

**PROVINCE OF NOVA SCOTIA  
NOVA SCOTIA PUBLIC SERVICE  
SUPERANNUATION FUND  
CONSOLIDATED FINANCIAL STATEMENTS  
MARCH 31, 2006**

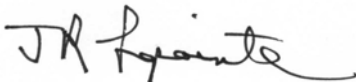
## **Auditor's Report**

To the Members of the Legislative Assembly of Nova Scotia; and  
To the Minister of Finance

I have audited the consolidated statement of net assets available for benefits and accrued pension benefits net of deficiency of the Nova Scotia Public Service Superannuation Fund as at March 31, 2006 and the consolidated statement of changes in net assets available for benefits for the year then ended. These consolidated financial statements are the responsibility of the Fund's management. 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 consolidated financial statements present fairly, in all material respects, the net assets available for benefits and accrued pension benefits net of deficiency of the Fund as at March 31, 2006 and the changes in net assets available for benefits for the year then ended in accordance with Canadian generally accepted accounting principles.



Jacques Lapointe, CA CIA  
Auditor General

Halifax, Nova Scotia  
June 5, 2006

**PROVINCE OF NOVA SCOTIA  
NOVA SCOTIA PUBLIC SERVICE SUPERANNUATION FUND  
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**PROVINCE OF NOVA SCOTIA  
NOVA SCOTIA PUBLIC SERVICE SUPERANNUATION FUND  
CONSOLIDATED STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS  
AND ACCRUED PENSION BENEFITS NET OF DEFICIENCY  
AS AT MARCH 31, 2006**

	<b>2006</b>	<b>2005</b>
	(000's)	(000's)
<b>NET ASSETS AVAILABLE FOR BENEFITS</b>		
<b>Assets</b>		
Investments (Note 3)	\$ 3,582,798	\$ 3,202,226
Contributions receivable		
Employees'	2,294	3,435
Employers'	2,638	4,084
Accrued income	15,857	14,833
Net investment transactions outstanding	-	5,838
Prepayment and sundry receivables	1,934	473
Cash	<u>3,549</u>	<u>2,083</u>
<b>Total assets</b>	<u><b>3,609,070</b></u>	<u><b>3,232,972</b></u>
<b>Liabilities</b>		
Real estate mortgages (Note 4)	33,851	17,614
Accounts payable	31,191	26,522
Net investment transactions outstanding	<u>2,264</u>	<u>-</u>
<b>Total liabilities</b>	<u><b>67,306</b></u>	<u><b>44,136</b></u>
<b>Net assets available for benefits</b>	3,541,764	3,188,836
Actuarial asset value adjustment (Note 5)	<u>276</u>	<u>411</u>
<b>Actuarial value of net assets available for benefits</b>	<u><b>\$ 3,542,040</b></u>	<u><b>\$ 3,189,247</b></u>
<b>ACCRUED PENSION BENEFITS NET OF DEFICIENCY</b>		
Accrued pension benefits (Note 6)	\$ 3,952,745	\$ 3,721,541
Deficiency (Note 6)	<u>(410,705)</u>	<u>(532,294)</u>
<b>Accrued pension benefits net of deficiency</b>	<u><b>\$ 3,542,040</b></u>	<u><b>\$ 3,189,247</b></u>

Approved:



Trustee - Minister of Finance

See accompanying notes to consolidated financial statements.

**PROVINCE OF NOVA SCOTIA  
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CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS  
FOR THE YEAR ENDED MARCH 31, 2006**

