BANK OF CANADA
BANQUE DU CANADA

2011 ANNUAL REPORT

bankofcanada.ca

The *Annual Report* is available on the Bank of Canada's website at **bankofcanada.ca**.

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BANK OF CANADA
BANQUE DU CANADA

Mark Carney
Governor – Gouverneur

29 February 2012

The Honourable James M. Flaherty, PC, MP
Minister of Finance
140 O'Connor Street
21st Floor
Ottawa, Ontario
K1A 0G5

Dear Minister,

In accordance with the provisions of the Bank of Canada Act, I am submitting the Bank of Canada's *Annual Report* for the year 2011 and the Bank's audited financial statements as at 31 December 2011.

Yours sincerely,

The Bank's Compass

As a public institution and a workplace, we take our bearings from our commitment to Canadians, to excellence and to one another.

Our commitment to Canadians

To promote the economic and financial welfare of Canada, we

- conduct monetary policy in a way that fosters confidence in the value of money
- promote the safety and efficiency of Canada's financial system
- supply quality bank notes that are readily accepted and secure against counterfeiting
- provide efficient and effective funds-management services
- communicate our objectives openly and effectively and stand accountable for our actions

Our commitment to excellence

Building on our strengths, we aim to meet our commitment to Canadians through performance that is second to none among the central banks of the world.

We strive for excellence through leading-edge research and analysis, through partnerships within the Bank and with outside organizations, and through

- innovation in all aspects of our work
- leadership that spurs us on to new success
- integrity in our business and in our actions
- diversity of people and ideas

Our commitment to one another

We aim to achieve our best in a workplace where we

- communicate clearly and openly
- share knowledge and experience
- develop our talents and careers
- recognize those who live up to our commitments
- respect one another and our lives outside work

Contents

Message from the Governor

2011 was a challenging year for the global economy as it marked the end of a decades-long process of steadily increasing leverage in advanced economies. The resulting market volatility, risk aversion, fiscal austerity and declining confidence prompted central banks in major advanced economies to expand the frontiers of unconventional monetary policy.

Amid this global turbulence, Canada's macroeconomic policy framework has stood us well. All of the economic output and the jobs lost during the last recession have been recovered, and private domestic demand is now higher than its pre-crisis peak. To support Canadian economic growth in the face of serious headwinds from abroad, the Bank of Canada provided considerable monetary policy stimulus in 2011, maintaining its policy interest rate at the exceptionally low rate of 1 per cent throughout the year.

The Bank sets monetary policy consistent with achieving the 2 per cent inflation target over the medium term. Although one-off factors briefly pushed total CPI inflation above the Bank's 1 to 3 per cent inflation-control range, underlying inflation pressures remained well contained throughout 2011, and inflation expectations well anchored.

Periods of economic uncertainty underline the importance of maintaining the Bank's credibility and clearly communicating its policy priorities, tools and tactics. Monetary policy works most effectively when Canadians understand what the Bank is doing and why. 2011 provided us with many opportunities to engage Canadians on our monetary policy goals and actions. The Bank's Governing Council mounted an intensive program of outreach events, speeches and media appearances.

One of the most significant decisions during 2011 was the renewal of the inflation-targeting agreement with the Government of Canada, to the end of 2016. The target continues to be 2 per cent total CPI inflation, the midpoint of a 1 to 3 per cent inflation-control range. A clear, credible inflation target is the cornerstone of a monetary policy framework that has served Canada exceptionally well. Inflation has averaged very close to 2 per cent over the past 20 years, and the standard deviation of inflation has fallen by roughly two-thirds. In other words, inflation has become low, stable and predictable.

As a result, Canadians have benefited in a number of important ways. An improved inflation environment has allowed consumers and businesses to manage their finances with greater certainty about the future purchasing power of their savings and income. Interest rates have also been lower in both nominal and real terms across a range of maturities. More broadly, low, stable and predictable inflation has helped to encourage more stable economic growth in Canada and lower and less-variable unemployment.

The experience since the last renewal of the inflation-control agreement in 2006 has underscored these benefits, especially the relative stability of Canada's economy during the recent global economic and financial crisis, the largest in 75 years.

The inflation-targeting framework remains flexible: the most appropriate time horizon for returning inflation to target will vary depending on the nature and persistence of the shocks buffeting the economy. Properly deployed, this flexibility reduces output volatility and the possible buildup of financial imbalances. This flexibility is possible because of the Bank's credibility and its demonstrated success in keeping inflation low, stable and predictable.

During 2011, the Bank increased its involvement in international and domestic efforts to strengthen the global financial system. In the international arena, the Bank worked with the federal government and partner agencies to help to advance international regulatory reform, especially with regard to the Basel III capital and liquidity requirements for banks. Other areas of focus have been global liquidity, market-based financing and the development of central counterparties for over-the-counter derivatives.

Domestically, Bank staff were working with federal and provincial partners and market participants to develop more robust market infrastructure for repo, fixed-income and over-the-counter derivatives products. The Bank made significant progress toward improving the processes and systems that support Government of Canada debt auctions and other domestic market operations. We believe these initiatives will significantly enhance the resilience of the Canadian financial system over the medium term.

In a rapidly evolving environment, the Bank continued to improve its assessment and communication of risks to the stability of the Canadian financial system. Risks were judged to be high and to have increased in the second half of 2011 as the European sovereign debt crisis worsened and the global economic outlook weakened. Domestically, the high and rising debt loads of Canadian households continued to be a significant vulnerability.

One of the Bank of Canada's main functions is to serve as fiscal agent for the Government of Canada. During 2011, in that role, the Bank implemented the government's new medium-term debt strategy and helped to develop and begin operation of the government's prudential liquidity plan, assuring the government's ability to meet its payment obligations, even during periods of market stress.

The most tangible product of the Bank's work passes through the hands of Canadians every day—our bank notes. In 2011, I had the honour, along with the Minister of Finance and the Commissioner of the Royal Canadian Mounted Police, to unveil Canada's next generation of bank notes. This series is the first in Canada to be printed on a polymer material. The security features in the new notes are a significant advance in the Bank's ongoing efforts to deter counterfeiting. These notes are more economical, lasting at least 2.5 times longer than conventional cotton-based paper notes. At the end of their lifespan, they will be recycled in Canada, making them greener as well. The $100 note was issued in November 2011. The $50 note will be issued this spring, while the $20 note will begin circulating in late 2012. The $10 and $5 denominations will be issued by the end of 2013.

During 2011, the Bank undertook several initiatives to ensure that it is well positioned to fulfill its mandate in the years to come. These efforts included new split operations of critical functions and further development of a detailed plan to renew the aging infrastructure at the Bank's head office complex. The Bank also implemented its new total compensation program to help the Bank recruit and retain the talent it needs.

It is imperative that we continuously improve the efficiency and effectiveness of our operations. In 2011, the Bank completed a Corporate Effectiveness Program to ensure that we could continue to invest in the people, infrastructure and research needed to deliver on our objectives while also respecting the federal government's guidance to hold operational spending at 2010 levels through 2012. As part of this program, difficult decisions were made that resulted in the reduction of about 7 per cent of the Bank's workforce. Where possible, these reductions occurred through retirements, the elimination of vacant positions and normal attrition. I commend my colleagues for the professionalism with which they managed this process, and I am grateful for the ongoing commitment of the Bank's dedicated staff during this challenging exercise.

2011 was a year in which economic and financial policies were tested around the world. The trying times and market turmoil fuelled intense debates on the role of governments and central banks. In periods such as this, it is easy to lose focus. We have not done so.

The Bank will continue to conduct monetary policy to keep inflation low, stable and predictable so that Canadian households and firms can invest and plan for the future with confidence. We will carry on our work with the federal government and other regulatory agencies to ensure that Canada's financial system remains resilient and efficient in bad times as well as good. We will continue to issue bank notes that Canadians can use with confidence. Finally, we will be prudent managers of the Government of Canada's debt and foreign exchange assets, and of our own operations.

This *Annual Report* is a testament to the Bank's work in 2011 to fulfill its ongoing mandate to promote the economic and financial well-being of Canadians. We are confident that the bold policy initiatives and clear-sighted managerial decisions we have taken in 2011 will serve us well as we face the challenges and opportunities ahead.

Mark Carney

Governor

The Year at a Glance

- The Canadian economy grew at a moderate pace and inflation expectations remained well anchored in 2011, despite the challenging and uncertain global economic environment.
- The Bank renewed its inflation-control agreement with the Government of Canada for an additional five-year period, maintaining the inflation target at 2 per cent.
- The Bank made a significant contribution to international regulatory reform in 2011, notably with regard to the development of the Basel III capital and liquidity requirements for banks.
- The Bank made progress in establishing more resilient financial market infrastructure, both in Canada and globally.
- Confidence in bank notes remained high in 2011, and the level of counterfeiting remained well below the Bank's target of 50 parts per million.
- With the issuance of the $100 note in November, a new series of more secure and longer-lasting bank notes printed on polymer was launched in 2011.
- The Bank collaborated with the federal government in the development and implementation of the government's prudential liquidity plan, ensuring that the government can meet its financial obligations even during periods of market stress.
- The Bank completed the implementation of its new total compensation program with a view to strengthening its ability to attract and retain the talent it needs.
- Operational resilience was strengthened through improvements made to the Bank's data centres and backup recovery site.

The Bank in 2011

The Bank of Canada's Mandate

The Bank of Canada Act is the Bank's legislative framework, which sets out its governance structure as well as its mandate to "promote the economic and financial welfare of Canada."

The Bank strives to meet this mandate through its work in four core areas of responsibility:

Monetary policy. The Bank contributes to solid economic performance and rising living standards for Canadians by keeping inflation low, stable and predictable. Since 1991, the Bank's monetary policy actions toward this goal have been guided by a clearly defined inflation target.

Financial system. The Bank promotes a stable and efficient financial system in Canada and internationally. To this end, the Bank oversees Canada's key payment, clearing and settlement systems; acts as lender of last resort; assesses risks to financial stability; and contributes to the development of financial system policies.

Currency. The Bank designs, produces and distributes Canada's bank notes and replaces worn notes. It deters counterfeiting through leading-edge bank note design, public education and collaboration with law-enforcement agencies.

Funds management. The Bank provides effective and efficient funds-management services for the Government of Canada, as well as on its own behalf and for other clients. For the government, the Bank provides treasury-management services and administers and advises on the public debt and foreign exchange reserves. In addition, the Bank provides banking services to foreign central banks, as well as to critical payment, clearing and settlement systems.

The Medium-Term Plan

To meet its mandate in a changing environment, the Bank develops a medium-term plan every three years. The current plan, *Achieving Excellence Together*, sets priorities for the 2010–12 period (available on the Bank's website: About the Bank>Management and corporate governance).

The plan sets out the key priorities for each of the Bank's four main functions: monetary policy, financial system, currency and funds management. At the corporate level, the plan also identifies three main priorities for 2010–12:

(i) **Conducting leading research and policy analysis**. To improve its capacity to respond to increasingly complex challenges in the economy and the financial system, the Bank conducts research and analysis to enhance its policy frameworks and strengthen its contributions to international discussions of economic and financial policy issues. Important areas of focus in 2011 were to complete the Bank's research agenda on the monetary policy framework, and to continue research and analysis of issues concerning system-wide financial stability.

(ii) **Strengthening business resilience and infrastructure.** The Bank must be able to carry out its critical business functions, even during disruptions such as power outages and pandemic alerts. To that end, the Bank will continue to increase the resilience and robustness of its business-continuity arrangements, notably by implementing "split operations" and pursuing plans to house the Bank's primary and secondary data centres. The Bank is also renewing its infrastructure by updating key elements of its head office complex and by refining its information technology strategy.

(iii) **Attracting, retaining and engaging quality staff.** In response to demographic trends, an increased need for specialized skills and changing labour markets, the Bank is focused on attracting, retaining and engaging staff. The Bank has renewed its total compensation strategy and is strengthening its talent-acquisition and career-development programs, promoting leadership effectiveness, improving the management of information, and refining its succession-planning strategy.

In 2010, the Bank launched a Corporate Effectiveness Program to ensure that it could achieve its priorities while being consistent with federal guidelines to contain expenditures and hold operational spending at 2010 levels through 2012. Information on the impact of this program in 2011 can be found in Our People and Work Environment (page 14), as well as in Management's Discussion and Analysis (page 26).

Key Achievements

Monetary Policy

Experience has shown that the most important contribution that monetary policy can make to the economic welfare of Canadians is to keep inflation low, stable and predictable. Since 1991, the Bank's monetary policy actions toward this objective have been guided by a clearly defined inflation-control target. In 2011, this target was renewed by the Bank and the Government of Canada for another five years.

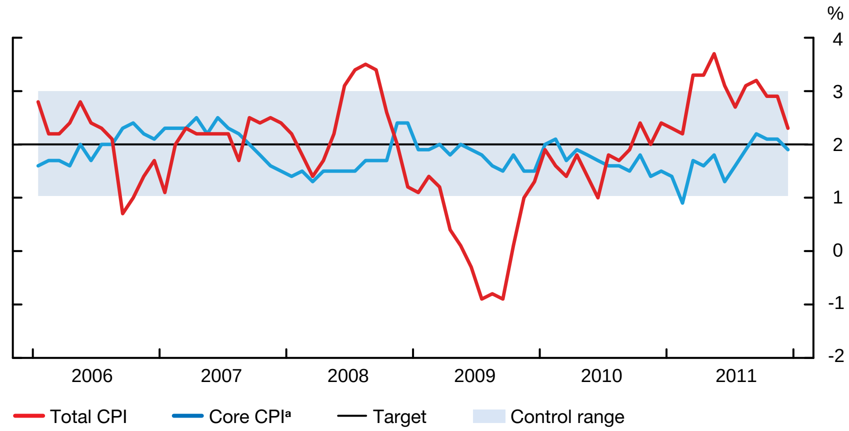
Monetary policy decisions must be forward looking. They rely importantly on the current analysis, forecasting and research activities of the Bank's economists, as well as on information drawn from external sources. Given the structure of Canada's economy, analysis of the external environment plays an important role in monetary policy decision making. In 2011, a weak recovery in the United States and the sovereign debt crisis in Europe posed serious challenges for the Canadian economy. In this context, the Bank maintained its policy rate at 1 per cent throughout the year, keeping considerable monetary policy stimulus in place. Detailed economic analysis and explanation of the Bank's monetary policy is published quarterly in the *Monetary Policy Report*.

Key Achievements in 2011

- The Canadian economy continued to grow at a moderate pace and inflation expectations remained well anchored, despite the challenging and uncertain global economic environment.
- Total CPI inflation, boosted by increases in energy and food prices and by base-year effects related to the introduction of the harmonized sales tax (HST) in Ontario and British Columbia in July 2010, temporarily exceeded the upper bound of the 1 to 3 per cent inflation-control range (**Chart 1**). Core inflation, however, remained close to 2 per cent throughout the year.

Chart 1: Total CPI inflation temporarily exceeded the upper bound of the inflation-control range; however, core inflation remained close to 2 per cent throughout the year

Year-over-year percentage change, monthly data



a. Consumer price index excluding eight of the most volatile components and the effect of changes in indirect taxes on the remaining components

Source: Statistics Canada

Last observation: December 2011

- The Bank's inflation-control agreement with the Government of Canada was renewed for five years, ending 31 December 2016. The inflation target continues to be 2 per cent, the midpoint of the 1 to 3 per cent inflation-control range, with inflation defined as the 12-month rate of change in the total CPI (**Box 1**).
- In support of the renewal of the inflation-control agreement, the Bank completed an ambitious multi-year research effort to examine potential improvements to its monetary policy framework.
- The Bank enhanced the analytic tools it uses to support monetary policy, with a focus on improving its analysis of the linkages between the financial sector and the real economy.
- The Bank continued to play an important role in international forums in 2011 by advancing the G-20 Framework for Strong, Sustainable and Balanced Growth, leading discussions on reform of the international monetary system and conducting research on the determination of commodity prices.

Box 1

Renewal of the Inflation-Control Agreement

In November 2011, the Bank renewed its inflation-control agreement with the Government of Canada for an additional five-year period ending 31 December 2016. The inflation target remains at 2 per cent, the midpoint of a 1 to 3 per cent control range, and it will continue to be defined in terms of the 12-month rate of change in the total CPI.

The effectiveness of Canada's inflation-targeting regime is well established. Since 1995, when Canada adopted a 2 per cent inflation target, inflation has averaged close to 2 per cent, and its variability has fallen by roughly two-thirds compared with the previous two decades. Canadians have benefited from low, stable and predictable inflation in a number of important ways:

- consumers and businesses have enjoyed greater certainty about the future purchasing power of their savings and income;
- nominal and real interest rates have been lower; and
- Canada has experienced more stable economic growth and lower, less-variable unemployment.

The relative stability of Canada's economy during the recent global economic and financial crisis underscored the benefits of flexible inflation targeting. The crisis of 2008–09 was larger than any shock the Canadian economy had previously experienced under inflation targeting, putting the regime to an unprecedented test. The value of the framework and its inherent flexibility were clearly demonstrated during this period.

A multi-year research program informed the renewal of the target. This research focused on three issues:

- **The optimal level of the target.** While the prospective benefits of a lower inflation target may be greater than previously estimated, recent experience points to important risks associated with the zero lower bound on interest rates.
- **The relative merits of a price-level target (PLT).** It is not clear that the theoretical advantages of PLT in providing for greater long-term price-level certainty and greater short-term macroeconomic stability would outweigh the costs and risks of moving away from the current framework.
- **The extent to which monetary policy should take financial stability considerations into account.** While not the first or even the second line of defence, monetary policy might—in exceptional circumstances—be an appropriate tool to support financial stability. A framework anchored on a solid and credible inflation target provides the flexibility for monetary policy to play this exceptional role.

The Bank will continue its research into potential improvements to the monetary policy framework over the course of the agreement period.

Additional information about inflation targeting and the renewal of the inflation-control target can be found on the Bank's website (Monetary Policy>Inflation).

The Bank of Canada's Fellowship Program

The Bank of Canada's Fellowship Program helps to foster excellence in research and analysis and to develop partnerships with experts outside the Bank in areas important to its mandate. Through this program, two research awards are available for academics working at Canadian universities.

The **Fellowship Award** is designed to recognize established researchers in Canada and is granted for a five-year term. In 2011, the recipients of this award were Professor Randall K. Morck of the University of Alberta and Professor Gregor W. Smith of Queen's University. Professor Morck's current research focuses on the behaviour of financial institutions, the associated linkages between the financial sector and the macroeconomy, and how these linkages affect monetary policy. Professor Smith's current research relates to econometric work on labour force participation decisions, portfolio models and behavioural perspectives on financial decisions.

The **Governor's Award** recognizes outstanding academics at a relatively early stage in their careers and is granted for a two-year period. The 2011 recipient of the Governor's Award was Professor Thorsten V. Koeppl of Queen's University. Professor Koeppl's current research examines various aspects of the stability of financial markets that operate without formal trading and clearing arrangements, such as over-the-counter markets.

Additional details about the Fellowship Program, as well as a list of current and previous recipients of Fellowship and Governor's awards, can be found on the Bank's website (Publications and Research>Research>Fellowship Program).

Financial System

The Bank promotes the stability and efficiency of Canada's financial system by providing liquidity; overseeing key domestic payment, clearing and settlement systems; participating in the development of financial system policies in Canada and globally; and assessing and communicating risks to the overall stability of the financial system. The Bank shares responsibility for the stability of the financial system with other federal financial regulatory authorities. Ultimately, the Minister of Finance is responsible for the sound stewardship of the financial system.

In 2011, the four major challenges were: (i) internationally, to advance the comprehensive G-20 program of reforms to strengthen the resilience of the global financial system; (ii) to implement these reforms in Canada, notably with regard to financial system infrastructure; (iii) to assess the evolution of risks to the stability of the financial system in light of changing economic and financial conditions; and (iv) to remain ready to implement an appropriate policy response in the event that risks materialized.

Key Achievements in 2011

- The Bank contributed significantly to the advancement of international regulatory reform in 2011, especially with regard to the Basel III capital and liquidity requirements for banks. It participated actively in key international forums, including the Financial Stability Board, the Committee on the Global Financial System, the Basel Committee on Banking Supervision, and the Committee on Payment and Settlement Systems. The Bank also participated in many international working groups and committees, making important contributions to reports on global liquidity; market-based financing (i.e., shadow banking); access arrangements for central counterparties for over-the-counter (OTC) derivatives; the system-wide effects of liquidity regulation; and a framework for identifying global systemically important banks.

- In collaboration with its partners, the Bank contributed to strengthening financial market infrastructure in Canada and globally. To implement the G-20 commitment to reform OTC derivatives markets, Bank staff helped to design arrangements for the central clearing of OTC derivatives at the global level, and examined policy options for Canada with a view to informing a decision in 2012. The Bank worked with the Canadian Derivatives Clearing Corporation and market participants to develop central counterparty services for the Canadian repo and fixed-income markets to ensure that new services offered meet applicable international standards.
- In a challenging environment, the Bank strengthened its monitoring and communication of risks to the stability of the Canadian financial system. The Bank judged that the overall level of risk was high and had increased markedly in the second half of 2011, owing primarily to an escalation of the sovereign debt crisis in the euro area and a weaker outlook for the global economy. The main source of domestic risk was judged to be the elevated levels of household debt, which make this sector vulnerable to adverse shocks. Risk assessments were communicated in the *Financial System Review* and in numerous speeches by members of the Bank's Governing Council.
- The Bank strengthened its tools and analytic framework for assessing system-wide risks and vulnerabilities. Notable accomplishments in 2011 were developing and applying a framework to assess the system-wide impact of shocks that might occur and refining the analysis of household vulnerabilities.
- The Bank made significant progress toward improving the processes and systems that support government debt auctions and other domestic market operations.

The Financial Stability Board

The Financial Stability Board (FSB) is an international agency dedicated to building a more resilient and efficient global financial system.[1] It coordinates the work of national financial authorities and international standard-setting bodies, and develops and promotes the implementation of effective regulatory, supervisory and other financial sector policies.

On 4 November 2011, Bank of Canada Governor Mark Carney was named Chairman of the FSB. The appointment, for a term of three years, was confirmed by G-20 leaders at their summit in Cannes, France. Mr. Carney will remain Governor of the Bank of Canada during his chairmanship of the FSB.

As the Chairman, Mr. Carney committed to strengthen the FSB's capacity and governance, as mandated by the G-20 leaders, and to work closely with national authorities and international agencies to coordinate and monitor the implementation of the G-20's comprehensive financial reform program. The FSB provides a system-wide perspective on this program.

Information about the Financial Stability Board, including a list of its members, can be found at financialstabilityboard.org.

1 The FSB was established in 2009 as the successor to the Financial Stability Forum (FSF), which included the G-7 finance ministers, central bank governors and prudential regulators. In April 2009, at the G-20 summit in London, England, it was announced that an expanded FSF was to be re-established as the Financial Stability Board with a broadened mandate to promote financial stability.

Currency

The Bank of Canada is responsible for supplying Canadians with bank notes that they can use with confidence. The Bank has a four-part strategy to maintain that confidence: (i) developing bank notes that are difficult to counterfeit and easy to authenticate; (ii) increasing the routine verification of bank notes by retailers; (iii) promoting the deterrence of counterfeiting by law-enforcement agencies and prosecutors; and (iv) ensuring a focus on quality throughout the life cycle of a bank note—from production to efficient distribution to the withdrawal of worn and obsolete notes for destruction and replacement.

In 2011, a key priority for the currency function was the launch of the next generation of bank notes, the first Canadian note series to be printed on a polymer material. The security features in the new notes are a significant advance in the Bank's ongoing efforts to deter counterfeiting.

