TEACHERS'™ PENSION PLAN
ONTARIO

LEADING THE WAY

2011 ANNUAL REPORT

The Ontario Teachers' Pension Plan has earned a reputation for leadership and innovation in pension fund management since it was established in 1990. We now face a recurring funding challenge and, together with our sponsors and members, we have an opportunity to lead the way...

AGAIN

The plan's governance structure has always been based on an independent board, equal funding and risk sharing. Our joint-sponsorship model is seen by many as a crucial factor in the plan's success and is being examined and adopted by other top pension plans around the world.

Teachers' unparalleled record of excellence is widely recognized. A recent independent study determined that our investment performance has been number one among our international peer funds during the past 10 years and our service to members is second to none among our peers.

As defined benefit pension plans everywhere deal with economic and demographic challenges, Teachers' board and management are committed to helping our sponsors remain at the forefront with fair, realistic and sustainable solutions.

About Ontario Teachers' Pension Plan

The Ontario Teachers' Pension Plan, better known as Teachers', is Canada's largest single-profession pension plan. Teachers' is an independent organization set up by its two sponsors, the Ontario government and Ontario Teachers' Federation (OTF).

OTF represents all teachers in the province's publicly funded schools. The Ministry of Education and the Ministry of Finance jointly represent the Ontario government.

WHAT DO THE SPONSORS DO?

The Ontario government and OTF appoint Teachers' board members. Each sponsor gets to appoint four members to the board, and together the sponsors appoint a ninth member to serve as the chair. Teachers' management reports to the board.

The sponsors also establish what benefits the plan will provide and set the level for members' and employers' contributions.

Most importantly, the plan sponsors are responsible for ensuring that the plan is appropriately funded – that it has enough money to fulfill its obligation to members.

WHAT DOES TEACHERS' DO?

The board and management of Teachers' have three primary responsibilities:

1 **Making money to help pay pensions** – Teachers' oversees, develops and executes investments and investment strategies designed to increase the value of the plan's assets.

2 **Paying out benefits** – Teachers' administers the pension plan and pays benefits to members and their survivors.

3 **Reporting on the State of the Plan** – Teachers' reports on the plan's funding status, which it monitors to help ensure that the plan can meet both current and long-term obligations.

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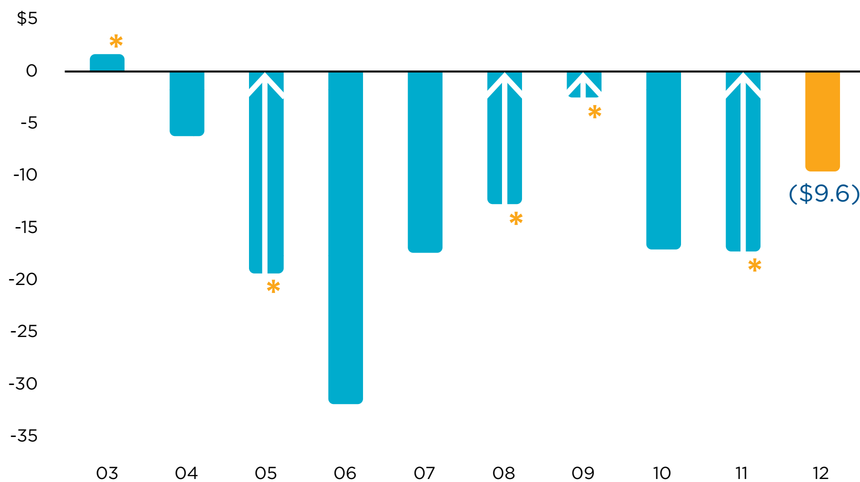
2011 HIGHLIGHTS

State of the Plan

We measure our assets against our liabilities looking out more than 70 years to calculate the annual preliminary funding valuation. Despite changes to contribution rates and benefits and strong asset growth, funding shortfalls have been recurring for the past 10 years.

PRELIMINARY FUNDING VALUATION
(as at January 1) ($ billions)



* Sponsors filed a funding valuation that brought the fund into balance through contribution, benefit and/or economic assumption changes

For the January 1, 2012, funding valuation, the plan's preliminary projected liabilities were $171.7 billion and actuarial assets (including future contributions) were $162.1 billion, leaving a shortfall of $9.6 billion.

The 2012 preliminary funding valuation reflects a gap between the plan's assets (current investments and future contributions) and its liabilities (cost of future pensions). Both sides of the equation are being negatively affected by economic and demographic factors:

ECONOMIC

Uncertain markets mean we must project modest investment returns

Low real interest rates indicate low future economic growth and require the plan to set aside more money for future pensions

DEMOGRAPHIC

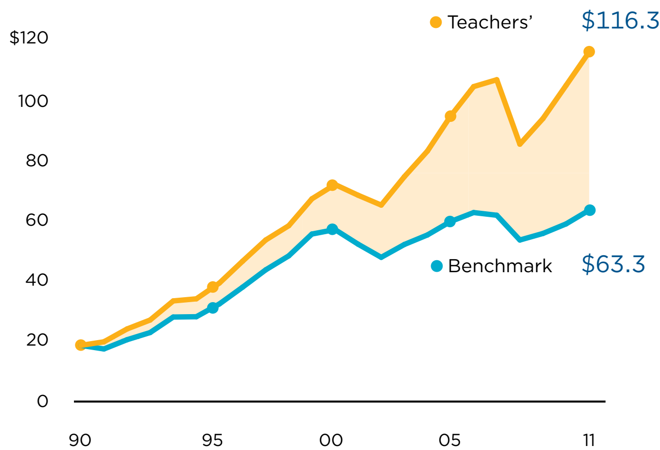
Increased longevity results in many teachers collecting pensions for more years than they worked

Declining ratio of working-to-retired members limits the amount of investment risk that can be taken to earn returns

Investments

Our investment performance exceeded expectations in 2011, with an 11.2% rate of return generating $11.7 billion in investment income and growing net assets available for benefits to $117.1 billion. Investment returns exceeded the 9.8% benchmark and created $1.4 billion in value added. Our ongoing focus on risk management directly supports members' long-term retirement security.

INVESTMENT ASSET GROWTH
(as at December 31) ($ billions)

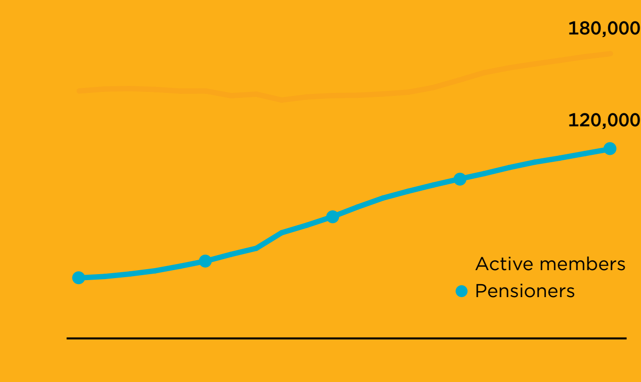


Active management has added $53.0 billion to the plan's asset size since inception.

Member Services

In 2011, we continued to provide outstanding, personalized service to members at a reasonable cost. More than half of surveyed members gave us a perfect 10 out of 10 for service delivery.

ACTIVE MEMBERS AND PENSIONERS
(as at December 31) (thousands)



The number of pensioners has tripled since 1990.

#1

Our investment and service performance have both been recognized as world leaders in a survey by CEM Benchmarking Inc., an independent authority on pension fund benchmarking.

The plan's 10-year total returns are the highest among global peer funds studied by CEM. And we were also number one in value added for the period.

Teachers' ranked first among its North American peers for exceptional pension service – the second time we've placed first in our group.

REPORT FROM THE CHAIR

"Since its inception, our plan has had a record of adapting to change and leading the way in the pension world through innovation."

EILEEN MERCIER, MA, MBA, FICB, F.ICD
CHAIR

The Ontario Teachers' Pension Plan had a very good year in 2011, with total returns of 11.2%. This is a particularly noteworthy feat, given the Eurozone debt problems that emerged last summer and the crisis of confidence and market volatility that ensued.

While this may have caused the S&P 500 Composite Index to languish and the TSX to plummet, Teachers' investment team increased net assets available for benefits to $117.1 billion. The Member Services team also outdid themselves on clients' behalf, achieving yet another 9 out of 10 in member ratings.

Such success does not go unnoticed here at home or internationally. A leading authority on pension fund performance, CEM Benchmarking Inc., noted that our 10-year total fund returns to the end of 2010 are the highest of the pension funds they study around the world.

Even with this success, however, and the sponsors' having raised contribution rates and lowered benefits to balance the plan as of January 1, 2011, the systemic issues of low real interest rates and demographic trends continued to challenge the plan. The result is a preliminary $9.6 billion funding shortfall, as of January 1, 2012.

With mounting risks and market volatility throughout the year, 2011 bore a more than passing resemblance to 2008. In addition to the Eurozone crisis, other significant and complex problems continue to stalk the global economy: a stubbornly sluggish recovery, political gridlock in the U.S., instability in the Middle East and signs of slowing growth in emerging markets. None of these will be solved quickly, and they can be expected to continue to dampen prospects for economic growth, particularly in developed economies.

In this economic environment, low real interest rates are expected to continue impacting the pension plan for at least the next two years. These rates boost the projected future costs of pensions as they are an indicator of slow economic growth in the years to come. As we've seen, even our investment results are not enough to close the gap between projected liabilities and assets. Liabilities continue to grow faster than assets.

This preliminary shortfall is all the more frustrating because it detracts from the results that the fund's management and staff turned in. But it also makes the point that we cannot expect to close the funding gap solely through investment earnings.

Plan changes for pension security

This leaves us with the reality that the cost of future benefits must be recalibrated.

Longer life expectancy is pushing future pension costs higher at a time when low interest rates make it difficult to forecast sufficient returns to cover the cost of future pensions. Longevity has increased to the point where retiring members in this plan are expected to collect a pension for longer than they worked. Typically, teachers work for 26 years and will collect a pension for 30 years – plus a survivor pension may also be paid. Our oldest pensioner at the end of 2011 was 109, and 2,600 pensioners were 90 or older.

In sum, combined economic and demographic factors are hitting both sides of the pension plan's balance sheet at once: we anticipate high pension costs and modest asset growth resulting in continued funding challenges. Defined benefit pension plans everywhere are facing the same dilemma.

Teachers are already scheduled to contribute up to 13% of their salaries to their pensions, an amount matched by the Ontario government and designated employers. There is likely a limit to how much plan members and the government will be willing to pay.

Plan sponsors are now addressing the question: What are the most acceptable and effective changes to make in order to maintain affordability and to more appropriately share the burden for covering shortfalls between working teachers and future retirees? If done proactively and properly, the possibility of ongoing and disruptive change can be reduced.

As populations age, providing pension security to future generations of retirees has become a broad challenge in developed economies. Defined benefit plans such as Teachers' have been particularly challenged. Many organizations have closed their defined benefit plans and shifted the risk of retirement security entirely to their employees. We believe that this is a regressive trend and fear it will lead to many seniors struggling to make ends meet in their later years.

Defined benefit plans must demonstrate that they can adapt to the new economic and retirement realities. Some employer and union groups have adopted a hybrid plan, preserving the defined benefit principle but introducing risk sharing between sponsors and members. Even the Canada Pension Plan has introduced changes encouraging people to work longer and has increased the penalty to receive a pension at 60 instead of waiting until 65, while introducing incentives to defer collecting until 70.

The February release of the Drummond Report, commissioned by the Ontario government to study how to reform and thus reduce public service costs, has several recommendations about public sector pensions. For Teachers', it recommends that funding shortfalls should be addressed with benefit changes instead of contribution increases.

Fortunately, our plan's governance structure, in which the funding risk is shared equally between the employer and employee, provides a forum for discussing funding issues and planning how to address them. The plan sponsors have taken appropriate action in the past to preserve the integrity of this plan, and this will have to continue.

It is not the board's role to determine how that should be done; plan changes are decided by the two plan sponsors, who are jointly responsible for keeping the plan fully funded. Under the Pension Benefits Act, the value of pension benefits accrued to retirees and working teachers cannot be reduced. The sponsors must therefore look ahead to ensure all generations are fairly sharing the plan's risk.

We meet regularly with the plan sponsors to update them on the plan's current funding status and outlook, and to discuss funding concerns. The plan sponsors recognize the challenges the plan faces and are studying potential remedies. Our Demographic Task Force, which includes actuaries from the plan and both sponsors, is working to better understand future retirement trends. We are conducting surveys with plan members on their awareness of the plan's funding challenges and their preferences for potential plan changes. This ongoing preparation means the plan sponsors will be well positioned to make informed decisions when the next filing occurs.

Adjustments keep the plan healthy for future retirees

The notion of change need not be unsettling for plan members. Our shared goal with the plan sponsors continues to be retirement security for all generations of plan members. Small adjustments to the plan today will have a big impact many years out and will keep it healthy for future retirees.

Our plan members have seen benefit improvements during past periods of surplus, as well as contribution increases and other plan changes to address funding shortfalls. Members should feel reassured that the plan sponsors, with the advice and counsel of the board, are working on your behalf to consider suitable options to ensure your pensions will be there for you at a reasonable cost. In uncertain times such as these, retirement security is more important than ever.

Board and management priorities

Plan funding matters, including the valuation assumptions, absorbed a significant amount of board members' time last year; however, a significant part of our role is to ensure that management fulfills its investment and service delivery mandate effectively. The board sets administrative, investment and compensation policies and oversees implementation of these policies and plan administration by management. We must also ensure that the plan operates in compliance with the laws and regulations that govern it.

Teachers' has a talented and experienced management team. Our investment track record and member satisfaction ratings are consistently strong. Board members support management's efforts to continue being an industry leader. To do this, we must attract and retain the best people and give them the tools they need to work effectively. Operational excellence, strong risk management and cost-consciousness are key to supporting the organization's investment and service delivery strategies and its ultimate goal – pension security for all generations of plan members.

We believe that the closure of defined benefit plans is a regressive trend and fear it will lead to many seniors struggling to make ends meet in their later years.

Board members, too, must be equipped to make good decisions and provide astute judgment. We invite experts to speak to the board members on economic and investment-related topics to increase our understanding of key areas of importance. During the year, we enhanced our board processes: how we operate and the type of information we receive. We should see the benefits of these changes in 2012, including more time for debate and enabling even better oversight and decision-making.

With the 2011 retirements of Helen Kearns and Louis Martel, we welcomed two new members to the board in early 2012. Patricia Anderson joins our board with a background in finance and extensive board experience. She brings us in-depth knowledge of board governance best practice, gained as a member of several boards and as past Chair of SickKids Foundation and the Corporation of Roy Thomson Hall and Massey Hall. Barbara Palk has more than three decades of banking and investment experience, and was most recently the President of TD Asset Management Inc. On behalf of all board members, I express our thanks and appreciation to Helen and Louis for sharing their valuable expertise and for their committed service to the board.

Leading the way

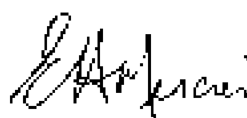
The plan's funding challenges can be overcome. Teachers' can be a model for those who are committed to providing defined benefit plans that are fair, realistic and sustainable. I am encouraged that both sponsors and members understand the need to match the benefits of this plan to its assets over the coming years.

As you see the stories in the media about the funding difficulties faced by public sector pension plans in the United States and elsewhere, it is important to keep in mind that thanks to a process of reform and modernization that was begun in the 1980s and continued under the leadership of all three of Ontario's major political parties, the situation in Ontario is dramatically different.

Since its inception, our plan has had a record of adapting to change and leading the way in the pension world through innovation, beginning with our joint-sponsorship model. With that foundation, we have shown we can adapt to changing economic and political conditions. And importantly, the board, the sponsors and management know how to work together to make difficult decisions.

While we at Teachers' face our own significant funding challenges – challenges we will come back to repeatedly in this report – it is important to keep these challenges in perspective. Frankly, there are pension plans around the world that would love to have our problems.

In challenging times, truly enlightened leaders take bold steps, and they do so calmly and deliberately because they are prepared. That has been our history to date, and I look forward to seeing it continue as we once again lead the way – this time to a sustainable funding solution.



EILEEN MERCIER
CHAIR

REPORT FROM THE CEO

"We have earned an average of 10% since 1990 and have maintained quality service scores in the 9 out of 10 range for many years."

JIM LEECH, MBA, ICD.D
PRESIDENT AND CHIEF EXECUTIVE OFFICER

We had an impressive year in 2011. We produced strong returns, well above industry averages, in a tough investment climate. We implemented a record number of plan changes and served more members. And we have a number of complex, multi-year system and operational improvement projects underway to support the goal of pension security for all plan members.

Solid returns amid market chaos

The fund earned a strong 11.2% return, increasing the plan's net assets to $117.1 billion. Investment income totalled $11.7 billion for the year. Taking a longer view, we have earned an average return of 8.0% over the last 10 years and 10.0% since 1990.

The 2011 investment gains were achieved amid difficult market conditions. We were one of the few pension plans globally to deliver this level of performance, which is notable given our risk tolerance. Growing sovereign debt risks and mounting economic uncertainty shook investor confidence and markets across the world in the last half of the year.

We can attribute part of our performance to being better prepared for market volatility in 2011 than we were in 2008, when that earlier financial crisis stressed our investments and risk systems. Changes we have made since 2008 are paying off today. We restructured our portfolio to better diversify risk across the total fund. More collaboration and stronger risk systems help us make the best risk-and-return decisions for the total fund, rather than for individual asset classes in isolation. Signing on to the United Nations-backed Principles for Responsible Investment in 2011 will, over time, make our investment managers better at assessing the implications of social and environmental risks. Maximizing our returns on the risk we can afford to take remains our priority.

I am also pleased to report that our rate of return exceeded the fund's 9.8% composite benchmark, generating $1.4 billion in value-added returns. Balancing asset growth with strong risk management is both responsible and necessary, and our ability to consistently earn extra returns supports our goal of pension security.

Pension services are second to none

In addition to investing, we deliver pension services directly to 300,000 working teachers and pensioners. We believe our members deserve timely, reliable service and pension information that is relevant to them at different stages of their careers. We try to improve every year and track member satisfaction through regular surveys conducted by a third party. This feedback forms our Quality Service Index (QSI), which measured 9 out of 10 last year. In addition, an independent survey by CEM Benchmarking Inc. determined that our service was the best among peer funds in its latest report.

We have maintained high QSI scores for several years, even though plan complexity from new regulations and compliance – and hence our workload – has increased. Ten years ago, there were 237,000 plan members; today there are 300,000. We completed 395,000 client interactions in 2011, a 4% increase over the prior year. Providing accurate and timely service in a complex pension plan is an accomplishment in itself, but we also continue to focus on offering exceptional service at a reasonable cost.

Funding shortfall

The plan's preliminary funding valuation showed a $9.6 billion shortfall between liabilities (the cost of future pensions for all members) and projected assets at January 1, 2012. As our members will recall, OTF and the Ontario government resolved a 2011 shortfall but, with liability growth continuing to outpace asset growth, the plan is once again in a deficit position.

As a result of decisions to resolve the 2011 shortfall, working teachers and the government are paying more to the plan this year (and contributions are scheduled to go up again in 2013 and 2014, by 0.35% each year). Retirees with pension credit subject to conditional inflation protection received less than 100% inflation protection for the first time – the dollar amount is small now but will grow as more of the post-2010 credited service is subject to conditional indexing and while this measure remains in effect.

There are three causes of the current funding shortfall. The first is a sharp decline in the real interest rate used as a basis to project future pension costs. When real interest rates drop, the plan needs more money invested today to earn enough to fully cover future pensions. Second, we absorbed another $5.2 billion of the 2008 investment loss. The third cause is demographics.

As our Chair explains in her message, demographic issues – primarily increasing longevity – are causing pension costs to escalate and are exerting pressure on the plan's sustainability. Despite our investment portfolio earning strong returns, we still have a systemic funding problem. Accordingly, the plan sponsors will have to change benefits and/or contributions to bring the plan into long-term balance.

Priorities aligned to pension security goal

In addition to pursuing asset growth and excellent service, we made progress last year on the following priorities:

- Enhanced risk management systems;
- Operational excellence; and
- Cost-effective operations.

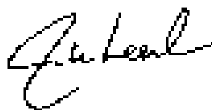
The pension business is as much about managing risk as managing assets. We have continually strengthened our risk systems, but there is more to do. In this complex world of international financial markets, increased investment in operational risk management is a necessity, not a choice. Working together in a coordinated, effective way also helps us understand and respond to the risks faced by the plan. Our enterprise Project Management Office – created in 2010 to oversee cross-departmental, multi-year projects – is ensuring that large cross-functional projects are properly planned, resourced and managed. We are making costs more transparent across the organization. Visibility on expenses creates a higher level of cost-consciousness and supports our drive to remain cost effective.

Committed and focused team

The biggest factor in our success is the expertise and commitment of our employees. I am proud of the way our employees remain focused on our service delivery and investment strategies despite the volatile economic environment in which we operate. Employees are encouraged to take an active role in managing their performance and development. We regularly review the organization's talent pool to ensure that we have the right mix and depth of talent to meet our current and future needs.

Our recent employee survey showed that Teachers' continues to be an attractive place to work. We had a 90% participation rate – a strong indication of employee engagement. Furthermore, the two things employees ranked the highest were the regard in which they hold their colleagues and their pride in working at Teachers'.

Finally, we appreciate the strong support of the board members and the plan sponsors. We remain committed to doing the best job for plan members in 2012 and beyond.



JIM LEECH
PRESIDENT AND CHIEF EXECUTIVE OFFICER

MANAGEMENT'S DISCUSSION & ANALYSIS

Management's Discussion & Analysis (MD&A) presents readers with a view of the pension plan through the eyes of management by interpreting the material trends and uncertainties affecting the results and financial condition of the plan.

In addition to historical information, the MD&A contains forward-looking statements regarding management's objectives, outlook and expectations. These statements involve risks and uncertainties and, as such, the plan's actual results will likely differ from those anticipated. Key elements of the plan's financial statements should be read in conjunction with the MD&A.

Mission

Outstanding service and retirement security for our members – today and tomorrow.

Vision and Values

As we strive to achieve our mission, our vision is to be the world's leading pension plan organization.

We are committed to being:

- the best at what we do;
- respected as industry thought leaders; and
- the partner of choice.

We are guided by our core values:

- recognizing that our people drive our success;
- promoting personal development, collaboration and innovation;
- communicating openly and honestly;
- demanding the highest level of integrity;
- championing accountability and risk consciousness; and
- embracing talent, respecting diversity and recognizing accomplishments.

PLAN OVERVIEW

The Ontario Teachers' Pension Plan (Teachers') administers the pension benefits of Ontario's 180,000 elementary and secondary school teachers and 120,000 pensioners. A pension plan was created for Ontario's educators in 1917. It was administered by the Teachers' Superannuation Commission of Ontario until 1990. At that time, the Ontario government established the Ontario Teachers' Pension Plan Board as an independent organization. The pension plan was primarily invested in non-marketable Province of Ontario debentures before 1990. The new organization was given authority to diversify the plan's holdings and administer the plan. Today, we have more than 800 employees in Toronto, Ontario, and London, England.

Teachers' is governed by the Teachers' Pension Act and must comply with the Pension Benefits Act and the federal Income Tax Act. The Teachers' Pension Act provides for the joint stewardship of the pension plan by the Ontario government, through the Minister of Education and the Executive of Ontario Teachers' Federation (OTF). OTF and the Ontario government are the plan sponsors. They must ensure the plan remains appropriately funded and jointly decide:

- the benefits the plan will provide;
- the contribution rate paid by working teachers, which is matched by the government and designated employers; and
- how any funding shortfall is addressed and any surplus is used.

A nine-member board, appointed by OTF and the government, oversees the administration of the pension plan and reports the plan's funding status to the plan sponsors. Board members are required to act independently of both the plan sponsors and management, and to make decisions in the best interests of all beneficiaries of the plan.

MANAGEMENT'S ROLE

The employees of the pension plan have three responsibilities:

- invest the plan's assets to help pay pensions;
- administer the pension plan and pay benefits to members and their survivors; and
- report and advise on the plan's funding status and regulatory requirements.

Fulfilling our responsibilities requires highly skilled and experienced investment professionals and pension experts who understand myriad risks and how to manage them. We must set the right long-term strategies that take pension demographics and economics into account.

STRATEGY AND PRIORITIES

We consider a number of factors as we set our long-term strategies for investments and member services. Our strategies and organizational priorities are based on the needs of plan members and the plan sponsors.

Our investment strategies are designed to earn strong returns that support stable contribution rates and pension sustainability and help meet the plan's long-term funding needs. Our approach is to manage funding and investment risk together. Taking plan demographics and future pension obligations into account, we aim to earn the best return possible at an appropriate level of risk. The need for investment returns must be balanced with strong risk management practices.

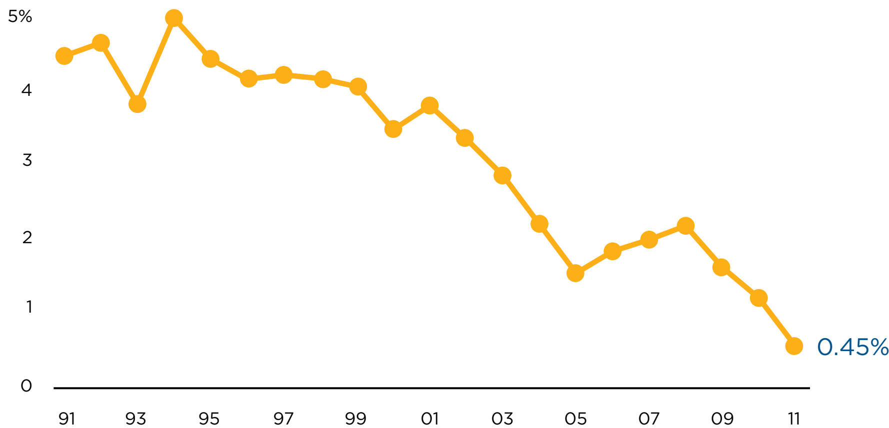
Our member services strategy is built to deliver outstanding, personalized service at a reasonable cost. Members have come to expect excellent service from us and consistently rate our services at the top of the scale.

We also have to consider the growing number of plan members and associated work volume, the quality of employment data received from 175 school boards and designated employers, our reliance on more highly trained IT staff to develop and manage electronic services, our Internet security needs, and the frequent regulatory changes that affect our systems, work processes and staff training needs. Our commitment to cost-effective service excellence keeps us focused on the best ways to manage these various factors.

Strategy is supported by seven priorities

1. Retirement security
2. Outstanding service to members
3. Risk management
4. Informed plan sponsors
5. Cost effectiveness
6. Operational excellence
7. Engaged employees

State of the Plan



A 1% change in the interest rate assumption has an impact of about $25 billion on the funding valuation. Falling rates are causing plan liabilities to grow faster than assets.

"The pension plan must have sufficient assets to cover future pension benefits stretching ahead more than 70 years."

BARBARA ZVAN, M.Math, FSA, FCIA
SENIOR VICE-PRESIDENT, ASSET MIX AND RISK AND CHIEF INVESTMENT RISK OFFICER

DAVID McGRAW, FCA, MBA, ICD.D
SENIOR VICE-PRESIDENT AND CHIEF FINANCIAL OFFICER

PROTECTING RETIREMENT SECURITY

Pension plan sustainability

The goal of the plan is to deliver defined pension benefits to retired members for life. Achieving this goal requires ongoing effort, collaboration and consensus between OTF and the Ontario government, who are responsible for all funding decisions and for determining the plan's contribution rates and benefits.

Pensions are financed with investment income generated by the pension fund, plus contributions from working teachers, the provincial government and designated employers.

The biggest funding risk facing the plan is low real interest rates, which are forecast to remain low for a long period. Low real interest rates are a proxy for continuing low economic growth. Lower economic growth reduces the expected investment returns. This makes funding future benefits more challenging.

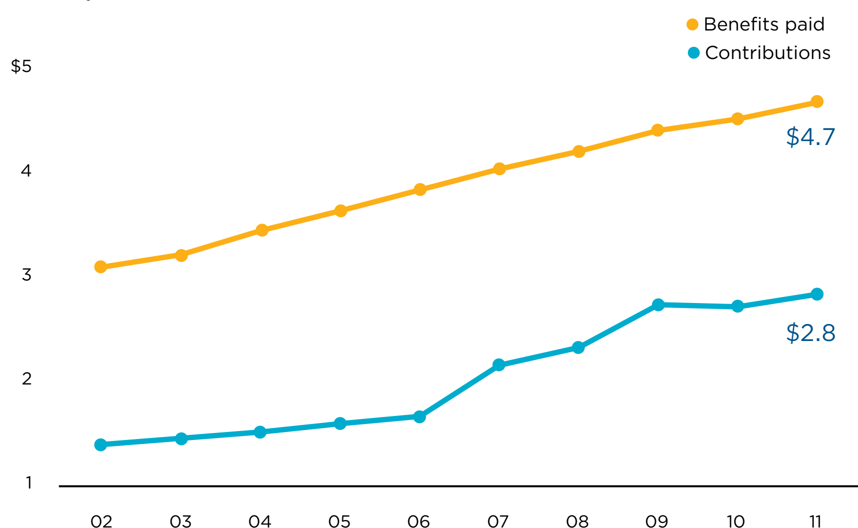
Keeping pension benefits fully funded

Funding valuations are conducted each year to assess the plan's long-term financial health. The valuation shows whether the plan has a surplus, shortfall or sufficient assets to cover future pensions for all current members.

Funding valuations showing that the plan has sufficient assets to cover the projected cost of future pensions must be filed with Ontario's pension regulator at least every three years. If a funding shortfall is projected, OTF and the Ontario government must address it before submitting a funding valuation to the regulator. (A history of plan funding decisions is found on page 124.)

OTF and the government jointly decide when, within the three-year time frame, to file the plan's funding valuations. The last funding valuation was filed in 2011 (see page 18) and the next is due in 2014, although the plan sponsors can elect to file sooner.

