

# IA Policies and Procedures Manual

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Schultz Collins Lawson Chambers Inc.

455 Market Street, Suite 1450  
San Francisco, CA 94105

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# 1 REGISTRATION, LICENSING, AND SUPERVISORY STRUCTURE

Schultz Collins Lawson Chambers, Inc., (SCLC) is an independent investment advisory firm headquartered in San Francisco, California, with branch offices in Towson, Maryland and Washington, D.C. In January of 1995 the firm incorporated, and opened its doors for business. The firm's primary business is the supervision of investment portfolios for institutional and individual investors. We provide this supervision in our capacity as investment counsel under the 1940 Investment Advisers Act.

The purpose of this document is to codify the Policies and Procedures all SCLC employees must follow every day in conducting business for the benefit of our customers, and to make all our employees aware of them. Secondly, it is intended to improve employee familiarity with the key elements of investment advisor regulation, so that employees grow in their awareness of the moral hazards inherent in the investment advisory business, which those regulations are designed to control. SCLC intends to eliminate conflicts of interest with our customers by structural means wherever possible, and in every case where we discover conflicts of interest that are systematic, first to disclose to customers their existence, and second to work to manage such conflicts so that they do not work to the detriment of our customers.

From the firm's inception, SCLC principals have sought to organize the firm and its services so as to make most of the regulations designed to protect customers of investment advisors simply inapplicable to the firm's operation, by making improper activities structurally impossible. Some examples:

- Insider Trading is practically impossible for SCLC employees by virtue of their connection with the firm, because with very few exceptions (e.g., legacy stocks with large embedded capital gains), client portfolios are invested only in pooled investment vehicles, and because the firm does not participate in investment banking or stock research. As a result, SCLC employees are extremely unlikely to learn of insider information as a result of their employment activities.
- Misrepresentation of the firm's investment performance is difficult, because SCLC does not maintain proprietary portfolios. Rather, because we are investment counsel, each client's portfolio is unique, is managed in terms of a unique investment policy, and trades independently of any other portfolios. Therefore we neither calculate nor advertise the firm's investment performance.
- Best execution concerns are minimized because SCLC does not recommend any particular broker/dealer. Broker/dealer selection is left to the client, and SCLC works with many different broker/dealers; furthermore, the firm is willing to work with any custodian the client may wish to select, provided only that SCLC is able to gain access to account information. Because each client portfolio is managed separately, client trades are not aggregated, and SCLC does not direct trades to any broker/dealer.
- The risk that customer funds will be invested unsuitably is minimized because SCLC does not accept investment discretion from clients. Rather, clients authorize all trades and disbursements (including those intended to pay investment advisory fees) before they are executed.
- Client funds are insulated from misappropriation of their assets, and from any risk posed by the firm's liquidity, by virtue of the fact that SCLC is not itself a custodian, trust company, mutual fund, fund manager, or broker/dealer, and never has any ownership interest in or control of client assets, either directly or via the agency of any person associated with the firm.
- The likelihood that SCLC will vote proxies in conflict with the best interests of customers is minimized because SCLC does not accept from customers the right to vote proxies. This policy is in harmony with our general determination never to act as investment manager, but only as investment counsel. SCLC's business purpose is, not to attract funds to our management, but to support rational,

informed client decisions.

- The risk that clients will suffer costs arising from their relationship with SCLC that exceed the fees specified in their advisory agreements with the firm is minimized by the fact that SCLC is an independent firm, owned by its principals, and not affiliated with any other provider of financial products or services. No other firm can exert influence over the investment advice we provide to customers, except insofar as they themselves are unable to execute client decisions derived therefrom, for reasons of their own structural organization, or of their regulatory constraints.

Despite the firm's determined, consistent efforts to eliminate them by structural means, nevertheless, moral hazards and conflicts of interest are to some extent inherent in our fiduciary relationship with customers, and so are not completely ineradicable. Employees are therefore urged to read this Manual carefully, and in all their work to apply the policies and procedures it specifies. Furthermore, however, employees should be always conscious that no set of formal policies, however extensive or comprehensive, can hope to cover all situations in which a customer's best interests may be jeopardized by their employment status or activities. This is as true of the body of highly evolved Federal and state regulations constraining investment advisers, as it is of this Manual. Employees should therefore endeavor to regulate all their activities in such a way as, above all, to serve the interests of the customer.

The Investment Advisers Act of 1940 ("the Advisers Act") defines an "investment adviser" in Section 202(1)(11) generally to include any person (including a natural person or an entity) who meets the "prongs" listed below:

- (1) for compensation
- (2) is engaged in the business
- (3) of providing advice to others or issuing reports or analyses regarding securities

Detail regarding these elements of the investment adviser definition are addressed by the SEC in Investment Advisers Act Release No 1092 ("Release 1092"). Release 1092 was developed jointly by the SEC and the North American Securities Administrators Association ("NASAA"). NASAA is an organization of state securities regulators. Release 1092 addresses the applicability of the Advisers Act to investment advisers commonly known as "financial planners." Release 1092 also clarifies numerous aspects of the definition of investment adviser as applies generally to all advisers.

## 1.1 Registration, Licensing

To effect its registration, SCLC has filed an application (Form ADV, Part 1) through the Investment Advisers Registration Depository ("IARD"). The information submitted in Part 1 includes information about the investment adviser's education, business, the persons who own SCLC, and disclosure regarding any sanctions for violating securities or other laws. SCLC has also completed Form ADV Part II and all relevant schedules. The information in Part II is geared primarily toward SCLC's clients, and provides the basis for the disclosures made to clients under Rule 204-3 of the Advisers Act. Part II contains information relating to the business practices, fees, investment strategies and conflicts of interest SCLC may have with its clients. Part II is not submitted to the SEC, but is deemed to be filed so long as a copy is maintained in SCLC's files. This record is subject to review by the SEC. Part II is required to be updated annually, within 90 days of SCLC's fiscal year end, and whenever it becomes materially inaccurate. Some states may require the form to be provided to the state.

## 1.2 IARD Maintenance

Any adviser registered with the SEC or state(s) is required to maintain current registration data through entitlement on the Registration Depository ("IARD"). Entitlement to the system is obtained through specific documentation submitted to the NASD as administrator of the system. Such documentation is found at <https://www.iard.com> or by contacting the IARD help desk at 240-386-4848.

Under state and SEC regulations, SCLC is required to file an Annual Updating Amendment through IARD within 90 days following the end of the firm's fiscal year.

SCLC is required to keep the information in its Form ADV current. Failure to maintain an updated Form ADV may result in disciplinary, administrative, injunctive or even criminal action against SCLC by the SEC or the state(s). Making a misleading claim in Form ADV could be the basis for a client or investor claim of fraud under state law.

SCLC must file an amendment to its Form ADV Part 1 electronically through the IARD according to the following requirements:

- Promptly for any changes to Items 1, 3, 9 or 11 of Part 1A
- Promptly for any change to Items 1, 2 (A through F), or 2I of Part 1B
- Promptly for any material changes to Items 4, 8 or 10 of Part 1A
- Within 90 days of the end of SCLC's fiscal year end (Annual Updating Amendment)
- If SCLC is required to provide an audited balance sheet with Schedule G, within 90 days of the close of SCLC's fiscal year (some states may have additional or differing requirements)

SCLC does not offer wrap fee arrangements. However, if such arrangements are ever made available to clients, any amendments to the wrap fee brochure (Schedule H) may be made by "sticker," provided any such supplemental information is dated and affixed to the brochure in a manner that can be readily understood by a client or potential client.

Part II of the Form ADV and any associated schedules form a written disclosure statement that provides information about business practices, fees, and conflicts of interest SCLC may have with its clients. Until an electronic facility is provided by the SEC through IARD, SCLC must maintain its Form ADV Part II in paper format and provide a copy to all of its clients. This document is called the SCLC Disclosure Brochure, and is a restatement in plain English, formatted for easy reading, of the information provided in Part II of the ADV.

The record of having provided either the SCLC Disclosure Brochure or Part II of the Form ADV shall include a record of the date(s) that the form was provided to any client or prospective client who subsequently became a client of SCLC. Rule 204-3 imposes requirements for the delivery of Form ADV Part II and relevant schedules (1) at least 48 hours prior to entering into the advisory relationship, or (2) at the time of entering into a contract with SCLC, provided the client can terminate the contract without penalty within 5 business days after entering the contract.

At least once annually, Rule 204-3 requires that SCLC must advise each of its clients that a current Form ADV Part II and applicable Schedules, or an equivalent set of documents (i.e., the SCLC Disclosure

Brochure), are available for review. The firm shall maintain a record of the clients to whom the form has been offered, the date and form of the offer (by representative sample copy), of those clients who accept the offer, and evidence that the request was fulfilled.

### 1.3 Supervisory Structure

In accordance with Rule 206(4)-7 of the Investment Advisers Act of 1940 (hereinafter "Advisers Act"), other SEC regulations, and applicable state regulations requiring supervision of specific firm activities, SCLC has established a supervisory structure that includes the designation of personnel in key positions and a description of those positions. Key personnel, their duties and supervisory obligations, as applicable, are identified in organization charts maintained in the firm's central electronic files.

In accordance with Rule 206(4)-7 of the Advisers Act, SCLC must designate one employed individual to act as its Chief Compliance Officer, whose duty it shall be to administer the firm's compliance policies and procedures. The Chief Compliance Officer shall have full responsibility and authority to develop and enforce all appropriate compliance related policies and procedures for the Adviser. SCLC identifies its Chief Compliance Officer ("CCO") in its organizational charts, and through the IARD system as required.

SCLC officers include, but are not limited to, principals such as the Founder, Managing Member, or others and a Chief Compliance Officer. These individuals are ultimately responsible for SCLC's supervisory system, including its implementation, maintenance and ongoing appraisals as more fully described in the Procedures section below. SCLC's principal officers may or may not supervise other officers, or managers, or other employees of the Adviser. SCLC's Chief Compliance Officer is responsible for development and enforcement of the firm's compliance program, unless specifically exempted in the Procedures section below.

The approach to licensing of SCLC's individual associated persons (including those in supervisory roles) differs from state to state. Many states impose requirements for SCLC's associated persons to meet certain licensing requirements, depending upon the nature or scope of services they offer. Section 203A(b)(1) of the Advisers Act prohibits a state from applying its registration and licensing laws to a federally-covered investment adviser and its supervised or associated persons. Nonetheless, a state can impose registration, licensing or other qualification requirements on an associated person (sometimes known as an "investment adviser representative") if the individual has a place of business in the state. These requirements may include filing a Form U-4, taking and passing Series 65 or 66 or achieving other proficiency exams. When they apply, compliance with these requirements may generally be reported through disclosures on the IARD system.

Rule 203A-3(a) of the Advisers Act defines an "investment adviser representative" as a supervised person of the investment adviser who has more than five clients who are natural persons and more than ten percent of whose clients are natural persons. Notwithstanding this, a supervised person is not considered an investment adviser representative if the supervised person does not regularly solicit, meet with, or otherwise communicate with clients of the investment adviser, or provides only impersonal investment advice.

## 1.4 Procedures for Compliance with Registration and Licensing

SCLC has established procedures that require review of its registration status no less frequently than annually, or more often in the event of material changes to the firm's business organization, personnel, or address of record, &c. This review shall include, but is not limited to: a review of the Form ADV, both Part 1 (filed with the SEC via IARD) and Part II and its related Schedules (filed in the SCLC central records); review of the underlying criteria and supporting information for the Form; and confirmation of all material responses. A record of the review shall be retained among SCLC's central records.

Because SCLC does not generally require individual licensure, no individual may conduct advisory services with the investing public without prior approval by SCLC.

To ensure that its supervisory structure is adequately formed and adhered to, SCLC maintains an updated record of its supervisory chain of command in organization charts stored in the firm's central electronic files. The organization charts are periodically distributed to individuals named as supervisors, to ensure that they will remain at all times informed of the supervisory requirements attributed to them.

Unless otherwise specifically enumerated, the CCO is responsible for implementation and ongoing oversight of these procedures, including the oversight of individuals to whom certain procedures may be delegated.

No less than annually, the CCO will oversee the renewal of SCLC's registration. No less than annually (within 90 days of the SCLC fiscal year end), the CCO will file an annual amendment, updating all forms and records as necessary.

The CCO or an individual to whom the CCO has delegated the responsibility for licensing will conduct periodic reviews of SCLC's regulatory filings, including at a minimum an annual amendment, and amendments upon any material change in its business practices. Such delegation will be reported on SCLC's organizational chart.

Amendments to SCLC's regulatory filings will be documented by electronic tracking on IARD, and by retention of all dated materials among SCLC's central compliance records.

# 2 BOOKS AND RECORDS REQUIREMENTS

Rule 204-2 of the Advisers Act requires that SCLC maintain certain books and records for certain specified periods of time.

## 2.1 Required Records

Pursuant to the Advisers Act at Rule 204-2, the following records are required to be maintained and preserved in an easily accessible place for a period of not less than 5 years from the end of the fiscal year during which the last entry was made on the document. For the first 2 years, the record must be maintained on the premises. This retention requirement applies to the records noted below, EXCEPT that organizational records must be retained for at least three years following the date on which SCLC terminates its registration.

### 2.1.1 Advertising File

SCLC must retain a copy of each notice, circular, advertisement, newspaper article, investment letter, bulletin or other communication that an investment adviser circulates or distributes, directly or indirectly, to 10 or more persons (other than persons connected with SCLC). If such notice, circular, advertisement, newspaper article, investment letter, bulletin or other communication recommends the purchase or sale of a specific security and does not state the reasons for such recommendation, a memorandum by SCLC including information to support the recommendation must be included in the file.

Such copies are to be found in the Advertising file, in the firm's central records.

### 2.1.2 Annual Offer of Form ADV Part II (Disclosure Brochure)

SCLC must offer a current form of its Disclosure Brochure no less than annually to all clients. SCLC must document and maintain a record of the offer. SCLC must also retain a sample version of the Form ADV Part II as evidence of timely amendment and distribution of the Disclosure Brochure. The file shall include the following:

- List of each individual or other party to whom the offer or an updated Disclosure Brochure (or Form ADV Part II) was provided
- Copy of the form of the offer (letter or other means of distribution)
- Form ADV Part II in effect at the time of the offer
- Any individual or other party that responds to the request
- List of evidence that any individual or other party who responded to the offer was provided with the current form, as requested

### 2.1.3 Annual Review

SCLC is required by Rule 204-2(a)17(ii) to maintain any record(s) that document the review of its written policies and procedures performed in connection with Rule 206(4)-7(a).

## 2.1.4 Associated Persons Personal Transactions Records

Rule 204-2(a)(12)(i) requires that SCLC retain a record of every transaction in any securities in which SCLC or any associated person (or investment advisory representative) has or acquires any direct or indirect beneficial ownership, unless the transaction is not subject to SCLC's or the associated person's control, or the transaction is in securities that are: direct obligations of the Government of the US; bankers' acceptances, CDs, commercial paper and high quality short term debt instruments including repurchase agreements; or shares issued by registered open-end investment companies.

For purposes of this rule, the term "associated person" shall mean:

- Any partner, officer or director of the investment adviser
- Any employee who makes any recommendation, who participates in the determination of which recommendation shall be made, or whose functions or duties relate to the determination of which recommendation shall be made
- Any employee who, in connection with his duties, obtains any information concerning which securities are being recommended prior to the effective dissemination of such recommendations or of the information concerning such recommendations
- Any persons who obtain information concerning securities recommendations being made by such an investment adviser prior to the effective dissemination of such recommendations or of the information concerning such recommendations, and who are in a control relationship to the investment adviser, or are an affiliated person of such a controlling person, or are any affiliated person of such affiliated person.

In addition to those associated persons included in the definition above, SCLC may at its sole discretion require that other employees, consultants, or others provide evidence of their personal trading to ensure that appropriate controls are in place at all times.

## 2.1.5 Financial Records

Records of SCLC's financial condition, and evidence of current and accurate accountings, are required by Rule 204-2. Included in this requirement are the following:

- Journal that lists all cash receipts and disbursement records, and any other records of original entry used to create the journal entries
- General and auxiliary ledgers (or other comparable records) reflecting asset, liability, reserve, capital, income and expense accounts
- All check books, bank statements, canceled checks and evidence of current reconciliations
- All bills or statements relating to the firm's business, and evidence of payment, which might include copies of checks received or other statements demonstrating payment of invoices
- Current financial statements, including trial balances and net capital computations, balance sheets, income and expense statements and internal audit working papers relating to the firm's business

## 2.1.6 Lists by Type of Client/Investor or Account

SCLC must maintain a list of all accounts in which it is vested with discretionary authority. However, because the firm does not accept any such vestment, the list will always be blank. It is kept in electronic form in the firm's client portfolio database management system, wherein there are three possible ways to specify the status of an asset:

- Discretionary: no assets may fall under this category.
- Limited Power of Attorney: an asset for which SCLC has been named as adviser of record, limited attorney in fact, or other interested party (OIP).
- Non-Discretionary: an asset for which, for reasons of the custodian's organization or policies, SCLC cannot be named as adviser of record, limited attorney in fact, or OIP, so that all correspondence, trades, and inquiries regarding that asset must be routed to the custodian through the client.

