FINANCIAL STATEMENTS

PENSION BENEFITS GUARANTEE FUND

FOR THE YEAR ENDED MARCH 31, 2014

MANAGEMENT'S STATEMENT

Financial Services Commission of Ontario

Deputy Superintendent
Pension Division

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Commission des services financiers de l'Ontario

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June 25, 2014

Pension Benefits Guarantee Fund
Management's Responsibility for Financial Information

The CEO and Superintendent of Financial Services of the Financial Services Commission of Ontario ("FSCO"), pursuant to the *Financial Services Commission of Ontario Act, 1997* and specifically, subsection 82(2) of the *Pension Benefits Act*, is responsible for the administration of the Pension Benefits Guarantee Fund (PBGF).

The PBGF Management Committee which comprises of senior management, professional actuarial, investment and accounting staff oversees the administration of the PBGF. The PBGF Management Committee meets quarterly to review and discuss issues related to the administration of the PBGF, and makes recommendations on these issues to the Superintendent of Financial Services.

In addition, Management maintains a system of internal controls, information systems and processes designed to provide reasonable assurance that the assets of the PBGF are safeguarded and that financial information is reliable and timely. The internal control systems include formal policies and procedures and an organizational structure which provides for appropriate Financial Delegation of Authority and the segregation of incompatible duties.

The Audit and Risk Committee, which includes the Superintendent of Financial Services, is responsible for ensuring Management fulfils its responsibilities for financial reporting and internal controls. The Audit and Risk Committee meets periodically with Management, internal and external auditors to address issues and to review the Financial Statements before recommending approval.

The accompanying Financial Statements of the PBGF have been prepared in accordance with the Canadian Public Sector Accounting Standards for Government Not-For-Profit Organizations (PSA-GNFPO). The preparation of the Financial Statements involves the use of Management's professional judgment and best estimates particularly when transactions affecting the current accounting period that cannot be finalized with certainty until future periods.

The Financial Statements have been audited by the Auditor General of Ontario. The Auditor General's responsibility is to express an opinion on whether the Financial Statements are presented fairly, in all material respects, in accordance with PSA-GNFPO. The Auditor's Report, which follows, outlines the scope of the Auditor's examination and the Auditor's opinion on the financial statements.

On behalf of management:

Brian Mills
Deputy Superintendent, Pensions

Leonard Lobo CGA; CPA
Senior Manager, Finance and Planning

AUDITOR'S STATEMENT

Ontario

Office of the Auditor General of Ontario
Bureau du vérificateur général de l'Ontario

Independent Auditor's Report

To the Financial Services Commission of Ontario and to the Minister of Finance

I have audited the accompanying financial statements of the Pension Benefits Guarantee Fund of the Financial Services Commission of Ontario, which comprise the statement of financial position as at March 31, 2014 and the statements of operations and fund surplus, cash flows and re-measurement gains and losses 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 public sector accounting standards, 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 my 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 about 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 accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In my opinion, the financial statements present fairly, in all material respects, the financial position of the Commission's Pension Benefits Guarantee Fund as at March 31, 2014, and the results of its operations and fund surplus, its cash flows and its re-measurement gains and losses for the year then ended in accordance with Canadian public sector accounting standards.

Toronto, Ontario
June 25, 2014

Gary R. Peall, CPA, CA, LPA
Deputy Auditor General

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STATEMENT OF FINANCIAL POSITION
AS AT MARCH 31, 2014

	March 31, 2014 ($ 000)	March 31, 2013 ($ 000)
ASSETS		
Current		
Cash	1	752
Accounts receivable	124,088	140,247
Investments (Note 4)	450,237	345,321
	574,326	486,320
LIABILITIES AND FUND SURPLUS		
Current		
Accounts payable and accrued liabilities	11,044	10,834
Current portion of loan payable (Note 5)	11,000	11,000
Claims payable	50,916	78,739
	72,960	100,573
Loan payable (Note 5)	125,657	129,577
	198,617	230,150
Fund surplus from operation	375,717	256,165
Accumulated remeasurement gains (losses)	(8)	5
Fund surplus	375,709	256,170
	574,326	486,320