	<u>2006</u>	<u>2005</u>
<b>Increase In Assets</b>	(000's)	(000's)
Investment activities (Note 3)	\$ <u>446,244</u>	\$ <u>243,207</u>
Contributions		
Employers' – matched	47,807	43,860
Employees' – matched	47,807	43,860
Employees' – unmatched	2,073	1,205
Interest on the purchase of prior years' service	91	564
Transfers from other pension plans	<u>1,380</u>	<u>810</u>
	<u>99,158</u>	<u>90,299</u>
 Total increase in assets	 <u>545,402</u>	 <u>333,506</u>
 <b>Decrease In Assets</b>		
Benefits paid	173,445	164,074
Operating expenses (Note 7)	8,548	8,233
Refund of contributions and interest and transfers to other pension plans	<u>10,481</u>	<u>8,139</u>
Total decrease in assets	<u>192,474</u>	<u>180,446</u>
 <b>Increase in Net Assets</b>	 352,928	 153,060
 <b>Net Assets Available for Benefits at Beginning of Year</b>	 <u>3,188,836</u>	 <u>3,035,776</u>
 <b>Net Assets Available for Benefits at End of Year</b>	 <u>\$ 3,541,764</u>	 <u>\$ 3,188,836</u>

See accompanying notes to consolidated financial statements

**PROVINCE OF NOVA SCOTIA**  
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**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
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**1. Authority and Description of Plan**

The Public Service Superannuation Fund (the “Fund”) was established by the Public Service Superannuation Act (the “Act”). It is the funding vehicle for the Public Service Superannuation Plan (the “Plan”), a pension plan which covers employees of the Province and certain other public sector organizations. The detailed provisions of the Plan, including pension eligibility criteria and benefit formulas are also contained in the Act and in the Regulations made under the Act.

The following description is a summary only. For more complete information, reference should be made to the Act and Regulations.

Employee and employer contributions and investment earnings are credited to the Fund. Pensions, payments to terminating employees and administration expenses are charged to the Fund. The Minister of Finance is trustee of the Fund, which is invested in federal, provincial, municipal and corporate securities that qualify as eligible investments under the Provincial Finance Act.

The Plan is funded by employee and matching employer contributions of 6.4% (5.4% prior to June 2004) of salary up to the Year's Maximum Pensionable Earnings (“YMPE”) per the Canada Pension Plan (“CPP”) and 8% (7% prior to June 2004) of salary above the YMPE. The basic pension formula is 2% for each year of pensionable service times the number of years of pensionable service. Pensions are integrated with CPP benefits at age 65. Pensions in pay and deferred pensions are increased on January 1 of each year at a rate equal to the increase in the Consumer Price Index for Canada to a maximum of 6%.

Plan members are eligible for a pension upon reaching any of the following criteria:

- age 50 with an age plus pensionable service factor of 80 – “Rule of 80”;
- age 55 with two years of service (reduced pension);
- age 60 with two years of service;
- age 65.

Certain pension payments are attributable to previous early retirement programs and other unfunded benefits. They are charged to the Consolidated Fund of the Province and participating employers and are not paid from the Fund. These payments amounted to \$16.6 million for the year ended March 31, 2006 (2005 - \$16.6 million).

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**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
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**2. Summary of Significant Accounting Policies**

(a) Basis of Presentation:

These consolidated financial statements are prepared on the going-concern basis and present the aggregate financial position of the Fund as a separate financial reporting entity. In the event there are insufficient funds within the Fund to make all payments required by the Act, the Province of Nova Scotia guarantees cash flow assistance with respect to the pension benefits in pay. These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles.

(b) Consolidation:

The Fund holds certain real estate investments through wholly-owned subsidiaries. The consolidated financial statements include the financial statements of the Plan and its subsidiaries.

(c) Foreign Currency Translation:

Transactions denominated in foreign currencies are translated into Canadian dollars at the rates of exchange prevailing on the trade dates of the transactions. The market value of foreign investments and cash balances 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 current period change in market value of investments.

(d) Investments:

- (i) Investments are reported as of trade date and are stated at market value as at year end. Market value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

Money market securities, fixed income securities and equities are valued at quoted market prices.

Private equity values are estimated with appropriate valuation techniques and best estimates of managers or appraisers.

- (ii) The derivative contracts held by the Fund at year-end are valued using quoted market indices. The gains or losses from derivative contracts are included in the realized and unrealized gains or losses on investments.

