



*Teachers'
Superannuation
Fund*

*Annual Report
2011-2012*





To His Honour,
the Honourable
H. Frank Lewis

Son Honneur,
L'honorable H. Frank Lewis

May it Please Your Honour:

Monsieur le lieutenant-
gouverneur,

In accordance with section 3 of the *Teachers' Superannuation Act*, I am pleased to present to you the Annual Report of the Prince Edward Island Teachers' Superannuation Commission for the plan year ended June 30, 2012.

Conformément à l'article 3 de la *Teachers' Superannuation Act*, j'ai l'honneur de vous présenter ce rapport annuel pour l'exercice terminé le 30 juin 2012.

Respectfully submitted
Your Obedient Servant,

Je vous prie d'agréer,
Madame la lieutenant-
gouverneure, l'expression
de ma haute considération.

A handwritten signature in dark ink, appearing to read "J. Alan McIsaac". The signature is fluid and cursive, with a long horizontal stroke at the beginning.

J. Alan McIsaac,
Minister of Education and Early Childhood Development
Ministre de l'Éducation et du Développement de la petite
enfance

Table of Contents

	Page
Introduction	1
Plan Description	1
Fund Administration	4
Highlights for 2011-2012	12
Teachers' Superannuation Commission	15
Master Trust Investment Advisory Committee	16
Audit Requirements	18
Contact Information	18
 Appendix	
Audited Financial Statements for 2011-2012	19

Introduction

The Teachers' Superannuation Fund (TSF) was established in 1931 and provides retirement income to members and the dependants of deceased members, in accordance with the *Teachers' Superannuation Act (TSA)*.

Plan Description

The TSF is a contributory, defined benefit pension plan financed by contributions from employees and employers, and by investment earnings from the Master Trust Investment Fund.

Contributions – In 2011-2012, members of the plan contributed the following:

- 7.30 percent of pensionable earnings up to the Yearly Maximum Pensionable Earnings (YMPE), and
- 9.00 percent of pensionable earnings in excess of the YMPE.

The YMPE was \$48,300 for 2011 and \$50,100 for 2012.

The employer matches contributions made by the members on a bi-weekly basis.

Membership – A teacher, as designated under the *School Act*, is eligible for membership. Substitute teachers are not eligible for membership.

Unreduced Pension – An unreduced monthly pension is payable for life to a member who meets one of the criteria below:

- has attained the age of 60 with two or more years of pensionable service;
- has attained the age of 55 with 30 or more years of pensionable service;
- has 35 or more years of pensionable service; or
- is deemed totally and permanently disabled and has two or more years of pensionable service.

The benefit is calculated as 2.0 percent multiplied by the years of pensionable service, multiplied by the average of the five highest years of pensionable earnings. Please note that for salary below the Canada Pension Plan's YMPE, the 2.0 percent benefit is comprised of:

- a) a 1.3 percent life-time benefit, and
- b) a 0.7 percent temporary bridge benefit, payable from the date of retirement to age 65.

Early Retirement – Eligible members can opt for an early retirement pension benefit as early as age 55. In these cases, the pension amount is reduced by the lesser of:

- a) 3.0 percent for each year prior to age 60, or
- b) 3.0 percent for each year prior to attaining 30 years of pensionable service.

It should be noted that the early retirement reduction is applied to both the life-time and bridge benefits, and remains in effect for their entire duration.

Benefits on Termination - A member in the TSF becomes vested after two years of pensionable service in the plan.

- a) Vested members are eligible for either a deferred pension or a refund of employee contributions plus interest.
- b) Non-vested members are eligible for a refund of employee contributions plus interest.

Inflation Protection – Pensions are increased by 60 percent of the change in the Consumer Price (all items) Index for Canada, to a maximum of 4.0 percent, on the first day of July of each year. The pension payment received upon retirement and the value of a deferred pension benefit are both indexed annually under the TSF. Indexation applied at July 1, 2011 was 1.10 percent.

Death Benefits – The TSF provides for both spousal and dependant benefits to eligible survivors of vested members.

Fund Administration

Administration of the TSA is assigned to the Pensions and Benefits Section of the Department of Finance, Energy and Municipal Affairs with investment management support provided by the Province of Prince Edward Island Master Trust.

The TSF's assets are managed independently by professional fund managers. The fund managers responsible for the TSF's investments at June 30, 2012 were:

Canadian Bonds

Beutel Goodman
MFS McLean Budden

Canadian Equities

Beutel Goodman
Burgundy Asset Management
MFS McLean Budden

Foreign Equities

Baillie Gifford Overseas Limited
Franklin Templeton
Lazard Asset Management

Real Estate Investment

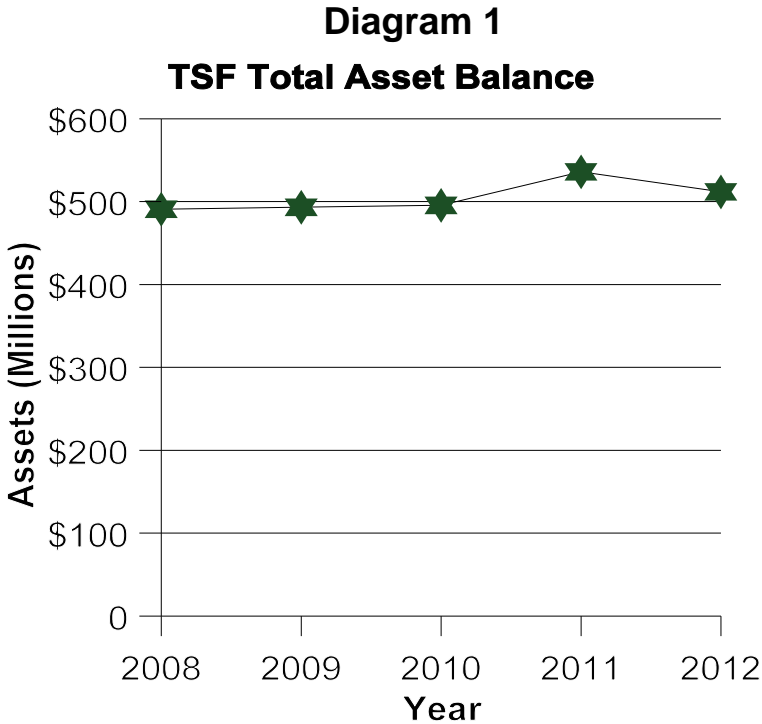
Bentall Kennedy (Canada) LP
Greystone Managed Investments Inc.

Currency Hedging

State Street Global Advisors

The total asset balance of the TSF at June 30, 2012 was approximately \$512 million, down from \$536 million at June 30, 2011.

Diagram 1 shows the TSF total asset balance from 2008 - 2012.

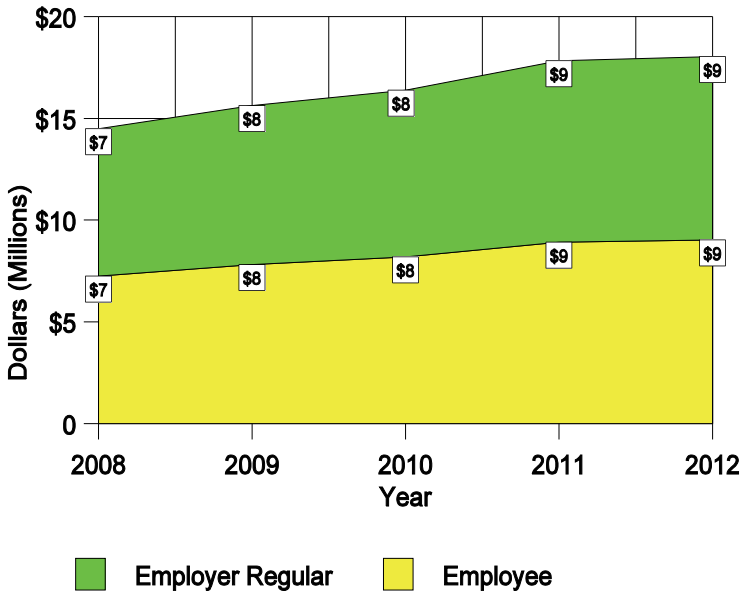


Employers – At June 30, 2012, there were four participating employers in the TSF with a total of 1,842 full- and part-time members. The PEI Teachers’ Federation accounted for four members. Additionally, 79 members were deferred at June 30, 2012.