CONTRIBUTIONS VS. BENEFITS PAID
(for the year ended December 31) ($ billions)

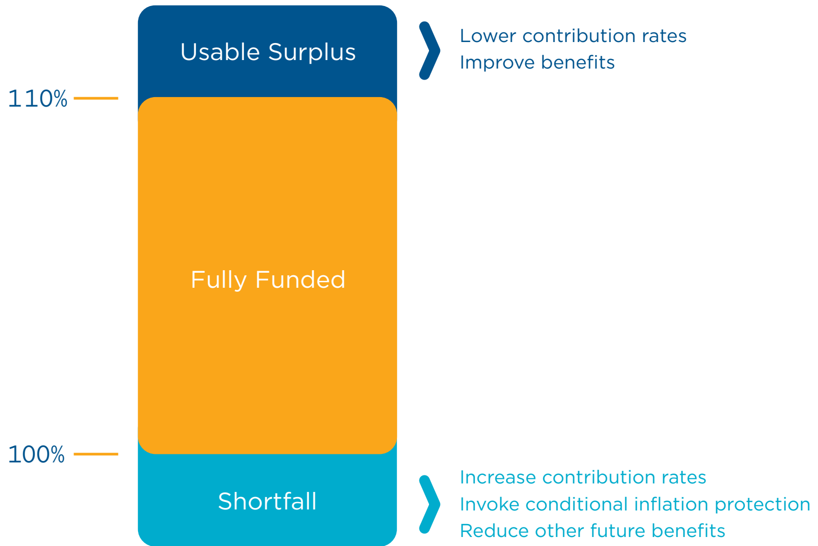


Benefit payments exceeded contributions from members, the government and designated employers by $1.9 billion in 2011. This gap reduces the assets available to invest for future pensions.

Funding policy guides decision-making

The plan sponsors adopted a Funding Management Policy in 2003 to guide decisions on when to use surplus funds and how to address funding shortfalls. If plan assets are equal to, or up to 10% greater than, the cost of future benefits, plan changes are not required. The 10% threshold is intended to create a buffer in good times to cushion the plan when economic conditions are less favourable. When assets exceed future benefits by more than 10%, the surplus can be used to lower contribution rates, improve benefits, or a combination of the two. When the cost of future benefits is greater than plan assets, the plan has a funding shortfall. To address a shortfall and rebalance the plan, the sponsors can:

1. increase contribution rates;
2. invoke conditional inflation protection;
3. reduce other future benefits; or
4. use a combination of these measures.



The current maximum contribution rate in the Funding Management Policy is 15% of members' base earnings above the Canada Pension Plan (CPP) limit, which is $50,100 in 2012. Member contributions are matched by the government and designated employers.

Conditional inflation protection

Conditional inflation protection (CIP) provides the plan sponsors with the flexibility to adjust cost-of-living increases when a shortfall arises. The goal is to pay 100% inflation protection annually if the plan can afford it. If a funding shortfall is projected, the plan sponsors can set cost-of-living increases at 50% to 100% of the annual inflation rate for the portion of members' pension credit earned after 2009.

This measure helps to distribute the risk of funding shortfalls between working teachers (contributors) and retirees. The provision does not apply to pension credit earned before 2010 and does not affect pensioners who retired before then. Any reduction in the indexation percentage (below 100%) would remain in effect until a subsequent funding valuation filing shows that there are sufficient funds to support a higher level of inflation protection.

The Ontario government and designated employers make extra payments to the pension plan equal to the total annual inflation increases that retirees forgo. These matching payments help reduce the funding deficit and are similar to the government and designated employers matching regular and special contributions from working teachers.

Real rate of return assumption

The Funding Management Policy guides the board on the real rate of return assumption (also known as the discount rate) used to prepare the preliminary funding valuation presented in the annual report each year; however, the final decision rests with the board.

The assumption is based on the real interest rate (the nominal rate less inflation) plus a premium of either 0.5% or 1.4%, depending on the plan's financial health. In order to reduce the impact of volatile real interest rates on the plan's funding status, in 2010 the board began smoothing the real rate of return over three years. The 0.5% premium is used when the plan is in a strong financial position. This helps to build up an asset cushion in good times. The 1.4% premium is used when the plan has a shortfall. This helps the plan absorb short-term changes in market returns.

The assumption reflects the expected after-inflation growth in the plan's assets. The board may adjust the real rate of return assumption if the plan's risk profile changes as a result of plan changes made by the plan sponsors (e.g., expansion of conditional inflation protection provisions or other benefit changes that de-risk the plan).

The real rate of return assumption must be realistic so as not to mask funding deficiencies. If the assumption is too high and investments earn less than expected in the future, a funding shortfall would result, forcing younger and future plan members to make even higher contributions, receive lower future benefits or both. If the assumption is too low, current members would pay more than necessary for their pensions.

What does "invoking conditional inflation protection" mean?

Pensions for Ontario's teachers include inflation adjustments – annual increases to keep pace with the cost of living. The inflation adjustment teachers receive for the portion of pension credit they earned after 2009 depends on the plan's financial condition.

Example: OTF and the Ontario government invoked conditional inflation protection at 60% because of the 2011 projected funding shortfall. The base inflation adjustment for 2012 was 2.8%. The indexation level to be paid in 2012 on the portion of members' pensions earned after 2009 will be 1.68% (2.8% x 60%).

The government and designated employers match the amount forgone by pensioners as a result of invoking conditional inflation protection.

FUNDING VALUATION FILED IN 2011

OTF and the Ontario government jointly decided to file a funding valuation in 2011, one year sooner than required. To complete the filing, the plan sponsors resolved a $17.2 billion preliminary funding shortfall that was projected as at January 1, 2011. This early filing proved to be astute because interest rates have continued to decline since then.

The Hearing Officer validated that the real rate of return assumption was reasonable given the plan's risk profile.

Hearing Officer review

OTF and the Ontario government initiated a Hearing Officer review in 2011 to determine if the discount rate used by the plan's board could have been too low, thus potentially overstating the pension plan's 2011 preliminary funding shortfall. The real rate of return assumption has historically been the subject of debate with the plan sponsors.

The sponsors and the board jointly appointed the former consulting actuary to OTF as the independent Hearing Officer to conduct the review.

The review concluded in May that the 3.15% discount rate used by the board for the plan's 2011 preliminary valuation was within a reasonable range. It also outlined the conditions to increase the discount rate, including de-risking the plan through future benefit changes.

How the 2011 funding shortfall was resolved

The plan sponsors made the three changes outlined below to resolve a $17.2 billion preliminary shortfall projected at January 1, 2011.

Conditional inflation protection set at 60% of the annual inflation rate starting January 1, 2012; applies to pension credit earned after 2009

1.1% special contribution rate increase phased in over three years matched by government and designated employers
(as a percentage of annual salary)

Year	Up to CPP limit[1]	Above CPP limit[1]	Increase
2011	10.4%	12.0%	–
2012	10.8%	12.4%	0.4%
2013	11.15%	12.75%	0.35%
2014	11.5%	13.1%	0.35%
Total	–	–	1.1%

[1] The CPP limit is the maximum earnings on which CPP contributions and benefits are based. The limit, which changes annually, is $50,100 in 2012.

Base contribution rate increased for funding valuations; future contributions assumed at a rate of 10.4% of earnings up to the CPP limit, plus 12% of earnings above it

The increased base contribution rate adopted by the sponsors partially reduced the plan's funding risk and allowed the board to increase the real rate of return assumption, consistent with the Hearing Officer's finding, to 3.25% (from 3.15% in the preliminary valuation) for the final valuation. The combination of these changes allowed the sponsors to file a balanced funding valuation.

The following tables compare the 2011 preliminary and filed funding valuations and the assumptions used for each.

FUNDING VALUATION
(as at January 1) ($ billions)

	2011 Filed	2011 Preliminary
Net assets	107.5	107.5
Smoothing adjustment	3.3	3.3
Future basic contributions	33.8	28.0
Future special contributions	3.8	5.3
Actuarial assets	148.4	144.1
Cost of future pensions	(158.4)	(161.3)
Conditional indexing adjustment	10.2	n/a
Surplus/(deficit)	0.2	(17.2)

FUNDING VALUATION ASSUMPTIONS
(percent)

	2011 Filed	2011 Preliminary
Rate of return	5.40	5.30
Inflation rate	2.15	2.15
Real rate of return	3.25	3.15

What is a funding valuation?

- An independent actuary's assessment of the plan's long-term (70+ years) financial health
- Using a number of assumptions, it projects whether the pension plan has sufficient assets to cover the cost of future pension benefits for all current members
- The plan sponsors use funding valuations to set contribution and benefit levels

Despite measures taken by the plan sponsors to eliminate the 2011 shortfall, this year's preliminary funding valuation shows the plan has another $9.6 billion shortfall as at January 1, 2012. This development was anticipated, and the factors contributing to the plan's persistent funding challenges and shortfalls are described in the following section.

FUNDING RISKS AND CHALLENGES

The main risk to the plan is funding risk – a shortfall of assets to pay future benefits to all current members. Due to several demographic and economic factors, the plan has experienced successive funding shortfalls because plan liabilities (the projected cost of future pensions) are growing faster than plan assets.

1. Historically low real interest rates

Long-term real interest rates (after inflation) are used to estimate the cost of providing pensions because they are a predictor of economic growth. When interest rates drop, the plan needs to set more money aside to earn the amount required to pay future pensions.

The yield on Government of Canada 30-year Real-Return Bonds (RRB) is the basis for the real rate of return assumption. This rate declined to 0.45% during 2011 from 1.1% at the start of the year. In order to reduce the impact of volatile real interest rates, we smooth the real rate of return using the trailing 36-month average of the real interest rate. Smoothing this assumption softens the effect when interest rates are falling, but will create a lag as rates increase.

It costs 14% more to secure a typical $40,000 pension when the real interest rate is 2% than when it is 3%.

ASSETS REQUIRED FOR A TYPICAL $40,000 PENSION

Real Interest Rate	Amount Required
1.0%	$970,000
1.5%	$900,000
2.0%	$835,000
3.0%	$730,000
4.0%	$645,000
5.0%	$575,000

2. 2008 investment loss

The plan will continue to absorb its 2008 investment loss until the end of 2012 due to the effect of smoothing losses on the funding valuation. In 2011, we recognized $0.6 billion in net losses in the smoothing adjustment, which included $5.2 billion of the 2008 loss (a similar amount will be recognized in 2012). These losses are now being offset by gains in 2009, 2010 and 2011, which are also smoothed over five years (2009) or three years (2010 and 2011).

3. Demographic factors

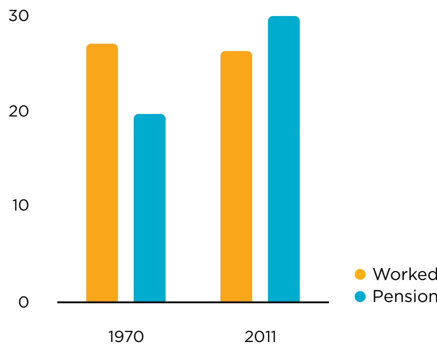
Increasing longevity and plan maturity affect the pension plan in several important ways, primarily through higher pension costs and less flexibility to manage assets.

Life expectancy is high for members of this plan (at the average retirement age of 59, life expectancy is age 90 for females and 87 for males) compared to the general population and continues to increase. It is impossible to accurately predict how long people will live. Despite using the most up-to-date longevity data available for the teacher population, plan members continue to outlive our actuarial assumptions.

The combined effect of early retirement rules and increased longevity now means that a teacher typically receives a pension for a greater number of years than he or she worked. This trend is caused by a combination of life expectancy and the age at which plan members are eligible to retire with an unreduced pension (when their age plus pension credit equals 85).

Teachers are living longer than they did in the past. It costs more to provide pensions for longer retirement periods.

YEARS ON PENSION COMPARED TO YEARS WORKED



The plan grows more mature each year. This means that the proportion of working members is declining relative to the growing number of retired members. As the plan matures, investment managers must carefully weigh the amount of risk that is taken to generate returns. Exposure to riskier asset classes, like equities, must be limited in favour of less risky asset classes, such as bonds, which typically have lower returns.

The shrinking ratio of active members to retirees means that overcoming funding shortfalls with contribution rate increases alone is more difficult when markets fall or the plan's investments underperform. For example, compensating for a 10% decline in plan assets would currently require a contribution rate increase of about 4% of salary, matched by a similar amount from the government and designated employers to close the gap. In 1970, the same 10% decline would have required a contribution rate increase of only 0.6% of salary.

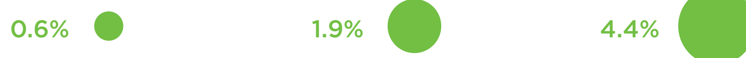
This long-term trend is expected to continue and must be managed accordingly. With risk spread across relatively fewer contributing members, risk management remains an issue. Taking less risk protects working teachers from undue losses, but reduces the fund's earning potential over the long term.

Currently, there are 1.5 working teachers for each retiree in the plan. We expect a further decline to 1.3:1 by 2020. When there is a low ratio of working-to-retired teachers, the adverse impact on each contributing member to cover potential shortfalls or investment losses is greater.

SIGNS OF PLAN MATURITY

Ratio of working-to-retired members

Increase in contribution rate for a 10% decline in assets



4. Modest investment returns expected

Plan maturity puts the investment program under increasing pressure to earn sufficient returns to cover longer, more costly pensions; however, we must use a lower-risk asset mix than less mature pension plans. Furthermore, the current economic outlook is not conducive to earning strong returns. As a result, we must project only modest investment returns going forward. It would not be realistic to assume that investments alone can earn enough to ensure the plan's long-term sustainability at current benefit and contribution levels.

PLAN FUNDING STATUS

Methods and assumptions used for the funding valuation

Achieving balance between plan assets and the cost of future benefits is an ongoing objective for OTF and the Ontario government. To assess the financial health of the plan, the board commissions a preliminary funding valuation each January, conducted by an independent actuary, and reports the outcome to the plan sponsors. Plan management also offers the plan sponsors advice and analytical support on plan funding issues throughout the year.

The funding valuation determines the financial health of the plan looking ahead more than 70 years at current scheduled contribution rates by calculating benefits earned to date, plus projected future benefit costs and contributions. These factors are used by OTF and the Ontario government to set contribution and benefit levels.

A separate valuation – the financial statement valuation – conducted for accounting purposes, is discussed on page 25.

The valuation uses a number of assumptions to project the value of future pension plan liabilities. Assumptions are made about the future inflation rate, salary increases, age at retirement, life expectancy and other factors. The valuation also includes an assumption for the real rate of return on the plan's assets, which includes a risk provision. This preliminary assumption is guided by the Funding Management Policy established by the sponsors. The final assumption is approved by the plan's board members.

The actuary must also project the cost of conditional inflation protection for pension credit earned after 2009. The plan expects to provide 100% inflation protection if there is sufficient funding to allow it. When conditional inflation protection is invoked (set at less than 100% because of a shortfall), the actuary assumes the lower indexation level will remain in effect for the remaining lifetime of all current plan members and pensioners.

Smoothing

Investments and investment-related liabilities are stated at fair market value. Changes in the fair value of net assets are smoothed to even out the impact of short-term fluctuations in investment returns on the plan's funding position. Smoothing is an accepted practice for funding valuations conducted by pension plans. It mitigates the need to frequently change contribution rates and benefit levels to keep the plan in balance. Annual returns of the fund that are above or below the assumed rate of return are smoothed over three years.

The asset smoothing methodology for the funding valuation changed in 2010. Previously, fixed income returns were excluded from smoothing, but gains and losses for all other asset classes, compared to the Consumer Price Index (CPI) plus 6%, were amortized over five years. As a transition measure, the gains and losses experienced before 2010 will continue to be amortized over five years.

The interest rate and inflation assumptions used to value the plan's liabilities are based on the trailing 36-month nominal and real yields and are aligned with the smoothing period for the assets. Smoothing was introduced for these interest rate assumptions in 2010 in response to concerns raised by the plan sponsors about using the spot interest rate as at December 31 each year.

Funding shortfall projected

The plan's funding valuation showed a preliminary shortfall of $9.6 billion at January 1, 2012. The projected cost of future benefits was estimated at $171.7 billion, while assets (including smoothing and future contributions) were estimated at $162.1 billion. The preliminary valuation determined the plan had 94.4% of the assets required to meet future pension liabilities at the start of 2012.

FUNDING VALUATION COMPARISON
(as at January 1) ($ billions)

	2012[1]	2011 Filed
Net assets	117.1	107.5
Smoothing adjustment	(3.0)	3.3
Value of assets	114.1	110.8
Future basic contributions	37.6	33.8
Future special contributions	3.6	3.8
Future matching of CIP benefit reduction	6.8	5.1
Total assets	162.1	153.5
Cost of future pensions	(178.5)	(158.4)
Reduction in cost due to CIP	6.8	5.1
(Deficit)/surplus	(9.6)	0.2

[1] Preliminary valuation, based on Funding Management Policy assumptions – not filed with pension regulator.

The current preliminary shortfall was expected and emerged despite the decision made last June to increase contributions and invoke 60% conditional inflation protection to resolve the 2011 funding shortfall. Net assets increased in 2011, but plan liabilities increased more, primarily due to the effect of falling real interest rates. The demographic and economic factors explained above, as well as the continuing impact of absorbing the 2008 investment loss, also contributed to the shortfall.

Fewer teachers than expected retired in 2011, which had a slightly positive impact on the value of the plan's liabilities. This difference was, however, offset by increasing longevity, which continues to exceed our most up-to-date and advanced mortality assumption figures.

The accompanying table shows assumptions used in the preliminary valuation. Consistent with the sponsors' Funding Management Policy, the board applied a real rate of return assumption for the preliminary funding valuation of 2.85% (with smoothing).

FUNDING VALUATION ASSUMPTIONS
(percent)

	2012[1]	2011 Filed
Rate of return	5.05	5.40
Inflation	2.20	2.15

[1] Preliminary valuation, based on Funding Management Policy assumptions – not filed with pension regulator.

Valuation assumptions change over time. While actual experience tracks most assumptions closely, annual fund returns typically fluctuate significantly compared to the assumptions.

FUNDING OUTLOOK AND PRIORITIES

We expect the cost of future pensions to continue growing faster than plan assets, resulting in recurring funding shortfalls. The next deadline to file a funding valuation with the pension regulator is 2014. Any shortfall existing at the time of the next filing must be resolved before it can be submitted.

The current $9.6 billion preliminary shortfall is too large to be resolved using the full extent of both measures included in the current Funding Management Policy: the ability to increase the contribution rate to 15% for earnings above the year's maximum pensionable earnings and to further invoke conditional inflation protection at the minimum of 50% for pension credit earned after 2009. Given the funding risks and challenges discussed in this report, the board believes other solutions will be necessary to ensure that the fund remains viable and affordable in the future.

We continue working with our sponsors to seek the best solutions to long-term funding challenges.

The board members and management meet with the plan sponsors regularly to update them on the funding status and discuss concerns. The plan sponsors recognize the challenges the plan faces and, together, we are undertaking important activities before the next filing is required, including: i) studying retirement trends to understand how they impact the plan's funding status; and ii) conducting surveys in 2012 to gauge working members' awareness of the plan's funding challenges and, separately, a survey of retired members to help the sponsors understand factors that influence decisions on when to retire. In 2013, working members will be surveyed about their preferences for potential plan changes. Additionally, a Demographic Task Force with sponsor and plan representatives is working with the University of Waterloo to update mortality tables, carefully review other non-economic assumptions and propose potential plan changes to address demographic challenges.

FINANCIAL STATEMENT VALUATION

Methods and assumptions used for the financial statement valuation

The financial statement valuation is prepared by an independent actuary for accounting purposes. It is based on the best estimates provided by management and approved by board members. It takes into account pension credit accrued to date by all plan members and contributions already received by the plan. Unlike the funding valuation, it does not assume future contributions or project the cost of benefits that members will earn in the future. This method is in compliance with the guidance from the Canadian Institute of Chartered Accountants (CICA). Use of estimates and valuation techniques are described further in Notes 1d and 1f and Note 4 to the financial statements.

Plan management reviewed the development and selection of critical accounting estimates with the Audit & Actuarial Committee of the board. Actuarial assumptions used in determining accrued pension benefits reflect best estimates of future economic and non-economic factors proposed by management and approved by the board. The primary economic assumptions are the discount rate, salary escalation rate and inflation rate. The non-economic assumptions include plan member mortality, withdrawal and retirement rates. The plan's actual experience typically differs from these estimates, and the differences are recognized as gains and losses in future years.

The best-estimate discount rate for the financial statement valuation is based on the market rate of long-term Government of Canada bonds, which have characteristics similar to the plan's liabilities, plus a spread to reflect the credit risk of the Province of Ontario. Commencing December 31, 2011, the spread was changed from 0.5% to 0.9%, the prevailing spread between the Government of Canada and the Province of Ontario long-term nominal bonds.

For this valuation, accrued pension benefits are assumed to include the minimum inflation protection benefits, which are 60% for post-2009 credited service until the next required filing in 2014 and 50% for the period thereafter. The indexation percentage for credited service earned before 2010 remains at 100%.

Financial statement valuation as at December 31, 2011

The plan ended 2011 with a financial statement deficit of $45.5 billion. This compares to a financial statement deficit of $39.4 billion for 2010. The deficit represents the difference between the cost of accrued pensions and net assets of $117.1 billion. The discount rate used was 3.40% (4.05% in 2010). The financial position of the plan is summarized in the three accompanying tables.

As **Table 1** shows, net assets available for benefits totalled $117.1 billion, up from $107.5 billion in 2010. The financial statement valuation no longer includes a smoothing adjustment for net assets in accordance with CICA Section 4600, adopted in 2011 (see Note 1b to the financial statements). Accrued pension benefits on a financial statement basis were $162.6 billion ($146.9 billion in 2010).

The $45.5 billion deficit represents the difference between the cost of pensions earned to date and net assets.

TABLE 1: YEAR-END FINANCIAL POSITION

(as at December 31) ($ billions)	2011	2010
Net assets		
Net investments	**$ 116.3**	$ 104.7
Contributions receivable from Province of Ontario	**2.7**	2.6
Other net assets/(liabilities)	**(1.9)**	0.2
Net assets	**117.1**	107.5
Financial status		
Net assets	**117.1**	107.5
Accrued pension benefits	**(162.6)**	(146.9)
Deficit	**$ (45.5)**	$ (39.4)

Table 2 notes that 2011 investment returns totalled $11.7 billion, compared to $13.3 billion in 2010. Contributions received from teachers, the government and designated employers totalled $2.8 billion, while $4.7 billion was paid out in pension benefits. This compares to contributions of $2.7 billion and benefit payments of $4.5 billion in 2010.

The contribution rate for teachers in 2011 was 10.4% of earnings up to the CPP limit of $48,300, plus 12.0% of earnings above that.

TABLE 2: CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

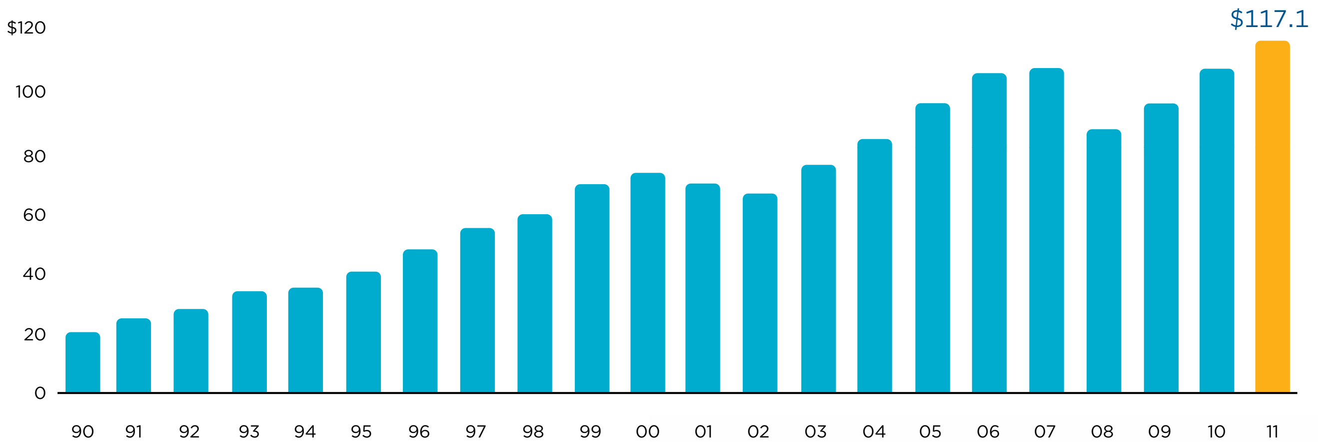
(for the year ended December 31) ($ billions)	2011	2010
Income		
Investment income	**$ 11.7**	$ 13.3
Contributions	**2.8**	2.7
	14.5	16.0
Expenditures		
Benefits	**4.7**	4.5
Administrative expenses	**0.3**	0.3
	5.0	4.8
Increase in net assets	**$ 9.5**	$ 11.2

Benefits paid, shown in **Table 3**, include the addition of 4,300 retirement and disability pensions and 760 survivor pensions during 2011, as well as a 1.4% cost-of-living increase, effective January 1, 2011.

TABLE 3: ACCRUED PENSION BENEFITS

(for the year ended December 31) ($ billions)	**2011**	2010
Accrued pension benefits, beginning of year	**$ 146.9**	$ 131.9
Interest on accrued pension benefits	**6.0**	6.1
Benefits earned	**4.4**	3.3
Benefits paid	**(4.7)**	(4.5)
	152.6	136.8
Changes in actuarial assumptions	**9.8**	10.4
Experience losses/(gains)	**0.2**	(0.3)
Accrued pension benefits, end of year	**$ 162.6**	$ 146.9

Investments



Net assets reached a record high at the end of 2011, a year in which investment gains were achieved amid difficult market conditions.

"We manage investment risk and a by-product is a solid return over the long run. This is the foundation of our performance."

NEIL PETROFF, MBA
EXECUTIVE VICE-PRESIDENT, INVESTMENTS AND CHIEF INVESTMENT OFFICER

OBJECTIVE AND STRATEGIES

The objective of Teachers' investment program is to help the plan meet its long-term funding needs, which in turn contributes to pension security, contribution rate stability and long-term sustainability.

We seek to achieve this objective by: i) maximizing returns at an appropriate level of risk, taking into account the pension liabilities and challenges presented by the plan's mature membership profile; and ii) minimizing the difference between asset values and pension obligations, which is the best way to achieve contribution rate and benefit stability.

To meet our objective, we use strategies for risk, asset mix, liquidity and active management.

Active risk management underpins Teachers' investment strategies.

Supplementary investment information is available on pages 118 to 121 and at otpp.com.

Determining appropriate risk

We allocate considerable resources to understanding and mitigating risks, and to ensuring the investment risks we take are appropriate and properly diversified. In simple terms, we manage investment risk and a by-product is a solid return over the long run.

Our risk management activities are focused on the ultimate risk facing the plan: that the plan's assets will fall short of its liabilities.

We recognize that funding risk can come from assets and liabilities. Both types of risk have a significant impact on the plan's funding status, both can be measured and, to varying degrees, both can be controlled and managed strategically.

The largest liability risk is a decrease in real or after-inflation interest rate projections. While falling real interest rates have a positive effect on certain assets, they have a negative and more significant impact on the estimated current value of future liabilities.

Asset risk, on the other hand, includes the risk that the value of our investments declines. We use risk budgeting to spread risk across the fund's asset classes and to generate superior returns on a risk-adjusted basis. In other words, we expect the fund to be paid for the risks taken. Our investment managers are limited in terms of how much active risk they can take to generate returns and must be as concerned about the potential for loss from an investment as they are about how much might be earned.

We maintain a comprehensive asset-liability model to understand long-term dynamics for investment planning purposes. We measure risk against the plan's liabilities and benchmarks, and we monitor and report the observed risk values against those budgeted on a daily basis through the plan's risk systems.

Proactive risk management

Proactively managing risks requires substantial attention by our board members and the investment department. The Investment Committee of the board, which comprises all board members and is scheduled to meet six times a year (and will meet more often as required), reviews and approves the risk budget annually, monitors overall investment risk exposure and reviews and approves risk management policies that affect the total portfolio, as well as new investment programs that introduce incremental risk.

Management's Investment Risk Committee, comprising investment, economics, finance and legal professionals, and our Investment Committee, comprising senior investment executives only, provide the dedicated focus we need to understand plan funding risks and to manage investments within appropriate risk tolerances. We believe that this segregated approach also allows for i) better portfolio construction and the facilitation of improved investment risk management across the fund in order to effectively diversify risk across asset classes; ii) the ongoing management of fund-wide liquidity; and iii) improved ongoing assessment of asset-mix decisions to enhance our long-term investment success.

A number of management committees monitor and manage fund-wide risk exposure including liquidity, emerging-market exposures, counterparty credit exposures and regulatory matters.

Risk management tools and culture

Daily risk management is aided by sophisticated tools and processes that we have developed and advanced over the past 16 years. In recent years, we updated our data and processing systems to improve reporting accuracy and developed a more holistic approach to data governance. The data in our risk system is updated continuously and includes recent extreme market experiences.

Integrated systems allow us to better manage data, more fully report total-fund risk, strengthen risk modelling and provide investment managers with useful reports to aid them in their decision-making. We have enhanced our ability to capture the terms and conditions relating to the complex financial products in which we invest and have made this and other information readily accessible to analysts and portfolio managers through electronic "dashboards."

Through our risk system, which provides consolidated, coordinated views of the entire fund and its components and collaboration across portfolios, we are able to measure potential loss in several ways:

- within each portfolio and series of portfolios;
- across departments;
- across asset classes; and
- at the total-fund level.

Our organization has a risk-conscious culture. We champion risk awareness and accountability across our investment teams. Understanding that broad diversification is our most important risk management tool, we focus on risk diversification across the total fund, taking care not to duplicate risks inadvertently across portfolios. We also put considerable effort into choosing an appropriate asset-mix policy.

A discussion of risk management policies and procedures relating to credit, market and liquidity risks, as required under IFRS 7, Financial Instruments – Disclosures, is included in Note 2 of the financial statements.

Selecting an appropriate asset mix

Asset-mix selection is the primary driver of the plan's long-term investment performance. Our asset-mix policy calls for a diversified portfolio, including equities, fixed income, commodities and real assets (real estate, infrastructure and timberland).

The board approves the asset-mix policy at least annually, making modifications when required. The board gives management limited discretion to increase or decrease the weighting to take advantage of investment opportunities as they arise.

Absolute return strategies and money market

The board gives management the discretion to use absolute return strategies to generate positive returns that are constructed to be uncorrelated to our other asset classes.

Our internally managed absolute return strategies generally look to capitalize on market inefficiencies. External hedge fund assets are used to earn uncorrelated returns or access unique strategies that augment returns. By using several hedge fund managers, we diversify risk across multiple managers, strategies and styles.

