

Income Fund Liability, Governance and Insurance

April 3, 2007



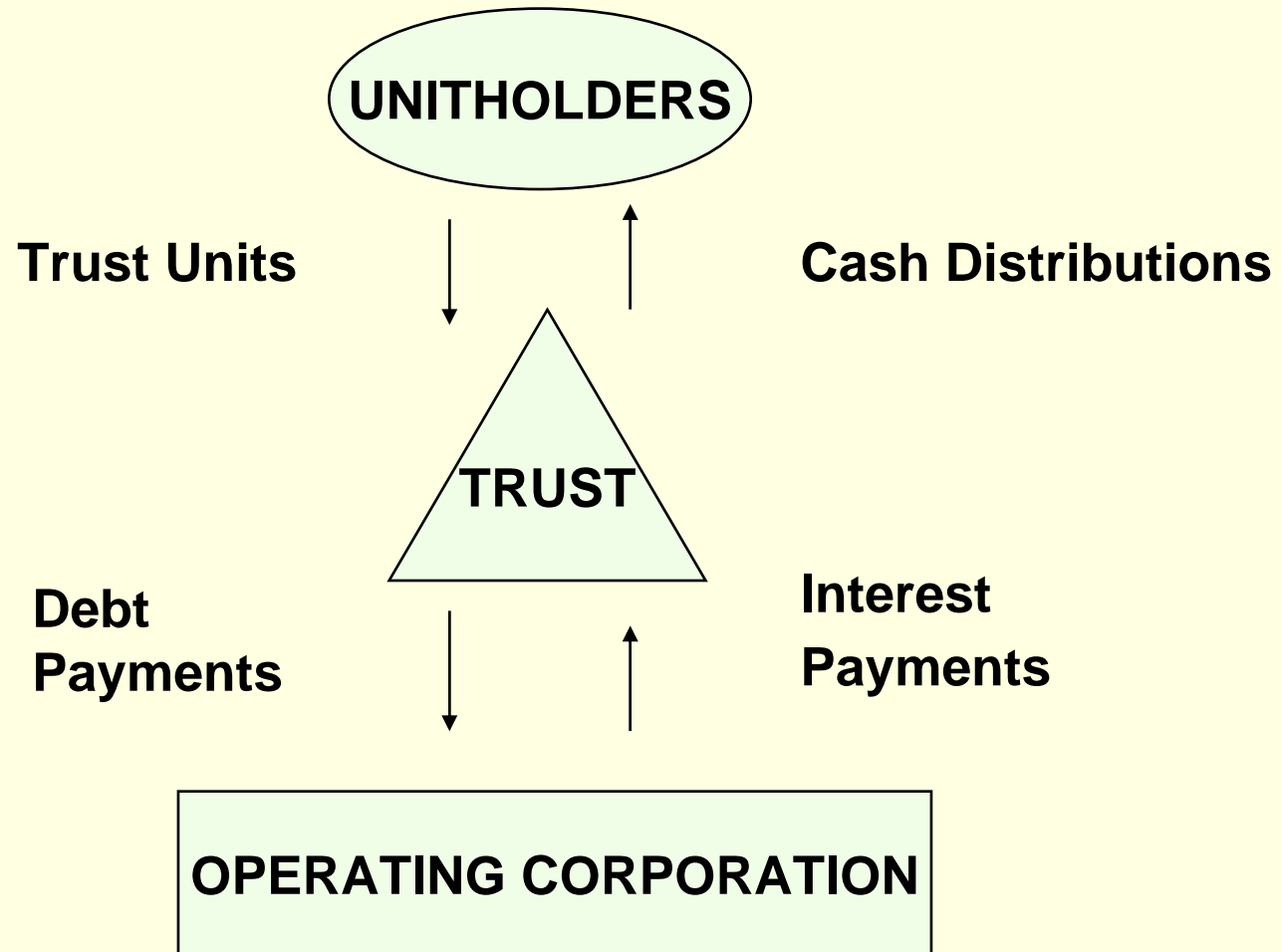
Today's Agenda

- **The Income Fund Business Model.**
- **The State of the Income Fund Marketplace.**
- **The Legal Framework for Trustees in Canada.**
- **What Drives Income Fund Claims in Canada.**
- **The Value of Effective Board Governance.**
- **Common Coverage Deficiencies and their Impact.**
- **Key Income Fund Policy Wording Considerations.**
- **The Executive Risk Insurance Solution.**
- **Why Purchase Income Fund Liability Insurance?**

What is an Income Fund

- A special purpose entity, often referred to as a **FLOW THROUGH ENTITY**, that sells equity to the public in the form of units.
- Proceeds from the sale are used to purchase an operating company that holds a set of **INCOME** generating assets.