Regular Contributions – Regular contributions are made to the TSF via payroll deductions. In 2011-2012, the regular contributions from both the employers and employees combined were approximately \$18.0 million, up from \$17.8 million in 2010-2011. Other contributions include special payments from the Province, payments for prior service, and transfers in from other plans via reciprocal agreements.

Diagram 2 depicts, by year, the regular employer and employee contributions made to the TSF from 2008 - 2012.

**Diagram 2
Regular Contributions**



Special Contribution - To help address the unfunded liability of the TSF, the Province of Prince Edward Island periodically makes special contributions to the TSF in the

form of a promissory note. There is currently one promissory note in place for which payments are being made.

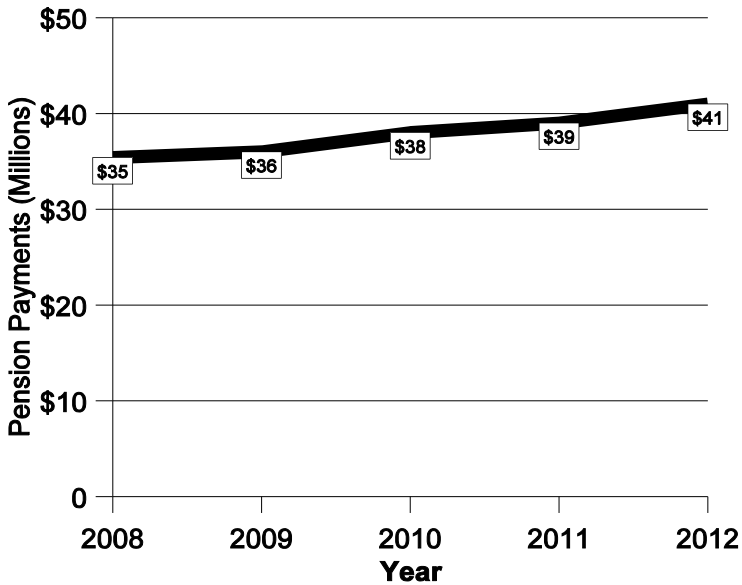
Beginning April 15, 2005, an investment of \$160 million was made to the Fund from the Province of Prince Edward Island. This note is receivable in ten equal, annual installments of \$16 million plus interest at the rate of 4.345 percent per annum. Interest is paid semi-annually on April 15 and October 15.

Pension Payments – Annual pension payments in 2011-2012 were approximately \$41 million. This is shown in **Diagram 3** on the next page.

Approximately 96 percent of the \$41 million pension payroll was paid to members and the remaining four percent was paid out as spousal and dependant benefits.

Pensioners – As of June 30, 2012, the number of persons receiving pension was 1,495. **Table 1**, on page 8, outlines the number of new pensioners, their average age and average annual pension for the most recent fiscal years.

Diagram 3 Pension Payments



**Table 1
Number of New Pensioners with
Average Age and Average Annual Pension**

Fiscal Year	No. of New Pensioners	Average Age	Average Annual Pension
2011-2012	64	59.42	\$ 33,246
2010-2011	56	58.21	\$ 36,332
2009-2010	48	57.58	\$ 37,315
2008-2009	26	56.94	\$ 32,267
2007-2008	41	57.06	\$ 35,575

Table 2 outlines the various categories of pension recipients along with the average annual pension for each category as at June 30th.

**Table 2
Pension Categories and
Average Annual Pension**

Category	Number of Pensions		Average Annual Pension	
	2012	2011	2012	2011
Members	1,329	1,288	\$ 28,582	\$ 28,370
Disability Pensions	46	48	\$ 20,465	\$ 19,147
Spousal	105	94	\$ 14,063	\$ 13,815
Dependants	15	16	\$ 3,122	\$ 3,111
Total Pensions	1,495	1,446		

Actuarial Requirement – Federal legislation requires that an actuarial valuation be performed once every three years to evaluate the funding status of the TSF. Actuarial valuation reports require best estimate assumptions about future events to determine the liabilities of the Fund as of the valuation date. The actual assets of the Fund, as of the valuation date, are then compared to the liabilities to determine the plan's funding status.

The most recent actuarial valuation was completed as of July 1, 2011. This valuation was based on the following membership data:

- 1) 1,888 Active Members
Average salary of \$67,256
Average age of 41.8 years
- 2) 1,485 Pensioners
Average annual pension of \$27,257
Average age of 68.9 years
- 3) 66 Deferred Pensioners
Average annual pension of \$8,669
- 4) 469 Inactives
Estimated average contributions with interest of \$3,394

The value of the Plan assets as at July 1, 2011 was \$534,623,000, which represents 76.9 percent of the actuarial liability of \$695,560,000.

Table 3 details the actuarial valuation statement of financial position as at July 1, 2011.

Table 3
Going-Concern Financial Position
July 1, 2011

Value of Assets		
Market Value	\$ 534,623,000	
	Actuarial Liability	Percentage of Total Liabilities
Active Members	\$ 264,607,000	38%
Inactives and Deferred Vested Members	5,309,000	1%
Pensioners and Beneficiaries	425,644,000	61%
Total	\$ 695,560,000	
Actuarial Surplus (Unfunded Liability)	\$ (160,937,000)	
Funding Ratio	76.9%	

Highlights for 2011-2012

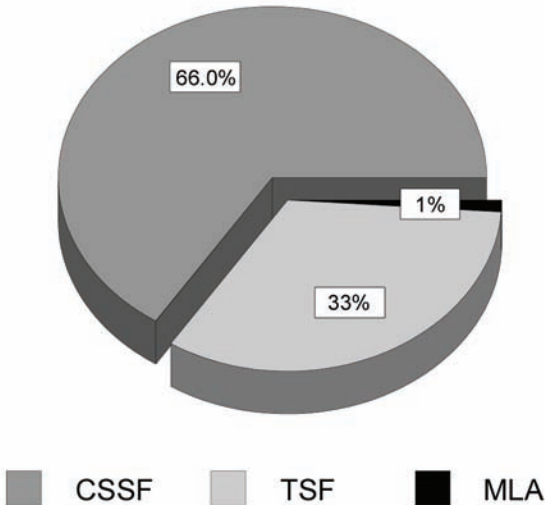
Investment Management

The largest contributor to the growth of TSF assets is normally investment income. These investments are held in the Province of Prince Edward Island Master Trust. The TSF, MLA Pension Fund and Civil Service Superannuation Fund participate in the Master Trust. In 2011-2012, approximately 33 percent of the funds in the Master Trust were assets of the TSF. An overview of the Master Trust at June 30, 2012 is shown below in **Diagram 4**.

As of June 30, 2012, the rate of return of the Master Trust was as follows:

- Annual rate of return: -0.50 %
- Ten year rate of return: 5.10 %

Diagram 4
Master Trust Investments



TSF Assets

During 2011-2012, there was a net decrease to TSF assets of approximately \$25 million (the difference between Table 4 and Table 5).

Table 4 shows the receipts and income, by source, which totalled approximately \$19 million.

Table 4
Receipts and Income

Type	Amount
Employee Contributions	\$ 9,018,973
Employer Contributions	9,018,776
Transfer from Other Plans	402,954
Purchased Service	383,927
Interest Income	1,955,804
Market Value Decrease	(1,853,042)
Total	\$ 18,927,392

Table 5 shows the expenditures for 2011-2012, which totalled approximately \$44 million.

