Joint Pension Board Special Meeting

Romspen Investment

June 25, 2012

10:30 AM

SSB4220

Present: Prof. Stephen Foerster, Ms. Krys Chelchowski, Mr. Jim Loupos, Mr. Martin Bélanger, Mr. Jeffrey Symons, Ms. Louise Koza, Prof. Craig Dunbar, Ms. Michelle Loveland, Ms. Lynn Logan, Ms. Cindy Servos, Ms. Jane O'Brien, Mr. Ab Birch

Guests: Mr. Bruce Curwood, Russell Investments, Lisa Mills – Hicks Morley (conference line), Jennifer Schroeder – Western Human Resources Counsel, Steve Jarrett – Western Counsel

Regrets: Ms. Shannon Butler

Mr. Martin Bélanger introduced the external and internal legal counsel present at this meeting to the Joint Pension Board. Mr. Bélanger reviewed the purpose of this meeting, which was to discuss potential issues raised during a further legal review, done by Hicks Morley, of the Romspen offering documents. The exhibit, which is attached to these minutes, was presented to the group, and it was asked that questions be held until the end.

A legal review performed by Davies Ward for the benefit of the Operating & Endowment Fund on all the legal documents related to the investment in Romspen had not identified the risk that unitholders of the Romspen fund be held liable for fund activities beyond the amount of their investment in the fund. This detailed compliance review of the Romspen fund took place prior to the Joint Pension Board's approval to allocate an amount to the Romspen fund in April 2012.

Mr. Bélanger presented the powerpoint slides attached as an exhibit to these minutes. Mr. Belanger explained that due to some of the language in the offering memorandum, there could be a remote possibility that unitholders of the Romspen fund be held liable for fund activities beyond the amount of their investment in the Romspen fund. Mr. Bélanger stated that this was unlikely due to several factors:

- the fund is not engaged in business activities on its own therefore the fund is unlikely to be exposed to legal claims that could give rise to unitholder liability. Some examples of the types of claims that are possible (but remote) are contract, tort, and tax claims.

- the principals at Romspen have their own money in the fund (approximately $40 million) and therefore have their interests aligned with other unitholders
- any claim that exposes unitholders beyond their investment would need to exhaust the fund first, which is in excess of $850 million CAD
- the Davies Ward opinion had not identified this risk.

Mr. Bélanger stated that his recommendation was still to make the investment as planned. Three options were given to the Joint Pension Board for discussion.

- Make the investment as planned.
- Make the investment through a blocker corporation, which provides an additional layer of separation between the pension plan and any possible liability. Costs for doing so include set up fees of approximately $1500, annual audit and admin costs of approximately $8500, as well as additional costs for custodial and servicing.
- Reverse the Joint Pension Board decision to make this investment, and negotiate with Romspen on any compensation for lost time and opportunity. Romspen had closed the fund to new investors due to our entry, and any shortfall in funding may have to be covered by their line of credit in the short term. Romspen could request that in light of our commitment, the University or the Pension Plans pay for this interest expense at prime plus 3.5 percent.

At this time the Joint Pension Board was given the opportunity for discussion and questions. Responses were given by either the internal or external counsel present.

Q. – Explain how the blocker corporation reduces or eliminates risk.

A. – The blocker corporation would stand in line after the assets of the Romspen fund and the limited partnership structure. The Romspen fund is the limited partner which is not responsible for debts and obligations of the partnership. Since the blocker corporation would become the unitholder in the Romspen fund and because of the blocker corporation's liability is limited to its assets, establishing a blocker corporation would reduce the risk that the Pension Plans would have exposure to claims made against the Romspen fund's unitholders. It would likely reduce risk, but cannot be guaranteed to eliminate it. Some past case law has shown that a corporation's limited liability can be pierced by a claim.

Q. – How quickly can a blocker corporation be set up?

A. – A blocker corporation can be set up within a few days, although some details may need to be worked on past our investment date.

Q. – Can you form a blocker corporation for the short term and then give the Pension Plan members choice? Should more information be given to members?

A.- Members were given information about the Romspen fund. However, this remote risk, that unitholders of the Romspen fund be held liable for fund activities beyond the amount of their investment in the fund, applies at the Pension Plan level, and therefore cannot be avoided by member choice. The decision to add Romspen to the Western Retirement Plans can be characterized as a Joint Pension Board decision, not a member decision because the risks of a claim affects the entire pension fund, not the Diversified Bond Fund specifically.

