

# **Form ADV Firm Brochure Morgan Stanley Smith Barney LLC**

Institutional Services Program (directed brokerage)

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**This Brochure provides information about the qualifications and business practices of Morgan Stanley Smith Barney LLC (“MSSB”). If you have any questions about the contents of this Brochure, please contact us at (914) 225-1000. The information in this Brochure has not been approved or verified by the United States Securities and Exchange Commission (“SEC”) or by any state securities authority. Additional information about MSSB also is available on the SEC’s website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). Registration with the SEC does not imply a certain level of skill or training.**

## Item 2: Material Changes

This section identifies and discusses material changes to the ADV Brochure since the version of this Brochure dated March 28, 2014. For more details on any particular matter, please see the item in this ADV Brochure referred to in the summary below.

**Description of Advisory Services.** MSSB's Global Investment Manager Analysis Group, known as "GIMA", was formerly known as Consulting Group Investment Advisor Research Group or "CGIAR". (Item 4.B)

## Item 3: Table of Contents

Item 1: Cover Page .....	1
Item 2: Material Changes .....	2
Item 3: Table of Contents .....	3
Item 4: Advisory Business .....	4
A. Description of MSSB, Principal Owners .....	4
B. Description of Advisory Services .....	4
Consulting Group Trust Services .....	6
Tax and Legal Considerations .....	7
C. Customized Advisory Services and Client Restrictions .....	7
D. Portfolio Management Services to Wrap Fee Programs .....	7
E. Assets Under Management (“AUM”) .....	7
Item 5: Fees and Compensation .....	7
A. Compensation for Advisory Services .....	7
B. Payment of Fees .....	8
C. Additional Fees and Expenses .....	8
D. Prepayment of Fees .....	12
E. Other Compensation to Financial Advisors .....	12
Conflicts Relating to Financial Advisor Compensation .....	12
Item 6: Performance Based Fees and Side by Side Management .....	13
Item 7: Types of Clients .....	13
Item 8: Methods of Analysis, Investment Strategies and Risk of Loss .....	13
A. Method of Analysis and Investment Strategies .....	13
B. Material, Significant, or Unusual Risks Relating to Investment Strategies .....	16
C. Risks Associated with Particular Types of Securities .....	17
Item 9: Disciplinary Information .....	17
Item 10: Other Financial Industry Activities and Affiliations .....	20
A. Broker-Dealer Registration Status .....	20
B. Futures Commission Merchant, Commodity Pool Operator, or Commodity Trading Adviser Registration Status .....	20
C. Material Relationships or Arrangements with Industry Participants .....	20
D. Material Conflicts of Interest Relating to Other Investment Advisers .....	22
Item 11: Code of Ethics, Participation or Interest in Client Transactions and Personal Trading .....	23
A. Code of Ethics .....	23
B. Securities in Which You or a Related Person Has a Material Financial Interest .....	24
C. Investing and Other Interests in Securities Which You or a Related Person Recommend to Clients .....	24
D. Conflicts of Interest Created by Contemporaneous Trading .....	24
Item 12: Brokerage Practices .....	24
A. Factors in Selecting or Recommending Broker-Dealers for Client Transactions .....	24
B. Aggregation of Securities Transactions for Clients .....	24
Item 13: Review of Accounts .....	24
A. Frequency and Nature of Review of Client Accounts or Financial Plans .....	24
B. Factors Prompting Review of Client Accounts other than a Periodic Review .....	24
C. Content and Frequency of Account Reports to Clients .....	24
Item 14: Client Referrals and Other Compensation .....	24
A. Economic Benefit for Providing Investment Advice to Clients .....	24
B. Compensation to Unsupervised Persons for Client Referrals .....	24
Item 15: Custody .....	25
Item 16: Investment Discretion .....	25
Item 17: Voting Client Securities .....	25
Item 18: Financial Information .....	25
Exhibit: Affiliated Money Market Funds Fee Disclosure Statement and Float Disclosure Statement .....	26

## Item 4: Advisory Business

***Special Note: The program described in this Brochure is currently offered to clients on an asset-based fee or “wrap fee” basis. For the descriptive Brochure on the MSSB Institutional Services wrap fee programs, please contact your Financial Advisor. In the past, certain MSSB clients engaged MSSB to be compensated for the services in this program on the basis of commissions paid on securities transactions. This Brochure is intended for those clients only.***

### A. Description of MSSB, Principal Owners

#### Introduction to MSSB

Morgan Stanley Smith Barney LLC (“MSSB”, “we”, “us” or “our”) is a registered investment adviser, a registered broker-dealer, and a member of the New York Stock Exchange. MSSB is one of the largest financial services firms in the U.S. with branch offices in all 50 states and the District of Columbia.

MSSB teams offer a wide range of investment consulting services. This Brochure focuses on one of those services, Institutional Services (“IS”). MSSB focuses on providing a wide range of investment consulting services to institutional and high net worth individual clients, including (i) assistance in developing investment policy statements, (ii) asset allocation, (iii) investment manager, mutual fund, commingled fund, collective investment trust, exchange traded fund (“ETF” and together with mutual funds, commingled funds and collective investment trusts, “Funds”) and alternative investment analysis, (iv) performance reporting and (v) custody services. These services are delivered through a select group of institutional consulting teams located across the country that have significant experience serving the investment advisory needs of institutional as well as high net worth individual clients and are supported by a management team dedicated to institutional consulting. Clients include corporations, Taft-Hartley plans, foundations and endowments public and private defined benefit plans, 401(k) plan sponsors, family offices and high net worth individuals.

MSSB offers clients (“you”, “your” or “Client”) many different advisory programs. Many of MSSB’s advisory services are provided by its Consulting Group (“CG”) business unit. You may obtain Brochures for other MSSB investment advisory programs at [www.morganstanley.com/ADV](http://www.morganstanley.com/ADV) or by asking your Financial Advisor or (for Morgan Stanley Private Wealth Management clients) your Private Wealth Advisor. (Throughout the rest of this Brochure, “Financial Advisor” means either your Financial Advisor or your Private Wealth Advisor, as applicable.)

In addition, we reasonably expect to provide services as a “fiduciary” (as that term is defined in Section 3(21)(A) of the Employee Retirement Income Security Act of 1974 (“ERISA”) and/or Section 4975 of the Internal Revenue Code of 1986, as amended (the “Code”)), with respect to “Retirement Accounts” (as that term is described herein). For purposes of this brochure, the term “Retirement Account” will be used to cover (i) “employee benefit plans” (as defined under Section 3(3) of ERISA, which include pension, profit-sharing or welfare plans sponsored by private employers, as well as similar arrangements sponsored by governmental or other public employers; (ii) individual retirement accounts “IRAs” (as described in Section 4975 of the Code); and “Coverdell Educational Savings Accounts (“CESAs”).

### B. Description of Advisory Services

MSSB offers the following institutional consulting services to its clients:

***Assistance in the Preparation of Investment Objectives and Policies.*** MSSB shall assist the Client in Client’s review, evaluation and preparation of investment policies and objectives for the account. As set forth in “Performance Reporting” below, MSSB shall assist the Client in developing benchmarks for the performance of the account. MSSB also will provide the performance of the total account so as to assist the Client with the ability to determine progress toward investment objectives. Your Financial Advisor has been retained as a non-discretionary investment consultant. Accordingly, the Client shall be responsible for monitoring compliance with their investment policies and guidelines.

***Asset Allocation.*** Your Financial Advisor will review your asset allocation and will make asset allocation recommendations in accordance with your investment goals.

***Investment Searches.*** Your Financial Advisor will assist you in identifying and recommending investment managers and Funds (“Investment Products”). These recommendations are based either on (i) MSSB’s Global Investment Manager Analysis Group (“GIMA”) (using different methods to evaluate investment managers and Funds -- analysis on investment managers is provided through MSSB’s Fiduciary Services (“FS”) and Consulting and Evaluation Services (“CES”) programs) or (ii) analysis provided by MSSB’s Graystone Consulting business unit (“Graystone”). Graystone analysis on managers is conducted through its Manager Assessment Program, a proprietary investment management scoring system that assesses investment manager products in that database.

***Non-Researched Managers.*** Clients also may select investment managers outside of those covered by GIMA or Graystone analysis. Such outside managers, if qualified, will be offered through MSSB’s Investment Management Services Program (“IMS”). MSSB does not evaluate or make any representations concerning such investment managers and shall not assume any

liability for any loss, claim, damage or expense attributable to the client's selection of such managers.

For more information about FS, CES, and IMS or any other investment advisory services offered by MSSB, as well as assistance in determining which service may be best suited to your needs and objectives, please contact your Financial Adviser or refer to [www.morganstanley.com/ADV](http://www.morganstanley.com/ADV).

**Performance Reporting.** MSSB provides clients with customized performance reports that assess portfolio performance relative to benchmarks. The reports may include comparisons to recognized benchmarks and market segments.

**Custody and Statements.** For clients who elect to hold their assets in custody with MSSB, we serve as the custodian of all cash, securities and other assets held in the portfolio and credit the portfolio with dividends and interest paid on securities held and principal paid on called or matured securities in the portfolio. You will be provided with written confirmation of securities transactions and account statements at least quarterly.

**Alternative Investments Performance Reporting Service.** MSSB may provide institutional clients with alternative investments performance reporting. This is a non-discretionary service, and clients are responsible for executing participation agreements directly with each alternative investment. MSSB offers IS clients the ability to receive periodic reports that provide historical performance reporting of their alternative investments that were not purchased through MSSB, are not held in custody by MSSB and are not researched by MSSB. The alternative investment historical performance information provided by this service is based upon information provided, directly or indirectly, to MSSB by the issuer of the alternative investment, or by its sponsor, investment manager, administrator ("Performance Reporting AI"). MSSB's ability to provide historical or other performance reporting on alternative investments is dependent upon its ability to obtain such information from each Performance Reporting AI.

The performance reporting service enables the client to receive from MSSB periodic reports containing the Client's historical performance information as reported by the applicable Performance Reporting AI. Client may also receive composite reports that show historical performance of alternative investments as reported by the Performance Reporting AI, along with historical or other performance information on other investments that were/are acquired through MSSB, are held in custody by MSSB or are followed by MSSB research.

The performance information provided in a periodic performance review is based on information provided to MSSB by the Performance Reporting AI and is not independently verified by MSSB. MSSB shall not be liable for any misstatement or omission made by the Performance Reporting AI nor for any loss, liability, claim, damage or expense arising out of such misstatement or omission.

This reporting service is not intended to constitute investment advice or a recommendation by MSSB of any alternative investment and MSSB is not evaluating the appropriateness of

the initial investment or the continued investment in the alternative investments reported on as part of this service. In addition, the service does not constitute, create or impose a fee-based brokerage relationship, a fiduciary relationship or an investment advisory relationship under the Investment Advisers Act of 1940, as amended, with regard to the investments covered under this service. If the Client is an employee benefit plan or is otherwise subject to ERISA, MSSB is **NOT** acting as a fiduciary (as defined in ERISA) with the respect to the provision of these reporting services as described herein). MSSB is not responsible for and will not provide tax reporting with respect to any alternative investment reported on under this service.

The fee charged to the client for this service does not include any fee or charge for other services in connection with the client's participation in any alternative investment.

**Asset/Liability Analysis Services.** MSSB works with third party vendors, whose proprietary asset/liability modeling software is used to generate customized asset liability studies for defined benefit plan clients. The asset/liability analysis service provides certain cash flow modeling, liability funding analysis and funding strategies including custom contribution policies.

#### ***Institutional Services Program – For Participant-Directed Defined Contribution Plans.***

MSSB also offers a non-discretionary investment-consulting platform for participant directed defined contribution plans ("DC Plans"). Through this program, MSSB offers initial and ongoing investment consulting services to Plan Sponsors, including investment policy statement review, asset style analysis, mutual fund and ETF search and selection and performance reporting.

**Investment Consulting Fund Screening Program.** For participant-directed retirement plan sponsor clients, MSSB offers the DC Investment Consulting Fund Screening Program which is explained further in Item 6A below.

**Risk-Based Models.** In addition to providing fund screening services as explained further in Item 6A below, MSSB may provide risk-based asset allocation advice to retirement plans that hold assets in custody at a custodian other than MSSB. If requested, MSSB will provide plan sponsor clients with certain strategic asset allocation models ("model portfolios") that are prepared by MSSB's Global Investment Committee (the "GIC"). These model portfolios consist of certain groupings of Funds that have already been approved by the client. As the services are non-discretionary, the client must make the final choice of Funds to populate the model portfolio.

It will be the client's responsibility to ensure model recommendations by MSSB can be implemented within their recordkeeping platform. MSSB may assist in determining the capabilities of the client's recordkeeping platform; however it will be the ultimate responsibility of the client to ensure any recommendations are implemented and offered to participants in a manner that is consistent with the client's overall goals and objectives.

MSSB will provide the client with performance reporting for such models which will include model performance comprised of the fund performance within the model. MSSB will also provide the client with any changes/updates made to the asset allocation percentages within such models.

The client will be responsible for making any updates or changes to such models with its retirement plan provider. If requested, MSSB may provide education to plan participants in regard to risk tolerance through various approved educational pieces, however any such education does not represent any attempt by MSSB to use discretion or extend its fiduciary liability under the program client agreement.