The demand for bank notes continued to rise in 2011, roughly in line with the growth of the economy. At year-end, there were 1.95 billion bank notes in circulation, little changed from 2010. However, the total value of bank notes outstanding increased by $3.2 billion to $61.0 billion.

In the 2010–12 medium-term plan, the Bank set a target of 50 counterfeits detected annually for each million genuine bank notes in circulation. Counterfeiting in 2011 was well below this target, and confidence in Canadian bank notes, as measured by surveys of retailers and the public, remained strong.

Key Achievements in 2011

- All milestones for introducing the next generation of bank notes were met. The first two designs for the *Polymer* series were unveiled in June and the new $100 note was issued in November. Development of the $50 and $20 notes was completed and preparations began for the issue of these denominations in 2012. In support of the new series, extensive communications, education and public awareness activities were undertaken across the country (**Box 2**).
- Counterfeiting remained low in 2011. At 34 parts per million (compared with 35 ppm in 2010), the number of counterfeits detected for each million notes in circulation was well below the target (**Chart 2**). The $2.6 million face value of the counterfeits detected in 2011 was little changed from 2010 (**Chart 3**).
- The Bank played a leadership role in international collaborative groups such as the Central Bank Counterfeit Deterrence Group (a group of 32 central banks); the Four Nations Group (Australia, Canada, England and Mexico); and the Reproduction Research Centre (an anti-counterfeiting laboratory operated by central banks).

Box 2

New *Polymer* Series

Celebrating Canada's Achievements at the Frontiers of Innovation

The Bank of Canada's new *Polymer* series of bank notes is more secure, more economical and better for the environment than the *Canadian Journey* series it is replacing.

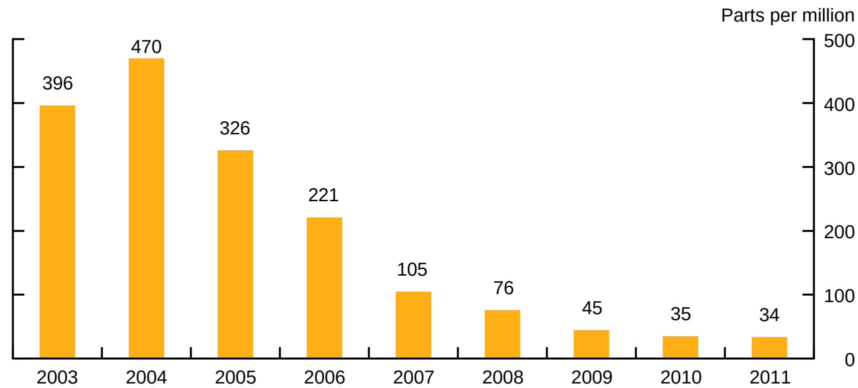
The bank notes, which celebrate Canada's achievements in innovation, represent a significant technical advance in design and security. The new polymer notes contain leading-edge security features that make them difficult to counterfeit but easy to verify. For example, a large transparent area that extends from the top to the bottom of the note contains complex holographic features that can be viewed from both sides. As well, these new notes will last at least 2.5 times longer than cotton-based paper notes, and will be recycled when they are removed from circulation.

The first denomination—the $100 note—was issued in November 2011. The $50 note will be issued in March 2012, and the $20 note will begin circulating in late 2012. The $10 and $5 denominations will be issued by the end of 2013.

In advance of the issue, the Bank worked closely with financial institutions and the manufacturers of bank note equipment to support a smooth transition to the new polymer notes. The entire cash-processing system needed to be ready to work with polymer. Each time a new series is issued, the equipment that accepts, processes or dispenses bank notes must be adapted by financial institutions, cash processers, retailers and other entities that accept bank notes. In addition, since the unveiling of the *Polymer* series in June 2011, Bank staff across the country have been training cash handlers and police officers on how to check the security features of the new notes.

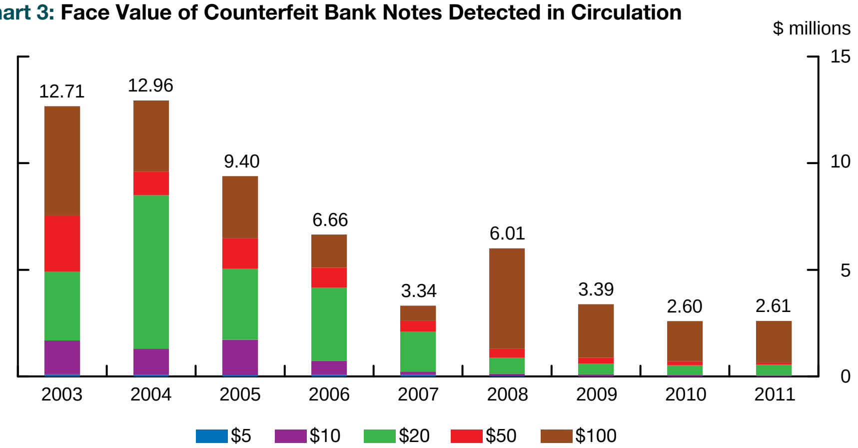
The Bank won an award for the Best Currency Public Education Program of 2011 from the International Association of Currency Affairs for these public awareness initiatives, in particular, an educational video showcasing the new $100 note.

Chart 2: Number of Counterfeit Bank Notes Detected Per Million Notes in Circulation[a]



a. Medium-term plan target for 2010–12: 50 ppm

Chart 3: Face Value of Counterfeit Bank Notes Detected in Circulation



Funds Management

As the federal government's fiscal agent and banker, the Bank administers and advises on the government's debt and reserves. The Bank also works with the Department of Finance to develop principles, policies and programs for managing the federal government's borrowing and investment programs. The Bank's goal is to provide fiscal-agent and related banking services effectively and efficiently within a strong risk-management framework.

In 2011, Government of Canada cash balances held at the Bank of Canada and with other financial institutions averaged $8.1 billion, compared with $13.5 billion in 2010, with the decrease primarily due to the residual effects of the unwinding of special liquidity facilities. Total official international reserves of the Government of Canada were US$66 billion in 2011, compared with US$57 billion in 2010. These reserves are managed by the Bank on behalf of the government.

The Bank also manages the risks associated with its own balance sheet, and manages and administers the assets held by its employee pension fund. In addition, the Bank undertakes banking activities on behalf of other central banks and international organizations, and provides banking services to financial institutions and designated payment, clearing and settlement systems.

Key Achievements in 2011

- The Bank collaborated with the federal government to develop and begin implementation of the government's prudential liquidity plan, which will help to ensure that the government can meet its financial obligations even during periods of market stress.
- In collaboration with the federal government, the Bank continued to make the Canada Savings Bonds program more efficient and identified opportunities to further reduce program costs.
- The Bank implemented the Government of Canada's new medium-term debt strategy, which will improve the cost-risk characteristics of the debt and reduce refinancing risk for the government.
- The framework for managing the credit risk associated with Canada's official international reserves was strengthened, and significant progress was made in the development of an asset-allocation model that will enhance the management of these reserves.
- Staff research and two conferences hosted by the Bank provided insight into the effects of liquidity policies and regulatory reforms on the infrastructure of payment, clearing and settlement systems.
- The Bank's critical payment and settlement operations ran smoothly, with no serious outages.

Unclaimed Balances

When a Canadian bank account has been inactive for 10 years and the relevant financial institution has been unable to contact the owner, the assets of the account are transferred to the Bank of Canada.

If you think that you (or someone you know, living or deceased) may have money in a forgotten account, you can go to the Bank of Canada's website, type "unclaimed balances" in the search box, and use the tool provided to see whether such an account exists. The Bank is currently the custodian of more than 1 million of these accounts, which have a total value of $466.6 million.

Owners of these accounts can claim their money if they are able to provide proof of ownership. In 2011, the Bank received 26,463 inquiries about unclaimed balances, and released more than $15.5 million of this money to the rightful owners.

Our People and Work Environment

The Bank relies on highly talented staff to fulfill its responsibilities. Most of the Bank's 1,228 staff work at the head office in Ottawa; about 10 per cent are located at operations centres in Montréal and Toronto, and in regional offices in Vancouver, Calgary, Toronto, Montréal, Halifax and New York.

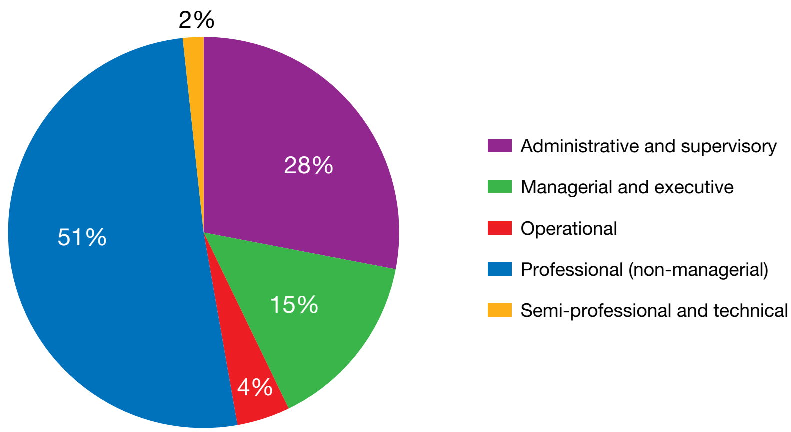
Bank staff come from a wide variety of professional and operational backgrounds and are recruited from across Canada and internationally (**Chart 4**). The Bank has an active university recruitment program for economists and financial sector specialists. In 2011, 37 employees were hired through this program.

In 2011, the Bank completed the implementation of its new total compensation program. This was a priority for the current medium-term plan, and it will help the Bank recruit and retain the talent it needs. Total compensation is anchored to the median of relevant markets of comparison. Key changes include the introduction of wider salary ranges to allow for the recognition of special skills and competencies, as well as a faster response to changing market conditions, and a separate salary scale for economists and financial sector specialists to reflect more directly the challenges of hiring for these groups.

Learning and development continue to be a priority for the Bank. In 2011, $2.7 million was dedicated to the continuous development of employees' skills and knowledge.

Information about working at the Bank, as well as a list of current job postings, can be found on the Bank's website at Careers.

Chart 4: Composition of Bank Staff, by Role



The Bank's Staff in 2011

The Bank's key resource is its people. The Bank is a knowledge-based institution, with many of its resources dedicated to research and analysis to support the formulation and implementation of policy in each of the four core functions. The Bank requires a significant number of highly skilled professionals to achieve its objectives.

In 2010, the Bank launched a Corporate Effectiveness Program to ensure that medium-term plan priorities would be met while holding operational spending at 2010 levels through 2012, consistent with federal government guidelines. As part of this program, plans were made for process and service changes that were expected to result in the reduction of 80 to 95 positions. This plan was implemented in 2011, with reductions occurring where possible through normal attrition and the ending of temporary positions. Employees whose positions were eliminated were supported with a transition package.

The Bank continued to hire in areas where specialized skills and knowledge are required, and the work environment remained positive. A staff turnover rate of less than 5 per cent and a sizable portion of staff moving to new roles as a result of promotions and temporary assignments are two indications of the Bank's healthy work environment (see **Table 1** and **Box 3**).

Table 1: Workforce Indicators

	2009	2010	2011
Number of regular employees	1,311	1,305	1,228
Average years of service for regular employees	13.1	12.8	12.6
Number of regular employees hired	119	69	47
Number of internal job changes for regular employees	283	277	214
Turnover rate for regular employees (per cent)	4.2	4.9	4.6

Box 3

Work Environment Checkup

Maintaining a superior work environment remains a priority for the Bank. Every three years, the Bank surveys its staff on how they view their work environment in order to assess strengths as well as areas for improvement. The survey covers more than 30 measures of employee engagement—from learning and development to compensation, workload and communications. In 2011, 85 per cent of Bank staff responded to the survey—in itself, evidence of a high level of employee engagement.

Survey results showed that the overall engagement index had improved since 2008, and placed the Bank above industry benchmarks. The survey helps guide plans for further improving the Bank's work environment.

Top 100 Employers in Canada

The Bank was named one of Canada's Top 100 Employers for 2012 based on an assessment of its work practices, policies and communications.

See eluta.ca/top-employer-bank-of-canada.

Public Education: Count on Us

The Bank has a variety of educational material on its website, including print and video resources that explain the work of the Bank, programs to teach students about money, and audience-specific resources for learning about bank notes and counterfeiting.

In 2011, the Bank launched a short video, *Count on Us*, in which Governor Mark Carney and eight Bank staffers explain how the Bank meets its responsibilities.

To view the video, go to the Bank's website: About the Bank > Who we are > Videos about the Bank.

Key Corporate Priorities for 2012

The Bank of Canada sets annual work priorities with reference to both its medium-term plan and the changing environment. The Bank's main priorities for 2012 are as follows:

Conducting leading research and policy analysis

- improve understanding of the linkages between the financial system and the real economy and their implications for monetary policy
- continue analysis of policy options in a low interest rate environment
- strengthen the monitoring of financial system risk, especially in a context of global fragility
- contribute to the domestic and international reform of financial regulation, particularly with regard to market-based financing and financial market infrastructure
- extend the Bank's analysis of the international monetary system and of the evolution of global imbalances
- continue research and policy analysis to improve the funds-management services provided to the government
- increase understanding of the digital alternatives to cash as a means of payment, and the policy and operational implications that could arise from greater use of these alternatives

Strengthening business resilience and infrastructure

- improve business resilience by migrating critical data to a new primary data centre and by concluding a program to improve processes and systems supporting domestic market operations
- strengthen the Bank's infrastructure by finalizing plans for the renewal of the head office complex

Attracting, retaining and engaging talented staff

- improve the process for hiring staff with specialized skills and redeveloping the Bank's intranet to enhance internal communication

Finally, an additional key corporate priority for 2012 is to issue the $50 and $20 denominations and complete the development of the $10 and $5 denominations in the new *Polymer* series of bank notes.

Financial Highlights

Table 2 below presents highlights of the Bank's 2011 financial statements and shows comparative figures for the previous four years. The statements themselves, as well as detailed explanation and commentary, are found in Management's Discussion and Analysis. Further information about the Bank's balance sheet is available on the Bank's website.

Table 2: Financial Statement Highlights
Millions of dollars

	Value at 31 December				
	2011	2010[a]	2009[b]	2008[b]	2007[b]
Total assets* and *Total liabilities and equity	**64,247**	61,216	71,355	78,584	53,897
Significant Financial Statement items					
Loans and receivables	**1,531**	2,087	25,377	37,234	4,002
Investments	**62,424**	58,767	45,989	41,023	49,679
Bank notes in circulation	**61,029**	57,874	55,468	53,731	50,565
Deposits	**2,481**	2,557	15,550	24,413	2,981
Comprehensive income					
Revenue	**1,607**	1,543	1,710	2,228	2,292
Expenses	**353**	381	366	376[c]	268
Other comprehensive income (loss)	**(179)**	(122)	(76)	58	23
Comprehensive income	**1,075**	1,040	1,268	1,910	2,047

a. Comparative figures have been restated in accordance with International Financial Reporting Standards (IFRS).
b. Comparative figures are reported in accordance with Canadian Generally Accepted Accounting Principles (GAAP).
c. The increase in expenses from 2007 to 2008 was primarily due to costs incurred by the Bank for retail debt services, costs that had previously been recovered from the Department of Finance.

The Bank's balance sheet increased by 5 per cent in 2011 compared with 2010. However, the balance sheet is substantially smaller than it was in 2008 and 2009 when, in response to the global financial crisis, the Bank provided extraordinary liquidity to the financial system, principally by means of term purchase and resale agreements (PRAs). Only one term PRA was outstanding at 31 December 2011, and was issued for general balance-sheet-management purposes.

Bank notes are the principal liability on the Bank's balance sheet. The value of bank notes in circulation increased by 5.5 per cent in 2011, roughly in line with the growth of nominal GDP.

Revenue growth of about 4 per cent in 2011 is mainly attributable to increased yields on government securities. This year-over-year growth in revenue reversed the trend from 2007 to 2010 of declining revenue, which was attributable to decreasing yields on government securities. The decrease in expenses in 2011 of about 7 per cent is attributable to reduced staff, technology and premises costs.

Expenses, by Function

The Bank's 2011 expenses, by function, are shown in **Chart 5** and **Table 3**.

Chart 5: Expenses, by Function

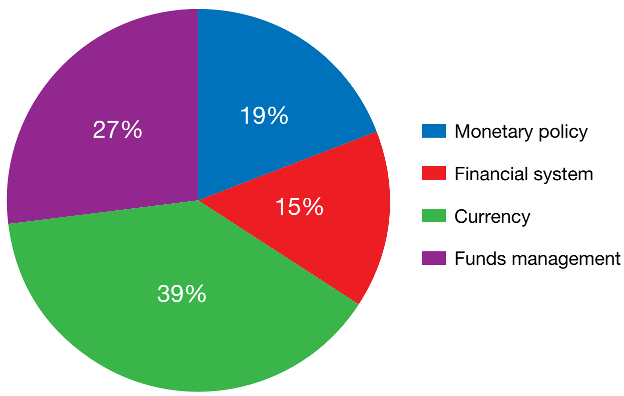
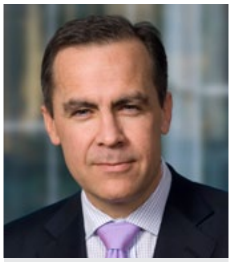


Table 3: Expenses, by Function
Millions of dollars

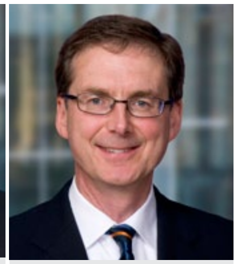
	2011	2010
Monetary policy	68.3	72.8
Financial system	51.0	52.6
Currency	137.1	145.5
Funds management	96.7	109.9
Total expenses	353.1	380.8

The costs associated with the currency function, which represent the largest share of the Bank's total expenses (39 per cent of the total), include the costs associated with the production of bank notes.

Board of Directors and Management of the Bank



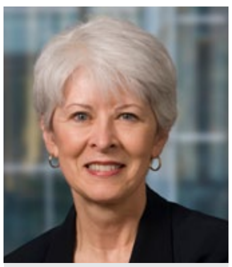
Mark Carney[6*]
Governor,
Chairman of the Board



Tiff Macklem[6, 7*]
Senior Deputy Governor

William Black[1, 6]

Philip Deck[3, 5]



Bonnie DuPont[3*, 4, 6]

Douglas Emsley[2, 5*, 6]

Jock Finlayson[3, 4, 8]

Carol Hansell[2, 3]

Brian Henley[5, 7]

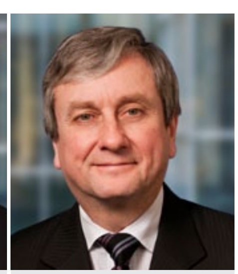
Daniel Johnson[2, 4*]

David Laidley[2*, 4, 5, 6]

Leo Ledohowski[3, 5]

Richard McGaw[4, 7]

Michael O'Brien[2, 7]



Michael Horgan[6]
Deputy Minister
of Finance,
Member ex officio

1. Lead Director
2. Member of Audit and Finance Committee
3. Member of Human Resources and Compensation Committee
4. Member of Corporate Governance Committee
5. Member of Capital Projects Committee
6. Member of Executive Committee
7. Member of Pension Committee
8. Chair of the Fellowship Nominating Committee

* Indicates committee chair

Role of the Board

Under the statutory governance framework established in the Bank of Canada Act, the Governor is the Chief Executive Officer of the Bank and Chair of its Board of Directors. The Governor has specific authority and responsibility for the business of the Bank, notably with respect to the formulation and implementation of monetary policy, the provision of fiscal-agent services to the government, the issuance of bank notes, the provision of liquidity to the financial system, and oversight of Canada's major clearing and settlement systems as set out in the Payment Clearing and Settlement Act.

The Board of Directors provides general oversight of the management and administration of the Bank with respect to strategic planning, financial and accounting matters, risk management, human resources, and other internal policies. The Board and the Governor work in close co-operation, since the oversight of financial and administrative matters by the Board is important to the conduct of the business of the Bank by the Governor.

The Board and the Bank regularly review and consider the relevant best practices of other public institutions, central banks and private sector organizations with a view to continuously improving and achieving excellence in the Bank's corporate governance.

Board Composition and Activities

The Board is composed of the Governor, the Senior Deputy Governor and 12 independent directors appointed for three-year renewable terms by the Governor in Council (the Cabinet). The Deputy Minister of Finance is an ex officio, non-voting member of the Board. The Board and its committees meet regularly throughout the year in accordance with a schedule determined in consultation with management and the directors.

The Board and each of its committees have adopted written terms of reference setting out their various responsibilities, as well as the responsibilities of the committee chairs. The Board and each committee agree on written work plans before the beginning of the calendar year.

Board Committees and Activities

The Board has established the following standing committees to enable it to carry out its responsibilities effectively:

- The **Audit and Finance Committee**, chaired by David Laidley, oversees the financial affairs of the Bank, including its medium-term plan, annual budget and expenditures, as well as the activities of the Bank's internal and external auditors. During 2011, the committee oversaw the Bank's transition to International Financial Reporting Standards and the transition to new quarterly reporting standards issued by Treasury Board.
- The **Human Resources and Compensation Committee**, chaired by Bonnie DuPont, provides Board oversight with respect to the Bank's human resources policies and practices, compensation policies, succession planning and senior executive performance, as well as, subject to approval by the Governor in Council, the compensation of the Governor and the Senior Deputy Governor.
- The **Corporate Governance Committee**, chaired by Daniel Johnson, is responsible for the oversight of the Bank's corporate governance practices, including annually assessing the Board's effectiveness, and reviewing both the composition of committees and the terms of reference of the Board and its committees.

- The **Pension Committee**, chaired by the Senior Deputy Governor, Tiff Macklem, is responsible for advising the Board regarding the Bank's responsibilities as sponsor and administrator of the Bank of Canada pension plan, including plan investment policies, plan administration, communication and stakeholder relations. The committee is composed of three independent directors, three members of management and the Senior Deputy Governor. Any quorum of the committee must include at least two independent directors. In 2011, a Pension Plan Governance Review was conducted. While the Review confirmed that the governance of the pension plan met current standards, a number of recommendations were made to enhance governance oversight, which are currently being implemented.
- The **Capital Projects Committee**, chaired by Douglas Emsley, provides Board oversight for significant capital projects being undertaken by the Bank. During 2011, the committee's primary focus was the Bank's plans for the renewal of its head office complex in Ottawa. A final decision with respect to the renewal plan is expected in 2012.

In addition, the Bank of Canada Act provides for an Executive Committee to act in the place of the Board. The Executive Committee met twice in 2011, in March to receive its regular annual report from the Human Resources and Compensation Committee regarding senior staffing matters, and in July to receive an in-depth economic briefing from senior management (all Board members are invited to this meeting).

With respect to the Bank's Fellowship Program, management has requested that an independent director act as Chair of its Nominating Committee. That post is currently held by Jock Finlayson. Highlights of this year's Fellowship Program are provided in the Monetary Policy section of this *Report*.

Meetings and Attendance

In 2011, the Board met eight times; the Executive Committee, twice; the Audit and Finance Committee, eight times; the Corporate Governance Committee, four times; the Capital Projects Committee, seven times; the Human Resources and Compensation Committee, five times; and the Pension Committee, five times. Attendance data are available on the Bank's website: About The Bank>Management and Corporate Governance>Board of Directors.

Board Independence

Since the Governor is both Chairman of the Board of Directors and Chief Executive Officer, the independent (non-management) directors elect a Lead Director to represent their interests and act as a link between them and the Governor. The Board has adopted written terms of reference outlining the Lead Director's responsibilities. William Black was re-elected as Lead Director for a further two-year term, which ends in September 2012.

