

2006
CHARTERHOUSE
PREFERRED SHARE INDEX CORPORATION

Annual Report

Period ended July 31, 2006

Table of Contents

Report to Shareholders.....	3
Annual Management Report of Fund Performance.....	4
Management Responsibility for Financial Reporting.....	13
Auditors' Report.....	14
Financial Statements.....	15
Corporate Information.....	24

To Our Shareholders

We are pleased to provide the audited financial results of Charterhouse Preferred Share Index Corporation (the “Company”) for the year ended July 31, 2006.

The Company offers investors:

1. cost-efficient exposure to an indexed portfolio (the “Index Portfolio”) of fixed-rate preferred shares and preferred securities of Canadian issuers that is representative of the investible universe of such securities; and
2. return of capital distributions, paid quarterly.

As at July 31, 2006, the Index Portfolio, comprised of 87 securities issued by 34 issuers, was broadly diversified in terms of both industry and security type. The constituent securities had an average DBRS rating of Pfd-2.

For the year ended July 31, 2006, the Company paid a total of \$1.0517 in return of capital distributions per preferred share.

This report, along with the accompanying consolidated annual financial statements of the Company and the Management Report of Fund Performance, is submitted to you on behalf of the Board of Directors.



Kevin Beatson
Chief Executive Officer



Jason Mackey
Chief Financial Officer

October 18, 2006

Annual Management Report of Fund Performance

This annual management report of fund performance contains financial highlights but does not contain the complete annual financial statements of the Company. The complete consolidated annual financial statements are appended to this report.

Securityholders may obtain a copy of the Company's proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure, at no cost by calling (866) 977-6311, or by sending a request to 26 Wellington Street East, Suite 920, Toronto, Ontario, M5E 1S2.

Management Discussion of Fund Performance

Introduction

The Company (referred to below as "we" or "our") effectively began operations on November 10, 2004 when we completed the initial public offering of 2,425,000 preferred shares (the "Preferred Shares") at a price of \$25.00 per share.

Change of Control of the Manager

On May 18, 2006, control of Charterhouse PSI Management Corporation, the manager of the Company and Charterhouse PSI Investment Corporation ("IndexCo"), was acquired by Jovian Capital Corporation ("Jovian") through the acquisition of the balance of the shares of Charterhouse Holding Corporation ("Holding") not already owned by Jovian. Jovian acquired its original minority stake in Holding in September 2004.

Jovian is a management and holding company with interests in a variety of financial service firms specializing in wealth and asset management. The Jovian group of companies operates as a national financial services organization with approximately \$12 billion of client assets as at August 31, 2006.

A wholly-owned subsidiary of Jovian, Jove Investment Management Inc. ("Jove"), acts as the index administrator for IndexCo.

Investment Objectives and Strategies

Our investment objectives are to provide holders of our Preferred Shares (our "Shareholders") with:

1. cost-effective exposure to an indexed portfolio (the "Portfolio") that is representative of the universe of Toronto Stock Exchange ("TSX") listed fixed rate preferred shares and preferred securities of Canadian issuers ("Portfolio Securities"); and
2. return of capital distributions, paid quarterly.

To qualify for our Portfolio, a preferred share or preferred security must meet certain minimum criteria, including credit rating and issue size.

Return of capital distributions are not generally subject to tax but do reduce the adjusted cost base of the Preferred Shares to an investor.

Risk

There are risks associated with an investment in our Preferred Shares. Our initial public offering prospectus (the "Prospectus") contains a full discussion of these risks. The Prospectus is available on our website at www.charterhousefinancial.com or SEDAR at www.sedar.com.

Our Preferred Shares are suitable for investors who are:

1. investing for the medium to long term;
2. interested in receiving tax efficient quarterly income; and
3. willing to accept moderate volatility in the net asset value of their investment.

For the year ending July 31, 2006, the following developments have influenced the overall performance and level of risk of our Preferred Shares:

1. The Portfolio, while continuing to average a Pfd-2 rating, included a higher percentage in Pfd-1 rated issues, 34% of the Portfolio as at July 31, 2006 versus 28% of the Portfolio as at July 31, 2005 ("2005 Year End"). The highlights of the rating changes during the year were:
 - a. On August 2, 2005, CIBC announced that it would pay US\$2.4 billion to settle a class action litigation relating to Enron Corp. Following the announcement, Dominion Bond Rating Service ("DBRS") reduced the rating of CIBC's preferred shares from Pfd-1 (Low) to Pfd-2 (High). This affected eleven securities in the portfolio (reduced to nine after taking into account the redemption of CIBC preferred share Series 20, 21 and 22 and the acquisition of Series 30 during the year). As a result of the net redemption of CIBC preferred shares, our exposure to CIBC fell from 9.83% at July 31, 2005, to 7.8% at July 31, 2006.
 - b. On November 3, 2005, DBRS downgraded the preferred share ratings of Bell Canada, BCE and Aliant from Pfd-2 (High), Pfd-2 and Pfd-2 (Low) to Pfd-2, Pfd-2 (Low) and Pfd-3 (High), respectively. The downgrades affected eight securities in our Portfolio. On June 30, 2006, Aliant Inc. redeemed its Series 2 preferred shares.
 - c. On February 17, 2006, DBRS upgraded the preferred share rating of Great-West Lifeco Inc. from Pfd-2 (High) to Pfd-1 (Low). The upgrade affected five securities in our Portfolio.
 - d. Finally, on April 18, DBRS upgraded the preferred share rating of Power Financial Corporation from Pfd-2 (High) to Pfd-1 (Low). The upgrade affected eight securities in our Portfolio.
2. During the year, we sold down some positions in Portfolio Securities in order to fund retractions and share repurchases under our normal course issuer bid. These sales reduced dividend income available for distribution. In total, the Portfolio Securities sold represented approximately 4.4% of the Portfolio Securities as at 2005 Year End.
3. The Canadian dollar strengthened during from 81.6 US cents to 88.4 US cents since our previous year-end. This had a negative impact on the Canadian dollar value of our US dollar securities. At the same time, our US dollar exposure has declined with the redemption of three of our five US dollar securities during the fiscal year.
4. We borrow on a short term basis at rates lower than the current yield of our Portfolio to invest in additional Portfolio Securities in order to increase our net investment income and quarterly distributions. We experienced a significant increase in borrowing rates in fiscal 2006, with short term BA borrowing rates increasing from 2.7% to 4.36% over the course of the year.

