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CANADA POST POSTES CANADA

From anywhere... to anyone

Canada Post Pension Plan
2011 Annual Report






Total Compensation

Canada Post Pension Plan
2011 Annual Report

Contents

Privacy of Pension Records

Canada Post is subject to the federal *Privacy Act* and complies with the *Canada Post Employee Privacy Policy*. Personal information, including pension information, is treated in a secure and confidential manner.

Notes:
For the purposes of this report, "Plan" refers to the Defined Benefit component of the Canada Post Corporation Registered Pension Plan only, unless the Defined Contribution component is specified.

Terms that appear in *italics*, except for the names of Acts, are defined in the Glossary.

This report presents the financial position and results of the operations of the Plan on an accrual basis. Refer to Note 2 to the Financial Statements for more information.

Glossary

Actuary(ies): A professional who is responsible for calculating the obligations of pension plans and the costs of providing pension plan benefits. Under the *Pension Benefits Standards Act, 1985* (PBSA) all actuarial reports must be prepared by a person who is a Fellow of the Canadian Institute of Actuaries.

Asset(s): Items with monetary value such as cash, stocks, *bonds*, and real estate.

Assumptions (Actuarial Assumptions): Factors used by an *actuary* in forecasting uncertain future events affecting pension cost. They involve such things as estimating interest and investment earnings, inflation, mortality rates and retirement patterns.

Benchmark: A point of reference used as a basis for evaluation or comparison. A market index can be used as a *benchmark* against which the performance of a group of similar *assets* can be measured or compared.

Bond(s): Debt issued by a corporation or government, which provides a promise to the holder that the principal and a specified amount of interest will be repaid within a specific period of time. Investing in a *bond* is like lending money to a government or organization.

Commuted Value: The value as of the date of calculation of future pension benefits expressed as a lump sum in today's dollars. It is calculated by the Plan administrator using *assumptions* set out in the laws governing pension plans. This value changes depending on the *assumptions* applicable at the time of calculation. For example, when *discount rates* decrease, the *commuted value* increases, and vice versa.

Custodian: Commercial bank or trust company that provides safekeeping for the securities owned by the Plan.

Discount Rate(s): Long-term interest rates used to calculate *pension obligations*.

Equity(ies): Common and preferred stock that represent a share in the ownership rights of a company and the right to collect dividends from profits.

Gross Domestic Product (GDP): The total market value of all final goods and services produced in a country in a given year. It equals total consumer investment and government spending, plus the value of exports minus the value of import.

Net Investment Assets: Investments and investment related receivables minus investment related liabilities.

Over-Weight / Under-Weight: Refers to differences from the *benchmark* portfolio, "*under-weight*" being less than the *benchmark*, "*over-weight*" more.

Pension obligation(s): The actuarial present value of pension benefits for service completed up to a particular date, calculated using best estimate *assumptions*.

Private Equity(ies): *Equities* that are not publicly traded.

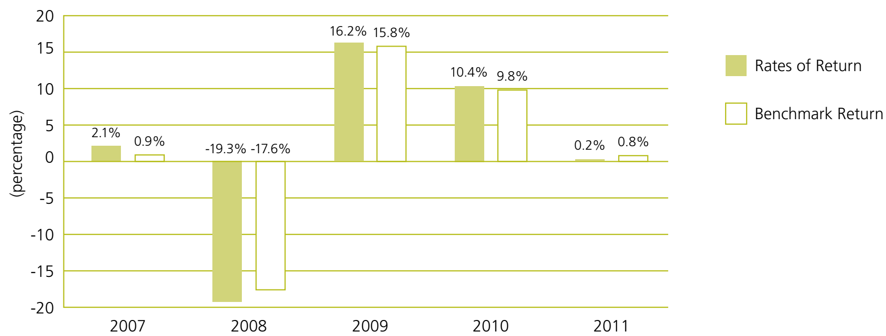
Rate(s) of Return: The amount gained or lost on an investment over a period of time, normally as a percentage of initial investment. Real return is a return that has been adjusted for inflation. Net return is a return that has been adjusted for expenses.

Yield(s): Interest (adjusted for amortization of discount or premium) or dividend income as related to the cost of an investment in *bonds* or shares.

Highlights

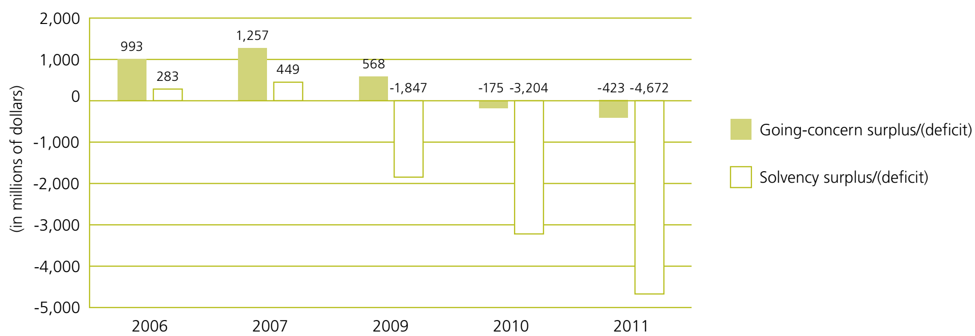
Actual Fund *Rates of Return* vs. *Benchmarks*

The Plan recorded a modest *rate of return* of 0.2 per cent in 2011, compared to its *benchmark* return of 0.8 per cent.



Plan Funded Status

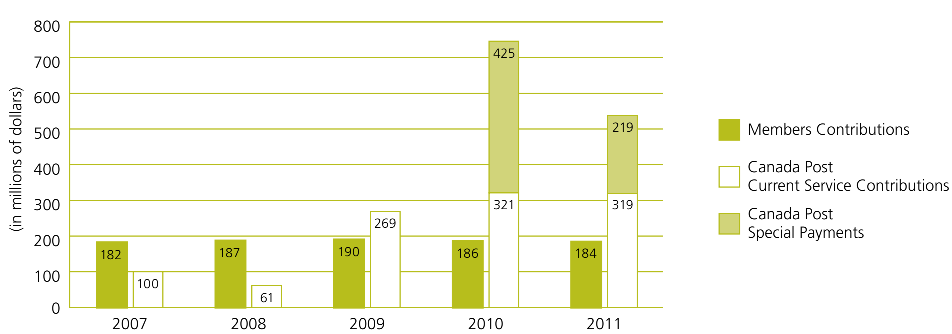
In 2011, the Plan's going-concern deficit to be funded increased to an estimated $423 million. The solvency deficit to be funded grew to an estimated $4,672 million.



Note: A funding valuation for the year 2008 was not required.

Contributions

The table below shows the contributions made by Canada Post and Plan members in the last five years.



Note: The special solvency relief measures introduced by the Federal government reduced the special payments by $433 million in 2011. Without these measures, applicable to all federal pension plans, the special payments for Canada Post would have been $652 million in total. Refer to the Funding Valuation section for more details about the special solvency relief measures.

Understanding the Challenges of Your Pension Plan

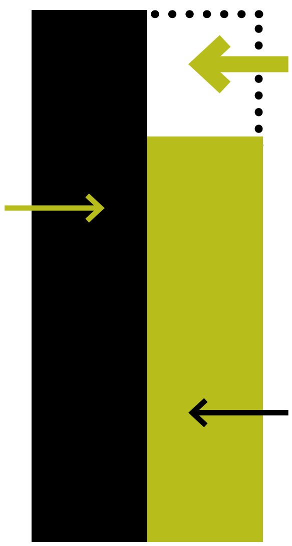
As a member of the Canada Post pension plan (the Plan), your retirement benefits are funded by contributions made by you and Canada Post, as well as investment income generated by the Plan's *assets*. Returns were negative for a portion of 2011, however by the end of the year, the Plan was able to achieve a small positive return of 0.2 per cent. The Plan's long-term expected net *rate of return* is 7.0 per cent.

The Perfect Storm

Defined benefit pension plans in general are struggling as a result of lower *discount rates* and market performance. Approximately 94 per cent of plans are in a solvency deficit situation, like Canada Post, with an average solvency ratio of 79 per cent.

Pension Obligations

Are the estimated amounts required to pay pension benefits in the future.



Deficit

When the *assets* in the Plan are less than our *pension obligations*, we are left with a deficit. It is Canada Post's responsibility to cover that shortfall.

Assets

Are made up of
- Member contributions
- Employer contributions
- Investment income

At the end of 2011, the estimated *pension obligations* were higher than the net *assets* available for benefits, increasing last year's going-concern deficit and solvency deficit. In 2011, solvency *discount rates* decreased by more than 0.5 per cent.

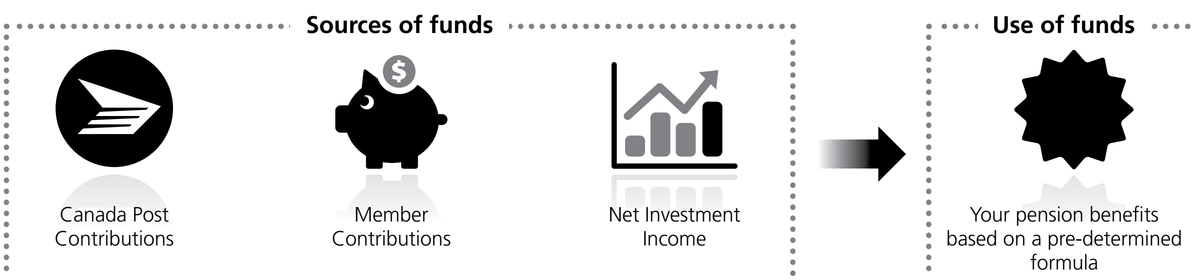
The Federal government recognizes the challenges faced by pension plans. It has put in place relief measures allowing plans to reduce their special solvency payments up to a maximum of 15 per cent of plan *assets*, with annual government approval. See the Funding Valuation section for more information.

There is a larger deficit this year because:

- The Plan experienced below-expected returns as a result of the volatility in the global capital markets; and
- The *discount rates* remain lower than they have been in the past. **Lower *discount rates* increase *pension obligations* and make it more costly to fund pension benefits.**

  For example: **A *discount rate* decrease of 0.5 per cent** results in **approximately $1 billion** of increased *pension obligations*. An increase in *discount rates* would have the opposite effect.

How the Plan works for you



You and Canada Post alone fund your Plan. The contributions you make now will make it possible for you to receive pension benefits during your retirement. **Your pension does not depend on how much you contribute to the Plan or how well the pension fund investments perform.** Canada Post, as the Plan sponsor, is responsible to fund any deficit.

Your 2011 Annual Report at a Glance

In 2011, our Plan's performance reflected the challenges of the global economy.

After a year of significant volatility in global markets and sharply lower *discount rates*, the Plan achieved a modest investment return. However, the rise in *pension obligations* exceeded the Plan's investment returns, increasing the Plan's estimated deficits to be funded.

2011 Investment Return:

How we did against our *benchmark*

Our *Benchmark*: 0.8%

Our Plan: 0.2%

Actuarial Valuation

Estimated deficits to be funded

Going-concern (long-term view):

$423 million – 97% funded

(Assumes that the Plan continues in operation indefinitely.)

Solvency (short-term view):

$4,672 million – 79% funded

(Assumes the Plan is terminated on the date of valuation. Tests whether members would be paid what would be owed to them, in such an unlikely situation.)

2011 Overview

Benefits paid:	$620 million
Contributions to the Plan:	
Members:	$184 million
Canada Post:	
Current Service:	$319 million
Special Payments:	$219 million

(After $433 million reduction for special relief measures)

Plan *Assets*

$15,431 million

Plan Members

Active:	58,958
Retirees and others:	25,648
Total:	**84,606**

Defined Contribution Component

Assets:	$2 million
Members:	271

Changes in 2011

Pension Reform

The Federal government made changes to our governing legislation and **some Plan provisions were changed** as a result. Employees who become members of the Plan are immediately eligible for a pension benefit and there have been improvements to death benefits. These prescribed changes represent an increase of $67 million in *pension obligations*.

New Accounting Standards

The Canadian Institute of Chartered Accountants (CICA) has set new standards for the measurement, presentation and disclosure of plan investments and *pension obligations*. For details see Note 3 to the Financial Statements.

Investment Review

As a result of an asset-liability study, the Plan added new *asset* classes to its investments. **The objective is to increase the fund's returns without increasing risk.**

2012: Looking forward

Estimated Contributions to the Plan:

Members: $208 million

Canada Post:

Current Service: $331 million

Special Payments: $63 million

(Assuming approval of a reduction of $892 million for special relief measures)

Investments Strategy

The Plan is positioned to take advantage of the future growth opportunities in the equity markets while holding an appropriate balance of fixed income *assets* based on the Plan's membership and long term obligations.

About your Pension Services team

In 2011, we:

Answered
54,486
calls

Received
86,439
website visits

Completed
38,631
transactions

CEM 2010 Benchmark Survey

	Our Plan	Peer Group Average
Pension Administration Costs (per member)	**$123**	**$170**
Pension Investments Costs (% of *assets*)	**0.235%**	**0.311%**
Service Score	**78**	**70**

Canada Post provides pensions and services to members at a cost lower than the average cost of the Canadian pension industry. We intend to keep doing so.

Risk Management and Plan's Sustainability

The sustainability of the Plan is directly linked to the financial sustainability of the Plan sponsor, Canada Post. Management and the Board of Directors will make decisions and pursue necessary changes to ensure that, with the help of all employees, Canada Post grows and remains financially sustainable.

Message from Marc A. Courtois

Chairman of the Board

The Board of Directors of Canada Post (the Board) has a fiduciary duty to provide oversight of the Canada Post Corporation Registered Pension Plan (the Plan). Accordingly, the Board kept a close eye on pension activities in 2011, with the goal of ensuring the fund remains secure for the benefit of its members.

The Plan represents a significant financial obligation for Canada Post. As the Plan sponsor, Canada Post is responsible for funding any deficits to the Defined Benefit component. Through sound management and a long-term vision, Canada Post will continue to fulfill its commitment to Plan members. It is also critical that Canada Post improves its profitability in order to meet these very important financial obligations.

During 2011, the economic conditions challenged all pension plans, both private- and public-sector. Careful stewardship allowed the Plan to achieve a modest positive return despite the volatility of the financial markets and sharply lower discount rates. The Plan's estimated going-concern deficit is relatively small; the estimated solvency shortfall is more significant and would normally require special solvency payments.

The Government of Canada has recognized the challenges faced by pension plans because of the economic conditions. To address the situation, the Government enacted legislation to provide solvency relief measures. These measures are designed to help pension plan sponsors meet their funding obligations with less sensitivity to short-term economic conditions while protecting plan members.

During the year, Canada Post requested and received approval from the Government of Canada to use these relief measures to postpone a portion of the special solvency payments planned for 2011. Canada Post will seek this relief again in 2012.

It is important to understand that use of this arrangement does not affect pension benefits. The Plan's fund, from which the benefits are paid, remains secure and Canada Post continues to be committed to meeting all of its obligations under the Plan.

On behalf of the Board, I would like to thank the Government of Canada for making solvency relief measures available to companies such as Canada Post. I also extend my thanks to Denyse Chicoyne, Chair of the Pension Committee, for her continued stewardship; the pension team for their excellent work and their commitment to offering quality service to all Plan members; the Investment Advisory Committee of Canada Post for their diligence and guidance; and the Pension Advisory Council for their valuable support.

Message from Deepak Chopra

President and CEO

In 2011, the global economy continued to struggle, while the U.S. and Canadian economies strengthened only in the second half of the year.

It was a very challenging year for businesses—and for Canada Post, as volumes in our core mail business continued to decline and a labour disruption proved costly, as did the pay equity ruling by the Supreme Court of Canada. Accordingly, after 16 consecutive years of posting a profit, the Canada Post segment experienced a loss before tax of $327 million in 2011.

Looking forward to 2012, Canada Post will continue to build its physical mail business on the pillars of quality, productivity and safety, while growing its digital business through epost™, data and analytics and improvements to its online properties.