See accompanying notes to financial statements

Approved by:

Philip Howell

Chief Executive Officer and
Superintendent of Financial Services
Financial Services Commission of Ontario

STATEMENT OF OPERATIONS AND FUND SURPLUS

FOR THE YEAR ENDED MARCH 31, 2014

	March 31, 2014 ($ 000)	March 31, 2013 ($ 000)
Revenue		
Premium revenue	138,819	145,295
Pension plan recoveries (Note 7)	9,424	52,770
Investment income (Note 4)	4,389	3,281
	152,632	201,346
Expenses		
Claims	18,532	12,051
Amortization of loan discount (Note 5)	7,081	7,268
Pension consulting services (Note 8)	6,886	1,420
Administration fee (Note 9)	451	474
Investment management fees (Note 9)	130	96
	33,080	21,309
Excess of revenue over expenses	119,552	180,037
Fund surplus, beginning of year	256,165	76,128
Fund surplus, end of year	375,717	256,165

See accompanying notes to financial statements

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED MARCH 31, 2014

	March 31, 2014 ($ 000)	March 31, 2013 ($ 000)
Net inflow (outflow) of cash related to the following activities		
Cash flows from operating activities		
Excess of revenue over expenses	119,552	180,037
Items not affecting cash:		
Amortization of loan discount (Note 5)	7,081	7,268
(Gains) losses on disposal of investments	116	(74)
	126,749	187,231
Changes in non cash working capital		
Accounts receivable	16,159	(35,559)
Claims payable	(27,823)	(30,548)
Accounts payable and accrued liabilities	210	2,897
	115,295	124,021
Cash flows from investing activities		
Purchases of investments	(3,633,576)	(3,792,182)
Proceeds from sale of investments	3,528,530	3,679,912
	(105,046)	(112,270)
Cash flows from financing activities		
Loan repayments	(11,000)	(11,000)
	(11,000)	(11,000)
Change in cash position	(751)	751
Cash position, beginning of year	752	1
Cash position, end of year	1	752

See accompanying notes to financial statements

STATEMENT OF RE-MEASUREMENT GAINS AND LOSSES

FOR THE YEAR ENDED MARCH 31, 2014

	March 31, 2014 ($ 000)	March 31, 2013 ($ 000)
Accumulated re-measurement gains, beginning of year	5	114
Unrealized gains (losses) attributed to portfolio investments	103	(183)
Realized gains (losses) reclassified to the statement of operations	(116)	74
Accumulated re-measurement gains (losses), end of year	**(8)**	**5**

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

MARCH 31, 2014

1. STATUTORY AUTHORITY

The Pension Benefits Guarantee Fund (the "Fund") is continued under the P*ension Benefits Act, R.S.O. 1990, c. P.8* (the "Act").

2. FUND OPERATIONS

The purpose of the Fund is to guarantee payment of pension benefits of certain defined benefit pension plans that are wound up under conditions specified in the *Act* and regulations thereto. The regulations also prescribe an assessment payable into the Fund by plan registrants.

The Act provides that if the assets of the Fund are insufficient to meet payments for claims, the Lieutenant Governor in Council may authorize the Minister of Finance of Ontario to make loans or grants on such terms and conditions as the Lieutenant Governor in Council directs. The total liability of the Fund to guarantee pension benefits is limited to the assets of the Fund including any loans or grants received from the Province.

The Superintendent of the Financial Services Commission of Ontario ("FSCO") pursuant to the *Financial Services Commission of Ontario Act, 1997* is responsible for the administration of the Fund, and the Fund reimburses FSCO for the costs of the services provided to the Fund. The investments of the Fund are managed by the Ontario Financing Authority, on a fee-for-service basis which is paid by the Fund.

3. SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Fund have been prepared by the management of FSCO in accordance with Public Sector Accounting Standards for Government Not-For-Profit organizations (PSA-GNFPO) as issued by the Public Sector Accounting Board (PSAB). Accordingly, management has used the following significant accounting policies in their preparation.