Results of Operations

a) Portfolio

At July 31, 2006, our Portfolio consisted of 87 securities issued by 34 different issuers, as compared with 82 securities and 29 issuers as at July 31, 2005. The average rating by DBRS of our Portfolio Securities was unchanged at Pfd-2.

Since July 31, 2005, six series of preferred shares were redeemed - CIBC Series 20, 21 and 22, at US\$25.50, \$26.00 and US\$26.00 per share respectively; Royal Bank Series P at US\$25.75 per share; The Toronto-Dominion Bank Series J at \$25.80; and the Aliant Inc. Series 2 at \$25 per share. Except for the Royal Bank and the Aliant issues, the other four were retractable preferred shares. Redemption proceeds were reinvested in 14 series of straight perpetual preferred shares, three of which were already Portfolio Securities, issued by 11 issuers.

During the year, we sold down some positions in Portfolio Securities in order to fund retractions and share repurchases under our normal course issuer bid. In total, the shares sold represented approximately 4.4% of the value of Portfolio Securities at July 31, 2005. Excluding these security sales, the Portfolio decreased in value by \$854,102 or 0.7%. This contributed to a decrease in NAV per Preferred Share from \$23.28 at 2005 Year End to \$22.83 on July 31, 2006 or about 1.93%.

b) Investment Income and Distributions

Our investment income for fiscal 2006 was \$3,367,411. After deducting expenses of \$884,036, including \$330,439 in interest expense, our net investment income before distributions on Preferred Shares totalled \$2,483,375.

In total, we paid cash distributions of \$2,495,714 or \$1.05 per Preferred Share during the period. For tax purposes, these distributions are treated as return of capital.

The first quarter distribution of \$0.2835 per Preferred Share (or \$0.2635 per Preferred Share after deducting approximately \$0.02 which was attributable to above estimate distributable net investment income earned in the previous fiscal year), was followed by distributions of \$0.2590, \$0.2570 and \$0.2522 per Preferred Share, in the second, third and fourth quarters respectively. The declining trend in distributions is the result of:

1. Less Portfolio income due to:
 - a. the sale of some Portfolio Securities to fund retractions, and
 - b. the redemption of certain Portfolio Securities as discussed under "Results of Operations – Portfolio" and the reinvestment of the proceeds in recently issued, lower coupon securities; and
2. Higher interest expense due to:
 - a. our short term BA borrowing rates rising from 2.7% at the start of fiscal 2006 to 4.36% by the end of fiscal 2006.

c) Liquidity and Capital Resources

At July 31, 2006, our outstanding borrowing, comprised of four bankers' acceptances at a weighted average rate of 4.42%, was \$8,548,490. This amount represented 13.86% of total assets or 16.1% of net assets, including the Preferred Shares. This was \$504,943 lower than the amount outstanding as at July 31, 2005 but represented approximately the same percentage of total assets. We used these borrowed funds to purchase Portfolio Securities in order to generate additional net investment income.

During the year ended July 31, 2006, our minimum and maximum borrowings were \$8.21 million and \$8.67 million, respectively. In every instance, these borrowings were drawn down in compliance with our borrowing restrictions and loan covenants.

The TSX approved our application to renew our normal course issuer bid program (the “NCIB”). Effective from January 16, 2006 to January 15, 2007, the NCIB allows us to buy up to 237,600 Preferred Shares for cancellation when they are trading below net asset value (“NAV”). Purchases under the NCIB are therefore accretive to NAV per Preferred Share.

During the year ended July 31, 2006, we bought 76,000 Preferred Shares for cancellation under the NCIB at an average price of \$22.98. Together with the 27,600 Preferred Shares tendered for retraction, the number of Preferred Shares outstanding fell by 103,600 or 4.3% since 2005 Year End.

Recent Developments

The Royal Bank of Canada announced the redemption of its Series S preferred shares at \$26.00 per share which will take place on October 6, 2006. Falconbridge Ltd announced the redemption of its Series G preferred shares at \$25.00 per share which will take place on November 1, 2006. We will reinvest the proceeds from the redemption of these issues in qualifying issues in accordance with our investment guidelines.

Short term rates which steadily increased over the fiscal year, appear to have stabilized and to be trending lower. According to the Bank of Canada, the benchmark 90-day bankers’ acceptance rate went from 4.48% in early July, 2006 to 4.31% as at September 20, 2006. If this trend continues, it will improve the spread we earn on Portfolio Securities acquired with borrowings under the loan agreement.

Management Report of Fund Performance

Financial Highlights

The following tables show selected key financial information about the Company and are intended to help readers better understand our financial performance for year ended July 31, 2006 and period from November 10, 2004 (date of inception) to July 31, 2005. Since the Company had only been in operation for approximately 8½ months at July 31, 2005, a period during which we were still assembling the Portfolio, we do not believe that such results are fully comparable to those achieved in the annual period ended July 31, 2006.

This information is derived from our audited annual consolidated financial statements

The Company's Net Asset Value (NAV) per Preferred Share

NAV per preferred share, beginning of the period (1)	\$	<u>23.28</u>	\$	<u>23.52</u> ¹
Increase (decrease) from operations:				
Total revenue		1.41		0.94
Total expenses		(0.37)		(0.22)
Realized gains for the period		(0.08)		0.01
Unrealized losses for the period		<u>(0.35)</u>		<u>(0.27)</u>
Total increase (decrease) from operations		<u>0.61</u>		<u>0.46</u>
Distributions (2,3):				
From income (excluding dividends)		-		-
From dividends		-		-
From capital gains		-		-
Return of capital		<u>(1.05)</u>		<u>(0.70)</u>
Total annual distributions		<u>(1.05)</u>		<u>(0.70)</u>
NAV per preferred share at July 31 of period shown	\$	22.86	\$	23.28

(1) Initial NAV per preferred share is calculated by deducting agents' fees and other expenses relating to our initial public offering from the issue price of \$25.00.

(2) NAV and distributions are based on the actual number of Preferred Shares outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of Preferred Shares over the financial period.

(3) Distributions were paid in cash.

Ratios and Supplemental Data

	<u>2006</u>	<u>2005</u>
Net Assets, including the Preferred Shares (000's) ⁽¹⁾	\$ 53,047	\$ 56,437
Number of Preferred Shares outstanding ⁽¹⁾	2,320,900	2,424,500
Management expense ratio ⁽²⁾		
Excluding interest expense and one-time issue costs	1.00%	.96%
Including interest expense but excluding one-time issue costs	1.59%	1.28%
Including interest expense and one-time issue costs before waivers or absorptions	1.59%	7.56%
Portfolio turnover rate ⁽³⁾	11.67%	9.65%
Trading expense ratio ⁽⁴⁾	0.01%	0.18%
Closing market price	\$ 23.00	\$ 24.50

(1) This information is provided as at July 31.