*Administrative Services.* MSSB may also assist the retirement plan and other institutional clients with certain administrative functions as described below. These are not investment advisory services and MSSB does not assume status as a fiduciary under ERISA, the Investment Advisers Act of 1940 or any other applicable law or regulation in performing these services. MSSB provides the following administrative services:

- *Asset Classification* – MSSB shall advise as to which asset classes the Client may want to consider offering within the plan. MSSB can also provide the Client with general financial and investment information relating to such concepts as diversification and asset classification with respect to various asset classes and historic rates of return.
- *Plan Sponsor Education* – MSSB makes educational materials available to plan fiduciaries. The available materials may cover topics such as retirement plan administration, fiduciary responsibilities, plan design features and investments.
- *Employee Education* – MSSB shall collaborate with the Client to develop strategies relating to participant enrollment and ongoing employee education, and MSSB can work with the plan to deliver general financial and investment information relating to such concepts as diversification, asset allocation and historic rates of return.
- *Plan Provider Search Support.* MSSB shall assist Client with the preparation and distribution of Requests for Proposals (“RFP”) with respect to Client's search for a party to provide recordkeeping or related services for the plan, and shall provide assistance with the evaluation of RFP responses and corresponding finalist interviews and conversion support.
- *Plan Services and Expense Review.* MSSB shall provide Client with a report for the purpose of assisting Client with the review of various fees and plan expenses as they relate to the services provided by the plan. This report will generally consist of an overall assessment of current services and expenses, as well as a comparison of such services and expenses to those incurred by other plans of similar size and composition.

**Account Opening.** To enroll in the program described in this Brochure, you must enter into the program client agreement

(“Client Agreement”).

## Consulting Group Trust Services

The programs described in this Brochure may offer fully integrated wealth management solutions, which may include trusts. MSSB does not accept nor will it act as a trustee (an MSSB affiliate, such as Morgan Stanley Private Bank, National Association, may be serving as trustee for existing accounts and is closed to new accounts). In order to offer to you complete solutions, MSSB has created the Consulting Group Trust Services Program (“CG Trust Services”) with external trust companies (including external banks which may serve as a corporate trustee) to provide trustee services for the assets in your account while you receive investment advisory services from MSSB.

To receive trustee services through CG Trust Services, you and your attorney will create separate agreements with an external trust company to govern the trust and you will appoint a trustee to act on your behalf; in certain situations, you may appoint separate administration and investment trustees. You or your designees will sign these separate agreements and may pay a separate fee to your attorney. External trust companies and MSSB typically charge separate fees to CG Trust Services client accounts for their respective services, which may be higher than fees charged to clients outside of the CG Trust Services Program for comparable services. In certain limited circumstances, MSSB will compensate an external trust company for the services it provides to a client account. Neither MSSB nor your Financial Advisor will be paid by the external trust company. In certain circumstances, MSSB or an affiliate may pay compensation to or receive an indirect economic benefit from an unrelated third party (see: “Client Referrals and Other Compensation”, Item 14 below).

As part of CG Trust Services, you or your selected trustee, with investment authority, may delegate investment discretion directly to MSSB or receive non-discretionary investment advisory services through the programs offered by Consulting Group. Additionally, certain external trust companies have contractually agreed to use the services (including MSSB custody services) described in this Brochure for each CG Trust Services client (and in some cases, former CG Trust Services clients), unless the client has issued contrary instructions, and so long as such use of MSSB services will not cause the external trust company to violate any duty or obligation.

Regardless of the external trust company you select, unless you have appointed another custodian, you can hold your assets in custody at MSSB through CG Trust Services. Accounts outside of CG Trust Services may be subject to different custody arrangements.

MSSB has made arrangements to have a number of external trust companies participate in CG Trust Services, as described above. While these arrangements are designed to enhance the administrative and operational experience of clients who appoint such an external trust company and MSSB to service the same assets, these arrangements could pose a conflict of interest for MSSB and its representatives by creating an incentive for them to introduce their clients to those external trust companies who

have such arrangements with CG Trust Services over other external trust companies.

The decision to participate in CG Trust Services and the selection of the trustee and attorney are your decision and responsibility. MSSB and its affiliates do not provide tax and legal advice (see: "Tax and Legal Considerations", Item 4(B) below). For additional information and to determine eligibility, please contact your Financial Advisor.

### **Tax and Legal Considerations**

Neither MSSB nor any of our affiliates provide tax or legal advice and, therefore, are not responsible for developing, implementing or evaluating any tax strategies that may be employed by the client. The client should develop any such strategies or address any legal or tax-related issues with a qualified legal or tax adviser.

Investment in MLPs entails different risks, including tax risks, than is the case for other types of investments. Investors in MLPs hold "units" of the MLP (as opposed to a share of corporate stock) and are technically partners in the MLP. Holders of MLP units are also exposed to the risk that they will be required to repay amounts to the MLP that are wrongfully distributed to them. Almost all MLPs have chosen to qualify for partnership tax treatment. Partnerships do not pay U.S. federal income tax at the partnership level. Rather, each partner of a partnership, in computing its U.S. federal income tax liability, must include its allocable share of the partnership's income, gains, losses, deductions, expenses and credits. A change in current tax law, or a change in the business of a given MLP, could result in an MLP being treated as a corporation for U.S. federal income tax purposes, which would result in such MLP being required to pay U.S. federal income tax on its taxable income. The classification of an MLP as a corporation for U.S. federal income tax purposes would have the effect of reducing the amount of cash available for distribution by the MLP and could cause any such distributions received by the an investor to be taxed as dividend income. If you have any questions about the tax aspects of investing into an MLP, please discuss with your tax advisor.

Investors in MLP portfolios will receive a Schedule K-1 for each MLP in the portfolio, so they will likely receive numerous Schedule K-1s. Investors will need to file each Schedule K-1 with their federal tax return. Also, investors in MLP portfolios may be required to file state income tax returns in states where the MLPs in the portfolio operate. Since some Schedule K-1s may not be provided until after the due date for the federal or state tax return, investors in MLP portfolios may need to obtain an extension for filing their federal or state tax returns. Please discuss with your tax advisor how an investment in MLPs will affect your tax return.

Tax laws impacting MLPs may change, and this could impact any tax benefits that may be available through investment in an MLP portfolio.

### **C. Customized Advisory Services and Client Restrictions**

In IS, services are provided based on an analysis of each client's objectives and risk tolerance.

**Restrictions.** The Client may impose reasonable restrictions on account investments. For example, you may restrict MSSB or the managers from buying specific securities, a category of securities (e.g., tobacco companies) or Fund shares. If you restrict a category of securities, we or the manager will determine which specific securities fall within the restricted category. In doing so, we or the manager may rely on research provided by independent service providers). Any restrictions you impose on individual securities have no effect on Fund holdings since Funds operate in accordance with the investment objectives and strategies described in their prospectuses.

### **D. Portfolio Management Services to Wrap Fee Programs**

This item does not apply to the advisory programs described in this Brochure. IS is also offered as a wrap fee-only program; please see your Financial Advisor for the descriptive Brochure for this program.

### **E. Assets Under Management ("AUM")**

MSSB managed client assets of \$783,409,682,555 as of December 31, 2014. Of this amount, MSSB managed \$299,334,359,159 on a discretionary basis and \$484,075,323,396 on a non-discretionary basis. These amounts represent the client assets in all of our investment advisory programs. We calculated them using a different methodology than the "assets under management" we report in our ADV Part 1 filed with the SEC.

## **Item 5: Fees and Compensation**

**Introduction.** Currently, the IS program is offered only as an asset-based fee based program. However in the past, the IS program was offered to certain clients with a fee structure in which MSSB is compensated by receiving brokerage commissions on account transactions. This Brochure applies only to accounts operated under that fee structure. For the descriptive Brochure on the asset-based or "wrap fee" IS program, please contact your Financial Advisor.

### **A. Compensation for Advisory Services**

You may pay MSSB for the services provided in the IS program by:

- directed brokerage (i.e. paying commission on a transaction-by-transaction basis);
- an asset-based fee (at a maximum annual fee rate of 2.5%). Our separate Wrap Brochure about the IS program, available from your Financial Advisor, describes the asset based fee option; or
- alternatively, in some cases, institutional clients may negotiate an annual fixed dollar amount, paid quarterly.

In the commission based advisory programs, we receive the brokerage commissions on transactions executed by MSSB. Clients may choose to pay brokerage transactions on a “cents per share” or as a “percentage discount” off MSSB’s standard brokerage commission schedule. The brokerage commission schedule is very complex and is dependent on many factors (i.e. the stock exchange where the security is executed or the liquidity of the security) for more information please discuss with your Financial Advisor. The brokerage fees are negotiable.

## B. Payment of Fees

In the advisory programs listed in this Brochure, you will pay for our advisory fee through the execution of securities transactions. Therefore, your fees will accrue each time your investment manager executes a trade. The maximum commissions charged to the account will not exceed the maximum advisory fee available for your program. In addition to the MSSB fee (paid with securities transactions), you may, at your choice, pay your investment management fee from your advisory account or you may be billed separately.

If client elects a third party custodian, the client has the option of paying us directly or we can bill the custodian.

You may terminate participation in the programs described in this Brochure at any time by giving written notice to us. We may (but are not obligated to) accept an oral notice of termination from you in lieu of the written notice. If participation in any of the programs described in this Brochure is terminated, any advisory fees paid in advance will be refunded on a pro-rata basis.

***ERISA Fee Disclosure for Retirement Accounts.*** In accordance with Department of Labor regulations under Section 408(b)(2) of ERISA, MSSB is required to provide certain information regarding our services and compensation to assist fiduciaries and plan sponsors of those retirement plans that are subject to the requirements of ERISA in assessing the reasonableness of their plan’s contracts or arrangements with us, including the reasonableness of our compensation. This information (the services we provide as well as the fees) is provided to you at the outset of your relationship with us and is set forth in your advisory contract with us (including the Fee table, other exhibits and, as applicable, this document), and then at least annually to the extent that there are changes to any investment-related disclosures for services provided as a fiduciary under ERISA.

## C. Additional Fees and Expenses

If you open an account in one of the programs described in this Brochure, you will pay commission on the transactions in your account for investment advisory services (except for IMS DB where we don’t provide advice), custody of securities and trade execution with or MSSB. For more information regarding brokerage commissions please see Item 4B and Item 12A (3) and 12B. The program fees do not cover:

- the costs of investment management fees and other expenses charged by the Funds that you selected
- “mark-ups,” “mark-downs,” and dealer spreads (A) that MSSB or its affiliates may receive when acting as principal

in certain transactions where permitted by law or (B) that other broker-dealers may receive when acting as principal in certain transactions effected through MSSB and/or its affiliates acting as agent, which is typically the case for dealer market transactions (e.g., fixed income and over-the-counter equity)

- brokerage commissions or other charges resulting from transactions not effected through MSSB or its affiliates
- MSSB account establishment or maintenance fees for its Individual Retirement Accounts (“IRA”) and Versatile Investment Plans (“VIP”), which are described in the respective IRA and VIP account and fee documentation (which may change from time to time)
- account closing/transfer costs
- processing fees or
- certain other costs or charges that may be imposed by third parties (including, among other things, odd-lot differentials, transfer taxes, foreign custody fees, exchange fees, supplemental transaction fees, regulatory fees and other fees or taxes that may be imposed pursuant to law).

### Funds in Advisory Programs

Investing in mutual funds and ETFs (collectively, “Funds”) may be more expensive than other investment options offered in your advisory account. In addition to our fee, you pay the fees and expenses of the Funds in which your account is invested. Fund fees and expenses are charged directly to the pool of assets the Fund invests in and are reflected in each Fund’s share price. These fees and expenses are an additional cost to you and are not included in the fee amount in your account statements. Each mutual fund and ETF expense ratio (the total amount of fees and expenses charged by the Fund) is stated in its prospectus. The expense ratio generally reflects the costs incurred by shareholders during the mutual fund’s or ETF’s most recent fiscal reporting period. Current and future expenses may differ from those stated in the prospectus.

You do not pay any sales charges for purchases of mutual funds in programs described in this Brochure. However some mutual funds may charge, and not waive, a redemption fee on certain transaction activity in accordance with their prospectuses.

**Expense Payments, Data Analytics and Administrative Service Fees.** MSSB receives expense payments and fees for data analytics, recordkeeping and related services, which are more fully described below. Administrative fees may be viewed in part as a form of revenue-sharing if and to the extent they exceed what the mutual fund would otherwise have paid for these services.

MSSB provides fund families or their affiliated service providers with opportunities to sponsor meetings and conferences and grants them access to our branch offices and Financial Advisors for educational, marketing and other promotional efforts. Fund representatives may work closely with our branch offices and Financial Advisors to develop business strategies and plan promotional and educational activities. In addition, MSSB typically receives payments from funds or their affiliates in connection with these promotional efforts to help offset expenses incurred for sales events and training programs as well



as client seminars, conferences and meetings. Fund families independently decide what they will spend on these activities and may also invite our Financial Advisors to attend fund family sponsored events. Expense payments may include meeting or conference facility rental fees and hotel, meal and travel charges.

Certain fund families (referred to as “Global Partners” or “Emerging Partners”) dedicate significant financial and staffing resources to these efforts and may receive supplemental sales data analytics as well as additional opportunities to sponsor firm events and promote their funds to our Financial Advisors and clients. Global Partners commit \$550,000 per year for training and sales meeting expenses and pay a fee of \$200,000 per year for data analytics. Emerging Partners commit \$250,000 per year for training and sales expenses and pay a fee of \$100,000 per year for data analytics. These facts present a conflict of interest for MSSB and our Financial Advisors to the extent they lead us to focus on funds from those fund families, including our Global and Emerging Partners, that commit significant financial and staffing resources to promotional and educational activities instead of on funds from fund families that do not purchase sales data analytics or do not commit similar resources to the activities. In order to mitigate this conflict, Financial Advisors and their Branch Office Managers do not receive additional compensation for recommending fund families sponsored by our Global or Emerging Partners or any other fund families that provide significant sales and training support.