The Board of Directors and management will pursue necessary changes to ensure Canada Post, the sponsor of the Canada Post Corporation Registered Pension Plan (the Plan), remains financially sustainable. Canada Post must continue to be a healthy, viable and profitable company in order to provide the strongest possible foundation for a sustainable Plan.

2011 was indeed a year of tumult in financial markets, impacting the Canada Post Pension Plan on two fronts. First, the discount rates sustained a significant drop during the year, and low discount rates make it more costly to fund pension benefits. Accordingly, most pension funds saw their financial positions weaken. The average solvency ratio of defined benefit plans in Canada stands at 79 per cent at the end of 2011.

Second, on average, major Canadian pension plans barely achieved a positive return. Canada Post's Plan was no exception. It achieved a very modest positive return of 0.2% compared to a benchmark return of 0.8% in 2011. As a result, at year-end the Plan had an estimated small going-concern deficit and larger solvency deficit.

In 2011, the Corporation made special payments totalling $219 million to reduce the solvency shortfall. This amount is on top of the Corporation's regular current service cost contributions of $319 million, as the Corporation bears the financial risk of the Plan.

During the year, the Government of Canada put in place measures to allow pension plan sponsors, such as Canada Post, to put off special payments. Canada Post requested and received ministerial permission to use these special relief measures in mid-2011, for which we are grateful. We intend to request the same relief in 2012. It is important to note that this arrangement does not reduce Canada Post's obligation or our commitment to fully fund the Plan.

I would like to thank Douglas Greaves, Vice-President Pension Fund and Chief Investment Officer, and the pension services team for their solid management of the Plan's assets and excellent service to members.

Plan members who wish to have more information, or view personal pension information in confidence, may visit cpcpension.com.

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Report to Members

From the Office of Douglas D. Greaves,
Vice-President Pension Fund and Chief
Investment Officer

Member Services

The Canada Post Corporation Registered Pension Plan (the Plan) began operations in 2000 with approximately 55,000 members. It has grown to more than 84,000 members by the end of 2011. There were 3,305 new retirees in 2011 with retirees now representing 27.9 per cent of the total.

The Pension Centre

The Pension Centre staff is responsible for providing and administering Plan member services. Services include processing of elective service purchases, pension estimates, retirements/terminations/deaths, replacement of personal identification numbers (PIN) to access the pension calculator on the website, updates to retirees' life insurance beneficiaries, new retirees' pension payments and the collection of employee contributions for leaves of absence.

Telephone Calls	**2011**	**2010**
received:		
All Members	48,561	45,951
Retirees – calls to RBC Dexia	5,925	5,402
made:		
All Members	9,109	8,378

Service Transactions Completed

38,631

Member Satisfaction Survey

Score	4.4 / 5.0
Target	4.3 / 5.0

Website: cpcpension.com

The pension website provides information about the Defined Benefit component of the Plan. It includes copies of publications and news updates about the Plan. Members can use the "Calculate my Pension" feature to get pension estimates. In 2011, two cost estimators were added: elective service (buyback) and leave without pay.

Visits to cpcpension.com	**2011**	**2010**
Increase of 23.7%	86,439	69,891

Pension Estimates using the Website Calculator	**2011**	**2010**
Decrease of 0.9%	190,812	192,528

Pre-retirement Seminars

The seminars are provided to Plan members who are entitled to an unreduced pension or who are within five years of retirement. They help members understand the value of their pension benefit and learn about other factors that affect their retirement decision such as financial, legal, health and lifestyle choices. Participant feedback for both the pre-retirement seminars and one-on-one consultations was consistently positive.

2011 Pre-retirement Seminars

73	Seminars held across Canada
2,846	Participants (members and spouses/common-law partners)
329	One-on-one consultations

Our Commitment to High Quality Service Standards and Cost-effectiveness

Pension Services participated in an annual survey with CEM Benchmarking Inc. in 2010. CEM provides independent and objective information by comparing how Pension Services administers the Plan against similar public and private sector defined benefit pension plans. The results provide insights into administration costs, service levels, and industry best practices.

The following provides the 2010 results of this survey:

	Average Administration Cost Active Members, Retirees and Survivors	Service Score
Canada Post	**$123**	**78**
Peer Group Average	$170	70

Pension Services is committed to continuous improvement to provide high quality service for Plan members in a cost-effective way.

Pension Services Contact

For pension or post-retirement information, questions or requests:

1-877-480-9220

613-734-8265 (TTY)

613-683-5908 (Outside North America)

08:00 to 18:00 (Eastern Time)

Monday to Friday

cpcpension.com

RBC Dexia Contact

Inquiries for RBC Dexia Investor Services related to pension payments:

1-800-876-4498

08:00 to 20:00 (Eastern Time)

Monday to Friday

Benefit Payment Services

East Wing 5th Floor

1 Place Ville Marie

Montreal QC H3B 1Z3

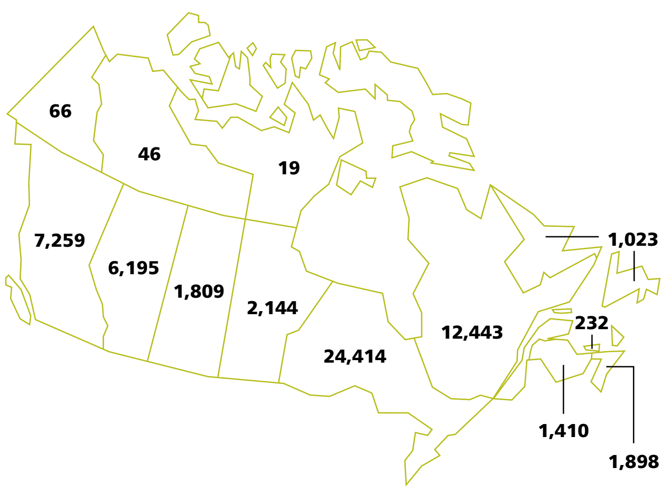
Membership Summary

Membership in the Plan continues to grow making it one of the largest single employer pension plans in Canada. The Plan has a total of 84,606 active members, retirees, deferred members, survivors and beneficiaries.

	2007	2008	2009	2010	2011
Active Members	63,531	63,239	61,755	59,817	58,958
% of Active Members	82.5%	79.8%	76.6%	73.0%	69.7%
Retirees	12,398	14,753	17,269	20,330	23,635
% of Retirees	16.1%	18.6%	21.4%	24.8%	27.9%
Deferred Members, Survivors and Beneficiaries	1,050	1,249	1,622	1,826	2,013
% of Deferred Members, Survivors and Beneficiaries	1.4%	1.6%	2.0%	2.2%	2.4%
Total	**76,979**	**79,241**	**80,646**	**81,973**	**84,606**

Total Active Members by Province and Territory

As of December 31, 2011, the 58,958 active members live in all regions of Canada.



Membership Age Distribution as of December 31, 2011

The Plan has 28,293 active members over age 50. The number of active members retiring year over year is continuing to increase. Retirees increased by 3,305 in 2011.

Age	< 30	30-39	40-49	50-59	60-69	70-79	> 79
Active Members	2,171	10,002	18,492	23,024	5,162	107	0
Retirees	0	16	151	7,347	13,796	2,270	55

The average active member is 48.2 years of age (48.3 years of age in 2010).
The average retiree age is 62.7 years of age (62.3 years of age in 2010).

Financial Summary

Net *Assets* Available for Benefits

The Canada Post Corporation Registered Pension Plan (the Plan) posted a modest return in 2011. The Plan ended the year with net *assets* available for benefits of $15,431 million, an increase of $73 million from $15,358 million[1] at the end of 2010.

Changes in Net *Assets* Available for Benefits

The $73 million increase in the net *assets* available for benefits represents investment income of $32 million and contributions of $722 million offset by pension benefits payments of $620 million and administration expenses of $61 million.

Investment income, which is made up of interest, dividend, realized and unrealized gains and losses, was $32 million for 2011 compared to $1,444 million for 2010. Despite the volatility of the financial markets in 2011, the Plan achieved a modest positive return of 0.2 per cent compared to 10.4 per cent in 2010.

During 2011, Plan contributions were $722 million compared to $932 million in 2010, a decrease of $210 million. The decrease is mainly due to lower special payments of $219 million in 2011 compared to $425 million in 2010. During the year, the Government of Canada put in place measures to allow pension plan sponsors to reduce special solvency payments. Canada Post received ministerial permission to use these special solvency relief measures and reduced special solvency payments by $433 million in 2011.

Pension benefits payments for 2011 were $620 million compared to $517 million in 2010, an increase of $103 million. The increase is mainly due to 16 per cent more retirees than in 2010.

Changes in *Pension Obligations*

Pension obligations were $16,570 million compared to $16,038 million in 2010, an increase of $532 million. The increase is partially due to the accrued interest on *pension obligations* offset by the changes in *actuarial assumptions*.

Actuarial assumptions are reviewed annually with the Plan *actuaries*, and approved by the Board of Directors of Canada Post (the Board), to ensure they remain appropriate with the changing economic, market and demographic conditions.

Changes in Surplus/Deficit

In accordance with the new Canadian Institute of Chartered Accountants Section 4600 and the International Financial Reporting Standards, effective January 1, 2011, the actuarial *asset* value adjustment (smoothing) is no longer permitted as a valuation methodology for accounting purposes. As a result, there is a difference between the deficit disclosed in the financial statements and the estimated going-concern deficit to be funded. As of December 31, 2011, the deficit of $1,139 million disclosed in the financial statements consists of an estimated going-concern deficit to be funded of $423 million and an actuarial value adjustment of net *assets* of $716 million.

[1] Adjusted to comply with the new Canadian Institute of Chartered Accountants Section 4600 and the International Financial Reporting Standards. See Note 3 to the Financial Statements.

Asset Performance

Overview

The Canada Post Corporation Registered Pension Plan's (the Plan) *rate of return* was 0.2 per cent in 2011 in comparison to its *benchmark rate of return* of 0.8 per cent. The Plan's *net investment assets* held by the *custodian* at the end of 2011 were $15,357 million, an increase of $100 million from the end of 2010.[1]

Canada Post Corporation (the Corporation) provides pension benefits to members through the Plan which is registered under the federal *Pension Benefits Standards Act, 1985* (PBSA). The PBSA requires that the Plan establishes a Statement of Investment Policies and Procedures (SIPP). This SIPP must be based on the "prudent person portfolio approach" so that the Plan's *assets* are invested in a way that a reasonable and prudent person would apply to the investment portfolio of a pension fund. The Board of Directors of the Corporation (the Board) has adopted the SIPP to ensure the continued prudent and effective management of the Plan so enough *assets* will be available to pay pension benefits when they become due. The SIPP outlines the broad ranges of allowable Plan investments and is reviewed annually by the Board and the Pension Committee.

Investment Objectives and Limitations

The SIPP describes the Plan's investment objectives and limitations. Under the SIPP, the Plan's primary objective is to ensure that the pension promise is met at a reasonable cost.

Over the long term, investment performance is evaluated on the Plan's ability to meet its pension obligations to Plan members.

Over the short term, the Plan uses a *benchmark* portfolio to measure investment performance. The Plan's *benchmark* portfolio represents the performance of the market index for each of the *asset* categories in the Plan. The SIPP contains a target percentage for each *asset* category as well as minimum and maximum limits to allow flexibility when market conditions change.

The Plan maintains at least the minimum diversification standards as established in the PBSA and also maintains appropriate diversification between industry sectors, geographic/economic areas and management styles.

Risk Management Strategy

To reduce risks, the Plan ensures that investment decisions are made in accordance with the SIPP. The SIPP sets the allowable *asset* mix ranges, which define how much can be invested in each *asset* class and is designed to provide the Plan with a long-term net *rate of return* of 4.5 per cent above inflation. Achieving this rate helps the Plan meet its funding objectives and the ongoing growth of its *pension obligations*. Each *asset* class has specific risks and limits associated with it. A risk management framework was developed through which all portfolios and their associated risk exposures are closely monitored by management and reported to the Pension Committee on a quarterly basis.

An asset-liability study was completed in 2010, with approval of the transition plan in 2011, to ensure the Plan's investment strategy remains appropriate in today's challenging environment. The study's aim was to identify new investments that would increase the fund's returns without increasing volatility and risk. The results recommended that the fund increase its investments in infrastructure and *private equity*. The study also identified new *asset* classes to be added to the Plan's portfolio: emerging markets *equity*, global high *yield bonds* and global developed markets small cap *equity*. A three-year transition timeline and allocation of funds to adjust to the new *asset* mix was approved by the Pension Committee. In June 2011, the Board approved changes to the SIPP based on the results of the asset-liability study and the Plan began to add the new *asset* classes to further diversify the portfolio.

The various *asset* related risks faced by the Plan are outlined in Note 6 to the Financial Statements.

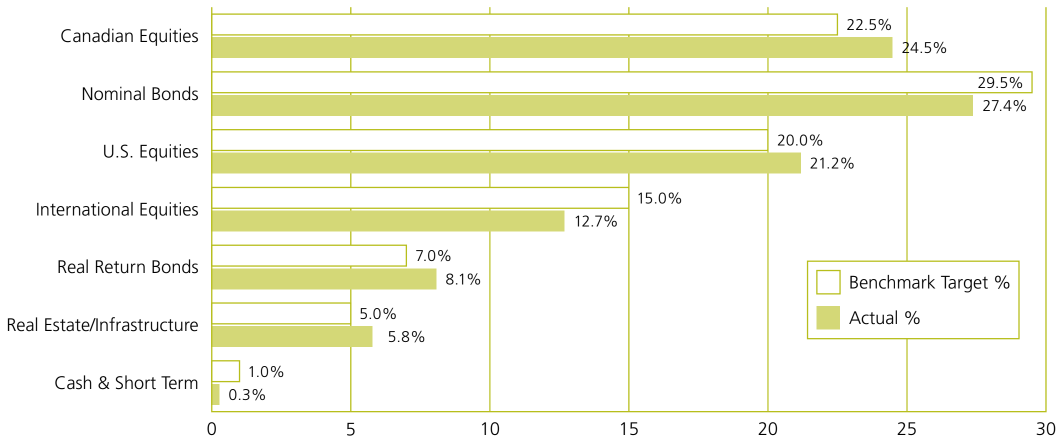
[1] Adjusted to comply with the new Canadian Institute of Chartered Accountants Section 4600 and the International Financial Reporting Standards. See Note 3 to the Financial Statements.

Investment Mix Strategy

The Plan currently maintains a long-term *asset* mix target of 62.5 per cent in *equities*, real estate and infrastructure, and 37.5 per cent in fixed income. The Plan's *asset* mix compared to the *benchmark* portfolio is shown in the following chart. Total equity exposure of 64.2 per cent of *assets* was above the *benchmark* of 62.5 per cent due to an *over-weight* position in Canadian *equities*, U.S. *equities*, and real estate, along with an *under-weight* position in international *equities*. The total fixed income weight of 35.8 per cent of *assets* is below the *benchmark* weight of 37.5 per cent, due to an *under-weight* position in nominal *bonds*. The real return *bond* exposure was above its target allocation.

Asset Mix

Actual Percentage Allocation at December 31, 2011 versus Benchmark Target Percentage

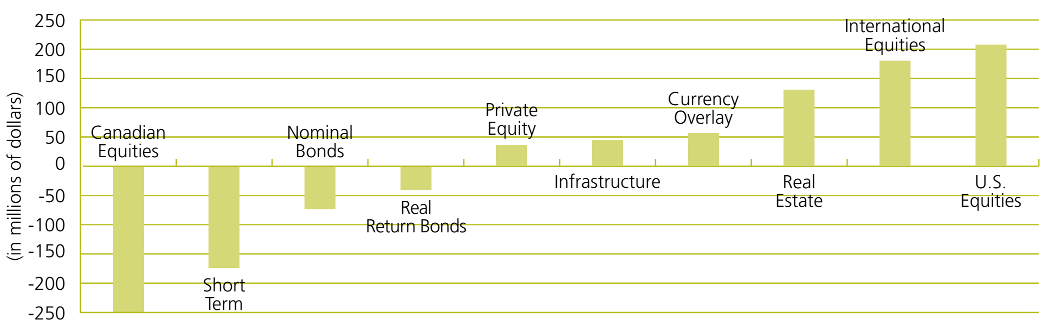


In the table above, International *Equities* includes Emerging Markets. *Private Equity* is allocated between Canadian, U.S. and International *Equities*.

