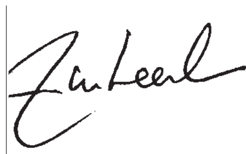
Management's Responsibility for Financial Reporting

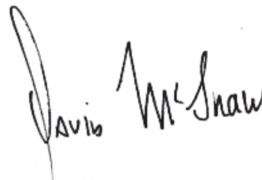
The consolidated financial statements of the Ontario Teachers' Pension Plan have been prepared by management, which is responsible for the integrity and fairness of the data presented, including the many amounts which must, of necessity, be based on estimates and judgments. The accounting policies followed in the preparation of these consolidated financial statements conform to Canadian generally accepted accounting principles. Financial information presented throughout the annual report is consistent with the consolidated financial statements.

Systems of internal control and supporting procedures are maintained to provide assurance that transactions are authorized, assets safeguarded and proper records maintained. These controls include quality standards in hiring and training of employees, a code of conduct, 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 through the organization.

Ultimate responsibility for the consolidated financial statements rests with the members of the Board. The Board is assisted in its responsibilities by the Audit & Actuarial Committee, consisting of six Board members who are not officers or employees of the plan administrator. In addition, the committee reviews the recommendations of the internal and external auditors for improvements in internal control and the action of management to implement such recommendations. In carrying out its duties and responsibilities, the committee meets regularly with management and with both the external and internal auditors to review the scope and timing of their respective audits, to review their findings and to satisfy itself that their responsibilities have been properly discharged. This committee reviews the consolidated financial statements and recommends them for approval by the Board.

The Plan's external auditors, Deloitte & Touche LLP, are directly accountable to the Audit & Actuarial Committee and have full and unrestricted access to the committee. They discuss with the committee their audit and related findings as to the integrity of the Plan's financial reporting and the adequacy of internal control systems. The plan's external auditors have conducted an independent examination of the consolidated financial statements in accordance with Canadian generally accepted auditing standards, performing such tests and other procedures as they consider necessary to express the opinion in their Report to the Administrator.





Jim Leech
President and Chief Executive Officer
February 18, 2009

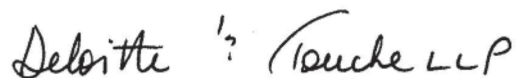
David McGraw
Senior Vice-President and Chief Financial Officer

Auditors' Report to the Administrator

We have audited the consolidated statement of net assets available for benefits and accrued pension benefits and deficit of the Ontario Teachers' Pension Plan as at December 31, 2008 and the consolidated statements of changes in net assets available for benefits, changes in accrued pension benefits and changes in deficit for the year then ended. These consolidated financial statements are the responsibility of the Plan's Administrator. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the net assets available for benefits and accrued pension benefits and deficit of the Plan as at December 31, 2008 and the changes in its net assets available for benefits, accrued pension benefits and deficit for the year then ended in accordance with Canadian generally accepted accounting principles.



Chartered Accountants
Licensed Public Accountants
February 18, 2009

Actuaries' Opinion

Mercer (Canada) Limited was retained by the Ontario Teachers' Pension Plan Board (the "Board") to perform an actuarial valuation of the assets and the going concern liabilities of the Ontario Teachers' Pension Plan (the "Plan") as at December 31, 2008, for inclusion in the Plan's financial statements. As part of the valuation, we examined the Plan's recent experience with respect to the non-economic assumptions and presented our findings to the Board.

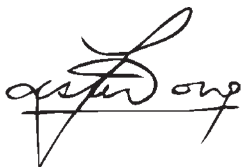
The valuation of the Plan's actuarial liabilities was based on:

- membership data provided by the Ontario Teachers' Pension Plan Board as at December 31, 2007;
- methods prescribed by Section 4100 of the Canadian Institute of Chartered Accountants' Handbook for pension plan financial statements;
- real and nominal interest rates on long term Canada bonds at the end of 2008;
- assumptions about future events (for example, future rates of inflation and future retirement rates) which have been communicated to us as the Board's best estimate of these events; and
- information obtained from the Ontario Ministry of Labour and other published data on negotiated wage settlements in the 2008/2009 to the 2011/2012 school years.

The objective of the financial statements is to fairly present the financial position of the Plan on December 31, 2008 as a going concern. This is different from the statutory valuation (the actuarial valuation required by the *Pension Benefits Act (Ontario)*), which establishes a prudent level for future contributions.

While the actuarial assumptions used to estimate liabilities for the Plan's financial statements represent the Board's best estimate of future events and market conditions at the end of 2008, 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, and the contributions required to fund it, at that time.

We have tested the 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 methods employed in the valuation are appropriate for the purposes of the valuation, and that the assumptions used in the valuation are in accordance with accepted actuarial practice. Our opinions have been given, and our valuation has been performed, in accordance with accepted actuarial practice.



Lester J. Wong, F.C.I.A.
February 18, 2009

Malcolm P. Hamilton, F.C.I.A.

Consolidated statement of net assets available for benefits and accrued pension benefits and deficit

as at December 31, 2008 ($ millions)	***2008***	*2007*
Net assets available for benefits		
Assets		
Investments (note 2)	**$132,045**	$155,830
Receivable from the Province of Ontario (note 3)	**2,187**	1,839
Receivable from brokers	**182**	245
Cash	**186**	88
Fixed assets	**33**	24
	134,633	158,026
Liabilities		
Investment-related liabilities (note 2)	**46,944**	47,829
Due to brokers	**88**	1,390
Accounts payable and accrued liabilities	**168**	261
	47,200	49,480
Net assets available for benefits	**87,433**	108,546
Actuarial asset value adjustment (note 4)	**19,524**	(3,629)
Actuarial value of net assets available for benefits	**$106,957**	$104,917
Accrued pension benefits and deficit		
Accrued pension benefits (note 5)	**$118,141**	$115,459
Deficit	**(11,184)**	(10,542)
Accrued pension benefits and deficit	**$106,957**	$104,917

On behalf of the Plan Administrator:

Chair

Board Member

Consolidated statement of changes in net assets available for benefits

for the year ended December 31, 2008 ($ millions)	*2008*	*2007*
Net assets available for benefits, beginning of year	$108,546	$106,014
Investment operations		
Investment (loss)/income (note 9)	(19,039)	4,678
Administrative expenses – Investments (note 14a)	(155)	(229)
Net investment operations	(19,194)	4,449
Member service operations		
Contributions (note 12)	2,311	2,138
Benefits paid (note 13)	(4,195)	(4,020)
Administrative expenses – Member Services (note 14b)	(35)	(35)
Net member service operations	(1,919)	(1,917)
(Decrease)/increase in net assets available for benefits	(21,113)	2,532
Net assets available for benefits, end of year	$ 87,433	$108,546

Consolidated statement of changes in accrued pension benefits

for the year ended December 31, 2008 ($ millions)	*2008*	*2007*
Accrued pension benefits, beginning of year	$115,459	$110,496
Increase in accrued pension benefits		
Interest on accrued pension benefits	5,352	5,177
Benefits accrued	3,458	3,332
Changes in actuarial assumptions (note 5a)	(2,319)	492
Experience losses/(gains) (note 5c)	386	(18)
	6,877	8,983
Decrease in accrued pension benefits		
Benefits paid (note 13)	4,195	4,020
Net increase in accrued pension benefits	2,682	4,963
Accrued pension benefits, end of year	$118,141	$115,459

Consolidated statement of changes in deficit

for the year ended December 31, 2008 ($ millions)	*2008*	*2007*
Deficit, beginning of year	$(10,542)	$(15,646)
(Decrease)/increase in net assets available for benefits	(21,113)	2,532
Change in actuarial asset value adjustment (note 4)	23,153	7,535
Increase in actuarial value of net assets available for benefits	2,040	10,067
Net increase in accrued pension benefits	(2,682)	(4,963)
Deficit, end of year	$(11,184)	$(10,542)

Notes to consolidated financial statements

for the year ended December 31, 2008

Description of Plan

The following description of the Ontario Teachers' Pension Plan (the Plan) is a summary only. For more complete information, reference should be made to the Teachers' Pension Act (Ontario) (the TPA) as amended.

(a) General

The Plan is governed by the TPA. It is a contributory defined benefit pension plan co-sponsored by the Province of Ontario (the Province) and Plan members, represented by the Ontario Teachers' Federation (the OTF) (the co-sponsors). The terms of the Plan are set out in the Partners' Agreement.

The Plan is registered with the Financial Services Commission of Ontario (FSCO) and under the Income Tax Act (Canada) (the ITA) (registration number 0345785) as a Registered Pension Plan which is not subject to income taxes.