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

- (iii) Real estate is composed of income producing properties and real estate pooled funds. Unless recently acquired in the current fiscal year, properties, including real estate mortgages, are valued annually by independent appraisers in accordance with generally accepted appraisal practices and procedures. This process utilizes discounted future cash flows. In estimating future cash flows certain assumptions are made with respect to future economic conditions and rates of return.

The fair value of any real estate which has been recently acquired is based on the purchase price.

(e) Investment Income/Loss:

Investment income/loss includes interest, dividends and operating income/loss from real estate, which is recorded on the accrual basis. Also included are gains and losses that have been realized on disposal of investments, and the unrealized appreciation and depreciation in the fair value of investments.

(f) Non-investment Assets and Liabilities:

The fair value of contributions receivable, accrued income, net investment transactions outstanding, sundry receivables, cash and accounts payable approximate their carrying amounts due to their short-term nature.

(g) Contributions:

Basic contributions from employers and members due to the Plan as at the end of the year are recorded on an accrual basis. Service purchases that include but are not limited to leaves of absence and transfers from other pension plans are recorded when received.

(h) Benefits:

Benefit payments to retired members, commuted value payments and transfers to other pension plans are recorded in the period in which they are paid. Accrued benefits are recorded as part of accrued actuarial liabilities.



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

(i) Use of Estimates:

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of changes in net assets available for benefits during the year. Actual results could differ from these estimates.

(j) Financial Instruments

The Fund's financial instruments include cash, contributions receivable, receivable from the Province of Nova Scotia, investments, net investment transactions outstanding, accounts payable and real estate mortgages. It is management's opinion, unless otherwise noted, that the Fund is not exposed to significant interest, currency or credit risks from its financial instruments.

The Fund's short-term financial instruments, consisting of cash, contributions receivable, receivable from the Province of Nova Scotia, net investment transactions outstanding, and accounts payable are carried at cost which, due to their short-term nature, approximates their fair value. Investments and real estate mortgages are carried at fair value as described in note 2 and are subject to interest, currency and credit risks as described in note 3.

**3. Investments and Derivatives**

The investment objectives of the Plan are to provide long-term security of pension benefits to members and to minimize any increases in contributions required by members and the employers. A strategy of investing in assets of Canadian and foreign equities, bonds, debentures, mortgages and money market securities is aimed at achieving these objectives.

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**3. Investments and Derivatives** continued

(a) Market value of investments and related income before allocating the effect of derivative contracts:

	<u>As at March 31, 2006</u>		<u>For the Year</u>	<u>As at March 31, 2005</u>		<u>For the Year</u>
	Asset	%	Income (Loss)*	Asset	%	Income (Loss)*
	(000's)		(000's)	(000's)		(000's)
Money market	\$ 280,322	7.8	\$ 9,900	\$ 385,743	12.1	\$ 7,726
Fixed income						
- Canadian	1,012,487	28.3	55,069	998,597	31.2	53,127
- US Funds	32,790	0.9	698	32,253	1.0	(1,511)
Equities						
- Canadian	1,035,680	28.9	240,076	986,797	30.8	163,797
- US	544,140	15.2	31,957	490,238	15.3	(3,288)
- Other foreign	474,085	13.2	54,472	199,209	6.2	(5,048)
Real Estate						
- Canadian	138,497	3.9	7,556	54,530	1.7	3,598
- Pooled fund	60,997	1.7	7,774	53,696	1.7	4,817
Derivatives	3,800	0.1	38,708	1,163	0.0	19,931
Other	-	-	34	-	-	58
	<u>\$ 3,582,798</u>	<u>100.0</u>	<u>\$ 446,244</u>	<u>\$ 3,202,226</u>	<u>100.0</u>	<u>\$ 243,207</u>

\* Includes realized gains of \$184.3 million (\$86.1 million - 2005) and unrealized gains of \$131.4 million (\$52.8 million - 2005).

(b) Derivative Contracts:

Derivatives are financial contracts, the value of which is “derived” from the value of underlying assets or interest or exchange rates. Derivatives provide flexibility in implementing investment strategy.