Assets employed in absolute return strategies totalled $12.3 billion at year end compared to $11.4 billion at December 31, 2010, reflecting strong performance throughout the year.

Money-market activity provides funding for investments in all asset classes, and is comparable to a treasury department in a corporation. Derivative contracts and bond repurchase agreements have played a large part in our investment program since the early 1990s. For efficiency reasons, we often use derivatives to gain passive exposure to global equity and commodity indices in lieu of buying the actual securities. We use bond repurchase agreements to fund investments in all asset classes because it is cost effective and allows us to retain our economic exposure to government bonds.

ACTUAL PORTFOLIO
(as at December 31, 2011)

- 44% **Equities** $51.7 billion
- 48% **Fixed income** $55.8 billion
- 5% **Commodities** $5.7 billion
- 22% **Real assets** $25.8 billion
- 11% **Absolute return strategies** $12.3 billion
- -30% **Money market** ($35.0 billion)

NET INVESTMENTS BY ASSET CLASS
(as at December 31) ($ billions)

	2011	2010
Canadian equities	**$10.6**	$9.3
Non-Canadian equities	**41.1**	38.2
Bonds	**26.5**	22.7
Real-rate products	**29.3**	23.2
Commodities	**5.7**	5.2
Real estate	**15.0**	16.9
Infrastructure	**8.7**	7.1
Timberland	**2.1**	2.2
Absolute return strategies	**12.3**	11.4
Money market	**(35.0)**	(31.5)
Total	**$116.3**	$104.7

Net investments are defined as investments of $156.6 billion minus investment-related liabilities of $40.3 billion, as noted in the statements of financial position (page 82).

Ensuring an adequate level of liquidity

Liquidity risk is inherent in the plan's operation and refers generally to the risk that the plan does not have sufficient cash to meet its current payment liabilities or to opportunistically acquire investments in a cost-effective manner. Having sufficient liquidity on hand is important to allow the plan to: i) adjust the asset mix in response to market movements; ii) avoid selling high-quality long-term assets to meet short-term funding needs at inopportune times; iii) meet short-term, mark-to-market payments embedded in the plan's derivative exposure; and iv) facilitate the allocation of risk to illiquid assets such as real estate, infrastructure, timberland and private equity.

The fund's liquidity position is governed by the plan's investment policy and is analyzed and reported regularly to the board's Investment Committee. Our policy is to hold at least 1% of the plan's assets in unencumbered Canadian treasury bills (increased to 1.25% as of January 1, 2012). To meet the plan's short-term liquidity needs, at year end we held $2.8 billion in treasury bills or 2.5% of assets and $27.3 billion in unencumbered government bonds, compared to $2.1 billion and $18.5 billion respectively at year-end 2010. The increase in liquidity supports our larger asset base and addresses uncertainty in global credit and equity markets. Furthermore, the fund's liquidity position is periodically tested through simulations of major catastrophic events such as significant movements in capital markets.

Looking forward, we expect the deleveraging process underway in a number of developed countries will lead to public asset privatizations and our liquidity strategy will allow us to invest opportunistically.

Actively managing assets to add value

Active management is a hallmark of the plan's investment success. It involves selecting investments that we believe are undervalued and employing both fundamental and quantitative strategies to optimize risk-adjusted returns. The objective is to exceed the returns available from passively investing in indices at asset-mix policy weights. We refer to such performance as value added and the relevant indices as benchmarks.

Several strategies are used to maximize returns within our risk limits and outperform the markets in which we invest, starting with our total-fund management approach. This approach encourages information sharing and movement of capital among managers of the different asset classes and portfolios in order to optimize risk-adjusted returns. Value-added decisions are also coordinated at the total-fund level, and portfolio managers are rewarded for maximizing value-added returns within the risk limit on total assets, not just on their own portfolios.

The largest active risk budgets are currently in public equities, private equity and real estate. These assets have earned significant returns above their benchmarks over time.

Long-term priorities

The investment department's long-term priorities directly contribute to the plan's objectives.

- Earn value-added returns above the policy asset-mix benchmark with reasonable risk to help ensure retirement security for members.
- Foster good communication with sponsors, board members and employees to promote an understanding of, and commitment to, the investment program.
- Continue building a collaborative planning process and improving coordination among investment departments in order to realize synergies and optimize the total-fund portfolio.
- Develop enhanced risk management tools and processes to support continued innovation and a risk-conscious culture.
- Mitigate operational risks related to managing complex cross-departmental projects and improve cost effectiveness.

MANAGING INVESTMENTS

The diligent application of our core strategies has resulted in strong long-term performance for the fund and the development of Teachers' global reputation as an innovative investor. We continue to advance our efforts on the following key activities that directly support our ability to innovate and perform.

Responsible investing

Under the Ontario Pension Benefits Act, we are required to exercise diligence when investing members' money and to do so in their best financial interest. We have a fiduciary duty to take the utmost care in our investment decisions, to consider all investment opportunities that are appropriate for a mature plan such as ours and to evaluate investments on a number of levels, including risk.

While we do not select or exclude investments solely on the basis of non-financial criteria, we have long recognized that environmental, social and governance (ESG) risks and opportunities can have a material impact on the investment value of the companies in which we invest.

Consequently, we take these factors into account within our approach to investing on behalf of our members. Responsible investing is an evolving concept, with no single generally accepted definition. To advance a common understanding of it, we are actively engaged with other global institutional investors and support enhanced disclosure of risks associated with ESG activities. Enhanced disclosure helps us to understand the risks that could impact the value of the fund's investments, and enables us to make the best possible investment decisions.

In general, we believe that profitable companies that are well managed, operate with respect for the environment and support human and labour rights are good candidates for long-term investment.

In practice, we aim to improve our tools for ESG evaluations. For example, climate change risk and investment opportunity are assessed across asset classes for materiality. If it is deemed that a material investment risk exists, we seek to quantify that risk and to understand management's plan for meeting any strategic challenges posed by it.

Consistent with our responsible investing approach, we subscribe to social investment monitoring services that cover Canadian, U.S. and international companies to ensure that we are aware of emerging issues and how corporations are responding.

Corporate governance

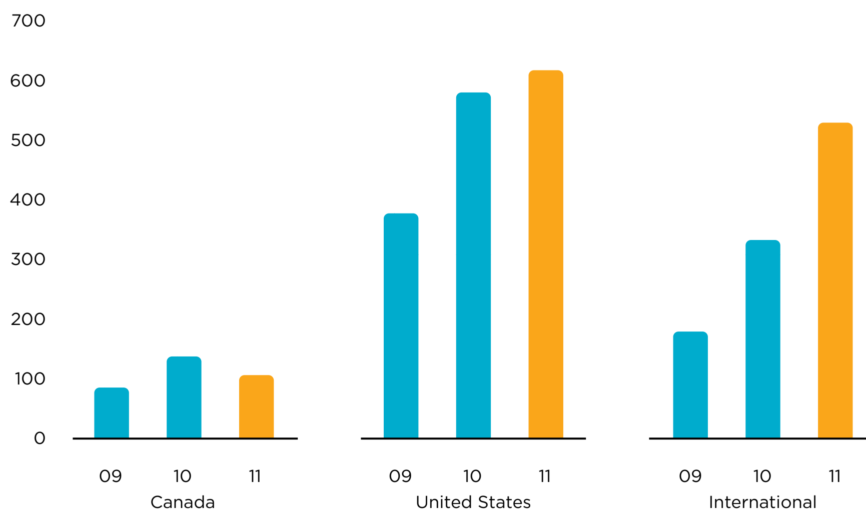
Our responsible investing approach flows directly from our legacy of championing sound corporate governance standards and practices with market regulators and companies globally. We do so based on our experience that good governance leads to long-term value creation.

Teachers' signs United Nations-backed Principles for Responsible Investment

In 2011, we became a signatory to the United Nations-backed Principles for Responsible Investment initiative (PRI). PRI provides a voluntary framework by which investors can incorporate ESG issues into their decision-making and ownership practices. Approximately 900 investment institutions and service providers, with assets totalling approximately US$25 trillion, have become signatories. Our investing practices are well aligned with the PRI principles, and PRI is consistent with our core values of championing accountability and risk consciousness.

In 2011, we voted 99.9% of our proxies and abstained only once as we sold our investment in a company shortly before our vote was required. We voted at 1,208 shareholder meetings, a 24% year-over-year increase. Continued growth in our direct holdings within indexed portfolios accounted for the increase, and this growth manifested itself in our voting at more non-North American company meetings. We also continued to share our views with external investment managers who are required to regularly submit their voting reports to us, which we review for consistency with Teachers' policies.

PROXY VOTING
(for the year ended December 31)



Reflecting the global nature of our investments and a shift to physical, direct investing within our index portfolios, in 2011 we voted in more shareholder meetings and more international meetings.

We vote from a total-plan perspective, which requires considerable collaboration among departments. We take a thoughtful and well-researched view and continue to believe that the election of qualified directors to supervise company activities is preferable to shareholders doing so directly.

In 2011, we voted against 64% of stock option plans presented to us for one of five reasons: i) the total number of options available for grant was greater than 5% of the total outstanding common shares of the company; ii) the annual option grant exceeded 1% of the company's total outstanding common shares; iii) automatic vesting of options on a change of control; iv) option exchanges where out-of-the-money options are exchanged for new options; and v) features that allow for a rolling maximum of shares available for grant.

We continued to support shareholder proposals to separate the roles of Chair and CEO, install majority voting for director election, and allow shareholders representing 10% or more of the outstanding shares to call a Special Meeting.

Our active approach to championing sound governance standards has earned Teachers' an international reputation as a corporate governance leader. Along with other responsible investing initiatives, we believe it continues to support our overall objective of helping the plan to meet its long-term funding needs.

2011 corporate governance activities

Our program is designed to identify and mitigate governance risk in the companies in which we invest. In addition to voting our proxies, we actively promote governance initiatives around the world. In 2011, this included:

- promoting our views on specific governance issues to more than 600 of the world's largest companies through our annual direct communications campaign;
- becoming the first international investor to comply with the *Stewardship Code* published by the Financial Reporting Council in the United Kingdom;
- continuing to sponsor research at the Clarkson Centre for Board Effectiveness at the University of Toronto; and
- commenting publicly on a variety of regulatory matters around the world, often in collaboration with other investors.

Internal asset management reduces costs

The success of the Investment Division is dependent on our employees continuously advancing and applying our strategies. As a learning organization, Teachers' is a leader in developing pension investment managers and is widely considered a global pioneer in our field. This requires ongoing investment in talent and the recognition that talent development is itself a key strategy.

Developing our talent has enabled Teachers' to create a repeatable investment process and has given us the intellectual capital and expertise that are fundamentally important in generating fund returns while containing costs.

As one of Canada's largest pension funds, we provide our people with the resources, training and career opportunities needed to meet the highest professional standards. These are important factors in our ability to attract and retain leading investment professionals. Our people are passionate about their work, innovative and deeply engaged with total-fund strategies and activities.

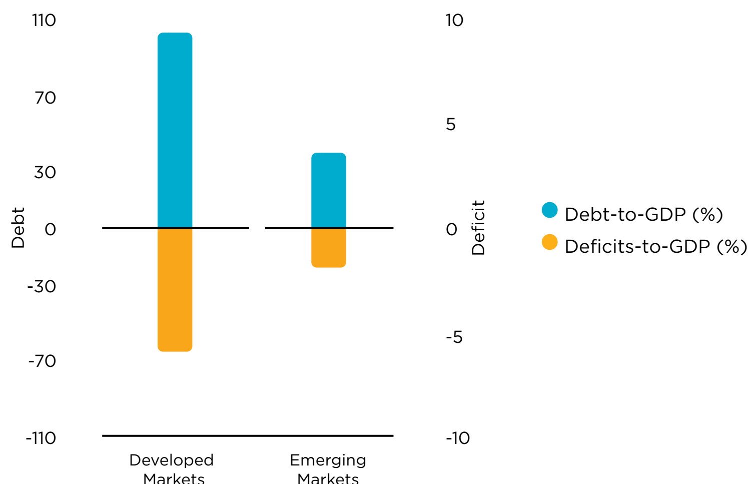
Nevertheless, there are markets in which it is more advantageous for us to invest through externally managed funds. We use external management to target investments that require local or specialized expertise that we have strategically decided not to develop in-house.

Identifying market trends

Our core investment strategies must work in the context of dynamic global markets, so it is incumbent upon us to engage in a robust annual investment planning process. This process focuses on identifying both long-term trends and medium-term risks that will impact the fund's future investment performance.

While outlooks are by nature subject to a high degree of imprecision, the process of reviewing trends and projecting possible outcomes is an important part of our approach to risk management and asset-mix positioning.

FISCAL CONDITIONS 2011



For example, in our most recent review, we observed a significant difference between the outlook for developed markets (DMs) and emerging markets (EMs). Developed economies and markets continue to suffer the lingering impact of the global financial crisis and remain challenged with high debt and fiscal deficits. This has resulted in their weaker-than-normal economic recovery following the global financial crisis. Furthermore, efforts to simultaneously reduce debt in both the private and public sectors raise the risk of continued slow growth over the medium term.

Alternatively, many EM countries have recovered well from the financial crisis due to stronger balance sheets, undervalued currencies and more flexibility on the economic policy front. Factors supporting economic growth in EMs over the longer term are their more favourable demographics and stronger productivity growth. However, EM countries cannot be viewed as being homogenous; each country has unique risks that must be carefully assessed. For example, an unwillingness of some EM countries to allow their currencies to appreciate increases their risk of experiencing inflation and could lead to asset price bubbles. An important part of our investment process is to identify these risks and ensure we have adequate diversification across all economies and asset classes.

PERFORMANCE

Measuring performance

We are long-term investors, and therefore the most relevant measure of our performance is over multiple years. In this annual report, we disclose our total-fund rate of return on an actual basis and against a benchmark on a one-, four- and ten-year basis, as well as since 1990 when we began our investment program. Investment returns are calculated net of trading costs, investment management expenses and external management fees, and are calculated in Canadian dollars.

We measure total plan return against a Canadian dollar-denominated composite benchmark, which is calculated by aggregating results from each of the policy asset-class benchmarks and weighting those benchmarks so that they are the same as the plan's asset-mix policy weightings.

Benchmarking is important to our board members, employees and plan members in that it enables us to evaluate the effectiveness of our investment strategies and activities relative to the risks taken. In each case, we strive to exceed the benchmark, and when we do, this is described as value added.

Establishing appropriate benchmarks is a complex task, and for that reason we have a benchmarking committee chaired by the CEO that provides oversight. The committee uses a rigorous process for recommending and adjusting benchmarks. Only our board members can approve changes to fund benchmarks.

Benchmarking enables us to evaluate the effectiveness of our investment strategies and activities relative to the risks taken.

BENCHMARKS USED TO MEASURE PLAN PERFORMANCE

	Benchmark
Canadian equities	S&P/TSX 60 Custom Long Term Canadian Equity
Non-Canadian equities	S&P 500 MSCI EAFE+EM MSCI All Country World ex Canada MSCI Emerging Markets MSCI Emerging Markets ETF Custom Non-Canadian National Indices Custom Global Private Capital Benchmark Custom Long Term Non-Canadian Equity
Fixed income	Custom Canada Bond Universe Custom Canada Long Bond Universe Custom Provincial Long Bond Custom Ontario Debentures Custom Canada Real Return Bond Custom U.S. Treasury Inflation Protected Securities DEX 91 Day T-Bill
Commodities	S&P GSCI S&P GSCI 3-Month Forward Custom Commodities Hedge
Real assets	CPI plus 5.0% plus IPD Canada Capital Growth (Real Estate) DEX BBB Real Estate Debt Local CPI plus 4% plus country risk premium (Infrastructure and Timberland)
Total plan	Custom Canadian CDOR Index Custom U.S. LIBOR Index Custom Canadian OIS Index Custom U.S. OIS Index

RATES OF RETURN COMPARED TO BENCHMARKS

	1 Year		4 Year	
(percent)	Actual	Benchmark	Actual	Benchmark
Equities	**(0.8)%**	**(5.1)%**	**(0.3)%**	**(3.4)%**
Canadian equities	(5.0)	(9.1)	(2.3)	(1.6)
Non-Canadian equities	0.2	(4.4)	0.2	(4.1)
Fixed income	**19.9**	**19.5**	**9.8**	**9.5**
Real-return products	21.7	21.7	10.5	8.8
Bonds	18.0	17.2	9.6	9.4
Commodities	**(2.3)**	**(1.5)**	**(10.3)**	**(10.0)**
Real assets	**13.1**	**13.3**	**7.1**	**7.8**
Real estate	18.2	21.8	9.1	10.4
Infrastructure	7.7	6.1	4.9	5.1
Timberland	0.8	10.2	0.5	6.8
Total plan[1]	**11.2%**	**9.8%**	**4.2%**	**4.4%**

[1] Returns generated by absolute return strategies and money market are included in the total plan return and not attributed to an asset class.

Investment costs

Managing a successful investment program involves costs in areas such as salaries and benefits, fees and commissions and research. The plan is committed to cost effectiveness and views certain expenditures as necessary to achieve long-term performance requirements. In 2011, total investment costs were $289 million or 27 cents per $100 of average net assets, compared to $290 million or 30 cents per $100 in 2010. This primarily reflects a decrease in incentive payments in 2011.

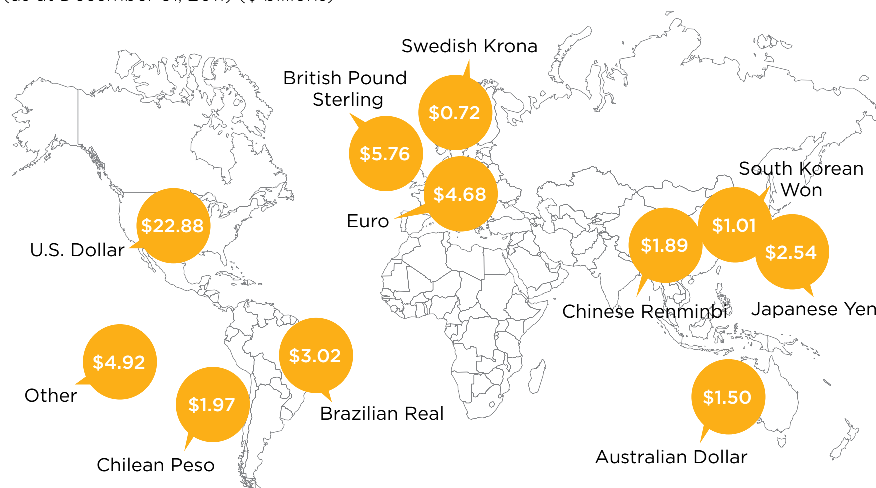
2011 Markets in review

While economic growth is a key driver of asset returns and bond yields over the long term, shorter-term performance is largely influenced by changes in market sentiment. Over much of the past two years, financial markets have oscillated between bouts of optimism and pessimism. These large swings in sentiment have been primarily driven by the highly uncertain economic conditions in a post-financial crisis environment. The strong rally in the early part of 2011 was triggered by a second round of quantitative easing in the U.S. However, this was soon overshadowed by pessimism in the third quarter due to the intensification of the Eurozone sovereign debt crisis and fears of another global recession. In late November, market sentiment turned once again as a result of better-than-expected economic performance in the U.S. and aggressive policy actions from the European Central Bank.

Overall, sectors and regions most susceptible to the sovereign crisis, such as European equities and the financial sector, underperformed. U.S. and Canadian bond markets performed well, and Canadian bond yields continued to decline, reaching new record lows. This was consistent with our "muddling-through" thesis that bond yields can stay low for a prolonged period of time in a below-trend growth environment. We note that central banks in most developed markets are not expected to raise their policy interest rates until 2014.

Since we measure the fund's performance in Canadian dollars, it is important to note how our currency fared against other currencies in which we have significant exposures. We actively manage these currency exposures.

NET CURRENCY EXPOSURE
(as at December 31, 2011) ($ billions)



Currency exposures are actively managed.

Total return

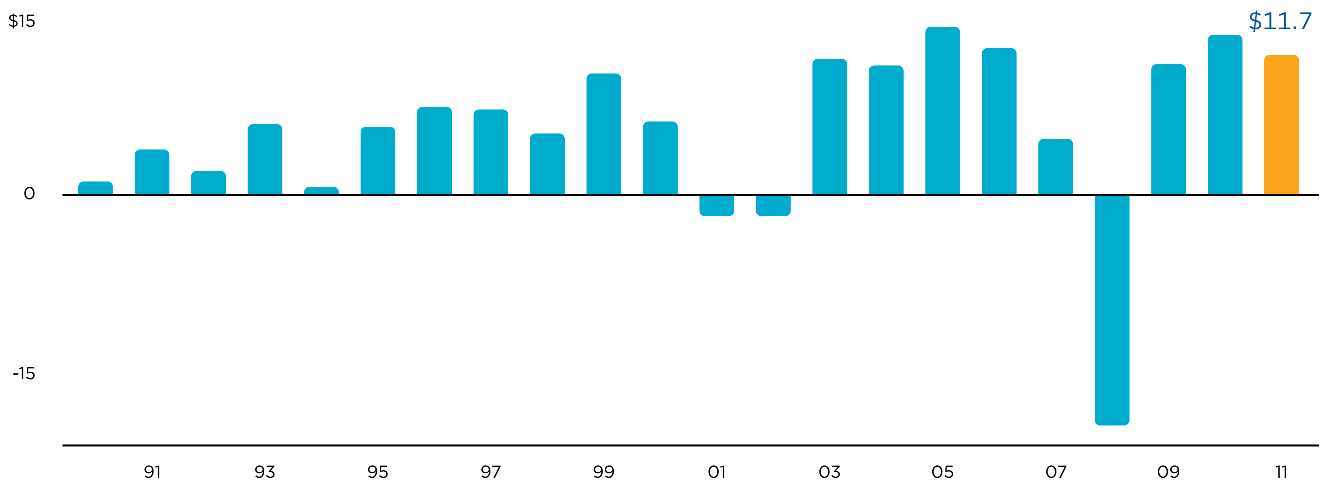
The plan posted an 11.2% return in 2011, generating $11.7 billion in investment income. Investment income was produced mainly by private equity, real estate, fixed income and infrastructure. Net assets were $117.1 billion compared to $107.5 billion at the end of 2010.

As detailed in the accompanying table, the total return exceeded the composite benchmark return of 9.8% by 1.4 percentage points. This added $1.4 billion in value above the benchmark. Value-added returns resulted mainly from private equity, fixed income and infrastructure. The total plan has an annual growth of 4.2% over the past four years, underperforming the composite benchmark by 0.2 percentage points for -$0.4 billion in value added primarily due to recognition of 2008 losses.

INVESTMENT PERFORMANCE

(percent)	**2011**	2010	4-year	10-year	Since Inception
Total return	**11.2**	14.3	4.2	8.0	10.0
Benchmark	**9.8**	9.8	4.4	6.0	7.8
Return above benchmark ($ billions)	**$1.4**	$4.0	$(0.4)	$16.5	$24.6

INVESTMENT INCOME EARNED
(for the year ended December 31) ($ billions)



ASSET-CLASS REVIEW

Equities

The plan uses equities to deliver investment growth for the plan. This asset class includes public equities (companies listed on a stock exchange) and private equities, which are less liquid and best suited for patient investors willing to participate for long-term gains.

WAYNE KOZUN,
MBA, CFA
SENIOR VICE-PRESIDENT,
PUBLIC EQUITIES

The value of the plan's equity investments (both public and private) totalled $51.7 billion at year end compared to $47.5 billion at December 31, 2010, as additional capital was deployed to maintain our policy asset-mix weighting at approximately 45%.

On a one-year basis, equities returned -0.80% compared to a benchmark return of -5.1% for total value added of $2.0 billion. Our equity portfolio earned $1.2 billion in dividends in 2011. On a four-year basis, equities generated a -0.3% compound annual return compared to the four-year benchmark of -3.4% for total value added of $4.8 billion. The asset-class benchmark is a composite of Canadian and international indices and global private equity benchmarks.

Most equity markets performed poorly in 2011. We delivered value-added performance in each of our equity segments, as described below. At year end, equity valuations remained attractive relative to historical norms, and dividend yields in North America were well above inflation.

Non-Canadian equities

Non-Canadian equities (both public and private) totalled $41.1 billion at year end compared to $38.2 billion at December 31, 2010, and returned 0.2% compared to a benchmark return of -4.4% for total value added of $1.6 billion. On a four-year basis, non-Canadian equities generated a 0.2% compound annual return compared to the four-year benchmark return of -4.1% for total value added of $5.3 billion.

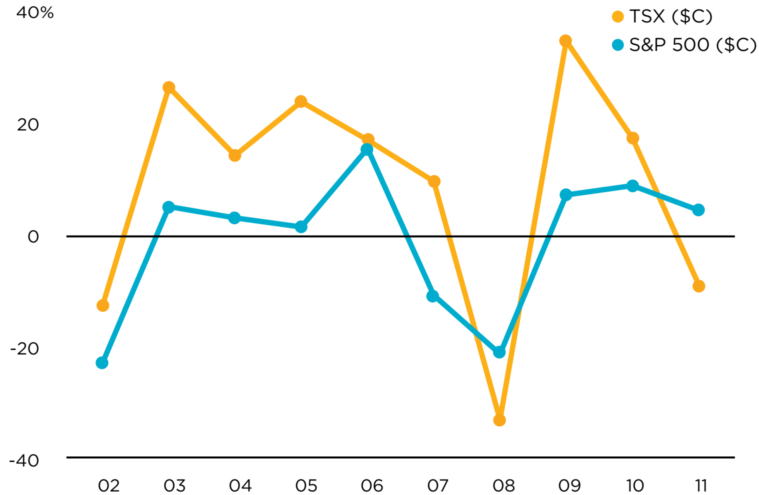
Equity market performance in major economies was generally weak due to fears of a Eurozone-led recession. Expressed in Canadian dollars, our reporting currency, the FTSE 100 was down -0.4% on the year, the DAX was off -15.4% and the CAC 40 and the Hang Seng were down -13.8% and -15.2% respectively. Brazil represents our largest emerging market exposure. Its main index closed down -25.3% at year end, also expressed in Canadian dollars.

The U.S. equity market was the outlier during 2011 and, for the first time in several years, outperformed the S&P/TSX Composite. Measured in Canadian dollars, the S&P 500 was up 4.6% year over year. Our increased U.S. holdings contributed to value-added performance.

Direct holdings increased in 2011, although derivatives remain a primary way to gain cost-effective exposure to global public equity markets. This approach also allows us to focus on a smaller universe of stocks for our more concentrated active and Relationship Investing portfolios.

Non-Canadian equities are overseen by both internal and external managers using a combination of active strategies and index funds. We continue to build internal capacities to directly manage emerging market stocks.

10-YEAR CANADIAN/U.S. MARKET INDEX COMPARISON
(percent)



Canadian equities

Canadian equities (both public and private) totalled $10.6 billion at year end compared to $9.3 billion at December 31, 2010, and returned -5.0% compared to a benchmark return of -9.1% for total value added of $0.4 billion. On a four-year basis, Canadian equities generated a -2.3% compound annual return, compared to the four-year benchmark of -1.6% for underperformance of -$0.5 billion.

Canadian equity markets are heavily weighted to extractive industries, which performed poorly in 2011. Performance against the benchmark during the year reflected outperformance of Canadian private equities, which is discussed below.

JANE ROWE, MBA, ICD.D
SENIOR VICE-PRESIDENT,
TEACHERS' PRIVATE CAPITAL

Teachers' Private Capital

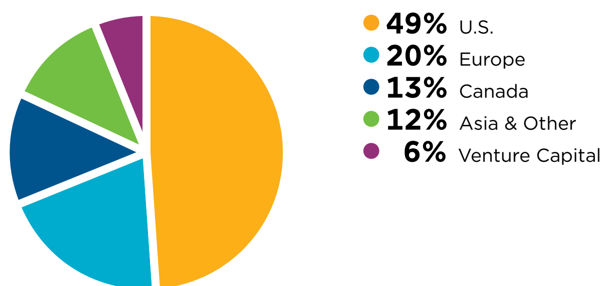
The performance of private equities managed by Teachers' Private Capital (TPC) is consolidated with the Canadian and non-Canadian segments noted above. However, due to the unique risk and liquidity profile of private equities, TPC results are segregated here for reference.

Formed in 1991, TPC invests directly in private companies, either on its own or with partners, and indirectly through private equity and venture capital funds managed by third parties. Today, it is one of the largest investment pools of its kind in the world and was inducted in 2011 into The Private Equity Hall of Fame – as chosen by the editors of Dow Jones Private Equity Analyst – for exemplary and enduring contributions to venture capital, buyout and related private equity disciplines. Since its inception, TPC's core portfolio (direct investments, co-direct investments and private equity funds) has generated an internal rate of return of 19.3%.

Private equity investments totalled $12.2 billion at year end compared to $12.0 billion at December 31, 2010, and returned 16.8% compared to a benchmark return of -0.2% for $1.6 billion in value added. On a four-year basis, these assets generated a 4.2% compound annual return compared to the four-year benchmark return of -1.0% for $1.4 billion in value added.

TPC's extraordinary value-added performance in 2011 reflected a significant number of monetizations and valuation adjustments within its portfolio holdings. Additionally, TPC redeployed approximately $1.7 billion of capital to new private equity investments during the year. Three significant direct investments were made along with investments in two new funds and reinvestments with five existing funds. TPC continues to expand its global reach by working with private funds around the world.

TPC PORTFOLIO
(as at December 31, 2011) (percent)



Fixed income

Our fixed income investments are used to provide investment security and steady income and, more generally, to stabilize fund returns and counteract the impact of interest rate changes on plan liabilities.

