



Manitoba Telecom Services Inc.  
and Participating Subsidiaries  
Employee Pension Plan



Annual Report  
**10**



### **For More Information**

If you have any questions about the information contained in this Annual Report, if you would like to receive a copy of the MTS Pension Plan's Statement of Investment Policies and Goals, or if you would like to provide any comments concerning this Annual Report, please contact:

#### **MTS Pension Plan**

Benefits Administration  
P.O. Box 6666  
19th Floor, 333 Main Street  
Winnipeg, Manitoba R3C 3V6  
Phone No.: (204) 941-7347 or 1-800-635-4973  
Fax No.: (204) 774-3163  
e-mail: [mtspensionplan@mtsallstream.com](mailto:mtspensionplan@mtsallstream.com)

If you would like more information on your personal retirement or termination benefits, please contact the MTS Pension Plan's administrative services provider:

#### **The Civil Service Superannuation Board**

1200 - 444 St. Mary Avenue  
Winnipeg, Manitoba R3C 3T1  
Phone No.: (204) 946-3200 or 1-800-432-5134  
Fax No.: (204) 945-0237

# TABLE OF CONTENTS

2 Message from the Chief Executive Officer

3 About Your Plan

12 About the Investments

18 Summary Financial Statements



## MESSAGE FROM THE CHIEF EXECUTIVE OFFICER

I am pleased to provide you with the MTS Pension Plan Annual Report for the year ending December 31, 2010.

The global economic recovery continued in 2010 and the assets of the MTS Pension Plan produced a strong annual return of 9.1%. The MTS Pension Plan assets ended the year with a market value of approximately \$1.35 billion, up from \$1.25 billion in 2009. The 2010 investment performance was generated by positive returns in every asset class in which the Plan is invested. Over the long-term, the MTS Pension Plan has generated a positive annualized return of 6.9% since its inception in 1997, exceeding its performance objective of 6.0%.

In 2010, the Company continued its support of the MTS Pension Plan, contributing \$57.0 million for the year, complemented by employee contributions of \$10.6 million. Since inception of the MTS Pension Plan in 1997, the Company has funded \$376.4 million and employees have funded \$134.1 million to the Plan.

In 2010, the Federal Government introduced several new pension reforms concerning the funding and administration of pension plans registered under the *Pension Benefits Standards Act, 1985* (Canada). The primary intent of the federal pension reform is to provide enhanced protection for pension plan members. Further details on the federal pension reform measures are outlined in the Pension Reform section of the report.

The MTS Pension Plan remains conservatively invested and well diversified to address the ever present risks that exist in financial markets. Growth opportunities also exist in those financial markets, so the MTS Pension Plan remains fully invested to capitalize on those opportunities. Regardless of the ebbs and flows of the economic and market cycles, the MTS Pension Plan will remain focused on its long-term investment strategy. In addition, the Company remains committed to ensuring that the MTS Pension Plan is secure and can meet its obligations to retirees and employees. The security of your future pension benefits remains a high priority.

Sincerely,



**Pierre Blouin**  
CHIEF EXECUTIVE OFFICER

# ABOUT YOUR PLAN

## HIGHLIGHTS

The MTS Pension Plan (the “Plan”) is a contributory defined benefit plan that provides pension benefits to certain employees and retirees of Manitoba Telecom Services Inc. (“MTS”) and its participating subsidiary, MTS Allstream Inc. (collectively the “Company”).

Here are some highlights of the Plan:

- Eligible employees contribute to the Plan by payroll deduction each pay period. These contributions are fully tax deductible. The Company contributes the amounts necessary to ensure that the Plan can meet its obligations. The Company contributed \$57 million to the Plan in 2010.
- Plan benefit payments to retirees and beneficiaries were \$56 million in 2010.
- At retirement, members are eligible for a pension based on a formula using their average earnings during the five years of employment when their earnings were the highest and their years of credited service as a member of the Plan.
- Members may retire with an unreduced pension at or after age 55 if their age plus years of continuous service total at least 80. Members also may retire with an unreduced pension at age 60 if they have at least 10 years of continuous service. Members may retire with a reduced pension at or after age 55 if they have completed at least two years of continuous service, or as early as age 45 if their age plus years of continuous service equals at least 70.
- The Plan provides for a guaranteed cost of living adjustment (“COLA”) equal to two-thirds of the increase in the Canadian Consumer Price Index (“CPI”) to a maximum CPI increase of 4%.
- Members who leave the Company before they are eligible to retire, but after at least two years of continuous service with the Company, are entitled to a deferred pension (which is a pension that is payable when they are eligible to retire). They also may choose to transfer the value of the pension to a locked-in RRSP.

For more details on the Plan, please refer to the MTS Pension Plan Web site at [www.mtspensionplan.ca](http://www.mtspensionplan.ca).

