

# **Form ADV Firm Brochure Morgan Stanley Smith Barney Venture Services, LLC**

**March 31, 2011**

485 Lexington Avenue  
NY, NY 10017  
Tel: 212-761-4000  
Fax: 866-897-9539

**This brochure provides information about the qualifications and business practices of Morgan Stanley Smith Barney Venture Services, LLC (“VS”). If you have any questions about the contents of this brochure, please contact us at tel. 212-761-4000. 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 VS 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

Not applicable

## Item 3: Table of Contents

Item 2: Material Changes.....	2
Item 3: Table of Contents .....	3
Item 4: Advisory Business .....	5
A. Description of VS, Principal Owners .....	5
B. Description of Advisory Services .....	5
C. Customized Advisory Services and Client Restrictions.....	6
D. Portfolio Management Services to Wrap Fee Programs .....	6
E. Assets Under Management (“AUM”).....	6
Item 5: Fees and Compensation .....	6
A. Compensation for Advisory Services .....	6
B. Payment of Fees.....	6
C. Additional Fees and Expenses .....	6
D. Prepayment of Fees.....	7
Item 6: Performance Based Fees and Side by Side Management .....	7
Item 7: Types of Clients.....	7
Item 8: Methods of Analysis, Investment Strategies and Risk of Loss.....	7
A. Method of Analysis and Investment Strategies .....	7
B. Material, Significant, or Unusual Risks Relating to Investment Strategies.....	7
C. Risks Associated with Particular Types of Securities .....	7
Item 9: Disciplinary Information .....	8
Item 10: Other Financial Industry Activities and Affiliations .....	12
A. Broker-Dealer Registration Status.....	12
B. Futures Commission Merchant, Commodity Pool Operator, or Commodity Trading Adviser Registration Status....	12
C. Material Relationships or Arrangements with Industry Participants.....	13
D. Material Conflicts of Interest .....	15
Item 11: Code of Ethics, Participation or Interest in Client Transactions and Personal Trading.....	17
A. Code of Ethics .....	17
B. Securities That You or a Related Person Has a Material Financial Interest .....	17
C. Investing in Securities That You or a Related Person Recommends to Clients or has a Financial Interest .....	17
D. Conflicts of Interest Created by Contemporaneous Trading .....	17
Item 12: Brokerage Practices .....	17
A. Factors in Selecting or Recommending Broker-Dealers for Client Transactions.....	17
B. Aggregation of Securities Transactions for Clients.....	18
Item 13: Review of Accounts.....	18
Item 14: Client Referrals and Other Compensation .....	18
Item 15: Custody.....	18
Item 16: Investment Discretion.....	19
Item 17: Voting Client Securities.....	19

Item 18: Financial Information .....	19
Item 19: Requirements for State-Registered Adviser .....	19

## Item 4: Advisory Business

### A. Description of VS, Principal Owners

#### Introduction to Morgan Stanley Smith Barney Venture Services, LLC

Morgan Stanley Smith Barney Venture Services LLC (“VS”) was organized in 1999 and is wholly-owned by Morgan Stanley Smith Barney Holdings LLC (“Holdings”), which is a joint venture between Morgan Stanley and Citigroup Inc. (“Citigroup”). As of March 31, 2011, Morgan Stanley owns 51% of Holdings and Citigroup owns 49%, in each case through subsidiaries.

VS serves as the investment adviser to several investment partnerships (individually a “Fund” and collectively the “Funds”) organized by Salomon Smith Barney Inc. (the predecessor of Citigroup Global Markets Inc. (“CGMI”)) to offer qualified investors the opportunity to invest in private equity investment “funds of funds.”

### B. Description of Advisory Services

As investment adviser, VS invests the assets of each Fund in various underlying private equity investment funds that it selects (the “Underlying Funds”). A complete description of each Fund, including its investment objective, operations and activities, management fees, incentive allocations and structure can be obtained from the Confidential Private Offering Memorandum for such Fund that is delivered to investors in such Fund prior to investment. VS does not provide investment advice directly to investors in the Funds. VS provides investment advisory services to each Fund pursuant to an investment advisory agreement between VS and such Fund. The investment advisory agreement sets forth the circumstances under which the Fund may terminate the services of VS prior to the end of the Fund’s term.

