



**RBC Insurance®**

*Audited Financial Statements of*

**RBC LIFE INSURANCE COMPANY FUNDS**

*December 31, 2010*

# **RBC LIFE INSURANCE COMPANY FUNDS**

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**December 31, 2010**

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## Independent Auditor's Report

To the Unit Holders of

RBC Life Equity Growth Fund ("Equity Growth Fund")  
RBC Life Bond Fund ("Bond Fund")  
RBC Life Balanced Fund ("Balanced Fund")  
(collectively referred to as "RBC Life Insurance Company Funds" or "the Funds")

We have audited the accompanying financial statements of the RBC Life Insurance Company Funds, which comprise the statement of net assets as at December 31, 2010, the statements of operations and of changes in net assets for the year then ended, and a summary of significant accounting policies and other explanatory information.

### Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, 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.

### Auditor's responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal 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 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 each of the Funds as at December 31, 2010 and the results of their operations and the changes in their net assets for the year then ended in accordance with Canadian generally accepted accounting principles.



Chartered Accountants  
Licensed Public Accountants  
March 15, 2011

# RBC LIFE INSURANCE COMPANY FUNDS

## Financial Statements

December 31, 2010

### Equity Growth Fund

Statement of Operations	Year ended	
	December 31, 2010	December 31, 2009
<b>Income</b>		
Distribution from underlying funds	\$ 2,880,509	\$ 1,731,737
Realized losses on sale of investments	(910,569)	(972,585)
Increase in unrealized appreciation of investments	4,631,581	9,290,233
	<b>6,601,521</b>	<b>10,049,385</b>
<b>Expenses</b>		
Management fees	926,265	858,691
Bank charges and interest	3,088	15,816
Audit	4,191	4,191
	<b>933,544</b>	<b>878,698</b>
<b>Net Income</b>	<b>\$ 5,667,977</b>	<b>\$ 9,170,687</b>
Net income per unit	\$ 4.67	\$ 7.02

Statement of Net Assets	As at	
	December 31, 2010	December 31, 2009
<b>Assets</b>		
Investments in underlying fund at fair value	\$ 41,030,113	\$ 39,210,485
Due from RBC Life Insurance Company	24,326	-
	<b>41,054,439</b>	<b>39,210,485</b>
<b>Liabilities</b>		
Bank indebtedness	-	117
Due to RBC Life Insurance Company	-	67,529
	-	<b>67,646</b>
<b>Net assets</b>	<b>\$ 41,054,439</b>	<b>\$ 39,142,839</b>
Net assets value per unit	\$ 35.60	\$ 30.77

Statement of Changes in Net Assets	Year ended	
	December 31, 2010	December 31, 2009
Net assets, beginning of the year	\$ 39,142,839	\$ 31,822,725
Premium deposits	2,929,255	2,809,532
Net income	5,667,977	9,170,687
	<b>47,740,071</b>	<b>43,802,944</b>
<b>Less</b>		
Withdrawals	6,685,632	4,660,105
	<b>6,685,632</b>	<b>4,660,105</b>
<b>Net Assets, end of the year</b>	<b>\$ 41,054,439</b>	<b>\$ 39,142,839</b>
Number of units outstanding	<b>1,153,169</b>	<b>1,272,037</b>

The accompanying notes are an integral part of these financial statements.

# RBC LIFE INSURANCE COMPANY FUNDS

## Supplementary Information

### December 31, 2010

#### Equity Growth Fund

		Management fee	Other expenses	MER <sup>(1)</sup>		
Management fees and other expenses (also see notes 7)	2010	\$ 926,265	\$ 7,279	2.33%		
	2009	\$ 858,691	\$ 20,007	2.43%		
Sales and redemption of units (also see note 8)		Units issued	Proceeds from issue of units	Units redeemed	Amounts paid on redemption	
	2010	88,641	\$ 2,929,255	207,509	\$ 6,685,632	
2009	111,482	\$ 2,809,532	178,558	\$ 4,660,105		
Investments in underlying fund at fair value (also see note 9)		Level 1	Level 2	Level 3	Total	
	2010	\$ 41,030,113	\$ -	\$ -	\$ 41,030,113	
2009	\$ 39,210,485	\$ -	\$ -	\$ 39,210,485		
Schedule of invested assets		Number of units	Cost	% fund owned	Fair value	Fair value per unit
RBC Canadian Equity Fund Series O	2010	1,562,932	\$ 45,212,867	1.90%	\$ 41,030,113	\$ 26.25
	2009	1,644,742	\$ 48,024,819	2.29%	\$ 39,210,485	\$ 23.84

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for the past 5 years.