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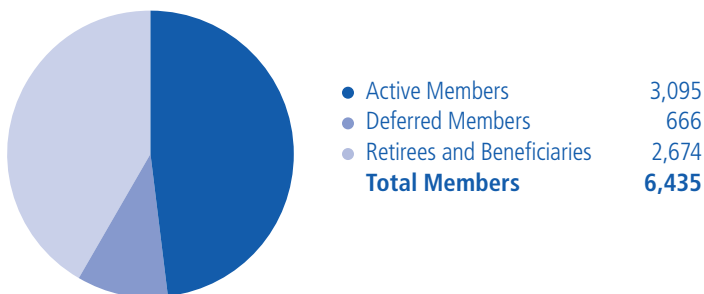
## PRIVACY

The Company is dedicated to protecting your privacy and safeguarding your personal information. The Company collects, uses or discloses personal information for the purpose of administering the Plan. Access to your personal information is limited to certain Company staff, The Civil Service Superannuation Board which provides administrative services in respect of the Plan, the Plan’s Actuary, persons to whom you have authorized access, and persons authorized by law.

## MEMBERSHIP

The Plan's membership falls into three categories: active, deferred, and retirees and their beneficiaries. Active members are those employees who currently contribute to the Plan. Deferred members are former employees who have left their pension benefits in the Plan to be paid at a later date. Retirees and beneficiaries are those individuals who currently receive a pension from the Plan.

The membership in the Plan at December 31, 2010 was as follows:



The total number of Plan members decreased by 91 from the end of 2009. There was a decrease in the number of active members (152), and an increase in the number of retirees (48) and deferred members (13).

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## YOUR PENSION BENEFIT

Your pension benefit is calculated using a defined benefit formula, which includes the average of your best five years of earnings ("Best Average Earnings"), multiplied by the number of years or partial years you have contributed to the Plan (referred to as "Credited Service").

The formula is as follows:

$$\begin{aligned} & \mathbf{2.0\%} \text{ of your Best Average Earnings} \\ & \quad \textit{Multiplied by} \\ & \quad \text{Your years of Credited Service} \\ & \quad \textit{Less} \\ & \mathbf{0.6\%} \text{ of the average YMPE (for the same five years of earnings)} \\ & \quad \textit{Multiplied by} \\ & \quad \text{Your years of Credited Service} \end{aligned}$$

(YMPE, or Year's Maximum Pensionable Earnings, is the limit set by the federal government each year to determine the maximum Canada Pension Plan contributions and benefits.)



- Donna Rawluk (retiree)

## BENEFIT CALCULATION EXAMPLE

Consider an employee who retires from the Plan at age 55 on December 31, 2010. The employee has Best Average Earnings of \$60,000 and 30 years of Credited Service. The average YMPE in this example is \$44,840.

2.0% x \$60,000 (Best Average Earnings)	\$	1,200
<i>Multiplied by</i>		
30 years Credited Service	X	30
		<u>\$ 36,000</u>
<i>Less</i>		
0.6% x \$44,840 (average YMPE)	\$	269
<i>Multiplied by</i>		
30 years Credited Service	X	30
		<u>\$ 8,071</u>
Annual Benefit*	\$	<u>27,929</u>

\*The actual benefit you receive will be affected by a number of factors, including your earnings, your age at retirement, your years of Credited Service, future COLA increases to pension payments and the survivor benefit option that you choose.

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## COST OF LIVING ADJUSTMENTS

The Plan provides for a guaranteed COLA increase to pension payments each year. This guaranteed COLA is equal to two-thirds of the increase in CPI to a maximum CPI increase of 4%. COLA increases are granted each July. In 2010, retirees received a COLA increase of 0.88%, which was two-thirds of the 2009 CPI increase of 1.32%. Past COLA increases account for approximately 18% of the pension benefits paid to retirees in 2010. In 2011, retirees will receive a COLA increase of 1.57% which is two-thirds of the 2010 CPI increase of 2.35%.

The guaranteed annual COLA increase is a valuable benefit that many other pension plans in Canada do not have.

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## IT'S A DEFINED BENEFIT PLAN

The Plan is a defined benefit pension plan. This means that your benefit is a predictable amount determined by a formula based on your earnings during the five years when they were the highest and your years of participation in the Plan. Your benefit does not depend on the rate of return earned by the Plan's investments. Employees contribute to the Plan based on a set formula, and the Company contributes the additional amounts necessary to pay the benefits that you earn. A predictable retirement income is the most desirable feature of a defined benefit pension plan.

## SOURCES OF FUNDING

The money necessary to pay the benefits promised by the Plan comes from three sources:

- Company contributions;
- Employee contributions; and
- Investment earnings.

In 2010, the Company's contributions were the largest cash inflow source for the Plan. Of the \$114.4 million in total cash inflows in 2010, the Company's contributions accounted for \$57.0 million or 50%, realized net investment income accounted for \$46.8 million or 41%, and employee contributions accounted for \$10.6 million or 9%.

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## COMPANY CONTRIBUTIONS

The Company contributes the amount necessary to ensure that benefits earned can be paid when they are due. This does not mean that the Company contributes \$1 at the same time you contribute \$1. The timing of the Company's contribution is determined by an actuarial valuation completed in accordance with pension legislation. In 2010, the Company contributed \$57.0 million, consisting of \$17.8 million in normal cost funding and \$39.2 million in additional contributions. Since the inception of the Plan in 1997, the Company has contributed \$376.4 million to the Plan. This level of funding demonstrates the Company's commitment to your secure retirement.

