Western Retirement Plans
Report to the Audit Committee
June 2013

Prepared on May 29, 2013

FOR INFORMATION

1. Summary

This report covers the calendar year January 1, 2012 to December 31, 2012. The Academic and Administrative Staff Pension Boards are responsible for the administration and oversight of two pension plans and the investment of assets for individual Retirement Income Funds (RIF) which are sponsored by the University. This report provides an overview of the plans, reviews the changes made to the plans in 2012 and describes the projects under way at the end of the year. Supplementary documents which have been distributed include the *Financial Statements* for the Master Trust, for each of the pension plans and the RIF.

2. Plan Overview

Asset Values, Membership and Investment Returns

The combined plans include about 7,100 investors and assets with a market value of approximately $1.1 billion. The *Master Trust* holds funds for both retirement plans and the individual RIF investors. As a defined contribution pension plan, members direct the investment of both their contributions and the University's contributions among 15 different investment options. The fund options are designed in tiers, meant to match the level of education or willingness to make independent diversification decisions. The funds are outlined below:

Tier 1: Comprehensive Funds	**Asset Value at 31/12/12**	**Number of Investors (can be in more than 1 fund)**	**Investment Returns in 2012**
Balanced Income	$40.5m	958	8.43%
Balanced Growth	$100.7m	2470	11.59%
Tier 2: Broad Asset Class Funds			
Diversified Bonds	$220.3m	2983	5.93%
Diversified Equity	$390.5m	3735	13.79%
Tier 3: Regional and Specific Strategy Funds			
Money Market	$61.2m	1310	1.17%
Target Date Funds	$56.5m	479	1.25% to 1.72%
Canadian Bond	$72.4m	878	3.54%
Long Term Bond	$33.5m	635	5.01%
Canadian Equity	$76.4m	1540	9.60%
US Equity Hedged	$16.5m	687	15.60%
US Equity Unhedged	$14.4m	484	13.08%
Non North American	$13.8m	748	13.97%
SRI Global Equity Fund	$3.4m	250	11.18%
Liquidating Trust	$14.6m	4353	21.41%

The Investments and Investment Income for each fund can be found in ***note 4 of the Master Trust*** *financial statements.*

Communication and Education

Members have access to various reports and material to assist them in the monitoring of their retirement funds. These resources include investment return sheets, annual report, newsletter, and access to external manager research, to name a few. These resources are in addition to the annual member pension plan statements which were sent out to members in April 2013, including all information as required by pension statute.

Various workshops are also available to assist members with their investment and retirement decisions. A total of 22 workshops were attended by 596 members / spouses in 2012. These include nine workshops developed to assist members of the Professional and Managerial Association (PMA) in making a one-time decision regarding their regular contributions to the retirement plans.

Some of these workshops are facilitated by an external provider, The Financial Education Institute of Canada. The University has contracted with them to provide two services to our members:

a) Financial and retirement planning workshops. The Financial Education Institute of Canada offered four full day financial and pre-retirement planning workshops in 2012. 53 members of the Retirement Plans have attended one of the sessions and feedback continues to be positive.
b) On-line financial education curriculum and tools. More than 800 members have registered for The Financial Educator ™ website.

Members can also use the services of two full time pension and benefit counselors to assist them with their retirement plan decisions. Members can bring their spouses, family members or investment advisors to these individual sessions with the pension and benefit counselors. The counselors held more than 1300 individual sessions with members in 2012. These sessions don't include numerous phone calls, email inquiries and group workshops that the counselors also handle.

Members of the retirement plans also have access to an on-line investment decision making tool. Through an Investment Personality Questionnaire (IPQ), they are asked to answer 16 multiple-choice questions on their investment horizon, risk tolerance, investment objectives and personal situation. Based on their answers members are directed to one of five portfolios comprised of specific investment funds available under the Western Retirement Plans. The IPQ has been very effective in assisting the pension and benefit counselors in orienting new members. In 2012, there were on average 50 to 60 hits per month on the IPQ webpage.

Resources Available

Each of the pension boards consist of 7 members: 4 elected by the membership and 3 appointed by the University. These boards work jointly together in the design of investment, communication and administrative policy (Joint Pension Board). The design and implementation of policy is completed with significant assistance from staff in human resources and financial services (8 full time dedicated staff). The board and staff also rely on the expert advice of external service providers to fulfill their duties including investment consultants, investment management firms, custodian and trustee, software vendors, actuarial consultants, legal consultants and auditors.

In total, the non-investment operational expenses are approximately ($2.0 million) or .18% of assets under management. The investment management and custodian costs are approximately .32% of assets under management. When compared to other Universities and institutional operations this level of operational costs is extremely lean.

*The operational costs are outlined in detail in **note 10 of the Master Trust** financial statement*.

