



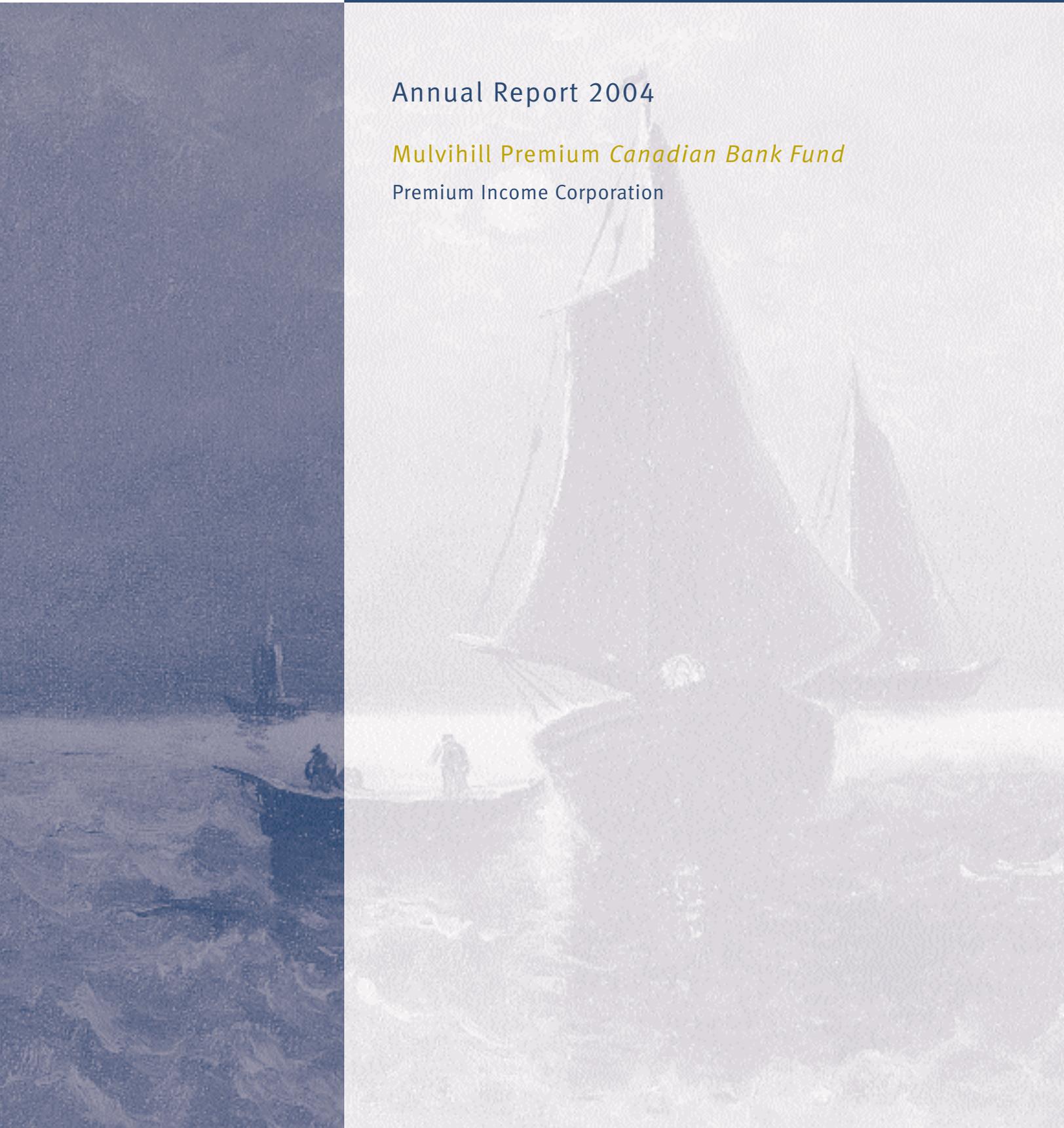
## Hybrid Income Funds



Annual Report 2004

*Mulvihill Premium Canadian Bank Fund*

Premium Income Corporation





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Message to Shareholders

We are pleased to present the Fund's financial statements for the fiscal year ended October 31, 2004.

During the year, the financial sector continued its strong performance. This positive environment contributed to another solid year of distributions and net asset value growth for the Fund.

Preferred shareholders received \$0.889263 per share in total distributions during the 12-month period, exceeding the target level of \$0.8625 per annum. Class A shareholders received \$1.20 per share, comprised of \$0.80 in regular quarterly distributions and \$0.40 in special distributions beyond the target level. The underlying net asset value of the Fund's Class A shares rose from \$10.55 on October 31, 2003, to \$10.96 on October 31, 2004.

A final prospectus for a follow-on treasury offering of Preferred and Class A shares closed on September 30, 2004. It offered 6,487,846 Preferred shares at \$15.65 each, and 6,487,846 Class A shares at \$11.23 each, for a total offering amount of \$174,393,301.

We would like to take this opportunity to thank all shareholders for their continuing support.



John P. Mulvihill  
Chairman & President  
Mulvihill Capital Management Inc.

## Investment Objectives

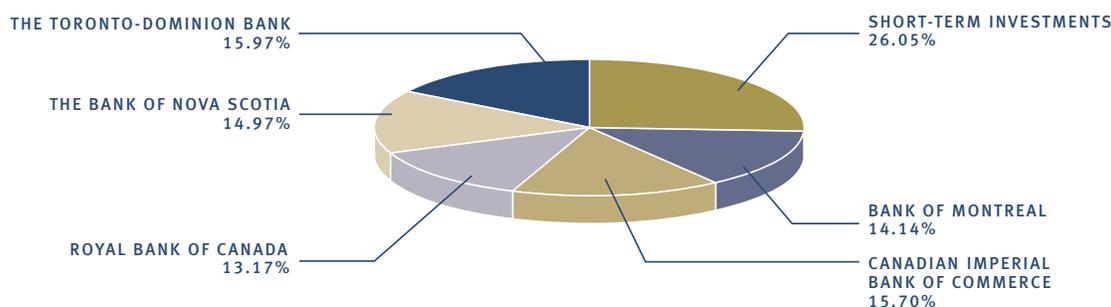
The Fund's investment objectives are (i) to provide Preferred shareholders with cumulative preferential quarterly cash dividends of \$0.22 per quarter; (ii) to provide Class A shareholders with all excess realized income of the Fund at each fiscal year end; and (iii) to return, at a minimum, the original issue prices to holders of both Preferred shares and Class A shares upon windup on November 1, 2010. The Fund has a dividend policy on the Class A shares of \$0.20 per quarter.

