,439	30,540	0.05
MORGAN STANLEY CO INCORPORATED	33	1,961	0.02
NATEXIS BLEICHROEDER INC	120	2,820	0.04
NATIONAL FINANCIAL SERVICES CORP.	2,484	61,812	0.04
NBCN INC.**	423	17,875	0.02
NEEDHAM + COMPANY	529	12,255	0.04
NEUBERGERAND BERMAN	9,914	295,825	0.03
OPPENHEIMER & CO. INC.	336	7,200	0.05
PENSION FINANCIAL	639	51,995	0.01
PENSION FINANCIAL SERVICES CANADA INC	321	16,035	0.02
PERSHING LLC	5,859	149,935	0.04
PETRIE PARKMAN & CO INC	130	4,345	0.03
PIPELINE TRADING SYSTEMS LLC	22	1,117	0.02
PIPER JAFFRAY	502	11,400	0.04
PRUDENTIAL EQUITY GROUP	184	4,596	0.04
RAYMOND JAMES AND ASSOCIATES INC	4,472	104,880	0.04
RBC CAPITAL MARKETS	17	420	0.04
ROSENBLATT SECURITIES INC	7,841	401,239	0.02
S.G. COWEN & CO., LLC	1,246	37,200	0.03
SCOTT & STRINGFELLOW, INC	46	915	0.05
SEASONGOOD + MAYER	374	7,475	0.05
SIDOTI + COMPANY LLC	44	2,200	0.02
SOUTHWESTSECURITIES, INC.	80	1,600	0.05
STATE STREET BROKERAGE SERVICES	7,488	390,475	0.02
STERNE, AGEE & LEACH, INC	547	13,060	0.04
STIFEL NICOLAUS + CO INC	1,226	28,229	0.04
UBS FINANCIAL SERVICES INC	1,025	34,161	0.03
UBS SECURITIES LLC	7,557	367,904	0.02
WACHOVIA SECURITIES, LLC	1,800	39,305	0.05
WEDBUSH MORGAN SECURITIES INC	246	5,135	0.05
WEEDEN + CO	3,649	166,967	0.02
Total	**238,840**	**8,352,371**	**0.03**

(concluded)

INVESTMENT SUMMARY

	Assets (mm)	% of Aggregate	% of System
Total System	**$718.5**	**100%**	**100%**
Total Domestic Equities	**$258.9**	**100%**	**36%**
Information Technology	35.7	14%	5%
Financials	54.4	21%	8%
Health Care	32.1	12%	4%
Consumer Discretionary	35.0	14%	5%
Industrials	35.2	14%	5%
Energy	19.9	8%	3%
Consumer Staples	18.1	7%	3%
Materials	9.8	4%	1%
Utilities	10.6	4%	1%
Telecommunications Services	8.0	3%	1%
Total Fixed Income	**$139.6**	**100%**	**19%**
Credit	67.5	48%	9%
U.S. Treasury	38.6	28%	5%
Mortgage Backed	22.5	16%	3%
U.S. Agency	6.4	5%	1%
Commercial Mortgage Backed	2.5	2%	0%
Asset Backed	0.3	0%	0%
Cash Equivalent	1.8	1%	0%
Total International Equities	**$155.9**	**100%**	**22%**
Europe - Developed	83.7	54%	12%
Pacific Rim/Australasia - Developed	46.2	30%	6%
Emerging Markets	17.4	11%	2%
Other (Non-EAFE)	8.6	6%	1%
Total Alternative Investments	**$160.5**	**100%**	**22%**
Real Estate	94.1	59%	13%
Absolute Return	35.6	22%	5%
Private Markets	30.8	19%	4%
Cash & Equivalents	**$3.6**	**100%**	**1%**

LIQUIDITY PROFILE

Benefits payments totaled approximately $53.4 million during the year and along with other payments of $5.1 million resulted in total cash outflows of $58.5 million in 2006. These payments were partially offset by a contribution of approximately $23.4 million from employers and other cash receipts of $16.4 million for a total of $39.8 million in 2006. This resulted in a negative cash flow of approximately $18.7 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 8.6%