Special Members

Prior to July 1970 (Academic) and March 1974 (Administrative Staff), the University pension plans were a defined benefit design: annual pension income at retirement was promised based on a formula. There are still some retired employees and active members who are entitled to that promised pension formula as a minimum guaranteed benefit. These individuals are referred to as "Special Members". As at December 31, 2012, there were 29 Special Members in the Academic Staff plan, all retired, and 69 Special Members in the Administrative Staff Plan, 29 of whom are still active and 40 who are retired.

Based on the most recent actuarial valuation report as at December 31, 2012, only four active Special Members are projected to receive a supplementary pension under the minimum guarantee provisions of the pension plan, thus creating an additional liability for the University. All other active Special Members are projected to receive a higher pension from their defined contribution account than that determined using the minimum guarantee benefit formula. Depending on the future performance of active Special Member defined contribution accounts, the number of Special Members projected to receive a supplementary pension under the minimum guarantee provisions of the plan may change. There are restrictions on how active Special Members can invest the funds in their regular account. They can invest up to 70% of their assets in equity funds.

The University has set aside some funds to pay for these promised pensions. These funds are in the general account of the pension plans. As at December 31, 2012, the Administrative Staff Pension Plan had $1.7 million in the general account, while the Academic Staff Pension Plan had $4.1 million. Our actuarial consultant determined that the Administrative Staff Pension Plan had a going-concern deficit of $69,000 and a statutory solvency deficit of $39,000 as of December 31, 2012, compared to a going-concern deficit of $193,000 and a statutory solvency deficit of $63,000 as of December 31, 2009. In order to fund these deficits, the University must make special payments of approximately $694 per month from January 2013 to August 2020, and $179 per month from September 2020 to December 2024. In addition, the University must contribute approximately $952 per month to fund the cost of the minimum guarantee benefit that is expected to be earned after the valuation date. The Academic Staff Pension Plan had a going-concern surplus of $373,000 and a statutory solvency surplus of $568,000 as of December 31, 2012, compared to a going-concern deficit of $157,000 and a statutory solvency deficit of $171,000 as of December 31, 2009. Because the Academic Plan is now fully funded on both going concern and solvency bases, the University does not have to make any special payments going forward.

For each of the Administrative plan and the Academic plan, almost all of the assets (100% for the Administrative Plan and 99% for the Academic Plan) are invested in "Immunized Bond Funds" that were created in October 2006 and July 2010, respectively. Immunizing the assets ensures that no significant funding deficit may occur in the future due to investment returns. Other factors, such as poor mortality experience, may still negatively impact the funding of the plan.

3. Changes Made in 2012

A number of changes were made in 2012. In May, the management of the Socially Responsible Global Equity Fund was transferred from Mackenzie Financial to Aberdeen Asset Management. This was an administrative change only as Aberdeen was an advisor on the fund managed by Mackenzie Financial. Mackenzie's mutual fund structure made it easier for the University Retirement Plans to make contributions and redemptions. As Mackenzie closed the fund, Western went directly to the manager of the fund. Also in May, as every two years, one Target-Date Fund matured (Target-Date Fund 2012) and a new one was introduced (Target-Date Fund 2018).

Two investment mandate transfers were made in June to optimize various portfolios on the Western Retirement Plans. First, an international equity portfolio was transferred from Fidelity Investments to MFS Investment Management. MFS is a highly successful investment firm that already manages money for the University's Operating and Endowment Fund. The Joint Pension Board felt that they had more potential to add value to the portfolio. In addition, the consolidation of assets with the Operating & Endowment Fund results in management fee savings that are completely passed on to plan members. The second change was related to a global equity mandate that was managed by T. Rowe Price. Following the retirement of the lead portfolio manager on the fund that the University was investing in, a decision was made to transfer the assets to another global equity mandate managed by a different portfolio manager at T. Rowe Price, with better expectations of value added.

In July the Retirement Plans implemented the addition of commercial mortgage mandate to the Diversified Bond Fund, one of the largest funds on the Western Retirement Plans. This new mandate is expected to improve the risk/return profile of the Diversified Bond Fund. The strategy is expected to generate higher returns than the traditional bond investments within the fund, while the short-term nature of its loans will protect the fund in a scenario of rising interest rates.

In November, the new contribution rates for members of the Professional and Managerial Association (PMA) were implemented. Members of the Administrative Staff Pension Plan who also belong to this employee group could elect to increase their required contributions to the plan from 2.5% to 5.5%. For those members with more than 20 years of service, electing to make contributions of 5.5% results in an increased employer contribution from 8.5% to 9.0%. The employer contribution was also increased from 7.5% to 8.0% for members with less than 10 years of service and from 8.0% to 8.5% for members with 10 to 20 years of service. Members with more than 20 years of service who chose to keep contributing at a 2.5% rate still get the same 8.5% employer contribution. Finally, an old option of contribution at a rate equal to 6% minus the contributions made to the Canada Pension Plan was discontinued for PMA members. The Librarian and Archivist pension plan moved from the Administrative Staff Plan to the Academic Staff Plan, also in November.