## 2.1.7 Order Tickets

A ticket or memorandum of each order placed by SCLC for every purchase or sale of any security, or any instruction received by SCLC from a client concerning the purchase, sale, receipt or delivery of any security, and of any modification or cancellation of any such order or instruction, must be retained and must include the following information:

- Terms and conditions of the order, instruction, modification or cancellation
- Person connected with SCLC who recommended the transaction
- Person who placed the order
- Account for which the order was entered
- Date
- Bank, broker or dealer by or through whom the order was executed
- Whether or not the order was discretionary

## 2.1.8 Organizational Documents

SCLC must maintain current and complete Articles of Incorporation, charters, minute books, partnership records, stock certificate books and other reports as evidence of its viability as an entity, as required by state or other jurisdictions. *Unlike the other types of records noted in this section, these records must be preserved for at least three years after the cessation of SCLC's operations as a Registered Investment Advisor.*

## 2.1.9 Performance Advertising Supporting Documentation

SCLC does not distribute advertisements of the firm's investment performance. However, if SCLC should ever distribute performance advertising (or reporting that includes Performance of any managed accounts/fund(s) and that is sent directly or indirectly to 10 or more persons), it must retain all accounts, books, internal working papers, and any other records or documents that are necessary to form the basis for

or demonstrate the calculation of the performance or rate of return of any or all managed accounts or securities recommendations.

### **2.1.10 Policies and Procedures**

Rule 204-2 requires that SCLC retain a copy of its policies and procedures formulated pursuant to Rule 206(4)-7 that are currently in effect or which were in effect within the most recent 5 year period.

### **2.1.11 Powers of Attorney**

SCLC is required to maintain all powers of attorney, including any documents that evidence the granting of discretionary powers to the firm.

### **2.1.12 Proxy Records**

It is SCLC policy never to vote proxies in the stead of clients or investors, nor does SCLC accept from any client the right to vote proxies. If in the future that policy should change, then in connection with Rule 206(4)-6, SCLC must retain:

- Copies of its policies and procedures for proxy voting
- Copy of each proxy statement that it receives regarding client securities (it may rely on a third party providing the agreement between SCLC and third party specifies responsibility for record-keeping)
- Record of each vote SCLC casts on behalf of a client
- Copy of any supporting documentation created by SCLC that was material to making a voting decision
- Copy of each client request for information on how SCLC voted proxies, including the SCLC response thereto

### **2.1.13 Solicitor Disclosure Document**

Whenever solicitors are involved in referring advisory clients to SCLC, the firm must retain written acknowledgements of receipt of SCLC disclosure documents and copies of solicitor disclosure documents provided to clients or prospective clients in connection with Rule 206(4)-3.

### **2.1.14 Transaction Records**

Whenever SCLC provides any investment supervisory services to any person, it must retain a record showing separately for each client the securities purchased and sold, and the date, amount and price of each such transaction; as well as by-security information for each client, so that SCLC can promptly furnish the name of each client with an interest in the security and the amount of that interest.

### **2.1.15 Written Agreements**

Copies of any and all written agreements (advisory agreements, subscription agreements, powers of attorney, etc.) in use with clients must be maintained. Side letters may be deemed to be part of this

requirement, as are any written agreements into which SCLC enters with any client or otherwise relating to its business. Accordingly all side letters and other written agreements with clients shall be retained among SCLC's client records.

SCLC shall maintain a representative template for each type of agreement, and a database of SCLC clients that are subject to each type of agreement. The actual executed agreements shall be retained in separate client files.

### **2.1.16 Written Communications**

Originals of all written communications received and copies of all written communications sent by SCLC relating to its advisory business must be retained. Note that this rule has been deemed to include electronic communications (including email and instant messages) and communications internal to SCLC. Because instant messages, unlike email messages, are not susceptible to "blind carbon copying" to a central archive where they may be reviewed by SCLC compliance personnel or algorithms, it is SCLC policy that no personnel may use instant messaging for business purposes. Use of email accounts mediated elsewhere than on SCLC mail servers pose the same risks to the firm and its clients as do instant messages. Thus while the use of such extramural email services is not prohibited altogether to SCLC employees, they may not use such services for business communications.

Unsolicited market letters and other similar communications of general public distribution not prepared by or for SCLC are not covered under this category.

## **2.2 Custodial Advisers Records**

Advisers with custody or possession of securities must retain the following:

- Journal or other record showing all purchases, sales, receipts and deliveries of securities (including certificate numbers) for custodial accounts
- Record of all debits and credits for custodial accounts
- Separate ledger account for each custodial client showing all purchases, sales receipts and deliveries of securities, the date and price of each purchase and sale, and all debits and credits
- Copies of confirmations of all transactions made in custodial accounts
- For each security, a record including the name of the client with an interest in such security, the amount or interest of each client, and the location of each such security

It is SCLC policy not to retain client securities or checks for more than three business days, and then only to forward such instruments, either to custodians specified therein by the client as payee or attorney in fact thereof, for custody and safekeeping, or to the client.

## **2.3 Additional Records**

Although not enumerated in specific regulations, certain files and records may be requested by a regulatory examiner at the time of an audit. SCLC maintains files and records of the types enumerated in the following list, which, it should be noted, is neither exhaustive nor all-inclusive.

### **2.3.1 Allocation Procedures, Trading Practices**

Advisers should maintain a file that contains allocation procedures and other trading practices, relevant representative order forms, and related documentation as evidence of its consistency in making pre-trade allocations of client orders. As investment counsel, SCLC does not aggregate trades across client portfolios, so pre-trade allocations of aggregated client orders are not possible. The firm does not therefore maintain evidence of consistency in making such orders.

SCLC executes client trades according to the temporal order in which the relevant client trading authorizations were received. This allocation procedure, along with all other trading policies, is recorded in the Trading section below.

### **2.3.2 Best Execution File**

Regulatory examiners will request that SCLC demonstrate its efforts to seek best execution in making client/investor transactions.

In order to minimize conflicts of interest that could arise in the event that SCLC were to steer clients toward a certain broker/dealer, it is SCLC policy not to recommend any particular broker/dealer for execution of client transactions, but rather to work with such broker/dealers as clients themselves select. This is in line with the general philosophy of SCLC, that its proper role is, not to manage portfolios for clients, but rather to enable them to make the most informed, rational investment decisions possible, and then to assist them in carrying out such decisions.

This policy includes the decision which custodians or broker/dealers to utilize. Therefore an important role of SCLC is to inform clients of the relevant costs and benefits of doing business with various different broker/dealers. The client, however, bears the final responsibility of negotiating terms and conditions with such broker/dealers. When a client has selected broker/dealers, SCLC is unable to seek better execution services or prices from other broker/dealers, or to consolidate trades at a given broker/dealer across client portfolios so as to obtain more advantageous pricing.

Clients must be informed of these considerations in their initial interviews with SCLC personnel, and annually thereafter via the annual offer of the SCLC Disclosure Brochure. These policies are disclosed in SCLC's Disclosure Brochure, and on Schedule F of Part II of Form ADV, which the Disclosure Brochure restates.

Client broker/dealer selections must be documented, and records of client broker/dealer selections must be retained by SCLC in each client's files.

### **2.3.3 Complaint File**

SCLC must, and does, maintain a record, in the firm's central files, of any and all written or oral client complaints. In the event that such a complaint should ever be received, the record thereof should include the method or status of resolution, any settlement or litigation related to the complaint, and current disposition of the matter.

### **2.3.4 Disaster Recovery**

Records of SCLC's efforts to monitor and maintain systems in a manner that would enable its continuous operation in the event of an unforeseen disaster or other interruption in business shall be maintained and available for review. The file should include evidence of distribution of SCLC's policies to appropriate parties, including advisory representatives and clients. At minimum, the plan should include means for recovery of SCLC's critical systems; restoration or recovery of any permanent record of the firm, such as its organizational documents, employee files and financial records; primary contact information; location and status of back-ups; alternative venue for employees and other systems; and procedures or access codes that might enable SCLC and its clients to regain effective operations.

### **2.3.5 Client/Investor Lists**

Upon regulatory examination, SCLC may be required to produce lists of its clients that, for each client, contain:

- Name
- State of Residence
- Relation to SCLC (includes spouse, dependent, same household, or any client subject to the direct or indirect control of SCLC)
- Type of Account (Fund or Funds in which the client is invested)
- Account establishment date
- Opening balance of account
- Current balance of account (as of most recent quarter end)
- Account redemption date, Balance at the time of redemption, reason for redemption
- Powers of Attorney
- Clients paying performance fees
- Whether the account is subject to ERISA
- Custodian for the account

All such records are maintained in SCLC's client portfolio management database or CRM.

### **2.3.6 Organizational Chart**

SCLC's organizational chart, or supervisory chain of command, should be kept current and complete at all times. The chart should include a reporting structure for each associated person that identifies the primary and secondary supervisors.

### **2.3.7 Privacy Policy**

Regulation S-P and the Federal Trade Commission Privacy of Consumer Financial Information; Final Rule require that SCLC maintain a privacy policy to ensure that nonpublic client data be subject to adequate controls and security. In connection with this Regulation, SCLC is required to distribute a privacy statement at the time of initial investment, and no less than annually thereafter to clients. Details regarding SCLC's privacy policy are provided in a later section of this manual. The Privacy Policy file should contain evidence of the statement's annual distribution to clients

### **2.3.8 Regulatory Inspections**

Documentation related to any regulatory inspection, including documentation of steps taken to remedy findings, shall be maintained in the SCLC's central files.

### **2.3.9 Trade Errors**

Evidence of SCLC's resolution of trade errors shall be maintained in a file kept among the firm's central records. The record for each trade error shall, as a de minimis requirement, include the manner in which the error was resolved, the client and transaction(s) effected by the error, and evidence that an SCLC supervisor was aware of the error and its resolution.

## **2.4 Books and Records Retention**

All SCLC records (except as noted below) must be retained for 5 years in an easily accessible place. The records must remain on the firm's premises for at least 2 years. Additionally, the following must be retained for 3 years beyond the firm's existence as an entity:

- Copies of the original documents filed with the SEC or state securities commission(s)
- Registration letters received from all regulatory agencies
- Organizational Records
- Annual filings (Schedule I)
- Withdrawal notification (Form ADV-W)

### **2.4.1 Electronic Maintenance of Records**

Rule 204-2(g) establishes special requirements for advisers using electronic media for retention of records. SEC Release IA 1945, dated May, 2001, provides further guidance for such retention methods. In general, the following requirements apply when electronic media are used for retention:

- SCLC is required to maintain an index of the records in a way that permits easy location, access and retrieval of any particular record.
- SCLC shall promptly provide a legible, true, and complete copy of the record in the medium and format in which it is stored, as well as the means to view such record. For instance, if stored on CD ROM, the record must be protected from alteration, and any software required to produce a copy of, or to read the record, must be available on the disk. Additionally, SCLC must ensure that electronic records are subject to an appropriate degree of security, including provisions to prevent viewing or access by unauthorized parties. SCLC must ensure that the SEC or other regulatory examiner is granted access to view the records.

## **2.5 Procedures for Compliance with Record-Keeping Policies**

The CCO is responsible for assuring that SCLC has established policies to ensure that its records are maintained in a secure central location, and in a manner consistent with applicable SEC and/or State requirements. Periodically, but no less than annually, SCLC conducts an internal review to ensure that records are maintained in a manner that is compliant with SEC and State regulations, and that ensures documents are retained for an appropriate period of time.

# 3 CODE OF ETHICS AND CONDUCT

As a Registered Investment Adviser, SCLC is by definition a fiduciary. It owes its clients the highest duty of loyalty, and relies on each employee to avoid conduct that is or may be inconsistent with that duty. It is also important for employees to avoid actions that, while they may not actually involve a conflict of interest or an abuse of a client's trust, may have the appearance of impropriety. In the interest of maintaining the highest standards of conduct on the part of all employees, SCLC has adopted a Code of Ethics setting forth policies and procedures, including the imposition of restrictions on itself and employees, to the extent reasonably necessary to prevent certain violations of applicable law. This Code of Ethics and Conduct ("Code") is intended to set forth those policies and procedures and to state SCLC's broader policies regarding its duty of loyalty to clients.

## 3.1 General

Rule 204A-1 requires advisers to establish, maintain and enforce a written code of ethics.

### 3.1.1 Basic Principles

This Code is based on a few basic principles that should pervade all investment related activities of all employees, personal as well as professional:

1. The interests of the clients supersede those of the firm or any of its employees;
2. Each employee's professional activities and personal investment activities must be consistent with this Code, and avoid any actual or potential conflict between the interests of clients and those of SCLC or the employee; and
3. Those activities must be conducted in a way that avoids any abuse of an employee's position of trust with and responsibility to SCLC and its clients, including taking inappropriate advantage of that position.

The Employee understands and agrees that any and all activities of the Employee during the term of this Agreement shall in all respects comply with applicable federal and state securities laws, and other laws, rules and regulations, any applicable laws of foreign jurisdictions, and the firm policies and procedures that have been adopted (or that may in future be adopted) by the Employer ("Firm Policies"), as each may be amended from time to time, including without limitation those prohibiting insider trading and front-running of client accounts.

### 3.1.2 Chief Compliance Officer

Many of the specific procedures, standards, and restrictions described in this Code involve consultation with the Chief Compliance Officer ("CCO"). The CCO will be designated by the SCLC executive committee.

### 3.1.3 Security

For purposes of this Code, the term "securities," insofar as it is used to refer to a financial instruments, is very broad. It includes not only stocks, mutual funds, variable contracts, exchange traded funds, unit investment trusts, and the like, but also options, rights, warrants, futures contracts, convertible securities or

other securities that are related to securities in which SCLC clients may invest or as to which SCLC may make recommendations (sometimes also referred to as "related securities").

### 3.1.4 Covered Accounts

Many of the procedures, standards and restrictions in this Code govern activities in "Covered Accounts." Covered Accounts consist of:

1. Securities accounts of which SCLC is a beneficial owner, provided that (except where the CCO otherwise specifies) investment partnerships or other funds of which SCLC or any affiliated entity is the general partner, investment adviser or investment manager or from which SCLC or such affiliated entity receives fees based on capital gains are generally not considered Covered Accounts, despite the fact that SCLC or employees may be considered to have an indirect beneficial ownership interest in them
2. Each securities account registered in an employee's name and each account or transaction in which an employee has any direct or indirect "beneficial ownership interest" (other than accounts of investment limited partnerships or other investment funds not specifically identified by the CCO as Covered Accounts).

### 3.1.5 Beneficial Ownership

The concept of "beneficial ownership" of securities is broad. It includes not only securities a person owns directly, and not only securities owned by others specifically for his or her benefit, but also (i) securities held by his or her spouse, minor children and relatives who live full time in his or her home, and (ii) securities held by another person if by reason of any contract, understanding, relationship, agreement or other arrangement the employee obtains benefits substantially equivalent to ownership.

**Note:** This broad definition of "beneficial ownership" does not necessarily apply for purposes of other securities laws or for purposes of estate or income tax reporting or liability. An employee may declare that the reporting or recording of any securities transaction should not be construed as an admission that he or she has any direct or indirect beneficial ownership in the security for other purposes.

### 3.1.6 Personal Account Trading and Investment Policy

It is SCLC's policy to impose specific requirements related to each covered person's personal trading and investment activity. The firm shall consider some types of trading, including short term trading and trading in new issues, as inherently constituting a potential conflict of interest. Such trading shall receive particular scrutiny by the CCO. Similarly, SCLC may impose specific requirements related to investments in private placements.

Approval may be refused for any proposed trade by an employee that:

1. Involves a security that is being or has been purchased or sold by SCLC on behalf of any client account, or that is being considered for purchase or sale

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2. Is otherwise prohibited under any internal SCLC policies (such as SCLC's Policy and Procedures to Detect and Prevent Insider Trading)
3. Breaches the employee's fiduciary duty to any client
4. Is otherwise inconsistent with applicable law, including Advisers Act and the Employee Retirement Income Security Act of 1974, as amended
5. Creates an appearance of impropriety

The Procedures section shall address SCLC's specific procedures for these types of investments and trading.