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Actuarial Section

SEGAL

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

May 4, 2007

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, 2007 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, 2018. The normal cost is expected to remain at a level percentage of payroll. The remaining liability of the 2002 ERI is amortized over an 11-year period (by June 30, 2018) with level payments. The 2003 ERI liability is amortized over a 5-year period (by June 30, 2012) with level payments. The Section 90 ACD liability is amortized over a 7-year period (by June 30, 2014) with level payments. The remaining unfunded liability is amortized over an 11-year period with payments increasing at the rate of 3.5% per year. The contribution will increase by approximately 3.5% per year, except for years when the ERI and Section 90 ACD liabilities are fully amortized.

There are several changes to the funding objective since the prior valuation. In the prior valuation, the remaining unfunded liability was being amortized over a period ending June 30, 2023 with payments increasing at the rate of 4.5% per year. The 2002 ERI was being funded by payments scheduled to increase at the rate of 1.5% 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, 2007.

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 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, 2007, which was adopted by the WRS on April 19, 2007.

Mortality Rates

Healthy	1994 Group Annuity Mortality Table
Disabled	1994 Group Annuity Mortality Table set forward 10 years

Termination Rates before Retirement

	Rate (%)			
	Mortality		Group 1 and 2	
Age	**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.

	Mortality		Group 4	
Age	**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

	Rate (%)		
Age	**Groups 1 and 2**	**Age**	**Group 4**
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

Female (or male) spouses 3 years younger (or older) 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 2007 (previously $600,000 for calendar 2006).

Actuarial Value of Assets

Market value

2006 Salary

2006 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 participants in unions identified by the City were reduced to adjust for retroactive pay amounts. The salaries of police officials were adjusted by approximately 6% to reflect unsettled bargaining agreements.

Total Service

Total creditable service based on adjusted date of hire, except special cases where date of hire was used.

Actuarial Cost Method

Entry Age Normal Actuarial Cost Method. Entry Age is the age of the participant at the Adjusted 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, 2004 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. Market value will be used thereafter.

II. Schedule of Active Member Valuation Data

Valuation date	Number	Projected annual payroll ($)	Annual average pay ($)	% Increase in average pay
1/1/2002	4,080	148,764,543	36,462	4.82
1/1/2003	3,679	142,802,508	38,816	6.45
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

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

	Added to Rolls		Removed from Rolls		Rolls - end of year			
Year ended	Number	Annual allowances[1]	Number	Annual allowances	Number	Annual allowances[1]	% Increase in annual allowances	Average annual allowances
2001	86	$ 2,057,603	131	N/A	2,905	$ 41,736,155	4.25	$ 14,367
2002	216	6,081,952	120	N/A	3,001	47,173,651	13.03	15,719
2003	115	3,212,097	120	N/A	2,996	49,606,369	5.16	16,558
2004	77	2,031,304	106	N/A	2,967	51,566,334	3.95	17,380
2005	76	1,890,735	124	N/A	2,919	52,623,545	2.05	18,028
2006	78	1,891,430	133	N/A	2,864	53,571,242	1.80	18,705

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

IV. Solvency Test

Valuation Date	Actuarial Accrued Liability: (1) Active member contributions	(2) Retirees and beneficiaries	(3) Active/Inactive members (Employer financed)	Actuarial value of assets	Portion of Actuarial Accrued Liability Covered by Assets: (1)	(2)	(3)
1/1/2002	$ 111,769,704	342,266,770	217,840,469	620,814,307	100	100	77
1/1/2003	111,507,319	397,136,220	207,212,025	554,190,090	100	100	22
1/1/2004	115,779,891	418,037,422	209,753,127	577,123,067	100	100	21
1/1/2005	122,748,711	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

