Prince Edward Island
CANADA

Teachers' Superannuation Fund

Annual Report 2010-2011

To Her Honour,
the Honourable
Barbara Hagerman

May it please your Honour:

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, 2011.

Respectfully submitted
Your Obedient Servant,

Son Honneur,
L'honorable
Barbara Hagerman

Madame la lieutenante-gouverneure,

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 2010.

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

Doug Currie

Doug W. Currie,
Minister of Education and Early Childhood Development
Ministre de l'Éducation et du Développement
de la petite enfance

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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 2010-2011, 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 $47,200 for 2010 and $48,300 for 2011.

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 Retirement – 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 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, 2010 was 0.2 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 and Municipal Affairs. The Office of the Comptroller within the Department of Finance and Municipal Affairs provides investment management support for 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 as at June 30, 2011 were:

1) Baillie Gifford Overseas Limited;

2) Beutel, Goodman & Company Limited;

3) Burgundy;

4) Franklin Templeton Investments Corporation;

5) Lazard Asset Management LCC;

6) McLean Budden; and

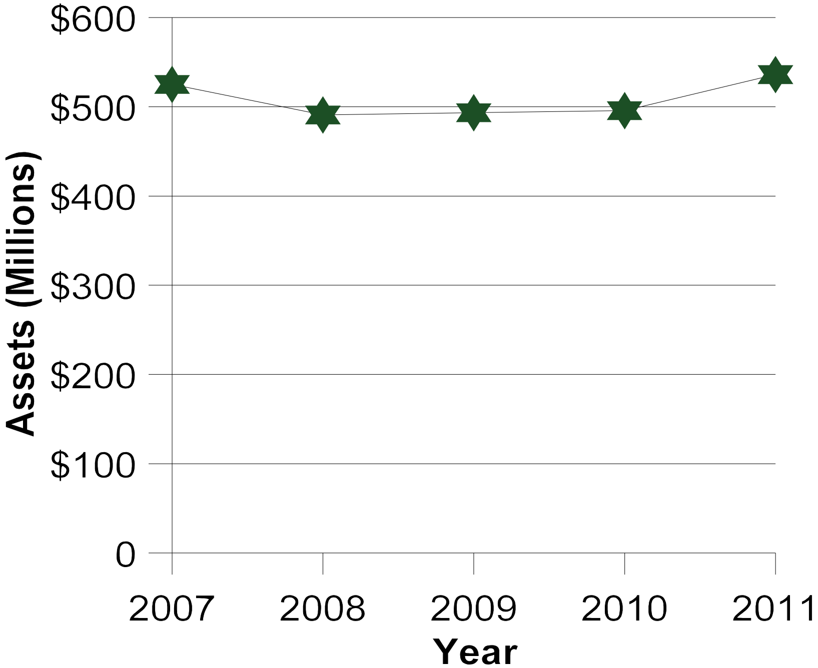
7) State Street Global Advisors Ltd.

The total asset balance of the TSF at June 30, 2011 was approximately $536 million, up from $496 million at June 30, 2010.

Diagram 1 shows the TSF total asset balance from 2007 - 2011.

