

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2002 and 2001 (In thousands of dollars, except shares and per share amounts)

1. Summary of significant accounting policies

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

GAAP require management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. Actual results may differ from such estimates.

Basis of consolidation

The consolidated financial statements include the accounts of the Company and all subsidiaries on a consolidated basis after elimination of intercompany transactions and balances.

Effective April 20, 2001, the Company acquired all of the outstanding common shares of Mackenzie Financial Corporation ("Mackenzie"). The acquisition was accounted for by the purchase method. The consolidated financial statements include the assets and liabilities of Mackenzie as at December 31, 2002 and 2001 and the results of operations from the date of acquisition.

The equity method is used to account for the Company's investment in Great-West Lifeco Inc., an affiliated company. Both companies are controlled by Power Financial Corporation. Investments in joint ventures that were jointly controlled were consolidated on a proportionate basis.

Revenue recognition

Management and certain administration fees are based on the net asset value of mutual fund assets under management and are recognized on an accrual basis when the service is performed.

Foreign currency translation

The Company follows the current rate method of foreign currency translation for its net investment in its self-sustaining foreign operations. Under this method, assets and liabilities are translated into Canadian dollars at the rate of exchange prevailing at the balance sheet date and all income and expense items are translated at average exchange rates prevailing throughout the year. Any resulting translation gains or losses are reported in shareholders' equity as a foreign currency translation adjustment. When a self-sustaining foreign operation is sold, the associated currency translation gains or losses, previously included in shareholders' equity, are recorded as part of the gain or loss on disposal of the investment.

Securities

Investment securities comprise debt and equity securities held for long-term investment. Bonds and debentures are carried at amortized cost plus accrued interest. Discounts or premiums on the purchase of bonds and debentures are amortized over the remaining life of the security. Common and preferred shares and all other securities are carried at original cost plus declared dividends. Securities are written down to their fair value when an other than temporary decline in value is identified. Trading securities related to the Company's derivative activities are carried at fair value.

Loans

Loans are carried at amortized cost plus accrued interest less an allowance for credit losses. Interest income is accounted for on the accrual basis for all loans other than impaired loans.

A loan is classified as impaired when, in the opinion of management, there no longer is reasonable assurance of the timely collection of the full amount of principal and interest. A loan is also classified as impaired when interest or principal is contractually past due 90 days, except in circumstances where management has determined that the collectibility of principal and interest is not in doubt. Once a loan is classified as impaired, any accrued and unpaid interest income is reversed and charged against interest income in the current period. Thereafter interest income is recognized on a cash basis.

The Company maintains an allowance for credit losses which is considered adequate by management to absorb all credit related losses in its portfolio. Specific allowances are established as a result of reviews of individual loans. There is a second category of allowance, designated general allowance, which is allocated against sectors rather than specifically against individual loans. This allowance is established where a prudent assessment by the Company suggests that losses may occur but where such losses cannot yet be identified on an individual loan basis.

Securitizations

The Company periodically securitizes mortgages and personal loans through sales to commercial paper conduits that in turn issue securities to investors. The Company retains servicing responsibilities and certain elements of recourse with respect to credit losses on transferred loans. The Company also securitizes NHA-insured mortgages through the issuance of mortgage-backed securities. Effective July 1, 2001, the Company adopted the recommendations of the Canadian Institute of Chartered Accountants ("CICA") Accounting Guideline 12 ("AcG-12"), "Transfers of Receivables", for transfers of loans occurring on or after July 1, 2001.



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1. Summary of significant accounting policies (cont'd)

Securizations (cont'd)

Under AcG-12, transfers of loans are accounted for as sales provided that control over the transferred loans has been surrendered and consideration other than beneficial interests in the transferred loans has been received in exchange. The loans are removed from the consolidated balance sheet and a gain or loss is recognized in income immediately based on the carrying value of the loans transferred. The carrying value is allocated between the assets sold and the retained interests in proportion to their fair values at the date of transfer. To obtain the fair value of the Company's retained interests, quoted market prices are used if available. However, quotes are generally not available for retained interests, so the Company estimates fair value based on the present value of future expected cash flows using management's best estimates of key assumptions such as prepayment rates, excess spread, expected credit losses and discount rates commensurate with the risks involved. The Company continues to service the loans sold. As a result, a servicing liability is recognized and amortized over the expected term of the transferred loans as servicing fees.

Transfers of loans occurring, or committed to, prior to July 1, 2001, are accounted for as sales when the significant risks and rewards of ownership have been transferred and there is reasonable assurance regarding the measurement of the consideration derived from the sale. Gains on these transactions are deferred and recognized over the term of the structure as and when realized. To the extent there is recourse on the transaction, any gain is deferred until the cash is collected and there is no further recourse. Fees earned by the Company to service the securitized loans are recognized as services are provided.

For all transfers of loans, gains/losses on sale and servicing fee revenues are reported in net investment income and other in the consolidated statements of income. The retained interests in the securitized loans are recorded in other assets and the servicing liability is recorded in other liabilities on the consolidated balance sheet.

Deferred selling commissions

Commissions paid on the sale of certain mutual fund products are deferred and amortized against related fee income over a maximum period of seven years. Prior to April 1, 2001, the maximum period for amortization was three years. The Company changed the period of amortization for these expenditures to reflect a more accurate estimate of their useful life. This estimate is also consistent with that used by Mackenzie. The change in accounting estimate was applied prospectively and resulted in a decrease of \$32,306 (\$19,829 after tax) in commissions expense in 2002. Commissions paid on the sale of deposits are deferred and amortized over the term of the deposit with a maximum amortization period of five years.

