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March 3, 2012

Thoughts on Fees

Ewing Morris' guiding principle is to build an investment firm of which we would want to be clients. A fair fee structure is a very important element of building this firm. We believe the fee structure must align the managers' incentives and clients' objectives . We also believe incentives can be closely aligned when a relatively small fund charges a reasonable management fee and a profit allocation (sometimes called a performance fee), above a hurdle.

Fixed management fees guarantee large funds and mediocre returns
If a manager is paid fees only as a percentage of assets under management, human nature dictates the manager will maximize revenue by focusing on gathering assets. We believe size is the enemy of returns so when assets under management accumulate, investment results almost always deteriorate. Clients of large funds are virtually assured of paying high prices for mediocre (at best) results. A fixed management fee that feeds off asset growth *does not align incentives and objectives*.

Profit allocation alone does not align incentives and objectives
It would appear compensation based **exclusively** on profit allocation is most appropriate since clients care about investment results. However, a manager who is paid exclusively for performance is encouraged to take excessive risk because he shares in gains but, unlike the client, is indifferent financially between a 2% loss and a 50% loss. Profit allocation alone *does not align manager incentives and client objectives*.

2 & 20 is inappropriate for a large fund
A firm managing $5 billion that charges 2% management fees plus a 20% profit allocation is guaranteed a revenue stream of $100 million, regardless of investment results, and its profitability is assured. A profit allocation is just icing on the cake. This is a "heads I win, tails I win even more" scenario for the manager and *does not align incentives*.

A Better Structure – Reasonable management fee and profit allocation above a hurdle
The management fee should be large enough to cover basic expenses but profitability should depend on profit allocation. In addition, we do not think it is reasonable for clients to share "risk-free" returns with the manager so the profit allocation should only be applied to returns above a hurdle. This structure *does align incentives and objectives*.

Fees at Ewing Morris
Our fee structure consists of:
- 1.5% management fee
- 20% profit allocation on returns in excess of 4%
- Perpetual highwater mark with no resets

Management fees should cover reasonable operating expenses. We believe our expenses are modest and invite you to visit our office to form your own opinion.

We believe a 10-year Government of Canada bond represents a "risk-free" long-term investment. In the last decade, the average yield on this bond is 4%. Consequently, we believe 4% is a reasonable hurdle.

Our Fund provides for a perpetual highwater mark. This means that if a client invests $100 and the Fund returns 10% in the next year, the new highwater mark is $110. If the Fund's value declines in the following year, the client will not pay a profit allocation until the investment's value exceeds $110. This means we only get paid for "new" results, not for recovering losses. We believe this is a fair way to share in true long-term investment success.

Our goal is to manage a relatively small amount of money and deliver long-term returns of 10-15% annually. This compares to the 5.9% long-term annual return of the S&P 500. It should be noted that we cannot guarantee investment results. If we can achieve our goal, clients will achieve results, net of fees, well in excess of long-term average equity returns.

In summary, we believe our fee structure is appropriate because it aligns our incentives with the objectives of our clients.

Cordially,

John Ewing
Co-Founder

Darcy Morris
Co-Founder