The Plan is administered and the investments are managed by the Ontario Teachers' Pension Plan Board (the Board). Under the TPA, the Board is constituted as a corporation without share capital to which the Corporations Act (Ontario) does not apply.

(b) Funding

Plan benefits are funded by contributions and investment earnings. Contributions are made by active members of the Plan and are matched by either the Province or designated private schools and organizations. The determination of the value of the benefits and required contributions is made on the basis of periodic actuarial valuations.

(c) Retirement pensions

A retirement pension is available based on the number of years of credited service, the average of the best five annual salaries and the age of the member at retirement. A member is eligible for a reduced retirement pension from age 50. An unreduced retirement pension is available at age 65 or if the sum of a member's age and qualifying service equals 85.

(d) Disability pensions

A disability pension is available at any age to a disabled member with a minimum of 10 years of qualifying service. The type of disability pension is determined by the extent of the disability.

(e) Death benefits

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

(f) Escalation of benefits

Pension benefits are adjusted in January each year for inflation at 100% of the change in the Consumer Price Index, subject to a limit of 8% in any one year with any excess carried forward. The Plan was amended in 2008 to reduce the level of guaranteed inflation protection for credit earned after December 31, 2009 to 50% of the change in the Consumer Price Index. Starting in January 2011, inflation adjustments by the co-sponsors above that level will depend upon the Plan's funded status.

(g) Retirement Compensation Arrangement

Restrictions in the ITA and its regulations on the payment of certain benefits from the registered pension plan for periods of service after 1991 may impact some Plan members. To address affected members, the Retirement Compensation Arrangement (the RCA) was established by agreement between the co-sponsors as a supplementary plan to provide for these benefits. Examples of these benefits include: (1) members of the Plan who retired with average earnings above $126,220 (CPP-exempt members $116,667) in 2008 and $120,440 (CPP-exempt members $111,111) in 2007; and (2) members whose pensions would require a larger reduction for early retirement to comply with the ITA limitations than the Plan would impose. Because the RCA is a separate trust, the net assets available for benefits and accrued benefits and deficit of the RCA are not included in these consolidated financial statements.

NOTE 1.

Summary of significant accounting policies

(a) Basis of presentation

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles.

The fair value of assets and liabilities and the results of operations of subsidiary companies and variable interest entities (VIEs) where the Plan is the primary beneficiary are consolidated as part of the Plan's financial statements.

A VIE is an entity which does not have sufficient equity at risk to finance its activities without additional subordinated financial support or an entity in which the holders of the equity at risk lack the characteristics of a controlling financial interest. The primary beneficiary, which is the enterprise that absorbs the majority of the expected losses or is entitled to the majority of the expected residual returns, is required to consolidate the VIE in its financial statements.

VIEs in which the Plan is the primary beneficiary or in which it has a significant variable interest are primarily private equity and alternative investments limited partnerships.

The Plan's consolidated financial statements also include its proportionate share of the fair value of assets, liabilities and operations of investments in joint ventures.

Intercompany transactions and balances are eliminated in preparing these consolidated financial statements.

Certain comparative figures have been reclassified to conform with the current year's presentation.

(b) Changes in accounting policies

On January 1, 2008, the Plan adopted three new presentation and disclosure standards that were issued by the Canadian Institute of Chartered Accountants (CICA): Handbook Section 1535, Capital Disclosures, Handbook Section 3862, Financial Instruments – Disclosures, and Handbook Section 3863, Financial Instruments – Presentation.

Capital disclosures

Section 1535 specifies the disclosure of (i) an entity's objectives, policies and procedures and process for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. Note 15 has been added to provide the required disclosures.

Financial instruments – disclosures and presentation

Sections 3862 and 3863 replaced Handbook Section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. These increased disclosures have been included in Note 2.

(c) Investments

Valuation of investments

Investments and investment-related liabilities 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.

Fair values of investments are determined as follows:

a. Short-term money-market securities are valued using either closing mid-market prices or discounted cash flows based on current market yields, when closing mid-market prices are unavailable.

b. Bonds are valued on the basis of quoted closing mid-market prices. If quoted closing mid-market prices are not available, estimated values are calculated using discounted cash flows based on current market yields and comparable securities, as appropriate.

c. Public equities are valued at quoted market closing prices. When the market for a public equity is not active or when there are restrictions on the sale of all or part of a public equity imposed on the Plan by external parties, management estimates the fair value by using appropriate techniques including valuation models.

d. Real estate, private equities, infrastructure and timber are valued based on estimated fair values determined by using appropriate techniques and best estimates by management, appraisers, or both. Where external appraisers are engaged to perform the valuation, management ensures the appraisers are independent and compares the assumptions used by the appraisers with management's expectations based on current market conditions and industry practice to ensure the valuation captures the business and economic conditions specific to the investment.

   At least 70% of the value of the rental property portfolio covering all product types and geographic regions is independently appraised annually. At a minimum, 90% of the real estate portfolio will be valued by independent appraisers at least every three years. The same appraisal firm is not permitted to value the same property more than three years in a row.

e. Derivative financial instruments are recorded at fair value using market prices where available. Where quoted market values are not readily available, appropriate alternative valuation techniques are used to determine fair value.

f. Alternative investments, comprised of hedge funds and managed futures accounts, are recorded at fair value based on net asset values obtained from each of the funds' administrators. These net asset values are reviewed by management.

The Plan uses a number of valuation techniques to determine the fair value of investments for which observable prices in active markets for identical investments are not available. These techniques include: valuation methodologies based on observable prices for similar investments; present value approaches where future cash flows generated by the investment are estimated and then discounted using a risk-adjusted interest rate; and option-pricing models. The principal inputs to these valuation techniques are listed below. Values between and beyond available data points may be obtained by interpolation and extrapolation.

- Bond prices – quoted prices are generally available for government bonds, certain corporate bonds and some other debt-related products.
- Credit spreads – where available, credit spreads are derived from prices of credit default swaps or other credit-based instruments, such as debt securities. For others, credit spreads are obtained from pricing services.
- Interest rates – principally derived from benchmark interest rates such as quoted interest rates from central banks and in swap, bond and futures markets. Benchmark interest rates are considered when determining discount rates used in the present-value approaches.
- Foreign currency exchange rates – there are observable markets, both spot and forward, and in futures in all major currencies.
- Public equity and equity index prices – quoted prices are generally readily available for equity shares listed on the stock exchanges and for indices on such shares.
- Commodity prices – many commodities are actively traded in spot, forward and futures on exchanges.
- Price volatilities and correlations – volatility is a measure of the tendency of a specific price to change over time. Correlation measures the degree to which two or more prices or other variables are observed to have moved together historically. Volatility is an input in valuing options and certain products such as derivatives with more than one underlying variable that is correlation-dependent. Volatility and correlation values are obtained from broker quotations, pricing services or derived from quoted option prices.
- Forecasts on operating cash flows of real estate, private equities, infrastructure and timber – forecasts include assumptions on revenue, revenue growth, expenses, capital expenditure, and capital structure. They are generally provided by management of the companies in which the Plan invests or external managers. Additional assumptions from external parties, for example, external appraisers, may also be used in the forecast.

The Plan refines and modifies its valuation techniques as markets and products develop and the pricing for individual products becomes more transparent.

While the Plan believes its valuation techniques are appropriate and consistent with other market participants, the use of different techniques or assumptions could result in different estimates of fair value at the balance sheet date. Management has assessed and determined that using possible alternative assumptions will not result in significantly different fair values.

Trade-date reporting
Purchases and sales of investments and derivative contracts are recorded as of the trade date (the date upon which the substantial risks and rewards have been transferred).

Investment income
Dividend income is recognized based on the ex-dividend date, and interest income and real estate income are recognized on the accrual basis as earned. Investment income also includes both realized and unrealized gains and losses. Unrealized gains and losses are recognized only when the fair value of the investment is based on a quoted market price in an active market or a valuation using appropriate valuation techniques is performed and approved by management. Since real estate income is determined on a fair value basis, a charge for depreciation and amortization is excluded from the determination of real estate income.

Transaction costs
Transaction costs are incremental costs directly attributable to the acquisition, issue or disposal of a financial asset or financial liability. Transaction costs incurred are expensed and recorded as transaction costs. Any transaction amounts received by the Plan that are directly attributable to the acquisition of an investment are netted against transaction costs paid.

Management fees
Management and performance fees for private equity funds and hedge funds are expensed as incurred.

(d) Foreign currency translation
Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rates prevailing on the year-end date. Income and expenses are translated into Canadian dollars at the exchange rates prevailing on the dates of the transactions. The realized and unrealized gains and losses arising from these translations are included within net realized and unrealized gains on investments in investment income.