(2) Management expense ratio is expressed as an annualized percentage of daily average net assets during the period

(3) The Company's portfolio turnover rate indicates how actively the Company's portfolio advisor manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Company buying and selling all of the securities in its portfolio once in the course of the year. The higher the company's portfolio turnover rate in a year, the greater the trading costs payable by the Company 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 the Company.

(4) The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net assets during the period.

Management Fees

Under our agreement with Charterhouse PSI Management Corporation (the "Manager"), the Manager is responsible for providing all management and administrative services and facilities to us. These services include monitoring the performance of Jove Investment Management Inc. ("Jove", formerly Felcom Management Corp.), the Index Administrator, administering distributions, providing financial reports to our Shareholders, making sure that we comply with all applicable laws and managing the relationships with our third party service providers, such as State Street Trust Company Canada, our custodian.

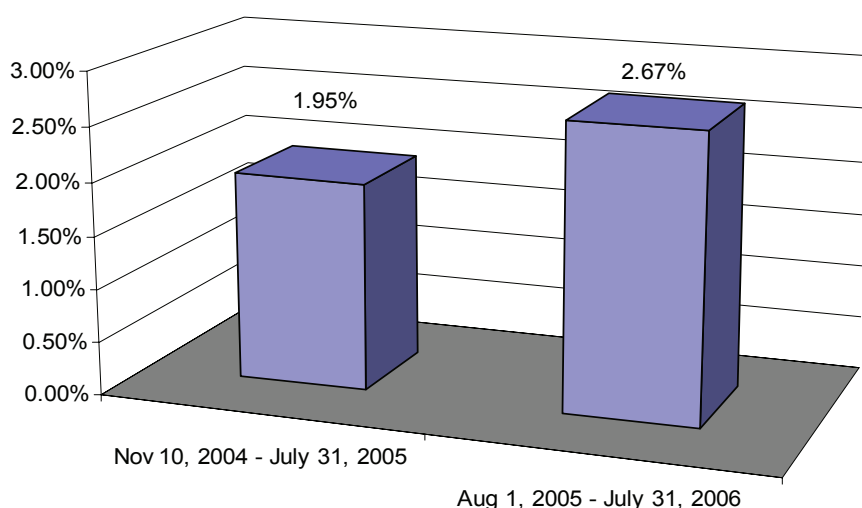
For these services, Charterhouse Preferred Share Index Corporation pays the Manager a fee equal to 0.05% per annum of its NAV and its wholly owned subsidiary, Charterhouse PSI Investment Corporation, pays the Manager a fee equal to 0.40% per annum of its NAV plus, in both cases, applicable taxes. For the year ended July 31, 2006, we paid the Manager a total (including GST) of \$266,324. The Manager is responsible for paying Jove's fees.

Past Performance

Period Returns

The following bar chart shows how the Preferred Shares performed during the period from Inception Date to July 31, 2005 and over the annual period ended July 31, 2006. It shows, in percentage terms, how much an investment made on the first day of the period would have grown or decreased by the last day of the period. The performance information assumes the reinvestment of all distributions in additional Preferred Shares and does not take into account sales, redemption, distribution or other optional charges that would have reduced returns. Past performance of our Preferred Shares does not necessarily indicate how they will perform in the future.

**Charterhouse Preferred Share Index Corporation
Period-by-Period Total Returns (Not Annualized)**



Annual Compound Returns

The table below shows the annual compound return for the Preferred Shares for the periods shown and ending on July 31, 2006. The annual compound return is also compared to the annual return of the BMO Nesbitt Burns 50 Total Return Index (the “BMO 50”).

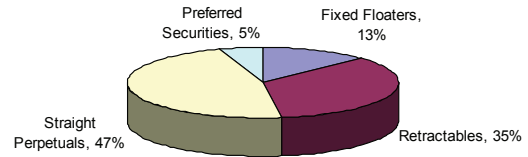
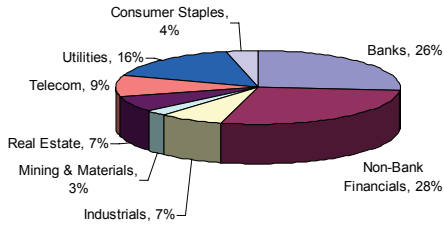
<i>Percentage Return</i>	<i>1 Year</i>	<i>Since Inception</i>
<i>Charterhouse Preferred Share Index</i>	<i>2.67%</i>	<i>2.68% ⁽¹⁾</i>
<i>BMO 50</i>	<i>3.08%</i>	

(1) Return since November 10, 2004

The BMO 50 is a market capitalization weighted index of 50 preferred shares issued by Canadian issuers with a minimum rating of pfd-3. The BMO 50 is constructed by BMO Nesbitt Burns Inc. to ensure broad diversification by issuer and to include the most actively traded issues. The return of the BMO 50 has been adjusted to include the effect of reinvested dividends. The BMO 50 is an unmanaged index with no management fees or operating costs and the underlying securities and structure of the BMO 50 and the Index Portfolio are not the same. Although it is a reasonable performance benchmark, the performance of the BMO 50 and the Index Portfolio will vary accordingly.

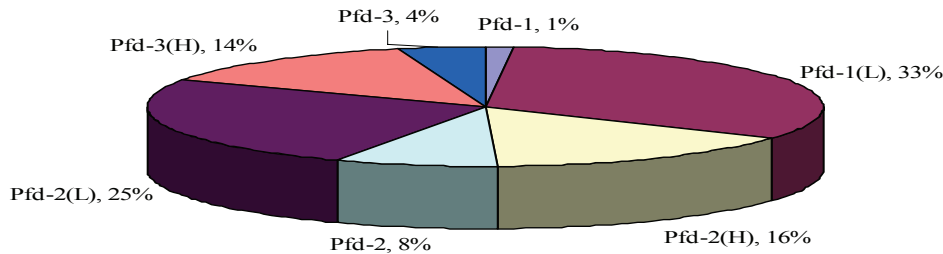
Summary of Investment Portfolio

As at July 31, 2006, our Portfolio was comprised of 87 classes or series of securities issued by 34 different issuers. As illustrated in the following charts, the Portfolio was broadly diversified both in terms of industry and security type:



In comparison to July 31, 2005, our exposure to non-bank financials (i.e. life insurance companies) and industrials increased by approximately 3% and 1%, respectively, whereas our exposure to banks fell by approximately 3%. Retractable accounted for 4% less of our Portfolio, offset by a 6% increase in straight perpetuals. This shift may increase our Portfolio's sensitivity to interest rates.