As well, both the Board and its committees regularly hold sessions without management or non-independent directors present. Each committee of the Board, except the Pension Committee, consists solely of independent directors. The Audit and Finance Committee meets privately on a regular basis with the co-auditors, the Chief Internal Auditor and the Chief Accountant. The Board and its committees have the right to retain independent advisers at the Bank's expense.

Board Effectiveness and Education

The Board regularly conducts a self-assessment of its effectiveness by means of a survey that solicits directors' views on various aspects of the Board's operations, governance and effectiveness. New directors are provided with comprehensive orientation briefings when they join the Board. The Board regularly examines its education requirements and receives training on matters pertinent to its duties.

Each year, the Board holds a meeting outside of Ottawa and uses the opportunity to gain an understanding of local concerns and to explain the Bank's policies. In 2011, the meeting was held in Vancouver.

In addition, the Board received its regular briefing, which occurs every second year, from senior staff of the International Monetary Fund's Western Hemisphere Department.

Director Compensation

Independent directors are paid within the ranges established under the *Remuneration Guidelines for Part-Time Governor in Council Appointees in Crown Corporations* administered by the Privy Council Office. During 2011, directors were paid an annual retainer of $8,000 and an additional $625 per diem for attendance at each Board meeting and committee meeting of which the director was a member. An additional annual retainer of $3,000 was paid to each director serving on the Executive Committee. Each director who chairs a committee of the Board was paid an additional retainer of $1,000 except for the Chair of the Corporate Governance Committee, who was paid an additional $2,000. In his role as Chair of the Nominating Committee of the Fellowship Program, Mr. Finlayson was paid on a per diem basis.

In addition, all independent directors are reimbursed for travel, accommodation and meal expenses incurred while attending meetings of the Board, its committees, or other Board-related events. The Governor, the Senior Deputy Governor and the Deputy Minister of Finance receive no compensation with respect to their duties as members of the Board.

Management of the Bank

The Governing Council is the Bank's policy-making body. It consists of the Governor, the Senior Deputy Governor and four Deputy Governors, and is responsible for monetary policy, decisions aimed at promoting a sound and stable financial system, and the strategic direction of the Bank.

Governing Council (*left to right*): Tiff Macklem, Senior Deputy Governor; Agathe Côté, Deputy Governor; Timothy Lane, Deputy Governor; Mark Carney, Governor; John Murray, Deputy Governor; Jean Boivin, Deputy Governor

The Management Council provides leadership and guidance on strategic management issues and corporate policies, as well as oversight of all Bank operations. Chaired by the Senior Deputy Governor, the Council consists of two Deputy Governors, two Advisers, the General Counsel and Corporate Secretary, and the Chief of Financial Services, who is also the Chief Accountant.

In 2011, the Chiefs' Committee was created to streamline Bank decision-making processes by strengthening the partnership between departments that share responsibilities for developing and executing common responses to corporate issues. The Committee is composed of the Chiefs of all Bank departments and the Director of Human Resources.

The Bank is organized into 12 departments: Audit, Canadian Economic Analysis, Communications, Corporate Services, Currency, Executive and Legal Services, Financial Markets, Financial Services, Financial Stability, Funds Management and Banking, Information Technology Services, and International Economic Analysis.

Risk Management—Highlights

Managing risk is an important element of management's oversight responsibilities. It encompasses the management of not only financial, but also business and enterprise risks. The Bank has a well-established framework for identifying, managing and monitoring these risks.

Risk Monitoring and Reporting

Each year, through the Bank's self-assessment process, senior managers identify and assess the key risks that could compromise the fulfillment of the Bank's responsibilities and the achievement of its strategic objectives. Approaches for managing these risks are identified, and quarterly assessments are made of the likelihood of the risks occurring and of their potential consequences. The preliminary results of the assessments are discussed with the Management Council to incorporate its views and perspective. Semi-annual risk reports are presented to and discussed with the Board of Directors.

The Audit Department conducts periodic reviews of Bank operations, including the Bank's risk-management process, to assess the appropriateness and effectiveness of the systems of internal control put in place by management to mitigate risk, and thus to provide reasonable assurance that the Bank's objectives will be achieved.

The Chief Risk Officer works closely with management to analyze changes in the environment that could affect the level of risk associated with each of the key risk areas, as well as to identify emerging risks. Deputy Governors and Department Chiefs are responsible to the Governor and Senior Deputy Governor for the management of risk in their respective areas of responsibility. As part of its ongoing monitoring, Management Council reviews any significant changes in the levels of risk or new risks, and reports these changes to the Board of Directors.

The Bank's Risk Profile

The Bank's risk profile largely reflects the challenges and uncertainties in the external and internal environments that are judged to persist over the short to medium term. The key areas of risk facing the Bank are financial risk, business risk and enterprise risk. Ineffective management of these risk areas could have an impact on the Bank's reputation, leading to a loss of confidence in the Bank's ability to fulfill its responsibilities.

Financial risk, which includes credit, liquidity and market risk, is associated with the management of the Bank's assets and liabilities. As fiscal agent of the Government of Canada, the Bank also manages the financial risk associated with the government's financial assets and liabilities. The financial risk associated with the management of the government's foreign exchange reserves is mitigated by means of a comprehensive framework that matches assets and liabilities and sets out strict criteria regarding credit and collateral.

Business risk in the areas of monetary policy, financial system and funds management arises from a number of sources, including uncertainties in the global economy and the international financial system. To mitigate these risks, the Bank has well-defined policy frameworks and an extensive body of research to guide its analysis and policy decisions, and it participates in key international forums and collaborates with other major central banks and financial sector regulatory partners. To mitigate the implementation risks related to the new *Polymer* series of bank notes, the Bank has detailed execution plans and works closely with external stakeholders.

Enterprise risks relate to: (i) staffing (for example, demographic changes and other challenges in attracting and retaining qualified staff); (ii) project execution, relating to the number of large, complex initiatives under way; and (iii) the Bank's arrangements for continuity of operations. To mitigate these key areas of risk, the Bank is strengthening its human resource programs, its project-management and reporting framework, and its continuity-of-operations capacity.

Additional details regarding the Bank's management of risk can be found on page 33 in the Management's Discussion and Analysis section.

Management's Discussion and Analysis

This Management's Discussion and Analysis (MD&A) is to be read in conjunction with the audited financial statements of the Bank of Canada (the Bank) and accompanying notes for the year ended 31 December 2011.

The Bank develops and implements policy within its mandate, specifically in relation to its four core functions: monetary policy, the financial system, currency and funds management.

The activities and operations of the Bank are not undertaken with the intention to generate revenue or profits and cannot be fully captured in a discussion of the financial statements. While the Bank strives to provide sufficient disclosure of its activities in its financial statements, those statements alone do not permit a full understanding of the Bank's activities. Additional details and perspectives concerning the full range of the Bank's policy activities are provided in this *Annual Report*.

The Bank's Operating Environment

The Business and Mandate of the Bank

The Bank of Canada began operations in 1935 as the nation's central bank. It is now a Crown corporation, wholly owned by the Government of Canada through the Minister of Finance, and governed by the Bank of Canada Act (the Act). The Act describes the Bank's legislative and governance framework, as well as its broad mandate to "promote the economic and financial welfare of Canada." The Bank of Canada is not a commercial bank and does not offer banking services to the public.

Understanding the Bank's Financial Results

Although the Bank's activities are not driven by profit-maximization objectives, its assets and liabilities, as well as its revenues and expenditures, support one or more of its functional mandates.

The Bank has the exclusive right to issue Canadian bank notes. The face value of these bank notes is recorded as a liability on the Bank's Statement of Financial Position (balance sheet). The Bank issues bank notes to financial institutions, which then credit the Bank with the face value of the bank notes. The proceeds are used immediately to purchase Government of Canada securities (treasury bills and bonds) that appear as assets on the Bank's balance sheet. The Bank acquires these securities on a non-competitive basis at auctions and structures its holdings to broadly reflect the composition of the federal government's stock of nominal domestic marketable debt.

Interest income derived from these Government of Canada securities is the Bank's primary source of revenue. The income generated from the assets backing the bank notes in circulation (net of bank note production and distribution costs) is referred to as "seigniorage." Other sources of revenue include interest earned on lending facilities and deposits and dividends received from the Bank for International Settlements (BIS).

A portion of the Bank's income is used to fund its operations. The balance of this income, subject to agreed reserves and deductions, is remitted to the Receiver General for Canada on a biweekly basis. This amount was $1.1 billion in 2011.

In addition to generating income, Government of Canada securities are used to support the Bank's monetary policy and financial system functions. The following sections describe how the operations of the Bank's four core functions relate to its financial results.

Monetary Policy

The Bank's monetary policy actions are guided by a clearly defined inflation-control target, which is set out in a written agreement with the Government of Canada. This agreement was renewed in 2011 for a five-year term, and establishes the inflation target as the 2 per cent midpoint of the 1 to 3 per cent inflation-control range.

The following table describes the relationship between the Bank's conduct of monetary policy and its balance sheet.

Tool used by the Bank	Impact on the Bank's financial results
The target for the overnight rate is the main tool used by the Bank to conduct monetary policy. Direct-clearing members of the Canadian Payments Association (CPA) can hold deposits with the Bank and earn interest at the target rate minus 25 basis points, or take collateralized advances at the target rate plus 25 basis points.	The Bank normally targets $25 million in net settlement balances but will adjust this amount as warranted to provide required liquidity to the financial system. The Bank of Canada can supply virtually unlimited amounts of these deposits to participants. See the Financial System section below for details on the impact of settlement balances on the Bank's financial statements.
When required, the Bank offers term purchase and resale agreements and sale and repurchase agreements to maintain the overnight rate close to the target.	These agreements are recorded as collateralized lending transactions in *Loans and receivables* or as collateralized borrowing transactions in *Other liabilities* on the Statement of Financial Position at the amounts at which the securities were acquired or sold, plus accrued interest.
Receiver General cash balances are invested through an auction process with participating financial institutions that is administered by the Bank.	Receiver General cash balances held at the Bank appear on the Statement of Financial Position as *Deposits—Government of Canada*.

Financial System

The Bank promotes the stability and efficiency of the Canadian financial system by: (i) providing liquidity; (ii) overseeing key domestic payment, clearing and settlement systems; (iii) participating in the development of financial system policies in Canada and globally; and (iv) assessing and communicating risks to the overall stability of the financial system.

The Bank's financial assets are used to support the financial system function, as described below.

Services provided by the Bank		Impact on the Bank's financial results
Settlement balances	Participants in the Large Value Transfer System use claims on the Bank to settle net payment obligations among direct participants.	Settlement balances appear as *Deposits—Members of the Canadian Payments Association* and as *Advances to members of the Canadian Payments Association* on the Statement of Financial Position.
Standing Liquidity Facility	Advances to financial institutions at a rate of 25 basis points above the target rate are routine under this facility. The framework for the target overnight interest rate provides an incentive for financial intermediaries to allocate liquidity among themselves without having to make significant use of the Bank's deposit facilities and collateralized advances.	These advances appear on the Statement of Financial Position as *Advances to members of the Canadian Payments Association*. Interest on these advances is included in the Bank's Statement of Comprehensive Income.
Securities-lending program	The Bank operates a securities-lending program to support the efficiency of the market for Government of Canada securities by providing a temporary, secondary source of securities. When specific Government of Canada treasury bills or bonds are in short supply in the secondary market and are trading below a predetermined threshold interest rate, the Bank will lend up to 50 per cent of its holdings in these securities on an overnight basis in exchange for other securities.	Securities-lending transactions are fully collateralized by securities. The securities loaned by the Bank continue to be accounted for as assets. Lending fees are recorded in *Other revenue* in the Statement of Comprehensive Income.
Securities purchased or sold under repurchase agreements	In the normal course of managing the Bank's balance sheet, the Bank needs to undertake repurchase operations from time to time. These assets are typically acquired to offset seasonal flows of bank notes, but can be used for other temporary purposes.	These agreements are recorded as collateralized lending transactions in *Loans and receivables* or as collateralized borrowing transactions in *Other liabilities* on the Statement of Financial Position at the amounts at which the securities were acquired or sold, plus accrued interest. Interest received is recorded in the Bank's Statement of Comprehensive Income.
Emergency Lending Assistance (ELA)	The Bank has the ability to provide emergency lending assistance to a financial institution requiring short-term liquidity. (The last such event was in 1986.)	ELA would appear as a collateralized loan of the Bank; the interest received would be recorded in the Bank's Statement of Comprehensive Income.

Currency

The Bank is the exclusive issuer of bank notes in Canada. It is responsible for supplying Canadians with bank notes that they can use with confidence and without concerns about counterfeiting. The Bank has been issuing bank notes since 1935 and periodically introduces new series that incorporate the most up-to-date security features. In November 2011, the Bank began issuing a new series of polymer bank notes that include a number of unique features designed to make them difficult to counterfeit and easy to verify.

Currency item	Impact on the Bank's financial results
Bank notes in circulation liability	Bank notes in circulation is the largest expense item on the Bank's Statement of Financial Position. This liability tends to increase over time with the growth in demand for bank notes and is subject to important seasonal variations (typically reaching its lowest level at the end of the first quarter and peaking in the second and fourth quarters around holiday periods).
Bank note production	The costs of producing bank notes are expensed as the bank notes are produced and received in finished form by the Bank. The raw materials purchased by the Bank for the production of notes are recorded as raw material inventory on the Bank's balance sheet until they are used in note production.

Funds Management

The Bank manages the investments and liabilities that are reported on its balance sheet, as well as the investments held by its pension fund (which are held and maintained in a pension trust separate from the Bank).

In addition, the Bank provides funds-management services for the Government of Canada and for other central banks and international organizations, including securities settlement and custodial services, as well as custodial services for gold. Assets held under custody agreements do not appear as assets on the Bank's Statement of Financial Position; however, fees earned for these services are included in the Bank's income. Settlement accounts held on behalf of other central banks and international organizations appear on the Statement of Financial Position as *Deposits—Other deposits*.

The Bank's fiscal-agent responsibilities relating to the management of public funds are presented below.

Responsibility	Role of the Bank	Impact on the Bank's financial results
Government banker and treasury manager	To manage the accounts of the Receiver General, through which almost all money collected and spent by the government flows, and to ensure that there are sufficient funds in these accounts to meet the government's daily requirements and to invest any surplus in term deposits.	Amounts are recorded as *Deposits—Government of Canada* on the Statement of Financial Position.
Foreign exchange reserves	Canada's official international reserves are held in the Exchange Fund Account, which the Bank manages on behalf of the Government of Canada. Unlike many central banks, the Bank does not hold foreign exchange reserves on its balance sheet, and holds only minimal foreign cash balances.	None. The foreign reserves are reported by the government in the Public Accounts of Canada and do not appear in the Bank's financial statements. The expenses associated with the provision of these fiscal-agent services are part of the Bank's expenses. No fees are earned for these services.
Debt management	The Bank advises the Department of Finance on the efficient management of the public debt (treasury bills and bonds) and sells the securities at auction to financial market distributors. The Bank advises the Department of Finance on the government's retail debt program (consisting of Canada Savings Bonds and Canada Premium Bonds). The Bank also administers the program (including operations and system support services, accounting, and sales and marketing initiatives).	None. The debt liabilities are reported by the government in the Public Accounts of Canada and do not appear within the Bank's financial statements. The costs associated with the provision of these fiscal-agent services are part of the Bank's expenses. No fees are earned for these services.

The Bank's Expenses, by Function

The expenses reported in the Bank's annual financial statements are reported by type of expense. These expenses are also presented on a functional basis (see note 16 to the financial statements). A complete analysis of these expenses is also included in the Financial Discussion section of this *Report*. The Bank's 2011 expenses by function are shown in the accompanying table and chart.

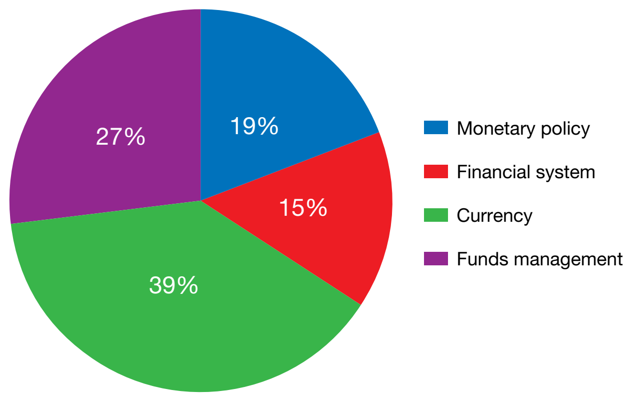
The costs associated with the currency function represent the largest portion of the Bank's expenses (39 per cent), because this item includes the costs incurred in the production of bank notes.

The Bank allocates expenses to each of its core functions on the following basis:

- Directly attributable expenses are charged to the function (including salaries and benefits, other operating expenses, and depreciation).
- Overhead costs, including information technology services and facilities services, are allocated on the basis of identified drivers, including LAN IDs and rentable square footage.
- Strategic initiatives and project costs are allocated to the business area that is responsible for the initiative.
- Remaining overhead costs are allocated on the basis of an allocation model that is established at the beginning of each medium-term plan.

Expenses, by Function
(Millions of dollars)

	2011	2010
Monetary policy	68.3	72.8
Financial system	51.0	52.6
Currency	137.1	145.5
Funds management	96.7	109.9
Total expenses	353.1	380.8



Capability to Deliver Results

Management Structure and Leadership

The Bank has identified the following key management personnel as being responsible for planning, directing and controlling the Bank: the Board of Directors, the Governing Council and the Management Council. The following table outlines the composition and responsibilities of the Bank's key management.

Board of Directors	Governing Council	Management Council
The Governor, Senior Deputy Governor and 12 independent directors[1] (the Deputy Minister of Finance is an ex officio, non-voting member).	The Governor,[2,3] Senior Deputy Governor,[2,4] and the four Deputy Governors	The Senior Deputy Governor, two Deputy Governors, the Chief Accountant, the General Counsel and Corporate Secretary, and two Advisers
The Board oversees the management and administration of the Bank, including strategic planning and risk management, finance and accounting, human resources, and other internal policies.	Members of Governing Council are collectively responsible for monetary policy, the financial system and the strategic direction of the Bank.	The Management Council provides leadership and guidance on strategic management issues and corporate policies, as well as oversight of all Bank operations.

1. Directors are appointed by the Governor in Council for three-year renewable terms.
2. Appointed by the Board of Directors with the approval of the Governor in Council for a term of seven years
3. The term of the Governor, Mark Carney, expires on 31 January 2015.
4. The term of the Senior Deputy Governor, Tiff Macklem, expires on 1 July 2017.

Under the statutory governance framework established in the Bank of Canada Act, the Governor is both Chief Executive Officer of the Bank and Chair of its Board of Directors. The Governor has specific authority and responsibility for the business of the Bank. The Senior Deputy Governor is the alternate to the Governor and *de facto* Chief Operating Officer.

The salaries of the Governor and the Senior Deputy Governor are set by the Board of Directors on advice from its Human Resources and Compensation Committee, within the guidelines established by the Privy Council Office, and are subject to the approval of the Governor in Council. As stipulated in Section 6(3) of the Bank of Canada Act, these salaries do not include any performance-based element. The Governor and Senior Deputy Governor also receive benefits available to all Bank employees, including participation in the Bank of Canada Registered Pension Plan and health and dental benefits.

People

The Bank's key resource is its people. As a knowledge-based institution, with many of its resources dedicated to research and analysis to support the formulation and implementation of policy in each of its four core functions, the Bank requires a significant number of highly skilled professionals to achieve its objectives.

In 2011, the Bank completed the implementation of its new total compensation package, with a view to strengthening its ability to attract and retain the talent it needs, in line with one of the objectives in the current medium-term plan. This approach to total compensation is performance based, and aims to ensure that the Bank's compensation package is competitive with relevant markets. Details about the Bank's staff are presented in the following table.

Human resources statistics

Number of employees	1,228 regular and 235 term or contract employees
Languages	831 (67.7 per cent) are bilingual (English/French)
Locations	1,085 (88.4 per cent) located at head office in downtown Ottawa and the operations centre in suburban Ottawa 102 (8.3 per cent) located at operations centres in Toronto and Montréal 41 (3.3 per cent) located at regional offices in Vancouver, Calgary, Toronto, Montréal, Halifax and New York

Tangible and Intangible Assets

The Bank's head office complex, located in downtown Ottawa, is its principal tangible capital asset. This facility consists of two major elements—the original building that was completed in 1938 and two adjoining towers connected by an atrium, which were designed by Arthur Erickson and completed in 1979.

A principal activity set out in the current medium-term plan is the development and planning associated with a Head Office Facilities Renewal Program with the objective of renovating or significantly repairing the interior components of the head office complex. In 2009, under the oversight of its Board of Directors, the Bank began to assess the condition of the building and to examine various options. In 2011, a number of alternatives for the renewal of the building were examined. In 2012, the Bank will further refine its cost estimates with a view to identifying a preferred renewal option.

Intangible assets are identified as non-monetary assets without physical substance. The Bank's intangible assets consist primarily of computer software that is developed internally or acquired externally. The Bank owns no other significant non-monetary assets.

Liquidity and Capital

Liquidity

Given the Bank's ability to create virtually unlimited quantities of settlement balances (see the table in the Monetary Policy section on page 27), its operations are not constrained by its cash flow or by its holdings of liquid assets, and its seigniorage income is predictable and greatly exceeds its expenses.

Capital

The Bank's primary capital includes $5 million of authorized capital and a $25 million statutory reserve.

The Bank's *Other comprehensive income* includes fluctuations in the fair value of the available-for-sale assets and actuarial gains and losses on the Bank's post-employment benefit plans. If, at any time, the cumulative net unrealized losses exceed the amount of the Bank's capital base of $30 million, the Bank would report a capital deficiency. To eliminate this risk, the Bank has the following agreements and reserves in place.

Description of agreements and reserves		**Value at 31 December 2011**
Memorandum of Understanding with the Department of Finance	The Memorandum of Understanding with the Department of Finance allows the Bank to deduct from its remittances to the Receiver General and hold within retained earnings an amount equal to unrealized losses on available-for-sale assets, unrealized actuarial losses on post-employment benefit plans and other unrealized or non-cash losses.	$188 million
Special reserve	The Bank of Canada Act authorizes the Bank to create a special reserve in order to offset any unrealized valuation losses arising from changes in the fair value of the Bank's available-for-sale assets. This reserve is currently $100 million but may be increased by the Board of Directors to a maximum of $400 million. Management and the Board review the adequacy of this reserve annually.	$100 million
Actuarial gains reserve	The actuarial gains reserve was established upon the Bank's transition to International Financial Reporting Standards at an initial amount of $119.7 million. Since its inception, this reserve has been reduced to nil by actuarial losses recognized on the Bank's post-employment defined-benefit plans.	$nil
Available-for-sale reserve	Available-for-sale assets comprise Government of Canada treasury bills and the Bank's investment in the BIS. Fair-value changes are reported in *Other comprehensive income* and are accumulated within the reserve for available-for-sale assets. The reserve consists primarily of the fair-value change in the Bank's investment in the BIS.	$294.6 million

Deferred employee benefit plans

The Bank sponsors a funded defined-benefit pension plan (supplemented by a defined-benefit supplementary pension arrangement) and other unfunded benefit plans. As reported in note 14 to the financial statements, the Bank had a funded net pension asset of $15.4 million and an unfunded non-pension benefit plan obligation of $164.7 million at 31 December 2011 ($165.1 million asset and $149.9 million obligation at 31 December 2010).

The Registered Pension Plan had a deficiency on a solvency basis[1] at 1 January 2011, and this deficiency is expected to increase at 1 January 2012, largely as a result of low returns on plan assets and low interest rates. The Bank has been conducting annual actuarial valuations since 2008 and has been making additional contributions toward eliminating the solvency deficit within five years. Since 2009, the Bank has contributed $141.3 million to the pension plan.