Diagram 1

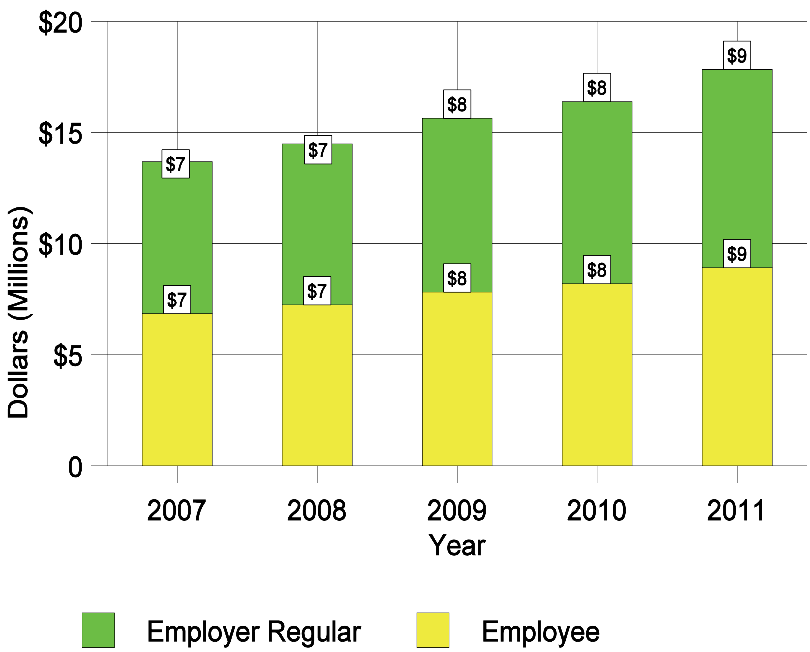
TSF Total Asset Balance



Regular Contributions – Regular contributions are made to the TSF via payroll deductions. In 2010-2011, the regular contributions from both the employer and employees combined were approximately $17.8 million, up from $16.4 million in 2009-2010. 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.

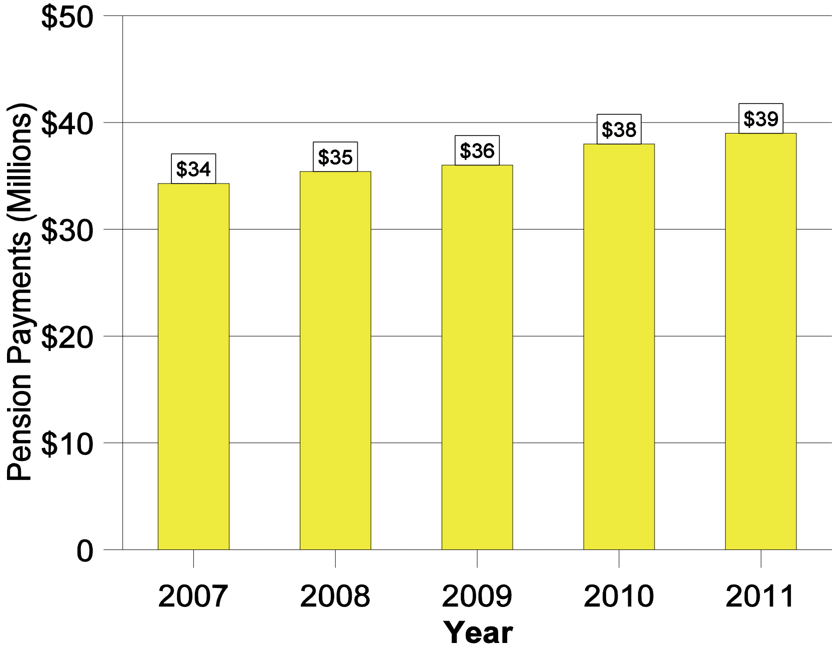
Diagram 2
Regular Contributions



Special Contribution - To reduce the unfunded liability of the TSF, the Province of Prince Edward Island agreed to invest $160 million in the Fund. The investment was in the form of a promissory note from the Province of Prince Edward Island to the Fund. This note is receivable in ten equal annual installments of $16 million beginning April 15, 2005, plus interest at the rate of 4.345 percent per annum. Interest is to be paid semi-annually on April 15 and October 15.

Pension Payments – Annual pension payments in 2010-2011 were approximately $39 million. This is shown in **Diagram 3**. In the fiscal year 2010-2011, approximately 96 percent of the pension payroll was paid to members and the remaining 4 percent was paid out as spousal and dependant benefits.

Diagram 3
Pension Payments



Pensioners – The number of persons receiving pension was 1,446 at June 30, 2011. **Table 1** outlines the number of new pensioners, their average age and average annual pension for the most recent fiscal years ending June 30, 2011.

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

Fiscal Year	No. of New Pensioners	Average Age	Average Annual Pension
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 categories with the average annual pension for each category at June 30, 2011.

Table 2
Pension Categories and Average Annual Pension

Category	Number of Pensions		Average Annual Pension	
	2011	**2010**	**2011**	**2010**
Members	1,288	1,252	$ 28,370	$ 28,232
Disability Pensions	48	46	$ 19,147	$ 18,638
Spousal	94	94	$ 13,815	$ 13,384
Dependants	16	11	$ 3,111	$ 2,174
Total Pensions	1,446	1,403		

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, 2008. This valuation was based on the following membership data:

1) 1,781 Active Members
   Average salary of $61,598
   Average age of 41.8 years
2) 1,348 Pensioners
   Average annual pension of $26,198
   Average age of 68.5 years
3) 65 Deferred Pensioners
   Average annual pension of $11,128
4) 352 Inactives
   Estimated average contributions with interest of $3,661

The value of the Plan assets as at July 1, 2008 was $490,419,000, which represents 79.0 percent of the actuarial liability of $620,909,000.