Table 5
TSF Expenditures

Type	Amount	% of Expenditures
Benefits Paid	\$ 40,553,991	
Refunds	117,471	
Transfers	904,529	
Total Benefit Expenses	\$ 41,575,991	94.85%
Benefit Administration	\$ 246,741	
Pension System Fees	34,081	
Investment Administration	53,647	
Total Administrative Expenses	\$ 334,469	0.76%
Consulting Fees	122,495	
Total Consulting Fees	\$ 122,495	0.28%
Manager Fees	\$ 1,660,520	
Monitoring Fees	77,407	
Custodial Fees	64,728	
Total Investment Expenses	\$ 1,802,655	4.11%
Total	\$ 43,835,610	100.00%

Teachers' Superannuation Commission

The TSA is administered by the Teachers' Superannuation Commission. The seven-member Commission consists of the following representatives at June 30, 2012:

No of Members	Member	
1	<i>Chairperson - Deputy Minister of Education & Early Childhood Development</i>	Dr. Alexander (Sandy) MacDonald
2	Department of Education & Early Childhood Development	Gordon MacFadyen Terry Keefe
3	PEI Teachers' Federation	Michel Plamondon Blaine Bernard Denise Gaudet-McPhail
1	Department of Finance, Energy and Municipal Affairs	Vacant

Master Trust Investment Advisory Committee

The Master Trust Investment Advisory Committee provides advice to the Minister of Finance, Energy and Municipal Affairs on the following items:

- protection of the principal assets of the Master Trust;
- monitoring of costs;
- recommendations on investment fund asset mix;
- review of investment fund and fund manager performance standards; and
- compliance with both federal and provincial requirements relating to ownership of foreign equities.

At June 30, 2012, the following were members of the Master Trust Investment Advisory Committee:

Chairperson - Comptroller, Treasury Board Secretariat	Doug Clow
Canadian Union of Public Employees	Leonard Gallant
International Union of Operating Engineers	Gerald Poirier
Member of the Legislative Assembly	Francis (Buck) Watts
PEI Nurses' Union	Susan Marchbank
PEI Teachers' Federation	Michel Plamondon
Provincial Government	Terry Hogan Gordon MacFadyen
Union of Public Sector Employees	Karen Jackson (acting) Donalda Docherty
Ex Officio Outside Designates - Fiscal Agents	Tim Van Alstyne, <i>RBC Dominion Securities Inc.</i> Bill Hastie, <i>Scotia Capital Inc.</i>
Ex Officio Outside Designates - Consultants	Paul Malizia and Tony Politano, <i>Aon Hewitt</i>

Audit Requirements

In accordance with section 31 of the *Teachers' Superannuation Act*, the financial statements have been examined by the Office of the Auditor General whose report is included in the appendix of this annual report.

Contact Information

For further information concerning the administration of the ***Teachers' Superannuation Act***, please contact:

Pensions and Benefits

Department of Finance, Energy and Municipal Affairs

3rd floor Sullivan Building, 16 Fitzroy Street

PO Box 2000

Charlottetown, PE C1A 7N8

Telephone: (902) 368-4200

Fax: (902) 620-3096

Terry Hogan, Manager

Crystal Burrows, Operations Supervisor

Pamela MacEachern, a/Pension Information Officer

For further information concerning the **Master Trust Fund** contact:

Alan Silliker, Manager

Debt, Investments and Pensions

Department of Finance, Energy and Municipal Affairs

Office of the Comptroller

Tel: (902) 569-7666

Appendix

Audited Financial Statements
for 2011-2012

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Financial Statements
June 30, 2013



Prince Edward Island Île-du-Prince-Édouard

Office of the
Auditor General

PO Box 2000, Charlottetown PE
Canada C1A 7N8

Bureau du
vérificateur général

C.P. 2000, Charlottetown PE
Canada C1A 7N8

September 29, 2014

Dr. Alexander MacDonald
Chair
Teachers' Superannuation Commission
Department of Education and Early Childhood Development
Province of Prince Edward Island

Dear Dr. MacDonald:

Enclosed is a copy of the financial statements of the **Prince Edward Island Teachers' Superannuation Fund** for the years ended June 30, 2012 and 2013.

If you have any questions, please do not hesitate to contact my Office.

Yours truly,

B. Jane MacAdam, CA
Auditor General

BJM/ts
Enclosure

cc: Hon. J. Alan McIsaac
Hon. Wesley J. Sheridan
Mr. David Arseneault, FCA
Mr. Terry Hogan ✓
Mr. Gordon MacFadyen, CPA, CA
Mr. Dan Campbell, CFA

Management's Report

Management's Responsibility for the Financial Statements

The financial statements have been prepared by management in accordance with Canadian accounting standards for pension plans and the integrity and objectivity of these statements are management's responsibility. Management is responsible for the notes to the financial statements and for ensuring that this information is consistent, where appropriate, with the information contained in the financial statements.

Management is responsible for implementing and maintaining a system of internal control to provide reasonable assurance that reliable financial information is produced.


The Teachers' Superannuation Commission is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Commission reviews internal financial reports on a regular basis and externally audited financial statements yearly.

The Auditor General conducts an independent examination, in accordance with Canadian generally accepted auditing standards and expresses her opinion on the financial statements. The Auditor General has full and free access to financial information and management of the Prince Edward Island Teachers' Superannuation Fund to meet as required.

On behalf of the Prince Edward Island Teachers' Superannuation Fund



Mr. David Arsenault, FCA
Deputy Minister, Department of Finance,
Energy and Municipal Affairs



Mr. Terry Hogar
Manager, Pension and Benefits

September 24, 2014



Prince Edward Island Île-du-Prince-Édouard

Office of the
Auditor General
PO Box 2000, Charlottetown PE
Canada C1A 7N8

Bureau du
vérificateur général
C.P. 2000, Charlottetown PE
Canada C1A 7N8

INDEPENDENT AUDITOR'S REPORT

To the Commissioners of the Prince Edward Island Teachers' Superannuation Fund

I have audited the financial statements of the **Prince Edward Island Teachers' Superannuation Fund** which comprise the statement of financial position as at July 1, 2011, June 30, 2012 and 2013, and the statements of changes in net assets available for benefits and changes in pension obligation for the 2012 and 2013 years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian accounting standards for pension plans and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audits. I conducted the audits in accordance with Canadian generally accepted auditing standards. Those standards require that I comply with ethical requirements and plan and perform the audits to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall financial statement presentation.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the financial statements present fairly, in all material respects, the financial position of the Fund as at July 1, 2011, June 30, 2012 and 2013, and the changes in its net assets and pension obligation for the 2012 and 2013 years then ended in accordance with Canadian accounting standards for pension plans.

B. Jane MacAdam, CA
Auditor General

Charlottetown, Prince Edward Island
September 24, 2014


**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**


Statement of Financial Position
June 30, 2013

	2013	2012	July 1, 2011
	\$	\$	\$
Assets			
Cash	5,393,906	4,862,771	3,210,004
Investments (Note 3)	538,608,981	474,351,041	482,971,869
Notes receivable (Note 5)	88,332,100	32,000,000	48,000,000
Receivables			
Contributions - employee	22,283	13,937	669,126
- employer	71,100	107,996	746,495
Accrued interest	665,901	288,717	433,075
Other	<u>198,310</u>	<u>237,380</u>	<u>125,689</u>
Total Assets	<u>633,292,581</u>	<u>511,861,842</u>	<u>536,156,258</u>
Liabilities			
Accounts payable and accrued liabilities	75,288	552,748	48,041
Income taxes payable	571,468	556,206	537,173
Investment fees payable	674,023	564,433	502,000
Other remittances payable	224,348	236,363	242,500
Due to the Province of Prince Edward Island	<u>229,116</u>	<u>237,606</u>	<u>203,840</u>
Total Liabilities	<u>1,774,243</u>	<u>2,147,356</u>	<u>1,533,554</u>
Net Assets Available for Benefits	<u>631,518,338</u>	<u>509,714,486</u>	<u>534,622,704</u>
Accrued Pension Obligation (Note 4)	<u>716,450,180</u>	<u>653,890,261</u>	<u>634,127,504</u>
Net Deficit	<u>84,931,842</u>	<u>144,175,775</u>	<u>99,504,800</u>

(The accompanying notes are an integral part of these financial statements.)