The actuarial funding valuation completed as at January 1, 2011, showed that the Plan was in a surplus position of \$39 million on a going concern basis, and in a deficit position of \$217 million on a solvency basis. The solvency valuation assumes that the Plan terminated on the date the valuation was done, while the going concern valuation assumes that the Plan will continue operating indefinitely. The Plan's going concern liabilities were \$1,309 million as at January 1, 2011. On a solvency basis the liabilities were \$1,677 million. The Plan's going concern funded ratio was 103%, while the Plan's solvency funded ratio was 87% as at January 1, 2011. Until the Plan is fully funded on a solvency basis while remaining fully funded on a going concern basis, the Company will continue to make additional contributions. The next actuarial funding valuation will be completed as at January 1, 2012.

In 2006, the Government of Canada enacted *Solvency Funding Relief Regulations* under the *Pension Benefits Standards Act, 1985* (Canada) ("PBSA") which apply to federally-regulated defined benefit pension plans. Pursuant to these regulations, the Company arranged for \$106.9 million in letters of credit to be held by RBC Dexia Investor Services Trust, the trustee for the Plan. A letter of credit is a guarantee of payment issued by a bank to a third party, which in this case is the Plan, for a specific amount of money.

With the introduction of new pension funding regulations in 2011, as detailed in the Pension Reform section starting on page 8, the Company intends to cease funding under the 2006 *Solvency Funding Relief Regulations* and leave the outstanding letters of credit in the Plan to be included in the Plan's solvency funded position calculation. Starting in 2011, the Company will also be able to use letters of credit to fund all or a portion of its annual additional contribution requirements as a result of the Plan's solvency deficit.

## EMPLOYEE CONTRIBUTIONS

Employee contributions to the Plan are based on the employee's earnings as follows:

- 5.1% of earnings up to the YMPE, and
- 7.0% of earnings over the YMPE

Employee contributions totaled \$10.6 million in 2010, and since the inception of the Plan in 1997, employees have contributed \$134.1 million.

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## INVESTMENT EARNINGS

The third source of funds for the Plan is earnings on the investments held in the Plan's trust fund. Further information on the Plan's investment earnings is available beginning on page 16 of this Annual Report.

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## PAYMENTS FROM THE PLAN

In 2010, payments made from the Plan were as follows:

Pension payments to retirees and beneficiaries	\$ 56.0 million
Termination and lump-sum death benefit payments	\$ 14.6 million
Administrative expenses	\$ 1.2 million
<b>Total</b>	<b>\$ 71.8 million</b>

Pension payments to retirees increased by \$1.5 million or 3% from 2009, and termination and lump-sum death benefit payments increased by \$5.3 million or 57% from 2009.

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## PENSION REFORM

In 2009, the Federal Government announced proposed new pension reform measures for pension plans regulated under the PBSA. The purpose of the pension reform proposals is to provide enhanced benefit protection for pension plan members while reducing funding volatility for pension plan sponsors. Many of the Federal pension reform measures were implemented in 2010, while the remainder are being implemented throughout 2011. The key pension reform measures applicable to the Plan include the following:

### Funding Reform

- An annual solvency funding valuation report is required unless the pension plan has a funded ratio of at least 120%, in which case a valuation report can then be completed every third year.
- Employer normal cost funding can only be reduced if the pension plan has a 105% solvency ratio and is in a going concern surplus position.



- Tom Anderson (retiree)



- Commencing in 2011, any required employer funding must be remitted to the pension plan monthly (previously quarterly).
- The minimum solvency funding requirements for the employer are determined based on a three year average solvency ratio.
- Plan sponsors can use letters of credit (issued by a highly rated financial institution) to satisfy solvency funding payment requirements up to a limit of 15% of pension plan assets.

### **Member Disclosure Reform**

- Plan sponsors are required to provide an explanation of any amendments to pension plan members within 60 days of making the amendment.
- Retirees and deferred members are to receive annual benefit statements.
- Plan sponsors must inform members about the last reported solvency ratio, the date of the next required funding valuation, the ten largest pension plan investment holdings and the pension plan's asset allocation. The Company is already providing this information to members in the Annual Report and will continue to do so.
- The Office of the Superintendent of Financial Institutions will be establishing rules that will permit plan sponsors to communicate information to pension plan members in electronic format.

### **Benefit Reform**

- Immediate vesting of pension benefits (previously those terminating with less than two years of service received back their contributions plus interest).
- For terminating employees who are eligible to retire, spousal or common-law partner consent is required before pension benefits can be transferred out of a pension plan.
- Plan amendments are considered void unless the pension plan has a designated solvency ratio of 85% or greater after taking into consideration the impact of the amendment.

## **BUYER BEWARE**

When employees retire or terminate their employment, they are faced with the decision of whether to keep their pension funds in the Plan or to transfer the funds to a locked-in RRSP. This is always a difficult decision to make, and one that should not be made without receiving some sound advice.

It may or may not be in your best interests to transfer your money out of the Plan once you are no longer an active employee. Everyone's situation is different. However, before making this decision, we strongly suggest that you seek professional advice, not only from your financial advisor, but from someone knowledgeable about income taxes. You also may want to speak to family and former co-workers who may have been through a similar situation.

If you decide to transfer your pension funds out of the Plan, it is important that you be absolutely sure of your decision. Once the funds have been transferred out of the Plan, the Company and the Plan no longer guarantee, or remain in any way responsible for, your pension. Any financial losses that you may incur due to your investment decisions or those of your financial advisor are entirely your responsibility.