The funding requirements of the deferred employee benefit plans are determined by actuarial funding valuations on a going-concern basis[2] and depend on a number of factors, including actual returns on plan assets, long-term interest rates, plan demographics, and applicable regulations and actuarial standards. The Bank's estimated funding requirement for 2012 is $65.5 million, which consists of $32.6 million in regular contributions to cover current service costs and $32.9 million toward the elimination of the solvency deficit within five years.

Systems and Processes

The Bank relies upon a number of information technology systems that support its functions. A primary objective of the current medium-term plan is to strengthen business resilience and infrastructure. To attain this objective, the Bank is undertaking a number of significant projects.

Project	Multi-year estimate[a]	Cost capitalized in 2011	Benefits to be achieved
Currency operations: implement three critical applications for bank note inventory	$12.1 million	$7.2 million	Replace aging legacy systems and provide for consolidated reporting of bank note inventories, inventory-management systems and management-control processes in advance of the full release of the new polymer bank note series.
Financial market operations: replace legacy systems that support liquidity provision, auction, treasury-management and collateral-management activities	$30.7 million	$10.9 million	Provide functionality to address operational risks and business requirements not available with the current legacy systems.
Economic and financial analysis: develop new software architecture and functionality	$9.5 million	$4.0 million	Enhance the Bank's capabilities to analyze data and provide data warehousing, and implement data-management solutions for economic and financial analysis.
Information technology: improve IT infrastructure	$14.5 million	$2.8 million	Upgrade obsolete network components, improve performance and reduce the risk of system failures.
Enhanced business continuity: split critical business operations and house the Bank's data centres	$60.5 million	$23.2 million	Enhance the Bank's resilience with respect to the operations of critical payment, clearing and settlement systems, and the location and resilience of its data centres.

a. Includes estimates for both capital and operating expenditures.

1. The solvency basis assumes that the plan would be wound up on the valuation date.
2. The funding or going-concern basis assumes that the plan will continue to operate indefinitely and, at 1 January 2011, the plan was in a surplus on a going-concern basis. Assumptions are based on a long-term perspective and relate to such items as interest rates, inflation rates, salary increases, retirement rates and mortality rates.

Risk

Risk-Management Framework and Strategy

Since it was first developed in the late 1990s, the Bank's risk-management framework has evolved by incorporating best practices relevant to its operations and activities. The Bank keeps abreast of best practices through its contacts at major central banks, public sector organizations and financial institutions, as well as by examining the evolution of well-established risk-management frameworks.[3]

Risk Self-Assessment Process

Through the self-assessment process, senior managers from across the Bank identify and assess the key risks for each function—monetary policy, the financial system, currency, funds management and corporate administration—that could compromise the fulfillment of the Bank's responsibilities, and the achievement of its strategic objectives and desired outcomes as set out in the medium-term plan. The broad categories of risk assessed are financial, business and enterprise risks. Ineffective management of these areas of risk could have an impact on the Bank's reputation, leading to a loss of confidence in the Bank's ability to fulfill its responsibilities.

Each function identifies the approaches in place for managing the risk for each key risk area. Taking into account the risk-mitigation strategies, quarterly assessments are then made of the likelihood of the risks occurring and the potential consequences. The preliminary results of the assessments are shared with the Management Council to incorporate its views and perspectives. Semi-annual risk reports that present the priority risk areas and risk-mitigation measures are discussed with the Board of Directors. To elaborate on the key areas of risk, briefings for each of the functions are also presented to the Board of Directors during the course of the year.

Risk Monitoring and Reporting

The Chief Risk Officer works closely with management to assess changes in the environment that could affect the level of the risks associated with each of the key risk areas and to identify emerging risks. Deputy Governors and Department Chiefs are responsible to the Governor and Senior Deputy Governor for the management of risk in their respective areas of responsibility. As part of its ongoing monitoring, the Management Council reviews any significant changes in the levels of risk or new risks, and reports these changes to the Board of Directors.

In order to provide reasonable assurance that objectives will be achieved, the Audit Department conducts periodic reviews of the Bank's operations, including its risk-management process, to assess the appropriateness and effectiveness of the risk-mitigation systems in place.

3. These frameworks include: ISO 31000: Risk Management Standard (2009); COSO (Committee of Sponsoring Organizations of the Treadway Commission—American Institute of Certified Public Accountants, American Accounting Association, Financial Executives International, the Institute of Internal Auditors, and the Institute of Management Accountants); AS/NZS 4360:2004—the Australia New Zealand Standard 2004 for Risk Management.

The Bank's Risk Profile

The Bank's risk profile largely reflects the short- to medium-term challenges and uncertainties in the external and internal environments that are likely to persist. The following summary identifies the key areas of risk facing the Bank. The following section outlines the measures undertaken to manage these risks.

Residual risk ratings	
Acceptable: Appropriate risk management is already in place.	●
Cautionary: Active monitoring and/or enhanced risk-mitigation processes are not fully implemented.	▲
Serious concern: Immediate and significant strengthening of risk-mitigation processes is required, as well as active monitoring and reporting to senior management and the Board of Directors.	■

Risks	Ratings at 31 December	
	2011	2010
Financial risks		
Credit: The Bank's investment portfolio is subject to credit risk, or the risk that a counterparty will fail to discharge its obligations in accordance with agreed-upon terms. The maximum exposure to credit risk is the carrying amount of the portfolio. This is offset by collateral taken in accordance with the Bank's publicly disclosed policies. Credit risk is assessed as low because the Bank's securities are primarily direct obligations of the Government of Canada.	●	●
Market: The Bank is exposed to market risk largely through its available-for-sale investments, including Government of Canada treasury bills and the Bank's investment in the BIS, which are held at fair value. Interest rate variations on the treasury bill portfolio are quantified and disclosed in note 7 to the financial statements. The investment in the BIS is subject to currency risks and other price risk, since the fair value of the shares is estimated on the basis of the net asset value of the BIS translated into Canadian dollars on the reporting date. These variations would not affect the Bank's ability to fulfill its obligations, since its income greatly exceeds its expenses.	●	●
Liquidity: The Bank's largest liability is *Bank notes in circulation*, which are non-interest-bearing liabilities with no fixed maturity. In the event of an unexpected redemption of bank notes, the Bank has the ability to settle the obligation by selling its portfolio of highly liquid, interest-bearing securities.	●	●
Business risks		
Monetary policy: Implementation risks arise from a number of sources, including significant uncertainty around the global economic outlook and the global financial system, and challenges in attracting a sufficient number of skilled and experienced staff.	▲	▲
Financial system: Policy and oversight risks arise from the expanding nature of the Bank's role in domestic and international financial system reforms, oversight of new central counterparties (CCPs) and challenges in attracting qualified staff.	▲	▲
Currency: Implementation risks relate to the possibility that the new *Polymer* series of bank notes does not meet program objectives.	▲	▲
Funds management: Risks are associated with the operations for safekeeping services; the payment, clearing and settlement system; and the management of foreign exchange reserves.	●	●
Enterprise risks		
People and capacity: Risks relate to the increasing complexity of the Bank's work, changes in the mix of skills required, the limited labour market pool for economists and financial system specialists, and changing demographics.	▲	▲
Project execution and impacts: Risks relate to the number of large, complex initiatives, and the interdependencies of projects.	▲	▲
Continuity of critical business processes: Business-continuity risks pertain to the possibility that the Bank would be unable to carry out its critical business processes owing to the unavailability of staff, information technology systems or the backup facility.	▲	●

Financial Risks

To mitigate financial risks, the Bank has a Financial Risk Office, which is independent of operations and is responsible for monitoring and reporting on financial risks relating to the Bank's balance sheet. Collateral policies are reviewed and updated regularly in connection with the Bank's liquidity operations. With respect to the Bank's overall operations, management has established and actively monitors a system of internal controls, and periodic reviews are conducted to assess the appropriateness and effectiveness of these controls. For further information about the Bank's financial risks, see note 7 to the financial statements.

Business Risks

To manage business risks in the areas of monetary policy, the financial system and funds management, the Bank has well-established policy frameworks, an extensive research program and analytic models that are enhanced on a regular basis. The Bank also participates in a number of key international forums, and collaborates with other major central banks and with Canadian and international financial sector regulatory partners. In addition, the Bank maintains a comprehensive communications strategy to inform Canadians about the goals and objectives of its policy decisions, as well as financial system issues and potential vulnerabilities.

Risk-mitigation measures in the currency function include detailed execution plans, careful monitoring and reporting of key milestones for the issuance of the new polymer notes in 2012 and 2013; comprehensive pre-production testing; ongoing interaction with financial institutions and bank note printing companies; and a comprehensive communications and education program.

The Bank's mission-critical and other important systems, processes and documentation are reviewed regularly, and enhanced as required, to ensure an appropriate control environment. (See also Enterprise Risks, below.)

Enterprise Risks

To mitigate its people and capacity risks, the Bank is strengthening its recruitment strategy (e.g., targeted, proactive recruitment for mid-career professionals and candidates with specialized skills); ensuring that its human resources policies and the delivery of programs related to talent development, the work environment and compensation remain relevant and effective; and enhancing capacity planning and change-management capabilities.

In the case of project execution, the Bank mitigates risks with a sound IT governance structure, project monitoring and reporting, portfolio-management practices, and the use of external expertise, where appropriate.

The Bank's continuity-of-operations program (COOP) is tested regularly and then strengthened based on the test results. Ongoing training on operational processes and systems is carried out to ensure the availability of adequately cross-trained staff. A database of operational events is maintained to develop and implement action plans to mitigate potential risks. Modifications are being made to enhance COOP plans, including backup facilities.

Performance Against Plan

The Medium-Term Plan (2010–12)

The three-year medium-term plan (MTP) is the main planning tool to establish the Bank's strategic priorities. The current MTP priorities are: to conduct leading research and policy analysis; to strengthen business resilience and infrastructure; to attract, retain and engage employees; and to unveil and issue a new series of bank notes.

Key Corporate Priorities

The Bank sets annual work priorities with reference to both its medium-term plan and the changing environment. The table below summarizes the Bank's key priorities for 2011, and lists the key achievements against these priorities. The activities carried out by the Bank in each of these strategic areas over the past year are described in the Key Achievements section of this *Report*.

Key corporate priorities for 2011	Key achievements in 2011
Conduct leading research and policy analysis	▪ completed the multi-year research program on the monetary policy framework and renewed the Bank's inflation-control agreement with the government ▪ played a leadership role in macroeconomic and financial reform initiatives, both domestically and internationally ▪ strengthened the analytical framework to assess system-wide risk to the Canadian financial system ▪ contributed to the design of the government's prudential liquidity plan, and debt-management strategy
Strengthen business resilience and infrastructure	▪ improved the resilience of the Bank's critical payment infrastructure, meeting key milestones in the upgrade of the data centre ▪ made solid progress in developing new information technology systems to support economic analysis, financial market operations, funds management and corporate administration; and continued analysis for the renovation of the head office complex
Attract, retain and engage staff	▪ completed the implementation of the new total compensation program and enhanced performance management ▪ developed a framework for recruiting mid-career staff with specialized skills ▪ conducted a work environment survey, with a response rate of 85 per cent and improved scores from the previous survey
Unveil a new series of bank notes and issue the first denomination in that series	▪ successfully launched the new polymer bank note series with enhanced security features and issued the $100 denomination

2011 Financial Performance Against Plan

The Bank monitors its expenses in two ways—total operating expenses as reported in the Bank's financial results in accordance with International Financial Reporting Standards and MTP operating expenses,[4] which are a subset of the total operating expenses reported in the financial statements.

MTP operating expenses exclude costs that have a record of volatility or that cannot be accurately predicted, and are less meaningful to the Bank's daily management of its operations.

The following expenses are excluded from the MTP operating expenses:

- expenses for non-current deferred employee benefits, which are subject to volatility because of changes in discount rates;
- costs related to the production of bank notes, which vary with note volumes; and
- significant one-time costs associated with two major capital projects: (i) the Enhanced Business-Continuity Program and (ii) the renewal of the Bank's head office complex in Ottawa.

4. Medium-term plan operating expenses are considered a non-IFRS measure that does not have a standardized meaning.

The Bank's MTP operating expense budget for 2011 was set at a level of $342 million, consistent with federal government guidelines to maintain spending at 2010 levels. This commitment was made when the MTP financial plan was updated in late 2010. At that time, the Bank launched the Corporate Effectiveness Program to ensure that the priorities outlined in the MTP were met while being consistent with federal government guidelines to hold spending at 2010 levels.

Actual 2011 MTP operating expenses were $316 million, $26 million lower than the $342 million budget, with the decrease due mainly to savings achieved through the Corporate Effectiveness Program and lower costs associated with restructuring activities. Total operating expenses were $353 million, and are explained in the Financial Discussion section of this *Report*.

	2011		2010	
	Actual	**Medium-term plan**	**Actual**	**Medium-term plan**
MTP operating expenses	316	342	344	342
Excluded expenses	37		37	
Total expenses	353		381	

The most significant item in *Excluded expenses* is the costs associated with bank note production, which did not change significantly compared with 2010. In 2011, the costs associated with non-current deferred employee benefit expenses were lower, mainly because of lower cost projections based on the most recent actuarial valuation.

Corporate Measures of Performance

In order to assess the Bank's performance in the execution of its strategy and the monitoring of its financial results, the Bank reviews key performance drivers and monitors key performance indicators. The following table summarizes the Bank's 2011 performance against key performance indicators.

Key performance indicator	**2011 performance**
Inflation	Total CPI inflation temporarily exceeded the upper bound of the 1 to 3 per cent inflation-control range; core inflation, however, remained close to 2 per cent throughout the year, and inflation expectations remained well anchored on the 2 per cent target.
Counterfeiting levels	At 34 parts per million (ppm), counterfeiting levels remained well below the MTP targeted level of 50 ppm.
Turnaround times for market operations	Turnaround times for market operations were below the 5-minute ceiling for responding to auction participants' bid submissions for treasury bill and bond auctions, and for responding to offering submissions for buybacks and switches.
Systems availability	The systems-availability target of 99.5 per cent for the Bank's critical banking system was exceeded.
Work environment	The Bank maintained its designation as a Top 100 Employer in Canada.

Financial Discussion

Changes in Financial Position and Comprehensive Income

This section discusses the financial performance of the Bank, as reflected in its financial statements.

Highlights of the Statement of Financial Position
(Millions of dollars)

	31 December 2011	31 December 2010[a]	$ change	% change
Assets				
Cash and foreign deposits	12	5	7	149.4
Loans and receivables	1,531	2,087	(556)	-26.7
Investments	62,424	58,767	3,657	6.2
Property and equipment	177	153	24	15.4
Intangible assets	44	26	18	69.9
Other assets	59	178	(119)	-66.7
	64,247	61,216	3,031	5.0
Liabilities and Equity				
Bank notes in circulation	61,029	57,874	3,155	5.5
Deposits	2,481	2,557	(76)	-3.0
Other liabilities	312	368	(56)	-15.1
Equity	425	417	8	1.8
	64,247	61,216	3,031	5.0

a. Comparative figures have been restated in accordance with International Financial Reporting Standards (IFRS).

At the close of 2011, the Bank had assets of $64,247 million in the form of *Loans and receivables*, *Investments*, *Property and equipment*, *Intangible assets* and *Other assets*. Compared with year-end 2010, assets increased by $3,031 million, primarily because a higher level of assets was needed to support bank notes in circulation.

Loans and receivables decreased by $556 million since 31 December 2010, because a lower level of term purchase and resale agreement (PRA) operations was outstanding at year-end compared with the previous year. These operations are undertaken to offset the seasonal demand for bank notes, and are no longer required once the demand for bank notes returns to pre-holiday levels. The Bank issued only one term PRA in December 2011 for general balance-sheet-management purposes, including the seasonal increase in the demand for bank notes.

Investments increased by $3,657 million, owing to net purchases of Government of Canada treasury bills and bonds in excess of maturities. Government of Canada bonds increased by $10,003 million, which was offset by a decline of $6,360 million in Government of Canada treasury bills, in line with a higher proportion of bonds issued by the government in 2011. The balance of the increase in *Investments* resulted from fair-value changes in the Bank's investment in the BIS.

Spending on *Property and equipment* and *Intangible assets* since 31 December 2010 totalled $60 million. Of this amount, spending related to the Enhanced Business-Continuity Program and the refurbishment of elevators at the head office complex totalled $26.5 million. In addition, $27.5 million was spent on strategic initiatives to support the Bank's achievement of its medium-term plan priorities. The largest component of these investments is the Auctions and Market Applications Program, which aims to support end-to-end post-trade processing and to strengthen business-continuity capacity.

Other assets decreased by $119 million since 31 December 2010, mainly because of a reduction in the net employee benefit asset related to the pension funds.

Bank notes in circulation liabilities increased by 5.5 per cent, reflecting typical growth in the demand for bank notes.

The main component of the *Deposits* liability is the deposit held for the Government of Canada. This liability is dependent on the cash needs of the Government of Canada, and fluctuations that occur are a result of cash-flow management decisions made by the government. Deposits at 31 December 2011 decreased by $76 million compared with the previous year.

Other liabilities decreased by $56 million compared with year-end 2010, mainly as a result of a lower balance owing to the Receiver General for Canada. Net income earned on the Bank's assets, after deductions for operating expenses and allocations to reserves, is paid each year to the Receiver General for Canada. At 31 December 2011, the unremitted balance was $79.8 million ($168 million at 31 December 2010).

Highlights of the Statement of Comprehensive Income
Results for the year ended 31 December 2011
(Millions of dollars)

	Twelve months ended 31 December			
	2011	2010[a]	$ change	% change
Income				
Interest revenue	1,621	1,574	47	3
Interest expense	(23)	(42)	19	-44
Other revenue	9	11	(2)	-20
Total income	1,607	1,543	64	4
Expenses				
Staff costs	154	171	(17)	-10
Bank note research, production and processing	54	54	0	1
Premises maintenance	24	29	(5)	-16
Technology and telecommunications	27	34	(7)	-21
Depreciation and amortization	17	15	2	12
Other expenses	77	78	(1)	-1
Total expenses	353	381	(28)	-7
Net Income	1,254	1,163	91	8
Other Comprehensive Income	(179)	(122)	(57)	—[b]
Comprehensive Income	1,075	1,040	35	3

a. Comparative figures have been restated in accordance with International Financial Reporting Standards (IFRS).
b. Comparison is not meaningful.

Income

Total income for 2011 was $1,607 million, an increase of $64 million, or 4 per cent, compared with the previous year.

The Bank's investment income of $1,621 million consisted of $1,615 million in interest revenue from treasury bills and bonds, $4 million in dividend revenue, and $2 million in interest from securities purchased under resale agreements. Higher yields on investments increased interest revenues by $89 million, or 6 per cent.

Decreases in other sources of revenue offset the growth in investment revenues. The Bank reported lower interest earned on purchase and resale agreements, since there were fewer term PRAs during 2011. This resulted in a decrease of $36 million in interest earned on securities purchased under these agreements.

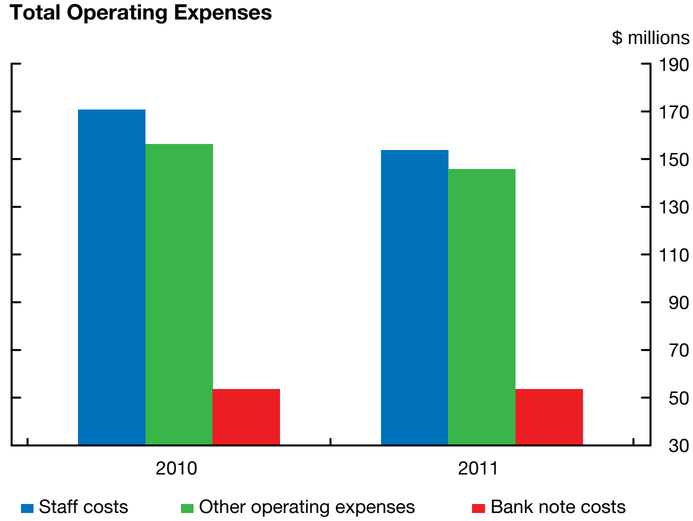
Dividend revenue from the BIS decreased by $6 million because revenue for 2010 had included a special dividend paid by the BIS that was not repeated in 2011.

Revenues are reported net of interest paid on Government of Canada deposits. The interest expense on deposits decreased by $19 million, compared with the previous year, owing mainly to a lower level of Government of Canada deposits as described in the Highlights of the Statement of Financial Position on page 38.

Expenses

Total operating expenses were $28 million lower than the previous year, primarily as a result of lower staff costs. Expenses on an MTP operating basis were $26 million lower than planned, as discussed in the 2011 Financial Performance Against Plan section. Savings were achieved through the Corporate Effectiveness Program in a number of cost elements, including staff costs, premises maintenance and costs associated with the Bank's role as fiscal agent for the Government of Canada debt program. These savings offset non-controllable cost increases in other areas of operations.

Total Operating Expenses



Staff costs for 2011 were $17 million lower than in 2010. Annual compensation increases were offset by lower costs associated with the Bank's deferred employee benefit plans. Expenses for 2010 included $11 million in restructuring costs that were not repeated in 2011.

Costs associated with bank note production did not change from 2010 levels. In 2011, the Bank received 205 million cotton and 107 million polymer notes from the printers, compared with 456 million cotton notes received in 2010. Increased costs associated with the production of the polymer notes offset the lower volumes of notes received. Production of the cotton notes occurred in the first quarter of 2011, while the production of the polymer notes took place in the second half of the year.

Other operating expenses, including premises, technology, and depreciation and amortization, decreased by $10 million compared with 2010. Expenses for premises maintenance decreased by $5 million in consideration of the ongoing analysis for renewing aging infrastructure. Technology costs decreased by $7 million, mainly as a result of a higher portion of costs dedicated to capital projects. Other expenses were kept flat on a year-over-year basis, owing to reductions of $4 million in the costs associated with the Bank's role as fiscal agent for the Government of Canada debt program.

Net income

Net income earned on the Bank's assets, after deductions for operating expenses and allocations to reserves, is paid each year to the Receiver General for Canada. In 2011, the Bank transferred $1,156 million to the Receiver General for Canada ($126 million related to 2010 net income and $1,030 million related to 2011 net income).

Other comprehensive income

Other comprehensive income of -$179 million consists of an increase of $24 million in the fair values of available-for-sale assets offset by an actuarial loss of $203 million related to the Bank's deferred employee benefit plans.

Actuarial losses are affected by the actual return, compared with the expected return, on plan assets, and the discount rate used to determine defined-benefit obligations. The loss recorded in 2011 is the result of a reduction in the discount rate used to value the defined-benefit obligation combined with low returns on plan assets. The reduced discount rate reflects the change in corporate bond yields over the past 12 months, in addition to the impact of a change in methodology adopted by the Bank in connection with the establishment of the accounting discount rate.[5]

Available-for-sale assets comprise Government of Canada treasury bills and the Bank's investment in the BIS. Fair-value changes are accumulated in the reserve for available-for-sale assets within the Bank's *Equity*. As at 31 December 2011, this reserve totalled $294.6 million and consisted primarily of the fair-value change in the Bank's investment in the BIS.

Adoption of International Financial Reporting Standards (IFRS)

As a publicly accountable organization and in accordance with public sector accounting standards, the Bank of Canada transitioned to reporting under IFRS on 1 January 2011. The Bank's 31 December 2011 financial statements are its first annual IFRS financial statements and, for comparison purposes, include restated figures for 2010. Full details on the financial impact of the transition to IFRS on the Bank's opening Statement of Financial Position, and for the year ended 31 December 2010, are available in note 20 to the financial statements.

The key components affected by the Bank's transition to IFRS at 1 January 2010 are shown below.