Approved on behalf of the Commission


Chair


Commissioner

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Statement of Changes in Net Assets Available for Benefits
for the year ended June 30, 2013

	2013	2012
	\$	\$
Increase in Assets		
Investment income (Note 3(a))		
Interest	5,614,539	6,784,798
Dividends	8,428,523	9,130,045
Change in fair value of investments	<u>47,535,557</u>	<u>(17,767,885)</u>
	61,578,619	(1,853,042)
Other interest income	4,115,822	1,955,804
Contributions		
Employee	9,948,453	9,018,973
Employer	9,949,353	9,018,776
Transfers from other plans	857,639	402,954
Purchased service	343,783	383,927
Government contribution towards unfunded liability (Note 5)	<u>80,369,000</u>	<u>-</u>
	<u>167,162,669</u>	<u>18,927,392</u>
Decrease in Assets		
Benefits paid	41,749,836	40,553,991
Operating expenses (Note 6)	2,911,751	2,259,619
Refunds	227,937	117,471
Transfers	<u>469,293</u>	<u>904,529</u>
	<u>45,358,817</u>	<u>43,835,610</u>
Change in Net Assets	121,803,852	(24,908,218)
Net Assets Available for Benefits, beginning of year	<u>509,714,486</u>	<u>534,622,704</u>
Net Assets Available for Benefits, end of year	<u>631,518,338</u>	<u>509,714,486</u>

(The accompanying notes are an integral part of these financial statements.)

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Statement of Changes in Pension Obligation
for the year ended June 30, 2013

	2013	2012	July 1, 2011
	\$	\$	\$
Accrued Pension Obligation, beginning of year	<u>653,890,261</u>	<u>634,127,504</u>	<u>597,346,018</u>
Change in Accrued Pension Obligation			
Interest accrued on benefits	47,227,123	45,776,587	45,181,756
Benefits accrued	15,069,551	14,775,281	13,606,794
Increase due to purchase service	1,201,422	786,881	1,064,220
Changes in actuarial assumptions	41,508,889	-	16,051,376
Benefits paid	<u>(42,447,066)</u>	<u>(41,575,992)</u>	<u>(39,122,660)</u>
Change in Accrued Pension Obligation	<u>62,559,919</u>	<u>19,762,757</u>	<u>36,781,486</u>
Accrued Pension Obligation, end of year (Note 4)	<u>716,450,180</u>	<u>653,890,261</u>	<u>634,127,504</u>

(The accompanying notes are an integral part of these financial statements.)

PRINCE EDWARD ISLAND TEACHERS' SUPERANNUATION FUND

Notes to Financial Statements
June 30, 2013

1. Plan Description

The following description of the Prince Edward Island Teachers' Superannuation Pension Plan (the Plan) is a summary only. For more complete information, reference should be made to the *Teachers' Superannuation Act and Regulations*.

a) General

The Plan is a contributory defined benefit plan covering members as defined in the *Teachers' Superannuation Act*.

b) Contributions

Under the Plan, employees and the employers contribute equally at a rate of 7.3 percent of that part of the members salary up to the amount of the year's maximum pensionable earnings (YMPE) as defined in the *Canada Pension Plan Act* and 9.0 percent on the amount that exceeds the YMPE.

Effective January 1, 2013, contribution rates for the Plan increased to 8.3 percent of pensionable earnings up to and including the YMPE and 10.0 percent of pensionable earnings above the YMPE.

c) Retirement Benefits

A member who has attained the age of 60 and has completed at least two years of pensionable service, or has attained the age of 55 and has completed 30 years of pensionable service, or has completed 35 years of pensionable service is entitled to an unreduced pension which is payable in equal monthly installments.

The annual amount of the pension is equal to two percent of the average of the five highest years pensionable salary multiplied by the number of years of pensionable service. When the member reaches the age of 65 (or if he or she is 65 or over at retirement) the amount of pension described above is integrated with the Canada Pension Plan. The pension is reduced by 0.7 percent of the average salary up to the average YMPE during the five year period over which the average salary has been computed, multiplied by the number of years of the member's pensionable service after July 1, 1972.

Reduced benefits are available at age 55 with at least two years of pensionable service. The pension for a member who retires prior to age 60 (and who is not entitled to an unreduced pension) is calculated as described in the previous paragraph but then is reduced by 0.25 percent for each full month by which the early retirement date precedes the member's earliest unreduced retirement age.

The above formula determines the amount of a member's initial pension at retirement. In subsequent years, the amount of a member's pension is increased by 60 percent of the percentage increase in the Consumer Price Index. The increase in any one year is limited to no more than four percent.

PRINCE EDWARD ISLAND TEACHERS' SUPERANNUATION FUND

Notes to Financial Statements
June 30, 2013

1. Plan Description (continued...)

d) Disability Benefits

Disability benefits are available at any age to a member who retires from teaching service because of total and permanent disability provided the member contributed to the Plan for two or more years.

e) Death Benefits

On the death of a member prior to completing two years of pensionable service, or after completing two years of service but leaving no surviving spouse or dependant children, the member's accumulated contributions with interest will be refunded. If a member dies prior to retirement but after completing two years of service, the member's spouse is entitled to an immediate pension equal to 60 percent of the accrued, unreduced pension of the member at the time of death. In addition to the spousal pension, an allowance equal to one quarter of the remaining 40 percent of pension is payable in respect of each dependent child until the child attains the age of 16 or until the age of 25 if the child is attending school full-time. In no case shall payment to such children exceed 75 percent of the remaining 40 percent of pension.

f) Termination and Portability of Benefits

In the event of termination of employment for reasons other than retirement or death, a member may elect to receive either:

- a refund of the member's own contributions with interest; or
- if the member has completed at least two years of service, a deferred unreduced pension commencing when the member attains the age of 60.

Where there are portability arrangements between the Plan and other plans, members may be able to carry certain pension benefits to those other plans or transfer contributions and service from those other plans to increase pension benefits under the Plan.

g) Marriage Breakdown

Upon application, the pension benefits to which a person is entitled may be divided between the person and the spouse or former spouse.

h) Income Tax

The Fund is a Registered Pension Plan as defined under the federal *Income Tax Act* and is not subject to taxation.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

2. Summary of Significant Accounting Policies

Basis of Accounting

The financial statements for the year ended June 30, 2013, have been prepared in accordance with Canadian accounting standards for pension plans as outlined in the Chartered Professional Accountants of Canada (CPA) Handbook Section 4600, Pension Plans. For accounting policies that do not relate to either investments or pension obligations, the Fund has elected to comply on a consistent basis with accounting standards for private enterprises (ASPE) in Part II of the CPA Handbook. To the extent that ASPE in Part II is inconsistent with Section 4600, Section 4600 takes precedence. Prior periods financial statements were prepared in accordance with Canadian generally accepted accounting principles for the private sector. The adoption of accounting standards for pension plans has been applied retroactively. The application of the new accounting framework did not affect previously reported results. Impacts on the financial statements were limited to presentation and disclosure.

These financial statements are prepared on a going concern basis and present the aggregate financial position of the Fund as a separate reporting entity.

a) Use of Estimates and Measurement Uncertainty

The preparation of financial statements in conformity with Canadian accounting standards for pension plans requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of the revenues and expenses during the period. Items requiring the use of significant estimates include investments, accrued interest, accrued liabilities, and the accrued pension obligation.

Estimates are based on the best information available at the time of preparation of the financial statements and are reviewed annually to reflect new information as it becomes available. Measurement uncertainty exists in these financial statements. Actual results could differ from these estimates and the differences could be material.

b) Foreign Currency Translation

Transactions denominated in foreign currencies are translated into Canadian dollars at the rate of exchange prevailing on the transaction date. The fair value of foreign investments and cash held at year-end are translated at the rates in effect at that date. The resulting gain or loss from changes in these rates is included in the current period change in fair value of investments.

c) Fair Value Measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

PRINCE EDWARD ISLAND TEACHERS' SUPERANNUATION FUND

Notes to Financial Statements
June 30, 2013

2. Summary of Significant Accounting Policies (continued...)

c) Fair Value Measurement (continued...)