The weighted average DBRS rating of our Portfolio Securities was Pfd-2. Below is a breakdown of our portfolio by DBRS rating:



As at July 31, 2006, our Portfolio was valued at \$61.3 million and the top 25 issuers ranked by market value were:

Issuer	Type of Security	No. of Classes or Series of Securities	% Total Portfolio Value
Power Financial Corporation	Preferred shares	8	9.81%
Brookfield Properties Corp.	Preferred shares	6	8.39%
Canadian Imperial Bank of Commerce	Preferred shares	9	7.81%
Great-West Lifeco Inc.	Preferred shares	5	5.73%
Bank of Montreal	Preferred shares	4	5.40%
BCE Inc.	Preferred shares	4	5.12%
Power Corp. of Canada	Preferred shares	4	4.52%
Brookfield Asset Management Inc.	Preferred shares	3	4.20%
Bell Canada	Preferred shares	3	3.81%
George Weston Ltd.	Preferred shares	4	3.51%
Toronto-Dominion Bank	Preferred shares	3	2.96%
Laurentian Bank of Canada	Preferred shares	2	2.76%

Canadian Utilities Ltd.	Preferred shares	2	2.75%
Westcoast Energy Inc.	Preferred shares	2	2.74%
Royal Bank of Canada	Preferred shares	2	2.74%
Falconbridge Ltd	Preferred shares	2	2.70%
Nova Scotia Power Inc.	Preferred shares	2	2.62%
Brookfield Asset Management Inc.	Preferred securities	2	2.60%
Fortis Inc.	Preferred shares	2	2.56%
National Bank of Canada	Preferred shares	2	1.84%
Bank of Nova Scotia	Preferred shares	2	1.78%
Manulife Financial Corp.	Preferred shares	2	1.41%
E L Financial Corporation	Preferred shares	1	1.41%
Enbridge Inc.	Preferred shares	1	1.40%
EPCOR Preferred Equity Inc.	Preferred shares	<u>1</u>	<u>1.37%</u>
		78	90.57%

This composition of the investment portfolio will change due to ongoing portfolio transactions of the Company. Quarterly updates of the portfolio are available.

Management Responsibility for Financial Reporting

The accompanying financial statements have been prepared by management of the Company and approved by the Board of Directors of the Company. The Company is responsible for the information and representations contained in these financial statements and other sections of the Annual Report. The Company has put in place procedures and maintains processes all designed to ensure that relevant and reliable financial information is collected and reported. The financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Certain amounts reported in these statements are based on estimates and judgments. Note 2 to the financial statements describes the significant accounting policies followed by the Company in the preparation of its financial statements



Kevin Beatson
Chief Executive Officer



Jason Mackey
Chief Financial Officer

Toronto, Canada
October 18, 2006

October 18, 2006

PricewaterhouseCoopers LLP
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Auditors' Report

To the Shareholders of Charterhouse Preferred Share Index Corporation (the Fund)

We have audited the consolidated statement of investment portfolio of the Fund as at July 31, 2006, the consolidated statements of financial position of the Fund as at July 31, 2006 and 2005 and the consolidated statements of operations, changes in shareholder's equity and retained earnings and cash flows for the year ended July 31, 2006 and the period from November 10, 2004 (date of inception) to July 31, 2005. These financial statements are the responsibility of the Fund's manager. 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 plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Fund as at July 31, 2006 and 2005 and the results of its operations and its cash flows for the year ended July 31, 2006 and the period from November 10, 2004 (date of inception) to July 31, 2005 in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

Toronto, Ontario

PricewaterhouseCoopers refers to the Canadian firm of PricewaterhouseCoopers LLP and the other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

Consolidated Statement of Financial Position

As at July 31, 2006

	2006	2005
Assets		
Investments, at market value	\$ 61,343,676	\$ 65,340,666
Cash, term deposits and short-term debt instruments	214,460	55,736
Accrued interest and dividends	118,504	255,164
Prepaid expenses	19,691	14,769
Total assets	\$ 61,696,331	\$ 65,666,335
Liabilities		
Due to brokers	\$ -	\$ 105,000
Accounts payable and accrued expenses	100,370	70,600
Loans payable (Note 6)	8,548,490	9,053,433
Preferred shares (Note 3)	53,047,371	56,437,202
Total liabilities	61,696,231	65,666,235
Shareholder's equity		
Class A shares (Note 3)	100	100
Retained earnings	-	-
Total shareholder's equity	100	100
Liabilities and shareholder's equity	\$ 61,696,331	\$ 65,666,335
Preferred shares outstanding	2,320,900	2,424,500
Net Asset Value per preferred share (Note 2f)	\$ 22.86	\$ 23.28
Cost of investments held (including short-term investments)	62,843,634	66,002,925

Signed and approved on behalf of the Board of Directors of Charterhouse Preferred Share Index Corporation



Director



Director

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

Consolidated Statement of Operations

For the year ended July 31, 2006 and for the period from November 10, 2004 to July 31, 2005

	2006	For the period from November 10, 2004 (date of inception) to July 31, 2005
Investment income		
Interest	\$ 263,834	\$ 198,942
Dividends	\$3,103,577	2,083,506
	3,367,411	2,282,448
Expenses		
Management fees (Note 5)	266,324	198,903
Audit fees	37,450	32,100
Directors' fees	31,200	32,145
Custodial fees	72,225	55,948
Shareholder reporting costs	17,250	9,807
Other administrative expenses	129,148	66,134
Interest and bank charges	330,439	135,463
	884,036	530,500
Net investment income before distributions on preferred shares	2,483,375	1,751,948
Realized and unrealized gain on investments		
Net realized gain (loss) on investments	(185,463)	24,625
Net realized gain (loss) on foreign exchange	(2,451)	115
Unrealized loss on investments	(837,699)	(662,259)
Unrealized gain on foreign exchange	112	-
Increase in net assets from operations before distributions on preferred shares	\$ 1,457,874	\$ 1,114,429
Increase in net assets from operations per preferred share*	\$ 0.61	\$ 0.46

* Calculated by dividing the increase (decrease) in net assets from operations by the weighted average outstanding units during the period.