Pursuant to an Amended and Restated Administration Agreement among Stepstone Group LLC (“StepStone”), Morgan Stanley Smith Barney Private Management LLC (“PM”), an affiliate of VS, Morgan Stanley Smith Barney Private Management II LLC (“PM II”), an affiliate of VS, the Funds and certain investment funds advised by affiliates of VS (“Affiliated Funds”), dated as of January 1, 2011 (“Administration Agreement”), Stepstone has been appointed administrator of each of the Funds. In that capacity, Stepstone may perform for the Funds, in place of VS, some of the activities (including certain administrative and investment advisory services) described in this Form ADV as being performed for the Funds by VS. As compensation for Stepstone’s provision of these services, PM, PM II and VS have agreed, pursuant to the Administration Agreement, to pay Stepstone an annual fee.

As investment adviser to a Fund, VS is responsible for selecting the Underlying Funds in which such Fund invests. The Underlying Funds, which generally will be structured as limited partnerships, limited liability companies and other similar structures, generally will acquire private equity and equity-related securities in connection with venture capital and similar negotiated transactions.

VS is responsible for investing cash held by a Fund in temporary investments pending investment in an Underlying Fund, pending distribution to investors in the Fund or for any other purpose. “Temporary Investments” include (a) cash or cash equivalents, (b) marketable direct obligations issued or unconditionally guaranteed by the United States of America, or issued by any agency thereof, maturing within one year from the date of acquisition thereof, (c) money market instruments or other short-term debt obligations having at the date of purchase by the Partnership the highest or second highest rating obtainable from either Standard & Poor’s Corporation or Moody’s Investor Services, Inc. or their successors, (d) interest bearing accounts at a registered broker-dealer, (e) obligations of, or fully guaranteed as to timely payment of principal and interest by, the United States of America and with a maturity date not in excess of 18 months from the date of purchase by the Partnership, (f) interest bearing accounts and/or certificates of deposit of any U.S. bank with capital and surplus in excess of \$200 million and whose debt securities are rated at least A by Moody’s Investor Services, Inc. and A2 by Standard and Poor’s Corporation, (g) repurchase agreements of any U.S. bank with capital and surplus in excess of \$200 million and whose debt securities are rated at least A by Moody’s Investor Services, Inc. and A2 by Standard and Poor’s Corporation, (h) a registered investment company that holds itself out as complying with Rule 2a-7 under the Investment Company Act, or (i) pooled investment funds or accounts which invest only in securities or instruments of the type described in (a) through (d). Temporary Investments may include instruments issued, or funds managed, by an affiliate of VS, in which case such affiliate will receive fees or other compensation in connection with such investment.

A Fund may receive distributions from an Underlying Fund in kind in the form of marketable securities of portfolio companies, some of which may be restricted securities. With respect to such distributions, VS has the discretion to sell such securities and distribute the cash proceeds, distribute such securities in kind or offer the Fund’s limited partners the option, subject to VS’s consent, either to receive the securities in kind or to have the Fund sell them and distribute the cash proceeds. While VS will use reasonable efforts either to sell or to distribute marketable securities promptly, a Fund’s investors will bear any associated costs or market risks during the disposition process.

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

Subject to the supervision and direction of a Fund's general partner, VS will manage a Fund's investment portfolio and make investment decisions for such Fund in accordance with the investment objective, policies, restrictions and limitations specified in such Fund's Confidential Private Offering Memorandum and such Fund's Limited Partnership Agreement or other applicable constituent documents.

VS establishes an Investment Selection Committee for each Fund which is responsible for the selection of the Underlying Funds in which the Fund invests. Each Investment Selection Committee may include senior professionals drawn from among the following investment resources of VS's affiliates: (i) Morgan Stanley Smith Barney LLC ("MSSB"), (ii) CGMI and (iii) Morgan Stanley, Citigroup and their respective affiliates.

The selection of Underlying Funds for a Fund by such Fund's Investment Selection Committee is based on a review and assessment of potential funds, their management teams, and such teams' track records, taking into consideration such Fund's investment objective, policies, restrictions and limitations set forth in such Fund's confidential Private Offering Memorandum and such Fund's Limited Partnership Agreement.

It should be noted that an investment in an Underlying Fund is an illiquid investment and generally will be held until the Underlying Fund terminates. A Fund generally has limited or no redemption or transfer rights with respect to an investment in an Underlying Fund. Accordingly, a Fund's Investment Selection Committee has no significant ongoing role following the selection of Underlying Funds for the Fund. Currently, the Investment Selection Committees have no active role since all Underlying Funds have been selected for all Funds.

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

VS does not provide portfolio management services to wrap fee programs.

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

Discretionary AUM at VS as of December 31, 2010 was approximately \$191,348,577.