When available, the Fund measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, then the Fund establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same and/or discounted cash flow analysis.

d) Financial Instruments

The Fund's financial instruments include cash, contributions and other receivables, accrued interest, notes receivable, investments, accounts payable, accrued liabilities, amounts due to the Province of Prince Edward Island, income taxes payable, investment fees payable, and other remittances payable. Due to their nature, the Fund's financial instruments, with the exception of investments, are carried at cost which approximate their fair values. Investments are carried at fair value and are subject to interest, credit, currency, price, and liquidity risks as described in Note 3.

e) Investments

Investments represent a pool of assets held in a master trust and allocated to each member by units of participation. The Prince Edward Island Master Trust represents a contract between the members (contributors) and the trustee (Minister of Finance, Energy and Municipal Affairs). All investments held by the Master Trust are classified as held for trading. Investments are designated at fair value through the statement of changes in net assets available for benefits. Investment purchase and sale decisions are based on their fair value in accordance with the Master Trust's Statement of Investment Policies and Procedures. Significant accounting policies for the pool of assets held in the Master Trust consist of:

(i) Investment transactions

Investment transactions are recognized on the transaction date. Distributions are recognized on the record date. Investments include receivables and payables at June 30, 2013, for interest, dividends, and settled derivative contracts.

(ii) Income recognition

Income from investments is recorded on an accrual basis and includes interest and dividends as well as gains and losses that have been realized on disposal of investments and the unrealized gains and losses on investments.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

2. Summary of Significant Accounting Policies (continued...)

e) Investments (continued...)

(iii) Investment valuation

Equity and debt

Equity and debt investments are valued at fair value based on quoted market value. Changes in the market value of investments, including realized and unrealized gains and losses, are reflected in the financial statements as a change in the fair value of investments.

Equity investment in real estate

Investment in real estate is represented by an equity investment in a corporation that invests in real estate, participating mortgages, and property for development or resale. Properties within the corporation are valued annually by independent appraisers in accordance with generally accepted appraisal practices and procedures. The appraisal methodology followed is an income approach which is mainly based on discounted cash flows. In estimating future cash flows, certain assumptions are made with respect to future economic conditions and rates of return.

Pooled funds

Pooled funds are valued at the unit values supplied by the pooled fund administrator, which represents the Fund's proportionate share of underlying net assets at fair values determined using closing market prices.

Derivative contracts

The derivative contracts held by the Fund are stated at fair value and are valued using quoted market indices. Realized and unrealized gains or losses on investments from derivative contracts are included in the change in the fair value of investments.

Investment in foreign infrastructure

The Fund owns units in a foreign infrastructure partnership. The partnership invests in portfolio companies that own, operate, develop, manage and support infrastructure assets. Fair value is based upon a number of factors, including readily available market quotes with appropriate adjustments for trading restrictions, the most recent round of financings, earnings-multiple analysis using comparable companies or discounted cash flow analysis.

(iv) Transaction costs

Investment management fees are costs directly attributable to the external management of the assets. Fees incurred on the management of equity holdings in real estate are paid directly as a reduction in the fair value of the investment. Fees incurred on the management of other investments are recorded as an investment expense.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

2. Summary of Significant Accounting Policies (continued...)

f) Revenue and Expenses

Revenue and expenses are recorded on an accrual basis in the period in which the transaction or event that gave rise to the revenue or expense occurred.

g) Accrued Pension Obligation

The value of the accrued pension obligation of the Fund is based on a tri-annual actuarial valuation prepared on an accounting basis by an independent actuary using the projected unit credit method pro-rated on service and best estimate assumptions. The accrued pension obligation is measured in accordance with accepted actuarial methods using actuarial assumptions and methods adopted by the Fund. An estimated update, which is calculated based on an extrapolation of the most recent valuation, is calculated by management at the end of each fiscal year.

h) Net Deficit

For financial statement reporting, the deficit of the Fund is based on the difference between the fair value of the Fund's net assets available for benefits and the Fund's accrued pension obligation.

3. Investments and Derivatives

a) Investments

Investments consist of units held in the Master Trust. At year-end, there were 412,713,451 units held in the Master Trust (2012 - 395,295,128) with a fair value of \$1,305.04 (2012 - \$1,199.99) per unit.

Investments of the Master Trust consist of the following listed assets:

	<u>2013</u>	<u>%</u>	<u>2012</u>	<u>%</u>
	\$		\$	
Canadian short-term investments	13,104,205	0.7	14,552,044	1.0
Other liquid assets	9,862,402	0.6	4,184,513	0.3
Bonds, debentures, and notes	484,552,200	29.6	511,818,601	35.7
Canadian equity securities	363,807,347	22.2	320,743,904	22.5
Equity investments in real estate	79,174,462	4.8	50,723,230	3.6
Foreign equity securities	678,031,664	41.4	521,784,333	36.5
Foreign infrastructure	12,698,150	0.8	-	-
Currency forwards	(5,377,295)	(0.3)	1,262,122	0.1
Accrued income	<u>3,723,006</u>	<u>0.2</u>	<u>4,662,301</u>	<u>0.3</u>
Total	<u>1,639,576,141</u>	<u>100.0</u>	<u>1,429,731,048</u>	<u>100.0</u>
Fund's pro-rated share	<u>32.8505%</u>		<u>33.1776%</u>	
Fund investments **	<u>538,608,981</u>		<u>474,351,041</u>	

** Rounded

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

a) Investments (continued...)

Investment income and realized and unrealized gains (losses) of the Master Trust consist of the following:

	Investment Income (Losses) <u>2013</u> \$	Realized/ Unrealized Gains (Losses)* <u>2013</u> \$	Investment Income <u>2012</u> \$	Realized/ Unrealized Gains (Losses)* <u>2012</u> \$
Canadian short-term investments	(9,471)	423	136,156	-
Other liquid assets	186,678	(705,160)	73,614	(41,295)
Bonds, debentures and notes	16,937,523	(16,378,517)	20,144,970	24,552,622
Canadian equity securities	12,460,694	34,921,888	13,011,038	(48,889,105)
Foreign equity securities	13,256,333	124,176,372	14,671,749	(27,617,208)
Equity investments in real estate	-	4,969,763	-	2,508,089
Foreign infrastructure	-	2,273,116	-	-
Currency forwards	-	(6,640,908)	-	(2,386,464)
Total	<u>42,831,757</u>	<u>142,616,977</u>	<u>48,037,527</u>	<u>(51,873,361)</u>
Fund's pro-rated share	<u>32.7866%</u>	<u>33.3309%</u>	<u>33.1300%</u>	<u>34.2524%</u>
Fund investments **	<u>14,043,062</u>	<u>47,535,557</u>	<u>15,914,843</u>	<u>(17,767,885)</u>

* Includes realized gains of \$15.0 million (2012 - losses of \$1.2 million) and unrealized gains of \$127.6 million (2012 - losses of \$50.7 million).

** Rounded

Investments include amounts which investment managers of the Master Trust have invested in their own pooled funds. The fair values of these investments are as follows:

	<u>2013</u> \$	<u>2012</u> \$
Beutel Goodman & Company Ltd.	16,665,115	16,155,609
Lazard Ltd.	218,349,527	177,249,820
Baillie Gifford Overseas Ltd.	229,391,757	173,336,402
Bentall Kennedy	42,802,727	39,218,446
Greystone Real Estate Fund Inc.	36,371,537	11,050,679
Global Infrastructure Partners	<u>12,698,150</u>	-
Total	<u>556,278,813</u>	<u>417,010,956</u>
Fund's pro-rated share	<u>32.8505%</u>	<u>33.1776%</u>
Fund's pooled funds	<u>182,740,371</u>	<u>138,354,226</u>

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

b) Derivative Contracts

Derivative contracts are financial contracts, the value of which is "derived" from the value of underlying assets or exchange rates. Derivative contracts provide flexibility in implementing investment strategy.

Forward contracts are used to manage currency exposure and mitigate risk with respect to investments held in foreign currencies. The net notional amount of the currency forwards represents the volume of outstanding transactions and serves as the basis upon which the return and market value of the contract is determined.

The following provides details of derivative contracts outstanding as of June 30, 2013.

	<u>2013</u> \$	<u>2012</u> \$
Notional Amount	<u>243,208,459</u>	<u>175,077,790</u>
Fair Value	<u>(5,377,295)</u>	<u>1,262,122</u>

c) Fair Value Disclosure

Fund investment assets recorded at fair value have been categorized based upon a fair value hierarchy on significant inputs used in measuring fair value. The following fair value hierarchy table presents information about the Fund's assets measured at fair value on a recurring basis at June 30, 2013.

The three levels of the fair value hierarchy are as follows:

Level 1: Inputs that reflect unadjusted quoted prices in active markets for identical assets or liabilities that the investment manager has the ability to access at the measurement date. Level 1 primarily includes publicly listed investments.