Office premises

Office premises, which are included in other assets, are recorded at cost of \$210,757 (2001 – \$203,583), less accumulated depreciation of \$118,094 (2001 – \$94,522). The depreciable properties and related equipment and furnishings are depreciated on a straight-line basis over their estimated lives.

Goodwill and intangible assets

Effective January 1, 2002, the Company adopted the recommendations of the CICA Handbook Section 3062 – Goodwill and Other Intangible Assets. Under this standard, goodwill and intangible assets with indefinite lives will no longer be amortized but must be reviewed at least annually for impairment, and written down for impairment losses. Previously, the Company amortized goodwill on a straight-line basis over 30 years. Goodwill and intangible assets related to the acquisition of Mackenzie were determined in the second quarter of 2002 after completing a comprehensive evaluation of the fair value of the assets acquired and liabilities assumed.

The Company completed its annual impairment testing on the balance of goodwill and indefinite life intangible assets and determined that no impairment charge was necessary.

This change in accounting policy was applied prospectively and resulted in a decrease of \$108,136 (\$108,090 after tax) in goodwill amortization in 2002. In addition, adoption of this standard resulted in an increase of \$4,981 in net investment income as goodwill relating to the Company's equity accounted investment in Great West Lifeco, Inc. was not amortized in 2002.



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1. Summary of significant accounting policies (cont'd)

Goodwill and intangible assets (cont'd)

The table below is provided to present the comparative net income available to common shareholders, earnings per share and diluted earnings per share for the years ended December 31, 2002 and 2001 on a consistent basis with the presentation in effect since January 1, 2002.

	2002	2001
Reported net income available		
to common shareholders	\$ 491,059	\$ 259,695
Add back:		
Goodwill amortization, net of tax ⁽¹⁾	–	76,950
Net income available to common shareholders adjusted for goodwill	\$ 491,059	\$ 336,645
Basic earnings per share (in dollars)		
– Reported	\$ 1.864	\$ 1.051
– Adjusted for goodwill	\$ 1.864	\$ 1.362
Diluted earnings per share (in dollars)		
– Reported	\$ 1.854	\$ 1.047
– Adjusted for goodwill	\$ 1.854	\$ 1.358

⁽¹⁾ Includes amortization of goodwill on investment in affiliate reported in Net investment income and other

Pension plans and other post-retirement benefits

The Company maintains a defined-benefit pension plan for substantially all of its eligible employees. The plan provides pensions based on length of service and final average earnings. The benefit obligation is actuarially determined and accrued using the projected benefit method pro-rated on service. Pension expense or income consists of the aggregate of the actuarially computed cost of pension benefits provided in respect of the current year's service, imputed interest on the funding excess or deficiency of the plan, and the amortization of actuarial gains or losses over the expected average remaining service life of employees. Plan assets are valued at fair value for purposes of calculating the expected long-term rate of return.

The Company also has an unfunded supplementary pension plan for certain executive officers. Pension expense related to current services are charged to income in the period during which the services are rendered.

The Company also provides certain post-retirement health care and life insurance benefits to eligible retirees. The cost of the benefits is actuarially determined and accrued using the projected benefit method pro-rated on service. The current cost of post-retirement health and life insurance benefits is charged to income in the period during which the services are rendered.

Income taxes

The Company follows the liability method in accounting for income taxes whereby future income tax assets and liabilities reflect the expected future tax consequences of temporary differences between the carrying amounts of assets and liabilities and their tax bases. Future income tax assets and liabilities are determined based on the enacted or substantively enacted tax rates which are expected to be in effect when the underlying items of income or expense are expected to be realized.

Earnings per share

Basic earnings per share is determined by dividing net income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted earnings per share is determined using the same method as basic earnings per share except that the weighted-average number of common shares outstanding includes the potential dilutive effect of outstanding stock options granted by the Company as determined by the treasury method.

Stock-based compensation

Effective January 1, 2002, the Company adopted the recommendations of the CICA Handbook Section 3870 – Stock-based Compensation and Other Stock-based Payments. All stock-based payments to non-employees are accounted for using a fair value-based method of accounting. The fair value-based method of accounting is not used for stock-based compensation for employees (see Note 15).



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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1. Summary of significant accounting policies (cont'd)

Derivative financial instruments

Derivative financial instruments are utilized by the Company in the management of interest rate and equity market exposures and for trading purposes to meet the needs of the Company's clients. The Company's policy is not to utilize derivative financial instruments for speculative purposes.

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the consolidated balance sheet or to assets under management. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

The Company enters into interest rate swaps in order to reduce the impact of fluctuating interest rates on its long-term debt and mortgage banking activities. The swap agreements require the periodic exchange of payments without the exchange of the notional principal amount on which the payments are based. The Company designates its interest rate swap agreements as hedges of the underlying assets and liabilities. Interest income and expense is adjusted to include the payments made or received under the interest rate swaps.

The Company enters into equity index swaps to offset changes that affect fee income earned on its mutual fund assets under management. The swap agreements require the periodic exchange of payments without the exchange of the notional principal amount on which the payments are based. The Company designates its equity swap agreements as hedges of the anticipated revenue stream. Management fee income is adjusted to include the payments made or received under the equity index swaps.

