

## Item 1: Cover Page

### **Part 2A of Form ADV Firm Brochure**

April 4, 2012

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CRD No. 110383

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This brochure provides information about the qualifications and business practices of Heritage Capital Management, Inc. If you have any questions about the contents of this brochure, please contact David Moenning at 303-670-9761 or at [Dave@heritagecapitalmanagement.com](mailto:Dave@heritagecapitalmanagement.com). The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission or by any state securities authority.

Additional information about Heritage Capital Management, Inc., is also available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). The searchable CRD number for the firm is 110383.

Heritage Capital Management, Inc., is a registered investment adviser. Registration with the SEC or State Regulatory Authority does not imply a certain level of skill or training.

## **Item 2: Material Changes**

This Firm Brochure, dated March 14, 2012, is our disclosure document prepared according to the SEC's new requirements and rules. As you will see, this document is a narrative that is substantially different in form and content, and includes some new information that we were not previously required to disclose.

Consistent with the new rules, we will ensure that you receive a summary of any material changes to this and subsequent Brochures within 120 days of the close of our business' fiscal year. Furthermore, we will provide you with other interim disclosures about material changes as necessary.

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## Item 4: Advisory Business

### A. Description of Your Advisory Firm

Heritage Capital Management, Inc. ("HCM," "Heritage," "Adviser," "we," "our," and/or "the firm"), is an independent, privately owned investment management firm which provides investment supervisory services to clients who invest in our programs via client agreements. HCM was established in 1989 by its president/owner David Moenning. Mr. Moenning's office is located in Evergreen, Colorado. HCM's main office is located in Schaumburg, IL.

### B. Description of Advisory Services Offered

Heritage Capital Management, Inc. provides investment supervisory services only. HCM employs various strategies which utilize; Exchange Traded Funds (ETFs), Inverse ETFs, stocks, mutual funds, closed end investment companies and various variable annuity products. HCM creates models for the various program strategies which then are managed via various platforms. HCM incorporates risk management strategies in all models offered although cannot guarantee that such strategies will limit loss.

Our programs are as follows:

- **FTS Program** Risk management programs that are layered on top of clients' existing mutual funds. HCM will attempt to reduce exposure to market risk during bear market periods and maintain a more invested position during bull market periods. The FTS Program is offered by HCM exclusively through Fidelity advisors and American Funds.
- **Top Stocks Strategy** Individual equity programs designed to focus on the top-rated stocks within each market sector. Our sector-neutral selection equity strategy is coupled with a long-term risk management strategy designed to reduce exposure to market risk during bear market cycles. This program is offered exclusively through Trust Company of America ("TCA").
- **Top Stocks Insider Buying Strategy** HCM utilizes its own rating system to identify the top-rated stocks for our models. In addition, we determine which stocks show the strongest performance and earnings strength. Our system utilizes hundreds of indicators. Analysis includes but is not limited to the following indicators:
  - Momentum and earnings reports
  - Corporate and industry performance
  - Corporate buying activities
- **Flexible Global Growth** A tactical asset allocation program incorporating both U.S. and foreign exposure and active risk management strategies. The management strategy focuses on "absolute return," which we define as seeking positive returns over a reasonable period of time regardless of market conditions. The advent of growing liquidity of the ETF universe, including inverse ETFs, affords HCM the added flexibility necessary to implement such a strategy. Inverse ETFs may entail more risk than non-inverse ETFs. Management seeks performance from a vast array of investment markets and asset classes, and may seek to profit from declining markets if, in our opinion,

conditions are right for such a position. This program is offered exclusively through Trust Company of America ("TCA").

- **Global Growth & Income** A balanced tactical asset allocation program incorporating both debt and equity exposure and active risk management strategies. The model utilizes HCM's Adaptive Leadership Asset Allocation and risk management strategies. This program is offered exclusively through Trust Company of America ("TCA").
- **Flexible US Growth** A tactical allocation program focusing on U. S. equity exposure and active risk management strategies. The management strategy focuses on "absolute return," which we define as seeking positive returns over a reasonable period of time regardless of market conditions. The advent of growing liquidity of the ETF universe, including inverse ETFs, affords HCM the added flexibility necessary to implement such a strategy. Management sees performance from a vast array of investment markets and asset classes, and may seek to profit from declining markets if, in our opinion, conditions are right for such a position. This program is offered exclusively through Trust Company of America ("TCA").
- **Tactical Asset Management Programs** Dynamic asset allocation strategies designed to keep portfolios focused on market leadership in terms of style and cap size. The programs also incorporate a risk management strategy designed to reduce exposure to market risk during bear market periods and maintain a more fully invested position during bull market periods. Heritage Capital Management is offered exclusively through variable annuity products offered by Pacific Life Insurance, Nationwide Life Insurance, ING, Prudential American Skandia, and Security Benefit Group. This program is also offered through Pro-funds mutual funds.
- **Flexible US – Graduated** - An actively managed tactical allocation program focusing on U. S. equity exposure and active risk management strategies. The management approach stresses "absolute return", which we define as seeking positive returns over a reasonable period of time regardless of market conditions. Via a graduated approach to building/exiting positions, we strive to be more fully invested in stock market (via ETF's) when stocks are rising and to either reduce exposure to the market or be "short" the market (via inverse ETF's) when the market is experiencing a negative cycle.
- **Flexible US – Hybrid** - An actively managed tactical allocation program focusing on U. S. equity exposure and active risk management strategies. The management approach stresses "absolute return", which we define as seeking positive returns over a reasonable period of time regardless of market conditions. We strive to be fully invested in stock market (via ETF's) when the trend of the stock market is rising and to reduce exposure to the market (or to be short via inverse ETF's) when the market is experiencing a negative cycle. The hybrid model may utilize leveraged ETF's at the discretion of management.
- **Flexible US – Aggressive** - An actively managed tactical allocation program focusing on U. S. equity exposure and active risk management strategies. The management approach stresses "absolute return", which we define as seeking positive returns over a reasonable period of time regardless of market conditions. We strive to be fully invested in stock market (via ETF's) when the trend of the stock market is rising and to be "short"