# **Item 5: Fees and Compensation**

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

VS's management fee generally ranges from 1.25% to 1.50% per annum of each investor's capital commitment to the Fund during the investment period; thereafter the fee is calculated on invested capital, as defined in each Fund's Confidential Private Offering Memorandum. VS may, in its sole discretion, reduce or waive the management fee with respect to any investor. In addition, VS receives an incentive allocation ("Carried Interest") when a Fund's investment returns exceed certain specified levels. VS's Carried Interest generally is 5% of a Fund's profits following return of capital and payment of a preferred return to investors. A Fund, in its sole discretion, may reduce or waive the Carried Interest to be received by VS with respect to any investor. Upon termination of a Fund, VS is required to restore funds to a Fund, if and to the extent VS received cumulative Carried Interest distributions (net of taxes) in excess of Carried Interest amounts otherwise distributable to VS pursuant to the specified formula applied on an aggregate basis to all distributions made by such Fund. Amounts so restored by VS will be distributed to the investors in the Fund. In addition, a Fund, as an investor in Underlying Funds, will be subject to all fees and expenses of such Underlying Funds as provided in their organizational documents, including any management fees and carried interest obligations. A complete description of the fees payable by a Fund can be obtained from the Confidential Private Offering Memorandum for such Fund that is delivered to investors in such Fund prior to investment.

## **B. Payment of Fees**

As compensation for providing investment advisory services to a Fund, VS is paid a quarterly management fee, in arrears, by the Fund at a per annum rate set forth in the Confidential Private Offering Memorandum for such Fund that is delivered to investors in such Fund prior to investment.

## **C. Additional Fees and Expenses**

The fees described in this brochure do not cover:

- the costs of investment management fees and other expenses charged by the investment manager to the Underlying Funds in which the Fund invests

- “mark-ups,” “mark-downs,” and dealer spreads (A) that affiliates of VS 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 VS 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 VS or its affiliates
- 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).

For more information regarding brokerage commissions, see Item 12.

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

VS does not offer Funds the ability to pay for fees in advance.

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

Please see Item 5.A for a description of the compensation VS receives based on Carried Interest. All Funds managed by VS are charged Carried Interest.

### **Item 7: Types of Clients**

VS serves as the investment adviser to Funds to offer qualified investors the opportunity to invest in private equity investment “funds of funds.” VS does not provide investment advice directly to investors in the Funds. VS provides investment advisory services to each Fund pursuant to an investment advisory agreement between VS and such Fund. While VS does not provide investment advisory services directly to investors in the Funds, each Fund requires a minimum capital commitment generally ranging from \$500,000 to \$1,000,000 from each investor. VS may accept a lower capital commitment in VS’s discretion.

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

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

As described in Item 4B, VS provides discretionary management to the Funds. Investing in securities involves risk of loss that the Funds and investors in the Funds should be prepared to bear. Investors in Funds should review the Confidential Private Offering Memorandum for their particular Fund for a discussion on the material risks associated with the types of investments in which the Fund invests.

**Other Relationships with Managers.** Some managers of the Underlying Funds that VS recommends may have business relationships with VS or its affiliates. For example, a manager may use MS&Co. or a Citi affiliate as its broker or may be an investment banking client of MS&Co. or a Citi affiliate. VS does not consider the existence nor lack of a business relationship in determining whether to recommend an Underlying Fund.

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

All trading by a Fund is at the Fund’s own risk. The value of the assets in a Fund is subject to a variety of factors. VS does not guarantee performance, and our past performance with respect to other funds does not predict any Fund’s future performance.

For other risks relating to the particular strategy you hold in your Investors in Funds should review the Confidential Private Offering Memorandum for their particular Fund(s) for a discussion on the material risks associated with the particular strategy used by VS for the Fund in which the investor participates.

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

**Risks Relating to Alternative Investments.** As further described in each Fund’s Confidential Private Offering Memorandum, an investment in alternative investments can be highly illiquid, is speculative and not suitable for all investors. 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, short-selling, 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. Individual funds will have specific risks related to their investment programs that will vary from fund to fund.

Investors in Funds should review the Confidential Private Offering Memorandum for their particular Fund for a discussion on the material risks associated with the types of investments in which the Fund invests.