Global and Emerging Partners may present a certain number of funds or other products to GIMA Group subject to a shorter timeline for GIMA to begin its review of such products if there is a backlog at the time the fund or product is being considered. However, products and funds offered by Global and Emerging Partners are subjected to the same GIMA due diligence process and standards as all other investment products and are not given preference in terms of approval by GIMA for offering in MSSB advisory programs.

MSSB selects the Global and Emerging Partners fund families based on a number of quantitative and qualitative criteria. Our Global Partners are denoted by an asterisk on the Revenue-Sharing Fund Families list available by going to our website, <http://www2.morganstanley.com/wealth/investmentsolutions/mutualfunds.asp> and clicking on “Revenue Sharing Arrangements” at the bottom of the page.

Fund family representatives are allowed to occasionally give nominal gifts to Financial Advisors, and to occasionally entertain Financial Advisors (subject to an aggregate entertainment limit of \$1,000 per employee per fund family per year). MSSB’s non-cash compensation policies set conditions for each of these types of payments and do not permit any gifts or entertainment conditioned on achieving any sales target.

**Client selection of MSSB affiliated funds.** Where clients select to invest in mutual funds where the investment adviser is a MSSB affiliate, in addition to the program fee paid by clients, MSSB and its affiliates may also receive investment management fees and related administrative fees. Since the affiliated sponsor or manager receives additional investment management fees and other fees, MSSB has a conflict to recommend MSSB affiliated mutual funds.

For more information, please refer to the document “Mutual Fund Share Classes and Compensation,” at [http://www2.morganstanley.com/wealth/investmentsolutions/pdfs/MF\\_share\\_classes.pdf](http://www2.morganstanley.com/wealth/investmentsolutions/pdfs/MF_share_classes.pdf) and also available from your Financial Advisor on request.

**Share classes.** Mutual fund companies typically offer different ways to buy mutual fund shares. In addition to the more broadly known retail share classes (A, B and C shares), fund companies have developed additional types of specialized share classes designed for specific advisory programs. If available, clients’ shares are converted into the share class required by the mutual fund for that type of account. Depending on the circumstances, clients’ shares are converted into a share class that has a lower or a higher expense ratio. Advisory share classes usually have a lower expense ratio than the share classes that MSSB previously offered in the program. However, we may continue to offer non-advisory share classes if, for example, there is no equivalent advisory share class available or we believe that the non-advisory share class is likely to be the most cost effective share class. Once we make an advisory share class available for a particular mutual fund, clients can only buy the advisory class shares (not the non-advisory class shares) of that mutual fund in the program.

If available, we (without notice to you) may convert any mutual fund in your IS Program account to a share class of the same mutual fund which is a load-waived or no-load share class such as an Institutional share or Financial Intermediary share, or to a share class that is available only to investment advisory clients (collectively, an “Investment Advisory Share”), to the extent available. On termination of your account, or the transfer of mutual fund shares out of your account into another account including a MSSB retail brokerage account, if, at the time of termination or transfer, your account includes Investment Advisory Shares or Managed Account Funds, we may convert these funds to a share class that is available in non-advisory accounts (even though the expense ratio for that share class may be higher than the expense ratio for the fund previously held in your account), or we may redeem these mutual fund shares. The non-advisory mutual fund share class generally has higher operating expenses than the corresponding Investment Advisory Share, which may negatively impact investment performance.

## Custody

**MSSB does not act as custodian.** If you retain a custodian other than MSSB, your outside custodian will advise you of your cash sweep options and, as described in the Client Agreement, you will have the option of instructing us on whether you want the fee billed to you directly or to the outside custodian selected by you, and the following sections on administrative service fees and cash sweeps will not apply to you.

**MSSB acts as custodian.** Unless you instruct us otherwise, MSSB will maintain custody of all cash, securities and other assets in the account and the following sections on cash sweeps and administrative service fees will apply to you.

**Administrative Service Fees When MSSB Acts as Custodian.** MSSB and/or its affiliates receive compensation from funds or

their affiliated service providers for providing certain recordkeeping and related services to the funds. These charges are typically based upon the number or aggregate value of client positions and the levels of services provided. We process transactions with certain fund families on an omnibus basis, which means we consolidate our clients' trades into one daily trade with the fund, and therefore maintain all pertinent individual shareholder information to the fund. Trading in this manner requires that we maintain the transaction history necessary to track and process sales charges, annual service fees and deferred sales charges for each position as applicable, as well as other transaction details required for ongoing position maintenance purposes. For these services, funds pay up to 0.16% (\$16 per \$10,000) on fund assets held by non-retirement investors in the advisory program covered by this Brochure.

In addition to the omnibus accounting services that we provide for the funds, we are also responsible for delivery of disclosure documents; processing of dividend distributions; tax reporting functions on their behalf.

Notwithstanding the foregoing, MSSB does not receive such payments from mutual fund assets held in Retirement Accounts.

## Cash Sweeps

Generally, some portion of your account will be held in cash. If MSSB acts as custodian for your account, it will effect "sweep" transactions of uninvested cash and allocations to cash, if any, in your account into:

- interest-bearing bank deposit accounts ("Deposit Accounts") established under the Bank Deposit Program ("BDP") or
- money market mutual funds (each, a "Money Market Fund" and, together with BDP Deposit Accounts, "Sweep Investments"). The Money Market Funds are managed by Morgan Stanley Investment Management Inc. or another MSSB affiliate.

If you do not select a Sweep Investment when you open your account, your Sweep Investment will be BDP if you are eligible.

Uninvested cash and allocations to cash including assets invested in Sweep Investments are included in the Fee calculation hereunder.

You acknowledge that MSSB may with 30 days written notice (i) make changes to these sweep terms; (ii) make changes to the terms and conditions of any available sweep investment; (iii) change, add, or delete the products available as a sweep option; (iv) transfer your sweep investment from one sweep product to another.

Clients that are considered Retirement Accounts or have Coverdell Education Savings Accounts should read the Exhibit to this Brochure ("Affiliated Money Market Funds Fee Disclosure Statement and Float Disclosure Statement").

The custodian will effect sweep transactions only to the extent permitted by law and if you meet the Sweep Investment's eligibility criteria.

**Bank Deposit Program.** Through the Bank Deposit Program, Deposit Accounts are established for you at one or more of the following banks (individually and collectively, the "Sweep Banks"): (i) Morgan Stanley Bank, N.A. and/or (ii) Morgan Stanley Private Bank, National Association. The Sweep Banks are affiliated with MSSB. The Sweep Banks pay interest on the Deposit Accounts established under the BDP. Your deposits at the Sweep Banks will be insured by the Federal Deposit Insurance Corporation ("FDIC") up to applicable limits, in accordance with FDIC rules, and subject to aggregation of all the accounts (including, without limitation, certificates of deposit) that you hold at the Sweep Banks in the same capacity. Bank deposits held through the BDP are not covered by SIPC or excess coverage.

If BDP is your Sweep Investment, you authorize us, as your agent, to establish the Deposit Accounts for you, and to make deposits into, withdrawals from and transfers among the Deposit Accounts.

Terms of the Bank Deposit Program are further described in the Bank Deposit Program Disclosure Statement, which will be provided to you upon your first investment in the Bank Deposit Program. You may also obtain the Bank Deposit Program Disclosure Statement as well as current interest rates applicable to your account, by contacting your Financial Advisor or through MSSB's website at [http://www.morganstanley.com/wealthinvestmentstrategies/pdf/BDP\\_disclosure.pdf](http://www.morganstanley.com/wealthinvestmentstrategies/pdf/BDP_disclosure.pdf) and [www.moganstanley.com/wealth/investmentstrategies/ratemonitor.asp](http://www.moganstanley.com/wealth/investmentstrategies/ratemonitor.asp). We may amend the list of Sweep Banks at any time with 30 days written notice to you. If you are participating in the Bank Deposit Program, please read the Bank Deposit Program Disclosure Statement carefully.

Please note the following: (i) you are responsible to monitor the total amount of deposits you have at each Sweep Bank in order to determine the extent of FDIC insurance coverage available to you; and (ii) MSSB is not responsible for any insured or uninsured portion of your deposits at any of the Sweep Banks.

If BDP is your Sweep Investment, you should be aware that, each Sweep Bank will pay MSSB a fee equal to the percentage of the average daily deposit balances in your Deposit Account at the Sweep Banks. Your Financial Advisor will not receive a portion of these fees or credits. In addition, MSSB will not receive cash compensation or credits in connection with the BDP for assets in the Deposit Accounts for Retirement Accounts or Coverdell Education Savings accounts. Also, the affiliated Sweep Banks have the opportunity to earn income on the BDP assets through lending activity, and that income is usually significantly greater than the fees MSSB earns on affiliated Money Market Funds. Thus, MSSB has a conflict of interest in selecting or recommending BDP as the Sweep Investment, rather than an eligible Money Market Fund.

***Unless otherwise specifically disclosed to you in writing, such as in connection with the Bank Deposit Program noted above, investments and services offered through MSSB are not insured by the FDIC, are not deposits or other obligations of, or guaranteed by, the Sweep Banks, and involve investment risks, including possible loss of the principal invested.***

**Money Market Funds.** We may, in our sole discretion, offer Money Market Funds as Sweep Investments. The Money Market Funds are affiliated with MSSB. You understand that purchases and redemptions of Money Market Fund shares may be effected only through MSSB and that you may not directly access the Money Market Fund.

If a Money Market Fund is your Sweep Investment, you authorize us, as your agent, to make investments in, and redemptions from, the Money Market Fund.

Each of these Money Market Funds is a separate investment with different investment objectives. Their fees, expenses, minimum investment requirements, dividend policies and procedures may vary. Before you invest in any Money Market Fund, read its prospectus carefully. Money Market Fund shares are neither insured nor protected by the FDIC. Investment in any money market fund is a purchase of securities issued by the money market fund, not a bank deposit.

Certain of the Money Market Funds described above have minimum investment requirements. In addition, MSSB may require a minimum initial investment to activate some or all of the Sweep Investments. If you do not meet the minimum initial investment, uninvested cash and allocations to cash in eligible accounts will remain un-invested or be invested in the BDP.

In addition, certain of the Money Market Funds have minimum balance requirements. For eligible accounts, if your investment falls below the minimum balance requirement, MSSB may redeem and reinvest all of your shares in the BDP. Once your sweep option has been changed, we will not automatically change it back to your previous Sweep Investment even if you meet the minimum initial investment and/or balance requirements. You must contact your Financial Advisor to do so. However, if a pattern develops of falling below the minimum balance requirement, we may preclude you from investing in that Sweep Investment in the future.

We may offer other money market funds as a non-sweep investment choice. You may purchase shares in these money market funds by giving specific orders for each purchase to your Financial Advisor. However, uninvested cash in your account will not be swept into these money market funds.

Since the Money Market Funds are sponsored or managed by MSSB affiliates, those MSSB affiliates receive advisory fees and may receive other fees from the Money Market Funds if your account cash balances are invested in the Money Market Funds. Therefore, MSSB has a conflict of interest in selecting or recommending the Money Market Funds as your Sweep Investment. **For Retirement Accounts with cash balances invested in Money Market Funds sponsored or managed by MSSB affiliates, certain fees received and retained by such MSSB affiliates will be credited to the account or offset against the advisory program fee. Please see the attached Exhibit “Affiliated Money Market Funds Fee Disclosure Statement and Float Disclosure Statement” for more details.**

The above provisions may not apply if you are not a U.S. resident. If you are not a U.S. resident, please contact your

Financial Advisor to determine whether the BDP or a Money Market Fund will be your default Sweep Investment.

**Alternatives to the Bank Deposit Program.** All accounts that are eligible can choose from among certain Sweep Investments as alternatives to the Bank Deposit Program.

Please contact your Financial Advisor for more information about choosing an alternative Sweep Investment. In addition, you may obtain information with respect to the current yields and interest rates on the available Sweep Investments by contacting your Financial Advisor or through MSSB’s web site at [www.morganstanley.com/wealth/investmentstrategies/ratemonitor.asp](http://www.morganstanley.com/wealth/investmentstrategies/ratemonitor.asp).

**Miscellaneous.** The rate of return on a default Sweep Investment may be higher or lower than the rate of return available in other Sweep Investments. Neither MSSB nor any affiliate is responsible to you if the default Sweep Investment has a lower rate of return than the other available Sweep Investments or causes any tax consequences resulting from your investment in the default Sweep Investment. We may, in our sole discretion determine and change the Sweep Investments available in your account. We may, at any time, discontinue offering any available Sweep Investment and, upon notice to you, cease offering your Sweep Investment. If we cease offering your Sweep Investment and you do not select a new Sweep Investment, your new Sweep Investment will be the default Sweep Investment as designated by us for such account.

Generally, temporary “sweep” transactions of all uninvested cash balances, allocations to cash and cash equivalents, if any, in the account will commence, to the extent permitted by applicable law, on the next business day, with dividends credited to the client on the second business day. (If cash is deposited after normal business hours, the deposit may be credited on our recordkeeping system, for purposes of the preceding sentence, as having been received on the following business day.) (For certain accounts — namely accounts established as Basic Security Accounts that have less than \$1,000 in the Sweep Investment — amounts awaiting investment will sweep weekly.)

Neither MSSB nor any affiliate will be responsible for any losses resulting from a delay in the investment of cash balances.

You authorize us to invest your funds in your Sweep Investment and to satisfy debits in your account by redeeming shares or withdrawing funds, as applicable, from your Sweep Investment. Upon any such sale, gains on your position may be taxable.