Table 3 details the actuarial valuation statement of financial position as at July 1, 2008.

Table 3

Going-Concern Financial Position

July 1, 2008

Value of Assets		
Market Value	$ 490,419,000	
	Actuarial Liability	***Percentage of Total Liabilities***
Active Members	$ 236,486,000	*38%*
Inactives and Deferred Vested Members	6,605,000	*1%*
Retired Members and Beneficiaries	377,818,000	*61%*
Total	**$ 620,909,000**	
Actuarial Surplus (unfunded liability)	$(130,490,000)	
Funding Ratio	79.0%	

Updated valuation results (July 1, 2011) will be available in the 2011-2012 annual report.

Highlights for 2010-2011

Legislative Amendments

In 2010-2011 there were a number of amendments both to the TSA and its accompanying regulations.

Effective January 1, 2011, the TSA was amended to standardize the contribution rates for active members whether in receipt of CPP benefits or not.

A housekeeping amendment was also made to clarify that pensioners who become re-employed must have their pension suspended.

There were also several housekeeping changes to the General Regulations of the TSA, i.e., removed conflicting language between the Act and these Regulations. In addition, amendments were added to:

a. clarify the pension treatment for members who are in receipt of a TSF disability pension and may or may not be in receipt of a CPP disability pension;

b. allow for the indexation of salary while on certain types of leave; and

c. the introduction of a 21 day waiting period for those members returning to active status in the plan and wishing to purchase a leave.

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 2010-2011, approximately 34 percent of the funds in the Master Trust were assets of the TSF.

As of June 30, 2011, the rate of return of the Master Trust was as follows:

- Annual rate of return: 13.90%
- Ten year rate of return: 5.10%

TSF Assets

During 2010-2011, there was a net increase to TSF assets of approximately $41 million.

Table 4 shows the receipts and income, by source, which totalled approximately $82 million.

Table 4
Receipts and Income

Type	Amount
Employer Contributions	$ 8,915,135
Employee Contributions	8,915,135
Transfer from Other Plans	633,091
Purchased Service	431,129
Investment Income	16,895,151
Market Value Increase	45,761,457
Total	**$ 81,551,098**

Table 5 shows the expenditures for 2010-2011, which totalled approximately $41 million.

Table 5
TSF Expenditures

Type	Amount	% of Expenditures
Benefits Paid	$ 38,935,092	
Refunds	73,891	
Transfers	113,678	
Total Benefit Expenses	**$ 39,122,661**	**94.65%**
Benefit Admin.	$ 215,078	
Pension System Fees	34,668	
Investment Admin.	50,449	
Total Administrative Expenses	**$ 300,195**	**0.73%**
Consulting Fees	25,439	
Total Consulting Fees	**$ 25,439**	**0.06%**
Manager Fees	$ 1,708,381	
Monitoring Fees	115,879	
Custodial Fees	61,053	
Total Investment Expenses	**$ 1,885,313**	**4.56%**
Total	**$ 41,333,608**	**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, 2011:

No of Members	Member	
1	*Chairperson* - Deputy Minister of Education & Early Childhood Development	Dr. Alexander (Sandy) MacDonald
2	Department of Education & Early Childhood Development	Gordon MacFadyen Vacant
3	PEI Teachers’ Federation	Michel Plamondon Blaine Bernard Denise Gaudet-McPhail
1	Department of Finance and Municipal Affairs	Scott Stevens

Master Trust Investment Advisory Committee

The Master Trust Investment Advisory Committee provides advice to the Minister of Finance 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, 2011, the committee is comprised of the following representatives:

Chairperson - Deputy Minister of Finance and Municipal Affairs	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 Scott Stevens
Union of Public Sector Employees	Shelley Ward Donalda Docherty
Ex Officio Outside Designates - Fiscal Agents	Tim Van Alstyne, *RBC Dominion Securities Inc.* Bill Hastie, *Scotia Capital Inc.*
Ex Officio Outside Designates - Consultants	Paul Malizia and Tony Politano, *Aon Hewitt*

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
Finance and Municipal Affairs
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
Investments and Banking
Department of Finance and Municipal Affairs
Tel: (902) 569-7666