the market (via inverse ETF's) when the market is experiencing a negative cycle. The aggressive model utilizes leveraged ETF's at all times.

### **C. Client-Tailored Services and Client-Imposed Restrictions**

Clients who invest with HCM complete various documents prior to agreement approval. Representatives (solicitors) provide a standard agreement package which includes a client risk profile and suitability questionnaire, standard client agreement, model disclosure paperwork, privacy disclosures, current ADV Part II, and where appropriate, outside custody agreements. Clients are offered the opportunity to place restrictions on their accounts. HCM maintains the right to deny acceptance of a new account should we find that the restrictions would inhibit normal trading strategy within the model(s). In many cases a client may obtain the restrictions requested by carefully choosing the appropriate model strategy. Solicitors for HCM first submit all agreements to their individual broker-dealers for review and approval.

HCM offers various strategies for portfolio diversification. Clients may mix and match models under one account registration to create a portfolio that best matches their profile, time horizon, risk tolerance level, and investment capability. All clients retain indicia of ownership even though all accounts in an individual model trade at the same time and receive identical pricing.

### **D. Wrap Fee Programs**

HCM does not participate in wrap fee programs. (Wrap fee programs offer services for one all-inclusive fee.)

### **E. Client Assets Under Management**

As of 12/31/2011 assets under management totaled \$30,404,707. All assets were managed on a discretionary basis. In addition, HCM acts as a sub-advisor for a model on Mack Investment Securities, Inc.'s Money Managers Plus platform.

## Item 5: Fees and Compensation

### A. Methods of Compensation and Fee Schedule

#### A.1. Programs Utilizing Only Mutual Funds and Variable Annuities

Fees are based on the value of the account as of the client's billing date. The market value of the account is calculated by multiplying the number of shares/unit values owned in the client's account by the net asset value of the product on the last business day of the month preceding the billing month. Clients pay fees in advance on a quarterly basis. Clients receive statements directly from the custodian detailing all transactions as they occur. Clients who opt to have fees deducted directly from accounts instruct HCM in writing; clients receive an invoice prior to each quarterly fee deduction. Confirmation of payment is also noted on individual client statements from mutual fund or annuity sub-account sponsors. In certain circumstances representatives may negotiate for an adjusted fee rate prior to origination of the account. In some cases representatives will accept a slightly lower compensation percentage to facilitate this reduction. Under no circumstances will the rate be more than the maximum fee schedule states. The following maximum fee schedules apply to each account.

- ***FTS Programs***

<u>Account Size</u>	<u>Maximum Annual Fee</u>
\$5,000 to \$149,999	2.00%
\$150,000 to \$499,999	1.75%
\$500,000 to \$999,999	1.50%
\$1,000,000 and over	1.00%

- ***Tactical Asset Management and Global Opportunities Programs***

<u>Account Size</u>	<u>Maximum Annual Fee</u>
\$5,000 to \$149,999	2.25%
\$150,000 to \$499,999	2.00%
\$500,000 to \$999,999	1.50%
\$1,000,000 and over	1.00%

#### A.2. For Programs Utilizing Custodial Accounts

Management fees are billed monthly in arrears and deducted directly from the client's account per their written approval. Trust Company of America (TCA) calculates the fees based on individual fee rate and market value of individual account as of the last business day of the month. The custodian calculates the first and last month of client fees on a prorated basis. Clients have daily online access to account activity and receive statements each quarter detailing all activity which occurred in the account.



Maximum Annual Fee:

▪ ***Flexible Global Growth, Global Growth & Income, Flex US Strategies***

	<u>TCA Custodial Fee</u>	<u>HCM Mgmt Fee</u>	<u>Annual Max Total Fee</u>
\$10,000 to \$50,000	0.35%	2.50%	2.85%
\$50,001 to \$100,000	0.35%	2.15%	2.50%
\$100,001 to \$200,000	0.25%	2.00%	2.25%
\$200,001 to \$500,000	\$500	1.75%	1.75% + \$500
Over \$500,000	\$500	As Agreed	As Agreed

▪ ***Top Stocks Strategy & Top Stocks Insider Buying Strategy***

	<u>TCA Custodial Fee</u>	<u>HCM Mgmt Fee</u>	<u>Annual Max Total Fee</u>
\$25,000 to \$100,000	0.35%	1.65%	2.00%
\$100,001 to \$200,000	0.25%	1.65%	1.90%
\$200,001 to \$250,000	\$500	1.65%	1.65% + \$500
\$250,001 to \$1,000,000	\$500	1.25%	1.25% + \$500
Over \$1,000,000	\$500	1.00%	1.00% + \$500

Any commissions charged to buy and/or sell equities within managed accounts at TCA are charged at an institutional rate and shared proportionately by all clients within the traded model.

