

2005 Annual Report



THE PUBLIC SECTOR
PENSION INVESTMENT
BOARD



CORPORATE PROFILE

The Public Sector Pension Investment Board (PSP Investments) is a Crown corporation established to invest in capital markets the net contributions received after April 1, 2000 from the pension plans of the Federal Public Service, Canadian Forces and Royal Canadian Mounted Police. PSP Investments operates at arm's length from the federal government. Its statutory objectives are to manage the funds entrusted to it in the best interests of the contributors and beneficiaries of the Plans and to maximize investment returns without undue risk of loss.

Highlights – Fiscal Year 2005

- Consolidated net assets increase 36% to \$19.4 billion
- Total portfolio return is 7.9%, compared to Policy Benchmark of 7.2%
- Policy Portfolio asset mix revised following strategic review
- Investments in additional new asset classes initiated
- New active-management policy and value-added activities implemented
- Robust Human Resources Policy put in place
- Team building continues-number of employees increases from 35 to 75

Contents

Annual Objectives	1
Chairperson's Report	2
President's Report	6
Fiscal Year 2005 Results	10
Investment Policy and Strategy	14
Governance	18
Glossary	23
Financial Statements and Notes	25
Board of Directors / Corporate Directory	67

ANNUAL OBJECTIVES

The legislation governing PSP Investments requires the annual report to include its objectives for the fiscal year under review, indicating to what extent they were met, and to state its objectives for the new fiscal year. This information is summarized below.

Fiscal Year 2005 Objectives	Status*
• Implement changes to the Policy Portfolio following strategic review	√
• Complete extensive review of value-added activities and implement changes	√
• Ensure that operations can support these new activities	√
• Implement a strong human-resources process to support the growth of PSP Investments	√

* √ indicates objective was substantially or completely achieved

Key Objectives for Fiscal Year 2006

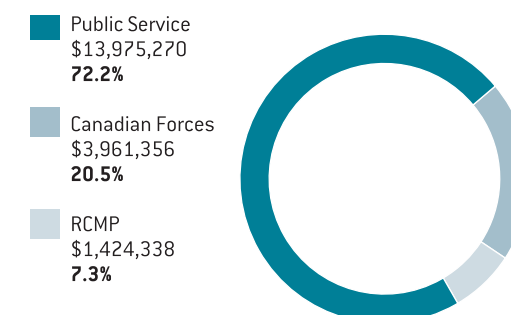
- Continue implementing investments in real estate, private equity and other new asset classes
- Further increase the level of active risk, within the authorized ceiling, in order to increase the level of returns
- Develop enhanced capabilities to manage private transactions
- Further strengthen infrastructure and support staff to keep pace with rapid growth of investment activities

Plan Accounts' Net Assets

(as of March 31, 2005)

(\$,000)

% of total net assets



Responding to a changing global investment climate

PSP Investments' response to a rapidly changing global economic and investment climate was reflected by the Board's adoption of a new vision statement and authorization of investments in a broader range of asset classes during fiscal 2005.

Objectives can and do change, as often as yearly. Strategies too are subject to periodic review and revision. But a vision should be more enduring. It should be a beacon that the organization can look to as it reviews its options and charts an appropriate course through a constantly evolving investment environment at home and abroad.

To that end, PSP Investments developed a vision statement that effectively bridges our legislative mandate and its strategy and objectives. The vision statement reads as follows:

We stand for superior investment performance aligned with our pension plans' financial obligations, and will look for it everywhere while upholding the highest ethical and professional standards.

Until now, we have invested primarily in stocks and bonds. But these are just parts of a much broader spectrum of opportunities available to us today. As you will see from the President's Report, PSP Investments already is moving forward with a considerably wider range of investments in real estate and private equity. Further down the road, we will be looking at still more asset classes, including infrastructure and natural resources/commodities. Moreover, we are increasingly seeking out investment opportunities in the broader global marketplace. As the vision statement implies, we are committed to exploring all appropriate avenues that will lead to superior investment performance.

Investments do not take place in a vacuum. So in addition to broadening our investment horizons, it is important to consider the major forces that are likely to impact the environment in which we invest.

One such force is the changing regulatory framework. For example, income trusts have emerged as major investment vehicles in Canada and recent legislative initiatives would protect investors from the risk of unlimited liability that made pension and mutual funds leery of these trusts. Now we can ask ourselves if income trusts offer good investment potential for us and act accordingly. In a similar vein, the federal government's proposal to set aside the 30% limit on foreign pension and retirement investments will allow PSP Investments to increase its direct exposure to non-Canadian opportunities.

We also need to consider our investments in the context of worldwide economic and market forces. Among them is the emergence of China and India as economic superpowers. With their enormous populations and rapidly expanding economies, these Asian giants have become low-cost venues of choice for the manufacturing of a wide range of consumer and industrial products, with voracious appetites for energy and raw materials. What will this mean for the global economy going forward—and how ought we to adjust PSP Investments' asset mix and geographic mix to take the anticipated impact into account?

As well, we must weigh opportunities abroad against economic and investment prospects closer to home, which carry their own measure of uncertainty. For instance, very sizeable trade and budgetary deficits in the United States—dominant partner in the North American Free Trade Agreement (NAFTA)—are the subject of increased scrutiny. Coupled with on-going security concerns and the NAFTA partners' differing policies on the Kyoto Accord, we see the makings of an unsettled investment environment. Of course, as investors we are not called on to formulate government policy on these issues. But we do have to make assessments of the potential impact of these various forces and factor those assessments into our investment decisions.

Complex though it may be, there is no doubt that today's global investment marketplace—characterized by increased investment options, a wealth of information sources and highly specialized expertise—offers attractive opportunities for sophisticated participants. However, we are conscious as well that seizing opportunities inevitably means taking risks. Accordingly, we are working diligently to build our risk-management skills as we build our portfolios, to ensure that PSP is, in fact, positioned among those sophisticated investors with the specialized expertise appropriate for today's market realities.

A governance role model

In keeping with the practice introduced during fiscal 2004, fellow Board members once again conducted their annual review of my performance as Board Chair. During fiscal 2006, we will institute a process of peer review for each Board member. Other governance-related undertakings during the course of the latest fiscal year included a review of our Human Resources Policy and the continuation of education and training sessions designed to ensure that Board members are kept up to date on relevant governance and investment issues. As well, the initial phase of the Special Examination of systems and practices was completed, in accordance with the legislation governing PSP Investments.

From the very outset, PSP Investments has been committed to best practices in corporate governance. So I am pleased to observe that our organization is serving as a model for some of the new rules being implemented by Ottawa for the governance of Crown corporations, such as the process whereby our CEO is selected and hired by the Board rather than through political appointment; as well as the arm's-length process used to identify qualified director candidates.

Proposed changes would alter framework

That being said, however, there is cause for concern about how proposed amendments to the *Public Sector Pension Investment Board Act* and the *Financial Administration Act*—as well as the government's stated intent to make PSP Investments subject to the *Access to Information Act* and the recently tabled *Conflict of Interest and Post-employment Code for Public Office Holders*—will alter the framework under which PSP Investments was established.

- Bill C-43 contains a proposed amendment to both the *Financial Administration Act* and the *Public Sector Pension Investment Board Act*. If Bill C-43 is adopted in its current form, the Governor in Council would be required to appoint the Auditor General of Canada as the auditor for PSP Investments, unless the Auditor General waives this requirement. Furthermore, the revised legislation would require that the Auditors' Reports on the financial statements of PSP Investments be submitted directly to the respective responsible Ministers. Currently, the Board of Directors appoints the external auditors and the Auditors' Reports are submitted to the Board of Directors, which forwards them to the Ministers.



Paul Cantor
Chairperson

- Currently, PSP Investments is not subject to the *Access to Information Act*. As part of the new rules relating to the governance of Crown corporations, it is the intention of the government to make PSP Investments subject to the *Access to Information Act* going forward. However, to ensure that vital commercial relationships with external investment managers are not compromised, the government is also formulating exemptions for PSP Investments from certain provisions of the *Access to Information Act*.
- Currently, directors are subject to PSP Investments' Conflict of Interest Policy. The recently tabled *Conflict of Interest and Post-employment Code for Public Office Holders* states that directors who are public office holders are required to arrange their private affairs in a manner that will prevent any actual or perceived conflict of interest even if permitted by law.

These changes may enhance transparency. At the same time, we believe that they will result in increased marketplace challenges.

Enhanced liaison with plan representatives

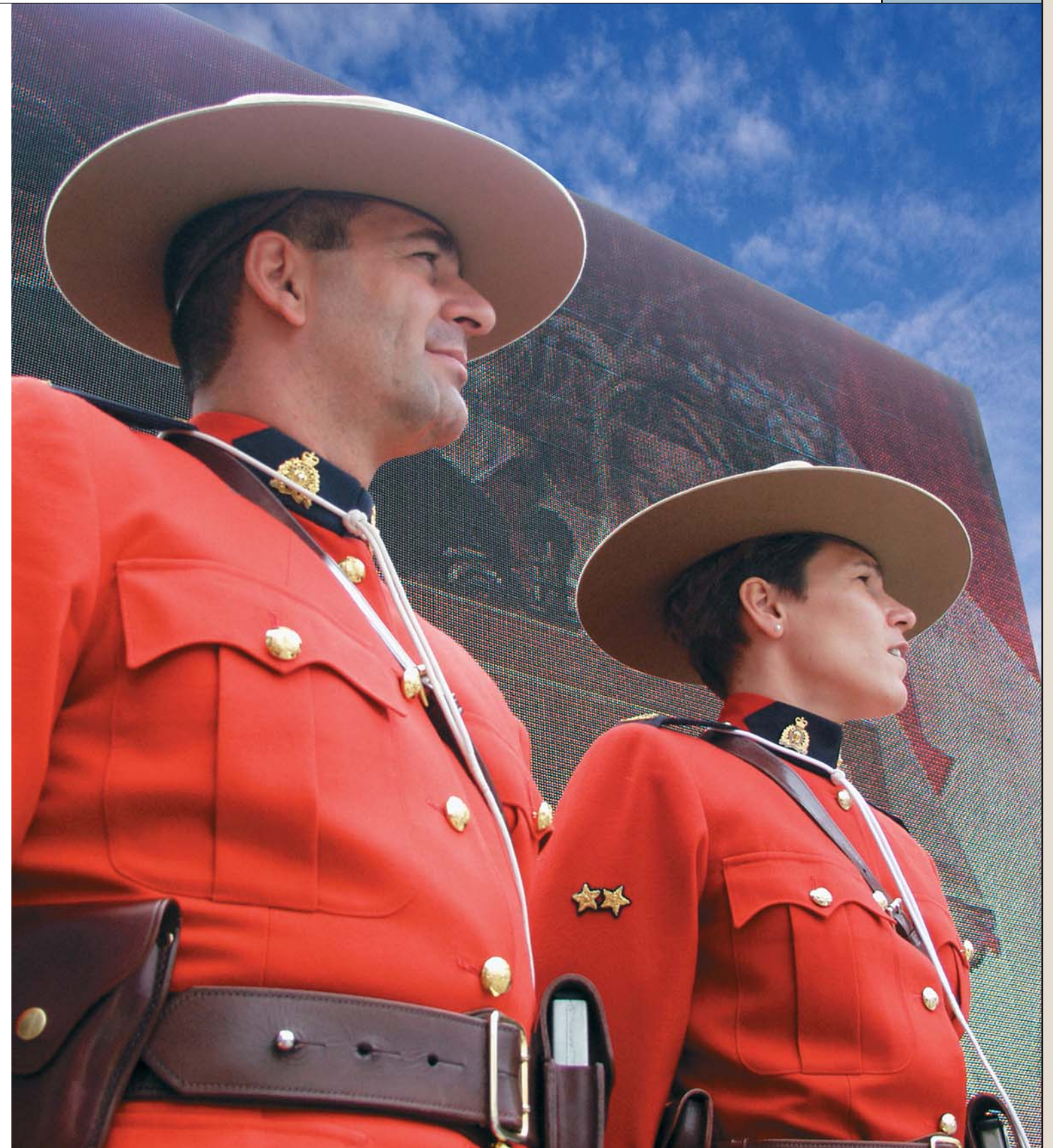
In October 2004, President Gordon Fyfe and I met with representatives of the three pension plans to review events of the previous year and outline our plans and objectives for fiscal year 2006. In addition to this annual review, plan representatives have been invited to attend an off-site conference with Board members and the senior management team, scheduled for June 2005, where they will have an opportunity to participate in in-depth discussions of PSP Investments' affairs.

Acknowledgements

I would like to take this opportunity to congratulate Gordon and his colleagues for their achievements over the past year and to thank my fellow Board members for their counsel and support. We welcome Anil K. Rastogi, who joined our Board in October 2004. A seasoned executive, Mr. Rastogi is Chief Information Officer of McCain Foods Ltd. and brings to our boardroom a wealth of expertise in operations.



Paul Cantor
Chairperson



PRESIDENT'S REPORT

I am pleased to report that we made good on the commitments set out in last year's annual report: revisions to the Policy Portfolio asset mix, stemming from a strategic review, were initiated; we completed an analysis of value-added activities and introduced changes designed to enhance our performance in that regard; we strengthened our risk-management and operational capabilities; and we put in place a robust human-resources process. As well, we continued to build our team.

Focused on diversification and team building

To put the initiatives of the past year in perspective, consider that the mandate of PSP Investments is to (a) generate solid returns; and (b) develop the capabilities to effectively manage future growth and increased diversification of assets. I believe we made excellent progress on both those fronts.

People are the key assets in the management of money. Accordingly, my top priority as CEO in fiscal year 2005 was to continue building a strong team that has the depth and specialized expertise required to manage an expanding, increasingly diversified pool of assets within a growing organization. Noteworthy initiatives in that regard included the establishment of specialized units to manage our investments in real estate and private equity; assembly of an internal team for index and quantitative investments; creation of a department to oversee external, public-market investment managers; and initiation of a comprehensive risk-management process.

As I indicated above, we undertook a reorganization of the underlying Policy Portfolio during fiscal year 2005, allocating more funds to less-liquid asset classes such as private equity, small-cap equities and emerging markets. The changes are designed to enhance long-term returns by taking advantage of PSP Investments' unique liquidity, which is driven by net inflows of well over \$3 billion a year in contributions. This exceptional level of liquidity provides us with a competitive advantage vis-à-vis other investors in capturing the return premiums offered on less-liquid investments.

Changes to the Policy Portfolio authorized by the Board of Directors in August 2004 included a reduction in the targeted allocation of assets to large-cap equities from approximately 65% to 43%—including 30% in Canadian equities, 5% in U.S. large-cap equities and 8% in international developed equities. The Board also authorized the targeted allocation of 5% of assets to U.S. small-cap equities, 7% to emerging-markets equities and 8% to private equity. The targeted allocation to debt has been reduced from 31.5% to 20%.

Other changes included approval of increased exposure to inflation-sensitive asset classes, in order to protect the portfolio against the prospect of higher inflation in the future. To that end, 10% has been allocated to real estate and 5% to "real-return" bonds whose value, contrary to ordinary bonds, rise with inflation.

By fiscal year-end, approximately \$800 million had been committed to real estate—most of it to be invested directly by PSP Investments. The initial real-estate portfolio includes residential and commercial assets in Canada, the United States, Europe and Asia.

PRESIDENT'S REPORT

Our Private Equity team has so far committed approximately \$30 million to external managers and we expect to commit up to \$3 billion during fiscal 2006. Going forward, we intend to continue building the relationships and capabilities that will enable us to invest—directly and indirectly—in additional private-equity situations, as appropriate opportunities arise. Investments in private equity typically entail an eight-to-10-year cycle, with negative returns early on and positive returns harvested during the latter part of the cycle.

To complement our wider diversification, we also have been working to increase the proportion of assets that are actively managed in order to add more incremental value on top of the Policy Portfolio return. With that aim in mind, we issued more investment mandates over the course of the year, both externally and internally, while terminating some under-performing managers. As well, we are utilizing a broader spectrum of active management strategies, including instruments related to foreign exchange. These activities generated 0.7% in added value for PSP Investments during the fiscal year. Over all, the Consolidated Pension Plan Account produced a rate of return of 7.9% for the year.