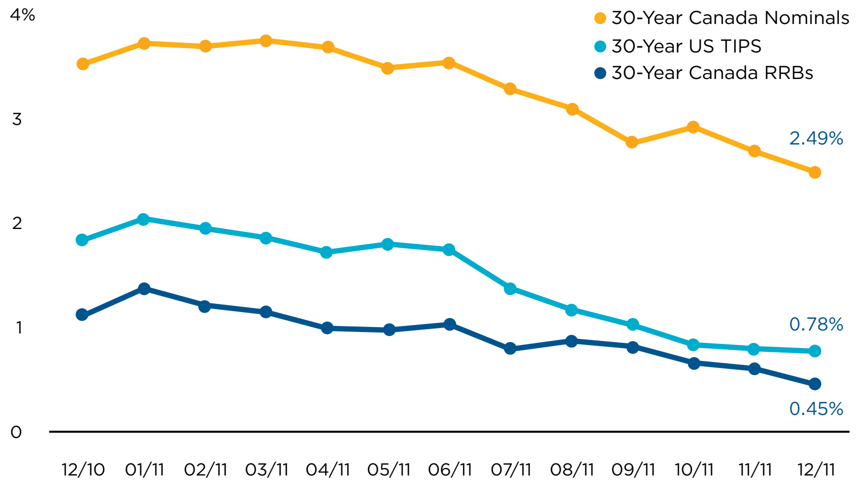
RON MOCK, MBA
SENIOR VICE-PRESIDENT, FIXED INCOME AND ALTERNATIVE INVESTMENTS

We own a diversified portfolio of Government of Canada bonds, Ontario debentures, provincial bonds, real-return bonds and inflation-linked bonds. Real-return bonds provide returns that are indexed to inflation, as measured by the consumer price index, and include debt issued primarily by the Canadian and U.S. governments, and the manager of Highway 407 in Ontario.

Fixed income assets totalled $55.8 billion at year end compared to $45.9 billion at December 31, 2010, and returned 19.9% compared to a benchmark return of 19.5% for $163.4 million in added value. On a four-year basis, fixed income generated a 9.8% compound annual return, outperforming the benchmark by 0.3% for $345.7 million in value added.

The value of our bond portfolio increased in 2011 as interest rates fell and global investors responded to the Eurocrisis and fears of recession by moving capital to government bonds that are perceived to be more creditworthy. This had the impact of increasing bond prices. Since the 2008 recession, we have increased fixed income investments as part of our total-fund risk management strategy.

GOVERNMENT BOND YIELDS
(percent)



MICHAEL WISSELL, MBA, CFA
SENIOR VICE-PRESIDENT,
TACTICAL ASSET ALLOCATION

Commodities

We invest in commodities, such as energy and agricultural products, as a hedge against the cost of paying inflation-protected pensions. In the short term, commodity prices reflect supply and demand imbalances in global markets as well as short-term changes in inflation. Over the long term, commodity prices reflect inflation expectations.

Investments in commodities totalled $5.7 billion at year end compared to $5.2 billion at December 31, 2010. The portfolio returned -2.3% compared to a benchmark return of -1.5%. On a four-year basis, these assets generated a -10.3% compound annual return compared to -10.0% for the benchmark.

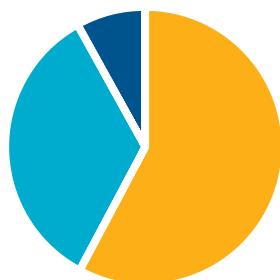
For our commodities portfolio and the benchmark, 2011 was another year of significant price volatility and low inflation. In fact, inflation has remained benign in Canada for most of the past decade. As commodities are generally a longer-term investment at Teachers', 10-year returns are a more relevant measure of performance.

Real assets

Investments in this category – real estate, infrastructure and timberland – are good long-term investments for the pension plan because they provide returns that are linked to changes in inflation and therefore also act as a hedge against the cost of paying inflation-protected pensions. Over the past 10 years, these investments have played an increasingly important role in helping us to meet our performance objectives and minimize risk.

In aggregate, real assets totalled $25.8 billion at year end compared to $26.2 billion at year-end 2010 and returned 13.1% compared to the benchmark return of 13.3% for value added of -$474.0 million. On a four-year basis, real assets generated a 7.1% compound annual return compared to the benchmark return of 7.8% for value added of -$1.4 billion.

REAL ASSETS
(as at December 31, 2011)



- **58%** Real Estate **($15.0 billion)**
- **34%** Infrastructure **($8.7 billion)**
- **8%** Timberland **($2.1 billion)**

Real estate

Real estate fits our plan because it provides strong, predictable income. Our portfolio is managed by The Cadillac Fairview Corporation Limited. This wholly owned subsidiary maintains a well-balanced portfolio of retail and office properties designed to provide dependable cash flows. Portfolio highlights in 2011 included the disposition of the investment in Hammerson plc, a U.K. real estate company, and the disposition of Hillcrest Mall in Toronto. In addition, there was major progress on a number of significant development projects including extensive renovations to the Toronto Eaton Centre and the ongoing revitalization of the Toronto-Dominion Centre office complex.

JOHN SULLIVAN, MBA
PRESIDENT & CEO,
CADILLAC FAIRVIEW

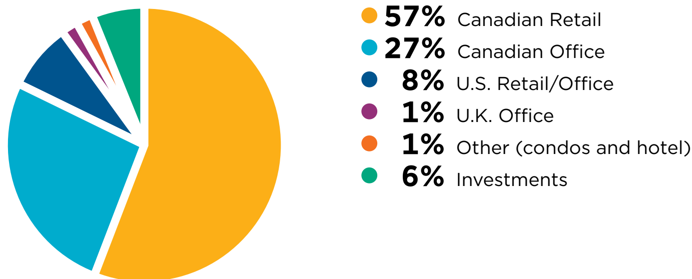
A new financing vehicle, Cadillac Fairview Finance Trust, was established in 2011 and it issued $2.6 billion in new AAA-rated debt guaranteed by Teachers'. This financing activity lowered borrowing costs for real estate and lowered the cost of capital for Teachers'.

The real estate portfolio earned operating income of $1.0 billion in 2011, primarily from retail and office properties. At year end, the retail occupancy rate was 94% (93% in 2010), while the office occupancy rate was 92% (91% in 2010).

The net value of the real estate portfolio totalled $15.0 billion at year end compared to $16.9 billion at December 31, 2010. The net decrease is primarily due to the issuance of new debt and disposition of our investment in Hammerson plc, offset by an appreciation in value of our real estate assets. The real estate portfolio returned 18.2% compared to a benchmark return of 21.8% for -$0.4 billion in value added (a new real estate benchmark was adopted for 2011). On a four-year basis, the real estate portfolio generated a 9.1% compound annual return, compared to the four-year benchmark of 10.4% for value added of-$0.8 billion.

Real estate markets overall performed strongly in 2011. Investor demand for retail and office properties continued to be robust, aided largely by lower interest rates, which drove down capitalization rates in North America. Quality retail and office properties also had higher revenue and occupancy growth in 2011.

REAL ESTATE PORTFOLIO
(as at December 31, 2011) (based on total assets)



STEPHEN DOWD, MBA, ICD.D
SENIOR VICE-PRESIDENT, INFRASTRUCTURE AND TIMBERLAND

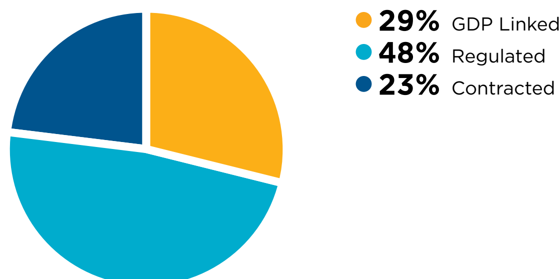
Infrastructure

We began investing directly in infrastructure in 2001 because these assets generally offer stable long-term cash flows linked to inflation. Our portfolio includes investments in airports, electrical power generation, water and natural gas distribution systems, container terminals, pipelines and a high-speed rail link. The majority of these assets are located outside Canada as opposed to our real estate portfolio, which is predominantly Canadian. This means currency fluctuations have a greater impact on infrastructure portfolio value and returns when translated into Canadian dollars.

Infrastructure investments totalled $8.7 billion at year end compared to $7.1 billion at December 31, 2010, due to new investments in European airports and Chilean utilities, and to valuation adjustments, net of the sale of our Sydney Airport interest. Infrastructure assets returned 7.7% compared to a benchmark return of 6.1% for $176.9 million in value added. On a four-year basis, these assets generated a 4.9% compound annual return, compared to the four-year benchmark of 5.1%.

Overall we seek to build a portfolio which will steadily increase in value, provide predictable cash flow and correlate to inflation. We segment the portfolio into three general categories: GDP-linked assets whose fundamentals are tied to a country's real macroeconomic flows; regulated companies whose revenues are explicitly linked to formal regulatory regimes; and contracted assets with a significant percentage of revenues tied to long-term contracts. Regulated and contracted assets generally performed well in 2011, while GDP-linked assets continued their slow recovery from the 2008-09 recession.

INFRASTRUCTURE PORTFOLIO
(as at December 31, 2011)



Timberland

Timberland investments correspond to, and are compatible with, the plan's lengthy investment horizon because they are long-lived assets and serve as a hedge against long-term inflation. While the value of timberland assets changes with the demand for wood and paper, if left in the ground, trees continue to grow, noticeably increasing their yield and value over time, unlike other extractive industry assets such as metals and minerals. To control risk, we invest solely in managed plantations that use proven techniques to grow, maintain, harvest and regenerate stock.

Timberland investments totalled $2.1 billion at year end, compared to $2.2 billion at December 31, 2010. These holdings returned 0.8% compared to a benchmark return of 10.2% for value added of -$194.5 million. On a four-year basis, timberland generated a 0.5% compound annual return compared to the four-year benchmark of 6.8% for value added of -$575.2 million.

Our timber properties are primarily located in the United States, and harvests have been delayed due to low housing starts and uncertain near-term U.S. housing prospects. Our properties in New Zealand have found strong export markets in China, while our Brazilian timberland is positioned for the long-term growth of this developing economy.

Notable transactions in 2011

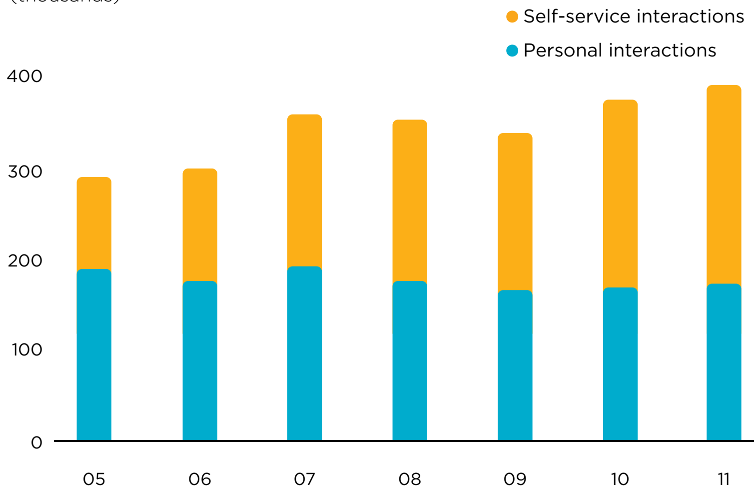
In 2011, Teachers' bought and sold many investments as part of our active approach to creating value and managing risk, including the transactions below, which are notable for their size and/or public profile.

- Maple Leaf Sports & Entertainment (MLSE): In December, we reached an agreement to sell our 79.53% ownership share in MLSE to Bell and Rogers Communications Inc. for $1.32 billion, based on an enterprise value of more than $2 billion. MLSE is one of Teachers' longest standing and most successful investments. The divestiture effort was led by Teachers' Private Capital and is expected to close in mid-2012 following regulatory and league approvals.

- Imperial Parking Corporation (Impark): We completed the acquisition of Babcock & Brown Gates Parking Investments LLC, which includes Impark, one of the largest parking management companies in North America. Impark leases or manages more than 2,000 parking locations, consisting of more than 400,000 parking spaces, in over 25 markets in Canada and the United States. The transaction was led by Teachers' Long-Term Equities group, which is focused on direct investments that have steady cash-flow growth potential over a long-term horizon and a low to moderate level of risk.

- Airports: We exchanged our interest in Sydney Airport plus a cash payment for MAp Airports' interests in two European airports. As a result, Teachers' Infrastructure Group added to our current airport holdings with ownership of 39% of Brussels Airport and 30% of Copenhagen Airport. We will work with fellow stakeholders, including the Belgian and Danish governments, to develop the full potential of these properties.

Member Services



Members are increasingly opting to go online for services. The growth in web usage, balanced by continued growth across other channels, underlines our service delivery strategy.

"We must balance service with costs, membership growth with web and system optimizations, and strategy with regulation."

ROSEMARIE McCLEAN, MBA, CMA, ICD.D
SENIOR VICE-PRESIDENT, MEMBER SERVICES

OBJECTIVE AND MANAGEMENT STRATEGIES

The Member Services Division delivers pension services directly to plan members and interacts with school boards and designated employers. This team takes in and processes billions of dollars of contributions and millions of pieces of personal information every year while administering one of Canada's largest payrolls – $4.7 billion in annual pension and lump-sum benefits payments – to 120,000 retirees and their survivors.

Our objective is to deliver outstanding, personalized service to all plan members at a reasonable cost. We consistently earn high service ratings from plan members and believe our members deserve timely, reliable services and the pension information that is accurate and relevant to them at different stages of their careers.

To meet our objective, we have a strategy called $e=(mc)^3$. In this strategy, "e" stands for excellence reached by offering more customization, more choice and more counselling to members.

Excellence = more customization
more choice
more counselling

Customization: The service and information requirements of members change throughout their careers. Their experiences with other service organizations influence expectations, as they get more and more used to immediate support models and real-time communication. We must find the right triggers and delivery methods to ensure that our message resonates. To do this, we anticipate members' needs to provide them with personalized service. Currently, we use database technology and employment data to better target our services and communication.

Choice: This reflects our commitment to properly serve members through their preferred channel. While the majority of members prefer the convenience of online services, other members prefer to be served over the telephone or by mail. We offer services in a variety of ways and can note preferences on each member's file.

Counselling: We combine the expertise of our front-line pension benefit specialists with our evolving technology capabilities to help members make informed decisions. Our decision to provide guidance, rather than merely disclose information, allows us to meet a demand that members have long requested. The benefits and rules of the pension plan are complex, and decisions made by individuals can have ramifications, not only for their lifetime but for their survivors' lifetimes as well.

As we integrate broader employment data into our systems, new opportunities to counsel members will emerge based on our deeper understanding of individual situations. Increasing our proactive outreach to members enables them to make consistent and optimal choices about a variety of pension-related matters.

2011 priorities and initiatives

To move our long-term strategy forward, in 2011 we expanded our services to offer more choice, counselling and customization. Specifically, we undertook the following major initiatives:

- We increased our level of proactive service significantly by informing 24,000 plan members of opportunities to buy back credit in the plan for leaves of absence.
- We developed three new counselling tools to help members decide among various options for buyback payments and to make more informed survivor benefit decisions. These tools, offered over the telephone and online, integrate members' personal information to guide them to the choices best suited to their individual circumstances.
- We improved our *i*Access™ Web facility by redesigning our pension calculator and upgrading other services. We also made it possible for pensioners to estimate inflation adjustments on their pensions, taking into account the conditional inflation protection component for pension credit earned after 2009. When members sign in to *i*Access™ Web, they can use their personal pension information to calculate pension and buyback estimates, for example, and obtain many other services.

- We began delivering news electronically to teachers and pensioners as it happens, instead of following a quarterly newsletter schedule. We are also incorporating more video content to increase understanding of pension rules and provisions. We send relevant news and information to specific segments of the membership when they need it, and bundle news into newsletters three or four times a year.

Of these initiatives, the buyback project was the largest. Using employer data that showed a leave of absence had occurred, we reached out to 24,000 members with buyback information. Many of these members would not otherwise have known that buying back credit in the plan was an option. (Previously, buyback estimates and transactions were initiated only when a member contacted us, usually for a maternity or paternity leave.)

Members reacted positively to this new service and, consequently, we saw a five-fold increase in requests for cost estimates to buy back credit. A total of 35,700 requests for estimates were completed in 2011, compared to 5,700 requests in the prior year. It is still too early to know how many members will decide to complete a buyback; our objective, however, was to ensure they were fully informed of their buyback opportunity and specific repayment options, which we achieved.

This experience illustrates the value to members of our approach. Obtaining more complete employment data from school boards and designated employers showed us that many teachers were taking leaves without learning about the option to buy back credit. Closing the information gap gives members the choice and opportunity to make informed decisions to maximize their pensions.

The volume of actual leaves of absence was higher than anticipated, and dealing with the resulting requests was a challenge. Use of our online buyback service, released in 2010, almost doubled and we optimized internal systems to help manage the accumulated requests. Further system optimizations are planned for 2012.

These initiatives are giving members better service and guidance on pension decisions and a clearer picture of their personal financial situation in retirement.

MEMBERSHIP FACTS AND TRENDS

Plan membership grows every year

The number of pensioners has grown every year since 1917, when this plan was first created. Consequently, the total membership reached 368,000 members at the end of 2011, including working teachers, pensioners and inactive members (former teachers who have an entitlement in the pension plan but are not currently contributing or receiving benefits).

The total number of pensioners grew by 3,000 and the number of active members (teachers) increased by 2,000 from 2010.

MEMBER PROFILE
(as at December 31, 2011)

180,000	+	68,000	+	120,000	=	368,000
ACTIVE MEMBERS		INACTIVE MEMBERS		PENSIONERS		TOTAL MEMBERS
49%		18%		33%		

Quick facts

- Number of pensioners has tripled since 1990
- 60% of pensioners are under age 70
- Oldest pensioner was 109 at the end of the year
- Average annual pension for new unreduced pensions starting in 2011 was $45,500

The average teacher is 42 years of age.

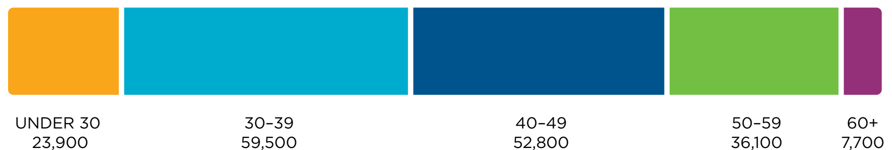
The average age of pensioners is 69. 102 pensioners are 100 years of age or older.

TRENDS

Average age of teachers retiring last year	59	Average age at retirement is increasing slowly
Number of retirements last year (retirement and disability pensions)	4,300	Retirements have been lower than expected since the financial crisis erupted in 2008
Number of teachers who entered or returned to the teaching profession	7,900	New and returning teachers have been declining slightly over the past five years
Average years retirees are expected to collect pensions	30 years	Members are typically retired for longer than they worked
Length of a typical teaching career	26 years	

TEACHERS AND PENSIONERS BY AGE

180,000 ACTIVE MEMBERS



UNDER 30 23,900 | 30–39 59,500 | 40–49 52,800 | 50–59 36,100 | 60+ 7,700

120,000 PENSIONERS

UNDER 60 11,500 | 60–69 60,700 | 70–79 32,800 | 80–89 12,400 | 90+ 2,600

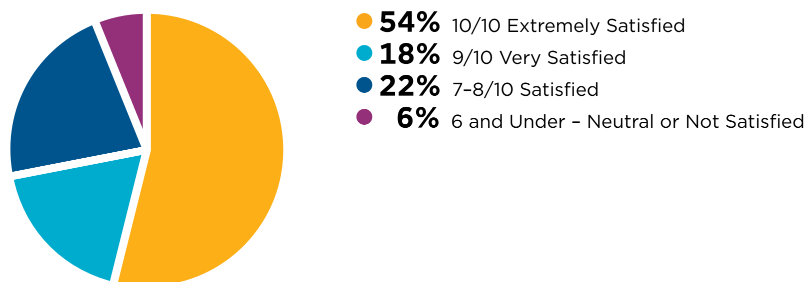
MANAGING SERVICE COMPLEXITIES

Our operating environment is continually changing and involves many factors that affect our performance. Plan membership is dynamic, and new pension regulations and plan changes are increasingly being introduced. We must balance services with costs, membership growth with web and system optimizations, and strategy with regulation. We rely heavily on highly trained staff, evolving technology and data quality from employers to meet our service obligations and execute our strategy.

Balancing services and costs

Members consistently rate our services very highly, and the majority of service requests are completed within one day. We have to raise the bar every year to maintain this high rating as expectations and work volumes increase due to the growing membership. Because we are cost conscious, we aim to strike the right balance between services and costs. We consider improvements that are cost effective and valuable for members, such as the introduction of pension counselling and web enhancements, and concentrate on improving our internal processes and systems in order to handle the growing work volume. We believe the return on investment for expenditures related to service improvements creates long-term value for our members.

SERVICE SATISFACTION – MEMBER SURVEY
(year ended December 31, 2011) (percent)



Expansion of service channels

The number of pensioners increases every year, as does the total number of members we serve. Their expectations also change over time. For example, there is less tolerance for delay in the era of instantaneous communication and online commercial transactions. Several years ago, we began expanding our service platforms to keep pace with growth and to meet members' changing expectations while maintaining service quality across all channels.

We offer services by telephone, by mail and e-mail, in person, and electronically through our secure member website, *i*Access™ Web. Members' usage of online services grows every year, and we regularly add new web capabilities. Offering services electronically adds costs for the highly trained IT staff and Internet security measures needed to protect the privacy of members' personal financial information. Our systems and personnel now handle 1,000 member interactions a day, 365 days a year. Before the introduction of online services, our contact centre could not have handled this volume of interaction. By enabling members to update personal information, apply for pensions and obtain pension and other estimates online, we free up our front-line pension benefit specialists to counsel members on pension decisions and choices – a key part of our value-added service strategy.

Receiving accurate employment data allows us to provide more complete and proactive services to members.

Employment data quality

Our ability to provide outstanding service, and to carry out our strategy, is largely dependent on getting accurate, up-to-date employment information from 175 school boards and designated employers. They have varying systems and resources, and we work with them closely to improve the quality and breadth of employment data we receive. We use this information to calculate benefits, respond to members' requests promptly, and anticipate their needs for service.

We offer employers hands-on assistance to understand pension reporting requirements and our online reporting technology. Each employer has a designated contact on our Employer Information Services Team who understands the employer's payroll system and can share knowledge with our development teams. We conducted seven workshops throughout Ontario last year in English and French, attended by 150 pension reporting staff members at school boards and other employers. Annually, we ask school board finance officers to certify that the contributions and service information delivered to us are correct. This has proven invaluable in receiving accurate data.

A larger proportion of our annual budget is now allocated to compliance activities.

Plan and regulatory compliance

Mandatory regulatory and plan changes must be implemented and understood. They affect our systems, processes and staff training needs, and challenge us to find ways to keep members informed with information that is relevant to them. For example, we had to adapt our systems to account for the sponsors' decision to invoke conditional inflation protection at the 60% level for pension credit earned after 2009 and increase contribution rates effective January 1, 2012, 2013 and 2014. We must also integrate the new pension division rules for marital breakdown, new eligibility requirements for breaks in service and other legislative changes.

We are dealing with an unprecedented number of plan and regulatory changes. A larger proportion of our annual budget is now allocated to compliance activities. In addition, changes prescribed in regulations are frequently at odds with our strategy to customize information and make it easy for members to obtain services through a variety of channels. Often these changes make the plan more complex, which increases the need to simplify and tailor information for members so that it is relevant and understandable. It is an ongoing challenge to balance regulatory requirements with our strategic direction.

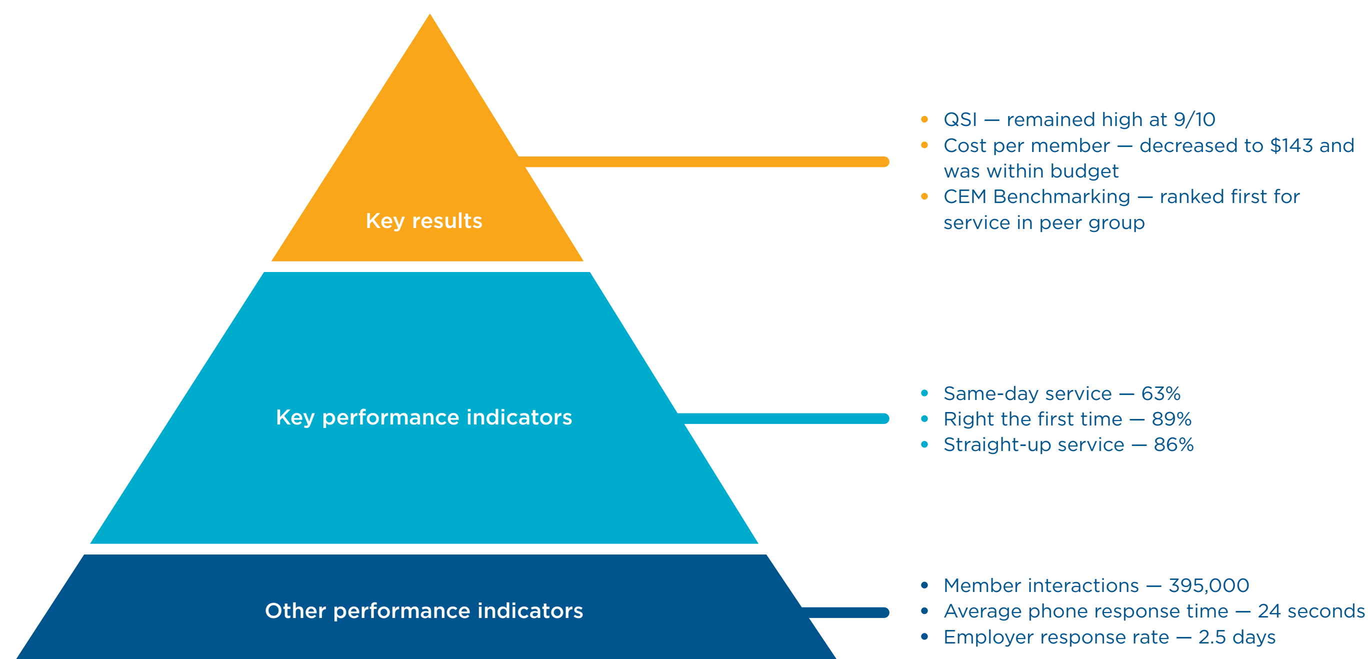
Training

We have 45 pension benefit specialists who interact directly with plan members through our contact centre. In order to meet the complex service needs of our clients, new specialists go through intensive, personalized training for the first year of employment. To underscore our commitment to service quality, our internal training staff periodically review interactions between our front-line agents and plan members and provide coaching and feedback. An independent survey company will also interview a sample of members within 24 hours of completed service. Pension benefit specialists receive feedback the next day.

PERFORMANCE

We take a comprehensive approach to measuring our performance using key service satisfaction and financial results, key performance indicators and other measurements of our overall service delivery levels.

HOW WE MEASURE PERFORMANCE



Quality Service Index

The Quality Service Index (QSI) is a primary performance measurement. We regularly ask members to rate our services through a third-party survey. We engage an independent company to survey a statistically valid membership sample in order to gauge the quality of our service and communications several times each year. We developed the survey protocol in the early 1990s and continually review and refine it to reflect current services and communications. All employees – from new recruits to executives – receive a variable component of compensation based on the levels of satisfaction expressed in these QSI measurements. Compensation also reflects the success achieved in managing costs and meeting organizational goals that are set annually to drive continuous improvement.

Our overall QSI score was 9.0 on a 10-point scale, and 54% of respondents awarded us 10 out of 10. As shown in the table on page 56, members rate us in terms of direct service and communications, with direct service representing 85% of the overall score.

We have maintained a high QSI score over the last five years, even as contributions increased and other measures were introduced to deal with funding shortfalls. We realize that it is difficult to improve on these already high ratings.

The QSI is a measurement of service satisfaction. Our 9.0 rating is based on member surveys conducted by a third party using a scale of zero to 10.

9 OUT OF 10

QUALITY SERVICE INDEX
(on a scale of 0 to 10)

	2011	2010
Total QSI	9.0	9.0
Service QSI (85%)	9.0	9.0
Communications QSI (15%)	8.8	8.8

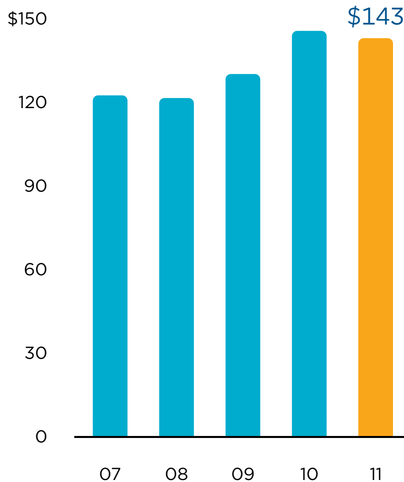
Service cost and expense management

Our total costs are increasing due to several factors, including:

- increasing number of plan members;
- expansion of services;
- increasing salary costs and the need for more highly skilled IT staff;
- regulatory and plan changes that affect systems, require staff training and more communication with plan members; and
- operation and replacement costs of legacy systems.

We measure our annual service cost per member to manage costs effectively. The cost per member in 2011 was $143 compared to $146 in 2010. We maintained costs within our allocated budget while complying with plan changes and investing in the technology and people required to build and maintain the increasingly automated environment needed to evolve our service model.

COST PER MEMBER SERVED
(for the year ended December 31) (dollars)



CEM Benchmarking Inc.

We measure our services against those of leading pension plans worldwide by participating in surveys conducted by CEM Benchmarking Inc., which carries out independent evaluations of 47 major pension plans. This evaluation helps us better understand whether we are striking the right balance between services and costs.

For 2010, we ranked first out of 13 peer pension plans and placed second overall for service. Our 2011 ranking will be released in 2012.

CEM BENCHMARKING RESULTS – SERVICE LEVEL SCORE COMPARISON

	2010	2009	2008	2007
Ontario Teachers' Pension Plan	86	86	85	86
CEM world average	74	74	73	71
CEM Peer group average	77	78	78	74
CEM Canadian participants – average	70	69	70	68

Sources: CEM Benchmarking Reports, CEM Benchmarking Inc.

Key performance indicators

Performance indicators change to reflect evolving service delivery approaches. For example, the Same-Day Service indicator will likely become less important as use of online services predominates. Our results demonstrate that we are improving performance for targeted aspects of service delivery every year.

Other performance indicators

We monitor several other performance indicators to help us understand how well we are meeting members' expectations and increased demand for services. Other data indicates which services members are using and how well our broad strategies are working. As our interactions with members grow across our service platforms, we use a number of measurements to ensure that service quality is not only maintained, but continuously improved.

Member interactions totalled 395,000 last year, up 4% from the prior year. We completed 181,000 personal member requests, compared to 177,000 in the prior year, and responded to 63% within one day (65% in 2010). Our contact centre answers calls within an average of 24 seconds.

The proportion of total service provided to members through our secure *i*Access™ Web facility continues to grow. Members logged on for 218,000 web sessions last year, compared to 205,000 in 2010. Pension estimates and updates to personal information were the most frequently accessed online services.