The Plan launched its three-year strategy to increase the allocation to real estate, infrastructure, emerging markets, and *private equity*. During 2011, as *bond* prices rose, the Plan took profits from the real return *bonds*, nominal *bonds* and the currency overlay account to increase the allocation to U.S. and emerging markets *equities* as well as real estate, *private equity* and infrastructure. The following graph shows the fund movements by *asset* class from the beginning to the end of the year.

Change in Fund Investments by Asset Class

January 1, 2011 to December 31, 2011



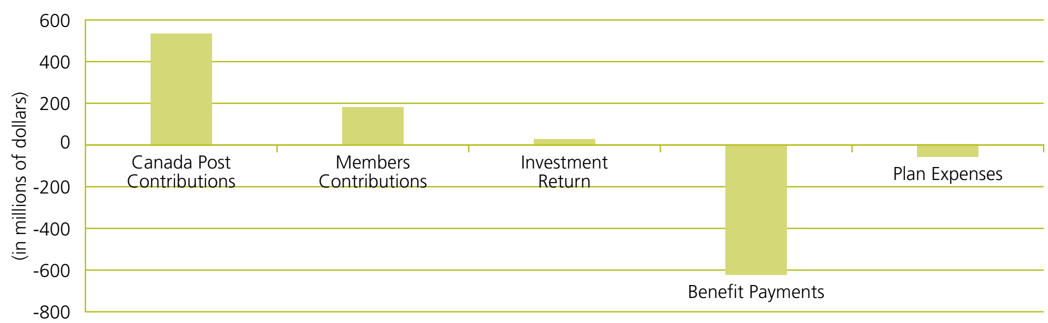
In the table above, International *Equities* includes Emerging Markets.

The following graph shows the sources of funds, i.e. the contributions from Canada Post, the contributions from members and the investment return, compared to the funds paid from the Plan for benefits and Plan expenses.

Net cashflows were slightly positive for the year.

Sources and Uses of Funds

January 1, 2011 to December 31, 2011



2011 Economic Backdrop and Key Events in Review

The global economy experienced modest growth in 2011, lower than the previous year and lower than historic growth rates. Overall, the world *Gross Domestic Product (GDP)* increased by a rate of 3.8 per cent. Developing and emerging economies grew at a rate of 6.2 per cent, below their historic rate of 7 to 10 per cent. Developed countries saw a 1.6 per cent increase, below their usual growth rate of between 2 and 3 per cent. Germany continued to lead the developed countries in *GDP* growth with 3.0 per cent growth.

In 2011, the European sovereign debt crisis escalated. While Ireland's crisis was contained, the crisis grew more serious for Greece, Portugal, Spain and Italy. These countries' ability to repay their debts and carry through with announced austerity measures was put in doubt. For them, the cost to borrow more money, to enable them to refinance their sovereign debt, increased sharply. This raised fears of losses in the European banking sector and caused bank lending to dry up in Europe and beyond. A series of meetings were held by European leaders followed by announcements of support measures. Over the year, the crisis deepened as Italy's prime minister resigned and Greece found itself on the brink of default.

In December 2011, the European Central Bank committed to providing unlimited liquidity to European banks for three years. This measure served to support bank lending and liquidity, avoided a credit crunch, and provided time for European banks and governments to work out their economic and political problems.

In the U.S., the economy grew at a rate of 1.8 per cent in 2011. The debt ceiling debate in July shook confidence on global markets. In August, the Standard & Poor's debt rating agency downgraded the U.S. credit rating. In an attempt to stimulate the economy, the U.S. Federal Reserve Bank initiated Operation Twist in September. Its aim is to lower long-term interest rates in order to reduce mortgage and other interest rates and stimulate consumer spending. In the latter part of the year, economic conditions began to recover and there was a modest improvement in the employment situation.

In Canada, the economy grew by 2.3 per cent in 2011. Lower demand for commodities meant the Canadian dollar depreciated. The balance of payments (net exports) was positive for the first time in three years due mainly to modest growth in U.S. demand for Canadian goods.

Political unrest in several Arab countries, concerns about how China would deal with inflation, and the effects of the earthquake in Japan further contributed to the slower economic growth. Many banks worldwide took measures to increase their capital positions, including reducing their lending, and governments in the developed countries reduced spending. Global demand was cut, leading to drops in imports and exports across the advanced, developing and emerging economies.

As 2011 drew to a close, fears remained about the uncertainty in Europe and the impact of China's inflation-fighting actions. These overshadowed the positive economic signals from the U.S. and the expectation that the American economy will expand in 2012.

Financial Market Performance

As events unfolded around the world in 2011, global *equity* markets experienced a significant decline. The steady gains made by *equity* markets in the first months of the year were reversed by the European sovereign debt crisis, the U.S. debt ceiling debate, and the events in Japan, several Arab countries and China.

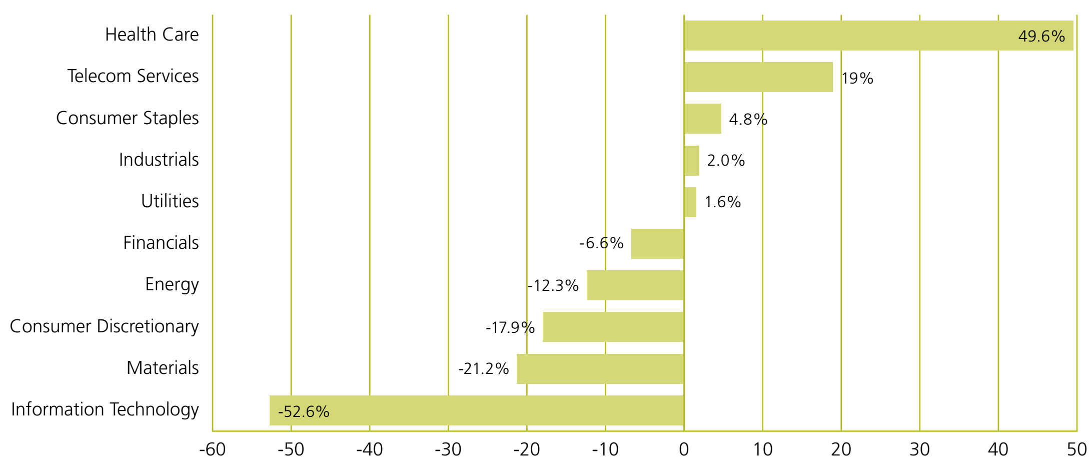
Commodity demand decreased and copper, widely considered a strong indicator for the broader economy, dropped 23 per cent to $3.43 US per pound. Oil prices moved up and down before settling up 8.1 per cent at $98.90 US at the end of December.

Currency markets were volatile, as the U.S. dollar, the Japanese yen and the Swiss franc increased in value while the Euro and many emerging market currencies decreased.

The S&P/TSX (Standard & Poor's/Toronto Stock Exchange) Composite Index ended the year down 8.7 per cent. As can been seen in the following chart, strong performance came from health care and the steadier defensive sectors such as telecom services and consumer staples. Economically sensitive sectors such as materials, consumer discretionary and energy were down. Information technology's negative returns reflected Research in Motion's (RIM) price decline in the face of strong market share gains by competitors.

TSX Composite Index Industry Sector Percentage Return

January 1, 2011 to December 31, 2011



In Canadian dollar terms, the S&P 500 (Standard & Poor's) gained 4.6 per cent while the international market, as represented by the MSCI EAFE (Morgan Stanley Capital International Europe, Australasia, Far East) index, was down 10.0 per cent. Internationally, the only developed market countries to show positive stock market returns were Ireland and New Zealand. Emerging markets were down 16.4 per cent in Canadian dollar terms.

Bond markets performed well in 2011 with the DEX Universe *bond* index up 9.7 per cent, and the DEX real return *bond* index up 18.3 per cent as interest rates moved lower and *bond* prices moved higher in 2011. Most central banks around the world kept interest rates low to stimulate growth.

Interest rates remained low at the end of the year, affecting the solvency position of the Plan. Low interest rates increase pension plan obligations and put the Plan in a larger deficit position.

Fund Performance

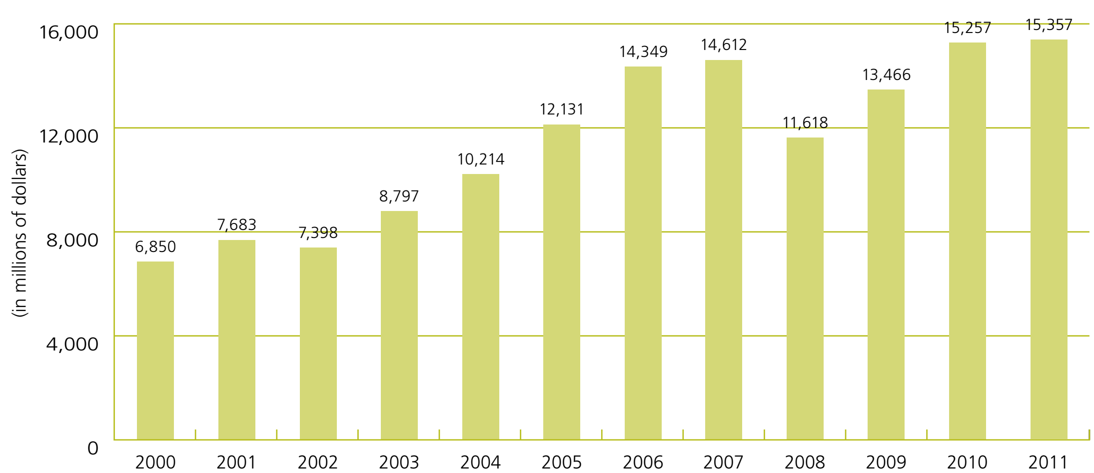
The Plan earned a *rate of return* of 0.2 per cent in 2011. This was below its *benchmark rate of return* of 0.8 per cent, and below the median gain of 1.7 per cent experienced by the RBC Dexia universe of large Canadian pension plans. This is only the second time since Plan inception 11 years ago that the Plan has not beaten its *benchmark*, the first being 2008, the year of the U.S. financial crisis.

The Plan's investment strategy is designed to take into account that it is a relatively young pension plan, founded in 2000. Compared to a typical plan, there is a greater percentage of active members (70%) compared to retired and non-active members (30%). The Plan is able to have a relatively higher *equity* weighting than typical plans. With a 62.5 per cent weighting in *equities*, real estate and infrastructure, its returns are sensitive to volatility in those markets. In 2011, *bond* returns were more favourable than *equity* returns. As a result of the investment decisions taken in 2011 and the direction provided by the asset-liability study, the fund is entering new investment areas which are aimed at providing returns without additional risk. The Plan is positioned to take advantage of the future growth opportunities in the *equity* markets while holding an appropriate balance of fixed income *assets* based on the Plan's membership and long term obligations.

Total Plan *net investment assets* are shown in the following chart.

Net Investment Assets

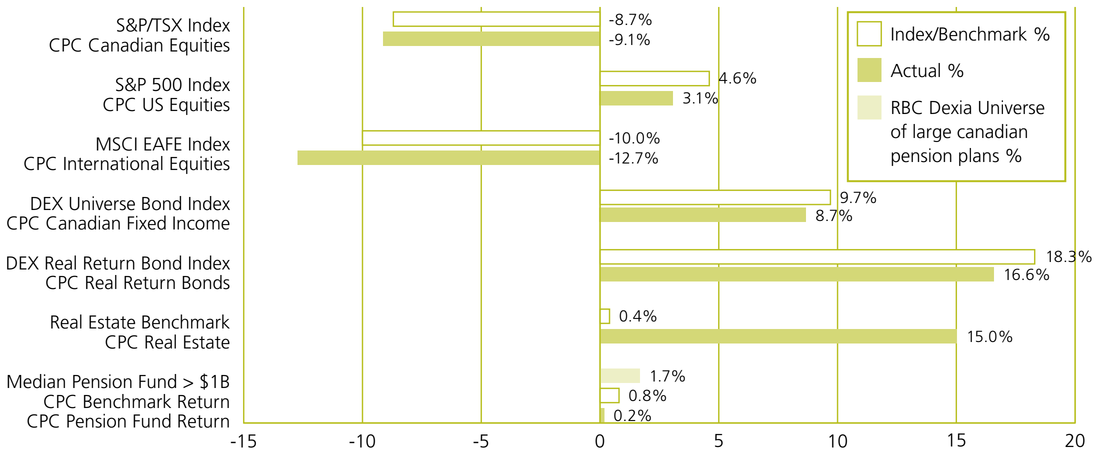
As at December 31, 2011



The 2011 *asset* class returns are shown in the following chart against their *benchmark* returns.

1 Year Returns as at December 31, 2011

By Asset class and Total Plan



Real return *bonds* performed the best of all *asset* classes as the prices of long-term *bonds* increased when interest rates moved lower. Real return *bonds* provide inflation protection and also have characteristics of long-term *bonds*.

Nominal *bond* returns were positive due to gains in all *bond* sectors, especially the provincial and municipal sectors. The modest, sustainable growth in the Canadian economy was reflected in the continued flattening of the *yield* curve. The *yield* curve reflects the expected *yields* for *bonds* with terms from one year to thirty years. When *bond yields* increase, *bond* prices decrease and when *bond yields* decrease, *bond* prices increase. Since *bond yields* were low in 2011, cash and short-term investments returns were almost zero for the year.

Real estate investments again benefited from increased demand. This *asset* class offers inflation protection and a stream of income. The Plan's real estate performance exceeded the median performance of the real estate holdings of other large pension plans as measured by RBC Dexia.

The Plan's largest *equity* holdings are shown in the following chart.

Equity holdings greater than 0.25% of overall fund

December 31, 2011 *(In millions)*		
Toronto Dominion Bank	$ 197	1.28%
Royal Bank of Canada	185	1.21%
Bank of Nova Scotia	149	0.97%
Suncor Energy Inc.	116	0.75%
Apple Inc.	104	0.68%
Canadian Natural Resources Ltd.	102	0.66%
BCE Inc.	88	0.57%
Canadian National Railway Co.	88	0.57%
Enbridge Inc.	79	0.52%
TransCanada Corp.	79	0.52%
Bank of Montreal	76	0.50%
Potash Corp. of Saskatchewan	71	0.47%
Rogers Communication Inc.	68	0.44%
Cenovus Energy Inc.	63	0.41%
Exxon Mobil Corporation	60	0.39%
Telus Corp.	59	0.38%
Google Inc.	57	0.37%
Chevron Corporation	56	0.37%
Barrick Gold Corp.	55	0.36%
Manulife Financial Corp	55	0.36%
Talisman Energy Inc.	55	0.36%
Canadian Imperial Bank of Commerce	54	0.35%
Qualcomm Inc.	54	0.35%
Goldcorp Inc.	51	0.33%
SNC-Lavalin Group Inc.	51	0.33%
Metro Inc.	48	0.31%
Thomson Reuters Corp.	47	0.30%
Pfizer Inc.	45	0.29%
Procter & Gamble Co.	44	0.29%
American Tower Corp.	43	0.28%
Schlumberger Ltd.	43	0.28%
EnCana Corporation	40	0.26%
Nexen Inc.	40	0.26%
Intel Corp.	39	0.25%
Pepsico Inc.	39	0.25%
Shoppers Drug Mart Corporation	39	0.25%
Wells Fargo & Co.	39	0.25%
General Electric Co.	38	0.25%
Shaw Communications Inc.	38	0.25%
	$ 2,654	**17.27%**

Investment Developments and Initiatives

In 2011, there were several important developments with regards to investments:

- Final approval was given to proceed with the recommendations of the asset-liability study, to be spread out over a three-year period. This resulted in the addition of new *asset* classes to the SIPP: global small cap *equity* (developed economies, excluding U.S.), emerging markets *equity*, global high *yield bonds*, and infrastructure.
- The asset-liability study reaffirmed the Plan's diversification strategy of increasing exposures to real estate, *private equity* and infrastructure, and decreasing exposure to Canadian *equities* over a three-year period starting in 2011.
- With additions to Canadian real estate investments and growth in market values, real estate was valued at $852 million at the end of 2011, up from $624 million at the end of 2010.
- Infrastructure investment activity got under way with two initial commitments totalling $71 million.
- As a result of the Plan's regular review of fund managers, it was decided to end the relationships with one Canadian *equity* manager and one international *equity* manager.
- With the addition of experienced staff, the Plan is now managing two *bond* portfolios in-house. This has resulted in reduced fund management costs, more flexibility and improved market knowledge.
- The Plan added three emerging markets stock portfolios near the end of the calendar year.
- At 0.235 per cent, the Plan's investment management costs were less than industry peers, as measured by the 2010 CEM Benchmarking Survey. The Plan's investments costs were $2.4 million lower than the CEM *benchmark*.