## PENSION COMMITTEE

The Pension Committee reports to the Audit Committee of the Board of Directors. The Pension Committee met twice in 2010. In accordance with its mandate, the Committee reviewed the results of the funding actuarial valuation and the COLA actuarial valuation, and reviewed the Plan's investment performance and other administrative aspects of the Plan.

The current members of the Pension Committee are as follows:

<b>Rod Pennycook</b> (Chair)	Retired (formerly with The Great-West Life Assurance Company)
<b>Bob Linsdell</b>	TEAM Representative
<b>Gord Mackay</b>	Director Pensions, MTS
<b>Debbie Marantz</b>	CEP Representative
<b>Brenda McInnes</b>	Vice-President & Treasurer, MTS
<b>Harry Restall</b>	Retiree Representative
<b>Don Rooney</b>	Director Labour Relations, MTS
<b>Don Senkow</b>	IBEW Representative
<b>Laurie Stewart</b>	Director Financial Planning & Analysis, MTS

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## LEGAL PROCEEDING

The lawsuit that was filed by the unions and certain retiree and employee representatives in September 1999 in relation to the Plan is continuing. An update on the lawsuit is provided in Note 8 to the Financial Statements beginning on page 25 of this Annual Report.

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## PLAN WEB SITE

The Plan Web site gives Plan members the opportunity to learn more about their Plan, keep up-to-date on what's new, and to even view this Annual Report. This Web site can be found at [www.mtspensionplan.ca](http://www.mtspensionplan.ca).

# ABOUT THE INVESTMENTS

## INVESTMENT COMMITTEE

The Investment Committee oversees and directs the investment of the Plan's funds by establishing investment principles and guidelines, recommending investment managers and monitoring the performance of the Plan's investments. The Investment Committee reports on the performance of the Plan's investments to the Audit Committee of the Board of Directors each year.

The current members of the Investment Committee are as follows:

<b>Wayne Demkey</b> (Chair)	Chief Financial Officer, MTS
<b>Brenda McInnes</b>	Vice-President & Treasurer, MTS
<b>Pat Solman</b>	Vice-President Regional Operations, MTS Allstream Inc.
<b>John Smith</b>	Senior Vice-President, Institutional Investment Counseling, GLC Asset Management Group
<b>Neil Benditt</b>	Retired (formerly Assistant Deputy Minister of Finance, Province of Manitoba)
<b>Rod Pennycook</b>	Chair, MTS Pension Plan Pension Committee

During 2010, the Investment Committee held four regular quarterly meetings to discuss the performance of the Plan's managers.

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## ASSET MIX

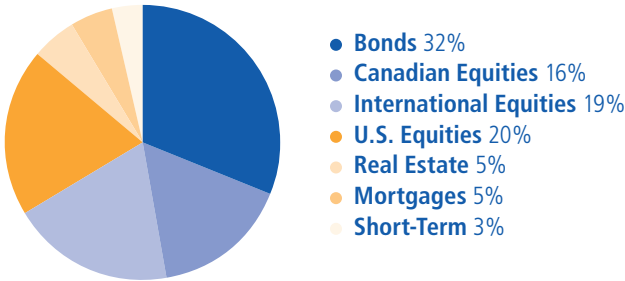
Strong investment returns are important to growing the Plan's assets. To achieve this in volatile financial markets, it also is important that the Plan has a diversified asset mix that is designed to achieve long-term growth, while preserving capital during years of negative performance in financial markets. The policies that govern the Plan are designed to ensure a disciplined and balanced approach to investing, which helps achieve both growth and capital preservation.

The Plan's asset mix is the combination of the different types of assets in which the Plan is invested, such as bonds, equities, mortgages and real estate. The Plan's funds are invested in a diversified portfolio of different types of assets because diversification—not putting all your eggs in one basket—is a fundamental principle of investing. If one type of asset results in a loss, a gain in another may offset the loss. For example, if Canadian equities perform poorly during the year, this may be offset by positive gains in bonds and real estate assets. Investing in a diversified asset mix is a strategy that minimizes risk and provides more stability in investment returns over time.

The Investment Committee is responsible for determining the asset mix guidelines for the Plan's investments. This is done in conjunction with an actuarial consultant during a process called an asset/liability study. The purpose of this study is to determine the most appropriate asset mix for the Plan's funds for the long-term. These studies are typically conducted every four to six years. An asset/liability study was completed for the Plan in 2007, and the result of this study led to the adoption of the target asset mix that currently is being used as a basis for the Plan's investments.

## INVESTMENTS AT DECEMBER 31, 2010

At the end of 2010, the Plan's investments (excluding cash and accrued income) totaled \$1,331 million. The following chart and table show how the Plan's assets were invested.