## Investment Strategy

The Fund achieves its investment objectives by investing its net assets in a portfolio consisting of short-term investments and common shares issued by Bank of Montreal, The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Royal Bank of Canada and The Toronto-Dominion Bank. To generate additional returns above the dividend income generated by the portfolio, the Fund writes covered call options in respect of all or part of the securities in the Portfolio. By nature of the covered option writing strategy employed by the Fund, the average portfolio turnover rate will tend to be relatively high due to the exercise of options. From time to time, the Fund may hold a portion of its assets in cash equivalents, which may be utilized to provide cover in respect of the writing of cash covered put positions.

## Asset Mix

October 31, 2004



## Distribution History

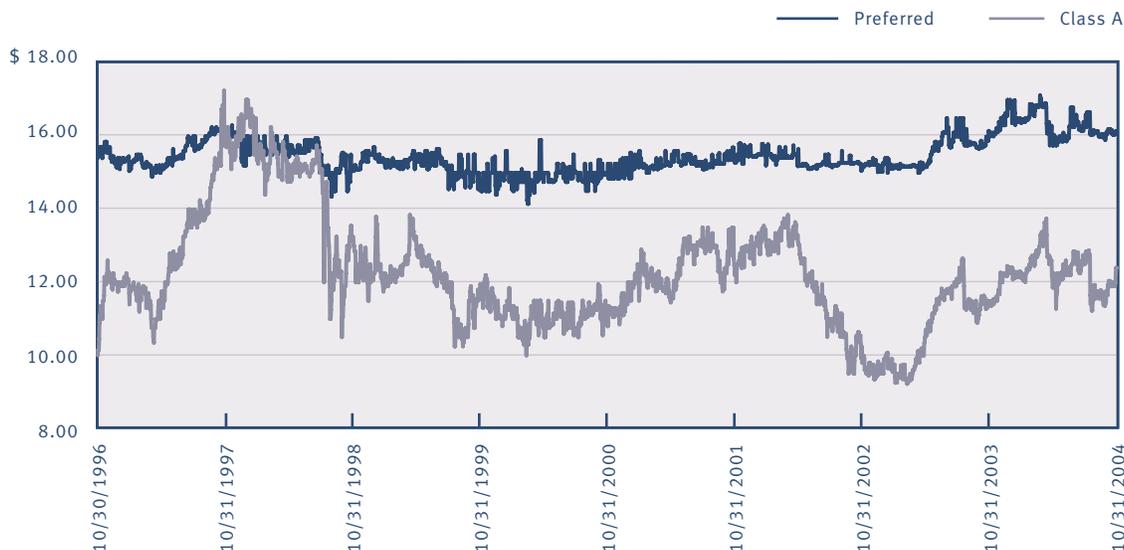
INCEPTION DATE: OCTOBER 1996	CLASS A REGULAR DISTRIBUTION	CLASS A SPECIAL DISTRIBUTION	TOTAL CLASS A DISTRIBUTION	REGULAR PREFERRED DISTRIBUTION
Total for 1997	\$ 0.80	\$ 1.90	\$ 2.70	\$ 0.877800
Total for 1998	0.80	0.50	1.30	0.884300
Total for 1999	0.80	0.40	1.20	0.888610
Total for 2000	0.80	0.60	1.40	0.880033
Total for 2001	0.80	1.35	2.15	0.884226
Total for 2002	0.80	0.60	1.40	0.884170
Total for 2003	0.80	0.40	1.20	0.892795
January 2004	0.20	0.10	0.30	0.222464
April 2004	0.20	0.10	0.30	0.225405
July 2004	0.20	0.10	0.30	0.218493
October 2004	0.20	0.10	0.30	0.222901
Total for 2004	0.80	0.40	1.20	0.889263
<b>Total Distributions to Date</b>	<b>\$ 6.40</b>	<b>\$ 6.15</b>	<b>\$ 12.55</b>	<b>\$ 7.081197</b>

**Eligible Holdings:**

- Bank of Montreal
- Canadian Imperial Bank of Commerce
- Royal Bank of Canada
- The Bank of Nova Scotia
- The Toronto-Dominion Bank

**Trading History**

October 30, 1996 to October 31, 2004



**Commentary**

The TSX Diversified Banks Index rose 16.9 percent during the fiscal year outperforming the S&P/TSX Composite Index, which was up 16.1 percent. Only the energy sector, buoyed by rising oil and gas prices, showed greater strength.

All the Big Five banks earned positive returns, with the Canadian Imperial Bank of Commerce and The Bank of Nova Scotia achieving the largest gains. Continuing credit improvement allowed the banks to reduce loan loss provisions and in some cases release prior reserves due to loss recoveries. Fundamentals remain strong throughout the sector, with high returns on equity, abundant capital positions, stable retail earnings growth, high dividends and improving capital markets.

The Bank of Canada cut interest rates by 75 basis points early in the year, but as the economy recovered its momentum, the Bank reversed its course with 25-point increases in September and October. The rising rate environment now in place will allow some improvements in retail margins, as rates for loans and mortgages are adjusted upward faster than rates paid for deposits. The rising value of the Canadian dollar will have some negative impact on banks with higher-than-average exposure to foreign earnings.

The outlook for the new fiscal year is positive as earnings growth is expected to remain strong. This growth will support the high dividend yields and share buybacks that in turn increase investor enthusiasm for the financial services sector.

The following table presents the financial highlights of the Fund for the most recent five-year period.