	Amount	Description of change
Financial instruments: carrying value of BIS shares	Increase in the carrying value of BIS shares of $281 million	The Bank's investment in shares of the Bank for International Settlements (BIS) is classified as available-for-sale and was carried at cost under Canadian GAAP, but is recorded at fair value in accordance with IFRS.
Employee benefits	The net impact of changes: ▪ an increase in the carrying amount of the pension asset of $113 million, and ▪ a reduction in the carrying amount of non-pension liabilities of $10 million	Upon transition to IFRS, the Bank adopted a policy to recognize all actuarial gains and losses on post-employment defined benefits immediately in *Other comprehensive income*, as well as other long-term benefits in *Net income*. At the date of transition, all previously unamortized transitional obligations and assets, vested past-service costs and credits, and net actuarial losses were recognized. Also recognized in *Retained earnings* were changes related to the adoption of IAS 19, which include using discount rates determined with reference to market yields of AA-rated corporate bonds.
Property and equipment	Increase in the carrying amount of the Bank's buildings of $28 million	Under IFRS, each component of an item of *Property and equipment* with a cost that is significant in relation to the total cost of the item is depreciated separately. The effect of this on the Bank's *Property and equipment* resulted from retroactive changes to the useful lives over which these components are depreciated.

5. The change in methodology was adopted to conform to guidance issued by the Canadian Institute of Actuaries on the establishment of the accounting discount rate.

Financial Controls and Procedures

Management is responsible for establishing and maintaining adequate internal controls over financial reporting, as well as establishing appropriate disclosure controls and procedures. The Bank maintains a certification regime to evaluate the design and effectiveness of internal controls over financial reporting, and disclosure controls and procedures. As of 31 December 2011, the Bank's certifying officers assessed the design and effectiveness of its internal controls over financial reporting, and its disclosure controls and procedures, and found them to be appropriate.

Significant Accounting Policies and Estimates

The Bank's accounting policies are presented in note 3 to the financial statements. The preparation of financial statements requires that management use judgment to make estimates and assumptions. The Bank's significant accounting estimates are primarily in the areas of the fair value of financial instruments and of pension and other future benefits costs, and are described in notes 7 and 14, respectively, to the financial statements and are summarized in the following table.

Investment in the Bank for International Settlements	
The Bank records its investment in BIS shares at fair value.	The fair value of the BIS shares is estimated to be 70 per cent of the Bank's interest in the net asset value of the BIS at the reporting date. This 30 per cent discount to net asset value is based on a decision by the International Court at the Hague relating to a share repurchase by the BIS in 2001 (the last share repurchase conducted by the BIS) and has been used by the BIS to determine the pricing of any new shares issued since that time.
	The Bank's financial statements incorporate the most recently available data from the BIS.
	The Bank expects the value of the BIS shares to fluctuate over time in conjunction with the strength of the BIS balance sheet and the exchange rate.
Employee benefits	
The costs of providing deferred employee benefits are charged to the income statement over the period during which benefit is derived from the employee's services. The assumptions on which these costs are calculated are disclosed in note 14 to the financial statements.	The key assumptions include the expected long-term rate of return on plan assets, the rate of compensation increase and the discount rate. The expected long-term rate of return on bonds is determined based on the portfolio mix of government and provincial bonds. The assumption with the greatest potential impact on the benefit obligation is the discount rate. The discount rate is determined with reference to yields on AA-rated corporate bonds.
	Sensitivity analysis is provided in note 14, "Employee benefit plans." An increase in the discount rate of 50 basis points would result in an increase in the net pension obligation of $96 million and an increase in the benefit expense of $2.6 million.

Significant Contracts and Agreements

During 2011, the Bank entered into the following agreements and contracts.

During the first quarter of 2011, the Bank signed a 10-year contract with Note Printing Australia Limited, a wholly owned subsidiary of the Reserve Bank of Australia, for the production and supply of the polymer substrate for the Bank's next generation of bank notes at a value not to exceed $250 million over the life of the contract.

In December 2011, the Bank entered into temporary bilateral liquidity swap facilities with the Federal Reserve Bank of New York, the Bank of Japan, the Swiss National Bank, the Bank of England and the European Central Bank. The temporary bilateral liquidity swap facilities were established to provide liquidity in each jurisdiction in any of their currencies, should market conditions warrant. The pre-existing US$30 billion facility with the Federal Reserve Bank of New York was extended and now expires on 1 February 2013. The unlimited swap facilities with the Bank of Japan, the Swiss National Bank, the Bank of England and the European Central Bank were established in December 2011 for an initial term that will expire on 1 February 2013. None of the liquidity swaps was accessed by either party in 2011.

The Bank's Enhanced Business-Continuity Program was initiated in 2009 to renew and update the current off-site operations centre in Ottawa with a view to splitting the Bank's critical financial market operations and to house its primary data centre. During the second quarter, the Bank entered into a $27 million fixed-price construction contract with a general contractor, and construction began in June. This is an important step toward achieving the Bank's medium-term plan priority to enhance business resilience and improve its infrastructure.

In the last quarter of 2011, the Bank and the Department of Finance signed a Memorandum of Understanding in relation to a deposit to be established at the Bank by the Government of Canada in connection with its prudential liquidity management. To meet its prudential liquidity needs, the government plans to deposit approximately $20 billion with the Bank. The Bank, in consultation with the Department of Finance, will determine the pace of the initial buildup of balances. The deposit will earn interest at rates that are equivalent to those paid on other Receiver General balances. To accommodate the projected increase in its liabilities, the Bank's minimum purchase of nominal bonds at auctions was increased in 2011 from 15 per cent to 20 per cent.

Related-Party Transactions

The Bank is related in terms of common ownership to all Government of Canada departments, agencies and Crown corporations. To achieve its monetary policy objectives, the Bank maintains a position of structural and functional independence from the Government of Canada through its ability to fund its own operations without external assistance and through its management and governance.

In the normal course of its operations, the Bank enters into transactions with related parties and material transactions and balances are reported as described in note 19 to the financial statements. The Bank provides funds-management, fiscal-agent and banking services to the federal government, and the costs of these services are recorded within the Bank's expenses. The assets and liabilities that are managed on behalf of the government are not included in the Bank's financial statements since they do not represent assets or liabilities of the Bank.

Financial Statement Outlook: 2012

The Bank's forecasts for its operations do not include projections of net income and financial position. Such projections would require assumptions of interest rates, which the Bank avoids in order to limit potential market influence.

The Bank projects its operating expenses in connection with the development of the medium-term plan. Consistent with the commitment made in late 2010, when the MTP financial plan was updated in response to federal government guidelines, the Bank intends to hold 2012 operating expenses at $342 million.

Expenses excluded from the medium-term plan

Spending associated with the Bank's Head Office Renewal Program is anticipated in 2012 as a result of further analysis and the development of detailed cost estimates.

The Bank expects to incur costs of $150 million for the production of the new generation of polymer bank notes in 2012. In addition to further production of the $100 notes, which were launched in November 2011, and the final order of the cotton $5 and $10 notes, the Bank will produce the new $50 and $20 polymer notes during the year; both of these denominations will be launched during 2012.

Capital spending

Capital expenditures for ongoing operations and strategic investments of $66 million are expected in 2012. This estimate may be updated during 2012 pending the outcome of further decisions taken regarding the Head Office Renewal Program.

Statement of Financial Position

In connection with the Government of Canada's prudential liquidity plan, government deposits held at the Bank are expected to increase by an amount that will range from $8 billion to $10 billion in 2012.

Financial Statements

As at 31 December 2011

FINANCIAL REPORTING RESPONSIBILITY

The accompanying financial statements of the Bank of Canada have been prepared by management in accordance with International Financial Reporting Standards and contain certain items that reflect the best estimates and judgments of management. The integrity and reliability of the data in these financial statements are management's responsibility. Management is responsible for ensuring that all information in the *Annual Report* is consistent with the financial statements.

In support of its responsibility for the integrity and reliability of these financial statements and for the accounting system from which they are derived, management has developed and maintains a system of internal controls to provide reasonable assurance that transactions are properly authorized and recorded, that financial information is reliable, that the assets are safeguarded and liabilities recognized, and that the operations are carried out effectively. The Bank has an internal Audit Department whose functions include reviewing internal controls, including accounting and financial controls and their application.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls and exercises this responsibility through the Audit and Finance Committee of the Board. The Audit and Finance Committee is composed of members who are neither officers nor employees of the Bank and who are financially literate. The Audit and Finance Committee is therefore qualified to review the Bank's annual financial statements and to recommend their approval by the Board of Directors. The Audit and Finance Committee meets with management, the Chief Internal Auditor, and the Bank's external auditors who are appointed by Order-in-Council. The Audit and Finance Committee has established processes to evaluate the independence of the Bank's external auditors and reviews all services provided by them. The Audit and Finance Committee has a duty to review the adoption of, and changes in, accounting principles and procedures that have a material effect on the financial statements, and to review and assess key management judgments and estimates material to the reported financial information.

These financial statements have been audited by the Bank's external auditors, KPMG LLP and Deloitte and Touche LLP, and their report is presented herein. The external auditors have full and unrestricted access to the Audit and Finance Committee to discuss their audit and related findings.

M. Carney, Governor

S. Vokey, CA, Chief Accountant

Ottawa, Canada
16 February 2012

INDEPENDENT AUDITORS' REPORT

To the Minister of Finance, registered shareholder of the Bank of Canada (the "Bank")

We have audited the accompanying financial statements of the Bank, which comprise the statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010 and the statements of comprehensive income, changes in equity, and cash flows for the years ended December 31, 2011 and 2010, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform an audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as at December 31, 2011, December 31, 2010 and January 1, 2010 and its financial performance and its cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards.

KPMG LLP

KPMG LLP
Chartered Accountants
Licensed Public Accountants

Deloitte & Touche LLP

Deloitte & Touche LLP
Chartered Accountants
Licensed Public Accountants

Ottawa, Canada
16 February 2012

STATEMENT OF FINANCIAL POSITION

(Millions of dollars)

	31 December 2011	As at 31 December 2010	1 January 2010
ASSETS			
Cash and foreign deposits (note 4)	**11.7**	4.7	20.4
Loans and receivables			
Securities purchased under resale agreements (note 5a)	**1,447.7**	2,062.4	25,374.8
Advances to members of the Canadian Payments Association (note 5b)	**81.5**	22.5	-
Other receivables	**1.6**	2.1	2.2
	1,530.8	2,087.0	25,377.0
Investments (note 6, 7)			
Government of Canada treasury bills	**18,545.6**	24,906.1	13,684.0
Government of Canada bonds	**43,553.3**	33,550.6	31,986.2
Other investments	**325.3**	310.7	318.7
	62,424.2	58,767.4	45,988.9
Property and equipment (note 8)	**176.6**	153.0	155.2
Intangible assets (note 9)	**44.6**	25.9	23.7
Other assets (note 10)	**59.3**	178.1	211.6
Total assets	**64,247.2**	61,216.1	71,776.8
LIABILITIES AND EQUITY			
Bank notes in circulation (note 11)	**61,028.8**	57,874.2	55,467.9
Deposits (note 12)			
Government of Canada	**1,512.5**	1,869.4	11,847.6
Members of the Canadian Payments Association	**106.7**	47.5	2,999.6
Other deposits	**861.8**	639.9	703.0
	2,481.0	2,556.8	15,550.2
Other liabilities (note 13)	**312.8**	368.3	189.8
	63,822.6	60,799.3	71,207.9
Equity (note 15)	**424.6**	416.8	568.9
Total liabilities and equity	**64,247.2**	61,216.1	71,776.8

Commitments, contingencies and guarantees (note 18)

M. Carney, Governor

S. Vokey, CA, Chief Accountant

On behalf of the Board

David H. Laidley, FCA,
Chair, Audit and Finance Committee

W. A. Black,
Lead Director

(See accompanying notes to the Financial Statements.)

STATEMENT OF COMPREHENSIVE INCOME

(Millions of dollars)

	For the year ended 31 December	
	2011	2010
INCOME		
Net interest income		
Interest revenue		
Interest earned on investments	**1,614.7**	1,525.3
Dividend revenue	**4.3**	10.1
Interest earned on securities purchased under resale agreements	**1.9**	38.4
Other interest revenue	**0.2**	0.1
	1,621.1	1,573.9
Interest expense		
Interest expense on deposits	**(23.4)**	(42.0)
	1,597.7	1,531.9
Other revenue	**9.1**	11.4
Total income	**1,606.8**	1,543.3
EXPENSES		
Staff costs	**153.8**	170.8
Bank note research, production and processing	**53.5**	53.7
Premises maintenance	**24.4**	28.7
Technology and telecommunications	**27.0**	34.3
Depreciation and amortization	**17.4**	15.2
Other operating expenses	**77.0**	78.1
Total expenses	**353.1**	380.8
NET INCOME	**1,253.7**	1,162.5
OTHER COMPREHENSIVE INCOME		
Change in fair value of available-for-sale financial assets	**23.6**	(16.5)
Actuarial losses	**(202.5)**	(105.6)
Other comprehensive income	**(178.9)**	(122.1)
COMPREHENSIVE INCOME	**1,074.8**	1,040.4

(See accompanying notes to the Financial Statements.)

STATEMENT OF CHANGES IN EQUITY

(Millions of dollars)

							For the year ended 31 December
	Share capital	Statutory reserve	Special reserve	Available-for-sale reserve	Actuarial gains reserve	Retained earnings	Total
Balance, 1 January 2011	**5.0**	**25.0**	**100.0**	**271.0**	**14.1**	**1.7**	**416.8**
Comprehensive income for the year							
Net income	**-**	**-**	**-**	**-**	**-**	**1,253.7**	**1,253.7**
Change in fair value of available-for-sale financial assets	**-**	**-**	**-**	**23.6**	**-**	**-**	**23.6**
Actuarial losses	**-**	**-**	**-**	**-**	**(14.1)**	**(188.4)**	**(202.5)**
	-	**-**	**-**	**23.6**	**(14.1)**	**1,065.3**	**1,074.8**
Transfer to Receiver General for Canada	**-**	**-**	**-**	**-**	**-**	**(1,067.0)**	**(1,067.0)**
Balance, 31 December 2011	**5.0**	**25.0**	**100.0**	**294.6**	**-**	**-**	**424.6**
Balance, 1 January 2010	5.0	25.0	100.0	287.5	119.7	31.7	568.9
Comprehensive income for the year							
Net income	-	-	-	-	-	1,162.5	1,162.5
Change in fair value of available-for-sale financial assets	-	-	-	(16.5)	-	-	(16.5)
Actuarial losses	-	-	-	-	(105.6)	-	(105.6)
	-	-	-	(16.5)	(105.6)	1,162.5	1,040.4
Transfer to Receiver General for Canada	-	-	-	-	-	(1,192.5)	(1,192.5)
Balance, 31 December 2010	5.0	25.0	100.0	271.0	14.1	1.7	416.8

(See accompanying notes to the Financial Statements.)

STATEMENT OF CASH FLOWS

(Millions of dollars)

	For the year ended 31 December 2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Interest received	**1,641.6**	1,606.0
Dividends received	**4.3**	10.1
Other revenue received	**9.9**	11.8
Interest paid	**(23.4)**	(42.0)
Payments to or on behalf of employees and to suppliers	**(385.8)**	(403.3)
Net decrease in advances to members of the Canadian Payments Association	**(59.0)**	(22.5)
Net decrease in deposits	**(76.4)**	(12,993.4)
Proceeds from maturity of securities purchased under resale agreements	**17,052.7**	60,784.5
Acquisition of securities purchased under resale agreements	**(16,438.6)**	(37,506.3)
Repayments of securities sold under repurchase agreements	**(764.8)**	(470.0)
Proceeds from securities sold under repurchase agreements	**764.8**	470.0
Net cash provided by operating activities	**1,725.3**	11,444.9
CASH FLOWS FROM INVESTING ACTIVITIES		
Net (increase) decrease in Government of Canada treasury bills	**6,362.5**	(11,180.9)
Purchases of Government of Canada bonds	**(15,422.9)**	(5,924.2)
Proceeds from maturity of Government of Canada bonds	**5,403.1**	4,302.2
Additions of property and equipment	**(36.2)**	(10.7)
Additions of intangible assets	**(23.5)**	(4.4)
Net cash used in investing activities	**(3,717.0)**	(12,818.0)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in bank notes in circulation	**3,154.6**	2,406.3
Remittance of ascertained surplus to the Receiver General for Canada	**(1,156.1)**	(1,048.6)
Net cash provided by financing activities	**1,998.5**	1,357.7
EFFECT OF EXCHANGE RATE CHANGES ON FOREIGN CURRENCY	**0.2**	(0.3)
INCREASE (DECREASE) IN CASH AND FOREIGN DEPOSITS	**7.0**	(15.7)
CASH AND FOREIGN DEPOSITS, BEGINNING OF YEAR	**4.7**	20.4
CASH AND FOREIGN DEPOSITS, END OF YEAR	**11.7**	4.7

(See accompanying notes to the Financial Statements.)

NOTES TO THE FINANCIAL STATEMENTS OF THE BANK OF CANADA

For the year ended 31 December 2011

(Amounts in the notes to the Financial Statements of the Bank of Canada are in millions of Canadian dollars, unless otherwise stated.)

1. The business of the Bank of Canada

The Bank of Canada (the Bank) is the central bank of Canada. The Bank is a corporation under the Bank of Canada Act and is wholly owned by the Government of Canada and is exempt from income taxes. The Bank is a Government Business Enterprise, as defined by the Public Sector Accounting Board Handbook and, as such, adheres to the standards applicable to publicly accountable enterprises as outlined by the Canadian Institute of Chartered Accountants (CICA).

The responsibilities of the Bank focus on the goals of low and stable inflation, financial system stability, a safe and secure currency, and the efficient management of government funds and public debt. These responsibilities are carried out as part of the broad functions described below.

Monetary policy
Contributes to solid economic performance and rising living standards for Canadians by keeping inflation low, stable and predictable.

Financial system
Promotes a safe, sound and efficient financial system, both within Canada and internationally.

Currency
Designs, produces and distributes Canada's bank notes, focusing on deterrence of counterfeiting through research on security features, public education and partnership with law enforcement; replaces and destroys worn notes.

Funds management
Provides high-quality, effective and efficient funds-management services: for the Government of Canada, as its fiscal agent; for the Bank; and for other clients.

2. Basis of preparation

Compliance with International Financial Reporting Standards (IFRS)

These financial statements have been prepared in accordance with IFRS accounting policies and conform to the disclosure and accounting requirements of the *Bank of Canada Act* and the Bank's bylaws.

These are the Bank's first annual IFRS financial statements. The Bank has elected 1 January 2010 as the date of transition to IFRS (the "transition date"). IFRS 1 *First-time Adoption of IFRS* (IFRS 1) has been applied. An explanation of how the transition to IFRS has affected the financial statements is included in note 20.

The Board of Directors approved the financial statements on 16 February 2012.

Measurement base

The financial statements have been prepared on the historical cost basis, except for the available-for-sale financial assets, which are measured at fair value, and the defined-benefit assets and obligations, which are recognized as the net of the plan assets, plus unrecognized past service costs, and the present value of the defined-benefit obligation.

Significant accounting estimates and judgments in applying accounting policies

The preparation of the financial statements requires management to make judgments, estimates and assumptions based on information available at the statement date that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results could differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. These estimates are primarily in the area of employee benefit plans (note 14) and the fair values of certain financial instruments and collateral taken (note 7).

Functional and presentation currency

The Bank's functional and presentation currency is the Canadian dollar.

Fiscal agent and custodial activities

Responsibility for the operational management of the Government of Canada's financial assets and liabilities is jointly borne by both the Bank (as fiscal agent for the Government) and the Department of Finance. In this fiscal agent role, the Bank provides transactional and administrative support to the Government of Canada in certain areas. Assets, liabilities, expenditures and revenues to which this support relates are those of the Government of Canada and are not included in the financial statements of the Bank.

Securities safekeeping and gold custodial activities are provided to foreign central banks and international organizations. The assets, and income arising thereon, are excluded from these financial statements, as they are not assets or income of the Bank.

3. Significant accounting policies

The significant accounting policies of the Bank are summarized below. These policies have been consistently applied to all years presented, unless otherwise stated.

a) Translation of foreign currencies

Investment income and expenses denominated in foreign currencies are translated at the exchange rate in effect at the date of the transaction. Fair-value items denominated in foreign currencies are translated at the exchange rate in effect at the date of the fair-value measurement. Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at the rates of exchange prevailing at the end of the reporting years. The resulting gains and losses are included in *Other revenue*. Gains or losses on equity investments classified as available-for-sale (AFS), along with any exchange-related gains or losses, are recognized in the available-for-sale reserve within *Other Comprehensive Income*.

b) Financial instruments

The Bank accounts for all financial instruments using settlement date accounting. Financial instruments are measured at fair value on initial recognition, plus transaction costs, if any, for all financial assets not carried at fair value through net income. Subsequent to initial recognition, they are accounted for based on their classification.

Subsequent to initial recognition, financial assets classified as AFS are measured at fair value using quoted market prices, with the exception of the Bank for International Settlements (BIS) shares, which are measured using significant non-observable inputs. Unrealized changes in values of AFS financial assets measured at fair value are recognized in *Other Comprehensive Income* and accumulated in the available-for-sale reserve in equity until the financial asset is derecognized or becomes impaired. At that time, the cumulative unrealized gain or loss previously recognized in *Other Comprehensive Income* is reclassified from equity to net income. The Bank's financial assets designated as AFS consist of Government of Canada treasury bills and other investments, which comprise BIS shares.

Financial assets that the Bank has the intent and ability to hold to maturity are classified as held-to-maturity (HTM). Subsequent to initial recognition, financial assets classified as HTM are measured at amortized cost using the effective interest method less any impairment losses. The effective interest method uses the rate inherent in a financial instrument that discounts the estimated future cash flows over the expected life of the financial instrument so as to recognize interest on a constant yield basis. Government of Canada bonds are classified as HTM.

The Bank has not classified any of its financial assets as fair value through net income, other than cash and foreign deposits.

All other financial assets are classified as loans and receivables. Subsequent to initial recognition, these are measured at amortized cost less any impairment losses using the effective interest method of amortization.

The Bank derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire. On derecognition of a financial asset measured at amortized cost, the difference between the asset's carrying amount and the sum of the consideration received and receivable is recognized in net income.

The Bank has classified its financial liabilities as other liabilities. These liabilities are initially recognized at fair value. Subsequent to initial recognition, financial liabilities are measured at amortized cost using the effective interest method, with the exception of bank notes in circulation, which are measured at face value. The Bank has not classified any of its financial liabilities as fair value through net income.

The Bank derecognizes financial liabilities when, and only when, the Bank’s obligations are discharged, cancelled or expire. The difference between the carrying amount of the financial liability derecognized and the sum of the consideration paid and payable, including any non-cash assets transferred or liabilities assumed, is recognized in net income.

c) Securities purchased under resale agreements

Securities purchased under resale agreements are reverse repo-type transactions in which the Bank purchases securities from designated counterparties with an agreement to sell them back at a predetermined price on an agreed transaction date. For accounting purposes, these agreements are treated as collateralized lending transactions and are recorded on the *Statement of Financial Position* at the amounts at which the securities were originally acquired plus accrued interest.

d) Securities sold under repurchase agreements

Securities sold under repurchase agreements are repo-type transactions in which the Bank sells Government of Canada securities to designated counterparties with an agreement to buy them back at a predetermined price on an agreed transaction date. For accounting purposes, these agreements are treated as collateralized borrowing transactions and are recorded on the *Statement of Financial Position* at the amounts at which the securities were originally sold plus accrued interest.

e) Securities Lending Program

The Bank operates a Securities Lending Program to support the liquidity of Government of Canada securities by providing a secondary and temporary source of these securities to the market. These securities-lending transactions are fully collateralized by securities and are generally one business day in duration. The securities loaned continue to be accounted for as investment assets. Lending fees charged by the Bank on these transactions are included in *Other revenue* at the maturity date of the transaction.

f) Property and equipment

Property and equipment consists of land, buildings, computer hardware, other equipment and related projects in progress. *Property and equipment* is recorded at cost less accumulated depreciation, except for land which is not depreciated, and is net of any related impairment loss. Projects in progress are recorded at cost but not depreciated until the asset is available for use. Cost includes expenditures that are directly attributable to the acquisition of the asset.