Looking Forward to 2012

- The Plan is committed to earning returns above the *benchmark* portfolio by selecting the appropriate *asset* mix and risk level to meet the Plan's long-term funding objectives.
- Pension Services and Pension Investments will strive to continue to provide pensions and services to all its Plan members at below median industry costs.
- The Plan will continue to implement strategies designed to increase returns without increasing risks.
- Activities for 2012 will include: completing the funding of the three emerging markets portfolios, adding a global high *yield bond* manager and a global small cap *equity* manager, and continuing to add to real estate, *private equity* and infrastructure holdings.
- Pension Risk Management reports will continue to be presented to the Pension Committee on a quarterly basis.

Funding Valuation

The Plan is currently required to file annual actuarial funding valuations with the pension regulator, the Office of the Superintendent of Financial Institutions (OSFI). Valuations are required regularly to establish the funded status of the Plan on a going-concern and solvency basis at a specific date. (Definitions of these terms and answers to other questions about actuarial valuations can be found on the next page.)

Pension obligations on a going-concern and solvency basis are compared to the Plan *assets* to measure the health of the Plan. The *pension obligations* represent the cost of future pension benefits, based on the Plan members' pensionable earnings and pensionable service earned to the date of the calculation. For this purpose, the Plan sponsor and the *actuary* make *assumptions* about the future such as expected inflation, returns on invested *assets*, salary increases, retirement age, life expectancy and other factors. The *pension obligations* are compared to the Plan *assets* to see if there is a surplus or a deficit. Canada Post, as the Plan sponsor, is responsible for funding any deficits.

The Plan sponsor is currently facing serious funding challenges as the projected cost of future pensions has surpassed the growth in *assets* over recent years. Lower *discount rates* and longer life expectancies of Plan members make it more costly to fund pension benefits. A small change in *discount rates* can have a significant impact on *pension obligations*. A *discount rate* decrease of 0.5 per cent would result in approximately $1 billion increase of *pension obligations*.

In June 2011, the Plan filed an actuarial valuation as of December 31, 2010, with OSFI showing a going-concern deficit of $175 million and a solvency deficit of $3,204 million[1].

The current estimate of the financial position of the Plan as of December 31, 2011, based on existing rules and regulations, is a going-concern deficit to be funded of approximately $423 million and a solvency deficit to be funded, using the average solvency ratio basis, of approximately $4,672 million[2]. The solvency deficit worsened during the year as a result of declining *discount rates*, which had the effect of increasing the present value of the Plan's future *pension obligations*. The lower-than-expected *rate of return* on investments also contributed to the increases in both the going-concern and solvency deficits.

Employer current service contributions in 2011 amounted to $319 million compared to $321 million in 2010. Employer current service contributions for 2012 are estimated at approximately $331 million. Employer special payments of $219 million were made in 2011 compared to $425 million in 2010. Canada Post used the special solvency relief measures permitted by legislation to reduce solvency payments by $433 million in 2011. Based on the expected actuarial valuation, special payments for going-concern and solvency deficits for 2012 are estimated at approximately $955 million. Approval for a reduction of $312 million in special solvency payments for the first six months of 2012 was obtained in August 2011. It is Canada Post's intention to request to use additional special relief measures as permitted by legislation for a reduction in special solvency payments of approximately $580 million for the second half of 2012.

[1] The solvency deficit when using fair value of Plan *assets* was $3,692 million.
[2] The solvency deficit when using fair value of Plan *assets* is estimated at $6,578 million.

Questions and Answers about Actuarial Valuations and the Special Relief Measures

What is an actuarial valuation and what does it determine?

An **actuarial valuation** is like a report card for the long-term financial health of a pension plan. An independent *actuary* is hired by the Canada Post Board of Directors to conduct an actuarial valuation as of a specific date. The valuation determines the plan's long-term financial health by comparing plan *assets* such as stocks and *bonds* to *pension obligations*. This shows whether there is a **surplus** or a **deficit** of funds to cover the value of accumulated pension benefits.

OSFI requires that the actuarial valuation is done on both a going-concern and solvency basis. These valuations assess the health of a pension plan in hypothetical situations, in order to protect the interests of plan members.

What is a going-concern valuation?

The **going-concern valuation** assumes that the Plan continues in operation and is longer term in focus. It determines if there are enough *assets* being held in the Plan for pension benefits to be paid in the future for accumulated service to date. It also assesses whether the level of contributions made by Plan members and Canada Post is enough to cover the additional *pension obligation* to be created over the coming year, as another year of credited service is added for current employees contributing to the Plan.

The last filed valuation as at December 31, 2010, showed that the Plan had a small going-concern deficit. This means that as at December 31, 2010, the *assets* were slightly below the amount required to pay for future pension benefits based on the *assumptions* and methods used for this valuation. The estimated December 31, 2011, going-concern position shows a deficit slightly higher than in 2010.

What is a solvency valuation?

The **solvency valuation** assumes the Plan is terminated on the date of valuation. This test exists so pension regulators can ensure that, in such an unlikely situation, Plan members are paid what would be fully owed to them to that point. It has a short-term view and the results are strongly affected by the *discount rates* on that date.

The last filed valuation as at December 31, 2010, showed that the Plan had a solvency deficit. This means that if the Plan had been terminated on December 31, 2010, there would not have been enough *assets* to pay for 100 per cent of the pension benefits. The estimated December 31, 2011, solvency position shows a larger deficit than in 2010. At this time, *discount rates* are at historically low levels which explains why *pension obligations* are at historically high levels. This situation can change rapidly depending on the movement of *discount rates*.

What happens if there are deficits?

Based on current federal pension legislation:

- If an actuarial valuation reports a solvency deficit – a shortfall of Plan *assets* to solvency obligations – Canada Post, as the Plan sponsor, is required to make special payments over five years or less to the Plan to eliminate the deficit. Canada Post may also request permission to use special solvency relief measures to reduce special solvency payments.
- If an actuarial valuation reports a going-concern deficit – a shortfall of Plan *assets* to going-concern obligations – the Plan sponsor is required to make special payments over 15 years or less to the Plan to eliminate the deficit.

In general, plan sponsors must, in a given year, pay the amount necessary to cover the ongoing current service cost, plus any special payments required in that year to pay down a funding deficiency over the appropriate time period, unless special solvency relief measures have been approved by the Federal government.

What are special solvency relief measures?

Special solvency relief measures are measures put in place by the Federal government that allow defined benefits pension plans to reduce their solvency special payments. The sum of all reductions applied to the required special payments cannot exceed 15 per cent of the market value of the Plan *assets* at the end of the most recent Plan year. They are available to all federally-regulated plans, including Crown corporations like Canada Post. They are designed to help pension plan sponsors meet their funding obligations with less sensitivity to short-term economic conditions.

To use the relief measures, Canada Post must obtain approval each year from the Minister of Finance and the Minister of Transport, Infrastructure and Communities.

The relief measures are not meant to simply defer the solvency special payments to a later date. They are based on the solvency position of the Plan which changes depending on investment returns and *discount rates*. At this time, *discount rates* are at historically low levels, increasing *pension obligations*. This situation can change rapidly depending on the movement of *discount rates*. If the Plan's solvency position improves, the amount of the special solvency payments could be reduced or even eliminated.

Canada Post remains responsible for funding any deficits and is committed to meeting all its obligations to the Plan and its members. The relief measures do not reduce or eliminate Canada Post's obligation to fully fund the Plan.

Plan Governance

The Canada Post Board of Directors (the Board) ensures the Plan is administered responsibly, in the best interest of all Plan members and of the Corporation. The table below shows the governance structure of the Plan and the roles of the Board, the Committees and management. It describes the accountabilities of those with pension fiduciary responsibilities so that sound decisions are made and the pension promise is kept through prudent investments.

To provide more information on the governance structure and fiduciary responsibilities, the Governance web page on **cpcpension.com** was updated during the year with the mandates, the memberships, the biographies and the pictures of the members of the Board, the Board Committees, the Investment Advisory Committee and the Pension Advisory Council.

In 2011, Internal Audit contributed to ensuring that the oversight and compliance governance principle was effectively followed by the Plan. The audit function conducted an assurance engagement assessing the effectiveness of control activities relating to the management and the administration of pension records, remittance of contributions to the fund, accuracy of pension benefits payments from the fund, and appropriateness of expenses charged to the pension fund. Internal Audit concluded that internal controls are established and operating effectively.

The Plan also fulfills its fiduciary responsibility regarding communications as outlined in federal pension legislation. In 2011, communications issued to members included the Canada Post Pension Plan 2010 Annual Report, personalized pension statements, communiqués, and the Pension Plan News and Intouch newsletters. All publications, along with general information about the Plan can be found on **cpcpension.com**.

Board of Directors, Board Committees, Investment Advisory Committee and Pension Advisory Council Memberships as of December 31, 2011

	Board of Directors	Audit Committee	Pension Committee	Human Resources and Compensation Committee	Investment Advisory Committee	Pension Advisory Council
Marc A. Courtois	Chairman	•	•	•		
Deepak Chopra	•					
Denyse Chicoyne, CFA, MBA	•		Chairperson		•	
Thomas Cryer, FCA	•	Chairperson	•			
A. Michel Lavigne, FCA	•	•	•			
Siân M. Matthews	•			•		
The Honourable Stewart McInnes, Q.C.	•			•		
Iris Petten	•			•		
Robert Pletch, Q.C.	•					
William H. Sheffield	•		•	Chairperson		
Donald Woodley	•	•		•		
J. Lorne Braithwaite, BComm, MBA					Chairperson	
Isla Carmichael, Ph.D, M.Ed, AM					•	
Phillip H. Doherty, BComm, MBA, CA					•	
Richard L. Knowles, BA (Hons), CFA					•	
Hugh Mackenzie, MA					•	
Douglas D. Greaves, BA (Hons), CFA (Canada Post)					•	Chairperson
Daryl Bean (PSAC/UPCE)						•
Mary Bishop (elected by all retirees of the Plan)						•
Gayle Bossenberry (CUPW)						•
Madeleine Cléroux (CUPW)						•
Terry Cotton (APOC)						•
Steven Galezowski, MBA, CA, CBV, CFA (Canada Post)						•
George Kuehnbaum (CUPW)						•
Sylvane Lacroix Fournier, CA (Canada Post)						•
Donald Lafleur (CUPW)						•
Daniel Maheux (CPAA)						•
Micki McCune (elected by all active members of the Plan)						•
Tim McGurrin (Canada Post)						•
Mike Moeller (UPCE/APOC/CPAA)						•
John Polak (elected by active members not represented by a bargaining agent)						•
William Price (elected by all retirees of the Plan)						•
Brad Smith (Canada Post)						•

APOC – Association of Postal Officials of Canada

CPAA – Canadian Postmasters and Assistants Association

CUPW – Canadian Union of Postal Workers

PSAC – Public Service Alliance of Canada

UPCE – Union of Postal Communications Employees

Financial Reporting

Management's Responsibility for Financial Reporting

The financial statements of the Canada Post Corporation Registered Pension Plan (the Plan) have been prepared by management, which is responsible for the integrity and fairness of the data presented therein. The accounting policies followed in the preparation of these financial statements conform to Canadian Accounting Standards for Pension Plans. Where appropriate, the financial statements include amounts based on management's best estimates and judgments.

In support of its responsibilities, management maintains systems of internal control and supporting procedures to provide assurance that transactions are authorized, assets are safeguarded and proper records are maintained. These controls include quality standards in hiring and training, the establishment of an organizational structure that provides a well-defined division of responsibilities and accountability for performance, and the communication of policies and guidelines. Internal Audit plans audits and reviews of pension activities on a cyclical basis, unless otherwise warranted through annual risk assessments.

Ultimate responsibility for the financial statements rests with the Canada Post Corporation Board of Directors. The Board of Directors ensures that management fulfills its responsibilities for financial reporting and internal control principally through the Audit Committee and the Pension Committee. The Audit Committee oversees the internal audit activities of the Plan, reviews the annual financial statements and the external auditors' report, and recommends them to the Board of Directors for approval. The Pension Committee, which is composed of the Chairman of the Board of Directors of Canada Post Corporation and four directors who are not employees of the Corporation, meets regularly with management to satisfy itself that the delegated responsibilities are properly discharged.

The Plan's actuary, Mercer (Canada) Limited, completed an actuarial assessment of the assets and going-concern obligations of the Plan as of December 31, 2011, for inclusion in the Plan's financial statements. The results of the actuaries' assessment are set out in the actuaries' opinion. This assessment was performed in accordance with accepted actuarial practice. The actuarial assumptions used in these financial statements reflect management's expectations of future economic events.

The Plan's external auditors, PricewaterhouseCoopers LLP, conducted an independent examination of the financial statements in accordance with Canadian generally accepted auditing standards and performed such tests and other procedures as they considered necessary to express an opinion. The external auditors have access to the Audit and Pension Committees to discuss their audit and related findings as to the fairness of the Plan's financial reporting and the internal control recommendations observed during the audit.

Deepak Chopra
President and
Chief Executive Officer
March 19, 2012

Wayne Cheeseman
Chief Financial Officer
March 19, 2012

Actuaries’ Opinion

Ottawa
March 19, 2012

Mercer (Canada) Limited was retained by Canada Post Corporation to perform an actuarial assessment of the assets and going-concern obligations of the Registered Pension Plan as of December 31, 2011, for inclusion in the Plan’s financial statements.

The objective of the financial statements is to fairly present the financial position of the Plan as of December 31, 2011, as a going concern. While the actuarial assumptions used to estimate obligations for the Plan’s financial statements reflect management’s expectations of future events, and while in our opinion these assumptions are reasonable, the Plan’s future experience will inevitably differ, perhaps significantly, from the actuarial assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations, and will affect the financial position of the Plan at that time, as well as the contributions required to fund it.

As part of our assessment, we examined the Plan’s recent experience relative to the economic and non-economic assumptions and presented our findings to management. In addition, we provided management with statistical, survey and other information used to develop its long-term assumptions.

Our assessment of the Plan’s actuarial assets and obligations was based on:

- an extrapolation to December 31, 2011 of the results of our December 31, 2010 actuarial valuation of the Plan’s going-concern obligations,
- pension fund data provided by Canada Post Corporation as of December 31, 2011,
- methods prescribed by the Canadian Institute of Chartered Accountants for pension plan financial statements, and
- assumptions about future events that have been developed by management and Mercer (Canada) Limited which reflect management’s expectations of these events.

We have tested the membership and pension fund data for reasonableness and consistency, and we believe it to be sufficient and reliable for the purposes of the valuation. We also believe that the assumptions and methods employed in the valuation and extrapolation are, on the whole, appropriate. Our opinions have been given and our valuation performed in accordance with accepted actuarial practice.