HCM reports its performance net of any and all costs incurred within the applicable investment model programs, including trading costs and only reports performance for accounts paying full advisory fee rates. We do not receive compensation derived from trading costs.

Representatives obtain the right to negotiate with HCM to obtain lower fees for their clients should circumstances warrant such action. Alternative fee schedules are available. TCA custodial fees are not negotiable. All details regarding custodial costs are included in TCA's client agreements.

Investment models incur a transaction fee when equity securities are purchased or sold. Potentially, transactions fees may be charged on mutual fund purchases and sales, although generally mutual funds are purchased at NAV. Transaction fees are paid directly to TCA. HCM, its representatives and its employees have no financial interest in and receive no benefit from the transaction fees. The cost is divided proportionately among all accounts within the model.

Qualified accounts may incur additional charges from TCA, the custodian, for special services. As indicated in the TCA custodial applications, all accounts may incur additional charges by TCA for special services such as check disbursements and wire redemptions. HCM receives no benefit from the custodian's service fees.

In the event that additions are made to an account, subsequent end-of-the-month fees will not be adjusted to represent the actual number of days that the additional money was under management. HCM management strategies emphasize risk management. To facilitate this, HCM generally maintains cash positions in accounts, which range from 3%–10%.

## **B. Client Payment of Fees**

HCM will not take custody or possession of client funds or securities at any time except to the extent that HCM may deduct fees directly from the client's account. For programs offered through TCA, HCM will deduct advisory and custodial fees directly from the client's account provided that (1) the client provides written authorization to the qualified custodian, and (2) the qualified custodian sends the client a statement, at least quarterly, indicating all amounts disbursed from the account.

The client is responsible for verifying the accuracy of the fee calculation, as the client's custodian will not verify the calculation.

For investment programs offered through insurance companies and mutual funds HCM does prepare invoices and then after approximately three days will instruct the insurance company or mutual fund to deduct and remit the fee to HCM. Of these, certain clients have arranged to pay by check subject to receiving an invoice from HCM.

## **C. Additional Client Fees Charged**

All fees paid to HCM are separate and distinct from the fees and expenses charged by exchange traded funds and mutual funds. These fees and expenses are described in each fund's prospectus. These fees generally include a management fee, other fund expenses, a distribution fee, embedded trading costs, and possibly an initial or deferred sales charge. A client could invest in a mutual fund directly without the management fee they are currently paying to HCM. HCM offers management services to registered representative solicitors for their personal/family accounts at no cost, with the exception of applicable custodial fees.

Clients are advised to read these materials carefully before investing. All fees paid for investment advisory services are separate and distinct from the fees and expenses charged by mutual funds, exchange traded funds, broker-dealers and custodians retained by clients. Such fees and expenses are described in each mutual fund's prospectus, and by any broker-dealer or custodian retained by the client. If a fund also imposes sales charges, a client may pay an initial or deferred sales charge as further described in the mutual fund's prospectus. A client using HCM may be precluded from using certain mutual funds because they may not be offered by the client's custodian.

## **D. Prepayment of Client Fees**

HCM's fees will either be paid directly by the client or disbursed to HCM by the qualified custodian of the client's investment accounts, subject to prior written consent of the client. The custodian will deliver directly to the client an account statement, at least quarterly, showing all investment and transaction activity for the period, including fee disbursements from the account.

With the exception of the programs managed at TCA which charge fees in arrears and do not require a refund policy, cancellation of investment management services may be done by either party by giving 15 days' written notice. Whenever possible, HCM will act on written instructions

upon receipt of request. Unearned fees will be refunded in full and will be calculated as of the last day of the terminating month in which written refund instructions are received. Accounts cancelled before the sixth day of service will be refunded in full. Fees will be payable initially on a prorated basis to the end of the nearest calendar quarter. Quarterly prorated calculations are based on an estimated 90-day quarter. Thereafter, fees will be paid in advance for the next quarter.

The client has the right to terminate an agreement without penalty within five business days after entering into the agreement.

### **E. External Compensation for the Sale of Securities to Clients**

HCM financial advisors are compensated solely through a salary and bonus structure. HCM is not paid any sales, service or administrative fees for the sale of mutual funds or any other investment products.

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

HCM does not charge performance fees. Performance fees are usually described as fees based on a share of capital gains or capital appreciation of the client's assets.

## Item 7: Types of Clients

HCM generally provides investment advice to; individual's pension and profit sharing plans, trusts and various business entities. Clients are obtained via referrals from investment advisory representatives. Potential clients are provided with information about our services and discuss portfolio model selections with their representatives.

