# MUNICIPAL EMPLOYEES' RETIREMENT SYSTEM - FUND B

# NOTES TO FINANCIAL STATEMENTS

# JUNE 30, 2011

**APPLICATION OF STATEMENT NO. 25 OF THE**
**GOVERNMENTAL ACCOUNTING STANDARDS BOARD**

**DISCLOSURE OF PENSION INFORMATION**

## A. Plan Description

1. The Municipal Employees' Retirement System (MERS) is a cost sharing multiple employer public employee retirement system (PERS) established by the State of Connecticut and administered by the State Retirement Commission to provide pension benefits for the employees of participating municipalities. MERS is considered to be a part of the State of Connecticut's financial reporting entity and is included in the State's financial reports as a pension trust fund.

2. Any local government authority in the State of Connecticut, including towns, cities, boroughs, regional school districts, housing authorities, or other special districts, may elect to participate for one or more of its departments, including elective officers; only teachers who are covered under the Connecticut State Teachers' Retirement System are ineligible. As of July 1, 2010, there were 186 participating local government units (counting departments of municipalities which joined or report separately as separate units).

Results shown in this report are based on the July 1, 2010 actuarial valuation of MERS. Actuarial valuations are performed biennially rather than annually and the next full valuation will be as of July 1, 2012. At July 1, 2010, the MERS membership consisted of:

| | Retirees & Beneficiaries | Terminated Vested | Active Vested | Active Non-Vested | Inactive Non-Vested |
|---|---|---|---|---|---|
| Police & Fire | | | | | |
| a. Without Social Security | 317 | 19 | 510 | 256 | 30 |
| b. With Social Security | 242 | 23 | 275 | 135 | 32 |
| General | | | | | |
| a. Without Social Security | 2,175 | 236 | 2,021 | 758 | 188 |
| b. With Social Security | 2,971 | 442 | 3,236 | 1,388 | 591 |
| Withdrawn Municipalities* | 7 | 0 | N/A | N/A | N/A |
| Total Members | 5,705 | 720 | 6,042 | 2,537 | 841 |

* The head count shown is included in the groups above.

3. Plan provisions are set by statute of the State of Connecticut. MERS provides retirement benefits, as well as death and disability benefits. Annual cost of living increases are applied to disabled and non-disabled retirement benefits and vary based upon member age and date of retirement. For members that retired prior to January 1, 2002, increases between 3.0% and 5.0% are paid to those who have reached age 65 and (effective January 1, 2002) increases of 2.5% are paid to those who have not yet reached age 65. For members that retire after December 31, 2001, increases between 2.5% and 6.0% are paid, regardless of age. Benefits vest after 5 years of continuous service or 15 years of active aggregate service. Vested members who retire after age 55 or after 25 years of service, irrespective of age, are entitled to an annual retirement benefit, payable monthly for life, in an amount for each year of service equal to:

   - If not covered by Social Security: 2% of the average of earnings for the three highest paid years of service.

   - If covered by Social Security: 1-1/2% of the average of earnings for the three highest paid years of service not in excess of the year's breakpoint, plus 2% of the average of earnings for the three highest paid years of service in excess of the year's breakpoint. The year's breakpoint for 2010 is $54,800.

4. Covered employees are required by State statute to contribute 2-1/4% of earnings upon which Social Security tax is paid plus 5% of earnings on which no Social Security tax is paid. Each participating municipality is required to contribute the amounts necessary to finance the remaining costs of the plan. Employees not covered by Social Security are required to contribute 5% of all earnings.

## B. Summary of Significant Accounting Policies and Plan Asset Matters

1. Basis of Accounting

   MERS financial statements are prepared using the accrual basis of accounting. Employee and employer contributions are recognized as revenues in the period in which employee services are performed.

2. Method Used to Value Investments

   Retirement trust funds can invest in the following investment pools maintained by the State of Connecticut.

   Mutual Fixed Income Fund - Investments consist principally of bonds and notes.

   Mutual Equity Fund - Investments consist principally of common stocks.

   Real Estate Fund - Investments consist principally of interest in commingled equity real estate funds.

Mutual Commercial Mortgage Fund - Investments consist principally of interest in commercial mortgages.

Mutual Venture Capital Fund - Investments consist principally of interests in venture capital partnerships which have common stock interests in emerging businesses.

Mutual International Stock Fund - Investments consist principally of international equity securities.

Liquidity Fund - Investments consist principally of money market instruments.

Private Equity - Investments comprised of various limited partnerships, limited liability companies and securities.