## 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 CGM are predecessor broker-dealer firms of MSSB.

- The National Association of Securities Dealers Inc. (“NASD”) alleged that between October, 1999 and December, 2002, MSDW violated the non-cash compensation provisions of the NASD Conduct Rules (under which MSDW was prohibited from providing its Financial Advisors with non-cash compensation for sales of mutual funds and variable annuities that were not based on total sales and equal weighting). MSDW offered rewards to its Financial Advisors for sales of affiliated mutual funds in general, or particular affiliated mutual funds or certain variable annuities. By a Letter of Acceptance, Waiver and Consent (“LAWC”) dated September 15, 2003, MSDW agreed to (1) fines totaling \$2.25 million; (2) update its compliance systems and procedures; and (3) retain an independent consultant to review and make recommendations on MSDW’s supervisory and compliance procedures.
- On April 28, 2003, the SEC filed a complaint alleging that MS&Co. violated certain NASD and New York Stock Exchange (“NYSE”) Conduct Rules (collectively, the “Conduct Rules”) by creating conflicts of interest for its research analysts with respect to investment banking activity, failing to adequately manage such conflicts, failing to ensure, in offerings where MS&Co. was the lead underwriter, that payments made to other broker-dealers for publishing research reports were disclosed by the issuers in the offering documents and the other broker-dealers in their research reports, and failing to supervise properly its research analysts, including with respect to the ratings, price targets and content of the reports of senior research analysts. Without admitting or denying the substantive allegations in the complaint, on October 31, 2003, MS&Co. consented to the entry of a final judgment that enjoined MS&Co. from violating the Conduct Rules and required it to make payments of \$50 million for past conduct and allocate \$75 million to fund independent research. In addition, MS&Co. agreed to a number of structural changes to the operations of its equity research and investment banking operations. Concurrently, MS&Co. also entered into a settlement with the NYSE, the NASD and the Attorney General of the State of New York with respect to the same conduct specified in the complaint. MS&Co. is also in the process of finalizing settlements with the other state and territorial securities administrators.
- In 2003, Solomon Smith Barney (“SSB”), now known as CGM, settled civil and regulatory actions brought by the SEC, the NYSE, the NASD, the Attorney General of the State of New York (“NYAG”), and state securities regulators, which alleged violations of certain federal and state securities laws and regulations, and certain NASD and NYSE rules, by SSB arising out of certain business practices concerning sell-side research during 1999 to 2001, and initial public offerings (“IPOs”) during 1996 to 2000. The actions alleged, among other things, that SSB published fraudulent research reports, permitted inappropriate influence by investment bankers over research analysts, and failed to adequately supervise the employees who engaged in those practices. It was also alleged that SSB engaged in improper “spinning” of shares to executives of investment banking clients and failed to maintain policies and procedures reasonably designed to prevent the potential misuse of material non-public information in certain circumstances. Without admitting or denying the findings, SSB consented to (1) censures by NASD and the NYSE; (2) cease and desist orders in state proceedings prohibiting SSB from violating certain state laws and regulations; (3) a judgment prohibiting SSB from violating certain laws and regulations; (4) certain operational reforms; (5) participating in a voluntary initiative pursuant to which SSB will no longer make allocations of securities in hot IPOs to accounts of executive officers or directors of U.S. public companies; and (6) a payment of \$400 million.
- The SEC alleged disclosure violations in connection with marketing arrangements between MSDW and certain mutual fund complexes in connection with the offer and sale of class B shares in certain Morgan Stanley proprietary mutual funds in the amount of \$100,000 or more in a single transaction. The SEC also alleged that receipt of directed brokerage commissions as payment for such marketing arrangements contravened NASD Rule 2830(k). On November 17, 2003, without admitting or denying the findings, MSDW consented to orders including a censure; a cease and desist; and an undertaking to distribute, for the benefit of certain customers, \$50 million dollars, consisting of disgorgement plus prejudgment interest in the amount of \$25 million and civil penalty of \$25 million. MSDW also made certain other undertakings including (1) preparing and distributing certain disclosures and a mutual fund bill of rights; (2) permitting certain class B shares to be converted to class A shares; and (3)



retaining an independent consultant to review, among other things, the completeness of the disclosures and conformity with other aspects of the order.