(a) Financial Instruments

The Fund follows PSA-GNFPO accounting standards relating to financial instruments. Under these standards, all financial instruments are included on the balance sheet and are measured either at fair value or at cost or amortized cost as follows:

- Cash and investments are recorded at fair value, with changes in fair value during the period recognized in the statement of re-measurement gains and losses until realized. Fair value is determined from quoted prices for similar investments.
- Accounts receivable, account payable and accrued liabilities are valued at cost which approximate fair value given their short term maturities.
- The non-interest bearing loan payable is reflected at amortized cost using the effective interest rate method due to the concessionary nature of the loan. The initial valuation was determined by discounting future cash flows using the provincial cost of borrowing. The resulting benefit (the difference between the face value of the loan and the net present value) was accounted for as a grant in the year received and is amortized to loan discount expense over the term of the loan.

(b) Claims Payable

Claims payable are estimates of the liabilities in respect of those defined benefit pension plans prescribed by the Act that are wound up or in the process of being ordered wound up under conditions specified in the Act, and the claim amounts can be reasonably estimated. Liabilities are also recognized when there is a high probability that a company will not emerge from creditor protection and the pension plan will be wound up on a specified date and the claim can be reasonably estimated. Claims payable are based on information provided by appointed pension plan administrators from estimates provided by actuarial consultants. These estimates represent the present value of future payments to settle claims for benefits and expenses by pension plans.

Differences in the liabilities, if any, between the amounts recognized based on estimates and the actual claims made, will be charged or credited to claims expense in the year when the actual amounts are determined.

(c) Premium Revenue

An estimate of the premium revenue due from defined benefit pension plans at rates prescribed by the Act is recorded until receipt of the annual assessment certificate nine months after the plan's fiscal year end.

Differences in premium revenue, if any, between the estimated amounts recognized and the actual revenues due are charged or credited to premium revenue in the year.

(d) Use of Estimates

The preparation of financial statements in accordance with PSA-GNFPO accounting standards requires that FSCO's management make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent liabilities as at the date of the financial statements and the reported amounts of revenue and expenses for the period. Estimates and assumptions may change over time as new information is obtained or subsequent developments occur. Actual results could differ from these estimates and the differences could be material. Areas where significant estimates must be made include premium revenue and claims payable.

(e) Comparative Figures

Certain of the prior year's comparative figures have been reclassified to conform to the current years' financial presentation.

NOTES TO FINANCIAL STATEMENTS

MARCH 31, 2014

4. INVESTMENTS

As the administrator, investing the assets of the Fund, FSCO has established a Pension Benefits Guarantee Fund Management Committee. The Committee has developed a Statement of Investment Policies and Guidelines which is reviewed regularly and provides operational objectives, investment principles, policies and guidelines for the management of the investments.

Investments consist of:

	2014		2013	
	($'000)			
	Fair Value	**Cost**	**Fair Value**	**Cost**
Discounted notes	443,819	443,819	252,205	252,204
Government bonds	6,418	6,426	93,116	93,111
	450,237	**450,245**	**345,321**	**345,315**

Investment income includes interest earned from interest bearing securities and realized gains and losses from the sale of securities.

The Fund's investment portfolio is exposed to various risks, which are mitigated by the type of investment and therefore risk is low.

The market value sensitivity of the portfolio at the end of the last quarter was $0.7M for a 1.00% change in rates.

Discounted notes with maturities between April 2014 and July 2014 have yields in the range of 0.880% to 1.130% (2013—maturities between April 2013 and July 2013 had yields in the range of 0.960% to 1.140%).

The Government bond matures in October 2014 and has yield of 1.515% (2013—maturities between June 2013 and December 2013 had yields of 1.275% to 1.294%).

5. LOAN PAYABLE

Non-interest Bearing Loan

On March 31, 2004, the Fund obtained a $330M loan from the Province, a related party. The loan is non-interest bearing and repayable to the Province in thirty equal annual installments of $11M. The loan agreement provides for the Minister of Finance to advance any installment payment date depending on the cash position of the Fund. Repayments over the next five years total $55M.