INVESTMENT	MARKET VALUE (\$ MILLIONS)
<b>Bonds</b>	\$ 416
<b>Canadian Equities</b>	\$ 216
<b>International Equities</b>	\$ 254
<b>U.S. Equities</b>	\$ 263
<b>Real Estate</b>	\$ 69
<b>Mortgages</b>	\$ 67
<b>Short-term Investments</b>	\$ 46
<b>Total Funds</b>	<b>\$ 1,331</b>

The following table shows the ten largest investment holdings held directly by the Plan and their percentage of the total portfolio market value:

MTS PENSION PLAN TOP 10 DIRECT HOLDINGS		
<b>Government of Canada<sup>1</sup></b>	\$ 87,760,332	6.6%
<b>Canada Housing Trust<sup>1</sup> (Government Guaranteed)</b>	\$ 81,585,846	6.1%
<b>Province of Ontario<sup>1</sup></b>	\$ 37,144,685	2.8%
<b>Bank of Nova Scotia<sup>1,2</sup></b>	\$ 20,523,552	1.5%
<b>Toronto Dominion Bank<sup>1,2</sup></b>	\$ 18,196,897	1.4%
<b>Canadian Imperial Bank of Commerce<sup>1,2</sup></b>	\$ 15,363,487	1.1%
<b>Royal Bank of Canada<sup>1,2</sup></b>	\$ 13,528,349	1.0%
<b>Apple Inc<sup>2</sup></b>	\$ 12,884,507	1.0%
<b>Google Inc<sup>2</sup></b>	\$ 11,154,692	0.8%
<b>Province of Quebec<sup>1</sup></b>	\$ 9,353,272	0.7%

<sup>1</sup>Bond investment <sup>2</sup>Equity investment

## ASSET TYPES

**Short-term Investments:** primarily cash and securities that mature within days, weeks or months (such as Government of Canada treasury bills). These investments generate income by receiving interest payments or by their purchase at a discount to mature at par. Income is based on the market's short-term interest rates.

**Bonds:** primarily investments in Canadian-issued federal, provincial and corporate bonds having semi-annual interest payments and terms to maturity over one year. Bonds generate income through interest payments and increases in value. Over the long-term, bonds historically have produced lower rates of return with more stability (smaller differences from year-to-year) relative to equities.

**Equities:** primarily investments in common shares of Canadian, U.S. and international companies. Equities generate income through dividends and increases in share value. Over the long term, equity investments historically have produced higher rates of return with more volatility (larger differences from year-to-year) relative to other asset types.

**Mortgages:** primarily investments in high quality mortgages on Canadian commercial properties. Mortgage investments generate income through interest payments.

**Real Estate:** primarily investments in buildings and property. Real estate investments generate income from rental income and increases in asset value.



- Warren Reimer (retiree)

## INVESTMENT MANAGERS

The responsibility for investing the Plan's assets rests with external investment managers under the direction of the Investment Committee and the Audit Committee of the Board of Directors. The investment managers and the types of assets that they manage are as follows:

- **AllianceBernstein Institutional Investment Management** (international equities)
- **Beutel, Goodman & Company Ltd.** (Canadian equities and Canadian bonds)
- **BonaVista Asset Management Ltd.** (Canadian equities)
- **The Great-West Life Assurance Company** (real estate and mortgages)
- **MFS Institutional Advisors, Inc.** (international equities)
- **Natcan Investment Management Inc.** (small capitalization Canadian equities)
- **Phillips, Hager & North Investment Management Ltd.** (Canadian bonds)
- **Sprucegrove Investment Management Ltd.** (U.S. and international equities)
- **T. Rowe Price Associates, Inc.** (U.S. equities)

The Plan's investment managers were chosen for the following reasons:

- the quality and experience of their investment management teams;
- their investment approach and style;
- their investment performance track record over several market cycles; and
- the level of fees that they charge.

Where more than one investment manager directs the investment of a single asset type, such as Canadian equities, the investment managers were chosen for their complementary investment styles.

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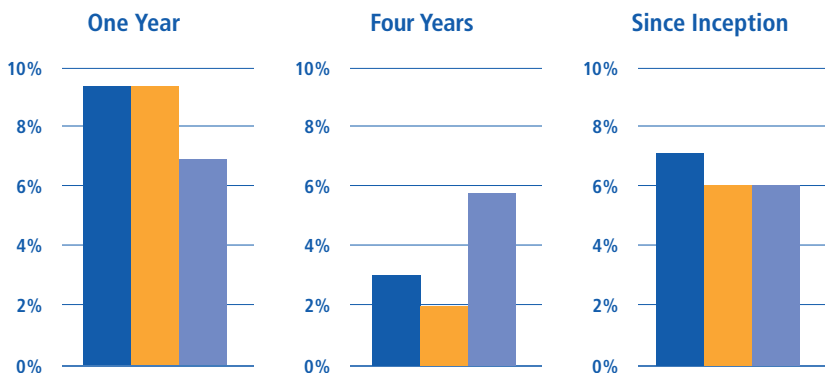
## CUSTODIAN/TRUSTEE

The custodian/trustee for the Plan is RBC Dexia Investor Services Trust, a joint venture that is equally owned by Royal Bank of Canada and Dexia. RBC Dexia Investor Services is responsible for the custody of the investment assets held in the Plan's trust fund.

## PLAN PERFORMANCE

The Investment Committee measures the Plan's rate of return against its long-term performance objective of the annual rate of inflation (which is the annual change in the CPI for Canada) plus 4%. In order to measure the success of the Plan's active investment managers, the Investment Committee also compares the Plan's rate of return against the weighted average of the markets' returns for the Plan's normal policy mix (the "benchmark").

