

PROVINCE OF PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

FINANCIAL STATEMENTS

JUNE 30, 2006

AUDITOR'S REPORT

**To the Commissioners of the
Teachers' Superannuation Commission
Province of Prince Edward Island**

I have audited the Statement of Net Assets Available for Benefits of the Province of Prince Edward Island Teachers' Superannuation Fund as at June 30, 2006 and the Statement of Changes in Net Assets Available for Benefits for the year then ended. These financial statements are the responsibility of the Teachers' Superannuation Commission. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at June 30, 2006 and the results of its operations for the year then ended in accordance with Canadian generally accepted accounting principles.

**Colin Younker, CA
Auditor General**

**Charlottetown, Prince Edward Island
May 3, 2007**

PROVINCE OF PRINCE EDWARD ISLAND
TEACHERS' SUPERANNUATION FUND
STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS
AS AT JUNE 30, 2006

	<u>2006</u>	<u>2005</u>
ASSETS		
Cash	\$ 218,944	\$ 274,131
Receivables		
Contributions receivable - employees	250,873	3,084
Contributions receivable - employers	322,381	38,656
Other	61,316	85,807
Short term loan to Province	-	2,200,000
Accrued interest receivable	1,154,867	1,447,540
Current portion of note receivable	<u>16,000,000</u>	<u>32,000,000</u>
	<u>18,008,381</u>	<u>36,049,218</u>
Investments (Note 3)	354,252,110	312,974,719
Note receivable (Note 5)	<u>112,000,000</u>	<u>128,000,000</u>
Total Assets	<u>\$484,260,491</u>	<u>\$477,023,937</u>
LIABILITIES		
Accounts payable	<u>\$ 487,532</u>	<u>\$ 475,895</u>
NET ASSETS AVAILABLE FOR BENEFITS	<u>\$483,772,959</u>	<u>\$476,548,042</u>

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

ON BEHALF OF THE COMMISSION

COMMISSIONER: _____

COMMISSIONER: _____

PROVINCE OF PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

FOR THE YEAR ENDED JUNE 30, 2006

	<u>2006</u>	<u>2005</u>
INCREASE IN ASSETS		
Investment income		
Interest	\$ 12,468,499	\$ 7,134,892
Dividends	3,960,308	4,106,790
Other income	52,323	129,517
	<u>16,481,130</u>	<u>11,371,199</u>
Market value increase	<u>11,411,106</u>	<u>13,198,762</u>
Contributions		
Employees' contributions	6,444,299	6,302,125
Employers' contributions	6,444,299	6,302,125
Transfers from other plans	791,734	766,938
Buybacks	303,315	292,131
Government Contribution towards unfunded liability (Note 5)	-	160,000,000
	<u>13,983,647</u>	<u>173,663,319</u>
Total Increase in Assets	<u>41,875,883</u>	<u>198,233,280</u>
DECREASE IN ASSETS		
Administrative expenses	182,892	106,468
Custodial and management fees	1,109,366	989,685
Refunds	75,730	70,658
Benefits paid	33,186,727	28,885,701
Transfers to other plans	<u>96,251</u>	<u>443,742</u>
Total Decrease in Assets	<u>34,650,966</u>	<u>30,496,254</u>
INCREASE IN NET ASSETS	7,224,917	167,737,026
NET ASSETS AVAILABLE FOR BENEFITS AT BEGINNING OF THE YEAR	<u>476,548,042</u>	<u>308,811,016</u>
NET ASSETS AVAILABLE FOR BENEFITS AT END OF THE YEAR	<u>\$483,772,959</u>	<u>\$476,548,042</u>

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

PROVINCE OF PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2006

1. Description of Plan

The following description of the Teachers' Superannuation Plan is a summary only. For more complete information, reference should be made to the Teachers' Superannuation Act.

a) General

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

b) Contributions

Under the Plan, employees and the employer make equal contributions amounting to 7.2% on that part of the salary on which Canada Pension Plan contributions are made and 9.0% on salary when Canada Pension Plan contributions are not required.

c) Retirement Benefits

A teacher who has attained age 60 and has completed at least 5 years of service or has attained age 55 and has completed 30 years of service or has completed 35 years of service is entitled to an immediate pension which is payable in equal monthly installments.