(e) Accrued pension benefits
The value of accrued pension benefits and changes therein during the year are based on an actuarial valuation prepared by an independent firm of actuaries. The valuation is made as at the beginning of the year and then extrapolated to year end. It uses the projected benefit method pro-rated on service and management's best estimate, as at the valuation date, of various economic and non-economic assumptions.

(f) Contributions
Contributions from the members, the Province and designated private schools and organizations are recorded on an accrual basis. Cash received from members for credited service and cash transfers from other pension plans are recorded when received.

(g) Benefits
Benefit payments to members and others, commuted value payments and refunds to former members, and transfer payments to other plans are recorded in the period in which they are paid. Any benefit payment accruals not paid are reflected in accrued pension benefits.

(h) Use of estimates
In preparing these consolidated financial statements, management uses estimates and assumptions that primarily affect the reported values of assets and liabilities, and related income and expenses. Significant estimates are used primarily in the determination of accrued pension benefits and the fair value of investments and investment-related receivables and liabilities. Note 5 explains how estimates are used in determining accrued pension benefits and note 1c explains how estimates are used to derive the fair value of investments and investment-related receivables and liabilities.

NOTE 2.

Investments

The Plan invests, directly or through derivatives, in fixed income, equities and inflation-sensitive investments in accordance with the Board's policy of asset diversification.

(a) Investments[1] before allocating the effect of derivative contracts

The schedule below summarizes the Plan's investments and investment-related liabilities, including net accrued interest and dividends of $374 million (2007 – $440 million), before allocating the effect of derivative contracts, as at December 31:

	2008		2007	
($ millions)	*Fair Value*	*Cost*	*Fair Value*	*Cost*
Fixed income				
Debentures	$ 4,340	$ 3,868	$ 5,936	$ 5,316
Bonds	21,202	21,947	34,137	34,619
Money-market securities	4,309	4,353	8,037	8,042
Alternative investments[2]	9,659	9,542	11,450	11,051
	39,510	39,710	59,560	59,028
Equity				
Publicly traded				
Canadian	3,302	3,881	10,020	6,153
Non-Canadian	15,051	19,251	18,136	18,444
Non-publicly traded				
Canadian	2,776	2,836	3,369	2,864
Non-Canadian	9,529	11,731	8,860	9,284
	30,658	37,699	40,385	36,745
Inflation-sensitive investments				
Real estate (note 8)	16,680	12,915	16,852	11,854
Real-rate products				
Canadian	10,325	9,053	7,946	6,103
Non-Canadian	7,625	6,913	3,733	3,820
Infrastructure and timber	16,916	16,853	15,418	14,693
	51,546	45,734	43,949	36,470
	121,714	123,143	143,894	132,243
Investment-related receivables				
Securities purchased under agreements to resell	3,002	3,000	7,896	7,937
Cash collateral deposited under securities borrowing arrangements	155	151	227	240
Derivative-related, net	7,174	3,882	3,813	1,814
	10,331	7,033	11,936	9,991
Investments	$132,045	$130,176	$155,830	$142,234

[1]For additional details, refer to the schedule of Investments over $100 million on page 99.

[2]Comprised of hedge funds and managed futures accounts.

	2008		2007	
($ millions)	Fair Value	Cost	Fair Value	Cost
Investment-related liabilities				
Securities sold under agreements to repurchase	$(20,569)	$(20,539)	$ (23,143)	$(23,205)
Securities sold but not yet purchased				
Fixed income	(1,808)	(1,771)	(6,188)	(6,233)
Equities	(155)	(152)	(226)	(237)
Joint ventures (note 6)	(4,944)	(6,262)	(3,995)	(3,983)
Subsidiaries and VIEs (note 7)	(6,872)	(7,629)	(8,693)	(8,699)
Real estate (note 8)	(3,200)	(3,151)	(3,440)	(3,428)
Cash collateral received under credit support annexes	(142)	(142)	(32)	(32)
Derivative-related, net	(9,254)	(1,855)	(2,112)	(1,172)
	(46,944)	(41,501)	(47,829)	(46,989)
Net investments (note 2c)	$ 85,101	$ 88,675	$108,001	$ 95,245

(b) Derivative contracts

Derivative contracts are financial contracts, the value of which is derived from the value of underlying assets, commodities, indices, interest rates or currency rates. Derivative contracts are transacted either in the over-the-counter (OTC) market or on regulated exchanges.

Notional amounts of derivative contracts represent the contractual amount to which a rate or price is applied for computing the cash to be paid or received. Notional amounts are the basis upon which the returns from, and the fair value of, the contracts are determined. They do not necessarily indicate the amounts of future cash flow involved or the current fair value of the derivative contracts and, therefore, do not indicate the Plan's exposure to credit or market risks. The derivative contracts become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market rates or prices relative to their terms. The aggregate notional amounts and fair values of derivative contracts can fluctuate significantly.

Derivative contracts, transacted either in the OTC market or on regulated exchanges, include:

Swaps

Swaps are OTC contracts in which two counterparties exchange a series of cash flows based on agreed upon rates to a notional amount. The various swap agreements that the Plan enters into are as follows:

Equity and commodity swaps are contracts in which one counterparty agrees to pay or receive from the other cash flows based on changes in the value of an equity or commodity index, a basket of stocks, a single stock or commodities.

Interest rate swaps are agreements where two counterparties exchange a series of payments based on different interest rates applied to a notional amount.

Currency swaps involve the exchange of fixed payments in one currency for the receipt of fixed payments in another currency.

Forwards and futures
Futures are standardized contracts traded on regulated future exchanges, whereas forward contracts are negotiated agreements that are transacted between counterparties in the OTC market. Examples of futures and forwards are described below:

Equity and commodity futures are contractual obligations to buy or sell at a fixed value (the contracted price) of an equity or commodity index, a basket of stocks, a single stock or commodities at a predetermined future date.

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.

Currency forwards and futures are contractual obligations to exchange one currency for another at a specified price or settlement at a predetermined future date.

Options
Options may be acquired in standardized amounts on regulated exchanges or may be customized and acquired in the OTC market. They are contractual agreements under which the seller (writer) grants the purchaser the right, but not the obligation, either to buy (call option) or sell (put option), a security, exchange rate, interest rate, or other financial instrument or commodity at a predetermined price, at or by a specified future date. The seller (writer) of an option can also settle the contract by paying the cash settlement value of the purchaser's right. The seller (writer) receives a premium from the purchaser for this right. The various option agreements that the Plan enters into include equity and commodity options, interest rate options, and foreign currency options.

Credit derivatives
Credit derivatives are OTC contracts that transfer credit risk related to an underlying financial instrument (referenced asset) from one counterparty to another. Examples of credit derivatives include credit default swaps, equity default swaps, total return swaps, and loan participations.

Credit default swaps and equity default swaps provide protection against the decline in value of the referenced asset as a result of specified events such as payment default or insolvency. These swaps are similar in structure to an option whereby the purchaser pays a premium to the seller of the credit default swap or an equity default swap in return for payment related to the deterioration in the value of the referenced asset. The referenced asset for credit default swaps is a debt instrument while the referenced asset for equity default swap is an equity instrument.

Total return swaps are contracts in which one counterparty agrees to pay or receive from the other cash flows based on changes in the value of the referenced asset.

Loan participations are contracts in which one counterparty provides funding to the other party in exchange for participation interests in sharing the risks and profits of the loans originated by the other party.

Other derivative products
The Plan also transacts in other derivative products including statistic swaps and dividend swaps in the OTC market. An investor may trade the statistic swaps with the objective of adding value or hedging for risks associated with the magnitude of movement, i.e. volatility, variance, correlation, covariance of some underlying products, such as exchange rates, or stock indexes. Dividend swaps are an over-the-counter contract where an investor agrees to match all dividends paid out by an underlying stock or index over a specified time period. In return, the dividend payer receives a fixed amount at expiry called the dividend swap rate.