Although annual returns are reviewed carefully, it is the Plan's performance over longer periods that best indicate how well the Plan's funds are invested.



	One Year (2010)	Four Years (Annualized) (2007–2010)	Since Inception (Annualized) (January 1997)
● MTS Pension Plan Return	9.1%	3.0%	6.9%
● Customized Benchmark	9.1%	1.9%	6.0%
● Performance Objective (CPI + 4%)	6.4%	5.8%	6.0%

### 9.1% INVESTMENT RETURN IN 2010

The Plan invests in a diversified portfolio of assets, including Canadian equities, U.S. equities, international equities, bonds, real estate, mortgages and short term investments.

Following a spectacular 2009, equity markets delivered another solid year due to growing confidence in the global recovery. This resulted from the combination of improving U.S. economic performance, strong corporate results, provisional containment of the European sovereign debt crisis and further rounds of monetary stimulus. Canadian equities in particular had a strong year, led by double digit returns in the Materials (mining, chemicals, plastics, metals, forest products, agriculture) and Energy (oil and gas) sectors which now account for over 50% of the S&P/TSX Composite Index. Although more volatile over the short-term, the investment of a portion of the

Plan's investments in equity assets provides the Plan with the greatest opportunity to achieve its performance objective over the long-term. The Plan's allocation to equity proved beneficial as Canadian equities returned 16.6%, Canadian small capitalization equities returned 25.9%, U.S. equities returned 10.7% and international equities returned 5.8%. The Plan also benefited from the strength of its fixed income and mortgage allocations, which returned 7.2% and 8.9% respectively, for the year. As a result of the strength of its components, the Plan returned 9.1% in 2010.

The performance of the Plan's investments is compared to a customized benchmark, which is based on the market returns of the Plan's target asset mix. This comparison measures the active management of the investments versus a passive or indexed approach. In 2010, the Plan's investments performed in-line with the customized benchmark return. The Plan has outperformed over longer periods, with the Plan's active managers adding value over the two, three and four-year time periods and since inception of the Plan.

The Plan's investment return outperformed the performance objective of the annual change in the CPI plus 4% by a significant margin over the one-year period. However, this performance objective is not a short-term goal, but instead, is an objective meant to be achieved over the long-term. The Plan's underperformance over the four-year period is attributable to the financial crisis that took place in 2008. The Plan has outperformed on an annualized basis since inception of the Plan.

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## SECURING YOUR FUTURE

It is the Company's responsibility to ensure that your pension benefits are secure, and this is a responsibility that the Company takes very seriously. Manitoba Telecom Services Inc. is a profitable, leading edge company with a solid capital structure and strong cash flow. It is this strength that ensures the Company's continued support for the Plan.

The Plan has a conservative approach and is more defensive in nature than many pension plans in Canada. Well-developed risk management and governance policies are in place, which has guided us through the financial turmoil and has helped us to avoid speculative investment strategies.



## SUMMARY FINANCIAL STATEMENTS

The following financial information is a summarized version of the financial information included in the Plan's audited financial statements. The Plan's audited financial statements have been audited by Deloitte & Touche LLP.

**STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS**  
AS AT DECEMBER 31

(in thousands)	2010	2009
<b>Assets</b>		
Cash	\$ 4,352	\$ 4,500
Investments (Note 4)	1,331,075	1,256,190
Receivables		
Investment income	3,559	3,569
Employee contributions	946	435
Employer contributions	15,730	3,906
	1,355,662	1,268,600
<b>Liabilities</b>		
Benefits payable	820	876
Pension asset transfer payable (Note 6)	-	15,061
Accounts payable & accrued liabilities	980	924
	1,800	16,861
<b>Net Assets Available for Benefits</b>	<b>\$ 1,353,862</b>	<b>\$ 1,251,739</b>

## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

FOR THE YEAR ENDED DECEMBER 31

(in thousands)	2010	2009
<b>Increase in Net Assets</b>		
Contributions		
Current:		
Employee	\$ 10,553	\$ 10,424
Employer	57,006	48,780
Past service purchases	50	46
Reciprocal transfers	-	565
Net investment income (Note 5)	46,756	28,392
Current period unrealized gains on investments	59,533	150,241
	173,898	238,448
<b>Decrease in Net Assets</b>		
Pension benefits	55,962	54,509
Termination benefits	14,624	9,346
Reciprocal transfers	-	596
Pension asset transfer (Note 6)	-	15,061
Administrative expenses	1,189	1,238
	71,775	80,750
<b>Increase in Net Assets for the Year</b>	<b>102,123</b>	<b>157,698</b>
<b>Net Assets Available for Benefits</b>		
<b>at Beginning of Year</b>	<b>1,251,739</b>	<b>1,094,041</b>
<b>Net Assets Available for Benefits</b>		
<b>at End of Year</b>	<b>\$ 1,353,862</b>	<b>\$ 1,251,739</b>

## NOTES TO FINANCIAL STATEMENTS

### 1. DESCRIPTION OF PLAN

The following description of the Manitoba Telecom Services Inc. and Participating Subsidiaries Employee Pension Plan (the "Plan") is a summary only. For more complete information, reference should be made to the Plan document.