The annual amount of the pension is equal to 2% of the average of the five highest annual pensionable salary rates, multiplied by the number of years of pensionable service. When the teacher reaches the age of 65 (or if he or she is 65 or over at retirement) the amount of pension described above is reduced by 0.7% of the average salary rate up to the average Yearly Maximum Pensionable Earnings under the Canada Pension Plan during the five year period over which the average salary has been computed, multiplied by the number of years of the teacher's pensionable service after July 1, 1972.

Reduced benefits are available at age 55 with at least 5 years of pensionable service. The pension for a teacher 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% for each full month by which the early retirement date precedes the teacher's earliest unreduced retirement age.

The above formula determines the amount of a teacher's initial pension at retirement. In subsequent years the amount of a teacher's pension is increased by 60% of the percentage increase in the Consumer Price Index. The increase in any one year is limited to no more than 4%.

PROVINCE OF PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

NOTES TO THE FINANCIAL STATEMENTS (continued)

JUNE 30, 2006

1. Description of Plan (continued)

d) Disability Benefits

Disability benefits are available at any age to a teacher who retires from teaching service because of total and permanent disability who contributed to the Fund for 5 or more years.

e) Death Benefits

On the death of a teacher prior to completing 5 years of pensionable service, or after completing 5 years of service but leaving no surviving spouse or dependant children, the teacher's contributions accumulated with interest will be refunded. If a teacher dies prior to retirement but after completing 5 years of service, the teacher's spouse is entitled to an immediate lifetime pension equal to 60% of the accrued, unreduced pension of the teacher at the time of death. In addition to the spousal pension, an allowance equal to one quarter of the remaining 2/5 of pension which the teacher was receiving is payable in respect of each dependent child, until the child attains age 16, or until 25 if the child is attending school full-time. In no case shall payment to such children exceed 3/4 of the remaining 2/5 of pension.

f) Termination and Portability of Benefits

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

- a refund of the teacher's own contributions with interest, or
- if the teacher has completed at least five years of service, a deferred annuity commencing when the teacher attains the age of 60.

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

g) Income Tax

The Plan is a Registered Pension Plan as defined under the Income Tax Act and is not subject to income tax.

PROVINCE OF PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

NOTES TO THE FINANCIAL STATEMENTS (continued)

JUNE 30, 2006

2. Significant Accounting Policies

These financial statements are prepared on the going concern basis and present the aggregate financial position of the Plan as a separate financial reporting entity independent of the Province of Prince Edward Island and Plan members. They are prepared to assist plan members and others in reviewing the activities of the Plan 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) Investments

With the exception of real estate investments which are valued at cost, investments are stated at market value, as reported by the custodian of the Master Trust.

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 market value adjustment.

b) Investment Transactions

Investment transactions are recorded on the settlement date. Transactions conducted in foreign currencies are translated into Canadian dollars using the exchange rate in effect at the transaction date. Distributions are recognized on the record date.

3. Investments

a) Investments consist of the following:

	<u>2006</u>	<u>2005</u>
Cash held for investment	\$ 772	\$ 772
Short term investment fund units	24,385	598
Province of Prince Edward Island Master Trust	<u>354,226,953</u>	<u>312,973,349</u>
	<u>\$354,252,110</u>	<u>\$312,974,719</u>

The investments of the Civil Service Superannuation Fund, MLA Pension Fund, and the Teachers' Superannuation Fund are consolidated into the Province of Prince Edward Island Master Trust. Units are held by each of these funds in the Master Trust. As of June 30, 2006 there were 775,352.393 (2005-731,350.414) units held in the Province of Prince Edward Island Master Trust, of which the Teachers' Superannuation Fund held the following:

	<u>2006</u>	<u>2005</u>
Units held	300,436.557	270,060.870
Market Value per unit	\$1,179.04	\$1,158.90
Total market value held	\$354,226,953	\$312,973,349

PROVINCE OF PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

NOTES TO THE FINANCIAL STATEMENTS (continued)

JUNE 30, 2006

3. Investments (continued)

Investments of the Province of Prince Edward Island Master Trust are as follows:

	<u>2006</u>	<u>2005</u>
Canadian T-Bills	\$ 19,960,808	\$ 18,112,932
U.S. T-Notes	2,667,470	-
Other liquid assets	(1,359,058)	(465,802)
Bonds, debentures and notes	289,495,516	281,097,071
Canadian equity securities	336,909,732	319,682,762
Foreign equity securities	260,856,335	221,051,269
Accrued income receivable	3,175,945	3,571,701
Real estate	<u>2,465,339</u>	<u>4,511,528</u>
Total	<u>\$914,172,087</u>	<u>\$847,561,461</u>