The following schedule summarizes the notional amounts and fair value of the Plan's derivative contracts held as at December 31:

		2008		2007	
($ millions)		*Notional*	*Fair Value*	*Notional*	*Fair Value*
Equity and commodity derivatives					
Swaps		$ 14,320	$(3,640)	$ 18,117	$ (117)
Futures		2,509	18	5,062	60
Options: Listed	– purchased	44	3	86	2
	– written	688	(11)	108	(3)
OTC	– purchased	10,641	425	4,476	469
	– written	1,688	(118)	1,380	(50)
		29,890	(3,323)	29,229	361
Interest rate derivatives					
Swaps		15,945	(253)	67,557	547
Futures		42,037	4	85,111	1
Options: Listed	– purchased	760	4	14,427	9
	– written	968	(3)	3,374	(8)
OTC	– purchased	3,843	106	21,777	294
	– written	809	(83)	21,556	(191)
		64,362	(225)	213,802	652
Currency derivatives					
Swaps		162	1	522	93
Forwards[3]		43,536	6	61,896	10
Futures		4	–	–	–
Options: OTC	– purchased	18,722	847	15,121	229
	– written	18,461	(852)	6,654	(125)
		80,885	2	84,193	207
Credit derivatives					
Loan participations		207	84	368	154
Credit default swaps	– purchased	14,708	1,512	17,489	720
	– written	7,898	(2,257)	4,520	(427)
Total return swaps		829	(264)	810	(19)
Equity default swaps		–	–	9	2
		23,642	(925)	23,196	430
Other derivatives					
Statistic swaps		23,116	295	24,332	17
Dividend swaps		299	(23)	376	3
		23,415	272	24,708	20
		222,194	(4,199)	375,128	1,670
Net cash collateral paid under derivative contracts		–	2,119	–	31
Notional and net fair value of derivative contracts		$222,194	$(2,080)	$375,128	$1,701

[3]Excludes currency forwards related to Real Estate assets as disclosed in note 8.

The net fair value of derivative contracts as at December 31 on the previous page is represented by:

($ millions)	2008	2007
Derivative-related receivables	$ 7,059	$4,048
Cash collateral paid under derivative contracts	2,236	406
Derivative-related liabilities	(11,258)	(2,378)
Cash collateral received under derivative contracts	(117)	(375)
	$(2,080)	$1,701

(c) **Investment asset mix**

The Plan had a policy asset mix of 45% equities, 22% fixed income and 33% inflation-sensitive investments at December 31, 2008 and 2007.

Direct investments, derivative contracts, and investment-related receivables and liabilities are classified by asset-mix category based on the intent of the investment strategies of the underlying portfolios of the Plan. The Plan's net investments as at December 31 are summarized below:

	2008		2007	
	Effective Net Investments at Fair Value ($ millions)	Asset Mix %	Effective Net Investments at Fair Value ($ millions)	Asset Mix %
Equity				
Canadian	$ 6,212	7%	$ 13,732	13%
Non-Canadian	28,719	34	36,314	34
	34,931	41	50,046	47
Fixed income				
Bonds	14,217	17	22,911	21
Alternative investments	7,795	9	9,889	9
Absolute return strategies	7,125	8	2,408	2
Money market	(21,144)	(25)	(13,584)	(12)
Debt on real estate properties (note 8)	(2,676)	(3)	(2,945)	(3)
	5,317	6	18,679	17
Inflation-sensitive				
Real estate, net (note 8)	16,156	19	16,357	15
Real-rate products	17,415	20	11,061	10
Infrastructure and timber	10,029	12	8,840	8
Commodities	1,253	2	3,018	3
	44,853	53	39,276	36
Net investments	$85,101	100%	$108,001	100%

(d) Risk management

Objectives

The Plan's primary long-term risk is that the Plan's assets will fall short of its liabilities (i.e., benefits owed to members). Therefore, the objective of investment risk management is to achieve a diversifying of risks and returns in a fashion that minimizes the likelihood of an overall reduction in total fund value and maximizes the opportunity for gains over the entire portfolio. This is achieved through asset diversification so that the market and credit exposure to any single issuer and to any single component of the capital markets is reduced to an acceptable level.

The Plan also manages its liquidity risk so that there is sufficient liquidity to meet short-term marked-to-market payments resulting from the Plan's derivative exposure and to give the Plan the ability to adjust the asset mix in response to the changes in the market conditions.

Policies

The Plan does not manage market and credit risk separately. To apply risk management to investments in a consistent manner, the Plan has a number of policies and guidelines, for example:

- Statement of Investment Policies and Procedures – The statement addresses the manner in which the fund shall be invested. Investments shall be selected and held in accordance with the criteria and limitations set forth in the statement and in accordance with all relevant legislation. The Board approves the policies in the statement and reviews them at least annually.
- Total Fund Guidelines and Objectives – They are developed to apply to the total fund and aggregate asset classes. They address the risks that are relevant and material at the total fund level. It includes guidelines on asset mix and risk budget allocation. They list the investment constraints, for example, the maximum exposures permitted for a single issuer, the liquidity requirements, and currency management. The Board approves these guidelines and reviews them regularly.
- Portfolio guidelines for each investment department – They are developed to apply to the individual portfolios within each asset class managed by the Investment Division. All portfolio guidelines include the departments' investment strategies, operating procedures, trading limits and approval requirements, risk factors and a description of how the risks will be managed and reporting requirements for each portfolio manager, particularly relating to reporting deviations from the approved portfolio guideline. All portfolio guidelines are reviewed annually and approved by the Executive Vice-President of the Investment Division and the Vice-President or Senior Vice-President responsible for the department.
- Trade Authorization and Execution Operation Guidelines – They include guidelines on trading with authorized counterparties and the procedures for obtaining authorization to trade with a new counterparty.
- Pre-Trade Clearance Policy – It formalizes the procedures to ensure the data needed for trade capture, pricing, risk management, and accounting is accurate, complete, and can be entered into the Plan's systems of record on a timely basis prior to commencement of trading.

Processes

Each investment department is responsible for managing the investment risks associated with the investments they manage. Each department is subject to compliance with the Statement of Investment Policies and Procedures, the Total Fund Guidelines and Objectives, Trade Authorization and Execution Operation Guidelines, Pre-trade Clearance Policy and the applicable portfolio guidelines, and the risk budget allocated to them. In addition, the Fixed Income Department is responsible to maintain the liquidity positions in accordance with the Plan's guidelines on liquidity. The Finance Division independently measures the investment risk exposure and the liquidity position of the Plan and provides the information to the Investment Division and the Investment Committee of the Board.

Each investment department has an investment committee, or an equivalent, which meets regularly to assess the investment risks associated with the portfolios it manages and determines action plans, if required. Individual managers in each investment department receive limited authority to invest from the Board by sub-delegation from senior management. Trading limits and approval requirements are set out in the portfolio guidelines for the department. For investments not traded on exchanges, such as alternative investments and private equity

investments, the investment departments conduct due diligence before acquisition and use it as a tool to monitor the investments after acquisition. The objective is to obtain as much transparency as possible for the departments to assess the risk exposure arising from these private and alternative investments.

The senior representatives from each investment department form the Investment Planning and Risk Committee which focuses on managing investment risks at a total fund level. The Chief Financial Officer attends all meetings of the committee as an observer. This committee brings together the experience, investment and operational business judgment required for assessing and managing market, credit and liquidity risks on a regular basis. It monitors and manages the currency positions, interest rate risk and liquidity risk at the total fund level. The committee meets every other week, or more frequently as required.

In 2008, management formed an Enterprise Risk Management Committee which oversees and manages investment and non-investment risks faced by the Plan. The committee is chaired by the Chief Executive Officer and includes senior representatives from all divisions. The Enterprise Risk Management Committee meets regularly and reports to the Board quarterly and more frequently as necessary.

The shaded section on pages 30 and 31 of the Management's Discussion and Analysis section provides further information on the risk budgeting process. The shaded section is an integral part of the Consolidated Financial Statements.

(e) Credit risk

The Plan is exposed to the risk that a counterparty defaults or becomes insolvent (credit risk). Credit risk is the risk of loss associated with a counterparty's inability to fulfill its payment obligations. A credit risk may arise directly from an obligor, an issuer of securities, or indirectly from a guarantor of a credit obligation.

Credit risk management

The Plan actively manages its credit exposures. When over exposures are detected – either in individual exposures or in groups of exposures – the Plan takes action to mitigate the risks. Such actions may include reducing the exposures and using credit derivatives.

Except for debt issued or guaranteed without significant conditions by the Government of Canada, by the government of a province or territory of Canada (with a minimum DBRS credit rating of "AA"), or by the Government of the United States of America, the Plan's total investment in securities of a single issuer across all asset classes shall not exceed 3% of the market value of the total fund without the approval of the Board. Further, not more than 20% of the market value of all bonds, debentures, real return debt products, mezzanine debt and other debt investments (excluding the market value of the non-marketable Ontario Debentures, debt owed by affiliated third parties in relation to real estate properties, and debt associated with an investment strategy approved by the Board) shall be made up of investments rated below a DBRS credit rating of "BBB" or its equivalent or that are unrated.

The Plan has a credit risk assessment process to determine authorized counterparties for repurchase agreements, reverse repurchase agreements, and derivative contracts. The Plan deals primarily with counterparties that have a credit rating of "A" or higher for derivative contracts. Guidelines are also in place to limit the maximum exposures to any individual counterparty for derivative contracts.