SELF-SERVICE ACTIVITIES ON *i*Access™ WEB
(for the year ended December 31, 2011)

97,200 Pension Estimates
46,700 Changes in Personal Information
35,500 E-statement Interactive Viewings
3,900 Pension Applications

Plan Governance

"Governance links decision-making authority with accountability, and ensures that those managing the organization are capable and fairly compensated and that management interests are properly aligned with the interests of those they serve."

MELISSA KENNEDY, ICD.D
GENERAL COUNSEL, CORPORATE SECRETARY AND SENIOR VICE-PRESIDENT, CORPORATE AFFAIRS

MARCIA MENDES-D'ABREU, M.Sc.
VICE-PRESIDENT, HUMAN RESOURCES

As an investor, we believe that good governance is good business because it helps companies deliver long-term shareholder value. As a plan administrator, we measure ourselves against standards for governance, internal controls and Enterprise Risk Management that reflect corporate best practices and high standards of stewardship.

Governance involves a system of checks and balances to help ensure that an organization pursues its mission in a legal, responsible and effective manner. It links decision-making authority with accountability, and ensures that those managing the organization are capable and fairly compensated and that management interests are properly aligned with the interests of those they serve. Governance also ensures that the organization identifies and addresses the myriad risks it might face.

STRONG GOVERNANCE PRACTICES

Teachers' governance structure plays a crucial role in the organization's success. Since its inception in 1990, Teachers' has been overseen by independent board members comprising professionals who have demonstrated a commitment to the best stewardship practices in every area of plan governance. The board members have consistently set the tone from the top for an innovative and successful investment program and have supported a commitment to excellence in service delivery.

Board member composition and independence

The pension plan is overseen by nine board members. Four board members are appointed by each of the plan's two sponsors – the Ontario government and Ontario Teachers' Federation (OTF). Both sponsors jointly appoint the board's chair. Board members are appointed for staggered two-year terms and can serve up to a maximum of four consecutive terms. This process ensures that the plan sponsors consider the qualifications and effectiveness of individual board members on an ongoing basis.

The plan's governance structure assigns roles to the plan sponsors and the independent board members who are appointed to oversee management's decisions and actions.

Board members act independently of the plan sponsors and management to make decisions in the best interests of all beneficiaries of the plan. The structure of the board, and the process for appointing its members, ensures that board members are able to operate independently of management. For example, the roles of the chair and the Chief Executive Officer (CEO) are separated and no member of management can be a board member. The board members meet regularly without management present and, when needed, obtain advice from external advisors in order to foster independent views on key board decisions. The board is required to retain external actuarial and audit experts.

Board member qualifications

Board members are drawn from the fields of business management, finance and investment management, actuarial science, economics, education and accounting. They possess extensive experience in a wide range of the disciplines necessary to oversee a complex pension plan. Teachers' is a founding sponsor and strong supporter of the Directors Education Program, which was jointly developed by the Institute of Corporate Directors (ICD) and the Rotman International Centre for Pension Management (ICPM), University of Toronto, to improve board governance in Canada. Enrolment is offered to board members as part of their education program. The new ICPM pension directors course is also offered to all board members. Board Chair Eileen Mercier is a leader in Canada's corporate governance community and is a Fellow of the ICD. The ICD annually confers Fellowship Awards on individuals who bring exceptional corporate governance leadership to boardrooms throughout the country.

Effective oversight

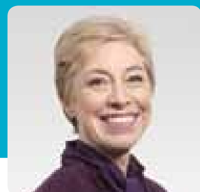
The board members are highly engaged in all aspects of plan oversight. Board members have high attendance levels and arrive at meetings well prepared to probe and engage in vigorous discussions. The board members oversee all aspects of the plan through five committees: Investment, Audit & Actuarial, Human Resources & Compensation, Governance and Benefits Adjudication. All board members serve on the Investment Committee.

The board's mandate, committee structure and terms of reference, as well as Teachers' Code of Conduct, are available on our website. Board member remuneration is discussed on page 76.

BOARD MEMBERS

Board and committee meeting attendance was 97% in 2011. For more information on board members and board committees, please see our website (otpp.com).

Two new members joined the board after the retirement of Helen Kearns and Louis Martel, who had served since 2005 and 2007 respectively. Ms. Kearns was Vice-Chair of the Benefits Adjudication Committee and Mr. Martel chaired the Human Resources & Compensation Committee. Patricia Anderson and Barbara Palk were appointed to the board in January 2012. Some committee responsibilities were re-assigned as a result of these changes.



Eileen Mercier

Board member, several public companies; Fellow, Institute of Canadian Bankers and the Institute of Corporate Directors

Chair

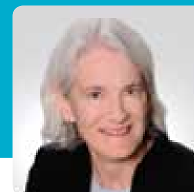
Appointed 2005; Chair since 2007
Attendance 94%

Rod Albert

Former President, Ontario Teachers' Federation

Benefits Adjudication and Audit & Actuarial Committees*

Appointed 2010
Attendance 100%



Patricia Anderson

Member, Arts & Science Advisory Council, Queen's University; Chair, Aldeburgh Connection; Former Chair, SickKids Foundation, and the Corporation of Roy Thomson Hall and Massey Hall

Audit & Actuarial and Governance Committees

Appointed 2012
Attendance n/a

Hugh Mackenzie

Principal, Hugh Mackenzie and Associates; Chair, Atkinson Foundation; ICD.D

Human Resources & Compensation and Governance Committees*

Appointed 2007
Attendance 100%

Barbara Palk

Board member, TD Asset Management USA Funds Inc.; Former President, TD Asset Management Inc.; Former Governance Chair, Canadian Coalition for Good Governance; ICD.D, CFA

*Benefits Adjudication**, Audit & Actuarial and Governance Committees*

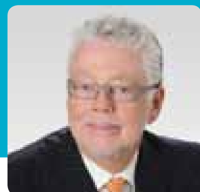
Appointed 2012
Attendance n/a

Sharon Sallows

Partner, Ryegate Capital Corp.; Former Senior Vice-President, Bank of Montreal; Board member, Chartwell Seniors Housing REIT and RioCan Real Estate Investment Trust; ICD.D

Human Resources & Compensation and Governance Committees*

Appointed 2007
Attendance 96%

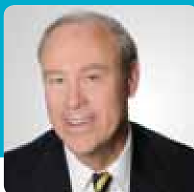


David Smith

Former Chair and Senior Partner, PricewaterhouseCoopers; Former President and CEO, Canadian Institute of Chartered Accountants; Chair, Government of Canada's Audit Committee; FCA, ICD.D

Audit & Actuarial and Human Resources & Compensation Committees*

Appointed 2009
Attendance 100%



Daniel Sullivan

Former Consul General of Canada in New York; Former Deputy Chairman, Scotia Capital; ICD.D

Human Resources & Compensation and Governance Committees

Appointed 2010
Attendance 92%

Jean Turmel

President, Perseus Capital Inc.; Former President, Financial Markets, Treasury and Investment Bank, National Bank of Canada

Investment, Audit & Actuarial and Human Resources & Compensation Committees*

Appointed 2007
Attendance 96%

*Committee Chair **Committee Vice-Chair

BOARD MEMBER RESPONSIBILITIES

Board members are responsible for overseeing the management of the pension plan. They delegate the day-to-day investment of the plan's assets to the CEO, who has the authority to sub-delegate. The board members and plan management are responsible for investment decision-making. The plan sponsors are not involved in investment decisions. Board members are responsible for approving strategic plans and budgets, investment policies, risk appetite and asset mix, benchmarks, performance and compensation, succession planning and monitoring enterprise-wide risks. In addition, they oversee annual performance objectives for the investment portfolio and review transactions that exceed limits set by the board for management. The collective wisdom of a group that is expert in financial matters, and yet removed from the day-to-day clamour of the markets, is an invaluable resource in the decision-making and approval process for strategic recommendations and significant investments.

Finally, the board must conduct regular funding valuations for the pension plan to assess its long-term financial health. The board sets key actuarial assumptions for these valuations (with input from the plan sponsors and plan actuary) and considers the Funding Management Policy that guides the plan sponsors' decisions on when to use surplus funds and how to address funding shortfalls. The board is responsible for reporting the plan's funding status to the plan sponsors. The board members review and approve Management's Discussion & Analysis in the annual report and approve the audited financial statements.

Board member activities

Board members met 13 times in 2011 for board and Investment Committee meetings. In addition, the Governance Committee met three times; the Human Resources & Compensation Committee met eight times; the Audit & Actuarial Committee met seven times; and the Benefits Adjudication Committee held three general meetings. Board members also spent considerable time working with the plan sponsors to file a balanced funding valuation with the pension regulator in 2011. All regularly scheduled meetings of the board, the Audit & Actuarial Committee and the Human Resources & Compensation Committee included sessions without management present.

The Governance Committee revised the CEO evaluation process during 2011, and a subcommittee of the board is working on the CEO succession plan.

As part of its commitment to effective governance and based on feedback garnered in the 2010 board self-assessment survey, the board members have enhanced their meeting processes. Board members reviewed the type and quantity of information needed to fulfill their oversight function, how often they met, how meetings were organized, how much time was available for in-depth discussion of strategic matters, and board member education.

In light of the increasing complexity of the fund's portfolio, board members receive timely investment status reports. For example, reports on enterprise risks inform board members of rapidly growing or critical risks.

Experts on key investment- and economic-related topics were invited to speak to board members last year to ensure they were well briefed on matters of key importance, such as emerging markets. Additional speakers are planned in 2012. Board members will conduct an offsite meeting next September as an integral part of the 2013 planning process and will consider broad strategic direction and pension stewardship issues outside the demands of regular board meetings.

The board also reviewed and adopted a new Code of Conduct for the pension plan last year. Teachers' three existing codes of conduct, which applied to different groups, were condensed into a single, four-page document that applies to board members and all employees. (A further three-page appendix applies to those subject to trading restrictions.) The new code is easier to understand and encourages application of the highest standards of business conduct. Long-standing employment policies, such as respect in the workplace, are now codified in this document, making it a more holistic, yet concise, expression of the behaviour Teachers' expects from its employees and board members. All board members and employees have signed off on the new code, which took effect at the beginning of 2012 and is available on our website.

EFFECTIVE OVERSIGHT AND CONTROLS

Management is responsible for establishing corporate strategy, objectives and an annual financial plan. Board members review progress against management's stated objectives and confirm that management's strategies and decisions are in the best interests of all pension beneficiaries. They also help ensure that management can attract and retain the best available staff. The more senior the management position, the more directly involved the board members are in their recruitment.

Board members must ensure that the organization's standards are respected and that its policies and procedures are appropriate and complied with. Supporting these responsibilities is an internal audit function that reports directly to the Audit & Actuarial Committee. The plan's Enterprise Risk Management framework and internal controls are also important elements of its governance structure.

Enterprise Risk Management (ERM)

The pension plan is exposed to a number of risks that have the potential to cause losses or other undesirable outcomes. The purpose of ERM is to ensure that risks are managed as effectively as possible. It provides a framework to identify and assess risks (investment and non-investment) facing the organization and to employ risk mitigating strategies, when appropriate, to address them.

Accountability and risk consciousness are core values for our employees.

The importance of risk awareness is embedded in Teachers' Mission, Vision and Values statement, which highlights "accountability and risk consciousness" as one of six core values for all employees. Teachers' ERM Policy recognizes that risk is present in all of our activities and states our commitment to ensure that risk management is a core focus across the organization. The policy establishes a process through which employees identify, manage, measure and report risks, and it serves as the decisive governance document for all at-risk activities.

The ERM framework is implemented by an executive-level committee that is chaired by the CEO and made up of the heads of all divisions and corporate support departments. A cross-organizational working committee supports the ERM Committee by implementing, documenting and communicating Teachers' ERM activities in a consistent manner throughout the organization. A formal annual risk assessment of the organization's risks is delivered to board members, with a mid-year update on top risks. Top risks are also reported internally to all employees through Teachers' intranet in order to increase risk awareness and encourage employees to think actively about the potential risks that could emerge in their departments.

We have strengthened our ERM framework in recent years. We improved our assessment process to identify risk events more precisely, and added specific tolerance levels for escalating issues to the ERM Committee and board members. We have also developed the Operational Excellence program – a multi-year program aimed at improving our organizational coordination and data governance, strengthening our risk management and adopting a more disciplined approach to process improvement. The program consists of some 15 projects, which will be completed over the next four years. In 2012, our program includes projects to replace a key investment risk system, improve data governance and investment systems architecture, and streamline and automate key processes. These are designed to improve the foundational business architecture of Teachers' and ultimately reduce operational risk.

Our Risk Culture Survey, conducted by a third party, analyzed our current environment by exploring 11 dimensions of risk. The survey identified specific areas of risk consciousness to focus on. As of 2011, questions about risk consciousness are now included in biennial employee surveys. This provides a measure of how well this value is instilled in employees and whether it needs to be strengthened. Based on the survey results, in 2012, we have an objective of improving two-way communication to encourage employees to discuss issues and mitigate risks. Every employee at every level will include at least one objective on their performance plan to improve two-way communication.

Disclosure controls and procedures, and internal control over financial reporting

The plan is not required to comply with National Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings, issued by the Canadian Securities Administrators, but we have voluntarily chosen to meet these standards as part of our commitment to good governance practices.

The President and CEO, and the Senior Vice-President and Chief Financial Officer (CFO), are responsible for establishing and maintaining disclosure controls and procedures, and internal control over financial reporting. We have designed disclosure controls and procedures to provide reasonable assurance that material information relating to the plan is gathered and reported to management in order to allow timely decisions regarding public disclosure. We have evaluated the effectiveness of our disclosure controls and procedures and concluded as at December 31, 2011, that they are effective.

We have also designed internal control over financial reporting, using the Integrated Framework issued by the Treadway Commission's Committee of Sponsoring Organizations (the COSO Framework), to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian generally accepted accounting principles. We have evaluated the effectiveness of the plan's internal controls over financial reporting and concluded they are effective as at year end. There were no changes in our internal control over financial reporting in 2011 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. The implementation of CICA Handbook Section 4600 in 2011 did not materially change the plan's internal control over financial reporting.

Protecting audit integrity

Teachers' and other corporate governance advocates have expressed concern over the years about accounting firms that audit public companies and also earn substantial revenue from those companies for non-audit consulting services. We believe that such consulting fees can compromise, or at least appear to compromise, the integrity of the audit function. As such, we have a policy for governing the nature and extent of non-audit consulting fees for the plan, its subsidiaries and joint ventures with oversight by the Audit & Actuarial Committee.

We strive to minimize our own use of consulting services involving the plan's auditors, and we always disclose the total amount paid for such services. In 2011, fees paid to Deloitte & Touche LLP, the plan's auditors, totalled $7.7 million ($7.2 million in 2010), of which $5.3 million was for audit activities and $2.4 million was for non-audit services. Of the $2.4 million paid for non-audit services, $0.1 million related to the plan, and the balance was for some of the plan's subsidiaries.

Transparent reporting

Teachers' board members receive regular reports from management on the financial and funding positions of the plan, investment performance, regulatory compliance, risk levels, client satisfaction ratings and key Member Services statistics. They also receive regular reports concerning the performance of each investment department, internal controls, enterprise risk, enterprise projects and all other significant events.

We also strive to keep stakeholders fully informed about the plan's services, investments, funding status and challenges by undertaking the following communication activities:

- In addition to publishing this annual report, an annual performance summary for plan members and annual pension statements, Teachers' delivers pension-related news electronically to members as it happens and provides regular newsletters to active teachers and pensioners. A separate website – FundingYourPension.com – was developed in partnership with the plan sponsors to explain the plan's persistent funding challenges through a series of webcasts, presentations, fact sheets, reports and questions and answers.
- Through these channels, we inform members of plan provisions and services, and update them on plan changes, funding challenges, investment news and other important information.

- Teachers' corporate website (otpp.com) details plan governance practices and facts about our investment strategy and major portfolios, as well as service initiatives and recent news. A new section of the site dedicated to the plan's approach to responsible investing was expanded in 2011.
- Each April, Teachers' holds an annual meeting that is open to the plan sponsors and all plan members. It will be held in Toronto on Thursday, April 12, 2012, at 5 p.m. A webcast will be available (live and archived for later viewing) for the convenience of members who live outside the Toronto area. Video highlights of the annual meeting and questions from plan members will be posted on otpp.com after the meeting.
- The board Chair addresses the OTF Board of Governors three times annually. Management has regular meetings with the Partners' Committee and the Partners' Consultative Committee, and takes part in discussions with the plan's and sponsors' actuaries. The Partners' Consultative Committee was reconstituted with broader representation after the Sustainability Working Group concluded its work in 2010. This change keeps representatives of both plan sponsors better informed of the plan's evolving funding status throughout each year. The Funding Education Group works with the Partners' Consultative Committee to ensure consistent communication about funding. The Demographic Task Force is a tri-party group that is reviewing and proposing changes to the demographic assumptions of the plan. The Technical Group, which consists of the board's external actuary, and actuarial and other technical staff and consultants identified by the sponsors, discusses best-estimate, non-economic assumptions related to the preliminary valuation.

Adoption of CICA Handbook Section 4600

Effective January 1, 2011, Teachers' implemented CICA Handbook Section 4600, which provides specific accounting guidance on pension obligations, fair value measurement of investments and risk management disclosure. For accounting policies not related to investments or pension obligations, a pension plan is required to elect consistently either International Financial Reporting Standards (IFRS) or Canadian accounting standards for private enterprises. Teachers' elected to apply IFRS. IFRS is mandatory for all public companies in Canada. Although the plan is not a publicly traded entity, our audited financial statements are posted on our website and accessible by the public. Through the adoption of IFRS, our financial statements will be comparable with other Canadian pension funds that have adopted IFRS, with current and future investee companies, and with investment partners that have adopted IFRS. Further information is provided in Notes 1a and 1b to the financial statements.

COMPENSATION DISCUSSION AND ANALYSIS

The Compensation Discussion & Analysis explains Teachers' approach to compensation, the various elements of our pay programs and the remuneration paid to our named executive officers. In fiscal 2011 our named executives were:

Jim Leech, President and CEO;

David McGraw, Senior Vice-President (SVP) and CFO;

Neil Petroff, Executive Vice-President (EVP), Investments;

Ron Mock, SVP, Fixed Income and Alternative Investments; and

Wayne Kozun, SVP, Public Equities.

Our compensation framework

Compensation philosophy and objectives

Teachers' compensation framework has been developed on a foundation of pay-for-performance. Our compensation programs consist of base salary, annual incentives, and long-term incentives and are structured to ensure that there is direct alignment between Teachers' total-fund net value added (after expenses) and the compensation paid to senior management.

Our philosophy and pay practices are based upon the following key objectives:

- attracting and retaining high-calibre employees;
- motivating and rewarding top performance, encouraging teamwork, aligning personal and organizational objectives and rewarding successful performance over the long term;
- measuring and monitoring our investment incentive compensation framework relative to our risk budget and ensuring our compensation programs do not encourage excessive risk-taking; and
- targeting total direct compensation (base salary, annual incentive, and long-term incentive) at the median of our peers. Exceptional performance at the total-fund, asset-class, divisional and corporate level will result in top-quartile pay relative to our peers, while performance below board-approved financial and operational targets results in pay below median levels.

Benchmarking process

Given the varied employment opportunities at Teachers', executive and non-executive positions are compared against relevant job groups and incentive programs in like markets. Our objective is to be competitive with those organizations against which we compete directly for talent. These organizations include other major Canadian pension funds, banks, insurance companies, and investment managers. For certain positions, we also compare to the general financial industry in Canada as well as U.S. and U.K. investment management organizations.

Design principles

The key design principle impacting each employee's incentive pay, at varying degrees, is our risk budget. At the beginning of each year, board members approve the active risk allocations for the total fund and each investment department, which in turn establish expected annual dollar value-added performance goals (i.e., dollars earned versus benchmark dollars earned) for the year. The greater the risk allocation for a department, the greater the value-added target to be achieved. Actual investment performance at the total-fund and departmental levels (measured in dollars of value added after expenses) is compared against the target for adding value above the benchmark. The Annual Incentive Plan (AIP) is based upon this value-added performance measured over two consecutive years. The Long-term Incentive Plan (LTIP) measures the annual total-fund net value added (after expenses), a percentage of which is allocated to reward employees over time. Additional measures used to monitor, assess and mitigate risk in our incentive programs include:

- setting an upper limit on annual incentive payments;
- modelling and testing our AIP and LTIP under multiple performance scenarios in order to ensure that the payouts align with expected performance outcomes;
- comprehensive balanced scorecards that measure progress against strategic objectives across each division/department including risk management initiatives; and
- clawback provisions stating that employees committing willful acts of dishonesty, fraud or theft shall be required to pay back to Teachers' all amounts paid to the participant under the AIP or LTIP.

Independent advisors

In 2011, board members retained the services of McLagan, an independent compensation consultant, and Eckler Ltd., an independent actuarial and pension consultant, to advise the board on executive compensation and pensions respectively.

Elements of our compensation program – Overview

The table below summarizes the elements of Teachers' compensation program[1].

Element	Purpose	Primary Performance Drivers	Variability with Performance	Applicability
Base Salary	Compensates employees commensurate with their demonstrated skills, knowledge and level of performance	Position description and individual proficiency	Low	All employees
Annual Incentive	Rewards employees for their contribution to the achievement of Teachers' results, divisional results, and their individual level of performance	Teachers', divisional, and individual performance	Moderate	All employees
		Investment value-added performance	High	Investment employees
Long-term Incentive	Designed to reward participating employees for the delivery of total-fund net value-added (after expenses) and positive actual returns, net of costs, over the long term	Total-fund value-added and actual returns	High	Investment employees at the assistant portfolio manager level and above Corporate and Member Services employees at the director level and above

[1] Compensation structures for bargaining unit staff have been negotiated into the collective agreement. The four-year agreement runs through to December 31, 2013.

Mix of pay

Investment, Corporate, and Member Services employees have different percentages of their compensation tied to our variable pay programs. Recognizing their direct influence on investment results, investment professionals, including our CEO, have a greater percentage of their total direct compensation (base salary, annual incentive, and long-term incentive) tied to our variable pay programs. Detailed below is the target total direct compensation mix for our named executive officers. The actual pay mix realized may be different depending upon Teachers' corporate and investment performance and the named executive officers' individual performance.

		Variable		
Position	**Base Salary**	**Annual Incentive**	**Long-term Incentive**	**% of Target Total Compensation Which Is Variable**
President and CEO	25%	37.5%	37.5%	75%
SVP and CFO	45%	27.5%	27.5%	55%
EVP, Investments	25%	37.5%	37.5%	75%
SVP, Investments	27%	33%	40%	73%

Base salary

Base salaries compensate employees for fulfilling their day-to-day responsibilities. Each employee at Teachers' is assigned a job level with a corresponding salary grade that is designed to provide market-competitive pay commensurate with the employee's responsibilities, demonstrated skills, knowledge and track record of performance.

Base salaries are reviewed annually, and salaries for vice-presidents and above are approved by the board members.

Annual Incentive Plan (AIP)

Our AIP rewards employees with cash awards based on business and individual performance results relative to pre-approved financial and non-financial measures. All non-union employees participate in the AIP. Weightings for each element vary for Investment, Corporate and Member Services employees. Detailed below are the components by which our named executive officers' performances are measured within the AIP:

Performance Measure	President and CEO	SVP and CFO	EVP, Investments	SVP, Investments
Teachers' Performance – Measured annually based on a company-wide scorecard that includes investment and non-investment measures	✓	✓	✓	✓
Division/Department Performance – Measured annually based on specific divisional scorecards		✓	✓	✓
Two-Year Total-Fund Performance – Value-added performance (after expenses) measured over two full calendar years relative to return on risk targets	✓		✓	✓
Two-Year Investment Department Performance – Pool of incentive dollars determined by net value-added dollars (after expenses) earned relative to the return required on the two-year risk allocation for that department; discretionary allocation based on individual performance				✓
Individual Performance – Based on the employee's performance against specific objectives established at the beginning of the calendar year	✓	✓	✓	✓

Deferred Incentive Plan (DIP)

Employees can choose to allocate all or a portion of their AIP payment to either a Total-Fund Plan or a Private Capital Plan, or a combination of the two, for up to two years. The deferred amount will increase or decrease in value over the two-year deferral period based on actual rates of return of the respective plan.

Long-Term Incentive Plan (LTIP)

Our LTIP is designed to reward participating employees for delivering total-fund net value added (after expenses) and positive actual returns, net of costs, over the long term. When total-fund net value added (after expenses) is positive, participants share in the positive gains; conversely, when total-fund net value added (after expenses) is negative, participants share in the loss. Each year, a small percentage of the year's total-fund net value added (after expenses) will fund an LTIP pool, which is allocated to participating employees' notional accounts. For these purposes, annual total-fund net value added (after expenses) can be positive or negative. There is no upper or lower limit on total-fund net value added (after expenses). In years when total-fund net value added (after expenses) is negative, participating employee accounts will be reduced accordingly; individual employee accounts cannot be reduced below zero. Individual LTIP accounts are adjusted in December based on the total-fund actual rate of return. For employees who participate in a previous LTIP (pre-2010), payments from that plan will also be transferred into the individual account as they crystallize at the end of each performance cycle. Each April, following the allocation related to the previous performance year, 25% of individual account balances are paid to eligible employees.

Benefits and other compensation

Teachers' provides a competitive benefit program that includes life insurance, disability, health and dental benefits, vacation and other leave policies and an Employee Assistance Program. Teachers' retirement benefit for employees is a defined benefit pension plan described on page 75.

Executive employment contracts

There are no executive employment contracts or severance guarantees in place.

Compensation decisions made in 2012 reflecting 2011

How decisions are made

Each year, the Human Resources & Compensation Committee of the board reviews compensation policies, including incentive components linked to corporate, investment and total-fund performance. In addition, the committee reviews:

- the achievement of the performance measures for the President and CEO and other senior officers;
- the total direct compensation of the President and CEO and recommends to the board members for approval; and,
- the total direct compensation for other senior officers as recommended by the President and CEO and recommends to the board members for approval.

Total direct compensation provides a view to compensation decisions that relate directly to the performance period.

The committee's review is supported by total direct compensation market data for similar investment and non-investment positions in our peer group. As previously noted, Teachers' board members approve at the beginning of each year the annual dollar value-added performance goals (i.e., dollars earned versus benchmark dollars earned) used to measure and determine investment incentive compensation for the year.

2011 performance results

Teachers' overall performance – Annual Incentive Plan

Each year, the executive team establishes enterprise and divisional objectives for the year. All employees are aligned with individual objectives to support the enterprise and/or divisional objectives. The enterprise objectives, which are approved by board members, include a measure of the rate of return, dollars of value added (i.e., dollars earned after costs versus benchmark dollars earned) and service quality in relation to expenses as well as significant strategic initiatives.

Quarterly, performance against enterprise and divisional objectives is assessed and a scorecard is prepared. The scorecard provides a visual snapshot of the overall level of performance achieved.

As illustrated in the scorecard below, for 2011, we were able to meet or exceed target goals for each of the enterprise objectives. The result is above-target performance with an incentive multiplier of 1.78 out of 2.

	Objective	Measure	Actual	Goal	Achieved
Customers	Outstanding service to members	Quality Service Index	8.98	> 8.6	Above target
	Retirement security	Value-added returns	$1.21 billion[1]	$720 million[1]	Above target
		Absolute returns	>10%	3.75% real returns	Above target
		Desensitizing to real interest rates	24%	20% to 28% real-rate exposure	Above target
	Informed partners	Executive assessment against plan	Complete	Complete plan	Above target
Financial	Cost effectiveness	Actual versus budget	Meets	Meet approved budget	Target
		Approved cost allocation and process	Complete	Improve cost transparency and allocation process	Above target
Internal Processes	Operational excellence	Planned initiatives	Complete	Complete plan	Above target
	Manage enterprise risk	Enterprise Risk Management assessment score	25% risk reduction	Reduce gap of top risks by 20%	Above target
Learning & Growth	Engaged employees	Employee survey results	Complete	Develop plan to respond to the survey	Above target
		Leadership program	Complete	Develop effective leadership program	Above target

[1] Net of expenses.

Two-year total-fund investment performance

The table below summarizes, at the total-fund level, the net value-added performance (after expenses) for 2010 and 2011 relative to the return on risk targets less cost allowance. For 2010 and 2011 we outperformed our target total-fund net value added (after expenses) of $1.45 billion by $3.55 billion, resulting in the maximum performance multiplier of 2.0x target.

Year	Total-Fund Net Value Added	Target[1]	Above Target[2]	Multiplier
2010	$3.79 billion	$0.73 billion	$1.47 billion	5.16x
2011	$1.21 billion	$0.72 billion	$1.44 billion	1.67x
2010 and 2011	$5.00 billion	$1.45 billion	$2.91 billion	2.0x (maximum)

[1] Target total-fund investment performance for 2011 is 9.6% return on risk less a cost allowance of 17 basis points.

[2] Above-target total-fund investment performance for 2011 is 19.2% return on risk less a cost allowance of 34 basis points.

Two-year investment department performance

The table below summarizes performance in terms of net value-added dollars (after expenses) earned relative to the return required on the two-year risk allocation for each of the respective investment departments listed below:

Year	Public Equities	Private Capital	Infrastructure and Timberland	Fixed Income and Alternatives	Tactical Asset Allocation
2010 and 2011	Below target	Significantly exceeded target	Above target	Significantly exceeded target	Below target

Investment performance – Long-Term Incentive Plan

In 2011, the total-fund net value-added performance (after expenses) was equal to $1.21 billion, resulting in an aggregate LTIP pool for distribution of $33.1 million. Notional deposits were made to eligible participants effective January 1, 2012.

Year	Total-Fund Net Value Added	Performance	Aggregate LTIP Notional Deposits
2010	$3.79 billion	Significantly exceeded target	$74.8 million
2011	$1.21 billion	Above target	$33.1 million

Executive compensation

The compensation table represents disclosure of base salary, annual incentive, long-term incentive and other compensation earned in 2009, 2010 and 2011 by the CEO, the CFO and the three other most highly compensated executives, excluding subsidiary companies.

