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Great-West Life
ASSURANCE COMPANY

Annual Report 2011

## CAUTIONARY NOTE REGARDING FORWARD-LOOKING INFORMATION

This report contains some forward-looking statements about the Company, including its business operations, strategy and expected financial performance and condition. Forward-looking statements include statements that are predictive in nature, depend upon or refer to future events or conditions, or include words such as "expects", "anticipates", "intends", "plans", "believes", "estimates" and similar expressions or negative versions thereof. In addition, any statement that may be made concerning future financial performance (including revenues, earnings or growth rates), ongoing business strategies or prospects, and possible future action by the Company, including statements made by the Company with respect to the expected benefits of acquisitions or divestitures, are also forward-looking statements. Forward-looking statements are based on current expectations and projections about future events and are inherently subject to, among other things, risks, uncertainties and assumptions about the Company, economic factors and the financial services industry generally, including the insurance and mutual fund industries. They are not guarantees of future performance, and actual events and results could differ materially from those expressed or implied by forward-looking statements made by the Company due to, but not limited to, important factors such as sales levels, premium income, fee income, expense levels, mortality experience, morbidity experience, policy lapse rates, taxes, general economic, political and market factors in North America and internationally, interest and foreign exchange rates, global equity and capital markets, business competition, technological change, changes in government regulations, changes in accounting policies and the effect of applying future accounting policy changes including future policy changes required under International Financial Reporting Standards (IFRS), unexpected judicial or regulatory proceedings, catastrophic events, and the Company's ability to complete strategic transactions and integrate acquisitions. The reader is cautioned that the foregoing list of important factors is not exhaustive, and there may be other factors, including factors set out under "Risk Management and Control Practices" and "Summary of Critical Accounting Estimates" in the Company's 2011 Annual Management's Discussion and Analysis, and any listed in other filings with securities regulators, which are available for review at www.sedar.com. The reader is also cautioned to consider these and other factors carefully and not to place undue reliance on forward-looking statements. Other than as specifically required by applicable law, the Company does not intend to update any forward-looking statements whether as a result of new information, future events or otherwise.

## CAUTIONARY NOTE REGARDING NON-IFRS FINANCIAL MEASURES

This report contains some non-IFRS financial measures. Terms by which non-IFRS financial measures are identified include, but are not limited to, "operating earnings", "constant currency basis", "premiums and deposits", "sales", and other similar expressions. Non-IFRS financial measures are used to provide management and investors with additional measures of performance. However, non-IFRS financial measures do not have standard meanings prescribed by IFRS and are not directly comparable to similar measures used by other companies. Please refer to the appropriate reconciliations of these non-IFRS financial measures to measures prescribed by IFRS.

## BASIS OF PRESENTATION AND SUMMARY OF ACCOUNTING POLICIES

The consolidated financial statements of the Company, which are the basis for data presented in this report, have been prepared in accordance with IFRS and are presented in millions of Canadian dollars unless otherwise indicated.

## CORPORATE PROFILE

Great-West Life is a leading Canadian insurer, with interests in life insurance, health insurance, investment, savings and retirement income and reinsurance businesses, primarily in Canada and Europe.

In Canada, Great-West Life and its subsidiaries, London Life and Canada Life, offer a broad portfolio of financial and benefit plan solutions and serve the financial security needs of more than 12 million people.

Great-West Life's products include a wide range of investment, savings and retirement income plans, payout annuities, as well as life, disability, critical illness and health insurance for individuals and families. These products and services are distributed through a diverse network of financial security advisors and brokers associated with Great-West Life; financial security advisors associated with London Life's Freedom 55 Financial™ division and the Wealth & Estate Planning Group; and the distribution channels Canada Life supports, including independent advisors associated with managing general agencies, as well as national accounts including Investors Group.

For large and small businesses and organizations, Great-West Life offers a variety of group benefit plan solutions featuring options such as life, healthcare, dentalcare, critical illness, disability and wellness, international benefits plans, plus convenient online services. The Company also offers group retirement and savings plans that are tailored to the unique needs of businesses and organizations. These products and services are distributed through financial security advisors associated with our companies, as well as independent advisors, brokers and consultants.

In Europe, Great-West Life has operations in the United Kingdom, Isle of Man, Ireland and Germany through Canada Life. Canada Life provides individuals and their families with a broad range of insurance and wealth management products. These include payout annuities, investments and group insurance in the United Kingdom; savings and individual insurance in the Isle of Man; individual insurance and savings, and pension products in Ireland; and fund-based pensions, critical illness and disability insurance in Germany.

Great-West Life participates in international reinsurance markets through Canada Life Reinsurance and London Reinsurance Group, providing life, annuity and property and casualty reinsurance in the United States and in international markets.

Great-West Life has $204 billion* in consolidated assets under administration and is a subsidiary of Great-West Lifeco Inc., a member of the Power Financial Corporation group of companies.

For more information on Great-West Life, including current ratings, visit **www.greatwestlife.com**.

**as of December 31, 2011*

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# DIRECTORS' REPORT

In 2011 Great-West Life and its subsidiaries in Canada and Europe continued to deliver strong performance. Our conservative investment practices and disciplined approach to introducing new products and managing expenses have served us well over the long term and position us well for organic growth.

### Performance measures

Measures of Great-West Life's performance in 2011 include:

- Premiums and deposits remained strong, at $28.3 billion.
- In Canada, mutual fund net deposits to the *Quadrus Group of Funds*™ at 5.2% of opening assets outpaced the mutual fund industry, which had 1.9% net sales.
- Common shareholder operating earnings of $1.8 billion, a non-IFRS financial measure, were 11.6% higher than in 2010.
- General account assets were $114.7 billion, an increase of 6% over 2010.
- Segregated fund net assets increased 1% from December 31, 2010.
- Policyholder dividends were $1.1 billion compared to $1.0 billion the prior year.
- Net earnings in the participating accounts after policyholder dividends was $117 million.

The Company's capital position remains very strong. Great-West Life reported a Minimum Continuing Capital and Surplus Requirements (MCCSR) ratio of 204% at December 31, 2011, compared to 203% at December 31, 2010. This measure of capital strength remains at the upper end of our target operating range. It does not include any benefit from the approximately $0.6 billion of net proceeds from capital transactions held by its parent, Great-West Lifeco.

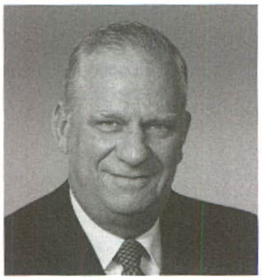
We have a high quality bond portfolio, with 99% rated investment grade at December 31, 2011.

### Canada – products and distribution

In Canada, Great-West Life, together with London Life and Canada Life, maintained leading market positions in our individual and group businesses. Our continued focus on prudent product and service enhancements, diversified distribution and operating efficiencies continue to position us for solid organic growth.

We continued to see strong sustained performance in our Canadian businesses. Our individual insurance business grew slightly faster than the market; our group retirement services business recorded solid growth; our group insurance business continued to experience strong persistency; and our individual segregated fund and mutual fund businesses maintained positive net cash flows.

Raymond L. McFeetors



D. Allen Loney

### Individual businesses

The Canadian operations continued to focus on distribution support and development in 2011, both in the exclusive and independent distribution channels. The relationship we have with advisors supports the very strong persistency of our business, provides a strategic advantage for us and contributes to strong market share across our multiple lines of business.

Together, Great-West Life, London Life and Canada Life remain Canada's number one provider of individual insurance solutions. From term, universal and participating life insurance to individual disability and critical illness insurance, our broad range of products gives advisors choice and flexibility in meeting clients' diverse individual needs. Our companies are the leading provider of participating life insurance and continue to focus on excellence in managing and growing our participating business. Within our group of companies participating products have been continuously offered since 1847 and policyholder dividends have been paid every year. With over 65 years' experience in the individual disability insurance market, Great-West Life, together with Canada Life, is a leading provider of individual disability and critical illness insurance in Canada.

Great-West Life, London Life and Canada Life offer a broad choice of investment, savings and income products. These include segregated funds, as well as mutual funds offered through Quadrus Investment Services Ltd., a mutual fund dealer affiliated with Great-West Life.

### Group businesses

In 2011, Great-West Life continued to use technology to enhance services and deepen our relationship with our customers. We were the first in the industry to offer text message notifications for plan members on their health and dental claims, and to launch an iPhone application: DrugHub™ – a virtual medicine cabinet to help people manage their prescription drugs. We significantly expanded our Provider eClaims service. The number of physiotherapy, chiropractic, massage and visioncare providers who can submit claims electronically on behalf of their patients more than doubled during the year to over 9,000.

As a leading provider of group benefit solutions, Great-West continues to advance the cause of workplace mental health in Canada. In 2011, the Great-West Life Centre for Mental Health in the Workplace™ launched *Managing Emotions*, a comprehensive awareness, education and training program offered at no cost to employers. This joins a range of resources to help employers understand and take steps to improve mental health in the workplace, all publicly available through the Centre's website.

Group capital accumulation plans are a core business for Great-West Life and education for plan members is an ongoing priority. We expanded and enhanced our retirement education tools in a range of formats, including videos, online resources and print materials to help plan members at any age and stage of retirement planning.

Our group retirement and savings plans are tailored to the unique needs of small, medium and large businesses and organizations.

Great-West Life continues to offer an important perspective on pension reform, to help ensure that Canadians save adequately and effectively for their retirement. The pending implementation of Pooled Registered Pension Plans is an important development in helping working Canadians save for retirement.

**Europe**

In Europe, Great-West Life, through its subsidiary Canada Life, has operations in the United Kingdom, Isle of Man, Ireland and Germany.

As a result of our continued focus on credit and expense controls, our European operations were in a strong position coming into 2011, and this focus was maintained throughout the year. Additionally, there was a renewed focus on risk and risk management as we prepare for the advent of Solvency II in Europe.

In the U.K., we continued to grow premium volumes, especially in our Isle of Man product range, despite economic challenges which adversely affected our group insurance business. Sales of payout annuities were very strong in the early part of 2011, though competitive pressures and a lack of quality investment opportunities resulted in slower sales throughout the rest of the year.

In Germany, Canada Life operates in the independent broker market and is one of the leading insurers for guaranteed unit linked products in the broker segment. Despite challenging market conditions for unit linked providers, our retirement savings product sales, and in particular sales of our market leading Guaranteed Minimum Withdrawal Benefit (GMWB) product, showed strong growth in 2011. Our serious illness and GMWB products retained their status as the leading products in their categories in a recent poll of insurance intermediaries.

In Ireland, Canada Life became the first company to launch a guaranteed variable annuity product, and also launched a new Income Opportunities Fund, managed by Setanta Asset Management, the group's asset manager in Ireland.

Great-West Life participates in international reinsurance markets through Canada Life Reinsurance and London Reinsurance Group, providing life, annuity and property and casualty reinsurance in the United States and in international markets.

In 2011, reinsurance demand remained strong, particularly for structured reinsurance solutions with U.S. life insurers. We continued to leverage our financial strength, disciplined risk-management practices and excellent client relationships to achieve strong business results in the face of significant catastrophe impacts early in the year. We continue to follow capital developments globally for potential business opportunities.

**Giving back to our communities**

As an organization and as individuals, we are proud to contribute to the development of stronger communities. As an Imagine Caring Company, the financial and volunteer support we provide to hundreds of charitable, non-profit and community-based organizations is aimed at meeting a high standard of corporate citizenship.

Key to our approach is the engagement of staff and distribution associates, whose efforts embody our commitment to responsible corporate citizenship.

**Board of Directors**

On behalf of the Board of Directors, it is our pleasure to recognize the professionalism and continuing dedication of the people across our companies who serve our clients and distribution associates worldwide. We also thank our clients and distribution associates for their continued support.

**Raymond L. McFeetors**
Chairman of the Board

**D. Allen Loney**
President and
Chief Executive Officer

# FINANCIAL HIGHLIGHTS *(unaudited)*

| (in Canadian $ millions except per share amounts) | As at or for the three months ended December 31 2011 | September 30 2011 | December 31 2010 | For the twelve months ended December 31 2011 | December 31 2010 |
|---|---|---|---|---|---|
| Premiums and deposits: | | | | | |
| Life insurance, guaranteed annuities and insured health products | **$ 3,521** | $ 3,433 | $ 3,716 | **$ 14,173** | $ 14,550 |
| Self funded premium equivalents (ASO contracts) | **651** | 660 | 654 | **2,645** | 2,575 |
| Segregated funds deposits: | | | | | |
| Individual products | **1,743** | 1,940 | 1,983 | **7,146** | 6,643 |
| Group products | **922** | 835 | 920 | **3,615** | 3,744 |
| Proprietary mutual funds deposits | **169** | 149 | 164 | **724** | 616 |
| Total premiums and deposits | **7,006** | 7,017 | 7,437 | **28,303** | 28,128 |
| Fee and other income | **437** | 409 | 401 | **1,673** | 1,575 |
| Paid or credited to policyholders | **5,327** | 5,489 | 2,811 | **18,962** | 18,862 |
| Operating earnings – common shareholder | **546** | 441 | 336 | **1,825** | 1,635 |
| Summary of net earnings attributable to: | | | | | |
| Participating account | **105** | 7 | (17) | **117** | (10) |
| Preferred shareholders | **–** | – | – | **–** | 7 |
| Common shareholder | **670** | 441 | 336 | **1,949** | 1,346 |
| **Per common share** | | | | | |
| Operating earnings | **$ 258.43** | $ 208.22 | $ 159.18 | **$ 862.30** | $ 781.11 |
| Basic earnings | **316.60** | 208.22 | 159.18 | **920.47** | 642.94 |
| Dividends paid | **140.06** | 131.60 | – | **540.46** | 415.44 |
| Book value | **5,627.00** | 5,510.00 | 5,184.00 | | |
| Total assets | **$ 188,942** | $ 186,618 | $ 182,256 | | |
| Proprietary mutual funds net assets | **3,318** | 3,179 | 3,272 | | |
| Total assets under management | **192,260** | 189,797 | 185,528 | | |
| Other assets under administration | **11,560** | 11,344 | 11,762 | | |
| Total assets under administration | **$ 203,820** | $ 201,141 | $ 197,290 | | |
| Participating account surplus | **$ 2,216** | $ 2,100 | $ 2,038 | | |
| Shareholders' equity | **11,913** | 11,664 | 10,974 | | |
| Total equity | **$ 14,129** | $ 13,764 | $ 13,012 | | |

The Company uses operating earnings, a non-IFRS financial measure, which excludes the impact of litigation provisions in note 29 to the Company's annual consolidated financial statements.

## FINANCIAL REPORTING RESPONSIBILITY

The consolidated financial statements are the responsibility of management and are prepared in accordance with International Financial Reporting Standards (IFRS) for life insurance enterprises, including the accounting requirements of the Office of the Superintendent of Financial Institutions Canada. The financial information contained elsewhere in the annual report is consistent with that in the consolidated financial statements. The consolidated financial statements necessarily include amounts that are based on management's best estimates. These estimates are based on careful judgments and have been properly reflected in the consolidated financial statements. In the opinion of management, the accounting practices utilized are appropriate in the circumstances and the consolidated financial statements present fairly, in all material respects, the financial position of the Company and its segregated funds and the results of its operations and its cash flows and the changes in assets of its segregated funds in accordance with IFRS, including the requirements of the Office of the Superintendent of Financial Institutions Canada.

In carrying out its responsibilities, management maintains appropriate internal control over financial reporting designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with IFRS, including the requirements of the Office of the Superintendent of Financial Institutions Canada.

The consolidated financial statements were approved by the Board of Directors, which has oversight responsibilities with respect to financial reporting. The Board of Directors carries out this responsibility principally through the Audit Committee, which comprises non-management directors. The Audit Committee is charged with, among other things, the responsibility to:

- Review the interim and annual consolidated financial statements and report thereon to the Board of Directors.
- Review internal control procedures.
- Review the independence of the external auditors and the terms of their engagement and recommend the appointment and compensation of the external auditors to the Board of Directors.
- Review other audit, accounting and financial reporting matters as required.

In carrying out the above responsibilities, this Committee meets regularly with management, and with both the Company's external and internal auditors to review their respective audit plans and to review their audit findings. The Committee is readily accessible to external and internal auditors and to the Appointed Actuary.

The Board of Directors of the Company, pursuant to the *Insurance Companies Act* (Canada), appoints an Actuary who is a Fellow of the Canadian Institute of Actuaries. The Actuary:

- Ensures that the assumptions and methods used in the valuation of policy liabilities are in accordance with accepted actuarial practice, applicable legislation and associated regulations and directives.
- Provides an opinion regarding the appropriateness of the policy liabilities at the balance sheet date to meet all policyholder obligations. Examination of supporting data for accuracy and completeness and analysis of assets for their ability to support the policy liabilities are important elements of the work required to form this opinion.
- Annually analyzes the financial condition of the Company and prepares a report for the Board of Directors. The analysis covers a five year period, and tests the projected capital adequacy of the Company, under adverse economic and business conditions.

Deloitte & Touche LLP Chartered Accountants, as the Company's external auditors, have audited the consolidated financial statements. The Auditors' Report to the Policyholders and Shareholders is presented following the consolidated financial statements. Their opinion is based upon an examination conducted in accordance with Canadian generally accepted auditing standards, performing such tests and other procedures as they consider necessary in order to obtain reasonable assurance that the consolidated financial statements present fairly, in all material respects, the financial position of the Company and its segregated funds and the results of its operations and its cash flows and the changes in assets of its segregated funds in accordance with IFRS.

| | |
|---|---|
| **D. Allen Loney** | **William W. Lovatt** |
| President and | Executive Vice-President and |
| Chief Executive Officer | Chief Financial Officer |

February 9, 2012

# CONSOLIDATED STATEMENTS OF EARNINGS

(in Canadian $ millions except per share amounts)

| For the years ended December 31 | 2011 | 2010 |
|---|---|---|
| **Income** | | |
| Premium income | | |
| Gross premiums written | $ 16,979 | $ 17,296 |
| Ceded premiums | (2,806) | (2,746) |
| Total net premiums | 14,173 | 14,550 |
| Net investment income (note 5) | | |
| Regular net investment income | 4,352 | 4,511 |
| Changes in fair value through profit or loss | 3,795 | 3,197 |
| Total net investment income | 8,147 | 7,708 |
| Fee and other income | 1,673 | 1,575 |
| | 23,993 | 23,833 |
| **Benefits and expenses** | | |
| Policyholder benefits | | |
| Insurance and investment contracts | | |
| Gross | 14,517 | 15,104 |
| Ceded | (1,472) | (2,042) |
| | 13,045 | 13,062 |
| Policyholder dividends and experience refunds | 1,224 | 1,261 |
| Change in insurance and investment contract liabilities | 4,693 | 4,539 |
| Total paid or credited to policyholders | 18,962 | 18,862 |
| Commissions | 1,335 | 1,270 |
| Operating and administrative expenses (note 27) | 919 | 1,818 |
| Premium taxes | 235 | 227 |
| Financing charges (note 15) | 79 | 74 |
| Amortization of finite life intangible assets | 54 | 47 |
| **Earnings before income taxes** | 2,409 | 1,535 |
| Income taxes (note 26) | 343 | 185 |
| **Net earnings before non-controlling interests** | 2,066 | 1,350 |
| Attributable to non-controlling interests | – | 7 |
| **Net earnings** | 2,066 | 1,343 |
| Net earnings (loss) – participating account (note 19) | 117 | (10) |
| **Net earnings – shareholders** | 1,949 | 1,353 |
| Preferred share dividends | – | 7 |
| **Net earnings – common shareholder** | $ 1,949 | $ 1,346 |
| **Earnings per common share** | $ 920.47 | $ 642.94 |

# CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in Canadian $ millions)

| For the years ended December 31 | 2011 | 2010 |
|---|---|---|
| **Net earnings** | $ 2,066 | $ 1,343 |
| **Other comprehensive income (loss)** | | |
| Unrealized foreign exchange gains (losses) on translation of foreign operations | 82 | (368) |
| Income tax (expense) benefit | 1 | – |
| Unrealized gains (losses) on available for sale assets | 218 | 99 |
| Income tax (expense) benefit | (47) | (19) |
| Realized (gains) losses on available for sale assets | (81) | (59) |
| Income tax expense (benefit) | 18 | 10 |
| | 191 | (337) |
| **Comprehensive income** | $ 2,257 | $ 1,006 |

# CONSOLIDATED BALANCE SHEETS

(in Canadian $ millions)

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| **Assets** | | | |
| Cash and cash equivalents (note 4) | $ 1,855 | $ 1,557 | $ 3,030 |
| Bonds (note 5) | 60,481 | 55,001 | 50,183 |
| Mortgage loans (note 5) | 14,849 | 14,393 | 15,033 |
| Stocks (note 5) | 6,384 | 6,265 | 5,904 |
| Investment properties (note 5) | 3,198 | 2,953 | 2,609 |
| Loans to policyholders | 2,858 | 2,808 | 2,786 |
| | 89,625 | 82,977 | 79,545 |
| Funds held by ceding insurers (note 6) | 9,923 | 9,856 | 10,984 |
| Goodwill (note 10) | 5,267 | 5,267 | 5,270 |
| Intangible assets (note 10) | 1,511 | 1,515 | 1,538 |
| Derivative financial instruments (note 28) | 927 | 930 | 693 |
| Owner occupied properties (note 11) | 357 | 310 | 291 |
| Fixed assets (note 11) | 97 | 85 | 91 |
| Reinsurance assets (note 14) | 4,046 | 4,433 | 4,889 |
| Other assets (note 12) | 2,935 | 3,226 | 3,068 |
| Deferred tax assets (note 26) | 31 | 19 | 63 |
| Segregated funds for the risk of unitholders (note 13) | 74,223 | 73,638 | 67,805 |
| **Total assets** | $ 188,942 | $ 182,256 | $ 174,237 |
| **Liabilities** | | | |
| Insurance contract liabilities (note 14) | $ 94,111 | $ 88,929 | $ 87,446 |
| Investment contract liabilities (note 14) | 746 | 764 | 820 |
| Debentures and other debt instruments (note 16) | 303 | 304 | 305 |
| Funds held under reinsurance contracts | 630 | 582 | 758 |
| Derivative financial instruments (note 28) | 273 | 148 | 188 |
| Other liabilities (note 17) | 2,937 | 3,371 | 2,686 |
| Deferred tax liabilities (note 26) | 796 | 621 | 557 |
| Repurchase agreements | 23 | 114 | 17 |
| Capital trust securities (note 18) | 771 | 773 | 778 |
| Investment and insurance contracts on account of unitholders (note 13) | 74,223 | 73,638 | 67,805 |
| **Total liabilities** | 174,813 | 169,244 | 161,360 |
| **Equity** | | | |
| Participating account surplus (note 19) | 2,216 | 2,038 | 2,040 |
| Non-controlling interests | – | – | 147 |
| Shareholders' equity | | | |
| Share capital (note 20) | | | |
| Preferred shares | 1 | 1 | 158 |
| Common shares | 6,426 | 6,426 | 6,116 |
| Accumulated surplus | 5,418 | 4,613 | 4,140 |
| Accumulated other comprehensive income (loss) | (150) | (280) | 65 |
| Contributed surplus | 218 | 214 | 211 |
| **Total equity** | 14,129 | 13,012 | 12,877 |
| **Total liabilities and equity** | $ 188,942 | $ 182,256 | $ 174,237 |

# CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(in Canadian $ millions)

| | December 31, 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Share capital | Contributed surplus | Accumulated surplus | Accumulated other comprehensive income (loss) | Total shareholders' equity | Non-controlling interests | Participating account surplus | Total equity |
| Balance, beginning of year | $ 6,427 | $ 214 | $ 4,613 | $ (280) | $ 10,974 | $ – | $ 2,038 | $ 13,012 |
| Net earnings | – | – | 1,949 | – | 1,949 | – | 117 | 2,066 |
| Other comprehensive income (loss) | – | – | – | 130 | 130 | – | 61 | 191 |
| | 6,427 | 214 | 6,562 | (150) | 13,053 | – | 2,216 | 15,269 |
| Dividends to common shareholder | – | – | (1,144) | – | (1,144) | – | – | (1,144) |
| Share based payments | – | 4 | – | – | 4 | – | – | 4 |
| Balance, end of year | $ 6,427 | $ 218 | $ 5,418 | $ (150) | $ 11,913 | $ – | $ 2,216 | $ 14,129 |

| | December 31, 2010 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Share capital | Contributed surplus | Accumulated surplus | Accumulated other comprehensive income (loss) | Total shareholders' equity | Non-controlling interests | Participating account surplus | Total equity |
| Balance, beginning of year | $ 6,274 | $ 211 | $ 4,140 | $ 65 | $ 10,690 | $ 147 | $ 2,040 | $ 12,877 |
| Net earnings | – | – | 1,353 | – | 1,353 | – | (10) | 1,343 |
| Other comprehensive income (loss) | – | – | – | (345) | (345) | – | 8 | (337) |
| | 6,274 | 211 | 5,493 | (280) | 11,698 | 147 | 2,038 | 13,883 |
| Redemption of preferred shares in subsidiary | – | – | (5) | – | (5) | (147) | – | (152) |
| Redemption of Series O preferred shares | (157) | – | – | – | (157) | – | – | (157) |
| Issue common shares to parent | 310 | – | – | – | 310 | – | – | 310 |
| Dividends to shareholders | | | | | | | | |
| Preferred shareholders | – | – | (7) | – | (7) | – | – | (7) |
| Common shareholder | – | – | (868) | – | (868) | – | – | (868) |
| Share based payments | – | 3 | – | – | 3 | – | – | 3 |
| Balance, end of year | $ 6,427 | $ 214 | $ 4,613 | $ (280) | $ 10,974 | $ – | $ 2,038 | $ 13,012 |

# CONSOLIDATED STATEMENTS OF CASH FLOWS

(in Canadian $ millions)

| For the years ended December 31 | 2011 | 2010 |
|---|---|---|
| **Operations** | | |
| Earnings before income taxes | $ 2,409 | $ 1,535 |
| Income taxes paid, net of refunds received | 197 | 75 |
| Adjustments: | | |
| Change in insurance and investment contract liabilities | 4,378 | 4,653 |
| Change in funds held by ceding insurers | 478 | 679 |
| Change in funds held under reinsurance contracts | 25 | (121) |
| Change in deferred acquisition costs | (15) | (49) |
| Change in reinsurance assets | 464 | 241 |
| Changes in fair value through profit or loss | (3,795) | (3,197) |
| Other | (554) | 816 |
| Cash flows from operations | 3,587 | 4,632 |
| **Financing Activities** | | |
| Issue of common shares to parent | – | 310 |
| Redemption of preferred shares | – | (157) |
| Redemption of preferred shares in subsidiary | – | (150) |
| Repayment of debentures and other debt instruments | (1) | (1) |
| Dividends paid on common shares | (1,144) | (868) |
| Dividends paid on preferred shares | – | (7) |
| | (1,145) | (873) |
| **Investment Activities** | | |
| Bond sales and maturities | 13,606 | 13,718 |
| Mortgage loan repayments | 1,660 | 1,939 |
| Stock sales | 2,227 | 2,238 |
| Investment property sales | 70 | 16 |
| Change in loans to policyholders | (38) | (46) |
| Investment in bonds | (14,760) | (18,894) |
| Investment in mortgage loans | (2,098) | (1,581) |
| Investment in stocks | (2,619) | (2,046) |
| Investment in investment properties | (209) | (376) |
| | (2,161) | (5,032) |
| Effect of changes in exchange rates on cash and cash equivalents | 17 | (200) |
| **Increase (decrease) in cash and cash equivalents** | 298 | (1,473) |
| **Cash and cash equivalents, beginning of year** | 1,557 | 3,030 |
| **Cash and cash equivalents, end of year** | $ 1,855 | $ 1,557 |
| **Supplementary cash flow information** | | |
| Interest income received | $ 3,749 | $ 3,754 |
| Interest paid | $ 81 | $ 76 |
| Dividend income received | $ 181 | $ 174 |

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in Canadian $ millions except per share amounts)

## 1. Corporate Information

The Great-West Life Assurance Company (Great-West Life or the Company) is incorporated and domiciled in Canada. The registered address of the Company is 100 Osborne Street North, Winnipeg, Manitoba, Canada, R3C 1V3. Great-West Life is wholly-owned by Great-West Lifeco Inc. (Lifeco).

Great-West Life is a leading Canadian insurer, with interests in the life and health insurance, investment, savings and retirement income and reinsurance businesses, primarily in Canada and Europe through its major subsidiaries London Insurance Group Inc. (LIG), Canada Life Financial Corporation (CLFC), GLC Asset Management Ltd. and GWL Realty Advisors Inc.

The consolidated financial statements of the Company for the year ended December 31, 2011 were authorized for issue by the Board of Directors on February 9, 2012.

## 2. Basis of Presentation and Summary of Accounting Policies

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB).

The financial statements are prepared using IFRS accounting policies which became Canadian generally accepted accounting principles (CGAAP) for publicly accountable enterprises and were adopted by the Company for fiscal years beginning on January 1, 2011. These accounting policies are based on the IFRS standards and IFRS Interpretations Committee (IFRIC) interpretations that the Company applied at December 31, 2011.

Prior to the adoption of IFRS the Company's financial statements were prepared in accordance with the previous CGAAP, which differs in some areas from IFRS. See note 3 for an explanation of how the adoption of IFRS has affected the reported financial position, financial performance and accounting policies of the Company. This note includes reconciliations of equity and comprehensive income under IFRS for the comparative periods and of equity at the date of transition reported under previous CGAAP for those periods and at the date of transition to IFRS.

### *Basis of Consolidation*

The consolidated financial statements comprise the financial statements of the Company as at December 31, 2011. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Company obtains control, and continue to be consolidated until the date that such control ceases. All intra-group balances, transactions, income and expenses and profits and losses, including dividends resulting from intra-group transactions, are eliminated on consolidation.