- ***HCM's Minimum Account Size Schedule- Variable Annuity and Mutual Fund Strategies***

<u>Program</u>	<u>Minimum</u>
FTS	\$5,000
Tactical Asset Management	\$5,000
Global Opportunities	\$5,000

- ***Programs Utilizing Trust Company of America as Custodian***

<u>Program</u>	<u>Minimum</u>
Flexible Global Growth Model	\$ 10,000
Global Growth & Income	\$ 10,000
Flexible US Strategies	\$ 10,000
Top Stocks Strategies	\$ 25,000

In many circumstances, HCM may waive account minimum requirements prior to acceptance of the account. HCM has discretionary authority over the accounts which a client has established. HCM will not accept custody of client funds and is authorized only to effect transactions via the purchase or sale of securities and both open-end and closed-end mutual funds through custodial account agreements. Discretionary authority is limited to the amount in a client's managed account.

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

### **A. Methods of Analysis and Investment Strategies**

HCM utilizes various methods of analysis including but not limited to: charting, fundamental and technical research, reports provided by outside research company, and published financial newspapers. HCM utilizes proprietary management signals for all managed programs. HCM does not receive any products, services, or research from broker-dealers.

#### **A.1. FTS Program**

Risk management programs are layered on top of clients' existing mutual funds. HCM will attempt to reduce exposure to market risk during bear market periods and maintain a more invested position during bull market periods. The FTS Program is offered by HCM exclusively through Fidelity advisors and American Funds.

#### **A.2. Top Stocks**

Individual equity programs designed to focus on the top-rated stocks within each market sector. Our sector-neutral selection equity strategy is coupled with a long-term risk management strategy designed to reduce exposure to market risk during bear market cycles. This program is offered exclusively through Trust Company of America ("TCA").

#### **A.3. Flexible Global Growth**

The Flexible Global Growth program utilizes a multi-strategy/risk-managed approach which seeks growth around the globe and across multiple asset classes. The management system provides total flexibility in terms of portfolio allocations to regions, countries, sectors, and asset classes via the use of ETFs (exchange-traded funds) and inverse ETFs. There are four tenets to the management strategy utilized for the Flexible Global Growth program:

1. Seek Absolute Returns
2. Go Where the Growth Is
3. Utilize Multiple Investment Disciplines
4. Manage Risk at All Times

No investment's safety can be guaranteed, therefore no HCM model is designed to be a client's sole investment. Trades in ETFs are subject to risk and transaction costs. Inverse ETFs are leveraged long and short mutual funds that are designed to perform in an inverse relationship to certain market indices. Due to the leverage component of the ETFs, there may be additional risk to such investments.

#### **A.4. Global Growth & Income**

The Global Growth & Income model is an asset allocation program which combines HCM's Risk Management and Adaptive Leadership Asset Allocation systems. The ETF-based Global Growth

& Income model has a normal asset allocation target of 75% equities (50% US market, 25% foreign) and 25% bonds.

The Global Growth & Income model also incorporates risk management strategies which allow HCM to, at the manager's discretion, increase money market and/or cash positions during weak and/or high-risk market environments.

Global Growth & Income utilizes ETFs as the primary investment vehicle. The model may also utilize government and/or high yield bonds. Portfolio reviews and reallocations are performed weekly.

#### **A.5. Flexible US Growth**

HCM's Flexible US Growth program is an actively managed investment strategy designed for investors seeking (i) growth of capital in the U.S. stock market, and (ii) a risk management approach to investing. While there is no guarantee that our objectives will be met, the program strives to maintain an invested position in the U.S. stock market via index-based ETFs when HCM's market models indicate a positive market environment, and to reduce exposure to market risk when our models suggest that a negative environment is present.

The management strategy employed by the Flexible US Growth program is based on three tenets:

1. Seek Absolute Returns
2. Focus on the Leaders
3. Manage Risk at All Times

Although there are never any guarantees in investing, beginning in January 2010 the primary objective of the Flexible US Growth strategy is to seek "absolute" returns. In simple terms, this means we will strive to produce positive returns regardless of market conditions over a reasonable period of time.

At HCM, our motto is "Own the best and ignore the rest." Thus, one of the primary tenets of our management style is to focus on the leading indices of the US stock market.

One constant in investing is market leadership is always on the move. Therefore, we believe it is vital to employ a management strategy that can adapt when market environments change. HCM's Flexible US Growth program has the flexibility to allocate assets to the indices which, in our opinion, are best suited for each market environment.

HCM's Flexible US Growth program has the discretion to move to a fully defensive position when we believe market conditions have turned negative. During negative market cycles, the Flexible US Growth program may utilize a cash position or ETFs designed to provide an inverse relationship to market indices.

#### **A.6. Flexible US – Graduated**

An actively managed tactical allocation program focusing on U. S. equity exposure and active risk management strategies. The management approach stresses "absolute return", which we

define as seeking positive returns over a reasonable period of time regardless of market conditions. Via a graduated approach to building/exiting positions, we strive to be more fully invested in stock market (via ETF's) when stocks are rising and to either reduce exposure to the market or be "short" the market (via inverse ETF's) when the market is experiencing a negative cycle.