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

Consolidated Statement of Changes in Shareholder's Equity & Retained Earnings

For the year ended July 31, 2006 and for the period from November 10, 2004 to July 31, 2005

For the year ended July 31,	2006	For the period from November 10, 2004 (date of inception) to July 31, 2005
Changes in shareholder's equity		
Share capital - beginning of period	\$ 100	\$ -
Proceeds from issuance of Class A shares	-	100
Share capital - end of period	<u>\$ 100</u>	<u>\$ 100</u>
Changes in retained earnings:		
Retained earnings - beginning of period	\$ -	\$ -
Increase in net assets from operations before distributions on preferred shares	1,457,874	1,114,429
Distributions paid to preferred shareholders	(2,495,714)	(1,703,290)
Deficit attributable to preferred shares	<u>1,037,840</u>	<u>588,861</u>
Retained earnings - end of period	<u>\$ -</u>	<u>\$ -</u>

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

Consolidated Statement of Cash Flows

For the year ended July 31, 2006 and for the period from November 10, 2004 to July 31, 2005

	For the year ended July 31,2006	For the period from November 10, 2004 (date of inception) to July 31, 2005
Cash flows from operating activities:		
Operations:		
Increase in net assets from operations before distributions on preferred shares	\$ 1,457,874	\$ 1,114,429
Items not affecting cash/other:		
Net realized gain on investments	185,463	(24,625)
Net realized gain on foreign exchange	2,451	(115)
Unrealized loss on investments	837,699	662,259
Net investment income before distributions on preferred shares	2,483,487	1,751,948
Changes in non-cash working capital:		
Increase in accrued interest and dividends	136,660	(255,164)
Increase (decrease) in prepaid expenses	(4,922)	(14,769)
Increase (decrease) in due to brokers	(105,000)	105,000
Increase in accounts payable and accrued expenses	29,770	70,600
Net realized gain (loss) on foreign exchange	(2,451)	115
Cash provided by operating activities	2,537,544	1,657,730
Cash flows from investing activities:		
Purchase of portfolio assets (Note 7)	(7,441,381)	(56,450,908)
Proceeds of disposition of portfolio assets	10,415,209	3,890,533
Cash used in investing activities	2,973,828	(52,560,375)
Cash flows from financing activities:		
Proceeds from issuance of preferred shares and Class A shares (Note 3)	-	47,207,175
Compensation paid in respect of the issuance of preferred shares	-	(3,587,274)
Amounts paid for repurchase of preferred shares	(2,351,991)	(11,663)
Increase (decrease) in borrowings	(504,943)	9,053,433
Distributions paid to preferred shareholders	(2,495,714)	(1,703,290)
Cash provided by financing activities	(5,352,648)	50,958,381
Increase (decrease) in cash, term deposits and short-term debt instruments	158,724	55,736
Cash, term deposits and short-term debt instruments, beginning of period	55,736	-
Cash, term deposits and short-term debt instruments, end of period	214,460	55,736

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

Consolidated Statement of Investment Portfolio –

As At July 31, 2006

<u>No. of Shares</u>	<u>Issuer</u>	<u>Security Description</u>	<u>Cost (\$)</u>	<u>Market Value (\$)</u>	<u>% of Portfolio</u>
CANADIAN \$ PREFERRED SHARES					
32,650	Bank Of Montreal	4.75% Non-Cum. Class B Pref., Series 6	857,227	840,411	
31,000	Bank Of Montreal	5.30% Non-Cum. Class B Pref., Series 5	853,113	825,375	
33,400	Bank Of Montreal	4.80% Non-Cum. Class B Pref., Series 4	872,318	860,050	
11,100	Bank Of Nova Scotia	4.80% Non-Cum. Pref., Series 13	283,702	279,498	
31,100	Bank Of Nova Scotia	5.25% Non-Cum. Pref., Series 12	851,466	813,887	
28,200	BCE Inc.	6.174% Cum. Redeem. First Pref., Series R	736,451	713,460	
31,950	BCE Inc.	5.54% Cum. Redeem. First Pref., Series AC	858,906	816,323	
32,020	BCE Inc.	5.45% Cum. Redeem. First Pref., Series AA	858,912	808,505	
31,900	BCE Inc.	5.319% Cum. Redeem. First Pref., Series Z	859,408	805,475	
32,800	Bell Canada	5.25% Cum. Redeem. Class A Pref., Series 17	859,408	823,280	
28,100	Bell Canada	4.40% Cum. Redeem. Class A Pref., Series 16	856,024	702,500	
32,350	Bell Canada	5.55% Cum. Redeem. Class A Pref., Series 19	730,189	808,750	
30,280	Brookfield Asset Management Inc.	5.75% Cum. Class A Pref., Series 10	856,911	824,827	
33,400	Brookfield Asset Management Inc.	5.40% Cum. Class A Pref., Series 12	884,983	911,820	
31,296	Brookfield Asset Management Inc	5.50% Non-Cum. Class A Pref., Series 11	859,064	837,481	
31,900	Brookfield Properties Corp.	6.00% Redeem. Cum. Class AAA, Pref., Series F	860,719	868,956	
33,200	Brookfield Properties Corp.	5.75% Redeem. Cum. Class AAA, Pref., Series H	857,349	880,464	
34,200	Brookfield Properties Corp.	5.20% Redeem. Cum. Class AAA, Pref., Series K	856,602	875,520	
34,800	Brookfield Properties Corp.	5.00% Redeem. Cum. Class AAA, Pref., Series J	861,154	881,832	
33,000	Brookfield Properties Corp.	5.20% Redeem. Cum. Class AAA, Pref., Series I	860,577	860,970	
30,300	Canada Life Financial Corp.	6.25% Non-Cum. Pref., Series B	859,878	800,829	
9,300	Canadian Imperial Bank of Commerce	4.80% Non-Cum. Class A Pref., Series 30	231,168	231,105	
21,400	Canadian Imperial Bank of Commerce	5.40% Non-Cum. Class A Pref., Series 29	577,800	560,894	
22,200	Canadian Imperial Bank of Commerce	5.60% Non-Cum. Class A Pref., Series 27	599,515	591,408	
22,000	Canadian Imperial Bank of Commerce	5.75% Non-Cum. Class A Pref., Series 26	593,780	585,640	
21,700	Canadian Imperial Bank of Commerce	6.00% Non-Cum. Class A Pref., Series 25	590,576	583,079	
21,300	Canadian Imperial Bank of Commerce	6.00% Non-Cum. Class A Pref., Series 24	580,961	563,811	
21,000	Canadian Imperial Bank of Commerce	5.30% Non-Cum. Class A Pref., Series 23	591,876	559,965	
20,910	Canadian Imperial Bank of Commerce	4.95% Non-Cum. Class A Pref., Series 19	579,705	549,097	
21,600	Canadian Imperial Bank of Commerce	5.50% Non-Cum. Class A Pref., Series 18	578,664	566,136	
31,000	Canadian Utilities Ltd.	6.00% Cum. Redeem. Second Pref., Series X	858,231	837,000	
31,300	Canadian Utilities Ltd.	5.80% Cum. Redeem. Second Pref., Series W	858,022	848,074	
33,200	E-L Financial Corporation	5.30% Non-Cum. Redeem. Pref., Series 1	858,173	863,200	
33,100	Enbridge Inc.	5.50% Cum. Redeem. Pref., Series A	858,197	858,283	
32,380	EPCOR Preferred Equity Inc.	5.50% Cum. Redeem. First Pref., Series I	859,729	840,261	
33,100	Falconbridge Ltd.(1)	6.10% Cum. Pref., Series G	856,119	827,500	
31,900	Falconbridge Ltd.	6.50% Cum. Pref., Series H	859,774	828,443	
30,840	Fortis Inc.	5.45% Cum. Redeem. First Pref., Series C	858,499	846,250	
26,600	Fortis Inc.	4.90% Cum. Redeem. First Pref., Series E	705,064	721,392	
30,980	Great-West Life Assurance Co.	5.55% Non-Cum. Pref., Series O	860,416	839,558	
31,940	Great-West Lifeco Inc.	4.70% Non-Cum. First Pref., Series D	860,001	838,106	
27,525	Great-West Lifeco Inc.	4.80% Non-Cum. First Pref., Series E	758,204	739,872	
31,600	Great-West Lifeco Inc.	5.90% Non-Cum. First Pref., Series F	858,714	857,940	
33,650	Great-West Lifeco Inc.	5.20% Non-Cum. First Pref., Series G	859,453	873,554	
8,100	Great-West Lifeco Inc.	4.85% Non-Cum. First Pref., Series H	200,556	202,500	
8,200	HSBC Bank Canada	5.10% Non-Cum. Redeem Class 1, Series C	211,540	212,954	
8,600	HSBC Bank Canada	5.00% Non-Cum. Class 1, Series D	215,000	223,686	