### *Critical Estimates and Judgments*

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the reporting date and the reported amounts of revenues and expenses during the reporting period. Areas where estimates and judgments are exercised by management include the valuation and classification of insurance and investment contract liabilities, determination of the fair value and classification for certain financial assets and liabilities, goodwill and indefinite life intangible assets, income taxes, contingencies and pension plans and other post-employment benefits. In addition, the financial statements required management's judgments in accounting for deferred income reserves (DIR) and deferred acquisition costs (DAC), the valuation of deferred income tax assets, the level of componentization of property, plant and equipment, determination of relationships with subsidiaries and special purpose entities and the identification of cash generating units and operating segments. Actual results will differ from those estimates. Areas where significant estimates and judgments have been applied by management are described further in the significant accounting policies below.

The annual results of the Company reflect management's judgments regarding the impact of prevailing global credit, equity and foreign exchange market conditions. The estimation of insurance and investment contract liabilities relies upon investment credit ratings. The Company's practice is to use third party independent credit ratings where available.

The significant accounting policies are as follows:

### (a) Portfolio Investments

Portfolio investments include bonds, mortgage loans, stocks, investment properties and loans to policyholders. Portfolio investments are classified as fair value through profit or loss, available for sale, held to maturity, loans and receivables or as non-financial instruments based on management's intention relating to the purpose and nature of the instrument or characteristics of the investment. The Company currently has not classified any investments as held to maturity.

2. Basis of Presentation and Summary of Accounting Policies (cont'd)

Investments in bonds and stocks normally actively traded on a public market are either designated or classified as fair value through profit or loss or classified as available for sale on a trade date basis, based on management's intention. Fair value through profit or loss investments are recognized at fair value on the Consolidated Balance Sheets with realized and unrealized gains and losses reported in the Consolidated Statements of Earnings. Available for sale investments are recognized at fair value on the Consolidated Balance Sheets with unrealized gains and losses recorded in other comprehensive income (OCI). Realized gains and losses are reclassified from OCI and recorded in the Consolidated Statements of Earnings when the available for sale investment is sold. Interest income earned on both fair value through profit or loss and available for sale bonds is recorded as investment income earned in the Consolidated Statements of Earnings.

Investments in equity instruments where a market value cannot be measured reliably are classified as available for sale and carried at cost. Investments in stocks which the Company exerts significant influence over but does not control are accounted for using the equity method of accounting. Investments in stocks include the Company's investment in an affiliated company, IGM Financial Inc. (IGM), a member of the Power Financial Corporation group of companies, over which it exerts significant influence but does not control. The investment is accounted for using the equity method of accounting.

Investments in mortgages and bonds not normally actively traded on a public market are classified as loans and receivables and are carried at amortized cost net of any allowance for credit losses. Interest income earned and realized gains and losses on the sale of investments classified as loans and receivables are recorded in the Consolidated Statements of Earnings and included in investment income earned.

Investment properties are initially measured at cost and subsequently carried at fair value on the Consolidated Balance Sheets. All changes in fair value are recorded as investment income earned in the Consolidated Statements of Earnings. Fair values for investment properties are determined using independent qualified appraisal services. Properties that are leased that would otherwise be classified as investment property if owned by the Company are also included with investment properties.

***Fair Value Measurement***

Financial instrument carrying values necessarily reflect the prevailing market liquidity and the liquidity premiums embedded within the market pricing methods the Company relies upon.

The following is a description of the methodologies used to value instruments carried at fair value:

*Bonds – Fair Value Through Profit or Loss and Available for Sale*

Fair values for bonds classified as fair value through profit or loss or available for sale are determined with reference to quoted market bid prices primarily provided by third party independent pricing sources. Where prices are not quoted in a normally active market, fair values are determined by valuation models. The Company maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. The Company obtains quoted prices in active markets, when available, for identical assets at the balance sheet date to measure bonds at fair value in its fair value through profit or loss and available for sale portfolios.

The Company estimates the fair value of bonds not traded in active markets by referring to actively traded securities with similar attributes, dealer quotations, matrix pricing methodology, discounted cash flow analyses and/or internal valuation models. This methodology considers such factors as the issuer's industry, the security's rating, term, coupon rate and position in the capital structure of the issuer, as well as yield curves, credit curves, prepayment rates and other relevant factors. For bonds that are not traded in active markets, valuations are adjusted to reflect illiquidity, and such adjustments generally are based on available market evidence. In the absence of such evidence, management's best estimate is used.

*Stocks – Fair Value Through Profit or Loss and Available for Sale*

Fair values for public stocks are generally determined by the last bid price for the security from the exchange where it is principally traded. Fair values for stocks for which there is no active market are determined by discounting expected future cash flows. The Company maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. The Company obtains quoted prices in active markets, when available, for identical assets at the balance sheet date to measure stocks at fair value in its fair value through profit or loss and available for sale portfolios.

*Mortgages and Bonds – Loans and Receivables*

Market values for bonds and mortgages classified as loans and receivables are determined by discounting expected future cash flows using current market rates.

*Investment Properties*

Market values for investment properties are determined using independent qualified appraisal services and include management adjustments for material changes in property cash flows, capital expenditures or general market conditions in the interim period between appraisals.

*Impairment*

Investments are reviewed regularly on an individual basis to determine impairment status. The Company considers various factors in the impairment evaluation process, including, but not limited to, the financial condition of the issuer, specific adverse conditions affecting an industry or region, decline in fair value not related to interest rates, bankruptcy or defaults and delinquency in payments of interest or principal. Investments are deemed to be impaired when there is no longer reasonable assurance of timely collection of the full amount of the principal and interest due. The market value of an investment is not a definitive indicator of impairment, as it may be significantly influenced by other factors including the remaining term to maturity and liquidity of the asset. However market price must be taken into consideration when evaluating impairment.

For impaired mortgages and bonds classified as loans and receivables, provisions are established or write-offs made to adjust the carrying value to the net realizable amount. Wherever possible the fair value of collateral underlying the loans or observable market price is used to establish net realizable value. For impaired available for sale loans, recorded at fair value, the accumulated loss recorded in accumulated other comprehensive income (AOCI) is reclassified to net investment income. Impairments on available for sale debt instruments are reversed if there is objective evidence that a permanent recovery has occurred. All gains and losses on bonds classified or designated as fair value through profit or loss are already recorded in income, therefore a reduction due to impairment of these assets will be recorded in income. As well, when determined to be impaired, interest is no longer accrued and previous interest accruals are reversed.

**(b) Transaction Costs**

Transaction costs are expensed as incurred for financial instruments classified as fair value through profit or loss. Transaction costs for financial assets classified as available for sale or loans and receivables are added to the value of the instrument at acquisition and taken into net earnings using the effective interest rate method. Transaction costs for financial liabilities classified as other than fair value through profit or loss are added to the value of the instrument issued and taken into net earnings using the effective interest rate method.

**(c) Cash and Cash Equivalents**

Cash and cash equivalents comprises cash, current operating accounts, overnight bank and term deposits with original maturities of three months or less, and fixed income securities with an original term to maturity of three months or less. Net payments in transit and overdraft bank balances are included in other liabilities. The carrying value of cash and cash equivalents approximates their fair value.

**(d) Financial Liabilities**

Financial liabilities, other than insurance and investment contract liabilities, are classified as either capital trust securities or other liabilities. Debentures and other debt instruments, capital trust securities and other liabilities are initially recorded on the Consolidated Balance Sheets at fair value and subsequently carried at amortized cost using the effective interest rate method with amortization expense recorded in the Consolidated Statements of Earnings.

**(e) Derivative Financial Instruments**

The Company uses derivative products as risk management instruments to hedge or manage asset, liability and capital positions, including revenues. The Company's policy guidelines prohibit the use of derivative instruments for speculative trading purposes.

The Company includes disclosure of the maximum credit risk, future credit exposure, credit risk equivalent and risk weighted equivalent in note 28 as prescribed by the Office of the Superintendent of Financial Institutions of Canada (OSFI).

All derivatives including those that are embedded in financial and non-financial contracts that are not closely related to the host contracts are recorded at fair value on the Consolidated Balance Sheets. The method of recognizing unrealized and realized fair value gains and losses depends on whether the derivatives are designated as hedging instruments. For derivatives that are not designated as hedging instruments, unrealized and realized gains and losses are recorded in net investment income on the Consolidated Statements of Earnings. For derivatives designated as hedging instruments, unrealized and realized gains and losses are recognized according to the nature of the hedged item.

Derivatives are valued using market transactions and other market evidence whenever possible, including market based inputs to models, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value a derivative depends on the contractual terms of, and specific risks inherent in the instrument, as well as the availability of pricing information in the market. The Company generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs.

To qualify for hedge accounting, the relationship between the hedged item and the hedging instrument must meet several strict conditions on documentation, probability of occurrence, hedge effectiveness and reliability of measurement. If these conditions are not met, then the relationship does not qualify for hedge accounting treatment and both the hedged item and the hedging instrument are reported independently as if there was no hedging relationship.

Where a hedging relationship exists, the Company documents all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedge transactions. This process includes linking derivatives that are used in hedging transactions to specific assets and liabilities on the Consolidated Balance Sheets or to specific firm commitments or forecasted transactions. The Company also assesses, both at the hedge's inception and on an ongoing basis, whether derivatives that are used in hedging transactions are effective in offsetting changes in fair values or cash flows of hedged items. Hedge effectiveness is reviewed quarterly through correlation testing.

***Derivatives not designated as hedges for accounting purposes***

For derivative investments not designated as accounting hedges, changes in fair value are recorded in net investment income.

***Fair value hedges***

For fair value hedges, changes in fair value of both the hedging instrument and the hedged item are recorded in net investment income and consequently any ineffective portion of the hedge is recorded immediately to net investment income.

The Company currently uses interest rate swaps designated as fair value hedges.

***Cash flow hedges***

Certain interest rate swaps and cross currency swaps are used to hedge cash flows. For cash flow hedges, the effective portion of the changes in fair value of the hedging instrument is recorded in the same manner as the hedged item in either net investment income or OCI while the ineffective portion is recognized immediately in net investment income. Gains and losses that accumulate in OCI are recorded in net investment income in the same period the hedged item affects net earnings. Gains and losses on cash flow hedges are immediately reclassified from OCI to net investment income if and when it is probable that a forecasted transaction is no longer expected to occur.

The Company currently has no derivatives designated as cash flow hedges.

***Net investment hedges***

Foreign exchange forward contracts are used to hedge the net investment in the Company's foreign operations. Changes in the fair value of these hedges are recorded in OCI. Hedge accounting is discontinued when the hedging no longer qualifies for hedge accounting.

The Company currently has no derivatives designated as net investment hedges.

**(f) Embedded Derivatives**

Embedded derivatives are treated as separate contracts and are recorded at fair value if their economic characteristics and risks are not closely related to those of the host contract and the host contract is not itself recorded at fair value through the Consolidated Statements of Earnings. Embedded derivatives that meet the definition of an insurance contract are accounted for and measured as an insurance contract.

**(g) Foreign Currency Translation**

The Company operates with multiple functional currencies. The Company's consolidated financial statements are presented in Canadian dollars as this presentation is most meaningful to financial statement users. For those subsidiaries with different functional currencies, exchange rate differences arising from the translation of monetary items that form part of the net investment in the foreign operation are taken to unrealized foreign exchange gains (losses) on translation of foreign operations in AOCI.

For the purpose of presenting consolidated financial statements, assets and liabilities are translated into Canadian dollars at the rate of exchange prevailing at the balance sheet dates and all income and expense items are translated at an average of daily rates. Unrealized foreign currency translation gains and losses on the Company's net investment in its foreign operations are presented separately as a component of OCI. Unrealized gains and losses will be recognized proportionately in net investment income on the Consolidated Statements of Earnings when there has been a disposal of the investment in the foreign operations. Foreign currency translation gains and losses on foreign currency transactions of the Company are included in net investment income and are not material to the financial statements of the Company.

**(h) Loans to Policyholders**

Loans to policyholders are shown at their unpaid principal balance and are fully secured by the cash surrender values of the policies. Carrying value of loans to policyholders approximates their fair value.

**(i) Funds Held by Ceding Insurers/Funds Held Under Reinsurance Contracts**

Under certain forms of reinsurance contracts, it is customary for the ceding insurer to retain possession of the assets supporting the liabilities ceded. The Company records an amount receivable from the ceding insurer or payable to the reinsurer representing the premium due. Investment revenue on these funds withheld is credited by the ceding insurer.

**(j) Reinsurance Contracts**

The Company, in the normal course of business, is both a user and provider of reinsurance in order to limit the potential for losses arising from certain exposures. Assumed reinsurance refers to the acceptance of certain insurance risks by the Company underwritten by another company. Ceded reinsurance refers to the transfer of insurance risk, along with the respective premiums, to one or more reinsurers who will share the risks. To the extent that assuming reinsurers are unable to meet their obligations, the Company remains liable to its policyholders for the portion reinsured. Consequently, allowances are made for reinsurance contracts which are deemed uncollectible.

Assumed reinsurance premiums, commissions and claim settlements, as well as the reinsurance assets associated with insurance and investment contracts, are accounted for in accordance with the terms and conditions of the underlying reinsurance contract. Reinsurance assets are reviewed for impairment on a regular basis for any events that may trigger impairment. The Company considers various factors in the impairment evaluation process, including but not limited to, collectability of amounts due under the terms of the contract. The carrying amount of a reinsurance asset is adjusted through an allowance account with any impairment loss being recorded in the Consolidated Statements of Earnings.

Any gains or losses on buying reinsurance are recognized in the Consolidated Statements of Earnings immediately at the date of purchase and are not amortized.

Premiums and claims ceded for reinsurance are deducted from premiums earned and insurance and investment contract benefits. Assets and liabilities related to reinsurance are reported on a gross basis in the Consolidated Balance Sheets. The amount of liabilities ceded to reinsurers is estimated in a manner consistent with the claim liability associated with reinsured risks.

**(k) Goodwill and Intangible Assets**

Goodwill represents the excess of purchase consideration over the fair value of net assets of acquired subsidiaries of the Company. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Intangible assets represent finite life and indefinite life intangible assets of acquired subsidiaries of the Company and software acquired or internally developed by the Company. Finite life intangible assets include the value of software, customer contracts and distribution channels. These finite life intangible assets are amortized over their estimated useful lives, generally not exceeding 10 years, 20 years and 30 years respectively.

Indefinite life intangible assets include brands and trademarks, customer contracts and the shareholder's portion of acquired future participating account profits. Amounts are classified as indefinite life intangible assets when based on an analysis of all the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the Company. The identification of indefinite life intangible assets is made by reference to relevant factors such as product life cycles, potential obsolescence, industry stability and competitive position.

*Impairment Testing*

Goodwill and intangible assets are tested for impairment annually or more frequently if events indicate that impairment may have occurred. Intangible assets that were previously impaired are reviewed at each reporting date for evidence of reversal. In the event that certain conditions have been met, the Company would be required to reverse the impairment charge or a portion thereof.

Goodwill has been allocated to cash generating units (CGU), representing the lowest level in which goodwill is monitored for internal reporting purposes. Goodwill is tested for impairment by comparing carrying value of the CGU groups to the recoverable amount to which the goodwill has been allocated. Intangible assets are tested for impairment by comparing the asset's carrying amount to its recoverable amount. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount.

The recoverable amount is the higher of the asset's fair value less costs to sell and value in use, which is calculated using the present value of estimated future cash flows expected to be generated.

**(l) Revenue Recognition**

Premiums for all types of insurance contracts, and contracts with limited mortality or morbidity risk, are generally recognized as revenue when due and collection is reasonably assured. When premiums are recognized, insurance contract liabilities are computed, with the result that benefits and expenses are matched with such revenue.

Fee and other income is recognized when earned, collectible and the amount can be reasonably estimated. Fee and other income primarily includes fees earned from the management of segregated fund assets, proprietary mutual funds assets, fees earned on administrative services only (ASO) Group health contracts and fees earned from management services.

2. Basis of Presentation and Summary of Accounting Policies (cont'd)

**(m) Fixed Assets and Owner Occupied Properties**

Fixed assets and property held for own use is carried at cost less accumulated depreciation and impairments. Depreciation is charged so as to write-off the cost of assets, over their estimated useful lives, using the straight-line method, on the following bases:

| | |
|---|---|
| Owner occupied properties | 15 – 20 years |
| Furniture and fixtures | 5 – 10 years |
| Other fixed assets | 3 – 10 years |

**(n) Other Assets**

Included in other assets are DAC relating to investment contracts. These are recognized if the costs are incremental and incurred due to the contract being issued.

**(o) Segregated Funds for the Risk of Unitholders**

Segregated funds assets and liabilities arise from contracts where all financial risks associated with related assets are borne by unit holders and are presented separately in the Consolidated Balance Sheets at fair value. Investment income and changes in market value of the segregated fund assets are offset by a corresponding change in the segregated fund liabilities.

**(p) Insurance and Investment Contract Liabilities**

***Contract Classification***

The Company's products are classified at contract inception, for accounting purposes, as insurance, service or investment contracts depending on the existence of significant insurance risk. Significant insurance risk exists when the Company agrees to compensate policyholders or beneficiaries of the contract for specified uncertain future events that adversely affect the policyholder and whose amount and timing is unknown. When significant insurance risk exists, the contract is accounted for as an insurance contract in accordance with IFRS 4, *Insurance Contracts* (IFRS 4). Refer to note 14 for a discussion of insurance risk.

In the absence of significant insurance risk, the contract is classified as an investment or service contract. Investment contracts with discretionary participating features (DPF) are accounted for in accordance with IFRS 4 and investment contracts without DPF are accounted for in accordance with IAS 39, *Financial Instruments: Recognition & Measurement*. The Company has not classified any contracts as investment contracts with DPF. Service contracts mainly relate to ASO contracts and are accounted for under IAS 18, *Revenue Recognition*.

Investment contracts may be reclassified as insurance contracts after inception if insurance risk becomes significant. A contract that is classified as an insurance contract at contract inception remains as such until all rights and obligations under the contract are extinguished or expire.

Investment contracts are contracts that carry financial risk, which is the risk of a possible future change in one or more of the following: interest rate, commodity price, foreign exchange rate, or credit rating. Refer to note 7 for discussion of risk management.

***Measurement***

Insurance contract liabilities represent the amounts required, in addition to future premiums and investment income, to provide for future benefit payments, policyholder dividends, commission and policy administrative expenses for all insurance and annuity policies in force with the Company. The Appointed Actuary of the Company is responsible for determining the amount of the liabilities to make appropriate provisions for the Company's obligations to policyholders. The Appointed Actuary determines the liabilities for insurance contracts and investment contracts using generally accepted actuarial practices, according to the standards established by the Canadian Institute of Actuaries. The valuation uses the Canadian Asset Liability Method (CALM). This method involves the projection of future events in order to determine the amount of assets that must be set aside currently to provide for all future obligations and involves a significant amount of judgment.

Investment contract liabilities are measured at fair value through profit or loss, except for certain annuity products measured at amortized cost.

**(q) Deferred Income Reserves**

Included in other liabilities are DIR relating to investment contract liabilities. These are amortized on a straight-line basis to recognize the initial policy fees over the policy term, not to exceed 20 years, to release revenue as it is earned over the policy term.

**(r) Participating Account**

The shareholder portion of participating earnings represents, as restricted by law, a portion of net earnings before policyholder dividends of the participating account, $91 in 2011 ($47 in 2010). The actual payment of the shareholder portion of participating earnings is legally determined as a percentage of policyholder dividends paid. $55 of shareholder surplus ($51 in 2010) that has been recognized but not paid is dependent on future payment of dividends to participating policyholders.

The Canada Life Assurance Company (Canada Life) participating account comprises two main subdivisions. The liabilities for participating policies issued or assumed by Canada Life prior to demutualization are held in closed block sub-accounts. These liabilities for guaranteed and other non-guaranteed benefits are determined using best estimate assumptions. If at any time the value of the assets allocated to these policies were, in the opinion of the Appointed Actuary, less than the assets required in the long term to support the liabilities of these policies and the future reasonable expectations of the policyholders, assets having a sufficient value to rectify the situation would be transferred first from the additional ancillary sub-accounts maintained in the participating account for this purpose and then, if the deficiency is expected to be permanent, from the shareholder account. Any such transfers from the shareholder account would be recorded as a charge to shareholder net earnings.

The second main subdivision comprises the open block sub-accounts containing all liabilities in respect of new participating policies issued on or after demutualization. On demutualization, $50 of seed capital was transferred from shareholder surplus to the participating account. The seed capital amount, together with a reasonable rate of return, may be transferred to the shareholder account if the seed capital is no longer required to support the new participating policies. Transfers of seed capital to the shareholder account would be returns of capital and would be recorded as adjustments to shareholder surplus. A reasonable rate of return on seed capital will be recognized as income in the shareholder account and as an expense in the participating account when paid. $15 (US$15) of seed capital remains to be repaid.

**(s) Income Taxes**

On December 20, 2010, the IASB issued "Deferred Tax: Recovery of Underlying Assets (Amendments to IAS 12)" concerning the determination of deferred tax on investment property measured at fair market value. IAS 12 was updated to include a rebuttable presumption that a deferred tax on investment property measured using the fair value model in IAS 40 should be determined on the basis that its carrying amount will be recovered through sale. The amendments are mandatory for annual periods beginning on or after January 1, 2012, but early adoption is permitted. The Company has elected to adopt the amendment effective January 1, 2011.

The income tax expense for the period represents the sum of current income tax and deferred income tax. Income tax is recognized as an expense or income in profit or loss except to the extent that it relates to items that are recognized outside profit or loss (whether in OCI or directly in equity), in which case the income tax is also recognized outside profit or loss.

***Current Income Tax***

Current income tax is based on taxable income for the year. Current tax liabilities (assets) for the current and prior periods are measured at the amount expected to be paid to (recovered from) the taxation authorities using the tax rates that have been enacted or substantively enacted at the balance sheet date. Current tax assets and current tax liabilities are offset if a legally enforceable right exists to offset the recognized amounts and the entity intends either to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

***Deferred Income Tax***

Deferred income tax is the tax expected to be payable or recoverable on differences arising between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable income and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is more likely than not that taxable profits will be available against which deductible temporary differences can be utilized. Such assets and liabilities are not recognized if the temporary difference arises from the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Deferred tax assets and liabilities are measured at the tax rates expected to apply in the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date. Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer more likely than not that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become more likely than not that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax liabilities are recognized for taxable temporary differences arising on investments in subsidiaries and associates, except where the group controls the timing of the reversal of the temporary difference and it is more likely than not that the temporary differences will not reverse in the foreseeable future.

Under the IFRS liability method, a provision for tax uncertainties which meet the more likely than not threshold for recognition are measured. Measurement of the provision is based on the probability weighted average approach.

**(t) Policyholder Benefits**

Gross benefits and claims for life insurance contracts include the cost of all claims arising during the year, settlement of claims, as well as changes in the gross valuation of insurance contracts. Death claims and surrenders are recorded on the basis of notifications received. Maturities and annuity payments are recorded when due.

**(u) Repurchase Agreements**

The Company enters into repurchase agreements with third-party broker-dealers in which the Company sells securities and agrees to repurchase substantially similar securities at a specified date and price. As substantially all of the risks and rewards of ownership of the assets are retained, the Company does not derecognize the assets. Such agreements are accounted for as investment financings.

**(v) Pension Plans and Other Post-Employment Benefits**

The Company and its subsidiaries maintain contributory and non-contributory defined benefit pension plans for certain employees and advisors. The Company and its subsidiaries also maintain defined contribution pension plans for certain employees and advisors. The cost of defined pension benefits is charged to net earnings using the projected unit credit method prorated on services (see note 23).

For the Company's defined benefit plans, actuarial gains and losses are amortized into the Consolidated Statements of Earnings using the straight-line method over the expected average remaining working lives of employees covered by the plan to the extent that the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceed corridor limits. The corridor is defined as ten percent of the greater of the present value of the defined benefit obligation or the fair value of plan assets. The amortization charge is re-assessed at the beginning of each year.

The Company and its subsidiaries also provide post-employment health, dental and life insurance benefits to eligible employees, advisors and their dependents. The cost of post-employment health, dental and life insurance benefits is charged to net earnings using the projected unit credit method prorated on service (see note 23).

**(w) Share Capital and Surplus**

Financial instruments issued by the Company are classified as share capital if they represent a residual interest in the assets of the Company. Preferred share capital is classified as equity if it is non-redeemable, or retractable only at the Company's option and any dividends are discretionary. Incremental costs that are directly attributable to the issue of share capital are recognized as a deduction from equity, net of income tax.

Contributed surplus represents the vesting of share options.

Accumulated other comprehensive income represents the total of the unrealized foreign exchange gains (losses) on translation of foreign operations, the gains (losses) on available for sale assets, and the unrealized gains (losses) on cash flow hedges.

Non-controlling interests represent the proportion of equity that is attributable to minority shareholders.

Participating account surplus represents the proportion of equity attributable to the participating account.

**(x) Share Based Payments**

Lifeco has a stock option plan that provides for the granting of options on common shares of Lifeco to certain officers and employees of Lifeco and its affiliates. The Company follows the fair value based method of accounting for the valuation of compensation expense for shares and share options granted to employees under its stock option plans (see note 22). Compensation expense is recognized as an increase to compensation expense in the Consolidated Statements of Earnings and an increase to contributed surplus over the vesting period of the granted options.

**(y) Earnings Per Common Share**

Earnings per common share is calculated using net earnings after preferred share dividends and the weighted average number of common shares outstanding of 2,117,015 in 2011 (2,093,861 in 2010).

**(z) Leases**

Leases that do not transfer substantially all the risks and rewards of ownership are classified as operating leases. Payments made under operating leases, where the Company is the lessee, are charged to net earnings over the period of use.

Where the Company is the lessor under an operating lease for its investment property, the assets subject to the lease arrangement are presented within the Consolidated Balance Sheets. Income from these leases is recognized in the Consolidated Statements of Earnings on a straight-line basis over the lease term.

**(aa) Operating Segments**

Operating segments have been identified based on internal reports that are regularly reviewed by the Company's Chief Executive Officer to allocate resources and assess performance of segments. The Company's reportable business segments are the participating and shareholder operations of the Company. Within these segments the major business units are Individual Insurance, Wealth Management, Group Insurance, Europe, Corporate, and Participating. Reinsurance operations and operations in all countries other than Canada and the United States are reported as part of the Europe segment. The Corporate segment represents activities and transactions that are not directly attributable to the measurement of the operating segments of the Company.

## 3. Reconciliations of IFRS Equity and Comprehensive Income

***Application of IFRS-1***

The Company's annual consolidated financial statements have been prepared in accordance with IFRS as issued by the IASB and as adopted by the Accounting Standards Board of Canada for financial reporting periods beginning on or after January 1, 2011. References made to IAS throughout refer to the application of IAS and related interpretations of IFRIC and interpretations of the Standing Interpretations Committee (SIC).

These are the first annual consolidated financial statements prepared in accordance with IFRS, with the 2010 comparatives restated accordingly. Prior to the adoption of IFRS, the consolidated financial statements were prepared in accordance with the previous CGAAP.

The effects of the transition to IFRS as of January 1, 2010 on the financial position, financial performance and cash flows for the periods presented are as follows:

***Reconciliations of Previous CGAAP to IFRS***

At transition to IFRS the Company applied IFRS 1, *First-time Adoption of International Financial Reporting Standards* (IFRS 1) which requires the Company to reconcile accumulated surplus and comprehensive income for prior periods presented. The adoption of IFRS has not changed the Company's cash flows however it has resulted in certain changes to the Company's reported financial position and results of operations. IFRS has also resulted in a number of presentation changes to the Company's financial statements. In order for users to understand the effects of adopting IFRS, reconciliations of the Company's financial statements from the previous CGAAP to IFRS along with narrative explanations have been provided below.

IFRS does not allow the use of hindsight to recreate or revise estimates and consequently the estimates previously made by the Company under the previous CGAAP were not revised when converting to IFRS except where necessary to reflect any difference in accounting policies.