- In 2004, the NYSE brought an administrative action alleging that MS&Co. and MSDW (1) failed to ensure delivery of prospectuses in connection with certain sales of securities; (2) failed to timely and accurately file daily program trade reports; (3) erroneously executed certain sell orders on a minus tick for securities in which MS&Co. held a short position; (4) failed to timely submit RE-3 in connection with certain matters; (5) hired certain individuals subject to statutory disqualification and failed to file fingerprint cards for certain non-registered employees; (6) failed to comply with requirements concerning certain market-on-close and limit-on-close orders; and (7) failed to reasonably supervise certain activities. MS&Co. and MSDW resolved the action on January 7, 2005, by consenting, without admitting or denying guilt, to a censure, a fine of \$13 million, and a rescission offer to those clients who should have received a prospectus during the period from June 2003 to September 2004.
- In January 2005, the SEC filed a complaint in federal court alleging that, during 1999 and 2000, MS&Co. violated Regulation M by attempting to induce certain customers who received allocations of IPOs to place purchase orders for additional shares in the aftermarket. The SEC did not allege fraud or impact on the market. On January 25, 2005, MS&Co. agreed to the entry of a judgment enjoining MS&Co. from future violations and the payment of a \$40 million civil penalty. The settlement terms received court approval on February 4, 2005.
- In March 2005, the SEC entered an administrative and cease and desist order against CGM for two disclosure failures by CGM in offering and selling mutual fund shares. Firstly, CGM received from mutual fund advisers and distributors revenue sharing payments, in exchange for which CGM granted mutual funds preferential sales treatment. The order found that CGM did not adequately disclose its revenue sharing program to its clients, in violation of the Securities Act of 1933 (“Securities Act”) and Rule 10b-10 under the Securities Exchange Act of 1934 (“Exchange Act”). Secondly, on sales of Class B mutual fund shares in amounts aggregating \$50,000 or more, the order found that CGM, in violation of the Securities Act, failed to disclose adequately at the point of sale that such shares were subject to higher annual fees. These fees could have a negative impact on client investment returns, depending on the amount invested and the intended holding period. The SEC order censured CGM, required CGM to cease and desist from future violations of the applicable provisions, and required CGM to pay a \$20 million penalty.
- In March 2005, the NASD censured and fined CGM with respect to CGM’s offer and sale of Class B and Class C mutual fund shares during 2002 and the first six months of 2003. The NASD found that CGM either had not adequately disclosed at the point of sale, or had not adequately considered in connection with its recommendations to clients to purchase Class B and Class C shares, the differences in share classes and that an equal investment in Class A shares generally would have been more advantageous for the clients. The NASD also found that CGM’s supervisory and compliance policies and procedures regarding Class B and Class C shares had not been reasonably designed to ensure that SB Financial Consultants consistently provided adequate disclosure of, or consideration to, the benefits of the various mutual fund share classes as they applied to individual clients. The NASD censured CGM and required CGM to pay a \$6.25 million fine.
- 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 Advisors, 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.

The Form ADV Part 1 of VS contains further information about its disciplinary history, and is available on request.

## Item 10: Other Financial Industry Activities and Affiliations

Morgan Stanley Parent indirectly owns 51% of VS. Morgan Stanley Parent is a financial holding company under the Bank Holding Company Act of 1956. Citi indirectly owns 49% of VS. Both Morgan Stanley Parent and Citi are corporations whose shares are publicly held and traded on the New York Stock Exchange.

**Activities of Morgan Stanley Parent and Citi.** Morgan Stanley Parent and Citi are both global firms engaging, through their 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

VS has a related person that is registered as a broker-dealer (MSSB).

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

VS has a related person that is registered as futures commission merchant (MSSB) and a related person that is a commodity pool operator (Ceres Managed Futures LLC). 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 VS is affiliated with MSSB, MS&Co., Citi and their affiliates, the following restrictions apply when executing client trades:

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

These restrictions may adversely impact client account performance.

**Different Advice.** VS, MSSB, MS&Co., Citi and their 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 a VS client.

**Trading or Issuing Securities in, or Linked to Securities in, Client Accounts.** MSSB, MS&Co., CGM and their affiliates may provide bids and offers, and may act as principal market maker, in respect of the same securities held in client accounts. VS, MSSB, MS&Co., CGM and their respective affiliates and employees may hold a position (long or short) in the same securities held in client accounts. MSSB, MS&Co., CGM and/or their 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.** Affiliates of VS and other proprietary investment accounts may co-invest with the Funds in the Underlying Funds on a side-by-side basis from time to time. The Funds may, from time to time, compete with such other investors for access to potential Underlying Funds. VS and its affiliates will seek to fairly and equitably allocate, based on the particular facts and circumstances, such investment opportunities between or among the Fund(s) and its affiliates and other proprietary investment accounts. However, such allocation will not necessarily be made pro rata based on available assets. There can be no assurance that a particular investment opportunity which comes to the attention of VS's affiliates will be referred to VS and the Funds. In addition, affiliates of VS may participate in additional excess investment opportunities offered by the Underlying Funds. VS believes that it may not be advisable to dispose of interests in the Underlying Funds, securities received in an in kind distribution from an Underlying Fund or securities purchased in these additional opportunities in "lock step," given that the Fund, such affiliate and such affiliate's clients may have differing investment objectives, liquidity requirements and regulatory constraints. To the extent that any dispositions are not made in lock step, they will be made under principles designed to avoid potential or actual conflicts of interest.