### **3.1.7 Service as a Director**

No SCLC employee may serve as a director of a publicly-held company without prior approval by the CCO (or a senior principal, if the CCO is the proposed board member) based upon a determination that service as a director would not be adverse to the interests of any client. In the few instances in which such service is authorized, employees serving as directors shall be isolated from other employees who are involved in making decisions as to the securities of that company, through procedures determined by the CCO to be appropriate in the circumstances. These practices may also constitute illegal "insider trading." Some of the specific trading rules described below are also intended, in part, to prevent front running and scalping. If an account is managed by an investment adviser, other than SCLC, to which full investment discretion has been granted, these rules will not apply for so long as the employee(s) who has (have) a beneficial ownership interest in the account do not have or exercise any discretion. Such accounts will remain subject to the reporting requirements set forth in the next section of this Code.

### **3.1.8 Gifts**

The receipt or giving of any gift of more than nominal value (\$100/year) from any person or entity that does business with or on behalf of any client is prohibited.

### **3.1.9 Duties of Confidentiality**

All information relating to client portfolios and activities, and to proposed recommendations, is strictly confidential. Consideration of a particular purchase or sale for a client account may not be disclosed, except to authorized persons.

### **3.1.10 General Ethical Conduct:**

The following are potentially compromising situations that must be avoided:

- Causing SCLC, acting as principal for its own account or for any account in which SCLC or any person associated with SCLC (within the meaning of the Investment Advisers Act) to sell any security to or purchase any security from a client in violation of any applicable law, rule or regulation of a governmental agency
- Communicating any information regarding SCLC, SCLC's investment products or any client to prospective clients, journalists, or regulatory authorities that is not accurate, is untrue, or that omits a material fact necessary in order to make the statements SCLC has made to such person

- Engaging in any act, practice, or course of business that is fraudulent, deceptive, or manipulative, particularly with respect to a client or prospective client
- Engaging in any conduct that is not in the best interest of the firm, or which might appear to be improper
- Engaging in any financial transaction with any of SCLC's vendors, clients or employees, including but not limited to:
  - ◆ Providing any rebate, directly or indirectly, to any person or entity that has received compensation from SCLC;
  - ◆ Accepting, directly or indirectly, from any person or entity, other than SCLC, compensation of any nature such as a bonus, commission, fee, gratuity or other consideration in connection with any transaction on behalf of SCLC;
  - ◆ Beneficially owning any security of, or having, either directly or indirectly, any financial interest in, any other organization engaged in securities, financial or related business, except for beneficial ownership of not more than one percent (1%) of the outstanding securities of any business that is publicly traded
- Engaging in any form of harassment
- Improperly using or authorizing the use of any inventions, programs, technology or knowledge that are proprietary to SCLC
- Investing or holding outside interests or directorships in clients, vendors, customers or competing companies, including financial speculations, where such investment or directorship might influence in any manner a decision or course of action of SCLC. In the limited instances in which service as a director is authorized by SCLC, employees serving as directors shall be isolated from other employees who are involved in making decisions as to the securities of that company through procedures determined by SCLC to be appropriate according to the circumstances
- Making any unlawful agreement with vendors, existing or potential investment targets or other organizations.
- Making any untrue statement of a material fact or omitting to state to any person a material fact necessary in order to make the statements SCLC has made to such person materially complete
- Participation in civic or professional organizations that might involve divulging confidential information of the company.
- Unlawfully discussing trading practices, pricing, clients, research, strategies, processes or markets with competing companies or their employees
- Using any device, scheme or artifice to defraud, or engaging in any act, practice, or course of conduct that operates or would operate as a fraud or deceit upon, SCLC, any client or prospective client, or any party to any securities transaction in which SCLC or any of its clients is a participant.

## 3.2 Insider Trading

SCLC has organized itself and its client service offerings in such a way as to minimize employee opportunities for insider trading. For example, the firm's client portfolios are invested almost exclusively in pooled investment vehicles of one kind or another, and SCLC does not issue recommendations or opinions regarding individual stocks. Because the firm does not recommend individual stocks, it does not engage in stock research. Finally, the firm does not offer any investment banking services. As a result, firm employees generally do not, as a consequence of their activities as employees, ever come into possession of insider information.

Nevertheless it is conceivable that employee insider trading could occur. Accordingly, SCLC has adopted the following policies and procedures to detect and prevent the misuse of material, non-public information

by its employees.

### **3.2.1 Policy Statement on Insider Trading**

SCLC forbids any officer, director or employee from trading, either personally or on behalf of others, on material nonpublic information or communicating material nonpublic information to others in violation of the law. This conduct is frequently referred to as "insider trading." SCLC's policy applies to every officer, director and employee and extends to activities within and outside their duties at SCLC. Each officer, director and employee must read this policy statement and acknowledge his or her understanding of it. Any questions regarding SCLC's policy and procedures should be referred to the CCO.

The term "insider trading" is not defined in the federal securities laws, but generally is used to refer to the use of material nonpublic information to trade in securities (whether or not one is oneself an "insider") or to communications of material nonpublic information to others.

While the law concerning insider trading is not static, it is generally understood that the law prohibits the following:

- Trading by an insider while in possession of material non-public information
- Trading by a non-insider, while in possession of material non-public information, where the information either was disclosed to the non-insider in violation of an insider's duty to keep it confidential or was misappropriated
- Communicating material nonpublic information to others in violation of one's duty to keep such information confidential.

### **3.2.2 Who Is An Insider?**

The concept of an "insider" is broad. It includes officers, directors and employees of a company. In addition, a person can be a "temporary insider" if he or she enters into a special confidential relationship in the conduct of a company's affairs and as a result is given access to information solely for the company's purposes. A temporary insider can include certain "outsiders" such as, among others, a company's attorneys, accountants, consultants, bank lending officers, and the employees of such organizations. According to the United States Supreme Court, before such an "outsider" may be considered a "temporary insider", the company's relationship with the outsider must be such that the company reasonably expects him or her to keep the disclosed nonpublic information confidential.

### **3.2.3 What Is Material Information?**

While covered persons are prohibited from trading on inside information, trading on inside information is not a basis for liability unless the information is "material." Information generally is material if there is a substantial likelihood that a reasonable client/investor would consider it important in making his or her investment decisions, or if public dissemination of the information is reasonably certain to have a substantial effect on the price of a company's securities. Information that should be presumed to be material includes, but is not limited to: dividend changes; earnings estimates; changes in previously released earnings estimates; significant merger or acquisition proposals or agreements; commencement of or developments in major litigation; liquidation problems; and extraordinary management developments.

Questions one might ask in determining whether information is material include:

- Is this information that an investor would consider important in making investment decisions? Is this information that would substantially affect the market price of the securities if generally disclosed?
- Is the information non-public? To whom has this information been provided? Has the information been effectively communicated to the marketplace by being published in a recognized national distribution agency or publication such as Reuters, *The Wall Street Journal* or other such widely circulated publications?

Caution must be exercised however, because material information need not necessarily relate to a company's business. The Supreme Court of the United States has broadly interpreted materiality in some cases, and has asserted criminal liability associated with inappropriate disclosures.

### 3.2.4 What Is Nonpublic Information?

Information is nonpublic until it has been effectively communicated to the market place. One must be able to point to some fact to show that the information is generally public. For example, information found in a report filed with the Securities and Exchange Commission, or appearing in Dow Jones, Reuters Economic Services, *The Wall Street Journal* or other publications of general circulation would be considered public.

### 3.2.5 Types of Liability

Actions by the U.S. courts, including the Supreme Court, have resulted in findings that assert liability to fiduciaries in the context of trading on material non-public information. In some cases it has been found that a non-insider can enter into a confidential relationship with the company through which they gain information, or can acquire a fiduciary duty to the company's shareholders as "tippees" if they are aware or should have been aware that they have been given confidential information by an insider who has violated his fiduciary duty to the company's shareholders. This is a circumstance into which an associate of SCLC may fall.

In the "tippee" situation, a breach of duty occurs only if the insider personally benefits, directly or indirectly, from the disclosure. It is important to note that the benefit does not have to be monetary; it can be a gift, and can even be a 'reputational' benefit that will translate into future earnings. Another basis for insider trading liability is the "misappropriation" theory, where trading occurs on material non-public information that was stolen or misappropriated from any other person. This theory can be used to apply liability to individuals not previously thought to be encompassed under the fiduciary duty theory.

## 3.3 Penalties for Insider Trading

Penalties for trading on or communicating material nonpublic information are severe, both for individuals involved in the trading (or tipping) and their employers. A person can be subject to some or all of the penalties below even if he or she does not personally benefit from the violation. Penalties include:

- Civil injunctions
- Damages in a civil suit as much as three times the amount of actual damages suffered by other buyers or sellers

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- Disgorgement of profits
- Jail sentences
- Fines for the person who committed the violation of up to three times the profit gained or loss avoided, whether or not the person actually benefited, and
- Fines for the employer or other controlling person of up to the greater of \$1,000,000 or three times the amount of the profit gained or loss avoided
- Prohibition from employment in the securities industry

In addition, any violation of this policy statement can be expected to result in serious disciplinary measures by the adviser, including dismissal of the persons involved.

### 3.4 Procedures for Compliance with Code of Ethics

All employees are covered by SCLC's Code of Ethics. In the following procedures, all employees shall be referred to as "covered persons."

The CCO shall assume responsibility for maintaining, in an accessible place, the following materials:

1. Copy of this Code of Ethics
2. Record of any violation of these procedures for the most recent five years, and a detailed synopsis of the actions taken in response
3. Copy of each transaction report submitted by each officer, director and employee of SCLC for the most recent five years
4. List of all persons who are or have been required to file transaction reports.

In an effort to prevent insider trading, either directly or through delegation to qualified covered persons under his or her supervision, the CCO will:

1. Answer employee questions and document responses regarding SCLC's policy and procedures
2. Provide, on a regular basis (no less than annually), an educational program to familiarize covered persons with SCLC's policy and procedures
3. Require each employee annually to acknowledge receipt of and agreement to comply with SCLC policy and procedures regarding insider trading
4. Retain such acknowledgements among SCLC's central compliance records
5. Resolve questions of whether information received by an SCLC employee is material and non-public, and document findings
6. Review on a regular basis and update as necessary SCLC's policy and procedures, and document any resulting amendments or revisions
7. When it is determined that an SCLC employee possesses material non-public information, implement measures to prevent dissemination of such information, and if necessary, restrict covered persons from trading in relevant securities

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In an effort to detect insider trading, either directly or through delegation to qualified covered persons under his or her supervision, the CCO will:

1. Review the trading activity reports filed by each SCLC officer, director, and employee, documenting findings by initialing and dating the forms or reports reviewed
2. Review the duplicate confirmations and statements and related documentation of personal and related accounts maintained by officers, directors and covered persons versus the activity in client accounts supervised by SCLC.
3. Require officers, directors and covered persons to submit periodic reports of personal trading activity, and to attest to the completeness of each individual's disclosure of outside accounts at the time of hiring and at least annually thereafter

To determine whether SCLC Covered Persons have complied with the rules described above (and to detect possible insider trading), such persons must provide the CCO with access to statements of Covered Accounts, so that the CCO can review transactions effected in Covered Accounts within 30 days after the end of each month, and can review duplicate trade confirmations provided pursuant to those rules within 10 days after their receipt. The CCO will compare transactions in Covered Accounts with transactions in client accounts for transactions or trading patterns that suggest violations of this Policy or potential front running, scalping, or other practices that constitute, or could appear to involve, abuses of Covered Persons' positions. Each Covered Person must annually certify that he or she has read and understands this Code, that he or she recognizes that this Code applies to him or her, and that he or she has complied with all of the rules and requirements of this Code that apply to him or her. The CCO is charged with responsibility for collection, review, and retention of the certifications submitted by Covered Persons.

Although Covered Persons are not prohibited under this policy from trading securities for their own accounts at the same time that they are involved in trading on behalf of SCLC, they must do so only in full compliance with this Policy and their fiduciary obligations. At all times, the interests of SCLC's clients must supersede the Covered Person's interest. No trades or trading strategies used by a Covered Person may conflict with SCLC's investment strategies. SCLC's Covered Persons may not use SCLC's proprietary trading strategies to develop or implement new strategies that might otherwise redound to the disadvantage either of SCLC or its clients. Personal account trading must be executed on the Covered Person's own time, without placing undue burden on SCLC's time. No transactions should be undertaken that are unsuitable, given the financial resources of the Covered Person.

No Covered Person may purchase or sell any non-exempt security for any Covered Account without first obtaining prior approval from the CCO. In the case of the CCO's own personal request to purchase or sell a non-exempt security, another officer of the firm shall render prior approval. For purposes of this Policy, the term "exempt securities" means:

- Securities that are direct obligations of the US Government or other foreign sovereignties
- Instruments derived from indices
- Mutual funds
- Exchange-traded funds
- Securities traded in accounts over which an employee does not exercise any investment discretion.

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It is the Covered Person's obligation to ensure that pre-clearance requests are provided to the CCO. The CCO may take any and all steps deemed appropriate in rendering or denying approval of the proposed trade. In the event that the CCO is not accessible, all pre-clearance requests will be forwarded directly to another officer of the firm. NO action may be taken until approval is attained. Pre-clearance authorization for a transaction is only valid for the day on which the approval is granted. If the transaction is not completed that day, the Covered Person must have the proposed transaction approved again. This requirement applies to transactions involving open market orders and limit or other types of orders.

No employee may purchase and subsequently sell a security within any thirty (30) day period, unless such a sale is approved in writing by the CCO. Each determination shall be made on a case-by-case basis. The CCO shall have the sole authority to grant or withhold permission to execute trades.

No employee may purchase new publicly offered issues of any securities ("New Issue Securities") for any Covered Account in the public offering of those securities without the prior written consent of the CCO.

Each Covered Person must, at the onset of employment and immediately following subsequent events involving the acquisition of securities (marriage, inheritance, etc.), disclose to the CCO the identities, amounts, and locations of all securities he or she owns. **On an annual basis, each employee is required to confirm the location of all Covered Accounts. In all cases, duplicate statements and trade confirmations must be sent directly to the CCO from the custodian.** All statements of holdings, duplicate trade confirmations, duplicate account statements, and monthly and quarterly reports will generally be held in confidence by the CCO. However, the CCO may provide access to any of those materials to other members of SCLC's management in order to resolve questions regarding compliance with this Policy and regarding potential purchases or sales for client accounts, and SCLC may provide regulatory authorities with access to those materials where required to do so under applicable laws, regulations, or orders of such authorities.

## 4 ANTI-MONEY LAUNDERING

In response to the September 11, 2001 attacks on America, On October 26, 2001, President Bush signed into law the USA PATRIOT Act. Title III of the USA PATRIOT Act, entitled the "International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001" (the Act), requires all "financial institutions" to establish an anti-money laundering program by April 24, 2002. In particular Section 352 of the USA PATRIOT Act states that each financial institution must establish an anti-money laundering program that includes at a minimum:

- Development of internal policies, procedures and controls
- Designation of a compliance officer ("AML CO")
- Ongoing employee training program

Although SCLC understands as of this writing that compliance with the Act is not yet mandated for SEC-covered investment advisers or for State registered advisers, SCLC has determined that it will voluntarily comply. In compliance with existing regulations, SCLC has:

- Established and implemented policies and procedures that can be reasonably expected to detect and cause the reporting of transactions that raise a suspicion of money laundering
- Established and implemented policies, procedures and internal controls reasonably designed to achieve compliance with the Bank Secrecy Act and regulations thereunder
- Designated an individual or individuals responsible for implementing and monitoring the day-to-day operations and internal controls of the program
- Provided, and will continue to provide, ongoing training for appropriate personnel
- Provided for compliance testing by SCLC personnel or a qualified outside party on a regular schedule but no less than annually.

SCLC is committed to the goals of the USA PATRIOT ACT. Further, anti-money laundering compliance is the responsibility of every associated person, and any associated person who detects activity that seems to be suspicious is hereby instructed to report such activity to the CCO. The responsibility of associated persons to participate in the AML Compliance Program is reinforced through training, no less frequently than annually, and through ongoing oversight performed by or at the instruction of the CCO.

SCLC will periodically update its AML Policies and Procedures to conform to regulatory changes and firm growth. SCLC will continue to seek guidance from the Department of Treasury, SEC and others regarding effective AML Policies and Procedures.

### 4.1 Definition

Money laundering is engaging in acts designed to conceal or disguise the true origins of criminally derived proceeds, so that the unlawful proceeds appear to have been derived from legitimate origins, or to constitute legitimate assets. Generally, money laundering occurs in three stages. Cash first enters the financial system

at the "placement" stage, where the cash generated from criminal activities is converted into monetary instruments, such as money orders or traveler's checks, or deposited into accounts at financial institutions. At the "layering" stage, the funds are transferred or moved into other accounts or other financial institutions to further separate the money from its criminal origin. At the "integration" stage, the funds are reintroduced into the economy and used to purchase legitimate assets or to fund other criminal activities or legitimate businesses. Terrorist financing may not involve the proceeds of criminal conduct, but rather an attempt to conceal the origin or intended use of the funds, which will later be used for criminal purposes.