3. Reconciliations of IFRS Equity and Comprehensive Income (cont'd)

## Reconciliation of consolidated equity from the previous CGAAP to IFRS

| | | Date of transition to IFRS January 1, 2010 | Comparative period reported under CGAAP December 31, 2010 |
|---|---|---|---|
| Total surplus under the previous CGAAP | | $ 13,268 | $ 13,550 |
| 2010 year to date IFRS equity adjustments | | | |
| Impact on shareholder surplus | | – | (579) |
| Impact on participating account surplus | | – | 41 |
| Net Impact of IFRS on equity | | – | (538) |
| Beginning surplus restated under IFRS | | 13,268 | 13,012 |
| IFRS 1 optional elections/exemptions | | | |
| Employee benefits cumulative unamortized actuarial gains and losses | a | (220) | – |
| Cumulative translation losses of foreign operations – shareholder | b | (1,091) | – |
| Redesignation of financial assets | c | (88) | – |
| Fair value as deemed cost of owner occupied properties | d | 21 | – |
| IFRS adjustments | | | |
| Measurement of investment properties and owner occupied properties | f | 119 | 1 |
| Derecognition of deferred net realized gains | g | 104 | (12) |
| Unamortized vested past service costs and other employment benefits | h | 120 | (10) |
| Uncertain income tax provisions | i | (230) | (22) |
| DAC and DIR on investment contracts | j | (471) | 18 |
| Other adjustments | k | (6) | 1 |
| Income tax effect of the above adjustments | l | 45 | (8) |
| Total IFRS adjustment to shareholder account | | (1,697) | (32) |
| Adjustment related to participating account surplus in subsidiaries | k | (41) | 9 |
| Total IFRS adjustment | | (1,738) | (23) |
| | | 11,530 | 12,989 |
| Accumulated other comprehensive income | | | |
| Cumulative translation losses of foreign operations – shareholder | b | 1,091 | 44 |
| Redesignation of financial assets | c | 88 | (16) |
| Tax impact on redesignation of financial assets | c | (20) | 4 |
| Total adjustment to accumulated other comprehensive income | | 1,159 | 32 |
| Total adjustment to shareholders' equity at transition to IFRS | | (579) | 9 |
| Total share capital and shareholders' equity under IFRS | | 12,689 | 13,021 |
| Reclassification of non-controlling interests for IFRS presentation | u | 147 | – |
| Cumulative translation losses of foreign operations – participating account surplus | b | (26) | – |
| Cumulative translation losses of foreign operations – participating account surplus | b | 26 | – |
| Total IFRS adjustment to participating account surplus | k | 41 | (9) |
| Total adjustment to participating account surplus and non-controlling interests | | 188 | (9) |
| Total equity | | $ 12,877 | $ 13,012 |

## Reconciliation of consolidated earnings and comprehensive income from the previous CGAAP to IFRS

| | | Comparative period reported under CGAAP for the year ended December 31, 2010 |
|---|---|---|
| Total comprehensive income under the previous CGAAP | | $ 1,006 |
| Adjustments for: | | |
| Measurement adjustment for owner occupied and investment properties | f | 1 |
| Derecognition of deferred net realized gains | g | (12) |
| | | (11) |
| Unamortized vested past service costs and other employment benefits | h | (10) |
| Uncertain tax provisions | i | (22) |
| Change in recognition of DAC on investment contracts | | 71 |
| Change in recognition of DIR on investment contracts | | (53) |
| | j | 18 |
| Other adjustments | k | 1 |
| Total impact on operating earnings before tax and OCI | | (24) |
| Income tax effect related to the above | l | (8) |
| Total after-tax adjustments to net earnings | | (32) |
| Other comprehensive income | | |
| Cumulative translation gains (losses) of foreign operations | b | 44 |
| Redesignation of financial assets | c | (16) |
| Tax impact on redesignation of financial assets | c | 4 |
| Total after-tax adjustments to comprehensive income | | 32 |
| Total IFRS comprehensive income | | $ 1,006 |

3. Reconciliations of IFRS Equity and Comprehensive Income (cont'd)

## Reconciliation of the Consolidated Balance Sheets from the previous CGAAP to IFRS

| (in Canadian $ millions)<br>December 31 | Comparative period reported under CGAAP December 31, 2009 | Conversion adjustments | | Presentation and reclassification adjustments | | Date of transition to IFRS January 1, 2010 |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash and cash equivalents | $ 3,030 | $ – | | $ – | | $ 3,030 |
| Bonds | 50,183 | – | | – | | 50,183 |
| Mortgage loans | 15,033 | – | | – | | 15,033 |
| Stocks | 5,904 | – | | – | | 5,904 |
| Investment properties | 2,964 | (85) | f | (270) | p | 2,609 |
| Loans to policyholders | 2,786 | – | | – | | 2,786 |
| Funds held by ceding insurers | 10,839 | – | | 145 | q | 10,984 |
| Goodwill | 5,270 | – | | – | | 5,270 |
| Intangible assets | 1,538 | – | | – | | 1,538 |
| Derivative financial instruments | 693 | – | | – | | 693 |
| Owner occupied properties | – | 21 | d | 270 | p | 291 |
| Fixed assets | 91 | – | d | – | p | 91 |
| Reinsurance assets | – | – | | 4,889 | q | 4,889 |
| Other assets | 2,686 | (65) | h | 447 | r | 3,068 |
| Deferred tax assets | 67 | (4) | o | – | | 63 |
| Segregated funds for the risk of unitholders | – | – | | 67,805 | t | 67,805 |
| **Total assets** | $ 101,084 | $ (133) | | $ 73,286 | | $ 174,237 |
| **Liabilities** | | | | | | |
| Insurance contract liabilities | $ 82,996 | $ (66) | f,g,j,s | $ 4,516 | q | $ 87,446 |
| Investment contract liabilities | – | – | | 820 | q,r | 820 |
| Debentures and other debt instruments | 305 | – | | – | | 305 |
| Funds held under reinsurance contracts | 613 | – | | 145 | q | 758 |
| Derivative financial instruments | 188 | – | | – | | 188 |
| Other liabilities | 2,042 | 644 | a,h,i,j,l | – | | 2,686 |
| Deferred tax liabilities | 603 | (46) | o | – | | 557 |
| Repurchase agreements | 17 | – | | – | | 17 |
| Deferred net realized gains | 127 | (127) | g | – | | – |
| Capital trust securities | 778 | – | | – | | 778 |
| Non-controlling interests | 147 | – | | (147) | u | – |
| Investment and insurance contracts on account of unitholders | – | – | | 67,805 | t | 67,805 |
| **Total liabilities** | 87,816 | 405 | | 73,139 | | 161,360 |
| **Equity** | | | | | | |
| Participating account surplus | | | | | | |
| Accumulated surplus | 2,016 | 41 | k | (26) | b | 2,031 |
| AOCI (L) | (17) | – | | 26 | b | 9 |
| Non-controlling interests | – | – | | 147 | u | 147 |
| Share capital | | | | | | |
| Preferred shares | 158 | – | | – | | 158 |
| Common shares | 6,116 | – | | – | | 6,116 |
| Shareholder surplus | | | | | | |
| Accumulated surplus | 5,852 | (1,712) | | – | | 4,140 |
| AOCI (L) | (1,068) | 1,133 | b,c,k | – | | 65 |
| Contributed surplus | 211 | – | | – | | 211 |
| **Total equity** | 13,268 | (538)* | | 147 | | 12,877 |
| **Total liabilities and equity** | $ 101,084 | $ (133) | | $ 73,286 | | $ 174,237 |

* Total impact on equity of $(538) consists of $41 impact on participating account and impact on non-participating of $(579).

**Statements of Cash Flows**

Under IFRS, the statements of cash flows will continue to be presented under the indirect method with limited presentation differences of operating earnings being presented before tax and cash flows related to tax expense presented separately within operating cash flows. The cash flows reported under the previous CGAAP for operating, financing, and investing activities have not been impacted by the adoption of IFRS requirements.

**IFRS 1 First-time Adoption of IFRS Optional Exemptions**

The Company has applied IFRS 1 in preparing the annual consolidated financial statements which requires retrospective application of IFRS except for certain optional exemptions and mandatory exceptions provided in the Standard. The optional exemptions adopted by the Company and the mandatory exceptions that apply to the Company are described within this transitional note.

**(a) Employee Benefits Cumulative Unamortized Actuarial Gains and Losses**

The Company has elected to apply the exemption available to recognize all cumulative unamortized actuarial gains and losses of the Company's defined benefit plans in equity upon transition to IFRS. This adjustment, referred to as the 'fresh start adjustment', decreased total equity by $220 before tax (decrease of $193 to shareholder accumulated surplus and $27 to participating account surplus). Subsequent to transition, the Company will continue to use the corridor approach available under the present IAS 19, *Employee Benefits* standard for deferring recognition of actuarial gains and losses that reside within the corridor.

**(b) Cumulative Translation Losses of Foreign Operations**

The Company has elected to reset its cumulative translation adjustment (CTA) account for all foreign operations to zero as of January 1, 2010. Future gains or losses on disposal of any foreign operation will therefore exclude translation differences that arose before January 1, 2010. The balance of the cumulative loss to be reclassified from AOCI to shareholder accumulated surplus at January 1, 2010 is approximately $1,091 and the balance reclassified within participating account surplus is $26 at January 1, 2010. As a result of the foreign exchange revaluation of the transitional IFRS adjustments the total impact to CTA was an increase of $44 for the year ended December 31, 2010.

**(c) Redesignation of Financial Assets**

The Company has elected to redesignate certain non-participating available for sale financial assets to the fair value through profit or loss classification and certain financial assets classified as held for trading under the previous CGAAP to available for sale. The redesignation will have no overall impact on the Company's opening equity at transition but will result in a reclassification within equity of $88 before tax ($68 after-tax) between accumulated surplus and AOCI (a decrease of $90 related to shareholder accumulated surplus and an increase of $2 related to participating account surplus). For the year ended December 31, 2010, the redesignation decreased net earnings by $12, net of tax.

The financial assets carried at fair value in December 31, 2009 CGAAP consolidated financial statements and at transition to IFRS are as follows:

| | Fair value January 1, 2010 | Unrealized gains reclassifed to AOCI January 1, 2010 |
|---|---|---|
| Financial assets redesignated to fair value through profit or loss | $ 269 | $ 15 |
| Financial assets redesignated to available for sale | $ 254 | $ 73 |

**(d) Fair Value as Deemed Cost for Owner Occupied Properties**

The Company has elected to measure owner occupied properties at fair value as their deemed cost at the January 1, 2010 transition date which has resulted in an increase to equity of $21 before tax (increases of $19 to shareholder accumulated surplus and $2 to participating account surplus). Subsequent to this date, owner occupied properties will be carried at amortized cost.

3. Reconciliations of IFRS Equity and Comprehensive Income (cont'd)

**(e) Business Combinations**

The Company has applied the IFRS 1 business combinations exemption and has not restated business combinations that took place prior to the January 1, 2010 transition date which has resulted in no impact on opening figures. The Company will apply IFRS 3, *Business Combinations* prospectively for business combinations occurring on or after January 1, 2010.

**Changes in Accounting Policies Mandatory at Conversion to IFRS**

***Measurement and Recognition Differences***

**(f) Measurement of Investment Properties and Owner Occupied Properties**

Under the previous CGAAP, real estate is carried at cost net of write-downs and allowance for loss, plus a moving average market value adjustment. Under IFRS, real estate held for investment purposes is classified as investment property and is measured at fair value. This measurement change has increased equity at January 1, 2010 by $119 before tax (increase of $114 to shareholder accumulated surplus and $5 to participating account surplus) and increased the Consolidated Statement of Earnings, offset by the change in accounting for owner occupied properties by $1 for the year ended December 31, 2010.

**(g) Derecognition of Deferred Net Realized Gains**

Under the previous CGAAP, net realized gains and losses associated with the sale of real estate were deferred and included in deferred net realized gains on the Consolidated Balance Sheets. These deferred net realized gains and losses were amortized to income at a rate of 3% per quarter on a declining balance basis. Under IFRS, gains and losses associated with the sale of investment properties are immediately recognized in income and consequently the balance of the unrecognized net deferred realized gains was recognized in equity at transition. This recognition change has increased equity at January 1, 2010 by $104 before tax (increase of $41 in shareholder accumulated surplus and $63 in participating account surplus) and decreased net earnings by $12 for the year ended December 31, 2010.

**(h) Unamortized Vested Past Service Costs and Other Employment Benefits**

Previous CGAAP and IFRS differ in their treatment of other employee benefits including the timing of recognition of unamortized vested past service costs and certain service awards. The change in recognition for these vested past service costs and other employee benefits under IFRS has increased equity at January 1, 2010 by $120 before tax (increased by $102 in shareholder accumulated surplus and $18 in participating account surplus) and decreased net earnings before tax by $10 for the year ended December 31, 2010.

**(i) Uncertain Income Tax Provisions**

The difference in the recognition and measurement of uncertain income tax provisions between the previous CGAAP and IFRS has decreased equity at January 1, 2010 by $230 (decreased by $221 in shareholder accumulated surplus and $9 in participating account surplus) and decreased net earnings by $22 for the year ended December 31, 2010.

**(j) Deferred Acquisition Costs and Deferred Income Reserves on Investment Contracts**

Under the previous CGAAP, DAC relating to policyholder liabilities were deferred in policy liabilities and amortized into consolidated net earnings over the anticipated period of benefit. Under IFRS, DAC on policyholder liabilities reclassified as investment contract liabilities are no longer deferred and amortized into earnings over the anticipated period of benefit but rather recognized through earnings in the period incurred for those costs not incremental to issuing the contract. In addition to DAC, DIR related to fee income on investment contracts will also be deferred and recognized over the term of the contract. The change in measurement for both DAC and DIR has decreased equity at January 1, 2010 by $114 and $357 before tax and increased net earnings by $18 for the year ended December 31, 2010.

**(k) Other Adjustments**

In addition to the items described above, several other items required adjustments due to the transition from the previous CGAAP to IFRS which resulted in measurement changes. The adjustments resulted in a decrease to opening equity at January 1, 2010 of $6 and an increase to net earnings of $1 for the year ended December 31, 2010.

Also included in the above adjustments is the related impact of the IFRS adjustments attributed to the participating account surplus. The total impact to the participating account resulted in an increase of $41 at transition and a decrease of $9 for the year ended December 31, 2010.

**(l) Tax Impact of IFRS Adjustments**

The tax effect of the above adjustments, excluding the uncertain tax provisions, is an increase to income tax liabilities of $45 at transition (an increase of $56 to shareholder accumulated surplus and a decrease of $11 to participating account surplus) and a decrease of $8 for the year ended December 31, 2010.

**(m) Goodwill and Intangible Asset Measurement and Impairment Testing**

Goodwill and intangible assets under IFRS are measured using the cost model, based on the recoverable amount which is the greater of the value-in-use and fair value less cost to sell. The recoverable amount calculated under IFRS approximates the previous CGAAP carrying value at January 1, 2010 and therefore no transitional adjustment was required.

At each reporting date, the Company reviews goodwill and intangible assets for indicators of impairment or reversals of impairment on the intangible assets. In the event that certain conditions have been met, the Company is required to reverse the impairment charge, or a portion thereof, on intangible assets.

Under the previous CGAAP, goodwill is tested for impairment by comparing the fair value of the reporting unit to which the goodwill is associated with its carrying value. Under IFRS, the carrying value of goodwill is tested for impairment by reference to the CGU in which goodwill is associated. A CGU represents the lowest level in which goodwill is monitored for internal reporting purposes. This change in impairment testing had no impact on the Company's financial statements at transition.

**(n) Recognition of Contingent Liabilities**

Under the previous CGAAP, contingent liabilities are recognized if it is 'likely' whereas under IFRS contingent liabilities are recognized if it is 'probable' that a loss will ultimately be incurred in relation to the matter. The change in the recognition threshold has not resulted in additional provisions being recognized at January 1, 2010.

**(o) Recognition of Deferred Tax Assets**

Previous CGAAP limited the amount of future income tax assets recognized to the amount that is 'more likely than not' to be realized whereas IFRS recognizes a deferred tax asset if it is more likely than not that sufficient future taxable profit will be available to recover the asset. The change in measurement criteria has not impacted consolidated net earnings and equity at January 1, 2010.

***Presentation and Classification Differences***

**(p) Presentation of Real Estate Properties**

Properties classified as real estate under the previous CGAAP are reclassified to investment properties of $2,609 and owner occupied properties of $270 in the Consolidated Balance Sheets under IFRS.

**(q) Presentation of Reinsurance Accounts**

Reinsurance accounts will be presented on a gross basis on the Consolidated Balance Sheets totaling $4,889 of reinsurance assets with an offsetting increase to insurance and investment contract liabilities with no impact to equity. Funds withheld asset and liability accounts have also been adjusted for gross presentation of $145. Gross presentation of the reinsurance revenue and expenses is also required within the Consolidated Statements of Earnings.

**(r) Reclassification of Deferred Acquisition Costs**

The DAC of $447 recognized on investment contracts that was previously included within policy liabilities under the previous CGAAP has been reclassified to other assets on the Consolidated Balance Sheets.

3. Reconciliations of IFRS Equity and Comprehensive Income (cont'd)

**(s) Presentation of Insurance and Investment Contract Liabilities**

Under the previous CGAAP, all policyholder related liabilities are classified as actuarial liabilities and valued using CALM. Under IFRS 4, contracts are classified and measured depending on the existence of significant insurance risk. If significant insurance risk exists, the contract is classified as an insurance contract and IFRS permits the Company to continue with measuring insurance contract liabilities using CALM. If significant insurance risk does not exist, then the contract is classified as an investment contract and measured at either fair value or amortized cost. The change in reclassification has had no impact on equity at January 1, 2010 or consolidated earnings and comprehensive income at December 31, 2011.

The reconciled amount of policy liabilities under the previous CGAAP to insurance and investment contract liabilities under IFRS at transition is as follows:

| | |
|---|---|
| Policy liabilities under CGAAP at December 31, 2009 comprises: | |
| Actuarial liabilities | $ 78,923 |
| Provision for claims | 1,203 |
| Provision for policyholder dividends | 569 |
| Provision for experience rating refunds | 168 |
| Policyholder funds | 2,133 |
| | $ 82,996 |
| IFRS conversion adjustments: | |
| Remeasurement of DAC | 114 |
| Fair value of investment properties backing liabilities | (203) |
| Fair value adjustment of deferred net realized gains | 23 |
| Sub-total – IFRS conversion adjustments | (66) |
| IFRS reclassification adjustments: | |
| DAC to other assets | 447 |
| Reinsurance assets offset by reinsurance liabilities | 4,889 |
| Sub-total – IFRS reclassification adjustments | 5,336 |
| Total insurance and investment contract liabilities under IFRS at January 1, 2010 | $ 88,266 |
| Attributable to: | |
| Insurance contract liabilities | $ 87,446 |
| Investment contract liabilities | $ 820 |

**(t) Presentation of Segregated Funds on the Consolidated Balance Sheets**

The assets and liabilities of the segregated funds, totaling $67.8 billion at January 1, 2010, will be included at fair value on the Consolidated Balance Sheets as a line item within both assets and liabilities under IFRS. There was no measurement change impacting equity.

**(u) Presentation of Non-Controlling Interests within Equity**

Under the previous CGAAP, non-controlling interests were presented in the mezzanine between liabilities and equity whereas under IFRS non-controlling interest is presented within the equity section of the Consolidated Balance Sheets. The reclassification of non-controlling interests from liabilities of $147 relates to the preferred shares issued by subsidiaries.

**(v) Future Accounting Policies**

In addition, the Company may be impacted in the future by the IFRS set out in the following table:

| Revised standard | Summary of proposed changes |
|---|---|
| IFRS 4 – *Insurance Contracts* | The IASB issued an exposure draft proposing changes to the accounting standard for insurance contracts in July 2010. The proposal would require an insurer to measure insurance liabilities using a model focusing on the amount, timing, and uncertainty of future cash flows associated with fulfilling its insurance contracts. This is vastly different from the connection between insurance assets and liabilities considered under CALM and may cause significant volatility in the results of the Company. The exposure draft also proposes changes to the presentation and disclosure within the financial statements.<br>The Company will continue to measure insurance contract liabilities using CALM until such time when a new IFRS for insurance contract measurement is issued. A final standard is not expected to be implemented for several years; the Company continues to actively monitor developments in this area. |
| IFRS 9 – *Financial Instruments* | The IASB tentatively approved the adoption of the proposed new IFRS 9, *Financial Instruments* standard to be effective January 1, 2015.<br>The new standard requires all financial assets to be classified on initial recognition at amortized cost or fair value while eliminating the existing categories of available for sale, held to maturity, and loans and receivables.<br>The new standard also requires:<br>• embedded derivatives to be assessed for classification together with their financial asset host;<br>• a single expected loss impairment method be used for financial assets; and<br>• amendments to the criteria for hedge accounting and measuring effectiveness.<br>The full impact of IFRS 9 on the Company will be evaluated after the remaining stages of the IASB's project to replace IAS 39, *Financial Instruments* – impairment methodology, hedge accounting, and asset and liability offsetting – are finalized. The Company continues to actively monitor developments in this area. |
| IFRS 10 – *Consolidated Financial Statements;*<br>IFRS 11 – *Joint Arrangements;*<br>IFRS 12 – *Disclosure of Interests in Other Entities* | Effective January 1, 2013, the Company plans to adopt IFRS 10, *Consolidated Financial Statements*, IFRS 11, *Joint Arrangements*, and IFRS 12, *Disclosure of Interests in Other Entities* for the presentation and preparation of its consolidated financial statements.<br>IFRS 10, *Consolidated Financial Statements* uses consolidated principles based on a revised definition of control. The definition of control is dependent on the power of the investor to direct the activities of the investee, the ability of the investor to derive variable benefits from its holdings in the investee, and a direct link between the power to direct activities and receive benefits.<br>IFRS 11, *Joint Arrangements* separates jointly controlled entities between joint operations and joint ventures. The standard has eliminated the option of using proportionate consolidation for accounting in the interests in joint ventures, now requiring an entity to use the equity method of accounting for interests in joint ventures.<br>IFRS 12, *Disclosure of Interests in Other Entities* proposes new disclosure requirements for the interest an entity has in subsidiaries, joint arrangements, associates, and structured entities. The standard requires enhanced disclosure including how control was determined and any restrictions that might exist on consolidated assets and liabilities presented within the financial statements.<br>The Company is currently evaluating the impact of the above standards on its consolidation procedures and disclosure in preparation of the January 1, 2013 transition date. |
| IFRS 13 – *Fair Value Measurement* | Effective January 1, 2013, the Company will adopt the guidance in IFRS 13, *Fair Value Measurement* for the measurement and disclosure of assets and liabilities held at fair value. The standard refines the measurement and disclosure requirements and aims to achieve consistency with other standard setters to improve the visibility to financial statement users.<br>The Company is currently evaluating the impact this standard will have on its financial statements when it becomes effective January 1, 2013. |
| IAS 1 – *Presentation of Financial Statements* | Effective on January 1, 2013, the Company will adopt the guidance in the amended IAS 1, *Presentation of Financial Statements*. The amended standard includes requirements that OCI be classified by nature and grouped between those items that will be reclassified subsequently to profit or loss (when specific conditions are met) and those that will not be reclassified. Other amendments include changes to discontinued operations and overall financial statement presentation.<br>The Company is evaluating the impact this standard will have on the presentation of its financial statements. |
| IAS 17 – *Leases* | The IASB issued an exposure draft proposing a new accounting model for leases where both lessees and lessors would record the assets and liabilities on the balance sheet at the present value of the lease payments arising from all lease contracts. The new classification would be the right-of-use model, replacing the operating and finance lease accounting models that currently exist.<br>The full impact of adoption of the proposed changes will be determined once the final lease standard is issued, which is proposed to be in 2012. |
| IAS 19 – *Employee Benefits* | The IASB published an amended version of this standard in June 2011 that eliminates the corridor approach for actuarial gains and losses resulting in those gains and losses being recognized immediately through OCI while the net pension asset or liability would reflect the full funded status of the plan on the Consolidated Balance Sheets. Further, the standard includes changes to how the defined benefit obligation and the fair value of the plan assets would be presented within the financial statements of an entity.<br>The Company will continue to use the corridor method until January 1, 2013 when the revised IAS for employee benefits becomes effective. |

## 4. Cash and Cash Equivalents

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Cash on hand and at bank | $ 713 | $ 542 | $ 701 |
| Short-term deposits | 1,142 | 1,015 | 2,329 |
| Balance, end of period | $ 1,855 | $ 1,557 | $ 3,030 |

As at December 31, 2011, December 31, 2010, and January 1, 2010 no cash has been restricted for use by the Company.

## 5. Portfolio Investments

(a) Carrying values and estimated market values of portfolio investments are as follows:

| | December 31, 2011 | | December 31, 2010 | | January 1, 2010 | |
|---|---|---|---|---|---|---|
| | Carrying value | Market value | Carrying value | Market value | Carrying value | Market value |
| **Bonds** | | | | | | |
| Designated fair value through profit or loss [1] | $ 47,298 | $ 47,298 | $ 42,965 | $ 42,965 | $ 40,017 | $ 40,017 |
| Classified fair value through profit or loss [1] | 1,702 | 1,702 | 1,605 | 1,605 | 1,612 | 1,612 |
| Available for sale | 5,041 | 5,041 | 4,258 | 4,258 | 2,474 | 2,474 |
| Loans and receivables | 6,440 | 7,103 | 6,173 | 6,527 | 6,080 | 6,154 |
| | 60,481 | 61,144 | 55,001 | 55,355 | 50,183 | 50,257 |
| **Mortgage Loans** | | | | | | |
| Residential | 5,252 | 5,654 | 5,255 | 5,550 | 5,783 | 6,009 |
| Non-residential | 9,597 | 10,275 | 9,138 | 9,538 | 9,250 | 9,233 |
| | 14,849 | 15,929 | 14,393 | 15,088 | 15,033 | 15,242 |
| **Stocks** | | | | | | |
| Designated fair value through profit or loss [1] | 5,502 | 5,502 | 5,364 | 5,364 | 4,928 | 4,928 |
| Available for sale | 544 | 544 | 571 | 571 | 648 | 648 |
| Other | 338 | 406 | 330 | 399 | 328 | 389 |
| | 6,384 | 6,452 | 6,265 | 6,334 | 5,904 | 5,965 |
| **Investment Properties** | 3,198 | 3,198 | 2,953 | 2,953 | 2,609 | 2,609 |
| | $ 84,912 | $ 86,723 | $ 78,612 | $ 79,730 | $ 73,729 | $ 74,073 |

(1) Investments can be fair value through profit or loss in two ways: designated as fair value through profit or loss at the option of management; or, classified as fair value through profit or loss if they are actively traded for the purpose of earning investment income.

As at December 31, 2011, the Consolidated Balance Sheets value of portfolio investments which were sold in repurchase agreements related to mortgages was nil ($3 at December 31, 2010).

**(b)** Carrying value of bonds and mortgages maturing over the current and non-current term are as follows:

| | December 31, 2011 | | | |
|---|---|---|---|---|
| | Carrying Value | | | |
| | Term to maturity | | | |
| | 1 year or less | 1–5 years | Over 5 years | Total |
| Bonds | $ 5,296 | $ 11,494 | $ 43,615 | $ 60,405 |
| Mortgage loans | 1,484 | 4,959 | 8,372 | 14,815 |
| | $ 6,780 | $ 16,453 | $ 51,987 | $ 75,220 |

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | Carrying Value | | | |
| | Term to maturity | | | |
| | 1 year or less | 1–5 years | Over 5 years | Total |
| Bonds | $ 4,828 | $ 9,772 | $ 40,281 | $ 54,881 |
| Mortgage loans | 1,186 | 4,509 | 8,657 | 14,352 |
| | $ 6,014 | $ 14,281 | $ 48,938 | $ 69,233 |

| | January 1, 2010 | | | |
|---|---|---|---|---|
| | Carrying Value | | | |
| | Term to maturity | | | |
| | 1 year or less | 1–5 years | Over 5 years | Total |
| Bonds | $ 3,989 | $ 9,144 | $ 36,935 | $ 50,068 |
| Mortgage loans | 1,276 | 4,502 | 9,183 | 14,961 |
| | $ 5,265 | $ 13,646 | $ 46,118 | $ 65,029 |

The above table excludes the carrying value of impaired bonds and mortgages, as the ultimate timing of collectability is uncertain.

**(c)** Stocks include the Company's investment in an affiliated company, IGM, a member of the Power Financial Corporation group of companies, over which it exerts significant influence but does not control. The Company's proportionate share of IGM's earnings is recorded in net investment income in the Consolidated Statements of Earnings. The Company owns 9,203,309 shares of IGM at December 31, 2011 (9,203,962 at December 31, 2010) representing a 3.57% ownership interest (3.52% at December 31, 2010). The Company uses the equity method to account for its investment in IGM as it exercises significant influence. Significant influence arises from several factors, including, but not limited to the following: common control of IGM by Power Financial Corporation, shared representation of directors on the Boards of Directors of the Company and IGM, interchange of managerial personnel, and certain shared strategic alliances and significant intercompany transactions and services agreements that influence the financial and operation policies of both companies.

5. Portfolio Investments (cont'd)

| | 2011 | 2010 |
|---|---|---|
| Carrying value, beginning of year | $ 330 | $ 328 |
| Equity method earnings | 27 | 21 |
| Dividends | (19) | (19) |
| **Carrying value, end of year** | $ 338 | $ 330 |
| **Share of equity, end of year** | $ 157 | $ 152 |
| **Fair value, end of year** | $ 406 | $ 399 |

The Company and IGM both have a year-end reporting date of December 31 and as a consequence, the Company reports IGM's financial information by estimating the amount of income attributable to the Company, based on prior quarter information as well as consensus expectations, to complete equity accounting. The difference between actual and estimated results is reflected in the subsequent quarter and is not material to the Company's financial statements.

IGM's financial information as at December 31, 2011 can be obtained in its publicly available information.

**(d)** Included in portfolio investments are the following:

(i) Carrying amount of impaired investments

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Impaired amounts by type [(1)] | | | |
| Fair value through profit or loss | $ 59 | $ 105 | $ 102 |
| Available for sale | 19 | 22 | 21 |
| Loans and receivables | 47 | 53 | 83 |
| Total | $ 125 | $ 180 | $ 206 |

Provisions on loans and receivables were $19 at December 31, 2011, $21 at December 31, 2010 and $32 at January 1, 2010.

(1) Excludes amounts in funds held by ceding insurers of nil at December 31, 2011, $11 at December 31, 2010 and $6 at January 1, 2010.

(ii) The allowance for credit losses and changes in the allowance for credit losses related to investments classified as loans and receivables are as follows:

| | 2011 | | | 2010 | | |
|---|---|---|---|---|---|---|
| | Bonds | Mortgage loans | Total | Bonds | Mortgage loans | Total |
| Balance, beginning of year | $ 9 | $ 12 | $ 21 | $ 11 | $ 21 | $ 32 |
| Net provision (recovery) for credit losses – in year | (3) | 7 | 4 | (2) | 2 | – |
| Write-offs, net of recoveries | (4) | (1) | (5) | – | (7) | (7) |
| Other (including foreign exchange rate changes) | – | (1) | (1) | – | (4) | (4) |
| Balance, end of year | $ 2 | $ 17 | $ 19 | $ 9 | $ 12 | $ 21 |

The allowance for credit losses is supplemented by the provision for future credit losses included in insurance contract liabilities.