Q. – What is the worst case scenario?

A. – A claim against the Romspen fund which is successful and the settlement is in excess of entire $850 million. The claimant then comes after the large unit holders in the fund including our pension plan. Western, Wilfrid Laurier University and other large unitholders are forced to defend individual cases. Joint Pension Board members would be accountable to pension plan members if they did not complete due diligence, just like any investment.

Q. - Would a blocker corporation make the investment in Romspen like the other investments offered by the Pension Plans?

A. – No the investment in Romspen would remain a unique situation, but it enhances our due diligence to have a blocker corporation.

Q. - How would a loss flow into the plan?

A. – A loss would be paid first by the master trust. The exact path, i.e. how the losses would be allocated to the different investment funds offered under the Western Retirement Plans, would be a Joint Pension Board decision.

Q. – Can the blocker corporation be added later?

A. – Not having the blocker corporation in place during the initial investment could reduce its effectiveness.

Q. – Is there a discussion that needs to happen among the Operating and Endowment committee?

A. – No, the Operating and Endowment Fund is already exposed to any risk related to the investment in Romspen, which was not identified in due diligence.

Q. – Can the members see the risk that unitholders of the Romspen fund could be held liable for fund activities beyond the amount of their investment in the fund in the material provided?

A. – Yes, the offering memorandum is online on the pension site. However, it is likely you need legal interpretation of the mosaic of information to be able to see this specific risk.

Q. - Have similar funds ever faced a lawsuit?

A. – No cases have been recorded under the same type of trust structure.

Q. - Does the Joint Pension Board take on any risk by not doing a blocker corporation structure?

A. – The key is that the Board follows a diligent process in coming to a decision. There are risks and advantages that need to be balanced. There is no one right decision.

Following the question period, Joint Pension Board members were each given the opportunity to comment on the investment and risks involved. As a group the Joint Pension Board made the following observations:

- The Board was comfortable with the investment itself and felt it was a good fit with member needs and our other investments, provides diversification and is responsive to member preferences.
- The Board was concerned with the possible liability, and the limited protection that a blocker corporation could offer from a prudence perspective.
- The Board was concerned with additional administrative complexity and costs associated with a blocker corporation.
- There is a concern with fairness and any spillover effect and how would we protect members if a claim arose.
- Enhancements to member disclosure may be necessary to ensure well-informed decisions by members.
- The majority of Board members stated a blocker corporation, while not a perfect solution, would be of some advantage.

Mr. Jeff Symons gave the Joint Pension Board his opinion that a blocker corporation would complicate the pension operations, making it more challenging for Northern Trust and the pension team to do financial reporting, auditing and could delay investment valuations each month. Mr. Symons also stated a blocker corporation adds to the operational risk as there is a need to work outside of the system controls to manage cashflow and investment return.

Mr. Martin Bélanger restated that he recommended continuing with the investment, and felt that it was best to do so without a blocker corporation.

The Joint Pension Board was asked to complete a straw vote on whether to make use of a blocker corporation for the investment. In the vote commentary, the Board members considered the benefits of using a blocker corporation weighed against the operational risks and costs it would add, in addition considerations of fairness and facilitating well-informed member decisions were discussed.

6 in favour of continuing, 4 against.

The Joint Pension Board members had further discussion on the ability of the blocker corporation to reduce the risk to Pension Plan members arising from the remote risk of unitholder liability in the context of an investment in the Romspen fund. The decision was expressed as a cost/benefit analysis requiring the weighing of the additional administrative costs and complexities against the risk reduction to the Pension Plans afforded by a blocker corporation.

Motion put to the Joint Pension Board

“That the Joint Pension Board instruct the administration to create an investment corporation to hold the Romspen Mortgage Investment Fund.”

Motion: Louise Koza

Second: Lynn Logan

6 in favour

4 against

Motion Passed

The meeting was adjourned at 11:45.