In addition, money laundering may include

1. Willfully ignoring ("willful blindness") the source of a client's assets or the nature of client transactions
2. Failing to report suspected money laundering activities
3. Failing to maintain required records of transactions.

In order to hide and transfer assets, money launderers require the intentional or unintentional assistance of an associated person or a financial institution.

In response to the USA PATRIOT ACT, SCLC has adopted the following policies and procedures, which are to be followed by every associated person of the firm.

## 4.2 Due Diligence

SCLC and its senior management are firmly committed to the Act. It is SCLC's policy to prohibit and actively prevent money laundering and any activity that facilitates money laundering in support of terrorist or criminal activities. Accordingly, SCLC requires a corresponding commitment by its associated personnel, irrespective of job duty or assignment. SCLC requires every associated person to diligently protect SCLC from exploitation by money launderers. If such exploitation were to succeed, SCLC and its associated persons could be subject to civil, criminal and disciplinary action, and irreparable harm to their reputation.

The purpose of SCLC's AML policies and procedures is to:

1. Uphold the law
2. Protect SCLC and its associated persons from those who would misuse SCLC facilities and resources
3. Safeguard SCLC and its associated persons from the appearance of impropriety and from the violation of anti-money laundering laws
4. Maintain SCLC's high level of service and responsiveness to clients and counter-parties, without undue disruption or inconvenience.

## 4.3 AML Compliance Officer

SCLC hereby assigns an individual, noted at the end of this chapter, as SCLC's AML Compliance Officer ("AML CO"). The AML CO will implement SCLC's AML Policies and Procedures. The AML CO must ensure appropriate firm personnel attend periodic AML training. Firm personnel should contact the AML

CO if they have any questions regarding SCLC's AML Policies and Procedures or how to implement them. The AML CO will ensure the accuracy of third party reports on which SCLC relies in complying with these policies and procedures. The AML CO will ensure that Suspicious Activity Reports (SAR-SFs) are filed when necessary. SCLC will provide the appropriate regulator with the AML Compliance Officer's contact information, including name, title, mailing address, email address, telephone number and facsimile number, provided an electronic facility is available for such notification.

Because the relationship between SCLC and custodians of SCLC client assets may divide or overlap responsibilities related to AML, causing complication or confusion regarding SCLC's AML Policies and Procedures implementation, SCLC maintains ongoing communication with custodians regarding the AML responsibilities of each entity.

The AML CO is responsible for knowing about and procuring any and all available reports that may be utilized in connection with these procedures.

## 4.4 Associated Person Awareness and Training

Periodically, SCLC requires associated persons to acknowledge receipt of these procedures, on a schedule the AML CO deems to be appropriate. SCLC shall establish a training program to include periodic training related to AML.

## 4.5 Client/Investor Identification Program

SCLC has implemented a Client Identification Program ("CIP") to ensure that the firm and its associated persons can form a reasonable belief that they know the true identity of each individual accepted as a client. Further, the CIP shall ensure that SCLC and its associated persons know the identity of individuals underlying any entity that is accepted as a client. Underlying the CIP is the policy that requires that the AML CO be involved in the acceptance of each and every new client.

SCLC will verify the identity of each of the following:

- New clients and persons to whom any client grants investment authority
- Existing clients for whom SCLC has not previously checked the identity, and those granted investment authority subsequent to any initial investment
- Any clients whose identity the AML CO deems should be verified.

Prior to opening an account, associated persons must obtain from the client/investor the following:

- Client's name
- For an individual client, the date of birth
- An address, which may be:
  - ◆ For an individual, a residential or business street address - note that a Post Office Box or Rural Free Delivery number does not satisfy this requirement
  - ◆ For an individual who does not have a residential or business street address, an Army Post

- Office (APO) or Fleet Post Office (FPO) box number, or the residential or business street address of next of kin or another contact individual; or
- ◆ For a person other than an individual (such as a corporation, partnership, or trust), a principal place of business, local office, or other physical location
- An identification number, which may be:
  - ◆ For a U.S. person:
    - ◇ Taxpayer identification number
    - ◇ Drivers license number
    - ◇ U.S. Passport number
    - ◇ State identification number
  - ◆ For a non-U.S. person:
    - ◇ U.S. Taxpayer Identification Number
    - ◇ Passport number and country of issuance
    - ◇ Alien identification card number
    - ◇ Number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photograph or similar safeguard

#### 4.5.1 ID Verification

SCLC will determine what and how much identification it will require a client to provide, based on SCLC's perceived client risk. SCLC will determine client risk using the following factors, among others at the discretion of the AML CO:

- Types of identifying information available about the client or parties associated with the client
- Input by qualified third parties, such as the custodian, fund Administrator, or other such counter-party

SCLC will verify the client's identity within a reasonable time before it opens the client account. SCLC will use documentary, non-documentary, or a combination of both methods to verify client identities.

#### 4.5.2 Documentary Verification

To verify client identity, SCLC will use the following documents (or others, depending upon the perceived client risk):

- For an individual, an unexpired government-issued identification evidencing nationality or residence and bearing a photograph or similar safeguard, such as a driver's license or passport
- For a person other than an individual (such as a corporation, partnership, or trust), documents showing the existence of the entity, such as certified articles of incorporation, a government-issued business license, a partnership agreement, or a trust instrument

In certain instances, SCLC's subscription or other account opening documents may require that the client:

1. Represent and covenant that all evidence of identity provided is genuine and all related information furnished is accurate

2. Agree to provide any information deemed necessary by SCLC, in its sole discretion, to comply with its anti-money laundering responsibilities and policies
3. Represent that it is investing solely as principal, and not for the benefit of any third parties.

### **4.5.3 Non-Documentary Verification**

SCLC will use the following non-documentary methods and others based on the perceived risk to verify client's identity:

- Contacting the client
- Independently verifying the client's identity through the comparison of information provided by the client with information obtained from a consumer reporting agency, public database, or other source
- Checking references with other financial institutions
- Obtaining a financial statement

SCLC will use this information to determine whether there is a logical consistency between the client's identifying information, such as name, street address, zip code, telephone number, date of birth, and Taxpayer Identification Number.

### **4.5.4 Special Situations**

If a client or potential client is unable to present an unexpired government-issued identification document that bears a photograph or similar safeguard, SCLC will attempt to use other documentary and non-documentary methods to verify the person's identity.

If SCLC is unfamiliar with the documents the client presents, SCLC will verify the authenticity of the document, or use other methods to verify the person's identity.

If SCLC opens a client account without obtaining the required documents, SCLC will discontinue transacting business for the client until SCLC obtains identifying information.

If SCLC opens the client account without the client having appeared in person, SCLC will use documentary and non-documentary verification methods as stated above.

Until SCLC verifies the client's identity, SCLC will determine whether each transaction is appropriate without client identity verification. If SCLC fails to verify the client's identity, it will close the client's account, and not reopen the account until it positively identifies the client. If SCLC suspects that clients are not who they purport to be, SCLC will not open accounts on those clients's behalf, and SCLC will file a suspicious activity report in accordance with the SAR section of these policies and procedures.

### **4.5.5 Clients/Investors Who Refuse to Provide Information**

If a potential or existing client either refuses to provide the information described above when requested, or appears to have intentionally provided misleading information, SCLC will not transact business for the client and, after considering the risks involved, SCLC will consider closing any existing account. In either case, the AML CO will be notified, so that a determination can be made regarding reporting the situation to

FinCEN by filing a Form SAR-SF. The AML CO shall be the final determinant of the client's status with respect to AML verification.

#### **4.5.6 Government List Comparison**

SCLC will verify within a reasonable time after the client opens an account, or earlier if Federal law, regulation or directive requires, that the client does not appear on any list of known or suspected terrorist or terrorist organization. SCLC will follow all Federal directives issued in connection with such lists.

On an ongoing basis, SCLC will check the Federal Office of Foreign Assets Control ("OFAC") list to ensure that, before transacting any business with them, potential clients and existing clients are not prohibited persons or entities, and are not from embargoed countries or regions.

From time to time, SCLC may receive notice that a Federal government agency has issued a list of known or suspected terrorists. Within a reasonable period of time after an account is opened (or earlier, if required by another Federal law or regulation or Federal directive issued in connection with an applicable list), SCLC will determine whether a client appears on any such list of known or suspected terrorists or terrorist organizations issued by any Federal government agency and designated as such by Treasury in consultation with the Federal functional regulators. SCLC will follow all Federal directives issued in connection with such lists.

SCLC will continue to comply with Treasury's Office of Foreign Asset Control rules prohibiting transactions with certain foreign countries or their nationals.

#### **4.5.7 FinCEN Requests Under PATRIOT Act Section 314**

Under Treasury's final regulations (published in the Federal Register on September 26, 2002), SCLC responds to a Financial Crimes Enforcement Network (FinCEN) request about accounts or transactions by immediately searching our records, at our head office or at one of our branches operating in the United States, to determine whether we maintain or have maintained any account for, or have engaged in any transaction with, each individual, entity, or organization named in FinCEN's request. Upon receiving an information request, the AML CO will designate one person to be the point of contact regarding the request and to receive similar requests in the future. Unless otherwise stated in FinCEN's request, we are required to search current accounts, accounts maintained by a named suspect during the preceding 12 months, and transactions conducted by or on behalf of or with a named subject during the preceding six months. If SCLC finds a match, SCLC will report it to FinCEN by completing FinCEN's subject information form. This form can be sent to FinCEN by electronic mail at [sys314a@fincen.treas.gov](mailto:sys314a@fincen.treas.gov), or by facsimile transmission to 703-905-3660. If the search parameters differ from those mentioned above (for example, if FinCEN requests longer periods of time or limits the search to a geographic location), SCLC will limit its search accordingly.

If SCLC searches its records and does not uncover a matching account or transaction, then SCLC will not reply to a 314(a) request.

SCLC will not disclose the fact that FinCEN has requested or obtained information, except to the extent necessary to comply with the information request. SCLC will maintain procedures to protect the security and confidentiality of requests from FinCEN, such as those established to satisfy the requirements of Section 501 of the Gramm-Leach-Bliley Act.

SCLC will direct any questions it has about the request to the requesting Federal law enforcement agency as

designated in the 314(a) request.

Unless otherwise stated in the information request, SCLC will not be required to treat the information request as continuing in nature, and SCLC will not be required to treat the request as a list for purposes of the fund clients identification and verification requirements. SCLC will not use information provided to FinCEN for any purpose other than:

1. To report to FinCEN as required under Section 314 of the PATRIOT Act
2. To determine whether to establish or maintain an account, or to engage in a transaction
3. To assist the firm in complying with any requirement of Section 314 of the PATRIOT Act.

## **4.6 Acceptable Types of Clients/Investors**

Generally SCLC will accept the following types of clients, subject to the final review and acceptance of the AML CO.

### **4.6.1 Individual Clients/Investors**

At minimum, SCLC will obtain the client's:

- Name and address
- Date of birth
- Investment experience and objectives
- Tax Identification Number
- Occupation, tenure, employer's address, and annual income
- Names of all persons authorized to trade on the account.

### **4.6.2 Confidential Accounts**

SCLC will keep client identities confidential, except as limited by the firm's Privacy Policy, or by operation of regulation or law.

### **4.6.3 Corporations, Partnerships and Comparable Legal Entities**

In order to confirm the identity of a legal entity, SCLC will obtain satisfactory evidence of its name, address, and authority to make the contemplated investment decisions. Where the client is neither a publicly traded company listed on a major, regulated exchange (or a subsidiary or a pension fund of such a company), nor a regulated institution organized in a FATF-Compliant Jurisdiction, SCLC may wish to gain additional comfort regarding the client identity by obtaining certain of the following, as appropriate under the circumstances:

- Evidence that the client has been duly organized in its jurisdiction of organization

- If SCLC believes it would be reasonable to rely upon a certification from the client, a certification ("AML Certificate") from the client that it has implemented and complies with anti-money laundering policies, procedures and controls that, for example, seek to ensure that none of its directors, officers or equity holders are prohibited clients, as set forth in a certificate or other list.

#### **4.6.4 Domestic Operating or Commercial Entities**

SCLC serves as investment consultant to numerous Qualified Retirement Plans and similar retirement programs. These retirement programs may be sponsored by publicly traded or privately held companies, by not-for-profit agencies or by governmental entities. The retirement programs are generally funded through a tax-qualified trust, with assets held in custody by a federally regulated institutional trustee.

For Qualified Retirement Plan engagements where all Plan assets are held in custody through a federally regulated institutional trustee, SCLC shall rely on the trustee's efforts to confirm the business identity of the sponsoring organization. SCLC plays no role in opening or establishing these accounts. Occasionally, SCLC may help Qualified Retirement Plan sponsors establish trust accounts through one of SCLC's custodial partners. In such cases, SCLC shall confirm the sponsor's identity by obtaining certified copies of the sponsoring organization's articles of incorporation or similar documents, and shall document the existence of the trust by obtaining executed copies of the Plan's trust agreement.

For all accounts held directly by commercial entities, SCLC shall verify the business identity and verify that the person investing has authority to transact investment business.

#### **4.6.5 Domestic Trusts**

For all domestic trusts, SCLC will identify the principal owner of the trust and confirm that the individual establishing the investment has authority to transact business on behalf of the trust. At the discretion of the AML CO, SCLC may accept evidence of the trustee's authority to make the contemplated investment decisions in the form of either an AML Certificate from the trustee, or the identities of beneficiaries, the provider of funds (e.g., settlor(s)), those who have control over funds (e.g., trustee(s)) and any persons who have the power to remove trustees.

#### **4.6.6 Electronic or Internet Accounts**

SCLC will not accept any account opening documents submitted electronically from clients otherwise unknown to the firm, and does not open or accept internet accounts.

#### **4.6.7 Foreign Operating Commercial Entities**

In determining whether SCLC will open a foreign operating commercial entity account, SCLC will consider the client's country of incorporation and primary business location jurisdiction. SCLC will not open an account for a foreign shell bank without a domestic affiliated institution. Upon written notice from the U.S. Treasury that one of SCLC's clients is a foreign bank or foreign operating commercial entity that has not responded to the U.S. Treasury's request for information, SCLC will terminate the account within ten (10) days.

#### **4.6.8 Intermediary Accounts (Other Hedge Funds, Investment Funds, Institutional Accounts)**

Establishing intermediary accounts, where another financial institution such as a bank or investment advisor opens an advisory account at SCLC which is registered to, and for the benefit of, one of its clients, may require SCLC to obtain more or less information before establishing the account. SCLC may request more information when it cannot determine the client's investment objective. SCLC may request less information if the client is deemed sophisticated. The AML CO will determine, on a case-by-case basis, how much information SCLC will require from such clients when establishing accounts. The AML CO may consider the following factors:

- Whether the intermediary has a long term relationship with SCLC
- Public reputation of the intermediary
- Whether the institution is from a jurisdiction generally characterized as an offshore banking or secrecy haven, non-cooperative country, or of other suspicious nature.

#### **4.6.9 Non-Resident Alien Accounts**

In addition to resident requirements, SCLC must obtain from non-resident alien clients a current passport number or other valid government ID number, and any necessary U.S. tax forms.

#### **4.6.10 Offshore Trusts**

SCLC does not open offshore trust accounts.

#### **4.6.11 Omnibus Accounts**

For omnibus accounts and sub-accounts established by financial intermediaries, the AML CO must verify the identity of the accountholder. The AML CO does not need to verify the identities of any beneficial owners since they are not considered to be clients of SCLC.

#### **4.6.12 Foreign Nationals**

When opening an account for a foreign national, SCLC will require the client to complete a Foreign Accounts Consent to Service of Process form similar to the attached example and check the appropriate box of the state of residence or the primary state where the client (if a corporation or other business organization) is doing business. By completing this form, a foreign national client becomes subject to the laws of the United States.

### **4.7 Prohibited Clients/Investors**

SCLC will not accept an investment from or on behalf of the following:

- Any client (a "Listed Client") whose name appears on the List of Specially Designated Nationals and Blocked Persons maintained by the U.S. Office of Foreign Assets Control ("OFAC") or such other lists of prohibited persons and entities as may be mandated by applicable law or regulation
- Foreign Shell Bank (with respect to clients that are Foreign Banks, SCLC may wish to consider obtaining a representation that the bank either (1) has a Physical Presence; or (2) does not have a physical presence, but is a regulated affiliate.)
- Senior Foreign Political Figure, any member of a Senior Foreign Political Figure's Immediate Family, and any Close Associate of a Senior Foreign Political Figure
- Any client resident in, or organized or chartered under the laws of, a Non-Cooperative Jurisdiction
- Any client resident in, or organized or chartered under the laws of, a jurisdiction that has been designated by the Secretary of the Treasury under Section 311 or 312 of the USA PATRIOT Act as warranting special measures due to money laundering concerns
- Any client who gives SCLC reason to believe that its investment funds originate from, or are routed through, an account maintained at an "offshore bank", or a bank organized or chartered under the laws of a non-cooperative jurisdiction
- Any client who gives SCLC reason to believe that the source of its investment funds may not be legitimate.