(iii) The Company holds investments with restructured terms or which have been exchanged for securities with amended terms. These investments are performing according to their new terms. Their carrying value is as follows:

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Bonds | $ – | $ 7 | $ 15 |
| Bonds with equity conversion features | 119 | 150 | 169 |
| Mortgages | 17 | 18 | 1 |
| | $ 136 | $ 175 | $ 185 |

(e) Net investment income comprises the following:

| 2011 | Bonds | Mortgage loans | Stocks | Investment properties | Other | Total |
|---|---|---|---|---|---|---|
| Regular net investment income: | | | | | | |
| Investment income earned | $ 2,982 | $ 757 | $ 181 | $ 254 | $ 195 | $ 4,369 |
| Net realized gains (losses) *(available for sale)* | 82 | – | 2 | – | – | 84 |
| Net realized gains (losses) *(other classifications)* | 7 | 14 | – | – | – | 21 |
| Net recovery (provision) for credit losses *(loans and receivables)* | 3 | (7) | – | – | – | (4) |
| Other income and expenses | – | – | – | (65) | (53) | (118) |
| | 3,074 | 764 | 183 | 189 | 142 | 4,352 |
| Changes in fair value on fair value through profit or loss assets: | | | | | | |
| Net realized/unrealized gains (losses) *(classified fair value through profit or loss)* | 66 | – | – | – | – | 66 |
| Net realized/unrealized gains (losses) *(designated fair value through profit or loss)* | 3,744 | – | (271) | 143 | 113 | 3,729 |
| | 3,810 | – | (271) | 143 | 113 | 3,795 |
| **Net investment income** | $ 6,884 | $ 764 | $ (88) | $ 332 | $ 255 | $ 8,147 |

| 2010 | Bonds | Mortgage loans | Stocks | Investment properties | Other | Total |
|---|---|---|---|---|---|---|
| Regular net investment income: | | | | | | |
| Investment income earned | $ 2,987 | $ 773 | $ 198 | $ 241 | $ 348 | $ 4,547 |
| Net realized gains (losses) *(available for sale)* | 63 | – | (2) | – | – | 61 |
| Net realized gains (losses) *(other classifications)* | 8 | 16 | – | – | – | 24 |
| Net recovery (provision) for credit losses *(loans and receivables)* | 2 | (1) | – | – | – | 1 |
| Other income and expenses | – | – | – | (64) | (58) | (122) |
| | 3,060 | 788 | 196 | 177 | 290 | 4,511 |
| Changes in fair value on fair value through profit or loss assets: | | | | | | |
| Net realized/unrealized gains (losses) *(classified fair value through profit or loss)* | 34 | – | – | – | – | 34 |
| Net realized/unrealized gains (losses) *(designated fair value through profit or loss)* | 2,387 | – | 602 | 162 | 12 | 3,163 |
| | 2,421 | – | 602 | 162 | 12 | 3,197 |
| Net investment income | $ 5,481 | $ 788 | $ 798 | $ 339 | $ 302 | $ 7,708 |

Investment income earned comprises income from investments that are classified as available for sale, loans and receivables and classified or designated as fair value through profit or loss. Investment income from bonds and mortgages includes interest income and premium and discount amortization. Income from stocks includes dividends and equity income from the investment in IGM. Investment properties income includes rental income earned on investment properties, ground rent income earned on leased and sub-leased land, fee recoveries, lease cancellation income, and interest and other investment income earned on investment properties.

(f) The carrying value of investment properties and changes in the carrying value of investment properties are as follows:

| | 2011 | 2010 |
|---|---|---|
| Balance, beginning of year | $ 2,953 | $ 2,609 |
| Additions | 159 | 353 |
| Change in fair value through profit or loss | 143 | 162 |
| Disposal | (97) | (16) |
| Foreign exchange rate changes | 40 | (155) |
| Balance, end of year | $ 3,198 | $ 2,953 |

## 6. Funds Held by Ceding Insurers

Included in funds held by ceding insurers of $9,923 at December 31, 2011 ($9,856 at December 31, 2010 and $10,984 at January 1, 2010) is an agreement with Standard Life Assurance Limited (Standard Life). During 2008, Canada Life International Re Limited (CLIRE), the Company's indirect wholly-owned Irish reinsurance subsidiary, signed an agreement with Standard Life, a U.K. based provider of life, pension and investment products, to assume by way of indemnity reinsurance, a large block of payout annuities. Under the agreement, CLIRE is required to put amounts on deposit with Standard Life and CLIRE has assumed the credit risk on the portfolio of assets included in the amounts on deposit. These amounts on deposit are included in funds held by ceding insurers on the Consolidated Balance Sheets. Income and expenses arising from the agreement are included in net investment income on the Consolidated Statements of Earnings (see note 5).

At December 31, 2011 CLIRE had amounts on deposit of $9,411 ($9,333 at December 31, 2010 and $10,329 at January 1, 2010). The details of the funds on deposit and related credit risk on the funds are as follows:

(a) Carrying values and estimated market values:

| | December 31, 2011 | | December 31, 2010 | | January 1, 2010 | |
|---|---|---|---|---|---|---|
| | Carrying value | Market value | Carrying value | Market value | Carrying value | Market value |
| Cash and cash equivalents | $ 49 | $ 49 | $ 138 | $ 138 | $ 25 | $ 25 |
| Bonds | 9,182 | 9,182 | 9,031 | 9,031 | 10,121 | 10,121 |
| Other assets | 180 | 180 | 164 | 164 | 183 | 183 |
| | $ 9,411 | $ 9,411 | $ 9,333 | $ 9,333 | $ 10,329 | $ 10,329 |
| Supporting: | | | | | | |
| Reinsurance liabilities | 9,082 | 9,082 | 8,990 | 8,990 | 9,999 | 9,999 |
| Surplus | 329 | 329 | 343 | 343 | 330 | 330 |
| | $ 9,411 | $ 9,411 | $ 9,333 | $ 9,333 | $ 10,329 | $ 10,329 |

(b) Included in the amounts on deposit are impaired investments with a carrying amount of nil ($11 at December 31, 2010 and $6 at January 1, 2010) that are net of impairments of nil ($17 at December 31, 2010 and $4 at January 1, 2010).

(c) The following table provides details of the carrying value of bonds included in the funds on deposit by industry sector:

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Bonds issued or guaranteed by: | | | |
| Provincial, state, and municipal governments | $ 88 | $ 37 | $ 41 |
| Other foreign governments | 3,074 | 3,250 | 3,913 |
| Government related | 369 | 252 | 292 |
| Supranationals | 128 | 107 | 115 |
| Asset-backed securities | 242 | 244 | 242 |
| Residential mortgage backed securities | 73 | 54 | 81 |
| Banks | 1,807 | 2,040 | 2,232 |
| Other financial institutions | 747 | 652 | 681 |
| Basic materials | 21 | 19 | 16 |
| Communications | 239 | 241 | 278 |
| Consumer products | 404 | 464 | 517 |
| Industrial products/services | 26 | 14 | 13 |
| Natural resources | 220 | 147 | 218 |
| Real estate | 381 | 373 | 393 |
| Transportation | 117 | 94 | 97 |
| Utilities | 1,135 | 950 | 962 |
| Miscellaneous | 111 | 93 | 30 |
| Total bonds | $ 9,182 | $ 9,031 | $ 10,121 |

**(d)** Asset quality:

| Bond Portfolio Quality | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| AAA | **$ 3,520** | $ 3,542 | $ 4,318 |
| AA | **1,819** | 1,725 | 1,843 |
| A | **3,116** | 3,019 | 3,181 |
| BBB | **468** | 396 | 409 |
| BB and lower | **259** | 349 | 370 |
| **Total bonds** | **$ 9,182** | $ 9,031 | $ 10,121 |

## 7. Financial Instrument Risk Management

The Company has policies relating to the identification, measurement, monitoring, mitigating, and controlling of risks associated with financial instruments. The key risks related to financial instruments are credit risk, liquidity risk and market risk (currency, interest rate and equity).

The following sections describe how the Company manages each of these risks.

**(a) Credit Risk**

Credit risk is the risk of financial loss resulting from the failure of debtors making payments when due.

The following policies and procedures are in place to manage this risk:

- Investment guidelines are in place that require only the purchase of investment-grade assets and minimize undue concentration of assets in any single geographic area, industry and company.
- Investment guidelines specify minimum and maximum limits for each asset class. Credit ratings are determined by recognized external credit rating agencies and/or internal credit review.
- Investment guidelines also specify collateral requirements.
- Portfolios are monitored continuously, and reviewed regularly with the Board of Directors or the Investment Committee of the Board of Directors.
- Credit risk associated with derivative instruments is evaluated quarterly based on conditions that existed at the balance sheet date, using practices that are at least as conservative as those recommended by regulators.
- The Company is exposed to credit risk relating to premiums due from policyholders during the grace period specified by the insurance policy or until the policy is paid up or terminated. Commissions paid to agents and brokers are netted against amounts receivable, if any.
- Reinsurance is placed with counterparties that have a good credit rating and concentration of credit risk is managed by following policy guidelines set each year by the Board of Directors. Management continuously monitors and performs an assessment of creditworthiness of reinsurers.

(i) Maximum Exposure to Credit Risk

The following table summarizes the Company's maximum exposure to credit risk related to financial instruments. The maximum credit exposure is the carrying value of the asset net of any allowances for losses.

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Cash and cash equivalents | **$ 1,855** | $ 1,557 | $ 3,030 |
| Bonds | | | |
| Fair value through profit or loss | **49,000** | 44,570 | 41,629 |
| Available for sale | **5,041** | 4,258 | 2,474 |
| Loans and receivables | **6,440** | 6,173 | 6,080 |
| Mortgage loans | **14,849** | 14,393 | 15,033 |
| Loans to policyholders | **2,858** | 2,808 | 2,786 |
| Funds held by ceding insurers (1) | **9,923** | 9,856 | 10,984 |
| Reinsurance assets | **4,046** | 4,433 | 4,889 |
| Other financial assets | **2,442** | 2,845 | 2,762 |
| Derivative assets | **927** | 930 | 693 |
| Total balance sheet maximum credit exposure | **$ 97,381** | $ 91,823 | $ 90,360 |

(1) Includes $9,411 ($9,333 at December 31, 2010 and $10,329 at January 1, 2010) of funds held by ceding insurers where the Company retains the credit risk of the assets supporting the liabilities ceded (see note 6).

7. Financial Instrument Risk Management (cont'd)

Credit risk is also mitigated by entering into collateral agreements. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and the valuation parameters. Management monitors the value of the collateral, requests additional collateral when needed and performs an impairment valuation when applicable. The Company has $10 of collateral received in 2011 ($16 of collateral received at December 31, 2010 and $35 of collateral received at January 1, 2010) relating to derivative assets.

(ii) Concentration of Credit Risk

Concentrations of credit risk arise from exposures to a single debtor, a group of related debtors or groups of debtors that have similar credit risk characteristics in that they operate in the same geographic region or in similar industries. The characteristics are similar in that changes in economic or political environments may impact their ability to meet obligations as they come due.

The following table provides details of the carrying value of bonds by industry sector and geographic distribution:

| | December 31, 2011 | | | |
|---|---|---|---|---|
| | Canada | Europe/ Reinsurance | United States | Total |
| Bonds issued or guaranteed by: | | | | |
| Canadian federal government | $ 4,328 | $ 41 | $ 2 | $ 4,371 |
| Provincial, state, and municipal governments | 6,430 | 53 | 71 | 6,554 |
| U.S. Treasury and other U.S. agencies | 271 | 968 | 516 | 1,755 |
| Other foreign governments | 185 | 8,216 | 25 | 8,426 |
| Government related | 1,293 | 955 | – | 2,248 |
| Supranationals | 443 | 211 | 12 | 666 |
| Asset-backed securities | 2,696 | 794 | 478 | 3,968 |
| Residential mortgage backed securities | 26 | 146 | 79 | 251 |
| Banks | 2,168 | 1,858 | 34 | 4,060 |
| Other financial institutions | 855 | 1,615 | 121 | 2,591 |
| Basic materials | 233 | 210 | 98 | 541 |
| Communications | 508 | 501 | 33 | 1,042 |
| Consumer products | 1,848 | 1,759 | 203 | 3,810 |
| Industrial products/services | 695 | 212 | 170 | 1,077 |
| Natural resources | 1,127 | 550 | 71 | 1,748 |
| Real estate | 608 | 1,610 | – | 2,218 |
| Transportation | 1,721 | 624 | 90 | 2,435 |
| Utilities | 3,792 | 3,148 | 470 | 7,410 |
| Miscellaneous | 2,024 | 266 | 43 | 2,333 |
| Total long term bonds | 31,251 | 23,737 | 2,516 | 57,504 |
| Short term bonds | 2,386 | 558 | 33 | 2,977 |
| | $ 33,637 | $ 24,295 | $ 2,549 | $ 60,481 |

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | Canada | Europe/ Reinsurance | United States | Total |
| Bonds issued or guaranteed by: | | | | |
| Canadian federal government | $ 3,548 | $ 31 | $ – | $ 3,579 |
| Provincial, state, and municipal governments | 5,619 | 61 | 61 | 5,741 |
| U.S. Treasury and other U.S. agencies | 335 | 932 | 517 | 1,784 |
| Other foreign governments | 216 | 7,617 | 11 | 7,844 |
| Government related | 1,057 | 946 | – | 2,003 |
| Supranationals | 381 | 224 | 11 | 616 |
| Asset-backed securities | 2,729 | 832 | 445 | 4,006 |
| Residential mortgage backed securities | 25 | 111 | 87 | 223 |
| Banks | 2,183 | 1,993 | 34 | 4,210 |
| Other financial institutions | 1,056 | 1,470 | 123 | 2,649 |
| Basic materials | 202 | 177 | 84 | 463 |
| Communications | 589 | 477 | 31 | 1,097 |
| Consumer products | 1,608 | 1,490 | 177 | 3,275 |
| Industrial products/services | 543 | 181 | 121 | 845 |
| Natural resources | 997 | 419 | 70 | 1,486 |
| Real estate | 422 | 1,400 | – | 1,822 |
| Transportation | 1,557 | 464 | 77 | 2,098 |
| Utilities | 3,266 | 2,788 | 417 | 6,471 |
| Miscellaneous | 1,728 | 222 | 36 | 1,986 |
| Total long term bonds | 28,061 | 21,835 | 2,302 | 52,198 |
| Short term bonds | 2,064 | 726 | 13 | 2,803 |
| | $ 30,125 | $ 22,561 | $ 2,315 | $ 55,001 |

| | January 1, 2010 | | | |
|---|---|---|---|---|
| | Canada | Europe/ Reinsurance | United States | Total |
| Bonds issued or guaranteed by: | | | | |
| Canadian federal government | $ 2,264 | $ 14 | $ – | $ 2,278 |
| Provincial, state, and municipal governments | 4,917 | 58 | 26 | 5,001 |
| U.S. Treasury and other U.S. agencies | 240 | 758 | 447 | 1,445 |
| Other foreign governments | 212 | 6,652 | – | 6,864 |
| Government related | 937 | 916 | – | 1,853 |
| Supranationals | 516 | 436 | 4 | 956 |
| Asset-backed securities | 2,636 | 842 | 463 | 3,941 |
| Residential mortgage backed securities | 46 | 60 | 86 | 192 |
| Banks | 2,201 | 2,299 | 40 | 4,540 |
| Other financial institutions | 1,021 | 1,507 | 127 | 2,655 |
| Basic materials | 151 | 198 | 72 | 421 |
| Communications | 598 | 473 | 38 | 1,109 |
| Consumer products | 1,384 | 1,664 | 218 | 3,266 |
| Industrial products/services | 516 | 206 | 119 | 841 |
| Natural resources | 1,000 | 577 | 78 | 1,655 |
| Real estate | 559 | 1,216 | – | 1,775 |
| Transportation | 1,414 | 495 | 81 | 1,990 |
| Utilities | 3,008 | 2,694 | 377 | 6,079 |
| Miscellaneous | 1,489 | 182 | 39 | 1,710 |
| Total long term bonds | 25,109 | 21,247 | 2,215 | 48,571 |
| Short term bonds | 1,475 | 137 | – | 1,612 |
| | $ 26,584 | $ 21,384 | $ 2,215 | $ 50,183 |

7. Financial Instrument Risk Management (cont'd)

The following table provides details of the carrying value of mortgage loans by geographic location:

| | December 31, 2011 | | | |
|---|---|---|---|---|
| | Single family residential | Multi-family residential | Commercial | Total |
| Canada | $ 1,591 | $ 3,407 | $ 7,022 | $ 12,020 |
| United States | – | 67 | 160 | 227 |
| Europe/Reinsurance | 79 | 108 | 2,415 | 2,602 |
| | $ 1,670 | $ 3,582 | $ 9,597 | $ 14,849 |

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | Single family residential | Multi-family residential | Commercial | Total |
| Canada | $ 1,622 | $ 3,528 | $ 6,691 | $ 11,841 |
| United States | – | 79 | 180 | 259 |
| Europe/Reinsurance | – | 26 | 2,267 | 2,293 |
| | $ 1,622 | $ 3,633 | $ 9,138 | $ 14,393 |

| | January 1, 2010 | | | |
|---|---|---|---|---|
| | Single family residential | Multi-family residential | Commercial | Total |
| Canada | $ 1,695 | $ 3,965 | $ 6,371 | $ 12,031 |
| United States | – | 94 | 249 | 343 |
| Europe/Reinsurance | – | 29 | 2,630 | 2,659 |
| | $ 1,695 | $ 4,088 | $ 9,250 | $ 15,033 |

(iii) Asset Quality

| Bond Portfolio Quality | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| AAA | $ 23,250 | $ 21,369 | $ 17,584 |
| AA | 10,455 | 9,247 | 8,916 |
| A | 18,198 | 16,721 | 16,284 |
| BBB | 8,043 | 6,990 | 6,666 |
| BB and lower | 535 | 674 | 733 |
| **Total bonds** | $ 60,481 | $ 55,001 | $ 50,183 |

| Derivative Portfolio Quality | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Over-the-counter contracts (counterparty ratings): | | | |
| AA | $ 336 | $ 456 | $ 325 |
| A | 591 | 474 | 368 |
| **Total** | $ 927 | $ 930 | $ 693 |

(iv) Loans Past Due, But Not Impaired

Loans that are past due but not considered impaired are loans for which scheduled payments have not been received, but management has reasonable assurance of collection of the full amount of principal and interest due. The following table provides carrying values of the loans past due, but not impaired:

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Less than 30 days | $ 3 | $ 5 | $ 45 |
| 30–90 days | 1 | 2 | 6 |
| Greater than 90 days | 1 | 2 | 9 |
| **Total** | $ 5 | $ 9 | $ 60 |

(v) The following outlines the future asset credit losses provided for in insurance and investment contract liabilities. These amounts are in addition to the allowance for asset losses included with assets:

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Participating | $ 822 | $ 771 | $ 703 |
| Non-participating | 1,388 | 1,280 | 1,476 |
| | $ 2,210 | $ 2,051 | $ 2,179 |

**(b) Liquidity Risk**

Liquidity risk is the risk that the Company will not be able to meet all cash outflow obligations as they come due. The following policies and procedures are in place to manage this risk:

- The Company closely manages operating liquidity through cash flow matching of assets and liabilities and forecasting earned and required yields, to ensure consistency between policyholder requirements and the yield of assets. Approximately 71% of insurance and investment contract liabilities are non-cashable prior to maturity or subject to market value adjustments.
- Management monitors the use of lines of credit on a regular basis, and assesses the ongoing availability of these and alternative forms of operating credit.
- Management closely monitors the solvency and capital positions of its principal subsidiaries opposite liquidity requirements at the holding company. Additional liquidity is available through established lines of credit or the capital markets.

In the normal course of business the Company enters into contracts that give rise to commitments of future minimum payments that impact short-term and long-term liquidity. The following table summarizes the principal repayment schedule of certain of the Company's financial liabilities.

| | Payments due by period | | | | | | |
|---|---|---|---|---|---|---|---|
| | Total | 1 year | 2 years | 3 years | 4 years | 5 years | Over 5 years |
| Debentures and other debt instruments | $ 303 | $ 1 | $ 1 | $ 1 | $ – | $ – | $ 300 |
| Capital trust securities [(1)] | 800 | – | – | – | – | – | 800 |
| Purchase obligations | 38 | 34 | 4 | – | – | – | – |
| Pension contributions | 96 | 96 | – | – | – | – | – |
| | $ 1,237 | $ 131 | $ 5 | $ 1 | $ – | $ – | $ 1,100 |

(1) Payments due have not been reduced to reflect that the Company held capital trust securities of $38 principal amount ($44 carrying value).

**(c) Market Risk**

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in market factors which include three types: currency risk, interest rate (including related inflation) risk and equity risk.

(i) Currency Risk

Currency risk relates to the Company operating and holding financial instruments in different currencies. For the assets backing insurance and investment contract liabilities that are not matched by currency, changes in foreign exchange rates can expose the Company to the risk of foreign exchange losses not offset by liability decreases. The Company has net investments in foreign operations. In addition, the Company's debt obligations are mainly denominated in Canadian dollars. In accordance with IFRS, foreign currency translation gains and losses from net investments in foreign operations, net of related hedging activities and tax effects, are recorded in AOCI. Strengthening or weakening of the Canadian dollar spot rate compared to the U.S. dollar, British pound and euro spot rates impacts the Company's total share capital and surplus. Correspondingly, the Company's book value per share and capital ratios monitored by rating agencies are also impacted. The following policies and procedures are in place to mitigate the Company's exposure to currency risk.

7. Financial Instrument Risk Management (cont'd)

- The Company uses financial measures such as constant currency calculations to monitor the effect of currency translation fluctuations.
- Investments are normally made in the same currency as the liabilities supported by those investments. Segmented Investment Guidelines include maximum tolerances for unhedged currency mismatch exposures.
- Foreign currency assets acquired to back liabilities are normally converted back to the currency of the liability using foreign exchange contracts.
- A 10% weakening of the Canadian dollar against foreign currencies would be expected to increase non-participating insurance and investment contract liabilities and their supporting assets by approximately the same amount resulting in an immaterial change to net earnings. A 10% strengthening of the Canadian dollar against foreign currencies would be expected to decrease non-participating insurance and investment contract liabilities and their supporting assets by approximately the same amount resulting in an immaterial change in net earnings.

(ii) Interest Rate Risk

Interest rate risk exists if asset and liability cash flows are not closely matched and interest rates change causing a difference in value between the asset and liability. The following policies and procedures are in place to mitigate the Company's exposure to interest rate risk:

- The Company utilizes a formal process for managing the matching of assets and liabilities. This involves grouping general fund assets and liabilities into segments. Assets in each segment are managed in relation to the liabilities in the segment.
- Interest rate risk is managed by investing in assets that are suitable for the products sold.
- Where these products have benefit or expense payments that are dependent on inflation (inflation-indexed annuities, pensions and disability claims) the Company generally invests in real return instruments to hedge its real dollar liability cash flows. Some protection against changes in the inflation index is achieved as any related change in the fair value of the assets will be largely offset by a similar change in the fair value of the liabilities.
- For products with fixed and highly predictable benefit payments, investments are made in fixed income assets or real estate whose cash flows closely match the liability product cash flows. Where assets are not available to match certain period cash flows such as long-tail cash flows a portion of these are invested in equities and the rest are duration matched. Hedging instruments are employed where necessary when there is a lack of suitable permanent investments to minimize loss exposure to interest rate changes. To the extent these cash flows are matched, protection against interest rate change is achieved and any change in the fair value of the assets will be offset by a similar change in the fair value of the liabilities.
- For products with less predictable timing of benefit payments, investments are made in fixed income assets with cash flows of a shorter duration than the anticipated timing of benefit payments, or equities as described below.
- The risk associated with the mismatch in portfolio duration and cash flow, asset prepayment exposure and the pace of asset acquisition are quantified and reviewed regularly.

Projected cash flows from the current assets and liabilities are used in CALM to determine insurance contract liabilities. Valuation assumptions have been made regarding rates of returns on supporting assets, fixed income, equity and inflation. The valuation assumptions use best estimates of future reinvestment rates and inflation assumptions with an assumed correlation together with margins for adverse deviation set in accordance with professional standards. These margins are necessary to provide for possibilities of misestimation and/or future deterioration in the best estimate assumptions and provide reasonable assurance that insurance contract liabilities cover a range of possible outcomes. Margins are reviewed periodically for continued appropriateness.

Projected cash flows from fixed income assets used in actuarial calculations are reduced to provide for potential asset default losses. The net effective yield rate reduction averaged 0.18% (0.20% in 2010). The calculation for future credit losses on assets is based on the credit quality of the underlying asset portfolio.

Testing under several interest rate scenarios (including increasing and decreasing rates) is done to assess reinvestment risk.

One way of measuring the interest rate risk associated with this assumption is to determine the effect on the insurance and investment contract liabilities impacting the shareholder earnings of the Company of a 1% immediate parallel shift in the yield curve. These interest rate changes will impact the projected cash flows.

- The effect of an immediate 1% parallel increase in the yield curve would be to decrease these insurance and investment contract liabilities by approximately $149 causing an increase in net earnings of approximately $102.
- The effect of an immediate 1% parallel decrease in the yield curve would be to increase these insurance and investment contract liabilities by approximately $579 causing a decrease in net earnings of approximately $413.

In addition to above, if this change in the yield curve persisted for an extended period the range of the tested scenarios might change. The effect of an immediate 1% parallel decrease or increase in the yield curve persisting for a year would have immaterial additional effects on the reported insurance and investment contract liability.

(iii) Equity Risk

Equity risk is the uncertainty associated with the valuation of assets arising from changes in equity markets. To mitigate price risk, the Company has investment policy guidelines in place that provide for prudent investment in equity markets within clearly defined limits. The risks associated with segregated fund guarantees have been mitigated through a hedging program for lifetime Guaranteed Minimum Withdrawal Benefit guarantees (GMWB) using equity futures, currency forwards, and interest rate derivatives. For policies with segregated fund guarantees, the Company generally determines insurance contract liabilities at a conditional tail expectation of 75 (CTE75) level.

Some insurance and investment contract liabilities are supported by investment properties, common stocks and private equities, for example segregated fund products and products with long-tail cash flows. Generally these liabilities will fluctuate in line with equity market values. There will be additional impacts on these liabilities as equity market values fluctuate. A 10% increase in equity markets would be expected to additionally decrease non-participating insurance and investment contract liabilities by approximately $26 causing an increase in net earnings of approximately $21. A 10% decrease in equity markets would be expected to additionally increase non-participating insurance and investment contract liabilities by approximately $76 causing a decrease in net earnings of approximately $57.

The best estimate return assumptions for equities are primarily based on long-term historical averages. Changes in the current market could result in changes to these assumptions and will impact both asset and liability cash flows. A 1% increase in the best estimate assumption would be expected to decrease non-participating insurance contract liabilities by approximately $389 causing an increase in net earnings of approximately $292. A 1% decrease in the best estimate assumption would be expected to increase non-participating insurance contract liabilities by approximately $423 causing a decrease in net earnings of approximately $316.

***Caution Related to Risk Sensitivities***

In this document we have provided estimates of sensitivities and risk exposure measures for certain risks. These include the sensitivity due to specific changes in interest rate levels projected and market prices as at the valuation date. Actual results can differ significantly from these estimates for a variety of reasons including:

- Assessment of the circumstances that led to the scenario may lead to changes in (re)investment approaches and interest rate scenarios considered,
- Changes in actuarial, investment return and future investment activity assumptions,
- Actual experience differing from the assumptions,
- Changes in business mix, effective tax rates and other market factors,
- Interactions among these factors and assumptions when more than one changes, and
- The general limitations of our internal models.

For these reasons, the sensitivities should only be viewed as directional estimates of the underlying sensitivities for the respective factors based on the assumptions outlined below. Given the nature of these calculations, we cannot provide assurance that the actual impact on net earnings attributed to shareholders will be as indicated.

(iv) Segregated funds guaranteed exposure

The Company offers retail segregated fund products, unitized with profits (UWP) products and variable annuity products that provide for certain guarantees that are tied to the market values of the investment funds. A significant decline in the market value of these funds could increase the Company's liability exposure for providing these guarantees. The Company's exposure to these guarantees at the balance sheet date was:

| | December 31, 2011 | | | | |
|---|---|---|---|---|---|
| | | Investment deficiency by benefit type | | | |
| | Market value | Income | Maturity | Death | Total* |
| **Canada** | **$ 22,883** | **$ –** | **$ 42** | **$ 301** | **$ 304** |
| **United States** | **972** | **640** | **–** | **40** | **680** |
| **Europe** | **2,214** | **1** | **121** | **134** | **134** |
| **Total** | **$ 26,069** | **$ 641** | **$ 163** | **$ 475** | **$ 1,118** |

| | December 31, 2010 | | | | |
|---|---|---|---|---|---|
| | | Investment deficiency by benefit type | | | |
| | Market value | Income | Maturity | Death | Total* |
| Canada | $ 23,324 | $ – | $ 24 | $ 135 | $ 137 |
| United States | 1,140 | 342 | – | 42 | 383 |
| Europe | 2,095 | – | 118 | 119 | 119 |
| Total | $ 26,559 | $ 342 | $ 142 | $ 296 | $ 639 |

* A policy can only receive a payout from one of the three trigger events (income election, maturity or death). Total deficiency measures the point-in-time exposure assuming the most costly trigger event for each policy occurred on December 31, 2011 and December 31, 2010.

## 8. Financial Instrument Fair Value Measurement

In accordance with IFRS 7, *Financial Instruments – Disclosures*, the Company's assets and liabilities recorded at fair value have been categorized based upon the following fair value hierarchy:

Level 1 inputs utilize observable, quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Financial assets and liabilities utilizing Level 1 inputs include actively exchange traded equity securities and mutual and segregated funds which have available prices in an active market with no redemption restrictions.

Level 2 inputs utilize other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. The fair values for some Level 2 securities were obtained from a pricing service. The pricing service inputs include, but are not limited to, benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, offers and reference data. Level 2 securities include those priced using a matrix which is based on credit quality and average life, government and agency securities, restricted stock, some private bonds and equities, most investment-grade and high-yield corporate bonds, most asset-backed securities (ABS) and most over-the-counter derivatives.