When parts of an item of property and equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment. Upon replacing a significant part of an item of property and equipment, the carrying amount of the replaced part is derecognized.

Depreciation is calculated using the straight-line method and is applied over the estimated useful lives of the assets, as shown below. The estimated useful life and depreciation method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Buildings	25 to 65 years
Computer hardware	3 to 7 years
Other equipment	5 to 15 years

g) Intangible assets

Intangible assets are identified non-monetary assets without physical substance. The Bank's intangible assets consist of computer software internally developed or externally acquired.

Costs that are directly associated with the internal development of identifiable software are recognized as intangible assets if, in management's best estimate, the asset can technically be completed and will provide a future economic benefit to the Bank. Subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates.

Computer software assets that are acquired by the Bank and have finite useful lives are measured at cost less accumulated amortization and accumulated impairment losses.

Amortization is calculated using the straight-line method and is applied over the estimated useful lives of the assets, which may vary from 3 to 15 years. The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

h) Leases

Where the Bank is a lessee

Leases of equipment where the Bank has assumed substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the lease's inception at the lower of the fair value of the leased asset or the present value of the minimum lease payments. The corresponding lease obligations, net of finance charges, are included in *Other liabilities*. Each lease payment is allocated between the liability and finance charges to achieve a constant rate of return on the finance lease obligation outstanding. Equipment acquired under finance leases is depreciated over the shorter of the asset's useful life and the lease term.

Other leases are classified as operating leases. Payments made under operating leases are charged to the *Statement of Comprehensive Income* on a straight-line basis over the period of the lease.

Where the Bank is a lessor

Leases granted on the Bank's property were assessed and classified as operating leases because the risks and rewards of ownership are not transferred to the lessees. Operating lease income is recognized on a straight-line basis over the period of the lease.

i) Impairment

Impairment of financial assets

For financial assets that are not classified as fair value through net income, the Bank assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of assets is impaired. Once impaired, financial assets carried at amortized cost are remeasured at net recoverable amount with the amount of impairment recognized in net income. Unrealized losses on impaired AFS financial assets are recognized in net income at the time of impairment.

Impairment of non-financial assets

Non-financial assets, including property and equipment, intangible assets and inventories, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount exceeds its recoverable amount.

Intangible assets under development are assessed for impairment on an annual basis.

j) Employee benefits

Short-term employee benefits

Short-term employee benefits include cash salary, bonus, annual leave, health benefits, dental care and statutory benefits and are measured on an undiscounted basis.

Long-term employee benefits

The Bank sponsors a long-term disability program.

The liability recognized in respect of this plan amounts to the present value of the defined-benefit obligation. The present value of the defined-benefit obligation is calculated by discounting estimated future cash flows using interest rates of high-quality corporate bonds with terms to maturity approximating the duration of the obligation. The expense recognized for the fiscal year consists of current service costs, interest costs, actuarial gains and losses, and past service costs.

The current service costs and the benefit obligations of the plan are actuarially determined on an event-driven accounting basis. Actuarial gains or losses are recognized immediately in net income in the period in which they occur. Past service costs arising from plan amendments are recognized immediately in *Staff costs* in the period in which they occur.

Post-employment defined-benefit plans

The Bank sponsors a funded defined-benefit pension plan (the Bank of Canada Registered Pension Plan) and a funded defined-benefit supplementary pension arrangement (the Bank of Canada Supplementary Pension Arrangement), which are designed to provide retirement income benefits to eligible employees. Benefits provided under these plans are calculated based on years of service and average full-time salary for the best five consecutive years and are indexed to reflect changes in the consumer price index on the date payments begin and each 1 January thereafter.

The Bank also sponsors other unfunded post-employment defined-benefit plans, which include life insurance and eligible health and dental benefits, as well as a long-service benefit program for employees hired before 1 January 2003.

The asset or liability recognized at fiscal year-end in respect of these plans is composed of the present value of the defined-benefit obligation less the fair value of plan assets, where applicable. The present value of the defined-benefit obligation is calculated by discounting estimated future cash flows using interest rates of high-quality corporate bonds with terms to maturity approximating the duration of the obligation. The expense recognized for the fiscal year consists of current service costs, interest costs, expected return on plan assets and past service costs.

The current service costs and the benefit obligations of the plans are actuarially determined using the projected unit credit method. Actuarial gains or losses arise from the difference between the actual rate of return and the expected rate of return on plan assets for that period and from changes in actuarial assumptions used to determine the accrued benefit obligation. Actuarial gains or losses are recognized immediately in the period in which they occur in *Other Comprehensive Income*. Past service costs arising from plan amendments that have vested are immediately recognized as an expense. Non-vested past service costs are amortized over the period until the related benefits become vested. Plan assets of funded obligations are determined according to their fair value at the end of the fiscal year.

k) Provisions

A provision is recognized if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably as at the statement of financial position date, and it is probable that an outflow of economic benefits will be required to settle the obligation.

l) Revenue recognition

Interest revenue earned on Government of Canada treasury bills and bonds is recorded using the effective interest method. Dividend revenue on the BIS shares is recorded as dividends are declared.

Realized gains (losses) on the sale of Government of Canada treasury bills are recorded at the time of sale as a reclassification from *Other Comprehensive Income* and are calculated as the excess of proceeds over the amortized cost at the transaction date.

Interest earned on securities purchased under resale agreements is recorded using the effective interest method.

Other revenue is composed mostly of interest earned on advances to members of the Canadian Payments Association (CPA) and is recorded using the effective interest method.

m) Bank notes expenses

The cost to produce finished bank notes is expensed as incurred.

n) Future changes in accounting policies

IFRS 9

IFRS 9 *Financial Instruments* (IFRS 9) as issued in November 2009 and revised in October 2010, and the related consequential amendments, will replace International Accounting Standard 39 *Financial Instruments: Recognition and Measurement* (IAS 39). IFRS 9 relates to the recognition and derecognition and measurement of financial assets and financial liabilities.

IFRS 9 eliminates the existing financial asset categories and requires all financial assets to be classified on initial recognition either at amortized cost or fair value on the basis of the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset.

Gains and losses on financial assets measured at fair value will be recognized through net income, with the exception of equity investments not held for trading, for which gains or losses will be recognized directly in equity.

The new standard also requires the use of a single impairment method for financial assets based on expected losses and incurred losses, replacing the multiple impairment methods in IAS 39.

IFRS 9 requires all financial liabilities not designated at fair value through net income to be subsequently measured at amortized cost using the effective interest method.

IFRS 9 is effective for annual periods beginning on or after 1 January 2015, although early adoption is permitted. The Bank is currently evaluating the impact of IFRS 9 on its financial statements, and will continue to do so as the remaining stages of this project, relating to hedge accounting and financial asset and liability offsetting, are finalized.

IFRS 7

IFRS 7 *Financial Instruments: Disclosures* (IFRS 7) was amended in October 2010 to provide additional disclosure on the transfer of financial assets, including the possible effects of any residual risks that the transferring entity retains. These amendments are effective for annual periods beginning on or after 1 July 2011. The Bank is currently evaluating the impact of these amendments to IFRS 7 on its financial statements.

IFRS 11

On 12 May 2011, the International Accounting Standards Board (IASB) issued IFRS 11 *Joint Arrangements* (IFRS 11). IFRS 11 provides for a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The standard addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities. IFRS 11 is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. The Bank is currently evaluating the impact, if any, of this new standard on its financial statements.

IFRS 12

On 12 May 2011, the IASB issued IFRS 12 *Disclosure of Interests in Other Entities* (IFRS 12). IFRS 12 is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities.

IFRS 12 is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. The Bank is currently evaluating the impact, if any, of this new standard on its financial statements.

IFRS 13

On 12 May 2011, the IASB issued IFRS 13 *Fair Value Measurement* (IFRS 13). IFRS 13, which is effective from 1 January 2013, defines fair value, sets out in a single IFRS a framework for measuring fair value and requires disclosures about fair-value measurements. IFRS 13 does not determine when an asset, a liability or an entity's own equity instrument is measured at fair value. Rather, the measurement and disclosure requirements of IFRS 13 apply when another IFRS requires or permits the item to be measured at fair value (with limited exceptions). The Bank is currently evaluating the impact, if any, of this new standard on its financial statements.

IAS 19

IAS 19 *Employee Benefits* (IAS 19) was amended on 16 June 2011 to eliminate the use of the "corridor" approach and mandates that all remeasurement impacts to be recognized immediately, and also affects aspects of measurement and disclosure. These amendments are effective as of 1 January 2013. The Bank will not be impacted by the elimination of the corridor approach since the policy to immediately recognize all actuarial gains and losses was adopted at the time of the Bank's transition to IFRS. The Bank is currently evaluating the impact on its financial statements of other amendments to IAS 19.

4. Cash and foreign deposits

Cash and foreign deposits is composed of cash on hand as well as highly liquid demand deposits in foreign currencies with other central banks or international financial institutions. Included in this balance is Can$5.6 million (Can$1.2 million at 31 December 2010 and Can$3.3 million at 1 January 2010) of U.S. dollars.

5. Loans and receivables

Loans and receivables are composed primarily of securities purchased under resale agreements and, if any, advances to members of the Canadian Payments Association. These transactions are fully collateralized in accordance with publicly disclosed collateral eligibility and margin requirements. Financial risks related to these instruments are discussed in note 7.

a) Securities purchased under resale agreements

Securities purchased under resale agreements for terms of one business day are acquired through buyback transactions with primary dealers in Government of Canada securities to reinforce the target overnight interest rate.

Securities purchased under resale agreements for terms of longer than one business day are acquired through an auction process for the purposes of providing liquidity in support of the efficient functioning of financial markets. Details of these auctions are announced by the Bank in advance. Bids are submitted on a yield basis, and funds are allocated in descending order of bid yields.

Balances outstanding at 31 December 2011 consist of an agreement with an original term to maturity of 14 days. (Balances outstanding at 31 December 2010 consist of agreements with original terms to maturity ranging from 20 to 34 days. Balances outstanding at 1 January 2010 consist of agreements with original terms to maturity ranging from 84 to 363 days.)

b) Advances to members of the Canadian Payments Association

Advances to members of the CPA are typically composed of liquidity loans made under the Bank's Standing Liquidity Facility. These advances mature the next business day. Interest on overnight advances is calculated at the Bank Rate. The Bank Rate is the rate of interest that the Bank charges on one-day loans to major financial institutions.

6. Investments

There were no securities loaned under the Securities Lending Program at 31 December 2011 ($Nil at 31 December 2010 and $Nil at 1 January 2010).

In *Other investments*, the Bank holds 9,441 BIS shares in order to participate in the BIS. Ownership of the BIS shares is limited to central banks, and new shares can only be acquired following an invitation to subscribe extended by the BIS Board of Directors. The shares are non-transferable unless prior written consent is obtained from the BIS.

7. Financial instruments and risk management

The Bank's financial instruments consist of cash and foreign deposits, securities purchased under resale agreements, advances to members of the Canadian Payments Association, other receivables, investments (consisting of Government of Canada treasury bills, Government of Canada bonds and shares in the BIS), bank notes in circulation, deposits and other liabilities (excluding post-employment and long-term employee benefit obligations).

Cash and foreign deposits, Government of Canada treasury bills and BIS shares are measured at fair value. All other financial instruments are measured at amortized cost using the effective interest method, with the exception of bank notes in circulation, which are measured at face value.

a) Fair value of financial instruments

(i) Carrying amount and fair value of financial instruments

The carrying amount and fair values of financial assets and liabilities are presented in the following table:

	31 December 2011		31 December 2010		1 January 2010	
	Carrying amount	Fair value	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets						
Cash and foreign deposits	**11.7**	**11.7**	4.7	4.7	20.4	20.4
Securities purchased under resale agreements	**1,447.7**	**1,447.7**	2,062.4	2,062.4	25,374.8	25,377.5
Advances to members of the Canadian Payments Association	**81.5**	**81.5**	22.5	22.5	-	-
Other receivables	**1.6**	**1.6**	2.1	2.1	2.2	2.2
Government of Canada treasury bills	**18,545.6**	**18,545.6**	24,906.1	24,906.1	13,684.0	13,684.0
Government of Canada bonds	**43,553.3**	**48,511.0**	33,550.6	36,296.4	31,986.2	34,128.0
Other investments	**325.3**	**325.3**	310.7	310.7	318.7	318.7
Total financial assets	**63,966.7**	**68,924.4**	60,859.1	63,604.9	71,386.3	73,530.8
Financial liabilities						
Bank notes in circulation	**61,028.8**	**61,028.8**	57,874.2	57,874.2	55,467.9	55,467.9
Deposits	**2,481.0**	**2,481.0**	2,556.8	2,556.8	15,550.2	15,550.2
Other financial liabilities	**132.1**	**132.1**	216.9	216.9	61.7	61.7
Total financial liabilities	**63,641.9**	**63,641.9**	60,647.9	60,647.9	71,079.8	71,079.8

(ii) Financial instruments measured at fair value

Financial instruments recorded at fair value are classified using a fair-value hierarchy that reflects the significance of the inputs used in making the measurements:

Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the assets or liabilities, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and

Level 3 – inputs for the assets or liabilities that are not based on observable market data (unobservable inputs).

The fair-value hierarchy requires the use of observable market inputs wherever such inputs exist. A financial instrument is classified at the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

	Level 1	Level 2	Level 3	Total
Financial assets at fair value as at 31 December 2011				
Cash and foreign deposits	**11.7**	**-**	**-**	**11.7**
Government of Canada treasury bills	**18,545.6**	**-**	**-**	**18,545.6**
BIS shares	**-**	**-**	**325.3**	**325.3**
	18,557.3	**-**	**325.3**	**18,882.6**
Financial assets at fair value as at 31 December 2010				
Cash and foreign deposits	4.7	-	-	4.7
Government of Canada treasury bills	24,906.1	-	-	24,906.1
BIS shares	-	-	310.7	310.7
	24,910.8	-	310.7	25,221.5
Financial assets at fair value as at 1 January 2010				
Cash and foreign deposits	20.4	-	-	20.4
Government of Canada treasury bills	13,684.0	-	-	13,684.0
BIS shares	-	-	318.7	318.7
	13,704.4	-	318.7	14,023.1

There were no transfers of amounts between Level 1 and Level 2 in 2011.

The fair value of the BIS shares is estimated as being 70 per cent of the Bank's interest in the BIS's net asset value (NAV) at the reporting date. This 30 per cent discount to NAV is based on a decision by the International Court at the Hague relating to a share repurchase by the BIS in 2001 and has been used by the BIS to determine the pricing of any new shares issued since that time. While the Bank considers that the 30 per cent discount against the BIS's net asset value continues to be the appropriate basis for valuation, the valuation inputs are not considered to be observable.

The following table reconciles the estimated fair value of the BIS shares determined using Level 3 fair value measurements for the period from 1 January to 31 December:

	31 December 2011	31 December 2010
Opening balance at beginning of year	**310.7**	318.7
Estimated fair-value (gain)/loss for the year recorded through OCI	**14.6**	(8.0)
Closing balance at end of year	**325.3**	310.7

(iii) Financial instruments not measured at fair value

Fair values of securities purchased under resale agreements are determined using market yields to maturity for similar instruments available at the statement of financial position date.

Fair values of Government of Canada bonds are determined based on unadjusted quoted market prices in an active market.

The carrying amount of cash and foreign deposits, advances to members of the Canadian Payments Association, other receivables, deposits and other financial liabilities (which is composed of other liabilities, excluding the portion representing accrued benefits liabilities as described in note 14) approximates fair value, given their short-term nature. The face value of bank notes in circulation is equal to their fair value.

b) Financial risk

The Bank has a well-established framework for identifying, managing and monitoring pertinent areas of risk. This framework is supported by the Board of Directors which ensures that the Bank has a robust risk-management process in place. The Bank is exposed to financial risk (credit risk, market risk, and liquidity risk) associated with the management of the Bank's assets and liabilities. The Financial Risk Office, which is independent of operations, monitors and reports on the financial risks relating to the Bank's balance sheet. The following is a description of those risks and how the Bank manages its exposure to them.

(i) Credit risk

Credit risk is the risk that a counterparty to a financial contract will fail to discharge its obligations in accordance with agreed-upon terms.

The Bank is exposed to credit risk through its cash and foreign deposits, investment portfolio, advances to members of the Canadian Payments Association, and through market transactions conducted in the form of securities purchased under resale agreements and loans of securities. The maximum exposure to credit risk is estimated to be the carrying value of the items listed above. There are no past due or impaired amounts.

Advances to members of the CPA and securities purchased under resale agreements are fully collateralized loans. Collateral is taken in accordance with the Bank's publicly disclosed eligibility criteria and margin requirements accessible on its website. Strict eligibility criteria are set for all collateral, and the Bank requires excess collateral relative to the size of the loan provided.

In the unlikely event of a counterparty default, collateral can be liquidated to offset credit exposure. The credit quality of collateral is managed through a set of restrictions based on asset type, term to maturity, and the credit ratings of the securities pledged.

Concentration of credit risk

Credit risk of the Bank's investment portfolio, representing 97 per cent of the carrying value of its total assets (97 per cent in 2010), is low because the securities held are primarily direct obligations of the Government of Canada which holds a credit rating of AAA. The Bank's advances to members of the CPA and securities purchased under resale agreements, representing 2 per cent of the carrying value of its total assets (3 per cent in 2010), are collateralized obligations of various Canadian-based financial institutions.

The fair value of collateral held against securities purchased under resale agreements at the end of the reporting period is $1,481.0 million, representing 102 per cent of the amortized cost of $1,447.7 million.

Collateral is concentrated in the following major categories:

	31 December 2011		31 December 2010		1 January 2010	
	$	**%**	**$**	**%**	**$**	**%**
Securities issued or guaranteed by the Government of Canada	**1,481.0**	**100.0**	2,126.9	100.0	15,517.3	58.3
Securities issued or guaranteed by a provincial government	-	-	-	-	8,621.4	32.3
Securities issued by a municipality	-	-	-	-	239.6	0.9
Corporate securities	-	-	-	-	1,918.5	7.2
Asset-backed commercial paper	-	-	-	-	359.0	1.3
Total fair value of collateral pledged	**1,481.0**	**100.0**	2,126.9	100.0	26,655.8	100.0
As a percentage of amortized cost		**102%**		103%		105%

Large Value Transfer System (LVTS) Guarantee

The Bank is exposed to credit risk through its guarantee of the LVTS. The maximum exposure under this guarantee is described in note 18, *Commitments, contingencies and guarantees*.

(ii) Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: interest rate risk, currency risk, and other price risk.

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Bank's investment in Government of Canada treasury bills and bonds counteract the non-interest-bearing bank notes in circulation liability, and supports the Bank's operational independence to conduct monetary policy. These assets are acquired in proportions that broadly resemble the structure of the Government of Canada's domestic debt outstanding to reduce interest rate risk from the perspective of the Government of Canada.

The Bank's exposure to fair-value interest rate risk arises principally through its investment in Government of Canada treasury bills, which are short term in duration, and Government of Canada bonds. The fair value of the treasury bills of Canada portfolio held by the Bank is exposed to fluctuations owing to changes in market interest rates since these securities are classified as AFS and are measured at fair value. Unrealized gains and losses on the treasury bills of Canada portfolio are recognized in the *Available-for-sale reserve* in the *Equity* section of the S*tatement of financial position* until they mature or are sold. Government of Canada bonds are carried at amortized cost and are acquired with the intention of holding them to maturity. All other financial assets or liabilities with an interest rate component are carried at amortized cost or at face value.

The Bank's revenue will vary over time in response to future movements in interest rates. These variations would not affect the ability of the Bank to fulfill its obligations since its revenues greatly exceed its expenses.

The figures below show the effect at 31 December of an (increase)/decrease of 25 basis points in interest rates on the fair value of the Government of Canada treasury bill portfolio and other comprehensive income.

	31 December 2011	**31 December 2010**
Government of Canada treasury bills	**$ (15.9) / 15.4**	$ (21.3) / 20.0

The Bank's exposure to interest rate risk in the form of fluctuations in future cash flows of existing financial instruments is limited to Government of Canada deposits and cash and foreign deposits, since these instruments are subject to variable interest rates. The remainder of the Bank's financial assets and liabilities have either fixed interest rates or are non-interest-bearing.

The figures below show the effect at 31 December of an increase/(decrease) of 25 basis points in interest rates on the interest expenses paid on Government of Canada deposits.

	31 December 2011	**31 December 2010**
Interest expense on Government of Canada deposits	**$5.0 / (5.0)**	$17.8 / (17.8)

For all financial instruments, except bank notes in circulation, the future cash flows of the Bank are dependent on the prevailing market rate of interest at the time of renewal.

The following table illustrates interest rate risk relative to future cash flows by considering the expected maturity or repricing dates of existing financial assets and liabilities.