At this writing, PSP Investments still is approximately 95% invested in public equities and bond markets. The goal over time is to see that proportion continue to decline as we further diversify our mix of investments in asset classes that play to PSP Investments' strengths in terms of size, growth and liquidity. In the future, we will be looking at other inflation-sensitive equity classes, such as natural resources/commodities—including timber—and infrastructure. On the non-equity side, we will give consideration to investing in certain less-liquid debt markets, such as mortgages, to increase returns in the portfolio.

However, public markets will continue to comprise 80%-90% of assets and account for virtually all of PSP Investments' returns over the next 12 months. The initial impact of the changes I have outlined will only be felt in fiscal 2007, when alternate asset classes, including real estate, begin to contribute meaningfully.

Turning to other areas of the organization, we significantly increased the number of employees in operations and support roles in fiscal 2005, building specialized Legal and Human Resources functions while strengthening our Finance and Information Technology teams. The head count at year's end reached 75, compared with 35 a year earlier.

The remuneration system for our investment personnel has been restructured. The annual incentive-compensation plan for investment-management professionals and the deferred incentive-compensation plan for key executives were both revised to ensure that the interests of management are closely aligned with those of PSP Investments' stakeholders. The plans are designed to reward participants for the achievement of superior investment performance and to ensure that we remain competitive in terms of being able to attract high-calibre employees. I should note, too, that our expanded Human Resources team currently is undertaking an enhancement of the performance-evaluation process for employees.



Gordon J. Fyfe
President and Chief
Executive Officer

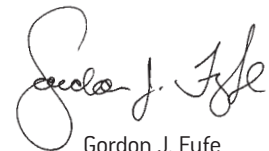
Priorities for fiscal year 2006

Looking ahead to priorities for fiscal year 2006, we will of course be proceeding with the implementation of investments in real estate, private equity and other new asset classes. We also will be gearing up the organization to further increase the level of active risk – which is still below the ceiling authorized by the Board – in order to increase the level of returns at a rate in line with the organization's growing risk-management capabilities. Another priority on the investment side entails enhancing our capabilities to manage private transactions, i.e. mortgage and infrastructure portfolios. At the same time, we will focus on further strengthening PSP Investments' infrastructure and support staff to keep pace with the rapid growth of investment activities.

Acknowledgements

In conclusion, I would like to formally welcome those who joined our management team during the past year, including Guy Archambault, Vice President, Human Resources; Bernard Augustin, Vice President, Index and Quantitative Investments; Assunta DiLorenzo, First Vice President, General Counsel and Corporate Secretary; and John Valentini, First Vice President and Chief Financial Officer.

I also want to thank our employees, whose efforts are instrumental to the success of a fast-growing and dynamic organization. Thanks are due as well to former chief financial officer Danielle Morin for her contributions to PSP Investments during its formative years. Finally, I wish to express my appreciation to the Board for its continued support.



Gordon J. Fyfe
President and Chief Executive Officer



FISCAL YEAR 2005 RESULTS

The Public Sector Pension Investment Board (PSP Investments) completed its fifth year of operation on March 31, 2005. During that period, it received \$3.8 billion in net contributions from the Public Service, Canadian Forces and Royal Canadian Mounted Police pension funds. The market value of invested assets as of March 31, 2005 totaled \$19.4 billion, compared with \$14.2 billion a year earlier.

Market Performance

In general, financial markets went through two distinct phases during fiscal 2005. The first six months were sluggish, with uncertainties regarding the presidential election in the United States hanging over the markets. The next six months saw more movement.

Two main stories dominated financial headlines. The first was the resolve of the U.S. Federal Reserve Board to stifle any inflationary pressures. To that end, it raised U.S. interest rates seven times over the 12-month period. Investors watched the movements of currency markets with keen interest. The U.S. dollar continued a downward slide that had begun in the previous fiscal year, as investors worried about the “twin deficits” (fiscal and trade) in the U.S. economy. Over the course of fiscal 2005, the U.S. dollar fell by 8% against the Canadian dollar and 5% against the Euro. The U.S. deficits are currently being funded in large part by Asian investors, both public and private, who appear content to hold U.S. government and corporate bonds.

The U.S. economy continued to move forward, even in the face of the twin deficits, inflation fears, the decline of the U.S. dollar and rising interest rates. Once again, the engine of growth in the United States was the consumer, who translated earlier tax cuts into a surge in retail sales. The S&P 500 Index rose 7% for the year in U.S. dollar terms. (However, the decline of the U.S. currency meant that, in Canadian-dollar terms, the S&P effectively fell by 2%.)

The other major economic story from the past year was a spike in commodity prices. The price of oil rose 60%, closing the year at around US\$55 per barrel. As well, commodity prices in general increased, reflecting investor sentiment about the current and anticipated demand for commodities in China.

The bull market in commodities and oil served to boost the Canadian equities market, which is heavily weighted towards energy and commodity issues. The S&P/TSX Composite Index rose 14% during the fiscal year.

European equity markets had a positive year despite a lack of encouraging news. Asian markets were mixed; a strong year for commodity-rich Australia was offset by a flat year for Japan, where the economy stagnated. Taken together, the MSCI EAFE Index rose 6% for the year in Canadian-dollar terms.

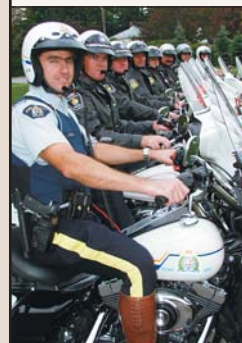
The Canadian bond market had another positive year. The Scotia Capital Universe Index rose 5%, as corporate-bond spreads tightened and the yield curve flattened.

Investment Results

In fiscal 2005, the Consolidated Pension Plan Account produced income of \$1.35 billion, before expenses. This compares with income of \$2.46 billion in fiscal 2004.

Performance Measurement and Evaluation

We use rigorous performance measurement as an essential tool for management to evaluate its investment strategies, as well as its internal and external managers.



FISCAL YEAR 2005 RESULTS

Benchmarks

- Each asset class has a benchmark defined in PSP Investments' Statement of Investment Policies, Standards and Procedures (SIP&P).
- The return for each asset class is compared against the relevant benchmark return.
- A combined Policy Benchmark has been created from the asset class benchmarks and the asset class weights established in the SIP&P.
- The Consolidated Pension Plan Account return is compared to the Policy Benchmark return.

Rates of Return on Consolidated Pension Plan Account (as of March 31, 2005)

	One year		Five-Year (annualized)		
	Portfolio Returns %	Benchmark Returns %	Portfolio Returns %	Benchmark Returns %	
Canadian Equities	15.7	13.9	3.4	3.5	S&P/TSX
Foreign Equities	1.7	1.5	-5.0	-4.9	Foreign Equity Benchmark ^a
Real Estate ^b	7.9	6.7	7.7	6.2	Real Estate Benchmark ^c
Fixed Income	5.0	4.7	7.7	7.6	Fixed income Benchmark ^d
Cash Equivalents	2.9	2.2	3.4	2.9	SC 91-Day T-Bill
Total Return	7.9	7.2	3.0	2.9	

These are time-weighted rates of return, before fees and expenses, for the consolidation of the three pension plan accounts. They are calculated in accordance with the methodology recommended by the CFA Institute, and are audited as such. Total Consolidated Pension Plan Assets include an initial investment in Private Equity.

^a A combination of S&P 500, MSCI EAFE, and MSCI Emerging Markets Free

^b Real Estate Investments commenced in fiscal year 2004.

^c Canadian Consumer Price Index + 5.5% per annum.

^d A combination of Scotia Capital Universe, Scotia Capital Short Term Federal Bond, and Scotia Capital Real Return Bond

Rate of Return

The rate of return for the Consolidated Pension Plan Account was 7.9%. The account outperformed its Policy Benchmark which returned 7.2% by 0.7%.

During fiscal 2005, PSP Investments aggressively took steps to further diversify the sources of both absolute performance (i.e. the asset classes in the Policy Portfolio) and relative performance (i.e. the active strategies and managers employed). Performance-enhancing initiatives were spread across a wider range of asset classes and active strategies. This trend will continue in fiscal 2006, as PSP Investments continues to work towards achieving its objectives. Further details can be found in the Investment Policy and Strategy section of this report.

Changes in Net Assets

The Consolidated Pension Plan Account began fiscal 2005 with net assets of \$14.2 billion at market value. Consolidated net contributions during the year added \$3.8 billion. After factoring in the net income from investment, consolidated net assets as of the fiscal 2005 year-end were \$19.4 billion at market value.

Expenses

The cost of operating PSP Investments during fiscal year 2005 totaled \$35.1 million, compared to \$21.1 million in fiscal year 2004. The total expenses are comprised of operating expenses (\$20.8 million in fiscal year 2005 versus \$12.1 million in 2004) and external investment management fees (\$14.3 million in fiscal year 2005 versus \$9.0 million in fiscal year 2004). The higher costs can be attributed mainly to the growth in assets under management, the hiring of additional staff to implement and support our investment strategies and the increase of activities in our real-estate and private-equity operations.

Total expenses amounted to 0.211% of average assets – or 0.125% of average assets, when external investment management fees are excluded. External investment management fees increased because of the significant growth in assets (36%) and the high proportion of those assets allocated to external managers.

Expenses will continue to increase in fiscal year 2006. External investment management fees will rise as a consequence of the expected growth in PSP Investments' assets and the high proportion that will again be allocated to external active managers. There will also be a substantial increase in operating expenses, reflecting the hiring of additional staff to support the implementation of more internally managed and active investment strategies, the continued development of specialty asset classes, such as private equity, real estate and infrastructure, indexed and quantitative investments and the continued amortization of investment in major new technology systems.

We remain vigilant about expenses and are committed to maintaining tight financial controls. Also, on a long-term basis, PSP Investments will increase its portion of investments managed internally and therefore lower the ratio of external management fees to average assets.



INVESTMENT POLICY AND STRATEGY

This section summarizes the statutory investment objectives of the Public Sector Pension Investment Board (PSP Investments) as well as the policy and strategy being used to achieve these objectives. A complete review of investment strategy during fiscal 2005 led to the development of a revised asset-mix policy, which includes allocating more money to asset classes that are less liquid and provide greater protection against inflation. Concurrently, management developed a new active-management policy. This focuses on the efficient utilization of active risk, in order to generate returns in excess of those of the Policy Portfolio.

Investment Objectives

The mission of PSP Investments is set out in section 4 of the Act:

- to manage funds in the best interests of contributors and beneficiaries under the Plans; and
- to maximize returns without undue risk of loss.

Based on these statutory objectives, the following investment objectives were established:

1. **Absolute Performance:** Achieving a return (net of expenses) at least equal to the actuarial rate of return as determined by the Chief Actuary of Canada; and
2. **Relative Performance:** Achieving a return exceeding the Policy Benchmark return by 0.50% (with a minimum value-added component equal to expenses).

These two objectives were met in fiscal 2005.

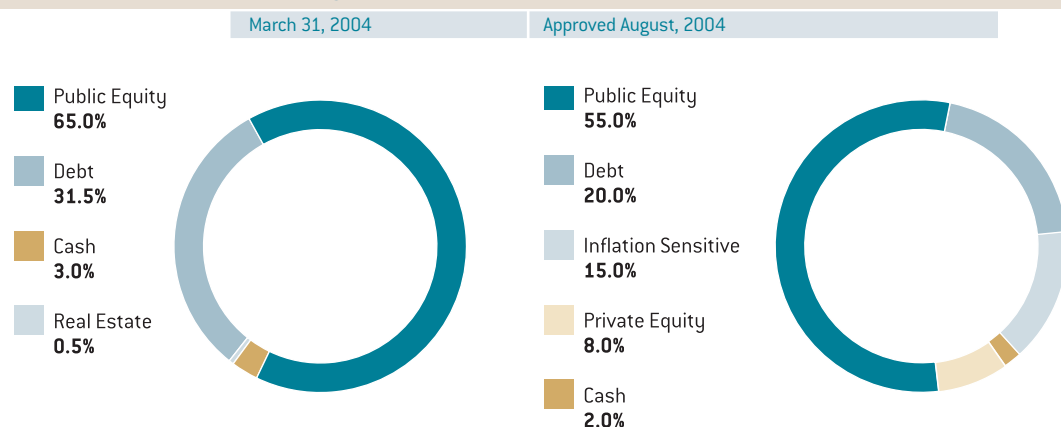
Asset-mix Policy

In fiscal 2005, PSP Investments conducted a complete review of its investment strategy. The main goal of this exercise was to determine the asset-mix policy that is best suited to achieving PSP's mission, as set out in the Act. Within this context, another goal was to emphasize "alternative" asset classes that provide a premium for lower liquidity as well as protection against inflation.

The outcome of the review was a new asset-mix policy that was approved by the Board of Directors in August 2004. The major changes are:

- A decrease in targeted allocations to global, large-cap public equity markets, in favour of less-liquid markets such as small-cap equities, private equities and emerging markets.
- A decrease in targeted allocation to liquid government debt (namely conventional government bonds), in favour of inflation-sensitive asset classes such as real-return bonds and real estate.

Evolution of the Asset-Mix Policy



INVESTMENT POLICY AND STRATEGY

The revised Policy Portfolio calls for the assets to be invested as follows:

Public Equities	55%
Canadian Equities	30%
Large Cap U.S. Equities	5%
Small Cap U.S. Equities	5%
International Developed Market Equities	8%
Emerging Market Equities	7%
Private Equities	8%
Debt	20%
Inflation-Sensitive	15%
Real Estate	10%
Real Return Bonds	5%
Cash Equivalents	2%

The process of reallocating assets to match the asset-mix policy is ongoing and should be substantially completed by the end of fiscal 2006.

Active Management Strategy

In addition to refining the asset-mix policy, PSP also adopted a more sophisticated approach to seeking added value on top of the Policy Portfolio. The Board has approved a "risk budget" that management can allocate to active strategies. Within this framework, management works to optimize its "roster" of active strategies, in order to meet the value-added objectives set out above.

In the past, the only active-management activities undertaken were within the asset classes of the Policy Portfolio (for example, as part of the allocation to Canadian Equities, a manager would be hired with a mandate to add value over the Toronto Stock Exchange's S&P/TSX Composite Index). Such activities remain an important element of PSP's approach, but the universe has been expanded: the asset classes of the Policy Portfolio are no longer a limiting factor in the search for added value. Mandates have been awarded to managers in other spheres, such as currency management and tactical asset allocation across countries and asset classes.

Over the course of fiscal 2005, PSP awarded a number of active mandates to internal and external managers. A number of managers were terminated during the year as well. Finally, an internal team has been assembled that will look to add value through quantitative management in equities and fixed income.

Investment Risk Management

A critical aspect of the revised asset-mix policy and active-management strategy is PSP's focus on measuring and managing investment risk. A fundamental law in investing is that the search for returns necessarily involves taking on some level of risk. In this context, risk is not something to be avoided. Rather, it is something to be *managed*, intelligently and efficiently, in the quest for superior investment performance.

The risk-management philosophy at PSP has evolved constantly since the organization's inception. Today, a rigorous process is in place, overseen by a dedicated team of professionals and supported by the appropriate systems. Risk is measured at all levels, from individual stocks up to total PSP assets. The diversification benefits of investment in different asset classes and investment styles also can be quantified.

The main benefit of the process is that new opportunities – in terms of asset classes, investment styles and individual managers – can be evaluated with regard to the additional risk they entail and the potential rewards and/or diversification benefits they offer.

Ultimately, by following the risk-management process, PSP can optimize its investment structure, with a view to maximizing returns for a given level of risk.



Effective governance is essential in order to safeguard the capital entrusted to the Public Sector Pension Investment Board (PSP Investments) and to ensure that appropriate objectives are pursued and achieved in line with the fulfillment of its legislated mandate. This section of the annual report presents pertinent information on PSP Investments' mandate, the roles of the Board of Directors and Board Committees and key policies designed to guide the organization's activities and behaviour.

Legislated Mandate

The legislated mandate of the Public Sector Pension Investment Board (PSP Investments) is:

- To manage funds received "in the best interests of the contributors and beneficiaries" of the three Plans; and
- To invest "with a view to achieving a maximum rate of return without undue risk of loss, having regard to the funding, policies and requirements of the Plans... and the ability of those Plans to meet their financial obligations."

The legislation states that PSP Investments shall not, directly or indirectly, carry on any business or activity or exercise any power inconsistent with these objectives.

