FRANKLIN REGIONAL
RETIREMENT SYSTEM

Annual Financial Statements

For the Year Ended December 31, 2011

TABLE OF CONTENTS

MH&Co

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INDEPENDENT AUDITORS' REPORT

To the Retirement Board
Franklin Regional Retirement System

We have audited the accompanying Statement of Plan Net Assets and Statement of Changes in Plan Net Assets of the Franklin Regional Retirement System as of and for the year ended December 31, 2011, which comprise the System's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Franklin Regional Retirement System'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. 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 respective financial position of the Franklin Regional Retirement System, as of December 31, 2011 and the respective changes in plan net assets thereof, in conformity with accounting principles generally accepted in the United States of America.

Additional Offices:
Andover, MA • Manchester, NH • Nashua, NH • Ellsworth, ME

The management's discussion and analysis, appearing on the following pages, and the supplementary information, appearing in the back of this report, 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.

Melanson Heath + Company P.C.

Greenfield, Massachusetts
October 1, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the Franklin Regional Retirement System (the System), we offer readers this narrative overview and analysis of the financial activities of the System for the fiscal year ended December 31, 2011.

A. OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the basic financial statements. The basic financial statements are comprised of three components: (1) the statement of plan net assets, (2) the statement of changes in plan net assets, and (3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

The statement of plan net assets presents information on all assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position is improving or deteriorating.

The statement of changes in plan net assets presents information showing how the System's net assets changed during the most recent fiscal year. All changes in plan net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected assessments and accrued interest).

Notes to financial statements. The notes provide additional information that are essential to a full understanding of the data provided in the basic financial statements.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information which is required to be disclosed by accounting principles generally accepted in the United States of America.

B. FINANCIAL HIGHLIGHTS

- As of the close of the current fiscal year, the total of assets exceeded liabilities by $ 82,042,905 (i.e., net assets), an increase of $ 646,489 in comparison to the prior year.
- Employer and employee contributions to the plan were $ 8,143,235 which represents a $ 266,948 increase from over the preceding year. The employer share of contributions represents 61% of the total contributions.

- Benefits paid to plan participants were $ 6,451,809. At December 31, 2011, there were 485 retirees and beneficiaries in receipt of pension benefits.
- The System's funded ratio as of the January 1, 2010 actuarial report was 67%.

C. GOVERNMENT-WIDE FINANCIAL ANALYSIS

The following is a summary of condensed financial data for the current and prior fiscal years.

PLAN NET ASSETS

	2011	2010
Cash and investments	$ 84,384,524	$ 83,207,343
Other assets	231,340	194,499
Total assets	84,615,864	83,401,842
Liabilities	2,572,959	2,005,426
Total liabilities	2,572,959	2,005,426
Net assets held in trust for pension benefits	82,042,905	81,396,416
Total net assets	$ 82,042,905	$ 81,396,416

CHANGES IN PLAN NET ASSETS

	2011	2010
Additions:		
Investment income, net	$ 1,404	$ 10,710,754
Contributions	8,143,235	7,876,287
Reimbursements and other income	382,475	364,705
Total additions	8,527,114	18,951,746
Deductions:		
Benefits paid to participants	6,451,809	6,249,418
Refunds to members and transfers to other systems	1,041,885	754,221
Administrative expenses	386,931	392,304
Total expenses	7,880,625	7,395,943
Change in net assets	646,489	11,555,803
Net assets - beginning of year	81,396,416	69,840,613
Net assets - end of year	$ 82,042,905	$ 81,396,416

Financial Highlights. As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. At the close of the most recent fiscal year, total net assets were $ 82,042,905, an increase of $ 646,489 in comparison to the prior year.

Key elements of this change are discussed in the following paragraphs.

Total revenue decreased $ (10,424,632) from the prior year. This was comprised of a decrease in investment income of $ (10,709,350), due mostly to the net decrease in investment value (realized and unrealized, net of management fees) of $ (10,978,775) offset by an increase in interest and dividends of $ 269,425. Other revenue changes include; employer contributions and reimbursements increase of $ 127,932; and employee contribution increase of $ 156,786.