								As at 31 December 2011
	Weighted-average interest rate %	Total	Non-interest-sensitive	1 business day to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years
FINANCIAL ASSETS								
Cash and foreign deposits	**0.03**	**11.7**	**-**	**11.7**	**-**	**-**	**-**	**-**
Loans and receivables								
Advances to members of the CPA	**1.25**	**81.5**	**-**	**81.5**	**-**	**-**	**-**	**-**
Securities purchased under resale agreements	**1.06**	**1,447.7**	**-**	**1,447.7**	**-**	**-**	**-**	**-**
Other receivables		**1.6**	**1.6**	**-**	**-**	**-**	**-**	**-**
Investments								
Government of Canada treasury bills	**1.01**	**2,999.3**	**-**	**2,999.3**	**-**	**-**	**-**	**-**
	0.97	**6,666.1**	**-**	**-**	**6,666.1**	**-**	**-**	**-**
	1.07	**8,880.2**	**-**	**-**	**-**	**8,880.2**	**-**	**-**
	1.03	**18,545.6**						
Government of Canada bonds[1]	**1.47**	**452.2**	**-**	**-**	**452.2**	**-**	**-**	**-**
	3.47	**4,573.2**	**-**	**-**	**-**	**4,573.2**	**-**	**-**
	2.56	**23,129.2**	**-**	**-**	**-**	**-**	**23,129.2**	**-**
	4.24	**15,398.7**	**-**	**-**	**-**	**-**	**-**	**15,398.7**
	3.23	**43,553.3**						
Shares in the BIS		**325.3**	**325.3**	**-**	**-**	**-**	**-**	**-**
		63,966.7	**326.9**	**4,540.2**	**7,118.3**	**13,453.4**	**23,129.2**	**15,398.7**
FINANCIAL LIABILITIES								
Bank notes in circulation		**61,028.8**	**61,028.8**	**-**	**-**	**-**	**-**	**-**
Deposits								
Government of Canada	**0.86**	**1,512.5**	**-**	**1,512.5**	**-**	**-**	**-**	**-**
Members of the CPA	**0.75**	**106.7**	**-**	**106.7**	**-**	**-**	**-**	**-**
Other deposits								
Unclaimed balances		**466.6**	**466.6**	**-**	**-**	**-**	**-**	**-**
Other	**0.85**	**395.2**	**-**	**395.2**	**-**	**-**	**-**	**-**
Other financial liabilities		**132.1**	**132.1**	**-**	**-**	**-**	**-**	**-**
		63,641.9	**61,627.5**	**2,014.4**	**-**	**-**	**-**	**-**
Interest rate sensitivity gap		**324.8**	**(61,300.6)**	**2,525.8**	**7,118.3**	**13,453.4**	**23,129.2**	**15,398.7**

1. Carrying amounts of Government of Canada bonds include accrued interest.

								As at 31 December 2010
	Weighted-average interest rate %	Total	Non-interest-sensitive	1 business day to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years
FINANCIAL ASSETS								
Cash and foreign deposits	0.13	4.7	-	4.7	-	-	-	-
Loans and receivables								
Advances to members of the CPA	1.25	22.5	-	22.5	-	-	-	-
Securities purchased under resale agreements	1.02	2,062.4	-	2,062.4	-	-	-	-
Other receivables		2.1	2.1	-	-	-	-	-
Investments								
Government of Canada treasury bills	0.85	4,498.8	-	4,498.8	-	-	-	-
	0.94	8,835.7	-	-	8,835.7	-	-	-
	1.17	11,571.6	-	-	-	11,571.6	-	-
	1.03	24,906.1						
Government of Canada bonds[1]	9.40	212.7	-	-	212.7	-	-	-
	4.08	5,226.8	-	-	-	5,226.8	-	-
	3.41	14,683.7	-	-	-	-	14,683.7	-
	4.74	13,427.4	-	-	-	-	-	13,427.4
	4.08	33,550.6						
Shares in the BIS		310.7	310.7	-	-	-	-	-
		60,859.1	312.8	6,588.4	9,048.4	16,798.4	14,683.7	13,427.4
FINANCIAL LIABILITIES								
Bank notes in circulation		57,874.2	57,874.2	-	-	-	-	-
Deposits								
Government of Canada	1.13	1,869.4	-	1,869.4	-	-	-	-
Members of the CPA	0.75	47.5	-	47.5	-	-	-	-
Other deposits								
Unclaimed balances		433.5	433.5	-	-	-	-	-
Other	0.81	206.4	-	206.4	-	-	-	-
Other financial liabilities		216.9	216.9	-	-	-	-	-
		60,647.9	58,524.6	2,123.3	-	-	-	-
Interest rate sensitivity gap		211.2	(58,211.8)	4,465.1	9,048.4	16,798.4	14,683.7	13,427.4

1. Carrying amounts of Government of Canada bonds include accrued interest.

Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The Bank is exposed to currency risk primarily by holding shares in the BIS. These shares are denominated in Special Drawing Rights (SDRs). The SDR serves as the unit of account for the International Monetary Fund (IMF) and its value is based on a "basket" of four major currencies: the euro, the U.S. dollar, the pound sterling and the Japanese yen. Since SDRs are translated into Canadian-dollar equivalents at rates prevailing at the date when the fair value is determined, the carrying value approximates fair value on the reporting date.

Consistent with 2010, at 31 December 2011, the Bank did not hold a significant amount of U.S. dollars.

Given the small size of the net foreign currency exposure relative to the total assets of the Bank, currency risk is not considered significant.

Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from changes in interest and exchange rates), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

The Bank is exposed to other price risk through its investment in the BIS. For accounting purposes, the Bank treats BIS shares as AFS and the fair value of these shares is estimated on the basis of the BIS's net asset value, less a discount of 30 per cent. Accordingly, these shares are revalued to reflect movements in the net asset value of the BIS and in the Canadian dollar. The price risk faced on BIS shares is incidental to the general reasons for holding them and is immaterial compared with other market risks faced by the Bank.

(iii) Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. As shown in the following table, the Bank's largest liability is *Bank notes in circulation*. As a counterpart to this non-interest-bearing liability with no fixed maturity, the Bank holds a portfolio of highly liquid, interest-bearing securities. In the event of an unexpected redemption of bank notes, the Bank has the ability to settle the obligation by selling its assets.

As the nation's central bank, the Bank is the ultimate source of liquid funds to the Canadian financial system, and has the power and operational ability to create Canadian-dollar liquidity in unlimited amounts at any time. This power is exercised within the Bank's commitment to keep inflation low, stable, and predictable.

Large Value Transfer System (LVTS) Guarantee

The Bank is exposed to liquidity risk through its guarantee of the LVTS. The maximum exposure under this guarantee is described in note 18, *Commitments, contingencies and guarantees*.

The following table presents a maturity analysis of the Bank's financial assets and liabilities. The balances in this table do not correspond to the balances in the *Statement of Financial Position*, since the table presents all cash flows on an undiscounted basis.

As at 31 December 2011

	Total	No fixed maturity	1 business day	1 business day to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years
FINANCIAL ASSETS								
Cash and foreign deposits	11.7	11.7	-	-	-	-	-	-
Loans and receivables								
Advances to members of the CPA	81.5	-	81.5	-	-	-	-	-
Securities purchased under resale agreements	1,447.7	-	-	1,447.7	-	-	-	-
Other receivables	1.6	-	-	1.6	-	-	-	-
Investments								
Government of Canada treasury bills	18,600.0	-	-	3,000.0	6,675.0	8,925.0	-	-
Government of Canada bonds[1]	42,994.6	-	-	-	450.0	4,560.0	22,990.8	14,993.8
Shares in the BIS	325.3	325.3	-	-	-	-	-	-
	63,462.4	337.0	81.5	4,449.3	7,125.0	13,485.0	22,990.8	14,993.8
FINANCIAL LIABILITIES								
Bank notes in circulation	61,028.8	61,028.8	-	-	-	-	-	-
Deposits								
Government of Canada	1,512.5	1,512.5	-	-	-	-	-	-
Members of the CPA	106.7	-	106.7	-	-	-	-	-
Other deposits								
Unclaimed balances	466.6	466.6	-	-	-	-	-	-
Other	395.2	395.2	-	-	-	-	-	-
Other liabilities	132.1	-	-	132.1	-	-	-	-
	63,641.9	63,403.1	106.7	132.1	-	-	-	-
Net maturity difference	(179.5)	(63,066.1)	(25.2)	4,317.2	7,125.0	13,485.0	22,990.8	14,993.8

1. Interest payments on Government of Canada bonds are classified according to their coupon date.

In cases where counterparties to securities purchased under resale agreements substitute collateral after the outset of an agreement, portions of the carrying values presented may mature earlier than as presented, where the amount maturing early is dependent on the value of the collateral being substituted. Where collateral has been substituted, agreements are typically re-established under the same terms and conditions. The information presented in the above table is prepared according to agreements in place as at 31 December 2011.

Liabilities with no fixed maturity include *Bank notes in circulation* and *Government of Canada Deposits*. Historical experience has shown that bank notes in circulation provide a stable source of long-term funding for the Bank. *Government of Canada Deposits* are deposits held in the Bank's capacity as the Government of Canada's fiscal agent.

As at 31 December 2010

	Total	No fixed maturity	1 business day	1 business day to 1 month	1 to 3 months	3 to 12 months	1 to 5 years	Over 5 years
FINANCIAL ASSETS								
Cash and foreign deposits	4.7	4.7	-	-	-	-	-	-
Loans and receivables								
Advances to members of the CPA	22.5	-	22.5	-	-	-	-	-
Securities purchased under resale agreements	2,062.4	-	-	2,062.4	-	-	-	-
Other receivables	2.1	-	-	2.1	-	-	-	-
Investments								
Government of Canada treasury bills	25,000.0	-	-	4,500.0	8,850.0	11,650.0	-	-
Government of Canada bonds[1]	33,072.1	-	-	-	206.6	5,200.9	14,585.8	13,078.8
Shares in the BIS	310.7	310.7	-	-	-	-	-	-
	60,474.5	315.4	22.5	6,564.5	9,056.6	16,850.9	14,585.8	13,078.8
FINANCIAL LIABILITIES								
Bank notes in circulation	57,874.2	57,874.2	-	-	-	-	-	-
Deposits								
Government of Canada	1,869.4	1,869.4	-	-	-	-	-	-
Members of the CPA	47.5	-	47.5	-	-	-	-	-
Other deposits								
Unclaimed balances	433.5	433.5	-	-	-	-	-	-
Other	206.4	206.4	-	-	-	-	-	-
Other liabilities	216.9	-	-	216.9	-	-	-	-
	60,647.9	60,383.5	47.5	216.9	-	-	-	-
Net maturity difference	(173.4)	(60,068.1)	(25.0)	6,347.6	9,056.6	16,850.9	14,585.8	13,078.8

1. Interest payments on Government of Canada bonds are classified according to their coupon date.

8. Property and equipment

	Land and Buildings	Computer Equipment	Other Equipment	Total
2011				
Cost				
Balances, 1 January 2011	197.3	25.8	122.2	345.3
Additions	21.1	10.2	4.9	36.2
Disposals	(0.2)	(5.2)	(27.6)	(33.0)
Transfers to other asset categories	-	-	-	-
Balances, 31 December 2011	218.2	30.8	99.5	348.5
Depreciation				
Balances, 1 January 2011	(80.1)	(13.9)	(98.3)	(192.3)
Depreciation expense	(5.0)	(3.5)	(4.0)	(12.5)
Disposals	-	5.2	27.6	32.8
Transfers to other asset categories	-	-	-	-
Balances, 31 December 2011	(85.1)	(12.2)	(74.7)	(171.9)
Carrying amounts				
At 1 January 2011	117.2	11.9	23.9	153.0
At 31 December 2011	133.1	18.6	24.8	176.6

	Land and Buildings	Computer Equipment	Other Equipment	Total
Projects in progress 2011				
Included in Net book value	25.1	12.3	4.6	42.0
Additions during 2011	20.5	10.2	4.4	35.1
Commitments at 31 December 2011	0.6	0.3	-	0.9

Projects in progress consist primarily of $26.2 million related to the Enhanced Business Continuity initiative (31 December 2010 - $3.0 million; 1 January 2010 - $0.1 million), $4.9 million related to the Head Office Renewal Program (31 December 2010 - $1.6 million; 1 January 2010 - $0.1 million), $1.2 million related to the Currency Systems Evolution Program (31 December 2010 - $1.2 million; 1 January 2010 - $Nil) and $1.0 million related to the BPS adaptation (31 December 2010 - $Nil; 1 January 2010 - $Nil). The completed streams of the Analytic Environment Program (31 December 2010 - $3.1 million; 1 January 2010 - $3.1 million) were put in service in 2011 and removed from Projects in progress.

	Land and Buildings	Computer Equipment	Other Equipment	Total
2010				
Cost				
Balances, 1 January 2010	185.8	29.2	130.0	345.0
Additions	5.6	2.2	2.9	10.7
Disposals	-	(5.8)	(4.8)	(10.6)
Transfers to other asset categories	5.9	0.2	(5.9)	0.2
Balances, 31 December 2010	197.3	25.8	122.2	345.3
Depreciation				
Balances, 1 January 2010	(74.1)	(16.1)	(99.6)	(189.8)
Depreciation expense	(5.2)	(3.6)	(3.8)	(12.6)
Disposals	-	5.8	4.3	10.1
Transfers to other asset categories	(0.8)	-	0.8	-
Balances, 31 December 2010	(80.1)	(13.9)	(98.3)	(192.3)
Carrying amounts				
At 1 January 2010	111.7	13.1	30.4	155.2
At 31 December 2010	117.2	11.9	23.9	153.0
Projects in progress 2010				
Included in Net book value	5.9	5.2	1.1	12.2
Additions during 2010	5.3	2.1	1.1	8.5
Commitments at 31 December 2010	1.5	0.1	1.1	2.7

9. Intangible assets

	Internally generated software	Other software	Total
2011			
Cost			
Balances, 1 January 2011	**42.8**	**16.8**	**59.6**
Additions	**-**	**23.5**	**23.5**
Disposals	**-**	**-**	**-**
Transfers to other asset categories	**-**	**(0.1)**	**(0.1)**
Balances, 31 December 2011	**42.8**	**40.2**	**83.0**
Amortization			
Balances, 1 January 2011	**(21.9)**	**(11.8)**	**(33.7)**
Amortization expense	**(3.9)**	**(0.8)**	**(4.7)**
Disposals	**-**	**-**	**-**
Transfers to other asset categories	**-**	**-**	**-**
Balances, 31 December 2011	**(25.8)**	**(12.6)**	**(38.4)**
Carrying amounts			
At 1 January 2011	**20.9**	**5.0**	**25.9**
At 31 December 2011	**17.0**	**27.6**	**44.6**

Projects in progress 2011			
Included in Net book value	**-**	**25.6**	**25.6**
Additions during 2011	**-**	**23.5**	**23.5**
Commitments at 31 December 2011	**0.9**	**-**	**0.9**

Projects in progress consist primarily of $11.2 million related to the Auctions and Market Applications Program (31 December 2010 - $1.0 million; 1 January 2010 - $Nil), $7.8 million related to the Currency Systems Evolution Program (31 December 2010 - $0.6 million; 1 January 2010 - $Nil), $1.5 million related to the BPS adaptation (31 December 2010 - $Nil; 1 January 2010 - $Nil) and $4.0 million related to the data management stream of the Analytic Environment Program, the completed streams of the Analytic Environment Program (31 December 2010 - $13.4 million; 1 January 2010 - $11.2 million) were put in service in 2011 and removed from Projects in progress.

	Internally generated software	Other software	Total
2010			
Cost			
Balances, 1 January 2010	48.0	13.0	61.0
Additions	2.2	2.2	4.4
Disposals	(5.6)	-	(5.6)
Transfers to other asset categories	(1.8)	1.6	(0.2)
Balances, 31 December 2010	42.8	16.8	59.6
Amortization			
Balances, 1 January 2010	(26.0)	(11.3)	(37.3)
Amortization expense	(1.5)	(0.5)	(2.0)
Disposals	5.6	-	5.6
Transfers to other asset categories	-	-	-
Balances, 31 December 2010	(21.9)	(11.8)	(33.7)
Carrying amounts			
At 1 January 2010	22.0	1.7	23.7
At 31 December 2010	20.9	5.0	25.9
Projects in progress 2010			
Included in Net book value	11.7	4.0	15.7
Additions during 2010	2.2	2.2	4.4
Commitments at 31 December 2010	-	-	-

10. Other assets

	31 December 2011	31 December 2010	1 January 2010
Accrued pension benefit asset (note 14)	**31.4**	166.6	196.3
All other assets	**27.9**	11.5	15.3
Total other assets	**59.3**	178.1	211.6

11. Bank notes in circulation

In accordance with the Bank of Canada Act, the Bank has the sole authority to issue bank notes for circulation in Canada. A breakdown by denomination is presented below.

	31 December 2011	31 December 2010	1 January 2010
$5	**1,138.0**	1,038.4	1,054.8
$10	**1,197.3**	1,159.8	1,125.7
$20	**16,894.1**	16,808.2	16,643.0
$50	**9,447.7**	8,443.7	7,773.0
$100	**31,027.1**	28,964.9	27,535.6
Other bank notes	**1,324.6**	1,459.2	1,515.8
Bank notes in circulation	**61,028.8**	57,874.2	55,647.9

Other bank notes include denominations that are no longer issued but remain as legal tender. Bank notes in circulation are non-interest-bearing liabilities and are due on demand.

12. Deposits

The liabilities within this category consist of $2,481.0 million in Canadian-dollar demand deposits (Can$2,556.8 million at 31 December 2010 and Can$15,550.2 million at 1 January 2010). The Bank pays interest on the deposits for the Government of Canada, banks and other financial institutions at market-related rates, and interest expense on deposits is included in the *Statement of Comprehensive Income*. Further information on the rates of interest is presented in the interest rate risk table in note 7.

13. Other liabilities

	31 December 2011	31 December 2010	1 January 2010
Post-employment defined-benefit obligations (note 14)	**180.7**	151.4	128.1
Accrued transfer payment to the Receiver General for Canada	**78.4**	167.5	23.6
All other liabilities	**53.7**	49.4	38.1
Total other liabilities	**312.8**	368.3	189.8

The accrued transfer payment to the Receiver General for Canada is included in the $1,067 million transfer to the Receiver General for the year presented in the *Statement of changes in equity* (31 December 2010 - $1,192.5 million).

For the year ended 31 December 2011, an amount of $126.1 million related to 2010 net income and $1,030 million related to 2011 net income was remitted to the Receiver General for Canada ($23.6 million in 2010 related to 2009 net income). Unpaid net income of $78.4 million (31 December 2010 - $167.5 million) is included under *Other liabilities* on the *Statement of Financial Position*.

In 2010, the Bank recognized employee severance expenses in connection with two restructuring initiatives: a program to achieve greater operational efficiency and effectiveness which resulted in a reduction in the number of corporate administration employees in 2011, and the sale of its Optical Security Material operations in 2011. In relation to the two restructurings, an expense of $11 million for employee severance costs was recognized in 2010 in Staff costs and accrued in Other liabilities. Payments made in 2011 in relation to the two restructuring initiatives is $4.1 million and the remaining accrued liability amounts to $6.9 million.

14. Employee benefit plans

The Bank measures its accrued benefits obligations and fair value of plan assets for accounting purposes as at 31 December of each year. The most recent actuarial valuation for funding purposes of the Registered Pension Plan was done as of 1 January 2011 and the next required valuation will be as of 1 January 2012.

The total cash payment for employee future benefits for 2011 was $52.2 million ($72.7 million in 2010), consisting of $43.1 million ($64.1 million in 2010) in cash contributed by the Bank to its pension plans and $9.1 million ($8.6 million in 2010) in cash payments directly to beneficiaries for its other post-employment benefit plans. The total cash payments expected for 2012 are $65.5 million, consisting of $57.7 million in cash contributed to its pension plans and $7.8 million in cash payments to its other post-employment benefit plans.

Benefit obligations and plan assets of post-employment defined-benefit and long-term benefit plans were composed of the following components during the year:

	Pension benefit plans[1]		Other benefit plans	
	31 December 2011	31 December 2010	31 December 2011	31 December 2010
Plan assets				
Fair value of plan assets at beginning of year	**1,081.8**	934.8	-	-
Actual return on plan assets				
Expected return on plan assets	**68.8**	60.3	-	-
Actuarial gains (losses)	**(18.1)**	53.0	-	-
	50.7	113.3	-	-
Bank contributions	**43.1**	64.1	-	-
Employee contributions	**11.0**	9.2	-	-
Benefit payments and transfers	**(43.5)**	(39.6)	-	-
Fair value of plan assets at end of year[2]	**1,143.1**	1,081.8	-	-
Benefit obligation				
Benefit obligation at beginning of year	**916.7**	738.5	**149.9**	128.1
Current service cost	**17.3**	14.4	**6.0**	5.0
Interest cost	**52.3**	51.3	**8.3**	8.5
Employee contributions	**11.0**	9.2	**-**	-
Past service costs	**1.4**	-	**-**	-
Actuarial losses	**172.5**	142.9	**9.6**	16.9
Benefit payments and transfers	**(43.5)**	(39.6)	**(9.1)**	(8.6)
Benefit obligation at end of year	**1,127.7**	916.7	**164.7**	149.9
Employee benefit asset/(liability)	**15.4**	165.1	**(164.7)**	(149.9)
Accrued pension benefit asset	**31.4**	166.6	**-**	-
Post-employment defined-benefit obligations	**(16.0)**	(1.5)	**(164.7)**	(149.9)
Employee benefit asset/(liability)	**15.4**	165.1	**(164.7)**	(149.9)

1. For the Supplementary Pension Arrangement, in which the accrued benefit obligation exceeds plan assets, the accrued benefit obligation and fair value of plan assets totalled $74.4 million ($58.1 million at 31 December 2010 and $46.2 million at 1 January 2010) and $58.4 million ($56.6 million at 31 December 2010 and $50.9 million at 1 January 2010), respectively.

2. The assets of the pension benefit plans were composed as follows: 53 per cent equities; 27 per cent bonds; 10 per cent Real Return Bonds; 5 per cent real estate assets; and 5 per cent short-term securities and cash (56 per cent; 26 per cent; 9 per cent; 4 per cent; and 5 per cent, respectively at 31 December 2010 and 56 per cent; 26 per cent; 9 per cent; 4 per cent; and 5 per cent, respectively at 1 January 2010).

Benefit plan expenses recognized in the *Statement of Comprehensive Income* are composed of the following components:

	Pension benefit plans		Other benefit plans	
	31 December 2011	**31 December 2010**	**31 December 2011**	**31 December 2010**
Current service cost, net of employee contributions	**17.3**	14.4	**6.0**	5.0
Interest cost	**52.3**	51.3	**8.3**	8.5
Actuarial (gain)/loss	**-**	-	**(2.3)**	1.0
Expected return on plan assets	**(68.8)**	(60.3)	**-**	-
Past services costs	**1.4**	-	**-**	-
Benefit plan expense recognized	**2.2**	5.4	**12.0**	14.5

Actuarial gains and losses pertaining to post-employment benefit plans are recognized in *Other Comprehensive Income* and cumulated in *Equity* in the Actuarial gains reserve.

Cumulative actuarial losses recognized in *Other Comprehensive Income*				
Cumulative actuarial losses recognized, beginning of year	**(89.9)**	-	**(15.9)**	-
Actuarial losses recognized in current year	**(190.5)**	(89.9)	**(11.9)**	(15.9)
Cumulative actuarial losses recognized, end of year	**(280.4)**	(89.9)	**(27.8)**	(15.9)

The significant assumptions used are as follows (on a weighted-average basis):

Accrued benefit obligation as at 31 December				
Discount rate	**4.60%**	5.75%	**4.44%**	5.50%
Rate of compensation increase	**3.30% + merit**	3.50% + merit	**3.30% + merit**	3.50% + merit
Benefit plan expense for year ended 31 December				
Discount rate	**5.75%**	7.00%	**5.50%**	6.60%
Expected rate of return on assets	**6.50%**	6.50%	**0%**	0%
Rate of compensation increase	**3.30% + merit**	3.50% + merit	**3.50% + merit**	3.50% + merit
Assumed medical cost trend				
Initial medical cost trend rate			**6.75%**	7.00%
Medical cost trend rate declines to			**4.50%**	4.50%
Year that the rate reaches the ultimate trend rate			**2029**	2029

The discount rate is determined by reference to Canadian AA-corporate bonds with terms to maturity approximating the duration of the obligation.

The expected rate of return on assets that is determined by management relates to the entire plan asset portfolio on a weighted-average basis, and is based on market expectations, at the beginning of the period, for returns over the entire life of the obligation. As such, the expected rate of return may not be indicative of short-term performance of Plan assets or of market conditions generally.

The assumption for life expectancy for the scheme valuations assumes that a male member reaching 60 in 2011 will live for 25 years (2010: 25 years) and a female member 27 years (2010: 27 years).

The mortality assumptions used in the scheme valuations are based on standard tables published by the Society of Actuaries, which were adjusted in line with both current industry and the actual experience of the relevant scheme.

Sensitivity analysis	Change in obligation	Change in expense
Impact of 0.50 percentage point increase/decrease in assumptions		
Pension benefit plans		
Change in discount rate	**96.4 / (84.9)**	**2.6 / (2.3)**
Change in long-term return on plan assets	**n.a / n.a**	**5.3 / (5.3)**
Other benefit plans		
Change in discount rate	**13.6 / (12.3)**	**0.4 / (0.3)**
Impact of 1.00 percentage point increase/decrease in assumptions		
Change in medical cost trend rates	**25.1 / (19.5)**	**2.2 / (1.5)**

Summary of historical adjustments	31 December 2011	31 December 2010	1 January 2010
Fair value of assets	**1,143.1**	1,081.8	934.8
Defined-benefit obligation	**(1,292.4)**	(1,066.6)	(866.6)
Surplus (deficit)	**(149.3)**	15.2	68.2
Experience adjustments on plan assets	**18.1**	(53.0)	-
Experience adjustments on plan benefits	**182.1**	159.8	-

15. Equity

The Bank's objectives in managing its capital, the elements of which are outlined in the table below, are in compliance with the Bank of Canada Act. The Bank is not in violation of any externally imposed capital requirements at the end of the reporting year. The Bank's objectives in managing its capital have not changed from the previous year.