Relationship to Pension Plans

Effective April 1, 2000, the federal government created three new pension funds—one each for the existing Public Service, Canadian Forces and Royal Canadian Mounted Police (RCMP) pension plans. These pension funds receive the employer and employee contributions in respect of each plan to provide for liabilities for service after April 1, 2000. The balances (that is, contributions after payment of benefits accrued since April 1, 2000 and after plan administration expenses) are transferred to separate accounts at PSP Investments, to be invested in accordance with the approved investment policy and strategy.

The government is the sponsor and administrator of the Plans. The President of the Treasury Board is responsible for the Public Service Plan, the Minister of National Defence for the Canadian Forces Plan, and the Solicitor General of Canada for the RCMP Plan.

The President and CEO and the Chairperson meet once a year with the Advisory Committees of the Plans. On-going communication also is in place with the Chief Actuary of Canada.

Accountability and Reporting

PSP Investments' President and CEO is appointed by and reports to the Board of Directors. The Board of Directors reports to Parliament through the President of the Treasury Board, who is responsible for PSP Investments' legislation and is required to table its annual report in Parliament. PSP Investments is required to provide quarterly financial statements and the annual report to the President of the Treasury Board, the Minister of National Defence and the Minister of Public Safety and Emergency Preparedness.

Annual meetings with the Advisory Committees of the Plans are also part of PSP Investments' reporting requirements.

Selection of Directors

A Board of Directors comprised of 12 members, including the Chairperson, governs PSP Investments. At March 31, 2005, 11 board positions were occupied and the nominating process had been initiated to fill current and anticipated vacancies. The Governor in Council appoints all members on the recommendation of the President of the Treasury Board. Qualified candidates for directorship are selected and recommended to the President of the Treasury Board by an eight-member nominating committee that operates at arm's length from the government. PSP Investments' legislation disqualifies as directors members of the Senate, the House of

Commons and provincial legislatures, federal government employees and those entitled to benefits from the three Plans. (The list of current Directors may be found on page 67.)

Biographical information about each of the Directors may also be viewed on PSP Investments' Web site: www.investpsp.ca under About Us—Board of Directors.

Duties of Directors

In order to ensure that legislated and regulatory objectives are met, the Board of Directors has defined its role to include, among other responsibilities, the following:

- Appointment of the President and Chief Executive Officer (CEO);
- Approval of a written Statement of Investment Policies, Standards and Procedures;
- Approval of strategies for achieving investment performance objectives;
- Adoption of appropriate policies for the proper conduct and management of PSP Investments, including a Code of Conduct, Conflict of Interest Procedures and risk-management policy;
- Approval of human-resources and compensation policies;
- Establishment of appropriate performance evaluation processes for the Board of Directors, the President and CEO and other members of senior management;
- Preparation and approval of quarterly and annual financial statements for each underlying pension plan account and for PSP Investments as a whole.

Board Committees

The Board of Directors has established the following four standing committees to assist in the fulfillment of its obligations:

- Investment Committee;
- Audit and Conflicts Committee;
- Governance Committee; and
- Human Resources and Compensation Committee.

Recommendations of Board committees are subject to the approval of the full Board. The Investment Committee includes all the members of the Board. The composition of the other committees is set out on page 67 of this report.

Further information relative to PSP Investments' committees, including their specific terms of reference, may be viewed on PSP Investments' Website: www.investpsp.ca under Governance—Duties & Responsibilities.

Directors' Compensation

The approach to director remuneration adopted by the Board, on the recommendation of the Governance Committee, reflects key requirements of the Act, which state that: (a) the Board should include: a "sufficient number of directors with proven financial ability or relevant work experience such that the Board will be able to effectively achieve its objectives"; and (b) that directors' compensation should be set "having regard to the remuneration received by persons having similar responsibilities and engaged in similar activities".

The Board reviews directors' compensation once every two years and considers whatever changes may be warranted based on a report and recommendations provided by the Governance Committee. The most recent review was conducted in fiscal year 2004. As of April 1, 2004, each director receives an annual retainer of \$20,000



and meeting fees of \$1,500 for each Board of Directors' meeting and \$1,000 for each committee meeting. However, only a single fee is paid when Board and Investment Committee meetings are held concurrently. In recognition of the significant additional time and responsibility demanded of the chairs of Board committees, committee chairs receive an additional retainer of \$7,500 per year.

The Board Chairperson – who is responsible for the effective overall operation of the Board and its activities, as well as for the relationship between the Board and management, and for PSP Investments' reporting relationship to its stakeholders – is paid a total of \$98,000 per annum in recognition of those services, while foregoing all other retainers and meeting fees.

The Board met nine times during fiscal year 2005 and its Committees held 25 meetings. In recognition of the added impact on Board members who are not from central Canada, an additional fee of \$1,000 is paid to directors who attend a meeting in person if their primary residence is not in Quebec or Ontario.

The compensation paid to directors during fiscal year 2005 is summarized in Note 7(a) to the financial statements of PSP Investments. The Terms of Reference for the Board Chairperson and for the Board of Directors may be viewed in their entirety on PSP Investments' Web site: www.investpsp.ca under Governance – Duties & Responsibilities.

Conflict of Interest Procedures

The Conflict of Interest Procedures for Directors are intended to provide a workable process for identifying, minimizing and resolving potential conflicts of interest. They help ensure that directors have a full understanding and appreciation of PSP Investments' principles and values to assist them in determining appropriate business practices and behaviour.

The Conflict of Interest Procedures for Directors sets out in detail the statutory and fiduciary duties of the directors relating to conflicts of interest. The Conflict of Interest Procedures include a requirement for the provision of written notice by directors to the Board of Directors of the nature and extent of the directors' interest in a transaction or proposed transaction; prohibit directors from voting on a resolution or participating in a discussion relating to any transaction involving their interests; require the disclosure of any other business activity which, directly or indirectly, affects the activities of, or is in competition with, PSP Investments; require the abstention from voting and the physical absence from discussions relating to any resolution if the director is also a director, employee or consultant of the bidder, has more than a 10% financial interest, when the investment represents more than 5% of the director's financial worth or an associate of the director's household is a director or employee of the bidder. The Audit and Conflicts Committee of the Board of Directors is responsible for monitoring the application of these procedures.

The Conflict of Interest Procedures may be viewed in their entirety on PSP Investments' Web site: www.investpsp.ca under Governance – Conflict of Interest Policy.



Assessment of Board Performance

The regulations adopted under PSP Investments' governing legislation require that the Board of Directors set out in the annual report the procedures in place for the assessment of its own performance. A formal performance evaluation policy, adopted in accordance with those requirements, focuses on procedures designed to encourage frank and confidential discussions between the Chairperson and individual directors, as well as between the Chairperson and the President and CEO of PSP Investments.

To facilitate the assessment process, guidelines for evaluating the performance of the Chairperson and of the Board as a whole are distributed once a year to every director as well as to the President and CEO. The guidelines take the form of a questionnaire. Directors submit their completed questionnaires to the Chair of the Governance Committee, who summarizes the information and presents it to the Board of Directors. The discussion focuses on concerns and opportunities for improvement, what is working properly or has improved since previous assessments. In fiscal 2006, board members will also conduct peer reviews of their performance.

Code of Conduct

In accordance with its governing legislation, PSP Investments has a Code of Conduct for officers and employees. As well as ensuring stringent compliance with the relevant statutory requirements, the Code serves as a framework that provides officers and employees with a full understanding of the organization's corporate principles and values to assist them in determining appropriate business practices and behaviour. It includes a "whistle-blowing" provision, designed to encourage officers and employees to step forward and report any questionable practices.

Among other things, the Code deals with honesty and integrity; compliance with the law; use of confidential information; reporting of personal investment transactions; receiving or giving entertainment, membership in and public representation of nonprofit and professional associations; and personal use of PSP Investments' resources, assets and facilities. As well, PSP Investments maintains a restricted list of securities in respect of which the organization has confidential knowledge. Officers and employees are prohibited from trading in securities on the restricted list.

The Audit and Conflicts Committee is responsible for monitoring the implementation and enforcement of the Code.

The Code of Conduct may be viewed on PSP Investments' Web site: www.investpsp.ca under Governance – Code of Conduct.

Proxy Voting Guidelines

The Proxy Voting Guidelines are designed to ensure that shares beneficially owned by PSP Investments will be voted in accordance with its investment policy and objectives.

The Guidelines stipulate that PSP Investments will be mindful of best corporate governance principles when considering the merits of an issue and will exercise its voting rights with a view to maximizing the value of its shareholdings. The Guidelines focus on four areas considered crucial in terms of their potential impact on performance:

- the independence, size and effectiveness of a company's board of directors;
- management and directors' compensation, including stock options and incentive compensation plans;
- takeover protection; and
- shareholder rights.



The Guidelines apply equally to securities managed internally and those held in portfolios managed for PSP Investments by external managers.

The Proxy Voting Guidelines may be viewed on PSP Investments' Web site: www.investpsp.ca under Investments – Proxy Voting Guidelines.

Policy on Social and Environmental Responsibility

The primary responsibility of PSP Investments is to provide for the financial benefit of contributors and beneficiaries of the Plans from which it receives funds and to support the fulfillment of the pension promise explicit in those plans. That responsibility notwithstanding, the Policy on Social and Environmental Responsibility states that “the environmental and social impact of the behaviour of corporations may be one of a number of factors that our investment professionals would wish to take into account in making investment decisions for the Plans”.

The Policy on Social and Environmental Responsibility may be viewed on PSP Investments' Web site: www.investpsp.ca under Investments – Policy on Social & Environmental Responsibility.

Special Examination

As provided in subsection 44(1) of the *Public Sector Pension Investment Board Act*, the President of the Treasury Board is required to cause a Special Examination to be carried out at least once every six years in respect of PSP Investments and its subsidiaries.

This is not an audit in the conventional sense. Rather, the purpose of the Special Examination is to determine if the financial and management control and information systems and management practices, referred to in paragraph 35(1)(b) the Act, “were... being maintained in a manner that provided reasonable assurance that they met the requirements of paragraphs

35(2)(a) and (c)” of the Act. Further information relative to these requirements may be viewed on PSP Investments' Web site: www.investpsp.ca under About Us – Mandate. Click on the link to the [Public Sector Pension Investment Board Act](#)

There are three phases to the Special Examination process: Phase I, completed in fiscal 2005, entailed the definition of focus areas; Phase II, scheduled for the first half of fiscal 2006, entails carrying out the actual examination; and Phase III entails reporting the findings.

A

Act

The Public Sector Pension Investment Board Act is the legislation which governs PSP Investments.

Active Investment Management

The application of manager skill in selecting investments, with the goal of earning higher returns than the general market.

Active Risk

The probability of investment losses relative to a benchmark—from active investment management.

Annual Report

A publication that includes the audited financial statements of an organization as well as management's discussion and analysis (MD&A) of its financial results and operations. PSP Investments' annual report must be issued within 90 days of its March 31 year-end and tabled by the President of the Treasury Board in the House of Commons.

Annualized Rate of Return

A rate of return expressed over one year, although the actual rates of return being annualized are for periods longer or shorter than one year.

Asset Mix

The proportion of assets invested in cash, fixed income securities, equities and other asset classes. Asset mix should reflect an investor's investment goals and risk tolerance.

Asset Mix Policy

Policy setting the guidelines for the management of the asset mix needed to achieve an expected level of investment returns. Pension funds set their asset mix policy to ensure that investment returns plus plan member contributions are sufficient to pay all current and future pension benefits. In making our investment decisions, we take into consideration the financial obligations of the three public sector pension funds for which PSP Investments invest money.

B

Basis Point

One-hundredth of a percentage point. The difference between 5.25 per cent and 5.50 per cent is 25 basis points.

Benchmark

A standard against which rates of return can be measured, such as stock and bond market indexes developed by stock exchanges and investment dealers.

Business Resumption Plan

Corporate plan to ensure the maintenance of essential business operations while recovering from a significant disruption. The Business Resumption Plan and the Disaster Recovery Plan combined ensure that the corporation maintains its essential activities while rebuilding the infrastructure of the corporation.

C

CFA Institute

The CFA Institute (CFI) is an international, nonprofit organization of more than 70,000 investment practitioners and educators in over 100 countries. The investment performance standards of CFA details methodology and guidelines that promote uniformity in reporting investment performance.

Cash Equivalents

Short-term, highly liquid securities (e.g. commercial papers, treasury bills, demand notes) with a term to maturity of less than one year from the date of issue. These investments are relatively easy to convert into cash.

Cost Value (or Book Value)

The purchase price, or original cost, of an investment.

Custodian

An independent organization entrusted with holding investments on behalf of the owner. The custodian maintains the financial records for the investments and may perform other services for the owner as well.

D

Derivatives

Financial contracts that derive their value from an underlying asset or index, such as an interest rate or foreign currency exchange rate. For example, a derivative contract based on the S&P 500 Index of large U.S. stocks fluctuates in value with the index, but involves buying one contract rather than each stock in the index. Derivatives can be less expensive and easier to acquire than the underlying assets. They can be used to manage risk, reduce cost and enhance returns. Some common derivatives are forwards, futures, swaps and options.

Disaster Recovery Plan

Corporate plan to address information technology disruption by identifying, documenting and testing processes aiming to facilitate recovery of technology capabilities.

Diversification

A strategy to spread investment risk among different asset classes (stocks and bonds), different types of assets (public and private equities), among securities (different stocks), among economic sectors (financial services and natural resources) and among different countries.

E

Equities (or Stocks)

Financial instruments that represent an ownership interest in a corporation, as well as a claim to proportionate shares of that corporation's assets and earnings.

F

Fair Value (or Market Value)

The most recent price at which a security transaction took place.

Fiscal Year

A company's accounting or financial reporting year. Our fiscal year commences April 1 and ends March 31.

Fixed Income Securities

Securities, such as bonds, mortgages, debentures and preferred shares, that generate a predictable stream of interest by paying a fixed rate of return until a specific date, maturity or redemption.

Foreign Currency Risk

The risk that an investment's value will be affected by changes in exchange rates. International investments cause investors to face the risk of currency fluctuations.

I

Index

A broad-based measurement of a general market trend. Called an index because it is designed to reflect not only price changes, but value changes as well.

Index Fund

An investment fund that closely replicates the return of a market index.

Infrastructure

Long duration assets—like highways, utilities, transportation, and pipelines—expected to produce low-volatility returns with a cash component similar to that of the fixed income markets.

Investment Management Fee

An annual fee paid to an investment manager for its services. The fee can be based on the level of assets under management, or on the performance of the portfolio.



M

Market Risk

Market risk is the risk that the value of an investment will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual investment, or factor affecting all securities traded in the market.

MSCI EAFE Index

A stock index created by Morgan Stanley Capital Inc. (MSCI) to measure the returns of investments in Europe, Australia and the Far East. It contains stocks from 21 countries, including Japan, Australia, Hong Kong, New Zealand, Singapore, the U.K. and the Euro zone countries.

O

Option

A derivative contract that grants the owner the right, but not the obligation, either to buy or sell a specified quantity of an asset at a fixed price on or before a specific date.

P

Passive Investment Management

A strategy designed to replicate a market index return by gaining exposure to individual securities in proportions that closely resemble their composition in an underlying index.

Pension Plan Account (or Plan Account)

Separate account established by PSP Investments for each of the pension plan funds to receive the pension fund's net contributions as well as the allocation of its investments and the results of its operations. There are three (3) pension plan accounts, one for each pension plan fund.

Pension Plan Fund

Created effective April 1, 2000 by the federal government to receive the employer and employee contributions in respect of the pension plans to provide for liabilities for service after April 1, 2000. There are three (3) pension plan funds, one for each of the Public Service Pension Plan; the Canadian Forces Pension Plan and the Royal Canadian Mounted Police (RCMP) Pension Plan.

Pension Plans (or Plans)

The pension plans of the federal Public Service, the Canadian Forces and the Royal Canadian Mounted Police.

Plan Liabilities

Plan liabilities represent the financial obligations of a pension plan relative to the benefits earned by the plan participants. The liabilities correspond to the value calculated by the pension actuary of all future benefits accrued as of the date of valuation.

Policy Portfolio

The asset mix, set by the Board of Directors, identifying how the funds managed should be allocated between different asset classes (example: cash, fixed income securities, equities, real estate, ...)