Level 3 inputs are unobservable and include situations where there is little, if any, market activity for the asset or liability. The prices of the majority of Level 3 securities were obtained from single broker quotes and internal pricing models. Financial assets and liabilities utilizing Level 3 inputs include certain bonds, certain ABS, and some private equities and investments in mutual and segregated funds where there are redemption restrictions and certain over the counter derivatives.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The following tables present information about the Company's financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2011, December 31, 2010 and January 1, 2010 and indicate the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value:

| | December 31, 2011 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Assets measured at fair value | | | | |
| Financial assets at fair value through profit or loss | | | | |
| Bonds | $ – | $ 48,971 | $ 29 | $ 49,000 |
| Stocks | 5,485 | 3 | 14 | 5,502 |
| Total financial assets at fair value through profit or loss | 5,485 | 48,974 | 43 | 54,502 |
| Available for sale financial assets | | | | |
| Bonds | – | 5,022 | 19 | 5,041 |
| Stocks | 2 | – | 1 | 3 |
| Total available for sale financial assets | 2 | 5,022 | 20 | 5,044 |
| Other assets – derivatives (1) | – | 927 | – | 927 |
| Total assets measured at fair value | $ 5,487 | $ 54,923 | $ 63 | $ 60,473 |
| Liabilities measured at fair value | | | | |
| Other liabilities – derivatives (2) | $ – | $ 273 | $ – | $ 273 |

(1) Excludes collateral received of $10
(2) Excludes collateral pledged of $45

During 2011 no assets have been transferred from level 1 to level 2 (or level 2 to level 1) due to the stock no longer being active in a quoted market.

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Assets measured at fair value | | | | |
| Financial assets at fair value through profit or loss | | | | |
| Bonds | $ – | $ 44,535 | $ 35 | $ 44,570 |
| Stocks | 4,947 | – | 417 | 5,364 |
| Total financial assets at fair value through profit or loss | 4,947 | 44,535 | 452 | 49,934 |
| Available for sale financial assets | | | | |
| Bonds | – | 4,238 | 20 | 4,258 |
| Stocks | 16 | – | 1 | 17 |
| Total available for sale financial assets | 16 | 4,238 | 21 | 4,275 |
| Other assets – derivatives [1] | – | 930 | – | 930 |
| Total assets measured at fair value | $ 4,963 | $ 49,703 | $ 473 | $ 55,139 |
| Liabilities measured at fair value | | | | |
| Other liabilities – derivatives [2] | $ – | $ 148 | $ – | $ 148 |

(1) Excludes collateral received of $16
(2) Excludes collateral pledged of $39

During 2010 no assets have been transferred from level 1 to level 2 (or level 2 to level 1) due to the stock no longer being active in a quoted market.

| | January 1, 2010 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Assets measured at fair value | | | | |
| Financial assets at fair value through profit or loss | | | | |
| Bonds | $ – | $ 41,538 | $ 91 | $ 41,629 |
| Stocks | 4,783 | – | 145 | 4,928 |
| Total financial assets at fair value through profit or loss | 4,783 | 41,538 | 236 | 46,557 |
| Available for sale financial assets | | | | |
| Bonds | – | 2,452 | 22 | 2,474 |
| Stocks | 65 | – | 1 | 66 |
| Total available for sale financial assets | 65 | 2,452 | 23 | 2,540 |
| Other assets – derivatives [1] | – | 676 | 17 | 693 |
| Total assets measured at fair value | $ 4,848 | $ 44,666 | $ 276 | $ 49,790 |
| Liabilities measured at fair value | | | | |
| Other liabilities – derivatives | $ – | $ 188 | $ – | $ 188 |

(1) Excludes collateral received of $35

8. Financial Instruments Fair Value Measurement (cont'd)

The following table presents additional information about assets and liabilities measured at fair value on a recurring basis and for which the Company has utilized Level 3 inputs to determine fair value for the years ended December 31, 2011 and 2010:

| | 2011 | | | | |
|---|---|---|---|---|---|
| | Fair value through profit or loss bonds | Available for sale bonds | Other assets – derivatives | Fair value through profit or loss stocks | Available for sale stocks |
| Balance, beginning of year | $ 35 | $ 20 | $ – | $ 417 | $ 1 |
| Total gains/(losses) | | | | | |
| Included in net earnings | 3 | – | – | 35 | – |
| Included in OCI | – | 1 | – | – | – |
| Purchases | – | – | – | 65 | – |
| Sales | (4) | – | – | (6) | – |
| Settlements | (5) | (2) | – | – | – |
| Transfers out of Level 3 | – | – | – | (497) | – |
| Balance, end of year | $ 29 | $ 19 | $ – | $ 14 | $ 1 |
| Total gains/(losses) for the year included in net earnings for assets held at December 31, 2011 | $ 3 | $ – | $ – | $ (3) | $ – |

| | 2010 | | | | |
|---|---|---|---|---|---|
| | Fair value through profit or loss bonds | Available for sale bonds | Other assets – derivatives | Fair value through profit or loss stocks | Available for sale stocks |
| Balance, beginning of year | $ 91 | $ 22 | $ 17 | $ 145 | $ 1 |
| Total gains/(losses) | | | | | |
| Included in net earnings | (2) | – | (17) | 16 | – |
| Purchases | – | – | – | 287 | – |
| Sales | – | – | – | (30) | – |
| Settlements | (6) | (2) | – | – | – |
| Transfers out of Level 3 | (48) | – | – | (1) | – |
| Balance, end of year | $ 35 | $ 20 | $ – | $ 417 | $ 1 |
| Total gains/(losses) for the year included in net earnings for assets held at December 31, 2010 | $ 1 | $ – | $ (17) | $ 16 | $ – |

## 9. Pledging of Assets

The amount of assets included in the Company's balance sheet which have a security interest by way of pledging $577 ($554 at December 31, 2010 and $595 at January 1, 2010), in respect of reinsurance agreements.

## 10. Goodwill and Intangible Assets

### (a) Goodwill

The carrying value of goodwill, all in the shareholder account, and changes in the carrying value of goodwill are as follows:

| | 2011 | 2010 |
|---|---|---|
| Balance, beginning of year | $ 5,267 | $ 5,270 |
| Sale of subsidiary by London Reinsurance Group (LRG) | – | (3) |
| Balance, end of year | $ 5,267 | $ 5,267 |

The Company has no accumulated impairment losses on goodwill at December 31, 2011 and 2010.

### (b) Intangible Assets

The carrying value of intangible assets and changes in the carrying value of intangible assets are as follows:

(i) Indefinite life intangible assets:

| 2011 | Brands and trademarks | Customer contract related | Shareholder portion of acquired future participating account profit | Total |
|---|---|---|---|---|
| Cost and net carrying amount | | | | |
| Balance, beginning of year | $ 371 | $ 354 | $ 354 | $ 1,079 |
| Changes in foreign exchange rates | 1 | – | – | 1 |
| **Balance, end of year** | $ 372 | $ 354 | $ 354 | $ 1,080 |

| 2010 | Brands and trademarks | Customer contract related | Shareholder portion of acquired future participating account profit | Total |
|---|---|---|---|---|
| Cost and net carrying amount | | | | |
| Balance, beginning of year | $ 382 | $ 354 | $ 354 | $ 1,090 |
| Changes in foreign exchange rates | (11) | – | – | (11) |
| Balance, end of year | $ 371 | $ 354 | $ 354 | $ 1,079 |

The Company has no accumulated impairment losses on indefinite life intangible assets at December 31, 2011 and 2010.

10. Goodwill and Intangible Assets (cont'd)

(ii) Finite life intangible assets:

| 2011 | Customer contract related | | Distribution channels | | Software | | Total | |
|---|---|---|---|---|---|---|---|---|
| Amortization period range | | 10–20 years | | 30 years | | 5–10 years | | |
| Weighted average remaining amortization period | | 11 years | | 22 years | | – | | |
| Amortization method | | Straight-line | | Straight-line | | Straight-line | | |
| Cost | | | | | | | | |
| Balance, beginning of year | $ | 329 | $ | 100 | $ | 242 | $ | 671 |
| Acquisitions | | – | | – | | 3 | | 3 |
| Other | | – | | – | | 48 | | 48 |
| **Balance, end of year** | $ | 329 | $ | 100 | $ | 293 | $ | 722 |
| Accumulated amortization and impairment | | | | | | | | |
| Balance, beginning of year | $ | (110) | $ | (24) | $ | (101) | $ | (235) |
| Impairment | | – | | – | | (4) | | (4) |
| Changes in foreign exchange rates | | – | | (1) | | (1) | | (2) |
| Amortization | | (18) | | (4) | | (28) | | (50) |
| **Balance, end of year** | $ | (128) | $ | (29) | $ | (134) | | (291) |
| **Net carrying amount** | $ | 201 | $ | 71 | $ | 159 | $ | 431 |

| 2010 | Customer contract related | | Distribution channels | | Software | | Total | |
|---|---|---|---|---|---|---|---|---|
| Amortization period range | | 10–20 years | | 30 years | | 5–10 years | | |
| Weighted average remaining amortization period | | 13 years | | 22 years | | – | | |
| Amortization method | | Straight-line | | Straight-line | | Straight-line | | |
| Cost | | | | | | | | |
| Balance, beginning of year | $ | 330 | $ | 108 | $ | 199 | $ | 637 |
| Acquisitions | | – | | – | | 2 | | 2 |
| Changes in foreign exchange rates | | (1) | | (8) | | (2) | | (11) |
| Other | | – | | – | | 43 | | 43 |
| Balance, end of year | $ | 329 | $ | 100 | $ | 242 | $ | 671 |
| Accumulated amortization and impairment | | | | | | | | |
| Balance, beginning of year | $ | (92) | $ | (21) | $ | (76) | $ | (189) |
| Changes in foreign exchange rates | | – | | 1 | | – | | 1 |
| Amortization | | (18) | | (4) | | (25) | | (47) |
| Balance, end of year | $ | (110) | $ | (24) | $ | (101) | $ | (235) |
| Net carrying amount | $ | 219 | $ | 76 | $ | 141 | $ | 436 |

**(c) Goodwill and indefinite life intangible assets have been assigned to cash generating units as follows:**

| 2011 | Goodwill | Indefinite life intangible assets | Total |
|---|---|---|---|
| Canada | | | |
| Group | $ 1,024 | $ – | $ 1,024 |
| Individual insurance/wealth management | 2,723 | 973 | 3,696 |
| Europe | | | |
| Insurance and annuities | 1,500 | 107 | 1,607 |
| Reinsurance | 1 | – | 1 |
| United States | | | |
| Financial services | 19 | – | 19 |
| | $ 5,267 | $ 1,080 | $ 6,347 |

| 2010 | Goodwill | Indefinite life intangible assets | Total |
|---|---|---|---|
| Canada | | | |
| Group | $ 1,024 | $ – | $ 1,024 |
| Individual insurance/wealth management | 2,723 | 973 | 3,696 |
| Europe | | | |
| Insurance and annuities | 1,500 | 106 | 1,606 |
| Reinsurance | 1 | – | 1 |
| United States | | | |
| Financial services | 19 | – | 19 |
| | $ 5,267 | $ 1,079 | $ 6,346 |

**(d) Recoverable Amount**

The recoverable amount is determined as the higher of fair value less costs to sell and value-in-use. Fair value is determined using a combination of commonly accepted valuation methodologies, namely comparable trading multiples, comparable transaction multiples and discounted cash flow analysis. Comparable trading and transaction multiples methodologies calculate value by applying multiples observed in the market against historical results or projections approved by management as applicable. Value calculated by discounted cash flow analysis use cash flow projections based on financial budgets approved by management covering an initial period (typically four or five years). Value beyond the initial period is derived from applying a terminal value multiple to the final year of the initial projection period. The terminal value multiple is a function of the discount rate and the estimated terminal growth rate. The estimated terminal growth rate is not to exceed the long-term average growth rate (inflation rate) of the markets in which the Company operates.

The key assumptions used for the discounted cash flow calculations are based on past experience and external sources of information. The key assumptions are as follows:

- Risk adjusted discount rates used for the calculation of present value are based on the Company's weighted average cost of capital.
- Economic assumptions are based on market yields on risk-free interest rates at the end of each reporting period.
- Terminal growth growth rate represents the rate used to extrapolate new business contributions beyond the business plan period, and is based on management's estimate of future growth and range between 1.5% and 3.0%, depending on the nature of the business.

## 11. Owner Occupied Properties and Other Fixed Assets

The carrying value of owner occupied properties and fixed assets and the changes in the carrying value of owner occupied properties and fixed assets is as follows:

| | 2011 | | 2010 | |
|---|---|---|---|---|
| | Owner occupied properties | Other fixed assets | Owner occupied properties | Other fixed assets |
| Carrying value, beginning of year | $ 323 | $ 380 | $ 303 | $ 368 |
| Less: accumulated depreciation/impairments | (13) | (295) | (12) | (277) |
| Net carrying value, beginning of year | 310 | 85 | 291 | 91 |
| Additions | 49 | 37 | 22 | 22 |
| Disposals | – | – | – | (1) |
| Depreciation | (2) | (26) | (2) | (25) |
| Net exchange differences | – | 1 | (1) | (2) |
| Net carrying value, end of year | 357 | 97 | 310 | 85 |
| Plus: accumulated depreciation/impairments | 16 | 321 | 13 | 295 |
| **Carrying value, end of year** | $ 373 | $ 418 | $ 323 | $ 380 |

The following table provides details of the carrying value of owner occupied properties and fixed assets by geographic location:

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Canada | $ 426 | $ 369 | $ 352 |
| Europe | 28 | 26 | 30 |
| | $ 454 | $ 395 | $ 382 |

There are no restrictions on the title of the owner occupied properties and fixed assets nor are they pledged as security for debt.

## 12. Other Assets

(a) Other assets consist of the following:

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Premiums in course of collection | $ 418 | $ 378 | $ 393 |
| Interest due and accrued | 854 | 809 | 826 |
| Current income taxes | 63 | 496 | 728 |
| Prepaid expenses | 73 | 79 | 58 |
| Accounts receivable | 425 | 376 | 261 |
| Accrued pension asset (note 23) | 420 | 302 | 248 |
| Deferred acqusition costs (note 12(b)) | 529 | 508 | 501 |
| Other | 153 | 278 | 53 |
| | $ 2,935 | $ 3,226 | $ 3,068 |

$1,986 of total other assets are expected to be realized within 12 months from the reporting date.

The above amounts due within 12 months exclude DAC. The changes in DAC are presented below in (b).

(b) Changes in deferred acquisition costs for investment contracts are as follows:

| | 2011 | 2010 |
|---|---|---|
| Balance, beginning of year | $ 508 | $ 501 |
| Additions | 123 | 136 |
| Amortization | (71) | (47) |
| Foreign exchange | 6 | (41) |
| Disposals | (37) | (41) |
| | $ 529 | $ 508 |

## 13. Segregated Funds for the Risk of Unitholders

### (a) Segregated funds – consolidated net assets

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Bonds | $ 10,356 | $ 9,086 | $ 8,379 |
| Mortgage loans | 2,303 | 2,058 | 1,744 |
| Stocks | 52,220 | 52,616 | 47,168 |
| Investment properties | 5,457 | 5,598 | 6,012 |
| Cash and cash equivalents | 5,302 | 5,336 | 5,538 |
| Accrued income | 241 | 203 | 156 |
| Other liabilities | (1,656) | (1,259) | (1,192) |
| | $ 74,223 | $ 73,638 | $ 67,805 |

### (b) Segregated funds – consolidated statements of changes in net assets

| | 2011 | 2010 |
|---|---|---|
| **Segregated funds net assets, beginning of year** | $ 73,638 | $ 67,805 |
| Additions (deductions): | | |
| Policyholder deposits | 10,761 | 10,387 |
| Net investment income | 130 | 499 |
| Net realized capital gains (losses) on investments | 974 | 1,869 |
| Net unrealized capital gains (losses) on investments | (3,020) | 3,151 |
| Unrealized gains (losses) due to changes in foreign exchange rates | 275 | (2,209) |
| Policyholder withdrawals | (8,552) | (8,018) |
| Net transfer from General Fund | 17 | 154 |
| | 585 | 5,833 |
| **Segregated funds net assets, end of year** | $ 74,223 | $ 73,638 |

## 14. Insurance and Investment Contract Liabilities

### (a) Insurance and investment contract liabilities

| | December 31, 2011 | | |
|---|---|---|---|
| | Gross | Ceded | Net |
| Insurance contract liabilities | $ 94,111 | $ 3,823 | $ 90,288 |
| Investment contract liabilities | 746 | 223 | 523 |
| | $ 94,857 | $ 4,046 | $ 90,811 |

| | December 31, 2010 | | |
|---|---|---|---|
| | Gross | Ceded | Net |
| Insurance contract liabilities | $ 88,929 | $ 4,192 | $ 84,737 |
| Investment contract liabilities | 764 | 241 | 523 |
| | $ 89,693 | $ 4,433 | $ 85,260 |

| | January 1, 2010 | | |
|---|---|---|---|
| | Gross | Ceded | Net |
| Insurance contract liabilities | $ 87,446 | $ 4,603 | $ 82,843 |
| Investment contract liabilities | 820 | 286 | 534 |
| | $ 88,266 | $ 4,889 | $ 83,377 |

14. Insurance and Investment Contract Liabilities (cont'd)

**(b) Composition of insurance and investment contract liabilities and related supporting assets**

(i) The composition of insurance and investment contract liabilities is as follows:

| | December 31, 2011 | | |
|---|---|---|---|
| | Gross | Ceded | Net |
| Participating | | | |
| Individual insurance | $ 26,470 | $ (49) | $ 26,519 |
| Europe/reinsurance | 1,230 | – | 1,230 |
| Corporate | 1,580 | 2 | 1,578 |
| Non-Participating | | | |
| Individual insurance | 6,609 | 823 | 5,786 |
| Wealth management | 13,752 | – | 13,752 |
| Group | 6,738 | 95 | 6,643 |
| Europe/reinsurance | 35,464 | 1,432 | 34,032 |
| Corporate | 3,014 | 1,743 | 1,271 |
| | $ 94,857 | $ 4,046 | $ 90,811 |

| | December 31, 2010 | | |
|---|---|---|---|
| | Gross | Ceded | Net |
| Participating | | | |
| Individual insurance | $ 25,094 | $ 6 | $ 25,088 |
| Europe/reinsurance | 1,209 | – | 1,209 |
| Corporate | 1,469 | 4 | 1,465 |
| Non-Participating | | | |
| Individual insurance | 5,692 | 1,132 | 4,560 |
| Wealth management | 13,391 | – | 13,391 |
| Group | 6,331 | 132 | 6,199 |
| Europe/reinsurance | 33,491 | 1,385 | 32,106 |
| Corporate | 3,016 | 1,774 | 1,242 |
| | $ 89,693 | $ 4,433 | $ 85,260 |

| | January 1, 2010 | | |
|---|---|---|---|
| | Gross | Ceded | Net |
| Participating | | | |
| Individual insurance | $ 23,113 | $ (12) | $ 23,125 |
| Europe/reinsurance | 1,456 | – | 1,456 |
| Corporate | 1,488 | 5 | 1,483 |
| Non-Participating | | | |
| Individual insurance | 4,998 | 1,084 | 3,914 |
| Wealth management | 12,700 | – | 12,700 |
| Group | 5,974 | 135 | 5,839 |
| Europe/reinsurance | 35,205 | 1,661 | 33,544 |
| Corporate | 3,332 | 2,016 | 1,316 |
| | $ 88,266 | $ 4,889 | $ 83,377 |

(ii) The composition of the assets supporting liabilities and equity is as follows:

| | December 31, 2011 | | | | | |
|---|---|---|---|---|---|---|
| | Bonds | Mortgage loans | Stocks | Investment properties | Other | Total |
| **Carrying value** | | | | | | |
| Participating liabilities | | | | | | |
| Individual insurance | 11,862 | 6,686 | 3,864 | 507 | 3,551 | 26,470 |
| Europe/reinsurance | 855 | 56 | 176 | 22 | 121 | 1,230 |
| Corporate | 1,316 | 79 | – | – | 185 | 1,580 |
| Non-participating liabilities | | | | | | |
| Individual insurance | 4,485 | 271 | 1,063 | 20 | 770 | 6,609 |
| Wealth management | 8,029 | 2,932 | 217 | – | 2,574 | 13,752 |
| Group | 4,159 | 1,536 | 49 | – | 994 | 6,738 |
| Europe/reinsurance | 20,348 | 2,506 | 119 | 2,093 | 10,398 | 35,464 |
| Corporate | 944 | 140 | – | – | 1,930 | 3,014 |
| Other | 6,520 | 328 | – | 6 | 73,102 | 79,956 |
| Total equity | 1,963 | 315 | 896 | 550 | 10,405 | 14,129 |
| **Total carrying value** | $ 60,481 | $ 14,849 | $ 6,384 | $ 3,198 | $ 104,030 | $ 188,942 |
| **Fair value** | $ 61,144 | $ 15,929 | $ 6,452 | $ 3,198 | $ 104,030 | $ 190,753 |

| | December 31, 2010 | | | | | |
|---|---|---|---|---|---|---|
| | Bonds | Mortgage loans | Stocks | Investment properties | Other | Total |
| Carrying value | | | | | | |
| Participating liabilities | | | | | | |
| Individual insurance | 10,872 | 6,158 | 3,775 | 419 | 3,870 | 25,094 |
| Europe/reinsurance | 805 | 65 | 185 | 27 | 127 | 1,209 |
| Corporate | 1,184 | 97 | – | – | 188 | 1,469 |
| Non-participating liabilities | | | | | | |
| Individual insurance | 3,574 | 240 | 857 | 13 | 1,008 | 5,692 |
| Wealth management | 8,586 | 3,327 | 516 | – | 962 | 13,391 |
| Group | 3,796 | 1,502 | 58 | – | 975 | 6,331 |
| Europe/reinsurance | 18,874 | 2,189 | 108 | 1,914 | 10,406 | 33,491 |
| Corporate | 928 | 146 | – | – | 1,942 | 3,016 |
| Other | 4,731 | 330 | – | 19 | 74,471 | 79,551 |
| Total equity | 1,651 | 339 | 766 | 561 | 9,695 | 13,012 |
| Total carrying value | $ 55,001 | $ 14,393 | $ 6,265 | $ 2,953 | $ 103,644 | $ 182,256 |
| Fair value | $ 55,355 | $ 15,088 | $ 6,334 | $ 2,953 | $ 103,644 | $ 183,374 |

| | January 1, 2010 | | | | | |
|---|---|---|---|---|---|---|
| | Bonds | Mortgage loans | Stocks | Investment properties | Other | Total |
| Carrying value | | | | | | |
| Participating liabilities | | | | | | |
| Individual insurance | $ 10,244 | $ 6,025 | $ 3,535 | $ 324 | $ 2,985 | $ 23,113 |
| Europe/reinsurance | 784 | 77 | 224 | 33 | 338 | 1,456 |
| Corporate | 1,162 | 134 | – | – | 192 | 1,488 |
| Non-participating liabilities | | | | | | |
| Individual insurance | 2,473 | 219 | 587 | 21 | 1,698 | 4,998 |
| Wealth management | 8,220 | 3,465 | 336 | – | 679 | 12,700 |
| Group | 3,615 | 1,643 | 68 | – | 648 | 5,974 |
| Europe/reinsurance | 18,903 | 2,535 | 131 | 1,683 | 11,953 | 35,205 |
| Corporate | 941 | 187 | – | – | 2,204 | 3,332 |
| Other | 2,287 | 322 | – | 4 | 70,481 | 73,094 |
| Total equity | 1,554 | 426 | 1,023 | 544 | 9,330 | 12,877 |
| Total carrying value | $ 50,183 | $ 15,033 | $ 5,904 | $ 2,609 | $ 100,508 | $ 174,237 |
| Fair value | $ 50,257 | $ 15,242 | $ 5,965 | $ 2,609 | $ 100,508 | $ 174,581 |

14. Insurance and Investment Contract Liabilities (cont'd)

Cash flows of assets supporting insurance and investment contract liabilities are matched within reasonable limits. Changes in the fair values of these assets are essentially offset by changes in the fair value of insurance and investment contract liabilities.

Changes in the fair values of assets backing capital and surplus, less related income taxes, would result in a corresponding change in surplus over time in accordance with investment accounting policies.

**(c) Changes in Insurance Contract Liabilities**

The change in insurance contract liabilities during the year was the result of the following business activities and changes in actuarial estimates:

| | 2011 | | |
|---|---|---|---|
| | Participating | | |
| | Gross liability | Reinsurance asset | Net |
| **Balance, beginning of year** | $ 27,731 | $ 10 | $ 27,721 |
| Crown ancillary reclassification | (89) | – | (89) |
| Impact of new business | 133 | – | 133 |
| Normal change in force | 1,509 | (12) | 1,521 |
| Management action and changes in assumptions | (110) | (45) | (65) |
| Impact of foreign exchange rate changes | 70 | – | 70 |
| **Balance, end of year** | $ 29,244 | $ (47) | $ 29,291 |

| | Non-participating | | | |
|---|---|---|---|---|
| | Gross liability | Reinsurance asset | Net | Total Net |
| **Balance, beginning of year** | $ 61,198 | $ 4,182 | $ 57,016 | $ 84,737 |
| Crown ancillary reclassification | 89 | – | 89 | – |
| Impact of new business | 2,025 | 141 | 1,884 | 2,017 |
| Normal change in force | 1,613 | (53) | 1,666 | 3,187 |
| Management action and changes in assumptions | (795) | (469) | (326) | (391) |
| Impact of foreign exchange rate changes | 737 | 69 | 668 | 738 |
| **Balance, end of year** | $ 64,867 | $ 3,870 | $ 60,997 | $ 90,288 |

| | 2010 | | |
|---|---|---|---|
| | Participating | | |
| | Gross liability | Reinsurance asset | Net |
| Balance, beginning of year | $ 26,006 | $ (7) | $ 26,013 |
| Impact of new business | 193 | – | 193 |
| Normal change in force | 1,742 | 16 | 1,726 |
| Management action and changes in assumptions | (4) | – | (4) |
| Impact of foreign exchange rate changes | (206) | 1 | (207) |
| Balance, end of year | $ 27,731 | $ 10 | $ 27,721 |

| | Non-participating | | | |
|---|---|---|---|---|
| | Gross liability | Reinsurance asset | Net | Total Net |
| Balance, beginning of year | $ 61,440 | $ 4,610 | $ 56,830 | $ 82,843 |
| Impact of new business | 2,997 | 141 | 2,856 | 3,049 |
| Normal change in force | 297 | (271) | 568 | 2,294 |
| Management action and changes in assumptions | (472) | (77) | (395) | (399) |
| Business movement from/to external parties | (1) | – | (1) | (1) |
| Impact of foreign exchange rate changes | (3,063) | (221) | (2,842) | (3,049) |
| Balance, end of year | $ 61,198 | $ 4,182 | $ 57,016 | $ 84,737 |

Under fair value accounting, movement in the market value of the supporting assets is a major factor in the movement of insurance contract liabilities. Changes in the fair value of assets are largely offset by corresponding changes in the fair value of liabilities. The change in the value of the insurance contract liabilities associated with the change in the value of the supporting assets is included in the normal change in force above.

In 2011, the major contributors to the increase in net insurance contract liabilities were the impact of new business ($2,017 increase) and the normal change in the in force business ($3,187 increase) primarily due to the change in fair value.

Net non-participating insurance contract liabilities decreased by $326 in 2011 due to management actions and changes in assumptions.

The Company adopted the revised Actuarial Standards of Practice for subsection 2350 relating to future mortality improvement in net insurance contract liabilities for life insurance and annuities. The resulting decrease in net non-participating insurance contract liabilities for life insurance was $331. The resulting change in net insurance contract liabilities for annuities was a $3 decrease.

The remaining decrease was primarily due to increased provisions for policyholder behavior in Individual Insurance ($213 increase), provisions for asset liability matching ($131 increase) and a reclassification from miscellaneous liabilities ($29 increase) offset by updated expenses and taxes ($132 decrease), updated morbidity assumptions ($86 decrease), updated base life insurance mortality ($30 decrease), and modeling refinements across the Canadian Segment ($109 decrease).

Net participating insurance contract liabilities decreased by $65 in 2011 due to management actions and assumption changes. The decrease was primarily due to decreases in the provision for future policyholder dividends ($1,556 decrease), modeling refinements in Canada ($256 decrease), improved Individual Life mortality ($230 decrease) and updated expenses and taxes ($15 decrease) partially offset by lower investment returns ($1,952 increase), and increased provisions for policyholder behavior ($40 increase).

In 2010, the major contributors to the increase in insurance contract liabilities was the impact of new business and the normal change in the in force business partially offset by the impact of foreign exchange rates.

Net non-participating insurance contract liabilities decreased by $395 in 2010 due to management actions and assumption changes. The decrease was primarily due to reduced provisions for asset liability matching ($169 decrease), modeling refinements ($111 decrease), updated expenses and taxes ($110 decrease), improved Life mortality ($57 decrease), and improved Group Insurance morbidity ($48 decrease) partially offset by increased provisions for policyholder behavior ($76 increase), strengthened longevity ($18 increase) and strengthened provisions for asset default ($8 increase).

Net participating insurance contract liabilities decreased by $4 in 2010 due to management actions and assumption changes. The decrease was primarily due to updated expenses ($260 decrease), improved investment ($20 decrease), and improved Individual Life mortality ($13 decrease) partially offset by modeling refinements ($213 increase), increases in the provision for future policyholder dividends ($66 increase) and increased provisions for policyholder behavior ($10 increase).