Total expenses increased from the prior year by $ 484,682. This was mostly the result of increases in both benefits paid to participants of $ 202,391 and refunds and transfers out of $ 287,664. These increases were offset by a decrease in administrative expenses of $ (5,373).

In addition, administrative expenses were less than budgeted by approximately $ 107,070, primarily as a result of budgeting for legal expenses that didn't take place during the year and over-budgeting other items such as management fees, equipment and salaries.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Franklin Regional Retirement System's finances for all those with an interest in the System's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

Dale Kowacki, Executive Director
Franklin Regional Retirement System
278 Main Street
Suite 311
Greenfield, MA 01301

FRANKLIN REGIONAL RETIREMENT SYSTEM

STATEMENT OF PLAN NET ASSETS

AS OF DECEMBER 31, 2011

ASSETS	2011	2010
Cash	$ 1,567,038	$ 909,053
Investments, at fair value:		
Equities	11,713,012	13,361,148
Pooled domestic equity funds	7,338,113	6,586,939
Pooled domestic fixed income funds	10,748,027	8,869,331
Pooled real estate funds	3,615,754	3,917,017
PRIT Fund	49,402,580	49,563,855
Receivables:		
Member deductions and makeup payments	183,410	189,325
State COLA receivable	43,535	-
Accrued interest and dividends	46	46
Prepaid expenses	4,349	5,128
TOTAL ASSETS	84,615,864	83,401,842
LIABILITIES		
Accounts payable	212,403	73,239
Employer contributions received in advance	2,360,556	1,932,187
TOTAL LIABILITIES	2,572,959	2,005,426
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS		
Designated:		
Annuity Savings Fund	24,574,861	26,004,392
Annuity Reserve Fund	8,197,683	6,766,401
Military Service Fund	3,481	3,481
Pension Fund	3,906,975	3,260,486
Pension Reserve Fund	45,359,905	45,361,656
TOTAL NET ASSETS HELD	$ 82,042,905	$ 81,396,416

See accompanying notes to financial statements.

FRANKLIN REGIONAL RETIREMENT SYSTEM

STATEMENT OF CHANGES IN PLAN NET ASSETS

FOR THE YEAR ENDED DECEMBER 31, 2011

	2011	2010
Additions		
Investment income:		
Net appreciation (depreciation) in fair value of investments	$ (2,413,046)	$ 7,726,506
Interest and dividends	1,864,840	1,595,415
Net gain (loss) on sale of investments	991,808	1,780,601
Less investment expenses	(442,198)	(391,768)
Total Net Investment Income	1,404	10,710,754
Contributions:		
Employer	4,941,103	4,830,941
Employee	3,202,132	3,045,346
Reimbursement from other systems	292,296	264,160
State reimbursements for COLA and survivor benefits	90,179	100,545
Total Additions	8,527,114	18,951,746
Deductions		
Benefits paid directly to participants	6,451,809	6,249,418
Refunds to members	594,635	312,564
Transfers to other systems	447,250	441,657
Administrative expenses	386,931	392,304
Total Deductions	7,880,625	7,395,943
Net change in plan net assets	646,489	11,555,803
Net assets held in trust for pension benefits:		
Beginning of Year	81,396,416	69,840,613
End of Year	$ 82,042,905	$ 81,396,416

See accompanying notes to financial statements.

Franklin Regional Retirement System

Notes to Financial Statements

The Franklin Regional Retirement System (the System) administers a multiple employer defined benefit pension plan covering all Franklin Regional Retirement System member unit employees deemed eligible by the Retirement Board. The System is governed by a Board made up of five elected and appointed members.

1. Summary of Significant Accounting Policies

The System's financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to each plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. Administrative costs of the System are financed through excess investment earnings.

The accounting records of the System are maintained on a calendar year basis in accordance with the standards and procedures established by the Commonwealth of Massachusetts, Public Employee Retirement Administration Commission (PERAC).

Method Used to Value Investments. Investments are reported at market value in accordance with PERAC guidelines. Investment procedures and restrictions stipulated under Massachusetts General Law must be followed.