Financial highlights (Unaudited)	2010	2009	2008	2007	2006
<i>The Fund's distribution and Net Asset Value per unit</i>					
Distributions: <sup>(*)</sup>					
Total annual distributions	\$ 2.50	\$ 1.36	\$ -	\$ 2.90	\$ 0.59
Net Asset Value at December 31	\$ 35.60	\$ 30.77	\$ 23.76	\$ 36.31	\$ 33.02
<i>Ratios and supplemental data</i>					
Net assets (\$ '000)	\$ 41,054	\$ 39,143	\$ 31,823	\$ 50,419	\$ 50,713
Number of units outstanding	1,153,169	1,272,037	1,339,113	1,396,642	1,535,877
Management expense ratio <sup>(1)</sup>	2.33%	2.43%	2.59%	2.58%	2.42%
Portfolio turnover rate of the underlying fund <sup>(2)</sup>	65.52%	82.78%	68.28%	41.28%	33.78%

<sup>(\*)</sup> Distributions were reinvested in the Fund.

<sup>(1)</sup> The management expense ratio ("MER") is based on total expenses for the stated period and is expressed as an annualized percentage of daily average net assets during the period.

<sup>(2)</sup> The underlying fund's portfolio turnover rate indicates how actively the Fund's portfolio advisor manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rate in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

Top 25 holdings of the underlying fund (Unaudited)	% of Assets	% of Assets	
Royal Bank of Canada	4.8	Power Corporation of Canada	2.0
Toronto-Dominion Bank	4.3	Talisman Energy Inc.	1.9
Suncor Energy Inc.	3.9	Teck Resources Ltd., Class B	1.9
Bank of Nova Scotia	3.6	Cenovus Energy Inc.	1.9
Barrick Gold Corp.	3.5	TransCanada Corp.	1.8
Canadian Natural Resources Ltd.	3.5	EnCana Corp.	1.8
Potash Corporation of Saskatchewan Inc.	3.1	Rogers Communications Inc., Class B	1.5
Goldcorp Inc.	2.7	Brook Field Asset Management Inc., Class A	1.4
Canadian National Railway Co.	2.3	Enbridge Inc.	1.4
Canadian Imperial Bank of Commerce	2.2	Thomson Corp.	1.3
Research In Motion Ltd.	2.2	Canadian Oil Sands Trust	1.2
Bank of Montreal	2.0	Magna International Inc., Class A	1.1
Manulife Financial Corporation	2.0	<b>Total % of top 25 holdings</b>	<b>59.3</b>

# RBC LIFE INSURANCE COMPANY FUNDS

## Financial Statements

December 31, 2010

### Bond Fund

<b>Statement of Operations</b>	<b>Year ended December 31, 2010</b>	<b>Year ended December 31, 2009</b>
<b>Income</b>		
Distribution from underlying funds	\$ 212,517	\$ 273,925
Realized gains (losses) on sale of investments	20,006	(3,271)
Increase in unrealized appreciation of investments	142,007	320,716
	<b>374,530</b>	<b>591,370</b>
<b>Expenses</b>		
Management fees	100,947	103,950
Bank charges and interest	868	976
Audit	748	748
	<b>102,563</b>	<b>105,674</b>
<b>Net Income</b>	<b>\$ 271,967</b>	<b>\$ 485,696</b>
Net income per unit	\$ 1.51	\$ 2.52

<b>Statement of Net Assets</b>	<b>As at December 31, 2010</b>	<b>As at December 31, 2009</b>
<b>Assets</b>		
Investments in underlying fund at fair value	\$ 5,024,093	\$ 5,159,181
	<b>5,024,093</b>	<b>5,159,181</b>
<b>Liabilities</b>		
Bank indebtedness	-	13
Due to RBC Life Insurance Company	1,300	6,728
	<b>1,300</b>	<b>6,741</b>
<b>Net assets</b>	<b>\$ 5,022,793</b>	<b>\$ 5,152,440</b>
Net assets value per unit	\$ 29.02	\$ 27.53

<b>Statement of Changes in Net Assets</b>	<b>Year ended December 31, 2010</b>	<b>Year ended December 31, 2009</b>
Net assets, beginning of the year	\$ 5,152,440	\$ 4,977,737
Premium deposits	375,694	390,409
Net income	271,967	485,696
	<b>5,800,101</b>	<b>5,853,842</b>
Less		
Withdrawals	777,308	701,402
	<b>777,308</b>	<b>701,402</b>
<b>Net Assets, end of the year</b>	<b>\$ 5,022,793</b>	<b>\$ 5,152,440</b>
Number of units outstanding	<b>173,070</b>	<b>187,169</b>

The accompanying notes are an integral part of these financial statements.