Jacques Demers
Fellow of the Canadian Institute
of Actuaries
Fellow of the Society of Actuaries

Cory Skinner
Fellow of the Canadian Institute
of Actuaries
Fellow of the Society of Actuaries

Mercer (Canada) Limited

Independent Auditor's Report

To the Board of Directors of Canada Post Corporation

We have audited the accompanying financial statements of the **Canada Post Corporation Registered Pension Plan**, which comprise the statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010 and the statements of changes in net assets available for benefits, changes in pension obligations and changes in deficit for the years ended December 31, 2011 and December 31, 2010 and the related notes which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian accounting standards for pension plans, 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

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we 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.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the **Canada Post Corporation Registered Pension Plan** as at December 31, 2011, December 31, 2010 and January 1, 2010 and the changes in its net assets available for benefits, changes in its pension obligations and changes in its deficit for the year ended December 31, 2011 and December 31, 2010 in accordance with Canadian accounting standards for pension plans.

PricewaterhouseCoopers LLP

Chartered Accountants, Licensed Public Accountants
March 21, 2012

Financial Statements

Statement of Financial Position

(In millions of dollars)	**December 31, 2011**	December 31, 2010	January 1, 2010
Net assets available for benefits			
Assets			
Investments (notes 5 and 6)	**$ 15,283**	$ 15,200	$ 13,376
Investment related receivables (note 5)	**118**	103	145
Contribution/other receivables (note 7)	**107**	123	130
	15,508	15,426	13,651
Liabilities			
Investment related liabilities (note 5)	**44**	46	78
Accounts payable and accrued liabilities (notes 8 and 17)	**33**	22	20
	77	68	98
Net assets available for benefits	**$ 15,431**	$ 15,358	$ 13,553
Pension obligations and deficit			
Pension obligations (notes 6 and 13)	**$ 16,570**	$ 16,038	$ 14,367
Deficit	**(1,139)**	(680)	(814)
Pension obligations and deficit	**$ 15,431**	$ 15,358	$ 13,553

See accompanying notes to the financial statements

Approved on behalf of the Board

Marc A. Courtois
Chairman of the Board of Directors

Thomas Cryer
Chairperson of the Audit Committee

Statement of Changes in Net Assets Available for Benefits

For the years ended December 31 *(in millions of dollars)*	**2011**	2010
Increases in Assets		
Net investment income (note 10)		
Investment income	**$ 489**	$ 644
Changes in fair values of investment assets and liabilities	**(457)**	800
	32	1,444
Sponsor contributions (note 11)	**538**	746
Members contributions (note 11)	**184**	186
	754	2,376
Decreases in Assets		
Retirement and survivor pension benefits	**554**	466
Commuted value transfers, lump sum death benefits and refunds	**66**	51
Administration expenses (notes 12 and 17)	**61**	54
	681	571
Increase in net assets available for benefits	**73**	1,805
Net assets available for benefits, beginning of year	**15,358**	13,553
Net assets available for benefits, end of year	**$ 15,431**	$ 15,358

See accompanying notes to the financial statements

Statement of Changes in Pension Obligations

For the years ended December 31 *(in millions of dollars)*	2011	2010
Pension obligations, beginning of year	**$ 16,038**	$ 14,367
Increase in pension obligations		
Interest on pension obligations	**928**	890
Benefits accrued	**533**	497
Changes in actuarial assumptions (note 13.b)	**–**	853
Changes in plan provisions (note 13.c)	**67**	–
Net experience losses (note 13.d)	**21**	–
	1,549	2,240
Decrease in pension obligations		
Retirement and survivor pension benefits	**554**	466
Commuted value transfers, lump sum death benefits and refunds	**66**	51
Changes in actuarial assumptions (note 13.b)	**397**	–
Net experience gains (note 13.d)	**–**	52
	1,017	569
Net increase in pension obligations	**532**	1,671
Pension obligations, end of year	**$ 16,570**	$ 16,038

Statement of Changes in Deficit

For the years ended December 31 *(in millions of dollars)*	2011	2010
Deficit, beginning of year	**$ (680)**	$ (814)
Increase in net assets available for benefits	**73**	1,805
Net increase in pension obligations	**(532)**	(1,671)
Deficit, end of year	**$ (1,139)**	$ (680)

See accompanying notes to the financial statements

Notes to the Financial Statements

1. Plan description

The following description of the Canada Post Corporation Registered Pension Plan (the Plan) is a summary only. An exact and complete description of the Plan provisions can be found in the official Plan document. If there is any conflict between this summary and the official Plan document, the official Plan document will govern.

a) General

The Plan is registered with the Canada Revenue Agency (CRA) under registration number 1063874. The Plan is a registered pension plan as defined in the *Income Tax Act* (ITA) and as such is not subject to income taxes for contributions or investment income received. The Plan is also registered with the Office of the Superintendent of Financial Institutions Canada (OSFI) under registration number 57136, and is subject to the *Pension Benefits Standards Act, 1985* (PBSA), and the Regulations thereunder. Canada Post Corporation (the Corporation) sponsors and administers the Plan.

The Plan is comprised of both a Defined Benefit component (DB component) and a Defined Contribution component (DC component). The DB component was established by the Corporation effective October 1, 2000 and covered all eligible employees. Effective January 1, 2010, the Corporation established the DC component for all newly hired Management and Exempt employees, along with those newly hired unionized employees who later transfer to a Management and Exempt position. These new employees are only eligible to participate in the DC component of the Plan.

b) Benefits

i. Defined Benefit component

Retirement pensions

A retirement pension is available based on pensionable service, the highest average pensionable earnings for five consecutive years of employment, and the age of the member at retirement. Members are eligible for an early retirement pension within 10 years of pensionable age. An unreduced retirement pension is available at pensionable age.

Pensionable age is defined as (a) the later of age 60 or the age at which a member has completed two years of eligibility service or the age at which a member would have completed two years of Plan membership assuming that the member's Plan membership continues, or (b) age 55 if a member has at least 30 years of eligibility service.

Termination of employment benefits

Termination of employment benefits depend on a member's years of pensionable service and age and may include a lump sum amount equivalent to the *commuted value* of the pension or a deferred pension.

Bridge benefits

A bridge benefit is a temporary benefit in addition to a retirement pension. It is payable from retirement until the member reaches age 65, unless death or payment of Canada or Quebec Pension Plan disability benefits occurs first.

Disability pensions

A disability pension is an immediate pension payable on an unreduced basis. It is available to qualified members prior to pensionable age.

Death benefits

Death benefits may include on-going financial support to survivors and dependent children, lump-sum payments equal to the *commuted value* of the pension benefit, and a minimum payment guarantee on the death of the member.

Indexing of benefits

Pension and survivor benefits are automatically indexed for inflation in January by a percentage that reflects the average increase in the Consumer Price Index.

ii. Defined Contribution component

Retirement benefits

Retirement benefits are based on the accumulation of contributions and investment income allocated to the member's account. The Corporation contributes 4% of each member's eligible earnings. Member contributions are optional up to a maximum of 4%. Additional matching contributions of up to 5% can be made by the Corporation based upon each member's age, years of eligible service and member's contributions. These contributions are invested as directed by each member from a selection of investment options authorized by the Plan's Pension Committee.

Termination of employment benefits and death benefits

Termination of employment benefits and death benefits would result in a return of the accumulation of contributions and investment income allocated to the member's account.

c) Funding

i. Defined Benefit component

Plan benefits are funded by contributions and investment earnings. Contributions are required from both the Corporation and the employee in order to fund benefits. These contributions, along with investment earnings, are designed to ensure the financial security of member benefits. The Plan's funding policy is reviewed annually and continually aims to achieve long-term stability in contribution rates for both the Corporation and Plan members. Contribution rates are established through actuarial funding valuations which are conducted annually to determine the funded position of the Plan. Employees who are members of the Plan are required to contribute a percentage of their pensionable earnings to the Plan fund. For 2011, employee contributions were 6.1% of earnings up to the Year's Maximum Pensionable Earnings (defined by the Canada Pension Plan and Quebec Pension Plan as $48,300 in 2011) and 9.6% of earnings in excess of this maximum. An annual increase to employee contributions of 0.4% of pensionable earnings will come into effect starting on January 1, 2012.

ii. Defined Contribution component

Plan benefits are funded by contributions and investment earnings. Contributions are made up of minimum automatic contributions by the Corporation and optional employee contributions matched by additional employer contributions. Employees make their own investment choices from a menu of funds. Canada Post periodically reviews the performance of the funds and proposes changes, if required.

d) Plan amendments

On November 24, 2011, the Board of Directors of the Canada Post Corporation (the Board) approved changes to the Plan following amendments to the PBSA and its supporting Regulations. These changes, applicable to the Defined Benefit and the Defined Contribution components, included immediate entitlement to pension benefits and improvements to death benefits. In addition, a change was made to permit a lump sum payment when the *commuted value* of the member's pension benefit is less than 20% of Year's Maximum Pensionable Earnings. These amendments resulted in an increase in the Plan's *pension obligation* of approximately $67 million (note 13.c). In 2010, no amendments were made to the Plan provisions.

2. Summary of significant accounting policies

a) Presentation

As required by the Accounting Standards Board for reporting periods beginning on or after January 1, 2011, these financial statements present, in Canadian dollars, the financial position and results of operations of the Plan in accordance with Part IV of the Canadian Institute of Chartered Accountants Handbook Section 4600, Canadian accounting standards for pension plans (CICA Section 4600).

CICA Section 4600 also requires that when selecting or changing accounting policies that do not relate to its investment portfolio or accrued *pension obligations*, a pension plan shall comply on a consistent basis with either International Financial Reporting Standards (IFRS) in Part I of the CICA Handbook, or accounting standards for private enterprises in Part II of the CICA Handbook, to the extent that those standards do not conflict with the requirements of CICA Section 4600. The Plan has elected to comply on a consistent basis with IFRS for its accounting policies that do not relate to its investment portfolio or its *pension obligations*.

Comparative financial information previously prepared in accordance with Canadian generally accepted accounting principles (CICA Section 4100) has been adjusted from January 1, 2010, the date of transition and these changes are summarized in Note 3.

These financial statements are prepared on a going-concern basis and present the information of the Plan as a separate financial reporting entity independent of the sponsor and Plan members.

b) Investments

Investments are stated at fair value. Fair value is an estimate of the amount of consideration that would be agreed upon in an arm's-length transaction between knowledgeable, willing parties who are under no compulsion to act. The calculations of fair value are based on market conditions at a specific point in time and may not be reflective of future fair value.

- Valuation of investments

  Fair value of investments is determined as follows:

  1. Short-term securities, which includes short-term government securities and bank notes are valued at cost or amortized cost that, together with accrued interest or discounts earned approximate fair value.
  2. Fixed income securities quoted in an active market are valued on the basis of quoted market prices using the bid prices. Where a quoted year-end price in an active market is not available, an estimated value is calculated using discounted cash flows based on current market *yields*, comparable securities, and financial analysis, as appropriate.
  3. *Equities* quoted in an active market are valued at year-end quoted market prices using the current bid prices for the instruments. Where a quoted price in an active market is not available for an investment *asset* or liability, a suitable method of valuation is used by management to determine fair value using appropriate valuation techniques. In making such valuations, consideration is given to the use of bid and ask prices, previous transaction prices, discounted cash flows, earnings multiples, prevailing market rates for instruments with similar characteristics or other valuation techniques that are judged relevant to the specific situation.
  4. Pooled funds are valued at year-end net *asset* values, as provided by the pooled fund manager, using the close prices of underlying securities held in the pooled fund.

5. Derivative contracts, including foreign exchange forward contracts, interest rate futures and interest rate swaps are valued at year-end quoted market prices. Foreign exchange forward contracts are valued based on the year-end foreign currency exchange rates. Interest rate futures are valued based on prices from the applicable exchange. Interest rate swaps are valued by third party swap pricing vendors.

6. Real estate investments are valued annually by professionally qualified independent appraisers, certified by the Appraisal Institute of Canada. The appraisals are in accordance with generally accepted appraisal practices and procedures, based mainly on the discounted cash flows or income approach. Direct and pooled fund investments are typically carried at cost in the year of acquisition, as an approximation of fair value, unless specific and conclusive reasons exist to change the value.

7. Investments in *private equity* and infrastructure include investments held directly and through ownership in limited partnership funds. These investments are valued using market quotes, values provided by the funds General Partners under limited partnership agreements or through the use of appropriate valuation techniques. In determining such valuations, consideration is given to previous transaction prices, discounted cash flows, earnings multiples, prevailing market rates for instruments with similar characteristics or other valuation techniques that are judged relevant to the specific situation.

- Investment transactions and income

All investment transactions are recorded at the point when the risks and rewards of ownership are transferred. Purchases and sales of publically traded investments are recognized on a trade-date basis. Real estate investment transactions are recognized on the date of closing for direct investments. Real estate and *private equity* pooled fund investment transactions are recognized on the cash call date. Investment income, including interest income, is recorded on an accrual basis. Dividend income is recognized on the ex-dividend date. Real estate, *private equity* and infrastructure incomes are recognized as dividends or distributions are received. Realized gains and losses on the sale of investments and the close of derivative contracts are included as gains and losses on disposition. Unrealized gains and losses on investments represent the change in the difference between the cost and fair value of investments at the beginning compared to the end of each year. Unrealized gains and losses on derivatives contracts represent the changes in fair values of the contracts from previously reported amounts or since the inception of the contracts if they were entered into during the year.

- Investment transaction costs

Transaction costs are incremental costs incurred in the purchase and sale of investments. Transaction costs are expensed and included in administration expenses in the statement of changes in net *assets* available for benefits.

- Management fees

Management fees for *private equity* funds and external portfolio management are expensed and included in administration expenses in the statement of changes in net *assets* available for benefits.

c) Non-investment *assets* and liabilities

The fair value of contribution/other receivables and accounts payable and accrued liabilities approximates the carrying value due to their short-term nature.

d) *Pension obligations*

Pension obligations are determined based on actuarial valuations prepared by an independent firm of *actuaries* using the projected accrued benefit actuarial cost method and management's estimate of future events. The year-end value of *pension obligations* is based on the most recent going-concern actuarial valuation prepared for funding purposes extrapolated to the year-end reporting date using management's best estimate *assumptions* (note 13).

e) Contributions

Contributions for current service are recorded in the year in which the related payroll costs are incurred. Elective service contributions are recorded in the year in which the member commits to buy back elective service. Contributions for approved leaves of absence without pay are recorded in the year in which the leave without pay occurred. Solvency contributions are recorded in the year recommended by the Plan *actuary* in the statutory actuarial valuation.

f) Foreign currency translation

Monetary *assets* and liabilities denominated in foreign currencies are translated into Canadian dollars at exchange rates in effect at year-end. Income and expenses are translated at the rate of exchange prevailing at the time of the transaction. The realized gains and losses arising from these translations are included in investment income. The unrealized gains and losses arising from these translations are included in the change in fair values in investment *assets* and liabilities.

g) Use of estimates

The preparation of financial statements in conformity with CICA Section 4600 and IFRS requires management to make estimates and *assumptions* that affect the reported amount of *assets*, liabilities and *pension obligations* as at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Significant estimates are used primarily in the determination of the *pension obligations* (note 13) and the valuation of investments (notes 5 and 6). Management monitors estimates and *assumptions* used in the preparation of the financial statements, as actual results may differ from these estimates, and the differences could be material.

h) Benefits

Benefits include payments to retired members made during the year and accruals for unpaid but earned benefits at December 31. *Commuted value* payments and transfers to other pension plans are recorded in the period in which the Plan is notified and any remaining unpaid amounts are included in accounts payable and accrued liabilities. Accrued benefits for active members of the Plan are recorded as part of the *pension obligation*.

i) Approval of the financial statements

These financial statements were approved by the Board of Directors of the Corporation on March 21, 2012.