Name and Principal Position	Year	Base Salary A	Annual Incentive B	Long-term Incentive Allocation C	Long-term Incentive Paid[1] D	Other[2] E	Change in Pension Value	Total Direct Compensation[3] A+B+C	Total Compensation[4] A+B+D+E
Jim Leech	2011	$523,077	$1,470,800	$1,350,000	$2,381,000	$2,938	$217,900	**$3,343,877**	$4,377,815
President and CEO	2010	500,000	1,400,000	3,500,000	2,011,900	10,440		**5,400,000**	3,922,340
	2009	500,000	706,300	2,800,000	1,098,200	10,455		**4,006,300**	2,314,955
David McGraw	2011	311,538	315,000	290,000	477,700	466	96,700	**916,538**	1,104,704
SVP and CFO	2010	300,058	285,000	670,000	394,700	7,075		**1,255,058**	986,833
	2009	285,000	144,600	580,000	169,700	7,612		**1,009,600**	606,912
Neil Petroff	2011	419,231	1,180,000	1,250,000	1,896,000	627	305,900	**2,849,231**	3,495,858
EVP, Investments	2010	400,192	1,120,000	3,000,000	1,645,200	651		**4,520,192**	3,166,043
	2009	350,000	581,000	2,400,000	751,200	592		**3,331,000**	1,682,792
Ron Mock	2011	295,385	743,400	800,000	1,405,300	442	152,000	**1,838,785**	2,444,527
SVP, Fixed Income and	2010	280,192	696,400	2,400,000	1,232,800	449		**3,376,592**	2,209,841
Alternative Investments	2009	230,000	460,000	1,750,000	537,300	9,239		**2,440,000**	1,236,539
Wayne Kozun	2011	305,769	509,500	700,000	1,465,600	458	(16,300)	**1,515,269**	2,281,327
SVP, Public Equities	2010	300,216	729,200	2,300,000	1,296,700	480		**3,329,416**	2,326,596
	2009	243,800	487,600	1,950,000	581,100	417		**2,681,400**	1,312,917

[1] A new LTIP program was introduced in 2010. Amounts payable relating to the previous program will be transferred to the participant's notional account balance under the new program as they crystallize at the end of each performance cycle. Effective January 1, 2012, amounts payable for the performance cycle 2008–2011 were added to notional account balances for participating individuals. Each participant is eligible for a payment equal to 25% of his or her account under the new program in April 2012.

[2] Other compensation includes one or more of the following: group term life insurance, automobile allowance and unused vacation cashout. The automobile allowance was discontinued in April 2011.

[3] When making compensation decisions, the board and management focus on Total Direct Compensation (TDC) which reflects base salary, annual incentive and long-term incentive allocation.

[4] Change in pension value is not included in total compensation.

Notional account balances

The table below outlines the notional account balances for each of our named executives.

Notional Account Activity

Name and Principal Position	Opening Balance	2011 Rate of Return	January 1, 2012 Allocation	Transfer from Prior LTIP	2012 Payment	Balance
Jim Leech *President and CEO*	$6,035,600	11.2%	$1,350,000	$1,460,800	$2,381,000	$7,143,000
David McGraw *SVP and CFO*	1,183,900	11.2%	290,000	303,900	477,700	1,433,000
Neil Petroff *EVP, Investments*	4,935,800	11.2%	1,250,000	844,000	1,896,000	5,688,000
Ron Mock *SVP, Fixed Income and Alternative Investments*	3,698,200	11.2%	800,000	707,700	1,405,300	4,215,800
Wayne Kozun *SVP, Public Equities*	3,889,900	11.2%	700,000	835,600	1,465,600	4,396,700

Retirement benefits

Teachers' employees participate in the Public Service Pension Plan (PSPP), OPSEU Pension Plan, and the Public Service Supplementary Plan (PSSP). Combined, these plans provide indexed pension benefits equal to 2% of the employee's best five-year average annual base salary for each year of service, less a Canada Pension Plan (CPP) integration formula. Benefits under these combined plans are capped by the base salary reached at the maximum pension contribution permitted under Income Tax Act (ITA) regulations.

Employees with 2011 pensionable earnings in excess of $191,100 also participate in a non-registered, unfunded Supplemental Employee Retirement Plan (SERP). This plan provides non-indexed retirement benefits equal to 2% of the employee's average pensionable earnings for each year of service, less the initial annual pension to which the employee is entitled under the PSPP and PSSP, combined. For roles at the vice-president level or above, a portion of their annual incentive may be included as pensionable earnings.

In 2011 the board completed a review of the SERP and made certain adjustments that will affect participants going forward and will manage the SERP expense.

The total liability for the SERP increased by a net amount of $3.4 million in 2011 for a total accrued SERP liability of $27.3 million as at December 31, 2011.

The table below outlines the estimated present value of the total pension from all sources (PSPP, PSSP and SERP) and estimated annual pension benefits at age 65 for the CEO, the CFO and the three other most highly compensated executives, excluding subsidiary companies.

Name and Principal Position	Projected Years of Service at Age 65	Estimated Total Annual Pension Benefit at Age 65	Present Value of Total Pension at January 1, 2011	2011 Compensatory Annual Change in Pension Value	2011 Non-Compensatory[1] Annual Change in Pension Value	Present Value of Total Pension at December 31, 2011
Jim Leech *President and CEO*	11	$260,300	$3,260,200	$482,600	$(264,700)	$3,478,100
David McGraw *SVP and CFO*	17	170,400	716,000	123,500	(26,800)	812,700
Neil Petroff *EVP, Investments*	32	837,200	4,323,100	350,600	(44,700)	4,629,000
Ron Mock *SVP, Fixed Income and Alternative Investments*	17	195,400	1,444,400	220,200	(68,200)	1,596,400
Wayne Kozun *SVP, Public Equities*	36	685,400	2,371,900	121,700	(138,000)	2,355,600

[1] Non-compensatory changes include interest on liabilities and impact of any assumption changes.

The values shown above are estimated based on assumptions and represent entitlements that may change over time.

Board and committee member remuneration

Each board member receives an annual retainer of $12,000, plus $12,000 as a member of the Investment Committee. The Chair of the Board receives an additional retainer of $100,000, and the Chairs of the Investment, Governance, Human Resources & Compensation, and Audit & Actuarial Committees receive additional retainers of $5,000 each.

Fees for committee and other eligible meetings are $1,200. Board meeting fees are combined with Investment Committee fees at $1,500 per day. The Chair of the Benefits Adjudication Committee receives an additional fee of $1,000 for each Benefits Adjudication Committee meeting or hearing attended to a maximum of five per year.

Board members are reimbursed for normal expenses for education programs, travel, meals and accommodation, as required. For 2011, these expenses totalled $64,500.

Board Member		Retainer and Chair Fee	Board Meetings	Committee Meetings	Meeting Fees	2011 Total Remuneration
Eileen Mercier	*Chair of the Board*	$124,000	9	28	$47,100	$171,100
Rod Albert		24,000	9	26	44,700	68,700
Helen Kearns	*Vice-Chair, Benefits Adjudication Committee*	24,000	9	22	39,900	63,900
Hugh Mackenzie	*Chair, Benefits Adjudication Committee*	25,000	9	22	39,900	64,900
Louis Martel[1]	*Chair, Human Resources & Compensation Committee*	21,750	7	19	33,300	55,050
Sharon Sallows	*Chair, Governance Committee*	29,000	9	25	43,500	72,500
David Smith	*Chair, Audit & Actuarial Committee*	29,000	9	30	49,500	78,500
Daniel Sullivan		24,000	8	23	39,600	63,600
Jean Turmel	*Chair, Investment Committee*	29,000	9	24	42,300	71,300

[1] Louis Martel resigned in September 2011.

The Governance Committee retained the Hay Group to review and benchmark board compensation. A revised structure will be in place for 2012.

LEGISLATIVE UPDATE

The pension plan must comply with provincial and federal legislation and investment regulations that govern and apply to registered pension plans in Ontario. The plan was affected by a record number of amendments approved by the plan sponsors and other pension reforms proposed or passed in 2011. Plan and regulatory changes have become more frequent due to significant changes to Ontario's pension legislation, which has increased our mandatory compliance activities.

Changes to the Teachers' Pension Act and Pension Benefits Act

Schedule 1 of the Teachers' Pension Act (TPA) was amended in 2011 to recognize plan changes made to address the 2011 funding shortfall, and to comply with the Ontario Pension Benefits Act (PBA) and the federal Income Tax Act (ITA).

To address the 2011 funding shortfall, the plan sponsors made changes to the pension plan that are detailed on page 18.

The Ontario government proclaimed amendments to the PBA and the Ontario Family Law Act relating to the division of pension assets for marital breakdowns (Bill 133), effective January 1, 2012. This reform is important for plan members and will impact our operations significantly. We support the government's efforts to simplify the complex rules for pension division and harmonize aspects of the PBA and the Family Law Act. We reviewed draft regulations for Bill 133 at length and submitted comments seeking clarifications for some provisions that would make the new pension division regime easier to administer for plan members.

Further compliance activities included changes related to the administration of survivor benefits (including same-sex survivor benefits for members who died prior to April 23, 1998), eligibility requirements to buy back credit for breaks in service, and clarification of plan rules for members on long-term income protection.

Pension reform

We strongly support ongoing efforts at the federal and provincial levels to achieve needed and productive pension reforms in Canada. Continuing its pension reform initiatives, the Ontario government released regulations last year relating to a solvency exemption for Jointly Sponsored Pension Plans (contained in Bill 120, passed in 2010). While the pension plan is now exempt from funding any deficiency on a solvency basis, new regulations included additional disclosure and certification requirements that affect the plan and our communications.

Bill 236, passed in May 2010, primarily addressed general administrative issues for pension plans, including better disclosure to pensioners, immediate vesting, grow-in benefits and other changes. This legislation will affect our operations substantially, and we will review regulations, expected sometime in 2012, to determine the impacts.

During 2011, the Financial Services Commission of Ontario (FSCO) proposed a new risk-based framework for regulating registered pension plans in Ontario. We support the initiative and expect to work with the regulator to consider our submission.

Investment regulations

The Ontario government included in its 2011 budget a new requirement for registered pension plans in Ontario to file their Statement of Investment Policies and Procedures with the FSCO and to disclose whether the policy addresses environmental, social and governance factors. We were already in compliance with this new requirement when it came into force.

Teachers' was an intervenor in the Supreme Court of Canada's reference on the proposed Securities Act that sought to establish a national securities regulator. As a significant participant in global capital markets, Teachers' supported the proposed Act, contending that Canada needs more efficient and transparent capital markets and that the current fragmentation of the Canadian regulatory system should be addressed. While the Court found in December 2011 that the proposed legislation was unconstitutional, we will continue to advocate for more consistency in Canadian regulatory policy and legislation, through a workable and constitutional regulatory model.

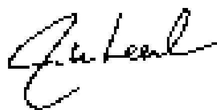
Management's Responsibility for Financial Reporting

The 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 financial statements conform to Canadian generally accepted accounting principles. Financial information presented throughout the annual report is consistent with the 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 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 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 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
MARCH 2, 2012

DAVID McGRAW
SENIOR VICE-PRESIDENT AND CHIEF FINANCIAL OFFICER

Auditor's Report to the Administrator

We have audited the accompanying financial statements of the Ontario Teachers' Pension Plan Board 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, statements of changes in accrued pension benefits, and statements of changes in deficit for the years ended December 31, 2011 and December 31, 2010, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Accounting Standards for Pension Plans, and for such internal controls as management determines are 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 audits. We conducted our audits 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 controls 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 controls. 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 in our audits 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 Ontario Teachers' Pension Plan Board as at December 31, 2011, December 31, 2010 and January 1, 2010, and its financial performance and changes in its net assets available for benefits, changes in accrued pension benefits and changes in deficit for the years ended December 31, 2011 and December 31, 2010 in accordance with Accounting Standards for Pension Plans.

Deloitte & Touche

CHARTERED ACCOUNTANTS
LICENSED PUBLIC ACCOUNTANTS
MARCH 2, 2012
TORONTO, ONTARIO

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, 2011, 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.

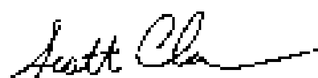
The valuation of the Plan's actuarial liabilities was based on:

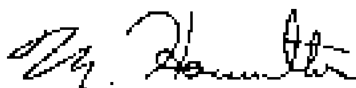
- membership data provided by the Ontario Teachers' Pension Plan Board as at August 31, 2011;
- methods prescribed by Section 4600 of the Canadian Institute of Chartered Accountants' Handbook for pension plan financial statements;
- real and nominal interest rates on long-term Canada bonds at the end of 2011;
- 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 2011/2012 school year.

The objective of the financial statements is to fairly present the financial position of the Plan on December 31, 2011 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 2011, 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 in Canada.





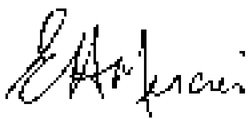
SCOTT CLAUSEN, F.C.I.A.
MARCH 2, 2012

MALCOLM P. HAMILTON, F.C.I.A.

Statements of Financial Position

(Canadian $ millions)	as at December 31 2011	as at December 31 2010	as at January 1 2010
Net Assets Available for Benefits			
Assets			
Cash	**$ 435**	$ 432	$ 493
Receivable from the Province of Ontario (note 3)	**2,717**	2,627	2,524
Receivable from brokers	**39**	101	93
Investments (note 2)	**156,563**	136,194	108,086
Premises and equipment	**37**	41	43
	159,791	139,395	111,239
Liabilities			
Accounts payable and accrued liabilities	**542**	250	181
Due to brokers	**1,847**	137	79
Investment-related liabilities (note 2)	**40,305**	31,473	14,577
	42,694	31,860	14,837
Net assets available for benefits	**$ 117,097**	$ 107,535	$ 96,402
Accrued pension benefits and deficit			
Accrued pension benefits (note 4)	**$ 162,587**	$ 146,893	$ 131,858
Deficit	**(45,490)**	(39,358)	(35,456)
Accrued pension benefits and deficit	**$ 117,097**	$ 107,535	$ 96,402

On behalf of the Plan Administrator:



Chair of the Board

Chair, Audit & Actuarial Committee

Statements of Changes in Net Assets Available for Benefits

for the year ended December 31 (Canadian $ millions)	2011	2010
Net assets available for benefits, beginning of year	**$ 107,535**	$ 96,402
Investment Operations		
Investment income (note 6)	**11,735**	13,269
Administrative expenses (note 11a)	**(289)**	(290)
Net investment operations	**11,446**	12,979
Member Service Operations		
Contributions (note 9)	**2,823**	2,697
Benefits paid (note 10)	**(4,663)**	(4,500)
Administrative expenses (note 11b)	**(44)**	(43)
Net member service operations	**(1,884)**	(1,846)
Increase in net assets available for benefits	**9,562**	11,133
Net assets available for benefits, end of year	**$ 117,097**	$ 107,535

Statements of Changes in Accrued Pension Benefits

for the year ended December 31 (Canadian $ millions)	2011	2010
Accrued pension benefits, beginning of year	**$ 146,893**	$ 131,858
Increase in Accrued Pension Benefits		
Interest on accrued pension benefits	**5,944**	6,057
Benefits accrued	**4,409**	3,354
Changes in actuarial assumptions and methods (note 4a)	**9,819**	10,440
Changes in plan provisions	**6**	–
Experience losses (note 4c)	**179**	–
	20,357	19,851
Decrease in Accrued Pension Benefits		
Benefits paid (note 10)	**4,663**	4,500
Experience gains (note 4c)	**–**	316
	4,663	4,816
Net increase in accrued pension benefits	**15,694**	15,035
Accrued pension benefits, end of year	**$ 162,587**	$ 146,893

Statements of Changes in Deficit

for the year ended December 31 (Canadian $ millions)	2011	2010
Deficit, beginning of year	**$ (39,358)**	$ (35,456)
Increase in net assets available for benefits	**9,562**	11,133
Net increase in accrued pension benefits	**(15,694)**	(15,035)
Deficit, end of year	**$ (45,490)**	$ (39,358)

Notes to Financial Statements

for the year ended December 31, 2011

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 Ontario Teachers' Federation (OTF) (the co-sponsors). The terms of the Plan are set out in Schedule 1 of the TPA.

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 in Canada. The Plan may be liable for taxes in other jurisdictions where full tax exemptions are not available.

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 employers. 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, subject to an upper limit of 8% and a lower limit of 0% in any one year with any excess above or below those limits carried forward. For credited service earned up to December 31, 2009, inflation protection is 100% of the change in the Consumer Price Index. Credited service earned after December 31, 2009 is subject to conditional inflation protection with a guaranteed level of inflation protection set at 50% of the change in the Consumer Price Index. Depending on the Plan's funded status as at the next filing, 100% inflation protection is possible and any years that did not receive full inflation protection can be restored to be fully indexed by the co-sponsors on a go-forward basis.

(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 $137,979 (CPP-exempt members $127,611) in 2011 and $134,811 (CPP-exempt members $124,722) in 2010; 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 financial statements.

Note 1.
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of presentation

These financial statements are prepared in Canadian dollars, the Plan's functional currency, in accordance with the accounting standards for pension plans in Part IV of the Canadian Institute of Chartered Accountants (CICA) Handbook (Section 4600). Section 4600 provides specific accounting guidance on investments and pension obligations. For accounting policies that do not relate to either investments or pension obligations, the Plan must consistently comply with either International Financial Reporting Standards (IFRS) in Part I or accounting for private enterprises in Part II of the CICA Handbook. The Plan has elected to comply with IFRS in Part I of the CICA Handbook commencing January 1, 2011. To the extent that IFRS in Part I is inconsistent with Section 4600, Section 4600 takes precedence.

Investment holding companies either acquired or created by the Plan are recognized as investment assets. Under Section 4600, investment assets, including those over which the Plan has control or has significant influence, are presented on a non-consolidated basis.

The financial statements for the year ended December 31, 2011 were authorized for issue through a resolution of the Board on March 2, 2012.

(b) Changes in accounting policies

These financial statements are the Plan's first in compliance with Section 4600 and IFRS. The comparatives as at January 1, 2010 and for the year ended December 31, 2010 have been restated accordingly. Prior to 2011, the financial statements were prepared in accordance with CICA Handbook Section 4100 – Pension Plans and Part V of the CICA Handbook.

The Plan has elected to early adopt IFRS 13, Fair Value Measurement, on a prospective basis, commencing January 1, 2010. The measurement requirements under IFRS 13 were applied consistently to the fair value of all investment assets and investment-related liabilities in the periods presented in the financial statements. The definition of fair value has been amended to comply with IFRS 13. There is no impact on the values of either investment assets or investment-related liabilities. As per Section 4600, the Plan is not required to comply with the disclosure requirements prescribed in IFRS 13.

The following accounting policies have been revised upon implementation of Section 4600 and IFRS:

Non-consolidation

Prior to the implementation of Section 4600, the Plan prepared consolidated financial statements. In accordance with Section 4600, the Plan presents investments on a non-consolidated basis. As a result of this requirement, investments and investment-related liabilities both decreased with no impact on net assets available for benefits.

Elimination of actuarial asset value adjustment

In accordance with Section 4100, the actuarial asset value adjustment was included in the determination of the financial statement surplus or deficit. As per Section 4600, the actuarial asset value adjustment is no longer permitted.

The tables on the following pages show the impact of these revised accounting policies on prior years' Statements of financial position and Statements of changes in deficit.

STATEMENT OF FINANCIAL POSITION

as at December 31, 2010 (Canadian $ millions)	As Previously Reported	Adjustments: Non-consolidation	Adjustments: Actuarial Asset Value Adjustment	**Revised per CICA Section 4600**
Assets				
Cash	$ 432	$ –	$ –	**$ 432**
Receivable from the Province of Ontario	2,627	–	–	**2,627**
Receivable from brokers	101	–	–	**101**
Investments	155,360	(19,166)	–	**136,194**
Premises and equipment	41	–	–	**41**
	158,561	(19,166)	–	**139,395**
Liabilities				
Accounts payable and accrued liabilities	250	–	–	**250**
Due to brokers	137	–	–	**137**
Investment-related liabilities	50,639	(19,166)	–	**31,473**
	51,026	(19,166)	–	**31,860**
Net assets available for benefits	$ 107,535	$ –	$ –	**$ 107,535**
Actuarial asset value adjustment	6,655	–	(6,655)	**–**
Actuarial value of net assets available for benefits	$ 114,190	$ –	$ (6,655)	**$ 107,535**
Accrued pension benefits and deficit				
Accrued pension benefits	$ 146,893	$ –	$ –	**$ 146,893**
Deficit	(32,703)	–	(6,655)	**(39,358)**
Accrued pension benefits and deficit	$ 114,190	$ –	$ (6,655)	**$ 107,535**

STATEMENT OF CHANGES IN DEFICIT

(Canadian $ millions)	As Previously Reported	Adjustments: Non-consolidation	Adjustments: Actuarial Asset Value Adjustment	**Revised per CICA Section 4600**
Deficit, January 1, 2010	$ (22,752)	$ –	$ (12,704)	**$ (35,456)**
Increase in net assets available for benefits	11,133	–	–	**11,133**
Change in actuarial asset value adjustment	(6,049)	–	6,049	**–**
Increase in actuarial value of net assets available for benefits	5,084	–	6,049	**11,133**
Net increase in accrued pension benefits	(15,035)	–	–	**(15,035)**
Deficit, December 31, 2010	$ (32,703)	$ –	$ (6,655)	**$ (39,358)**

OPENING STATEMENT OF FINANCIAL POSITION

as at January 1, 2010 (Canadian $ millions)	As Previously Reported	Adjustments: Non-consolidation	Adjustments: Actuarial Asset Value Adjustment	**Revised per CICA Section 4600**
Assets				
Cash	$ 493	$ –	$ –	**$ 493**
Receivable from the Province of Ontario	2,524	–	–	**2,524**
Receivable from brokers	93	–	–	**93**
Investments	123,900	(15,814)	–	**108,086**
Premises and equipment	43	–	–	**43**
	127,053	(15,814)	–	**111,239**
Liabilities				
Accounts payable and accrued liabilities	181	–	–	**181**
Due to brokers	79	–	–	**79**
Investment-related liabilities	30,391	(15,814)	–	**14,577**
	30,651	(15,814)	–	**14,837**
Net assets available for benefits	$ 96,402	$ –	$ –	**$ 96,402**
Actuarial asset value adjustment	12,704	–	(12,704)	**–**
Actuarial value of net assets available for benefits	$ 109,106	$ –	$ (12,704)	**$ 96,402**
Accrued pension benefits and deficit				
Accrued pension benefits	$ 131,858	$ –	$ –	**$ 131,858**
Deficit	(22,752)	–	(12,704)	**(35,456)**
Accrued pension benefits and deficit	$ 109,106	$ –	$ (12,704)	**$ 96,402**

STATEMENT OF CHANGES IN DEFICIT

(Canadian $ millions)	As Previously Reported	Adjustments: Non-consolidation	Adjustments: Actuarial Asset Value Adjustment	**Revised per CICA Section 4600**
Deficit, January 1, 2009	$ (11,184)	$ –	$ (19,524)	**$ (30,708)**
Increase in net assets available for benefits	8,969	–	–	**$8,969**
Change in actuarial asset value adjustment	(6,820)	–	6,820	**–**
Increase in actuarial value of net assets available for benefits	2,149	–	6,820	**8,969**
Net increase in accrued pension benefits	(13,717)	–	–	**(13,717)**
Deficit, January 1, 2010	$ (22,752)	$ –	$ (12,704)	**$ (35,456)**

The implementation of Section 4600 has no effect on either the statements of changes in net assets available for benefits or the statements of changes in accrued pension benefits for the year ended December 31, 2010.

(c) Future changes in accounting policies

The International Accounting Standards Board has issued a number of new and amended standards that are not yet effective as at December 31, 2011. The relevant new guidance not yet adopted by the Plan includes:

- IFRS 12, Disclosures of Interests in Other Entities and IAS 27, Separate Financial Statements. The new standards set out the required disclosures for interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. The new standards are effective for annual periods beginning on or after January 1, 2013 and early application is permitted.
- IFRS 9, Financial Instruments. The new standard will replace IAS 39, Financial Instruments: Recognition and Measurement and includes guidance on recognition and derecognition of financial assets and financial liabilities. The new standard is effective for annual periods beginning on or after January 1, 2015 and early application is permitted.

Management does not expect any significant impact on either the Plan's financial position or performance when adopting these new standards.

(d) Investments

Valuation of investments

Investments are either directly or indirectly owned by the Plan. Investment-related liabilities are incurred by the Plan directly. Details of investments and investment-related liabilities are presented in note 2a and are stated at fair value. Fair value is the price that would either be received to sell an asset or paid to transfer a liability in an orderly transaction (i.e., an exit price) between market participants at the measurement date. In an active market, fair value is best evidenced by an independent quoted market price. In the absence of an active market, fair value is determined by valuation techniques that make maximum use of inputs observed from markets.

Fair values of investments are determined as follows:

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

b. Bonds, including both nominal and real return, 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. Securities sold under agreements to repurchase and securities purchased under agreements to resell are valued using discounted cash flows based on current market yields.

d. Public equities are valued at quoted closing mid-market prices. When the market for a public equity is not active, management assesses if the quoted prices represent fair value. If not, management adjusts the quoted prices or estimates the fair value by using appropriate techniques including valuation models.

e. Real estate, private equities, infrastructure and timberland are valued based on estimated fair values determined by using appropriate techniques and best estimates by either 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.

f. 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. In determining fair value, consideration is also given to the credit risk of the counterparty.

g. 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 markets.
- 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 either obtained from broker quotations, from pricing services or are derived from quoted option prices.
- Forecasts on operating cash flows of real estate, private equities, infrastructure and timberland – forecasts include assumptions on revenue, revenue growth, expenses, capital expenditure, and capital structure. They are generally provided by either 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.

Fair value hierarchy
Investment assets and investment-related liabilities are classified and disclosed in one of the following categories reflecting the significance of inputs used in making the fair value measurement:

- Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 – inputs other than quoted prices included within Level 1 that are observable for the assets or liabilities, either directly or indirectly; and
- Level 3 – unobservable inputs.

If different levels of inputs are used to measure the fair value of an investment, the classification within the hierarchy is based on the lowest level input that is significant to the fair value measurement.

Trade-date reporting
Purchases and sales of investments and derivative contracts are recorded as of the trade date.

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.

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.

Direct management fees
Direct management and performance fees for external investment managers and administrators are expensed as incurred.

(e) 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.

(f) Accrued pension benefits
The value of accrued pension benefits and changes therein during the year are based on an actuarial valuation prepared by Mercer (Canada) Limited, an independent firm of actuaries. The valuation is made annually as at September 1 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.

As described in paragraph (f) of the Description of Plan note, the inflation protection benefits for credited service earned after December 31, 2009 will vary between 50% and 100% of the change in the Consumer Price Index. For the financial statement valuation, the Plan accrues the minimum guaranteed inflation protection benefits and discloses the maximum amounts of potential inflation protection benefits at the 100% level in note 4b.

(g) Contributions

Contributions from the members, the Province and designated employers are recorded on an accrual basis. Cash received from members for credited service and cash transfers from other pension plans are recorded when received.

(h) 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.

(i) Premises and equipment

Premises and equipment are recorded at cost and amortized on a straight-line basis over their estimated useful lives.

(j) Use of estimates

In preparing these financial statements, management uses estimates and assumptions that primarily affect the reported values of assets and liabilities, and related income and expenses. Estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable and relevant under the circumstances. The effect of a change in an estimate or assumption is recognized in the period in which the estimate and assumption is revised if the revision affects only that period. Significant estimates and assumptions are used primarily in the determination of accrued pension benefits and the fair value of investments and investment-related receivables and liabilities. Note 4 explains how estimates and assumptions are used in determining accrued pension benefits and note 1d explains how estimates and assumptions are used to derive the fair value of investments and investment-related receivables and liabilities.

(k) Contingencies

A contingent liability is a possible obligation that depends on the occurrence or non-occurrence of one or more future events not controlled by the Plan. Contingent liabilities are not recognized but the nature and extent are disclosed in the notes to the financial statements. A provision for a present obligation is recognized when a reliable estimate can be determined and the settlement of the obligation is probable.

Note 2.
INVESTMENTS

The Plan invests, directly or through derivatives, in fixed income, equities and real asset 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 $270 million (December 31, 2010 – $298 million and January 1, 2010 – $263 million), before allocating the effect of derivative contracts:

	as at December 31, 2011		as at December 31, 2010		as at January 1, 2010	
(Canadian $ millions)	**Fair Value**	**Cost**	Fair Value	Cost	Fair Value	Cost
Fixed income						
Debentures	**$ 662**	**$ 635**	$ 1,333	$ 1,223	$ 2,499	$ 2,258
Bonds	**31,033**	**27,806**	27,622	27,552	18,089	19,548
Money-market securities	**7,545**	**7,562**	4,735	4,835	3,207	3,308
Alternative investments[2]	**5,821**	**5,482**	5,231	5,021	5,829	6,139
Canadian real-rate products	**19,766**	**13,109**	16,207	12,119	13,031	10,159
Non-Canadian real-rate products	**9,066**	**7,210**	6,869	6,892	6,518	6,621
	73,893	**61,804**	61,997	57,642	49,173	48,033
Equity						
Publicly traded						
Canadian	**5,188**	**5,325**	5,411	4,831	1,761	1,373
Non-Canadian	**28,934**	**29,752**	25,947	24,873	20,658	19,464
Non-publicly traded						
Canadian	**2,280**	**1,422**	1,961	1,470	1,464	1,314
Non-Canadian	**10,252**	**10,507**	9,673	9,885	7,163	8,148
	46,654	**47,006**	42,992	41,059	31,046	30,299
Real assets						
Real estate (note 5)	**14,960**	**8,660**	16,861	11,898	14,209	10,456
Infrastructure	**8,709**	**7,460**	7,070	5,771	5,568	4,824
Timberland	**2,166**	**2,092**	2,220	2,108	2,339	2,116
	25,835	**18,212**	26,151	19,777	22,116	17,396
	146,382	**127,022**	131,140	118,478	102,335	95,728
Investment-related receivables						
Securities purchased under agreements to resell	**7,245**	**7,219**	2,286	2,291	2,453	2,455
Cash collateral deposited under securities borrowing arrangements	**841**	**841**	249	249	983	1,005
Derivative-related, net	**2,095**	**1,141**	2,519	1,128	2,315	1,208
	10,181	**9,201**	5,054	3,668	5,751	4,668
Investments	**$ 156,563**	**$ 136,223**	$ 136,194	$ 122,146	$ 108,086	$ 100,396

[1] For additional details, refer to the schedule of Investments over $100 million on pages 118–121.