Level 2: Inputs other than quoted prices that are observable either directly or indirectly, including inputs in markets that are not considered to be active. Level 2 primarily includes debt securities and derivative contracts not traded in an open market.

Level 3: Inputs that are unobservable. There is little, if any, market activity. Inputs into the determination of fair value require significant management judgement and/or estimation. Level 3 primarily consists of MAV II notes as described in Section (e) of this note and foreign infrastructure investments.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

c) Fair Value Disclosure (continued...)

The following table illustrates the classifications of the Fund's financial instruments using the fair value hierarchy as at June 30.

	2013			Total \$
	Level 1 \$	Level 2 \$	Level 3 \$	
Canadian short-term investments	4,708,903	8,395,302	-	13,104,205
Other liquid assets	9,862,402	-	-	9,862,402
Bonds, debentures, and notes	-	464,623,221	19,928,979	484,552,200
Canadian equity securities	363,807,347	-	-	363,807,347
Foreign equity securities	678,031,664	-	-	678,031,664
Equity investments in real estate	-	79,174,265	197	79,174,462
Foreign infrastructure	-	-	12,698,150	12,698,150
Currency forwards	-	(5,377,295)	-	(5,377,295)
Totals	<u>1,056,410,316</u>	<u>546,815,493</u>	<u>32,627,326</u>	1,635,853,135
Accrued income				<u>3,723,006</u>
Total financial assets at fair value				1,639,576,141
Fund's pro-rated share				<u>32.8505%</u>
Fund investments*				<u>538,608,981</u>

	2012			Total \$
	Level 1 \$	Level 2 \$	Level 3 \$	
Canadian short-term investments	9,566,262	4,985,782	-	14,552,044
Other liquid assets	4,184,513	-	-	4,184,513
Bonds, debentures and notes	-	491,651,756	20,166,845	511,818,601
Canadian equity securities	320,743,904	-	-	320,743,904
Foreign equity securities	521,784,333	-	-	521,784,333
Equity investments in real estate	-	50,723,033	197	50,723,230
Currency forwards	-	1,262,122	-	1,262,122
Totals	<u>856,279,012</u>	<u>548,622,693</u>	<u>20,167,042</u>	1,425,068,747
Accrued income				<u>4,662,301</u>
Total financial assets at fair value				1,429,731,048
Fund's pro-rated share				<u>33.1776%</u>
Fund investments*				<u>474,351,041</u>

* Rounded

There were no significant transfers between level 1 and level 2 financial instruments during the years ended June 30, 2013 or 2012.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

c) Fair Value Disclosure (continued...)

The following table details changes in fair value measurement in Level 3 of the fair value hierarchy:

	<u>Fixed Income</u> \$	<u>Equity</u> \$	<u>Foreign Infrastructure</u> \$	<u>Total</u> \$
Level 3 investments, July 1, 2012	20,166,845	197	-	20,167,042
Net purchases (sales)	(237,866)	-	10,425,034	10,187,168
Realized gains	-	-	36,395	36,395
Unrealized gains	-	-	<u>2,236,721</u>	<u>2,236,721</u>
Total financial assets at fair value	<u>19,928,979</u>	<u>197</u>	<u>12,698,150</u>	32,627,326
Fund's pro-rated share				<u>32.8505%</u>
Level 3 investments, June 30, 2013				<u>10,718,240</u>

	<u>Fixed Income</u> \$	<u>Equity</u> \$	<u>Total</u> \$
Level 3 investments, July 1, 2011,	17,401,664	197	17,401,861
Unrealized gains	<u>2,765,181</u>	-	<u>2,765,181</u>
Total financial assets at fair value	<u>20,166,845</u>	<u>197</u>	20,167,042
Fund's pro-rated share			<u>33.1776%</u>
Level 3 investments, June 30, 2012			<u>6,690,941</u>

d) Investment Risk Management

Risk management relates to the understanding and active management of risks associated with all areas of the business and the associated operating environment. Investments are primarily exposed to foreign currency, interest rate volatility, market price fluctuations, credit risk, and liquidity risk. The Fund has set formal goals, policies, and operating procedures that establish an asset mix among equity and fixed income, required diversification of investments within categories, and set limits on the size of exposure to individual investments and counter parties. Risk and credit considerations are periodically assessed in consultation with external consultants, the Department of Finance, Energy and Municipal Affairs, and the Master Trust Investment Advisory Committee. Plan sponsor oversight, procedures, and compliance functions are incorporated into Fund processes to achieve consistent controls and to mitigate operational risk.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

d) Investment Risk Management (continued...)

(i) Interest Rate Risk

Interest rate risk refers to the fact that the Fund's financial position will change with market interest rate changes as fixed income securities are sensitive to changes in nominal interest rates. Interest rate risk is inherent in the management of a pension plan due to prolonged timing differences between cash flows related to the Fund's assets and liabilities.

Assuming all other variables are held constant, a one percentage point change in nominal interest rates would change the fair value of the Fund by \$8.9 million.

	<u>Value of Fixed Income Securities</u> \$	<u>Weighted Average Duration</u> yrs	<u>Percentage Point Change</u> %	<u>Impact on Fair Value of the Master Trust</u> \$	<u>Fund's Pro-rated Share</u> %	<u>Pro-rated Impact on Fair Value of the Fund</u> \$
2013	464.6 m	5.80	1	26.9 m	32.8505	8.9 m
2012	491.7 m	5.78	1	28.4 m	33.1776	9.4 m

(ii) Price Risk

Price risk is the risk of fluctuation in market values of investments from influences specific to a particular investment or from influences on the market as a whole. Price risk includes interest rate risk and foreign currency risk. Market price risk is managed by the Fund through the use of diversified investment portfolios traded on various markets and across various industries. Assuming all other variables are held constant, a ten percent change in market values of all public equities would change the fair value of the Fund by \$37.9 million.

	<u>Value of Public Equities</u> \$	<u>Percentage Change</u> %	<u>Impact on Fair Value of the Master Trust</u> \$	<u>Fund's Pro-rated Share</u> %	<u>Pro-rated Impact on Fair Value of the Fund</u> \$
2013	1,121.0 m	10	112.1 m	32.8505	36.8 m
2012	893.3 m	10	89.3 m	33.1776	29.6 m

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

d) Investment Risk Management (continued...)

(iii) Credit Risk

Credit risk is the risk of loss in the event the counter party to a transaction fails to discharge an obligation and causes the other party to incur a loss. Credit risk associated with the Fund is periodically assessed in consultation with external consultants, the Department of Finance, Energy and Municipal Affairs, and the Master Trust Investment Advisory Committee.

Fixed Income

The Fund is exposed to credit risk from the following interest earning investments at June 30 as follows:

	2013	2012
	(millions)	(millions)
	\$	\$
Federal government	164.0	195.9
Provincial government	20.1	77.1
Municipal government	-	2.6
Corporate	<u>308.9</u>	<u>241.2</u>
Total investment credit risk exposure	493.0	516.8
Fund's pro-rated share	<u>32.8505%</u>	<u>33.1776%</u>
Fund's investment credit risk exposure	162.0	171.5
Provincial government promissory note	<u>88.3</u>	<u>32.0</u>
Fund's total credit risk exposure	<u>250.3</u>	<u>203.5</u>

Security Lending

The Fund participates in a Securities Lending Program whereby it lends securities for a fee to approved borrowers. To alleviate the credit risk, borrowers must provide collateral with a value of 105 percent of the value of the securities lent. The market value of the collateral is monitored by the custodian at least daily to ensure that the 105 percent threshold is maintained. In addition, security loans are allocated across various borrowers within the program and the Fund holds indemnification coverage which mitigates the credit and market risk on the collateral.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

d) Investment Risk Management (continued...)

(iii) Credit Risk (continued...)

Security Lending (continued...)