3. Change in accounting standards

In preparing its first financial statements in accordance with CICA Section 4600 and IFRS, the Plan has adjusted amounts reported previously in accordance with CICA Section 4100. An explanation of how the transition has affected the Plan's financial position is set out in the following tables and the notes that accompany the tables:

Reconciliation of Statement of Financial Position as at January 1, 2010

(in millions of dollars)	CICA Section 4100	Actuarial asset value adjustment (i)	Fair value measurement (ii)	CICA Section 4600 & IFRS
Net assets available for benefits				
Assets				
Investments	$ 13,399	$ –	$ (23)	$ 13,376
Investment related receivables	145	–	–	145
Contribution/other receivables	130	–	–	130
	13,674	–	(23)	13,651
Liabilities				
Investment related liabilities	78	–	–	78
Accounts payable and accrued liabilities	20	–	–	20
	98	–	–	98
Net assets available for benefits	13,576	–	(23)	13,553
Actuarial asset value adjustment	1,344	(1,344)	–	–
Actuarial value of net assets available for benefits	$ 14,920	$ (1,344)	$ (23)	$ 13,553
Pension obligations and surplus/(deficit)				
Pension obligations	$ 14,367	$ –	$ –	$ 14,367
Surplus/(deficit)	553	(1,344)	(23)	(814)
Pension obligations and surplus/(deficit)	$ 14,920	$ (1,344)	$ (23)	$ 13,553

Reconciliation of Statement of Financial Position as at December 31, 2010

(in millions of dollars)	CICA Section 4100	Actuarial asset value adjustment (i)	Fair value measurement (ii)	CICA Section 4600 & IFRS
Net assets available for benefits				
Assets				
Investments	$ 15,218	$ –	$ (18)	$ 15,200
Investment related receivables	103	–	–	103
Contribution/other receivables	123	–	–	123
	15,444	–	(18)	15,426
Liabilities				
Investment related liabilities	46	–	–	46
Accounts payable and accrued liabilities	22	–	–	22
	68	–	–	68
Net assets available for benefits	15,376	–	(18)	15,358
Actuarial asset value adjustment	488	(488)	–	–
Actuarial value of net assets available for benefits	$ 15,864	$ (488)	$ (18)	$ 15,358
Pension obligations and deficit				
Pension obligations	$ 16,038	$ –	$ –	$ 16,038
Deficit	(174)	(488)	(18)	(680)
Pension obligations and deficit	$ 15,864	$ (488)	$ (18)	$ 15,358

i) Actuarial *Asset* Value Adjustment

Under CICA Section 4600, the actuarial *asset* value adjustment is no longer permitted as a valuation methodology for accounting purposes since it does not meet the definition of an *asset* or a liability. As a result, the Plan no longer includes the actuarial *asset* value adjustment in the determination of the surplus or deficit for financial reporting purposes. The actuarial *asset* value adjustment that existed as at December 31, 2009, of $1,344 million is not included in the opening statement of financial position as at January 1, 2010, and the aggregate reduction has been applied to the previously reported surplus of $553 million.

ii) Fair value measurement of investment *assets*

Under CICA Section 4600, investment *assets* are required to be measured in accordance with the IFRS guidance on fair value measurement, International Accounting Standards 39, Financial Instruments: Recognition and Measurement (IAS 39). This resulted in a change in the valuation methodology of the financial instruments that are quoted in an active market from close price to bid price. The effect of the change was a decrease of $23 million in the investment *assets* as at January 1, 2010, with an offsetting reduction to the previously reported surplus of $553 million.

For the year ended December 31, 2010, the effects of these changes are as follows:

- a decrease of $18 million, from $15,218 million to $15,200 million to investments *assets*;
- an increase of $5 million, from $795 million to $800 million to changes in fair values of investments *assets*, liabilities and net *assets* available for benefits, due to recognizing the $18 million reduction in *net investment assets* as at December 31, 2010, offset by the reversal of the $23 million reduction in *net investment assets* as at January 1, 2010.

4. Future changes in accounting policies

The following new standards and amendments, issued by the International Accounting Standards Board (IASB), have been identified as having a possible impact on the Plan in the future. Management is currently determining the impact of these standards and amendments on its financial statements.

- **IFRS 9 "Financial Instruments: Classification and Measurement"**
  In November 2009, the IASB issued IFRS 9 as the first part of Phase 1: Classification and Measurement in its project to replace IAS 39. This first part of the standard addressed the classification and measurement of financial *assets*. Initial measurement will be at fair value, and for financial *assets* not classified at fair value through profit or loss, certain transaction costs will be included. Subsequent measurement of financial *assets* will be at amortized cost or fair value.

  In October 2010, the IASB completed Phase 1 by adding requirements for liabilities to the standard, which are mostly unchanged from IAS 39.

  IFRS 9 is to be applied retrospectively for annual periods beginning on or after January 1, 2015, with early adoption permitted.

- **IFRS 13 "Fair Value Measurement"**
  In May 2011, the IASB issued IFRS 13, which defines fair value, sets out in a single IFRS a framework to measure fair value, and requires disclosures of fair value measurements. One of the options under IFRS 13 is to use the closing market prices of securities as a basis for fair value, whereas IAS 39 requires the use of bid prices. This standard is effective for annual periods beginning on or after January 1, 2013, and is applied prospectively. Early adoption is permitted.

- **IAS 32 "Financial Instruments: Presentation"**
  In December 2011, the IASB issued amendments to IAS 32, which provides additional guidance to the requirements for the offsetting of financial *assets* and financial liabilities. This standard is effective for annual periods beginning on or after January 1, 2014, and is applied retrospectively. Early adoption is permitted.

5. Investments

(in millions of dollars)	**December 31, 2011** Fair Value	**December 31, 2011** Cost	December 31, 2010 Fair Value	December 31, 2010 Cost	January 1, 2010 Fair Value	January 1, 2010 Cost
Cash and short-term securities	$ 237	$ 238	$ 374	$ 374	$ 168	$ 168
Fixed income						
Canadian	3,898	3,669	3,633	3,528	3,476	3,437
United States	102	103	120	121	83	86
International	160	153	140	137	101	96
Real return bonds	1,195	826	1,097	859	1,102	929
	5,355	4,751	4,990	4,645	4,762	4,548
Equities						
Canadian	3,548	3,061	4,203	3,094	3,587	2,820
United States	3,126	3,158	2,809	2,912	2,367	2,629
International	2,045	2,297	2,161	2,168	1,971	2,071
	8,719	8,516	9,173	8,174	7,925	7,520
Real estate (note 9.a)	852	771	624	608	508	553
Private equity (note 9.c)						
Canadian	6	6	–	–	–	–
United States	61	57	35	35	11	14
International	11	11	4	5	2	3
	78	74	39	40	13	17
Infrastructure (note 9.e)						
Canadian	42	41	–	–	–	–
Investments	**15,283**	**14,391**	15,200	13,841	13,376	12,806
Accrued investment income	50	50	42	42	39	39
Investment trades to settle	8	8	18	18	83	83
Derivatives	60	13	43	3	23	–
Investment related receivables	**118**	**71**	103	63	145	122
Investment trades to settle	(34)	(34)	(39)	(39)	(77)	(77)
Derivatives	(10)	(6)	(7)	–	(1)	–
Investment related liabilities	**(44)**	**(40)**	(46)	(39)	(78)	(77)
Net investment assets	**$ 15,357**	**$ 14,422**	$ 15,257	$ 13,865	$ 13,443	$ 12,851

a) Fair value measurements

i. Fair value hierarchy

Net investment assets, recognized at fair value in the statement of financial position, must be classified in three fair value hierarchy levels, based on the transparency of the inputs used to measure the fair value as follows:

Level 1: Fair value is based on quoted market prices in active markets for identical *assets* or liabilities.

Level 2: Fair value is based on observable inputs other than Level 1 prices, such as quoted market prices for similar *assets* or liabilities in active markets, quoted market prices for identical *assets* or liabilities in markets that are not active and other inputs that are observable or can be corroborated by observable market data for substantially the full term of the *assets* or liabilities.

Level 3: Fair value is based on valuation methods where inputs that are based on non-observable market data have a significant impact on valuation. Non-observable inputs are supported by little or no market activity.

The classification of *net investment assets* by fair value hierarchy as at December 31, 2011, was as follows:

(in millions of dollars)	**Level 1**	**Level 2**	**Level 3**	**Total**
Cash and short-term securities	$ 69	$ 167	$ –	$ 236
Fixed income	22	5,344	–	5,366
Equities	8,698	35	–	8,733
Real Estate	–	–	852	852
Private equity	–	–	78	78
Infrastructure	–	–	42	42
Derivatives	–	51	(1)	50
	$ 8,789	**$ 5,597**	**$ 971**	**$ 15,357**

The classification of *net investment assets* by fair value hierarchy as at December 31, 2010, was as follows:

(in millions of dollars)	**Level 1**	**Level 2**	**Level 3**	**Total**
Cash and short-term securities	$ 95	$ 279	$ –	$ 374
Fixed income	46	4,960	–	5,006
Equities	9,159	15	4	9,178
Real Estate	–	–	624	624
Private equity	–	–	39	39
Derivatives	2	36	(2)	36
	$ 9,302	**$ 5,290**	**$ 665**	**$ 15,257**

The classification of *net investment assets* by fair value hierarchy as at January 1, 2010, was as follows:

(in millions of dollars)	**Level 1**	**Level 2**	**Level 3**	**Total**
Cash and short-term securities	$ 71	$ 97	$ –	$ 168
Fixed income	14	4,770	10	4,794
Equities	7,912	24	2	7,938
Real Estate	–	–	508	508
Private equity	–	–	13	13
Derivatives	1	22	(1)	22
	$ 7,998	**$ 4,913**	**$ 532**	**$ 13,443**

ii. Significant transfers between level 1 and level 2

Changing market conditions during the year may result in transfers between the various fair value hierarchy levels if there is a change in the availability of quoted market prices or observable market inputs. In 2011, *equities* with a fair value of $2 million transferred from level 1 to level 2 (2010 – $3 million).

iii. Changes in level 3 fair value measurements

Level 3 investments include certain *equities*, derivative contracts, infrastructure, *private equity* and real estate investments (note 2.b). Non-observable market inputs used to determine the fair value of level 3 investments include broker quotes, pricing services, fund managers, financial models as well as the use of market rental rates, occupancy rates, growth rates and *discount rates* for its real estate investments. Total net unrealized gains reported as changes in fair values of investment *assets* and liabilities in the statement of changes in net *assets* available for benefits relating to investments valued using non-observable inputs and held at December 31, 2011, were $79 million (December 31, 2010 – gain of $76 million, January 1, 2010 – loss of $94 million). Transfers from level 3 to level 1 occurred as the fair value was based on year-end quoted market prices using the current bid price for the instrument.

Changes in the fair value of level 3 investments during 2011 are as follows:

(in millions of dollars)	Balance December 31, 2010	Net Purchases (Sales)	Gains/(losses) Realized	Gains/(losses) Unrealized	Net Transfers In/(Out) – Level 3	Balance December 31, 2011
Equities	$ 4	$ –	$ –	$ –	$ (4)	$ –
Fixed income	–	–	–	–	–	–
Infrastructure	–	41	–	1	–	42
Private equity	39	34	2	3	–	78
Real Estate	624	141	7	80	–	852
Derivatives	(2)	6	–	(5)	–	(1)
	$ 665	**$ 222**	**$ 9**	**$ 79**	**$ (4)**	**$ 971**

Changes in the fair value of level 3 investments during 2010 are as follows:

(in millions of dollars)	Balance January 1, 2010	Net Purchases (Sales)	Gains/(losses) Realized	Gains/(losses) Unrealized	Net Transfers In/(Out) – Level 3	Balance December 31, 2010
Equities	$ 2	$ (2)	$ –	$ –	$ 4	$ 4
Fixed income	10	(12)	(12)	15	(1)	–
Private equity	13	23	–	3	–	39
Real Estate	508	55	–	61	–	624
Derivatives	(1)	3	(1)	(3)	–	(2)
	$ 532	**$ 67**	**$ (13)**	**$ 76**	**$ 3**	**$ 665**

Level 3 investments are based on valuation models that use non-observable inputs such as capitalization rates. The following analysis illustrates the sensitivity of real estate investments valuations to reasonably possible alternative capitalization rate assumptions. Direct real estate investments used capitalization rates that vary from 5.4% to 7.75%. An increase/decrease of 25 basis points in the capitalization rate would decrease/increase the total value of the real estate investments by $44.6 million (2010 - $37.6 million). The impact on the valuation from changes to the capitalization rate has been calculated independently of the impact of changes in other key variables. In actual experience, the factors that would cause a change in the capitalization rate would also cause changes in other valuation *assumptions* which could amplify or reduce the impact on the valuation.

b) Derivative financial instruments

Derivative financial instruments are financial contracts, the value of which is derived from the value of the underlying *assets*, indices, interest rates or currency rates. The Plan uses derivatives to manage financial risk and to enhance returns. Derivative contracts are transacted either in the over-the-counter (OTC) market or on regulated exchanges. Derivative financial instruments held by the Plan include interest rate swaps, interest rate futures and foreign exchange forward contracts.

Interest rate swaps are negotiated agreements that are transacted between counter-parties in the OTC market in which the counter-parties agree to exchange periodic cash flows based on agreed upon reference rates applied to a specified notional amount. No exchange of principal takes place.

Interest rate futures are standard contracts traded on regulated futures exchanges. Interest rate futures are contractual obligations to buy or sell an interest-rate sensitive financial instrument on a predetermined future date at a specified price.

Foreign exchange forward contracts are negotiated agreements that are transacted between counter-parties in the OTC market. Foreign exchange forward contracts are contractual obligations to exchange one currency for another currency at a specified price at a predetermined future date.

Notional values of derivative contracts represent the contracted amount to which a rate or price is applied for computing the cash flows to be exchanged. Notional amounts are the basis upon which the returns from, and the fair value of, the contract is determined. They are not recorded as *assets* or liabilities in these financial statements and they do not necessarily indicate the amount of future cash flow or the current fair value of the derivative contracts. Accordingly, notional amounts do not indicate the Plan's exposure to credit or market risks.

Derivative contracts represent unrealized gains or losses and are recorded in the statement of financial position. Derivative contracts become favourable (*assets*) or unfavourable (liabilities) as a result of fluctuations in market rates or prices relative to their terms. Fair values of derivative contracts can fluctuate significantly.

The notional value and fair value of derivative contracts, as at December 31, 2011, was as follows:

	Notional Value		**Fair Value**	
(in millions of dollars)	**Long**	**Short**	**Assets**	**Liabilities**
Foreign exchange forward contracts	$ 1,324	$ (1,273)	$ 51	$ –
Interest rate futures	51	(51)	1	(1)
Interest rate swaps	57	(58)	8	(9)
	$ 1,432	**$ (1,382)**	**$ 60**	**$ (10)**

The notional value and fair value of derivative contracts, as at December 31, 2010, was as follows:

	Notional Value		**Fair Value**	
(in millions of dollars)	**Long**	**Short**	**Assets**	**Liabilities**
Foreign exchange forward contracts	$ 1,328	$ (1,292)	$ 38	$ (2)
Interest rate futures	104	(102)	2	–
Interest rate swaps	140	(142)	3	(5)
	$ 1,572	**$ (1,536)**	**$ 43**	**$ (7)**

The notional value and fair value of derivative contracts, as at January 1, 2010, was as follows:

	Notional Value		Fair Value	
(in millions of dollars)	**Long**	**Short**	**Assets**	**Liabilities**
Foreign exchange forward contracts	$ 1,106	$ (1,084)	$ 22	$ –
Interest rate futures	79	(79)	–	–
Interest rate swaps	114	(114)	1	(1)
	$ 1,299	**$ (1,277)**	**$ 23**	**$ (1)**

The net fair value of derivative contracts as at December 31, 2011, is $50 million (December 31, 2010 – $36 million, January 1, 2010 – $22 million). Note 6.a provides the collateral or margin fair value of securities deposited with and received from various financial institutions.