Portfolio

A group of investments, such as equities and bonds and possibly financial instruments such as derivatives grouped for investment purposes.

Private Equity

Ownership interest in assets that do not trade on public exchanges or over the counter.

Proxy Voting Rights

Written authorization by a shareholder for someone else to represent them and vote their shares at a shareholders' meeting, generally under stipulated guidelines or conditions.

R

Return (or Rate of Return)

The percentage change in assets in a particular period, consisting of income (such as interest, dividends or rent), plus realized and unrealized capital gains or capital losses.

Risk

The probability of investment losses, either in absolute terms, or versus a benchmark.

Risk-Adjusted Return

A measure of investment return adjusted to reflect the risk that was assumed to produce that return.

S

Scotia Capital Debt Market Indices

A series of indices created and maintained by Scotia Capital to measure the performance of Canadian bond and money markets. The Universe Index includes all marketable Canadian bonds with a term to maturity greater than one year, and is a broad measure of the performance of the Canadian bond market.

The 91-Day T-Bill Index is one of a number of money market indices maintained by Scotia Capital.

Social Investing

An investment process that uses screens to select or avoid investing in certain companies or industries to reflect religious, economic, political, social or personal priorities.

S&P/TSX Composite Index

The most diversified Canadian market index representing almost 90 percent of the capitalization of Canadian-based companies listed on the TSX. A committee of the Toronto Stock Exchange and Standard and Poor's selects companies for inclusion in the S&P/TSX Composite Index.

Standard and Poor's 500 Composite Index (S&P 500 Index)

A U.S. index consisting of 500 stocks chosen for market size, liquidity and industry group representation. It is a market-value-weighted index (stock price times number of shares outstanding), with each stock's weight in the index proportionate to its market value. The Standard & Poor's company selects stocks for inclusion in the index.

Statement of Investment Policies, Standards and Procedures (or Investment Policy)

A written investment policy approved by the Board of Directors, and reviewed at least annually, relating to each pension plan fund. This is a requirement under paragraph 7(2) (a) of the Act. It addresses matter such as categories of investments; use of derivative products; asset diversification and expected investment returns; management of credit, market and other financial risks; liquidity of investments; lending of cash and securities; evaluation of investments that are not regularly traded on a public exchange; and the exercise of any voting rights that PSP Investments has through its investments.

T

Time-Weighted Rate of Return

A return calculation methodology that eliminates the impact of cash flows into (or out of) a portfolio. This methodology recognizes the fact that managers have no control over the size and timing of cash flows.

V

Volatility

Generally refers to variability (in frequency and magnitude) of returns around an average or reference point over a period of time.

FINANCIAL STATEMENTS AND NOTES TO THE FINANCIAL STATEMENTS

Management's Responsibility for Financial Reporting	26
Investment Certificate	26

PUBLIC SERVICE PENSION PLAN ACCOUNT

Auditors' Report	27
Balance Sheet	28
Statement of Changes in Net Assets	28
Statement of Net Income and Accumulated Net Income from Operations	29
Statement of Investment Portfolio	29
Notes to the Financial Statements	30-34

CANADIAN FORCES PENSION PLAN ACCOUNT

Auditors' Report	35
Balance Sheet	36
Statement of Changes in Net Assets	36
Statement of Net Income and Accumulated Net Income from Operations	37
Statement of Investment Portfolio	37
Notes to the Financial Statements	38-42

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Auditors' Report	43
Balance Sheet	44
Statement of Changes in Net Assets	44
Statement of Net Income and Accumulated Net Income from Operations	45
Statement of Investment Portfolio	45
Notes to the Financial Statements	46-50

PUBLIC SECTOR PENSION INVESTMENT BOARD

Auditors' Report	51
Consolidated Balance Sheet	52
Consolidated Statement of Changes in Net Assets	52
Consolidated Statement of Net Income from Operations	53
Consolidated Statement of Investment Portfolio	53
Notes to the Consolidated Financial Statements	54-66

Management's Responsibility for Financial Reporting

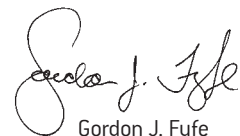
The consolidated financial statements of the Public Sector Pension Investment Board ("PSP Investments") have been prepared by management and approved by the Board of Directors. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Management is responsible for the contents of the consolidated financial statements and the financial information contained in the annual report.

PSP Investments maintains records and systems of internal control and supporting procedures to provide reasonable assurance that PSP Investments' assets are safeguarded and controlled, and that transactions are in accordance with the *Public Sector Pension Investment Board Act* (the "Act"), the accompanying regulations, the by-laws, and the Statement of Investment Policies, Standards and Procedures (the "SIP & P").

In this regard, investments of PSP Investments held during the year ended March 31, 2005, were in accordance with the Act, by laws and SIP&P with the exception of the foreign property limits set out in the SIP&P which were exceeded during the period from March 15 to March 31, 2005 in anticipation of the adoption of the Federal Budget which provides for the elimination of the foreign property limits.

The Audit and Conflicts Committee assists the Board of Directors in discharging its responsibility to approve the annual consolidated financial statements. The Committee meets regularly with both management and the external auditors to discuss the scope and findings of audits and other work that the external auditors may be requested to perform from time to time, to review financial information, and to discuss the adequacy of internal controls. The Committee reviews the annual consolidated financial statements and recommends them to the Board of Directors for approval.

The PSP Investments' external auditors, Deloitte & Touche LLP, have conducted an independent examination of the consolidated financial statements in accordance with Canadian generally accepted auditing standards, performing such tests and other procedures as they consider necessary to express an opinion in their Auditors' Report. The external auditors have full and unrestricted access to management and the Audit and Conflicts Committee to discuss findings related to the integrity of PSP Investments' financial reporting and the adequacy of internal control systems.



Gordon J. Fyfe
President and Chief Executive Officer
April 29, 2005



John Valentini
First Vice President and Chief Financial Officer
April 29, 2005

Investment Certificate

The *Public Sector Pension Investment Board Act* (the "Act") requires that a certificate be signed by a director on behalf of the Board of Directors, stating that the investments of the Public Sector Pension Investment Board ("PSP Investments") held during the financial year were in accordance with the Act and PSP Investments' investment policies, standards and procedures. Accordingly, the Investment Certificate follows:

"The investments of PSP Investments held during the year ended March 31, 2005, were in accordance with the Act and PSP Investments' Statement of Investment Policies, Standards and Procedures (the "SIP&P") with the exception of the foreign property limits set out in the SIP&P which were exceeded during the period from March 15 to March 31, 2005 in anticipation of the adoption of the Federal Budget which provides for the elimination of the limits on investments in property that constitutes foreign property for the purposes of the Income Tax Act (Canada)."



Paul Cantor
Chairperson
June 8, 2005

Auditors' report

To the Board of Directors
Public Sector Pension Investment Board – Public Service Pension Plan Account

We have audited the Balance Sheet and the Statement of Investment Portfolio of the Public Sector Pension Investment Board – Public Service Pension Plan Account (the "Public Service Pension Plan Account") as at March 31, 2005 and the Statements of Net Income and Accumulated Net Income from Operations and of Changes in Net Assets for the year then ended. These financial statements are the responsibility of the Public Sector Pension Investment Board's ("PSP Investments") management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Public Service Pension Plan Account and the investments held as at March 31, 2005 and the results of its operations and of changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

Further, in our opinion, the transactions of the Public Service Pension Plan Account that have come to our attention during our audit of the financial statements have, in all significant respects, been in accordance with the *Public Sector Pension Investment Board Act* (the "Act") and the by-laws, with the exception of the foreign property limits set out in the Statement of Investments Policies, Standards and Procedures which were exceeded during the period from March 15 to March 31, 2005 in anticipation of the adoption of the Federal Budget which provides for the elimination of the limits on investments in property that constitutes foreign property for the purposes of the *Income Tax Act* (Canada).

Further, in our opinion, the record of investments kept by PSP Investments' management pursuant to paragraph 35 (1) (c) of the Act fairly presents, in all material respects, the information required by the Act.



Chartered Accountants
Toronto, Ontario
April 29, 2005

PUBLIC SERVICE PENSION PLAN ACCOUNT

Balance Sheet

As at March 31 (\$000's)	2005	2004
ASSETS		
Investments – at fair value (Note 2)	\$13,977,850	\$10,204,912
Other assets (Note 3)	1,659	2,284
Due from the Canadian Forces Pension Plan Account (Note 6a)	2,071	1,268
Due from the Royal Canadian Mounted Police Pension Plan Account (Note 6a)	737	452
	13,982,317	10,208,916
LIABILITIES		
Accounts payable and accrued liabilities	7,047	2,994
NET ASSETS	\$13,975,270	\$10,205,922
NET ASSETS REPRESENTED BY		
Accumulated net income from operations	\$ 1,958,743	\$ 1,014,481
Accumulated fund transfers	12,016,527	9,191,441
	\$13,975,270	\$10,205,922

On behalf of the Board of Directors:



Keith Martell
Director and Chair of the Audit and Conflicts Committee

Statement of Changes in Net Assets

For the year ended March 31 (\$000's)	2005	2004
NET ASSETS, BEGINNING OF YEAR	\$10,205,922	\$ 5,756,832
CHANGES IN NET ASSETS		
Fund transfers (Note 4)	2,825,086	2,708,522
Net income from operations	944,262	1,740,568
NET ASSETS, END OF YEAR	\$13,975,270	\$10,205,922

PUBLIC SERVICE PENSION PLAN ACCOUNT

Statement of Net Income and Accumulated Net Income from Operations

For the year ended March 31 (\$000's)	2005	2004
INVESTMENT INCOME		
Interest and dividends	\$ 299,283	\$ 214,740
Net realized gains	167,250	126,580
Change in unrealized appreciation in value of investments	502,945	1,414,288
	969,478	1,755,608
EXPENSES		
Operating expenses (Note 6b)	14,905	8,607
External investment management fees	10,311	6,433
	25,216	15,040
NET INCOME FROM OPERATIONS	944,262	1,740,568
ACCUMULATED NET INCOME (LOSS) FROM OPERATIONS, BEGINNING OF THE YEAR		
	1,014,481	(726,087)
ACCUMULATED NET INCOME FROM OPERATIONS, END OF THE YEAR		
	\$ 1,958,743	\$ 1,014,481

Statement of Investment Portfolio

As at March 31 (\$000's)	2005		2004	
Investments (Note 2)	Cost	Fair Value	Cost	Fair Value
PSP Canadian Equities Fund 448,432,869.150611 units (2004 – 339,919,202.635087 units)	\$ 4,488,469	\$ 5,598,410	\$ 3,229,760	\$ 3,822,838
PSP Foreign Equities Fund 410,578,363.410520 units (2004 – 303,562,389.690353 units)	3,765,272	3,810,007	2,767,387	2,816,047
PSP Private Equities Fund 325,111.200140 units (2004 – Nil)	2,599	2,151	—	—
PSP Real Estate Fund 6,523,194.126872 units (2004 – 5,222,027.004991 units)	66,642	70,893	51,590	53,237
PSP Foreign Real Estate Fund 27,120,446.007601 units (2004 – Nil)	279,559	278,113	—	—
PSP Hedging Fund 719,436.777118 units (2004 – Nil)	8,151	11,282	—	—
PSP Fixed Income Fund 379,503,014.686497 units (2004 – see note 2c)	4,009,574	4,077,263	3,350,480	3,450,033
PSP Absolute Return Fund 14,026,130.124790 units (2004 – 8,283,355.378224 units)	134,876	129,731	85,932	62,757
	\$12,755,142	\$13,977,850	\$ 9,485,149	\$10,204,912

Notes to the Financial Statements

For the year ended March 31, 2005

ORGANIZATION

The Public Sector Pension Investment Board (“PSP Investments”) was formed pursuant to the *Public Sector Pension Investment Board Act* (the “Act”) with a mandate to invest in financial markets the contributions to the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans.

The Public Service Pension Fund was established by amendments to the *Public Service Superannuation Act*, to receive contributions and make benefit payments in respect of member service after April 1, 2000. The excess of contributions over benefits is transferred, by the Public Service Pension Fund, to PSP Investments – Public Service Pension Plan Account for investment. PSP Investments maintains records of the Pension Fund’s net contributions, as well as the allocation of its investments and the results of its operations to each of the Plan Accounts.

PSP Investments is responsible for managing amounts that are transferred to it in the best interests of the beneficiaries and contributors under the *Public Service Superannuation Act*. The amounts are to be invested with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the *Public Service Superannuation Act*.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

These financial statements present the financial position and operations of PSP Investments as they pertain to the investment of the excess funds transferred to it from the Public Service Pension Fund. Accordingly, they do not reflect all of the assets, or the details of the pension contributions, payments and liabilities of the Public Service Pension Fund. The statements have been prepared in accordance with Canadian generally accepted accounting principles and the requirements of the Act.

Valuation of investments

Investments consist of the unit interest in PSP Investments’ assets (The “PSP Funds”) that are allocated to this Plan Account. Investments are recorded as of the trade date and are stated at fair value. Fair value is the amount of the consideration that would be agreed upon in an arm’s length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value for investments in pooled funds is based on unit values, which reflect the quoted market prices or other generally accepted pricing methodologies for the underlying securities.

Income recognition

The investment income has been allocated by PSP Investments according to the number of units of PSP Funds held by the Public Service Pension Plan Account.

Investment income is recorded on the accrual basis and represents realized gains and losses on the disposal of investments, change in unrealized appreciation (depreciation) on investments held at the end of the year, interest income and dividends. These income items include the related distributions from PSP Funds.

Translation of foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange on the transaction date. Investments denominated in foreign currencies and held at the end of the year are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses on foreign exchanges are included in investment income.

Fund transfers

Amounts received from the Public Service Pension Fund are recorded on a cash basis.

Notes to the Financial Statements

For the year ended March 31, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income Taxes

PSP Investments is exempt from Part I tax under paragraph 149(1)(d) of the *Income Tax Act* (Canada).

Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions which can affect the reported values of assets and liabilities, related income and expenses and note disclosures. Actual results may differ from estimates.

2. INVESTMENTS

The Statement of Investment Portfolio provides details of investments held as at March 31, 2005.

(a) Investment Policy

PSP Investments has established a Statement of Investment Policies, Standards and Procedures, (the “Investment Policy”) which sets out the manner in which the assets shall be invested for the Public Service Pension Plan Account.

Target asset mix policy and benchmarks, as at March 31, 2005, were as follows:

Asset Class	Policy Mix	Benchmark
Cash Equivalents	2%	SC 91 day T-Bill
Bonds		
Fixed Return	20%	SC Universe
Real Return ⁽¹⁾	5%	SC RRB
Public & Private Equities		
Public Equities		
Canadian Equity	30%	S&P TSX
US Equities		
Large Cap	5%	S&P 500
Small Cap	5%	S&P 600
EAFE Equity	8%	MSCI EAFE
Emerging Equity	7%	MSCI EMF
Private Equity ⁽²⁾	8%	S&P 600 ^(1/3) and S&P 400 ^(2/3) + 4%
Real Estate ⁽³⁾	10%	CPI + 5.5%

(1) Real Return Bonds (“RRB”) target weight is 5%. Until the target weight of 5% is reached, assets destined for RRB’s will be invested in Fixed Income and measured against the SC Universe.
 (2) Private Equity (“PE”) target weight is 8%. Until the target weight of 8% is reached, assets destined for PE will be invested in Public Equities and measured against the corresponding public equity benchmarks.
 (3) Real Estate (“RE”) target weight is 10%. Until the target weight of 10% is reached, assets destined for RE will be invested in a short-term bond benchmarked to the SM ST Fed. Gov. Index.