#### **A.7. Flexible US – Hybrid**

An actively managed tactical allocation program focusing on U. S. equity exposure and active risk management strategies. The management approach stresses "absolute return", which we define as seeking positive returns over a reasonable period of time regardless of market conditions. We strive to be fully invested in stock market (via ETF's) when the trend of the stock market is rising and to reduce exposure to the market (or to be short via inverse ETF's) when the market is experiencing a negative cycle. The hybrid model may utilize leveraged ETF's at the discretion of management.

#### **A.8. Flexible US Aggressive**

An actively managed tactical allocation program focusing on U. S. equity exposure and active risk management strategies. The management approach stresses "absolute return", which we define as seeking positive returns over a reasonable period of time regardless of market conditions. We strive to be fully invested in stock market (via ETF's) when the trend of the stock market is rising and to be "short" the market (via inverse ETF's) when the market is experiencing a negative cycle. The aggressive model utilizes leveraged ETF's at all times.

#### **A.9. Top Stocks Insider Buying Strategy**

HCM utilizes its own rating system to identify the top-rated stocks for our models. In addition, we determine which stocks show the strongest performance and earnings strength. Our system utilizes hundreds of indicators. Analysis includes but is not limited to the following indicators:

- Momentum and earnings reports
- Corporate and industry performance
- Corporate buying activities

#### **A.10. Material Risks of Investment Instruments**

The investment vehicles most commonly purchased for HCM clients are shares of registered open-end mutual funds and exchange traded funds. Many of these investments can be purchased directly by clients without utilizing the services of an advisor. Registered investment companies charge their own management fees and expenses. These fees and expenses are detailed in each respective mutual fund's prospectus and are in addition to any fees charged by HCM.

HCM typically invests in open-end mutual funds and exchange-traded funds for the vast majority of its clients. However, for certain clients, HCM may effect transactions in the following types of securities:

- Equity securities



- Warrants
- Fixed Income securities

**A.10.a. Equity Securities (stocks, warrants, and related equity securities)**

Investing in individual companies involves inherent risk. The major risks relate to the company's capitalization, quality of the company's management, quality and cost of the company's services, the company's ability to manage costs, efficiencies in the manufacturing or service delivery process, management of litigation risk, and the company's ability to create shareholder value (i.e., increase the value of the company's stock price). Foreign securities, in addition to the general risks of equity securities, have geopolitical risk, financial transparency risk, currency risk, regulatory risk and liquidity risk.

**A.10.b. Mutual Fund Securities**

Investing in mutual funds carries inherent risk. The major risks of investing in a mutual fund include the quality and experience of the portfolio management team and its ability to create fund value by investing in securities that have positive growth, the amount of individual company diversification, the type and amount of industry diversification, and the type and amount of sector diversification within specific industries. In addition, mutual funds tend to be tax inefficient and therefore investors may pay capital gains taxes on fund investments while not having yet sold the fund.

**A.10.c. Exchange Traded Funds**

Investing in exchange traded funds ("ETF") carries inherent risk. Specifically, ETFs, depending on their underlying portfolio size, can have wide price (bid and ask) spreads, thus diluting or negating any upward price movement of the ETF. Also, ETFs require more frequent portfolio reporting by regulators and are thereby more susceptible to actions by hedge funds that could have a negative impact on the price of the ETF. Certain ETFs may employ leverage, which creates additional volatility and price risk depending on the amount of leverage utilized, the collateral and the liquidity of the supporting collateral.

**A.10.d. Fixed Income Securities**

Fixed income securities carry additional risks than those of equity securities described above. These risks include the company's ability to retire its debt at maturity, the current interest rate environment, the coupon interest rate promised to bondholders, legal constraints, jurisdictional risk (U.S or foreign) and currency risk. If bonds have maturities of 10 years or greater, they will likely have greater price swings when interest rates move up or down. The shorter the maturity the less volatile the price swings. Foreign bonds have liquidity and currency risk.

## **B. Investment Strategy and Method of Analysis Material Risks**

### **B.1. Margin Leverage**

Although HCM, as a general business practice, does not utilize leverage, there may be instances in which exchange-traded funds, other separate account managers and, in very limited circumstances, HCM will utilize leverage. In this regard please review the following:

The use of margin leverage enhances the overall risk of investment gain and loss to the client's investment portfolio. For example, investors are able to control \$2 of a security for \$1. So if the price of a security rises by \$1, the investor earns a 100% return on their investment. Conversely, if the security declines by \$.50, then the investor loses 50% of their investment.

The use of margin leverage entails borrowing, which results in additional interest costs to the investor.

Broker-dealers who carry customer accounts require a minimum equity requirement when clients utilize margin leverage. The minimum equity requirement is stated as a percentage of the value of the underlying collateral security with an absolute minimum dollar requirement. For example, if the price of a security declines in value to the point where the excess equity used to satisfy the minimum requirement dissipates, the broker-dealer will require the client to deposit additional collateral to the account in the form of cash or marketable securities. A deposit of securities to the account will require a larger deposit, as the security being deposited is included in the computation of the minimum equity requirement. In addition, when leverage is utilized and the client needs to withdraw cash, the client must sell a disproportionate amount of collateral securities to release enough cash to satisfy the withdrawal amount based upon similar reasoning as cited above.