Appendix

Audited Financial Statements
for 2010-2011

AUDITOR GENERAL

CHARLOTTETOWN
PRINCE EDWARD ISLAND

PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

FINANCIAL STATEMENTS

JUNE 30, 2011

AUDITOR'S REPORT

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

I have audited the financial statements of the **Prince Edward Island Teachers' Superannuation Fund**, which comprise the statement of net assets available for benefits as at June 30, 2011, and the statement of changes in net assets available for benefits for the year 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 generally accepted accounting principles for the private sector 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 audit. I conducted the audit in accordance with Canadian generally accepted auditing standards. Those standards require that I comply with ethical requirements and plan and perform the audit 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 June 30, 2011, and its financial performance and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles for the private sector.

Colin Younker

Colin Younker, CA
Auditor General

Charlottetown, Prince Edward Island
February 3, 2012

PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS

AS AT JUNE 30, 2011

	2011 $	2010 $
ASSETS		
Current Assets		
Cash	3,210,004	1,401,949
Receivables		
Contributions receivable - employee	669,126	1,269,532
- employer	746,495	1,538,667
Other	125,689	113,867
Accrued interest	433,075	577,812
Current portion of note receivable	16,000,000	16,000,000
	21,184,389	20,901,827
Investments (Notes 2(a, b) and 3)	482,971,869	426,830,345
Note receivable (Note 5)	32,000,000	48,000,000
	514,971,869	474,830,345
Total Assets	536,156,258	495,732,172
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	753,881	586,596
Income taxes payable	537,173	513,071
Other remittances payable	242,500	227,291
	1,533,554	1,326,958
Net assets available for benefits	534,622,704	494,405,214

(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, 2011

	2011 $	2010 $
INCREASE IN ASSETS		
Investment income (Note 3(a))		
Interest	7,133,992	6,866,673
Dividends	7,110,268	4,758,543
Change in fair value of investments	45,761,457	9,138,781
	60,005,717	20,763,997
Other income		
Promissory note interest	2,636,063	3,331,642
Bank interest	14,828	4,207
	2,650,891	3,335,849
Contributions		
Employee contributions	8,915,135	8,194,615
Employer contributions	8,915,135	8,194,615
Transfers from other plans	633,091	547,363
Purchased service	431,129	316,125
	18,894,490	17,252,718
Total increase in assets	81,551,098	41,352,564
DECREASE IN ASSETS		
Operating expenses (Note 6)	2,210,947	1,813,792
Benefits paid	38,935,092	37,726,070
Refunds	73,891	96,151
Transfers to other plans	113,678	85,678
Total decrease in assets	41,333,608	39,721,691
Increase in net assets	40,217,490	1,630,873
Net assets available for benefits, beginning of the year	494,405,214	492,774,341
Net assets available for benefits, end of the year	534,622,704	494,405,214

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

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 employer 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. For those employees whose employment is excluded from the *Canada Pension Plan Act* and is not subject to that Act, they contribute 9.0 percent of their salary.

Effective January 1, 2011, the *Teachers Superannuation Act* was amended and members whose employment is excluded from the *Canada Pension Plan Act* and is not subject to that Act will no longer contribute 9 percent of their salary as previously arranged. Like all members, they will contribute 7.3 percent of that part of the members' salary up to the amount of the YMPE and 9 percent on the amount that exceeds the YMPE.

c) Retirement Benefits

A member who has attained the age of 60 and has completed at least 2 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 2 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 2 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.

1. Plan Description (continued...)

c) Retirement Benefits (continued...)

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 4 percent.

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 2 or more years.

e) Death Benefits

On the death of a member prior to completing 2 years of pensionable service, or after completing 2 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 2 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 2 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) Income Tax

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

2. Summary of Significant Accounting Policies

Basis of Accounting

These financial statements are prepared on a going concern basis and in accordance with Canadian generally accepted accounting principals and presents the aggregate financial position of the Fund as a separate financial reporting entity independent of the Province of Prince Edward Island and the Plan members. They are prepared to assist plan members and others in reviewing the activities of the Fund for the fiscal period but they do not portray the funding requirements of the Plan or the benefit security of individual members. The following accounting policies are considered significant.

a) Foreign Currency Translation

Transactions denominated in foreign currencies are translated into Canadian dollars at the rates of exchange prevailing on the transaction dates. The fair values 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.

b) Investments

(i) Investments are represented by units of participation in a master trust. A master trust is a pool of assets in which contributions from pension plans are deposited for investing. The pro-rated share of each of the assets, liabilities, revenues and expenses of the Prince Edward Island Master Trust (the Master Trust) are allocated by units of participation.