#### a) General

The Plan is a contributory defined benefit pension plan covering certain current and former Manitoba employees of Manitoba Telecom Services Inc. ("MTS") and its participating subsidiary. The Plan came into effect on January 1, 1997 in accordance with *The Manitoba Telephone System Reorganization and Consequential Amendments Act*. On January 1, 1997, all employees and former employees of The Manitoba Telephone System and its subsidiaries who were members of The Civil Service Superannuation Fund became members of the Plan. Effective January 1, 2010, MTS adopted a new registered pension plan to provide retirement benefits on a defined contribution basis (the "DC Plan") for Manitoba employees hired by MTS and its participating subsidiary after December 31, 2009 and Plan members who elect to participate in the DC Plan for future service. Effective January 1, 2010, membership in the Plan is limited to individuals who became employees prior to that date. At December 31, 2010, the participating subsidiary was MTS Allstream Inc. The Plan is registered under the *Pension Benefits Standards Act, 1985* (Canada) ("PBSA").

#### b) Funding Policy

The Plan document sets out the arrangements for MTS and its participating subsidiary, as the Plan sponsors, to fund the benefits determined under the Plan together with the employees. The amount of funding by employees is based on a defined formula. The determination of funding by the Plan sponsors is made on the basis of an actuarial valuation performed on at least a triennial basis. As required by the PBSA, MTS is responsible for making special payments to finance any unfunded liabilities of the Plan over a period not exceeding 15 years in the case of a going concern deficiency, and over a period not exceeding five years (10 years under the temporary *Solvency Funding Relief Regulations*) in the case of a solvency deficiency.

The most recent actuarial valuation for funding purposes was prepared by Towers Watson Canada Inc. as at January 1, 2010, and a copy of this valuation was filed with the Office of the Superintendent of Financial Institutions and the Canada Revenue Agency. This valuation disclosed an unfunded solvency liability as at January 1, 2010. In accordance with the PBSA, unless the Plan has a solvency ratio of 120% or greater, completion of an annual actuarial funding valuation is required, and as a result, the amount of the special annual payment is subject to change.

In 2006, the Government of Canada enacted *Solvency Funding Relief Regulations* for defined benefit pension plans regulated under the PBSA, which enabled the extension of solvency funding payments from five years to 10 years. MTS filed a January 1, 2010 actuarial valuation to enable continued funding under the *Solvency Funding Relief Regulations*. To facilitate the solvency funding relief, MTS has arranged for \$106.9 million (2009 - \$106.9 million) in letters of credit to be held by RBC Dexia Investor Services Trust, the trustee for the Plan. The letters of credit are not reflected in the net

assets available for benefits of the Plan. In 2009, the Federal Government once again enacted temporary solvency relief, the *Solvency Funding Relief Regulations, 2009*, which enabled companies to fund any new solvency deficiency over a period of 10 years. MTS did not utilize the 10 year funding provision under the *Solvency Funding Relief Regulations, 2009*. Commencing in 2011, proposed new Federal pension regulations are expected to enable the use of letters of credit to meet solvency special payment requirements.

**c) Retirement Pensions**

A retirement pension is based on the number of years of pensionable service and the highest five-year average earnings. A retirement pension is payable to members who retire after completion of at least one year of membership in the Plan and who have attained age 65. Unreduced pensions are payable to members who have reached at least age 55 and the sum of their age plus continuous service equals 80, or have reached age 60 with 10 years of service. With certain restrictions, reduced early retirement benefits are available to members as early as age 45.

**d) Disability Benefits**

Members who are on long term disability after January 1, 1997 may be credited with pensionable service while disabled without making contributions to the Plan. Members also may be able to retire immediately and receive a disability pension from the Plan.

**e) Termination Benefits**

Subject to lock-in provisions, refunds and commuted value transfers are available when an active member ceases employment.

**f) Death Benefits**

Death benefits are available upon the death of an active member or deferred member and may be available upon the death of a retired member depending on the pension option chosen. The benefit may take the form of a lump-sum payment or a survivor pension.

**g) Cost-of-Living Adjustments**

The Plan provides for a guaranteed cost of living increase each year equal to 2/3 of the increase in the Consumer Price Index ("CPI") for Canada to a maximum CPI increase of 4.0%.

**h) Income Taxes**

The Plan is a Registered Pension Plan as defined in the *Income Tax Act* (Canada). The Plan is not subject to income taxes.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include the following significant accounting policies:

### a) Basis of Presentation

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 Plan sponsor and Plan members.

### b) Investments and Investment-Related Receivables and Liabilities

Investments and investment-related receivables and liabilities are recorded at market value where quoted prices are readily available. Real estate values are estimated based upon external appraisals conducted throughout the year. Investment transactions are recorded as of the trade date (the date upon which the substantial risks and rewards of ownership have been transferred).

### c) Foreign Exchange

Foreign currency transactions are translated into Canadian dollars at rates of exchange prevailing at the dates of the transactions. At year-end, the market values of investments denominated in a foreign currency are translated at the year-end exchange rate. Exchange differences are included in the determination of net investment income (loss) or current period unrealized gains (losses) on investments.