# RBC LIFE INSURANCE COMPANY FUNDS

## Supplementary Information

### December 31, 2010

#### Bond Fund

		Management fee	Other expenses	MER <sup>(1)</sup>			
Management fees and other expenses (also see notes 7)	2010	\$ 100,947	\$ 1,616	2.02%			
	2009	\$ 103,950	\$ 1,724	2.09%			
Sales and redemption of units (also see note 8)		Units issued	Proceeds from issue of units	Units redeemed	Amounts paid on redemption		
	2010	13,024	\$ 375,694	27,123	\$ 777,308		
	2009	17,803	\$ 390,409	29,505	\$ 701,402		
Investments in underlying fund at fair value (also see note 9)		Level 1	Level 2	Level 3	Total		
	2010	\$ 5,024,093	\$ -	\$ -	\$ 5,024,093		
	2009	\$ 5,159,181	\$ -	\$ -	\$ 5,159,181		
Schedule of invested assets		Number of units	Cost	% fund owned	Fair value	Fair value per unit	
	RBC Bond Fund Series O	2010	783,069	\$ 4,814,719	0.10%	\$ 5,024,093	\$ 6.42
		2009	829,917	\$ 5,093,846	0.17%	\$ 5,159,181	\$ 6.22

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for the past 5 years.

Financial highlights (Unaudited)	2010	2009	2008	2007	2006
<i>The Fund's distribution and Net Asset Value per unit</i>					
Distributions: <sup>(*)</sup>					
Total annual distributions	\$ 1.23	\$ 1.46	\$ 1.35	\$ 1.24	\$ 0.90
Net Asset Value at December 31	\$ 29.02	\$ 27.53	\$ 25.03	\$ 25.26	\$ 24.94
<i>Ratios and supplemental data</i>					
Net assets (\$ '000)	\$ 5,023	\$ 5,152	\$ 4,676	\$ 5,267	\$ 5,788
Number of units outstanding	173,070	187,169	198,871	208,537	232,108
Management expense ratio <sup>(1)</sup>	2.02%	2.09%	2.02%	2.24%	2.18%
Portfolio turnover rate of the underlying fund <sup>(2)</sup>	44.95%	60.39%	49.72%	61.05%	47.90%

<sup>(\*)</sup> Distributions were reinvested in the Fund.

<sup>(1)</sup> The management expense ratio ("MER") is based on total expenses for the stated period and is expressed as an annualized percentage of daily average net assets during the period.

<sup>(2)</sup> The underlying fund's portfolio turnover rate indicates how actively the Fund's portfolio advisor manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rate in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

Top 25 holdings of the underlying fund (Unaudited)	% of Assets	% of Assets
RBC Emerging Market Fund	2.9	Province of ontario 9.500% Jul 13 22
Cash & Cash Equivalents	2.4	Province of Quebec 4.500% Dec 1 17
Royal Bank of Canada	1.9	Government of Canada 1.250% Dec 1 11
Toronto-Dominion Bank	1.6	Government of Canada 3.750% Jun 1 19
Government of Canada 5.000% Jun 1 37	1.5	Goldcorp Inc.
Suncor Energy Inc.	1.5	Canadian National Railway Co.
Barrick Gold Corp.	1.5	Canadian Imperial Bank of Commerce
Bank of Nova Scotia	1.4	Research in Motion Ltd.
Government of Canada 1.250% Jun 1 11	1.3	Province of Quebec 6.000% Oct 1 12
Canadian Natural Resources Ltd.	1.3	Government of Canada 4.000% Jun 1 41
Province of Ontario 4.750% Jun 2 13	1.3	Province of Manitoba 6.500% Sep 22 17
Potash Corporation of Saskatchewan Inc.	1.2	Province of Ontario 4.400% Jun 2 19
Province of Quebec 5.250% Oct 1 13	1.2	<b>Total % of top 25 holdings</b>
		<b>32.3</b>