### Financial Highlights

Years ended October 31

Unaudited

	2004	2003	2002	2001	2000
DATA PER CLASS A SHARE					
Net Asset Value, Beginning of Year	\$ 10.55	\$ 8.38	\$ 10.26	\$ 12.35	\$ 8.77
INCOME (LOSS) FROM INVESTMENT OPERATIONS					
Net investment income (loss)	(0.47)	(1.05)	(0.47)	(0.25)	(0.21)
Net gain (loss) on investments and options	2.08	4.42	(0.01)	0.31	5.19
<b>Total from Investment Operations</b>	<b>1.61</b>	<b>3.37</b>	<b>(0.48)</b>	<b>0.06</b>	<b>4.98</b>
DISTRIBUTION TO CLASS A SHAREHOLDERS					
From net realized gain on sale of investments and options	(1.20)	(1.14)	(1.40)	(2.15)	(1.40)
From taxable income	–	(0.06)	–	–	–
<b>Total Distribution</b>	<b>(1.20)</b>	<b>(1.20)</b>	<b>(1.40)</b>	<b>(2.15)</b>	<b>(1.40)</b>
<b>Net Asset Value, End of Year</b>	<b>\$ 10.96</b>	<b>\$ 10.55</b>	<b>\$ 8.38</b>	<b>\$ 10.26</b>	<b>\$ 12.35</b>
RATIOS/SUPPLEMENTAL DATA					
Total net assets, end of year (\$millions)	\$ 207.8	\$ 132.2	\$ 33.3	\$ 40.8	\$ 49.1
Total net assets excluding liability for Redeemable Preferred shares and unamortized premium on issue of Preferred shares, end of year (\$millions)	\$ 496.6	\$ 322.9	\$ 93.0	\$ 100.5	\$ 108.8
Average net assets (\$millions)	\$ 140.3	\$ 47.3	\$ 44.6	\$ 49.2	\$ 40.4
Management expense ratio	1.20%	2.62% *	1.20%	1.23%	1.17%
Portfolio turnover rate	157%	150%	63%	75%	98%
Annual rate of return on Class A shares	15.2%	40.2%	(4.7)%	0.5%	56.8%
Annual yield on Preferred shares	5.9%	6.0%	5.9%	5.9%	5.9%
DISTRIBUTION TO PREFERRED SHAREHOLDERS					
From net realized gain on sale of investments and options	\$ 0.41	\$ 0.30	\$ 0.34	\$ 0.34	\$ 0.37
From taxable income	0.48	0.59	0.54	0.54	0.51
<b>Total Distribution</b>	<b>\$ 0.89</b>	<b>\$ 0.89</b>	<b>\$ 0.88</b>	<b>\$ 0.88</b>	<b>\$ 0.88</b>

\* Management expense ratio for 2003 includes the special resolution expense. The management expense ratio excluding the special resolution expense is 1.17%.

The net asset value per Class A share is the net asset value per unit less the lessor of (i) \$15.00, or (ii) the net asset value per unit.

Net asset value per unit is calculated as (i) the aggregate value of the assets of the Fund, less (ii) the aggregate value of the liabilities of the Fund including any distributions declared and not paid that are payable to shareholders on or before such date and excluding any unamortized premium on issue of Preferred shares, less (iii) the stated capital of the Class B shares of \$1,000, divided by the number of units outstanding.

Net investment income (loss) per Class A share consists of interest and dividend revenue less expenses, including Preferred share distributions, and is calculated based on the weighted average number of Class A shares outstanding during the year.

Net gain (loss) on investments and options per Class A share includes the impact of timing of shareholder transactions.

Distributions to Class A shareholders are based on the number of Class A shares outstanding on the record date for each distribution.

Management expense ratio is the ratio of all fees and expenses, including GST and capital taxes but excluding income taxes and Preferred share distributions, charged to the Fund to average net assets, excluding the liability for the Redeemable Preferred shares and unamortized premium on issue of Preferred shares.

Portfolio turnover rate is calculated based on the lesser of purchases or sales of investments, excluding short-term investments, divided by the average value of portfolio securities during the year. Portfolio turnover rates for 2004 and 2003 are higher than previous years due to follow-on treasury offerings completed in each of these years. The portfolio turnover rate for 2003 has been restated to exclude short-term bonds.

Annual rate of return represents the historical annual total rate of return of an investment in a Class A share for the year, assuming reinvestment of current year distributions. Annual yield on Preferred shares represents the cumulative preferential quarterly cash distributions (See Note 6).

## Management's Responsibility for Financial Reporting

This report has been prepared in accordance with the Accounting Standards Board guidelines.

The accompanying financial statements of Premium Income Corporation (operating as Mulvihill Premium Canadian Bank Fund) (the "Fund") and all the information in this annual report are the responsibility of the management of Mulvihill Capital Management Inc., (the "Manager"), and have been approved by the Board of Directors (the "Board").

The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and include certain amounts that are based on estimates and judgments. Management has ensured that the other financial information presented in this annual report is consistent with the financial statements. The significant accounting policies which management believes are appropriate for the Fund are described in Note 2 of the financial statements.

The Manager is also responsible for maintaining a system of internal controls designed to provide reasonable assurance that assets are safeguarded and that accounting systems provide timely, accurate and reliable financial information.

The Audit Committee meets periodically with management and the external auditors to discuss internal controls, the financial reporting process, various auditing and financial reporting issues, and to review the annual report, the financial statements and the external auditors' report. Deloitte & Touche LLP has full and unrestricted access to the Audit Committee and the Board.



John P. Mulvihill  
Chairman & President  
Mulvihill Capital Management Inc.  
November 24, 2004



Sheila S. Szela  
CFO  
Mulvihill Capital Management Inc.

## To the Shareholders

We have audited the accompanying statement of investments of Premium Income Corporation (operating as Mulvihill Premium Canadian Bank Fund) (the "Fund") as at October 31, 2004, the statements of financial position as at October 31, 2004 and 2003, the statements of operations and retained earnings (deficit), of changes in net assets and of changes in investments and options for the years then ended. 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 financial statements present fairly, in all material respects, the financial position of the Fund and its investments as at the dates indicated above, and the results of its operations, the changes in its net assets, and the changes in its investments and options for the periods indicated above, in accordance with Canadian generally accepted accounting principles.