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Western Retirement Plans

Joint Pension Board Meeting

June 25, 2012

Western

Human Resources

Agenda

- Background
- Options
- Risk Mitigating Factors
- Other Pension Plans
- Additional Information

Background

- On April 9, 2012 JPB approved allocating 15% of the Diversified Bond Fund to Romspen Mortgage Investment Fund
- Onsite business due diligence conducted by Director, Investments, Russell Consultant and one Operating & Endowment Fund investment committee member in July 2011
- Assessed the firm's key personnel, its investment process, its back office, it compliance processes, the deal pipeline and reviewed the existing portfolio
- Legal due diligence conducted by Davies Ward
- Documents reviewed:
  - Offering Memorandum dated November 24, 2009
  - Declaration of Trust dated May 20, 2005
  - Limited Partnership Agreement dated May 20, 2005
  - Mortgage Management Agreement dated January 16, 2006
  - Listing of the Fund's Mortgage Portfolio as of September 30, 2011
  - Subscription agreement
- Title searches done

Background

- Conclusions of the legal due diligence:
  - Davies Ward's "searches confirmed that with respect to each property searched, the ranking of Romspen's mortgage is correctly identified on the Mortgage Portfolio List."
  - "Overall, while we consider the terms and conditions of the Fund to be relatively sponsor friendly, we have no significant concerns regarding such terms and conditions."
  - Verbal confirmation that conclusion of the legal opinion would not change if it had been done for a Defined Contribution Pension Plan.
- Based on results of business due diligence and legal due diligence, verbal commitment to invest $40 million on July 1 was made.

Background

- Commercial mortgage option introduced at the annual member meetings:
  - What do members have to do?
    - Learn more about commercial mortgages
      - Read Romspen Mortgage Investment Fund Offering Memorandum, available on the Retirement Plans website
    - Ensure that it is a good fit for your portfolio
      - Yes: Nothing to do
      - No: Consider other fixed income options
- Communication website for pension plan members set up on May 29, 2012
- Information available to members
  - Introduction to Romspen presented at the annual member meetings
  - Romspen's presentation to the Joint Pension Board on March 12, 2012
  - Romspen's Offering Memorandum
    - Includes disclosure on unitholder liability
  - Q&A
- Article in the Pension Newsletter, available on June 13, 2012
  - Mass email sent to all active pension plan members
  - "If you are a Western Retirement Plan member who holds the Diversified Bond Fund in your portfolio you may want to learn more about Romspen and commercial mortgages. Visit http://www.uwo.ca/humanresources/facultystaff/comp/pension/commercialmort.htm. If this investment does not seem suitable for your portfolio you may wish to access Target Date Funds or the Canadian Bond Fund or Long Term Bond Fund. "

Background

- Hicks, Morley asked to review the legal structure of the Diversified Bond Fund in May 2012
- On June 4, 2012 Hicks Morley raised the issue around unitholder liability
- Despite the fact that the issue had been reviewed, management decided to disclose the information to the Joint Pension Board

Options

1. Invest directly in the Romspen Mortgage Investment Fund
   - Unitholder personal liability remains, although remote
   - Lowest cost option
   - Least complex structure
2. Invest through a blocker corporation:
   - Additional costs:
     - Legal costs: one time $1500 plus disbursements and $500 per year for maintenance
     - Financial reporting costs: $8500 per year for financial statements and $750 per year for tax return.
     - Northern Trust: Setting up additional account; additional costs (% of AUM, additional trust agreement)
     - FSCO reporting
   - Significantly increases the complexity of the Fund
   - Requires selecting 1-3 directors
   - Small reduction in risk that's already remote
   - Romspen is o.k. with Western using a blocker and would allow us to implement the blocker after the initial investment.

Options

3. Delay or cancel the proposed investment
   - Interest penalty if we fund the investment past July 3, 2012
   - Romspen has a line of credit at prime + 3.5%
   - Potential lawsuit if we completely renege on the $40 million commitment
     - Romspen has closed the fund based on Western's expected commitment but they continue to fund mortgages with the assumption that our $40 million would be coming
   - Reputational risk

Risk Mitigating Factors

- The Romspen Mortgage Investment Fund that the Retirement Plans will invest in does not conduct any business operation. The Fund is the sole limited partner of, and invests its assets in, Romspen Mortgage Limited Partnership (the "Partnership"). The Partnership carries on the active business. The only risks at the Fund level are contract and tort claims or possible claims arising in relation to tax or other statutory liabilities.
- Third-party claims would be first satisfied out of the assets of the Fund, which are currently around $850 million.
- Principals of Romspen have about $40 million of their own money invested in the Fund. As such their interests are aligned with those of the Retirement Plans and it's unlikely that they will deliberately do anything that would create unnecessary liability and they will vigorously fight any third party lawsuit.
- Disclosure fairly typical for an investment trust.
- No investment risk.