You may change your Sweep Investment to another Sweep Investment, if available for your account, by contacting your Financial Advisor. You agree that upon selection of a new Sweep Investment we may, as applicable, sell your shares in, or withdraw your funds from, your current Sweep Investment and, as applicable, purchase shares or deposit funds in your new Sweep Investment. There may be a delay between the time we sell shares or withdraw funds from your current Sweep Investment and the time we purchase shares or deposit funds in your new Sweep Investment. You may not earn interest or dividends during the time your funds are not invested.

**Conflicts of Interest Regarding Sweep Investments.** If your Sweep Investment is a Money Market Fund, as available, then

the account, as well as other shareholders of the Money Market Fund, will bear a proportionate share of the other expenses of the Money Market Fund in which the account's assets are invested.

If your Sweep Investment is a Money Market Fund, you understand that Morgan Stanley Investment Management Inc. (or another MSSB affiliate) may receive an investment management fee for managing the Money Market Fund and that Morgan Stanley Distributors Inc., or another one of our affiliates, may receive compensation in connection with the operation and/or sale of shares of the Money Market Fund, which may include a distribution fee pursuant to Rule 12b-1 under the Investment Company Act of 1940, to the extent permitted by applicable law.

You understand that unless you are a Retirement Plan, the Fee will not be reduced by the amount of the Money Market Fund management fee or any shareholder servicing and/or distribution or other fees we or our affiliates may receive in connection with the assets invested in the Money Market Fund. For additional information about the Money Market Fund and applicable fees, you should refer to each Money Market Fund's prospectus.

If your Sweep Investment is the Bank Deposit Program, you should be aware that, each Sweep Bank will pay MSSB a fee equal to the percentage of the average daily deposit balances in your Deposit Account at the Sweep Banks. The fee received by MSSB may affect the interest rate paid by the Sweep Banks on your Deposit Accounts. Your Financial Advisor will not receive a portion of the fee. In addition, MSSB will not receive the fee in connection with the Program for assets in the Deposit Accounts for Retirement Accounts. Affiliates of MSSB, however, may receive a financial benefit in the form of credit allocations made for financial reporting purposes. The amount of this benefit will vary and will be based on the average daily deposit balances in the Deposit Accounts at each Sweep Bank. Generally, these benefits will increase as more funds are deposited through the Bank Deposit Program. No separate charges, fees or commissions will be imposed on your account as a result of or otherwise in connection with the Bank Deposit Program.

In addition, MSSB, the Sweep Banks and their affiliates receive other financial benefits in connection with the Bank Deposit Program. Through the Bank Deposit Program, each Sweep Bank will receive a stable, cost-effective source of funding. Each Sweep Bank intends to use deposits in the Deposit Accounts at the Sweep Bank to fund current and new businesses, including lending activities and investments. The profitability on such loans and investments is generally measured by the difference, or "spread," between the interest rate paid on the Deposit Accounts at the Sweep Banks and other costs of maintaining the Deposit Accounts, and the interest rate and other income earned by the Sweep Banks on those loans and investments made with the funds in the Deposit Accounts. The income that a Sweep Bank will have the opportunity to earn through its lending and investing activities is expected to be greater than the fees earned by us and our affiliates from managing and distributing the money market funds available to you as a sweep investment.

## **D. Prepayment of Fees**

You will pay your investment management fees quarterly in advance. If you terminate your advisory agreement with the

investment manager or with us anytime during billing quarter, we will refund you the pro rata fee.

## **E. Other Compensation to Financial Advisors**

MSSB is a full service broker dealer and we offer many types of financial products to clients. A sample of the investment products include, stocks, bonds, futures, mutual funds, private funds, insurance, options and structured products. We allocate to your Financial Advisor, on an ongoing basis, part of the fees payable to us in connection with your account. The Financial Advisor may receive different compensation depending on which program you invest in, the asset class within a program that you select (e.g. equity vs. fixed income), and the rate and amount of your fee. The amount we allocate to your Financial Advisor in connection with accounts opened in programs described in this Brochure may be more than, if you participate in other MSSB investment advisory programs, or if you pay separately for investment advice, brokerage and other services. Your Financial Advisor may therefore have a financial incentive to recommend one of the programs in this Brochure instead of other MSSB programs or services.

If you invest in one of the programs described in this Brochure, your Financial Advisor may charge a fee less than the maximum fee stated above. The amount of the fee you pay is a factor we use in calculating the compensation we pay your Financial Advisor. Therefore, Financial Advisors have a financial incentive not to reduce fees. If your fee rate is below a certain threshold, we give your Financial Advisor credit for less than the total amount of your fee in calculating his or her compensation. Therefore, Financial Advisors also have a financial incentive not to reduce fees below that threshold.

## **Conflicts Relating to Financial Advisor Compensation**

The sale of some financial products will benefit your Financial Adviser more than others. Therefore, your Financial Advisor has an incentive to recommend certain investment products that pay your Financial Advisor a greater amount. We generally disclose the conflicts to clients at the point of sale or on the confirmation.

**Mutual Funds.** Traditional mutual funds are not available in the advisory programs described in this Brochure. Generally, if an investment manager wants to use a mutual fund, they will use a no fee fund (a fund that has no expenses). If you have a no fee fund within your portfolio, you will have to liquidate the fund upon termination of the relationship with the investment manager.

You may be able to invest with managers directly or through brokers or agents not affiliated with MSSB, instead of investing through the IS program described.

In the programs described in this Brochure, we do not charge any advisory fee in addition to commissions. Less than 50% of our revenue generated from our advisory business comes from commissions and compensation such as distribution fees for the sale of investment products we recommend to clients

## Item 6: Performance Based Fees and Side by Side Management

This item is not applicable to the programs described in this Brochure.

## Item 7: Types of Clients

MSSB's clients include individuals, trusts, and institutions, including, banking or thrift institutions, pension and profit sharing plans, plan participants, other pooled investment vehicles (e.g., hedge funds), charitable organizations, corporations, other businesses, state or municipal government entities, investment clubs and other entities.

In the IS program, minimum account sizes are set by each manager.

## Item 8: Methods of Analysis, Investment Strategies and Risk of Loss

### A. Method of Analysis and Investment Strategies

MSSB does not provide portfolio management services in the programs listed in this Brochure. Your investment manager provides the discretionary management of your account. Financial Advisors may recommend a particular investment manager focusing on a particular strategy to clients in the IS program. Investing in securities involves risk of loss that you should be prepared to bear.

In IS we offer a wide range of investment products (including managers, mutual funds and ETFs) that we have selected and approved. This Item 8.A describes more generally how we select and terminate Investment Products from these programs. If managers have more than one strategy, we may include only some of those strategies in the programs described in this Brochure, may carry different strategies in different programs, and assign different statuses to different strategies. Please refer to the discussion in Item 4.B for a complete description of the programs.

### MSSB's Global Investment Manager Analysis Group

GIMA evaluates Investment Products. GIMA may delegate some or all of its functions to an affiliate or third party. Managers may only participate in the FS or CES program if they are on GIMA's Focus List or Approved List discussed below. You may obtain these lists from your Financial Advisor. In each program, only some of the Investment Products may be available.

As well as requiring Investment Products to be on the Focus List or Approved List, we look at other factors in determining which Investment Products we offer in these programs, including:

- program needs (such as whether we have a sufficient number of Investment Products available in an asset class)
- client demand and
- the manager's or Fund's minimum account size.

We automatically terminate Investment Products in the CES and FS programs if GIMA downgrades them to "Not Approved." We may terminate Investment Products from the program for other reasons (e.g., the manager or Fund has a low level of assets under management in the program, the manager or Fund has limited capacity for further investment, or the manager or Fund is not complying with our policies and procedures).

**Focus List.** To be considered for the Focus List, a manager or Fund provides GIMA with relevant documentation on the strategy being evaluated, which may include a request for information ("RFI"), asset allocation histories, its Form ADV (the form that investment managers use to register with the SEC), past performance information and marketing literature. Additional factors for consideration may include personnel depth, turnover and experience, investment process, business and organization characteristics and investment performance. GIMA personnel may also interview the manager or Fund and its key personnel, and examine its operations. Following this review process, Investment Products are placed on the Focus List if they meet the required standards for Focus List status.

GIMA periodically reviews Investment Products on the Focus List. GIMA considers a broad range of factors (including investment performance, staffing, operational issues and financial condition). Among other things, GIMA personnel interview each manager or Fund periodically to discuss these matters. If GIMA is familiar with a manager or Fund following repeated reviews, GIMA is likely to focus on quantitative analysis and interviews and not require in-person meetings. GIMA may also review the collective performance of a composite of the MSSB accounts managed by a manager or Fund and compare this performance to overall performance data provided by the manager/Fund, and then investigate any material deviations.

**Approved List.** The process for including Investment Products on the Approved List is less comprehensive. Investment Products provide GIMA with relevant documentation on the strategy being evaluated, which may include a Request for Information ("RFI"), sample portfolios, asset allocation histories, its Form ADV (the form that investment managers use to register with the SEC), past performance information and marketing literature. GIMA personnel may also interview the Sub-Manager or Fund and its key personnel, typically via conference call. Additional factors for consideration may include personnel depth, turnover and experience; investment process; business and organization characteristics; and investment performance.

In general, GIMA may use an algorithm – a rules-based scoring mechanism – that reviews various qualitative and quantitative

factors and ranks each Investment Product in a third party database. (Not all Investment Products reviewed for the Approved List or Focus List are subject to this algorithm.) GIMA analysts analyze the information contained in the algorithm to gauge the completeness and consistency of the data which drive the rankings, and then send the manager/Fund additional information requests. GIMA then determines whether the Investment Product meets the standards for Approved List status.

GIMA periodically evaluates Investment Products on the Approved List and Focus List to determine whether they continue to meet the appropriate standards.

***Changes in Status from Focus List to Approved List.*** GIMA may determine that a manager/Fund no longer meets the criteria for the Focus List, but meets the criteria for the Approved List. If so, MSSB generally notifies program clients regarding such status changes on a quarterly basis.

***Changes in Status to Not Approved.*** GIMA may determine that an Investment Product no longer meets the criteria for either the Focus List or the Approved List and therefore the Investment Products will no longer be recommended in MSSB investment advisory programs. We notify affected clients of these downgrades. You cannot retain downgraded Investment Products in your account and must select a replacement from the Approved List or Focus List, and that is available in the program, if you wish to retain the program's benefits in respect of the affected assets.

In some circumstances, you may be able to retain terminated Investment Products in another advisory program or in a brokerage account subject to the regular terms and conditions applying to that program or account. Ask your Financial Advisor about these options. MSSB generally specifies a replacement Investment Product for a terminated Investment Product (as discussed in Item 4.A above). In selecting the replacement Investment Product, GIMA generally looks for an Investment Product in the same asset class, and with similar attributes and holdings to the terminated Investment Product.

***Evaluation of Material Changes to Investment Products.*** If GIMA learns of a material change to an Investment Product (e.g., the departure of an Investment Manager or Manager Team), MSSB, an affiliate or a third party retained by MSSB or an affiliate, will evaluate the Investment Product in light of the change. This evaluation may take some time to complete. While this evaluation is being performed, the Investment Product will remain eligible for the IS Program. The GIMA designation (Focus List or Approved List) for this Investment Product will not be altered solely because this evaluation is in progress. MSSB will not necessarily notify clients of any such evaluation.

***Watch Policy.*** GIMA has a "Watch" policy for Investment Products on the Focus List and Approved List. Watch status indicates that, in reviewing Investment Products, GIMA has identified specific areas of the manager's/Fund's business that (a) merit further evaluation by GIMA and (b) may, but are not certain to, result in the Investment Product becoming "Not Approved." Putting Investment Product on Watch does not

signify an actual change in GIMA opinion nor is it a guarantee that GIMA will downgrade the Investment Product. The duration of a Watch status depends on how long GIMA needs to evaluate the Investment Product and for the Investment Product to address any areas of concern. For additional information, ask your Financial Advisor for a copy of GIMA's Watch Policy.

***Tactical Opportunities List.*** GIMA also has a Tactical Opportunities List. This consists of certain Investment Products on the Focus List or Approved List recommended for investment at a given time based in part on then-existing tactical opportunities in the market.

***Other Relationships with Managers.*** Some Investment Product on the Approved List or Focus List may have business relationships with us or our affiliates. For example, a manager may use MS&Co. or an affiliate as its broker or may be an investment banking client of MS&Co. or an affiliate. GIMA does not consider the existence or lack of a business relationship in determining whether to include or maintain Investment Product on the Approved List or Focus List.

Please review your investment managers ADV Part 2 for a discussion on the method of analysis and investment strategy.

## **MAP Due Diligence**

Select Graystone teams and the Morgan Stanley Private Wealth Management ("PWM") Wealth Strategies Group may approve a manager or Investments Products managed by approved managers through the Graystone Manager Assessment Program or the PWM Manager Assessment Program. (PWM is a division of MSSB.)

The reviewing team uses quantitative analysis that assesses all separate account managers in a third party database to narrow the list of potential investment managers for consideration. It then generally conducts further analysis on managers, focusing on qualitative factors (e.g., quality of investment professionals and the manager's investment process).

If the manager is being reviewed by a Graystone team, the Graystone Director of Institutional Investments reviews the analysis for completeness. If the manager is being reviewed by a PWM team, the Research Management Committee also reviews and, if appropriate, approves the manager. (The Research Management Committee reviews certain products made available in Consulting Group programs.) Once a manager has been approved by either reviewing team, it is available for Graystone Consulting, PWM MAP and certain other clients.

The reviewing team generally conducts periodic follow-up due diligence on approved managers (including follow-up interviews with the manager).