Money market-to-equity swaps have been used during the year to adjust the asset mix.

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**3. Investments and Derivatives (continued)**

The Fund is exposed to credit-related losses in the event of non-performance by counterparties to derivative financial instruments. In order to mitigate this risk, the Fund:

- deals only with highly rated counterparties 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; and
- enters into derivatives only for the purposes of managing risk.

Credit risk represents the maximum amount that would be at risk as at the reporting date if the counterparties 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 counterparties, less any prepayment collateral or margin received, as at the reporting date.

The following table provides details of these derivative contracts outstanding as at March 31, 2006:

<u>Notional Principal</u>	<u>Original Term</u>	<u>Credit Rating of Counter-party</u>	<u>Equity Index</u>	<u>BA Index</u>	<u>Market Value</u>
(000's)					(000's)
\$ 66,766	1.0 yr	AA(low)	S&P/TSE60	CAD-BA-CDOR	\$ 2,243
<u>107,460</u>	1.0 yr	AA(low)	S&P/TSE60	CAD-BA-CDOR	<u>1,557</u>
<u>\$ 174,226</u>					<u>\$ 3,800</u>

Notional amounts of these derivative contracts represent the volume of outstanding transactions and serve as the basis upon which the return from and the market value of the contracts are determined.

Money market-to-equity swap contracts are denominated in Canadian dollars and are reset quarterly.

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**3. Investments and Derivatives (continued):**

(c) Market value of investments and related income after allocating the effects of derivative contracts:

	<u>As at March 31, 2006</u>		<u>For the Year</u>	<u>As at March 31, 2005</u>		<u>For the Year</u>
	Asset	%	Income*	Asset	%	Income *
	(000's)		(000's)	(000's)		(000's)
Money market	\$ 105,745	3.0	\$ 5,743	\$ 230,218	7.2	\$ 4,197
Fixed income						
- Canadian	1,012,487	28.3	55,069	998,597	31.2	53,642
- US Funds	32,790	0.9	698	32,253	1.0	(1,511)
Equities						
- Canadian	1,214,057	33.8	282,941	1,143,485	35.7	186,742
- US	544,140	15.2	31,957	490,238	15.3	(3,288)
- Other foreign	474,085	13.2	54,472	199,209	6.2	(5,048)
Real Estate						
- Canadian	138,497	3.9	7,556	54,530	1.7	3,598
- Pooled fund	60,997	1.7	7,774	53,696	1.7	4,817
Other	-	0.0	34	-	-	58
	<u>\$ 3,582,798</u>	<u>100.0</u>	<u>\$ 446,244</u>	<u>\$ 3,202,226</u>	<u>100.0</u>	<u>\$ 243,207</u>

\* Includes realized gains of \$184.3 million (\$86.1 million - 2005) and unrealized gains of \$131.4 million (\$52.8 million - 2005).

(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 and credit risk. The Fund has set formal policies and procedures that establish an asset mix among equity, fixed income and real estate investments, require diversification of investments within categories, and set limits on the size of exposure to individual investments and counterparties. In addition, derivative financial instruments are used, where appropriate, to assist in the management of these risks.

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**3. Investments and Derivatives (continued):**

(i) Interest rate risk:

Interest rate risk refers to the fact that the Plan's financial position will change as market interest rates change. Interest rate risk is inherent in the nature of the pension plan business due to prolonged timing differences between cash flows related to the Plan's assets and cash flows related to the Plan's liabilities.

The value of the Plan's assets is affected by short-term changes in nominal interest rates and equity markets. Pension liabilities are exposed to the long-term expectation of rate of return on the investments as well as expectations of inflation and salary escalation. To meet these liabilities the Plan has established an asset mix policy of approximately 60% equities, 33% fixed income securities and 7% real estate. Long-term equity returns have historically shown high correlation with changes in inflation and salary escalation, while fixed income securities are sensitive to changes in nominal interest rates.