In addition, members of the Investment Selection Committees and other employees of VS and its affiliates may invest directly in the Underlying Funds.

VS and its affiliates have adopted policies and procedures imposing certain conditions and restrictions on transactions for accounts of employees. Such policies and procedures are designed to prevent, among other things, any improper or abusive conduct when potential conflicts of interest may exist with respect to clients, including the Funds.

**Services Provided to Other Clients.** VS, MSSB, MS&Co., CGM, and their respective 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 VS may recommend for purchase or sale by clients or are otherwise held in client accounts. VS, MS&Co., CGM, MSSB, and their respective affiliates receive compensation and fees in connection with these services. VS 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 MS&Co., CGM, MSSB, investment managers and their affiliates or an affiliate performs investment banking or other services.

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

VS, MSSB and their affiliates may also develop analyses and/or evaluations of securities 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 VS will not disclose them to clients. VS may not be able to act, in respect of clients' account, on any such information, analyses or evaluations.

VS and its affiliates are not obligated to effect any transaction that VS or any of its affiliates believe would violate federal or state law, or the regulations of any regulatory or self-regulatory body.

**Conflicts Related to Citigroup and MS Research.** VS may receive and use investment research prepared by MS's, CGMI's and MSSB's respective research groups. It is possible that CGMI's research group, MSSB's research group, and MS's research group, may each reach different conclusions, and may make different recommendations, with respect to the same issuer or investment manager. This may, among other things, result in different investment decisions or recommendations regarding the same issuer or investment manager being made for or given to VS advisory clients.

CGMI, MSSB and MS do business with companies covered by their respective research groups. Furthermore, CGMI, MSSB and MS and their respective affiliates may hold a trading position (long or short) in, and client accounts may hold, the securities of companies subject to such research. Therefore, CGMI, MSSB and MS have a conflict of interest that could affect the objectivity of their research reports.

**Certain Trading Systems.** If MSSB directly or indirectly effects client trades through exchanges, electronic communication networks or other alternative trading systems ("Trading Systems") in which its affiliates have an ownership interest, these affiliates may receive an indirect economic benefit based on their ownership interest. Currently, affiliates of VS (including affiliates of MS&Co. and Citi) own over 5% of the voting securities of certain Trading Systems, including BATS Trading, Inc., operator of BATS Electronic Trading Network (commonly known as "BATS"); the entities that own and control the Block Interest Discovery System (commonly known as "BIDS"); LavaFlow Inc.; EBX Group, LLC; ELX Futures Holdings, LLC; ELX Futures, LP; TheMuniCenter; Automated Trading Desk Financial Services LLC; Automated Trading Desk Brokerage Services LLC; Boston Options Exchange, LLC; FX Alliance Inc.; and National Securities Exchange. Other Trading Systems on which MSSB may execute trades for client accounts include Archipelago; eSpeed; Instinet; NYFIX; Track ECN; BondDesk; ValuBond; NYSE Euronext; TradeWeb; and MarketAxe. The Trading Systems on which MSSB trades for Client accounts and in which affiliates of MSSB 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 affiliates of MSSB own interests and on which MSSB and/or MS&Co. trades 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 VS 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 VS 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) VS or one of its affiliates acting for its own proprietary accounts.

**Transaction-Related Agreements with MS&Co., Citi and Affiliates.** In connection with creating the joint venture, certain agreements were entered into between or involving some or all of MSSB, MS&Co, Citi, CGM and their affiliates, including the following:

- **Clearing.** An agreement providing that, subject to best execution, MS&Co. and CGM (or their applicable affiliates) will act as fully-disclosed clearing brokers for MSSB, which will act as an introducing broker. MSSB may have a conflict of interest in introducing client trades to MS&Co. and CGM. (As of the date of this brochure, MSSB is the clearing broker for most of the MS Channel's investment advisory programs. MS&Co. is the clearing broker for some investment advisory programs offered by the MS Channel's Private Wealth Management division. CGM is the clearing broker for SB Channel clients.)
- **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., Citi, CGM and their 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., Citi or their 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.
- **Investment Research.** An agreement that MS&Co. and CGM (or their applicable affiliates) will supply investment research prepared by their respective research groups to MSSB for its use. It is possible that MS&Co.'s research group, on the one hand, and Citi's research group, on the other hand, may reach different conclusions, and may make different recommendations, with respect to the same issuer or investment manager. This may, among other things, result in different investment decisions or recommendations regarding the same issuer or investment manager being made for or given to MSSB investment advisory clients.