PUBLIC SERVICE PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(b) Investment asset mix

The investment asset mix, as at March 31, was as follows:

Asset Class	2005		2004	
	Fair Value (\$000's)	% of Portfolio	Fair Value (\$000's)	% of Portfolio
Cash Equivalents	\$ 316,115	2.3%	\$ 68,602	0.7%
Bonds				
Fixed Return	3,711,173	26.6	3,434,154	33.6
Real Return	158,399	1.1	—	—
Public & Private Equities				
Public Equities				
Canadian Equity	5,598,409	40.1	3,822,838	37.5
US Equities				
Large Cap	1,670,120	12.0	1,523,501	14.9
Small Cap	75,906	0.5	46,632	0.5
EAFE Equity	1,808,483	12.9	1,245,914	12.2
Emerging Equity	255,498	1.8	—	—
Private Equity	2,151	—	—	—
Real Estate	309,616	2.2	53,237	0.5
Absolute Return Strategies	71,980	0.5	10,034	0.1
	\$13,977,850	100.0%	\$10,204,912	100.0%

Direct investments, derivative contracts and investment-related receivables and liabilities are classified by asset-mix category based on the intent of the investment strategies of the underlying portfolios of PSP Investments.

(c) Changes in PSP Funds

On November 30, 2004, PSP Investments restructured its funds.

The nature of the PSP Fixed Income Fund has changed to include cash equivalent investments. As a result, the investments previously held in the PSP Cash Equivalents Fund were transferred into the PSP Fixed Income Fund. For comparative purposes, the amount shown as PSP Cash Equivalents Fund for the prior year has been reclassified. As at March 31, 2004, this Plan Account held 1,600,319.402448 units of the PSP Cash Equivalents Fund and 319,551,329.862296 units of the PSP Fixed Income Fund.

The PSP Foreign Real Estate Fund was created to hold foreign real estate investments.

The PSP Absolute Return Fund was created and investments previously held in the PSP Currency Overlay Fund were transferred to it. For comparative purposes, the amount shown as PSP Currency Overlay Fund for the prior year has been reclassified.

(d) Foreign currency exposure

This Plan Account is exposed to currency risk through holdings of units in PSP Funds of non-Canadian assets where investment values will fluctuate due to changes in foreign exchange rates.

PUBLIC SERVICE PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(d) Foreign currency exposure (continued)

The underlying net foreign currency exposures, as at March 31, were as follows:

Currency (in Canadian \$)	2005		2004	
	Fair Value (\$000's)	% of Total	Fair Value (\$000's)	% of Total
US Dollars	\$ 1,984,909	49.8%	\$ 1,575,025	55.8%
Euro	691,634	17.3	469,649	16.6
British Pound	376,349	9.4	233,156	8.3
Yen	358,723	9.0	309,453	11.0
Others	576,948	14.5	235,262	8.3
	\$ 3,988,563	100.0%	\$ 2,822,545	100.0%

Further details of Investments are shown in the PSP Investments financial statements.

3. OTHER ASSETS

Other assets as at March 31 consist of the following:

((\$000's))	2005	2004
Fixed assets	\$ 1,623	\$ 1,524
Other assets	36	760
	\$ 1,659	\$ 2,284

4. FUND TRANSFERS

During the year, PSP Investments received \$2,825.1 million (2004 – \$2,708.5 million) of transfers from the Public Service Pension Fund. The transfers result from net current employer and employee contributions to the Public Service Pension Plan.

5. INVESTMENT PERFORMANCE

Portfolio and benchmark returns for the year ended March 31 were as follows:

	2005		2004	
	Portfolio Returns	Benchmark Returns	Portfolio Returns	Benchmark Returns
Cash Equivalents	2.9%	2.2%	3.2%	3.0%
Fixed Income	5.0%	4.7%	10.9%	10.8%
Canadian Equities	15.7%	13.9%	36.1%	37.7%
Foreign Equities	1.7%	1.5%	30.7%	28.8%
Real Estate	7.9%	6.7%	3.6%	2.5%
Total Return	7.9%	7.2%	26.1%	25.4%

Notes to the Financial Statements

For the year ended March 31, 2005

5. INVESTMENT PERFORMANCE (continued)

The total benchmark return aggregates the asset class benchmark returns according to the weights specified in the Investment Policy. The total return includes the impact of the PSP Hedging Fund and the PSP Absolute Return Fund. Returns have been calculated in accordance with the methodology recommended by the CFA Institute. Returns are presented gross of expenses.

6. EXPENSES

(a) Allocation of expenses

The Act requires that the costs of operation of PSP Investments be charged to the three plans for which it provides investment services. Under section 4(3) of the Act, the President of the Treasury Board shall determine to which Plan Account these costs will be charged, in consultation with the Minister of National Defence and the Solicitor General of Canada. An allocation policy has been developed which allocates the direct costs of investment activities, such as external investment management fees and custodial fees, to each Plan Account, and allocates, on a quarterly basis, operating expenses excluding custodial fees, based upon the asset value of each Plan Account.

Operating expenses, excluding custodial fees, have been allocated as follows:

	2005	2004
Public Service Pension Plan Account	71.7%	71.1%
Canadian Forces Pension Plan Account	20.9%	21.3%
Royal Canadian Mounted Police Pension Plan Account	7.4%	7.6%
	100.0%	100.0%

Expenses are financed by the Public Service Pension Plan Account, which are reimbursed by the other Plan Accounts on a quarterly basis.

(b) Operating expenses

Operating expenses allocated to this Plan Account consist of the following:

(\$000's)	2005	2004
Salaries and benefits	\$ 7,579	\$ 3,969
General operating expenses	5,142	3,291
Professional and consulting fees	2,184	1,347
	\$ 14,905	\$ 8,607

Further details of Operating expenses are shown in the PSP Investments financial statements.

7. COMPARATIVE FIGURES

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

Auditors' report

To the Board of Directors
Public Sector Pension Investment Board – Canadian Forces Pension Plan Account

We have audited the Balance Sheet and the Statement of Investment Portfolio of the Public Sector Pension Investment Board – Canadian Forces Pension Plan Account (the "Canadian Forces Pension Plan Account") as at March 31, 2005 and the Statements of Net Income and Accumulated Net Income from Operations and of Changes in Net Assets for the year then ended. These financial statements are the responsibility of the Public Sector Pension Investment Board's ["PSP Investments"] management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Canadian Forces Pension Plan Account and the investments held as at March 31, 2005 and the results of its operations and of changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

Further, in our opinion, the transactions of the Canadian Forces Pension Plan Account that have come to our attention during our audit of the financial statements have, in all significant respects, been in accordance with the *Public Sector Pension Investment Board Act* (the "Act") and the by-laws, with the exception of the foreign property limits set out in the Statement of Investments Policies, Standards and Procedures which were exceeded during the period from March 15 to March 31, 2005 in anticipation of the adoption of the Federal Budget which provides for the elimination of the limits on investments in property that constitutes foreign property for the purposes of the *Income Tax Act* (Canada).

Further, in our opinion, the record of investments kept by PSP Investments' management pursuant to paragraph 35 (1) (c) of the Act fairly presents, in all material respects, the information required by the Act.

Deloitte & Touche LLP

Chartered Accountants
Toronto, Ontario
April 29, 2005

CANADIAN FORCES PENSION PLAN ACCOUNT

Balance Sheet

As at March 31 (\$000's)	2005	2004
ASSETS		
Investments – at fair value (Note 2)	\$ 3,964,971	\$ 2,971,057
Other assets	486	464
	3,965,457	2,971,521
LIABILITIES		
Accounts payable and accrued liabilities	2,030	884
Due to the Public Service Pension Plan Account (Note 5a)	2,071	1,268
	4,101	2,152
NET ASSETS	\$ 3,961,356	\$ 2,969,369
NET ASSETS REPRESENTED BY		
Accumulated net income from operations	\$ 568,650	\$ 297,328
Accumulated fund transfers	3,392,706	2,672,041
	\$ 3,961,356	\$ 2,969,369

On behalf of the Board of Directors:



Keith Martell

Director and Chair of the Audit and Conflicts Committee

Statement of Changes in Net Assets

For the year ended March 31 (\$000's)	2005	2004
NET ASSETS, BEGINNING OF YEAR	\$ 2,969,369	\$ 1,723,935
CHANGES IN NET ASSETS		
Fund transfers (Note 3)	720,665	728,979
Net income from operations	271,322	516,455
NET ASSETS, END OF YEAR	\$ 3,961,356	\$ 2,969,369

CANADIAN FORCES PENSION PLAN ACCOUNT

Statement of Net Income and Accumulated Net Income from Operations

For the year ended March 31 (\$000's)	2005	2004
INVESTMENT INCOME		
Interest and dividends	\$ 85,849	\$ 63,344
Net realized gains	47,059	37,909
Change in unrealized appreciation in value of investments	145,717	419,683
	278,625	520,936
EXPENSES		
Operating expenses (Note 5b)	4,348	2,582
External investment management fees	2,955	1,899
	7,303	4,481
NET INCOME FROM OPERATIONS	271,322	516,455
ACCUMULATED NET INCOME (LOSS) FROM OPERATIONS, BEGINNING OF THE YEAR	297,328	(219,127)
ACCUMULATED NET INCOME FROM OPERATIONS, END OF THE YEAR	\$ 568,650	\$ 297,328

Statement of Investment Portfolio

As at March 31 (\$000's)	2005		2004	
Investments (Note 2)	Cost	Fair Value	Cost	Fair Value
PSP Canadian Equities Fund 127,203,667.618307 units (2004 – 98,964,475.025539 units)	\$1,264,031	\$1,588,059	\$ 938,071	\$1,112,986
PSP Foreign Equities Fund 116,460,575.763523 units (2004 – 88,376,832.678660 units)	1,069,744	1,080,709	808,573	819,842
PSP Private Equities Fund 94,161.037099 units (2004 – Nil)	753	623	—	—
PSP Real Estate Fund 1,852,858.269436 units (2004 – 1,536,657.515258 units)	18,915	20,137	15,181	15,665
PSP Foreign Real Estate Fund 7,700,888.462009 units (2004 – Nil)	79,380	78,971	—	—
PSP Hedging Fund 203,674.625146 units (2004 – Nil)	2,305	3,194	—	—
PSP Fixed Income Fund 107,657,110.746798 units (2004 – see note 2c)	1,137,428	1,156,634	975,731	1,004,276
PSP Absolute Return Fund 3,961,830.929116 units (2004 – 2,413,807.740989 units)	38,269	36,644	25,071	18,288
	\$3,610,825	\$3,964,971	\$2,762,627	\$2,971,057

Notes to the Financial Statements

For the year ended March 31, 2005

ORGANIZATION

The Public Sector Pension Investment Board (“PSP Investments”) was formed pursuant to the *Public Sector Pension Investment Board Act* (the “Act”) with a mandate to invest in financial markets the contributions to the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans.

The Canadian Forces Pension Fund was established by amendments to the *Canadian Forces Superannuation Act*, to receive contributions and make benefit payments in respect of member service after April 1, 2000. The excess of contributions over benefits is transferred, by the Canadian Forces Pension Fund, to PSP Investments – Canadian Forces Pension Plan Account for investment. PSP Investments maintains records of the Pension Fund’s net contributions, as well as the allocation of its investments and the results of its operations to each of the Plan Accounts. PSP Investments is responsible for managing amounts that are transferred to it in the best interests of the beneficiaries and contributors under the *Canadian Forces Superannuation Act*. The amounts are to be invested with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the *Canadian Forces Superannuation Act*.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

These financial statements present the financial position and operations of PSP Investments as they pertain to the investment of the excess funds transferred to it from the Canadian Forces Pension Fund. Accordingly, they do not reflect all of the assets, or the details of the pension contributions, payments and liabilities of the Canadian Forces Pension Fund. The statements have been prepared in accordance with Canadian generally accepted accounting principles and the requirements of the Act.

Valuation of investments

Investments consist of the unit interest in PSP Investments’ assets (The “PSP Funds”) that are allocated to this Plan Account. Investments are recorded as of the trade date and are stated at fair value. Fair value is the amount of the consideration that would be agreed upon in an arm’s length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value for investments in pooled funds is based on unit values, which reflect the quoted market prices or other generally accepted pricing methodologies for the underlying securities.

Income recognition

The investment income has been allocated by PSP Investments according to the number of units of PSP Funds held by the Canadian Forces Pension Plan Account. Investment income is recorded on the accrual basis and represents realized gains and losses on the disposal of investments, change in unrealized appreciation (depreciation) on investments held at the end of the year, interest income and dividends. These income items include the related distributions from PSP Funds.

Translation of foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange on the transaction date. Investments denominated in foreign currencies and held at the end of the year are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses on foreign exchanges are included in investment income.

Notes to the Financial Statements

For the year ended March 31, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fund transfers

Amounts received from the Canadian Forces Pension Fund are recorded on a cash basis.

Income Taxes

PSP Investments is exempt from Part I tax under paragraph 149(1)(d) of the *Income Tax Act* (Canada).

Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions which can affect the reported values of assets and liabilities, related income and expenses and note disclosures. Actual results may differ from estimates.

2. INVESTMENTS

The Statement of Investment Portfolio provides details of investments held as at March 31, 2005.

(a) Investment Policy

PSP Investments has established a Statement of Investment Policies, Standards and Procedures, (the “Investment Policy”) which sets out the manner in which the assets shall be invested for the Canadian Forces Pension Plan Account.

Target asset mix policy and benchmarks, as at March 31, 2005, were as follows:

Asset Class	Policy Mix	Benchmark
Cash Equivalents	2%	SC 91 day T-Bill
Bonds		
Fixed Return	20%	SC Universe
Real Return ⁽¹⁾	5%	SC RRB
Public & Private Equities		
Public Equities		
Canadian Equity	30%	S&P TSX
US Equities		
Large Cap	5%	S&P 500
Small Cap	5%	S&P 600
EAFE Equity	8%	MSCI EAFE
Emerging Equity	7%	MSCI EMF
Private Equity ⁽²⁾	8%	S&P 600 ^(1/3) and S&P 400 ^(2/3) + 4%
Real Estate ⁽³⁾	10%	CPI +5.5%

(1) Real Return Bonds (“RRB”) target weight is 5%. Until the target weight of 5% is reached, assets destined for RRB’s will be invested in Fixed Income and measured against the SC Universe.
 (2) Private Equity (“PE”) target weight is 8%. Until the target weight of 8% is reached, assets destined for PE will be invested in Public Equities and measured against the corresponding public equity benchmarks.
 (3) Real Estate (“RE”) target weight is 10%. Until the target weight of 10% is reached, assets destined for RE will be invested in a short-term bond benchmarked to the SM ST Fed. Gov. Index.



CANADIAN FORCES PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(b) Investment asset mix

The investment asset mix, as at March 31, was as follows:

Asset Class	2005		2004	
	Fair Value (\$000's)	% of Portfolio	Fair Value (\$000's)	% of Portfolio
Cash Equivalents	\$ 89,610	2.3%	\$ 19,746	0.6%
Bonds				
Fixed Return	1,052,782	26.6	999,893	33.7
Real Return	44,934	1.1	—	—
Public & Private Equities				
Public Equities				
Canadian Equity	1,588,060	40.1	1,112,986	37.5
US Equities				
Large Cap	473,730	12.0	443,540	14.9
Small Cap	21,531	0.5	13,576	0.5
EAFE Equity	512,976	12.9	362,726	12.2
Emerging Equity	72,472	1.8	—	—
Private Equity	623	—	—	—
Real Estate	87,922	2.2	15,665	0.5
Absolute Return Strategies	20,331	0.5	2,925	0.1
	\$ 3,964,971	100.0%	\$ 2,971,057	100.0%

Direct investments, derivative contract, and investment-related receivables and liabilities are classified by asset-mix category based on the intent of the investment strategies of the underlying portfolios of PSP Investments.

(c) Changes in PSP Funds

On November 30, 2004, PSP Investments restructured its funds.

The nature of the PSP Fixed Income Fund has changed to include cash equivalent investments. As a result, the investments previously held in the PSP Cash Equivalents Fund were transferred into the PSP Fixed Income Fund. For comparative purposes, the amount shown as PSP Cash Equivalents Fund for the prior year has been reclassified. As at March 31, 2004, this Plan Account held 441,694.101721 units of the PSP Cash Equivalents Fund and 93,040,969.189282 units of the PSP Fixed Income Fund.

The PSP Foreign Real Estate Fund was created to hold foreign real estate investments.

The PSP Absolute Return Fund was created and investments previously held in the PSP Currency Overlay Fund were transferred to it. For comparative purposes, the amount shown as PSP Currency Overlay Fund for the prior year has been reclassified.

CANADIAN FORCES PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(d) Foreign currency exposure

This Plan Account is exposed to currency risk through holdings of units in PSP Funds of non-Canadian assets where investment values will fluctuate due to changes in foreign exchange rates.