*Deloitte + Touche LLP*

Chartered Accountants  
Toronto, Ontario  
November 24, 2004

Statements of Financial Position

October 31, 2004 and 2003

	2004	2003
<b>ASSETS</b>		
Investments at market value (average cost - \$343,667,174; 2003 - \$197,339,936)	\$ 364,035,243	\$ 206,226,648
Short-term investments (average cost - \$129,431,429; 2003 - \$119,640,605)	129,405,435	119,554,586
Cash	451,898	33,923
Interest, dividends and other receivables	3,446,713	2,647,705
Due from brokers	-	4,747,200
<b>TOTAL ASSETS</b>	<b>\$ 497,339,289</b>	<b>\$ 333,210,062</b>
<b>LIABILITIES</b>		
Accrued liabilities	\$ 444,360	\$ 302,151
Share issue expenses payable	297,102	555,005
Due to brokers	-	9,404,480
Redemptions payable	-	22,995
	<b>741,462</b>	<b>10,284,631</b>
Redeemable preferred shares (Note 3)	286,893,690	189,576,000
Unamortized premium on issue of preferred shares (Note 3)	1,914,855	1,174,152
	<b>289,550,007</b>	<b>201,034,783</b>
<b>EQUITY</b>		
Class A and Class B shares (Note 3)	194,073,151	125,289,712
Retained earnings	13,716,131	6,885,567
	<b>207,789,282</b>	<b>132,175,279</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$ 497,339,289</b>	<b>\$ 333,210,062</b>
<b>Number of Units Outstanding (Note 3)</b>	<b>19,126,246</b>	<b>12,638,400</b>
<b>Net Asset Value per Unit</b>		
Preferred share (Note 2)	\$ 15.00	\$ 15.00
Class A share	10.96	10.55
	<b>\$ 25.96</b>	<b>\$ 25.55</b>

On Behalf of the Board of Directors

  
John P. Mulvihill, Director

  
Robert W. Korthals, Director

## Statements of Operations and Retained Earnings (Deficit)

Years ended October 31, 2004 and 2003

	2004	2003
<b>REVENUE</b>		
Interest	\$ 3,854,079	\$ 1,381,639
Dividends	6,729,146	2,249,216
	<b>10,583,225</b>	<b>3,630,855</b>
Net realized gains on investments and options	19,466,825	5,810,126
Net realized gains (losses) on short-term investments	(1,085,855)	17,991
	<b>18,380,970</b>	<b>5,828,117</b>
<b>TOTAL REVENUE</b>	<b>28,964,195</b>	<b>9,458,972</b>
<b>EXPENSES (Note 4)</b>		
Management fees	3,168,596	1,073,462
Administrative and other expenses	238,527	136,302
Custodian fees	36,683	49,487
GST and capital taxes	614,117	126,184
<b>TOTAL EXPENSES</b>	<b>4,057,923</b>	<b>1,385,435</b>
<b>Net Realized Income before Special Resolution Expense and Preferred Share Transactions</b>	<b>24,906,272</b>	8,073,537
Special resolution expense (Note 3)	-	(1,722,923)
<b>Net Realized Income before Preferred Share Transactions</b>	<b>24,906,272</b>	<b>6,350,614</b>
Preferred share distributions (Note 6)	(12,685,009)	(5,515,358)
<b>Net Realized Income</b>	<b>12,221,263</b>	<b>835,256</b>
Change in unrealized appreciation (depreciation) of investments and options	11,481,357	15,590,864
Change in unrealized appreciation (depreciation) of short-term investments	60,025	(98,130)
	<b>11,541,382</b>	<b>15,492,734</b>
Amortization of premium on issue of preferred shares (Note 3)	180,353	13,978
	<b>11,721,735</b>	<b>15,506,712</b>
<b>NET INCOME FOR THE YEAR</b>	<b>\$ 23,942,998</b>	<b>\$ 16,341,968</b>
<b>NET INCOME PER CLASS A SHARE</b>		
(based on average number of units outstanding during the year of 13,205,643; 2003 - 4,758,311)	<b>\$ 1.81</b>	<b>\$ 3.43</b>
<b>RETAINED EARNINGS (DEFICIT)</b>		
Balance, beginning of year	\$ 6,885,567	\$ (2,083,241)
Net income for the year	23,942,998	16,341,968
Distributions on Class A shares	(17,112,434)	(7,373,160)
<b>BALANCE, END OF YEAR</b>	<b>\$ 13,716,131</b>	<b>\$ 6,885,567</b>

### Statements of Changes in Net Assets

Years ended October 31, 2004 and 2003

	2004	2003
NET ASSETS, BEGINNING OF YEAR	\$ 132,175,279	\$ 33,332,116
<b>Net Realized Income before Preferred Share Transactions</b>	<b>24,906,272</b>	<b>6,350,614</b>
<b>Class A Share Capital Transactions</b>		
Proceeds from shares issued, net of issue costs (Note 3)	68,783,439	89,883,850
Amounts paid for shares redeemed	-	(9,495)
	<b>68,783,439</b>	<b>89,874,355</b>
<b>Amortization of Premium on Issue of Preferred Shares</b>	<b>180,353</b>	<b>13,978</b>
<b>Distributions (Note 6)</b>		
Preferred shares	(12,685,009)	(5,515,358)
Class A shares	(17,112,434)	(7,373,160)
	<b>(29,797,443)</b>	<b>(12,888,518)</b>
<b>Change in Unrealized Appreciation (Depreciation) of Investments, Options and Short-Term Investments during the Year</b>	<b>11,541,382</b>	<b>15,492,734</b>
<b>Change in Net Assets during the Year</b>	<b>75,614,003</b>	<b>98,843,163</b>
NET ASSETS, END OF YEAR	\$ 207,789,282	\$ 132,175,279

The statement of changes in net assets excludes cash flows pertaining to the Preferred shares as they are reflected as liabilities. During the year proceeds from Preferred shares issued, net of issue costs, amounted to \$98,238,746 (2003 - \$131,088,130) (see Note 3).

### Statements of Changes in Investments and Options

Years ended October 31, 2004 and 2003

	2004	2003
INVESTMENTS AND OPTIONS AT MARKET VALUE, BEGINNING OF YEAR	\$ 206,226,648	\$ 64,157,713
Unrealized appreciation (depreciation) of investments and options, beginning of year	(8,886,712)	6,704,152
<b>Investments at Cost, beginning of Year</b>	<b>197,339,936</b>	<b>70,861,865</b>
<b>Cost of Investments Purchased during the Year</b>	<b>496,520,130</b>	<b>238,684,216</b>
<b>Cost of Investments Sold during the Year</b>		
Proceeds from sales	369,659,717	118,016,271
Net realized gains on sales	19,466,825	5,810,126
	<b>350,192,892</b>	<b>112,206,145</b>
<b>Investments at Cost, End of Year</b>	<b>343,667,174</b>	<b>197,339,936</b>
<b>Unrealized Appreciation of Investments and Options, End of Year</b>	<b>20,368,069</b>	<b>8,886,712</b>
INVESTMENTS AND OPTIONS AT MARKET VALUE, END OF YEAR	\$ 364,035,243	\$ 206,226,648