(ii) Investments are valued at fair value, which is based on quoted or estimated market values. Changes in the market value of investments, including realized and unrealized gains resulting from changes in foreign exchange, are reflected in the financial statements as a change in the fair value of investments.

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 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.

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

b) Investments (continued...)

(iii) 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 from derivative contracts are included in the change in fair value of investments.

(iv) Investment transactions are recognized on the transaction date. Distributions are recognized on the record date.

(v) Investments include receivables and payables at June 30, 2011, for interest, dividends and settled derivative contracts.

c) Revenues and Expenses

Revenues 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.

d) Use of Estimates and Measurement Uncertainty

The preparation of financial statement in conformity with Canadian generally accepted accounting standards for the private sector requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and 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 liabilities and the present value of accrued benefits.

e) Financial Instruments

The Fund's financial instruments include cash, contributions and other receivables, investments, accounts payable and withholding taxes payable.

Due to their short-term nature, the Fund's short-term financial instruments, consisting of cash, contributions and other receivables, accounts payable and accrued liabilities, income taxes payable and other remittances payable are carried at cost which approximate their fair values. Investments are carried at fair values as described in Note 2(b) and are subject to interest, market, credit, currency, price and liquidity risks as described in Note 3.

f) Future Accounting Pronouncements

The Fund intends to adopt the recommendations of the Canadian Institute of Chartered Accountants Section 4600 which will replace Section 4100 for financial statements relating to fiscal years beginning on or after January 1, 2011. Management is reviewing these standards and will assess the impact on the financial statements.

3. **Investments**

a) **Investments**

Investments consist of units held in the Master Trust. At year-end, there are 388,528.868 (2010 - 372,683.616) units held in the Master Trust with a fair value of $1,243.08 (2010 - $1,145.29) per unit.

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

	2011	%	Income for the Year*	2010	%	Income for the Year*
	$	%	$	$	%	$
Canadian short-term investments	13,644,028	0.9	143,393	8,947,886	0.7	32,415
Other liquid assets	1,171,500	0.1	5,013,168	2,027,662	0.2	4,386,437
Bonds, debentures and notes	522,482,230	36.3	25,989,361	510,691,287	40.6	25,240,255
Canadian equity securities	336,050,201	23.4	71,898,769	316,406,521	25.1	40,271,837
Foreign equity securities	522,760,223	36.4	70,338,320	419,658,359	33.3	255,765
Equity investments in real estate	35,777,905	2.5	777,906	-	-	-
Currency forwards	788,905	0.1	4,716,097	(3,329,723)	(0.3)	3,586,283
Accrued income	4,273,180	0.3	-	4,215,615	0.4	-
Total	1,436,948,172	100.0	178,877,014	1,258,617,607	100.0	73,772,992
Fund's pro-rated share	33.6110%		33.5458%	33.9127%		28.1458%
Fund's investments**	482,972,650		60,005,725	426,831,213		20,763,999

* Includes realized gains of $29.7 million (gains of $16.1 million in 2010) and unrealized gains of $106.7 million (losses of $20.9 million in 2010).

** The totals will not recalculate to the financial statements due to rounding in the pro-rated share.

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:

	2011	2010
	$	$
Beutel, Goodman & Company Ltd.	12,627,178	13,922,397
Lazard Ltd.	172,248,069	129,409,824
Baille Gifford Overseas Ltd.	170,438,088	139,621,192
Total	355,313,335	282,953,413
Fund's pro-rated share	33.6110%	33.9127%
Fund's pooled funds	119,424,365	95,957,142

3. Investments (continued...)

b) Derivative Contracts

Derivative contracts are financial contracts, the value of which is "derived" from the value of underlying assets or exchange rates. Derivatives 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 net purchased and sold notional contract amounts that the Fund has in place as at June 30, 2011. These contracts will be settled at a future date. The fair value of the various forward currency contracts is the difference between the contracted forward rates and the current market values relative to the contracted notional amounts.

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 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.

The following provides details of derivative contracts outstanding as of June 30, 2011:

Notional Amount $	Fair Value $
182,621,826	788,905

c) 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 the external consultants, Department of Finance, Energy and Municipal Affairs staff 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.