The following breakdown of fixed income securities as at March 31, 2006 is summarized in the following table:

	March 31, 2006					Average effective yield	March 31, 2005	
	Within 1 year	1 to 5 years	5 to 10 years	Over 10 years	Total		Total	Average effective yield
	(000's)	(000's)	(000's)	(000's)	(000's)	%	(000's)	%
Money market	\$ 280,322	-	-	-	\$ 280,322	3.8	\$ 385,743	2.6
Bonds and debentures	15,306	\$ 333,263	\$ 203,250	\$ 332,715	884,534	5.3	878,104	5.3
Real return bonds	-	-	-	127,953	127,953	3.1	120,493	3.0
US Fixed Income	<u>787</u>	<u>10,558</u>	<u>18,986</u>	<u>2,459</u>	<u>32,790</u>	6.5	<u>32,253</u>	6.7
Total	<u>\$ 296,415</u>	<u>\$ 343,821</u>	<u>\$ 222,236</u>	<u>\$ 463,127</u>	<u>\$ 1,325,599</u>		<u>\$ 1,416,593</u>	

The average effective yield reflects the estimated annual income of a security as a percentage of its year-end market value.

(ii) Market risk:

Market risk is the risk that the value of an investment will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual investment, or factors affecting all securities traded in the market.

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**3. Investments and Derivatives (continued):**

The Fund's policy is to invest in a diversified portfolio of investments, based on criteria established in the Statement of Investment Policies and Guidelines, and to utilize derivative financial instruments, which are designed to mitigate the impact of market risk.

(iii) Credit risk:

Credit risk is the risk of loss in the event the counterparty to a transaction fails to discharge an obligation and causes the other party to incur a loss.

The Plan limits credit risk by purchasing fixed income securities with a credit rating of "BBB" and higher. In addition, the Plan limits derivative contract risk by dealing with counterparties that have a minimum "A" credit rating.

(iv) Foreign currency risk:

Foreign currency exposure arises from the Plan's holding of equities denominated in foreign currency. From time to time some of this exposure will be hedged based on interest rates or other economic fundamentals.

The Plan's currency exposure from net investment assets as at March 31, 2006 is summarized in the following table.

<u>Currency</u>	<u>March 31, 2006</u>	<u>March 31, 2005</u>
	(000's)	(000's)
Canada	\$ 2,506,128	\$ 2,477,590
United States	610,995	551,936
Euro Zone	136,850	44,977
Japan	136,475	56,176
United Kingdom	78,455	26,911
Other	<u>96,455</u>	<u>49,503</u>
Total	<u>\$ 3,565,358</u>	<u>\$ 3,207,093</u>

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**4. Real Estate Mortgages:**

Real estate mortgages are carried at fair value and have various terms to maturity to 2018 with each mortgage secured by a specific real property. Nominal rates range from 5.2% to 7.0%

Scheduled principal repayments in each of the next five years, beginning April 1, 2006 are as follows:

2006	\$ 5,136
2007	1,618
2008	839
2009	5,517
2010	566
Thereafter	<u>23,450</u>
Total	<u>\$ 37,126</u>

The real estate mortgage payables are valued at fair value based on prevailing interest rates.

**5. Actuarial Asset Value Adjustment:**

The actuarial asset value adjustment is comprised of the following:

	<u><b>2006</b></u>	<u><b>2005</b></u>
	(000's)	(000's)
Service Buy-Back Receivable	<u>\$ 276</u>	<u>\$ 411</u>

This receivable represents the present value of outstanding employee and employer contributions which are due as a result of service buy-backs.

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**6. Accrued Pension Benefits and Deficiency:**

Actuarial valuations of the Fund are carried out annually and provide an estimate of the accrued pension benefits ("Fund liabilities") calculated using various economic and demographic assumptions, based on membership data as at the valuation date. The Plan's consulting actuaries, Mercer Human Resource Consulting, performed a valuation as at December 31, 2005 and issued their report in June 2006. The report indicated that the Plan had an unfunded liability of \$471.8 million (December 31, 2004 - \$542.7 million). A projection to March 31, 2006, applying the same assumptions, indicated an unfunded liability of \$410.7 million (March 31, 2005 - \$532.3 million).