# RBC LIFE INSURANCE COMPANY FUNDS

## Financial Statements

December 31, 2010

### Balanced Fund

#### Statement of Operations

	Year ended December 31, 2010	Year ended December 31, 2009
<b>Income</b>		
Distribution from underlying funds	\$ -	\$ -
Realized losses on sale of investments	(144,001)	(226,701)
Increase in unrealized appreciation of investments	1,656,870	2,303,325
	<b>1,512,869</b>	<b>2,076,624</b>
<b>Expenses</b>		
Management fees	341,243	338,443
Bank charges and interest	1,439	1,579
Audit	2,297	2,297
	<b>344,979</b>	<b>342,319</b>
<b>Net Income</b>	<b>\$ 1,167,890</b>	<b>\$ 1,734,305</b>
Net income per unit	\$ 2.42	\$ 3.36

#### Statement of Net Assets

	As at December 31, 2010	As at December 31, 2009
<b>Assets</b>		
Investments in underlying fund at fair value	\$ 14,470,035	\$ 14,601,084
Due from RBC Life Insurance Company	30,297	-
	<b>14,500,332</b>	<b>14,601,084</b>
<b>Liabilities</b>		
Bank indebtedness	-	12
Due to RBC Life Insurance Company	-	18,564
	-	18,576
<b>Net assets</b>	<b>\$ 14,500,332</b>	<b>\$ 14,582,508</b>
Net assets value per unit	\$ 31.49	\$ 28.98

#### Statement of Changes in Net Assets

	Year ended December 31, 2010	Year ended December 31, 2009
Net assets, beginning of the year	\$ 14,582,508	\$ 13,587,808
Premium deposits	1,134,307	1,177,625
Net income	1,167,890	1,734,305
	<b>16,884,705</b>	<b>16,499,738</b>
Less		
Withdrawals	2,384,373	1,917,230
	<b>2,384,373</b>	<b>1,917,230</b>
<b>Net Assets, end of the year</b>	<b>\$ 14,500,332</b>	<b>\$ 14,582,508</b>
Number of units outstanding	460,499	503,125

The accompanying notes are an integral part of these financial statements.

# RBC LIFE INSURANCE COMPANY FUNDS

## Supplementary Information

### December 31, 2010

#### Balanced Fund

		Management fee	Other expenses	MER <sup>(1)</sup>		
Management fees and other expenses (also see notes 7)	2010	\$ 341,243	\$ 3,736	2.37%		
	2009	\$ 338,443	\$ 3,876	2.43%		
		Units issued	Proceeds from issue of units	Units redeemed	Amounts paid on redemption	
Sales and redemption of units (also see note 8)	2010	38,191	\$ 1,134,307	80,817	\$ 2,384,373	
	2009	43,965	\$ 1,177,625	71,358	\$ 1,917,230	
		Level 1	Level 2	Level 3	Total	
Investments in underlying fund at fair value (also see note 9)	2010	\$ 14,470,035	\$ -	\$ -	\$ 14,470,035	
	2009	\$ 14,601,084	\$ -	\$ -	\$ 14,601,084	
Schedule of invested assets		Number of units	Cost	% fund owned	Fair value	Fair value per unit
RBC Balanced Fund Series O	2010	1,085,801	\$ 14,381,502	32.18%	\$ 14,470,035	\$ 13.33
	2009	1,219,489	\$ 16,169,420	37.18%	\$ 14,601,084	\$ 11.79

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for the past 5 years.

Financial highlights (Unaudited)	2010	2009	2008	2007	2006
<i>The Fund's distribution and Net Asset Value per unit</i>					
Distributions: <sup>(*)</sup>					
Total annual distributions	\$ -	\$ -	\$ -	\$ 2.38	\$ 0.90
Net Asset Value at December 31	\$ 31.49	\$ 28.98	\$ 25.61	\$ 25.61	\$ 30.40
<i>Ratios and supplemental data</i>					
Net assets (\$ '000)	\$ 14,500	\$ 14,583	\$ 13,588	\$ 17,767	\$ 18,273
Number of units outstanding	460,499	503,125	530,517	550,997	601,037
Management expense ratio <sup>(1)</sup>	2.37%	2.43%	2.46%	2.59%	2.51%
Portfolio turnover rate of the underlying fund <sup>(2)</sup>	82.19%	83.17%	68.60%	55.04%	60.75%

<sup>(\*)</sup> Distributions were reinvested in the Fund.