The fair value of derivative contracts by term to maturity was as follows:

	Terms to maturity				**December 31, 2011**	December 31, 2010	January 1, 2010
(in millions of dollars)	Within 1 Year	> 1 to 5 Years	> 5 to 10 Years	Over 10 Years	**Total**	Total	Total
Foreign exchange forward contracts	$ 51	$ –	$ –	$ –	$ 51	$ 36	$ 22
Interest rate futures	–	–	–	–	–	2	–
Interest rate swaps	6	(2)	–	(5)	(1)	(2)	–
	$ 57	$ (2)	$ –	$ (5)	**$ 50**	$ 36	$ 22

6. Risk management

Funding Risk

One of the main risks that the Plan faces is funding risk, the risk that the Plan's investment *asset* growth and contribution rates will not be sufficient to cover the Plan's *pension obligations* resulting in an unfunded liability.

The Plan's net funded position can change relatively quickly if there are changes in the value of the Plan's *net investment assets* or *pension obligations*. Either can result in a mismatch between the Plan's *assets* and its obligations. The most significant contributors to funding risk are the declines in *discount rates* and investments failing to achieve expected returns. In addition, the Plan's *pension obligations* are also affected by non-economic factors like changes in member demographics.

The Board manages funding risk by monitoring and reviewing the funded ratio on an ongoing basis and ensuring that investment decisions are made in accordance with the Statement of Investment Policies and Procedures (SIPP). The SIPP is designed to provide the Plan with a long-term *rate of return* net of expenses of 4.5% above inflation. Achieving the 4.5% target will assist the Plan in meeting its funding objectives and the ongoing growth of its *pension obligations*. Asset-liability studies are conducted periodically to ensure that the Plan's investment strategy remains appropriate in challenging economic environments.

Financial Risk Management

The Plan is subject to a variety of financial risks as a result of its investment activities that could adversely affect its cash flows, financial position, and income. The objective of investment risk management is to minimize the potential adverse effect of these risks and to optimize the gains over the entire portfolio.

The Board, with the assistance of the Pension Committee, staff, agents and advisors, is responsible for prudently managing, investing, and administering the Plan in order to secure the pension promise for Plan members. This requires the Board's oversight of the *assets* and liabilities to ensure they are being managed in the best interest of the members. The Board has established an investment risk management framework, which outlines the Board's appetite for risk and guides the development of investment strategies to meet the Plan's overall objectives.

Risk management for the Plan is performed by the Investment Management team through compliance with various processes and policies. Some of the policies in place include the SIPP and each of the Fund Mandates. The SIPP, approved by both the Pension Committee and the Board, prescribes a long-term debt-equity *asset* mix policy, requires portfolio investment diversification, sets guidelines on investment categories, and limits exposure to individual investments and major *asset* classes.

Risks assessment analysis for each risk category is performed and monitored regularly against the strategy and actions taken, when appropriate, according to the Plan's approved policies. In addition, as required these risks are reviewed with the Investment Advisory Committee, the Pension Committee and the Board.

a) Credit risk

Credit risk is the risk of loss should the counterparty to a transaction default or otherwise fail to perform under the terms of the contract. The Plan is exposed to direct credit risk through its short-term securities, fixed income securities, derivative contracts, and real estate rental income. Credit risk on short-term securities is mitigated by only transacting with highly-rated counterparties and establishing limits on the amount and term of short-term investments. Credit risk on fixed income investments is mitigated by establishing limits on exposure to individual counter-parties, monitoring credit ratings, and adhering to the investment criteria as set out in the Plan's SIPP.

The Plan's fixed income investment credit risk exposure is as follows:

Credit rating *(in millions of dollars)*	**December 31, 2011**		December 31, 2010		January 1, 2010	
AAA/AA	$ 3,640	68%	$ 3,472	70%	$ 3,564	75%
A	1,341	25%	1,229	25%	996	21%
BBB	373	7%	289	5%	201	4%
<BBB	1	–	–	–	1	–
	$ 5,355	**100%**	$ 4,990	100%	$ 4,762	100%

Credit risk on OTC derivative foreign exchange forward contracts and interest rate swap contracts is mitigated through the use of master netting agreements with counterparties. In addition, for derivative interest rate swaps there is an exchange of collateral between the parties in the event the fair value of outstanding transactions between the parties exceeds an agreed threshold. Credit risk on exchange traded interest rate futures derivatives is limited as these transactions are standardized contracts executed on established exchanges, each of which is associated with a well-established clearing house that assumes the obligations of both counterparties and guarantees performance. Counterparties also require a minimum credit rating of "A". Counterparty exposure is determined daily and collateral, consisting of cash and other acceptable securities, is either requested or delivered based on contracted terms.

Cash and securities with a fair value of $7 million (2010 – $3 million) have been deposited with various financial institutions as collateral or margin. The Plan is not allowed to pledge the same securities with other financial institutions or sell them to another entity unless the Plan is able to substitute such securities with other securities that the counterparties accept.

Cash with a fair value of $2 million (2010 – $1 million) has been received from various financial institutions as collateral. The Plan holds the collateral received as long as the counterparty is not a defaulting party or an affected party in connection with a specified condition listed on the contractual agreements and there is no early termination of the contractual agreement. The Plan is permitted to sell or re-pledge the collateral in the event of default by the owner of the collateral. There have been no counterparty defaults as of December 31, 2011.

Credit risk on the Plan's real estate investments arises from the possibility that tenants may be unable to fulfill their lease commitments. The Plan mitigates this risk by diversifying investments by property type and geographic location and ensuring investments are managed by professional property managers.

b) Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices whether these changes are caused by factors specific to an individual investment or factors affecting all securities traded in the market. Market risk comprises interest rate risk, currency risk, and other price risk.

i. Interest rate risk

Interest rate risk is the risk that the fair value or future cash flow of the Plan's investments will fluctuate due to changes in market interest rates. It arises primarily on interest-bearing financial instruments held in the Plan's short-term securities, fixed income portfolio and derivative interest rate contracts. Interest rate risk indirectly affects *equities* as earnings multiples change with changes in interest rates and the relative attractiveness of *equities* also changes with changes in interest rates. Excess cash is invested in short-term securities.

To properly manage the Plan's interest rate risk, guidelines on the weighting, term to maturity and duration for the short-term securities and fixed income securities are set and monitored. In addition, to further mitigate interest rate risk the Plan may enter into interest rate futures and interest rate swap contracts.

The terms to contractual maturity of the Plan's fixed income securities, excluding interest rate swaps, are as follows:

(in millions of dollars)		Terms to maturity			**December 31, 2011**		December 31, 2010		January 1, 2010	
Interest-bearing financial instruments	Within 1 Year	1 to 5 Years	> 5 to 10 Years	Over 10 Years	**Total**	**Yield to Maturity**	Total	Yield to Maturity	Total	Yield to Maturity
Fixed income – bonds										
Government of Canada	$ 335	$ 538	$ 254	$ 212	$ 1,339	1.4%	$ 1,235	2.1%	$ 1,311	2.1%
Canadian corporate	33	431	501	741	1,706	2.3%	1,621	3.6%	1,386	3.6%
Government of United States	1	–	–	–	1	0.1%	1	0.5%	21	4.2%
United States corporate	10	30	45	16	101	4.8%	119	4.4%	62	5.1%
International corporate	4	72	48	36	160	4.0%	140	3.8%	101	4.2%
Provincial and municipal	48	180	260	365	853	2.5%	777	3.6%	779	3.8%
Real return – Canada	–	–	167	799	966	0.2%	901	1.0%	920	1.5%
Real return – Provincial	–	13	69	147	229	0.3%	196	1.3%	182	1.8%
	$ 431	$ 1,264	$ 1,344	$ 2,316	**$ 5,355**	**1.8%**	$ 4,990	2.7%	$ 4,762	2.8%

As at December 31, 2011, an increase or decrease of 1% in the prevailing interest rates, assuming a parallel shift in the *yield* curve, with all other variables remaining constant, would decrease or increase the value of net *assets* available for benefits by approximately $427 million (2010 – $445 million). The Plan's interest rate sensitivity was determined based on the weighted duration of the Plan's portfolio. In practice, actual results may differ from this sensitivity analysis and the difference could be material.

ii. Currency risk

Currency risk is the risk that the value of the Plan's investments will fluctuate due to changes in foreign exchange rates. It arises from Plan investments that are denominated in a currency other than the Canadian dollar, which is the Plan's reporting currency. The Plan is exposed to the risk that the value of these securities denominated in other currencies will fluctuate due to changes in foreign currency exchange rates.

The Plan does not speculate in currencies or hold net short positions. To mitigate its overall currency exposure, the Plan enters into derivative contracts for the purchase or sale of foreign currency to adjust the exposure to a particular currency. To mitigate counterparty risk, all transactions settle on a net basis. The Plan hedges between 15% and 45% of its total foreign currency exposure. No single foreign currency exposure can exceed 20% of Plan *assets*. All current contracts expire within 3 months. The Plan only deals with highly-rated counterparties, typically major financial institutions, with a minimum credit rating of "A" as reported by a recognized credit rating agency.

The Plan's exposure, net of derivatives, by geographical location of the issuer and by currency is as follows:

(in millions of dollars)		**Geographical location**			**Currency**	
Currency – Canadian $ equivalent, net of foreign exchange forward contracts	**December 31, 2011**	December 31, 2010	January 1, 2010	**December 31, 2011**	December 31, 2010	January 1, 2010
Canadian dollar	$ 9,864	$ 9,933	$ 8,845	$ 11,252	$ 11,332	$ 10,025
United States dollar	3,312	3,052	2,575	2,689	2,373	1,966
Euro	519	717	796	278	455	562
Other European	629	613	491	409	433	391
Japanese yen	356	482	310	199	328	219
Other Pacific	259	232	187	323	242	188
Emerging markets	418	228	239	207	94	92
	$ 15,357	$ 15,257	$ 13,443	**$ 15,357**	$ 15,257	$ 13,443

Based on the Plan's net exposure as at December 31, 2011, if the Canadian dollar strengthened or weakened by 10% in relation to all foreign currencies, with all other factors remaining constant, net *assets* available for benefits would have decreased or increased by approximately $410 million (2010 – $392 million). In practice, actual results may differ from this sensitivity analysis and the difference could be material.

The Plan's derivative foreign currency forward contracts by currency are as follows:

(in millions of dollars)

	December 31, 2011			
	Notional Value			**Average**
Currency	**Receivable**	**Payable**	**Net**	**rate**
United States dollar	$ 828	$ (799)	$ 29	$ 1.06
Euro	226	(214)	12	1.40
Japanese yen	163	(156)	7	0.01
British pound	107	(104)	3	1.63
	$ 1,324	**$ (1,273)**	**$ 51**	

(in millions of dollars)

	December 31, 2010			
	Notional Value			Average
Currency	Receivable	Payable	Net	rate
United States dollar	$ 833	$ (813)	$ 20	$ 1.02
Euro	230	(218)	12	1.41
Japanese yen	155	(155)	–	0.01
British pound	102	(99)	3	1.61
Hong Kong dollar	8	(7)	1	0.13
	$ 1,328	$ (1,292)	$ 36	

(in millions of dollars)

	January 1, 2010			
	Notional Value			Average
Currency	Receivable	Payable	Net	rate
United States dollar	$ 699	$ (689)	$ 10	$ 1.06
Euro	228	(220)	8	1.56
Japanese yen	96	(92)	4	0.01
British pound	73	(73)	–	1.69
Hong Kong dollar	10	(10)	–	0.14
	$ 1,106	$ (1,084)	$ 22	

iii. Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices other than those arising from interest rate risk or currency risk. Changes in market prices may be caused by factors specific to an individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market. The Plan is subject to other price risk through its public *equity* investment as well as its *private equity* investments as they are impacted by many market variables. The Plan moderates other price risk through its policy of diversifying its investments across *asset* classes and geographical locations based on criteria established in the SIPP. Fund managers and investment staff regularly monitor the portfolio by sector, country, market capitalization and trading liquidity.

The Plan's exposure to other price risk is as follows:

	December 31, 2011		December 31, 2010		January 1, 2010	
(in millions of dollars)	**Effective other price risk exposure**	**% of total other price risk exposure**	Effective other price risk exposure	% of total other price risk exposure	Effective other price risk exposure	% of total other price risk exposure
Equities and private equity						
Canadian	$ 3,554	40%	$ 4,203	46%	$ 3,587	45%
United States	3,187	36%	2,844	31%	2,378	30%
International	2,056	24%	2,165	23%	1,973	25%
	$ 8,797	**100%**	$ 9,212	100%	$ 7,938	100%

As at December 31, 2011, 57% (2010 – 60%) of the Plan's net investments were in *equities*. If *equity* prices increased or decreased by 10% as at year-end, with all other factors remaining constant, net *assets* available for benefits would have increased or decreased by approximately $877 million (2010 – $964 million). In practice, actual results may differ from this sensitivity analysis and the difference could be material.

c) Liquidity risk

Liquidity risk is the risk that the Plan will not be able to meet its financial obligations as they fall due. Liquidity risk also includes the risk of not being able to liquidate *assets* in a timely manner at a reasonable price. The financial liabilities of the Plan include investment related liabilities, all of which will become due within the next year. The Plan is also exposed to the settlement of derivatives, margin calls on derivatives and pension related payments. Note 5.b provides the terms to contractual maturity of the Plan's derivative contracts.

The Plan forecasts its cash requirements over the short and long-term to determine whether sufficient funds will be available. The Plan's primary sources of liquidity are funds generated from the Plan's investments and employer and employee contributions. The Plan primarily invests in securities that are traded in active markets and can be readily sold. Real estate, *private equity* and infrastructure investments are also subject to liquidity risk which is mitigated by managing the overall amount invested in those *asset* classes and by limiting the amount invested in any one property or pooled fund. The Plan retains sufficient cash and short-term security positions to maintain a reasonable level of liquidity.

The Plan's primary future liabilities include the *pension obligations* (note 13). In the normal course of operations, the Plan enters into contracts that give rise to commitments (note 18) which may also impact liquidity.

7. Contribution / other receivables

(in millions of dollars)		**December 31, 2011**	December 31, 2010	January 1, 2010
Current service contributions	– Sponsor	$ 28	$ 39	$ 36
	– Members	15	21	24
Other contributions[1]	– Leave of absence	35	32	31
	– Elective service	27	29	30
Other		2	2	9
		$ 107	$ 123	$ 130

[1] Leave of absence contribution receivables for approved leave of absence without pay are generally payable over a period equal to twice the period of leave of absence. Elective service contribution receivables for eligible service are payable over a maximum payment period of 20 years for members 45 years or older at the date of election, or to age 65 for members less than age 45 at the date of election.