At March 31, 2005, an amount of \$7.7 million attributable to termination benefits was included in net assets available for benefits. The amount was also included in the actuarial valuation of accrued pension benefits. Consequently, the deficiency of the Fund included the amount twice. The accrued pension benefits and deficiency at March 31, 2005 have been reclassified in the current year's statements to properly reflect this amount. The reconciliation of changes in accrued pension benefits has also been adjusted to reflect this reclassification.

The following table reflects the unfunded liability as at March 31, 2006 and as at March 31, 2005 after the reclassification.

	<u>2006</u>	<u>2005</u>
	(000's)	(000's)
Actuarial value of assets:	\$ 3,542,040	\$ 3,189,247
Accrued pension benefits:	<u>3,952,745</u>	<u>3,721,541</u>
Unfunded liability:	<u>(\$ 410,705)</u>	<u>(\$ 532,294)</u>

**Reconciliation of changes in accrued pension benefits:**

	<u>2006</u>	<u>2005</u>
	(000's)	(000's)
Accrued pension benefits at beginning of year	\$ 3,721,541	\$ 3,522,000
Interest on accrued pension benefits at 7.38%	274,557	259,836
Contributions and transfers from other pension plans	99,158	90,299
Current service cost in excess of contributions	11,545	18,500
Net impact of experience gains and losses relating to accrued pension benefits	29,870	3,119
Benefits paid	(173,445)	(164,074)
Refunds of contributions and interest and transfers to other pension plans	<u>(10,481)</u>	<u>(8,139)</u>
Accrued pension benefits at end of year	<u>\$ 3,952,745</u>	<u>\$ 3,721,541</u>



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**6. Accrued Pension Benefits and Deficiency (continued):**

The actuarial valuation projects liabilities for each member on the basis of service earned to date and the member's projected five year average salary at the expected date of retirement. The actuaries have used the unit credit method of determining the current cost and actuarial liability.

The major economic and demographic assumptions used in the last valuation are as follows:

	<b>Valuation <u>December 31, 2005</u></b>	<b>Valuation <u>December 31, 2004</u></b>
Inflation	3.0% per annum	3.0% per annum
Average Salary Increase	0.5% per annum real plus merit ranging from 0.0% to 2.5%	0.5% per annum real plus merit ranging from 0.0% to 2.5%
Real Rate of Return on Investment	4.25% per annum	4.25% per annum
Average Retirement Age	20% - age 55 or "Rule of 80" 80% - age 60 or 35 years service	20% - age 55 or "Rule of 80" 80% - age 60 or 35 years service
Mortality	1994 Group Annuity Mortality Table projected to 2000 using scale AA	1994 Group Annuity Mortality Table projected to 2000 using scale AA

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**7. Operating Expenses:**

The Fund is charged with administrative and certain other expenses incurred on behalf of the Fund by the Department of Finance. The following is a summary of these operating expenses:

	<u>2006</u>	<u>2005</u>
	(000's)	(000's)
<b>Plan Administration</b>		
Professional services	\$ 165	\$ 322
Salaries	805	799
Supplies and services	167	303
Travel	6	7
Other	90	108
	<u>\$ 1,233</u>	<u>\$ 1,539</u>
<b>Investment Expenses</b>		
Investment management fees	\$ 6,596	\$ 6,138
Professional services	57	60
Salaries	471	376
Supplies and services	114	90
Travel	12	12
Other	65	18
	<u>\$ 7,315</u>	<u>\$ 6,694</u>
<b>Total Operating Expenses</b>	<u>\$ 8,548</u>	<u>\$ 8,233</u>

**8. Related Party Transactions:**

Investments include debentures of the Province of Nova Scotia with total market value of \$14.4 million (0.4% of total assets) as at March 31, 2006 (\$18.3 million (0.6% of total assets) as at March 31, 2005).