4. Projects Underway as at December 31, 2012

A number of projects were underway at the end of 2012.

Review of the Diversified Equity Fund

In January 2012 pension staff held town hall meetings to allow members of the Retirement Plans to provide feedback and ask questions regarding the ongoing review of the Diversified Equity Fund. The Joint Pension Board spent a significant amount of time in 2012 reviewing several investment strategies for inclusion in the fund to meet its goal of increasing the expected return of the Fund while reducing its volatility. At its December meeting, the Joint Pension Board approved adding three new strategies to the Diversified Equity Fund: 1) an emerging markets equity strategy, 2) a global small cap equity strategy and 3) a low volatility U.S. equity strategy. The first two strategies are expected to generate higher returns for the Fund. Emerging markets equities offer potential for higher returns than developed markets as emerging markets are expected to generate most of the world's economic growth in coming years. Smaller companies tend to grow faster than larger ones and as such, provide higher expected returns. Both emerging markets equities and global small cap stock strategies are relatively more volatile than developed markets equities and larger cap equities. To counterbalance the additional risk to the portfolio, the Joint Pension Board decided to add a low volatility U.S. equity strategy. This is a type of strategies that focuses on stocks that are expected to exhibit less volatility due to their sector of operations or the leverage on their balance sheet. This type of strategy has also demonstrated an ability to generate attractive returns compared to traditional equity strategies. The changes are expected to be implemented in the second half of 2013.

Liquidating Trust

The University Retirement Plans still hold some restructured non-bank asset-back commercial paper notes in the Liquidating Trust. Members are allowed to redeem their units of the Liquidating Trust on a monthly basis and re-allocate to other investments, as for any other investment option. During the year, members made average monthly redemptions of $126,000. In July 2012 the University sold restructured notes for an amount of $1.25 million of par value to fund members' future redemptions. There was $1.2 million in cash in the Liquidating Trust at the end of 2012. Subsequent to year-end, the Class 13 Notes held by the Liquidating Trust distributed approximately $415,000 to its noteholders, which resulted in a cash balance of $1.4 million at the end of April, 2013.

At the end of 2012 the Liquidating Trust had a value of $14.7 million. The quality of the notes has remained strong. The A-1 Notes, which represented 53% of the Liquidating Trust at the end of 2012, are still rated A (High) by DBRS and the A-2 Notes, which represented 29% of the Liquidating Trust at the end of the year, are still rated BBB (High) by DBRS.

The University will continue to monitor the Notes with the advice of the Kilgour Williams Group, a consulting firm specializing in monitoring non-bank ABCP and other structured assets. As the final maturity of the Notes is approaching, the likelihood of recuperating most of the capital invested is improving.

Grievance

As mentioned in last year's report, the University and the University of Western Ontario Faculty Association (UWOFA) agreed on a framework for settlement in early 2012. UWOFA made a presentation at the Joint Pension Board retreat in August 2012 to make recommendations on process and/or program changes. In February 2013, UWOFA withdrew the grievance.

Unitization Error

We have identified a valuation error made by Northern Trust in regard to incorrect unit values in late 2009 and early January 2010 affecting the Diversified Equity Fund, Balanced Income Fund and Balanced Growth Fund. At that time the non-bank ABCP was being carved out of the affected pension funds and moved to the Liquidating Trust. The error resulted in the unit values for January 2010 being understated for the Diversified Equity Fund and overstated for the Balanced Funds which has resulted in misstated returns for these Funds. A note is included in the audit findings of KPMG. This is a unitization error causing a misallocation between Funds. Other than for those members who have left with more money than they should have from the Balanced Funds, the assets remain within the pension plan and RRIF trusts held by Northern Trust. The error negatively impacted approximately 4000 unitholders of the Diversified Equity Fund by 0.34% in January 2010, for an average dollar value of $333. The total value of the misallocation was approximately $1.4 million and the largest impact on a single member was about $4700. Adjusted for subsequent returns as of April 30, 2013, the average impact per member is around $451 and the total value of the misallocation is about $1.8 million. External and internal counsel have been contacted and are evaluating options to address any impact of this error for affected plan members.

We appreciate the opportunity to present this report to Audit Committee and welcome any comments or questions you may have.

Academic Pension Board Membership

Stephen Foerster, Ivey School of Business (Chair)
Michelle Loveland, Management and Org. Studies
Craig Dunbar, Ivey School of Business
Shannon Butler, Management and Org. Studies

Administrative Staff Pension Board Membership

Krys Chelchowski, Office of the Registrar (Chair)
Jim Loupos, Internal Audit
Ab Birch, Financial Services
Josh Morgan, Department of Political Science

Appointed University Representatives on Each Board

Lynn Logan, Associate Vice-President Financial Services (Designate of VP Resources & Operations)
Jane O'Brien, Associate Vice-President Human Resources
Louise Koza, Director Human Resources (Total Compensation)