The underlying net foreign currency exposures, as at March 31, were as follows:

Currency (in Canadian \$)	2005		2004	
	Fair Value (\$000's)	% of Total	Fair Value (\$000's)	% of Total
US Dollars	\$ 563,120	49.8%	\$ 458,542	55.8%
Euro	196,178	17.3	136,730	16.6
British Pound	106,751	9.4	67,880	8.3
Yen	101,813	9.0	90,092	11.0
Others	163,574	14.5	68,492	8.3
	\$ 1,131,436	100.0%	\$ 821,736	100.0%

Further details of Investments are shown in the PSP Investments financial statements.

3. FUND TRANSFERS

During the year, PSP Investments received \$720.7 million (2004 – \$729.0 million) of transfers from the Canadian Forces Pension Fund. The transfers result from net current employer and employee contributions to the Canadian Forces Pension Plan.

4. INVESTMENT PERFORMANCE

Portfolio and benchmark returns for the year ended March 31 were as follows:

	2005		2004	
	Portfolio Returns	Benchmark Returns	Portfolio Returns	Benchmark Returns
Cash Equivalents	2.9%	2.2%	3.2%	3.0%
Fixed Income	5.0%	4.7%	10.9%	10.8%
Canadian Equities	15.7%	13.9%	36.1%	37.7%
Foreign Equities	1.7%	1.5%	30.7%	28.8%
Real Estate	7.9%	6.7%	3.6%	2.5%
Total Return	8.0%	7.2%	26.1%	25.4%

The total benchmark return aggregates the asset class benchmark returns according to the weights specified in the Investment Policy. The total return includes the impact of the PSP Hedging Fund and the PSP Absolute Return Fund. Returns have been calculated in accordance with the methodology recommended by the CFA Institute. Returns are presented gross of expenses.

Notes to the Financial Statements

For the year ended March 31, 2005

5. EXPENSES

(a) Allocation of expenses

The Act requires that the costs of operation of PSP Investments be charged to the three plans for which it provides investment services. Under section 4(3) of the Act, the President of the Treasury Board shall determine to which Plan Account these costs will be charged, in consultation with the Minister of National Defence and the Solicitor General of Canada. An allocation policy has been developed which allocates the direct costs of investment activities, such as external investment management fees and custodial fees, to each Plan Account, and allocates, on a quarterly basis, operating expenses excluding custodial fees, based upon the asset value of each Plan Account.

Operating expenses, excluding custodial fees, have been allocated as follows:

	2005	2004
Public Service Pension Plan Account	71.7%	71.1%
Canadian Forces Pension Plan Account	20.9%	21.3%
Royal Canadian Mounted Police Pension Plan Account	7.4%	7.6%
	100.0%	100.0%

Expenses are financed by the Public Service Pension Plan Account, which is reimbursed by the other Plan Accounts on a quarterly basis.

(b) Operating expenses

Operating expenses allocated to this Plan Account consist of the following:

(\$000's)	2005	2004
Salaries and benefits	\$ 2,209	\$ 1,189
General operating expenses	1,502	989
Professional and consulting fees	637	404
	\$ 4,348	\$ 2,582

Further details of Operating expenses are shown in the PSP Investments financial statements.

6. COMPARATIVE FIGURES

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

Auditors' report

To the Board of Directors
Public Sector Pension Investment Board – Royal Canadian Mounted Police Pension Plan Account

We have audited the Balance Sheet and the Statement of Investment Portfolio of the Public Sector Pension Investment Board – Royal Canadian Mounted Police Pension Plan Account (the "Royal Canadian Mounted Police Pension Plan Account") as at March 31, 2005 and the Statements of Net Income and Accumulated Net Income from Operations and of Changes in Net Assets for the year then ended. These financial statements are the responsibility of the Public Sector Pension Investment Board's ("PSP Investments") management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Royal Canadian Mounted Police Pension Plan Account and the investments held as at March 31, 2005 and the results of its operations and of changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

Further, in our opinion, the transactions of the Royal Canadian Mounted Police Pension Plan Account that have come to our attention during our audit of the financial statements, have, in all significant respects, been in accordance with the *Public Sector Pension Investment Board Act* (the "Act") and the by-laws, with the exception of the foreign property limits set out in the Statement of Investments Policies, Standards and Procedures which were exceeded during the period from March 15 to March 31, 2005 in anticipation of the adoption of the Federal Budget which provides for the elimination of the limits on investments in property that constitutes foreign property for the purposes of the *Income Tax Act* (Canada).

Further, in our opinion, the record of investments kept by PSP Investments' management pursuant to paragraph 35 (1) (c) of the Act fairly presents, in all material respects, the information required by the Act.

Deloitte & Touche LLP
Chartered Accountants
Toronto, Ontario
April 29, 2005

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Balance Sheet

As at March 31

(\$000's)	2005	2004
ASSETS		
Investments – at fair value (Note 2)	\$ 1,425,627	\$ 1,057,240
Other assets	173	164
	1,425,800	1,057,404
LIABILITIES		
Accounts payable and accrued liabilities	725	314
Due to the Public Service Pension Plan Account (Note 5a)	737	452
	1,462	766
NET ASSETS	\$ 1,424,338	\$ 1,056,638
NET ASSETS REPRESENTED BY		
Accumulated net income from operations	\$ 202,253	\$ 104,815
Accumulated fund transfers	1,222,085	951,823
	\$ 1,424,338	\$ 1,056,638

On behalf of the Board of Directors:



Keith Martell

Director and Chair of the Audit and Conflicts Committee

Statement of Changes in Net Assets

For the year ended March 31

(\$000's)	2005	2004
NET ASSETS, BEGINNING OF YEAR	\$ 1,056,638	\$ 614,945
CHANGES IN NET ASSETS		
Fund transfers (Note 3)	270,262	258,066
Net income from operations	97,438	183,627
NET ASSETS, END OF YEAR	\$ 1,424,338	\$ 1,056,638

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Statement of Net Income and Accumulated Net Income from Operations

For the year ended March 31

(\$000's)	2005	2004
INVESTMENT INCOME		
Interest and dividends	\$ 30,818	\$ 22,658
Net realized gains	16,920	13,618
Change in unrealized appreciation in value of investments	52,299	148,947
	100,037	185,223
EXPENSES		
Operating expenses (Note 5b)	1,540	921
External investment management fees	1,059	675
	2,599	1,596
NET INCOME FROM OPERATIONS	97,438	183,627
ACCUMULATED NET INCOME (LOSS) FROM OPERATIONS, BEGINNING OF THE YEAR		
	104,815	(78,812)
ACCUMULATED NET INCOME FROM OPERATIONS, END OF THE YEAR		
	\$ 202,253	\$ 104,815

Statement of Investment Portfolio

As at March 31

(\$000's)	2005		2004	
Investments (Note 2)	Cost	Fair Value	Cost	Fair Value
PSP Canadian Equities Fund	\$ 456,126	\$ 571,073	\$ 334,410	\$ 396,018
45,742,979.665686 units (2004 – 35,213,173.590086 units)				
PSP Foreign Equities Fund	384,698	388,594	288,002	291,785
41,876,145.951163 units (2004 – 31,453,586.722645 units)				
PSP Private Equities Fund	267	221	—	—
33,358.967270 units (2004 – Nil)				
PSP Real Estate Fund	6,776	7,210	5,271	5,440
663,462.149861 units (2004 – 533,575.860052 units)				
PSP Foreign Real Estate Fund	28,520	28,335	—	—
2,763,174.577038 units (2004 – Nil)				
PSP Hedging Fund	830	1,149	—	—
73,242.002601 units (2004 – Nil)				
PSP Fixed Income Fund	409,001	415,895	347,191	357,452
38,710,600.952962 units (2004 – see note 2c)				
PSP Absolute Return Fund	13,732	13,150	8,987	6,545
1,421,696.457209 units (2004 – 863,902.396206 units)				
	\$1,299,950	\$ 1,425,627	\$ 983,861	\$ 1,057,240

Notes to the Financial Statements

For the year ended March 31, 2005

ORGANIZATION

The Public Sector Pension Investment Board (“PSP Investments”) was formed pursuant to the *Public Sector Pension Investment Board Act* (the “Act”) with a mandate to invest, in financial markets, the contributions to the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans.

The Royal Canadian Mounted Police Pension Fund was established by amendments to the *Royal Canadian Mounted Police Superannuation Act*, to receive contributions and make benefit payments in respect of member service after April 1, 2000. The excess of contributions over benefits is transferred, by the Royal Canadian Mounted Police Pension Fund, to PSP Investments – Royal Canadian Mounted Police Pension Plan Account for investment. PSP Investments maintains records of the Pension Fund’s net contributions, as well as the allocation of its investments and the results of its operations to each of the Plan Accounts.

PSP Investments is responsible for managing amounts that are transferred to it in the best interests of the beneficiaries and contributors under the *Royal Canadian Mounted Police Superannuation Act*. The amounts are to be invested with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the *Royal Canadian Mounted Police Superannuation Act*.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

These financial statements present the financial position and operations of PSP Investments as they pertain to the investment of the excess funds transferred to it from the Royal Canadian Mounted Police Pension Fund. Accordingly, they do not reflect all of the assets, or the details of the pension contributions, payments and liabilities of the Royal Canadian Mounted Police Pension Fund. The statements have been prepared in accordance with Canadian generally accepted accounting principles and the requirements of the Act.

Valuation of investments

Investments consist of the unit interest in PSP Investments’ assets (The “PSP Funds”) that are allocated to this Plan Account. Investments are recorded as of the trade date and are stated at fair value. Fair value is the amount of the consideration that would be agreed upon in an arm’s length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value for investments in pooled funds is based on unit values, which reflect the quoted market prices or other generally accepted pricing methodologies for the underlying securities.

Income recognition

The investment income has been allocated by PSP Investments according to the number of units of PSP Funds held by the Royal Canadian Mounted Police Pension Plan Account.

Investment income is recorded on the accrual basis and represents realized gains and losses on the disposal of investments, change in unrealized appreciation (depreciation) on investments held at the end of the year, interest income and dividends. These income items include the related distributions from PSP Funds.

Translation of foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange on the transaction date. Investments denominated in foreign currencies and held at the end of the year are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses on foreign exchanges are included in investment income.

Notes to the Financial Statements

For the year ended March 31, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fund transfers

Amounts received from the Royal Canadian Mounted Police Pension Fund are recorded on a cash basis.

Income Taxes

PSP Investments is exempt from Part I tax under paragraph 149(1)(d) of the *Income Tax Act* (Canada).

Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions which can affect the reported values of assets and liabilities, related income and expenses and note disclosures. Actual results may differ from estimates.

2. INVESTMENTS

The Statement of Investment Portfolio provides details of investments held as at March 31, 2005.

(a) Investment Policy

PSP Investments has established a Statement of Investment Policies, Standards and Procedures, (the “Investment Policy”) which sets out the manner in which the assets shall be invested for the Royal Canadian Mounted Police Pension Plan Account.

Target asset mix policy and benchmarks, as at March 31, 2005, were as follows:

Asset Class	Policy Mix	Benchmark
Cash Equivalents	2%	SC 91 day T-Bill
Bonds		
Fixed Return	20%	SC Universe
Real Return ⁽¹⁾	5%	SC RRB
Public & Private Equities		
Public Equities		
Canadian Equity	30%	S&P TSX
US Equities		
Large Cap	5%	S&P 500
Small Cap	5%	S&P 600
EAFE Equity	8%	MSCI EAFE
Emerging Equity	7%	MSCI EMF
Private Equity ⁽²⁾	8%	S&P 600 ^(1/3) and S&P 400 ^(2/3) + 4%
Real Estate ⁽³⁾	10%	CPI +5.5%

(1) Real Return Bonds (“RRB”) target weight is 5%. Until the target weight of 5% is reached, assets destined for RRB’s will be invested in Fixed Income and measured against the SC Universe.

(2) Private Equity (“PE”) target weight is 8%. Until the target weight of 8% is reached, assets destined for PE will be invested in Public Equities and measured against the corresponding public equity benchmarks.

(3) Real Estate (“RE”) target weight is 10%. Until the target weight of 10% is reached, assets destined for RE will be invested in a short-term bond benchmarked to the SM ST Fed. Gov. Index.



Notes to the Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(b) Investment asset mix

The investment asset mix, as at March 31, was as follows:

Asset Class	2005		2004	
	Fair Value (\$000's)	% of Portfolio	Fair Value (\$000's)	% of Portfolio
Cash Equivalents	\$ 32,201	2.3%	\$ 7,107	0.6%
Bonds				
Fixed Return	378,552	26.6	355,844	33.7
Real Return	16,157	1.1	—	—
Public & Private Equities				
Public Equities				
Canadian Equity	571,073	40.1	396,018	37.5
US Equities				
Large Cap	170,341	12.0	157,858	14.9
Small Cap	7,741	0.5	4,832	0.5
EAFE Equity	184,454	12.9	129,095	12.2
Emerging Equity	26,059	1.8	—	—
Private Equity	221	—	—	—
Real Estate	31,533	2.2	5,440	0.5
Absolute Return Strategies	7,295	0.5	1,046	0.1
	\$1,425,627	100.0%	\$1,057,240	100.0%

Direct investments, derivative contracts, and investment-related receivables and liabilities are classified by asset-mix category based on the intent of the investment strategies of the underlying portfolios of PSP Investments.

(c) Changes in PSP Funds

On November 30, 2004, PSP Investments restructured its funds.

The nature of the PSP Fixed Income Fund has changed to include cash equivalent investments. As a result, the investments previously held in the PSP Cash Equivalents Fund were transferred into the PSP Fixed Income Fund. For comparative purposes, the amount shown as PSP Cash Equivalents Fund for the prior year has been reclassified. As at March 31, 2004, this Plan Account held 162,067,776,519 units of the PSP Cash Equivalents Fund and 33,111,660,436,000 units of the PSP Fixed Income Fund.

The PSP Foreign Real Estate Fund was created to hold foreign real estate investments.

The PSP Absolute Return Fund was created and investments previously held in the PSP Currency Overlay Fund were transferred to it. For comparative purposes, the amount shown as PSP Currency Overlay Fund for the prior year has been reclassified.

Notes to the Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(d) Foreign currency exposure

This Plan Account is exposed to currency risk through holdings of units in PSP Funds of non-Canadian assets where investment values will fluctuate due to changes in foreign exchange rates.

The underlying net foreign currency exposures, as at March 31, were as follows:

Currency (in Canadian \$)	2005		2004	
	Fair Value (\$000's)	% of Total	Fair Value (\$000's)	% of Total
US Dollars	\$ 202,428	49.8%	\$ 163,199	55.8%
Euro	70,540	17.3	48,664	16.6
British Pound	38,380	9.4	24,158	8.3
Yen	36,620	9.0	32,064	11.0
Other	58,803	14.5	24,377	8.3
	\$ 406,771	100.0%	\$ 292,462	100.0%

Further details of Investments are shown in the PSP Investments financial statements.

3. FUND TRANSFERS

During the year, PSP Investments received \$270.2 million (2004 – \$258.1 million) of transfers from the Royal Canadian Mounted Police Pension Fund. The transfers result from net current employer and employee contributions to the Royal Canadian Mounted Police Pension Plan.

4. INVESTMENT PERFORMANCE

Portfolio and benchmark returns for the year ended March 31 were as follows:

	2005		2004	
	Portfolio Returns	Benchmark Returns	Portfolio Returns	Benchmark Returns
Cash Equivalents	2.9%	2.2%	3.2%	3.0%
Fixed Income	5.0%	4.7%	10.9%	10.8%
Canadian Equities	15.7%	13.9%	36.1%	37.7%
Foreign Equities	1.7%	1.5%	30.7%	28.8%
Real Estate	7.9%	6.7%	3.6%	2.5%
Total Return	8.0%	7.2%	26.1%	25.4%

The total benchmark return aggregates the asset class benchmark returns according to the weights specified in the Investment Policy. The total return includes the impact of the PSP Hedging Fund and the PSP Absolute Return Fund. Returns have been calculated in accordance with the methodology recommended by the CFA Institute. Returns are presented gross of expenses.