Investments in the pooled funds are valued at cost. Market values of the investment pools are determined by the Master Custodian based on the performance of the underlying securities. Investment income is recognized as earned. Gains and losses on sales and redemptions of investments are recognized on the transaction date. There are no investments in any organizations that represent 5% or more of the net assets available for benefits.

## C. **Funding Status and Progress**

1. The actuarial accrued liability is a measure that uses the benefit provisions and is intended to (i) help users assess the plan's funding status on a going-concern basis, and (ii) assess progress being made in accumulating sufficient assets to pay benefits when due. Allocation of the actuarial present value of projected benefits between past and future service was based on service using the entry age actuarial cost method. Entry age was established by subtracting credited service from current age on the valuation date. Assumptions, including projected pay increases, were the same as those used to determine the annual required contribution between entry age and assumed exit age.

   The actuarial value of assets is based on a market-related method that recognizes i) 20% of any difference between actual and expected investment income (gain/loss) in the valuation year and ii) 20% of any previous years' unrecognized investment gains/losses. Such smoothed actuarial asset value shall not be less than 80% or greater than 120% of the market value of assets.

2. The actuarial accrued liability was determined as part of an actuarial valuation as of July 1, 2010.

3. Significant actuarial assumptions used include:

a. Rate of return on the investment of present and future assets of 8.25% per year compounded annually.

b. Projected salary increases of 3.75% per year compounded annually, attributable to inflation.

c. Additional projected salary increases ranging from 7.50% to 0.75%, per year, attributable to seniority/merit.

d. Annual cost of living increases are applied to disabled and non-disabled retirement benefits and vary based upon member age and date of retirement. For members that retired prior to January 1, 2002, increases of 3.50% are assumed for those who have reached age 65 and (effective January 1, 2002) increases of 2.5% are assumed for those who have not yet reached age 65. For members that retire after December 31, 2001, increases of 2.6% are assumed, regardless of age.

| | | |
|---|---|---|
| 4. | Actuarial Accrued Liability as of July 1, 2010 | $1,880,664,552 |
| 5. | Actuarial Value of Assets | 1,662,583,369 |
| 6. | Unfunded Actuarial Accrued Liability | $ 218,081,183 |

7. During the year there were no changes in benefit provisions or actuarial assumptions.

## D. Contributions Required and Contributions Made

1. Each covered municipality is required by State statute to pay an actuarially determined percentage of covered payroll to provide for benefits based on service from the municipality's date of participation in MERS. This percentage varies for police and fire versus general employees, and within those two groups, may vary for populations covered by Social Security versus those not covered by Social Security. The statute also requires each municipality to pay an annual amount for benefits based on service prior to the unit's date of participation, if any. This amount is a level dollar amortization (including interest and principal) over varying time periods depending upon the unit's date of participation and other factors.

2.
   a. The contributions are actuarially determined using the entry age normal method.

   b. The actuarial assumptions are the same as those used to compute the actuarial accrued liability discussed in Section C above.

   c. Contributions totaling $67,179,955 ($51,125,808 employer and $16,054,147 employee) were made for the plan year ending June 30, 2011 in accordance with the contribution requirements approved by the Retirement Commission based on the measurement of the System as of July 1, 2009. These contributions consisted of: (a) $52,751,455 normal cost and (b) $14,428,500 amortization of the unfunded actuarial accrued liability. The employer and employee contributions represent 11.7% and 3.7% of the expected covered payroll, respectively, for the fiscal year ending June 30, 2011.

**Schedule of Employer Contributions**

| **Fiscal Year 7-1/6-30** | **Valuation Date 7-1** | **Percentage of ARC Contributed** |
|---|---|---|
| 2004-05 | 2003 | 100.0% |
| 2005-04 | 2004 | 100.0 |
| 2006-07 | 2005 | 100.0 |
| 2007-08 | 2006 | 100.0 |
| 2008-09 | 2007 | 100.0 |
| 2009-10 | 2008 | 100.0 |
| 2010-11 | 2009 | 89.0 |

Note that for the fiscal years ending June 30, 2010 and prior, the sum of the actual employer contributions made plus a credit from the stabilization reserve resulted in 100% of the ARC being contributed.

## E. <u>Ten Year Historical Trend Information</u>

Ten-year historical trend information designed to provide information about MERS' progress made in accumulating sufficient assets to pay benefits when due is presented in the supplement immediately following these notes to financial statements.