Collateral is an important mitigator of credit risk. The Plan routinely obtains collateral, such as in the case of reverse repurchase agreements and OTC derivative contracts. Note 2h provides further details on securities collateral.

The Plan also enters into master netting agreements with counterparties to restrict its exposure to credit losses. The International Swaps and Derivatives Association (ISDA) Master Agreement is a standardized contract for derivative transactions and is signed by all counterparties with which the Plan enters into derivative contracts. It standardizes how the transactions are conducted across a full range of OTC products. The ISDA Master Agreement also contractually binds both parties to apply close-out netting across all outstanding transactions covered by the agreement when either party defaults or other pre-determined events occur. The Plan also negotiates an ISDA Credit Support Annex (CSA) with its key counterparties. The CSA gives the Plan the power to realize any collateral placed with it in the event of a default.

Maximum exposure to credit risk before collateral held

The following table presents the maximum exposure at December 31 to credit risk of balance sheet and off-balance sheet financial instruments, after netting under the ISDA master netting agreement but before taking account of any collateral held. The analysis includes financial assets subject to credit risk only; other financial assets, mainly equity securities, as well as non-financial assets are excluded. For guarantees and loan commitments, the maximum exposure to credit risk is the maximum amount that the Plan would have to pay if the guarantees were to be called upon and the full amount of the loan commitments.

($ millions)	***2008***
On balance sheet:	
Receivable from the Province of Ontario	$ 2,187
Receivable from brokers	182
Cash	186
Fixed income	
Debentures	4,340
Bonds	21,202
Money-market securities	4,309
Inflation-sensitive investments	
Real-rate products	
Canadian	10,325
Non-Canadian	7,625
Securities purchased under agreements to resell	3,002
Derivative-related receivables	7,174
Total on balance sheet	$60,532
Off balance sheet:	
Guarantees	$ 8,521
Loan commitments	975
Total off balance sheet	9,496
Total maximum exposure at December 31	$70,028

While the Plan's maximum exposure to credit risk is the carrying value of the assets, or, in the case of off-balance sheet items, the amount guaranteed or committed, in most cases the likely exposure is far less due to collateral, credit enhancements (e.g. guarantees in favour of the Plan) and other actions taken to mitigate the Plan's exposure, as described previously.

Credit risk concentrations

As at December 31, 2008, the Plan has a significant concentration of credit risk with the Government of Canada and the Province. This concentration relates primarily to the holding of $21.2 billion of Government of Canada issued securities, $4.3 billion of non-marketable Province of Ontario debentures, $0.7 billion in Province of Ontario bonds, $2.2 billion receivable from the Province (see note 3), and future provincial funding requirements of the Plan.

(f) **Market risk**

Market risk is the risk of loss that results from fluctuations in equity and commodity prices, interest and foreign exchange rates, and credit spreads. The Plan is exposed to market risk from its investing activities. The level of market risk to which the Plan is exposed varies depending on market conditions, expectations of future price and yield movements and the composition of the asset-mix.

Market risk management

The Plan manages market risk primarily through diversifying the investments across industry sectors, investment strategies and on a global basis. A variety of derivative contracts are also utilized to manage the Plan's market risk exposures.

Market and credit risk measurement

The Plan uses a statistical Value-at-Risk (VaR)-type approach, the expected tail loss (ETL) methodology, to measure investment risk comprising of market and credit risk over a one-year horizon at a 99% confidence level. The ETL methodology captures the effect of more extreme loss events than VaR for the same confidence level as it is the average of all the losses in the tail.

In 2008, a new risk report, the Asset Class Risk Report, using the ETL methodology was developed for the Investment Planning and Risk Committee. The new report captures the investment risk exposure by asset class reflecting the risk of potential losses in net assets due to both market and credit risk factors relative to the Plan's pension obligations. Statistically, the Plan would expect to see losses in excess of the risk exposure on the report only 1% of the time over a one year period, subject to certain assumptions and limitations discussed below.

The ETL methodology is a statistical approach that accounts for market volatility and credit risk as well as risk diversification achieved by investing in various products and markets. Risks are measured consistently across all markets and products and can be aggregated to arrive at a single risk number. The one-year 99% ETL number used by the Plan is generated using a historical simulation and bootstrap sampling approach that reflects the expected annual return on the portfolio in the worst 1% of the cases. The Plan currently uses the previous 22 years of market data. When sufficient historical data is not available, proxies and statistical methods are used to complete the data series.

There are limitations to the ETL methodology in use. For example, historical data may not provide the best estimate of future changes. It may fail to capture the correlation in asset returns in extreme adverse market movements which have not occurred in the historical window. The bootstrap sampling approach and long historical window, however, mitigate this limitation to some extent by enabling the generation of a set of scenarios that include extreme adverse events. Another limitation is that the Plan computes the risk relative to pension obligations at the close of the business day. Positions may change substantially during the course of a trading day. These limitations and the nature of the ETL measure mean that the Plan's losses may exceed the risk exposure amounts indicated in any risk reports.

The Plan continuously monitors and enhances the risk calculation methodology, striving for better estimation of risk exposure. The Plan also has a number of initiatives that are underway to enhance the process of collecting the risk system data, particularly for the complex financial instruments that the Plan trades. The new initiatives will focus on the accuracy and completeness of risk system data such as the relevant market information and the data related to the terms and conditions of the financial instruments.

The Plan's risk exposure by asset class as at December 31 is as follows:

($ billions)[1]	*2008*
Equity	
Canadian	$ 3.0
Non-Canadian	15.0
Fixed income	
Bonds	4.5
Debt on real estate properties	1.0
Money market	8.5
Other	5.0
Inflation-sensitive	
Real estate, net	6.0
Real-rate products	4.0
Infrastructure and timber	3.5
Commodities	1.0
Total ETL exposure[2]	$29.0

[1]Rounded to the nearest $0.5 billion.

[2]Total ETL Exposure does not equal the sum of ETL exposure for each asset class because diversification reduces total risk exposure.

Interest rate risk

Interest rate risk refers to the effect on the market value of the Plan's assets and liabilities due to fluctuations in interest rates. The value of the Plan's assets is affected by short-term changes in nominal and real interest rates. Pension liabilities are exposed to fluctuations in long-term interest rates as well as expectations for salary escalation.

The Plan manages the interest rate risk by using interest rate derivatives as detailed in note 2b to the financial statements. After giving effect to the derivative contracts and investment-related receivables and liabilities discussed in note 2b, a 1% increase in nominal interest rates would result in a decline in the value of the Plan's investments in fixed-income securities of 7% (2007 – 7%). Similarly, a 1% increase in real interest rates would result in a decline in the value of the Plan's investments in real-rate products of 14% (2007 – 16%).

As at December 31, 2008, holding the inflation and salary escalation assumptions constant, a 1% decrease in the assumed long-term real rates of return would result in an increase in the pension liabilities of approximately 17% (2007 – 17%).

Foreign currency risk

Foreign currency exposure arises from the Plan's holdings of foreign currency-denominated investments and related derivative contracts.

In 2008, the Plan changed its hedging policy at the total fund level. Prior to 2008, the Plan used a currency overlay program to hedge approximately 50% of its foreign currency policy allocation to certain non-North American equities. The new policy does not require a specific percentage of currency exposure or specific currency to be hedged throughout the year. It provides greater flexibility for the Investment Planning and Risk Committee to determine when and how to hedge the foreign currency exposure. At the portfolio level, the Plan hedges its exposure to certain foreign currencies to reduce the impact of currency fluctuations on the value of the foreign investments. The Plan also takes trading positions in foreign currencies with the objective of adding value.

As at December 31, the Plan had investments exposed to foreign currency. In Canadian dollars this exposure is as follows:

($ millions)	*2008*	*2007*
Currency	*Net Exposure*	*Net Exposure*
United States Dollar	$22,077	$10,279
Euro	4,941	5,203
British Pound Sterling	4,133	3,865
Brazilian Real	2,494	2,740
Australian Dollar	2,471	2,326
Japanese Yen	2,304	895
Chilean Peso	1,120	644
Swiss Franc	850	(292)
Norwegian Krone	(620)	1,039
South Korean Won	422	1,047
Other	1,468	3,153
	$41,660	$30,899

The impact of a change in the exchange rate between Canadian dollars and any of the major currencies would be:

- A higher or lower value of investments denominated in the foreign currency
- A higher or lower investment income, arising from changes in the exchange rates used to translate items in the consolidated financial statements

(g) Liquidity risk

Liquidity risk refers to the risk that the Plan does not have sufficient cash to meet its current payment liabilities and acquire investments in a timely and cost-effective manner. Liquidity risk is inherent in the Plan's operations and can be impacted by a range of situation specific and market-wide events including, but not limited to, credit events and significant movements in the market.