## Statement of Investments

October 31, 2004

	Par Value/ Number of Shares	Average Cost	Market Value	% of Portfolio
<b>SHORT-TERM INVESTMENTS</b>				
<b>Treasury Bills</b>				
Government of Canada - December 30, 2004	320,000	\$ 318,080	\$ 318,080	
Government of Canada - January 27, 2005	7,170,000	7,122,988	7,122,988	
<b>Total Treasury Bills</b>		<b>7,441,068</b>	<b>7,441,068</b>	<b>5.6 %</b>
<b>Bonds</b>				
Canada Mortgage & Housing Corporation - December 1, 2004	121,660,000	121,990,361	121,964,367	92.2 %
		129,431,429	129,405,435	97.8 %
<b>Accrued interest</b>			<b>2,917,873</b>	<b>2.2 %</b>
<b>TOTAL SHORT-TERM INVESTMENTS</b>		<b>\$ 129,431,429</b>	<b>\$ 132,323,308</b>	<b>100.0 %</b>

## INVESTMENTS

## Canadian Common Shares

Bank of Montreal	1,220,000	\$ 67,063,587	\$ 70,211,000	
Canadian Imperial Bank of Commerce	1,055,000	72,346,214	77,964,500	
Royal Bank of Canada	1,031,900	62,815,277	65,422,460	
The Bank of Nova Scotia	1,877,500	68,860,918	74,349,000	
The Toronto-Dominion Bank	1,620,000	74,340,004	79,347,600	
<b>Total Canadian Common Shares</b>		<b>\$ 345,426,000</b>	<b>\$ 367,294,560</b>	<b>100.9 %</b>

	Number of Contracts	Proceeds	Market Value	% of Portfolio
<b>OPTIONS</b>				
<b>Written Cash Covered Put Options</b> (100 shares per contract)				
The Bank of Nova Scotia - November 2004 @ \$38	(1,000)	\$ (44,000)	\$ (7,889)	
Canadian Imperial Bank of Commerce - December 2004 @ \$70	(1,000)	(98,750)	(16,009)	
<b>Total Written Cash Covered Put Options</b>		<b>(142,750)</b>	<b>(23,898)</b>	<b>0.0 %</b>
<b>Written Covered Call Options</b> (100 shares per contract)				
Bank of Montreal - November 2004 @ \$56	(1,250)	(60,750)	(207,061)	
Bank of Montreal - November 2004 @ \$57	(500)	(29,000)	(55,391)	
Bank of Montreal - November 2004 @ \$59	(750)	(38,625)	(42,388)	
Bank of Montreal - December 2004 @ \$59	(1,500)	(116,500)	(124,213)	

Statement of Investments (continued)

October 31, 2004

	Number of Contracts	Proceeds	Market Value	% of Portfolio
INVESTMENTS (continued)				
OPTIONS (continued)				
<b>Written Covered Call Options</b> (100 shares per contract) (continued)				
Canadian Imperial Bank of Commerce - November 2004 @ \$70	(1,000)	(97,000)	<b>(444,692)</b>	
Canadian Imperial Bank of Commerce - November 2004 @ \$73	(750)	(67,500)	<b>(104,904)</b>	
Canadian Imperial Bank of Commerce - December 2004 @ \$74	(1,000)	(133,000)	<b>(160,812)</b>	
Canadian Imperial Bank of Commerce - December 2004 @ \$75	(750)	(88,500)	<b>(92,824)</b>	
Canadian Imperial Bank of Commerce - January 2005 @ \$74	(1,350)	(134,325)	<b>(267,854)</b>	
Royal Bank of Canada - November 2004 @ \$61	(1,000)	(41,000)	<b>(235,139)</b>	
Royal Bank of Canada - November 2004 @ \$63	(1,000)	(44,000)	<b>(86,103)</b>	
Royal Bank of Canada - December 2004 @ \$62	(1,533)	(132,176)	<b>(299,936)</b>	
The Bank of Nova Scotia - November 2004 @ \$38	(1,000)	(44,500)	<b>(174,437)</b>	
The Bank of Nova Scotia - November 2004 @ \$40	(1,000)	(44,000)	<b>(43,597)</b>	
The Bank of Nova Scotia - December 2004 @ \$38	(1,000)	(62,500)	<b>(173,774)</b>	
The Bank of Nova Scotia - December 2004 @ \$39	(500)	(29,500)	<b>(79,836)</b>	
The Bank of Nova Scotia - December 2004 @ \$40	(1,400)	(63,700)	<b>(102,578)</b>	
The Bank of Nova Scotia - January 2005 @ \$40	(1,000)	(58,500)	<b>(104,086)</b>	
The Toronto-Dominion Bank - November 2004 @ \$49	(1,000)	(48,000)	<b>(61,176)</b>	
The Toronto-Dominion Bank - December 2004 @ \$48	(1,000)	(60,000)	<b>(131,531)</b>	
The Toronto-Dominion Bank - December 2004 @ \$49	(1,000)	(70,000)	<b>(72,221)</b>	
The Toronto-Dominion Bank - December 2004 @ \$51	(1,000)	(77,000)	<b>(39,126)</b>	
The Toronto-Dominion Bank - January 2005 @ \$49	(1,000)	(76,000)	<b>(131,740)</b>	
<b>Total Written Covered Call Options</b>		<b>(1,616,076)</b>	<b>(3,235,419)</b>	<b>(0.9) %</b>
TOTAL OPTIONS		<b>\$ (1,758,826)</b>	<b>\$ (3,259,317)</b>	<b>(0.9) %</b>
TOTAL INVESTMENTS		<b>\$343,667,174</b>	<b>\$364,035,243</b>	<b>100.0 %</b>

## 1. Corporate Information

Premium Income Corporation (the "Fund") is a mutual fund corporation incorporated under the laws of the Province of Ontario on August 27, 1996. All shares outstanding on November 1, 2010 will be redeemed by the Fund on that date.

The Fund operates under the registered name Mulvihill Premium Canadian Bank Fund.

The Fund invests in a portfolio consisting principally of common shares of Bank of Montreal, The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Royal Bank of Canada and The Toronto-Dominion Bank.