The Company also manages its exposure to market risk on its securities by entering into forward sale contracts as well as simultaneously purchasing a put option and writing a call option on the same security. The Company designates these contracts as hedges of the specified securities. Any unrealized gains and losses on the forward sales and options are accounted for on a basis consistent with the related securities.

In the event a designated hedged item is sold, extinguished or matures prior to the termination of the related derivative instruments, any realized or unrealized gain or loss on such derivative instrument is recognized in income.

The Company acts as a counterparty to forward contracts used in trading activities. As at December 31, 2002, the Company had equity-linked forward contracts outstanding with a notional amount of \$1,618,177 (2001 – nil), expiring January 9, 2003. Unrealized gains and losses on these contracts have been reported on a net basis in the Company's consolidated financial statements since the Company has both the legal right and intent to settle these amounts simultaneously with the related on-balance sheet asset or liability. The credit risk exposure arising from these forward contracts is eliminated by the ability of the Company to settle on a net basis.

Assets under management and assets under administration

The Company manages and administers assets owned by clients and third parties that are not reflected on the consolidated balance sheet. Mutual fund assets managed by the Company on behalf of its clients are considered assets under management. Mortgages serviced for third parties and assets administered in the Company's securities operations are considered assets under administration.

Comparative figures

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



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2. Securities

	Carrying Value	2002 Fair Value	Carrying Value	2001 Fair Value
Government bonds	\$ 2,050	\$ 2,096	\$ 3,116	\$ 3,209
Corporate bonds	93	93	796	796
Preferred shares	11,098	11,276	12,570	12,966
Common shares	111,146	239,510	166,961	353,336
Investments in mutual funds	31,799	31,893	64,762	61,443
	\$ 156,186	\$ 284,868	\$ 248,205	\$ 431,750

	Term to Maturity			2002 Total	2001 Total
	1 Year or Less	1 – 5 Years	No Specific Maturity		
Government bonds	\$ 2,050	\$ –	\$ –	\$ 2,050	\$ 3,116
Corporate bonds	–	93	–	93	796
Preferred shares	8,666	2,432	–	11,098	12,570
Common shares	–	–	111,146	111,146	166,961
Investments in mutual funds	–	–	31,799	31,799	64,762
	\$ 10,716	\$ 2,525	\$ 142,945	\$ 156,186	\$ 248,205

3. Loans

	Term to Maturity			2002 Total	2001 Total
	1 Year or Less	1 – 5 Years	Over 5 Years		
Residential mortgages	\$ 148,651	\$ 207,325	\$ 6,958	\$ 362,934	\$ 470,077
Commercial mortgages	8,459	12,331	577	21,367	17,909
	157,110	219,656	7,535	384,301	487,986
Personal loans	36,791	122,681	26,738	186,210	188,429
	\$ 193,901	\$ 342,337	\$ 34,273	570,511	676,415
Less: General allowance				21,542	21,321
				\$ 548,969	\$ 655,094
Impaired loans included above				2,158	3,446
Less: General allowance				21,542	21,321
				\$ (19,384)	\$ (17,875)

The change in the allowance for credit losses is as follows:

Balance, beginning of year	\$ 21,321	\$ 8,435
Mackenzie, balance at date of acquisition	–	13,307
Write-offs	(1,460)	(1,967)
Recoveries	799	304
Provision for credit losses	882	1,242
Balance, end of year	\$ 21,542	\$ 21,321



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4. Securitizations

During the year the Company securitized the following loans with gains, net of transactions costs, being recognized in net investment income:

	2002		2001	
	Principal Amount Securitized	Net Gain	Principal Amount Securitized	Net Gain
Residential mortgages	\$ 131,103	\$ 1,974	\$ 631,767	—
NHA insured mortgages	\$ 57,772	\$ 353	\$ 75,041	\$ 1,082
Personal investment loans	\$ 32,153	\$ 1,670	\$ 10,445	—

The Company's retained interest in the securitized loans is subordinated to the interests of the related commercial paper conduits and mortgage-backed securities holders (the "Purchasers"). The Purchasers do not have recourse to the Company's other assets for any failure of the borrowers to pay when due.

The key economic assumptions used to value the retained interests at the date of securitization issuances for transactions completed during the year were as follows:

	Residential Mortgages	NHA Insured Mortgages	Personal Investment Loans
Weighted-average			
Remaining service life (in years)	2.0	5.6	n/a
Interest rate	5.61%	5.82%	Prime +1%
Coupon rate of securities issued	4.43%	4.92%	2.24%
Prepayment rate	15.00%	6.00%	10.00%
Discount rate	5.33%	5.16%	9.04%
Servicing fees	0.25%	0.21%	0.15%
Expected credit losses	0.05%	—	0.15%

At December 31, 2002, the current fair value of retained interests was \$14,982. The sensitivity to immediate 10% and 20% adverse changes to key assumptions was considered to be immaterial.

The total loans reported on the Company's consolidated balance sheet, the securitized loans serviced by the Company, as well as cash flows related to securitization arrangements are as follows:

	2002	2001
Total principal amount of:		
Mortgages	\$ 1,153,048	\$ 1,473,579
Personal investment loans	235,994	226,561
	1,389,042	1,700,140
Less: Securitized loans serviced	840,073	1,045,046
Total on-balance sheet loans	\$ 548,969	\$ 655,094
Proceeds from new securitizations	\$ 217,443	\$ 703,227
Cash flows received on retained interest	\$ 3,997	\$ 2,891



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5. Investment in affiliate

The Company holds a 4.4% equity interest in Great-West Lifeco Inc. Goodwill of \$128,870 (2001 – \$128,870) is included in the carrying value of the investment.