## **DC Investment Consulting Fund Screening (For Participant-Directed Defined Contribution Plans only)**

In addition to the mutual funds and ETFs that appear on the Focus List and Approved List of GIMA described above, for clients in the Institutional Services program for participant directed defined contribution plans, funds may be "approved"



for the program in an alternate manner, as well. MSSB applies a proprietary screening process to funds in the Morningstar mutual fund database, which it applies in part using third party software. The screening algorithm, applied quarterly, is based on factors such as performance, ranking, stewardship grade, fees and manager tenure. Funds subject to this process are either approved or not approved for use in the Institutional Services program for participant directed defined contribution plans. MSSB does not maintain a Watch List for these funds equivalent to GIMA's Watch List.

### **Selection of Alternative Investments**

Managers may only participate in the IS program if they are on MSSB's Alternatives Approved List (described below). Managers often offer more than one alternative investment and we may include only some of those alternative investments (or only certain share classes of such alternative investment) in our programs, may carry different alternative investments (or share classes) in different programs, and assign different statuses to different alternative investments.

As well as requiring alternative investments to be on the Alternatives Approved List or Approved List, we look at other factors in determining which alternative investments we offer in these programs, including program needs (such as whether we have a sufficient number of managers available in an asset class), and client demand.

In the programs, investment and business risk due diligence on alternative investments is provided by MSSB through (i) GIMA, (ii) an affiliate of MSSB that may provide due diligence and monitoring services, or (iii) an independent, third-party consulting firm or other organization retained by MSSB and approved by the AIPRC ("Due Diligence Provider") that is also in the business of evaluating the capabilities of alternative investments. Any firm providing due diligence is expected to follow a methodology similar to that used by GIMA (described below) or a methodology approved by the AIPRC in reviewing such alternative investments.

On an ongoing basis, the Due Diligence Provider conducts both quantitative and qualitative research on potential candidates. Their research includes, among other things, a review of relevant documents, calls and meetings with the investment team, and an analysis of investment performance. Generally, although the process may be modified for a particular manager or alternative investment as the Due Diligence Provider may deem appropriate, the Due Diligence Provider will typically also conduct on-site visits, review a separate business risk due diligence questionnaire and examine areas such as portfolio pricing, contingency planning, background checks on key principals and other items. Their due diligence covers the alternative investment in question, not the investments in which that alternative investment may in turn invest. For example, for a fund of funds, GIMA's research process is applied to the fund of funds, and not to each individual fund in which the fund of funds invests. Also, when evaluating portfolio managers that may be recommended to clients to provide portfolio services, the due diligence typically covers the portfolio manager, not the investments which that portfolio manager may recommend.

If a new alternative investment is viewed as an appropriate candidate by the Due Diligence Provider, the vehicle is presented to an MSSB alternative investment product review committee ("AIPRC"). The AIPRC consists of senior MSSB representatives who are mandated to approve proposed candidates and reconfirm existing vehicles on a periodic basis. Once a new alternative investment is approved by the AIPRC, and all required due diligence materials are verified, it receives an "Approved" status, is placed on the Alternatives Approved List, a list of alternative investment vehicles in which qualified clients may invest, and is available for allocations to qualified clients on a placement and/or advisory basis. Certain Alternatives Investments on the Alternatives Approved List are available to qualified clients in the programs.

Ongoing monitoring of managers and investment vehicles on the Alternatives Approved List is provided by the Due Diligence Provider. In addition to manager-specific monitoring, the reviewer monitors overall market conditions in their specific strategies of expertise.

MSSB may remove alternative investments from the programs if GIMA or the Due Diligence Provider of the alternative investment downgrades the alternative investment to "Terminate". We may also terminate managers from these programs for other reasons (e.g., the manager has a low level of assets under management in the program, the manager has limited capacity for further investment, or the manager is not complying with our policies and procedures). Also, GIMA's head of research can remove an alternative investment vehicle from the Alternatives Approved List without consulting the AIPRC, but all actions must be assessed by the AIPRC at the next meeting.

**Watch Policy.** MSSB has a "Watch" policy for alternative investments on the Approved List. Watch status indicates that, in reviewing an alternative investment, GIMA or the Due Diligence Provider has identified specific areas related to the alternative investment, the manager of the alternative investment, or the markets in general that (i) merit further evaluation by GIMA or the Due Diligence Provider and (ii) may, but are not certain to, result in the removal of the alternative investment from the "Approved List". Putting an alternative investment on Watch does not signify an actual change in GIMA opinion nor is it a guarantee that GIMA will remove the alternative investment. The duration of a Watch status depends on how long GIMA needs to evaluate the reason for the status change, which may include, among things, an evaluation of the markets, the alternative investment, and the manager of the alternative investment.

## **B. Material, Significant, or Unusual Risks Relating to Investment Strategies**

The strategies employed by MSSB and the managers entail all of the risks inherent in the markets in which managers or Investment Products are invested. All trading in your account is at your risk. The value of the assets in your account is subject to a variety of factors, such as the liquidity and volatility of the securities markets. We and the managers do not guarantee performance, and a manager's or Investment Option's past performance with respect to other accounts does not predict your account's future performance.

***Risks Relating to Money Market Funds.*** An investment in a money market fund is neither insured nor guaranteed by the Federal Deposit Insurance Corporation ("FDIC") or any other government agency. Although money market funds seek to preserve the value of your investment at \$1.00 per share, there is no assurance that will occur, and it is possible to lose money if the fund value per share falls. Moreover, in some circumstances, money market funds may be forced to cease operations when the value of a fund drops below \$1.00 per share. If this happens, the fund's holdings are liquidated and distributed to the fund's shareholders. This liquidation process could take up to a month or more. During that time, these funds would not be available to you to support purchases, withdrawals and, if applicable, check writing or ATM debits from your account.

***Risks Relating to Differing Classes of Securities.*** Different classes of securities have different rights as creditor if the issuer files for bankruptcy or reorganization. For example, bondholders' rights generally are more favorable than shareholders' rights in a bankruptcy or reorganization.

***Risk Relating to ETFs.*** There may be a lack of liquidity in certain ETFs which can lead to a large difference between the bid-ask prices (increasing the cost to you when you buy or sell the ETF). A lack of liquidity also may cause an ETF to trade at a large premium or discount to its net asset value. Additionally, an ETF may suspend issuing new shares and this may result in an adverse difference between the ETF's publicly available share price and the actual value of its underlying investment holdings. At times when underlying holdings are traded less frequently, or not at all, an ETF's returns also may diverge from the benchmark it is designed to track.

***Risks Relating to Master Limited Partnerships.*** Master Limited Partnerships ("MLPs") are limited partnerships or limited liability companies whose interests (limited partnership or limited liability company units) are generally traded on securities exchanges like shares of common stocks. Investments in MLPs entail different risks, including tax risks, than is the case for other types of investments.

Currently, most MLPs operate in the energy, natural resources or real estate sectors. Investments in MLP interests are subject to the risks generally applicable to companies in these sectors (including commodity pricing risk, supply and demand risk, depletion risk and exploration risk). Depending on the ownership vehicle, MLP interests are subject to varying tax treatment. Please see "Tax and Legal Considerations" below and any Fund

prospectus, for more information. You may obtain any Fund prospectus by asking your Financial Advisor.

***Risks Relating to Funds that Primarily Invest in Master Limited Partnerships.*** In addition to the risks outlined above relating to Master Limited Partnerships, Funds that primarily invest in MLPs generally accrue deferred tax liability. The fund's deferred tax liability (if any) is reflected each day in the fund's net asset value. As a result, the fund's total annual operating expenses may be significantly higher than those of funds that do not primarily invest in Master Limited Partnerships. Please see the fund prospectus for additional information.

***Risks Relating Funds that Pursue Complex or Alternative Investment Strategies or Returns.*** These Funds may employ various investment strategies and techniques for both hedging and more speculative purposes such as short selling, leverage, derivatives and options, which can increase volatility and the risk of investment loss. Alternative investment strategies are not suitable for all investors.

While mutual funds and ETFs may at times utilize non-traditional investment options and strategies, they have different investment characteristics from unregistered privately offered alternative investments. Because of regulatory limitations, mutual funds and ETFs may not invest in as broad a spectrum of investments as privately offered alternative investments. As a result, investment returns and portfolio characteristics of alternative mutual funds may vary from traditional hedge funds pursuing similar investment objectives. They are also more likely to have relatively higher correlation with traditional market returns than privately offered alternative investments. Moreover, traditional hedge funds have limited liquidity with long "lock-up periods allowing them to pursue investment strategies without having to factor in the need to meet client redemptions. On the other hand, mutual funds typically must meet daily client redemptions. This differing liquidity profile can have a material impact on the investment returns generated by a mutual fund pursuing an alternative investing strategy compared with a traditional hedge fund pursuing the same strategy.

Non-traditional investment options and strategies are often employed by a portfolio manager to further a fund's or ETFs investment objective and to help offset market risks. However, these features may be complex, making it more difficult to understand the fund's or ETF's essential characteristics and risks, and how it will perform in different market environments and over various periods of time. They may also expose the fund or ETF to increased volatility and unanticipated risks particularly when used in complex combinations and/or accompanied by the use of borrowing or "leverage".

***Risks Relating to Alternative Investments.*** Alternative investments have different features and risks from other types of investment products. As further described in the offering documents of any particular alternative investment, an investment in alternative investments can be highly illiquid, is speculative and not suitable for all investors. For example, alternative investment products may place substantial limits on liquidity and the redemption rights of investors, including only permitting withdrawals on a limited periodic basis and with a significant period of notice and may impose early withdrawal



fees. Investing in alternative investments is intended for experienced and sophisticated investors only who are willing to bear the high economic risks of the investment. Investors should carefully review and consider potential risks before investing. Certain of these risks may include: loss of all or a substantial portion of the investment due to leveraging, shortselling, or other speculative practices; lack of liquidity, in that there may be no secondary market for the fund and none expected to develop; volatility of returns; restrictions on transferring interests in the fund; potential lack of diversification and resulting higher risk due to concentration of trading authority when a single advisor is utilized; absence of information regarding valuations and pricing; complex tax structures and delays in tax reporting; less regulation and higher fees than mutual funds; and advisor risk. Alternative investment products may also have higher fees (including multiple layers of fees) compared to other types of investments.

Individual funds will have specific risks related to their investment programs that will vary from fund to fund. For more details on these and other features and risks, please carefully read the documentation (including risk disclosures) relating to any selected Investment Option, as well as your client agreement.

Please review your investment managers ADV Part 2 or the prospectus or offering document for any mutual fund, alternative investment or ETF in which your account may be invested for a discussion on the material risks associated with your account.

## **C. Risks Associated with Particular Types of Securities**

Please see response to Item 8 B.

## **Item 9: Disciplinary Information**

This section contains information on certain legal and disciplinary events.

In this section, “MSDW” means Morgan Stanley DW Inc., a predecessor broker-dealer of MS&Co. and registered investment adviser that was merged into MS&Co. in April 2007. MS&Co. and Smith Barney and/or Citigroup Global Markets Inc. (“CGM”) are predecessor broker-dealer firms of MSSB.

- On May 31, 2005, the SEC issued an order in connection with the settlement of an administrative proceeding against Smith Barney Fund Management LLC (“SBFM”) and CGM relating to the appointment of an affiliated transfer agent for the Smith Barney family of mutual funds (“Smith Barney Funds”). SBFM was an affiliate of CGM during the applicable period.

The SEC order found that SBFM and CGM willfully violated section 206(1) of the Investment Advisers Act of 1940 (“Advisers Act”). Specifically, the order found that SBFM and CGM knowingly or recklessly failed to disclose to the Boards of the Smith Barney Funds in 1999 when proposing a new transfer agent arrangement with an affiliated transfer agent that: First Data Investors Services Group (“First

Data”), the Smith Barney Funds’ then-existing transfer agent, had offered to continue as transfer agent and do the same work for substantially less money than before; and Citigroup Asset Management (“CAM”), the Citi business unit that includes the Smith Barney Funds’ investment manager and other investment advisory companies, had entered into a side letter with First Data under which CAM agreed to recommend the appointment of First Data as sub-transfer agent to the affiliated transfer agent in exchange, among other things, for a guarantee by First Data of specified amounts of asset management and investment banking fees to CAM and CGM. The order also found that SBFM and CGM willfully violated section 206(2) of the Advisers Act by virtue of the omissions discussed above and other misrepresentations and omissions in the materials provided to the Smith Barney Funds’ Boards, including the failure to make clear that the affiliated transfer agent would earn a high profit for performing limited functions while First Data continued to perform almost all of the transfer agent functions, and the suggestion that the proposed arrangement was in the Smith Barney Funds’ best interests and that no viable alternatives existed. SBFM and CGM did not admit or deny any wrongdoing or liability. The settlement did not establish wrongdoing or liability for purposes of any other proceeding.

The SEC censured SBFM and CGM and ordered them to cease and desist from violations of sections 206(1) and 206(2) of the Advisers Act. The order required Citi to pay \$208.1 million, including \$109 million in disgorgement of profits, \$19.1 million in interest, and a civil money penalty of \$80 million. Approximately \$24.4 million has already been paid to the Smith Barney Funds, primarily through fee waivers. The remaining \$183.7 million, including the penalty, has been paid to the U.S. Treasury.

The order required SBFM to recommend a new transfer agent contract to the Smith Barney Fund Boards within 180 days of the entry of the order; if a Citi affiliate submitted a proposal to serve as transfer agent or sub-transfer agent, an independent monitor must be engaged at the expense of SBFM and CGM to oversee a competitive bidding process. Under the order, Citi also must comply with an amended version of a vendor policy that Citi instituted in August 2004. That policy, as amended, among other things, requires that when requested by a Smith Barney Fund Board, CAM will retain at its own expense an independent consulting expert to advise and assist the Board on the selection of certain service providers affiliated with Citi.