**(d) Change in investment contract liabilities measured at fair value**

| | 2011 | | | 2010 | | |
|---|---|---|---|---|---|---|
| | Gross | Ceded | Net | Gross | Ceded | Net |
| **Balance, beginning of year** | **$ 764** | **$ 241** | **$ 523** | $ 820 | $ 286 | $ 534 |
| Normal change in force business | **(55)** | **(26)** | **(29)** | (35) | (29) | (6) |
| Investment experience | **29** | **1** | **28** | – | – | – |
| Impact of foreign exchange rate changes | **8** | **7** | **1** | (21) | (16) | (5) |
| **Balance, end of year** | **$ 746** | **$ 223** | **$ 523** | $ 764 | $ 241 | $ 523 |

The carrying value of investment contract liabilities approximates its fair value.

14. Insurance and Investment Contract Liabilities (cont'd)

**(e) Canadian Universal Life Embedded Derivatives**

The Company bifurcated the index linked component of the universal life contracts as this embedded derivative is not closely related to the insurance host and is not itself an insurance contract. The forward contracts are contractual agreements in which the policyholder is entitled to the performance of the underlying index. The policyholder may select one or more of the following indices: the TSX, the S&P and the AEX.

**(f) Actuarial Assumptions**

In the computation of insurance contract liabilities, valuation assumptions have been made regarding rates of mortality/morbidity, investment returns, levels of operating expenses, rates of policy termination and rates of utilization of elective policy options or provisions. The valuation assumptions use best estimates of future experience together with a margin for adverse deviation. These margins are necessary to provide for possibilities of misestimation and/or future deterioration in the best estimate assumptions and provide reasonable assurance that insurance contract liabilities cover a range of possible outcomes. Margins are reviewed periodically for continued appropriateness.

The methods for arriving at these valuation assumptions are outlined below:

***Mortality***

A life insurance mortality study is carried out annually for each major block of insurance business. The results of each study are used to update the Company's experience valuation mortality tables for that business. When there is insufficient data, use is made of the latest industry experience to derive an appropriate valuation mortality assumption. The actuarial standards were amended to remove the requirement that, for life insurance, any reduction in liabilities due to mortality improvement assumption be offset by an equal amount of provision for adverse deviation. Appropriate provisions have been made for future mortality deterioration on term insurance.

Annuitant mortality is also studied regularly and the results used to modify established industry experience annuitant mortality tables. Mortality improvement has been projected to occur throughout future years for annuitants.

***Morbidity***

The Company uses industry developed experience tables modified to reflect emerging Company experience. Both claim incidence and termination are monitored regularly and emerging experience is factored into the current valuation.

***Property and casualty reinsurance***

Insurance contract liabilities for property and casualty reinsurance written by LRG, a subsidiary of the London Life Insurance Company (London Life), are determined using accepted actuarial practices for property and casualty insurers in Canada. Reflecting the long-term nature of the business, insurance contract liabilities have been established using cash flow valuation techniques including discounting. The insurance contract liabilities are based on cession statements provided by ceding companies. In certain instances, LRG management adjusts cession statement amounts to reflect management's interpretation of the treaty. Differences will be resolved via audits and other loss mitigation activities. In addition, insurance contract liabilities also include an amount for incurred but not reported losses (IBNR) which may differ significantly from the ultimate loss development. The estimates and underlying methodology are continually reviewed and updated and adjustments to estimates are reflected in earnings. LRG analyzes the emergence of claims experience against expected assumptions for each reinsurance contract separately and at the portfolio level. If necessary, a more in depth analysis is undertaken of the cedant experience.

***Investment returns***

The assets which correspond to the different liability categories are segmented. For each segment, projected cash flows from the current assets and liabilities are used in CALM to determine insurance contract liabilities. Cash flows from assets are reduced to provide for asset default losses. Testing under several interest rate and equity scenarios (including increasing and decreasing rates) is done to provide for reinvestment risk (see note 7(c)).

***Expenses***

Contractual policy expenses (e.g. sales commissions) and tax expenses are reflected on a best estimate basis. Expense studies for indirect operating expenses are updated regularly to determine an appropriate estimate of future operating expenses for the liability type being valued. Improvements in unit operating expenses are not projected. An inflation assumption is incorporated in the estimate of future operating expenses consistent with the interest rate scenarios projected under CALM as inflation is assumed to be correlated with new money interest rates.

***Policy termination***

Studies to determine rates of policy termination are updated regularly to form the basis of this estimate. Industry data is also available and is useful where the Company has no experience with specific types of policies or its exposure is limited. The Company has significant exposures in respect of the T-100 and Level Cost of Insurance Universal Life products in Canada and policy termination rates at the renewal period for renewable term policies in Canada and Reinsurance. Industry experience has guided our persistency assumption for these products as our own experience is very limited.

***Utilization of elective policy options***

There are a wide range of elective options embedded in the policies issued by the Company. Examples include term renewals, conversion to whole life insurance (term insurance), settlement annuity purchase at guaranteed rates (deposit annuities) and guarantee re-sets (segregated fund maturity guarantees). The assumed rates of utilization are based on Company or industry experience when it exists and when not on judgment considering incentives to utilize the option. Generally, whenever it is clearly in the best interests of an informed policyholder to utilize an option, then it is assumed to be elected.

***Policyholder dividends and adjustable policy features***

Future policyholder dividends and other adjustable policy features are included in the determination of insurance contract liabilities with the assumption that policyholder dividends or adjustable benefits will change in the future in response to the relevant experience. The dividend and policy adjustments are determined consistent with policyholders' reasonable expectations, such expectations being influenced by the participating policyholder dividend policies and/or policyholder communications, marketing material and past practice. It is our expectation that changes will occur in policyholder dividend scales or adjustable benefits for participating or adjustable business respectively, corresponding to changes in the best estimate assumptions, resulting in an immaterial net change in insurance contract liabilities. Where underlying guarantees may limit the ability to pass all of this experience back to the policyholder, the impact of this non-adjustability impacting shareholder earnings is reflected in the impacts of changes in best estimate assumptions above.

**(g) Risk management**

(i) Insurance risk

Insurance risk is the risk that the insured event occurs and that there are large deviations between expected and actual actuarial assumptions including mortality, persistency, longevity, morbidity, expense variations and investment returns.

As an insurance company, Great-West Life is in the business of accepting risk associated with insurance contract liabilities. The objective of the Company is to mitigate its exposure to risk arising from these contracts through product design, product and geographical diversification, the implementation of the Company's underwriting strategy guidelines, and through the use of reinsurance arrangements.

The following table provides information about the Company's insurance contract liabilities sensitivities to management's best estimate of the approximate impact as a result of changes in assumptions used to determine the Company's liability associated with these contracts.

| | 2011 | |
|---|---|---|
| | Changes in assumptions | Impact on profit or loss |
| Mortality | 2% | $ (150) |
| Annuitant mortality | 2% | $ (170) |
| Morbidity | 5% | $ (181) |
| Investment returns | | |
| Parallel shift in yield curve | | |
| Increase | 1% | $ 102 |
| Decrease | 1% | $ (413) |
| Change in equity markets | | |
| Increase | 10% | $ 21 |
| Decrease | 10% | $ (57) |
| Change in best estimate returns for equities | | |
| Increase | 1% | $ 292 |
| Decrease | 1% | $ (316) |
| Expenses | 5% | $ (49) |
| Policy termination | 10% | $ (369) |

| | 2010 | |
|---|---|---|
| | Changes in assumptions | Impact on profit or loss |
| Mortality | 2% | $ (132) |
| Annuitant mortality | 2% | $ (166) |
| Morbidity | 5% | $ (151) |
| Investment returns | | |
| Parallel shift in yield curve | | |
| Increase | 1% | $ (19) |
| Decrease | 1% | $ (281) |
| Change in equity markets | | |
| Increase | 10% | $ 25 |
| Decrease | 10% | $ (53) |
| Change in best estimate returns for equities | | |
| Increase | 1% | $ 241 |
| Decrease | 1% | $ (279) |
| Expenses | 5% | $ (45) |
| Policy termination | 10% | $ (267) |

14. Insurance and Investment Contract Liabilities (cont'd)

Concentration risk may arise from geographic regions, accumulation of risks and market risk. The concentration of insurance risk before and after reinsurance by geographic region is described below.

| | December 31, 2011 | | | December 31, 2010 | | | January 1, 2010 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Gross | Ceded | Net | Gross | Ceded | Net | Gross | Ceded | Net |
| Canada | $ 53,569 | $ 869 | $ 52,700 | $ 50,508 | $ 1,270 | $ 49,238 | $ 46,785 | $ 1,207 | $ 45,578 |
| Europe | 36,694 | 1,432 | 35,262 | 34,700 | 1,385 | 33,315 | 36,661 | 1,661 | 35,000 |
| United States | 4,594 | 1,745 | 2,849 | 4,485 | 1,778 | 2,707 | 4,820 | 2,021 | 2,799 |
| | $ 94,857 | $ 4,046 | $ 90,811 | $ 89,693 | $ 4,433 | $ 85,260 | $ 88,266 | $ 4,889 | $ 83,377 |

(ii) Reinsurance risk

Maximum limits per insured life benefit amount (which vary by line of business) are established for life and health insurance and reinsurance is purchased for amounts in excess of those limits.

Reinsurance costs and recoveries as defined by the reinsurance agreement are reflected in the valuation with these costs and recoveries being appropriately calibrated to the direct assumptions.

Reinsurance contracts do not relieve the Company from its obligations to policyholders. Failure of reinsurers to honour their obligations could result in losses to the Company. The Company evaluates the financial condition of its reinsurers to minimize its exposure to significant losses from reinsurer insolvencies.

Certain of the reinsurance contracts are on a funds withheld basis where the Company retains the assets supporting the reinsured insurance contract liabilities, thus minimizing the exposure to significant losses from reinsurer insolvency on those contracts.

## 15. Financing Charges

Financing charges consist of the following:

| | 2011 | 2010 |
|---|---|---|
| Interest on long-term debentures and other debt instruments | $ 20 | $ 20 |
| Net interest on capital trust securities | 48 | 48 |
| Other | 11 | 6 |
| | $ 79 | $ 74 |

## 16. Debentures and Other Debt Instruments

Debentures and other debt instruments consist of the following:

| | December 31, 2011 | | December 31, 2010 | | January 1, 2010 | |
|---|---|---|---|---|---|---|
| | Carrying value | Market value | Carrying value | Market value | Carrying value | Market value |
| **Long term** | | | | | | |
| **Operating:** | | | | | | |
| Notes payable with interest rate of 8.0% due May 6, 2014, unsecured | $ 3 | $ 3 | $ 4 | $ 4 | $ 5 | $ 5 |
| **Capital:** | | | | | | |
| **Great-West** | | | | | | |
| 6.74% debentures due November 24, 2036, unsecured | 200 | 200 | 200 | 200 | 200 | 200 |
| **Canada Life** | | | | | | |
| 6.40% subordinated debentures due December 11, 2028, unsecured | 100 | 115 | 100 | 110 | 100 | 105 |
| | 300 | 315 | 300 | 310 | 300 | 305 |
| **Total debentures and other debt instruments** | $ 303 | $ 318 | $ 304 | $ 314 | $ 305 | $ 310 |

## 17. Other Liabilities

(a) Other liabilities consist of the following:

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Current income taxes | $ 370 | $ 354 | $ 369 |
| Accounts payable | 539 | 914 | 430 |
| Pension and other post-employment benefits (note 23) | 547 | 459 | 460 |
| Deferred income reserve (note 17(b)) | 406 | 377 | 357 |
| Other | 1,075 | 1,267 | 1,070 |
| | $ 2,937 | $ 3,371 | $ 2,686 |

$1,984 of total other liabilities are expected to be realized within 12 months from the reporting date.

The above amounts due within 12 months exclude DIR. The changes of DIR are presented below in (b).

(b) Changes in deferred income reserves are as follows:

| | 2011 | 2010 |
|---|---|---|
| Balance, beginning of year | $ 377 | $ 357 |
| Additions | 97 | 108 |
| Amortization | (38) | (27) |
| Foreign exchange | 5 | (33) |
| Disposals | (35) | (28) |
| | $ 406 | $ 377 |

## 18. Capital Trust Securities

| | December 31, 2011 | | December 31, 2010 | | January 1, 2010 | |
|---|---|---|---|---|---|---|
| | Carrying value | Market value | Carrying value | Market value | Carrying value | Market value |
| Capital trust securities | | | | | | |
| 5.995% Capital trust securities due December 31, 2052, unsecured (GWLCT) | $ 350 | $ 363 | $ 350 | $ 375 | $ 350 | $ 383 |
| 6.679% Capital trust securities due June 30, 2052, unsecured (CLCT) | 300 | 307 | 300 | 320 | 300 | 331 |
| 7.529% Capital trust securities due June 30, 2052, unsecured (CLCT) | 150 | 197 | 150 | 198 | 150 | 186 |
| | 800 | 867 | 800 | 893 | 800 | 900 |
| Acquisition related fair market value adjustment | 15 | – | 17 | – | 19 | – |
| Trust securities held by consolidated group as temporary investments | (44) | (44) | (44) | (44) | (41) | (41) |
| Total | $ 771 | $ 823 | $ 773 | $ 849 | $ 778 | $ 859 |

Great-West Life Capital Trust (GWLCT), a trust established by Great-West Life, had issued $350 of capital trust securities, the proceeds of which were used by GWLCT to purchase Great-West Life senior debentures in the amount of $350, and Canada Life Capital Trust (CLCT), a trust established by Canada Life, had issued $450 of capital trust securities, the proceeds of which were used by CLCT to purchase Canada Life senior debentures in the amount of $450. Distributions and interest on the capital trust securities are classified as financing charges on the Consolidated Statements of Earnings (see note 15).

Pursuant to the CLFC acquisition in 2003, the Canadian regulated subsidiaries had purchased certain of these Capital Trust Debentures. During the year ended December 31, 2009, the Company disposed of $138 principal amount of capital trust securities held by the consolidated group as temporary investments.

Subject to regulatory approval, GWLCT and CLCT may redeem the GREATs and CLiCS, in whole or in part, at any time. The CLiCS Series A securities are callable at par on June 30, 2012 and the GREATs Series A securities are callable at par on December 31, 2012.

## 19. Participating Account

The Company controlled a 100% equity interest in London Life and Canada Life at December 31, 2011 and 2010. The participating operations and the participating balance sheets are presented as combined or consolidated in the operations in the Company's financial statements. The following tables provide additional information related to the operations and financial position of each entity.

### (a) Net earnings, participating account:

| | 2011 | 2010 |
|---|---|---|
| Net earnings attributable to participating account before policyholder dividends | | |
| Great-West Life | $ 173 | $ 146 |
| London Life | 825 | 697 |
| Canada Life | 253 | 241 |
| | 1,251 | 1,084 |
| Policyholder dividends | | |
| Great-West Life | (134) | (129) |
| London Life | (758) | (730) |
| Canada Life | (242) | (235) |
| | (1,134) | (1,094) |
| Net earnings (loss) – participating account | $ 117 | $ (10) |

### (b) Participating account surplus:

| | December 31 2011 | December 31 2010 | January 1 2010 |
|---|---|---|---|
| Participating account accumulated surplus: | | | |
| Great-West Life | $ 492 | $ 453 | $ 436 |
| London Life | 1,598 | 1,531 | 1,564 |
| Canada Life | 49 | 38 | 32 |
| | 2,139 | 2,022 | 2,032 |
| Participating account accumulated other comprehensive income (loss): | | | |
| Great-West Life | 18 | 8 | 6 |
| London Life | 53 | 5 | (1) |
| Canada Life | 6 | 3 | 3 |
| Accumulated other comprehensive income (loss) – participating account | 77 | 16 | 8 |
| | $ 2,216 | $ 2,038 | $ 2,040 |

### (c) Participating account – other comprehensive income:

| | 2011 | 2010 |
|---|---|---|
| Other comprehensive income (loss) attributable to participating account | | |
| Great-West Life | $ 10 | $ 2 |
| London Life | 48 | 6 |
| Canada Life | 3 | – |
| Other comprehensive income (loss) – participating account | $ 61 | $ 8 |

## 20. Share Capital

Authorized

Unlimited Preferred Shares

Unlimited Common Shares

Issued and outstanding

| | December 31, 2011 | | December 31, 2010 | | January 1, 2010 | |
|---|---|---|---|---|---|---|
| | Number | Carrying value | Number | Carrying value | Number | Carrying value |
| Preferred shares: | | | | | | |
| Series O, 5.55% Non-Cumulative Preferred Shares | – | $ – | – | $ – | 6,278,671 | $ 157 |
| Series Q, 5.00% Non-Cumulative Preferred Shares | 40,000 | 1 | 40,000 | 1 | 40,000 | 1 |
| | 40,000 | $ 1 | 40,000 | $ 1 | 6,318,671 | $ 158 |
| Common shares: | | | | | | |
| Balance, beginning of year | 2,117,015 | $ 6,426 | 2,088,655 | $ 6,116 | 2,088,655 | $ 6,116 |
| Issued to parent | – | – | 28,360 | 310 | – | – |
| Balance, end of year | 2,117,015 | $ 6,426 | 2,117,015 | $ 6,426 | 2,088,655 | $ 6,116 |
| Total share capital | | $ 6,427 | | $ 6,427 | | $ 6,274 |

***Preferred Shares***

On October 29, 2010, the Company redeemed all of its outstanding 5.55% Non-Cumulative Preferred Shares Series O at a price of $25.00 per share.

The Series Q, 5.00% Non-Cumulative Preferred Shares are redeemable at the option of the Company for $25.00 per share on the later of December 31, 2007 and the date on which there are no Great-West Life Capital Trust Securities outstanding in GWLCT, subject to regulatory approval.

***Common Shares***

On October 26, 2010 the Company issued 28,360 common shares to its parent, Lifeco, for a total of $310. The Company then invested $255 in common shares of its wholly owned subsidiary LIG which in turn invested $255 in common shares of its indirect wholly owned subsidiary London Life.

## 21. Capital Management

At the consolidated company level, the Company monitors the amount of consolidated capital available, and the amounts deployed in its various operating subsidiaries. The amount of capital deployed in any particular company or country is dependent upon local regulatory requirements as well as the Company's internal assessment of capital requirements in the context of its operational risks and requirements and strategic plans.

Since the timing of available funds cannot always be matched precisely to commitments, imbalances may arise when demands for funds exceed those on hand. Also, a demand for funds may arise as a result of the Company taking advantage of current investment opportunities. The sources of the funds that may be required in such situations include bank financing and the issuance of debentures and equity securities.

The Company's practice is to maintain the capitalization of its regulated operating subsidiaries at a level that will exceed the relevant minimum regulatory capital requirements in the jurisdictions in which they operate.

The capitalization of the Company and its operating subsidiaries will also take into account the views expressed by the various credit rating agencies that provide financial strength and other ratings to the Company.

In Canada, OSFI has established a capital adequacy measurement for life insurance companies incorporated under the Insurance Companies Act (Canada) and their subsidiaries, known as the Minimum Continuing Capital and Surplus Requirements (MCCSR).

21. Capital Management (cont'd)

For Canadian regulatory reporting purposes, capital is defined by OSFI in its MCCSR guideline. The following table provides the MCCSR information and ratios for Great-West Life:

| | 2011 | 2010 |
|---|---|---|
| **Capital Available:** | | |
| **Tier 1 Capital** | | |
| Common shares | $ 6,426 | $ 6,426 |
| Shareholder surplus | 5,638 | 6,563 |
| Innovative instruments | 769 | 771 |
| Other Tier 1 Capital Elements | 2,022 | 609 |
| Gross Tier 1 Capital | 14,855 | 14,369 |
| **Deductions from Tier 1:** | | |
| Goodwill & intangible assets in excess of limit | 5,661 | 5,699 |
| Other deductions | 1,240 | 1,211 |
| **Net Tier 1 Capital** | 7,954 | 7,459 |
| Deductions/Adjustments to Net Tier 1 Capital | (36) | (37) |
| **Adjusted Net Tier 1 Capital** | 7,918 | 7,422 |
| **Tier 2 Capital** | | |
| Tier 2A | 182 | 77 |
| Tier 2B allowed | 300 | 300 |
| Tier 2C | 1,252 | 1,206 |
| Tier 2 Deductions/Adjustments | (36) | (37) |
| **Net Tier 2 Capital** | 1,698 | 1,546 |
| **Total Available Capital** | $ 9,616 | $ 8,968 |
| **Capital Required:** | | |
| Assets Default & market risk | $ 1,815 | $ 1,679 |
| Insurance Risks | 1,961 | 1,877 |
| Interest Rate Risks | 927 | 851 |
| Other | 6 | 7 |
| **Total Capital Required** | $ 4,709 | $ 4,414 |
| **MCCSR ratios:** | | |
| **Tier 1** | 168% | 168% |
| **Total** | 204% | 203% |

The result of adoption of IFRS as at January 1, 2011 is a reduction in Total Available Capital subject to phase-in of $636. This impact is to be phased-in over eight quarters beginning March 31, 2011 in accordance with the IFRS transition guidance outlined by OSFI.

In the United Kingdom, Canada Life U.K. is required to satisfy the capital resources requirements set out in the Integrated Prudential Sourcebook, part of the Financial Services Authority Handbook. The capital requirements are set prescribed by a formulaic capital requirement (Pillar 1) and an individual capital adequacy framework which requires an entity to self-assess an appropriate amount of capital it should hold, based on the risks encountered from its business activities. At the end of 2011, Canada Life U.K. complied with the capital resource requirements in the United Kingdom.

As at December 31, 2011 and 2010 the Company maintained capital levels above the minimum local regulatory requirements in each of its other foreign operations.

The Company is both a user and a provider of reinsurance, including both traditional reinsurance, which is undertaken primarily to mitigate against assumed insurance risks, and financial or finite reinsurance, under which the amount of insurance risk passed to the reinsurer or its reinsureds may be more limited. The Company is required to put amounts on deposit for certain reinsurance transactions. These amounts on deposit are presented in funds held by ceding insurers on the Consolidated Balance Sheets. Some of these amounts on deposit support surplus.

The Company has also established policies and procedures designed to identify, measure and report all material risks. Management is responsible for establishing capital management procedures for implementing and monitoring the capital plan. The Board of Directors reviews and approves all capital transactions undertaken by management.

## 22. Share-Based Payments

(a) Lifeco has a stock option plan (the Plan) pursuant to which options to subscribe for common shares of Lifeco may be granted to certain officers and employees of Great-West Life and its affiliates. Lifeco's Compensation Committee (the Committee) administers the Plan and, subject to the specific provisions of the Plan, fixes the terms and conditions upon which options are granted. The exercise price of each option granted under the Plan is fixed by the Committee, but cannot under any circumstances be less than the weighted-average trading price per Lifeco common share on the Toronto Stock Exchange for the five trading days preceding the date of the grant. Termination of employment may, in certain circumstances, result in forfeiture of the options, unless otherwise determined by the Committee.

During 2011, 1,115,400 options were granted (583,000 options were granted during 2010). The weighted average fair value of options granted during 2011 was $4.40 per option. The fair value of each option was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions used for those options granted in 2011: dividend yield 4.53%, expected volatility 23.29%, risk-free interest rate 2.87%, and expected life of 7 years.

To date, four categories of options have been granted under the Plan. The exercise of the options in three of these four categories is subject to the attainment of certain financial targets of the Company. Options vest over a period of up to 8 years. All of the options have a maximum exercise period of ten years. The maximum number of Lifeco common shares that may be issued under the Plan is currently 52,600,000.

The following table summarizes the status of, and changes in, options outstanding and the weighted-average exercise price:

| | 2011 | | 2010 | |
|---|---|---|---|---|
| | **Options** | **Weighted-average exercise price** | Options | Weighted-average exercise price |
| Outstanding, beginning of year | **9,101,729** | **$ 28.10** | 11,403,922 | $ 24.71 |
| Granted | **1,115,400** | **27.16** | 583,300 | 26.82 |
| Exercised | **(565,164)** | **17.91** | (2,815,959) | 14.05 |
| Forfeited/expired | **(96,926)** | **31.65** | (69,534) | 32.99 |
| Outstanding, end of year | **9,555,039** | **$ 28.55** | 9,101,729 | $ 28.10 |
| Options exercisable at end of year | **6,954,981** | **$ 27.89** | 6,209,883 | $ 26.19 |

Compensation expense due to transactions accounted for as equity-settled share-based payments of $4 after-tax in 2011 ($3 after-tax in 2010) arising from transactions in which the services received did not qualify for recognition as an asset, has been recognized in the Consolidated Statements of Earnings.

The entity measured the compensation for the Director's services based on fair market value when measuring the services received in the deferred share unit plan (DSPP/DSUP).

The following table summarizes information on the ranges of exercise prices including weighted-average remaining contractual life at December 31, 2011:

| | Outstanding | | | Exercisable | | |
|---|---|---|---|---|---|---|
| Exercise price ranges | Options | Weighted-average remaining contractual life | Weighted-average exercise price | Options | Weighted-average exercise price | Expiry |
| $19.42–$29.84 | 106,299 | 0.58 | 26.61 | 106,299 | 25.61 | 2012 |
| $19.42–$29.84 | 1,932,500 | 1.51 | 21.54 | 1,932,500 | 21.54 | 2013 |
| $24.37–$26.00 | 569,000 | 2.34 | 25.23 | 569,000 | 25.23 | 2014 |
| $29.84–$29.84 | 1,595,000 | 3.95 | 29.84 | 1,595,000 | 29.84 | 2015 |
| $27.16–$31.27 | 482,000 | 4.50 | 30.35 | 482,000 | 30.35 | 2016 |
| $35.36–$37.22 | 1,042,800 | 5.20 | 37.06 | 445,548 | 37.01 | 2017 |
| $31.27–$31.27 | 2,315,000 | 6.37 | 31.27 | 1,717,334 | 31.27 | 2018 |
| $27.13–$27.13 | 531,140 | 8.34 | 26.78 | 107,300 | 26.79 | 2020 |
| $27.16–27.16 | 981,300 | 9.17 | 27.16 | – | – | 2021 |

22. Share-Based Payments (cont'd)

**(b)** The Company has both a voluntary Deferred Share Unit Plan and a mandatory Deferred Share Unit Plan (the "Voluntary DSU Plan" and the "Mandatory DSU Plan" respectively) for its Directors to promote a greater alignment of interests between the Directors and the shareholders of the Corporation. Under the Voluntary DSU Plan, each Director may elect to receive his or her annual retainer and attendance fees entirely in the form of Deferred Share Units, entirely in cash, or equally in cash and Deferred Share Units. Under the Mandatory DSU Plan, which was created as of April 29, 2004, each Director who is a resident of Canada or the United States receives $45,000 of his or her annual retainer in the form of Deferred Share Units. In both cases the number of Deferred Share Units granted is determined by dividing the amount of remuneration payable to the Director by the weighted average trading price per Common Share on the TSX for the last five trading days of the preceding fiscal quarter (such weighted average trading price being the "value of a Deferred Share Unit"). Directors receive additional Deferred Share Units in respect of dividends payable on the Common Shares based on the value of a Deferred Share Unit at that time. Deferred Share Units are redeemable at the time that an individual ceases to be a Director by a lump sum cash payment, based on the value of the Deferred Share Units on the date of redemption. This amount is fully taxable as income in the year in which it is received. In 2010, $1 in directors fees were used to acquire Deferred Share Units.

## 23. Pension Plans and Other Post-Employment Benefits

The Company and its subsidiaries maintain contributory and non-contributory defined benefit pension plans for certain employees and advisors. The Company and its subsidiaries also maintain defined contribution pension plans for certain employees and advisors.

The defined benefit pension plans provide pensions based on length of service and final average pay. For most plans, active plan participants share in the cost of benefits through employee contributions. Certain pension payments are indexed either on an ad hoc basis or a guaranteed basis. The determination of the defined benefit obligation reflects pension benefits in accordance with the terms of the plans. The assets supporting the funded pension plans are held in separate trusteed pension funds. The obligations for the wholly unfunded plans are included in other liabilities and are supported by general assets. The recognized current cost of pension benefits is charged to operating expenses.

The defined contribution pension plans provide pension benefits based on accumulated employee and Company contributions. Company contributions to these plans are a set percentage of employees' annual income and may be subject to certain vesting requirements.

The Company and its subsidiaries also provide post-employment health, dental and life insurance benefits to eligible employees, advisors and their dependents. Retirees share in the cost of benefits through deductibles, co-insurance and caps on benefits. The amount of some of the post-employment benefits other than pensions depends on future cost escalation. These post-employment benefits are not pre-funded and the amount of the obligation for these benefits is included in other liabilities and is supported by general assets. The recognized current cost of post-retirement non-pension benefits is charged to operating expenses.

Prior years' cumulative experience gains or losses in excess of the greater of 10% of the beginning of year fair value of plan assets and defined benefit obligation are amortized over the expected average remaining working lives of the employee/advisor group.

Subsidiaries of the Company have declared partial windups in respect of certain defined benefit pension plans, the impact of which has not been reflected in the pension plan accounts.

The overall expected rate of return on plan assets for the year is determined based on long-term market expectations prevailing at the beginning of the year for each asset class, weighted by portfolio allocation, less an allowance in respect of all expenses expected to be charged to the fund. Anticipated future long-term performance of individual asset categories is considered, reflecting management's best estimates of expected future inflation and expected real yields on fixed income securities and equities. Since the prior year end there have been no changes in the method used to determine the overall expected rate of return.

The period of time over which benefits are assumed to be paid is based on best estimate of future mortality, including allowances for mortality improvements. Mortality assumptions are significant in measuring the defined benefit obligation for defined benefit plans. The mortality assumptions applied by the Company take into consideration average life expectancy, including allowances for future mortality improvement as appropriate, and reflect variations in such factors as age, gender and geographic location. The assumptions also take into consideration an estimation of future improvements in longevity. This estimate is subject to considerable uncertainty and judgment is required in establishing this assumption.

The mortality tables are reviewed at least annually, and assumptions are in accordance with accepted actuarial practice in Canada. Emerging plan experience is reviewed and considered in establishing the best estimate for future mortality.