	2002	2001
Carrying value, beginning of year	\$ 297,810	\$ 293,481
Share of earnings	38,516	21,970
Goodwill amortization	–	(4,981)
Dividends	(15,338)	(12,660)
Carrying value, end of year	\$ 320,988	\$ 297,810

6. Other assets

	2002	2001
Accounts and other receivables	\$ 155,299	\$ 199,597
Office premises	92,663	109,061
Accrued pension asset (Note 11)	39,919	36,832
Real estate	3,423	4,420
Other	45,652	39,031
	\$ 336,956	\$ 388,941

7. Goodwill and intangible assets

During the second quarter of 2002, the Company completed a comprehensive evaluation of the fair value of the assets acquired and liabilities assumed from the acquisition of Mackenzie. The amount assigned to intangible assets represents the fair value of mutual fund management contracts and trade names acquired. Both of these intangible assets have indefinite useful lives and are therefore not subject to amortization.

Changes in the Company's goodwill and intangible assets are as follows:

	2002
Goodwill	
Carrying value, beginning of year	\$ 3,020,922
Reclassification between goodwill and intangible assets	(859,948)
Reclassification between goodwill and future income taxes	130,153
Goodwill disposed of during the year	(25,462)
Carrying value, end of year	\$ 2,265,665
Allocated to reportable segments as follows:	
Investors Group	\$ 1,346,245
Mackenzie	919,420
	\$ 2,265,665
Intangible assets	
Carrying value, beginning of year	\$ –
Reclassified from goodwill	
Mutual fund management contracts	591,580
Trade names	268,368
Carrying value, end of year	\$ 859,948



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8. Deposits and certificates

Included in the assets of the consolidated balance sheets are cash and investments amounting to \$709,012 (2001 – \$671,248) held in trust and set aside in respect of the deposits of Investors Group Trust Co. Ltd., The Trust Company of London Life and M.R.S. Trust Company, and the certificates issued by Investors Syndicate Limited.

	Demand	Term to Maturity			2002 Total	2001 Total
		1 Year or Less	1 – 5 Years	Over 5 Years		
Deposits	\$ 412,099	\$ 103,559	\$ 177,218	\$ 5,116	\$ 697,992	\$ 656,722
Certificates	–	1,149	5,064	4,807	11,020	14,526
	\$ 412,099	\$ 104,708	\$ 182,282	\$ 9,923	\$ 709,012	\$ 671,248

9. Bankers' acceptances

In 2001, a Schedule I Canadian chartered bank provided the Company with a non-revolving bridge credit facility which was used in part to provide the cash consideration for the acquisition of Mackenzie. Interest rates on the credit facility fluctuated with Canadian bankers' acceptances. The balance of the credit facility was repaid on November 20, 2002.

10. Other liabilities

	2002	2001
Accounts payable and accrued liabilities	\$ 202,981	\$ 292,350
Restructuring costs	105,665	130,456
Taxes payable	77,036	84,596
Dividends and interest payable	80,332	73,703
Deferred revenue	13,950	13,440
Accrued employee benefit obligations (Note 11)	39,977	37,384
Other	119,422	147,924
	\$ 639,363	\$ 779,853



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11. Pension plans and other post-retirement benefits

Employee pension plan

The Company maintains a defined benefit pension plan which covers substantially all of its eligible employees. Changes in the fair value of plan assets and the accrued pension obligation are as follows:

	2002	2001
Fair value of plan assets		
Balance, beginning of year	\$ 142,581	\$ 145,797
Employee contributions	2,529	2,909
Benefits paid	(7,204)	(7,358)
Return on plan assets	2,419	1,233
Balance, end of year	<u>140,325</u>	<u>142,581</u>
Accrued benefit obligation		
Balance, beginning of year	84,250	77,660
Benefits paid	(7,204)	(7,358)
Current service cost	2,953	2,519
Employee contributions	2,529	2,909
Interest cost	5,986	5,717
Actuarial losses	6,142	2,803
Balance, end of year	<u>94,656</u>	<u>84,250</u>
Funded status - plan surplus	45,669	58,331
Unamortized net actuarial gains	(5,750)	(21,499)
Accrued pension asset	<u>\$ 39,919</u>	<u>\$ 36,832</u>
Pension income was determined as follows:		
Current service cost	\$ 2,953	\$ 2,519
Interest cost	5,986	5,717
Expected return on plan assets	(9,817)	(10,032)
Amortization of net actuarial gains	(2,209)	(3,334)
	<u>\$ (3,087)</u>	<u>\$ (5,130)</u>

Significant weighted-average actuarial assumptions:

Discount rate	6.95%	6.95%
Expected long-term rate of return on plan assets	7.00%	7.00%
Rate of compensation increase	6.10%	6.10%

Supplementary employee retirement plan

The Company maintains an unfunded supplementary pension plan for certain executive officers.

	2002	2001
Accrued benefit obligation	\$ 10,476	\$ 12,446
Unamortized actuarial gains	2,833	—
Accrued benefit liability, end of year	<u>\$ 13,309</u>	<u>\$ 12,446</u>
Pension expense	<u>\$ 1,585</u>	<u>\$ 2,847</u>

Significant weighted-average actuarial assumptions:

Discount rate	6.88%	6.88%
Rate of compensation increase	6.10%	6.10%



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11. Pension plans and other post-retirement benefits (cont'd)

Post-retirement benefit plans

The Company also provides certain unfunded post-retirement health care and life insurance benefits to eligible retirees.