Regulations concerning the use of margin leverage are established by the Federal Reserve Board and vary if the client's account is held at a broker-dealer versus a bank custodian. Broker-dealers and bank custodians may apply more stringent rules as they deem necessary.

### **B.2. Short-Term Trading**

Although HCM, as a general business practice, does not utilize short-term trading, there may be instances in which short-term trading may be necessary or an appropriate strategy. In this regard, please read the following:

There is an inherent risk for clients who trade frequently in that high-frequency trading creates substantial transaction costs that in the aggregate could negatively impact account performance.

### **B.3. Short Selling**

HCM generally does not engage in short selling but reserves the right to do so in the exercise of its sole judgment. Short selling involves the sale of a security that is borrowed rather than owned. When a short sale is effected, the investor is expecting the price of the security to decline in value so that a purchase or closeout of the short sale can be effected at a significantly lower price. The primary risks of effecting short sales is the availability to borrow the stock, the

unlimited potential for loss, and the requirement to fund any difference between the short credit balance and the market value of the security.

#### **B.4. Technical Trading Models**

Technical trading models are mathematically driven based upon historical data and trends of domestic and foreign market trading activity, including various industry and sector trading statistics within such markets. Technical trading models, through mathematical algorithms attempt to identify when markets are likely to increase or decrease and identify appropriate entry and exit points. The primary risk of technical trading models is that historical trends and past performance cannot predict future trends and there is no assurance that the mathematical algorithms employed are designed properly, updated with new data, and can accurately predict future market, industry and sector performance.

### **C. Security-Specific Material Risks**

There is an inherent risk for clients who have their investment portfolios heavily weighted in one security, one industry or industry sector, one geographic location, one investment manager, one type of investment instrument (equities versus fixed income). Clients who have diversified portfolios, as a general rule, incur less volatility and therefore less fluctuation in portfolio value than those who have concentrated holdings. Concentrated holdings may offer the potential for higher gain, but also offer the potential for significant loss.

## **Item 9: Disciplinary Information**

Registered investment advisers are required to disclose all material facts regarding any legal or disciplinary events which would be material to a client or prospective client's evaluation of HCM's business or the integrity of our management.

### **A. Criminal or Civil Actions**

There is nothing to report on this item.

### **B. Administrative Enforcement Proceedings**

There is nothing to report on this item.

### **C. Self-Regulatory Organization Enforcement Proceedings**

There is nothing to report on this item.

## **Item 10: Other Financial Industry Activities and Affiliations**

### **A. Broker-Dealer or Representative Registration**

Neither HCM nor its affiliates are registered as a broker dealer, registered representatives of a broker dealer and do not have an application to register pending.

### **B. Futures or Commodity Registration**

Neither HCM nor its affiliates are registered as a commodity firm, futures commission merchant, commodity pool operator or commodity trading advisor and do not have an application to register pending.

### **C. Material Relationships Maintained by this Advisory Business and Conflicts of Interest**

HCM employs various Solicitors who solicit business on behalf of HCM and receive a portion of HCM's ongoing investment management fee. See Item 14 for additional disclosure.

HCM acts as a sub-advisor for the Money Manager Plus Program, an investment advisory program sponsored by Mack Investment Securities, Glenview, IL. HCM's compensation is based on a percentage of assets managed in MPP models.

### **D. Recommendation or Selection of Other Investment Advisors and Conflicts of Interest**

HCM does not recommend separate account managers or other investment products in which it receives any form of compensation from the separate account manager or investment product sponsor.

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

### **A. Code of Ethics Description**

HCM has adopted a Code of Ethics ("Code") for all supervised persons to ensure that the high ethical standards long maintained by Heritage Capital Management, Inc., continue to be applied. The purpose of the Code is to preclude activities which may lead to or give the appearance of conflicts of interest, insider trading, and other forms of prohibited or unethical business conduct.

Pursuant to Section 206 of the Advisers Act, both HCM and its employees are prohibited from engaging in fraudulent, deceptive, or manipulative conduct. Compliance with this section involves more than acting with honesty and good faith alone. It means that HCM has an affirmative duty of utmost good faith to act solely in the best interests of its clients. All supervised persons must acknowledge the terms of the Code annually or as amended. We will provide a copy of the Code to any prospective or current client upon request.

### **B. Investment Recommendations Involving a Material Financial Interest and Conflicts of Interest**

HCM does not engage in principal trading (i.e., the practice of selling stock to advisory clients from a firm's inventory or buying stocks from advisory clients into a firm's inventory). In addition, HCM does not recommend any securities to advisory clients in which it has some proprietary or ownership interest.

### **C. Advisory Firm Purchase of Same Securities Recommended to Clients and Conflicts of Interest**

HCM or its employees may at any time own the same mutual fund or securities HCM recommends to clients. Employees are required to submit or provide online access to duplicate brokerage statements to Compliance to avoid any potential conflict of interest. In addition, HCM has adopted a Code of Ethics covering such areas as personal securities trading, client confidentiality, insider trading, and gifts and gratuities.