<sup>(1)</sup> The management expense ratio ("MER") is based on total expenses for the stated period and is expressed as an annualized percentage of daily average net assets during the period.

<sup>(2)</sup> The underlying fund's portfolio turnover rate indicates how actively the Fund's portfolio advisor manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rate in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

Top 25 holdings of the underlying fund (Unaudited)	% of Assets	% of Assets	
<i>Long Positions</i>			
Cash & Cash Equivalents	4.2	Toronto-Dominion Bank 4.854% Feb 13 13	1.1
Government of Canada 5.000% Jun 1 37	2.5	Canada Housing Trust No. 1 3.350% Dec 15 20	1.1
Government of Canada 4.000% Jun 1 41	2.0	Government of Canada 3.750% Jun 1 19	1.1
Province of Ontario 4.650% Jun 2 41	1.8	Canada Housing Trust NO. 1 3.600% Jun 15 13	1.1
Province of Ontario 4.700% Jun 2 37	1.5	Toronto-Dominion Bank 5.480% Apr 2 20	1.1
Bank of Nova Scotia 5.040% Apr 8 13	1.5	Canada Housing Trust No. 1 3.550% Sep 15 13	0.9
Province of Quebec 5.000% Dec 1 41	1.4	Canada Housing Trust No. 1 2.450% Dec 15 15	0.9
Province of Ontario 4.600% Jun 2 39	1.4	Government of Canada 3.000% Jun 1 14	0.9
Province of Quebec 4.500% Dec 1 19	1.4	Toronto-Dominion Bank 4.779% Dec 1 416	0.8
Province of Ontario 4.200% Jun 2 20	1.3	<b>Total - long positions</b>	<b>32.9</b>
Canada Housing Trust No. 1 4.100% Dec 15 18	1.3	<i>Short Positions</i>	
Canadian Imperial Bank of Commerce 4.110% Apr 30 20	1.2	United States 2-Year Note Future, March 2011	-1.3
Province of Quebec 5.000% Dec 1 38	1.2	United States 5-Year Note Future, March 2011	-4.2
Royal Bank of Canada 4.350% Jun 15 20	1.2	<b>Total - short positions</b>	<b>-5.5</b>
		<b>Total % of top 25 holdings</b>	<b>27.4</b>



# RBC LIFE INSURANCE COMPANY FUNDS

## Notes to the Financial Statements

December 31, 2010

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### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### c) Net asset value per unit

Net asset value per unit is computed by dividing the net assets attributable to a series of units on a business day by the total number of units of the series outstanding on that day.

#### d) Net income per unit

Net income per unit in the Statements of Operations represents the increase (decrease) in net assets from operations attributable to the series for the period, divided by the average number of units outstanding during the year.

#### e) Use of estimates

These financial statements are prepared in accordance with Canadian generally accepted accounting principles, and include estimates and assumptions by management that affect the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

#### f) Expenses of funds

Each Fund is responsible for the payment of the fees and expenses related to the operation of that Fund. Such fees and expenses include custodian fees, management fees, insurance fees, legal fees, audit fees, operations and administration fees, bank charges, interest, brokerage on securities transactions and all indirect taxes.

#### g) Income taxes

Each Fund is deemed to be an inter-vivos trust under the provisions of the Income Tax Act (Canada) and is deemed to have allocated its income to the contract holders. Each Fund's net capital gains (losses) are deemed to be those of the contract holders. Accordingly, each Fund is not subject to income tax on its net income, including net realized capital gains.

### 4. FINANCIAL INSTRUMENTS RISK

The Funds may be exposed to a variety of financial risks. Each of the Fund's exposures to financial risks is concentrated in its investment holdings. The Schedule of Invested Assets on each Fund's Supplementary Information presents the details of units held by each Fund as at December 31, 2010 and groups the underlying funds by their nature. The Funds do not manage their underlying funds and therefore the quantitative and qualitative risk disclosures have not been disclosed. For further information on the financial instruments risk of the underlying fund and the sensitivity to price changes please refer to the financial statements of the underlying fund which are filed on Sedar.

Each of the Fund's risk management practice includes the monitoring of compliance to investment guidelines. The fund manager manages the potential effects of these financial risks on the Funds' performance by employing and overseeing professional and experienced portfolio advisors that regularly monitor the Funds' positions, market events and diversify investment portfolios within the constraints of the investment guidelines.