Charterhouse Preferred Share Index Corporation

<u>No. of Shares</u>	<u>Issuer</u>	<u>Security Description</u>	<u>Cost (\$)</u>	<u>Market Value (\$)</u>	<u>% of Portfolio</u>
30,243	IGM Financial Inc.	5.75% Non-Cum. First Pref., Series A	860,902	837,731	
33,800	Laurentian Bank of Canada	5.25% Non-Cum. Class A Pref., Series 10	855,987	872,378	
31,800	Laurentian Bank of Canada	6.00% Non-Cum. Class A Pref., Series 9	859,318	822,666	
25,100	Manulife Financial Corp.	4.10% Non-Cum. Class A Pref., Series 1	658,600	650,341	
8,800	Manulife Financial Corp.	4.65% Non-Cum. Class A Pref., Series 2	214,918	216,480	
11,200	National Bank of Canada	4.85% Non-Cum. First Pref., Series 16	283,974	282,240	
31,700	National Bank of Canada	5.85% Non-Cum. First Pref., Series 15	853,585	847,024	
30,400	Nova Scotia Power Inc.	4.90% Cum. First Pref., Series C	834,958	830,832	
27,700	Nova Scotia Power Inc.	5.90% Cum. First Pref., Series D	859,330	775,600	
32,600	Power Corp. of Canada	5.35% Non-Cum. First Pref., Series B	854,524	835,049	
32,440	Power Corp. of Canada	5.80% Non-Cum. First Pref., Series C	876,372	854,145	
10,000	Power Corp. of Canada	5.00% Non-Cum. First Pref., Series D	250,000	257,400	
32,600	Power Corp. of Canada	5.60% Non-Cum. First Pref., Series A	859,188	829,018	
30,400	Power Financial Corp.	5.20% Non-Cum. First Pref., Series C	859,046	827,032	
32,000	Power Financial Corp.	5.50% Non-Cum. First Pref., Series D	858,220	861,760	
31,500	Power Financial Corp.	6.00% Non-Cum. First Pref., Series I	859,826	841,208	
26,940	Power Financial Corp.	4.70% Non-Cum. First Pref., Series J	718,934	707,175	
10,000	Power Financial Corp.	4.95% Non-Cum. First Pref., Series K	249,000	249,600	
31,700	Power Financial Corp.	5.75% Non-Cum. First Pref., Series H	852,076	837,831	
32,100	Power Financial Corp.	5.90% Non-Cum. First Pref., Series F	873,008	846,798	
32,900	Power Financial Corp.	5.25% Non-Cum. First Pref., Series E	857,308	845,859	
34,100	Royal Bank of Canada	4.90% Non-Cum. First Pref., Series W	855,169	869,209	
31,000	Royal Bank of Canada (2)	6.10% Non-Cum. First Pref., Series S	859,614	811,270	
8,200	Sun Life Financial Inc.	4.75% Non-Cum. Class A, Series 1	203,340	204,180	
8,600	Sun Life Financial Inc.	4.80% Non-Cum. Class A, Series 2	213,474	215,000	
12,000	Toronto-Dominion Bank	4.85% Class A First Pref., Series O	300,000	302,400	
27,800	Toronto-Dominion Bank	4.60% Non-Cum. Redeem. Class A First Pref., Series N	756,481	750,878	
27,800	Toronto-Dominion Bank	4.70% Non-Cum. Redeem. Class A First Pref., Series M	759,439	763,110	
33,200	Westcoast Energy Inc.	5.60% Cum. Redeem. First Pref., Series 8	865,886	838,300	
33,000	Westcoast Energy Inc.	5.50% Cum. Redeem. First Pref., Series 7	860,300	845,130	
11,100	George Weston Ltd.	5.20% Cum. Pref., Series IV	281,609	280,275	
9,100	George Weston Ltd.	5.20% Cum. Pref., Series III	232,007	231,595	
31,360	George Weston Ltd.	5.15% Cum. Redeem. Pref., Series II	855,412	815,360	
31,900	George Weston Ltd.	5.80% Cum. Pref., Series I	864,064	828,762	
SUBTOTAL			57,709,503	56,573,555	92.2%
US \$ PREFERRED SHARES					
26,150	Bank of Montreal	5.95% Non-Cum. Class B, Series 10	854,934	785,791	
27,500	Brookfield Properties Corp.	5.25% Class AAA Series G	853,990	779,084	
SUBTOTAL			1,708,923	1,564,874	2.6%
PREFERRED SECURITIES					
30,900	Brookfield Asset Management Inc.	8.30% Preferred Securities, due Jun. 30, 2051	856,746	801,855	
31,000	Brookfield Asset Management Inc.	8.35% Preferred Securities, due Dec. 31, 2050	856,248	794,840	
30,900	Enbridge Inc.	7.80% Preferred Securities, due Mar. 31, 2051	854,013	793,512	
32,000	TransAlta Corp.	7.75% Preferred Securities, due Dec. 31, 2050	858,200	815,040	
SUBTOTAL			3,425,208	3,205,247	5.2%
PORTFOLIO TOTAL			62,843,634	61,343,676	100%