## 4.8 Suspicious Transactions and Activity

SCLC will monitor its account activity to identify patterns of unusual size, volume, pattern or type of transactions, geographic factors such as whether jurisdictions designated as "non-cooperative" are involved, or any other "red flags." SCLC will review transactions, including trading and wire transfers, in the context of other account activity to determine if a transaction lacks financial sense or is suspicious because it is an unusual transaction or strategy for that client. The AML CO is responsible for monitoring, documenting, and reporting this activity to the appropriate authorities. SCLC will submit Suspicious Activity Reports (SARs) for suspicious client activity when opening accounts and when transacting business.

### 4.8.1 Suspicious Activity at Initial Investment

At the inception of any supervisory account, associated persons should report suspicious activities such as the following to the AML CO:

- Client has a suspicious background or originates from a suspicious area
- Client exhibits reluctance to provide pertinent information related to source of investment funds, business background or other information
- Client expresses objections to SCLC's compliance procedures, restrictions, disclosures or other practices
- Client appears to be acting as an agent for an undisclosed principal, but declines or is reluctant, without legitimate commercial reasons, to provide information or is otherwise evasive regarding that person or entity
- Client is from, or has accounts in, a country identified as a non-cooperative country or territory by the FATF
- Client cannot describe in reasonable terms the nature of his or her business or investment experience
- Client cannot adequately document appropriate authority for the account
- Client wishes to engage in investments that are inconsistent with the client's apparent investment

strategy

- Client (or a person publicly associated with the client) is the subject of news reports indicating possible criminal, civil or regulatory violations.

## 4.8.2 Transactions

If at any time in the life of a supervisory account, an associated person observes suspicious client activities such as the following, he or she should report them to the AML CO:

- Cash - i.e., currency - transactions in excess of \$10,000
- Transactions that may be structured to fall just below such reporting thresholds
- Wire transfers, journals or cash transactions that have no apparent investment purpose, especially if conducted among countries considered to be tax or bank secrecy havens
- Where brokerage account activity is limited to cash and cash equivalents
- Any significant deposit initially earmarked for investment which is subsequently or suddenly subject to a client request for withdrawal
- Multiple accounts for the same individual where there is no apparent reason for separate accounts
- Customer activity limited to investments often utilized in connection with fraudulent schemes and money laundering, such as "Reg. S" stocks, bearer bonds, penny stocks, etc.
- Deposit of bearer bonds with immediate subsequent request for liquidation
- Investment activity not affected by any apparent consideration of risk, return or other performance
- Sudden change in activity, especially wire activity, in an account previously not active
- Where deposits and withdrawals to the account appear to be well beyond the financial means, income or resources of the client.

## 4.8.3 Reporting Suspicious Initial Investment Activity

Any associated person who detects suspicious client activity must immediately notify the AML CO. Such reports must be made whether or not a supervisory account is opened, or any transaction is consummated. Following the initial report, the AML CO, at his or her discretion, will take one of the following actions:

- Notify SCLC's CCO, general counsel or other legal representative
- File a Suspicious Activity Report, using Form SAR-SF (any such filing is to remain confidential, and SCLC may not disclose the filing to any person involved in the transaction or with the account)
- Contact state or federal authorities, as required
- Other action the AML CO deems appropriate

SCLC will contact Federal Law Enforcement immediately if it determines that:

1. A client is on the OFAC list;
2. A client's legal or beneficial account owner is listed on the OFAC list; or
3. A client attempts to bribe, coerce, unduly influence, or take any other inappropriate action to open an account or proceed with a suspicious or unlawful activity or transaction.

The AML CO will record each reported instance in SCLC's Suspicious Activity log.

The AML CO will investigate all reported suspicious activities. To the best of his or her ability the AML CO will freeze the account of any client subject to such a report during the investigation, so as to prevent further activity (such as a wire or redemption) in the account. The AML CO shall maintain confidentiality with respect to each and every reported incident of suspicious activity.

## 4.9 Suspicious Activity Related to Transactions

The AML CO will file form SAR-SF for any attempted or conducted account activity where SCLC knows, suspects, or has reason to suspect one or more of the following:

- The transaction involves funds derived from illegal activity, or is intended or conducted in order to hide or disguise funds or assets derived from illegal activity as part of a plan to violate or evade federal law or regulation or to avoid any transaction reporting requirement under federal law or regulation.
- The transaction is designed, whether through structuring or otherwise, to evade the requirements of the Bank Secrecy Act regulations.
- The transaction has no business or apparent lawful purpose or is not the sort in which the client would normally be expected to engage, and SCLC knows, after examining the background, the possible purpose of the transaction and other facts, of no reasonable explanation for the transaction.
- The transaction involves the use of SCLC to facilitate criminal activity.

The AML CO will file form SAR-SF and notify law enforcement of all transactions that raise an identifiable suspicion of criminal, terrorist, or corrupt activities. In high-risk situations, SCLC will notify the government immediately and file the SAR with FinCEN.

The AML CO will file a SAR within 30 days of the date of the initial detection of the facts that constitute a basis for filing the SAR. If SCLC cannot identify any suspect on the date of initial detection, SCLC may delay filing the SAR for an additional 30 days pending identification of a suspect.

The AML CO will retain copies of any SAR filed, as well as the original or business record equivalent of any supporting documentation, for five years from the date of filing the SAR. The AML CO will maintain supporting documentation and make such information available to FinCEN, any other appropriate law enforcement agencies, or federal or state securities regulators, upon request.

The AML CO will not notify any person involved in the transaction that the transaction has been reported, except as permitted by the BSA regulations.

## 4.10 Procedures for Compliance With Anti-Money Laundering Policies

The AML CO for SCLC is Kristor J. Lawson.

The AML CO shall be responsible for implementation of the AML program, including its CIP and employee

training.

The AML CO will supervise the retention of CIP records of all client identity and verification information. For each document SCLC uses to verify client identity the AML CO will maintain a record of either the documentary or non-documentary evidence used to verify the individual's ID.

# 5 BUSINESS CONTINUITY

In a publication released by the SEC (SEC 34-498445) the regulator commented that "...a critical 'lesson learned' from the events of September 11, 2001 is the need for more rigorous business continuity planning in the financial sector to address problems of wider geographic scope and longer duration than those previously addressed."

The publication went on to describe the methods by which the events of September 11, 2001 made clear the possibility of a large scale regional disaster, and the effect to which this new reality affected business planning and risk management. Because of the importance of the U.S. financial markets, the broad consensus in the financial community was that business continuity planning would be required to adapt to plan for events of wider scope and, in general to become more robust and resilient. In 2001, The National Association of Securities Dealers (NASD) surveyed its industry membership to evaluate:

- Existence and content of Business Continuity Plans
- Data back-up procedures
- Location of books and records
- Effect of September 11 on its members' ability to conduct business

Similarly, the SEC added a review of business continuity plans and risk management to its regular examination program, requiring registered investment advisers to produce written plans for business continuity or to describe the methods in place for controlling risk, and for securing the ongoing operation of their business in the face of an otherwise unanticipated interruption or disaster.

In February 2004, with its approval of SEC Rule 206(4)-7, the SEC required registered investment advisers to create and maintain written terms for business continuity as part of overall supervisory systems. Since that time, regulatory inspections of advisers have included review of the continuity plans.

## 5.1 Content of Plan

A Business Continuity Plan (BCP) is a comprehensive document outlining SCLC's procedures for recovering from an event that interferes with operations, such as natural disasters and other emergencies. Recent events have brought the importance of creating and maintaining business continuity plans to light. Regulators now believe that advisers should be required to create and maintain a BCP, ensuring preparedness for any future business disruptions.

SCLC has separately developed a disaster recovery and business continuity plan to meet its responsibilities to clients/investors, staff, business associates and others who may be affected by a disruption in the firm's business. A member of senior management, who is also a principal of the firm, must approve the plan. It must also be updated at least annually, or as soon as possible in the event of a material change in operations, structure, business or location(s).

Although a detailed copy of the BCP is retained under separate cover, in general terms it includes:

- Description of a back up system for recovery of data (both hard copy and electronic data) as protection against market and other risk
- Plan for rapid recovery of mission critical systems, including means of testing the system

- Plans for alternate communications for use between employees and SCLC, as well as between clients and SCLC
- Identification of and instructions regarding an alternative physical location of employees
- Instructions for required and other communications with regulators and regulatory reporting
- Identification of and risk assessment related to primary business constituents, banks and other counter parties
- How SCLC will assure clients regarding prompt access to their funds and securities in the event SCLC determines that it is unable to continue its business.

To add value to the Plan, the SEC recommends that advisers also consider developing and publicizing alternate communication plans for clients, service providers, and regulators to use if regular channels are not working. The alternate communications plan should assign personnel to communicate with regulators, government agencies, and mission critical vendors, providing for the type of information to be shared.

Communication planning should identify alternate modes of communication, such as pagers, cellular phones or email. Periodically SCLC and its associated persons should exchange emergency telephone numbers, email address(es), and physical address(es) to facilitate communication during an unanticipated interruption in SCLC's business. The list should provide all alternatives, since one or more telecommunications systems could be unavailable.

An adviser's capability to conduct business is tested, and ultimately determined, by its own financial and operation assessments.

## 5.2 Employee Training

Employee training and preparation are crucial parts of maintaining the BCP. Key personnel must be involved in development of both the BCP and maintenance strategies. To be effective, this preparation must encompass industry standards, along with specific training for the individual business. As an outcome of training addressing emergency preparedness, employees should be able to answer the following questions:

- Who is the immediate contact for each division or unit?
- What events trigger implementation of all or parts of the BCP?
- Who is responsible for implementing the BCP for each division or unit and for the organization as a whole?
- Where they should report if normal means of communication are unavailable?
- What to do if key persons become unavailable?

A comprehensive BCP should also outline employee responsibilities, to both clients/investors as well as to the business following a disaster. In order to anticipate staffing needs in the absence of key personnel, employees must also be cross trained regularly and in non emergency conditions.

Posting on websites, or well known bulletin boards, and using telephone banks are ways to distribute information during a disaster. Reporting or calling locations can also serve the dual purpose of accounting for missing personnel. Business continuity training should be scheduled and updated consistently to reflect changes to the BCP.

## **5.3 Procedures for Compliance with Business Continuity Planning**

The CCO shall ensure that SCLC maintains a BCP under separate cover. The CCO shall conduct training or shall ensure that training is conducted, such that SCLC's employees are informed of components of the BCP relevant to their job function. A record of the training shall be retained among the central compliance files.

Each employee shall be required to provide emergency contact information to SCLC. Upon material change, each associated person shall notify the CCO of changes in emergency contact information. No less than annually, the CCO shall re-evaluate the efficacy of the plan, and shall amend the plan as is necessary. To the extent that testing is performed, the CCO shall retain evidence of the test results and subsequent corrective action.

# 6 RISK MANAGEMENT AND INTERNAL CONTROLS

The SEC's approach to evaluating the risk management and internal control systems used by funds and registered investment advisers has become increasingly structured. One of the SEC's goals is to focus its exams on areas of real risk to clients. Consistent with this approach, the SEC requires that operating managers and compliance staff of a registered investment adviser obtain an understanding of the firm's control procedures in the most critical or strategic areas.

To the extent it is possible, SCLC seeks to quantify and manage risk in line with its fiduciary responsibility to clients.

One of the roles of the risk monitoring function is to identify the factors affecting the risk and return of client investments, both within individual portfolios and across the entire range of activities of SCLC.

While it is important to note that the various risks faced by SCLC are interrelated, SCLC's policy is to seek to address risk in four primary categories:

- Market Risk
- Credit Risk
- Liquidity Risk
- Operational Risk

## 6.1 Market Risk

Market Risk is the risk of loss for a portfolio and its subcomponents based on market conditions. Because SCLC does not manage proprietary portfolios, but rather supervises customized client portfolios, the market risk faced by clients and the market risk faced by SCLC are completely discrete. SCLC is subject to market risk because much of its fee revenue is calculated as a function of the market value of client portfolios, so that a general decline in securities prices will directly affect SCLC revenues. But, while client portfolios might decline in their own right due to market conditions, they would not decline as a result of deleterious changes in the firm's financial condition.

SCLC regularly monitors market risk to client portfolios, and the firm's entire investment philosophy aims at controlling such risks through prudent, thorough and comprehensive diversification. But market risk control measures are aimed only at controlling the market risk to client portfolios, and not directly to the market risk to the firm. To the extent that market risk control measures are effective for client portfolios, they should be effective indirectly for SCLC.

### 6.1.1 Credit Risk

Investors assume credit risk when they loan money to others, either by executing notes or by buying bonds. SCLC clients are directly exposed to such risk only by virtue of the fact that their portfolios are partly invested in debt instruments, such as publicly traded bonds, Guaranteed Income Contracts, fixed annuities, or bond mutual funds. They are indirectly exposed to such risks by virtue of the fact that their portfolios are also partly invested in equity instruments, such as stock and stock mutual funds; and most of the companies whose stock they own in one form or another are themselves either borrowers, or lenders, or both. Credit

risk to SCLC clients is diluted to the extent possible by thorough diversification, which reduces the effect of credit risk imposed through any given investment instrument upon a client portfolio.

SCLC clients are not, however, exposed to credit risks arising from the credit operations of the firm. Credit risk to SCLC can result from the firm's dealings with third parties, including among other dealings the settlement of securities and derivatives transactions, repurchase agreements, collateral arrangements, and margin accounts. Except for routine operational financing through bank lines of credit, loans, etc., SCLC does not engage in such activities. Because client assets are not commingled in any way with those of the firm, and are held in accounts at unaffiliated third party financial institutions, client assets are not at all at risk by virtue of the firm's dealings with its creditors.

### **6.1.2 Liquidity Risk**

Investment strategies that are subject to market risk and credit risk expose investors to liquidity risk. SCLC may face liquidity risk when client portfolios suffer an unanticipated loss, when positions must be liquidated in a manner inconsistent with the customary investment strategy, when market conditions adversely and unexpectedly affect the portfolios, and other such circumstances. However, because SCLC client assets are not invested in portfolios or instruments in which SCLC itself takes any position, liquidity problems suffered by SCLC do not affect client portfolios.

### **6.1.3 Operational Risk**

SCLC faces operational risk due to human error on the part of its employees (data entry errors, fraud, reconciliation errors, among others), through its system (technical failures, systematic errors in valuation or risk measurement models, others) and through the activities of third parties that provide services to SCLC.

### **6.1.4 SEC Risk Management Interview**

To determine the risk exposures of a registered investment advisory firm, the SEC commonly interviews principals, or requires a written narrative addressing common risk areas.

The SEC interview/request list includes such areas as:

- Consistency of portfolio management decisions with client's mandates
- Order placement practices
- Allocation of block and IPO trades
- Personal trading of access persons consistent with the advisers' code of ethics
- Accurate securities pricing and net-asset values
- Regular reconciliation of custodian records with fund and Adviser records
- Controls over information
- Independent custodians providing clients with information about activity in their accounts
- Calculations and presentations of performance
- Accurate reconciliations of shareholder transactions
- Internal Risk Assessment

Preparing in advance to address these topics may be useful in facilitating a regulatory examination.

## **6.2 Procedures for Compliance with Risk Management and Internal Controls**

The CCO is charged with responsibility for assessment of the primary areas of SCLC's risk. Following an assessment of the risk areas, the CCO shall devise and implement internal controls.

In respect to Market Risk, the primary risk facing the firm results from the fact that the majority of the firm's revenue derives from fees that are calculated as a percentage of assets under supervision, so that a steep or persistent or long-lasting decline in prices on capital markets would directly erode the firm's cash flow, and thus its operating capacity. It is the experience of the firm that bear markets tend to increase the number of new clients seeking SCLC's advice, and to increase the loyalty of existing clients. Nevertheless, it is possible that an extended bear market could persuade some of the firm's clients to withdraw their assets from coverage by supervisory arrangements with the firm, compounding the firm's Liquidity Risk.

To monitor its credit risk, the CCO shall maintain periodically updated records of its arrangements with third parties providing credit to SCLC. The types of records the CCO will maintain may include financial statements, annual or other periodic reports, or the contract in place between SCLC and the third party related to situations in which credit might be at risk.