The investments include amounts which three of the five Master Trust Fund managers have invested in their own pooled funds. The market values of these investments are as follows:

	<u>2006</u>	<u>2005</u>
Beutel, Goodman & Company Ltd.	\$ 25,996,871	\$ 27,061,779
Northwater Capital Management Inc.	106,018,114	96,502,353
Capital Guardian	<u>125,547,566</u>	<u>102,951,186</u>
Total	<u>\$257,562,551</u>	<u>\$226,515,318</u>

b) Risk Management

Rates of return vary based on the degree of uncertainty. The fundamental sources of uncertainty to which investments are exposed are credit risk and price risk. Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk is the risk that the value of an investment will fluctuate due to future changes in foreign exchange rates. Interest rate risk is the risk that the value of an investment will fluctuate due to future changes in market interest rates. Market risk is the risk the value of a financial instrument will fluctuate as a result of future changes in the market prices, whether those changes are caused by factors specific to the individual security or its issuer or factors affecting all securities traded in the market.

The policy of the Master Trust is to invest in a diversified portfolio of investments based on criteria established in the Statement of Investment Policies and Procedures.

PROVINCE OF PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

NOTES TO THE FINANCIAL STATEMENTS (continued)

JUNE 30, 2006

4. Obligations for Pension Benefits for Accounting Purposes

The present value of accrued pension benefits was determined using the projected benefit method prorated on service and best estimate assumptions. The most recent Actuarial Valuation for accounting purposes prepared by Morneau Sobeco disclosed an unfunded liability as at April 1, 2005 of \$47,509,000.

The estimated present value of benefits as of June 30, 2006, the principal components of changes in actuarial present values during the year and the estimated unfunded liability, were as follows:

	<u>2006</u>	<u>Restated 2005</u>
Estimated present value of accrued benefits at beginning of year	\$521,133,000	\$482,891,000
Interest accrued on benefits	38,872,000	37,983,000
Benefits accrued	9,848,000	9,645,000
Benefits paid	(33,187,000)	(28,886,000)
Changes due to actuarial valuation	<u>-</u>	<u>19,500,000</u>
Estimated present value of accrued benefits at end of year	\$536,666,000	\$521,133,000
 Net assets available for benefits	 <u>483,773,000</u>	 <u>476,548,000</u>
 Unfunded liability	 <u>\$ 52,893,000</u>	 <u>\$ 44,585,000</u>

The 2005 figures have been restated to reflect the April 1, 2005 Actuarial Valuation which was issued on January 16, 2007.

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. Significant actuarial assumptions used in the valuation were:

Asset rate of return	7.63%
Basic salary escalation rate (excluding promotional increases)	2.75%
Pension cost of living increases	1.60%

The Consolidated (Summary) Financial Statements of the Province record the obligation using the accounting method.

PROVINCE OF PRINCE EDWARD ISLAND

TEACHERS' SUPERANNUATION FUND

NOTES TO THE FINANCIAL STATEMENTS (continued)

JUNE 30, 2006

5.

Funding Policy

In accordance with the Teachers' Superannuation Act, employees are required to contribute 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. The most recent actuarial valuation for funding purposes was prepared by Morneau Sobeco as of July 1, 2005. This valuation disclosed an unfunded liability as at July 1, 2005 of \$74,291,000.

To reduce the unfunded liability of the Teachers' Superannuation Fund the Province of Prince Edward Island has agreed to invest \$160,000,000 in the Fund. The investment is in the form of a \$160,000,000 promissory note from the Province of Prince Edward Island to the Fund. This note is receivable in ten equal annual installments of \$16,000,000 beginning April 15, 2005 plus interest at the rate of 4.345% per annum receivable semi annually on April 15 and October 15. Provided that at any such time prior to April 15, 2014 any monies owing may be suspended, on six months prior notice, if the Provincial Treasurer deems the funding level of the Teachers' Superannuation Fund to be at a level of 90%, as defined in the Pension Fund Policy. Any interest shall include accrued interest to the date of any suspension implemented. Any monies suspended at any time or times prior to and including April 15, 2014 are no longer due and owing and no further monies are payable and the Promissory note shall be deemed paid in full.

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

<u>Date of Payment</u>	<u>Principal Payments</u>		<u>Interest Payable</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	16,000,000	347,600	-	
	<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 principle 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.