To generate additional returns above the dividend income earned on the portfolio, the Fund will from time to time write covered call options in respect of all or part of the common shares in the portfolio. In addition, the Fund may write cash covered put options in respect of securities in which the Fund is permitted to invest. The Fund may also use put options to preserve the value of the portfolio where appropriate. From time to time, the portfolio may include debt securities having a remaining term to maturity of less than one year issued or guaranteed by the government of Canada or a province or short-term commercial paper issued by one or more of the Banks.

## 2. Summary of Significant Accounting Policies

These financial statements have been prepared in accordance with accounting principles generally accepted in Canada, which include estimates and assumptions by management that may affect the reported amounts of assets, liabilities, income and expenses during the reported periods. Actual results may differ from estimates. The significant accounting policies of the Fund are as follows:

### Investment valuation policies

Investments and short-term bonds are recorded in the financial statements at their market value at the end of the period, determined as follows:

Shares or other securities for which market quotations are readily available are valued at the closing sale price or, if there is no sale price, the average of the closing bid and ask prices.

Listed options are valued at market values as reported on recognized exchanges. Over-the-counter options are valued using an appropriate valuation model.

Short-term investments excluding short-term bonds are valued at cost plus accrued interest which approximates market values.

### Investment transactions and income

Investment transactions are accounted for on a trade date basis. Realized gains and losses on the sale of investments and change in unrealized appreciation/depreciation of investments and options and are determined on an average cost basis. Realized gains and losses relating to written options may arise from:

(i) Expiration of written options whereby realized gains are equivalent to the premium received;

(ii) Exercise of written covered call options whereby realized gains or losses are equivalent to the premium received in addition to the realized gain or loss from disposition or the related investments at the exercise price of the option; and

(iii) Closing of written options whereby realized gains or losses are equivalent to the cost of purchasing options to close the positions, net of any premium received.

Realized gains and losses related to options are included in net realized gains (losses) on sale of investments and options.

Option premiums received are reflected as deferred credits in investments so long as the options are outstanding. Any difference resulting from revaluation is included in change in unrealized appreciation/depreciation of investments, options and foreign currency. Premiums received on written put options that are exercised are included in the cost of the security purchased.

Dividend income is recorded on the ex-dividend date. Interest income is recorded daily as it is earned.

### Redeemable Preferred shares

Each Redeemable Preferred share is valued for financial statement purposes at the lesser of: (i) \$15.00; and (ii) the net asset value of the Fund divided by the number of Preferred shares outstanding.

### Premium on Preferred shares

Premium on Preferred shares net of issue costs is amortized over the remaining life of the Fund. The premium on Preferred shares retracted will be recognized on the date they are retracted.

### Generally Accepted Accounting Principles

The Canadian Institute of Chartered Accountants ("CICA") issued Section 1100, "Generally Accepted Accounting Principles ("GAAP")", which describes what constitutes GAAP and its sources. Since Section 1100 applies for fiscal years beginning on or after October 1, 2003, certain disclosures previously considered GAAP by virtue of general use in the investment funds industry, are no longer considered GAAP. This section primarily impacts the presentation of financial highlights, net income per Class A share and certain additional disclosures pertaining to cash flows, future tax liabilities and Preferred share liabilities. These disclosures have no impact on the valuation of the Fund or in the calculation of the net asset value per unit of the Fund.

### Cash Flow Statements

Cash flow statements have not been prepared as all relevant information has been included in the statement of changes in net assets and the footnote to the statement.

## 3. Share Capital

The Fund is authorized to issue an unlimited number of Preferred shares and Class A shares and 1,000 Class B shares.

On May 16, 2003 the shareholders of the Fund approved a special resolution to extend the life of the Fund for an additional seven years to November 1, 2010. The resolution extended the participation of holders

of Class A shares and Preferred shares in the performance of the Fund's underlying portfolio of Canadian Bank shares beyond the original redemption date of November 1, 2003 while maintaining the rights originally provided to shareholders. Costs of \$1,722,923 were incurred in connection with the special resolution.

On September 22, 2003, the Fund issued 8,500,000 units for total gross cash proceeds of \$226,525,000. On October 7, 2003, the Fund issued an additional 160,000 units for total gross cash proceeds of \$4,264,000. Costs of \$5,376,150 for Class A shares were incurred in connection with these offerings and have been charged to equity. The Preferred shares were issued at a premium of \$1,188,130 net of issue costs of \$4,440,870. This premium will be amortized over the remaining life of the Fund.

On September 23, 2004, the Fund issued 6,487,846 units for total gross cash proceeds of \$174,393,301. Costs of \$4,075,072 for Class A shares were incurred in connection with these offerings and have been charged to equity. The Preferred shares were issued at a premium of \$921,056 net of issue costs \$3,296,044. This premium will be amortized over the remaining life of the Fund.

Preferred shares and Class A shares may be surrendered at any time for retraction at specified retraction amounts. Holders of Preferred shares and Class A shares may concurrently retract one Preferred share and one Class A share on an October 31 valuation date at their net asset values. Shares retracted at any other valuation date or not retracted concurrently at an October 31 valuation date will be retracted at a discount to net asset value. Under the terms of a Recirculation Agreement, the Fund may, but is not obligated to, require the Recirculation Agent to use its best efforts to find purchasers for any Preferred shares and Class A shares tendered for retraction. The Preferred shares rank in priority to the Class A shares and the Class A shares rank in priority to the Class B shares with respect to the payment of dividends and repayment of capital on the dissolution, liquidation or winding up of the Fund.

The holders of Class B shares are not entitled to receive dividends. The Class B shares are retractable at a price of \$1.00 per share.

Class B shares are entitled to one vote per share. Preferred shares and Class A shares are entitled to vote on certain shareholder matters.

The Fund's Preferred shares have been classified as liabilities in accordance with the accounting requirements of The Canadian Institute of Chartered Accountants. Accordingly, net income for the year is stated after Preferred share distributions.

A net of nil (2003 - 900) each of Preferred shares and Class A shares were redeemed during the year.