- In a LAWC dated August 1, 2005, the NASD found that MSDW failed to establish and maintain a supervisory system, including written procedures, reasonably designed to review and monitor MSDW’s fee-based brokerage business, between January 2001 and December 2003. Without admitting or denying the allegations, MSDW consented to the described sanctions and findings and was censured and fined \$1.5 million, and agreed to the payment of restitution to 3,549 customers in the total amount of approximately \$4.7 million, plus interest.

- The SEC alleged that MS&Co. violated the Exchange Act by inadvertently failing to timely produce emails to the SEC staff pursuant to subpoenas in the SEC's investigation into MS&Co.'s practices in allocating shares of stock in IPOs and an investigation into conflicts of interest between MS&Co.'s research and investment banking practices. Without admitting or denying the allegations, MS&Co. consented to a final judgment on May 12, 2006 in which it was permanently restrained and enjoined from violating the Exchange Act. MS&Co. agreed to make payments aggregating \$15 million, which amount was reduced by \$5 million contemporaneously paid by MS&Co. to the NASD and the NYSE in related proceedings. MS&Co. also agreed to notify the SEC, the NASD and the NYSE that it has adopted and implemented policies and procedures reasonably designed to ensure compliance with the Exchange Act. MS&Co. also agreed to provide annual training to its employees responsible for preserving or producing electronic communications and agreed to retain an independent consultant to review and comment on the implementation and effectiveness of the policies, procedures and training.
- On June 27, 2006, the SEC announced the initiation and concurrent settlement of administrative cease and desist proceedings against MS&Co. and MSDW for failing to maintain and enforce adequate written policies and procedures to prevent the misuse of material nonpublic information. The SEC found that from 1997 through 2006, MS&Co. and MSDW violated the Exchange Act and the Advisers Act by failing to (1) conduct any surveillance of a number of accounts and securities; (2) provide adequate guidance to MS&Co.'s and MSDW's personnel charged with conducting surveillance; and (3) have adequate controls in place with respect to certain aspects of "Watch List" maintenance. The SEC's findings covered different areas from the 1997 through 2006 time period. MS&Co. and MSDW were ordered to pay a civil money penalty of \$10 million and agreed to enhance their policies and procedures.
- On August 21, 2006, MS&Co. and MSDW entered into a LAWC relating various finds that, at various times between July 1999 and 2005, MS&Co. violated a number of NASD and SEC rules. The violations related to areas including trade reporting through the Nasdaq Market Center (formerly Automated Confirmation Transaction Service (ACT)), Trade Reporting and Compliance Engine (TRACE) and Order Audit Trail System (OATS); market making activities; trading practices; short sales; and large options positions reports. The NASD also found that, at various times during December 2002 and May 2005, MSDW violated NASD rules and Municipal Securities Rulemaking Board ("MSRB") rules related to areas including trade reporting through TRACE, short sales, and OATS. The NASD further found that, in certain cases, MS&Co. and MSDW violated NASD Rule 3010 because their supervisory systems did not provide supervision reasonably designed to achieve compliance with securities laws, regulations and/or rules.

Without admitting or denying the findings, MS&Co. and MSDW consented to the LAWC. In the LAWC, MS&Co. and MSDW were censured, required to pay a monetary fine of \$2.9 million and agreed to make restitution to the parties

involved in certain transactions, plus interest, from the date of the violative conduct until the date of the LAWC. MS&Co. and MSDW also consented to (1) revise their written supervisory procedures; and (2) provide a report that described the corrective action that they completed during the year preceding the LAWC to address regulatory issues and violations addressed in the LAWC, and the ongoing corrective action that they were in the process of completing.

- On May 9, 2007, the SEC issued an Order ("May 2007 Order") settling an administrative action with MS&Co. In this matter, the SEC found that MS&Co. violated its duty of best execution under the Exchange Act. In particular, the SEC found that, during the period of October 24, 2001 through December 8, 2004, MS&Co.'s proprietary market-making system failed to provide best execution to certain retail OTC orders. In December 2004, MS&Co. removed the computer code in the proprietary market-making system that caused the best execution violations. MS&Co. consented, without admitting or denying the findings, to a censure, to cease and desist from committing or causing future violations, to pay disgorgement of approximately \$5.9 million plus prejudgment interest on that amount, and to pay a civil penalty of \$1.5 million. MS&Co. also consented to retain an Independent Compliance Consultant to review its policies and procedures in connection with its market-making system's order handling procedures and its controls relating to changes to those procedures, and to develop a better plan of distribution.
- On July 13, 2007, the NYSE issued a Hearing Board Decision in connection with the settlement of an enforcement proceeding brought in conjunction with the New Jersey Bureau of Securities against CGM. The decision held that CGM failed to (1) adequately supervise certain branch offices and Financial Advisors who engaged in deceptive mutual fund market timing on behalf of certain clients from January 2000 through September 2003 (in both proprietary and non-proprietary funds); (2) prevent the Financial Advisors from engaging in this conduct; and (3) make and keep adequate books and records. Without admitting or denying the findings, CGM agreed to (a) a censure; (b) establishing a \$35 million distribution fund for disgorgement payments; (c) a penalty of \$10 million (half to be paid to the NYSE and half to be paid to the distribution fund); (d) a penalty of \$5 million to be paid to the State of New Jersey; and (e) appointing a consultant to develop a plan to pay CGM's clients affected by the market timing.
- On September 27, 2007, MS&Co. entered into a LAWC with the Financial Industry Regulatory Authority ("FINRA"). FINRA found that, from October 2001 through March 2005, MSDW provided inaccurate information to arbitration claimants and regulators regarding the existence of pre-September 11, 2001 emails, failed to provide such emails in response to discovery requests and regulatory inquiries, failed adequately to preserve books and records, and failed to establish and maintain systems and written procedures reasonably designed to preserve required records and to ensure that it conducted adequate searches in response to regulatory inquiries and discovery requests. FINRA also found that MSDW failed to provide arbitration claimants

with updates to a supervisory manual in discovery from late 1999 through the end of 2005. MS&Co. agreed, without admitting or denying these findings, to establish a \$9.5 million fund for the benefit of potentially affected arbitration claimants. In addition, MS&Co. was censured and agreed to pay a \$3 million regulatory fine and to retain an independent consultant to review its procedures for complying with discovery requirements in arbitration proceedings relating to its retail brokerage operations.

- On October 10, 2007, MS&Co. became the subject of an Order Instituting Administrative and Cease-And-Desist Proceedings (“October 2007 Order”) by the SEC. The October 2007 Order found that, from 2000 until 2005, MS&Co. and MSDW failed to provide to their retail customers accurate and complete written trade confirmations for certain fixed income securities in violation of the Exchange Act and MSRB rules. In addition, MS&Co. was ordered to cease and desist from committing or causing any future violations, and was required to pay a \$7.5 million penalty and to retain an independent consultant to review MS&Co.’s applicable policies and procedures. MS&Co. consented to the issuance of the October 2007 Order without admitting or denying the SEC’s findings.
- On December 18, 2007, MS&Co. became the subject of an Order Instituting Administrative Cease-and-Desist Proceedings (“December 2007 Order”) by the SEC. The December 2007 Order found that, from January 2002 until August 2003, MSDW (1) failed to reasonably supervise four Financial Advisors, with a view to preventing and detecting their mutual fund market-timing activities and (2) violated the Investment Company Act of 1940 by allowing multiple mutual fund trades that were placed or amended after the close of trading to be priced at that day’s closing net asset value. The December 2007 Order also found that, from 2000 through 2003, MSDW violated the Exchange Act by not making and keeping records of customer orders placed after the market close and orders placed for certain hedge fund customers in variable annuity sub-accounts. Without admitting or denying the SEC’s findings, MS&Co. agreed to a censure, to cease and desist from future violations of the applicable provisions, to pay a penalty of approximately \$11.9 million, to disgorge profits related to the trading activity (including prejudgment interest) of approximately \$5.1 million and to retain an independent distribution consultant.
- In May 2005, MS&Co. and MSDW discovered that, from about January 1997 until May 2005, their order entry systems did not check whether certain secondary market securities transactions complied with state registration requirements known as Blue Sky laws. This resulted in the improper sale of securities that were not registered in 46 state and territorial jurisdictions. MS&Co. and MSDW conducted an internal investigation, repaired system errors, self-reported the problem to all affected states and the New York Stock Exchange, identified transactions which were executed in violation of the Blue Sky laws, and offered rescission to affected customers. MS&Co. settled the state regulatory issues in a multi-state settlement with the 46 affected state and territorial jurisdictions. Under the settlement, MS&Co.

consented to a cease and desist order with, and agreed to pay a total civil monetary penalty of \$8.5 million to be divided among, each of the 46 state and territorial jurisdictions. The first order was issued by Alabama on March 19, 2008, and orders are expected to be issued by subsequent states over the coming months.

- On August 13, 2008, MS&Co. agreed on the general terms of a settlement with the NYAG and the Office of the Illinois Secretary of State, Securities Department (“Illinois”) (on behalf of a task force of the North American Securities Administrators Association (“NASAA”)) with respect to the sale of auction rate securities (“ARS”). MS&Co. agreed, among other things, to repurchase at par approximately \$4.5 billion of illiquid ARS held by certain clients of MS&Co. which were purchased prior to February 13, 2008. Additionally, MS&Co. agreed to pay a total fine of \$35 million. Final agreements were entered into with the NYAG on June 2, 2009 and with Illinois on September 17, 2009. The Illinois agreement serves as the template for agreements with other NASAA jurisdictions.
- On November 13, 2008, in connection with the settlement of a civil action arising out of an investigation by the SEC into CGM’s underwriting, marketing and sale of ARS, CGM, without admitting or denying the allegations of the SEC’s complaint, except as to those relating to personal and subject matter jurisdiction, which were admitted, consented to the entry in the civil action of a Judgment As To Defendant Citigroup Global Markets Inc. (“November 2008 Judgment”). Thereafter, on December 11, 2008, the SEC filed its civil action in the federal district court for the Southern District of New York (“Court”). The November 2008 Judgment, which was entered on December 23, 2008 (i) permanently enjoined CGM from directly or indirectly violating section 15(c) of the Exchange Act; (ii) provides that, on later motion of the SEC, the Court is to determine whether it is appropriate to order that CGM pay a civil penalty pursuant to section 21(d)(3) of the Exchange Act, and if so, the amount of the civil penalty; and (iii) ordered that CGM’s Consent be incorporated into the November 2008 Judgment and that CGM comply with all of the undertakings and agreements in the Consent, which include an offer to buy back at par certain ARS from certain customers. The SEC’s complaint alleged that (1) CGM misled tens of thousands of its customers regarding the fundamental nature of and risks associated with ARS that CGM underwrote, marketed and sold; (2) through its financial advisers, sales personnel and marketing materials, CGM misrepresented to customers that ARS were safe, highly liquid investments comparable to money market instruments; (3) as a result, numerous CGM customers invested in ARS funds they needed to have available on a short-term basis; (4) in mid-February 2008, CGM decided to stop supporting the auctions; and (5) as a result of the failed auctions, tens of thousands of CGM customers held approximately \$45 billion of illiquid ARS, instead of the liquid short-term investments CGM had represented ARS to be. CGM reached substantially similar settlements with the NYAG and the Texas State Securities Board (“TSSB”), although those settlements were administrative in nature and neither involved the filing of a civil action in state court. The settlements with the NYAG

and the TSSB differed somewhat from the settlement with the SEC in that the state settlements (a) made findings that CGM failed to preserve certain recordings of telephone calls involving the ARS trading desk; and (b) required CGM to refund certain underwriting fees to certain municipal issuers. In addition, as part of the settlement with New York, CGM paid a civil penalty of \$50 million. CGM also agreed in principle to pay to states other than New York with which it enters into formal settlements a total of \$50 million. CGM paid \$3.59 million of this \$50 million to Texas as part of the settlement with that state. CGM expects it will reach settlements with the remaining states.

- On March 25, 2009, MS&Co. entered into a LAWC with FINRA. FINRA found that, from 1998 through 2003, MSDW failed to reasonably supervise the activities of two Financial Advisors in one of its branches. FINRA found that these Financial Advisors solicited brokerage and investment advisory business from retirees and potential retirees of certain large companies by promoting unrealistic investment returns and failing to disclose material information. FINRA also held that MS&Co. failed to ensure that the securities and accounts recommended for the retirees were properly reviewed for appropriate risk disclosure, suitability and other concerns. MS&Co. consented, without admitting or denying the findings, to a censure, a fine of \$3 million, and restitution of approximately \$2.4 million plus interest to 90 former clients of the Financial Advisors.

MSSB's Form ADV Part 1 contains further information about its disciplinary history, and is available on request from your Financial Advisor.

## Item 10: Other Financial Industry Activities and Affiliations

Morgan Stanley ("Morgan Stanley Parent") is a financial holding company under the Bank Holding Company Act of 1956. Morgan Stanley Parent is a corporation whose shares are publicly held and traded on the New York Stock Exchange. Prior to June 28, 2103, MSSB was owned by a joint venture company which was indirectly owned 65% by Morgan Stanley Parent and 35% by Citi. On June 28, 2013, Morgan Stanley Parent purchased Citi's 35% interest in MSSB. Accordingly, MSSB is now a wholly owned indirect subsidiary of Morgan Stanley Parent.