	2002	2001
Accrued benefit liability		
Balance, beginning of year	\$ 20,733	\$ 20,713
Benefits paid	(879)	(835)
Current service cost	1,325	1,306
Interest cost	1,567	1,596
Actuarial losses (gains)	935	(2,047)
	23,681	20,733
Unamortized actuarial gains	2,987	4,205
Balance, end of year	\$ 26,668	\$ 24,938

Benefit expense was determined as follows:

Current service cost	\$ 1,325	\$ 1,306
Interest cost	1,567	1,596
Amortization of net actuarial gains	(283)	(142)
	\$ 2,609	\$ 2,760

Significant weighted-average actuarial assumptions:

Discount rate	7.00%	7.25%
Medical trend rate	5.60%	6.70%

The medical trend rate is expected to decline to 4.5% annually in 2004.

12. Income taxes

The effective income tax rate differs from the statutory rate, as described below:

	2002		2001	
Income before income taxes, non-controlling interest, goodwill amortization and discontinued operations	\$ 827,670		\$ 597,480	
Income taxes at federal and provincial statutory rates	\$ 334,876	40.46%	\$ 258,410	43.25%
Effect of:				
Dividend income	(2,760)	(0.33)	(4,659)	(0.78)
Net capital gains and losses	(391)	(0.05)	(3,268)	(0.55)
Tax on large corporations	143	0.02	345	0.06
Lower effective rate of tax on income not subject to tax in Canada and other items	(14,467)	(1.75)	1,646	0.28
Income taxes provided	\$ 317,401	38.35%	\$ 252,474	42.26%

Components of income tax expense are:

Current income taxes	\$ 263,254	\$ 277,939
Future income taxes	54,147	(25,465)
	\$ 317,401	\$ 252,474



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12. Income taxes (cont'd)

Future income tax balances result from temporary differences between the tax basis of assets and liabilities and their carrying amount on the consolidated balance sheet.

Sources of future income tax balances are as follows:

	2002	2001
Future income tax assets		
Restructuring costs	\$ 40,703	\$ 50,949
Accrued employee benefit obligations	14,974	13,651
Investment revaluations	9,935	15,025
Deferred revenue	7,664	9,496
Other	49,756	59,666
	123,032	148,787
Future income tax liabilities		
Deferred selling commissions	258,161	242,739
Intangible assets	130,153	–
Other	36,462	26,282
	424,776	269,021
Future income taxes	\$ 301,744	\$ 120,234

13. Long-term debt

	2002	2001
5.52% Preferred A units, due December 31, 2002	\$ –	\$ 47,118
– Note Payable to Quadrus Investment Services Ltd., due December 31, 2003, non-interest bearing	6,000	8,000
10.60% Note Payable to Power Financial Corporation, due January 16, 2006	30,365	32,150
– Floating Bankers' Acceptance, due May 30, 2006	450,000	550,000
6.75% Debentures 2001 Series, due May 9, 2011	450,000	450,000
6.65% Debentures 1997 Series, due December 13, 2027	125,000	125,000
7.45% Debentures 2001 Series, due May 9, 2031	150,000	150,000
7.00% Debentures 2002 Series, due December 31, 2032	175,000	–
	\$ 1,386,365	\$ 1,362,268

A syndicate of banks has provided the Company with a \$550,000 non-revolving credit facility which is due on May 30, 2006. In 2002, the Company repaid \$100,000 of this credit facility. Interest rates on the credit facility fluctuate with Canadian bankers' acceptances.

The debentures are redeemable by the Company, in whole or in part, at any time, at the greater of par and a formula price based upon yields at the time of redemption.

Interest expense relating to long-term debt was \$81,650 (2001 – \$61,707).

The annual principal payments in each of the next five years are: 2003 – \$7,785; 2004 – \$1,785; 2005 – \$1,785; 2006 – \$475,010; and 2007 – nil.

14. Share capital

Authorized

Unlimited number of:

- First preferred shares, issuable in series
- Second preferred shares, issuable in series
- Class 1 non-voting shares
- Common shares



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14. Share capital (cont'd)

Issued and outstanding

	Shares	2002 Stated Value	Shares	2001 Stated Value
First preferred shares, Series A	14,400,000	\$ 360,000	14,400,000	\$ 360,000
Common shares				
Balance, beginning of year	263,081,731	\$ 1,431,163	209,742,580	\$ 272,756
Issued to related parties (Note 22)	—	—	14,732,000	368,300
Issued on acquisition of Mackenzie (Note 22)	—	—	38,802,952	789,252
Issued under Stock Option Plan	763,602	9,900	512,199	4,704
Purchased for cancellation	—	—	(708,000)	(3,849)
Balance, end of year	263,845,333	\$ 1,441,063	263,081,731	\$ 1,431,163

Preferred shares

On May 9, 2001, the Company issued 14,400,000 5.75% first preferred shares, Series A, for consideration of \$360,000. The shares are non-voting except in certain instances. Non-cumulative cash dividends are payable quarterly. The shares are redeemable by the Company beginning June 30, 2009, on a declining premium basis, for cash or, subject to regulatory approval, through the issuance of common shares. On and after June 30, 2013, the shares may be converted into common shares at the option of the holder, subject to the right of the Company to redeem or find substitute purchasers prior to the conversion date at the purchase price of \$25.00 cash per share.