Other Pension Plans

- Talked to several pension plans
- Most have never faced the same situation
- Ontario Power Generation Pension Plan uses corporations to invest in private assets (hedge funds and infrastructure)
- 3M uses blockers to invest in private equity (offshore fund in the Cayman Islands; similar to how Western Operating & Endowment Fund invests in private equity)
- Wilfrid Laurier Pension Plan invests directly in Romspen Mortgage Investment Fund; have not had the personal liability issue raised by their legal counsel

Additional Disclosure from Romspen

1. What risks in particular the Offering Memorandum is referencing at page 44?

No risk in particular. This is boiler plate language and all private trusts have similar provisions. The fund has never been sued.

Beneficiaries of trusts that are not reporting issuers under Ontario's *Securities Act* are not able to avail themselves of the protection of the *Trust Beneficiaries' Liability Act*, which, in response to lobbying during the growth in income trusts, eliminated beneficiary liability for any third-party claims against the trust or the trustees.

Most lawyers who have studied the issue agree that the risks are remote. The following is a brief explanation of the legal issues.

Absent an exculpatory or disclaimer clause in a contract with a third party, whereby the third party agrees that no recourse may be had by it against the trustees, a trustee may be liable to the third party for a claim under the contract. Courts have held that in a private trust scenario, beneficiaries may be liable to indemnify trustees for liabilities properly incurred. Another theoretical source of liability for beneficiaries is if the relationship between the trustee and the beneficiaries is characterized as one of principal and agent. If the trustees are seen as being the agents for the beneficiaries (principals) (if, for instance, the beneficiaries exert a certain degree of control over the trust's affairs, as is the case in a bare trust situation), the actions of the trustees could bind the beneficiaries as principals.

Importantly, the Fund's trust declaration provides that the trustees are to be indemnified against third-party liabilities only from the property of the Fund (i.e. there is no obligation on unitholders to indemnify the trustees from personal assets). Additionally, it provides that unitholders will not have any personal liability and no resort will be had to their private property for any liability in connection with the Fund's affairs, and that unitholders are entitled to be reimbursed from the Fund assets for any personal liability that might be imposed.

Additional Disclosure from Romspen

2. What steps they have taken to minimize the risks?

The Fund itself does not carry any business operation, which mitigates the risk.

The active mortgage lending business of the Fund is carried on by Romspen Mortgage Limited Partnership (RMLP), of which the Fund is the sole limited partner. The Fund does occasionally provide guarantees or indemnities to third parties, primarily to financial institutions providing financing or financial accommodations to RMLP or its subsidiaries. We ensure that any such guarantees contain specific language whereby recourse by the counterparty is limited to the Fund's assets and is disclaimed as against any beneficiaries or any of their assets.

Given the nature of the Fund's activities, the chances of the Fund being involved in tort claims are remote. With respect to statutory claims by government authorities, as the Fund carries on no active business itself and pays no income taxes itself, so it is difficult to contemplate what statutory claims or penalties would possibly apply.

Remember that third-party claims would first be satisfied out of the assets of the Fund, so any potential personal liability of Fund unitholders would come into play only upon those assets being insufficient to satisfy the claim, i.e. the quantum of the claim would have to be over $800 million. It is difficult to envision circumstances under which a claim of such a magnitude would ever occur.

3. Whether there are currently any investments that raise these risks?

If you are referring to mortgage investments, the risk we are talking about in the present context is not at the mortgage investment level. Risk of loss to RMLP at the mortgage investment level is constantly monitored and assessed, and, in any event, such risk is ring-fenced within the RMLP structure. The risk for the purposes of this discussion is at the Fund level for claims against the Fund qua investment fund. The only risks at this level are contract and tort claims or possible claims arising in relation to tax or other statutory liabilities.

Additional Disclosure from Romspen

4. Whether and in what amount insurance is carried?

The mortgage manager (Romspen Investment Corporation), on behalf of RMLP, is named as an insured on the property and liability insurance for each mortgage origination, in accordance with the specific insurance recommendations of our insurance consultant. In addition, title insurance in the amount of each mortgage loan is obtained for each mortgage origination, protecting against loss from title defects. Further, RMLP has a blanket policy of mortgage impairment insurance.

The Fund itself, given our assessment of the remoteness of risks and the prophylactic language in contracts entered into by the Fund described above, does not itself carry insurance.

5. Can we obtain representations in the subscription agreement to allow us to minimize risk?

The fund does not typically give different representations to different subscribers.

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