The fair value of the security loans outstanding and collateral held is as follows:

	<u>2013</u> \$	<u>2012</u> \$
Total security loans outstanding	345,192,176	17,646,508
Fund's pro-rated share	<u>32.8505%</u>	<u>33.1776%</u>
Fund's security loans outstanding	<u>113,397,356</u>	<u>5,854,688</u>
Total collateral held	362,451,930	18,527,962
Fund's pro-rated share	<u>32.8505%</u>	<u>33.1776%</u>
Fund's collateral held	<u>119,067,271</u>	<u>6,147,133</u>

Derivatives

The Fund is exposed to credit related losses in the event of non performance by counter parties to derivative financial instruments. In order to mitigate this risk, the Fund deals only with highly rated counter parties, with whom International Swap and Derivative Association agreements have been executed, normally major financial institutions with a minimum credit standard of "A" rating, as supported by a recognized credit rating agency.

Credit risk represents the maximum amount that would be at risk as at the reporting date if the counter parties failed completely to perform under the contracts and if the right of offset proved to be non enforceable. Credit risk exposure on derivative financial instruments is represented by the receivable replacement cost of contracts with counter parties, less any prepayment collateral or margin received as at the reporting date.

(iv) Foreign Currency Risk

Foreign currency risk is the risk that the value of the future cash flow of the financial instrument will fluctuate because of changes in foreign exchange rates. Consequently, the Fund is exposed to the risk that the exchange rates of the various currencies may change in a manner that has an adverse effect on the value of the portion of the Fund's assets denominated in currencies other than the Canadian dollar. Foreign currency exposure arises from the holding of investments denominated in foreign currencies. A policy of hedging from 30 to 70 percent of the currency exposure is used to mitigate this risk.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

d) Investment Risk Management (continued...)

(iv) Foreign Currency Risk (continued...)

The Fund's unhedged currency exposure from net investment assets as at June 30, is summarized in the following table.

	2013	2012
	(millions)	(millions)
	\$	\$
Currency		
Brazil	4.2	9.3
Switzerland	16.0	11.5
Euro Zone	43.2	34.1
United Kingdom	46.3	43.9
Hong Kong	19.7	17.0
Japan	37.6	23.9
Sweden	12.3	8.8
United States	193.7	130.4
Other	<u>42.5</u>	<u>39.2</u>
Total	415.5	318.1
Fund's pro-rated share	<u>32.8505%</u>	<u>33.1776%</u>
Fund's foreign currency exposure	<u>136.5</u>	<u>105.5</u>

After the effect of hedging, and without a change in all other variables, a 10 percent change in the Canadian dollar against all other currencies would change the fair value of the Fund by \$13.7 million.

(v) Liquidity Risk

Liquidity risk is the risk of not meeting the cash obligations of the Fund in an efficient manner. Cash obligations are fulfilled from contributions to the Fund, cash income of the Fund, and dispositions of Fund assets as required. Cash requirements of the Fund are reviewed on an ongoing basis to provide for the orderly availability of resources to meet the financial obligations of the Fund.

The Fund's cash management policy ensures that the quality and liquidity of the investment vehicles within the portfolio are consistent with the needs of the Fund.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

3. Investments and Derivatives (continued...)

e) MAV II Notes

The Master Trust holds MAV II notes (originally bank-sponsored asset backed commercial paper) in its bonds, debentures, and notes portfolios. The carrying value of the MAV II notes held at June 30, 2013 was \$19,928,979 (or \$23,117,719 face value less a \$3,188,740 discount). The carrying value of the MAV II notes are recorded at the amount for which they were sold subsequent to the year-end.

4. Accrued Pension Obligation

a) Actuarial and Extrapolated Valuation

The present value of the accrued pension obligation was determined using the projected unit credit method pro-rated on services and management's best estimate, as at the valuation and extrapolation dates, of future economic events and involve economic and non economic assumptions. The non economic assumptions include considerations such as mortality and retirement rates. The primary economic assumptions include the return on investment, discount, inflation, and salary escalation rates.

The most recent actuarial valuation for accounting purposes prepared by the actuarial consulting firm Morneau Shepell, disclosed an unfunded liability of \$90,587,000 as at April 1, 2011. The next actuarial valuation is scheduled to be completed in 2014.

The economic assumptions used in determining the value of accrued pension obligations for accounting purposes were developed by reference to expected long term market conditions. Significant long-term assumptions used in the June 30 extrapolation were as follows:

	<u>2013</u>	<u>2012</u>
	%	%
Economic Assumptions		
Basic salary escalation rate (excluding promotional increases)	2.50	2.50
Discount rate used to determine accrued obligation	6.86	7.37
Expected rate of return on fund assets	6.86	7.37
Pension cost of living increase	1.40	1.40

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

4. Accrued Pension Obligation (continued...)

a) Actuarial and Extrapolated Valuation (continued...)

	<u>2013</u>	<u>2012</u>
Non-Economic Assumptions		
Mortality	GAR94 projected to 2000 using Scale AA for both males and females.	GAR94 projected to 2000 using Scale AA for both males and females.
Retirement Age	35 years of pensionable service or when age plus pensionable service is 86 (but not under 55 or with less than 30 years of service); in any case, not over age 60 unless already over age 60, and no earlier than one year after the valuation date.	35 years of pensionable service or when age plus pensionable service is 86 (but not under 55 or with less than 30 years of service); in any case, not over age 60 unless already over age 60, and no earlier than one year after the valuation date.

b) Sensitivity of Changes in Major Assumptions

The Fund's future experience may differ from the assumptions used in the actuarial valuation and the extrapolation. Any differences between the actuarial assumptions and future experience could be significant and will emerge as experienced gains or losses in future valuations which will affect the financial position of the Fund.

5. Funding Policy

In accordance with the *Teachers' Superannuation Act*, employees are required to contribute to the Plan as described in Note 1(b). The employer matches employee contributions to the Fund. Under Section 9 of the *Teachers' Superannuation Act*, payments out of the Fund are guaranteed by the Province of Prince Edward Island.

As a result of an unfunded liability at July 1, 2005, the Province of Prince Edward Island made a special contribution through the signing of a \$160,000,000 promissory note. The note, which is held by the Fund, is receivable in ten equal annual installments of \$16,000,000 beginning April 15, 2005. Interest on the note is accrued at a rate of 4.345 percent per annum and is receivable semi-annually on April 15 and October 15. Prior to April 15, 2014, any monies owing may be suspended on six months prior notice if the Minister of Finance, Energy and Municipal Affairs deems the funded level, excluding any outstanding balances on promissory notes, to be 90 percent on a going concern basis as defined in the Province of Prince Edward Island Funding Policy for Government Sponsored Registered Pension Plans. Interest will be accrued to the date of any suspension implemented. Any monies suspended prior to and including April 15, 2014, are no longer due and owing. Provided no further monies are payable, the promissory note shall be deemed paid in full.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

5. Funding Policy (continued...)

The following is a schedule of principal and interest payments as disclosed in the promissory note:

<u>Date of Payment</u>	<u>Principal Payments</u>	<u>Interest Payments</u>	
	<u>Principal Payment</u> \$	<u>April 15</u> \$	<u>October 15</u> \$
April 15, 2005	16,000,000	-	3,128,400
April 15, 2006	16,000,000	3,128,400	2,780,800
April 15, 2007	16,000,000	2,780,800	2,433,200
April 15, 2008	16,000,000	2,433,200	2,085,600
April 15, 2009	16,000,000	2,085,600	1,738,000
April 15, 2010	16,000,000	1,738,000	1,390,400
April 15, 2011	16,000,000	1,390,400	1,042,800
April 15, 2012	16,000,000	1,042,800	695,200
April 15, 2013	16,000,000	695,200	347,600
April 15, 2014	<u>16,000,000</u>	<u>347,600</u>	-
	<u>160,000,000</u>	<u>15,642,000</u>	<u>15,642,000</u>

Since the promissory note was not signed until February 16, 2006, but provided for a principal payment as of April 15, 2005, additional interest was paid on the scheduled principal payment of April 15, 2005, as the first payment was not made until March 16, 2006.