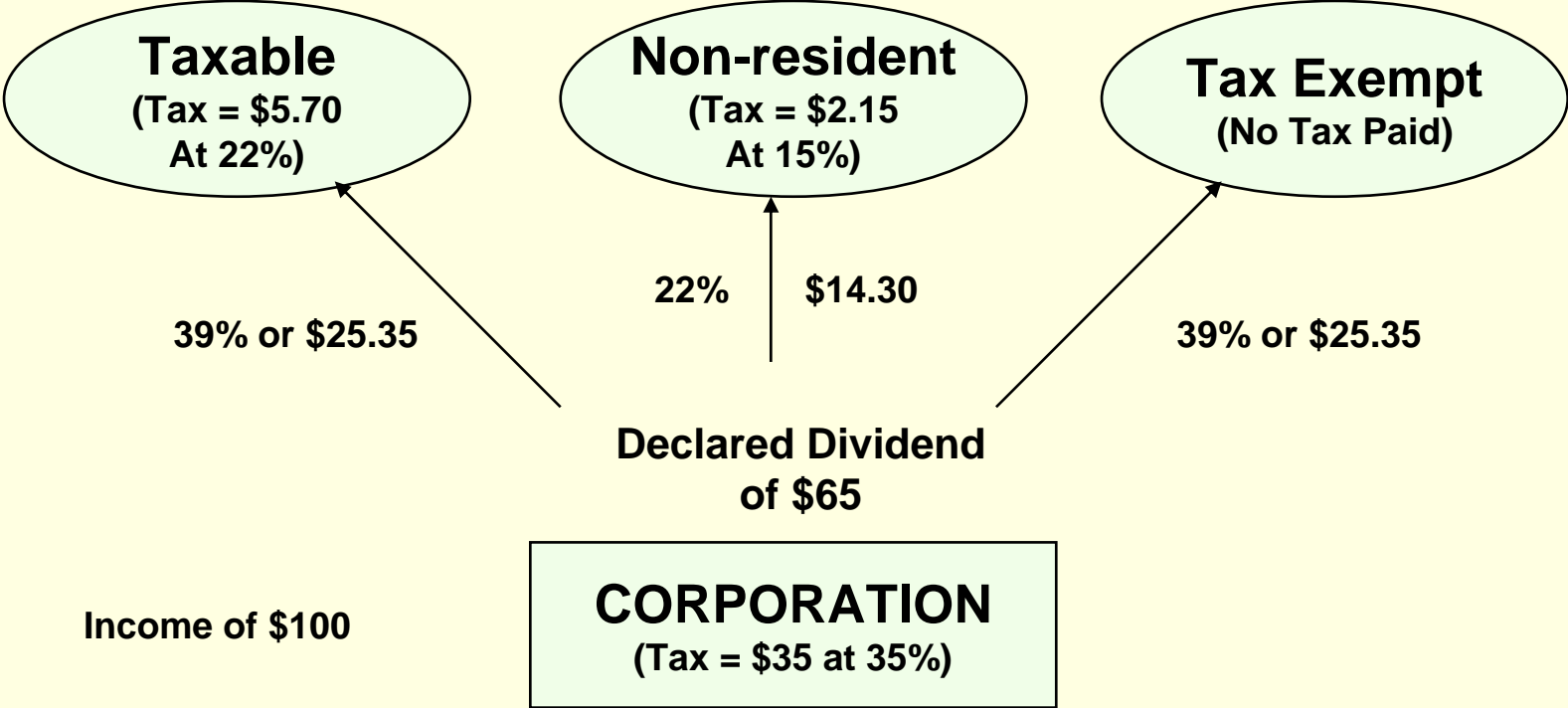
Basic Concept of an Income Fund



Income Fund Business Models

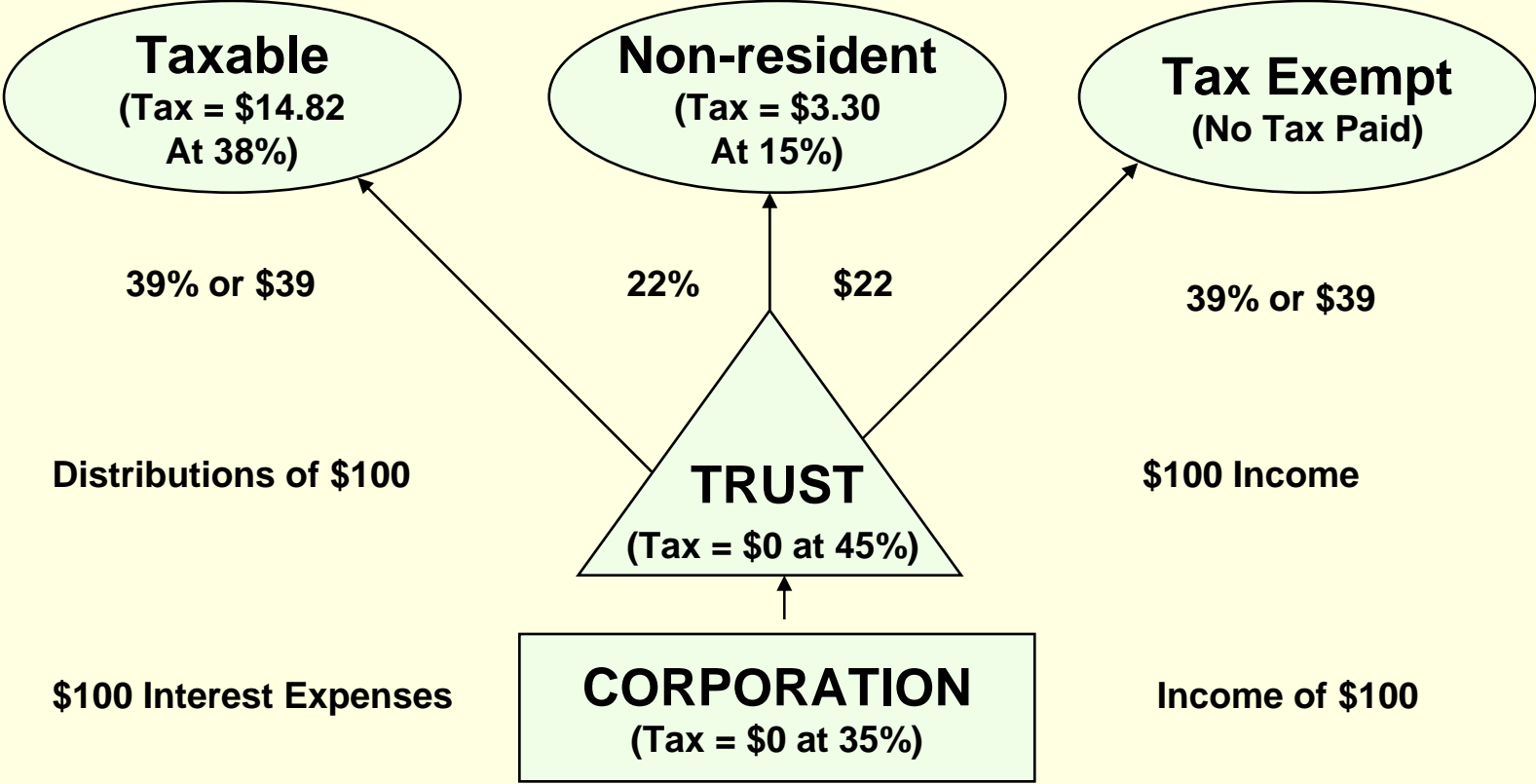
1. Business Trusts
2. Trademark Royalty Trusts
3. Oil & Gas Royalty Trusts
4. Real Estate Investment Trusts

Simplified Example of Taxes Paid by a Corporation



Total Taxes Paid = \$42.85

Simplified Example of Taxes Paid by an Income Fund



Total Taxes Paid = \$18.12

Today's Income – ROB Video

- *BCE Trust Conversion*

Today's Income – ROB Video

- *Canada to Tax Income Trusts*

Today's Income Fund Marketplace

- A Haunted Halloween – October 31, 2006
 - Tax levy of 31.5% in 20011
 - Specified Investment Flow Through Vehicles (SIFTS)
 - Publicly Traded Canadian Trust Holdings
 - Limited Partnership Holdings
 - SIFTS will not include
 - Real Estate Investment Trusts
 - US IDS Type Structures for US business

Today's Income Fund Marketplace

- The Trust market declined by 16.1% or \$32 Billion
- New taxes imposed at the Trust level
- Income received by the unit holder to be constituted as dividend income
- ALL new Trusts to be taxed immediately at the levy rate of 31.5%

The Impact of October 31, 2006

1. A decline in financings, IPO and secondary
2. Sector consolidation underway:
 - 13 Trusts have expressed intent in a sale / merger
 - Combined market value of \$3.7 Billion
 - REITS also experiencing consolidation
 - RIDEA and US REIT's
3. The search is on for "Hidden Tax Value"

2006 / 2007 Business Trusts M&A Transactions

- Atlas Cold Storage
- ACS Media
- SCI Income Fund
- Halterm Income Fund
- Coast Wholesale Appliances
- Bell Nordiq Income Fund
- Great Lakes Carbon Income Fund
- Lakeport Brewing Income Fund
- Norcast Income Fund
- Entertainment One Income Fund
- KCP Income Fund