2. Plan Description and Contribution Information

The System's plan is a cost-sharing, multiple-employer defined benefit pension plan covering the employees of its 39 member units, except school department employees who serve in a teaching capacity. The pensions of such employees are administered by the Massachusetts Teachers' Retirement Board.

The System is a member of the Massachusetts Contributory Retirement System and is governed by Chapter 32 of the Massachusetts General Laws. Chapter 32 also establishes contribution percentages and benefits paid. The System does not have the authority to amend benefit provisions. As required by Massachusetts General Laws, the System issues a separate report annually to PERAC.

The System provides retirement, disability, and death benefits to plan members and their beneficiaries. Cost-of-living adjustments (COLA) are provided at the discretion of the System's Retirement Board.

Membership consisted of the following at January 1, 2010, the date of the latest actuarial valuation:

Retirees and beneficiaries receiving benefits	442
Terminated plan members entitled to but not yet receiving benefits	637
Active plan members	969
Total	2,048
Number of participating employers	39

At January 1, 2010, the 39 participating employers consisted of:

Towns	24
School Districts	6
Special Districts	9
Total	39

Employers are required to contribute at actuarially determined rates as accepted by the Public Employee Retirement Administration Commission (PERAC).

A. Participation

Participation is mandatory for all full-time employees. Eligibility with respect to part-time, provisional, temporary, seasonal, or intermittent employment is governed by regulations promulgated by the Retirement Board, and approved by PERAC. Membership is optional for certain elected officials.

There are 3 classes of membership in the System:

- Group 1: General employees, including clerical, administrative, technical, and all other employees not otherwise classified.
- Group 2: Certain specified hazardous duty positions.
- Group 4: Police officers, firefighters, and other specified hazardous positions.

B. Member Contribution

Participants contribute a set percentage of their gross regular compensation annually. Employee contribution percentages are specified in Chapter 32 of the Massachusetts General Laws. The employee's individual contribution percentage is determined by their date of entry into the system. In addition, all employees hired after January 1, 1979 contribute an additional 2% on all gross regular compensation over the rate of $ 30,000 per year. The percentages are as follows:

Before January 1, 1975	5%
January 1, 1975 to December 31, 1983	7%
January 1, 1984 to June 30, 1996	8%
Beginning July 1, 1996	9%

C. Cost of Living

Under MGL Chapter 17 of the Acts of 1997, if the Retirement Board votes to pay a cost of living increase for the year, the percentage is determined based on the increase in the Consumer Price Index (CPI) used for indexing Social Security benefits, but cannot exceed 3.0% . Section 51 of Chapter 127 of the Acts of 1999, if accepted, allows boards to grant COLA increases greater than that determined by CPI but not to exceed 3.0%. The first $ 13,000 of a retiree's total allowance is subject to a cost of living adjustment. The total cost of living adjustment for periods from 1981 through 1996 is paid for by the Commonwealth of Massachusetts.

D. Funded Status and Funding Progress

The funded status of the plan as of January 1, 2010, the most recent actuarial valuation date, is as follows (in thousands):

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percent-age of Covered Payroll [(b-a)/c]
01/01/10	$79,459	$119,349	$39,890	67%	$29,457	135%

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

Additional information as of the latest actuarial valuation follows:

Valuation date	1/1/10
Actuarial cost method	Entry Age Normal
Amortization method	Approximate level percent of payroll
Remaining amortization period	19 years
Asset valuation method	Market value adjusted by payables and receivables
Actuarial assumptions:	
Investment rate of return	7.875% per year
Projected salary increase	4.25% per year

3. Cash and Short-Term Investments

Custodial Credit Risk - Deposits. Custodial credit risk is the risk that in the event of a bank failure, the System's deposits may not be returned. Massachusetts General Law Chapter 32, Section 23, limits the System's deposits "in a bank or trust company to an amount not exceeding ten percent of the capital and surplus of such bank or trust company." The System does not have a deposit policy for custodial credit risk.

As of December 31, 2011, $ 507,871 of the System's bank balance of $ 1,647,093 was exposed to custodial credit risk as uninsured, uncollateralized, and collateral held by pledging bank's trust department not in the System's name.