V. Analysis of Financial Experience

	Year Ended December 31, 2006	2005	2004	2003	2002
1. Unfunded actuarial accrued liability as of January 1	$ 162,940,960	$ 165,848,695	166,447,373	161,665,474	51,062,636
2. Normal cost as of January 1	21,159,434	20,362,054	19,170,321	19,902,898	21,597,468
3. Employer and employee contributions during year	(35,961,906)	(35,484,556)	(31,843,173)	(29,261,377)	(24,139,117)
4. Interest					
(a) For whole year on (1)+(2)	15,188,283	15,827,913	15,777,504	15,433,311	6,176,109
(b) For half year on (3)	(1,340,348)	(1,362,059)	(1,222,286)	(1,123,184)	(926,569)
(c) Total interest	13,847,935	14,465,854	14,555,218	14,310,127	5,249,540
5. Expected unfunded actuarial liability	161,986,423	165,192,047	168,329,739	166,617,122	53,770,527
6. Actual unfunded actuarial accrued liability	120,811,463	162,940,960	165,848,695	166,447,373	161,665,474
7. (Gain) or loss for the year: (6)-(5)	$ (41,174,960)	$ (2,251,087)	(2,481,044)	(169,749)	107,894,947
8. Investment (gain) or loss	$ (39,177,515)	$ (4,698,351)	405,058	4,639,654	98,499,864
9. (Gains) or losses from sources other than investments	(1,997,445)	(14,912,389)	(5,367,076)	(8,634,577)	3,781,977
10. Plan changes	-	370,567	2,480,974	3,825,174	12,987,821
11. Assumption changes	-	16,989,086	-	-	(7,347,715)

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 fifteen dollars per year of creditable service, not exceeding three hundred dollars. 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, 1974 and before January 1, 1984 contribute 7 percent; employees hired after January 1, 1984 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 WRS).

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 is 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.

"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 or permanent member of a police department 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.

Statistical Section

Schedule of Additions to Plan Net Assets by Source

Fiscal Year	Plan Member Contributions	Employer Contributions	Employer Contributions as % of Covered Payroll	Investment Income(a)	Other(b)	Total
1997	$ 8,656,891	23,969,792	20.90	$ 37,490,010	4,922,608	75,039,301
1998	9,278,830	23,813,831	20.60	39,160,437	4,238,960	76,492,058
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	8.52	(67,805,128)	3,615,546	(38,839,710)
2003	11,691,887	18,928,252	13.00	115,614,944	2,783,268	149,018,351
2004	12,187,208	20,150,377	14.24	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

(a) Net of Investment expenses

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

Schedule of Deductions from Plan Net Assets by Type

Fiscal Year	Benefits	Administrative Expenses	Withdrawals(a)	Total
1997	$ 35,382,767	423,386	2,432,813	38,238,966
1998	36,110,087	372,216	2,844,845	39,327,148
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

(a) Includes amounts for employee withrawals and employee transfers to other state agencies.

Schedule of Total Change in Net Assets

Fiscal Year	Total Change in Net Assets
1997	$ 36,800,335
1998	37,164,910
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

Schedule of Benefit Expenses by Type

Year ended December 31	Regular	Disability	Beneficiary	COLA	Annuities	Total
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

Schedule of Retired Members by Type of Benefit

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

Source: Actuarial valuation as of January 1, 2007

Schedule of Average Benefit Payments

Year ended December 31	Number	Annual benefits ($)	Monthly average ($)	Annual average ($)
2000	2,950	39,696,596	1,121	13,456
2001	2,905	41,095,677	1,179	14,147
2002	3,001	43,540,572	1,209	14,509
2003	2,996	47,848,502	1,331	15,971
2004	2,967	50,517,094	1,419	17,026
2005	2,919	52,105,583	1,488	17,850
2006	2,864	53,350,080	1,552	18,628

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

Fiscal Year	Employer Name	Number of Covered Employees	Percentage of Total Covered Employees
1997	City of Worcester	3,352	94.4%
1997	Worcester Housing Authority	197	5.6%
2006	City of Worcester	3,240	95.2%
2006	Worcester Housing Authority	164	4.8%

Source: The WRS administrative staff