To monitor its liquidity risk, the CCO shall periodically review records that demonstrate its cash position, its borrowing capacity, and its need for liquidity (such as historical draw downs).

To address its operational risk, the CCO shall perform periodic random spot checks of its electronic systems and shall maintain a single consolidated data set including the contingency plans for responding to failures.

# 7 US REGULATORY FILINGS

SCLC is required to make certain regulatory filings on an ongoing basis, depending on the firm's trading activity or status as a regulated entity. The regulatory filings that could be required of SCLC are listed and described below, organized by regulatory agency. The list specifically excludes tax filings and those that may be required of registered broker/dealers.

The filings actually made to particular regulators by SCLC will depend on the type and volume of trading in which it engages, its business model, and the jurisdictions in which it operates. These requirements may change from time to time based on various triggering events. For example, the size of the positions held may trigger certain regulatory filings (e.g., Form 13F). SCLC may also be subject to regulatory reporting and filing requirements in foreign jurisdictions in which it conducts its business; however, this document does not address these types of filings.

Given the organization and business practices of SCLC, which have perdured since the founding of the firm, and are not expected to change, it is unlikely that most of the following filings will ever become necessary, with the exception of regular annual filings of Investment Adviser Registration forms. Thus except for SCLC compliance personnel, their significance to the firm's employees is likely to remain merely hypothetical. Nevertheless, because the firm must periodically determine whether each of these filings is necessary, it is important that they be noted herein, and explained.

## 7.1 Procedures for Compliance with Regulatory Filing Requirements

The CCO shall determine which of the regulatory filings must be made by the Adviser, and shall assign data collection and reporting duties accordingly to ensure timely filings are made.

## 8 NEW ISSUES

Restrictions on trading new issues are set forth by the SEC in Regulation M and by the NASD in Rule 2790. While most investment advisers are not also broker-dealers, the NASD rules may apply to activities conducted by the Adviser directly or indirectly, and therefore will be briefly discussed in this chapter.

New issues are defined by NASD Rule 2790 (the "rule") as any initial public offering of an equity security, as defined in Section 3(a)(11) of the Securities Exchange Act of 1934, made pursuant to a registration statement or offering circular. The rule does not apply several types of offerings including secondary offerings or offerings of convertible or preferred securities.

In late 1996, the SEC passed Regulation M, which generally prohibits participants in the distribution of an offering (such as underwriters, broker-dealers, and others) or any other affiliate from purchasing or bidding certain securities during an initial offering. This condition of Regulation M would affect SCLC if its clients or affiliates included broker-dealer(s) and if it elected to purchase securities for these or other clients during or immediately before such offerings.

The Regulation also prohibits covering a short sale with securities obtained in a public offering if the sale occurred within 5 business days before the pricing of the public offering. The SEC has enforced compliance with this condition of the Regulation over investment advisers in its jurisdiction.

Because contingent liability may inure to SCLC, the firm should be cognizant of the terms and conditions of Regulation M, and of prevailing NASD regulations related to new issues that may affect or be affected by its clients or affiliates.

### 8.1 Procedures for Compliance with New Issues

SCLC does not trade in new issues, either directly or for the benefit of client accounts.

## 9 GIFTS AND ENTERTAINMENT

For purposes of the following policies on receipt of gifts and sending gifts, a gift of nominal value shall be defined as cash, cash equivalent, physical item, service or event tickets with a value not to exceed \$100.00. Any gifts given or received by SCLC or any of its associated person are considered in aggregate whether or not they were conferred by the same or different people at SCLC or the other (recipient) firm or party.

For purposes of SCLC's policies regarding Entertainment, an entertainment event shall include any conference, meal or sponsored outing.

No associated person or member of an associated person's immediate family may receive any gift of more than nominal value from any person or entity that is a business contact, including clients and their service providers, vendors and competitors. Gifts of nominal value are subject to disclosure requirements as outlined in the Procedures Section below.

No associated person or member of an associated person's immediate family may send any gift of more than nominal value to any person or entity that is a business contact, including clients and their service providers, vendors and competitors. Procedures for gifts of nominal value are outlined in the Procedures Section below.

Associated persons are generally permitted to attend an approved event, provided that the purpose of the meeting is to discuss the firm's business, and provided that the associated person *AND* the vendor, service provider or client paying for the event must be in attendance. Events sponsored by professional associations, such as the Financial Planning Association or the Western Pension & Benefits Conference, are not covered under this policy; no documentation of attendance at such events is required.

Similarly, associated persons may invite clients to an event, provided that the purpose of the meeting is to discuss SCLC's business, and the event has been approved by a responsible principal.

### 9.1 Procedures for Gifts and Entertainment

The CCO is the principal charged with responsibility for SCLC's Gift and Entertainment policies.

To monitor compliance, the CCO requires that associated persons report gifts given and received in a timely manner, deemed to be 30 business days prior to giving or after receiving the gift.

To monitor compliance, the CCO shall require that associated persons report events attended or hosted within a timely manner, deemed to be 30 business days prior to extending an invitation or upon receipt of an invitation to attend an event.

As evidence of compliance, the CCO shall record gifts given and received on a log, retained among the firm's central compliance files.

# 10 TRADING

SCLC's trading policies must address allocation procedures, best execution guidelines, resolution of trade errors, treatment of soft dollars and other issues.

SCLC's trading practices must be fair and equitable to customers, and must be subject to an allocation system that is reasonable, and which does not favor one class of client over another.

Order executions must be periodically tested to ensure that the firm has met its obligation to seek best execution.

## 10.1 Aggregation of Orders

SCLC develops trading recommendation for each client account individually, so that trades are never aggregated. Thus considerations of order aggregation do not currently apply to the firm.

## 10.2 Best Execution

SCLC has an obligation to seek best execution of clients' transactions under the circumstances of the particular transaction. Accordingly, SCLC must execute securities transactions for clients in such a manner that the clients' total cost or proceeds in each transaction is the most favorable under the circumstances. It is important to note that best execution is not identical with the lowest possible price.

In order to minimize conflicts of interest that could arise in the event that SCLC were to steer clients toward a certain broker/dealer, it is SCLC policy not to recommend any particular broker/dealer for execution of client transactions, but rather to work with such broker/dealers as clients themselves select. This is in line with the general philosophy of SCLC, that its proper role is, not to manage portfolios for clients, but rather to enable them to make the most informed, rational investment decisions possible, and then to assist them in carrying out such decisions.

This policy includes the decision which custodians or broker/dealers to utilize. Therefore an important role of SCLC is to inform clients of the relevant costs and benefits of doing business with various different broker/dealers. The client, however, bears the final responsibility of negotiating terms and conditions with such broker/dealers. When a client has selected broker/dealers, SCLC is unable to seek better execution services or prices from other broker/dealers, or to consolidate trades at a given broker/dealer across client portfolios so as to obtain more advantageous pricing.

Clients must be informed of these considerations in their initial interviews with SCLC personnel, and annually thereafter via the annual offer of the SCLC Disclosure Brochure. Client broker/dealer selections must be documented, and records of client broker/dealer selections retained by SCLC in each client's files. These policies are disclosed in SCLC's Disclosure Brochure, and on Schedule F of Part II of Form ADV, which the Disclosure Brochure restates.

## 10.3 Trade Errors

SCLC's handling of trade errors must be conducted in a manner that does not disadvantage the client, irrespective of the cause of the error. In no event shall an employee of SCLC resolve a trade error without

the approval of a senior principal or other supervisor.

The SCLC Trade Error Policy is specified in the following step-by-step procedure for dealing with trade errors in client accounts. These procedures are to be followed by all associated persons involved in executing trades on behalf of clients, in our capacity as a non-discretionary investment advisor. When a trade error is discovered:

- Immediately notify the CCO and primary adviser(s) in person, via e-mail or voice mail.
  - Provide the CCO and the adviser with a complete report of the circumstances that contributed to the error and the outcome.
  - The report should include a detailed calculation of the dollar amount of any costs incurred by SCLC in correcting the error.
  - Record the explanation in: the SCLC CRM; the Client's electronic file; and SCLC's Trade Error file, in both electronic and paper versions (the paper file is located in the firm's central files; the electronic file may be found in SCLC/Trading).
  - Each trade error should have its own electronic subfolder, containing all documents relevant thereto, including any trade worksheets, order tickets, confirms, notes, memos, email messages, etc. The electronic file naming convention for each trade error folder should be: YY-MM-DD Client Surname Trade Error.
- SCLC Traders should not engage in independent negotiations with the account custodian concerning which party is at fault or the amount of any "make-good" charges. Consult with the CCO or the adviser concerning your position, in this regard.
- Providing the client with a prompt and complete explanation of any trading errors, and their impact on the client account, is of critical importance. Please assist the adviser or CCO in drafting a letter of explanation to the client, for their signature. Make certain that any correspondence in this regard is filed in the locations cited above.
- To avoid future errors, conduct a careful examination of the facts and circumstances that contributed to the error. Develop a plan to mitigate the contributing circumstances, so as to avoid such errors in the future. Submit your report to the CCO for review and comment.

To ensure compliance with SCLC's trade error policies, the CCO will conduct, or will instruct another qualified party to conduct, a review of trade errors on a quarterly basis. The review shall include a review of 'broken' or 'dk' trades and may be based on records generated internally or through independent third parties such as broker/dealers or custodians.

## 10.4 Agency Cross Transactions

The SEC imposes specific regulations for transactions in which a registered investment adviser (or any entity it controls or is under common control of) acts as broker on both sides of a transaction ("agency cross transaction"). SCLC does not act as a broker, and so by definition cannot participate in agency cross transactions.

## 10.5 Procedures for Compliance With Trading Policies

The CCO is the individual charged with responsibility for implementation, monitoring and retention of documentation related to SCLC's trading policies. The CCO shall ensure that any individual with the authority to place a trade in an account supervised by SCLC shall be provided with the overall trading strategy for a client for a given round of trading in the client's accounts. Trading policy is as follows:

As a non-discretionary investment adviser, SCLC does not execute any trades in client accounts without the prior approval of the client.

- Clients must therefore approve trades before they are executed, and until client authorization is received, no trades may be entered.
- Where the client provides authorization orally, trades may be executed on the basis of that authorization, provided written ex post facto authorization is timely sought from the client.
  - ◆ Oral trade authorizations must be noted to the history of the client record in the SCLC Client Relationship Management (CRM) system.
  - ◆ Copies of such notations must be posted to the client electronic trading folder.
  - ◆ Written ex post facto authorization of orally approved trades must be sought from the client at least three times.
  - ◆ A record of each attempt to obtain ex post facto authorizations must be posted to the SCLC CRM and to the client electronic trading folder.
- Client authorizations must be documented in an email message, letter, or facsimile from the client, which refers specifically to the trades submitted to them for approval.
- Client trade authorizations must be filed electronically in the client's trading folder, and the files linked to the SCLC CRM.

Upon receipt of client authorization, SCLC traders may enter the trades for execution on the trading platform of the broker/dealer or custodian of each client account where trading is needed.

- Trades should be entered timely, client by client, in the order in which their authorizations were received.
- All client trades pending must be executed prior to any personal trading.
- Advisers may not enter trades; trading is restricted to authorized traders.
- Electronic copies of trade tickets must be retained in the client's electronic files.
- Fluctuations in market prices, or changes in trading policies at broker/dealers, or other factors may make it necessary to adjust approved trades so as to obtain the overall portfolio effect the approved trades are intended to achieve.
- Where necessary adjustments constitute a significant change to the set of trades already approved by the client, a new client approval must be obtained before they may be entered for execution. While it is necessarily a matter of judgement whether an adjustment is significant, some examples will provide guidance:
  - ◆ Where one security must be substituted for another - e.g., when a fund recommended for purchase has become unavailable on a given trading platform - the adjustment is significant, and a new client authorization must be obtained.
  - ◆ Where one class of mutual fund is substituted for another class of the same fund, so as to reduce client fund expenses, the adjustment does not rise to significance.

An authorized person must review all executed trades, to be sure that they accurately reflect the intentions of the client.

- No trader may review her own trades.
- Confirmations should be compared with tickets or trade orders, to be sure that the broker/dealer or custodian has executed the trades as entered.

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- Confirmations should also be compared with the trades originally approved by the client, to ensure that all approved trades have been executed in substantially the same respects in which they were approved.
- Any discrepancies discovered in these two steps should be reported immediately to the trader(s) who entered the trades, and to an adviser for the client account, for appropriate resolution. Discrepancies consist of:
  - ◆ Trading a security other than the securities authorized by the client, except for different share classes of a client-approved fund.
  - ◆ Trading dollar or share amounts different than those approved by the client.
  - ◆ Trading of securities in accounts other than those indicated in the trades approved by the client.
- Resolution of any discrepancies should be noted in the Trade Set subfolder of the client's electronic trading folder.
- All paperwork or documents generated in connection with a set of trades for a client account should also be filed in the client's electronic trading folder.

Completion of a set of trades for a given client should be denoted in the client's contact record in the SCLC CRM. Electronic records of documents generated in connection with a given round of trading in a client's accounts must be filed in a special "Trade Set" folder, located in the client's Trading folder.

- The file name for each Trade Set folder must include the client surname and the inception date of the round of trades, understood as the date that SCLC communication to or from the client in regard to the trades first occurred, and using the format YY-MM-DD Client Surname Trade Set.
- Each Trade Set folder must include at least:
  - ◆ Recommended trades, in pdf format, as follows: YY-MM-DD Trades.pdf.
  - ◆ Note recording client oral authorization, if applicable, in pdf or txt format, as follows: YY-MM-DD Oral Client Authorization.txt.
  - ◆ Written client authorization in txt or pdf format, named as follows: YY-MM-DD Written Client Authorization.pdf.
  - ◆ Trade Order Ticket, in pdf format, named as follows: YY-MM-DD Order.pdf.
  - ◆ Records of trade review in pdf format, named according to the following template: YY-MM-DD Review.pdf.
  - ◆ Internal memos, email messages, or any other documentation created in the process of execution.
  - ◆ All documents relating to discrepancies or trade errors in pdf format.
- Files posted to the Trade Set folder should be named using a specific format, e.g., "YY-MM-DD Author Initials Document Subject.pdf"

The CCO is charged with oversight of the SCLC's efforts to achieve best execution. From time to time, the CCO may require principals of the Adviser and other qualified persons to participate in the review. Included among the documents and information reviewed in this regard may be:

- Reports of executions posted publicly by clearing firms and other entities through which SCLC routes orders
- Time and sales data reviewed from a reliable resource, such as Bloomberg, or NASDAQ Trader
- Internal reviews and reports

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- Cost appraisals related to SCLC's custodial, clearing and settlement relationships, and any and all other information deemed appropriate by the CCO

Because SCLC is a non-discretionary adviser, and because the client selects broker/dealers and custodians, the gathering of information in support of best execution is designed, not to enable the firm to select among custodians and broker/dealers, but to enable it to inform and educate clients about them, so as to support the client's decision.

Documentation of SCLC's appraisal of execution quality, including the nature and scope of the review, shall be reviewed and documented regularly.

# 11 PROTECTION OF NONPUBLIC CUSTOMER DATA

Federal, state and other governmental regulations require advisers to protect nonpublic customer data.

## 11.1 Regulation S-P

The Securities and Exchange Commission passed Regulation S-P in June of 2000, implementing privacy rules among affiliated and non-affiliated financial institutions, in response to the Gramm-Leach-Bliley Act ("GLB"), which passed in November of 1999. GLB eliminates the restrictions on banking, securities and insurance activities being conducted under one roof. GLB also addresses privacy concerns through provisions for sharing information among various entities, as advocated by consumer privacy groups. Included in GLB's Title V are complex privacy rules that require financial institutions (including investment advisers) to adopt policies and procedures and provide consumers and clients with various notices regarding the steps the firms will take to protect nonpublic client information.

Since the passage of Regulation S-P, states and other government agencies have enacted laws and regulations governing the protection of client/investor nonpublic data.

SCLC is required to adhere to the privacy laws and regulations in each and every state in which it has clients. Regulation S-P is binding on all federally-covered investment advisers. Regulations of the Federal Trade Commission (similar to Regulation S-P) and other state laws are applicable to state covered investment advisers and govern the sharing of client information. The recently enacted California Financial Information Privacy Act governs client information sharing and applies to investment advisers with Californian clients. Every investment adviser must therefore develop and implement a "privacy policy" in order to control the management and disclosure of client information.

### 11.1.1 Affiliate

An "Affiliate" is any company that controls, is controlled by, or is under common control with SCLC.

### 11.1.2 Clear and Conspicuous

"Clear and conspicuous" means that a privacy policy notice must be designed to call attention to the information contained in the notice, and that the notice must be reasonably understandable. This means that the typeface and size must be large enough to be easily read, and of such a design that will illustrate the significance of the disclosure.