### d) Future Accounting Policy Change

In February 2010, the Canadian Accounting Standards Board approved Section 4600, Pension Plans, as Part IV of the Handbook to replace Section 4100 Pension Plans, in Part V of the Handbook. These standards will apply for annual financial statements relating to fiscal years beginning on or after January 1, 2011. These standards apply retrospectively to all prior periods presented. The Plan is currently evaluating the impact that these new standards will have on the financial statements.

## 3. FINANCIAL RISKS

The Plan actively manages the risks that arise from its use of financial instruments, including liquidity, credit and market risk. The Plan adheres to an investment policy that outlines the objectives, constraints, and parameters related to its investing activities. This policy prescribes limits around the quality and concentration of investments held by the Plan. Management regularly reviews the Plan's investments to ensure all activities adhere to the investment policy. The Plan's exposure to and management of these risks has not changed materially since December 31, 2009.

## 4. INVESTMENTS

(in thousands)	2010	2009
Short-term investments		
Notes and securities	\$ 37,703	\$ 22,722
Cash equivalent pooled funds	8,026	21,548
Pending trades	(169)	2,095
Total short-term	45,560	46,365
Bonds and debentures		
Government guaranteed	245,367	249,734
Corporate	170,896	153,256
Total bonds and debentures	416,263	402,990
Mortgages		
Pooled funds	66,880	63,331
Total mortgages	66,880	63,331
Equities		
Investment corporations	50,802	48,046
Real estate corporations	5,507	4,110
Resource corporations	72,708	62,712
Other Canadian and Foreign corporations	469,407	435,088
Pooled funds	134,456	122,956
Total equities	732,880	672,912
Real Estate		
Pooled funds	69,492	70,592
Total real estate	69,492	70,592
	\$ 1,331,075	\$ 1,256,190

The Plan invests in accordance with a Statement of Investment Policies and Goals which specifies allocation limits for each asset class. In addition, as a federally regulated pension plan, the investments must be in accordance with the PBSA regulations.

## 5. NET INVESTMENT INCOME

(in thousands)	2010	2009
Investment income	\$ 33,433	\$ 37,714
Realized gains (losses)	18,528	(4,543)
Investment management and custodial expenses	(4,761)	(4,341)
Transaction costs	(444)	(438)
	\$ 46,756	\$ 28,392

## 6. PENSION ASSET TRANSFER PAYABLE

MTS Allstream Inc. entered into a Pension Asset Transfer Agreement, dated October 2, 2006, with Yellow Pages Group Co. ("YPG") related to certain transferred employees of the former MTS Media Division. The amount of the pension assets to be transferred from the Plan to a YPG pension plan was determined by the actuary for the Plan and was subject to review and agreement by the actuary for the YPG pension plan. In addition, the transfer of assets under the Pension Asset Transfer Agreement was subject to regulatory approval by the Office of the Superintendent of Financial Institutions ("OSFI"). Approval was received from OSFI on September 22, 2009. The pension asset transfer payment in the amount of \$15.06 million was made on January 29, 2010.

## 7. IRREVOCABLE LETTERS OF CREDIT

Irrevocable letters of credit in the amount of \$106.9 million (2009 - \$106.9 million) are held by the Plan's trustee, RBC Dexia Investor Services Trust, on behalf of the Plan. The letters of credit, issued by major Canadian banks, have been arranged by the Plan sponsor to enable continued funding under the *Solvency Funding Relief Regulations*. The trustee can make a demand for payment on the letters of credit in the event the Plan sponsor does not meet its obligations under the *Solvency Funding Relief Regulations* or the Trust Agreement. The amount of the letters of credit is amended each year to reflect the most recent actuarial valuation results and ongoing funding under the *Solvency Funding Relief Regulations*. The letters of credit are not included in the net assets available for benefits of the Plan.

## 8. CONTINGENCIES

In September 1999, three of MTS's unions and a retiree suing on behalf of other retirees and their surviving spouses filed a claim in the Court of Queen's Bench of Manitoba against MTS in respect of the Plan. This claim sought various declarations to the effect that MTS was not entitled to use any portion of the surplus in the Plan to reduce contributions, and that such utilization by MTS was a breach of MTS's obligations to its employees and former employees. The claim also sought, among other things, a mandatory order directing MTS to reimburse the Plan for all amounts of the surplus that MTS has used to reduce its contributions, as well as an injunction prohibiting MTS from utilizing any future surplus in the Plan.

MTS filed a statement of defence in this action in December 1999. This matter proceeded to trial in the fall of 2008, and MTS received a decision from the Court on January 19, 2010. In its decision, the Court upheld the governance of the Plan and affirmed the position of MTS with respect to the issue of ongoing surplus. As a result, there will be no changes to MTS's expected future ongoing funding requirements and administration of the Plan. The Court also ruled that MTS was obligated to make a \$43 million one-time payment, retroactive to 1997, the year MTS was privatized and the Plan was implemented, plus interest from that date at the effective rate of return earned by

the Plan during this period. These funds are to be used to enhance pension benefits on the understanding that the enhanced benefits will not result in an increase of MTS's costs. The appeal of this decision was heard in December 2010. A decision is still pending. As such, any potential financial implications to the Plan of the Court's decision cannot be determined at this time.

## **9. AUDITORS' REPORT**

The financial information presented in these statements is an excerpt of the financial information included in the Plan's audited financial statements. The Plan's audited financial statements have been audited by Deloitte & Touche LLP









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