**Activities of Morgan Stanley Parent.** Morgan Stanley Parent is a global firm engaging, through its various subsidiaries, in a wide range of financial services including:

- securities underwriting, distribution, trading, merger, acquisition, restructuring, real estate, project finance and other corporate finance advisory activities
- merchant banking and other principal investment activities
- brokerage and research services
- asset management
- trading of foreign exchange, commodities and structured financial products and

- global custody, securities clearance services, and securities lending.

### A. Broker-Dealer Registration Status

As well as being a registered investment advisor, MSSB is registered as a broker-dealer.

### B. Futures Commission Merchant, Commodity Pool Operator, or Commodity Trading Adviser Registration Status

As well as being a registered investment advisor, MSSB has related persons that are commodity pool operators (Ceres Managed Futures LLC, Morgan Stanley AIP GP LP, Morgan Stanley Investment Management Inc., Morgan Stanley Cayman Ltd., Morgan Stanley AIP Cayman GP Ltd., Morgan Stanley Alternative Investment Partners LP, Morgan Stanley Hedge Premier GP, and Morgan Stanley GWM Feeder Strategies LLC) and commodity trading advisers (Ceres Managed Futures LLC, Morgan Stanley AIP GP LP, Morgan Stanley Investment Management Inc.). For a full listing of affiliated investment advisers please see the ADV Part I.

### C. Material Relationships or Arrangements with Industry Participants

**Restrictions on Executing Trades.** As MSSB is affiliated with MS&Co. and its affiliates, the following restrictions apply when executing client trades:

- MSSB and MS&Co. generally do not act as principal in executing trades for MSSB investment advisory clients (except to the extent permitted by a program and the law).
- Regulatory restrictions may limit your ability to purchase, hold or sell equity and debt issued by Morgan Stanley Parent and its affiliates in some investment advisory programs.
- Certain regulatory requirements may limit MSSB's ability to execute transactions through alternative execution services (e.g., electronic communication networks and crossing networks) owned by MSSB, MS&Co. or their affiliates.

These restrictions may adversely impact client account performance.

**Different Advice.** MSSB and its affiliates may give different advice, take different action, receive more or less compensation, or hold or deal in different securities for any other party, client or account (including their own accounts or those of their affiliates) from the advice given, actions taken, compensation received or securities held or dealt for your account.

**Trading or Issuing Securities in, or Linked to Securities in, Client Accounts.** MSSB and its affiliates may provide bids and offers, and may act as a principal market maker, in respect of the same securities held in client accounts. MSSB, the investment managers in its programs, and its affiliates and employees may hold a position (long or short) in the same securities held in client accounts. MSSB and/or its affiliates are regular issuers of traded financial instruments linked to securities that may be

purchased in client accounts. From time to time, the trading of MSSB, a manager or their affiliates – both for their proprietary accounts and for client accounts – may be detrimental to securities held by a client and thus create a conflict of interest. We address this conflict by disclosing it to you.

**Trade Allocations.** MSSB may aggregate the securities to be sold or purchased for more than one client to obtain favorable execution to the extent permitted by law. MSSB will then allocate the trade in a manner that is equitable and consistent with MSSB's fiduciary duty to its clients (including pro rata allocation, random allocation or rotation allocation). Allocation methods vary depending on various factors (including the type of investment, the number of shares purchased or sold, the size of the accounts, and the amount of available cash or the size of an existing position in an account). The price to each client is the average price for the aggregate order.

**Services Provided to Other Clients.** MSSB and its affiliates provide a variety of services (including research, brokerage, asset management, trading, lending and investment banking services) for each other and for various clients, including issuers of securities that MSSB may recommend for purchase or sale by clients or are otherwise held in client accounts, and investment management firms in the programs described in this Brochure. MSSB, MS&Co. investment managers and their affiliates receive compensation and fees in connection with these services. MSSB believes that the nature and range of clients to which such services are rendered is such that it would be inadvisable to exclude categorically all of these companies from an account. Accordingly, it is likely that securities in an account will include some of the securities of companies for which MSSB, MS&Co. investment managers and their affiliates or an affiliate performs investment banking or other services.

**Restrictions on Securities Transactions.** There may be periods during which MSSB or investment managers are not permitted to initiate or recommend certain types of transactions in the securities of issuers for which MSSB, or one of its affiliates is performing broker-dealer or investment banking services or have confidential or material non-public information. Furthermore, in certain investment advisory programs, MSSB may be compelled to forgo trading in, or providing advice regarding, Morgan Stanley Parent securities, and in certain related securities. These restrictions may adversely impact your account performance.

MSSB, the managers and their affiliates may also develop analyses and/or evaluations of securities sold in a program described in this Brochure, as well as buy and sell interests in securities on behalf of its proprietary or client accounts. These analyses, evaluations and purchase and sale activities are proprietary and confidential, and MSSB will not disclose them to clients. MSSB may not be able to act, in respect of clients' account, on any such information, analyses or evaluations.

MSSB, investment managers and their affiliates are not obligated to effect any transaction that MSSB or a manager or any of their affiliates believe would violate federal or state law, or the regulations of any regulatory or self-regulatory body.

**Research Reports.** MS & Co. LLC ("MS&Co.") does business with companies covered by their respective research groups. Furthermore, MS&Co. and their affiliates and client accounts may hold a trading position (long or short) in the securities of companies subject to such research. Therefore, MS&Co. has a conflict of interest that could affect the objectivity of its research reports.

**Certain Trading Systems.** MSSB may effect trades or securities lending transactions on behalf of client accounts through exchanges, electronic communication networks or other alternative trading systems ("Trading Systems"), including Trading Systems with respect to which MSSB or its affiliates may have a non-controlling direct or indirect ownership interest, or on which MSSB or right to appoint a board member or observer. If MSSB directly or indirectly effects client trades or transactions through Trading Systems in which MSSB or its affiliates have an ownership interest, MSSB or its affiliates may receive an indirect economic benefit based on their ownership interest. In addition, subject at all times to its obligations to obtain best execution for its customers' orders, it is contemplated that MSSB will route certain customer order flow to its affiliates. Currently, MSSB and/or its affiliates (including affiliates of MS&Co.) may own over 5% of the equity interests of certain Trading Systems or their parent companies, including BATS Global Markets, Inc., which owns and operates BATS Exchange, Inc., BATS Trading Limited and Direct Edge (commonly known as "BATS"); BIDS Holdings LP and BIDS Holdings GP LLC (commonly known as "BIDS"); BOX Holdings Group LLC; Eris Exchange Holdings LLC; Equilend; iSWAP Limited; MTS Associated Markets; MuniCenter (TheDebtCenter, LLC); OTCDeriv Limited; Source Holding Ltd; TradeWebMarkets LLC; and Turquoise Global Holdings Ltd. The Trading Systems on which MSSB trades or effects securities lending transactions for client accounts and in which MSSB or its affiliates own interests may change from time to time. You may contact your Financial Advisor for an up-to-date list of Trading Systems in which MSSB or its affiliates own interests and on which MSSB and/or MS&Co. trade for client accounts.

Certain Trading Systems offer cash credits for orders that provide liquidity to their books and charge explicit fees for orders that extract liquidity from their books. From time to time, the amount of credits that MSSB and/or MS&Co. receives from one or more Trading System may exceed the amount that is charged. Under these limited circumstances, such payments would constitute payment for order flow.

Certain Trading Systems through which MSSB and/or MS&Co. may directly or indirectly effect client trades execute transactions on a "blind" basis, so that a party to a transaction does not know the identity of the counterparty to the transaction. It is possible that an order for a client account that is executed through such a Trading System could be automatically matched with a counterparty that is (i) another investment advisory or brokerage client of MSSB or one of its affiliates or (ii) MSSB or one of its affiliates acting for its own proprietary accounts.

**Transaction-Related Agreements with MS&Co. and Affiliates.** In connection with creating MSSB, certain agreements were entered into between or involving some or all of MSSB, MS&Co. and their affiliates. Some of these agreements,

including the following, remain in effect even though MSSB is now a wholly owned subsidiary of Morgan Stanley Parent:

- **Order Flow.** An agreement that, subject to best execution, MSSB will transmit an agreed percentage of client orders for the purchase and sale of securities to MS&Co and its affiliates. MSSB has a conflict of interest in transmitting client orders to these entities.
- **Distribution.** An agreement that, in return for the payment of certain fees and expenses, MSSB will market and promote certain securities and other products underwritten, distributed or sponsored by MS&Co., or its affiliates. MSSB has a conflict of interest in offering, recommending or purchasing any such security or other product to or for its investment advisory clients.
- **Affiliated Sweep Investments.** MSSB has a conflict of interest in selecting or recommending BDP or Money Market Funds as the Sweep Investment. See Item 5.C above for more information.

**MSSB Affiliate in Underwriting Syndicate.** If an affiliate of MSSB is a member of the underwriting syndicate from which a security is purchased, we or our affiliates may directly or indirectly benefit from such purchase.

**Related Investment Advisors and Other Service Providers.** MSSB has related persons that are registered investment advisers in various investment advisory programs (including Morgan Stanley Investment Management Inc., Morgan Stanley Investment Management Limited and Consulting Group Advisory Services LLC). If you invest your assets and use an affiliated firm to manage your account, MSSB and its affiliates earn more money than if you use an unaffiliated firm. Generally, for Retirement Accounts, MSSB rebates or offsets fees so that MSSB complies with IRS and Department of Labor rules and regulations.

Morgan Stanley Investment Management Inc. and its wholly owned subsidiary Morgan Stanley Services Company Inc. serve in various advisory, management, and administrative capacities to open-end and closed-end investment companies and other portfolios (some of which are listed on the NYSE).

Morgan Stanley Distribution Inc. serves as distributor for these open-end investment companies, and has entered into selected dealer agreements with MSSB and affiliates. Morgan Stanley Distribution Inc. also may enter into selected dealer agreements with other dealers. Under these agreements, MSSB and affiliates, and other selected dealers, are compensated for sale of fund shares to clients on a brokerage basis, and for shareholder servicing (including pursuant to plans of distribution adopted by the investment companies pursuant to Rule 12b-1 under the Investment Company Act of 1940).

Morgan Stanley Services Company Inc., an affiliate of MSSB, serves as transfer agent and dividend disbursing agent for investment companies advised by Morgan Stanley Investment Management Inc. and other affiliated investment advisers and may receive annual per shareholder account fees from or with respect to them and certain nonaffiliated investment companies.

Related persons of MSSB act as general partner, administrative agent or managing member in a number of funds in which clients may be solicited in a brokerage or advisory capacity to invest. These include funds focused on private equity investing, investments in leveraged buyouts, venture capital opportunities, research and development ventures, real estate, managed futures, hedge funds, funds of hedge funds and other businesses.

See Item 5.C above for a description of cash sweep investments managed or held by related persons of MSSB.

## **D. Material Conflicts of Interest Relating to Other Investment Advisers**

In the advisory programs described in this Brochure, MSSB recommends investment advisers to clients. Many of the investment advisers that are available in the MSSB advisory program provide conferences and other training sessions to the Financial Advisors.

In addition, certain investment advisers also manage Funds, alternative products or act as a sub adviser to Mutual Funds affiliated with MSSB. Since MSSB receives fees from the mutual fund or its adviser, MSSB has a conflict to recommend the mutual fund products instead of the investment adviser managing the account directly.

**Payments from Managers.** Managers may also sponsor their own educational conferences and pay expenses of Financial Advisors attending these events. MSSB's policies require that the training or educational portion of these conferences comprises substantially the entire event. Managers may sponsor educational meetings or seminars in which clients as well as Financial Advisors are invited to participate.

Managers are allowed to occasionally give nominal gifts to Financial Advisors, and to occasionally entertain Financial Advisors, subject to a limit of \$1,000 per employee per year. MSSB's non-cash compensation policies set conditions for each of these types of payments, and do not permit any gifts or entertainment conditioned on achieving a sales target. On request, your Financial Advisor can provide you with an annual estimate of the aggregate value of gifts or entertainment that managers pay or provide to MSSB or particular Financial Advisors.

We address conflicts of interest by ensuring that any payments described in this "Payments to Managers" section do not relate to any particular transactions or investment made by MSSB clients with managers. Managers participating in programs described in this Brochure are not required to make any of these types of payments. The payments described in this section comply with FINRA rules relating to such activities. Please see the discussion of Global and Emerging Partners under "Funds in Advisory Programs" in Item 4.C for more information.

**Payments from Mutual Funds.** Please see the discussion of payments from fund companies under "Funds in Advisory Programs" in Item 5.C.

**Payments from Managers of Alternative Investments.** Managers of alternative investments offered in the programs

described in this Brochure may agree to pay us additional fees. We have a conflict of interest in offering alternative investments because we or our affiliates earn more money in your account from your investments in alternative investments than from other investment options. However, in cases where we receive a portion of the management fee paid by you to a manager of an alternative investment and we charge a program fee under the programs in this Brochure, we credit such fee to your account. Also, we do not share this money with your Financial Advisor (i.e. the compensation we pay to your Financial Advisor is not affected by the payments we receive from the alternative investments). Therefore, your Financial Advisor does not have a resulting incentive to buy alternative investments in your account, or to buy certain alternative investments rather than other alternative investments in any of the programs in this Brochure.

***Affiliate Acting as Portfolio Manager.*** Where permitted by law, (except for plan accounts), an affiliate of MSSB may have been selected to act as the manager for one or more your investments. Where this occurs, we or our affiliates earn more money than from other investment options. MSSB and the Financial Advisor are also likely to earn more compensation if you invest in a program described in this Brochure than if you open a brokerage account to buy individual securities.