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

	as at December 31, 2011		as at December 31, 2010		as at January 1, 2010	
(Canadian $ millions)	**Fair Value**	**Cost**	Fair Value	Cost	Fair Value	Cost
Investment-related liabilities						
Securities sold under agreements to repurchase	**$ (35,088)**	**$ (35,112)**	$ (28,245)	$ (28,741)	$ (9,684)	$ (9,701)
Securities sold but not yet purchased						
Fixed income	**(2,076)**	**(2,048)**	(898)	(901)	(1,429)	(1,467)
Equities	**(847)**	**(826)**	(249)	(212)	(983)	(911)
Cash collateral received under credit support annexes	**(458)**	**(458)**	(383)	(383)	(268)	(268)
Derivative-related, net	**(1,836)**	**(532)**	(1,698)	(915)	(2,213)	(1,512)
	(40,305)	**(38,976)**	(31,473)	(31,152)	(14,577)	(13,859)
Net investments (note 2d)	**$ 116,258**	**$ 97,247**	$ 104,721	$ 90,994	$ 93,509	$ 86,537

(b) Fair value hierarchy

The schedule below presents the Plan's investments and investment-related liabilities within the fair value hierarchy as outlined in note 1d:

				December 31, 2011
(Canadian $ millions)	Level 1	Level 2	Level 3	**Total**
Fixed income	$ 59,389	$ 4,309	$ 10,195	**$ 73,893**
Equity	32,013	1,069	13,572	**46,654**
Real assets	856	205	24,774	**25,835**
Net investment-related receivables/(liabilities)	(2,533)	(27,885)	294	**(30,124)**
Net investments	$ 89,725	$ (22,302)	$ 48,835	**$ 116,258**

				December 31, 2010
(Canadian $ millions)	Level 1	Level 2	Level 3	Total
Fixed income	$ 46,817	$ 4,847	$ 10,333	$ 61,997
Equity	30,096	192	12,704	42,992
Real assets	1,435	286	24,430	26,151
Net investment-related liabilities	(1,233)	(24,998)	(188)	(26,419)
Net investments	$ 77,115	$ (19,673)	$ 47,279	$ 104,721

				January 1, 2010
(Canadian $ millions)	Level 1	Level 2	Level 3	Total
Fixed income	$ 31,695	$ 5,426	$ 12,052	$ 49,173
Equity	20,893	351	9,802	31,046
Real assets	1,378	301	20,437	22,116
Net investment-related liabilities	(1,617)	(6,739)	(470)	(8,826)
Net investments	$ 52,349	$ (661)	$ 41,821	$ 93,509

Comparative figures have been restated due to non-consolidation under Section 4600. There is no impact on the net investments.

The schedule below presents a reconciliation of investments and investment-related receivables/(liabilities) measured at fair value using significant unobservable inputs (Level 3) during the year. Realized and unrealized gains (losses) are included in investment income.

2011

(Canadian $ millions)	Fixed Income	Equity	Real Assets	Net Investment-related Receivables/ (Liabilities)	**Total**
Balance, beginning of year	$ 10,333	$ 12,704	$ 24,430	$ (188)	**$ 47,279**
Purchases	3,394	3,408	5,833	3,671	**16,306**
Sales	(4,202)	(3,678)	(7,308)	(3,582)	**(18,770)**
Transfers in[3]	253	–	–	(9)	**244**
Transfers out[3]	(170)	(259)	–	27	**(402)**
Gains included in investment income (note 6)					
Realized	31	854	286	84	**1,255**
Unrealized	556	543	1,533	291	**2,923**
Balance, end of year	$ 10,195	$ 13,572	$ 24,774	$ 294	**$ 48,835**

2010

(Canadian $ millions)	Fixed Income	Equity	Real Assets	Net Investment-related Receivables/ (Liabilities)	Total
Balance, beginning of year	$ 12,052	$ 9,802	$ 20,437	$ (470)	$ 41,821
Purchases	4,827	3,929	10,084	5,039	23,879
Sales	(6,785)	(2,550)	(7,782)	(5,048)	(22,165)
Transfers in[3]	–	–	–	5	5
Transfers out[3]	(87)	(69)	–	41	(115)
Gains/(losses) included in investment income (note 6)					
Realized	(601)	423	68	(77)	(187)
Unrealized	927	1,169	1,623	322	4,041
Balance, end of year	$ 10,333	$ 12,704	$ 24,430	$ (188)	$ 47,279

[3] Transfers in and transfers out of level 3 are due to the change in the availability of observable inputs used for fair value measurement of investment assets or related liabilities. Similarly, transfers between level 2 and level 1 are due to the change in the availability of observable inputs. See note 1d Fair Value Hierarchy.

(c) 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 either 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 either pay or receive from the other cash flows based on changes in the value of either an equity or commodity index, a basket of stocks or commodities, or a single stock or commodity.

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 either 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 either 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 either acquired in standardized amounts on regulated exchanges or 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 swaps 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 OTC 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, 2011		as at December 31, 2010		as at January 1, 2010	
(Canadian $ millions)		**Notional**	**Fair Value**	Notional	Fair Value	Notional	Fair Value
Equity and commodity derivatives							
Swaps		**$ 22,496**	**$ (178)**	$ 15,332	$ 884	$ 15,102	$ 977
Futures		**10,003**	**(97)**	5,494	(4)	6,920	3
Options: Listed	– purchased	**158**	**3**	185	3	136	4
	– written	**149**	**(3)**	278	(5)	213	(6)
OTC	– purchased	**5,271**	**423**	5,492	337	4,563	324
	– written	**4,059**	**(111)**	6,325	(294)	2,924	(216)
		42,136	**37**	33,106	921	29,858	1,086
Interest rate derivatives							
Swaps		**26,557**	**5**	19,347	16	5,146	7
Futures		**92,951**	**24**	28,479	–	29,669	(8)
Options: Listed	– purchased	**–**	**–**	1,308	–	–	–
	– written	**7**	**–**	1,463	(1)	73	(1)
OTC	– purchased	**1,815**	**76**	5,382	28	5,739	37
	– written	**4,384**	**(80)**	2,115	(26)	1,098	(20)
		125,714	**25**	58,094	17	41,725	15
Currency derivatives							
Swaps		**274**	**5**	44	4	44	2
Forwards[4]		**38,177**	**20**	35,548	200	31,004	138
Futures		**62**	**–**	16	–	16	–
Options: OTC	– purchased	**5,660**	**30**	14,583	125	10,431	180
	– written	**5,526**	**(31)**	12,300	(114)	8,877	(145)
		49,699	**24**	62,491	215	50,372	175
Credit derivatives							
Loan participations		**–**	**–**	35	–	189	101
Credit default swaps	– purchased	**8,510**	**300**	8,043	82	10,825	209
	– written	**1,729**	**(308)**	2,049	(267)	2,494	(567)
Total return swaps		**10**	**1**	–	–	37	(16)
		10,249	**(7)**	10,127	(185)	13,545	(273)
Other derivatives							
Statistic swaps		**4,147**	**(61)**	4,968	(76)	15,481	(246)
Dividend swaps		**439**	**(37)**	364	(24)	263	(28)
		4,586	**(98)**	5,332	(100)	15,744	(274)
		232,384	**(19)**	169,150	868	151,244	729
Net cash collateral (received)/paid under derivative contracts		**–**	**278**	–	(47)	–	(627)
Notional and net fair value of derivative contracts		**$ 232,384**	**$ 259**	$ 169,150	$ 821	$ 151,244	$ 102

[4] Excludes currency forwards related to Real Estate assets as disclosed in note 5.

The net fair value of derivative contracts in the previous table is represented by:

	as at December 31	as at December 31	as at January 1
(Canadian $ millions)	**2011**	2010	2010
Derivative-related receivables	**$ 2,025**	$ 2,578	$ 3,004
Cash collateral paid under derivative contracts	**307**	113	132
Derivative-related liabilities	**(2,044)**	(1,710)	(2,275)
Cash collateral received under derivative contracts	**(29)**	(160)	(759)
	$ 259	$ 821	$ 102

(d) Investment asset mix

The Plan had a policy asset mix of 45% equities, 49% fixed income, 5% commodities, 25% real assets and (24%) money market as at December 31, 2011.

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 are summarized in Canadian dollars below:

	as at December 31, 2011		as at December 31, 2010		as at January 1, 2010	
	Effective Net Investments at Fair Value ($ millions)	**Asset Mix %**	Effective Net Investments at Fair Value ($ millions)	Asset Mix %	Effective Net Investments at Fair Value ($ millions)	Asset Mix %
Equity						
Canadian	**$ 10,636**	**9%**	$ 9,286	9%	$ 8,427	9%
Non-Canadian	**41,034**	**35**	38,203	36	32,755	35
	51,670	**44**	47,489	45	41,182	44
Fixed income						
Bonds	**26,500**	**23**	22,728	22	15,462	17
Real-rate products[5]	**29,291**	**25**	23,245	22	19,882	21
	55,791	**48**	45,973	44	35,344	38
Commodities[6]	**5,645**	**5**	5,226	5	1,939	2
Real assets						
Real estate (note 5)	**14,960**	**13**	16,861	16	14,209	15
Infrastructure	**8,709**	**7**	7,070	7	5,568	6
Timberland	**2,166**	**2**	2,220	2	2,338	3
	25,835	**22**	26,151	25	22,115	24
Absolute return strategies[7]						
Internal absolute return strategies	**7,679**	**7**	6,845	7	6,299	7
Alternative investments	**4,652**	**4**	4,531	4	5,367	5
	12,331	**11**	11,376	11	11,666	12
Money market[7]	**(35,014)**	**(30)**	(31,494)	(30)	(18,737)	(20)
Net investments	**$ 116,258**	**100%**	$ 104,721	100%	$ 93,509	100%

[5] Beginning January 1, 2010, real rate products are included in fixed income instead of real assets. January 1, 2010 comparative figures have been reclassified to reflect this change.

[6] Beginning January 1, 2010, commodities, previously included in real assets, are reported in a separate asset class. January 1, 2010 comparative figures have been reclassified to reflect this change.

[7] Beginning January 1, 2010, absolute return strategies and money market, previously included in fixed income, are each reported in a separate asset class. January 1, 2010 comparative figures have been reclassified to reflect this change.

(e) 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, 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.
- Board Investment Policy – This policy applies to the total fund and aggregate asset classes. The policy addresses the risks that are relevant and material at the total fund level. The policy specifies asset mix and risk budget allocation and lists investment constraints such as maximum exposures permitted for a single issuer, liquidity requirements, and currency management. The Board approves this policy and reviews it regularly.
- Portfolio policies for each investment department – These policies are developed to apply to the individual portfolios within each asset class managed by the Investment Division. All portfolio policies 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 policy. All portfolio policies are reviewed annually and approved by the Executive Vice-President of the Investment Division and the Senior Vice-President responsible for the department.
- Trade Authorization and Execution Operation Policy – This policy provides guidance on trading with authorized counterparties and the procedures for obtaining authorization to trade with a new counterparty.
- Pre-Trade Clearance Policy – This policy 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

The Plan uses risk budgeting to allocate risk across the investment asset classes. The risk budget is presented to the Board annually for review and approval. Each investment department is responsible for managing the investment risks associated with the investments they manage within the risk budget allocated to them. Each department is subject to compliance with the Statement of Investment Policies and Procedures, the Board Investment Policy (which includes the risk budget allocated to them), Trade Authorization and Execution Operation Policy, Pre-trade Clearance Policy and the applicable portfolio policies. In addition, the Fixed Income Department is responsible to maintain the liquidity positions in accordance with the Plan's policies 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 policies 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 Risk Committee (IRC) 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 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. Reporting to the IRC are the Investment Division Credit Committee and the Investment Division Liquidity Committee.

The Enterprise Risk Management Committee 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 semi-annually and more frequently as necessary.

(f) 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. Policies are also in place to limit the maximum exposures to any individual counterparty for derivative contracts.

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

The Plan enters into agreements with counterparties to limit its exposure to credit losses. An International Swaps and Derivatives Association (ISDA) Master Agreement is executed with all OTC derivative counterparties, which allows both parties to settle obligations on a net basis when termination or other pre-determined events occur. The Plan also negotiates a collateral agreement known as Credit Support Annex (CSA) with its key counterparties to further mitigate counterparty credit risk. A CSA gives the Plan the power to realize collateral posted by counterparties in the event of a default by such counterparties.

Maximum exposure to credit risk before collateral held

The following table presents the maximum exposure as at December 31, 2011, December 31, 2010 and January 1, 2010 to credit risk from balance sheet and off-balance sheet financial instruments and arrangements 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 off-balance sheet guarantees, 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. For loan commitments and risk participation agreements, the maximum exposure is the committed amount under the agreements. For credit derivatives, the maximum exposure is the notional amount of written credit derivatives as presented in note 2c.

	as at December 31	as at December 31	as at January 1
(Canadian $ millions)	**2011**	2010	2010
On balance sheet:			
Cash	**$ 435**	$ 432	$ 493
Receivable from the Province of Ontario	**2,717**	2,627	2,524
Receivable from brokers	**39**	101	93
Fixed income			
Debentures	**662**	1,333	2,499
Bonds	**31,033**	27,622	18,089
Money-market securities	**7,545**	4,735	3,207
Canadian real-rate products	**19,766**	16,207	13,031
Non-Canadian real-rate products	**9,066**	6,869	6,518
Securities purchased under agreements to resell	**7,245**	2,286	2,453
Derivative-related receivables	**2,025**	2,578	3,004
Total on balance sheet	**$ 80,533**	$ 64,790	$ 51,911
Off balance sheet:			
Guarantees	**$ 2,867**	$ 233	$ 1,532
Loan commitments	**33**	380	611
Risk participation agreements	**113**	133	125
Notional amount of written credit derivatives	**1,729**	2,049	2,494
Total off balance sheet	**4,742**	2,795	4,762
Total maximum exposure	**$ 85,275**	$ 67,585	$ 56,673

Comparative figures for guarantees, total off-balance sheet amounts and total maximum exposure decreased by $192 million for the year ended December 31, 2010 and increased by $1,149 million as at January 1, 2010 due to non-consolidation under Section 4600.

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, 2011, the Plan has a significant concentration of credit risk with the Government of Canada, the Province of Ontario and the U.S. Treasury. This concentration relates primarily to holding Government of Canada issued securities of $42.1 billion (December 31, 2010 – $34.9 billion, January 1, 2010 – $22.0 billion), U.S. Treasury issued securities of $9.6 billion (December 31, 2010 – $8.4 billion, January 1, 2010 – $6.5 billion), Province of Ontario bonds of $2.9 billion (December 31, 2010 – $1.4 billion, January 1, 2010 – $0.8 billion), receivable from the Province (see note 3) of $2.7 billion (December 31, 2010 – $2.6 billion, January 1, 2010 – $2.5 billion), non-marketable Province of Ontario debentures of $0.7 billion (December 31, 2010 – $1.3 billion, January 1, 2010 – $2.5 billion), and future provincial funding requirements of the Plan.

(g) 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 movements, the occurrence of certain catastrophic events (e.g., hurricanes and earthquakes) affecting the prices of insurance linked securities, expectations of future 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.

Total Asset Risk is prepared using the ETL methodology. This risk 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. 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 25 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 asset positions 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. A number of initiatives were completed in the past year that significantly improved the accuracy of calculated risk measures. Existing risk methodologies were modified to incorporate more accurate risk models and more reliable risk data.

The chart below shows the year-over-year change in Total Asset Risk ETL of the Plan. The $3 billion increase for the year is mainly due to a change in the modelling of real interest rates by employing a method based on level changes observed in comparable historical periods versus one based on random sampled percentage changes. This change was necessitated by the current low interest rate environment and impacted directly the real rate product assets. The changes in the other assets are mainly due to changes in the market value of the Plan's holdings, foreign exchange hedging and additional risk model changes.

as at December 31

(Canadian $ billions)[8]	2011	2010
Equity		
Canadian	**$ 4.0**	$ 3.5
Non-Canadian	**12.5**	11.0
Fixed income		
Bonds	**2.0**	2.0
Real-rate products	**4.5**	1.5
Commodities	**3.5**	2.5
Real assets		
Real estate	**1.5**	2.5
Infrastructure	**1.5**	1.0
Timberland	**0.5**	0.5
Absolute return strategies	**1.0**	2.0
Money market	**4.5**	3.5
Total Asset Risk ETL Exposure[9][10]	**$ 21.5**	$ 18.5

[8] Rounded to the nearest $0.5 billion.

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

[10] In prior years, Total Risk ETL was presented instead of Total Asset Risk ETL. Total Risk ETL is the risk of the Plan associated with the difference in value between the assets and the liabilities or the funding surplus/deficit over a one-year horizon. With the changes to the real interest model, Total Risk ETL is driven primarily by real interest rate movements through the impact on the liability value. Total Asset Risk ETL is the risk associated with the net investment assets only. In the context of investment risk, market or credit risks, and changes made to the investment portfolio and their resulting impacts to the risk of loss of the Plan's assets, Total Asset Risk ETL is the risk measure that summarizes the impact of changes in the Plan's holdings. Total Asset Risk ETL is monitored and reported to both management and the Board. The Board Investment Policy sets out limits in the management of the Plan's Total Asset Risk ETL. Total Risk ETL continues to be monitored and reported to both management and the Board; however, it is managed in conjunction with longer-term Asset-Liability Studies.

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 2c to the financial statements. After giving effect to the derivative contracts and investment-related receivables and liabilities discussed in note 2c, 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 6% (December 31, 2010 – 6%, January 1, 2010 – 6%). 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 17% (December 31, 2010 – 16%, January 1, 2010 – 14%).

As at December 31, 2011, 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 19% (December 31, 2010 – 18%, January 1, 2010 – 18%).

Foreign currency risk

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

As at December 31, 2011, December 31, 2010, and January 1, 2010 the Plan had investments exposed to foreign currency. In Canadian dollars this exposure is as follows:

	December 31	December 31	January 1
(Canadian $ millions)	**2011**	2010	2010
Currency	**Net Exposure**	Net Exposure	Net Exposure
United States Dollar	**$ 22,877**	$ 20,970	$ 19,978
British Pound Sterling	**5,759**	5,565	4,673
Euro	**4,684**	4,632	5,358
Brazilian Real	**3,021**	3,202	4,237
Japanese Yen	**2,538**	2,655	2,155
Chilean Peso	**1,968**	1,492	1,279
Chinese Renminbi	**1,892**	410	220
Australian Dollar	**1,495**	2,361	1,935
South Korean Won	**1,011**	520	391
Swedish Krona	**723**	678	68
Other	**4,920**	4,045	3,086
	$ 50,888	$ 46,530	$ 43,380

A 1% increase/decrease in the value of the Canadian dollar against all currencies, with all other variables and underlying values held constant, would result in an approximate decrease/increase in the value of net investments of $509 million as at December 31, 2011 (December 31, 2010 – $465 million, January 1, 2010 – $434 million).

(h) 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 one year 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 $51,695 million as at December 31, 2011 (December 31, 2010 – $43,285 million, January 1, 2010 – $28,495 million). The Plan also has publicly traded equities of $34,122 million (December 31, 2010 – $31,358 million, January 1, 2010 – $22,419 million) which are listed on major recognized stock exchanges. These securities are readily realizable and convertible to cash.

Contractual maturity

The Plan's liabilities include accrued pension benefits, investment-related liabilities, due to brokers, accounts payable and accrued liabilities. Due to brokers, accounts payable and accrued liabilities are all due within one year. As the Plan may settle derivatives at fair value before contractual maturity, they are considered to mature within one year.

The Plan's investment-related liabilities by maturity as at December 31 are as follows:

			2011
(Canadian $ millions)	Within One Year	One to Five Years	**Total**
Securities sold under agreements to repurchase	$ (29,565)	$ (5,523)	**$ (35,088)**
Securities sold but not yet purchased			
Fixed income	(2,076)	–	**(2,076)**
Equities	(847)	–	**(847)**
Cash collateral received under credit support annexes	(458)	–	**(458)**
Derivative-related, net	(1,836)	–	**(1,836)**
Total	$ (34,782)	$ (5,523)	**$ (40,305)**

			2010
(Canadian $ millions)	Within One Year	One to Five Years	Total
Securities sold under agreements to repurchase	$ (28,245)	$ –	$ (28,245)
Securities sold but not yet purchased			
Fixed income	(898)	–	(898)
Equities	(249)	–	(249)
Cash collateral received under credit support annexes	(383)	–	(383)
Derivative-related, net	(1,698)	–	(1,698)
Total	$ (31,473)	$ –	$ (31,473)

The Plan's investment-related liabilities by maturity as at January 1 are as follows:

			2010
(Canadian $ millions)	Within One Year	One to Five Years	Total
Securities sold under agreements to repurchase	$ (9,684)	$ –	$ (9,684)
Securities sold but not yet purchased			
Fixed income	(1,429)	–	(1,429)
Equities	(983)	–	(983)
Cash collateral received under credit support annexes	(268)	–	(268)
Derivative-related, net	(2,213)	–	(2,213)
Total	$ (14,577)	$ –	$ (14,577)

The comparative figure for total investment-related liabilities decreased by $19,166 million (December 31, 2010), $15,814 million (January 1, 2010) due to non-consolidation under Section 4600.

(i) Securities collateral

Canadian and U.S. government securities with a fair value of $1,260 million (December 31, 2010 – $858 million, January 1, 2010 – $2,378 million) have been either deposited or pledged with various financial institutions as either collateral or margin. The Plan is not allowed to either pledge the same securities with other financial institutions or to 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 $1,838 million (December 31, 2010 – $447 million, January 1, 2010 – $269 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 either sell or repledge the collateral in the absence of default by the owner of the collateral but it has neither sold nor repledged any collateral as of December 31, 2011, December 31, 2010, or January 1, 2010.

Note 3.
RECEIVABLE FROM THE PROVINCE OF ONTARIO

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

	as at December 31	as at December 31	as at January 1
(Canadian $ millions)	**2011**	2010	2010
Contributions receivable	**$ 2,663**	$ 2,554	$ 2,445
Accrued interest receivable	**54**	73	79
	$ 2,717	$ 2,627	$ 2,524

The receivable as at December 31, 2011 from the Province consists of $1,344 million, which was received in January 2012, and an estimated $1,373 million to be received with interest in January 2013. The receivable as at December 31, 2010 from the Province consisted of $1,316 million, which was received in January 2011, and an initial estimate of $1,311 million to be received in January 2012. The receivable as at January 1, 2010 from the Province consisted of $1,245 million, which was received in January 2010, and an initial estimate of $1,279 million to be received in January 2011. The difference between the initial estimates and the actual amount received was due to interest.

Note 4.
ACCRUED PENSION BENEFITS

(a) Actuarial assumptions

The actuarial assumptions used in determining the value of accrued pension benefits of $162,587 million (December 31, 2010 – $146,893 million, January 1, 2010 – $131,858 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 bonds, which have characteristics similar to the Plan's liabilities, plus a spread 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.

In 2011, the spread was changed from 50 basis points to the prevailing spread at December 31 between the Government of Canada and the Province of Ontario long-term nominal bonds. This change in accounting estimate is applied prospectively beginning December 31, 2011. The effect of the change was a decrease in the value of accrued pension benefits by $12,397 million in 2011.

A summary of the primary economic assumptions is as follows:

	as at December 31 2011	as at December 31 2010	as at January 1 2010
Discount rate	**3.40%**	4.05%	4.60%
Salary escalation rate	**3.05%**	3.40%	3.55%
Inflation rate	**2.05%**	2.40%	2.55%
Real rate	**1.35%**	1.65%	2.05%

The primary economic assumptions were changed as a result of changes in capital markets during 2011. These changes resulted in a net increase in the value of accrued pension benefits of $22,284 million (December 31, 2010 – $10,242 million, January 1, 2010 – $9,941 million). No changes to the non-economic assumptions were adopted in 2011. The valuation methods were adjusted to reflect membership data being provided as at the end of each school year rather than as at the end of each calendar year commencing in 2011. Changes in non-economic assumptions and the valuation methods decreased the accrued pension benefits by $68 million including the impact of updating the membership data from calendar year to school year (December 31, 2010 – $198 million increase, January 1, 2010 – nil). The changes in economic and non-economic assumptions and the change in valuation methods resulted in a net increase in the value of accrued pension benefits of $9,819 million (December 31, 2010 – $10,440 million, January 1, 2010 – $9,941 million).

(b) Plan provisions

Credited service earned after December 31, 2009 is subject to conditional inflation protection as described in paragraph (f) of the Description of Plan note. The inflation protection benefits vary between 50% and 100% of the change in the Consumer Price Index. The co-sponsors may only invoke the conditional inflation protection provision at the time of a funding valuation filing, depending on the Plan's funded status. The Ontario government and designated employers participating in the Plan will make extra contributions to the Plan equal to any inflation protection benefits members forego.

Conditional inflation protection was invoked in the filed funding valuation as at January 1, 2011. Effective January 1, 2012, inflation protection is 60% of the change in the Consumer Price Index for the post-2009 credited service. The co-sponsors are permitted to change the level of inflation protection when filing a subsequent funding valuation. The next required filing date is in 2014.

For financial statement valuations, the Plan accrues the minimum amount of inflation protection benefits estimated at 60% for post-2009 credited service until the next required filing and at the guaranteed level of 50% for the period thereafter. The indexation percentage for credited service earned before 2010 remains at 100%.

If 100% indexation had been assumed starting after the next statutory filing, with full inflation protection restored on a go-forward basis, the accrued pension benefits would increase $1,620 million (December 31, 2010 – $755 million) to $164,207 million (December 31, 2010 – $147,648 million). The present value of the maximum extra contributions the Plan will receive from the Ontario government and designated employers will be $1,620 million (December 31, 2010 – $755 million).

(c) Experience gains and losses

Experience losses on the accrued pension benefits of $179 million (December 31, 2010 – $316 million gain) arose from differences between the actuarial assumptions and actual results.

Note 5.
INVESTMENT IN REAL ESTATE

The Plan's real estate investments comprise real estate-related investments that are either owned or managed on behalf of the Plan by Cadillac Fairview Corporation Limited, a wholly-owned subsidiary. The tables below provide information on the net investment in real estate:

	as at December 31, 2011		as at December 31, 2010		as at January 1, 2010	
(Canadian $ millions)	**Fair Value**	**Cost**	Fair Value	Cost	Fair Value	Cost
Assets[1]						
Real estate properties[2]	**$ 18,866**	**$ 12,593**	$ 17,100	$ 12,505	$ 15,461	$ 12,167
Investments	**1,234**	**869**	1,831	1,392	1,992	1,509
Other assets[2]	**306**	**268**	361	321	319	248
Total assets	**20,406**	**13,730**	19,292	14,218	17,772	13,924
Liabilities[1]						
Long-term debt[2]	**4,665**	**4,527**	1,719	1,792	2,947	2,984
Other liabilities[2]	**781**	**543**	712	528	616	484
Total liabilities	**5,446**	**5,070**	2,431	2,320	3,563	3,468
Net investment in real estate	**$ 14,960**	**$ 8,660**	$ 16,861	$ 11,898	$ 14,209	$ 10,456

[1] As at December 31, 2011, U.S. Dollar and British Pound Sterling net assets have been hedged by way of foreign currency forward contracts for a notional amount of $915 million (December 31, 2010 – $1,253 million, January 1, 2010 – $1,698 million) with a combined fair value of ($43) million (December 31, 2010 – $24 million, January 1, 2010 – $71 million).

[2] Includes the proportionate share of assets and liabilities in real estate joint ventures of $3,717 million (December 31, 2010 – $3,259 million, January 1, 2010 – $3,489 million) and $1,144 million (December 31, 2010 – $1,305 million, January 1, 2010 – $1,371 million), respectively.

(Canadian $ millions)	**2011**	2010
Revenue		
Rental	**$ 1,804**	$ 1,773
Investment and other	**77**	66
	1,881	1,839
Expenses		
Property operating	**793**	776
General and administrative	**37**	32
Other[3]	**47**	24
	877	832
Operating income	**1,004**	1,007
Interest expense	**(176)**	(159)
Income (note 6)	**828**	848
Net investment gain[4][5]	**1,545**	1,519
Net real estate income	**$ 2,373**	$ 2,367

[3] Includes transaction costs of $24 million (2010 – $11 million).

[4] Includes unrealized net gain of $1,337 million (2010 – $1,210 million).

[5] This amount is included in net realized and unrealized gain on investments shown in note 6.

Note 6.
INVESTMENT INCOME

(a) Investment income/(loss) before allocating net realized and unrealized 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:

(Canadian $ millions)	2011	2010
Fixed income interest		
Debentures	$ 99	$ 156
Money-market securities	(124)	(138)
Bonds	1,334	1,049
Net repo interest expense	(166)	(56)
Net swap interest expense	(154)	(106)
Canadian real-rate products	428	393
Non-Canadian real-rate products	171	150
	1,588	1,448
Equity dividend income		
Canadian equity	179	148
Non-Canadian equity	979	643
	1,158	791
Real assets		
Real estate (note 5)	828	848
Infrastructure	201	273
Timberland	60	43
	1,089	1,164
	3,835	3,403
Net realized and unrealized gain on investments[1][2]	8,233	10,210
Direct management fees	(218)	(256)
Transaction costs	(115)	(88)
Investment income	$ 11,735	$ 13,269

[1] Includes unrealized net gains of $5,284 million (2010 – $6,755 million).

[2] Includes net foreign currency gains/(losses) of ($546) million (2010 – gains of $569 million).

(b) Investment income/(loss)

Investment income/(loss) 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:

(Canadian $ millions)	**2011**	2010
Fixed income	**$ 9,306**	$ 4,172
Canadian equity	**(267)**	1,659
Non-Canadian equity	**(248)**	3,678
Commodities	**(46)**	660
Real assets	**2,990**	3,100
	$ 11,735	$ 13,269

Note 7.
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:

		2011		2010
(percent)	**Investment Returns**	**Investment Benchmark Returns**	Investment Returns	Investment Benchmark Returns
Fixed income	**19.9%**	**19.5%**	9.9%	9.5%
Canadian equity	**(5.0)**	**(9.1)**	14.6	13.8
Non-Canadian equity	**0.2**	**(4.4)**	9.4	5.9
Commodities	**(2.3)**	**(1.5)**	3.2	3.3
Real assets	**13.2**	**13.3**	13.9	5.5
Total Plan	**11.2%**	**9.8%**	14.3%	9.8%

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.

Note 8.
STATUTORY ACTUARIAL VALUATIONS

Statutory actuarial valuations are prepared periodically to determine the funding requirements of the Plan. Active members are currently required to contribute 10.4% of the portion of their salaries covered by the CPP and 12.0% of salaries above this level. Member contributions are matched by the Province and designated 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:

	Contribution Rate	
(percent)	Covered by CPP	Not Covered by CPP
2012	10.80%	12.40%
2013	11.15%	12.75%
2014	11.50%	13.10%

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 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, 2011 by Mercer (Canada) Limited and disclosed a funding surplus of $212 million, after adopting conditional inflation protection of 60% for post-2009 service and the contribution increases summarized above which will be payable over the fifteen year period commencing January 1, 2012.