Notes to the Financial Statements

For the year ended March 31, 2005

5. EXPENSES

(a) Allocation of expenses

The Act requires that the costs of operation of PSP Investments be charged to the three plans for which it provides investment services. Under section 4(3) of the Act, the President of the Treasury Board shall determine to which Plan Account these costs will be charged, in consultation with the Minister of National Defence and the Solicitor General of Canada. An allocation policy has been developed which allocates the direct costs of investment activities, such as external investment management fees and custodial fees, to each Plan Account, and allocates, on a quarterly basis, operating expenses excluding custodial fees, based upon the asset value of each Plan Account.

Operating expenses, excluding custodial fees, have been allocated as follows:

	2005	2004
Public Service Pension Plan Account	71.7%	71.1%
Canadian Forces Pension Plan Account	20.9%	21.3%
Royal Canadian Mounted Police Pension Plan Account	7.4%	7.6%
	100.0%	100.0%

Expenses are financed by the Public Service Pension Plan Account, which is reimbursed by the other Plan Accounts on a quarterly basis.

(b) Operating expenses

Operating expenses allocated to this Plan Account consist of the following:

(\$000's)	2005	2004
Salaries and benefits	\$ 782	\$ 424
General operating expenses	533	353
Professional and consulting fees	225	144
	\$ 1,540	\$ 921

Further details of Operating expenses are shown in the PSP Investments financial statements.

6. COMPARATIVE FIGURES

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

Auditors' report

To the Board of Directors
Public Sector Pension Investment Board

We have audited the consolidated Balance Sheet and the consolidated Statement of Investment Portfolio of the Public Sector Pension Investment Board ("PSP Investments") as at March 31, 2005 and the consolidated Statements of Net Income from Operations and of Changes in Net Assets for the year then ended. These financial statements are the responsibility of PSP Investments' management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of PSP Investments and the investments held as at March 31, 2005 and the results of its operations and of changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

Further, in our opinion, the transactions of PSP Investments and those of its subsidiaries that have come to our attention during our audit of the consolidated financial statements, have, in all significant respects, been in accordance with the Public Sector Pension Investment Board Act (the "Act") and the by-laws, and any by-laws of the subsidiaries, with the exception of the foreign property limits set out in the Statement of Investments Policies, Standards and Procedures which were exceeded during the period from March 15 to March 31, 2005 in anticipation of the adoption of the Federal Budget which provides for the elimination of the limits on investments in property that constitutes foreign property for the purposes of the Income Tax Act (Canada).

Further, in our opinion, the record of investments kept by PSP Investments' management pursuant to paragraph 35 (1) (c) of the Act fairly presents, in all material respects, the information required by the Act.

Deloitte & Touche LLP

Chartered Accountants
Toronto, Ontario
April 29, 2005

PUBLIC SECTOR PENSION INVESTMENT BOARD

Consolidated Balance Sheet

As at March 31 (\$000's)	2005	2004
ASSETS		
Investments – at fair value (Note 2)	\$19,368,448	\$14,233,209
Cash	3,341	1,571
Other assets (Note 3)	4,508	3,039
	19,376,297	14,237,819
LIABILITIES		
Accounts payable and accrued liabilities	15,333	5,890
NET ASSETS	\$19,360,964	\$14,231,929
NET ASSETS REPRESENTED BY		
Public Service Pension Plan Account	\$13,975,270	\$10,205,922
Canadian Forces Pension Plan Account	3,961,356	2,969,369
Royal Canadian Mounted Police Pension Plan Account	1,424,338	1,056,638
	\$19,360,964	\$14,231,929

Commitments (Note 10)

On behalf of the Board of Directors:



Keith Martell

Director and Chair of the Audit and Conflicts Committee

Consolidated Statement of Changes in Net Assets

For the year ended March 31 (\$000's)	2005	2004
NET ASSETS, BEGINNING OF YEAR	\$14,231,929	\$8,095,712
CHANGES IN NET ASSETS		
Fund transfers (Note 4)	3,816,013	3,695,567
Net income from operations	1,313,022	2,440,650
NET ASSETS, END OF YEAR	\$19,360,964	\$14,231,929

PUBLIC SECTOR PENSION INVESTMENT BOARD

Consolidated Statement of Net Income from Operations

For the year ended March 31 (\$000's)	2005	2004
INVESTMENT INCOME (Note 5)		
Interest and dividends	\$441,640	\$312,240
Net realized gains	432,138	192,369
Change in unrealized appreciation in value of investments	474,362	1,957,158
	1,348,140	2,461,767
EXPENSES		
Operating expenses (Note 7a)	20,793	12,110
External investment management fees	14,325	9,007
	35,118	21,117
NET INCOME FROM OPERATIONS (Note 8)	\$1,313,022	\$2,440,650

Consolidated Statement of Investment Portfolio

As at March 31 (\$000's)	2005		2004	
Investments (Note 2)	Cost	Fair Value	Cost	Fair Value
PSP Canadian Equities Fund				
Active management	\$3,801,302	\$4,581,405	\$2,092,955	\$2,467,869
Indexed management	2,624,880	3,176,137	2,456,707	2,863,973
	6,426,182	7,757,542	4,549,662	5,331,842
PSP Foreign Equities Fund				
Active management	3,285,107	3,463,143	1,419,440	1,612,849
Indexed management	1,763,889	1,816,167	2,234,584	2,314,825
	5,048,996	5,279,310	3,654,024	3,927,674
PSP Private Equities Fund				
Private Equities investment (Note 2h)	3,618	2,995	—	—
PSP Real Estate Fund				
Real Estate investment (Note 2i)	90,985	98,240	72,042	74,342
PSP Foreign Real Estate Fund				
Real Estate investment (Note 2i)	390,595	385,419	—	—
PSP Hedging Fund				
Net cash and derivative instruments	15,110	15,625	—	—
PSP Fixed Income Fund				
Active management	2,585,533	2,629,590	2,192,974	2,252,362
Indexed management	2,993,842	3,020,202	2,517,941	2,559,399
	5,579,375	5,649,792	4,710,915	4,811,761
PSP Absolute Return Fund				
Net cash and derivative instruments	181,619	179,525	88,960	87,590
	\$17,736,480*	\$19,368,448*	\$13,075,603*	\$14,233,209*

* Includes investment receivables of \$55.7 million (2004 – \$19.1 million) and investment payables of \$81.9 million (2004 – \$58.0 million) pertaining to pending trades and forward currency contracts for a net payable of \$26.2 million (2004 – \$38.9 million). Also includes accrued income of \$37.3 million (2004 – \$36.0 million).

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

ORGANIZATION

The Public Sector Pension Investment Board ("PSP Investments") was formed pursuant to the *Public Sector Pension Investment Board Act* (the "Act") with a mandate to invest in financial markets the contributions to the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans.

The Public Service, Canadian Forces and Royal Canadian Mounted Police Pension Funds were established by amendments to the *Public Service Superannuation Act*, the *Canadian Forces Superannuation Act* and the *Royal Canadian Mounted Police Superannuation Act* (the "Superannuation Acts"), to receive contributions and make benefit payments in respect of member service after April 1, 2000. The excess of contributions over benefits is transferred, by each Pension Fund, to their respective PSP Investments-Plan Account for investment.

PSP Investments is responsible for managing amounts that are transferred to it in the best interests of the beneficiaries and contributors under the *Superannuation Acts*. The amounts are to be invested with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the pension plans established under the *Superannuation Acts*.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**Basis of presentation**

These consolidated financial statements present the financial position and operations of PSP Investments as they pertain to the investment of the excess funds transferred to it from the Public Service, Canadian Forces and Royal Canadian Mounted Police Pension Funds. Accordingly, they do not reflect all of the assets, or the details of the pension contributions, payments and liabilities of all three Pension Funds. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and the requirements of the Act. These consolidated financial statements include the accounts of PSP Investments and, from the respective date of creation, its wholly-owned subsidiaries.

Plan Accounts

PSP Investments maintains records of each Pension Funds' net contributions, as well as the allocation of its investments and the results of its operations to each of the Plan Accounts.

Separate financial statements for each Plan Accounts have been published.

Valuation of investments

Investments are recorded as of the trade date and are stated at fair value. Fair value is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

Fair values of investments are determined as follows:

- (a) Short-term deposits are recorded at cost which, together with accrued interest income, approximates fair value.
- (b) Market prices for equities and unit values for pooled funds are used to represent the fair value of investments. Unit values reflect the quoted market prices of the underlying securities.
- (c) Private Equity investments, where quoted market prices are not available, are fair-valued annually by external managers of pooled funds or of limited partnerships in which the investments are made. The fair value is determined by the external managers using acceptable industry valuation methods. These methods include considerations such as earnings multiples of comparable publicly traded companies, discounted cash flows and third party transactions.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**Valuation of investments (continued)**

(d) The fair value of investments in Real Estate is determined at least annually, using acceptable industry valuation methods, such as discounted cash flows and comparable transactions.

In the first year of ownership, the fair value of direct investments is based on the net book value of such investments, using the purchase price of the underlying assets. If the investment is denominated in foreign currency, the fair value reflects the change in foreign exchange rates.

(e) Fixed Income securities are valued at year-end quoted market prices where available. Where quoted market prices are not available, estimated values are calculated using either an appropriate interest rate curve with a spread associated with the credit quality of the issuer or other generally accepted pricing methodologies.

(f) Derivative instruments, including swaps, futures, options and forward contracts are valued at year-end quoted market prices where available. Where quoted market prices are not available, estimated values are calculated using methods such as discounted cash flows using market yields and other pricing models, as appropriate.

Income recognition

Investment income is recorded on the accrual basis and represents realized gains and losses on the disposal of investments, change in unrealized appreciation (depreciation) on investments held at the end of the year, interest income and dividends. These income items include the related distributions from pooled funds and limited partnerships.

Translation of foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange on the transaction date. Investments denominated in foreign currencies and held at the end of the year are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses on foreign exchange are included in investment income.

Fund transfers

Amounts received from each Pension Fund are recorded on a cash basis in their respective Plan Account.

Income Taxes

PSP Investments and certain of its subsidiaries are exempt from Part I tax under paragraph 149(1) (d) of the *Income Tax Act* (Canada).

Use of estimates

In preparing these consolidated financial statements, management must make certain estimates and assumptions which can affect the reported values of assets and liabilities, related income and expenses and note disclosures. Actual results may differ from estimates.



Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS

The Consolidated Statement of Investment Portfolio provides details of investments held as at March 31, 2005.

(a) Investment Policy

PSP Investments has established a Statement of Investment Policies, Standards and Procedures, (the "Investment Policy") which sets out the manner in which the assets shall be invested for the three Plan Accounts.

Target asset mix policy and benchmarks, as at March 31, 2005, were as follows:

Asset Class	Policy Mix	Benchmark
Cash Equivalents	2%	SC 91 day T-Bill
Bonds		
Fixed Return	20%	SC Universe
Real Return ⁽¹⁾	5%	SC RRB
Public & Private Equities		
Public Equities		
Canadian Equity	30%	S&P TSX
US Equities		
Large Cap	5%	S&P 500
Small Cap	5%	S&P 600
EAFE Equity	8%	MSCI EAFE
Emerging Equity	7%	MSCI EMF
Private Equity ⁽²⁾	8%	S&P 600 ^(1/3) and S&P 400 ^(2/3) + 4%
Real Estate ⁽³⁾	10%	CPI +5.5%

(1) Real Return Bonds ("RRB") target weight is 5%. Until the target weight of 5% is reached, assets destined for RRB's will be invested in Fixed Income and measured against the SC Universe.

(2) Private Equity ("PE") target weight is 8%. Until the target weight of 8% is reached, assets destined for PE will be invested in Public Equities and measured against the corresponding public equity benchmarks.

(3) Real Estate ("RE") target weight is 10%. Until the target weight of 10% is reached, assets destined for RE will be invested in a short-term bond benchmarked to the SM ST Fed. Gov. Index.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(b) Investment asset mix

The investment asset mix, as at March 31, was as follows:

Asset Class	2005		2004	
	Fair Value (\$000's)	% of Portfolio	Fair Value (\$000's)	% of Portfolio
Cash Equivalents	\$ 437,926	2.3%	\$ 95,455	0.7%
Bonds				
Fixed Return	5,142,507	26.6	4,789,891	33.6
Real Return	219,490	1.1	—	—
Public & Private Equities				
Public Equities				
Canadian Equity	7,757,542	40.1	5,331,842	37.5
US Equities				
Large Cap	2,314,191	12.0	2,124,900	14.9
Small Cap	105,178	0.5	65,040	0.5
EAFE Equity	2,505,913	12.9	1,737,735	12.2
Emerging Equity	354,029	1.8	—	—
Private Equity	2,995	—	—	—
Real Estate	429,071	2.2	74,342	0.5
Absolute Return Strategies	99,606	0.5	14,004	0.1
	\$19,368,448	100.0%	\$14,233,209	100.0%

Direct investments, derivative contracts, and investment-related receivables and liabilities are classified by asset-mix category based on the intent of the investment strategies of the underlying portfolios of PSP Investments.

(c) Changes in PSP Funds

On November 30, 2004, PSP Investments restructured its funds.

The nature of the PSP Fixed Income Fund has changed to include cash equivalent investments. As a result, the investments previously held in the PSP Cash Equivalents Fund were transferred into the PSP Fixed Income Fund. For comparative purposes, the amount shown as PSP Cash Equivalents Fund for the prior year has been reclassified.

The PSP Foreign Real Estate Fund was created to hold foreign real estate investments.

The PSP Absolute Return Fund was created and investments previously held in the PSP Currency Overlay Fund were transferred to it. For comparative purposes, the amount shown as PSP Currency Overlay Fund for the prior year has been reclassified.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(d) Foreign currency exposure

PSP Investments and its subsidiaries are exposed to currency risk through holdings of securities, units in pooled funds and units in limited partnerships of non-Canadian assets where investment values will fluctuate due to changes in foreign exchange rates. To mitigate this risk, PSP Investments may take, through derivative contracts, trading positions in foreign currencies.

The underlying net foreign currency exposures, as at March 31, were as follows:

Currency (in Canadian \$)	2005		2004	
	Fair Value (\$000's)	% of Total	Fair Value (\$000's)	% of Total
US Dollars	\$ 2,750,457	49.8%	\$ 2,196,766	55.8%
Euro	958,352	17.3	655,043	16.6
British Pound	521,480	9.4	325,194	8.3
Yen	497,156	9.0	431,609	11.0
Others	799,325	14.5	328,131	8.3
	\$ 5,526,770	100.0%	\$ 3,936,743	100.0%

PSP Investments and its subsidiaries also have commitments in real estate-related investments for an amount of \$276.4 million (\$216.7 million US and £6.2 million GBP) which is not included in the foreign currency exposure table above.

(e) Credit risk

Credit risk arises in the Cash Equivalents, the Fixed Income and the Real Estate asset classes. Credit risk is managed through minimum DBRS (or equivalent) rating requirements, and for the Real Estate class, by performing thorough due diligence analysis.

PSP Investments' highest concentration of credit risk is with the Government of Canada through its holding of \$2.0 billion of Government of Canada issued securities. PSP Investments, to minimize derivative contract credit risk, deals only with counterparties, which are major financial institutions with a minimum credit standard rating of "A", as supported by a recognized credit rating agency.

(f) Market risk

Market risk is the risk that the value of an investment will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual investment, or factors affecting all securities traded in the market. PSP Investments has a diversification strategy to manage this risk.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(f) Market risk (continued)

PSP Canadian Equities Fund – 10 largest holdings

Company Name	Fair Value (\$000's)	% of PSP Canadian Equities Fund
1 Royal Bank of Canada	\$ 382,408	4.9%
2 Manulife Financial Corporation	374,213	4.8
3 Bank of Nova Scotia	339,914	4.4
4 Encana Corporation	316,115	4.1
5 Toronto Dominion Bank	259,690	3.3
6 Canadian Imperial Bank of Commerce	200,764	2.6
7 Talisman Energy Inc.	186,579	2.4
8 Bank of Montreal	170,029	2.2
9 BCE Inc.	169,290	2.2
10 Sun Life Financial Inc.	141,279	1.8
Total 10 largest Holdings	\$ 2,540,281	32.7%

Some of the holdings shown above are held through Indexed Pooled Fund participation.