### 11.1.3 Consumer

A "consumer" is an individual who obtains financial products or services that are to be used primarily for personal, family, or household purposes. The legal representative(s) of the consumer are included in the definition. Financial products and services include the investments themselves and those evaluations or analyses that led to the investment.

Consumers are not any of the following persons:

- Individuals who provide only a name, address, or other general contact information for the purpose of obtaining information, such as a response request
- Individuals who have accounts with SCLC solely for the purpose of executing a transaction, such as those accounts cleared through SCLC by an introducing broker-dealer or contracted broker-dealer
- Individuals who have accounts or engage in transactions with SCLC solely due to agent or service contracts
- Other individuals who are not directly defined as consumers of SCLC.

### **11.1.4 Continuing Relationship**

A "continuing relationship" is one in which a consumer has contracted with SCLC for continuous and ongoing investment services, or investment supervisory services. A continuing relationship is not established in cases where there is an isolated engagement that is not expected to result in future services.

### **11.1.5 Customer**

A "customer" is an individual or consumer who has a "customer relationship" with SCLC.

### **11.1.6 Customer Relationship**

A "customer relationship" is a continuing relationship between the individual and SCLC in which the firm provides a financial or investment product or service that is to be used primarily for personal, family or household purposes.

### **11.1.7 Nonpublic Personal Information**

"Non-public personal information" is financial information obtained or collected by SCLC that is personally identifiable. The definition includes lists, groups, or other categories that have been created or derived on the basis of individual or household nonpublic information. For instance, a list of names derived from specific account numbers is nonpublic personal information.

### **11.1.8 Personally Identifiable Financial Information**

"Personally identifiable financial information" is that information provided to SCLC by the individual that results in a transaction with the consumer, that results in the provision of any service to the consumer, or is obtained by SCLC through the use of account applications, client profiles or questionnaires, or through other means.

### **11.1.9 Publicly Available Information**

"Publicly Available Information" is that which SCLC may reasonably believe is legally available to the general public through federal, state, or local governments, or broadly through public media such as phone books, web listings, or newspapers.

## 11.2 Consumers & Customers

Regulation S-P draws distinctions between customers and consumers, requiring different levels of protection to each. Entities covered by the regulation must provide customers with notice about the entity's privacy policies, and must give consumers a method to opt out of any sharing practices by giving reasonable notice.

Under the Regulation, a "consumer" is an individual who obtains financial products or services to be used primarily for personal purposes. Products and services can include evaluations of information, in addition to the product or service itself. By contrast, a "customer" is a consumer with a continuing relationship with the entity firm. Therefore, all customers are also consumers.

## 11.3 Notification Requirement

Regulation S-P requires that notice of SCLC privacy policies be provided to consumers and customers initially and annually.

### 11.3.1 Initial Notice

The initial notice to the customer of the SCLC Privacy Policy must be clear and conspicuous. The Privacy Policy must be provided to customers at or before the beginning of a customer relationship, or within a reasonable time frame for such instances as an account transfer or telephone order, when the notice requirements may interfere with the transaction itself.

Provision of the Privacy Policy to consumers is only required if SCLC intends to share non-public information with a non-affiliated third party. The Privacy Policy must nevertheless be distributed to all consumers.

### 11.3.2 Annual Notice

During each 12 month period in which an ongoing client relationship exists, an investment adviser must provide a subsequent notice of its privacy policy to all customers. If there is a change in the privacy policy, notice must be given to all customers whose information may be affected by the change.

### 11.3.3 Content of Notice

Privacy policy notices must contain specific information, including:

- Types of non-public information collected by the entity, including the names of forms on which the information is collected
- Categories of non-public information shared by the entity, including the same for former customers
- Categories of affiliated and non-affiliated third parties to whom information is disclosed by the entity
- Separate disclosure is required for any servicing or joint marketing agreements, including the categories of information and of the third parties involved
- Notice of opt out rights available to customers, which must adhere to the regulation's standard of "reasonable," and any state regulation regarding the sharing of information

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- General disclosures regarding the policies of the entity to protect and secure confidential information
- Disclosure regarding shared information among affiliated parties as defined by the SEC and the state(s) in which the Adviser is registered
- Statement(s) regarding allowed third party sharing relationships, such as those conducted under the transactional exemption or others.

### 11.3.4 Privacy Policies

Access to the completed documents and client files must be restricted to following persons:

- Only those associated persons who are required by their job function to access this information
- Applicable staff, such as individuals in Management, Legal or Compliance Departments in cases where the information is requested to resolve a customer dispute
- Management, Legal and Compliance personnel in cases where such information is requested by a regulatory agency
- Others as specifically permitted by the CCO

### 11.3.5 Customer Information

SCLC collects and records client information on the following types of forms that contain personal and financial data:

- Account Applications
- Client Questionnaires
- Subscription Documents
- Trust, Organizational records, and other documents used to conduct due diligence, among other purposes
- Other internal documentation

Because this data contains non-public client information, it is subject to every available protection under these policies.

### 11.3.6 California Residents

The California Financial Information Privacy Act (Privacy Act) provides for more stringent consumer protection provisions than are available under federal law. The Privacy Act took effect on July 1, 2004 and applies to all advisers with customers who are California residents.

Relevant provisions that apply to California customers include the following:

- An investment adviser cannot share non-public personal client information with a non-affiliated

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third party without first obtaining explicit written client consent.

- An investment adviser cannot share non-public personal client information with an affiliate unless the adviser clearly and conspicuously notifies the client annually in writing that the information may be disclosed, gives the client the opportunity to refuse permission and the client does not opt out. An investment adviser with assets in excess of \$25 million must include a self addressed stamped return envelope with each annual notice. An investment adviser with assets of up to \$25 million need only enclose a self-addressed return envelope.

An investment adviser may share non-public personal client information with a non-affiliated financial institution in order to jointly offer a financial product or service if:

- The financial product or service is provided by one of the institutions as part of a written agreement;
- The financial product or service is jointly offered, endorsed, or sponsored, and clearly and conspicuously identifies for the client the advisers that disclosed and received the disclosed information;
- The written agreement requires that the receiving institution maintain the confidentiality of the information and disclose it only for the purpose of carrying out the terms of the joint offering;
- the client has not prohibited the disclosure of the non-public personal information.

Advisers with wholly owned subsidiaries or firms with the same ownership structure might share non-public personal client information if all of the following conditions are met:

- The advisers are regulated by the same functional regulator.
- The adviser disclosing the nonpublic personal client information and the adviser receiving it are both principally engaged in the same line of business (insurance, banking or securities only).
- Both the disclosing firm and the receiving firm share a common brand.

Examples of standard exceptions to the Privacy Act disclosure requirements include allowing disclosure of non-public client information in such circumstances as to complete a transaction authorized by the client; to prevent actual or potential fraud, identity theft, or unauthorized transactions; to resolve client disputes or inquiries; or as required by law.

An investment adviser is required to comply with any client directions on sharing his or her non-public personal information within 45 days of receipt. No written notice is required if an investment adviser does not disclose nonpublic personal client information except as allowed under the exceptions to the Privacy Act.

## 11.4 Procedures for Compliance with Regulation S-P

The CCO is charged with responsibility for SCLC's privacy policies and procedures designed to protect non-public client data from unauthorized access.

In its efforts to ensure that such data will be secure from unauthorized access, SCLC mandates that each associated person observe its procedures and respect the privacy of non-public data by carrying out his or her specific duties with care. Included in the duties of certain associates with access to non-public data is a high degree of discretion in maintaining the privacy of that data.

SCLC strictly prohibits any individual whose job duties do not require access to non-public client data from any attempt to procure nonpublic information about any client or group of clients. As evidence of compliance, the CCO will maintain or will instruct to be maintained a list of all employees including job descriptions. Those with restricted access will be denoted on the list.

Computer systems and phone systems, which may contain any manner of nonpublic data and information regarding clients shall be protected by passcode. The CCO shall ensure that upon termination, or at any time in which job functions are reassigned and access to nonpublic information is no longer required of any employee, that the password assigned to that individual shall be terminated. Compliance with this requirement will be evidenced by a notation in each individual's file denoting that password has been terminated.

In its further efforts to maintain security, SCLC shall restrict all unauthorized access to areas in the office in which non-public client data are retained. This is accomplished by maintaining client records in locked storage rooms or file cabinets.

# 12 PUBLIC COMMUNICATIONS

SCLC's communications with the public, which include its advertisements, its website, correspondence (both electronic and written) including internal communications are subject to SEC and State Regulations that require each such communication to be fair, reasonable and balanced. The regulations subject the communications to record-keeping requirements.

Regular and ongoing oversight of SCLC's communications with the public is a fundamental component of its compliance program.

## 12.1 Advertisements

The SEC defines "advertisement" in Investment Advisers Act Release No. 1083 as any written communication addressed to more than one individual, or any notice or announcement in any publication or by other means (such as radio, web/internet, cable or television) that offers any analysis, report, or publications regarding securities; or any graph, chart, formula or other device for making investment or investment advisory decisions.

All advertisements developed by or for SCLC or its promoters, including third parties, if applicable, shall be consistent with the provisions of Rule 206(4) of the Investment Advisers Act of 1940, applicable state standards, and other rules. These rules require that no associated person of SCLC shall publish, circulate, distribute, or otherwise use any advertisement that is incomplete, false, or misleading.

While the definition requires that the material must include an offer of services of some nature, the SEC has broadly interpreted the definition to include an adviser's brochure, websites, any form letter, chat room participation, materials used to maintain existing client relationships, materials intended to solicit new clients, the adviser's "pitch book" and other such materials.

### 12.1.1 Investment Counsel

Under the 1940 Investment Advisers Act, "it shall be unlawful for any [registered investment adviser] to represent that [it] is an investment counsel unless ... a substantial part of [its] business consists of rendering investment supervisory services." (15 U.S.C. Section 208(c)) The Act defines investment supervisory services as "the giving of continuous advice as to the investment of funds on the basis of the individual needs of each client." (15 U.S.C. Section 202(a)(13))

SCLC believes that it meets the definition of investment counsel, and may therefore use the term to refer to itself and its business.

### 12.1.2 "RIA"

In rendering effective licensure for a registered investment adviser or its registered agents, the SEC does not approve or endorse the firm. Therefore, while an adviser may represent that it is "registered," the SEC prohibits the use of the term "RIA" on stationery, business cards, or in advertising, as it may imply to the investment community that the individual or firm has achieved approval, endorsement, or other credential. The adviser may use "registered investment adviser," provided the words are spelled out.

### 12.1.3 Testimonials

A "testimonial" includes, but is not limited to, a summary of a specific case situation, real or fictional, which may create an inference that all clients of an adviser typically experience favorable results. Client surveys conducted by third party service providers are considered by the SEC to be testimonials, but may be used in an advertisement as long as they are consistent with regulatory requirements. These regulatory requirements include, but are not limited to requirements that results must represent a valid sample, represent unbiased analysis, and do not favor positive or negative results.

In addition, representative client lists may be testimonials and may only be used if the following conditions are met:

- Criteria for determining which clients are included in the list are not based on performance.
- Such criteria are disclosed.
- The list includes a disclaimer stating that it is not known whether the clients listed approve or disapprove of SCLC or its advisory services.

Furthermore, whenever testimonials of any kind are used in advertising, they must be accompanied by disclosures that include at least:

- A statement that no client or prospective client should construe the testimonial as a guarantee that they will experience certain investment results
- A statement that the testimonial should not be construed as an endorsement of SCLC by any of its clients
- For lists or rankings published by magazines, web sites, or other public media, a statement that such lists and rankings are generally based exclusively on information or client lists prepared and submitted by SCLC.

### 12.1.4 Past Recommendations

Advisers are prohibited under Rule 206(4)-1 to use any promotional materials that refer to any past profitable recommendations absent specific disclosure regarding all recommendations made by the adviser.

It is SCLC policy never to produce any advertisement that includes past recommendations.

### 12.1.5 Performance Data

Clients and potential clients are likely to consider past performance an important factor in selecting an adviser. The SEC has established guidelines for certain types of language and other restrictions regarding what may and may not be included in performance data used for the purpose of marketing the services of an investment adviser.

Because SCLC designs and supervises client accounts individually, according to the particular requirements of each client's situation, objectives, and predilection for the assumption of investment risk, and does not

manage proprietary portfolios, data on the past performance of portfolios supervised by the firm would be both irrelevant and meaningless to any particular client or prospective client. It is therefore SCLC policy not to advertise past performance.

### 12.1.6 Actual Performance

In the case of the use of actual performance results, the following omissions or practices may be considered misleading:

- Any representation that model, hypothetical, or back-tested performance is actual performance is not allowed.
- Assets held with other than the adviser's primary or approved custodian should not be included in the asset base for performance reporting purposes.
- Assets that are managed at different approved custodians may be included in the adviser's performance reports; however, it should be made clear to the client that assets are being held with different custodians due to unique fees and charges that may apply, among other variations.
- Illiquid assets such as limited partnerships and non-variable annuities should not be included in the asset base for performance reporting purposes. The adviser should take care to justify the liquidity of any asset included in its performance base.
- Inaccurately reporting the size of the adviser's asset base is considered to be misleading, as it may lead a client/investor to the wrong conclusion regarding the adviser.
- Investment advisers who present their performance results in compliance with the Global Investment Performance Standards of the CFA Institute (CFA Institute Standards), must ensure that any claim of compliance with Global Investment Presentation Standards (GIPS) can be verified through factual documentary evidence.
- Predecessor returns, such as those an adviser may have generated under prior employment or other prior organization, may not be used in a misleading manner.

### 12.1.7 Model Performance

In the case of the use of model performance results, the following omissions or practices may be considered misleading:

- Failing to disclose material changes in the conditions, objectives, or investment strategies of the model portfolio during the performance period covered in the report
- Failing to report any effect of changes in the conditions, objectives or strategies on the current portfolio
- Failing to disclose any variation in actual performance versus that reported in the model performance
- Any other failure that would cause the model to be an inaccurate portrayal of the adviser's currently offered or managed portfolio

### **12.1.8 Gross vs. Net Performance Data**

The use of gross performance data in presentations and advertising is prohibited except in one-on-one presentations to individuals, pension funds and other institutions. One-on-one presentations are not clearly defined by the SEC, but some guidance is provided through No-Action letters issued by the SEC. In particular, provided the presentation is private and confidential, it can be permitted that more than one prospective client, consultant or other individuals are present. Furthermore, the presentation should be made in such a forum that it is reasonable to expect that attendees will have an opportunity to question the adviser about the nature, scope and affect of fees on the overall cost structure to the investment, style, or strategy being proposed. Additional information regarding the SEC's position on the use of gross performance in one-on-one presentations can be found in a No-Action letter issued to the Investment Company Institute ("ICI") in the late 1980's, and in No-Action relief provided to the Securities Industry Association in a letter dated 1989. For instance, in the ICI No-Action letter, the SEC established the parameters for the use of gross performance as requiring that four specific conditions are met:

1. Disclosure that the performance figures do not reflect the deduction of investment advisory fees
2. Disclosure that the client's return will be reduced by the advisory fees and any other expenses it may incur in the management of its advisory account
3. Disclosure to describe where further information regarding fees may be found
4. A representative example (e.g., a table, chart, graph, or narrative), which shows the effect an investment advisory fee, compounded over a period of years, could have on the total value of a client portfolio

Other than in one-on-one presentations conforming to the SEC's No-Action letters, the use of gross performance in advertising is deemed to be misleading. Therefore, in all other instances, performance must be shown net of fees.

SCLC reports returns on assets under supervision (as distinct from assets under consultation) to clients one-on-one, and gross of fees. The disclosures required above are made to supervisory clients in their annual Portfolio Performance Evaluations.

### **12.1.9 Retention of Performance Documentation**

Under Rule 204(2) of the Investment Advisers Act of 1940, an adviser must retain all performance advertisements and all supporting documents and information used to form the basis for that performance information for a period of at least five (5) years from the end of the fiscal year in which the material was last used or distributed, the first two (2) years in an easily accessible location. The record of supporting documentation must include records of ALL materials for the entire reporting period included in any distributed report or advertisement. For instance, if the adviser distributes its performance for a decade or more, ALL supporting documentation for the entire period is subject to the retention requirement.

### **12.1.10 Requests for Proposal**

Requests for Proposal are questionnaires distributed generally by large institutions or other money managers as part of their due diligence in selecting investment advisers. These questionnaires are not advertising, as they are completed in connection with a single request for information for a specific investment. Nonetheless, they are commonly requested for review by regulators in connection with a regulatory examination. Therefore, SCLC shall address all responsive content within the questionnaire according to the

standards of accuracy, fairness, balance and performance reporting applied to advertising materials.