Income Trusts M&A Expressions of Interest

- **Gienow Windows Income Fund**
- **Movie Distribution Income Fund**
- **Cinram International Income Fund**
- **Specialty Foods Group Income Fund**
- **E.D. Smith Income Fund**
- **Stephenson's Rental Services Income Fund**
- **Hartco Income Fund**
- **Custom Direct Income Fund**

*The Legal Framework for Trustees in Canada
and
What Drives Income Fund Claims in Canada
by
Eric Dolden*

Our Board Effectiveness Model



Improves Performance

Governance Infrastructure

- Board Structure, Process and Accountability
- Financial Reporting and Internal Controls
- Code of Conduct & Ethics
- Executive Compensation
- Performance Evaluation

Corporate Business Model

- Mission, vision and values
- Strategic outlook
- Business planning
- Market position
- Financial performance
- Industry outlook
- Value Proposition



Best Coverage - Best Rate

Is Board Effectiveness Important?

- Trust Indenture
- External Management Contracts
- Related Party Transactions
- The Election of Management
- Ensuring the Trust of Unitholders
- Stability Ratings:
 - Standard & Poor's (SR-1 to SR-7)
 - Dominion Bond Rating Services (STA-1 to STA-7)

Is Board Effectiveness Important?

- Canadian Securities Administrator
- Staff Notice 52-306 - MD&A Disclosure
 - Income Trust Disclosure Review
 - Goodwill
 - Executive Compensation
 - Timely Disclosure
 - Credit Facilities Management
- National Policy 58-201 – Corporate Governance Guidelines
- Staff Notice 41-304 – Prospectus Disclosure of Distributable Cash

The Regulatory Horizon - 2007

- Uniform Law Conference of Canada – 2006 Report
- 40 Comprehensive recommendations similar to CBCA
 - Election of trustees
 - Unitholder proposals
 - Oppression remedy and derivative legal actions
 - Statutory investigations
 - Related party transactions
 - Insurance and indemnification for trustees

Common Coverage Deficiencies

- *Insured Organization(s)*
- *Subsidiaries*
- *Insured Person(s)*
- *Change in Control Provision*
- *Order of Payment Provision*
- *Indemnification of Trustees*
- *Limited Insured versus Insured Modifications*
- *Income Trust Exclusions*
- *Tax Exclusion*

Inappropriate Income Trust Exclusions

Read the wording – it “may” cost your clients millions:

- Avoid Unit holder defense coverage – Dilutes limit's
- Avoid Conflict of Interest Exclusion – Chartwell REIT
- Avoid Failure to Maintain Trust status – Specialty Foods
- Avoid Tax Limitation - Obtain Affirmative Tax and Wage Liability Coverage

The Scope of Income Fund Liability Insurance

1. The identification of coverage priorities with the client is critical in the development of a meaningful insurance solution.
2. Policy wordings and how underwriters respond differs significantly.
3. A competitive analysis now needs to be utilized in communicating the strengths and weaknesses of the coverage quoted.
4. Opportunities now exist to expand the scope of coverage through effective negotiation.

Key Coverage Considerations

1. **Dedicated Coverage Format**
2. **No Panel of Legal Council**
3. **Non Rescindable and Non Cancelable Coverage**
4. **Full Severability and Final Adjudication**

The Executive Risk Income Fund Solution

- \$30 Million in Primary Canadian Capacity
- Appropriate Coverage for all Insureds Involved
- *Minimum* 80% Predetermined Defense Costs Allocation
- Clients CHOICE of Defense Costs Format and Legal Council:
 - Underwriters Duty to Defend, or the
 - Assureds Duty to Defend
 - No “Panel” of Lawyers

The Executive Risk Income Fund Solution

- Side “A” Non-Rescindable coverage
- \$1,000,000 Side “A” Excess Coverage for Trustees
- \$250,000 of Investigative Costs Coverage
- Affirmative Tax and Wage Liability Coverage
- No Run-Off Requirement in language
- Retention can apply to Defense or Settlement
- Entity Coverage for Securities Claims
- Order of Payments Clause
- No Restrictive Income Trust language

Our Underwriting Appetite

- **Stable, Predictable and Consistent Cash Flow Model**
- **Performing Well Financially**
- **Well Governed Risks**
- **Healthy Retained Ownership by Management**

Why Purchase Income Fund Liability Insurance ?

- Changing business and legal environment.
- Trustee vulnerability within the trust model.
- Class action proceedings across Canada.
- Limitations associated with trustee indemnification.
- Deficiencies of traditional D&O policies.
- Plaintiff firms are watching this market sector closely.

“A dedicated policy is now available”

Mitigating Risk for Directors, Officers and Trustees