### **D. Client Securities Recommendations or Trades and Concurrent Advisory Firm Securities Transactions and Conflicts of Interest**

HCM, its affiliates, employees and their families, trusts, estates, charitable organizations, and retirement plans established by it may effect securities transactions for their own accounts that differ from those recommended or effected for other HCM clients. HCM will make a reasonable attempt to trade securities in client accounts at or prior to trading the securities in its affiliate, corporate, employee or employee-related accounts. Trades executed the same day will likely be subject to an average pricing calculation. It is the policy of HCM to place the client's interests above those of HCM and its employees.

## Item 12: Brokerage Practices

### A. Factors Used to Select Broker-Dealers for Client Transactions

HCM has brokerage discretion. We receive no financial benefit from choosing one broker-dealer over another. We do not participate in any soft-dollar arrangements. We have chosen TCA to act as custodian for our various managed models due to our long standing relationship and overall experience with the firm. TCA together with BNY ConvergeEx provide us with competitive trade pricing and execution. Generally, HCM does not allow clients to direct their brokerage away from TCA.

Custodial accounts may invest in shares of open-end mutual fund companies, closed-end investment companies, unit investment trusts and common stock, money markets, interest bearing accounts, exchange-traded index funds (ETFs), and equity traded funds. As a result, commission charges under these programs may be greater than those in other programs because of additional commission charges incident to execution of these trades.

In addition, shares of closed-end investment management companies traditionally trade at a discount or premium; therefore, clients in the programs managed at TCA which purchase and sell shares of closed-end investment companies may not receive the stated and expected net asset value of these shares. Revise to reflect that although HCM may recommend TCA it's only because certain of their services are offered exclusively through TCA.

### B. Aggregating Securities Transactions for Client Accounts

#### B.1. Best Execution

HCM, pursuant to the terms of its investment advisory agreement with clients, has discretionary authority to determine which securities are to be bought and sold, the price of such securities, the executing broker, and the commission rates to be paid to effect such transactions. HCM recognizes that the analysis of execution quality involves a number of factors, both qualitative and quantitative. HCM will follow a process in an attempt to ensure that it is seeking to obtain the most favorable execution under the prevailing circumstances when placing client orders. These factors include but are not limited to the following:

- The financial strength, reputation and stability of the broker
- The efficiency with which the transaction is effected
- The ability to effect prompt and reliable executions at favorable prices (including the applicable dealer spread or commission, if any)
- The availability of the broker to stand ready to effect transactions of varying degrees of difficulty in the future
- The efficiency of error resolution, clearance and settlement
- Block trading and positioning capabilities
- Performance measurement
- Online access to computerized data regarding customer accounts

- Availability, comprehensiveness, and frequency of brokerage and research services
- Commission rates
- The economic benefit to the client
- Related matters involved in the receipt of brokerage services

Consistent with its fiduciary responsibilities, HCM seeks to ensure that clients receive best execution with respect to the clients' transactions by blocking client trades to reduce commissions and transaction costs. To the best of HCM's knowledge, these custodians provide high-quality execution, and HCM's clients do not pay higher transaction costs in return for such execution.

Commission rates and securities transaction fees charged to effect such transactions are established by the client's independent custodian and/or broker-dealer. Based upon its own knowledge of the securities industry, HCM believes that such commission rates are competitive within the securities industry. Lower commissions or better execution may be able to be achieved elsewhere.

## **B.2. Directed Brokerage**

### **B.2.a. HCM Recommendations**

HCM generally does not recommend broker-dealers or custodians. HCM offers its investment management services through specific custodians and or program sponsors with which it has a contractual relationship. An investor may only utilize HCM if he has an account with such custodian or investment sponsor.

### **B.2.b Client-Directed Brokerage**

HCM does not allow for directed brokerage.

## **B.3. Security Allocation**

Since HCM may be managing accounts with similar investment objectives, HCM may aggregate orders for securities for such accounts. In such event, allocation of the securities so purchased or sold, as well as expenses incurred in the transaction, is made by HCM in the manner it considers to be the most equitable and consistent with its fiduciary obligations to such accounts.

HCM's allocation procedures seek to allocate investment opportunities among clients in the fairest possible way, taking into account the clients' best interests. HCM will follow procedures to ensure that allocations do not involve a practice of favoring or discriminating against any client or group of clients. Account performance is never a factor in trade allocations.

HCM's advice to certain clients and entities and the action of HCM for those and other clients are frequently premised not only on the merits of a particular investment, but also on the suitability of that investment for the particular client in light of his or her applicable investment objective, guidelines and circumstances. Thus, any action of HCM with respect to a particular investment may, for a particular client, differ or be opposed to the recommendation, advice, or actions of HCM to or on behalf of other clients.



**B.4. Block Trading/Trading Aggregation**

The aggregation of client transactions allows HCM to execute transactions in a more timely, equitable, and efficient manner and seeks to reduce overall commission charges to clients. Our firm's policy is to aggregate client transactions where possible and when advantageous to clients. Employees may be invested within models and will receive an average share price identical to non-employee clients. HCM's allocation procedures are designed to be fair and equitable to each individual account invested in a model.

In addition, when HCM trades for its models, the trading may result in fractional shares of certain securities in order to mathematically fit the proportionate ownership in the model. In that case, HCM will round to the nearest whole share amount and each client's account will be credited accordingly.