**Issued and Outstanding**

	2004	2003
19,126,246 Preferred shares (2003 - 12,638,400)	<b>\$ 286,893,690</b>	\$ 189,576,000
19,126,246 Class A shares (2003 - 12,638,400)	<b>\$ 194,072,151</b>	\$ 125,288,712
1,000 Class B shares (2003 - 1,000)	<b>1,000</b>	1,000
	<b>\$ 194,073,151</b>	\$ 125,289,712

**Net Asset Value**

Net asset value per unit is the difference between the aggregate value of the assets of the Fund and the aggregate value of the liabilities of the Fund (excluding Redeemable Preferred shares and unamortized premium on issue of Preferred shares) on that date divided by the number of units then outstanding. The following are the net asset values of a unit, where Preferred shares are valued at the redemption value as defined in the prospectus, at October 31 for the most recent five years :

	2004	2003	2002	2001	2000
Preferred share	<b>\$15.00</b>	\$15.00	\$15.00	\$15.00	\$15.00
Class A share	<b>10.96</b>	10.55	8.38	10.26	12.35
	<b>\$25.96</b>	\$25.55	\$23.38	\$25.26	\$27.35

On October 31, 2004 Preferred shares on the TSX closed at \$16.12 (2003 - \$16.09), while Class A shares closed at \$12.40 (2003 - \$11.40).

**4. Management Fees, Expenses and Management Expense Ratios**

The Fund is responsible for all ongoing custodian, manager, legal, accounting and audit fees as well as all other expenses incurred by the custodian and manager in the ordinary course of business relating to the Fund's operations.

Fees are paid to Mulvihill Capital Management Inc. ("MCM") under the terms of an investment management agreement and to Mulvihill Fund Services Inc. ("Mulvihill") under the terms of a management agreement. The fees are comprised of monthly fees calculated at 1/12 of 0.80% and 1/12 of 0.10%, respectively, of the net assets of the Fund at each month end, excluding the liability for redeemable Preferred shares and unamortized premium on issue of Preferred shares.

**Management Expense Ratio**

The management expense ratio is the ratio of all fees and expenses charged to the Fund to average net assets excluding the liability for Redeemable Preferred shares and unamortized premium on issue of Preferred shares. The following are the management expense ratios for the years ended October 31 for the most recent five years:

	2004	2003	2002	2001	2000
	<b>1.20%</b>	2.62%*	1.20%	1.23%	1.17%

\* Management expense ratio for 2003 includes the special resolution expense. The management expense ratio excluding the special resolution expense is 1.17%.

**5. Income Taxes**

The Fund is a "mutual fund corporation" as defined in the Income Tax Act (Canada) (the "Act") and is subject to tax in respect of its net realized capital gains. This tax is refundable in certain circumstances. Also, the Fund is generally subject to a tax of 33 1/3% under Part IV of the Act on taxable dividends received in the year. This tax is fully refundable

upon payment of sufficient dividends. The Fund is also subject to tax on the amount of its interest income that is not offset by operating expenses and share issue expenses.

The Fund is also a “financial intermediary corporation” as defined in the Act and, as such, is not subject to tax under Part IV.1 of the Act on dividends received nor is it generally liable to tax under Part VI.1 on dividends paid on taxable preferred shares.

Under the dividend policy of the Fund, premiums received in respect of written options that are still outstanding at year end are not to be distributed in the year to the shareholders. The premiums retained by the Fund are subject to a refundable tax. This tax was nil for 2004 (2003 - nil).

The Fund has offset the future tax liability for refundable taxes payable with the refund expected upon payment of capital gains or ordinary dividends. As a result, the future tax liability for refundable taxes payable is eliminated.

## 6. Distributions

Distributions per Preferred share paid during the year were allocated as follows:

	2004	2003
Capital gains dividends	\$ 0.4122	\$ 0.3029
Taxable dividends	0.4771	0.5899
	<b>\$ 0.8893</b>	<b>\$ 0.8928</b>

Preferred shares are entitled to a cumulative preferential quarterly dividend of \$0.215625 per share payable on the last day of January, April, July and October in each year. To the extent that a quarterly dividend is a capital gains dividend funded by net realized capital gains or option premiums, holders of Preferred shares will receive an additional capital gains dividend of \$0.068 for each \$1.00 of Preferred share dividend so funded.

Distributions per Class A share paid during the year were allocated as follows:

	2004	2003
Capital gains dividends	\$ 1.20	\$ 1.14
Taxable dividends	-	0.06
	<b>\$ 1.20</b>	<b>\$ 1.20</b>

## 7. Commissions

Total commissions paid in 2004 in connection with portfolio transactions were \$395,623 (2003 - \$230,245).

## 8. Financial Instruments and Risk Management

The Fund’s financial statements consist of cash, investments, and certain derivative contracts (options).

Risks of these contracts arise from the potential inability of the counterparties to meet the terms of their contracts and from future movement in currency, stock values and interest rates. The maximum credit risk exposure is the aggregate of all contracts with a positive value as disclosed in the statement of investments. The Fund manages these risks through the use of various risk limits and trading strategies.

Investments and derivative contracts are carried at fair market values. Other Instruments are carried at cost, which approximates fair value.

## 9. Statement of Portfolio Transactions

The Fund will provide, without charge, a Statement of Portfolio Transactions (unaudited) upon written request by any shareholder to the Fund at 121 King Street West, Suite 2600, Toronto, Ontario, M5H 3T9.

### Statement of Corporate Governance Practices

The Board of Directors (the “Board”) bear responsibility for the stewardship of Premium Income Corporation (operating as Mulvihill Premium Canadian Bank Fund) (the “Fund”). Stewardship includes responsibility for the adoption of a strategic planning process, the identification of the principal risks of the Fund and ensuring the implementation of appropriate systems to manage these risks, succession planning, communications policy, and the integrity of the Fund’s internal control and management information systems.

The Board consists of five directors, three of whom are independent of the Fund. The Board believes that the number of directors is appropriate for the Fund and only directors independent of the Fund are compensated. Amounts paid as compensation are reviewed for adequacy to ensure that they realistically reflect the responsibilities and risk involved in being an effective director. Individual directors may engage an outside advisor at the expense of the Fund in appropriate circumstances subject to the approval of the Board.

To assist the Board in its monitoring of the Fund’s financial reporting and disclosure, the Board has established, and hereby continues the existence of, a committee of the Board known as the Audit Committee. The Audit Committee consists of three members, all of whom are independent of the Fund. The responsibilities of the Audit Committee include, but are not limited to, review of the annual financial statements and the annual audit performed by the external auditor, oversight of management’s reporting on internal control and oversight of the Fund’s compliance with tax and securities laws and regulations. The Audit Committee has direct communication channels with the external auditors to discuss and review specific issues as appropriate.

The Board is responsible for developing the Fund’s approach to governance issues and, together with the Investment Manager, is evolving a best practices governance procedure.