Liquidity risk management

The liquidity position of the Plan is analyzed daily to ensure the Plan maintains at least 1% of its assets in unencumbered Canadian treasury bills. The Plan also manages its liquidity by holding additional unencumbered Government of Canada securities (bonds, treasury bills and real-rate bonds) and U.S. Government securities that are available for repurchase agreements so that the Plan is able to withstand the liquidity effects of an equity market downturn that have 1-in-10 and 1-in-100 chance of occurring over a three-month time horizon. The Plan's liquidity position is periodically tested by simulations of major events such as significant movements in the market.

Liquid assets

The Plan maintains a portfolio of highly marketable assets including Canada and U.S. government bonds that can be sold or funded on a secured basis as protection against any unforeseen interruption to cash flow. The fair value of the Canada and U.S. government bonds is $28,816 million as at December 31, 2008 (2007 – $27,174 million). The Plan also has publicly traded equities of $18,353 million (2007 – $28,156 million) which are listed on major recognized stock exchanges. These securities are readily realizable and convertible to cash.

Contractual maturity

The Plan holds all investments and investment-related liabilities for trading purposes. Liquidity risk on these items is not managed on the basis of contractual maturity since they are not held for settlement according to such maturity and will frequently be settled before contractual maturity at fair value. Therefore all investments and investment-related liabilities (other than the consolidated liabilities from subsidiaries, VIEs and joint ventures) are considered to mature within one year.

The Plan also has consolidated liabilities from subsidiaries, VIEs and joint ventures as it consolidates subsidiaries and VIEs and proportionately consolidates joint ventures in accordance with Canadian generally accepted accounting principles. However, the Plan does not have any contractual obligation related to the consolidated liabilities to deliver cash or other financial assets to another party or to exchange any financial instruments with another party under conditions that are potentially unfavorable to the Plan. The Plan's other liabilities include due to brokers, accounts payable and accrued liabilities that are due within one year. The Plan's investment-related liabilities by maturity as at December 31 are as follows:

($ millions)				***2008***
	Within One Year	*One to Five Years*	*Over Five Years*	*Total*
Securities sold under agreements to repurchase	$(20,569)	$ –	$ –	$(20,569)
Securities sold but not yet purchased				
Fixed income	(1,808)	–	–	(1,808)
Equities	(155)	–	–	(155)
Joint ventures	(753)	(1,609)	(2,582)	(4,944)
Subsidiaries and VIEs	(1,768)	(1,070)	(4,034)	(6,872)
Real estate	(487)	(1,907)	(806)	(3,200)
Cash collateral received under credit support annexes	(142)	–	–	(142)
Derivative-related, net	(9,254)	–	–	(9,254)
Total	$(34,936)	$(4,586)	$(7,422)	$(46,944)

(h) **Securities collateral**

Canadian and U.S. government securities with a fair value of $2,331 million (2007 – $1,124 million) have been deposited or pledged 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 could substitute such securities with other securities that the counterparties accept.

Canadian and U.S. government securities with a fair value of $712 million (2007 – $431 million) have been received from various financial institutions as collateral. The Plan holds the collateral received as long as the Plan 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 repledge the collateral in the absence of default by the owner of the collateral but it has not sold or repledged any collateral as of December 31, 2008.

NOTE 3.

Receivable from the Province of Ontario

The receivable from the Province consists of required matching contributions and interest thereon.

($ millions)	2008	2007
Contributions receivable	$2,120	$1,791
Accrued interest receivable	67	48
	$2,187	$1,839

The receivable as at December 31, 2008 from the Province consists of $1,070 million, which was received in January 2009, and an estimated $1,117 million to be received with interest in 2010. The receivable as at December 31, 2007 from the Province consisted of $808 million, which was received in January 2008, and an initial estimate of $1,031 million to be received in January 2009.

NOTE 4.

Actuarial asset value adjustment

The actuarial value of net assets available for benefits is determined by reference to market rates consistent with assumptions underlying the valuation of accrued pension benefits. The adjustment represents accumulated deferred net loss/(gains), being the unamortized difference between the actual, and management's best estimate of, return on the Plan's equity investments (including real estate, commodities, alternative investments, and infrastructure and timber). Annual returns that are in excess of (gains) or below (losses) management's best estimate of returns are amortized over five years. The change in actuarial asset value adjustment for the year was $23,153 million (2007 – $7,535 million).

Fixed income securities are valued at fair value on a basis consistent with the discount rate used to value the Plan's accrued pension benefits, and therefore do not give rise to the need for an adjustment to net assets.

The following schedule summarizes the composition of the actuarial asset value adjustment as at December 31:

	Unamortized (Gains)/Losses	Unamortized (Gains)/Losses To Be Recognized In				Unamortized (Gains)/Losses
($ millions)	2008	2009	2010	2011	2012	2007
2004	$ –	$ –	$ –	$ –	$ –	$ (727)
2005	(1,186)	(1,186)	–	–	–	(2,372)
2006	(2,536)	(1,268)	(1,268)	–	–	(3,804)
2007	2,456	819	819	818	–	3,274
2008	20,790	5,198	5,198	5,197	5,197	–
	$19,524	$3,563	$4,749	$6,015	$5,197	$(3,629)

NOTE 5.

Accrued pension benefits

(a) Actuarial assumptions

The actuarial assumptions used in determining the value of accrued pension benefits of $118,141 million (2007– $115,459 million) reflect management's best estimate of future economic events and involve both economic and non-economic assumptions. The non-economic assumptions include considerations such as mortality as well as withdrawal and retirement rates. The primary economic assumptions include the discount rate, salary escalation rate and the inflation rate. The discount rate is based on the market rate, as at the valuation date, of long-term Government of Canada real-return bonds, which have characteristics similar to the Plan's liabilities, plus 50 basis points to reflect the credit risk of the Province of Ontario. The inflation rate is the difference between the yield on Government of Canada long-term nominal bonds and Government of Canada real-return bonds. The salary escalation rate incorporates the inflation rate assumption and long-term expectation of growth in real wages.
A summary of the primary economic assumptions, as at December 31, is as follows:

	2008	*2007*
Discount rate	**4.00%**	4.65%
Salary escalation rate	**2.35%**	3.20%
Inflation rate	**1.35%**	2.20%
Real rate	**2.65%**	2.45%

The primary economic assumptions were changed as a result of changes in capital markets during 2008. These changes resulted in a net decrease in the value of accrued pension benefits of $2,319 million (2007– $2,594 million). In 2007, changes in non-economic assumptions increased the value of accrued pension benefits by $3,086 million. There were no changes to the non-economic assumptions in 2008. The changes in economic and non-economic assumptions resulted in a net decrease in the value of accrued pension benefits of $2,319 million (2007 – $492 million increase).

(b) Plan provisions

The Plan was amended in 2008 to introduce conditional inflation protection for credit accrued after 2009 as described in paragraph (f) of the Description of Plan note and to alter the re-employment provisions for pensioners. No material amendments were made to the Plan provisions in 2007.

(c) Experience gains and losses

Experience losses of $386 million (2007 – $18 million gains) arose from differences between the actuarial assumptions and actual results.

NOTE 6.

Investments in joint ventures

The Plan's proportionate share of the fair value of assets and liabilities in joint ventures as at December 31, 2008 (excluding joint ventures related to real estate which are disclosed in note 8) is $7,783 million (2007 – $5,923 million) and $4,944 million (2007 – $3,995 million), respectively.

NOTE 7.

Consolidation of subsidiaries and variable interest entities

Subsidiaries and variable interest entities

The Plan's fair value of assets and liabilities of subsidiaries (excluding the real estate subsidiaries included in note 8) and VIEs at December 31, 2008 is $11,198 million (2007 – $14,675 million) and $6,872 million (2007 – $8,693 million), respectively.

Subsidiaries

In 2008, the Plan invested total cash of US$518 million in mezzanine debt and equity securities to acquire a 98.6% interest in Aquilex Holdings, LLC (Aquilex). Aquilex is a provider of mission-critical and routine maintenance, repair and industrial cleaning services to the oil refining, fossil and nuclear power generation, petrochemical and waste-to-energy industries in the United States and Europe. On the date of acquisition, the consideration paid represented the cumulative fair value of the net assets.

NOTE 8.