The face value of this non-interest bearing loan has been discounted at an effective interest rate of 5.0368% to reflect its amortized cost outstanding as of March 31, 2014 as follows:

	2014 ($'000)	2013 ($'000)
Face Value	220,000	231,000
Less: Discount	(83,343)	(90,423)
Amortized Cost	136,657	140,577
Classified as:		
Current Portion	11,000	11,000
Long Term Portion	125,657	129,577
Balance	136,657	140,577

The discount of $83.3M is amortized to loan discount expense over the term of the loan, based on the effective interest rate method. The amortization schedule for the subsequent five fiscal years is as follows:

Fiscal Year	($'000)
2015	6,883
2016	6,676
2017	6,458
2018	6,229
2019	5,989

6. FINANCIAL INSTRUMENTS

The main risks that the Fund's financial instruments are exposed to are credit risk, liquidity risk and market risk.

Credit risk

Credit risk is the risk that the counterparty to a financial instrument may fail to discharge an obligation or commitment that it has entered into. The Fund is exposed to credit risk relating to the collection of receivables. The Fund considers this risk to be low.

The Fund's accounts receivable consists of premium revenue receivable of $124M, investment income receivable of $0.28M and the HST receivable of $0.19M.

The premium revenue receivable recorded is based on an assessment formula set out in section 37 of Regulation 909 of the Act and is calculated as follows:

- Base assessment of $5 per Ontario plan beneficiary plus specified percentages of the plans PBGF assessment base.
- Maximum assessment of $300 per Ontario plan beneficiary and
- Minimum assessment of $250 for each plan

NOTES TO FINANCIAL STATEMENTS

MARCH 31, 2014

The probability for a pension plan to become insolvent and not pay the premium within a year is very low. In addition, in the event that a pension plan would become insolvent within a year, there are legal options for the Fund that can be exercised to collect the premiums. Historically, the Fund has been able to collect the amounts estimated as premium receivable.

The risk of not collecting the investment income and the HST receivable is considered to be minimal.

Liquidity Risk

Liquidity risk is the risk that the Fund will not be able to meet its cash flow obligations as they fall due. The Fund's exposure to liquidity risk is minimal as the Fund has sufficient funds in its investment portfolio to settle all current liabilities. As at March 31, 2014, the Fund has an investment balance of $450M (2013 – $345M) to settle current liabilities of $73M (2013 – $101M). In addition, the Fund has the ability to meet sudden and unexpected claims by converting the investment holdings to cash without delay or significant transaction costs.

Market risk

Market risk arises from the possibility that changes in market prices will affect the value of the financial instruments of the Fund. Short-term financial instruments (receivables, accounts payable) are not subject to significant market risk. The Fund manages its market risk by investing assets in low-risk and liquid securities. The Fund's market risk is considered to be low.

7. PENSION PLAN RECOVERIES

Following the settlement of all benefits, payment of expenses and the submission of the final wind up report, any remaining funds are recovered by the Fund. During fiscal 2014, the Fund had $9.4M (2013 – $52.8M) in recoveries. Approximately $1M in recoveries is expected in the fiscal year 2015.

8. PENSION CONSULTING SERVICES

The Fund periodically engages the services of external experts to represent the Fund's interests in insolvency proceedings respecting employers who are unable to meet their funding obligations under the *Pension Benefits Act*. For fiscal 2014, $6.9M was paid to such external experts (2013 – $1.4M paid).

9. RELATED PARTY TRANSACTIONS

For fiscal 2014, an administration fee of $0.5M (2013 - $0.5M) was incurred and has been paid to FSCO for management salaries and benefits, accounting, information technology, legal, pension and other services. The Fund and FSCO are related parties.

Investment Management fees consist mainly of fees paid to the Ontario Financing Authority, a related party.

The costs of processing premium revenue transactions are absorbed by FSCO without charge to the Fund.

Other related party transactions during the year have been disclosed in note 5.