Note

- (1) These securities will be redeemed on November 1, 2006, with proceeds to be reinvested in other eligible securities
- (2) These securities will be redeemed on October 6, 2006, with proceeds to be reinvested in other eligible securities.

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

Notes to Consolidated Annual Financial Statements

For the year ended July 31, 2006 and for the period from November 10, 2004 to July 31, 2005

1. OPERATIONS

Charterhouse Preferred Share Index Corporation (the “Company”) was incorporated pursuant to the *Business Corporations Act* (Ontario) on September 22, 2004. These consolidated financial statements incorporate the results of the Company’s wholly-owned subsidiary, Charterhouse PSI Investment Corporation (“IndexCo”). The Company holds all of IndexCo’s outstanding Class A shares and preferred shares (“IndexCo Preferred Shares”).

Charterhouse PSI Management Corporation (the “Manager”) is responsible for managing the affairs of the Company and IndexCo. Jove Investment Management Inc. (formerly Felcom Management Corp.) has been retained by the Manager to acquire and maintain the investment portfolio (the “Index Portfolio”).

The Company and IndexCo effectively commenced operations on November 10, 2004 when the Company issued 2,425,000 preferred shares at \$25.00 per share through an initial public offering and in turn, the Company acquired preferred shares issued by IndexCo. The Company’s preferred shares are listed on the Toronto Stock Exchange.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles and they include estimates and assumptions made by management that affect the reported amounts of assets and liabilities at the date of these financial statements and the reported amounts of income and expenses during the period. Actual results could differ from these estimates.

The following is a summary of significant accounting policies followed by the Company in the preparation of its financial statements:

(a) Valuation of investments

The Company’s investments are presented at market value. Investments in publicly traded securities are valued at their closing prices. If a closing price is not available, then that investment is valued at the latest available sale price, or lacking any recent sales or any record thereof, the value will be calculated as the simple average of the latest available offer price and the latest available bid price. The difference between market value and average cost, as recorded in the accounts, is shown as unrealized gain (loss) of the investment portfolio. Short-term investments are valued at cost which, when taken together with accrued interest income thereon, approximates their market value.

(b) Investment transactions and income recognition

Investment transactions are recorded on trade date. Realized gains or losses from investment transactions and unrealized gains or losses in the value of investments are calculated on an average cost basis. Interest income and expenses are recognized daily on an accrual basis. Dividend income is recognized on the ex-dividend date. Net realized gains or losses on investments include net realized gains or losses from foreign currency changes.

(c) Foreign currency translation

The market value of investments and other assets and liabilities that are denominated in foreign currencies are translated into Canadian dollars at the rate of exchange applicable on the valuation date. Investment transactions and income derived from investments are translated at the rate of exchange on the date of such transactions.

(d) Fair value of financial instruments

The fair value of the Company’s financial instruments, which are composed of cash, term deposits and short-term debt instruments, accrued interest and dividends, accounts payable and accrued expenses approximates their carrying value.

(e) Income taxes

The Company is a “mutual fund corporation” as defined in the Income Tax Act (Canada) (the “Tax Act”). As a mutual fund corporation, the Company is entitled, in certain circumstances, to a refund of tax paid by it in respect of its net realized capital gains.

Charterhouse Preferred Share Index Corporation

IndexCo will be required to include any dividends received on the securities comprising the Index Portfolio (“Index Portfolio Securities”) in computing its income, and will be entitled to deduct such dividends in computing its taxable income. In computing its income, IndexCo will also include net taxable capital gains realized on dispositions of Index Portfolio Securities and interest received or accrued on the Index Portfolio Securities.

Having regard to expected income, gains and deductions, neither the Company nor IndexCo expects to be subject to any appreciable amount of non-refundable income tax. Accordingly, no income tax provision has been recorded.

The Company follows the liability method of measuring income taxes based on temporary differences. Future income taxes arise from differences in the timing of recognition of certain items of income and expenses for financial statement and tax purposes including share issuance costs and tax loss carry-forwards. Management does not believe that it is more likely than not that the benefit of the future tax asset will be realized. Therefore, no future tax asset has been recorded on the financial statements.

(f) Net Asset Value per Preferred Share

Net Asset Value per Preferred Share is calculated by dividing the value attributable to preferred shares by the total number of preferred shares outstanding on the valuation date. The value attributable to preferred shares is defined as the aggregate value of the assets of the Company, less the aggregate value of the liabilities of the Company excluding the preferred shares, less the redemption value of the Class A shares then outstanding.

(g) Increase in net assets from operations per preferred share

Increase in net assets from operations per preferred share is calculated by dividing increase in net assets from operations before distributions on preferred shares by the weighted average number of preferred shares outstanding during the period. The weighted average number of preferred shares outstanding for the year ended July 31, 2006 was 2,384,695 (2005: 2,425,000).

3. SHARE CAPITAL

Class A Shares

The Company is authorized to issue an unlimited number of Class A shares. The Company issued 100 Class A shares to a trust for cash consideration of \$100. As of July 31, 2006, 100 Class A shares are outstanding.

The Class A shares rank subsequent to the preferred shares with respect to the payment of dividends, distributions upon a redemption, retraction or otherwise and distributions upon a dissolution, liquidation or winding-up of the Company. Holders of the Class A shares are entitled to one vote per share.