4. Investments

A. *Credit Risk*

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment.

Massachusetts General Law, Chapter 32, Section 23, limits the investment of System funds (to the extent not required for current disbursements) in the PRIT Fund or in securities (other than mortgages or collateral loans), which are legal for the investment of funds in savings banks under the laws of the Commonwealth, provided that no more than the established percentage of assets is invested in any one security.

Due to their nature, none of the System's investments are subject to credit risk disclosure. Fair value of the PRIT Fund is the same as the value of the pool share. The Pension Reserves Investment Trust (PRIT) was created under Massachusetts General Law, Chapter 32, Section 22, in

December 1983. The PRIT is operated under contract with a private investment advisor, approved by the Pension Reserves Investment Management Board.

B. <u>Custodial Credit Risk</u>

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g. broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The System's policy is to limit custodial credit risk by diversifying plan assets as described under <u>Asset Allocation</u> and <u>Management Structure</u> below.

C. <u>Concentration of Credit Risk</u>

Massachusetts General Law Chapter 32, Section 23 limits the amount the System may invest in any one issuer or security type, with the exception of the PRIT Fund. The System's policy with respect to asset allocation and management structure is as follows:

<u>Asset Allocation</u>

The Board of Trustees of the Retirement System originally adopted an asset allocation policy in 2002 and modified the policy in 2009 to the following. It should be noted that this is a target allocation policy and the Board of Trustees has the authority to override these targets if market conditions warrant such action.

	Percentages of Allocation			
	Target	Minimum	Maximum	Correponding Index
Diversified investments	60%	45%	75%	Customized
Domestic stocks	22.5%	12.5%	32.5%	Customized
Domestic bonds	12.5%	10%	15%	Barclays Aggregate Bond Index
Real estate	5%	0%	7.5%	NCREIF Real Estate Index

In February 2012 the System modified the asset allocation policy as follows:

Effective 2/29/12	Percentages of Allocation			
	Target	Minimum	Maximum	Correponding Index
Diversified investments	55%	45%	65%	Customized
Domestic stocks	27.0%	22.0%	32.0%	Customized
Domestic bonds	13.0%	10%	16%	Barclays Aggregate Bond Index
Real estate	5%	0%	7.5%	NCREIF Real Estate Index

Although cash is not included in the asset allocation of the Fund, the Trustees realize the need to provide liquidity to pay obligations as they come due. Surplus cash flows, additional contributions, and investment manager cash will be utilized to pay obligations of the Fund and periodic re-balancing of the assets. The Fund's investment manager(s) shall be kept informed of the liquidity requirements of the Fund, and to the extent possible, avoid untimely sales of assets which could be detrimental to the performance of the Plan.

Management Structure

To diversify plan assets so as to minimize the risk associated with dependence on the success of one enterprise, the Board of Trustees has decided to employ a multi-manager team approach to investing plan assets.

Investment managers will be employed to utilize individual expertise within their assigned area of responsibility. Each manager will be governed by individual investment guidelines. Separate manager guidelines for each investment manager shall serve as addenda to the Policy.

D. Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The System does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates; however, the System's investments consist of equities and pooled funds, neither of which has specified maturity dates. Consequently, none of the System's investments are subject to interest rate risk.

E. Foreign Currency Risk

Foreign currency risk is the risk that changes in foreign exchange rates will adversely affect the fair value of an investment. The System does not have policies for foreign currency risk.

5. Receivables

Amounts due from other entities are classified as follows:

Member Deductions and Makeup Payments: This balance represents employee member deductions and makeup payments for 2011 that were not received by the System until after year end.

State COLA Receivable: This balance represents a cost of living payment due from the Commonwealth as of December 31, 2011 and received after year end.

Accrued Interest and Dividends: This balance represents interest and dividends earned on investments as of December 31, 2011 and received after year end.

6. Prepaid Expenses

This balance represents fiscal year 2012 rent, administrative, and employee insurance expense paid in fiscal year 2011.