Note 9.
CONTRIBUTIONS

(Canadian $ millions)	**2011**	2010
Members		
Current service	**$ 1,352**	$ 1,294
Optional credit	**25**	19
	1,377	1,313
Province of Ontario		
Current service	**1,345**	1,280
Interest	**40**	52
Optional credit	**21**	16
	1,406	1,348
Other employers	**26**	25
Transfers from other pension plans	**14**	11
	40	36
	$ 2,823	$ 2,697

Note 10.
BENEFITS PAID

(Canadian $ millions)	**2011**	2010
Retirement pensions	**$ 4,329**	$ 4,190
Death benefits	**259**	244
Disability pensions	**29**	30
Commuted value transfers	**33**	21
Transfers to other plans	**10**	10
Refunds	**3**	5
	$ 4,663	$ 4,500

Note 11.
ADMINISTRATIVE EXPENSES

(a) Investment expenses

(Canadian $ millions)	2011	2010
Salaries, incentives and benefits	$ 180.6	$ 195.3
Premises and equipment	31.5	30.6
Professional and consulting services	37.0	26.0
Information services	14.9	14.5
Communication and travel	12.0	10.0
Custodial fees	8.0	9.0
Statutory audit fees	1.6	1.3
Board and committee remuneration	0.6	0.6
Other	3.2	2.7
	$ 289.4	$ 290.0

(b) Member Services expenses

(Canadian $ millions)	2011	2010
Salaries, incentives and benefits	$ 28.6	$ 27.9
Premises and equipment	8.8	9.2
Professional and consulting services	3.5	4.0
Communication and travel	1.7	1.5
Statutory audit fees	0.1	0.1
Board and committee remuneration	0.1	0.1
Other	0.8	0.8
	$ 43.6	$ 43.6

(c) Compensation of key management personnel

Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of the Plan, being the Board, the Executive Team and the Senior Vice Presidents of the Investment Division.

The compensation of the key management personnel is included in the administrative expenses of the Plan. There are no other related party transactions between the key management personnel and the Plan.

The compensation of the key management personnel as at December 31 is summarized below:

(Canadian $ millions)	2011	2010
Short-term employee benefits	$ 12.0	$ 11.0
Post-employment benefits	3.1	3.0
Other long-term benefits	23.5	23.5
Termination payments	–	0.1
Total	$ 38.6	$ 37.6

(d) Employee post-employment benefits
The employees of the Plan are either members of the Ontario Public Service Employees Union (OPSEU) Pension Plan or Public Service Pension Plan (PSPP). Some employees are also members of the Public Service Supplementary Plan (PSSP). These three pension plans are sponsored by the Province of Ontario and information is available on www.optrust.com and www.opb.ca. As the employer, the Plan matches the employees' contributions to these pension plans. Some senior management employees also participate in a non-registered, unfunded Supplemental Employee Retirement Plan (SERP) managed by the Plan to provide the employees non-indexed retirement benefits equal to 2% of the employee's best three-year average pensionable earnings for each year of service, less the initial annual pension to which the employee is entitled under the PSPP and PSSP, combined. The contributions expensed by the Plan during the year was $10.1 million (2010 – $11.9 million). Contributions are included in the salaries, incentives and benefits expenses.

Note 12.
CAPITAL

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 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 4), 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 8.

Note 13.
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 control 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 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 members, the Province and designated employers. 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 2012, the actuary determined that the limit should increase from $14,500 to $15,000. 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.

The RCA financial statements are in compliance with Section 4600 and IFRS. The comparatives as at January 1, 2010 and for the years ended December 31, 2010 and 2011 are shown below:

(Canadian $ thousands)	**December 31 2011**	December 31 2010	January 1 2010
STATEMENTS OF FINANCIAL POSITION			
Net assets available for benefits			
Assets	**$ 17,152**	$ 16,781	$ 14,931
Liabilities	**(1,595)**	(1,412)	(1,206)
	$ 15,557	$ 15,369	$ 13,725
Accrued benefits and deficit			
Accrued benefits	**$ 391,835**	$ 383,582	$ 295,992
Deficit	**(376,278)**	(368,213)	(282,267)
	$ 15,557	$ 15,369	$ 13,725
STATEMENTS OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS			
Contributions	**$ 6,142**	$ 6,467	
Investment income	**49**	42	
	6,191	6,509	
Benefits paid	**5,917**	4,810	
Expenses	**86**	55	
	6,003	4,865	
Increase in net assets	**$ 188**	$ 1,644	

The actuarial assumptions and the accrual of conditional inflation protection used in determining the value of accrued benefits are consistent with 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 14.
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, 2011, these commitments totalled $4,962 million (2010 – $4,628 million). The comparative figures decreased by $2,821 million due to non-consolidation under Section 4600.

Note 15.
GUARANTEES AND INDEMNIFICATIONS

The Plan provides guarantees to third parties related to certain companies the Plan invests in and will be called upon to satisfy the guarantees if the companies fail to meet their obligations. The Plan expects most guarantees to expire unused. No payments have been made by the Plan in either 2011 or 2010 under these guarantees.

The Plan guarantees three debentures issued by a real estate trust in 2011. The real estate trust is an investment holding company included in the Plan's net real estate investments. The debentures comprised of $1.25 billion 3.24% Series A Debentures maturing on January 25, 2016, $0.75 billion 4.31% Series B Debentures maturing on January 25, 2021 and $0.6 billion 3.64% Series C Debentures maturing on May 9, 2018. The debentures may be redeemed by the issuer at any time prior to maturity. The Plan's maximum exposure is $2,635 million as at December 31, 2011.

The Plan guarantees loan and credit agreements which will expire between 2012 and 2014. The Plan's maximum exposure is $149 million as at December 31, 2011 (December 31, 2010 – $155 million, January 1, 2010 – $163 million). As at December 31, 2011, the companies have drawn $127 million under the agreements (December 31, 2010 – $133 million, January 1, 2010 – $141 million).

The Plan guarantees lease agreements for a subsidiary with expiry dates ranging from 2012 to 2059. The Plan's maximum exposure is $83 million as at December 31, 2011 (December 31, 2010 – $78 million, January 1, 2010 – $75 million). There were no default lease payments in either 2011 or 2010.

Note 16.
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:

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 still at the discovery stage. At this time it is not possible to predict the outcome.

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. The plaintiff has taken no steps to advance the claim since 2008. A certification motion has not been scheduled. At this time it is not possible to predict the outcome.

Major Investments

FIXED INCOME AND SHORT-TERM INVESTMENTS OVER $100 MILLION

(as at December 31, 2011)

Type ($ millions)	Maturity	Coupon (%)	Fair Value	Cost
Government of Canada bonds	2012–2041	1.00–10.50	$ 20,960	$ 17,591
Securities purchased under agreements to resell	2012–2012	-0.30–1.02	7,245	7,219
Canada treasury bills	2012–2012	0.00–0.00	5,829	5,822
Provincial bonds	2016–2043	0.00–9.50	3,363	2,989
Canadian corporate bonds	2011–2108	0.00–30.00	2,435	2,470
International corporate bonds	2012–2037	0.00–13.53	2,335	2,709
United States treasury bonds	2012–2015	0.38–9.25	401	388
United States treasury bills	2012–2012	0.00–0.00	130	131
Securities sold under agreements to repurchase	2012–2012	0.05–1.57	(35,088)	(35,112)

REAL-RETURN INVESTMENTS OVER $100 MILLION

Type ($ millions)	Maturity	Coupon (%)	Fair Value	Cost
Real-return Canada bonds	2021–2044	1.50–4.25	$ 15,333	$ 10,797
United States treasury inflation protection	2014–2041	0.50–3.88	9,043	7,188
Real-return provincial bonds	2013–2036	2.00–4.50	2,228	1,333
Real-return Canada corporate bonds	2016–2046	0.00–5.33	2,041	841
Index-linked mortgages	2023–2030	4.63–5.53	165	137

PROVINCE OF ONTARIO DEBENTURES OVER $100 MILLION

Maturity Date ($ millions)	Coupon (%)	Fair Value	Cost
2012-2012	11.06–11.31	$ 662	$ 635

CORPORATE SHARES/UNITS OVER $100 MILLION

(as at December 31, 2011) (millions)

Security Name	Shares	Fair Value
iShares MSCI Emerging Markets Index	49.7	$1,918.4
Multiplan Empreendimentos Imobiliarios S.A.	52.1	1,103.0
GNC Holdings, Inc.	26.3	742.5
Hitachi, Ltd.	131.6	703.6
Canadian Natural Resources Limited	15.1	576.9
Total SA	11.2	570.9
Vodafone Group Plc	184.8	544.1
The McGraw-Hill Companies, Inc.	11.9	543.6
ACE Limited	6.3	447.7
Nippon Telegraph and Telephone Corporation	8.2	427.3
Wells Fargo & Company*	15.2	404.3
Potash Corporation of Saskatchewan Inc.	9.6	402.3
Royal Dutch Shell plc	5.2	333.6
Michael Kors Holdings Limited	13.2	325.7
Deutsche Telekom AG	27.7	324.2
Goldcorp Inc.	6.8	307.6
Marathon Petroleum Corporation	8.9	301.2
Transocean Ltd.	7.5	291.6
Continental AG	4.6	290.0
Royal Bank of Canada	5.5	284.4
Barrick Gold Corporation	6.1	282.1
MMX Mineracao e Metalicos SA	147.7	278.9
Toronto-Dominion Bank, The	4.2	274.3
BRF–Brasil Foods S.A.	13.4	267.9
Nestlé SA	4.5	261.9
Safeway Inc.	11.9	256.8
Intel Corporation	10.3	253.2
Akzo Nobel N.V.	5.1	251.9
Unilever N.V.	7.2	251.4
Microsoft Corporation	9.5	250.5
Chow Tai Fook Jewellery Company Limited	130.7	238.6
LLX Logistica S.A.	124.1	228.3
HSBC Holdings plc	28.5	224.2
Sprint Nextel Corporation	91.6	218.2
Macdonald, Dettwiler and Associates Ltd.	4.4	208.5
GlaxoSmithKline plc	8.7	204.0
Novartis AG	3.3	193.5
Apple Inc.	0.5	190.1
Rockwell Collins, Inc.	3.3	185.1
Bank of Nova Scotia	3.5	178.0
The Walt Disney Company	4.4	169.2
Metlife, Inc.	5.2	165.1
Google Inc.	0.2	164.0
Canadian Pacific Railway Limited	2.3	157.0
Pfizer Inc.	7.1	156.1
PNC Financial Services Group, Inc.*	3.1	153.5
Suncor Energy, Inc.	5.1	151.2
3M Company	1.8	148.5
Itaú Unibanco Holding S.A.	7.8	147.9
DaimlerChrysler AG	3.2	143.9
JPMorgan Chase & Co.*	4.2	141.9
Education Management Corporation	5.0	141.1
BAE Systems plc	31.1	140.4
Johnson & Johnson	2.1	139.5
Canadian Imperial Bank of Commerce	1.9	136.8
Exxon Mobil Corporation	1.5	132.6
Wolseley plc	3.9	131.4
SunTrust Banks, Inc.*	7.3	129.7
Applied Materials, Inc.	11.6	126.8
Rio Tinto plc	2.5	122.4
OGX Petróleo e Gás Participações S.A.	16.4	121.7
Dell Inc.	8.0	118.9
CVS Caremark Corporation	2.9	118.7
Samsung Electronics Co., Ltd.	0.1	117.2
Chesapeake Energy Corporation	5.2	116.9
Thermo Fisher Scientific Inc.	2.6	116.8
Sampo Oyj	4.6	116.3
Tiffany & Co.	1.7	115.5
Toyota Motor Corporation	3.3	113.7
QE National	31.6	113.0
Hewlett-Packard Company	4.2	111.3
Cisco Systems, Inc.	6.0	109.9
News Corporation	6.0	109.3
Woodside Petroleum Ltd.	3.4	108.9
Credit Suisse Group AG	4.5	108.6
TransCanada Corporation	2.4	108.1
Illinois Tool Works Inc.	2.3	108.1
PSA Peugeot Citroen	6.7	107.3
Danaher Corporation	2.2	105.9
Metalurgica Gerdau S.A.	10.7	104.0
Nissan Shatai Co., Ltd.	10.5	103.5
Koninklijke (Royal) Philips Electronics N.V.	4.8	103.4
Canon Inc.	2.2	101.9
Kroger Co., The	4.1	100.3

*Includes fair market value of warrants and subscription receipts.

REAL ESTATE INVESTMENTS OVER $100 MILLION

(as at December 31, 2011)

Property	Total Square Footage (thousands)	Effective % Ownership
Canadian Regional Shopping Centres		
Champlain Place, Dieppe	719	100%
Chinook Centre, Calgary	1,383	100%
Fairview Mall, Toronto	875	50%
Fairview Park Mall, Kitchener	746	100%
Fairview Pointe Claire, Montreal	1,047	50%
Georgian Mall, Barrie	626	100%
Le Carrefour Laval, Montreal	1,360	100%
Les Galeries D'Anjou, Montreal	1,200	50%
Les Promenades St. Bruno, Montreal	1,138	100%
Lime Ridge Mall, Hamilton	814	100%
Market Mall, Calgary	971	50%
Markville Shopping Centre, Markham	979	100%
Masonville Place, London	684	100%
McAllister Place, St. John	483	100%
Pacific Centre, Vancouver	1,440	100%
Polo Park Mall, Winnipeg	1,233	100%
Regent Mall, Fredericton	494	100%
Richmond Centre, Richmond	793	50%
Rideau Centre, Ottawa	1,389	100%
Sherway Gardens, Toronto	986	100%
Shops at Don Mills, Toronto	470	100%
The Promenade, Toronto	704	100%
Toronto Eaton Centre, Toronto	1,710	100%

Property	Total Square Footage (thousands)	Effective % Ownership
Canadian Office Properties		
Encor Place, Calgary	359	100%
Granville Square, Vancouver	407	100%
HSBC Building, Vancouver	395	100%
Pacific Centre Office Complex, Vancouver	1,549	100%
PricewaterhouseCoopers Place, Vancouver	241	100%
RBC Centre, Toronto	1,226	100%
Shell Centre, Calgary	683	50%
Toronto-Dominion Centre Office Complex, Toronto	4,438	100%
Toronto Eaton Centre Office Complex, Toronto	1,897	100%
Waterfront Centre, Vancouver	410	100%
Yonge Corporate Centre, Toronto	669	100%
U.S. Regional Shopping Centres		
Lakewood Mall, Lakewood, California	2,093	49%
Los Cerritos Center, Cerritos, California	1,317	49%
Queens Center, Queens, New York	950	49%
Stonewood Center, Downey, California	923	49%
Washington Square, Tigard, Oregon	1,317	49%
U.K. Office Properties		
Thomas More Square Estate, London	558	50%

PRIVATE COMPANIES AND PARTNERSHIPS OVER $100 MILLION

(as at December 31, 2011)

AB Acquisition Holdings Ltd.
Acorn Care and Education Limited
Alliance Laundry Systems, LLC
AOT Bedding Holding Corp.
Apollo Overseas Partners (Delaware 892) VI, L.P.
Apollo Overseas Partners (Delaware 892) VII, L.P.
AQR Offshore Multi-Strategy Fund, Ltd.
ARC Energy Fund 5 Canadian Limited Partnership
Ares Corporate Opportunities Fund II, L.P.
Ares Corporate Opportunities Fund III, L.P.
Avaya Inc.
Barclays Private Credit Partners Fund L.P.
BC European Capital VIII
BDCM Intermediate Company A
BDCM Offshore Opportunity Fund II Ltd.
Birmingham International Airport
Bridgewater Pure Alpha Fund II Ltd.
Bristol Airports (Bermuda) Limited
The Brussels Airport Company
BANCO BTG Pactual S.A.
Camelot Group plc
The Campbell Global Assets Fund Limited SAC
Copenhagen Airport A/S
Crestline OT Opportunity Fund, L.P.
DaVinciRe Holdings Ltd.
Diamond Castle Partners IV-A, L.P.
Donnet Participações S.A.
Downsview Managed Account Platform Inc.
Easton-Bell Sports, LLC
Empresa de Servicios Sanitarios del Bio-Bio S.A.
EQT V (No. 2) Limited Partnership
Esval S.A.
Exal International Limited
Express Pipeline Ltd.
Flexera Holdings, LP
FountainVest China Growth Fund, L.P.
GCT Global Container Terminals Inc.
GMO Mean Reversion Fund (Offshore) L.P.
Gottex Real Asset Fund, L.P.
Grupo Corporativo Ono, S.A.
Hancock Timber Resource Group
HS1 Limited
Hudson Catastrophe Fund, Ltd.
INC Research, Inc.
IntelSat, Ltd.
InterGen N.V.
Ivanplats Ltd.
Manabi Holding S.A.
Maple Financial Group Inc.
Maple Leaf Sports & Entertainment Ltd.
Marathon Special Opportunity Fund Ltd.
MBK Partners Fund II, L.P.
MBK Partners, L.P.
Mitra Energy Limited
Munchkin, Inc.
NBCG Eaton Sub-Fund
Northern Star Generation LLC
Nuevosur, S.A.
NXT Capital Holdings, L.P.
OLE Media Management, L.P.
Orbis SICAV Global Equity Fund
Park Square Capital, LLC
Permira IV L.P.2
Pershing Square International, Ltd.
Providence Equity Partners Fund V L.P.
Providence Equity Partners Fund VI L.P.
Quinte Limited
R3, Ltd.
Resource Management Service Inc.
Rhône Offshore Partners III L.P.
Scotia Gas Networks PLC
Silver Creek Low Vol CO Cayman LP
Silver Creek Special Opportunities Fund Cayman II, L.P.
Silver Creek Special Opportunities Fund Cayman III, L.P.
Silver Lake Partners III, L.P.
Sociedad Austral de Electricidad S.A.
SonicWALL, Inc.
Steward Trust
TDR Capital II, L.P.
Trez Capital Corporation
ValueAct Capital International II, L.P.
Wellspring Capital Partners IV, L.P.
York Street Capital Partners II, L.P.

Eleven-year Review

(Canadian $ billions)	**2011**	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001
CHANGE IN NET ASSETS											
Income											
Investment income	**$11.74**	$13.27	$10.89	$(19.03)	$4.68	$12.31	$14.09	$10.80	$11.42	$(1.41)	$(1.74)
Contributions											
Members/transfers	**1.41**	1.35	1.29	1.13	1.06	0.83	0.79	0.75	0.71	0.68	0.64
Province of Ontario	**1.41**	1.35	1.43	1.18	1.08	0.82	0.78	0.75	0.72	0.70	0.68
Total income	**14.56**	15.97	13.61	(16.72)	6.82	13.96	15.66	12.30	12.85	(0.03)	(0.42)
Expenditures											
Benefits paid	**4.66**	4.50	4.39	4.20	4.02	3.82	3.62	3.43	3.20	3.08	3.08
Investment expenses	**0.29**	0.29	0.21	0.15	0.23	0.22	0.21	0.19	0.16	0.10	0.12
Client service expenses	**0.05**	0.05	0.04	0.04	0.04	0.03	0.03	0.03	0.03	0.03	0.04
Total expenditures	**5.00**	4.84	4.64	4.39	4.29	4.07	3.86	3.65	3.39	3.21	3.24
Increase/(decrease) in net assets	**$9.56**	$11.13	$8.97	$(21.11)	$2.53	$9.89	$11.80	$8.65	$9.46	$(3.24)	$(3.66)
NET ASSETS											
Investments											
Fixed income											
Bonds	**$26.50**	$22.73	$15.46	$14.22	$22.91	$20.86	$5.28	$8.96	$10.30	$13.80	$7.56
Real-rate products	**29.29**	23.24	19.88	17.41	11.06	11.80	10.56	11.90	7.07	5.92	6.98
Equities											
Canadian	**10.64**	9.29	8.43	6.21	13.73	16.39	19.26	16.80	15.19	13.43	17.06
Non-Canadian	**41.03**	38.20	32.75	28.72	36.31	32.42	25.78	23.09	19.13	18.19	24.28
Commodities	**5.64**	5.22	1.94	1.25	3.02	2.32	2.65	2.13	1.89	1.48	1.09
Real assets											
Real estate	**14.96**	16.86	14.21	13.48	13.41	11.12	8.75	7.20	6.20	7.28	7.25
Infrastructure	**8.71**	7.07	5.57	7.23	6.72	4.73	3.80	2.29	1.50	0.88	0.03
Timberland	**2.17**	2.22	2.34	2.80	2.12	2.05	0.97	0.70	0.40	0.09	–
Absolute return strategies	**12.33**	11.38	11.67	14.75	12.30	15.21	9.49	11.18	10.69	2.52	2.80
Money market	**(35.01)**	(31.49)	(18.74)	(20.97)	(13.58)	(11.22)	8.26	(2.53)	2.06	1.85	1.07
Net investments	**116.26**	104.72	93.51	85.10	108.00	105.68	94.80	81.72	74.43	65.44	68.12
Receivable from Province of Ontario	**2.72**	2.63	2.52	2.19	1.84	1.58	1.50	1.42	1.36	1.32	1.28
Other assets[1]	**40.81**	32.04	15.21	32.33	32.06	23.14	10.67	18.23	6.28	17.91	19.49
Total assets	**159.79**	139.39	111.24	119.62	141.90	130.40	106.97	101.37	82.07	84.67	88.89
Liabilities[1]	**(42.69)**	(31.86)	(14.84)	(32.18)	(33.35)	(24.39)	(10.84)	(17.04)	(6.39)	(18.46)	(19.43)
Net assets	**117.10**	107.53	96.40	87.44	108.55	106.01	96.13	84.33	75.68	66.21	69.46
Accrued pension benefits	**162.59**	146.89	131.86	118.14	115.46	110.50	110.53	96.73	83.12	73.67	65.43
(Deficit)/surplus[1]	**$(45.49)**	$(39.36)	$(35.46)	$(30.70)	$(6.91)	$(4.49)	$(14.40)	$(12.40)	$(7.44)	$(7.46)	$4.03

[1] Comparative figures have been revised to reflect the adoption of CICA Handbook Section 4600 and IFRS (see Note 1b to the financial statements).

PERFORMANCE (%)											
Rate of return	**11.2**	14.3	13.0	(18.0)	4.5	13.2	17.2	14.7	18.0	(2.0)	(2.3)
Benchmark	**9.8**	9.8	8.8	(9.6)	2.3	9.4	12.7	10.6	13.5	(4.8)	(5.3)

Funding Valuation History

Funding valuations must be filed with the pension regulator at least every three years. Valuation dates and voluntary filings are determined by OTF and the Ontario government. Filings must show the plan has sufficient assets to pay all future benefits to current plan members. For reference, all previously filed funding valuations and decisions made to use surplus or address shortfalls are detailed in this section. Assumptions used for each valuation are also reported below. The table summarizes all filed funding valuations that reflect the decisions of the sponsors as specified on page 124 of this annual report. In previous reports, figures for the years 1998–2001 were shown before the application of gains. Gains arose in those years as the plan performed better than the actuarial assumptions.

FILED FUNDING VALUATIONS[1]

(as at January 1) ($ billions)	2011	2009	2008	2005	2003	2002	2001	2000	1999	1998
Net assets	107.5	87.4	108.5	84.3	66.2	69.5	73.1	68.3	59.1	54.5
Smoothing adjustment	3.3	19.5	(3.6)	(1.5)	9.7	3.0	(4.3)	(7.3)	(5.1)	(6.0)
Value of assets	110.8	106.9	104.9	82.8	75.9	72.5	68.8	61.0	54.0	48.5
Future basic contributions	33.8	25.9	23.6	16.7	14.7	13.7	12.7	13.4	12.0	12.3
Future special contributions	3.8	5.5	5.6	6.2	–	–	–	–	–	–
Future matching of CIP benefit reduction	5.1	–	–	–	–	–	–	–	–	–
Special payments[2]	–	–	–	–	–	–	–	–	0.2	3.9
Total assets	153.5	138.3	134.1	105.7	90.6	86.2	81.5	74.4	66.2	64.7
Cost of future pensions	(158.4)[3]	(137.5)[3]	(134.1)[3]	(105.6)	(89.1)	(84.3)	(80.9)	(69.9)	(66.2)	(64.7)
Reduction in cost due to CIP	5.1	–	–	–	–	–	–	–	–	–
Surplus	0.2	0.8	0.0	0.1	1.5	1.9	0.6	4.5	0.0	0.0

[1] Valuation filing dates determined by the plan sponsors.

[2] Owed by the Ontario government to pay off the plan's initial unfunded liability in 1990. The government used its portion of plan surpluses in the 1990s to eliminate the remaining payments.

[3] Assumes 100% inflation protection.

ASSUMPTIONS USED FOR FILED VALUATIONS

(as at January 1) (percent)	2011	2009	2008	2005	2003	2002	2001	2000	1999	1998
Rate of return	5.40	5.00	5.65	6.475	6.40	6.30	6.25	6.50	7.50	7.50
Inflation	2.15	1.35	2.20	2.750	2.05	1.90	2.20	2.25	3.50	3.50
Real rate of return	3.25	3.65	3.45	3.725	4.35	4.40	4.05	4.25	4.00	4.00

FUNDING DECISIONS

The plan sponsors jointly decide what benefits the plan will provide; the contribution rate paid by working members and matched by government and other designated employers; and how any funding shortfall is addressed and any surplus is used. A history of the sponsors' plan funding decisions follows:

1990: A preliminary unfunded liability of $7.8 billion to be amortized over 40 years by special payments from the Ontario government; basic contribution rate increased to 8% from 7%.

1993: A preliminary $1.5 billion surplus was distributed; $1.2 billion used to reduce government's special payments; $0.3 billion used to offset government cost reductions in the education sector (social contract days).

1996: A preliminary $0.7 billion surplus was distributed; $0.6 billion used to reduce early retirement penalty to 2.5% from 5% for each point short of 90 factor and lower the CPP reduction after age 65 (to 0.68% from 0.7%).

1998: A preliminary $6.8 billion surplus was distributed; $2.2 billion to pay for the 85 factor window from 1998 to 2002 and further lower the CPP reduction to 0.6%; $4.6 billion to reduce the value of special payments owed by the government; OTF and Ontario government agree future surplus would be used to eliminate the government's remaining special payments, and the next $6.2 billion would be available to OTF for benefit improvements.

1999: A preliminary $3.5 billion surplus was distributed; $3.5 billion to eliminate government's remaining special payments.

2000: $4.5 billion surplus; no changes to benefits or contribution levels.

2001: A preliminary $6.8 billion surplus was distributed; $6.2 billion to pay for benefit improvements: permanent 85 factor; 10-year pension guarantee; reduced pension as early as age 50; lower CPP reduction (to 0.45%); 5-year average Year's Maximum Pensionable Earnings (YMPE) to calculate CPP reduction; pension recalculation based on approximate best-5 salary for older pensioners; and top-up waived for Long-Term Income Protection (LTIP) contributions; $76 million was set aside in a contingency reserve to be used by OTF at a later date.

2002: $1.9 billion surplus; no changes to benefits or contribution levels.

2003: $1.5 billion surplus; no changes to benefits or contribution levels; Funding Management Policy adopted by plan sponsors.

2005: $6.1 billion preliminary funding shortfall resolved, leaving plan with a $0.1 billion surplus; plan sponsors introduced special contribution rate increases to resolve the shortfall, totalling 3.1% of base earnings by 2009 for teachers, the Ontario government and other employers; OTF used the $76 million contingency reserve set aside in 2001 to reduce contribution rate increases for members in 2008.

2008: $12.7 billion preliminary funding shortfall resolved, leaving the plan in a balanced position; plan sponsors introduced conditional inflation protection for pension benefits earned after 2009 and increased the basic contribution rate to 9% from 8%.

2009: $2.5 billion preliminary funding shortfall resolved primarily by assuming a slightly higher long-term rate of return on investments: RRB yield plus 1.5% versus RRB plus 1.4%. Other minor changes made to assumptions to reflect recent plan experience.

2011: $17.2 billion preliminary shortfall resolved with 1.1% contribution rate increase (phased in over three years), slightly smaller annual cost-of-living increases for teachers who retired after 2009, and recognition of current contribution rate as the permanent base rate.

Corporate Directory

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Jim Leech

Audit Services
Carol Gordon, Vice-President

enterprise Project Management Office
Jacqueline Beaurivage, Vice-President

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David McGraw, Senior Vice-President and Chief Financial Officer
Calum McNeil, Vice-President
Jennifer Newman, Vice-President
George Wong, Vice-President

Human Resources
Marcia Mendes-d'Abreu, Vice-President

Legal
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Jeff Davis, Vice-President

Information and Technology
Russ Bruch, Vice-President, Chief Information Officer
Douglas Gerhart, Vice-President
Maryam Ghiai, Vice-President
Phil Nichols, Vice-President

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Rosemarie McClean, Senior Vice-President

Investment Division
Neil Petroff, Executive Vice-President and Chief Investment Officer

Asset Mix and Risk
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James Davis, Vice-President
Scott Picket, Vice-President

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Olivia Steedman, Vice-President

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Lee Sienna, Vice-President

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Jo Taylor, Vice-President

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THE CADILLAC FAIRVIEW CORPORATION LIMITED

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Finance
Cathal J. O'Connor, Executive Vice-President and Chief Financial Officer

General Counsel and Secretary
Sandra J. Hardy, Executive Vice-President

Investments
Russell Goin, Executive Vice-President

Operations
Ron Wratschko, Executive Vice-President

ANNUAL MEETING

April 12, 2012 at 5 p.m.
The Carlu
444 Yonge Street, 7th floor
Toronto

We welcome your comments and suggestions on this annual report.

Please contact:
Deborah Allan
Director, Communications and Media Relations
Tel: 416-730-5347
E-mail: communications@otpp.com

Ontario Teachers' Pension Plan
5650 Yonge Street,
Toronto, Ontario M2M 4H5
416-228-5900

London U.K. Office:
Leconfield House, Curzon Street
London W1J 5JA
+44 20 7659 4450

New York Office:
375 Park Avenue, Suite 3508
New York, NY 10152
212-888-5799

Concept and Design: THE WORKS DESIGN COMMUNICATIONS LTD. www.worksdesign.com

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