Normal course issuer bid

The Company commenced a normal course issuer bid, effective for one year, on February 22, 2002. Under this bid, the Company may purchase up to 13.2 million or 5% of its common shares as at January 31, 2002. There were no purchases under this bid during 2002. On February 15, 2001, the Company commenced a normal course issuer bid, effective for one year, authorizing it to purchase up to 10.5 million or 5% of its common shares outstanding as at February 1, 2001. As at December 31, 2001, 708,000 common shares were purchased at a cost of \$14,137 and the premium paid to purchase the shares was charged to retained earnings.

15. Stock-based compensation

Share purchase plans

Under the Company's share purchase plans, eligible employees and financial planning consultants can choose each year to have a percentage of their annual earnings withheld, subject to a maximum, to purchase the Company's common shares. The Company matches 50% of the contribution amounts. All contributions are used by the plan trustee to purchase common shares in the open market. Shares purchased with Company contributions vest after a maximum period of three years following the date of purchase. The Company's contributions are recorded in non-commission expense as paid and totalled \$3,433 (2001 – \$4,443).

Stock option plan

Under the terms of the Company's Stock Option Plan, options to purchase common shares are periodically granted to designated officers, employees and financial planning consultants at prices not less than the market price of such shares immediately prior to the grant date. The options are subject to time and/or performance vesting conditions set out at the date of grant and are exercisable no later than 10 years after date of grant.

In 2002, the Company's Stock Option Plan was amended to provide that an additional 15,000,000 common shares of the Company be reserved for issuance under the Plan. At December 31, 2002, a maximum number of 19,265,099 (20,028,701 at December 31, 2001) common shares were reserved for issuance under the plan. Compensation expense of \$101 was recorded for the year ended December 31, 2002 for stock-based compensation related to non-employees. During 2002, 21,990 stock options were issued to employees. Utilization of fair-value based accounting would have no material impact on net income or earnings per share on a pro forma basis. Any consideration paid on exercise of stock options to purchase stock is credited to share capital.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2002 and 2001 (In thousands of dollars, except shares and per share amounts)

15. Stock-based compensation (cont'd)

Stock option plan (cont'd)

	Number of Options	2002 Weighted- Average Exercise Price	Number of Options	2001 Weighted- Average Exercise Price
Balance, beginning of year	6,389,231	\$ 18.65	2,827,740	\$ 14.68
Granted	106,740	27.81	4,125,835	20.22
Exercised	(763,602)	12.96	(512,199)	9.18
Cancelled	(195,535)	20.35	(52,145)	20.50
Balance, end of year	5,536,834	\$ 19.55	6,389,231	\$ 18.65
Exercisable, end of year	1,636,995	\$ 17.32	1,469,961	\$ 13.30

Options outstanding at December 31, 2002	Expiry Date	Exercise Price \$	Options Outstanding	Options Exercisable
	2005	8.66	376,499	376,499
	2006	8.89	-	-
	2007	12.98-13.54	142,040	142,040
	2008	18.85-20.99	101,800	77,920
	2009	18.99-24.27	743,000	536,500
	2010	17.00	117,000	32,400
	2011	19.83-22.78	3,951,255	471,636
	2012	27.81	105,240	-
			5,536,834	1,636,995

16. Off-balance sheet financial instruments

The Company enters into derivative contracts which are negotiated in the over-the-counter market with Schedule I and Schedule II Chartered bank counterparties on a diversified basis. In all cases the derivative contracts are used for non-trading purposes and they are designated as hedges. Interest rate swaps are contractual agreements between two parties to exchange the related interest payments based on a specified notional amount and reference rate for a specified period. Interest rate swaps are used for the purpose of asset and liability management to manage interest rate risk. Equity index swaps are contractual agreements to exchange payments based on a specified notional amount and the stock market index reference for a specific period. Options are contractual agreements which convey the right, but not the obligation, to buy or sell specific securities at a fixed price at a future date. Forward sales are contractual agreements to sell a financial instrument on a future date at a specified price. Equity index swaps, options and forward sales are used to manage equity market risk through hedging activities that are designed to offset changes in the equity markets that affect income earned on the Company's securities and on the Company's assets under management.

The amount subject to credit risk is limited to the current market value of the instruments which are in a gain position. This represents only a small percentage of the notional amount. The credit risk is presented without giving effect to any netting agreements or collateral arrangements and does not reflect actual or expected losses. The total estimated fair value represents the total amount that the Company would receive or pay to terminate all agreements at each year end. However, this does not result in a gain or loss to the Company as the derivative instruments which correlate to certain assets and liabilities provide offsetting gains or losses.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2002 and 2001 (In thousands of dollars, except shares and per share amounts)

16. Off-balance sheet financial instruments (cont'd)

The following table summarizes the Company's off-balance sheet financial instruments at December 31:

	Notional Amount			Credit Risk	Total Estimated Fair Value
	1 Year or Less	1 – 5 Years	Total		
2002					
Swaps	\$ 71,000	\$ 560,300	\$ 631,300	\$ –	\$ (21,541)
Options purchased	22,129	62,086	84,215	6,005	6,005
Options written	23,473	77,998	101,471	–	(9,626)
Forward sales	–	16,545	16,545	3,837	3,753
	\$ 116,602	\$ 716,929	\$ 833,531	\$ 9,842	\$ (21,409)
2001					
Swaps	\$ 173,300	\$ 619,600	\$ 792,900	\$ 10,630	\$ (6,237)
Options purchased	30,921	67,439	98,360	3,276	3,276
Options written	31,961	81,825	113,786	–	(23,070)
Forward sales	9,837	16,545	26,382	1,256	394
	\$ 246,019	\$ 785,409	\$ 1,031,428	\$ 15,162	\$ (25,637)