Investment in real estate

(a) Investment in real estate

The Plan's investment in real estate, which is comprised of real estate-related investments that are either owned or managed on behalf of the Plan by The Cadillac Fairview Corporation Limited, a wholly-owned subsidiary, as at December 31, is as follows:

		2008		*2007*
($ millions)	***Fair Value***	***Cost***	*Fair Value*	*Cost*
Assets[1]				
Real estate properties[2]	**$15,323**	**$11,265**	$15,110	$10,457
Investments[3]	**1,091**	**1,384**	1,550	1,205
Other assets[2]	**266**	**266**	192	192
Total assets	**16,680**	**12,915**	16,852	11,854
Liabilities				
Debt on real estate properties[2][4]	**2,676**	**2,658**	2,945	2,996
Other liabilities[2]	**524**	**493**	495	432
Total liabilities	**3,200**	**3,151**	3,440	3,428
Net investment in real estate	**$13,480**	**$ 9,764**	$13,412	$ 8,426

[1] As at December 31, 2008, U.S. Dollar and British Pound Sterling assets have been hedged by way of foreign currency forward contracts for a notional amount of $2,276 million (2007 – $2,188 million) with a combined fair value of $(13) million (2007 – $(3) million).

[2] Includes the proportionate share of assets and liabilities in real estate joint ventures of $3,435 million (2007 – $3,132 million) and $1,030 million (2007 – $853 million), respectively.

[3] As at December 31, 2008, investments include a total return equity swap with a notional value of $191 million and a fair value of $2 million.

[4] As at December 31, 2008, there are no contingent liabilities for the obligations of certain co-owners (2007 – $4 million).

(b) Real estate (loss)/income

The Plan's real estate (loss)/income for the year ended December 31, is as follows:

($ millions)	*2008*	*2007*
Revenue		
Rental	$1,631	$1,586
Investment	77	27
	1,708	1,613
Expenses		
Property operating	744	725
General and administrative	11	25
Other[8]	17	13
	772	763
Operating income (note 9)	936	850
Interest expense (note 9)	(158)	(189)
	778	661
Net investment (loss)/gain on real estate assets[5][7]	(1,665)	1,260
Net investment (loss)/gain on debt on real estate properties[6][7]	(68)	145
Net real estate (loss)/income	$ (955)	$2,066

[5]Includes unrealized net loss on real estate assets and other liabilities, of $1,201 million (2007 – gains of $906 million).

[6]Includes unrealized net loss on debt on real estate properties of $69 million (2007 – gains of $146 million).

[7]This amount is included in net realized and unrealized (loss)/gain on investments shown in note 9.

[8]Includes transaction costs of $10 million in 2008 (2007 – $6 million).

NOTE 9.

Investment (loss)/income

(a) Investment (loss)/income before allocating net realized and unrealized (losses)/gains on investments, direct management fees and transaction costs to asset classes

Investment income, before allocating the net realized and unrealized gains on investments and transaction costs to asset classes, for the year ended December 31, is as follows:

($ millions)	*2008*	*2007*
Fixed income interest		
Debentures	$ 476	$ 690
Money-market securities	104	219
Bonds	1,409	1,138
Net repo interest expense	(557)	(457)
Net swap interest expense	(440)	(1,541)
Real estate interest expense (note 8b)	(158)	(189)
	834	(140)
Equity dividend income		
Canadian equity	204	408
Non-Canadian equity	1,042	979
	1,246	1,387
Inflation-sensitive investment income		
Real estate operating income (note 8b)	936	850
Real-rate products		
Canadian	220	216
Non-Canadian	111	90
Infrastructure and timber	385	380
	1,652	1,536
	3,732	2,783
Net realized and unrealized (loss)/gain on investments[1][2][3]	(22,499)	1,971
Direct management fees[4]	(168)	–
Transaction costs	(104)	(76)
Investment (loss)/income	$(19,039)	$4,678

[1] Includes unrealized net losses of $16,330 million (2007 –$8,152 million).

[2] Includes net foreign currency losses of $3,066 million (2007 – gains of $2,193 million).

[3] Includes a net loss of $2,518 million, representing the change in fair values estimated using a valuation technique based on assumptions that are not supported by prices from observable current market transactions in the same instrument (i.e., without modification or repackaging) and not based on available observable market data was recognized in net income for the year.

[4] Includes Private Equity fund management fees and external manager fees. On January 1, 2008, the Plan began deducting all direct management fees from investment income. In previous years, Private Equity fund management fees were included in its original asset class as a reduction to investment income while external manager fees from other asset classes were classified as administrative expenses. Comparative figures have not been restated because the difference is not material.

(b) **Investment (loss)/income**

Investment (loss)/income by asset class, after allocating net realized and unrealized gains and losses on investments, direct management fees, and transaction costs for the year ended December 31, is as follows:

($ millions)	*2008*	*2007*
Fixed income	$ (6,004)	$ 472
Canadian equity	(3,792)	2,272
Non-Canadian equity	(9,589)	(1,206)
Inflation-sensitive investments	346	3,140
	$(19,039)	$4,678

NOTE 10.

Investment returns and related benchmark returns

Investment returns and related benchmark returns by investment asset class for the year ended December 31 are as follows:

	2008		*2007*	
(percent)	*Investment Returns*	*Investment Benchmark Returns*	*Investment Returns*	*Investment Benchmark Returns*
Fixed income[1]	(43.6)%	12.0%	5.4%	9.6%
Canadian equity[2]	(27.5)	(31.2)	14.5	9.8
Non-Canadian equity[2]	(23.0)	(26.4)	(5.4)	(5.6)
Inflation-sensitive investments[2]	0.2	6.8	7.0	2.9
Total Plan	(18.0)%	(9.6)%	4.5%	2.3%

[1] Includes currency policy hedge trading, internal absolute return strategy investments and alternative investments. The currency policy hedge trading was eliminated effective April 1, 2008.

[2] On September 1, 2007, the Plan commenced the inclusion of transaction costs in the calculation of investment returns for the year ended on December 31, 2007. All transaction costs incurred in 2007 prior to September 1, 2007 were included in investment returns except for $11 million. The impact of excluding these transactions costs is not material to the investment returns for the asset class or total Plan.

Investment returns have been calculated in accordance with the acceptable methods set forth by the CFA Institute and the Pension Investment Association of Canada.

The Plan identifies benchmarks to evaluate the investment management performance. The performance of each asset class is measured against benchmarks that simulate the results based on the investment strategies employed by the investment managers identified for the asset class.

The total Plan return is measured against a Canadian dollar-denominated composite benchmark produced by aggregating returns from each of the policy asset class benchmarks, using the Plan's asset-mix policy weights.

Effective March 1, 2008, certain benchmarks have been revised to reflect changes in investment strategy and objectives.

NOTE 11.
Statutory actuarial valuations

Statutory actuarial valuations are prepared periodically to determine the funding requirements of the Plan. Until 2007, active members were required to contribute 7.3% of the portion of their salaries covered by the CPP and 8.9% of salaries above this level. Member contributions are matched by the Province and other employers. In addition, the Funding Management Policy established by the co-sponsors provides procedures for the co-sponsors to determine contributions and benefits.

Under an agreement between the co-sponsors, contribution rates are as follows:

	Members		*Government and Designated Employers*	
	Contribution Rate on Portion of Salaries:		*Contribution Rate on Portion of Salaries:*	
(percent)	*Covered by CPP*	*Not Covered by CPP*	*Covered by CPP*	*Not Covered by CPP*
2007	9.3%	10.9%	9.3%	10.9%
2008	9.6%	11.2%	10.4%	12.0%
2009	10.4%	12.0%	10.4%	12.0%

The actuarial methods used to prepare statutory actuarial valuations are different than those used to prepare a financial statement actuarial valuation and the amounts disclosed in these consolidated financial statements. The statutory actuarial valuations use a valuation method which takes into account future benefits to be earned and future contributions to be made by members of the Plan as at the valuation date.

The most recent statutory actuarial valuation that has been filed with regulatory authorities was prepared as at January 1, 2008 by Mercer (Canada) Limited and disclosed a funding surplus of $16 million.

Using the assumptions prescribed by the Funding Management Policy, the estimate of the funding deficit is approximately $2,519 million as at January 1, 2009, assuming no change to the contribution rates, and that conditional indexing for post-2009 service will be at the 100% level. A funding valuation is not required to be filed with FSCO until 2011.

NOTE 12.
Contributions

($ millions)	***2008***	*2007*
Members		
Current service	**$1,098**	$1,023
Optional credit	**19**	17
	1,117	1,040
Province of Ontario		
Current service	**1,089**	1,008
Interest	**50**	37
Optional credit	**17**	15
	1,156	1,060
Other employers	**21**	19
Transfers from other pension plans	**17**	19
	38	38
	$2,311	$2,138

NOTE 13.

Benefits paid

($ millions)	*2008*	*2007*
Retirement pensions	$3,898	$3,725
Death benefits	228	219
Disability pensions	32	32
Commuted value transfers	22	30
Transfers to other plans	8	6
Refunds	7	8
	$4,195	$4,020

NOTE 14.