**MUNICIPAL EMPLOYEES' RETIREMENT FUND**

**REQUIRED SUPPLEMENTARY INFORMATION**

**ANALYSIS OF FUNDING PROGRESS**

**(IN MILLIONS OF DOLLARS)**

| Fiscal Year Ending | Value Of Assets (1) | | Rate Of Return (2) | | Actuarial Accrued Liability (AAL) (3) | % Funded (4) = (1) / (3) | | Unfunded AAL (5) = (3) - (1) | | Annual Covered Payroll (6) | Unfunded AAL as a % of Covered Payroll (7) = (5) / (6) | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Actuarial | Market | Actuarial | Market | | Actuarial | Market | Actuarial | Market | | Actuarial | Market |
| 2001 | $1,353 | $1,300 | 10.41% | (3.62)% | $1,238 | 109.3% | 105.0% | $(115) | $(62) | $311 | (37)% | (20)% |
| 2002 | 1,403 | 1,187 | 6.02 | (6.47) | 1,319 | 106.4 | 90.0 | (84) | 132 | 322 | (26) | 41 |
| 2003 | 1,418 | 1,175 | 3.46 | 1.89 | 1,379 | 102.8 | 85.2 | (39) | 204 | 326 | (12) | 63 |
| 2004 | 1,434 | 1,306 | 3.80 | 14.49 | 1,393 | 102.9 | 93.8 | (41) | 87 | 333 | (12) | 26 |
| 2005 | 1,512 | 1,398 | 6.51 | 9.89 | 1,465 | 103.2 | 95.4 | (47) | 67 | 352 | (13) | 19 |
| 2006 | 1,588 | 1,509 | 7.19 | 10.39 | 1,550 | 102.5 | 97.4 | (38) | 41 | 366 | (10) | 11 |
| 2007 | 1,701 | 1,729 | 8.96 | 16.60 | 1,640 | 103.7 | 105.4 | (61) | (89) | 388 | (16) | (23) |
| 2008 | 1,779 | 1,632 | 6.32 | (4.03) | 1,722 | 103.3 | 94.8 | (57) | 90 | 412 | (14) | 22 |
| 2009 | 1,619 | 1,349 | (6.86) | (15.10) | 1,821 | 88.9 | 74.1 | 202 | 472 | 427 | 47 | 111 |
| 2010 | 1,663 | 1,479 | 5.38 | 12.98 | 1,881 | 88.4 | 78.6 | 218 | 402 | 422 | 52 | 95 |

**MUNICIPAL EMPLOYEES' RETIREMENT FUND**

**REQUIRED SUPPLEMENTARY INFORMATION**

**REVENUES BY SOURCE AND EXPENSES BY TYPE**

**(IN MILLIONS OF DOLLARS)**

| Revenues by Source | | | | | | | Expenses by Type | | |
|---|---|---|---|---|---|---|---|---|---|
| Fiscal Year | Employee Contributions | Employer Contributions* | Investment Income | Realized Gains | Other | Total | Benefits | Refunds | Total |
| 2001 - 02 | $11.4 | $15.3 | $44.8 | $0.0 | $0.0 | $71.5 | $55.8 | $1.2 | $57.0 |
| 2002 – 03 | 11.2 | 15.9 | 52.1 | 1.4 | 0.0** | 80.6 | 59.7 | 1.1 | 60.8 |
| 2003 – 04 | 11.7 | 16.3 | 51.6 | 7.9 | 0.0 | 87.5 | 63.6 | 0.9 | 64.5 |
| 2004 – 05 | 12.2 | 21.8 | 54.0 | 0.2 | 0.0 | 88.2 | 68.4 | 1.3 | 69.7 |
| 2005 – 06 | 12.9 | 28.7 | 53.2 | 1.6 | 0.0 | 96.4 | 72.8 | 1.2 | 74.0 |
| 2006 – 07 | 13.1 | 39.4 | 61.0 | 19.3 | 0.0 | 132.8 | 78.9 | 1.5 | 80.4 |
| 2007 – 08 | 17.6 | 38.8 | 66.1 | 135.5 | 0.0 | 258.0 | 83.5 | 1.1 | 84.6 |
| 2008 – 09 | 14.8 | 35.9 | 48.5 | 1.5 | 0.0 | 100.7 | 89.3 | 1.3 | 90.6 |
| 2009 – 10 | 14.7 | 38.4 | 40.4 | 49.9 | 0.0 | 143.4 | 93.9 | 1.1 | 95.0 |
| 2010 – 11 | 16.1 | 51.1 | 56.1 | 7.2 | 0.0 | 130.5 | 98.9 | 1.1 | 100.0 |

** Contributions were made in accordance with contribution rates approved by the Retirement Commission.*
*** Transfer of assets from Fund A of $9,977.*