These relationships create a conflict of interest for us or our affiliates as there is a financial incentive to recommend the investments. We address this conflict of interest by disclosing it to you and by requiring Financial Advisors' supervisors to review your account at account-opening to ensure that it is suitable for you in light of matters such as your investment objectives and financial circumstances.

***MSSB as Placement Agent.*** MSSB also acts a placement agent for certain alternative investments whereby such investments are available through MSSB on a non-advisory basis. When an alternative investment is purchased on a placement basis, different terms and conditions, including different fee arrangements, may apply. For example, when a client invests on a placement basis, they do not pay an ongoing advisory fee, however, they pay an upfront placement fee and the program manager receives a higher program participation fee which is shared with MSSB and its Financial Advisors. A Client investing on an advisory basis may pay higher fees, in the aggregate, than if such investment had been made on a placement basis.

***Affiliated Sweep Investments.*** MSSB has a conflict of interest in selecting or recommending BDP or Money Market Funds as the Sweep Investment. See Item 5.C above for more information.

## Item 11: Code of Ethics, Participation or Interest in Client Transactions and Personal Trading

### A. Code of Ethics

The MSSB US Investment Advisory Code of Ethics ("Code") applies to MSSB employees, supervisors, officers and directors engaged in offering or providing investment advisory products and/or services (collectively, the "Employees"). In essence, the Code prohibits Employees from engaging in securities transactions or activities that involve a material conflict of interest, possible diversion of a corporate opportunity, or the appearance of impropriety. Employees must always place the interests of MSSB's clients above their own and must never use knowledge of client transactions acquired in the course of their work to their own advantage. Supervisors are required to use reasonable supervision to detect and prevent any violations of the Code by the individuals, branches and departments that they supervise.

The Code generally operates to protect against conflicts of interest either by subjecting Employee activities to specified limitations (including pre-approval requirements) or by prohibiting certain activities. Key provisions of the Code include:

- An Employee who wishes to conduct business activity outside of his or her employment with MSSB, regardless of whether that Employee receives compensation for this activity, must first obtain written authorization from his or her supervisor. (Outside activities include serving as an officer or director of a business organization or non-profit entity, and accepting compensation from any person or organization other than MSSB.)
- Employees are generally prohibited from giving or receiving gifts or gratuities greater than \$100 per recipient per calendar year to or from persons or organizations with which MSSB has a current or potential business relationship, clients, or persons connected with another financial institution, a securities or commodities exchange, the media, or a government or quasi-governmental entity.
- Employees cannot enter into a lending arrangement with a client (unless they receive prior written approval from their supervisor and MSSB's Compliance Department).
- MSSB maintains a "Restricted List" of issuers for which it may have material non-public information or other conflicts of interest. Employees cannot, for themselves or their clients, trade in securities of issuers on the "Restricted List" (unless they receive prior written approval from the Compliance department).
- Certain Employees, because of their potential access to non-public information, must obtain their supervisors' prior written approval or provide pre-trade notification before executing certain securities transactions for their personal securities accounts. All Employees must also follow special procedures for investing in private securities transactions.
- Certain Employees are subject to further restrictions on their securities transaction activities (including Financial Advisors and other MSSB employees who act as portfolio managers in MSSB investment advisory programs).

You may obtain a copy of the Code of Ethics from your Financial Advisor.

## **B. Securities in Which You or a Related Person Has a Material Financial Interest**

Please the paragraph entitled “*Cash Sweeps*” located in Item 5C.

## **C. Investing and Other Interests in Securities Which You or a Related Person Recommend to Clients**

See the following in Item 10.C:

- “Trading or Issuing Securities in, or Linked to Securities in, Client Accounts”
- “Restrictions on Securities Transactions”
- “Research Reports”
- “Certain Trading Systems”
- “Transaction-Related Agreements with MS&Co., Citi and Affiliates”

## **D. Conflicts of Interest Created by Contemporaneous Trading**

See “Different Advice” in Item 10.C.

# **Item 12: Brokerage Practices**

## **A. Factors in Selecting or Recommending Broker-Dealers for Client Transactions**

MSSB does not recommend broker-dealers to effect client securities transactions. For the programs listed in this Brochure, securities are executed through MSSB.

For the programs described in this Brochure, we do not receive research or soft dollars, nor recommend other broker-dealers.

We offer, but do not recommend, request or require clients to select directed brokerage as the option to pay their investment advisory program fees.

At the client’s request, MSSB permits clients to use direct brokerage commissions to pay for the MSSB investment advisory fee. As described above in Item 4B, you will enter into a separate agreement with each investment manager. Your investment manager as per your direction will direct trades to MSSB (the “Executing Broker-Dealer”). The Executing Broker-Dealer will execute trade on a best execution basis and the commissions generated will compensate MSSB and the Financial Advisor. The commissions will be capped by the maximum advisory allowed for this program (2.50%). Notwithstanding the commissions that pay for MSSB’s investment advisory fee, you will still pay you investment manager’s fee.

If you select a manager that has a high portfolio turn over ratio (executes many trades in the portfolio) you may pay an overall fee that is higher than if you negotiated an asset based fee that is lower than the overall transaction costs.

## **B. Aggregation of Securities Transactions for Clients**

Investment managers submit trade orders for all clients in the same strategy to the Executing Broker-Dealer. It is the investment manager’s decision as to allocation of the trade orders. Please review your investment managers ADV for more information.

# **Item 13: Review of Accounts**

## **A. Frequency and Nature of Review of Client Accounts or Financial Plans**

At account opening, your Financial Advisor must ensure that, and the Financial Advisor’s Branch Manager (or the Branch Manager’s designee) confirms that, the account and the investment style are suitable investments for you.

As an IS client, your Financial Advisor is then responsible for reviewing your account on an ongoing basis and will recommend different asset allocations at any time according to market conditions. Your Financial Advisor will ask you at least annually if your investment objectives have changed. If your objectives change, your Financial Advisor will modify your asset allocation to be suitable for your needs.

See Items 4.B and 15 for a discussion of account statements and performance reporting.

## **B. Factors Prompting Review of Client Accounts other than a Periodic Review**

On an annual basis, your Financial Advisor will discuss with you if your investment criteria has changed. Additionally, unusual market or other events may prompt an off-cycle review of client accounts.

## **C. Content and Frequency of Account Reports to Clients**

Please see Item 15 for a discussion relating to the quarterly reports.

# **Item 14: Client Referrals and Other Compensation**

## **A. Economic Benefit for Providing Investment Advice to Clients**

See Item 10.D for more details.

## **B. Compensation to Unsupervised Persons for Client Referrals**

Our Professional Alliance Group program allows certain unaffiliated third parties to refer clients to MSSB. If the client invests in an investment advisory program, we pay the third party an ongoing referral fee (generally about 25% of the portion of the client fee that we would otherwise allocate to the



Financial Advisor). We may pay a fee greater or less than 25% depending on the facts and circumstances of the relationship.

## **Item 15: Custody**

MSSB is the custodian and provides you with written confirmation of securities transactions, and account statements at least quarterly. You may waive the receipt of trade confirmations after the completion of each trade in favor of alternative methods of communication where available. You may also receive mutual fund prospectuses, where appropriate. MSSB services are also provided to clients who engage third-party custodians. In the event that client accounts are held in custody outside of MSSB, the custodian will provide such statements.

We provide performance reporting to clients with a frequency as requested by the client. See Item 4.B for additional details.

## **Item 16: Investment Discretion**

In the program described in this Brochure, we do not accept investment discretion.

## **Item 17: Voting Client Securities**

MSSB does not accept proxy-voting authority in the program listed in this Brochure.

Clients may elect the investment manager to vote proxies or they may vote on their own and MSSB will send the proxy materials to you.

## **Item 18: Financial Information**

MSSB is not required to include a balance sheet in this Brochure because MSSB does not require or solicit prepayment of more than \$1,200 in fees per client, six months or more in advance.

MSSB does not have any financial conditions that are reasonably likely to impair its ability to meet its contractual commitments to clients.

MSSB and its predecessors have not been the subject of a bankruptcy petition during the past ten years.

## **Exhibit: Affiliated Money Market Funds Fee Disclosure Statement and Float Disclosure Statement**

### **Sweep Vehicles in Retirement Accounts and CESAs**

Since the dates below (“Effective Dates”), the following “Retirement Plan Accounts” (IRAs, Employee Benefit Trusts (“EBTs”), Retirement Plan Manager (“RPM” accounts) and Versatile Investment Program (“VIP”) accounts) and Coverdell Education Savings Accounts (“CESAs”) have generally been effecting temporary sweep transactions of new uninvested cash balances into Deposit Accounts established under the Bank Deposit Program:

- September 17, 2007 for “IRAs” (e.g., Traditional, Roth, Rollover, SEP, SAR-SEP, SIMPLE), and
- May 19, 2008 for the remaining Retirement Plan Accounts (i.e., EBT, RPM and VIP accounts) and CESAs.

Before the Effective Dates, MSSB affected such sweep transactions using the Morgan Stanley money market funds listed in the table below as follows

- IRAs or CESAs in advisory programs swept into the Morgan Stanley Liquid Asset Fund Inc. (“ILAF”) and
- all other Retirement Plan Accounts in advisory programs swept into one or a number of different proprietary mutual funds (which could have included ILAF) depending on the type of account and the advisory program.

As of the Effective Dates, any existing balances in these Morgan Stanley money market funds remained in the funds, pending use for account charges and other purposes. Therefore, these accounts could still maintain cash balances in these funds.

*Now, as an alternative to the Deposit Account, Retirement Plan Accounts and CESAs can choose to sweep into ILAF.*

For Retirement Plan Accounts that swept into affiliated money market funds before the Effective Dates and continue to hold cash amounts in these funds, or that now select one of these funds:

- any fee designated in the table below as “Advisory Fee” received by an MSSB affiliate is offset against the advisory program fees and
- any fees designated in the table as “Distribution and Service Fees” received by MSSB or its affiliates is credited to the account.

Accordingly, changes in these fees over time did not affect the fees paid by Retirement Plan Accounts.

### **Interest Earned on Float**

If MSSB is the custodian of your account, MSSB may retain as compensation, for providing services, the account’s proportionate share of any interest earned on cash balances held by MSSB (or an affiliate) with respect to assets awaiting investment including:

- new deposits to the account (including interest and dividends) and
- uninvested assets held by the account caused by an instruction to the custodian to buy and sell securities (which may, after the period described below, be automatically swept into a sweep vehicle).

This interest is generally at the prevailing Federal Funds interest rate.

Generally, with respect to such assets awaiting investment:

- when the custodian receives the assets on a day on which the NYSE is open (“Business Day”) and before the NYSE closes, the custodian earns interest through the end of the following Business Day and
- when the custodian receives the assets on a Business Day but after the NYSE closes, or on a day which is not a Business Day, the custodian earns interest through the end of the second following Business Day.

### **MSSB as an ERISA fiduciary**

If MSSB is a fiduciary (as that term is defined under ERISA or the Code) with respect to the Retirement Plan Account, the table below describes the fees and expenses charged to assets invested in shares of the money market funds in which the account invests (expressed as a percentage of each fund’s average daily net assets for the stated fiscal year). Note that:

- The rate of Advisory Fee and Distribution and Service Fees (including 12b-1 fees) (whether in basis points or dollars) may not be increased without first obtaining shareholder approval.
- Expenses designated as “Other Expenses” include all expenses not otherwise disclosed in the table that were deducted from each fund’s assets or charged to all shareholder accounts in the stated fiscal year (and may change from year to year).

These fees and expenses may be paid to MSSB and its affiliates for services performed. The aggregate amount of these fees is stated in the tables below. The amounts of expenses deducted from a fund's assets are shown in each fund's statement of operations in its annual report.

Morgan Stanley Investment Management (and/or its affiliates) may, from time to time, waive part of its advisory fee or assume or reimburse some of a fund's operating expenses. (This may be for a limited duration.) Such actions are noted in the fund's prospectus and/or statement of additional information. The table below shows the Total Annual Fund Operating Expenses (before management fee waivers and/or expense reimbursements) and the Total Annual Fund Operating Expenses After Fee Waivers and/or Expense Reimbursements.

MSSB believes that investing in shares of the funds for sweep purposes may be appropriate for Retirement Plans because using professionally managed money market funds allows you to access cash on an immediate basis, while providing a rate of return on your cash positions pending investment. As is typical of such arrangements, we use only affiliated money funds for this purpose.

MSSB also believes that investing a Retirement Plan's assets in the Deposit Accounts may also be appropriate. Terms of the Bank Deposit Program are further described in the Bank Deposit Program Disclosure Statement, which has been provided to you with your account opening materials.

The fund expense information below reflects the most recent information available to us as of February 12, 2015, and is subject to change. Please refer to the funds' current prospectuses, statements of additional information and annual reports for more information.

<b>Fund</b>	<b>Advisory Fee</b>	<b>Distribution and Service Fees</b>	<b>Other Expenses</b>	<b>Total Annual Fund Operating Expenses</b>	<b>Total Annual Fund Operating Expenses After Fee Waivers and/or Expense Reimbursements</b>
Active Assets Money Trust	0.25%	0.10%	0.07%	0.42%	0.18%
Active Assets Government Securities Trust	0.45%	0.10%	0.12%	0.67%	0.08%
Active Assets Institutional Government Securities Trust	0.10%	None	0.07%	0.17%	0.17%
Active Assets Institutional Money Trust	0.10%	None	0.08%	0.18%	0.17%
Morgan Stanley Liquid Asset Fund Inc.	0.23%	0.10%	0.12%	0.45%	0.19%
Morgan Stanley U.S. Government Money Market Trust	0.35%	0.10%	0.10%	0.55%	0.10%