8. Accounts payable and accrued liabilities

(in millions of dollars)	**December 31, 2011**	December 31, 2010	January 1, 2010
Accounts payable and accrued liabilities	$ 9	$ 10	$ 7
Accrued benefits payable	24	12	13
	$ 33	$ 22	$ 20

9. Investment in real estate, *private equity* and infrastructure

(a) Investment in real estate

The investment in real estate is as follows:

	December 31, 2011		December 31, 2010[1]		January 1, 2010[1]	
(in millions of dollars)	**Fair Value**	**Cost**	Fair Value	Cost	Fair Value	Cost
Direct investments	$ 485	$ 471	$ 315	$ 337	$ 248	$ 299
Pooled funds	367	300	309	271	260	254
	$ 852	**$ 771**	$ 624	$ 608	$ 508	$ 553

[1] Presentation of direct investments and pooled funds have been reclassified for comparability

(b) Real estate net investment income

Real estate net investment income for the year ended December 31, is as follows:

(in millions of dollars)	**2011**	2010
Investment income	$ 33	$ 22
Net realized gains	7	–
Net unrealized gains	80	61
	$ 120	$ 83

(c) Investment in *private equity*

The investment in *private equity* is as follows:

	December 31, 2011		December 31, 2010		January 1, 2010	
(in millions of dollars)	**Fair Value**	**Cost**	Fair Value	Cost	Fair Value	Cost
Pooled funds	**$ 78**	**$ 74**	$ 39	$ 40	$ 13	$ 17

(d) *Private equity* net investment income

Private equity net investment income for the year ended December 31, is as follows:

(in millions of dollars)	**2011**	2010
Net realized gains	$ 2	$ –
Net unrealized currency gains (losses)	4	(1)
Net unrealized (losses) gains	(1)	4
	$ 5	$ 3

(e) Investment in infrastructure

The investment in infrastructure is as follows:

	December 31, 2011		December 31, 2010		January 1, 2010	
(in millions of dollars)	**Fair Value**	**Cost**	Fair Value	Cost	Fair Value	Cost
Direct investments	$ 21	$ 21	$ –	$ –	$ –	$ –
Pooled funds	21	20	–	–	–	–
	$ 42	**$ 41**	$ –	$ –	$ –	$ –

(f) Infrastructure net investment income

Infrastructure net investment income for the year ended December 31, is as follows:

(in millions of dollars)	**2011**	2010
Investment income	$ 2	$ –
Net unrealized gains	1	–
	$ 3	$ –

10. Net investment income

Net investment income by primary financial instrument type for the year ended December 31, is as follows:

(in millions of dollars)	**2011**	2010
Interest income (losses)		
Cash and short-term securities	$ 4	$ 2
Fixed income	162	158
Fixed income – real return bonds	29	28
Derivatives	(12)	3
	183	191
Dividend income		
Canadian equities	102	93
United States equities	70	52
International equities	66	48
	238	193
Real estate (note 9.b)	33	22
Infrastructure (note 9.f)	2	–
Realized gains (losses) on disposal		
Short-term securities	1	–
Canadian fixed income	91	38
International fixed income	–	3
United States fixed income	2	2
Canadian equities	142	152
United States equities	16	93
International equities	(120)	13
Derivatives	2	1
Real estate (note 9.b)	7	–
Private equity (note 9.d)	2	–
	143	302
Realized currency (losses) gains on disposal		
Canadian fixed income	–	5
United States fixed income	(1)	1
International fixed income	(1)	–
Canadian equities	(1)	(1)
United States equities	(94)	(32)
International equities	(13)	(37)
	(110)	(64)
Net realized investment income	**489**	644
Net unrealized (losses) gains	(658)	888
Net unrealized currency gains (losses)	201	(88)
Changes in fair values of investment assets and liabilities	**(457)**	800
	$ 32	$ 1,444

11. Contributions

(in millions of dollars)		**2011**	2010
Sponsor	– Current service	$ 319	$ 321
	– Special payments	219	425
Members	– Current service	177	177
	– Past service	5	7
	– Transfers from other plans	2	2
		$ 722	$ 932

The Plan's December 31, 2010, actuarial valuation disclosed a solvency deficit of $3,204 million and a going-concern deficit of $175 million requiring the Corporation to make special payments of approximately $623 million and $17 million to reduce the solvency and going-concern deficits respectively in 2011. Special payments of $202 million for solvency and $17 million for going-concern were made by the Corporation to the Defined Benefit component of the Plan during 2011. The reduction in special payment is in accordance with the new funding measures as permitted by legislation. In August of 2011, the Corporation obtained approval from the Minister of Finance and the Minister of Transport, Infrastructure and Communities to reduce the special solvency payments from January 1, 2011, to June 30, 2012. This reduction is $433 million in 2011.

12. Administration expenses

(in millions of dollars)	**2011**	2010
Plan administration	$ 13	$ 11
Investment fees	27	29
Transaction costs	19	12
Professional fees	2	2
Custodial fees	1	1
Other	(1)	(1)
	$ 61	$ 54

13. *Pension obligations*

a) Actuarial methodology

The actuarial present value of the *pension obligations* is an estimate of the value of *pension obligations* of the Plan in respect of benefits accrued to date for all active and inactive members. The obligation is measured using the same *actuarial assumptions* and methods required for the Plan's going-concern funding requirements by OSFI and the PBSA which reflect management's best estimates. The most recent actuarial valuation for funding purposes, prepared by Mercer (Canada) Limited as at December 31, 2010, was extrapolated to determine the *pension obligations* as at December 31, 2011. The valuation used the projected accrued benefit actuarial cost method with respect to benefits, and assumes that the Plan will continue on a going-concern basis. The next valuation for funding purposes will be prepared as of December 31, 2011.

b) ***Actuarial Assumptions***

The *actuarial assumptions* used in determining the *pension obligations* reflect management's expectations of long-term economic and demographic conditions. Each of the *assumptions* is updated periodically based on a detailed review of the Plan's actual results and on expectations for future trends. During 2011, a review of these *assumptions* was conducted to ensure their adequacy and appropriateness. As well, significant events that occurred in 2011 have been factored into the extrapolation as at December 31, 2011. The actuarial present value of *pension obligations* was determined based on the following long-term economic *assumptions*:

	December 31, 2011	December 31, 2010	January 1, 2010
Discount rate	**5.8%**	5.8%	6.2%
Salary escalation rate			
– Union groups	per the most recent collective agreement		
– Following expiry of collective agreements and non-unionized groups – average of	**3.0%**	3.0%	3.0%
Consumer price index (CPI)	**2.5%**	2.5%	2.5%

The *pension obligations* are sensitive to changes in the above economic *assumptions*. Various *assumptions* were also made for salary/promotional scale, mortality, retirement and turnover. Changes in the retirement age *assumption* resulted in a decrease in *pension obligations* of $203 million (2010 – increase of $867 million was mostly as a result of the change in *discount rate*) and the impact of the changes in salary escalation *assumptions* due to new collective agreements resulted in a decrease in the *pension obligations* of $194 million (2010 – decrease of $14 million).

c) Plan provisions

In 2011, amendments, as described in note 1.d, were made to the Plan's provisions and resulted in an increase in *pension obligations* of $67 million. The increase is mostly due to the improvements to death benefits.

d) Experience losses (gains)

The composition of experience (gains) losses, as at December 31, is summarized below:

(in millions of dollars)	**2011**	2010
Past service buyback	$ 11	$ 15
Economic	14	(32)
Demographic	(4)	(35)
	$ 21	$ (52)

e) Sensitivity analysis

The *discount rate* used to estimate the present value of the *pension obligation* has a significant effect on the *pension obligations* at the end of the year. A decrease of fifty-basis points in the *discount rate* would have increased the value of the *pension obligations* by $1,236 million and an increase of fifty-basis points in the *discount rate* would have decreased the value of the *pension obligations* by $1,105 million.

14. Supplementary Retirement Arrangement (SRA)

The SRA provides Plan members and their survivors with benefits that, because of limitations imposed by the ITA, cannot be provided under a registered pension plan. The SRA, together with the Plan, provides overall pension benefits to eligible members.

The SRA is registered with CRA as a Retirement Compensation Arrangement under registration number RC4102229 and is administered in accordance with the applicable requirements of the ITA. Because the *assets* of the SRA are held in a separate fund, the net *assets* available for benefits and the *pension obligations* of the SRA are not included in these financial statements.

15. Funding valuation

In accordance with the PBSA and the ITA, an actuarial valuation is required to be filed every year unless the funded status is greater than 120%, to estimate the Plan's surplus or deficit on a going-concern and solvency basis, and to determine the Plan's minimum funding requirements. The last actuarial valuation filed with OSFI and CRA, as at December 31, 2010, disclosed a going-concern deficit to be funded of $175 million and a solvency deficit to be funded of $3,204 million at that date.

The current extrapolated estimate of the financial position of the Plan as at December 31, 2011, based on existing rules and regulations, reported a going-concern deficit to be funded of approximately $423 million and a solvency deficit to be funded of approximately $4,672 million. Based on the expected actuarial valuation, special contributions for going-concern and solvency deficits for 2012 are estimated at approximately $955 million.

In March 2011, regulations under the PBSA came into effect which allow Crown corporations to reduce special solvency payments. The sum of all reductions applied to the required special payments cannot exceed 15% of the market value of the Plan *assets* at the end of the most recent Plan year. The Corporation obtained the approval from the Minister of Finance and the Minister of Transport, Infrastructure and Communities to reduce the special solvency contribution from January 1, 2011, to June 30, 2012. This reduction is $433 million for 2011 and $312 million for the first 6 months of 2012.

Under CICA Section 4600, the actuarial *asset* value adjustment is no longer included in the valuation methodology for accounting purposes. Therefore the Plan deficit in these financial statements is different from the deficit determined by the funding valuation. The following table provides a reconciliation between the going-concern deficit recorded in the valuation for funding purposes to the amount recorded in these financial statements.

(in millions of dollars)	Extrapolation **2011**	Filed Valuation 2010
Deficit to be funded	$ (423)	$ (175)
Actuarial asset value adjustment	(716)	(488)
Other	–	(17)
Deficit per financial statements	**$ (1,139)**	$ (680)

16. Capital

Management of the Plan defines its capital as the funded status (surplus/(deficit)) as determined annually based on the fair value of the *net investment assets* less the *pension obligations* as determined by an actuarial valuation prepared by an independent *actuary*. The funding surpluses or deficits are used to measure the long term health of the Plan to meet its obligations to its members and their survivors.

Management's objective, when managing the Plan's capital, is to ensure the Plan is fully funded to meet its benefit obligations over the long term through the management of investments, contribution rates and benefits.

The Pension Committee is responsible for ensuring the Plan *assets* are managed in accordance with the SIPP and the objectives and goals outlined therein.

17. Related party transactions

The Plan had the following transactions with related parties:

a) The Corporation

Transactions with the Corporation were conducted in the normal course of activities and measured at the exchange amount. Included in administration expenses is $8 million (2010 – $6 million) for administration services provided by the Corporation to the Plan. Included in accounts payable and accrued liabilities is $1 million (2010 – $1 million) due to the Corporation for administration services provided to the Plan which are unsecured and will be settled in cash.

b) Key Management Personnel Compensation

The Plan defines its key management personnel (KMP) as Canada Post Corporation's Board of Directors and other senior executives responsible for planning, controlling and directing the activities of the Plan. As some of the Plan's KMP are employees of Canada Post Corporation, their remuneration, which includes short-term and post-employment benefits, is paid by the Corporation and the Plan reimburses the Corporation for a portion of these expenses.

The reimbursement for 2011 and 2010 for senior executives was $614 thousand and $528 thousand respectively and is included in the amount disclosed in note 17.a). No remuneration is charged back from the Corporation to the Pension Plan for the services provided by the Board of Directors of Canada Post Corporation. Full disclosure of the Board of Directors remuneration can be found in the Canada Post Corporation consolidated financial statements.

18. Commitments

In addition to derivative contracts (note 5.b), the Plan has committed to enter into real estate and *private equity* investments which may be funded over the next several years in accordance with agreed upon terms and conditions. The future commitments are generally payable on demand based on the capital needs of the investment manager. As at December 31, 2011, potential commitments amounted to $355 million (2010 – $275 million).

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(in millions of dollars) (Unaudited)	2011	2010[1]	2009[2]	2008	2007
Assets					
Investments	$ 15,283	$ 15,200	$ 13,399	$ 11,676	$ 14,573
Investment related receivables	118	103	144	82	85
Contribution/other receivables	107	123	130	109	74
Total assets	**15,508**	**15,426**	**13,673**	**11,867**	**14,732**
Liabilities					
Investment related liabilities	44	46	77	140	46
Accounts payable and accrued liabilities	33	22	20	18	20
Total liabilities	**77**	**68**	**97**	**158**	**66**
Net assets available for benefits	**15,431**	**15,358**	**13,576**	**11,709**	**14,666**
Actuarial asset value adjustment	–	–	1,344	1,171	(266)
Actuarial value of net assets available for benefits	**$ 15,431**	**$ 15,358**	**$ 14,920**	**$ 12,880**	**$ 14,400**
Pension obligations and surplus/(deficit)					
Pension obligations	$ 16,570	$ 16,038	$ 14,367	$ 14,107	$ 13,071
Surplus/(deficit)	(1,139)	(680)	553	(1,227)	1,329
Total pension obligations and surplus/(deficit)	**$ 15,431**	**$ 15,358**	**$ 14,920**	**$ 12,880**	**$ 14,400**

(in millions of dollars) (Unaudited)	2011	2010[1]	2009[2]	2008	2007
Changes in net assets available for benefits					
Investment income/(losses)	**$ 32**	**$ 1,444**	**$ 1,882**	**$ (2,778)**	**$ 317**
Contributions – sponsor					
Current Service	319	321	269	61	100
Special payments	219	425	–	–	–
Transfer	–	–	–	–	–
Contributions – members					
Current Service	177	177	184	181	173
Past Service	5	7	5	5	8
Other	2	2	1	1	1
Total contributions	**722**	**932**	**459**	**248**	**282**
Less					
Benefits					
Retirement and survivor pensions	554	466	392	325	262
Commuted value transfers and other	66	51	49	48	48
Transfers to other plans	–	–	3	1	1
Total benefits	**620**	**517**	**444**	**374**	**311**
Administration expenses					
Plan administration	13	11	10	10	10
Investment fees	46	41	26	40	39
Other	2	2	(6)	3	3
Total administration expenses	**61**	**54**	**30**	**53**	**52**
Increase/(decrease) in net assets	**$ 73**	**$ 1,805**	**$ 1,867**	**$ (2,957)**	**$ 236**
Performance					
Rate of return	0.2%	10.4%	16.2%	-19.3%	2.1%
Benchmark	0.8%	9.8%	15.8%	-17.6%	0.9%

[1] In preparing its first financial statements in accordance with CICA Section 4600 and IFRS, the Plan has adjusted the amounts reported in 2010 (which were previously reported in accordance with CICA Section 4100) for comparative purposes.
[2] In 2010, the Plan changed its accounting policy for determining the actuarial asset value adjustment and 2009 has been restated for comparability.

Funding Valuation History

Funding valuations must be filed with the Office of the Superintendent of Financial Institutions (OSFI). OSFI requires that the funding valuation be done on both a going-concern and solvency basis. Prior to 2010, mandatory funding valuations had to be filed every three years unless the plan was in a solvency deficit position. However, plan sponsors could voluntarily file earlier, if desired. Starting in 2010, funding valuations must be filed every year unless the solvency funded status is greater than 120 per cent. 2011 funding valuation will be filed by June 2012. For reference, all previously filed funding valuations are detailed below.

Filed Funding Valuations*

(in millions of dollars) (Unaudited)	**2010**	**2009**	**2007**	**2006**	**2005**	**2004**	**2003**	**2002**	**2001**	**2000**
Going-concern – assumed the Plan continues in operation										
Fair value of assets	$ 15,376	$ 13,576	$ 14,666	$ 14,430	$ 12,211	$ 10,307	$ 8,918	$ 7,500	$ 7,756	$ 7,058
Asset smoothing adjustment	488	1,357	(266)	(1,340)	(715)	(103)	325	974	113	–
Smoothed value of assets	15,864	14,933	14,400	13,090	11,496	10,204	9,243	8,474	7,869	7,058
Funding target	16,039	14,365	13,143	12,097	11,145	10,108	9,359	8,446	7,762	6,856
Funding surplus (deficit)	$ (175)	$ 568	$ 1,257	$ 993	$ 351	$ 96	$ (116)	$ 28	$ 107	$ 202
Funding ratio	98.9%	104.0%	109.6%	108.2%	103.1%	100.9%	98.8%	100.3%	101.4%	102.9%
Assumptions used for going-concern valuations										
Discount rate	5.8%	6.2%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%
Inflation rate	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%
Solvency – assumed the Plan is terminated on the date of valuation										
Fair value of assets	$ 15,364	$ 13,573	$ 14,664	$ 14,428	$ 12,209	$ 10,305	$ 8,916	$ 7,481	$ 7,737	$ 7,040
Asset smoothing adjustment	488	1,357	–	–	–	(103)	325	–	–	–
Solvency assets	15,852	14,930	14,664	14,428	12,209	10,202	9,241	7,481	7,737	7,040
Solvency obligations	19,056	16,777	14,215	14,145	13,410	11,338	9,425	7,940	6,933	6,218
Solvency excess (deficit)	$ (3,204)	$ (1,847)	$ 449	$ 283	$ (1,201)	$ (1,136)	$ (184)	$ (459)	$ 804	$ 822
Solvency ratio	83.2%	89.0%	103.2%	102.0%	91.0%	90.0%	98.0%	94.2%	111.6%	113.2%

* A funding valuation for the year 2008 was not required by OSFI.