**RBC LIFE INSURANCE COMPANY FUNDS**

**Notes to the Financial Statements**

**December 31, 2010**

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# RBC LIFE INSURANCE COMPANY FUNDS

## Notes to the Financial Statements

December 31, 2010

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### 4. FINANCIAL INSTRUMENTS RISK (continued)

#### **Credit risk**

Credit risk is the possibility that a borrower, or the counterparty to a derivatives contract, repurchase agreement or reverse repurchase agreement, is unable or unwilling to repay the loan or obligation, either on time or at all. Companies and governments that borrow money, and the debt securities they issue, are rated by specialized rating agencies.

Debt securities issued by companies or governments in emerging markets often have higher credit risk (lower rated debt), while debt securities issued by well-established companies or by governments of developed countries tend to have lower credit risk (higher rated debt). A downgrade in an issuer's credit rating or other adverse news regarding an issuer can reduce a security's market value. Lower rated and unrated debt instruments generally offer a better return than higher grade debt instruments, but have the potential for substantial loss. Funds that invest in companies or markets with higher credit risk tend to be more volatile in the short term. However, they may offer the potential of higher returns over the long term.

Credit risk arises when an underlying mutual fund invests in fixed income securities. Credit risk is considered as part of the investment decision making process. The underlying mutual funds only buy and sell investments through brokers which are considered to be approved counterparties, thus minimizing the risk of default during settlement.

#### **Currency risk**

Most underlying funds are valued in Canadian dollars. However, underlying funds that purchase foreign securities may be required to pay for such securities using a foreign currency and receive a foreign currency when they sell them. As a result, changes in the value of the Canadian dollar compared to foreign currencies will affect the value of any foreign securities. For example, if the Canadian dollar rises relative to a foreign currency (like the U.S. dollar or the euro), the Canadian dollar value of an investment denominated in that foreign currency may decline. This decline may reduce, or even eliminate, any return the Fund has earned on the security. On the other hand, a Fund may also benefit from changes in exchange rates. Currency exposure may increase the volatility of foreign investments relative to Canadian investments. Some underlying funds may hedge (protect against) the risk of changes in foreign currency exchange rates of the underlying assets of the Fund.

As the Funds only invest in Canadian denominated underlying funds, the Funds do not have a direct currency risk exposure.

#### **Interest rate risk**

If a Fund invests primarily in bonds and other fixed-income securities, the biggest influence on the Fund's value will be changes in the general level of interest rates. If interest rates fall, the value of the Fund's Units will tend to rise. If interest rates rise, the value of the Fund's Units will tend to fall. Short-term interest rates can have a different influence on a Fund's value than long-term interest rates. If a Fund invests primarily in bonds and other fixed-income securities with longer-term maturities, the biggest influence on the Fund's value will be changes in the general level of long-term interest rates. If a Fund invests primarily in bonds and other fixed-income securities with shorter-term maturities, the biggest influence on the Fund's value will be changes in the general level of shorter-term interest rates. Investors seeking current income should be aware that the level of interest income from a money market fund will fluctuate as short-term interest rates vary.

# RBC LIFE INSURANCE COMPANY FUNDS

## Notes to the Financial Statements

December 31, 2010

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### 4. FINANCIAL INSTRUMENTS RISK (continued)

Interest rate risk arises when the underlying mutual fund invests in interest bearing financial instruments such as a bond. The underlying mutual fund is exposed to the risk that the value of such financial instruments will fluctuate due to changes in the prevailing levels of market interest rates. In general, as interest rates rise, the price of a fixed rate bond will fall, and vice versa.

#### **Liquidity risk**

Liquidity refers to the speed and ease with which an asset can be sold and converted into cash. Most securities owned by an underlying fund can be sold easily and at a fair price. In highly volatile markets, such as in periods of sudden interest rate changes, certain securities may become less liquid, which means they cannot be sold as quickly or easily. Some securities may be illiquid because of legal restrictions, the nature of the investment, or because of features like guarantees. Another reason for illiquidity is a lack of buyers interested in a particular security or market. Difficulty in selling securities may result in a loss or reduced return for a Fund.

The Funds' assets are comprised of units of underlying mutual funds which can be redeemed upon request from the issuer on a valuation date. A valuation date occurs every day that the principal exchange is open for trading and a value is available for the assets of the relevant fund. The Toronto Stock Exchange currently is the principal exchange used for purposes of determining the valuation dates.