17. Fair value of financial instruments

The following table represents the fair value of on and off-balance sheet financial instruments using the valuation methods and assumptions described below. Fair value represents the amount that would be exchanged in an arm's length transaction between willing parties under no compulsion to act and best evidenced by a quoted market price, if one exists. Fair values are management's estimates and are generally calculated using market conditions at a specific point in time and may not reflect future fair values. The calculations are subjective in nature, involve uncertainties and matters of significant judgment.

	Carrying Value	Fair Value	2002 Fair Value Over (Under) Carrying Value	Carrying Value	Fair Value	2001 Fair Value Over (Under) Carrying Value
Assets						
Cash and short term investments	\$ 771,522	\$ 771,522	\$ –	\$ 854,275	\$ 854,275	\$ –
Securities	156,186	284,868	128,682	248,205	431,750	183,545
Loans	548,969	555,508	6,539	655,094	661,797	6,703
Investment in affiliate	320,988	604,605	283,617	297,810	556,723	258,913
Accounts and other receivables	155,299	155,299	–	199,597	199,597	–
Total financial assets	1,952,964	\$ 2,371,802	\$ 418,838	2,254,981	\$ 2,704,142	\$ 449,161
Non-financial assets	4,033,988			3,867,487		
Total assets	\$ 5,986,952			\$ 6,122,468		
Liabilities						
Deposits and certificates	\$ 709,012	\$ 718,155	\$ 9,143	\$ 671,248	\$ 681,552	\$ 10,304
Bankers' acceptances	–	–	–	497,000	497,000	–
Other financial liabilities	548,377	548,377	–	627,837	627,837	–
Long-term debt	1,386,365	1,429,178	42,813	1,362,268	1,373,998	11,730
Total financial liabilities	2,643,754	\$ 2,695,710	\$ 51,956	3,158,353	\$ 3,180,387	\$ 22,034
Non-financial liabilities	393,243			285,871		
Total liabilities	\$ 3,036,997			\$ 3,444,224		
Derivatives (Note 16)	\$ –	\$ (21,409)	\$ (21,409)	\$ –	\$ (25,637)	\$ (25,637)



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2002 and 2001 (In thousands of dollars, except shares and per share amounts)

17. Fair value of financial instruments (cont'd)

Fair value is determined using the following methods and assumptions:

- The fair value of short term financial instruments approximate carrying value. These include cash and short term investments, accounts and other receivables, bankers' acceptances, and other liabilities.
- Securities are valued at quoted market prices, when available. When a quoted market price is not readily available, alternative valuation methods may be used.
- Loans are valued by discounting the expected future cash flows at market interest rates for loans with similar credit risk.
- Deposits and certificates are determined by discounting the contractual cash flows using market interest rates currently offered for deposits with similar terms and credit risks.
- Long-term debt is determined by reference to current market prices for debentures and notes payable with similar terms and risks.
- Derivative financial instruments fair values are based on quoted market prices, where available, prevailing market rates for instruments with similar characteristics and maturities, or net present value analysis.

18. Earnings per common share

	2002	2001
Earnings		
Income before discontinued operations	\$ 509,948	\$ 272,878
Discontinued operations	1,811	116
Net income	511,759	272,994
Preferred dividends	20,700	13,299
Net income available to common shareholders	\$ 491,059	\$ 259,695
Number of common shares (in thousands)		
Weighted-average number of common shares outstanding	263,487	247,093
Add:		
– Potential exercise of outstanding stock options	1,386	839
Weighted-average number of common shares outstanding		
– diluted basis	264,873	247,932
Earnings per common share (in dollars)		
Basic		
Excluding discontinued operations	\$ 1.857	\$ 1.051
Including discontinued operations	\$ 1.864	\$ 1.051
Diluted		
Excluding discontinued operations	\$ 1.847	\$ 1.047
Including discontinued operations	\$ 1.854	\$ 1.047

In certain circumstances, the preferred shares referred to in Note 14 are convertible into common shares. These conversions are not included in the calculation of diluted earnings per share as the Company has the option to settle in cash instead of shares.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2002 and 2001 (In thousands of dollars, except shares and per share amounts)

19. Contingencies and commitments

The Company is committed to the following annual lease payments under its operating leases: 2003 – \$40,959; 2004 – \$31,686; 2005 – \$24,437; 2006 – \$20,614 and 2007 – \$18,253.

20. Related party transactions

The Company enters into transactions with The Great-West Life Assurance Company and London Life Insurance Company, subsidiaries of its affiliate, Great-West Lifeco Inc. These transactions are in the normal course of operations and at market terms and conditions.

During the year, the Company provided to and received from Great-West Life, a member of the Power Financial Corporation group of companies, certain administrative services. The Company distributes life insurance and disability insurance products under a distribution agreement with Great-West Life and received \$17,082 in distribution fees (2001 – \$16,878). London Life distributes certain mutual funds of the Company.

During 2002, the Company sold residential mortgage loans to Great-West Life and London Life for \$200,088 (2001 – \$278,031).