3. **Investments (continued...)**

c) **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 Plan's assets and liabilities.

Assuming all other variables are held constant, a 1 percent increase (decrease) in nominal interest rates would decrease (increase) the fair value of the Fund by $7.5 million.

Value of Fixed Income Securities	Weighted Average Duration	Percent Change	Impact on Fair Value of the Master Trust	Fund's Pro-rated Share	Pro-rated Impact on Fair Value of the Fund
$		%	$	%	$
504.9 m	4.39 Yrs	1	22.2 m	33.6110	7.5 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 which are also discussed in this note. Assuming all other variables are held constant, a 10 percent increase (decrease) in market values of all public equities would increase (decrease) the fair value of the Fund by $30.1 million.

Value of Public Equities	Percent Change	Impact on Fair Value of the Master Trust	Fund's Pro-rated Share	Pro-rated Impact on the Fair Value of the Fund
$	%	$	%	$
894.6 m	10	89.5 m	33.6110	30.1 m

3. Investments (continued...)

c) 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, Department of Finance, Energy and Municipal Affairs staff and the Master Trust Investment Advisory Committee.

The Fund is exposed to credit risk from the following interest earning investments at June 30, 2011:

	2011 (millions) $	2010 (millions) $
Federal Government	220.9	199.5
Provincial Government	77.3	98.9
Municipal Government	2.3	2.2
Corporate	229.0	214.2
Total investment credit risk exposure	529.5	514.8
Fund's pro-rated share	33.6110%	33.9127%
Fund's investment credit risk exposure	178.0	174.6
Provincial Government Promissory Note	48.0	64.0
Fund's total credit risk exposure	226.0	238.6

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.

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

3. Investments (continued...)

c) Investment Risk Management (continued...)

(iii) Credit Risk (continued...)

	2011 $	2010 $
Total security loans outstanding	170,837,306	215,450,019
Fund's pro-rated share	33.6110%	33.9127%
Fund's security loans outstanding	57,420,127	73,064,919
Total collateral held	179,380,234	226,239,913
Fund's pro-rated share	33.6110%	33.9127%
Fund's collateral held	60,291,490	76,724,063

(iv) Foreign Currency Risk

Foreign currency exposure arises from the holding of investments denominated in foreign currencies. A policy of hedging from 30 percent up to 70 percent of the currency exposure is used to mitigate this risk.

The Fund's unhedged currency exposure from net investment assets as at June 30, 2011, is summarized in the following table:

Currency	2011 (millions) $	2010 (millions) $
Brazil	12.8	12.1
Switzerland	12.9	9.2
Euro Zone	33.1	24.5
United Kingdom	38.2	30.1
Hong Kong	19.3	11.5
Japan	29.5	20.3
Sweden	10.6	1.2
United States	109.7	83.6
Other	44.6	44.8
Total	310.7	237.3
Plan's pro-rated share	33.6110%	33.9127%
Plan's foreign currency exposure	104.4	80.5

After the effect of hedging, and without a change in all other variables, a 10 percent increase (decrease) in the Canadian dollar against all other currencies would decrease (increase) the fair value of the Fund by $10.4 million.

3. Investments (continued...)

c) Investment Risk Management (continued...)

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 planned 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.

d) Fair Value Disclosure

The Fund's assets recorded at fair value have been categorized based upon a fair value hierarchy on significant inputs used in measuring their fair value. The three levels of 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 2: Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly, including inputs in markets that are not considered to be active.

Level 3: Inputs that are unobservable. There is little, if any, market activity. Inputs into the determination of fair value require significant management judgement or estimation.

The following fair value hierarchy table presents information about the Fund's assets measured at fair value on a recurring basis at June 30, 2011.

3. **Investments (continued...)**

d) Fair Value Disclosure (continued...)

	Level 1 $	Level 2 $	Level 3 $	2011 Total $	2010 Total $
Canadian short-term investments	6,427,882	7,216,146	-	13,644,028	8,947,886
Other liquid assets	1,171,303	-	197	1,171,500	2,027,662
Bonds, debentures and notes	-	505,080,566	17,401,664	522,482,230	510,691,287
Canadian equity securities	336,050,201	-	-	336,050,201	316,406,521
Foreign equity securities	522,760,223	-	-	522,760,223	419,658,359
Equity investment in real estate	-	35,777,905	-	35,777,905	-
Currency forwards	-	788,905	-	788,905	(3,329,723)
Totals	866,409,609	548,863,522	17,401,861	1,432,674,992	1,254,401,992
Accrued income				4,273,180	4,215,615
Total financial assets at fair value				1,436,948,172	1,258,617,607
Fund's pro-rated share				33.6110%	33.9127%
Fund's investments				482,972,650	426,831,213

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, 2011 was $17,401,664 (or $23,355,585 face value less a $5,953,921 discount). Carrying value of the MAV II notes are calculated using management's best estimates based on available information reflecting an illiquid market.