#### **Market risk**

Market risk is the risk that the value of investments will fluctuate as a result of changes in market condition. Several factors can influence market trends, such as economic developments, changes in interest rates, political changes, and catastrophic events. The Funds are exposed to the market risk of the underlying funds.

### 5. FINANCIAL RISK MANAGEMENT

The Funds use a fund-of-fund structure to invest in underlying mutual funds exclusively managed by RBC Global Asset Management and its partners. As part of the fund selection process for the Funds, the existing funds line-up are reviewed at least annually to identify any product gaps that result from the changing needs of the market and distribution partners.

The screening criteria may include qualitative as well as quantitative measures of performance and must satisfy internal risk management standards and require approval from the Investment Executive Committee.

Ongoing monitoring throughout the year by the Funds' management includes monitoring any organizational or fund changes announced by fund managers or news items that may affect organizational stability or Funds' performance as well as analysis on the Funds' rate of return to verify that it is appropriate compared to the underlying mutual fund or fund's benchmark.

Included in the ongoing due diligence process, managers of the underlying mutual funds are required to verify that the Funds have adhered to the Funds' Investment Policies and that the underlying mutual funds are managed in accordance with the investment objectives and strategies.

# RBC LIFE INSURANCE COMPANY FUNDS

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### 6. CAPITAL MANAGEMENT

CICA Handbook section 1535 “Capital Disclosure”, requires that the Fund disclose information about its objectives, policies and process for managing capital including disclosure of any externally imposed capital requirements and the consequences of any non-compliance. The Funds consider their net assets to be their respective capital, the relevant capital movements are disclosed in the Statement of Changes in Net Assets. The Funds have no externally imposed capital requirements.

### 7. MANAGEMENT FEES AND OTHER EXPENSES

In consideration for management services and investment advice, RBC Life Insurance Company, a related party, is entitled to a management fee. The maximum management fee, exclusive of HST, is based on the following annual percentages, applied on a weekly basis to the respective net asset values of the Fund

Equity Growth Fund	Up to 2.275%
Bond Fund	Up to 1.900%
Balanced Fund	Up to 2.275%

The management expense ratios for the Funds are based on expenses charged directly to the Fund (other than brokerage commissions and taxes on securities transactions) plus, if applicable, expenses of the underlying funds, calculated on a weighted average basis on the percentage weighting of underlying funds and is expressed as a percentage of the annual average net asset value calculated for the purpose of the issue of units of the Funds. Custodian fee, audit fee, interest and bank charges are payable by the Funds.

As of July 1, 2010, management fees and other administrative expenses charged to the Funds are subject to the Harmonized Sales Tax (HST) in Ontario, British Columbia, Nova Scotia, New Brunswick and Newfoundland and Labrador. This replaces the previous 5% federal GST charge.

Based on the rules and guidance issued by the Department of Finance, the effective HST rate will reflect the tax rates that are applicable in the Provinces/Territories where the fund’s unitholders reside. Since each fund will have unitholders in more than one Province/Territory, the *blended* rate will be a weighted average based on the tax rate in each Province/Territory and the value of unitholder assets. Therefore the blended rate is likely to be different for each fund.

The HST will result in an increase in the funds’ Management Expense Ratio (MER) that will impact the returns of the Funds in 2010 and thereafter.

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### 8. UNITHOLDERS' EQUITY

Units of the Funds, which are redeemable at the option of the holder in accordance with the provisions of the related policy contracts, do not have any nominal or par value and the number of units which may be issued is unlimited. Units of the Fund are issued or redeemed on a weekly basis at the net asset value per unit next determined after the purchase order or redemption request, respectively, is received by RBC Life Insurance Company.

### 9. FAIR VALUE

Investments recorded at fair value on the Funds' Statement of Net Assets are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Hierarchical levels, defined by Section 3862 and directly related to the amount of subjectivity associated with inputs to fair valuation of these assets, are as follows:

Level 1 – Quoted prices are available in active markets for identical investments as of the reporting date. Quoted price for these investments are not adjusted even in situations where a large position and a sale could reasonably impact the quoted price.

Level 2 – Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.

Level 3 – Pricing inputs are unobservable for the investment and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation.

### 10. COMPARATIVE FIGURES

The Company restated for 2009, net income per unit for all Funds. The net income, previously divided by end of year outstanding units, was divided by weighted average number of units for the year. The restatement had no effect on net income.