The Fund maintains an Investor Relations line and web site to respond to inquiries from shareholders.

## Mulvihill Capital Management Inc.

Mulvihill Capital Management is a leading independent investment manager responsible for managing more than \$3.2 billion in segregated and pooled funds on behalf of institutional and high net worth clients. Founded by Canada Trust in 1985, Mulvihill Capital Management emerged in 1995 as an independent company. Today, Mulvihill is managed by a cohesive team of senior managers and owners who have worked together for more than a decade. Our scale and independent structure allow us to provide our clients with a uniquely customized approach to asset management.

Mulvihill Capital Management operates three main lines of business:

- Mulvihill Institutional Asset Management → provides asset growth management of pension funds, corporations, management companies, endowment foundations and mutual funds with a wide variety of investment mandates. Our reputation has been built on the ability to provide customized portfolios that meet the stated needs of our clients.
- Mulvihill Wealth Management → offers a comprehensive specialized approach tailored to a client's personal investment strategies. Personalized service and customized reporting ensure that our clients are fully aware of the progress they are making.
- Mulvihill Structured Products → is responsible for the development and management of Mulvihill Hybrid Income Funds tailored to meet very specific investment objectives. Assets are generally managed to meet absolute rather than relative returns.

Mulvihill's Hybrid Income Funds are exchange-traded, equity-based funds that are enhanced by virtue of their broad distribution, special structure and performance characteristics. The Hybrid Income Funds are prime examples of our customized approach to asset management.

MULVIHILL HYBRID INCOME FUNDS	SYMBOL	HIGH	LOW
For the year ended October 31, 2004			
<b>MULVIHILL PLATINUM</b>			
Mulvihill Pro-AMS U.S. Fund	PAM.UN	\$ 20.81	\$ 19.66
Mulvihill Pro-AMS RSP Fund	PR.UN	\$ 19.74	\$ 18.46
Mulvihill Pro-AMS 100 Plus (Cdn \$) Fund	PRC.UN	\$ 19.45	\$ 15.72
Mulvihill Pro-AMS 100 Plus (U.S. \$) Fund	PRU.U	\$ 18.25 USD	\$ 13.66 USD
Mulvihill Pro-AMS RSP Split Share Fund	SPL.A/SPL.B	\$ 9.77/\$ 17.49	\$ 8.70/\$ 12.64
<b>MULVIHILL PREMIUM</b>			
Mulvihill Premium Canadian Fund	FPI.UN	\$ 22.25	\$ 18.76
Mulvihill Premium U.S. Fund	FPU.UN	\$ 15.30	\$ 11.43
Mulvihill Premium Oil & Gas Fund	FPG.UN	\$ 10.50	\$ 9.03
Mulvihill Premium 60 Plus Fund	SIX.UN	\$ 22.00	\$ 18.77
Mulvihill Premium Global Plus Fund	GIP.UN	\$ 14.24	\$ 11.59
Mulvihill Premium Canadian Bank Fund	PIC.A/PIC.PR.A	\$ 13.75/\$ 17.12	\$ 11.23/\$ 15.75
Mulvihill Premium Split Share Fund	MUH.A/MUH.PR.A	\$ 12.20/\$ 16.75	\$ 9.25/\$ 15.25
Mulvihill Premium Global Telecom Fund	GT.A/GT.PR.A	\$ 1.90/\$ 12.60	\$ 0.35/\$ 10.95
Mulvihill World Financial Split Fund	WFS/WFS.PR.A	\$ 15.00/\$ 10.80	\$ 11.45/\$ 10.21
<b>MULVIHILL SUMMIT</b>			
Mulvihill Summit Digital World Fund	DWT.UN	\$ 4.10	\$ 3.09

#### Board of Directors

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**John P. Mulvihill**

Chairman & President,  
Mulvihill Capital Management Inc.

**Sheila S. Szela**

Vice President, Finance & CFO,  
Mulvihill Capital Management Inc.

**Michael M. Koerner\***

Corporate Director

**Robert W. Korthals\***

Corporate Director

**C. Edward Medland\***

President, Beauwood Investments Inc.

\*Audit Committee

#### Information

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**Auditors:**

Deloitte & Touche LLP  
BCE Place  
181 Bay Street, Suite 1400  
Toronto, Ontario M5J 2V1

**Transfer Agent:**

Computershare  
100 University Avenue, 8th Floor  
Toronto, Ontario M5J 2Y1

**Shares Listed:**

Toronto Stock Exchange  
trading under  
PIC.A, PIC.PR.A

**Custodian:**

Royal Trust  
Royal Trust Tower  
77 King Street West, 11th Floor  
Toronto, Ontario M5W 1P9

Visit our website at [www.mulvihill.com](http://www.mulvihill.com) for additional information on all Mulvihill Hybrid Income Funds.

#### Hybrid Income Funds

##### Managed by Mulvihill Structured Products

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#### Mulvihill Platinum

Mulvihill Pro-AMS *U.S. Fund*  
Mulvihill Pro-AMS *RSP Fund*  
Mulvihill Pro-AMS *100 Plus (Cdn \$) Fund*  
Mulvihill Pro-AMS *100 Plus (U.S. \$) Fund*  
Mulvihill Pro-AMS *RSP Split Share Fund*

#### Mulvihill Premium

Mulvihill Premium *Canadian Fund*  
Mulvihill Premium *U.S. Fund*  
Mulvihill Premium *Oil & Gas Fund*  
Mulvihill Premium *60 Plus Fund*  
Mulvihill Premium *Canadian Bank Fund*  
Mulvihill Premium *Global Plus Fund*  
Mulvihill Premium *Split Share Fund*  
Mulvihill Premium *Global Telecom Fund*  
Mulvihill *World Financial Split Fund*

#### Mulvihill Summit

Mulvihill Summit *Digital World Fund*

#### Mutual Funds Managed by Mulvihill Capital Management

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Mulvihill Canadian *Money Market Fund*  
Mulvihill Canadian *Equity Fund*  
Mulvihill Canadian *Bond Fund*  
Mulvihill *Global Equity Fund*  
Mulvihill *U.S. Equity Fund*  
*Premium Global Income Fund*  
*Premium Canadian Income Fund*

#### Head Office:

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Contact your broker directly for address changes.



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**Mulvihill Structured Products**

Investor Relations

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Mulvihill Capital Management Inc.

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