The carrying value assigned to the MAV II notes held by the Master Trust may differ from the actual value realized on any sale or other liquidation. As a result of these uncertainties, the reported value may change materially in subsequent periods.

4. **Obligation for Pension Benefits for Accounting Purposes**

The present value of accrued pension benefits was determined using the projected unit credit method pro-rated on service and best estimate assumptions. The most recent actuarial valuation for accounting purposes prepared by the actuarial consulting firm Morneau Sobeco, disclosed an unfunded liability of $78,400,000 as at April 1, 2008.

4. Obligation for Pension Benefits for Accounting Purposes (continued...)

The estimated present value of accrued benefits as of June 30, 2011, the principal components of changes in actuarial present values during the year and the estimated unfunded liability were as follows:

	2011 $	2010 $
Estimated present value of accrued benefits, beginning of year	597,345,000	594,388,000
Interest accrued on benefits	45,182,000	45,807,000
Benefits accrued	13,607,000	11,920,000
Increase due to purchase of service	1,064,000	863,000
Benefits paid	(39,123,000)	(37,908,000)
Changes due to actuarial projection	16,052,000	(17,725,000)
Estimated present value of accrued benefits, end of year	634,127,000	597,345,000
Net assets available for benefits	534,623,000	494,405,000
Unfunded liability	99,504,000	102,940,000

The economic assumptions used in determining the actuarial value of accrued pension benefits for accounting purposes were developed by reference to expected long-term market conditions. For 2011, projections were performed for the Prince Edward Island Teachers' Superannuation Fund to reflect changes to the discount rate and expected rate of return assumptions. Significant actuarial assumptions used in the projections for 2011 were:

Basic salary escalation rate (excluding promotional increases)	2.50%
Discount rate used to determine accrued obligation	7.37%
Expected rate of return on plan assets	7.37%
Pension cost of living increases	1.40%

The estimated present value of accrued benefits includes amounts owing to terminate non-vested members in the form of contributions plus interest.

The Consolidated Financial Statements of the Province records the obligation using the method of accounting disclosed above.

5. Funding Policy and Special Contributions

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.

5. Funding Policy and Special Contributions (continued...)

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.

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

Principal Payments		Interest Payments	
Date of Payment	Principal Payment $	April 15 $	October 15 $
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	16,000,000	347,600	-
	160,000,000	15,642,000	15,642,000

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.

5. Funding Policy and Special Contributions (continued...)

An objective of the funding policy is to be 90 percent funded at each actuarial valuation date. If the funded level is less than 90 percent, the policy requires a special contribution to be made by the Province to bring the Fund to a 90 percent funded level. The most recent going concern actuarial valuation for funding purposes, dated July 1, 2008, determined an unfunded liability of $130,500,000. At the valuation date, after taking into consideration net assets, the outstanding balance on the promissory note and the present value of excess contributions as stipulated in the Funding Policy, the funded level was 81 percent. As a result, the Province made a special cash contribution of $53,000,000 to the Fund on March 12, 2010, to bring the funded level, including the outstanding balance on the promissory note, to 90 percent.

6. Operating Expenses

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

		2011 $	2010 $
Administrative expenses	- pension section	249,746	275,173
	- investment section	50,449	63,526
		300,195	338,699
Consulting fees		25,439	20,686
Investment expenses		1,885,313	1,454,407
Total		2,210,947	1,813,792

7. Related Party Transactions

The Province of Prince Edward Island is the sponsor of the Plan and a participating employer. 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. Contributions receivable from the Province as at June 30, 2011, totalled $742,878 (2010 - $1,534,978).

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 $203,840 (2010 - $146,190) and recoveries related to the Investment section totalled $50,449 (2010 - $63,526). Other costs recovered by the Province totalled $34,668 (2010 - $116,858).

Total amounts payable to the Province at June 30, 2011, was $203,840 (2010 - $93,734).