**Related Investment Advisors and Other Service Providers.** VS has related persons that are registered investment advisers in various investment advisory programs (including Morgan Stanley Investment Management Inc., Morgan Stanley Investment Advisors Inc. and Morgan Stanley Investment Management Limited). If a Fund invests its assets and uses an affiliated firm to manage its account, VS and its affiliates earn more money than if a Fund uses an unaffiliated firm.

Morgan Stanley Investment Advisors Inc., its wholly owned subsidiary Morgan Stanley Services Company Inc., and Morgan Stanley Investment Management 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 Distributors Inc. serves as distributor for these open-end investment companies, and has entered into selected dealer agreements with MSSB and affiliates. Morgan Stanley Distributors 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 Trust FSB, an affiliate of VS, serves as transfer agent and dividend disbursing agent for investment companies advised by Morgan Stanley Investment Advisors 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 VS 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 VS.

As noted above, the Underlying Funds in which the Funds invest are selected by VS through the respective Investment Selection Committees, the members of which are drawn from certain investment resources of VS's affiliates (see response to Item 4).

VS also may share resources, employees and management, as well as investment ideas and opportunities, with affiliated investment advisers engaged in similar activities.

CGMI and MSSB, which are affiliates of VS, may serve as placement agents with respect to interests in the Funds.

As noted above, pursuant to the Administration Agreement, Stepstone may perform some of the services for the Funds described as being performed by VS in this Form ADV (see response to Items 1.D and 2.G).

Certain affiliates of VS may invest directly in an Underlying Fund on a side-by-side basis with a Fund. Such investment may benefit the Fund by providing access to an Underlying Fund and by allowing the Fund to leverage off of VS's affiliates' expertise in evaluating and negotiating an investment in the Underlying Fund. It also may give rise to potential conflicts of interest (see response to Item 9).

If a designated Underlying Fund holds its closing prior to the initial closing of a Fund, an affiliate of VS may make a commitment to the designated Underlying Fund on behalf of such Fund. Under such circumstances, the affiliate of VS subsequent to the initial closing of the Fund will transfer the interest so acquired to the Fund in exchange for payment by the Fund to such affiliate of VS of the amounts funded by such affiliate of VS plus interest. Prior to the initial closing of a Fund, a Fund may also purchase interests directly in an Underlying Fund. In order to make such a purchase, the Fund may borrow money from VS or an affiliate. VS or its affiliate will charge the Fund interest on such a loan. In order to lend money to the Fund, VS or its affiliate may borrow money at a lower interest rate than that charged to the Fund. By executing the subscription agreement to invest in a Fund, each investor consents to such transfer or purchase of interests and to the Fund's payment of a stated rate of interest.

As noted above in the response to Item 1, VS serves as the investment adviser of several investment partnerships organized by CGMI (or its predecessors) and other members of Citigroup to offer qualified investors the opportunity to invest in private equity investment "fund of funds."

#### **D. Material Conflicts of Interest**

**General.** Potential conflicts of interest are fully disclosed in each Fund's Confidential Private Offering Memorandum. Each Fund's Confidential Private Offering Memorandum provides that by acquiring an interest in the Fund, each investor will be deemed to have acknowledged the existence of any such actual and potential conflicts of interest and to have waived any claim with respect to any liability arising from the existence of any such conflict of interest.

On any issue involving actual conflicts of interest, VS will be guided by its good faith judgment as to a Fund's best interests. In the event that any matter arises that VS determines in its good faith judgment constitutes an actual conflict of interest between the Fund and VS's affiliates, under the Fund's applicable agreements VS may refer the matter to the Investment Selection Committee for resolution. VS may also take such other actions as it may deem necessary or appropriate to ameliorate the conflict. These actions may include disposing of the security held by the Fund giving rise to the conflict of interest, or appointing an independent fiduciary.

VS's affiliates, including CGMI, Citigroup, MS and MSSB, engage or may engage in a broad spectrum of activities, including financial advisory activities, and have extensive investment activities that are independent from, and may from time to time conflict with, those of the Funds or the Underlying Funds. In the future, there might arise instances where the interests of such affiliates conflict with the interests of the Underlying Funds and their investors, including the Funds. Certain affiliates of VS will engage in transactions with, and may provide services to, portfolio companies and potential portfolio companies of the Underlying Funds. Certain affiliates, including CGMI and MS, engage in activities in the normal course of their investment banking businesses which may conflict with the interests of a Fund's investors. Certain affiliates of VS may provide services to, invest in, advise, sponsor and/or act as investment manager to investment vehicles and other persons or entities (including prospective investors in the Underlying Funds) which may have similar structures and investment objectives and policies to those of the Underlying Funds and which may compete with the Underlying Funds for investment opportunities and which may co-invest with the Underlying Funds in certain transactions. In addition, certain affiliates of VS and their respective clients may themselves invest in securities that would be appropriate for the Underlying Funds and may compete with the Underlying Funds for investment opportunities.