The following tables reflect the financial position of the Company's contributory and non-contributory defined benefit plans at December 31, 2011 and 2010 and January 1, 2010:

**(a) Plan Assets, Benefit Obligation and Funded Status**

| | Defined benefit pension plans | | | Other post-employment benefits | | |
|---|---|---|---|---|---|---|
| | **December 31 2011** | December 31 2010 | January 1 2010 | **December 31 2011** | December 31 2010 | January 1 2010 |
| **Change in Fair Value of Plan Assets** | | | | | | |
| Fair value of plan assets, beginning of period | **$ 2,842** | $ 2,671 | $ 2,671 | **$ –** | $ – | $ – |
| Expected return on plan assets | **170** | 161 | – | **–** | – | – |
| Employee contributions | **16** | 16 | – | **–** | – | – |
| Employer contributions | **80** | 78 | – | **16** | 17 | – |
| Actuarial gains (losses) | **(111)** | 81 | – | **–** | – | – |
| Benefits paid | **(163)** | (129) | – | **(16)** | (17) | – |
| Settlement | **–** | (2) | – | **–** | – | – |
| Foreign currency exchange rate changes | **4** | (34) | – | **–** | – | – |
| Fair value of plan assets, end of period | **$ 2,838** | $ 2,842 | $ 2,671 | **$ –** | $ – | $ – |
| **Change in Defined Benefit Obligation** | | | | | | |
| Defined benefit obligation, beginning of period | **$ 2,779** | $ 2,438 | $ 2,438 | **$ 389** | $ 333 | $ 333 |
| Employer current service cost | **58** | 44 | – | **1** | 1 | – |
| Employee contributions | **16** | 16 | – | **–** | – | – |
| Interest on defined benefit obligation | **151** | 147 | – | **21** | 20 | – |
| Actuarial (gains) losses | **138** | 304 | – | **(4)** | 52 | – |
| Benefits paid | **(163)** | (129) | – | **(16)** | (17) | – |
| Past service cost | **1** | 5 | – | **–** | – | – |
| Settlements | **–** | (2) | – | **–** | – | – |
| Foreign currency exchange rate changes | **5** | (44) | – | **–** | – | – |
| Defined benefit obligation, end of period | **$ 2,985** | $ 2,779 | $ 2,438 | **$ 391** | $ 389 | $ 333 |
| **Asset (Liability) recognized in the Balance Sheets** | | | | | | |
| Funded status of plans – surplus (deficit) | **$ (147)** | $ 63 | $ 233 | **$ (391)** | $ (389) | $ (333) |
| Unrecognized past service costs (credits) | **5** | 5 | – | **(22)** | (28) | (34) |
| Net actuarial (gains) losses | **453** | 203 | – | **46** | 52 | – |
| Unrecognized amount due to limit on asset | **(71)** | (63) | (78) | **–** | – | – |
| Asset (liability) recognized in the Consolidated Balance Sheets | **$ 240** | $ 208 | $ 155 | **$ (367)** | $ (365) | $ (367) |
| Recorded in: | | | | | | |
| Other assets | **$ 420** | $ 302 | $ 248 | **$ –** | $ – | $ – |
| Other liabilities | **(180)** | (94) | (93) | **(367)** | (365) | (367) |
| Asset (liability) recognized in the Consolidated Balance Sheets | **$ 240** | $ 208 | $ 155 | **$ (367)** | $ (365) | $ (367) |
| **Analysis of defined benefit obligation** | | | | | | |
| Wholly or partly funded plans | **$ 2,821** | $ 2,622 | $ 2,306 | | | |
| Wholly unfunded plans | **$ 164** | $ 157 | $ 132 | **$ 391** | $ 389 | $ 333 |
| Actual return on plan assets | **$ 59** | $ 242 | | | | |

The Company expects to contribute $92 to its funded and unfunded defined benefit pension and other post-employment benefit plans in 2012.

23. Pension Plans and Other Post-Employment Benefits (cont'd)

### (b) Pension and Other Post-Employment Benefits Expense Recognized in Profit or Loss

| | All pension plans | | Other post-employment benefits | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Defined benefit current service cost | $ 74 | $ 60 | $ 1 | $ 1 |
| Defined contribution current service cost | 4 | 4 | – | – |
| Employee contributions | (16) | (16) | – | – |
| Employer current service cost | 62 | 48 | 1 | 1 |
| Past service costs recognized | 1 | – | (6) | (6) |
| Interest cost on defined benefit obligation | 151 | 147 | 21 | 20 |
| Actuarial (gain) loss recognized | (1) | 19 | 2 | – |
| Expected return on plan assets | (170) | (161) | – | – |
| Amount recognized due to limit on asset | 7 | (14) | – | – |
| Pension and other post-employment benefits expense recognized | $ 50 | $ 39 | $ 18 | $ 15 |

### (c) Asset Allocation by Major Category Weighted by Plan Assets

| | Defined benefit pension plans | | |
|---|---|---|---|
| | December 31 2011 | December 31 2010 | January 1 2010 |
| Equity securities | 45% | 49% | 48% |
| Debt securities | 41% | 37% | 38% |
| Real estate | 5% | 4% | 5% |
| Cash and cash equivalents | 9% | 10% | 9% |
| | 100% | 100% | 100% |

No plan assets are directly invested in the Company's or related parties' securities. Plan assets include investments in segregated funds managed by subsidiaries of the Company in the Consolidated Balance Sheets of $1,430 ($1,438 in 2010). Plan assets do not include any property occupied or other assets used by the Company.

### (d) Principal Actuarial Assumptions Used at the Balance Sheets Date

| | Defined benefit pension plans | | Other post-employment benefits | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| **To determine benefit cost:** | | | | |
| Discount rate | 5.5% | 6.1% | 5.5% | 6.3% |
| Expected rate of return on plan assets, during the year | 6.0% | 6.1% | – | – |
| Expected rate of compensation increase | 3.6% | 3.7% | – | – |
| Future pension increases | 2.2% | 2.4% | – | – |
| **To determine defined benefit obligation (DBO):** | | | | |
| Discount rate | 5.1% | 5.5% | 5.1% | 5.5% |
| Rate of compensation increase | 3.5% | 3.6% | – | – |
| Future pension increases | 2.0% | 2.2% | – | – |
| % of DBO subject to future pension increases | 46.0% | 47.0% | – | – |
| **Medical cost trend rates:** | | | | |
| Initial medical cost trend rate | | | 6.7% | 7.0% |
| Ultimate medical cost trend rate | | | 4.5% | 4.5% |
| Year ultimate trend rate is reached | | | 2024 | 2024 |

### (e) Impact of Changes to Assumed Medical Cost Trend Rates – Other Post-Employment Benefits

| | 1% increase | | 1% decrease | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Impact on defined benefit obligation | $ 40 | $ 39 | $ (33) | $ (33) |
| Impact on current service cost and interest cost | $ 2 | $ 2 | $ (2) | $ (2) |

### (f) Amounts for the current and previous annual periods are as follows:

| | 2011 | 2010 |
|---|---|---|
| ***Defined benefit pension plans:*** | | |
| Defined benefit obligation | $ (2,985) | $ (2,779) |
| Fair value of plan assets | 2,838 | 2,842 |
| Funded status of plans – surplus (deficit) | (147) | 63 |
| Experience adjustments on plan liabilities | (138) | (304) |
| Experience adjustments on plan assets | (111) | 81 |
| **Other post-employment benefits:** | | |
| Defined benefit obligation | (391) | (389) |
| Experience adjustments on plan liabilities | 4 | (52) |

## 24. Accumulated Other Comprehensive Income (Loss)

| | 2011 | | | | | |
|---|---|---|---|---|---|---|
| | Unrealized foreign exchange gains (losses) on translation of foreign operations | Unrealized gains (losses) on available for sale assets | Unrealized gains (losses) on cash flow hedges | Total | Participating account | Shareholder |
| Balance, beginning of year | $ (368) | $ 103 | $ 1 | $ (264) | $ 16 | $ (280) |
| Other comprehensive loss | 82 | 137 | – | 219 | 83 | 136 |
| Income tax | 1 | (29) | – | (28) | (22) | (6) |
| | 83 | 108 | – | 191 | 61 | 130 |
| Balance, end of year | $ (285) | $ 211 | $ 1 | $ (73) | $ 77 | $ (150) |

| | 2010 | | | | | |
|---|---|---|---|---|---|---|
| | Unrealized foreign exchange gains (losses) on translation of foreign operations | Unrealized gains (losses) on available for sale assets | Unrealized gains (losses) on cash flow hedges | Total | Participating account | Shareholder |
| Balance, beginning of year | $ – | $ 72 | $ 1 | $ 73 | $ 8 | $ 65 |
| Other comprehensive loss | (368) | 40 | – | (328) | 14 | (342) |
| Income tax | – | (9) | – | (9) | (6) | (3) |
| | (368) | 31 | – | (337) | 8 | (345) |
| Balance, end of year | $ (368) | $ 103 | $ 1 | $ (264) | $ 16 | $ (280) |

## 25. Related Party Transactions

### (a) Principal subsidiaries

The financial statements of the Company include the operations of the following subsidiaries:

| Company | Incorporated in | Primary business operation | % Held |
|---|---|---|---|
| GLC Asset Management Group Ltd. | Canada | Wealth management | 100.00% |
| GWL Realty Advisors Inc. | Canada | Real estate investment management | 100.00% |
| London Insurance Group Inc. | Canada | Insurance and wealth management | 100.00% |
| Canada Life Financial Corporation | Canada | Insurance and wealth management | 100.00% |

### (b) Transactions with related parties included in the consolidated financial statements

***Reinsurance Transactions***

During 2005, Great-West Life & Annuity Insurance Company of South Carolina (GWSC), an affiliated company, assumed on a coinsurance basis with funds withheld, certain of Canada Life's U.S. term life reinsurance business. During 2007, an additional amount of U.S. term life reinsurance business was retroceded by Canada Life to GWSC. In 2011, for the Consolidated Statements of Earnings, these transactions resulted in a reduction in premium income of $124 ($127 in 2010) and total paid or credited to policyholders of $176 ($103 in 2010). The transaction was at market terms and conditions.

***Other Related Party Transactions***

In the normal course of business, the Company provided insurance benefits to other companies within the Power Financial Corporation group of companies. In all cases, transactions were at market terms and conditions.

During 2011, the Company provided and received from IGM certain administrative services. The Company also provided life insurance, annuity and disability insurance products under a distribution agreement with IGM. London Life provided distribution services to IGM.

At December 31, 2011 the Company held $39 ($47 in 2010) of debentures issued by IGM.

| | 2011 | 2010 |
|---|---|---|
| 6.75%, matured May 9, 2011 | $ – | $ 10 |
| 6.65%, matures December 13, 2027 | 15 | 14 |
| 7.45%, matures May 9, 2031 | 12 | 12 |
| 7.00%, matures December 31, 2032 | 12 | 11 |
| | $ 39 | $ 47 |

During 2011, the Company and segregated funds maintained by the Company purchased residential mortgages of $202 from IGM ($226 in 2010).

During the year, GWL&A provided certain administrative services to the Company. The expense to the Company for these services was $5 ($5 in 2010).

The Company has 6.74% debentures due to Lifeco, its parent, which have an outstanding balance of $200 ($200 in 2010). Financing charges of $13 is included in the Consolidated Statements of Earnings ($13 in 2010).

In 2008, the Company issued $2.0 billion of 7.127% debentures to Lifeco. The Company made a corresponding investment of $2.0 billion in preferred shares of a wholly-owned subsidiary of Lifeco. The Company also issued $1.2 billion of 5.75% debentures to Lifeco in 2003. The Company made a corresponding investment of $1.2 billion in preferred shares of a wholly-owned subsidiary of Lifeco. The Company has legally enforceable rights to settle these financial instruments on a net basis, and the Company intends to exercise these rights. Accordingly the investments and debentures are offset in the consolidated financial statements of the Company.

**(c) Key management compensation**

Key management personnel constitutes those individuals who have the authority and responsibility for planning, directing and controlling the activities of Great-West Life, directly or indirectly, including any Director. The individuals who comprise the key management personnel are the Board of Directors as well as certain key management and officers.

The following table describes all compensation paid to, awarded to, or earned by each of the key management personnel in 2011 for services rendered in all capacities to the Company and its subsidiaries:

| | 2011 | 2010 |
|---|---|---|
| Salary | $ 10 | $ 10 |
| Share based awards | 2 | – |
| Option based awards | 1 | – |
| Annual non-equity incentive plan compensation | 5 | 6 |
| Pension value | 4 | 9 |
| | $ 22 | $ 25 |

## 26. Income Tax

(a) Income tax receivable (payable)

| | 2011 | 2010 |
|---|---|---|
| Balance, beginning of year | $ 142 | $ 359 |
| Current tax expense | (203) | (90) |
| Recorded in OCI | (28) | (10) |
| Payments made on account | (197) | (75) |
| Other | (21) | (42) |
| **Balance, end of year** | $ (307) | $ 142 |

(b) Deferred income taxes consist of the following losses carried forward and taxable temporary differences:

| | 2011 | 2010 |
|---|---|---|
| Insurance and investment contract liabilities | $ (119) | $ (232) |
| Portfolio assets | (525) | (435) |
| Losses carried forward | 97 | 105 |
| Intangible assets | (68) | (68) |
| Other | (150) | 28 |
| Net deferred income tax asset (liability) | $ (765) | $ (602) |
| Balance, beginning of year | $ (602) | $ (494) |
| Amounts recorded in: | | |
| Statements of net earnings | (140) | (95) |
| Statement of other comprehensive income | – | 1 |
| Insurance and investment contract liabilities | (17) | (29) |
| Foreign exchange rate changes | (6) | 15 |
| **Balance, end of year** | $ (765) | $ (602) |

A deferred tax asset is recognized for a tax loss carryforward only to the extent that realization of the related tax benefit through the future taxable profits is more likely than not.

26. Related Party Transactions (cont'd)

Recognition is based on the fact that it is more likely than not that the entity will have taxable profits and/or can utilize tax planning opportunities before expiration of the deferred tax assets. Changes in circumstances in future periods may adversely impact the assessment of the recoverability. The uncertainty of the recoverability is taken into account in establishing the deferred tax assets.

Management assesses the recoverability of the deferred tax asset carrying values based on future years taxable income and believes the carrying values of the deferred tax assets as of December 31, 2011 are recoverable.

At December 31, 2011, the Company had tax loss carryforwards, totaling $507 ($1,572 in 2010). Of this amount, $282 expire between 2011 and 2031, while $225 have no expiry date. The Company will realize this benefit in future years through a reduction in current income taxes payable.

A deferred tax liability has not been recognized in respect of the investment in subsidiaries, branches and associates as the Company is able to control the timing, which is not probable in the foreseeable future, of the reversal of the temporary difference.

**(c)** Income tax expense for the year comprises current and deferred tax:

(i) Current income tax

| | 2011 | 2010 |
|---|---|---|
| Current tax expense | $ 193 | $ 88 |
| Previously unrecognized tax loss; tax credit or temporary difference of prior period | 5 | (4) |
| Other | 5 | 6 |
| Total current income tax | $ 203 | $ 90 |

(ii) Deferred income tax

| | 2011 | 2010 |
|---|---|---|
| Origination and reversal of temporary difference | $ 165 | $ 72 |
| Changes in tax rates or imposition of new taxes | (7) | (4) |
| Write-down or reversal of previous write-down of deferred tax assets | 1 | 8 |
| Previously unrecognized tax loss; tax credit or temporary difference of prior period | (7) | (2) |
| Other | (12) | 21 |
| Total deferred income tax | $ 140 | $ 95 |
| **Total income tax expense** | $ 343 | $ 185 |

(iii) Tax recorded in other comprehensive income (see note 24)

| | 2011 | 2010 |
|---|---|---|
| Current tax | $ 28 | $ 10 |
| Deferred tax | – | (1) |
| | $ 28 | $ 9 |

**(d)** The Company's effective income tax rate is derived as follows:

| | 2011 | | 2010 | |
|---|---|---|---|---|
| Combined basic Canadian federal and provincial tax rate | $ 674 | 28.0% | $ 468 | 30.5% |
| Increase (decrease) in the income tax rate resulting from: | | | | |
| Non-taxable investment income | (188) | (7.8) | (175) | (11.4) |
| Lower effective income tax rates on income not subject to tax in Canada | (114) | (4.8) | (84) | (5.4) |
| Other | (22) | (0.9) | (20) | (1.3) |
| Impact of rate changes on future income taxes | (7) | (0.3) | (4) | (0.3) |
| Effective income tax rate applicable to current year | $ 343 | 14.2% | $ 185 | 12.1% |

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

## 27. Operating and Administrative Expenses

| | 2011 | 2010 |
|---|---|---|
| Salaries and other employee benefits | $ 987 | $ 933 |
| Amortization of fixed assets | 28 | 27 |
| Other | (96) | 858 |
| | $ 919 | $ 1,818 |

## 28. Derivative Financial Instruments

In the normal course of managing exposure to fluctuations in interest and foreign exchange rates, and to market risks, the Company is an end user of various derivative financial instruments. It is the Company's policy to transact in derivatives only with the most creditworthy financial intermediaries. Note 7 illustrates the credit quality of the Company's exposure to counterparties. As at December 31, 2011, the Company received assets of $10 ($16 in 2010) as collateral for derivative contracts from counterparties and pledged assets of $45 ($39 in 2010) as collateral for derivative contracts to counterparties.

**(a) The following table summarizes the Company's derivative portfolio and related credit exposure:**

| | 2011 | | | | |
|---|---|---|---|---|---|
| | Notional amount | Maximum credit risk* | Future credit exposure | Credit risk equivalent | Risk weighted equivalent |
| **Interest rate contracts** | | | | | |
| Swaps | $ 1,979 | $ 330 | $ 13 | $ 341 | $ 36 |
| Options purchased | 197 | 53 | 2 | 48 | 4 |
| | 2,176 | 383 | 15 | 389 | 40 |
| **Foreign exchange contracts** | | | | | |
| Forward contracts | 224 | – | 3 | 3 | – |
| Cross-currency swaps | 6,175 | 544 | 423 | 966 | 61 |
| | 6,399 | 544 | 426 | 969 | 61 |
| **Other derivative contracts** | | | | | |
| Equity contracts | 58 | – | 4 | 4 | – |
| Futures – long | 7 | – | – | – | – |
| Futures – short | 146 | – | – | – | – |
| | 211 | – | 4 | 4 | – |
| | $ 8,786 | $ 927 | $ 445 | $ 1,362 | $ 101 |

* Credit risk equivalent amounts are presented net of collateral received ($10).

28. Derivative Financial Instruments (cont'd)

| | 2010 | | | | |
|---|---|---|---|---|---|
| | Notional amount | Maximum credit risk* | Future credit exposure | Credit risk equivalent | Risk weighted equivalent |
| Interest rate contracts | | | | | |
| Futures – short | $ 18 | $ – | $ – | $ – | $ – |
| Swaps | 1,440 | 200 | 8 | 198 | 21 |
| Options purchased | 221 | 26 | 3 | 23 | 1 |
| | 1,679 | 226 | 11 | 221 | 22 |
| Foreign exchange contracts | | | | | |
| Forward contracts | 86 | 1 | 1 | 2 | – |
| Cross-currency swaps | 5,778 | 703 | 397 | 1,100 | 68 |
| | 5,864 | 704 | 398 | 1,102 | 68 |
| Other derivative contracts | | | | | |
| Equity contracts | 64 | – | 4 | 4 | – |
| Futures – long | 8 | – | – | – | – |
| Futures – short | 37 | – | – | – | – |
| | 109 | – | 4 | 4 | – |
| | $ 7,652 | $ 930 | $ 413 | $ 1,327 | $ 90 |

* Credit risk equivalent amounts are presented net of collateral received ($16).

The following has been disclosed in the tables above, as prescribed by OSFI:

| | |
|---|---|
| Maximum Credit Risk | The total replacement cost of all derivative contracts with positive values. |
| Future Credit Risk | The potential future credit exposure is calculated based on a formula prescribed by OSFI. The factors prescribed by OSFI for this calculation are based on derivative type and duration. |
| Credit Risk Equivalent | The sum of Maximum Credit Risk and the potential Future Credit Exposure less any collateral held. |
| Risk Weighted Equivalent | Represents the credit risk equivalent, weighted according to the creditworthiness of the counterparty, as prescribed by OSFI. |

**(b)** The following table provides the notional amount, term to maturity and estimated fair value of the Company's derivative portfolio by category:

| | 2011 | | | | |
|---|---|---|---|---|---|
| | Notional Amount | | | | Total estimated market value |
| | 1 year or less | 1–5 years | Over 5 years | Total | |
| **Interest rate contracts** | | | | | |
| Swaps | $ 404 | $ 992 | $ 564 | $ 1,960 | $ 312 |
| Options purchased | – | 95 | 102 | 197 | 53 |
| | 404 | 1,087 | 666 | 2,157 | 365 |
| **Foreign exchange contracts** | | | | | |
| Forward contracts | 224 | – | – | 224 | – |
| Cross-currency swaps | 43 | 1,509 | 4,623 | 6,175 | 307 |
| | 267 | 1,509 | 4,623 | 6,399 | 307 |
| **Other derivative contracts** | | | | | |
| Equity contracts | 40 | 18 | – | 58 | (17) |
| Futures – long | 7 | – | – | 7 | – |
| Futures – short | 146 | – | – | 146 | (1) |
| | 193 | 18 | – | 211 | (18) |
| | 864 | 2,614 | 5,289 | 8,767 | 654 |
| **Fair value hedges** | | | | | |
| **Interest rate contracts** | | | | | |
| Interest rate swaps | – | 10 | 9 | 19 | – |
| **Total** | $ 864 | $ 2,624 | $ 5,298 | $ 8,786 | $ 654 |

| | 2010 | | | | |
|---|---|---|---|---|---|
| | Notional Amount | | | | Total estimated market value |
| | 1 year or less | 1–5 years | Over 5 years | Total | |
| Interest rate contracts | | | | | |
| Futures – short | $ 6 | $ – | $ – | $ 6 | $ – |
| Swaps | 419 | 716 | 305 | 1,440 | 188 |
| Options purchased | – | – | 221 | 221 | 26 |
| | 425 | 716 | 526 | 1,667 | 214 |
| Foreign exchange contracts | | | | | |
| Forward contracts | 86 | – | – | 86 | – |
| Cross-currency swaps | 70 | 1,284 | 4,424 | 5,778 | 588 |
| | 156 | 1,284 | 4,424 | 5,864 | 588 |
| Other derivative contracts | | | | | |
| Equity contracts | 43 | 21 | – | 64 | (20) |
| Futures – long | 8 | – | – | 8 | – |
| Futures – short | 37 | – | – | 37 | – |
| | 88 | 21 | – | 109 | (20) |
| | 669 | 2,021 | 4,950 | 7,640 | 782 |
| Fair value hedges | | | | | |
| Interest rate contracts | | | | | |
| Futures – short | 12 | – | – | 12 | – |
| Total | $ 681 | $ 2,021 | $ 4,950 | $ 7,652 | $ 782 |

Futures contracts included in the above table are exchange traded contracts; all other contracts are over-the-counter.

(c) ***Interest Rate Contracts***

Interest rate swaps, futures and options are used as part of a portfolio of assets to manage interest rate risk associated with investment activities and insurance and investment contract liabilities. Interest rate swap agreements require the periodic exchange of payments without the exchange of the notional principal amount on which payments are based. Call options grant the Company the right to enter into a swap with predetermined fixed-rate payments over a predetermined time period on the exercise date. Call options are used to hedge minimum rate guarantees.

***Foreign Exchange Contracts***

Cross-currency swaps are used in combination with other investments to manage foreign currency risk associated with investment activities and insurance and investment contract liabilities. Under these swaps principal amounts and fixed or floating interest payments may be exchanged in different currencies. The Company also enters into certain foreign exchange forward contracts to hedge certain product liabilities.

***Other Derivative Contracts***

Equity index swaps, futures and options are used to hedge certain product liabilities. Equity index swaps are also used as substitutes for cash instruments and are used to periodically hedge the market risk associated with certain fee income. The Company may use credit derivatives to manage its credit exposures and for risk diversification in its investment portfolio.

## 29. Legal Provisions, Contingent Liabilities and Subsequent Event

The Company and its subsidiaries are from time to time subject to legal actions, including arbitrations and class actions, arising in the normal course of business. It is inherently difficult to predict the outcome of any of these proceedings with certainty, and it is possible that an adverse resolution could have a material adverse effect on the consolidated financial position of the Company. However, based on information presently known, it is not expected that any of the existing legal actions, either individually or in the aggregate, will have a material adverse effect on the consolidated financial position of the Company.

A subsidiary of the Company has declared a partial windup in respect of an Ontario defined benefit pension plan which will not likely be completed for some time. The partial windup could involve the distribution of the amount of actuarial surplus, if any, attributable to the wound up portion of the plans. In addition to the regulatory proceedings involving this partial windup, a related class action proceeding has been commenced in Ontario related to the partial windup and three potential partial windups under the plan. The class action also challenges the validity of charging expenses to the plan. The provisions for certain Canadian retirement plans in the amounts of $97 after-tax established by the Company's subsidiaries in the third quarter, 2007 have been reduced to $68. Actual results could differ from these estimates.

The Court of Appeal for Ontario released a decision on November 3, 2011 in regard to the involvement of the participating accounts of London Life and Great-West Life in the financing of the acquisition of LIG in 1997 (the "Appeal Decision").

The Appeal Decision made substantial adjustments to the original trial judgment (the "Trial Decision"). The impact is expected to be favourable to the Company's overall financial position. Any monies to be returned to the participating accounts will be dealt with in accordance with the companies' participating policyholder dividend policies in the ordinary course of business. No awards are to be paid out to individual class members.

During the fourth quarter of 2011, in response to the Appeal Decision, the Company re-evaluated and reduced the litigation provision established in the third quarter of 2010, which positively impacted common shareholder net earnings by $223 after-tax.

Regardless of the ultimate outcome of this case, all of the participating policy contract terms and conditions will continue to be honoured.

Based on information presently known, the Trial Decision, if affirmed on further appeal, is not expected to have a material adverse effect on the consolidated financial position of the Company.

The Company and a subsidiary of the Company have an investment in a USA based private equity partnership wherein a dispute arose over the terms of the partnership agreement. The Company acquired the investment in 2007 for purchase consideration of US$350. The dispute was resolved on January 10, 2012 and the Company has established a provision for $99 after-tax.

***Subsequent Event***

On January 3, 2012 the plaintiffs filed an application in the Supreme Court of Canada for leave to appeal the Appeal Decision.

## 30. Commitments

### (a) Syndicated Letters of Credit

Clients residing in the United States are required pursuant to their insurance laws to obtain letters of credit issued on LRG's behalf from approved banks in order to further secure LRG's obligations under certain reinsurance contracts.

LRG has a syndicated letter of credit facility providing US$650 in letters of credit capacity. The facility was arranged in 2010 for a five year term expiring November 12, 2015. Under the terms and conditions of the facility, collateralization may be required if a default under the letter of credit agreement occurs. LRG has issued US$479 in letters of credit under the facility as at December 31, 2011 (US$507 at December 31, 2010).

In addition, LRG has other bilateral letter of credit facilities totaling US$18 (US$18 in 2010). LRG has issued US$7 in letters of credit under these facilities as at December 31, 2011 (US$6 at December 31, 2010).

### (b) Other Letters of Credit

Canada Life issues letters of credit in the normal course of business. Letters of credit in the amount of $1 were outstanding at December 31, 2011 ($1 at December 31, 2010), none of which have been drawn upon at that date.

### (c) Lease Obligations

The Company enters into operating leases for office space and certain equipment used in the normal course of operations. Lease payments are charged to operations over the period of use. The future minimum lease payments in aggregate and by year are as follows:

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 and thereafter | Total |
|---|---|---|---|---|---|---|---|
| Future lease payments | $ 68 | 52 | 42 | 34 | 24 | 36 | $ 256 |

## 31. Segmented Information

The major reportable segments of the Company are the participating and shareholder operations. The Company operates through Great-West Life and its wholly owned subsidiaries LIG and CLFC. Within these segments the major business units are: Individual Insurance, Wealth Management, Group Insurance, Europe/Reinsurance, and Corporate. These business units reflect the Company's management structure and internal financial reporting. Each of these segments operates in the financial services industry and the revenues from these business units are derived principally from life, health and disability insurance, annuity products, and life, property and casualty, accident and health and annuity reinsurance. Business activities and operations that are not associated with the specific business units are attributed to Corporate.