21. Segmented information

The Company acquired Mackenzie effective April 20, 2001. As a result, the Company revised its reportable segments from fee-based operations and intermediary operations to Investors Group, Mackenzie, and Corporate and Other to conform to the current organizational structure and to the basis upon which management measures and evaluates performance.

Investors Group and Mackenzie earn fee-based revenues in the conduct of their core business activities which are primarily related to the distribution, management and administration of their mutual funds. Fee revenues are also derived from the provision of brokerage services. Intermediary revenues are derived primarily from the assets funded by deposit and certificate products and from mortgage banking and servicing activities. In addition, Investors Group earns fee revenue from the distribution of insurance products.

Corporate and Other includes primarily net investment income on unallocated investments and interest expense on corporate debt.

2002	Investors Group	Mackenzie	Corporate and Other	Total
Total assets under management and administration:	\$ 39,678,103	\$ 35,281,603	\$ 648,644	\$ 75,608,350
Income	\$ 1,130,042	\$ 801,518	\$ 8,476	\$ 1,940,036
Expenses	449,581	583,271	–	1,032,852
Earnings before undernoted	\$ 680,461	\$ 218,247	\$ 8,476	907,184
Interest expense				79,514
Income before income taxes, non-controlling interest and discontinued operations				827,670
Income taxes				317,401
Non-controlling interest				321
Income before discontinued operations				509,948
Discontinued operations				1,811
Net income				\$ 511,759



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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21. Segmented information (cont'd)

2001	Investors Group	Mackenzie	Corporate and Other	Total
Total assets under management and administration:	\$ 43,786,454	\$ 39,410,912	\$ 827,968	\$ 84,025,334
Income	\$ 1,168,459	\$ 549,637	\$ 42,512	\$ 1,760,608
Expenses	578,586	415,737	–	994,323
Earnings before undernoted	\$ 589,873	\$ 133,900	\$ 42,512	766,285
Restructuring costs				95,610
Interest expense				73,195
Income before income taxes, non-controlling interest, goodwill amortization and discontinued operations				597,480
Income taxes				252,474
Non-controlling interest				159
Income before goodwill amortization and discontinued operations				344,847
Goodwill amortization, net of tax				71,969
Income before discontinued operations				272,878
Discontinued operations				116
Net income				\$ 272,994

22. Acquisition of Mackenzie Financial Corporation

Effective April 20, 2001, the Company acquired all of the outstanding common shares of Mackenzie, a Canadian financial services company, for a cash consideration of \$3.202 billion and the issue of 38,802,952 common shares of the Company which represented a total consideration of \$3.991 billion including transaction costs. Consideration paid consisted of the following:

(\$ millions)	
Cash	\$ 427
Bridge credit facility	897
Bank term loan	550
Issue of debentures	600
Issue of preferred shares	360
Issue of common shares	368
Total cash consideration	3,202
Fair value of share exchange	789
Total consideration	\$ 3,991

To support this transaction, on April 19, 2001 The Great-West Life Assurance Company, an affiliate of the Company, invested \$230 million to acquire 9,200,000 common shares while Power Financial Corporation invested \$138.3 million to acquire 5,532,000 common shares and now owns 56.1% of the outstanding common shares of the Company.

The acquisition was accounted for by the purchase method and the results of Mackenzie's operations have been included in the consolidated statements of income from the date of acquisition.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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22. Acquisition of Mackenzie Financial Corporation (cont'd)

Details of the consideration paid and the fair values of the net assets acquired are as follows:

(\$ millions)

Fair value of assets acquired:

Cash and short term investments	\$	600
Securities		47
Loans		427
Deferred selling commissions		585
Management contracts		606
Trade names		275
Other assets		132
		<u>2,672</u>

Less liabilities assumed and non-controlling interest:

Deposits		423
Other liabilities		215
Restructuring costs allocated to purchase price		24
Future income taxes on intangible assets		133
Future income taxes		194
Non-controlling interest		14
		<u>1,003</u>

Fair value of net assets acquired

Goodwill		2,322
Total purchase consideration	\$	<u>3,991</u>

The purchase price has been allocated to tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date. The excess of consideration paid over the estimated fair value of net assets acquired has been recorded as goodwill.

23. Restructuring

In connection with the acquisition of Mackenzie, the Company commenced the integration and rationalization of its administration, systems and operations in 2001. Estimated costs of \$95.6 million (\$56.0 million after tax) were charged to earnings in the second quarter of 2001. These costs include severance and related expenses, decommissioning of systems, and restructuring certain businesses. At December 31, 2002, the unexpended portion of the restructuring provision was \$69.8 million (2001 – \$85.2 million).

24. Discontinued operations

On August 29, 2002 ("measurement date"), Mackenzie and its majority owned (85.7%) subsidiary, Mackenzie Investment Management, Inc. ("Mackenzie Investment"), a U.S. financial services company, entered into an agreement to sell Mackenzie Investment to Waddell & Reed Financial, Inc. On December 16, 2002 ("disposal date"), Mackenzie completed the sale. The disposition was made for proceeds of \$94,674, net of the amount allocated to non-controlling interest, resulting in a net gain of \$1,973. The gain on sale includes the recognition of the cumulative foreign currency translation adjustment at the disposal date of \$1,085 and the results of operations between the measurement date and disposal date.

	2002	2001
Revenue	\$ 29,822	\$ 34,567
(Loss) income from operations	(162)	116
Net gain on sale of discontinued operations	1,973	–
Discontinued operations	\$ 1,811	\$ 116