**B.5. Allocation of Trades**

All allocations will be made prior to the close of business on the trade date. In the event an order is "partially filled", the allocation will be made in the best interests of all the clients in the order, taking into account all relevant factors including, but not limited to, the size of each client's allocation, clients' liquidity needs and previous allocations. In most cases, accounts will get a pro forma allocation based on the initial allocation. This policy also applies if an order is "over-filled."

HCM acts in accordance with its duty to seek best price and execution and will not continue any arrangements if HCM determines that such arrangements are no longer in the best interest of its clients.

**B.6. Soft Dollar Arrangements**

HCM does not utilize soft dollar arrangements. HCM does not direct brokerage transactions to executing brokers for research and brokerage services.

**B.7. Brokerage for Client Referrals**

HCM does not engage in the practice of directing brokerage commissions in exchange for the referral of advisory clients.

**B.8. Cross-Trading**

HCM does not engage in agency cross trading. In the event a client wishes to liquidate their account, HCM is only able to sell whole shares through TCA as a broker-dealer.

## **Item 13: Review of Accounts**

### **A. Schedule for Periodic Review of Client Accounts or Financial Plans and Advisory Persons Involved**

HCM determines the appropriate strategy for all accounts within each management program offered. The determinations are based on proprietary technical systems which apply to each model managed. Since all accounts are provided equal priority, any change in an account holding a particular security would effect changes in all accounts holding that security. Account and model reviews are conducted by our Chief Portfolio Manager as well as qualified administrative personnel.

Daily, HCM reviews a sampling of client accounts which represent many of our actively managed models held at TCA. Accounts are reviewed and compared to the portfolio manager's daily performance expectations.

### **B. Review of Client Accounts on Non-Periodic Basis**

Accounts may be reviewed upon request of representatives or clients.

HCM may perform ad hoc reviews on an as-needed basis if there have been material changes in the client's investment objectives or risk tolerance, or a material change in how HCM formulates investment advice.

### **C. Content of Client-Provided Reports and Frequency**

HCM offers a report on a quarterly basis which indicates the performance in percentage terms for each specific type of program managed. Mutual fund sponsors supply clients with confirmation for orders executed, periodic statements, and other material supplied to their shareholders. TCA program clients have continuous online access to account information and receive detailed quarterly statements from TCA showing all transactions which occurred in the client's account. Clients are encouraged to refer to their personalized statements provided by their custodians. Such custodian statements are the official record of the customer's account.

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

### **A. Economic Benefits Provided to the Advisory Firm from External Sources and Conflicts of Interest**

HCM does not refer clients to third party in exchange for economic benefit.

### **B. Advisory Firm Payments for Client Referrals**

In certain circumstances, HCM compensates investment representatives of investment advisers and broker-dealers who refer new clients to our programs. Compensation is based on written agreements, and representatives who participate in these arrangements must disclose their arrangement in writing to clients as part of their disclosure pursuant to rule 206-(4)-3 under the Investment Advisors Act of 1940. Generally, the payments are a percentage of management fees collected by HCM.

Investment adviser representatives of HCM with at least \$7 million under management will receive an additional 10% payout on their share of collected fees. Therefore, solicitors may have an incentive to market our products over others. The fee for the services from HCM will be identical to that charged by HCM if no additional payment was made. Solicitors must provide approved client agreements which disclose the fact that they are receiving a higher than average payout.

## Item 15: Custody

HCM does not accept custody of client assets. All assets are held by Trust Company of America ("TCA") or a qualified custodian appointed by the client.

HCM clients receive quarterly detailed statements directly from TCA. Outside custodians, mutual funds, and variable annuity accounts also provide direct quarterly reporting to their clients that detail all transactions, fee dispersal, and performance information. TCA as well as many other custodial firms HCM utilizes provide 24/7 online account viewing.

Clients are encouraged to review their own individual statements provided by their custodians for accuracy.

## **Item 16: Investment Discretion**

Clients who utilize HCM's portfolio management services provide HCM with limited discretionary trading authority and the authority to deduct portfolio management fees from an account. This means HCM will have authority to execute securities transactions, to include the determination of the securities and amount to be bought and sold. HCM executes orders directly with the client's custodian or investment sponsor. HCM will never assume full power of attorney. HCM will not have the authority to withdraw funds or take custody of account funds or securities (other than distributions directly to the account holder or for HCM portfolio management fees). The limited discretionary trading authority and authority to deduct advisory fees is provided to HCM through the execution of TCA authorization initiated by the account holder.

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

HCM votes client proxies. As described in our proxy voting policies, HCM casts most of its proxy votes, particularly on routine matters, in accordance with the company management recommendations unless we believe that the position of the management of a portfolio company may not be in the best interest of shareholders. Records are maintained in our corporate headquarters and are available for viewing upon request.

## **Item 18: Financial Information**

### **A. Balance Sheet**

HCM does not require the prepayment of fees of \$1200 or more, six months or more in advance, and as such is not required to file a balance sheet.

### **B. Financial Conditions Reasonably Likely to Impair Advisory Firm's Ability to Meet Commitments to Clients**

HCM does not have any financial issues that would impair its ability to provide services to clients.

### **C. Bankruptcy Petitions During the Past Ten Years**

There is nothing to report on this item.