At any time when there are any preferred shares issued and outstanding, holders of Class A shares are not entitled to receive any dividends but are entitled to \$1.00 per share on the dissolution, liquidation or winding-up of the Company. During such time, the Class A shares are retractable and redeemable at a price of \$1.00 per share.

Preferred Shares

The Company is authorized to issue an unlimited number of preferred shares. For accounting purposes, the preferred shares have been presented as liabilities in these financial statements in accordance with Section 3860 of the CICA Handbook.

Issued	Number of shares	Amount
Preferred shares - beginning of period	2,424,500	\$56,437,202
Purchased for cancellation	(103,600)	(2,351,991)
Deficit attributable to preferred shares	-	(1,037,840)
Preferred shares - end of period	2,320,900	53,047,371

Charterhouse Preferred Share Index Corporation

On November 10, 2004, the Company completed its initial public offering of 2,425,000 preferred shares at a price of \$25.00 per share, including 536,717 preferred shares issued pursuant to an exchange offer. The amount of agents' fees and issuance costs paid totalled \$3,587,274, resulting in net proceeds to the Company, including the securities acquired through the exchange offer, of \$57,037,726.

During the year ended July 31, 2006, 27,600 (2005: nil) preferred shares were retracted at an average price of \$22.98. An additional 76,000 (2005: 500) were purchased for cancellation under the Company's normal course issuer bid program at an average price of \$22.60.

The Company received approval from the Toronto Stock Exchange to renew its normal course issuer bid program for the period from January 16, 2006 to January 15, 2007. Pursuant to the issuer bid, the Company may purchase up to 237,600 of its preferred shares for cancellation when the Net Asset Value per Preferred Share exceeds its trading price.

The preferred shares rank in priority to the Class A shares with respect to the payment of dividends, distributions upon a redemption, retraction or otherwise and distributions upon a dissolution, liquidation, or winding up of the Company. Except under certain limited circumstances related to fundamental changes to the Company and as required by law, holders of preferred shares are not entitled to receive notice of, to attend or to vote at any meeting of shareholders of the Company.

The preferred shares will be redeemed by the Company on July 31, 2014. The redemption price will be the net amount realized on the disposition of the portfolio securities held by IndexCo (the "Index Portfolio Securities") plus (minus) any other assets (liabilities) of both IndexCo and the Company.

Preferred shares may be surrendered between October 15 and November 15 in any year for retraction on the last business day of November in that year for a retraction price equal to the net amount realized on the disposition of the *pro rata* share of the Index Portfolio Securities plus (minus) the *pro rata* share of any other assets (liabilities) of both IndexCo and the Company represented by the retracted preferred shares. Preferred shares surrendered at any other time will be retracted on the last business day of the relevant month at a price based upon the market value of the preferred shares as of that date.

4. DISTRIBUTIONS TO PREFERRED SHAREHOLDERS

The Company intends to pay quarterly distributions, to the extent that cash dividends received by the Company on the IndexCo Preferred Shares and other income received by the Company in such quarter exceed estimated expenses and any taxes payable by the Company. The policy of the Company is to pay quarterly distributions on the last day of January, April, July and October in each year.

For the year ended July 31, 2006, the Company declared and paid return of capital distributions of \$1.05 (2005: \$0.7025) per preferred share.

5. MANAGEMENT FEES

Pursuant to a management agreement, the Manager provides management and administrative services to the Company and IndexCo, for which it is paid a management fee equal to 0.05% per annum of the net asset value of the Company and 0.40% per annum of the net asset value of IndexCo plus, in both cases, applicable taxes. Management fees are calculated weekly and payable monthly in arrears. The Manager is responsible for paying fees to Jove Investment Management Inc., the Index Administrator. Both the Manager and Jove are indirect wholly-owned subsidiaries of Jovian Capital Corporation.

6. LOANS PAYABLE

Pursuant to an agreement with a Canadian chartered bank, IndexCo has a 364-day renewable revolving credit facility that provides for maximum borrowings of \$10.0 million at either the prime rate of interest or the bankers' acceptance rate plus a fixed percentage stamping fee. The credit facility is secured by a first priority security interest over all of IndexCo's assets.

Charterhouse Preferred Share Index Corporation

The credit facility is used by IndexCo (i) to provide leverage in order to increase the quarterly dividends on the IndexCo Preferred Shares; (ii) to acquire Index Portfolio Securities between rebalancings of the Index Portfolio; and (iii) for working capital purposes. Borrowings are limited to 15% of the aggregate value of IndexCo's assets.

At July 31, 2006, total borrowings aggregated \$8,548,490 (2005: \$9,053,433). The borrowings consisted of four bankers' acceptances at a weighted average rate of 4.42% (2005: 2.67%).

During the year ended July 31, 2006, the Company's minimum and maximum borrowings were \$8.21 million (2005: \$ Nil) and \$ 8.67 million (2005: \$9,053,433), respectively.

7. INVESTMENT TRANSACTIONS

Investment transactions for year ended July 31, 2006 and for the period from November 10, 2004 to July 31, 2005 were as follows:

	2006	2005
Proceeds from sale of investments	\$ 10,415,209	\$ 3,890,533
Less cost of investments sold:		
Investments at cost – beginning of period	66,002,925	-
Investments purchased during the period – cash	7,441,381	56,450,908
Investments purchased during the period – exchange offer	-	13,417,925
Investments at cost – end of period	(62,843,634)	(66,002,925)
Cost of investments sold during the period	10,600,672	3,865,908
Net realized gain (loss) on sale of investments	\$ (185,463)	\$ 24,625

Total commissions paid to dealers for portfolio transactions during the year totalled \$4,320 (2005 - \$73,037)

8. TAX LOSSES

Capital losses realized over and above realized capital gains in the current taxation year can be carried forward indefinitely and may be applied against future years' taxable capital gains. Non-capital losses may be carried forward for a period of ten years and applied against future years' taxable income. If the non-capital losses are not applied within ten years from the taxation year in which the non-capital loss was realized, the non-capital loss will expire.

As at July 31, 2006, the Company's capital and non-capital losses, with the year of expiry, are:

Capital Losses	Non-Capital Losses	Year of Expiry
\$900	\$77,158	2015

Corporate Information

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Director & Chief Executive Officer

Jason Mackey

Director & Chief Financial Officer

Robert Marcus⁽¹⁾

Director & Chairman of the Board

Harvey Naglie⁽¹⁾

Director & Chairman, Audit Committee

Peter Rizakos

Director

(1) Audit Committee Member

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The Toronto Stock Exchange

Ticker Symbol

PFD.PR.A

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