### (a) Consolidated Net Earnings

| | 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Shareholder | | | | | | Participating | |
| | Individual insurance | Wealth management | Group insurance | Europe/ reinsurance | Corporate | Total | Total | Total company |
| **Income:** | | | | | | | | |
| Premium income | $ 1,128 | $ 1,091 | $ 4,521 | $ 4,718 | $ 55 | $ 11,513 | $ 2,660 | $ 14,173 |
| Net investment income | | | | | | | | |
| Regular net investment income | 277 | 572 | 291 | 1,758 | (9) | 2,889 | 1,463 | 4,352 |
| Changes in fair value through profit or loss | 831 | 394 | 186 | 1,840 | 128 | 3,379 | 416 | 3,795 |
| Total net investment income | 1,108 | 966 | 477 | 3,598 | 119 | 6,268 | 1,879 | 8,147 |
| Fee and other income | – | 905 | 147 | 583 | 39 | 1,674 | (1) | 1,673 |
| **Total income** | 2,236 | 2,962 | 5,145 | 8,899 | 213 | 19,455 | 4,538 | 23,993 |
| **Benefits and expenses:** | | | | | | | | |
| Paid or credited to policyholders | 1,532 | 2,001 | 3,824 | 7,515 | 148 | 15,020 | 3,942 | 18,962 |
| Other | 330 | 593 | 805 | 548 | (244) | 2,032 | 457 | 2,489 |
| Financing charges | – | – | – | 11 | 68 | 79 | – | 79 |
| Amortization of finite life intangible assets | 4 | 11 | 10 | 13 | 15 | 53 | 1 | 54 |
| **Earnings before income taxes** | 370 | 357 | 506 | 812 | 226 | 2,271 | 138 | 2,409 |
| Income taxes | 61 | 79 | 135 | 122 | (75) | 322 | 21 | 343 |
| **Net earnings** | 309 | 278 | 371 | 690 | 301 | 1,949 | 117 | 2,066 |
| Net earnings – participating policyholder | – | – | – | – | – | – | 117 | 117 |
| **Net earnings – common shareholder** | $ 309 | $ 278 | $ 371 | $ 690 | $ 301 | $ 1,949 | $ – | $ 1,949 |

31. Segmented Information (cont'd)

| | 2010 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Shareholder | | | | | | Participating | |
| | Individual insurance | Wealth management | Group insurance | Europe/ reinsurance | Corporate | Total | Total | Total company |
| Income: | | | | | | | | |
| Premium income | $ 1,069 | $ 1,497 | $ 4,327 | $ 5,141 | $ 63 | $ 12,097 | $ 2,453 | $ 14,550 |
| Net investment income | | | | | | | | |
| Regular net investment income | 224 | 650 | 278 | 1,793 | 149 | 3,094 | 1,417 | 4,511 |
| Changes in fair value through profit or loss | 419 | 248 | 111 | 1,464 | 61 | 2,303 | 894 | 3,197 |
| Total net investment income | 643 | 898 | 389 | 3,257 | 210 | 5,397 | 2,311 | 7,708 |
| Fee and other income | – | 851 | 144 | 549 | 31 | 1,575 | – | 1,575 |
| Total income | 1,712 | 3,246 | 4,860 | 8,947 | 304 | 19,069 | 4,764 | 23,833 |
| Benefits and expenses: | | | | | | | | |
| Paid or credited to policyholders | 990 | 2,197 | 3,538 | 7,717 | 180 | 14,622 | 4,240 | 18,862 |
| Other | 356 | 604 | 764 | 530 | 380 | 2,634 | 681 | 3,315 |
| Financing charges | – | – | – | 7 | 67 | 74 | – | 74 |
| Amortization of finite life intangible assets | 3 | 10 | 10 | 7 | 15 | 45 | 2 | 47 |
| Earnings before income taxes | 363 | 435 | 548 | 686 | (338) | 1,694 | (159) | 1,535 |
| Income taxes | 83 | 111 | 157 | 101 | (118) | 334 | (149) | 185 |
| Net earnings before non-controlling interests | 280 | 324 | 391 | 585 | (220) | 1,360 | (10) | 1,350 |
| Non-controlling interests | – | – | – | – | 7 | 7 | – | 7 |
| Net earnings | 280 | 324 | 391 | 585 | (227) | 1,353 | (10) | 1,343 |
| Net earnings – participating policyholder | – | – | – | – | – | – | (10) | (10) |
| Net earnings – shareholders | 280 | 324 | 391 | 585 | (227) | 1,353 | – | 1,353 |
| Preferred share dividends | – | – | – | – | 7 | 7 | – | 7 |
| Net earnings – common shareholder | $ 280 | $ 324 | $ 391 | $ 585 | $ (234) | $ 1,346 | $ – | $ 1,346 |

## (b) Consolidated Total Assets

| | December 31, 2011 | | |
|---|---|---|---|
| | Shareholder | Participating account | Total |
| **Assets** | | | |
| Invested assets | **$ 58,500** | **$ 31,125** | **$ 89,625** |
| Goodwill and intangible assets | **6,778** | **–** | **6,778** |
| Segregated funds for the risk of unitholders | **74,223** | **–** | **74,223** |
| Other assets | **17,692** | **624** | **18,316** |
| **Total assets** | **$ 157,193** | **$ 31,749** | **$ 188,942** |

| | December 31, 2010 | | |
|---|---|---|---|
| | Shareholder | Participating account | Total |
| Assets | | | |
| Invested assets | $ 53,358 | $ 29,619 | $ 82,977 |
| Goodwill and intangible assets | 6,782 | – | 6,782 |
| Segregated funds for the risk of unitholders | 73,638 | – | 73,638 |
| Other assets | 17,777 | 1,082 | 18,859 |
| Total assets | $ 151,555 | $ 30,701 | $ 182,256 |

| | January 1, 2010 | | |
|---|---|---|---|
| | Shareholder | Participating account | Total |
| Assets | | | |
| Invested assets | $ 52,034 | $ 27,511 | $ 79,545 |
| Goodwill and intangible assets | 6,808 | – | 6,808 |
| Segregated funds for the risk of unitholders | 67,805 | – | 67,805 |
| Other assets | 19,186 | 893 | 20,079 |
| Total assets | $ 145,833 | $ 28,404 | $ 174,237 |

## (c) Geographic Distribution of Total Assets and Income:

| | 2011 | | 2010 | |
|---|---|---|---|---|
| | **Income** | **Assets** | Income | Assets |
| Canada | **$ 14,556** | **$ 113,906** | $ 14,351 | $ 111,256 |
| International | **9,437** | **75,036** | 9,482 | 71,000 |
| **Total assets** | **$ 23,993** | **$ 188,942** | $ 23,833 | $ 182,256 |

## INDEPENDENT AUDITOR'S REPORT

**To the Policyholders and Shareholders,**
**The Great-West Life Assurance Company**

We have audited the accompanying consolidated financial statements of The Great-West Life Assurance Company, which comprise the consolidated balance sheets as at December 31, 2011, December 31, 2010 and January 1, 2010, and the consolidated statements of earnings, comprehensive income, changes in equity and cash flows for the years ended December 31, 2011 and December 31, 2010, and the notes to the financial statements.

*Management's Responsibility for the Consolidated Financial Statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated 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 consolidated financial statements present fairly, in all material respects, the financial position of The Great-West Life Assurance Company as at December 31, 2011, December 31, 2010 and January 1, 2010, and the results of its operations and its cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards.

Deloitte & Touche LLP

Chartered Accountants

Winnipeg, Manitoba
February 9, 2012

## APPOINTED ACTUARY'S REPORT

**To the Policyholders, Shareholders and Directors**
**of The Great-West Life Assurance Company**

I have valued the policy liabilities of The Great-West Life Assurance Company for its consolidated balance sheet at December 31, 2011 and their change in its summary of consolidated operations for the year then ended in accordance with accepted actuarial practice, including selection of appropriate assumptions and methods.

In my opinion, the amount of policy liabilities makes appropriate provision for all policyholder obligations and the consolidated financial statements fairly present the results of the valuation.

Tyrone G Faulds

**Tyrone Faulds**
Fellow, Canadian Institute of Actuaries

Winnipeg, Manitoba
February 9, 2012

## PARTICIPATING POLICYHOLDER DIVIDEND POLICY

This policyholder dividend policy has been established by the Board of Directors and applies to all participating insurance policies issued or assumed by Great-West. The Board of Directors may amend this policy from time to time at its discretion. The factors most likely to be considered in deciding whether to amend this policy include changes in applicable legal or regulatory requirements, professional guidelines, industry practices or significant business changes.

Earnings are generated in the participating account when the experience in the participating account for factors such as investment income, asset defaults, mortality, lapses, expenses and taxes is collectively more favourable than the assumptions for these factors used when establishing the guaranteed values associated with participating insurance policies. Great-West may distribute a portion of the earnings as declared at the discretion of the Board of Directors in accordance with this policy.

Participating insurance policies are eligible for periodic policyholder dividends. The amount to be distributed from the participating account as policyholder dividends is determined at least annually following a review of the actual and expected experience of the participating account, taking into account significant changes in factors such as investment income, asset defaults, mortality, lapses, expenses and taxes. The amount distributed in any year will vary up or down depending on the actual and expected experience. The amount distributed is also influenced by considerations such as the need to retain earnings as surplus and reducing short-term volatility in dividends.

The amount distributed as policyholder dividends is divided among classes of policies by setting the policyholder dividend scale. These dividend classes are groupings of participating policies with certain product and policy attributes in common.

Great-West follows the contribution principle when setting the policyholder dividend scale. This means the amount distributed as policyholder dividends is divided among dividend classes over the long term in proportion to their contribution to earnings. A contribution to earnings will be made from a particular dividend class to the extent the experience for that particular class is different from the assumptions used when establishing the guaranteed values for that class. When applying the contribution principle, attention is paid to achieving reasonable equity between dividend classes and between generations of policies, taking into account practical considerations and limits, legal and regulatory requirements, professional guidelines and industry practices. For certain blocks of policies, the policyholder dividend scale may be determined using methods designed to approximate the contribution to earnings of those blocks.

The policyholder dividends are credited according to the terms of each policy. A change made by a policyholder to a policy after it is issued may, in some cases, result in a change to the policy's dividend class and thus a change to the amount of policyholder dividends credited thereafter.

Termination dividends are not payable under any participating policies issued by Great-West.

Prior to the declaration of policyholder dividends by the Board, the Appointed Actuary reports to the Board of Directors with his opinion on the fairness to participating policyholders of the proposed policyholder dividends and on their compliance with this policy, applicable legislative and regulatory requirements and applicable professional practice standards. Policy illustrations will reflect changes to the policyholder dividend scale as soon as practical.

## PARTICIPATING ACCOUNT FINANCIAL DISCLOSURE

(in Canadian $ millions)

| Participating Account | Accounting Item | 2010 | 2011 |
|---|---|---|---|
| Canada | Opening surplus and accumulated other comprehensive income (OCI) | $ 442 | $ 461 |
| | Net earnings (including OCI) before distributions | 152 | 187 |
| | Amounts transferred to shareholders under section 461 of the ICA | 3 | 3 |
| | Other transfers or accruals under section 462 of the ICA | 0 | 1 |
| | Net earnings (including OCI) before payment of policyholder dividends | 148 | 183 |
| | Policyholder dividends distributed during the year | 129 | 134 |
| | Closing surplus and accumulated other comprehensive income (OCI) | 461 | 510 |
| | Total assets at year end | 3,583 | 3,693 |
| | Section 461 transfer as a % of total distributions | 2.5% | 2.5% |

# PARTICIPATING ACCOUNT MANAGEMENT POLICY

This participating account management policy has been established by the Board of Directors and may be amended by the Board from time to time at its discretion. The factors most likely to be considered in deciding whether to amend this policy include changes in applicable legal or regulatory requirements, professional guidelines, industry practices or significant business changes.

As required by the Insurance Companies Act, the Company maintains accounts for its participating insurance policies separately from those maintained in respect of other policies. This facilitates the measurement of the earnings attributable to the participating account.

The participating account is maintained in respect of participating life insurance policies and a small block of participating annuities that have been issued or assumed by the Company. The participating account remains open to new participating policies issued or assumed by the Company.

Assets of the Company held within its general funds are allocated to the participating account and non-participating account segments for the purpose of determining investment income for each account. Assets are allocated to each segment according to the investment guidelines established for the segments. These guidelines outline criteria for asset mix, liquidity, currency risk and interest rate risk. These guidelines are intended to recognize considerations such as the business objectives, liability characteristics, liquidity requirements, tax considerations and interest rate risk tolerance of each segment. Assets allocated to a segment may from time to time be reallocated to another segment within the same account or another account provided the assets exchanged comply with the investment policy of the respective segments. Any such exchanges are effected at fair value.

On an annual basis the Board of Directors reviews and approves investment policies and guidelines which govern investment activities. The investment policies outline a number of principles for investing in assets, including risk tolerance and the approach to managing investment risk. Investment risk is managed through underwriting standards, exposure limits and specific guidelines governing asset classes and investment operations. The investment policies establish limits for the concentration of assets in single geographic areas, industries, companies and types of businesses as part of the risk management process.

A large portion of the participating account assets are invested in fixed-income assets to support long-term stable growth and the core guarantees within participating policies. The Company employs cash-flow-matching techniques so that asset cash flows are sufficient to meet obligations and to help control exposure to interest rate fluctuations. In addition, a portion of the portfolio is reinvested each year so returns reflect the trend in interest rates. The Company may use derivative products as risk management instruments to hedge asset and liability positions, or as substitutes for cash instruments within specified guideline limits.

Investment income is allocated to the participating account in accordance with the Company's investment income allocation policy. Generally, investment income results are allocated directly to a segment based on the assets allocated to the segment. Each year the Appointed Actuary reviews the method used for allocating investment income to the participating account and reports to the Board of Directors on its fairness and equitableness.

Expenses and taxes incurred by the Company are allocated to the participating account in accordance with the Company's expense allocation and tax allocation policies.

In general, expenses that are exclusively related to participating business are allocated directly to the participating account. Expenses related to both participating and non-participating business are allocated based on business statistics when the expenses vary based on those statistics, based on managers' estimates supported by time studies or other assessments, or in proportion to the total expenses allocated using all of the methods previously mentioned.

From time to time, material non-recurring expenses may be incurred by the Company. Management will determine and report to the Appointed Actuary the allocation of any such expenses, including the basis or justification for it. The Appointed Actuary's approval is required for any allocation of such expenses to the participating account.

Taxes are allocated to the participating account using the characteristics of the participating and non-participating accounts that are determinative of the relevant tax costs.

Each year the Appointed Actuary reviews the method used for allocating expenses and taxes to the participating account and reports to the Board of Directors on its fairness and equitableness.

The participating account surplus is managed in accordance with the Company's capital management policy and participating account surplus policy and with regard to regulatory requirements. The surplus position is reviewed annually to assess its continuing appropriateness, having regard for the specific circumstances of the participating account. Surplus may be used for a number of purposes including to help ensure the Company can meet its obligations to participating policyholders, help ensure financial strength and stability, finance new business growth and acquisitions which may benefit the participating account, provide for transitions during periods of major change, and smooth the reflection of experience fluctuations in dividends; subject to items such as practical considerations and limits, legal and regulatory requirements, and industry practices.

As permitted by the Insurance Companies Act, the Company may distribute to the shareholder account a percentage of the amount distributed to policyholders in respect of a financial year. Prior to any such distribution, the Appointed Actuary will confirm to the Board of Directors that the proposed distribution is permitted under the terms of the Insurance Companies Act. The proportion distributed to the shareholder account will not exceed the prescribed amount as determined under section 461 of the Insurance Companies Act. Any distribution made to the shareholder account will be published in the Company's annual report.

## SOURCES OF EARNINGS

The following is provided in accordance with the OSFI guideline requiring Sources of Earnings (SOE) disclosure. SOE is not an International Financial Reporting Standards (IFRS) measure. There is no standard SOE methodology. The calculation of SOE is dependent on, and sensitive to, the methodology, estimates and assumptions used.

SOE identifies various sources of IFRS net earnings. It provides an analysis of the difference between actual net earnings and expected net earnings based on assumptions made at the beginning of the reporting period. The terminology used in the discussion of sources of earnings is described below:

**Expected Profit on In-Force Business**

This component represents the portion of the consolidated net income on business in-force at the start of the reporting period that was expected to be realized based on the achievement of the best-estimate assumptions. It includes releases of provisions for adverse deviations, expected net earnings on deposits, and expected net management fees.

**Impact of New Business**

This component represents the point-of-sale impact on net income of writing new business during the reporting period. This is the difference between the premium received and the sum of the expenses incurred as a result of the sale and the new liabilities established at the point of sale.

**Experience Gains and Losses**

This component represents gains and losses that are due to differences between the actual experience during the reporting period and the best-estimate assumptions at the start of the reporting period.

**Management Actions and Changes in Assumptions**

This component represents the impact on net income resulting from management actions, changes in actuarial assumptions or methodology, changes in margins for adverse deviations, and correction of errors.

**Other**

This component represents the amounts not included in any other line of the sources of earnings.

**Earnings on Surplus**

This component represents the earnings on the Company's surplus funds.

Great West Life's sources of earnings are shown below for 2011 and 2010.

### Sources of Earnings

(in Canadian $ millions)

| | Shareholder net earnings | | | | | |
|---|---|---|---|---|---|---|
| For the year ended December 31, 2011 | Group Insurance | Individual Insurance | Wealth Management | Europe/ Reinsurance | Corporate | Total |
| Expected profit on in-force business | $ 498 | $ 179 | $ 406 | $ 442 | $ 6 | $ 1,531 |
| Impact of new business | 0 | (47) | 48 | (9) | 0 | (8) |
| Experience gains and losses | (22) | 43 | (9) | (74) | (37) | (99) |
| Management actions and changes in assumptions | 30 | 195 | (88) | 276 | 13 | 426 |
| Other | 0 | 0 | 0 | 0 | 0 | 0 |
| Earnings on surplus | 0 | 0 | 0 | 177 | 102 | 279 |
| **Net earnings before tax** | 506 | 370 | 357 | 812 | 84 | 2,129 |
| Taxes | (135) | (61) | (79) | (122) | 93 | (304) |
| **Net earnings before non-controlling interests** | 371 | 309 | 278 | 690 | 177 | 1,825 |
| Non-controlling interests | 0 | 0 | 0 | 0 | 0 | 0 |
| **Net earnings – shareholders** | 371 | 309 | 278 | 690 | 177 | 1,825 |
| Preferred share dividends | 0 | 0 | 0 | 0 | 0 | 0 |
| **Net earnings – common shareholder before adjustments** | 371 | 309 | 278 | 690 | 177 | 1,825 |
| Adjustments after tax | 0 | 0 | 0 | 0 | 124 | 124 |
| **Net earnings – common shareholder** | $ 371 | $ 309 | $ 278 | $ 690 | $ 301 | $ 1,949 |

### Sources of Earnings

(in Canadian $ millions)

| For the year ended December 31, 2010 | Shareholder net earnings: Group Insurance | Individual Insurance | Wealth Management | Europe/ Reinsurance | Corporate | Total |
|---|---|---|---|---|---|---|
| Expected profit on in-force business | $ 495 | $ 176 | $ 365 | $ 470 | $ 27 | $ 1,533 |
| Impact of new business | 0 | (33) | 38 | (14) | 0 | (9) |
| Experience gains and losses | (22) | 69 | 5 | (61) | (47) | (56) |
| Management actions and changes in assumptions | 75 | 151 | 27 | 129 | 8 | 390 |
| Other | 0 | 0 | 0 | 0 | 0 | 0 |
| Earnings on surplus | 0 | 0 | 0 | 162 | 34 | 196 |
| Net earnings before tax | 548 | 363 | 435 | 686 | 22 | 2,054 |
| Taxes | (157) | (83) | (111) | (101) | 47 | (405) |
| Net earnings before non-controlling interests | 391 | 280 | 324 | 585 | 69 | 1,649 |
| Non-controlling interests | 0 | 0 | 0 | 0 | (7) | (7) |
| Net earnings – shareholders | 391 | 280 | 324 | 585 | 62 | 1,642 |
| Preferred share dividends | 0 | 0 | 0 | 0 | (7) | (7) |
| Net earnings – common shareholder before adjustments | 391 | 280 | 324 | 585 | 55 | 1,635 |
| Adjustments after tax | 0 | 0 | 0 | 0 | (289) | (289) |
| Net earnings – common shareholder | $ 391 | $ 280 | $ 324 | $ 585 | $ (234) | $ 1,346 |

**Analysis of Results**

Expected profit on in-force business is the major driver of earnings and accounted for 72% of pre-tax earnings in 2011. The expected profit on in-force business of $1,531 in 2011 was $2 lower than the 2010 level.

New business issued in 2011 led to losses of $8 at issue compared to losses of $9 in 2010, largely due to reduced strain on retirement products in Canada and new business in Reinsurance largely offset by increased strain on insurance sales in Canada.

Experience losses in 2011 were primarily due to unfavourable expense, morbidity and policyholder behaviour experience in Europe, policyholder behavior and Group morbidity experience in Canada offset by favourable investment experience. Experience losses in 2010 were primarily due to unfavourable investment and expense experience in Europe, policyholder behavior and Group morbidity experience in Canada and reinsurance claim provisions. Experience losses of $(99) in 2011 were $43 lower than in 2010 primarily due to unfavourable morbidity, policyholder behavior and expense experience partially offset by favourable investment experience.

In 2011 the Company adopted the revised Actuarial Standards of Practice for subsection 2350 relating to the future mortality improvement in insurance contract liabilities for life insurance and annuities. The resulting increase to earnings was $331 for life insurance and $3 for annuities.

Other management actions and changes in assumptions contributed $92 to pre-tax earnings. The most significant contributors to assumption changes and management actions were $141 due to model refinements across the Canadian segment, $132 due to updated expenses and taxes, $86 due to updated morbidity assumptions, $30 due to updated base life insurance mortality, $9 due to reinsurance related management actions, $(213) due to increased provisions for policyholder behavior in Individual insurance, and $(88) due to increased provisions for asset liability matching.

In 2010 management actions and changes in assumptions contributed $390 to pre-tax earnings, including $(3) due to the shareholder portion of assumption changes in the participating lines and $395 due to assumption changes and management actions for insurance contract liabilities. The most significant contributors to assumption changes and management actions were $168 due to reduced provisions for asset liability management, $111 due to model refinements, $110 due to updated expenses and taxes, $57 improved life mortality, $48 due to improved group insurance morbidity, $(76) due to increased provisions for policyholder behaviour, $(18) due to strengthened longevity, and $(8) due to strengthened provisions for asset default.

Pre-tax earnings on surplus increased by $83 in 2011 compared to 2010.

## SUBSIDIARIES OF THE GREAT-WEST LIFE ASSURANCE COMPANY*

| Name | Principal Office Address | Carrying Value ($ millions) | Voting Share Ownership |
|---|---|---|---|
| GLC Asset Management Group Ltd. | Winnipeg, Manitoba | 29 | 100.0% |
| GWL Realty Advisors Inc. | Winnipeg, Manitoba | – | 100.0% |
| London Insurance Group Inc. | London, Ontario | 3,779 | 100.0% |
| Canada Life Financial Corporation | Toronto, Ontario | 12,728 | 100.0% |

* The table above depicts the material and certain other subsidiaries of the Company as at December 31, 2011.

# FIVE YEAR SUMMARY

| (in Canadian $ millions except per share amounts) | 2011 | 2010 | *2009 | *2008 | *2007 |
|---|---|---|---|---|---|
| **At December 31** | | | | | |
| Total assets under administration | $ 203,820 | $ 197,290 | $ 182,715 | $ 173,184 | $ 179,756 |
| **For the Year Ended December 31** | | | | | |
| Premiums and deposits: | | | | | |
| Life insurance, guaranteed annuities and insured health products | $ 14,173 | $ 14,550 | $ 15,085 | $ 27,425 | $ 19,221 |
| Self-funded premium equivalents (ASO contracts) | 2,645 | 2,575 | 2,499 | 2,410 | 2,233 |
| Segregated funds deposits: | | | | | |
| Individual products | 7,146 | 6,643 | 5,765 | 6,932 | 8,544 |
| Group products | 3,615 | 3,744 | 4,231 | 3,321 | 3,311 |
| Proprietary mutual funds deposits | 724 | 616 | 565 | 708 | 835 |
| Total premiums and deposits | $ 28,303 | $ 28,128 | $ 28,145 | $ 40,796 | $ 34,144 |
| **Condensed Summary of Operations** | | | | | |
| **Income** | | | | | |
| Premium income | $ 14,173 | $ 14,550 | $ 15,085 | $ 27,425 | $ 19,221 |
| Net investment income | | | | | |
| Regular net investment income | 4,352 | 4,511 | 4,807 | 4,802 | 4,321 |
| Changes in fair value through profit or loss | 3,795 | 3,197 | 2,637 | (4,056) | (1,015) |
| Total net investment income | 8,147 | 7,708 | 7,444 | 746 | 3,306 |
| Fee and other income | 1,673 | 1,575 | 1,599 | 1,685 | 1,705 |
| Total income | 23,993 | 23,833 | 24,128 | 29,856 | 24,232 |
| **Benefits and expenses** | | | | | |
| Paid or credited to policyholders | 18,962 | 18,862 | 19,226 | 24,461 | 18,982 |
| Other | 2,568 | 3,389 | 2,800 | 2,851 | 2,999 |
| Amortization of finite life intangible assets | 54 | 47 | 38 | 32 | 18 |
| **Earnings before income taxes** | 2,409 | 1,535 | 2,064 | 2,512 | 2,233 |
| Income taxes | 343 | 185 | 289 | 543 | 450 |
| **Net earnings before non-controlling interests** | 2,066 | 1,350 | 1,775 | 1,969 | 1,783 |
| Non-controlling interests | – | 7 | 7 | 7 | 7 |
| **Net earnings** | 2,066 | 1,343 | 1,768 | 1,962 | 1,776 |
| Net earnings (loss) – participating account | 117 | (10) | 24 | 59 | 129 |
| **Net earnings – shareholders** | 1,949 | 1,353 | 1,744 | 1,903 | 1,647 |
| Preferred share dividends | – | 7 | 9 | 9 | 11 |
| **Net earnings – common shareholder** | $ 1,949 | $ 1,346 | $ 1,735 | $ 1,894 | $ 1,636 |
| **Earnings per common share** | $ 920.47 | $ 642.94 | $ 830.46 | $ 906.69 | $ 783.48 |
| **Book value per common share** | $5,627.00 | $ 5,184.00 | $ 5,320.00 | $ 5,350.00 | $ 4,889.00 |
| **Dividends to common shareholder – per share** | $ 540.46 | $ 415.44 | $ 613.78 | $ 465.83 | $ 412.26 |

* The years 2007, 2008 and 2009 are presented on a previous CGAAP basis.

# DIRECTORS AND OFFICERS

As of January 1, 2012

## BOARD OF DIRECTORS

**Raymond L. McFeetors** [3, 4, 5, 6]
Chairman of the Board of the Company
Vice-Chairman,
Power Financial Corporation

**George S. Bain** [1]
Corporate Director

**Marcel R. Coutu** [3, 4, 5, 6]
President and Chief Executive Officer,
Canadian Oil Sands Limited

**André Desmarais, O.C., O.Q.** [3, 4, 5, 6]
Deputy Chairman, President and
Co-Chief Executive Officer,
Power Corporation of Canada
Co-Chairman,
Power Financial Corporation

**Paul Desmarais, Jr., O.C., O.Q.** [3, 4, 5, 6]
Chairman and Co-Chief Executive Officer,
Power Corporation of Canada
Co-Chairman,
Power Financial Corporation

**H. David Graves** [3, 4, 5]
Chairman and Chief Executive Officer,
IMRIS Inc.

**Michael L. Hepher** [1, 5]
Corporate Director

**Chaviva M. Hošek, O.C., Ph.D., LL.D.** [1, 2]
President and Chief Executive Officer,
The Canadian Institute for Advanced Research

**D. Allen Loney, FIA, FCIA** [3, 4]
President and Chief Executive Officer
of the Company,
Great-West Lifeco Inc.,
London Life Insurance Company,
Canada Life Financial Corporation,
The Canada Life Assurance Company,
Crown Life Insurance Company

**Jerry E.A. Nickerson** [1]
Chairman of the Board,
H.B. Nickerson & Sons Limited

**David A. Nield** [2, 3, 4, 5, 6]
Corporate Director

**R. Jeffrey Orr** [3, 4, 5, 6]
President and Chief Executive Officer,
Power Financial Corporation

**Michel Plessis-Bélair, FCA** [1]
Vice-Chairman,
Power Corporation of Canada

**Henri-Paul Rousseau, Ph.D.** [3, 4]
Vice-Chairman,
Power Corporation of Canada and
Power Financial Corporation

**Raymond Royer, O.C., O.Q., FCA** [1]
Corporate Director

**Philip K. Ryan** [1, 3, 4]
Executive Vice-President and
Chief Financial Officer,
Power Corporation of Canada and
Power Financial Corporation

**T. Timothy Ryan, Jr.** [3, 4, 5]
President and Chief Executive Officer,
Securities Industry and Financial
Markets Association

**Emőke J.E. Szathmáry, C.M., O.M., Ph.D., FRSC** [2, 3]
President Emeritus,
University of Manitoba

**Brian E. Walsh** [5, 6]
Chairman and Chief Investment Officer,
Saguenay Strathmore Capital, LLC

1 member of the Audit Committee
2 member of the Conduct Review Committee
3 member of the Executive Committee
4 member of the Investment Committee
5 member of the Compensation Committee
6 member of the Governance and Nominating Committee

## EXECUTIVE OFFICERS

**D. Allen Loney**
President and Chief Executive Officer

**Arshil Jamal**
President and Chief Operating Officer,
Europe

**Paul A. Mahon**
President and Chief Operating Officer,
Canada

**Brian R. Allison**
Executive Vice-President and
Chief Investment Officer

**Andrew D. Brands**
Senior Vice-President and
General Counsel

**Elwood C. Haas**
Senior Vice-President,
Corporate Resources

**Helen R. Kasdorf**
Senior Vice-President
and Chief Internal Auditor

**William W. Lovatt**
Executive Vice-President and
Chief Financial Officer

**Garry MacNicholas**
Senior Vice-President and
Chief Actuary

**Ronald D. Saull**
Executive Vice-President,
Chief Information Officer

**Laurie A. Speers**
Vice-President and
Corporate Secretary

# POLICYHOLDER AND SHAREHOLDER INFORMATION

### Head Office

100 Osborne Street North, Winnipeg, Manitoba, Canada R3C 1V3

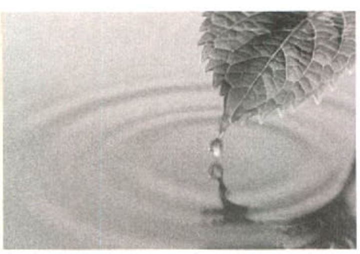
### Financial Information

For financial information about Great-West Life, please contact the Senior Vice-President and Chief Financial Officer, Canada at 204-946-8396.

For copies of the annual or quarterly reports, please contact the Corporate Secretary's Office at 204-946-4388 or visit **www.greatwestlife.com**.

THE
Great-West Life
ASSURANCE COMPANY

A MEMBER OF THE POWER FINANCIAL CORPORATION GROUP OF COMPANIES™



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