As a result of an unfunded liability at July 1, 2011, the Province of Prince Edward Island made a special contribution through the signing of a \$80,369,000 promissory note. The note issued December 11, 2012, is held by the Fund, is receivable in ten equal annual instalments of \$8,063,900 beginning April 1, 2013. Interest on the note is accrued from April 1, 2012, at a rate of 2.9 percent per annum and is receivable semi-annually on April 1 and October 1. Prior to April 1, 2022, any monies owing may be cancelled on six months prior notice if the actuary to the Teachers' Superannuation Fund deems the funded level, excluding any outstanding balances of this promissory note, to be 90 percent pursuant to an actuarial valuation for funding purposes conducted in accordance with accepted actuarial practice in Canada. Interest will be accrued to the date of any cancellation implemented.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

5. Funding Policy (continued...)

The following is a schedule of principal and interest payments as disclosed in the promissory note:

<u>Date of Payment</u>	<u>Principal Payments</u>	<u>Interest Payments</u>	
	<u>Principal Payment</u> \$	<u>April 1</u> \$	<u>October 1</u> \$
April 1, 2012	-	-	1,165,351
April 1, 2013	8,036,900	1,165,351	1,048,815
April 1, 2014	8,036,900	1,048,815	932,281
April 1, 2015	8,036,900	932,281	815,746
April 1, 2016	8,036,900	815,746	699,210
April 1, 2017	8,036,900	699,210	582,675
April 1, 2018	8,036,900	582,675	466,140
April 1, 2019	8,036,900	466,140	349,605
April 1, 2020	8,036,900	349,605	233,070
April 1, 2021	8,036,900	233,070	116,535
April 1, 2022	<u>8,036,900</u>	<u>116,535</u>	-
	<u>80,369,000</u>	<u>6,409,428</u>	<u>6,409,428</u>

Subsequent to year-end, legislation was passed stating that a promissory note issued by the Government to the Fund cannot be cancelled or recalled by the Government before the maturity of the promissory note, unless the Government contributes to the Fund an asset equal to or greater than the value of the promissory note on the date the promissory note is cancelled or recalled.

6. Operating Expenses

The Fund is charged with administrative and operating expenses. The following is a summary of these expenses.

	<u>2013</u> \$	<u>2012</u> \$
Administrative expenses - pension section	273,721	280,822
- investment section	<u>54,483</u>	<u>53,647</u>
	328,204	334,469
Consulting fees	243,015	81,176
Actuarial fees	-	41,319
Investment expenses		
Custodian	87,722	64,728
Monitoring	68,917	77,407
Management	<u>2,183,893</u>	<u>1,660,520</u>
	<u>2,911,751</u>	<u>2,259,619</u>

PRINCE EDWARD ISLAND TEACHERS' SUPERANNUATION FUND

Notes to Financial Statements
June 30, 2013

7. Related Party Transactions

The Province of Prince Edward Island is the sponsor of the Plan. The Province guarantees all payments owing by the Fund and has committed to the funding requirements as defined by the Funding Policy (Note 5). As a participating employer, the Province matches regular bi-weekly employee and eligible prior period service contributions. Employer contributions receivable from the Province as at June 30, 2013, totalled \$69,001 (2012 - \$106,147).

The Province provides pension and investment administration services to the Fund. A portion of the Province's costs relating to these services is recovered annually from the Fund. Costs recovered for the Pension section totalled \$226,240 (2012 - \$234,450) and recoveries related to the Investment section totalled \$54,483 (2012 - \$53,647). Other costs recovered by the Province totalled \$34,432 (2012 - \$34,081).

Total amount payable to the Province at June 30, 2013, was \$229,116 (2012 - 237,606).

Total notes and interest receivable from the Province at June 30, 2013, was \$88,998,001 (2012 - \$113,237,208).

8. Capital Management

The main objective of the Fund is to sustain a level of net assets in order to meet the pension obligations of the Fund. The Plan sponsor manages the contributions received and benefits issued as required by the Teachers' Superannuation Act.

In efforts to utilize economies of scale, contributions for the Province's three registered pension plans are pooled and invested together in the Province's Master Trust (the Master Trust). Each pension plan holds units of the Master Trust in proportion to the value of contributions made. The Province has developed a Statement of Investment Policies and Procedures (SIP&P) to provide the framework for how the Master Trust's assets are to be invested, monitored, and evaluated. Assets are managed by engaging knowledgeable, external investment managers who are charged with the responsibility of investing new and existing funds in accordance with the SIP&P. A Master Trust Investment Advisory Committee exists for the purpose of protecting the pension fund assets, monitoring asset mix, reviewing costs, reviewing investment returns, and assessing investment manager performance, as well as providing advice to the Minister of Finance, Energy and Municipal Affairs who serves as Trustee for the Province's three registered pension plans.

9. Commitment

The Master Trust has entered into an arrangement where it has committed to invest \$35 (US) million with Global Infrastructure Partners (GIP) Fund. GIP is an independent infrastructure fund manager that invests in high quality infrastructure assets in the energy, transport, water, and waste sectors. \$11.6 (US) million had been invested as at the financial statement release date.

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

10. Subsequent Events

a) Plan Amendments

Subsequent to the financial statement date, legislation was passed to amend the *Teachers' Superannuation Act*. These amendments take effect January 1, 2014, and are summarized as follows:

- As part of the transition to this new plan design, the Province will provide a one-time funding injection that will bring the funded status of the plan to 122 percent as at January 1, 2014. The funding injection will be made after plan amendments and assumption changes are accounted for.
- The salary component of the benefit formula will be calculated based on average indexed earnings. The earnings attributed to each year of pre 2014 pensionable service, and indexed thereafter, will be the December 31, 2013, 5-year highest average salaries calculated under the *Teachers' Superannuation Act*, prior to the plan amendment. Annual indexation of salaries is guaranteed for 2014, 2015, and 2016 at a rate of 1.5 percent per annum. After 2016, salary indexing will be contingent on the plan having a funded status greater than 100 percent and limited to the assets determined to be available for that purpose.
- Annual indexation of deferred and retiree pensions is guaranteed for 2014, 2015, and 2016 at a rate of 0.9 percent per annum for the Teachers' Superannuation Fund. After 2016, indexation of deferred and retiree pensions will be contingent on the plan having a funded status greater than 110 percent and limited to the assets determined to be available for that purpose.
- Commencing January 1, 2019, the unreduced retirement rules will change such that pension earned on pensionable service credited after 2018 will be payable on an unreduced basis when a member, at his or her date of retirement, is at least 62 years of age or at least 55 years of age with 32 or more years of pensionable service. The pre-amendment unreduced retirement rules will continue to apply to pensionable service credited prior to 2019.
- After 2016, contribution rates will vary as follows depending on the funded status of each plan as measured at each valuation date:

**PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND**

Notes to Financial Statements
June 30, 2013

10. Subsequent Events (continued...)

a) Plan Amendments (continued...)

- If the funded status falls below 110 percent, employee and employer contribution rates will increase by 1 and 2 percentage points, respectively, and these rates will remain in force until the funded status improves to at least 115 percent.
- If the funded status falls below 100 percent, the employer contribution rate will increase by a further 2 percentage points in addition to the rate increases for a funded status below 110 percent. This additional employer contribution rate increase will remain in effect until the funded status improves to at least 105 percent.
- If the funded status improves to 135 percent or higher, employee and employer contribution rates will decrease by 1 and 2 percentage points, respectively, until the funded status falls to or below 130 percent.
- If the funded status improves to 145 percent or higher, the employer contribution rate will decrease by a further 2 percent in addition to the rate decreases for a funded status at or above 135 percent. This additional decrease will remain in effect until the funded status falls to or below 140 percent.
- The benefits guaranteed by the Province no longer include indexation after 2016 as it has been made contingent on the plan's ability to pay for those benefits. The funding of deficits under this new guarantee is the Province's responsibility with special payments being required whenever the plan has a funded status below 100 percent and the contributions required, as noted above, are not projected to achieve a funded status of at least 100 percent within 5 years.

The above plan design and actuarial assumption changes are estimated to potentially decrease the Plans gross pension obligation.

b) Province of Prince Edward Island Master Trust

Subsequent to June 30, 2013, Executive Council approved changes to the Statement of Investment Policies and Procedures (SIP&P) for the Province of Prince Edward Island Master Trust. Proposed changes reflect a revised interim benchmark for asset mix under the SIP&P to reflect a higher level of fixed income holdings and an amendment for the re-balancing policy within asset classes. It is anticipated that these changes will decrease the discount rate assumption going forward and result in a significant increase in the accrued pension obligation.



Design and Printing: Communications PEI
2015

15AN35-41246