### **12.1.11 Prohibited Advertisements**

It is SCLC's duty to ensure that its advertising is fair, balanced, and accurate. Certain types of advertising are prohibited:

- Materials including the acronym "RIA"
- Materials including statement(s) to the effect that any report, analysis or other service will be furnished without a charge unless such report or other service is actually furnished without charge or obligation
- Testimonial(s) of any kind concerning the investment adviser, or any advice, analysis, report or other services rendered by SCLC
- Statement(s) of material fact that are false or misleading
- Direct or indirect specific past profitable recommendations absent appropriate disclosure statement and a list of all recommendations made in the most recent year
- Statement(s) that any graph, chart, formula or other device being offered can be used in and of itself by a client to determine what securities should be bought and sold, or that such a device will assist any person in making decisions concerning specific securities transactions.

## **12.2 Correspondence**

Rule 206(4)-7 requires that advisers have in place written policies and procedures reasonably designed to prevent violations of the Act and other rules. It is reasonable to expect that written policies and procedures so designed would include an adviser's internal and external business related communications. Further, upon regulatory examination, representatives of regulatory agencies are likely to request to review copies of communications by client, by associated person, or by date. The regulators will therefore expect that SCLC's communications are subject to adequate control by a principal of SCLC, such that individual associated persons are not able to communicate inappropriately with existing or prospective clients.

In its enforcement of procedures related to its communications with the public, SCLC has established the following policies:

- Use of any stationery, email or server other than that under the control and subject to the review of the CCO for business related communications is prohibited
- Use for business purposes of instant messaging or electronic communications from any means that might prevent the oversight of the CCO are prohibited
- The name of the firm must be prominently displayed on stationery and in electronic 'tag lines,' on email messages, and must include contact information for the primary office of SCLC
- All communications are subject to the prior or timely review of the CCO or a designee
- The review of written and electronic communications shall include: monitoring content (to detect potential misleading or fraudulent communications, violations of SCLC's internal policies and procedures, etc), reviewing the state of the recipient (to detect potential license or registration violations), among numerous other types of reviews.

## 12.2.1 Electronic Communications

SEC officials have stated that they interpret certain regulations as requiring investment advisers to review their electronic communications for investment advisory matters.

Electronic communications, including those among the general investing public and other internal business related communications that fall under Rule 204-2 of the Investment Advisers Act of 1940, require the same review and retention as any other type of written communication. Non-business related communications may be destroyed if this is done on a regular and routine basis pursuant to an established policy of the Adviser that is adequately designed to prevent the unauthorized destruction of business communications.

## 12.2.2 Retention

SEC Rule 204(2) requires that advisers retain originals of all written communications received and copies of all written communications sent by them relating to (1) any recommendation made or proposed to be made and any advice given or proposed to be given; (2) any receipt, disbursement or delivery of funds or securities; or (3) the placing or execution of any order to purchase or sell any security: *Provided, however, (a) that the investment adviser shall not be required to keep any unsolicited market letters and other similar communications of general public distribution not prepared by or for the investment adviser, and (b) that if the investment adviser sends any notice, circular or other advertisement offering any report, analysis, publication or other investment advisory service to more than 10 persons, the investment adviser shall not be required to keep a record of the names and addresses of the persons to whom it was sent; except that if such notice, circular or advertisement is distributed to persons named on any list, the investment adviser shall retain with the copy of such notice, circular or advertisement a memorandum describing the list and the source thereof.*

The above referenced advertising and communications along with supporting documentation for the same must be maintained for a period of at least five (5) years, the first two (2) years in an easily accessible location.

## 12.3 Procedures for Compliance with Public Communications Requirements

The CCO is charged with responsibility for implementation, ongoing monitoring and retention of SCLC's communications with the public.

To monitor SCLC's written communications, the CCO requires that all communications be provided for review in a timely manner. The CCO may implement an electronic surveillance system designed internally or provided by a third party to assist in the process of review and retention of SCLC's communications.

To ensure compliance with Rule 206(4), SCLC has charged the CCO with the responsibility and authority to review and approve any and all forms of advertisements in advance of their use. This mandate is to include the firm's marketing materials, slide presentations, responses to Requests for Proposal, responses to third party questionnaires, and any and all other materials used in presentations whether to one individual or to multiple parties. Evidence of the review and approval will be retained among the central files.

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To assist in monitoring compliance with these procedures, the CCO will perform or will instruct another individual to perform a periodic review of the separate files and records maintained by individuals who promote investment in the accounts supervised by SCLC, such that assurances may be attained (or exceptions identified) that materials used in promotions have been approved in advance.

In regard to the review of communications, SCLC has implemented a system of review that requires the following:

- All incoming written (paper) communications shall be centrally opened, and substantive communications shall be copied and provided to the CCO for review. The permanently filed copies of such communications shall be those bearing evidence of a supervisory review, generally the date of review and the reviewer's initials.
- Outgoing written (paper) communications shall be provided to the CCO for review in a timely manner (deemed to be within 10 business days of the date of the communication); the review copy shall be the copy ultimately destined for filing in the firm's general Correspondence file.

Periodically, associated persons with access to incoming and outgoing paper communications shall be trained regarding the procedures for opening and processing SCLC's communications.

# 13 THE FIDUCIARY STANDARD

The Advisers Act laid the groundwork for regulation of investment advisers and helped codify the fiduciary relationship investment advisers have with their advisory clients. This initial groundwork has been refined over the years. In 1960, the Advisers Act was amended to add a books and records requirement and an antifraud provision. 1970 saw some further amendments, which gave the SEC greater enforcement powers. By 1997, the National Securities Markets Improvements Act ("NSMIA") became effective. Before that time, regulation of investment advisers took place at both the federal and state level. NSMIA divided regulation of investment advisers between the SEC and the states, thereby ending dual regulation.

With respect to its clients, SCLC is a fiduciary. The firm's first duty is therefore to the interests of the client, over and above its own interests or those of its employees. These interests can come into conflict. Consequently the firm has sought from its inception to organize itself, its business practices, and its operating procedures so as to eliminate such conflicts of interest. Where this is not possible, we fully disclose them in the firm's Disclosure Brochure. In particular, we avoid conflicts of interest by shunning relationships with any firms that would oblige or otherwise motivate us to do business with them on behalf of our clients, other than by virtue of their financial soundness and the quality of their products or services.

Furthermore, the advice provided to clients must at least meet the most widely promulgated standards for fiduciaries, the Prudent Investor Rule. (Restatement of the Law Third, Trusts (Prudent Investor Rule), adopted and promulgated by the American Law Institute (Washington, D.C., May 1990) p. 30. See also the Uniform Prudent Investor Act, National Conference of Commissioners on Uniform State Laws (Chicago, 1994); and California's version of the UPIA, effective January 1, 1996, (West's Ann. Cal. Probate Code, Sections 16045-16054) The Prudent Investor Rule is a key principle, and informs all the firm's work. Specifically, we acknowledge and affirm that:

- Investment decisions concerning individual assets must be evaluated not in isolation, but in the context of the portfolio as a whole. Our firm assists investors in developing coherent and practical strategies for combining disparate assets into a viable whole.
- Risk and return are directly related. We help clients analyze and make conscious decisions about the level of risk appropriate for their accounts.
- Sound diversification is fundamental to risk management. We help clients reduce unnecessary risk by carefully diversifying their accounts.
- Fiduciaries must balance the need for current income and the protection of purchasing power. We take all prudent measures to achieve a real long term return, once inflation and taxes are taken into account.
- A prudently managed portfolio avoids unjustified expenses. Our firm is adamant in its drive to reduce fees and transaction costs borne by clients. All such costs are fully disclosed to clients as soon as they become ascertainable.

## 13.1 Antifraud Provisions

Section 206 of the Advisers Act contains an antifraud provision. In *Securities and Exchange Commission v. Capital Gains Research Bureau, Inc.* the Court recognized in applying the antifraud provision that a fiduciary relationship exists between an investment adviser and its clients.

Whereas registered representatives have transaction-based responsibilities to their customers, investment advisers have responsibilities arising from their status as fiduciaries to their clients. The fiduciary standard is therefore important throughout SCLC's activities.

The CCO, other principals and associated persons are all extensions of SCLC. As such, all these individuals must act in the best interests, first of the firm's clients, and second of SCLC. Failure to do so can personally subject such individuals to enforcement actions.

## 13.2 Fiduciary Duties

In general, the fiduciary duty owed by SCLC to its clients will guide employees, officers and directors in avoiding conflicts of interest, providing full and fair disclosure of services and fees, seeking best execution, and a number of other areas.

In clarifying the nature of fiduciary responsibilities, Section 206 states that it is unlawful for any investment adviser, using the mails or any means or instrumentality of interstate commerce, to carry out any of the following:

1. Employ any device, scheme, or artifice to defraud a client or prospective client
2. Engage in any transaction, practice, or course of business which defrauds or deceives a client or prospective client
3. Knowingly sell any security to or purchase any security from a client when acting as principal for his or her own account, or knowingly to effect a purchase or sale of a security for a client account when also acting as broker for the person on the other side of the transaction, without disclosing to the client in writing before the completion of the transaction the capacity in which SCLC is acting and obtaining the client's consent to the transaction
4. Engage in fraudulent, deceptive or manipulative practices.

Section 206 of the Adviser's Act sets forth some specific areas of concern, such as advertising (performance reporting, use of testimonials, other) and custody, along with prohibitions or applicable guidelines.

## 13.3 Procedures for Compliance with Fiduciary Requirements

The CCO is the individual charged with monitoring the Adviser's performance of services in the context of its fiduciary duties.

The CCO shall take steps designed to ensure that associated persons perform their job duties and responsibilities within the context of its fiduciary responsibility. Among these, each associated person will be required to complete an annual attestation of compliance. Record of the completion shall be maintained among the Adviser's central compliance files.

The CCO shall conduct or shall instruct a qualified party to conduct an annual fiduciary review. The results of the review shall be documented and retained among the Adviser's central compliance files. Findings of significance shall be reported to other senior managers.

# 14 REGULATORY AND INTERNAL INSPECTIONS

Registered investment advisers are subject to the ongoing scrutiny of regulatory agencies, including the states and or the SEC, depending upon the registration status of the entity, and are also likely to be affected by "cause" (client complaints or other investigation examinations). Regulatory examinations may be announced or unannounced.

SEC Rule 206(4)-7, effective February 2004, requires that advisers conduct an annual review of their policies and procedures to ensure their effective implementation.

## 14.1 Regulatory Inspections Background

The SEC's examination program was first established under the Securities Exchange Act of 1934, after the stock market crash of 1929 revealed alarming misconduct in the investments industry. The Exchange Act of 1934 created a federal regulatory system for securities exchanges and over-the-counter markets, and authorized the SEC to examine those markets. The powers granted to the SEC enabled it to conduct examinations in the public interest and for the protection of clients whenever it was deemed appropriate, as often as it deemed appropriate, on a regular cycle, or otherwise. This purpose underlies all of the SEC's examination authority.

In 1940, the examination authority of the SEC was broadened to cover investment companies and their affiliates when Congress enacted the Investment Company Act of 1940. The Investment Company Act authorized the SEC to mandate that investment companies keep records relating to their financial statements. It also authorized the SEC to conduct examinations and to require investment companies, their affiliates and auditors to provide copies or extracts of these records. Over the course of the next seventeen years, the SEC began to establish an active examination program for investment companies, ultimately leading to the formation of a cyclical examination program. The program was designed to cover a representative sampling of advisers, with a review of the field results conducted in the regional offices.

In 1960, Congress amended the Investment Advisers Act, authorizing the SEC to require investment advisers to keep specific books and records and to conduct examinations of advisers. By 1963, the SEC was conducting 219 yearly inspections of investment advisers.

The current inspection program began to evolve with the formation of the OCIE in 1995. In 1998, following the effectiveness of the National Securities Markets Improvement Act (NSMIA) a five-year inspection program was announced to include a five-year cycle for examination of most advisers, with only those advisers deemed to require special attention being examined more frequently. Accordingly, over the subsequent years, the SEC succeeded in inspecting more than 8,000 advisers no less than once every 5 years.

## 14.2 Scope of the Regulatory Inspection

At the onset of an examination, the regulatory representative should present identification to verify the jurisdiction that the individual represents. Questions regarding the legitimacy of the individual should be directed to the state or regional office to which the individual reports. Verification of the identification is important to ensure that non-public client data will not be revealed to or shared with unqualified persons.

The regulatory examination typically begins with an opening interview. At times, the interview questions are

provided in advance of the examination.

The duration of the regulatory examination can be as long as several weeks, but more commonly several days. The examination itself may conclude over time, with follow-up work conducted off-premises and through the mails, or telephonic exchanges of information.

### **14.3 Regulatory Exam Topics**

The regulatory exam will likely open with an interview to discuss the primary business systems of the adviser, and its internal controls. In each of these areas, the examiner will inquire about the adviser's compliance and control policies and procedures, and will evaluate their implementation and effectiveness. The adviser should be prepared to discuss several topics (with supporting documentation ready at hand) that may include:

- Consistency of portfolio management decisions with client mandates
- Order placement practices consistent with seeking best execution and disclosures made to clients
- Allocation of block and IPO trades
- Personal trading of access persons consistent with the firm's code of ethics
- Accurate securities pricing and net-asset values, if applicable
- Regular reconciliation of custodian records with Adviser records
- Controls over information
- Calculations and presentations of performance
- Accurate reconciliations of shareholder transactions, if applicable.

The SEC examiners typically provide a checklist of documentation that the adviser is required to produce.

### **14.4 Internal Inspection**

The adviser's annual review of its policies and procedures should consider, at minimum, any compliance matters that arose throughout the year, any changes in the business of the adviser or its affiliates, and any regulatory updates or changes that may affect the adviser's operations, administration, compliance or other business division. More frequent interim reviews are encouraged, but are not required.

To carry out its responsibility, SCLC is committed to conducting an annual inspection designed to evaluate the efficacy of its supervisory system, and to test its internal controls.

### **14.5 Procedures for Compliance with Inspection Requirements**

To meet SCLC's requirements under Rule 206(4)-7, the CCO will conduct an annual review that will include, at a minimum, a review of its written procedures, a review of new business areas, consideration of new regulations and regulatory trends, and appraisal of compliance matters that have occurred over the past year. The CCO may employ an independent third party to conduct the review.

A written record shall be maintained to record the annual review, and shall include a summary of the topics

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reviewed as well as plans or proposals for any relevant corrective action. The CCO shall document and oversee all corrective actions. Upon completion, the CCO shall present a report of the annual review to the senior principal(s) for sign off and final evaluation.

Either the CCO or a duly designated employee shall be responsible for coordinating all activities during a regulatory examination, so that the examiners are provided with documentation they request in a reasonable and acceptable time frame.

# 15 PROXY VOTING

In 2003, the SEC adopted Rule 206(4)-6 and rule amendments under the Act that address an investment adviser's fiduciary obligation to its clients/investors when the adviser has authority to vote their proxies. Rule 206(4)-6 requires that an investment adviser with such authority satisfy three general requirements:

- Adopt and implement written proxy voting policies and procedures reasonably designed to ensure that adviser votes client securities in the best interests of clients, and addressing how conflicts of interest shall be handled
- Disclose its proxy voting policies and procedures to clients and furnish them with a copy of those policies and procedures if they request it, and inform clients as to how they can obtain information from the adviser regarding the manner in which proxies on their securities were voted
- Maintain records as evidence of compliance with Rule 206(4)-6.

The adviser's proxy voting policies must be reasonably designed to ensure that individuals charged with voting responsibilities carry out those duties with the best interest of the clients in mind. According to SEC guidance, the policies and procedures should include:

- Factors used in determining whether or not the adviser will vote proxies
- Specific methodologies applied in voting proxies (such as actions to be taken in the case of proposed changes in corporate governance, compensation or stock option plans, expansion of investment authority, tender offers and related matters)
- Identifying and addressing material conflicts of interest
- Names and roles of personnel charged with proxy voting procedures ranging from decision-making to record-keeping, among other associated roles and responsibilities.

The adviser is required to disclose how a client can obtain a copy of the adviser's proxy voting policy, and how the client can obtain information on how its securities were voted.

Proxy voting records that must be maintained include:

- Written policies and procedures
- Proxy statements received for client securities
- Records of proxy votes cast for client securities, including any material supporting documentation relied upon in the process
- Record of the disclosure to clients of the adviser's policies and access to voting decisions, including client requests to view the adviser's proxy policies or proxy voting record, and the adviser's response.

## **15.1 Procedures for Compliance with Proxy Voting Requirements**

SCLC does not accept the right to vote proxies on behalf of clients.

SCLC discloses how a client can obtain a copy of SCLC's proxy voting policy in its Form ADV Part II Schedule F and in its plain English version, the SCLC Disclosure Brochure. The Disclosure Brochure is offered to clients at least once annually.