PSP Foreign Equities Fund – 10 largest holdings

Company Name	Fair Value (\$000's)	% of PSP Foreign Equities Fund
1 Vodafone Group	\$ 74,847	1.4%
2 Royal Dutch Petroleum Company	61,197	1.1
3 United Health Group Inc.	59,801	1.1
4 Citigroup Inc.	59,408	1.1
5 Nextel Communications Inc.	51,897	1.0
6 Tyco International Ltd	49,966	1.0
7 General Electric Company	48,190	1.0
8 Exxon Mobil Corporation	48,094	1.0
9 JP Morgan Chase & Company	45,871	1.0
10 Total SA	45,327	1.0
Total 10 largest Holdings	\$ 544,598	10.7%

Some of the holdings shown above are held through Indexed Pooled Fund participation.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(f) Market risk (continued)

The PSP Fixed Income Fund holds securities invested in Canada as follows:

	Fair Value	% of PSP Fixed Income Fund
	(\$000's)	
Government of Canada	\$ 1,960,170	34.7%
Provincial	1,263,705	22.4
Municipal	23,281	0.4
Corporate	2,105,765	37.3
Cash and Cash Equivalents	296,871	5.2
Total of PSP Fixed Income Fund	\$ 5,649,792	100.0%

Some of the holdings shown above are held through Indexed Pooled Fund participation.

As at March 31, 2005, 47% of the PSP Fixed Income Fund was managed actively with a duration of 4.8 years (a 1% increase in interest rates would result in a decline in the value of the actively managed fixed income securities of 4.8%). The balance of portfolio is managed passively against the SC Bond Universe index. The index has a duration of 6.2 years.

(g) Securities lending

PSP Investments participates in securities lending programs whereby it lends securities it owns to other parties. Any such securities lending requires collateral in cash or high quality debt instruments or shares securities with a fair value equal to no less than 105% of the value of the securities lent. As at March 31, 2005, securities with an estimated fair value of \$1,981.2 million (2004 – \$763.9 million) were loaned out, while securities contractually receivable as collateral had an estimated fair value of \$2,118.4 million (2004 – \$805.9 million).

(h) PSP Private Equity Fund

The PSP Private Equity Fund comprises an interest in a limited partnership with an expected term of 10 years. The fund is managed by a General Partner. Management fees are 2% of the total amount committed to the fund and are paid directly by the fund.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

2. INVESTMENTS (continued)

(i) Real Estate Investments

The PSP Real Estate Fund and PSP Foreign Real Estate Fund comprise real estate-related investments which are owned by either PSP Investments or its wholly-owned subsidiaries and managed by General Partners or external advisors. The underlying investments comprise a diversified portfolio of income-producing properties.

Investment management fees for these real estate investments are generally incurred by the partnerships and funds. Therefore, PSP Investments' gains (losses) on investments are net of those fees.

The underlying real estate exposures by location as at March 31, were as follows:

Location	2005		2004	
	Fair Value (\$000's)	% of total	Fair Value (\$000's)	% of total
Canada	\$ 117,135	27.3%	\$ 74,342	100.0%
United States	300,710	70.1	—	—
Western Europe	9,754	2.3	—	—
Asia	1,472	0.3	—	—
	\$ 429,071	100.0%	\$ 74,342	100.0%

(j) Derivative Financial Instruments

Derivative financial instruments are financial contracts, the value of which is derived from underlying assets or interest or exchange rates.

PSP Investments uses derivative financial instruments to reduce the risk associated with an existing investment or, as an alternative to holding or investing in the underlying asset itself. Derivative financial instruments also assist in the management of financial risks, including interest rate risk and foreign exchange risk.

The following table summarizes PSP Investments derivatives portfolio as at March 31:

Investments	2005		2004	
	Notional Value*	Fair Value	Notional Value*	Fair Value
Equity derivatives				
Swaps	\$ 365,581	\$ 1,314	—	—
Futures	94,987	(436)	—	—
Options	4,597	484	—	—
Currency derivatives				
Forwards	261,695	(2,091)	\$ 374,561	\$ (7,000)
Options	181,475	3,552	785,775	13,294
		\$ 2,823		\$ 6,294

* Notional value represents the amount to which a rate or price is applied in order to calculate the exchange of cash flows and it does not represent the potential gain, loss or net exposure associated with the market or credit risk of such transactions. Rather, it serves as the basis upon which the returns from, and the fair value of the contracts, are determined. All amounts are in Canadian dollars.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

3. OTHER ASSETS

Other assets as at March 31 consist of the following:

(\$000's)	2005	2004
Fixed assets	\$ 2,281	\$ 2,152
Other assets	1,576	887
Real estate receivables	651	—
	\$ 4,508	\$ 3,039

4. FUND TRANSFERS

During the year, PSP Investments received \$3,816.0 million (2004-\$3,695.6 million) of transfers from the three Pension Funds. The transfers result from net current employer and employee contributions to their respective Pension Plan.

The breakdown of the fund transfers for the year ended March 31 is as follows:

(\$000's)	2005	2004
Public Service Pension Fund	\$ 2,825,086	\$ 2,708,522
Canadian Forces Pension Fund	720,665	728,979
Royal Canadian Mounted Police Pension Fund	270,262	258,066
Total fund transfers	\$ 3,816,013	\$ 3,695,567

5. INVESTMENT INCOME

(a) Investment income

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

(\$000's)	2005	2004
Interest – Bearing Investments		
Short-term	\$ 14,572	\$ 4,881
Canadian bonds and debentures	222,613	178,741
	237,185	183,622
Equity Investments		
Canadian equities dividends	113,306	71,819
Foreign equities dividends	84,002	55,602
	197,308	127,421
Real Estate Investments	7,147	1,197
Total interest and dividends	441,640	312,240
Net gain on investments	906,500	2,149,527
Investment income	\$ 1,348,140	\$ 2,461,767

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

5. INVESTMENT INCOME (continued)

(b) Investment income by Asset Class

Investment income by asset class for the year ended March 31, is as follows:

(\$000's)	2005	2004
Asset Class		
Cash Equivalents	\$ 35	\$ 4,881
Fixed Income	245,112	369,396
Canadian Equities	1,012,918	1,275,930
Foreign Equities ¹	83,935	808,064
Real Estate	11,119	3,496
Private Equity	(623)	—
Absolute Return	(4,356)	—
	\$ 1,348,140	\$ 2,461,767

¹ Including foreign currency realized loss of \$15.5 million (2004—realized gain of \$2.0 million) and foreign currency unrealized loss of \$159.4 million (2004—unrealized gain of \$152.3 million)

Derivative contracts are classified by asset-mix category based on the intent of the investment strategies of the underlying portfolios of PSP Investments.

6. INVESTMENT PERFORMANCE

Portfolio and benchmark returns for the year ended March 31 were as follows:

	2005		2004	
	Portfolio Returns	Benchmark Returns	Portfolio Returns	Benchmark Returns
Cash Equivalents	2.9%	2.2%	3.2%	3.0%
Fixed Income	5.0%	4.7%	10.9%	10.8%
Canadian Equities	15.7%	13.9%	36.1%	37.7%
Foreign Equities	1.7%	1.5%	30.7%	28.8%
Real Estate	7.9%	6.7%	3.6%	2.5%
Total Return	7.9%	7.2%	26.1%	25.4%

The total benchmark return aggregates the asset class benchmark returns according to the weights specified in the Investment Policy. The total return includes the impact of the PSP Hedging Fund and the PSP Absolute Return Fund. Returns have been calculated in accordance with the methodology recommended by the CFA Institute. Returns are presented gross of expenses.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

7. EXPENSES

(a) Operating expenses

Operating expenses consist of the following:

(\$000's)	2005	2004
Salaries and benefits	\$ 10,570	\$ 5,582
Professional and consulting fees*	3,046	1,867
Office supplies and equipment	2,461	1,476
Custody	994	460
Occupancy costs	770	729
Depreciation of fixed assets	749	621
Remuneration earned by Directors	536	434
Communication expenses	148	224
Travel and related expenses for Directors	123	177
Other operating expenses	1,396	540
	\$ 20,793	\$ 12,110

* Included in Professional and consulting fees are audit and audit-related fees of \$653,000 (2004 – \$428,000) and non-audit fees of \$21,000 (2004 – Nil) that were paid and accrued to the external auditors of PSP Investments.

Total remuneration earned by Directors in fiscal year 2005 includes 1) an annual retainer of \$98,000 for the Board Chairperson and of \$20,000 for each Director; 2) an annual retainer of \$7,500 for each committee chair; 3) Board meeting fees of \$1,500 per meeting (\$500 for meetings less than one hour); 4) Committee meeting fees of \$1,000 per meeting (\$500 for meetings less than one hour) and 5) a travel time meeting fee of \$1,000 if distance to and from the meeting is greater than 1,000 km from the director's primary residence. Separate fees are not paid for investment committee meetings when they are held as a committee of the whole during Board meetings. The Board Chairperson is not eligible for Board and committee meeting fees.

Directors of PSP Investments come from various regions of the country and accordingly they incur travel and accommodation expenses in attending meetings of the Board and committees.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

7. EXPENSES (continued)

(b) Salaries and benefits

Included in salaries and benefits is compensation earned by executive officers. The total compensation earned during the fiscal year by the executive officers was as follows:

Employee / Position	Year	Base Salary (\$)	Annual Bonus ⁶ (\$)	Long Term Incentive Plan ⁶ (\$)	Benefits ⁷ (\$)	Total Compensation (\$)
Gordon J. Fyfe¹	2005	385,000	454,300	184,800	36,000	1,060,100
President and Chief Executive Officer	2004	188,000	244,000	—	17,000	449,000
André Collin²	2005	221,000	324,000	—	23,000	568,000
First Vice President, Real Estate Investments						
Derek Murphy³	2005	200,000	224,000	—	41,000	465,000
First Vice President, Private Equity	2004	—	—	—	—	—
Pierre Malo⁴	2005	200,000	119,600	—	24,000	343,600
First Vice President and Co-Chair of the Management Investment Committee	2004	65,000	78,500	—	8,000	151,500
Danielle G. Morin⁵	2005	194,000	—	—	28,000	222,000
First Vice President and Chief Financial Officer (CFO)	2004	208,000	144,000	—	29,000	381,000

1 The President and Chief Executive Officer commenced employment on October 9, 2003, and in addition to the above, was awarded a signing bonus of \$450,000 in fiscal year 2004.

2 The First Vice President, Real Estate Investment commenced employment on May 17, 2004.

3 The First Vice President, Private Equity commenced employment on March 31, 2004, and was awarded a signing bonus of \$51,000 in fiscal year 2004. Benefits include an amount for relocation assistance.

4 The First Vice President and Co-Chair of the Management Investment Committee commenced employment on December 8, 2003, and in addition to above, was awarded a signing bonus of \$325,000 in fiscal year 2004.

5 The First Vice President and CFO left PSP Investments on March 15, 2005. The Bonus for fiscal year 2004 includes a special bonus of \$50,000 for being acting CEO.

6 Bonus awards include short-term and long-term components and are based on the achievement of agreed objectives. PSP Investments has modified its program for the short-term and long-term bonus in fiscal year 2005.

7 Benefits include other miscellaneous non-cash remuneration. In addition to the above, the executive officers are covered by a contributory defined benefit pension plan which provides them with a pension benefit of 2% of the best three years average earnings for each year of service. Furthermore, the President and CEO, the CFO and the First Vice President, Real Estate are members of a supplementary executive retirement plan.

8. ALLOCATION OF NET INCOME FROM OPERATIONS

The allocation of the net income from operations of PSP Investments to each Plan Account is as follows:

(a) Investment Income

The investment income has been allocated according to the number of units of PSP funds held by each Plan Account.

Notes to the Consolidated Financial Statements

For the year ended March 31, 2005

8. ALLOCATION OF NET INCOME FROM OPERATIONS (continued)

(b) Expenses

The Act requires that the costs of operation of PSP Investments be charged to the three plans for which it provides investment services. Under section 4(3) of the Act, the President of the Treasury Board shall determine to which Plan Account these costs will be charged in consultation with the Minister of National Defence and the Solicitor General of Canada. An allocation policy has been developed which allocates the direct costs of investment activities, such as external investment management fees and custodial fees, to each Plan Account, and allocates, on a quarterly basis, operating expenses excluding custodial fees, based upon the asset value of each Plan Account.

Operating expenses, excluding custodial fees, have been allocated as follows:

	2005	2004
Public Service Pension Plan Account	71.7%	71.1%
Canadian Forces Pension Plan Account	20.9%	21.3%
Royal Canadian Mounted Police Pension Plan Account	7.4%	7.6%
	100.0%	100.0%

Expenses are paid by PSP Investments by way of an advance from the Public Service Pension Plan Account, which is reimbursed by the other Plan Accounts on a quarterly basis.

9. GUARANTEES AND INDEMNITY

PSP Investments provides guarantees to its directors. Under these agreements, PSP Investments may be required to compensate, without limitation but subject to the Act, these parties for costs incurred, such as claims, actions or litigations. This indemnity is explicitly declared to be in excess and in addition to any indemnity of any policy of insurance purchased and maintained by PSP Investments under the subsection 18 (1) of the Act. To date, PSP Investments has not received any claims nor made any payment for such indemnity.

10. COMMITMENTS

PSP Investments and its subsidiaries have committed to enter into investment transactions which will be funded over the next several years in accordance with agreed terms and conditions. As at March 31, 2005, the outstanding commitments, in funds and real estate-related investments amounted to \$320.7 million (\$26.4 million for private equity investments and \$294.3 million for real estate investments).

Subsequent to March 31, 2005, PSP Investments and its subsidiaries entered into investment transactions which will be funded over the next several years in accordance with agreed terms and conditions. The total commitments resulting from these transactions, in funds and real estate-related investments amounted to \$29.2 million, of which \$9.0 million was paid after year-end.

11. COMPARATIVE FIGURES

Certain comparative figures have been reclassified in order to conform to the current year presentation.

Board of Directors and Investment Committee

BOB BALDWIN

National Director,
Social and Economic Policy
Canadian Labour Congress
Ottawa, Ontario

RICHARD BRADSHAW

Former Chairman
Phillips, Hager & North
Investment Management Ltd
Vancouver, British Columbia

PAUL CANTOR, LL.B., FICB

Chairperson of the Board
Chairman of the Board, Canada
Russell, Reynolds Associates
Toronto, Ontario

JEAN E. DOUVILLE, FCA

President
Schroders Ventures Canada Inc.
Montreal, Quebec

CAROL HANSELL

Partner
Davies Ward Phillips & Vineberg LLP
Toronto, Ontario

JEAN LEFEBVRE, FCIA

Montreal, Quebec

LYNN LOEWEN, CA

Vice President, Finance Operations
Bell Canada
Montreal, Quebec

KEITH G. MARTELL, CA

Chairman of the Board
First Nations Bank of Canada
Saskatoon, Saskatchewan

CARL H. OTTO, CFA

Chairman
Cordiant Capital Inc.
Montreal, Quebec

ANIL K. RASTOGI

Chief Information Officer
McCain Foods Limited
Florenceville, New Brunswick

SUSAN SHERK

Senior Associate, Human Environment
AMEC Earth & Environmental
St. John's, Newfoundland and Labrador

Committees

AUDIT AND CONFLICTS COMMITTEE

Jean E. Douville
Carol Hansell
Lynn Loewen
Keith G. Martell, Chair
Anil K. Rastogi

GOVERNANCE COMMITTEE

Bob Baldwin
Carol Hansell
Lynn Loewen, Chair
Carl H. Otto

HUMAN RESOURCES AND COMPENSATION COMMITTEE

Bob Baldwin, Chair
Richard Bradshaw
Jean Lefebvre
Susan Sherk

Management

GUY ARCHAMBAULT

Vice President, Human Resources

BERNARD AUGUSTIN

Vice President,
Index and Quantitative Investments

ANDRÉ COLLIN

First Vice President,
Real Estate Investments

ASSUNTA DI LORENZO

First Vice President,
General Counsel and Corporate Secretary

GORDON J. FYFE

President & Chief Executive Officer

ASIF HAQUE

Senior Director,
External Manager Search & Monitoring

PIERRE MALO

First Vice President and Co-Chair
of the Management Investment
Committee

DEREK MURPHY

First Vice President, Private Equity

JOHN VALENTINI

First Vice President and
Chief Financial Officer

CATALIN ZIMBRETEANU

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