Administrative expenses

(a) Investment expenses

($ millions)	*2008*	*2007*
Salaries, incentives and benefits	$ 79.2	$119.4
Investment management fees[1]	–	37.6
Premises and equipment	21.1	17.4
Professional and consulting services	18.4	24.5
Custodial fees	12.2	10.6
Information services	11.6	9.7
Communication and travel	8.4	7.5
Statutory audit fees	0.9	0.8
Board and committee remuneration	0.6	0.5
Other	2.1	1.4
	$154.5	$229.4

[1] On January 1, 2008, the Plan began including all external manager fees in direct management fees as a reduction to investment income. External manager fees are no longer included within administrative expenses. Comparative figures have not been restated because the difference is not material.

(b) Member Services expenses

($ millions)	*2008*	*2007*
Salaries, incentives and benefits	$23.9	$23.4
Premises and equipment	6.9	6.8
Professional and consulting services	2.2	2.5
Communication and travel	1.1	1.2
Statutory audit fees	0.3	0.3
Board and committee remuneration	0.2	0.2
Other	0.9	0.8
	$35.5	$35.2

NOTE 15.
Capital

Under CICA Section 1535, Capital Disclosures, the Plan is required to disclose the Plan's capital and how it is managed. For disclosure purposes under this requirement, the funding surpluses or deficits determined regularly in the funding valuations prepared by an independent actuary are described as the Plan's capital in the consolidated financial statements. The actuary's funding valuation is used to measure the long-term health of the Plan. The actuary tests the Plan's ability to meet its obligations to all current Plan members and their survivors. Using an assumed rate of return, the actuary projects the Plan's benefits to estimate the current value of the liability (see note 5), which is compared to the sum of the Plan assets, the future contributions for all current Plan members and the present value of the contribution increases for future members. The result of the comparison is either a surplus or a deficit.

The objective of managing the Plan's capital is to ensure the Plan is fully funded to pay the plan benefits over the long term. The co-sponsors change the benefit and contribution levels to eliminate any deficits. The Funding Management Policy set by the co-sponsors in the Partners' Agreement provides guidance on how the co-sponsors manage the Plan's capital.

A funding valuation including a plan to eliminate any deficit is required to be filed with the pension regulator at least every three years. A preliminary funding valuation is performed by the actuary when the valuation is not filed with the regulator assisting the co-sponsors in managing the Plan's capital.

The most recent funding valuation filed and preliminary funding status are disclosed in note 11.

NOTE 16.
Retirement Compensation Arrangement (RCA)

Restrictions in the ITA on the payment of certain benefits from a registered plan for periods of service after 1991 may impact some Plan members. To address affected members, the RCA was established by agreement between the co-sponsors as a supplementary plan to provide these benefits.

The RCA is administered under a trust separate from the assets of the Plan. The Board has been appointed by the co-sponsors to act as the trustee of the RCA.

Because the RCA is a separate trust and the Plan does not hold any variable interest in the RCA, the net assets available for benefits and the value of accrued benefits and deficit, referred to below, have not been included in the consolidated financial statements of the Plan.

The RCA is funded on a pay-as-you-go basis from a portion of the contributions made to the Plan by teachers, the Province and designated private schools and organizations. The portion is based on a limit on contributions to the Plan with contributions above the limit being remitted to the RCA. The limit is determined annually by the Plan's independent actuary such that the RCA contributions are expected to be sufficient to pay the benefits over the next 12 months. At the beginning of 2009, the actuary determined that the limit should increase from $11,800 to $14,800. Due to the funding policy adopted by the co-sponsors, the net assets available for benefits will continue to be substantially less than the accrued benefits.

In addition, because it is difficult to predict the benefits expected to be paid over the next 12 months, it is possible that the assets may be insufficient to pay the benefits. In such a case, the payment of benefits will be temporarily suspended and contributions raised in order to fund the payments that are due under the RCA.

A summary of the financial statements for the RCA as at December 31 is as follows:

($ thousands)	*2008*	*2007*
Statement of net assets available for benefits and accrued benefits and deficit		
Net assets available for benefits		
Assets	$ 15,594	$ 11,400
Liabilities	(1,854)	(823)
	$ 13,740	$ 10,577
Accrued benefits and deficit		
Accrued benefits	$ 227,294	$ 245,401
Deficit	(213,554)	(234,824)
	$ 13,740	$ 10,577
Statement of changes in net assets available for benefits		
Contributions	$ 6,788	$ 3,189
Investment income	165	172
	6,953	3,361
Benefits paid	3,712	3,221
Expenses	78	49
	3,790	3,270
Increase in net assets	$ 3,163	$ 91

The actuarial assumptions used in determining the value of accrued benefits are consistent with the assumptions used in the Plan except that the assumed discount rate has been adjusted to reflect the effect of the 50 percent refundable tax under the RCA.

The estimate of the value of accrued benefits is highly sensitive to salary increases, both actual and assumed. Any changes to the salary assumptions will have a significant effect on the liabilities for future benefits. In addition, significant uncertainty exists in projecting the liabilities of the RCA due to changes in the number of future participants as well as changes to the income tax regulations relating to pensions.

NOTE 17.

Commitments

The Plan has committed to enter into investment and other transactions, which may be funded over the next several years in accordance with the terms and conditions agreed to. As at December 31, 2008, these commitments totalled $11,439 million (2007– $15,008 million).

NOTE 18.

Guarantees and indemnifications

Guarantees

In 2004, as part of an investment transaction, the Plan agreed to guarantee a letter of credit facility of a counterparty. In the event that the counterparty defaults on the letter of credit, the Plan would assume 50% of the line of credit facility amount up to US$25 million as at December 31, 2008 (2007 – US$25 million) plus interest and transaction costs. These letters of credit facilities have a term of one year and are renewable annually. As at December 31, 2008, the counterparty has issued US$18 million in letters of credit which are guaranteed by the Plan (2007 – US$19 million).

In 2006, as part of an investment transaction, the Plan agreed to guarantee an equipment lease of a counterparty. In the event the counterparty defaults on the lease, the Plan would assume 25% of the lease amount up to $28 million as at December 31, 2008 (2007 – $15 million). The guarantee expires on December 1, 2013 upon termination of the lease agreement. No payments have been made by the Plan regarding this guarantee.

Certain joint ventures and subsidiaries have provided performance guarantees and/or letters of credit facilities during their normal course of business. The beneficiaries of these guarantees and/or letters of credit facilities have the ability to draw against these facilities to the extent the contractual obligations, as defined in the related agreements, are not met. The term of these guarantees and/or facilities can range from one year to twenty-two years. As at December 31, 2008, the maximum exposure is $573 million (2007 – $784 million).

The Plan also indirectly guarantees the underlying reference obligations when writing credit derivatives. The maximum potential exposure is the notional amount of written credit derivatives as shown in note 2b. In 2008, net payments related to written credit derivatives were made in the amount of $6 million (2007 – nil).

Indemnifications

The Plan provides that Board members, employees and certain others are to be indemnified against the expenses related to certain proceedings against them. In addition, in the normal course of operations, the Plan may, in certain circumstances, agree to indemnify a counterparty. Under these agreements, the Plan, its subsidiaries and joint ventures may be required to compensate counterparties for costs incurred as a result of various contingencies such as legal claims or changes in laws and regulations. The number of such agreements, the variety of indemnifications and their contingent character prevents the Plan from making a reasonable estimate of the maximum amount that would be required to pay all such counterparties.

NOTE 19.

BCE litigation

In 2007, the Board on behalf of the Plan made an equity commitment in respect of a proposed transaction pursuant to which a corporation (the "Purchaser") organized by several investors was proposing to acquire BCE Inc ("BCE"). Pursuant to the definitive agreement that was entered into between BCE and the Purchaser in respect of the proposed transaction, a break-up fee would have been payable by BCE in certain circumstances, and a reverse break-up fee would have been payable by the Purchaser in certain circumstances. Certain of the investors, including the Board, are parties to a limited guarantee of this reverse break-up fee. The transaction was terminated in 2008 because not all of the conditions required under the definitive agreement could be satisfied. In connection with the BCE transaction, the Board has been named as a defendant in the following cases:

BCE break fee litigation

BCE has made a claim in the Superior Court of Quebec for the reverse break-up fee of $1.2 billion under the BCE acquisition agreement. The Board would be responsible for 58.7% of such fee if the claim is successful. This action is at a very early stage. At this time it is not possible to predict the outcome.

BCE proposed class action

A proposed class action lawsuit was commenced in the Province of Saskatchewan in October 2008 regarding the non-payment of second and third quarter common share dividends by BCE. This action is at a very early stage – no certification motion has yet been scheduled. At this time it is not possible to predict the outcome.