	31 December 2011	31 December 2010	1 January 2010
Share capital	**5.0**	5.0	5.0
Statutory reserve	**25.0**	25.0	25.0
Special reserve	**100.0**	100.0	100.0
Available-for-sale reserve	**294.6**	271.0	287.5
Actuarial gains reserve	-	14.1	119.7
Retained earnings	-	1.7	31.7
	424.6	416.8	568.9

Share capital

The authorized capital of the Bank is $5.0 million divided into 100,000 shares with a par value of $50 each. The shares are fully paid and have been issued to the Minister of Finance, who is holding them on behalf of the Government of Canada.

Statutory reserve

The statutory reserve was accumulated out of net income until it reached the stipulated maximum amount of $25.0 million in 1955.

Special reserve

The special reserve was created in 2007 further to an amendment to the Bank of Canada Act to offset potential unrealized valuation losses due to changes in the fair value of the Bank's available-for-sale portfolio. The amount held in the special reserve is reviewed regularly for appropriateness using value-at-risk analysis and scenario-based stress tests and may be amended, pursuant to a resolution passed by the Board of Directors. The value-at-risk analysis uses historical data to estimate the maximum possible extent of unrealized valuation losses of the Bank's treasury bill portfolio. The scenario-based stress tests assess the impact of a rapid increase in interest rates on the value of the Bank's treasury bill portfolio. This reserve is subject to a ceiling of $400 million; an initial amount of $100 million was established in September 2007.

Available-for-sale reserve

The available-for-sale reserve represents cumulative movements in the fair value of the Bank's available-for-sale portfolios, as shown below.

	31 December 2011	**31 December 2010**	**1 January 2010**
Government of Canada treasury bills	**7.4**	(1.7)	6.8
BIS shares	**287.2**	272.7	280.7
Available-for-sale reserve	**294.6**	271.0	287.5

Actuarial gains reserve

The actuarial gains reserve was established upon the Bank's transition to IFRS at an initial amount of $119.7 million and accumulates the net actuarial gains and losses recognized on the Bank's post-employment defined-benefit plans subsequent to transition.

	31 December 2011	**31 December 2010**	**1 January 2010**
Actuarial gains reserve created on transition to IFRS	**119.7**	119.7	119.7
Accumulated actuarial loss	**(119.7)**	(105.6)	-
Actuarial gains reserve	**-**	14.1	119.7

Retained Earnings

The net income of the Bank, less any allocation to reserves, is considered to be ascertained surplus and is transferred to the Receiver General for Canada, consistent with the requirement of Section 27 of the Bank of Canada Act. Prior to 2010, the Bank did not hold Retained earnings.

Effective 1 January 2010, based on an agreement signed with the Minister of Finance, the Bank will deduct from its remittances to the Receiver General and hold within Retained earnings an amount equal to unrealized losses on AFS financial assets, unrealized actuarial losses on post-employment benefit plans and other unrealized or non-cash losses that would expose the Bank to the risk of negative capital arising as a result of changes in accounting standards or legislation. As at 31 December 2011, the Bank had withheld $188.4 million from its remittances ($1.7 million in 2010).

16. Operating expenses by function

Expenses are reported below on the basis of the four functions of the Bank described in note 1.

	31 December 2011	31 December 2010
Monetary policy	**68.3**	72.8
Financial system	**51.0**	52.6
Currency	**137.1**	145.5
Funds management	**96.7**	109.9
Total expenses	**353.1**	380.8

17. Leases

a) Operating leases commitments

The Bank occupies leased premises in Halifax, Montréal, Toronto, Calgary, and Vancouver. The minimum payments are determined at the beginning of the lease and may vary during the term of the lease. Contingent rent on premises leases is based on building operating costs; contingent rent is based on usage for office equipment leases.

At 31 December 2011, the future minimum payments are $10.7 million for rent, real estate taxes and building operations. The expiry dates vary for each lease, from October 2012 to October 2020.

Premises leases

	31 December 2011	31 December 2010	1 January 2010
Commitments			
Due within one year	**1.6**	1.4	1.6
Due within one to five years	**4.5**	3.9	3.7
Due later than five years	**4.6**	2.3	1.8
Total premises lease commitments	**10.7**	7.6	7.1

b) Lease payments receivable

The Bank owns buildings in Ottawa, Montréal and Toronto and leases space to Government of Canada departments and agencies under operating leases. Under the current non-cancellable lease agreements, the total minimum lease payments receivable and contingent rent included in income are as follows:

Lease payments receivable

	31 December 2011	31 December 2010	1 January 2010
Receivable within one year	**4.1**	3.8	2.9
Receivable within one to three years	**2.7**	2.0	5.8
Total lease payments receivable	**6.8**	5.8	8.7

18. Commitments, contingencies and guarantees

a) Long-term contracts other than leases

The Bank has a long-term contract with an outside service provider for retail debt services that expires in 2021. At 31 December 2011, fixed payments totalling $193.2 million remained, plus a variable component based on the volume of transactions.

In 2010, the Bank entered into a long-term agreement with an outside service provider for data centre services that commences in 2013 and expires in 2022. Fixed payments over the term of the agreement totalling $17.6 million will begin on 1 January 2013.

Minimum annual payments for long-term contracts other than leases

	Outsourced services
Due within one year	**20.3**
Due within one to three years	**44.2**
Due within three to five years	**44.2**
Thereafter	**102.1**
Total minimum annual payments	**210.8**

b) Foreign currency contracts

The Bank is a counterparty to several foreign currency swap facilities as follows:

	Maximum available
Bilateral liquidity swap facilities with central banks	
Bank of Japan (denominated in Japanese yen)	**Unlimited**
Swiss National Bank (denominated in Swiss francs)	**Unlimited**
Bank of England (denominated in British pounds)	**Unlimited**
European Central Bank (denominated in euros)	**Unlimited**
Federal Reserve Bank of New York (denominated in U.S. dollars)	**30,000.0**
Other swap facilities	
Exchange Fund Account of Canada (denominated in Canadian dollars)	**Unlimited**
Federal Reserve Bank of New York (denominated in U.S. dollars)	**2,000.0**
Banco de México (denominated in Canadian dollars)	**1,000.0**

Bilateral liquidity swap facilities with central banks

The temporary bilateral liquidity swap facilities were established to provide liquidity in each jurisdiction in any of their currencies, should market conditions warrant.

The existing US$30 billion facility with the Federal Reserve Bank of New York expires on 1 February 2013. The swap facilities with the Bank of Japan, the Swiss National Bank, the Bank of England and the European Central Bank were established in December 2011 for an initial term expiring on 1 February 2013.

These facilities can be structured as either a Canadian-dollar liquidity or a foreign currency liquidity swap arrangement and can be initiated by either party. The exchange rate applicable to the swap facilities is based on the prevailing market spot exchange rate as mutually agreed upon by the parties.

Other swap facilities

The other swap facilities established with the Federal Reserve Bank of New York and with the Banco de México have indefinite terms and are subject to annual renewal.

The Bank is also party to a standing foreign currency swap facility with the Exchange Fund Account of Canada. There is no stated maximum amount under this agreement.

None of the liquidity or other swaps were accessed, by either party, in 2011 or 2010. No related commitments exist at 31 December 2011 ($Nil at 31 December 2010 and $Nil at 1 January 2010).

c) Contingency

The 9,441 shares in the BIS have a nominal value of 5,000 special drawing rights (SDRs) per share, of which 25 per cent, i.e., SDR1,250, is paid up. The balance of SDR3,750 is callable at three months' notice by decision of the BIS Board of Directors. The Canadian equivalent of this contingent liability was $55.3 million at 31 December 2011 ($54.6 million at 31 December 2010 and $58.1 million at 1 January 2010), based on prevailing exchange rates.

d) Guarantees

In the normal course of operations, the Bank enters into certain guarantees, which are described below.

Large Value Transfer System (LVTS) Guarantee

The LVTS is a large-value payment system, owned and operated by the CPA. Any deposit-taking financial institution that is a member of the CPA can participate in the LVTS, provided that it maintains a settlement account at the Bank, has the facilities to pledge collateral for LVTS purposes, and meets certain technical requirements. The system's risk-control features, which include caps on net debit positions and collateral to secure the use of overdraft credit, are sufficient to permit the system to obtain the necessary liquidity to settle in the event of the failure of the single LVTS participant having the largest possible net amount owing. The Bank guarantees to provide this liquidity, and in the event of a single-participant failure, the liquidity loan will be fully collateralized. In the extremely unlikely event that there were defaults by more than one participant during the LVTS operating day, in an aggregate amount in excess of the largest possible net amount owing by a single participant, there would not likely be enough collateral to secure the amount of liquidity that the Bank would need to provide to settle the system. This might result in the Bank having unsecured claims on the defaulting participants in excess of the amount of collateral pledged to the Bank to cover the liquidity loans. The Bank would have the right, as an unsecured creditor, to recover any amount of its liquidity loan that was unpaid. The amount potentially at risk under this guarantee is not determinable, since the guarantee would be called upon only if a series of extremely low-probability events were to occur. No amount has ever been provided for in the liabilities of the Bank, and no amount has ever been paid under this guarantee.

Other indemnification agreements

In the normal course of operations, the Bank provides indemnification agreements with various counterparties in transactions such as service agreements, software licences, leases and purchases of goods. Under these agreements, the Bank agrees to indemnify the counterparty against loss or liability arising from acts or omissions of the Bank in relation to the agreement. The nature of the indemnification agreements prevents the Bank from making a reasonable estimate of the maximum potential amount that the Bank would be required to pay such counterparties.

e) Insurance

The Bank does not insure against direct risks of loss to the Bank, except for potential liabilities to third parties and where there are legal or contractual obligations to carry insurance. Any costs arising from risks not insured are recorded in the accounts at the time they can be reasonably estimated.

19. Related parties

The Bank is related in terms of common ownership to all Government of Canada departments, agencies and Crown corporations. To achieve its monetary policy objectives, the Bank maintains a position of structural and functional independence from the Government of Canada through its ability to fund its own operations without external assistance and through its management and governance.

In the normal course of its operations, the Bank enters into transactions with related parties, and material transactions and balances are presented in these financial statements. Not all transactions between the Bank and government-related entities have been disclosed as permitted by the partial exemption available to wholly owned government entities in International Accounting Standard 24 Related Parties (IAS 24).

The Bank provides funds-management, fiscal agent and banking services to the Government of Canada, as mandated by the Bank of Canada Act, and does not recover the costs of these services.

Bank of Canada pension plans

The Bank provides management, investment and administrative support to the Bank of Canada registered Pension Plan. Services in the amount of $0.6 million ($0.5 million in 2010) were fully recovered from the Plan in 2011.

Key management personnel and compensation

The key management personnel, responsible for planning, directing and controlling the activities of the Bank, include the members of the Governing Council, the Management Council and the Board of Directors. The number of key management personnel as at 31 December 2011 was 23 (23 in 2010).

The compensation of key management personnel is presented in the following table:

	31 December 2011	31 December 2010
Short-term employee benefits[1]	**3.1**	3.0
Post-employment benefits	**0.7**	0.5
Directors' fees	**0.3**	0.3
Total compensation	**4.1**	3.8

1 In 2010, three members of the Governing Council retired and were subsequently replaced. The compensation paid during their employment in 2010 related to both the departing and new members of the Governing Council has been included in short-term employee benefits.

Short-term employee benefits and post-employment benefits apply to Bank of Canada employees only.

There were no other long-term employee benefit costs or termination benefits related to key management personnel in 2011.

20. Explanation of transition to IFRS

As stated in note 2, these are the Bank's first annual IFRS financial statements. The accounting policies set out in note 3 have been applied in preparing the financial statements for the year ended 31 December 2011, the comparative information presented in these IFRS financial statements for the year ended 31 December 2010, and in the preparation of an opening IFRS *Statement of Financial Position* at 1 January 2010 (the Bank's date of transition to IFRS).

In preparing its opening IFRS *Statement of Financial Position*, the Bank has adjusted amounts reported previously in financial statements prepared in accordance with former Canadian GAAP. An explanation of how the transition from previous Canadian GAAP to IFRS has affected the Bank's financial position and comprehensive income is set out in the following tables and the notes that accompany the tables.

Reconciliation of cash flows

There were no differences in reported cash flows under IFRS as compared to Canadian GAAP.

Reconciliation of Financial Position and Equity as at 1 January 2010

(Millions of dollars)

	Note	Canadian GAAP	Effect of transition to IFRS	Opening IFRS
ASSETS				
Cash and foreign deposits		20.4	-	20.4
Loans and receivables				
Securities purchased under resale agreements		25,374.8	-	25,374.8
Other receivables		2.2	-	2.2
		25,377.0	-	25,377.0
Investments				
Government of Canada treasury bills		13,684.0	-	13,684.0
Government of Canada bonds		31,986.2	-	31,986.2
Other investments	(a)	38.0	280.7	318.7
		45,708.2	280.7	45,988.9
Property and equipment	(b,g)	126.8	28.4	155.2
Intangible assets	(g)	23.7	-	23.7
Other assets	(c)	98.6	113.0	211.6
Total assets		71,354.7	422.1	71,776.8
LIABILITIES AND EQUITY				
Bank notes in circulation		55,467.9	-	55,467.9
Deposits				
Government of Canada		11,847.6	-	11,847.6
Members of the Canadian Payments Association		2,999.6	-	2,999.6
Other deposits		703.0	-	703.0
		15,550.2	-	15,550.2
Other liabilities	(c,d,e)	199.8	(10.0)	189.8
		71,217.9	(10.0)	71,207.9
Equity	(a,b,c,d,e)	136.8	432.1	568.9
Total liabilities and equity		71,354.7	422.1	71,776.8

(See the notes to the reconciliations of Financial Position and Equity, and Comprehensive Income.)

Reconciliation of Financial Position and Equity as at 31 December 2010

(Millions of dollars)

	Note	Canadian GAAP	Effect of transition to IFRS	IFRS
ASSETS				
Cash and foreign deposits		4.7	-	4.7
Loans and receivables				
Securities purchased under resale agreements		2,062.4	-	2,062.4
Advances to members of the Canadian Payments Association		22.5	-	22.5
Other receivables		2.1	-	2.1
		2,087.0	-	2,087.0
Investments				
Government of Canada treasury bills		24,906.1	-	24,906.1
Government of Canada bonds		33,550.6	-	33,550.6
Other investments	(a)	38.0	272.7	310.7
		58,494.7	272.7	58,767.4
Property and equipment	(b,g)	123.4	29.6	153.0
Intangible assets	(g)	25.9	-	25.9
Other assets	(c)	149.1	29.0	178.1
Total assets		60,884.8	331.3	61,216.1
LIABILITIES AND EQUITY				
Bank notes in circulation		57,874.2	-	57,874.2
Deposits				
Government of Canada		1,869.4	-	1,869.4
Members of the Canadian Payments Association		47.5	-	47.5
Other deposits		639.9	-	639.9
		2,556.8	-	2,556.8
Other liabilities	(c,d,e)	323.8	44.5	368.3
		60,754.8	44.5	60,799.3
Equity	(a,b,c,d,e)	130.0	286.8	416.8
Total liabilities and equity		60,884.8	331.3	61,216.1

(See the notes to the reconciliations of Financial Position and Equity, and Comprehensive Income.)

Reconciliation of Comprehensive Income for the year ended 31 December 2010

(Millions of dollars)

	Note	Canadian GAAP	Effect of transition to IFRS	IFRS
INCOME				
Net interest income				
Interest revenue				
Interest earned on investments		1 525,3	-	1 525,3
Interest earned on securities purchased under resale agreements		38,4	-	38,4
Other interest revenue	(g)	0,1	-	0,1
		1 563,8	-	1 563,8
Interest expense				
Interest expense on deposits		(42,0)	-	(42,0)
		1 521,8	-	1 521,8
Dividend revenue		10,1	-	10,1
Other revenue	(g)	11,4	-	11,4
Total income		1 543,3	-	1 543,3
EXPENSES				
Staff costs	(c,d)	179,3	(8,5)	170,8
Bank note research, production and processing		53,7	-	53,7
Premises maintenance		28,7	-	28,7
Technology and telecommunications	(g)	34,3	-	34,3
Depreciation and amortization	(b)	16,4	(1,2)	15,2
Other operating expenses		78,1	-	78,1
Total expenses		390,5	(9,7)	380,8
NET INCOME		1 152,8	9,7	1 162,5
OTHER COMPREHENSIVE INCOME				
Change in fair value of available-for-sale financial assets	(a)	(8,5)	(8,0)	(16,5)
Actuarial losses	(c)	-	(105,6)	(105,6)
Other comprehensive income		(8,5)	(113,6)	(122,1)
COMPREHENSIVE INCOME		1 144,3	(103,9)	1 040,4

(See the notes to the reconciliations of Financial Position and Equity, and Comprehensive Income.)

Notes to the reconciliations of Financial Position and Equity, and Comprehensive Income

Measurement changes

a) In accordance with IAS 39, investments in equity instruments classified as AFS that do not have a quoted market price in an active market but for which a market value can be reasonably estimated have been recognized at fair value. The Bank's investments in BIS shares are classified as AFS and were carried at cost under previous Canadian GAAP.

The impact of the change is summarized as follows:

Statement of Comprehensive Income	**Year ended 31 December 2010**	
Decrease in Other Comprehensive Income	8.0	
Statement of Financial Position	**31 December 2010**	**1 January 2010**
Increase in Other investments	272.7	280.7
Change in Equity		
Increase in Available-for-sale reserve	(272.7)	(280.7)

b) In accordance with International Accounting Standard 16 (IAS 16), each component of an item of property and equipment with a cost that is significant in relation to the total cost of an item is depreciated separately. At the date of transition, the only items of *Property and equipment* impacted are the buildings owned by the Bank. The effect of the componentization resulted in changes to the useful lives over which these assets are depreciated.

The impact of the change is summarized as follows:

Statement of Comprehensive Income	**Year ended 31 December 2010**	
Decrease in Depreciation expense	1.2	
Statement of Financial Position	**31 December 2010**	**1 January 2010**
Increase in Property and equipment	29.6	28.4
Change in Equity		
Increase in Retained earnings	(29.6)	(28.4)

c) In accordance with International Accounting Standard 19 (IAS 19), the Bank has adopted the policy to recognize all actuarial gains and losses on post-employment defined benefits immediately in *Other Comprehensive Income*. At the date of transition, all previously unamortized transitional obligations and assets, vested past service costs and credits, and net actuarial losses were recognized in Retained earnings.

Also recognized in Retained earnings were the changes relating to the adoption of IAS 19, which include using discount rates determined by reference to market yields of AA-corporate bonds.

Subsequent to the recording of IFRS transition adjustments, the net impact of the transition related to post-employment defined benefits was transferred to establish the actuarial gains reserve.

The net impact of the changes is summarized as follows:

Statement of Comprehensive Income	**Year ended 31 December 2010**
Decrease in benefit expenses	9.3
Actuarial losses taken to Actuarial gains reserve	(105.6)

Statement of Financial Position	**31 December 2010**	**1 January 2010**
Increase in Other assets	29.0	113.0
Decrease (increase) in Other liabilities	(5.6)	6.7
Change in Equity		
Increase in Actuarial gains reserve	(14.1)	(119.7)
Increase in Retained earnings	(9.3)	-

d) In accordance with IAS 19, the Bank's IFRS accounting policy for other long-term employee benefits is to recognize all actuarial gains and losses immediately in net income. At the date of transition, all previously unamortized actuarial gains and losses, and changes relating to the adoption of IAS 19 were recognized in Retained earnings.

The net impact of the changes is summarized as follows:

Statement of Comprehensive Income	**Year ended 31 December 2010**
Increase in benefit expenses	0.8

Statement of Financial Position	**31 December 2010**	**1 January 2010**
Decrease in Other liabilities	2.5	3.3
Change in Equity		
Increase in Retained earnings	(2.5)	(3.3)

e) In accordance with the requirement of Section 27 of the Bank of Canada Act, the increase in Retained earnings from the transition to IFRS will be payable to the Receiver General for Canada. The amount that will be payable upon completion of the Bank's transition has been accrued in Other liabilities.

Statement of Financial Position	**31 December 2010**	**1 January 2010**
Increase in Other liabilities	(41.4)	-
Change in Equity		
Decrease in Retained earnings	41.4	-

f) **Principal exemptions elected on transition to IFRS**

IFRS 1 sets out the requirements that the Bank must follow when it adopts IFRS for the first time as the basis for preparing its financial statements. The Bank is required to establish its IFRS accounting policies for the year ended 31 December 2011, and apply these retrospectively to determine the IFRS opening *Statement of Financial Position* at the date of transition of 1 January 2010. To assist entities in the transition process, the standard permits a number of specified exemptions from the general principle of retrospective restatement. The Bank has elected to disclose the Summary of historical adjustments in note 14 on a prospective basis following the transition to IFRS. Except for the above mentionned disclosure, the Bank has not elected to use any of the optional exemptions from certain IFRS or any of the exemptions to retrospective application of certain IFRS that are available under IFRS 1 in the preparation of these financial statements.

g) **Reclassification for IFRS presentation**

Certain balances have been reclassified to conform with the presentation adopted by the Bank in its transition to IFRS.

The net impact of the changes is summarized as follows:

Statement of Comprehensive Income	**Year ended 31 December 2010**
Decrease in Other revenue	(0.1)
Increase in Other interest revenue	0.1
Decrease in Other operating expenses	34.3
Increase in Technology and telecommunications	(34.3)

Statement of Financial Position	**31 December 2010**	**1 January 2010**
Decrease in Property and equipment	(25.9)	(23.7)
Increase in Intangible assets	25.9	23.7

The presentation of the *Statement of Comprehensive Income* changed from reporting by function under previous Canadian GAAP to a presentation by nature under IFRS. The expenses are reported in note 16 on the basis of the four functions of the Bank described in note 1.

Senior Officers

Governing Council

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Tiff Macklem, *Senior Deputy Governor**

Deputy Governors
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W. John Jussup**

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Canadian Economic Analysis
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Stephen Murchison, *Deputy Chief*
Robert Amano, *Research Director*
Greg Bauer, *Research Director*
Césaire Meh, *Research Director*
Pierre St-Amant, *Research Director*

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John Robert Fortin, *Director*
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Charles Spencer, *Director*
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Marco Petta, *Special Director*
Scott Hendry, *Research Director*
Stéphane Lavoie, *Director*
Miville Tremblay, *Senior Representative*, *Director*
Eric Tuer, *Director*

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Rudy Wytenburg, *Deputy Chief*

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Toni Gravelle, *Deputy Chief*
Arthur Berger, *Director*
Carol Ann Northcott, *Director*
Graydon Paulin, *Director*

Funds Management and Banking
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Eric Wolfe, *Deputy Chief*
Louise Hyland, *Director*
Miguel Molico, *Research Director*

Information Technology Services
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Daniel Lamoureux, *Director*
Janne Shaw, *Director*

International Economic Analysis
Donald Coletti, *Chief*
Eric Santor, *Deputy Chief*
René Lalonde, *Research Director*
Rhys Mendes, *Director*

Note: Positions as of 17 February 2012

* Chair of Management Council
** Member of Management Council
1. Also Chair of the Board of Directors of the Canadian Payments Association
2. Special Adviser to the Governor
3. Visiting Special Adviser

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Internet
bankofcanada.ca
Provides timely access to press releases, speeches by the Governor, the Bank's major publications, and current financial data.

Public Information
For general information on the role and functions of the Bank of Canada, contact our Public Information Office.
Telephone: **1 800 303-1282**
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For information on unclaimed balances:
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