7. Accounts Payable

Accounts payable represents calendar year 2011 expenditures paid after December 31, 2011.

8. Employer Contributions Received In Advance

The balance in this account represents calendar year 2012 member assessments received before December 31, 2011.

9. Commitments And Contingencies

Litigation – There are several pending legal issues in which the System is involved. The System's management is of the opinion that the potential future settlement of some claims may result in gains to the System. However, the outcomes of these claims is uncertain.

10. Risk Management

The System is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the System carries commercial insurance. There were no significant reductions in insurance coverage from the previous year and have been no material settlements in excess of coverage in any of the past three fiscal years.

11. Net Asset Designations

The System's net assets are designated by the Retirement Board, in accordance with PERAC guidelines as follows:

	Balance at December 31	
	2011	2010
The *Annuity Savings Fund* is the fund in which members' contributions are deposited. Voluntary contributions, redeposits and transfers to and from other systems are also accounted for in this fund. Members' contributions to the fund earn interest at a rate determined by PERAC. Interest for some members who withdraw with less than ten years of service is transferred to the *Pension Reserve Fund*. Upon retirement, member's contributions and interest are transferred to the *Annuity Reserve Fund*. Dormant account balances must be transferred to the *Pension Reserve Fund* after a period of ten years of inactivity.	$ 24,574,861	$ 26,004,392
The *Annuity Reserve Fund* is the fund to which a member's account is transferred from the *Annuity Savings Fund* and *Military Service Fund* upon retirement. The annuity portion of the retirement allowance is paid from this fund. Interest is credited monthly to this fund at the rate of 3% annually, calculated on the previous month's balance.	8,197,683	6,766,401
The *Military Service Fund* contains contributions and interest for members while on a military leave for service in the Armed Forces who will receive creditable service for the period of that leave.	3,481	3,481
The *Pension Fund* contains the amounts appropriated by the governmental units as established by PERAC to pay the pension portion of each retirement allowance.	3,906,975	3,260,486
The *Pension Reserve Fund* contains the amounts appropriated by the governmental units for the purposes of funding future retirement benefits. Any profit or loss realized on the sale or maturity of any investment or on the unrealized gain of a market valued investment as of the valuation date is credited to the *Pension Reserve Fund*. Additionally, any investment income in excess of the amount required to credit interest to other fund balance accounts is credited to this reserve account.	45,359,905	45,361,656
	$ 82,042,905	$ 81,396,416

FRANKLIN REGIONAL RETIREMENT SYSTEM
REQUIRED SUPPLEMENTARY INFORMATION

Schedules of Funding Progress and Employer Contributions

Employer Contributions. Participating governmental entities are required to contribute at actuarially determined rates as accepted by PERAC.

The following schedules are presented in accordance with the Governmental Accounting Standards Board Statement 25.

Schedule of Funding Progress: (in thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b - a)/c]
01/01/10	$ 79,459	$ 119,349	$ 39,890	67%	$ 29,457	135%
01/01/08	77,859	105,972	28,113	73%	30,302	93%
01/01/06	61,539	91,823	30,284	67%	26,229	115%
01/01/03	41,299	72,770	31,471	57%	23,638	133%
01/01/01	42,002	57,235	15,233	73%	17,923	85%
01/01/98	41,568	64,535	22,967	64%	15,254	151%

Schedule of Employer Contributions:

Year Ended June 30	Annual Required Contribution	Percentage Contributed
2002	$ 2,484,787	100%
2003	3,186,298	100%
2004	3,340,859	100%
2005	3,923,420	100%
2006	4,127,192	100%
2007	4,295,275	100%
2008	4,487,246	100%
2009	4,645,462	100%
2010	4,789,021	100%
2011	5,093,076	100%

The required information presented above was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows.

Valuation date	1/1/10
Actuarial cost method	Entry Age Normal
Amortization method	Approximate level percent of payroll
Remaining amortization period	19 years

See Independent Auditor’s Report.

Asset valuation method	Market value adjusted by payables and receivables
Actuarial assumptions:	
Investment rate of return	7.875% per year
Projected salary increase	4.25% per year

See Independent Auditor’s Report.