There can be no assurance that an investment opportunity which comes to the attention of VS's affiliates will be appropriate for the Underlying Funds or will be referred to the Underlying Funds. None of such affiliates (including CGMI, MS and MSSB) is obligated to refer any investment opportunity to the Underlying Funds.

***Conflicting Client Relationships.*** Certain of VS's affiliates have pre-existing relationships with a significant number of corporations which may be potential portfolio companies of the Underlying Funds. VS may take into consideration these relationships in its management of a Fund, and the Underlying Funds may also take these relationships into consideration. For instance, there may be certain investments that VS will not undertake on behalf of the Fund in view of such relationships.

***Inside Information.*** From time to time, certain of VS's affiliates may come into possession of inside information concerning specific companies, although internal information barrier structures are in place to prevent such exchanges of information. Under applicable securities laws this may limit the flexibility of an Affiliated Underlying Fund to buy or sell portfolio securities issued by such company. A Fund's investment flexibility may be constrained as a consequence of VS's inability to use such information for investment purposes.

***Investment Banking Relationships.*** Certain of VS's affiliates may receive investment banking fees from portfolio companies and other parties engaged in transactions in which the Underlying Funds invest. Such fees would be paid to such affiliates for providing services in connection with: (i) the acquisition, disposition or sale of companies in which the Underlying Funds invest; (ii) equity or debt financings; or (iii) other investment banking services. The arrangement between such affiliates and such parties will be made on an arm's length basis consistent with industry practices.

***Conflicting Representations of Buyers.*** Certain of VS's affiliates may represent potential buyers of businesses through their merger and acquisition activities. When such an affiliate represents a buyer seeking to acquire a company, an Affiliated Underlying Fund will be limited or precluded during the pendency of such assignment from investing in or selling securities issued by such company.

***Conflicting Representations of Sellers.*** In the regular course of business, certain of VS's affiliates may be engaged to act as financial adviser to a company in connection with the sale of such company, or subsidiaries or divisions thereof. The compensation provided to such affiliates for such activities will be typically based upon realized consideration and is expected to be contingent, in substantial part, upon closing. Such affiliates may be precluded from offering such company to any Affiliated Underlying Funds if the seller has required such affiliates to act exclusively on its behalf. Additionally, there may be seller assignments in which the seller permits the Underlying Funds to act as a buyer. If an Affiliated Underlying Fund were to be that buyer, certain conflicts of interest would be inherent in the situation, including those involved in negotiation of a purchase price.

***Restructuring Activities.*** Certain of VS's affiliates may be engaged to act as financial adviser to financially troubled companies in connection with the restructuring of their capital structures or in connection with their bankruptcy. The compensation provided to such affiliates for such activities is generally based upon the successful completion of a restructuring, which may include raising funds for the purchase of existing securities or for an equity infusion. If any Affiliated Underlying Funds were investors in such a company, certain conflicts of interest would be inherent in the situation, including those involved in negotiation of a purchase price.

***Principal Investments.*** There may be situations in which the interests of a Fund or one or more of the Underlying Funds in a portfolio company may conflict with the interests of one or more general accounts of VS's affiliates or accounts managed by such affiliates. This may occur because these accounts hold public and private debt and equity securities of a large number of issuers that



may be or become portfolio companies, or from whom portfolio companies may be acquired. VS believes that the participation of its affiliates in the capital markets is a significant factor in ensuring its continuing access to Underlying Funds for investment by the Fund, and this participation is believed by VS to be, on balance, beneficial to the Funds.

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

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

VS has adopted a Code of Ethics that memorializes VS's fundamental duties as a fiduciary. The Code of Ethics includes standards of business conduct and incorporates a personal investments policy. Each employee receives a copy of the Code of Ethics upon hiring and annually thereafter and must sign an attestation that such employee has read and understood such Code of Ethics.

VS's Code of Ethics requires each employee to prioritize the interests of the client, to avoid conflicts of interest, to never abuse such employee's position of trust and responsibility and to comply with all federal securities laws. Employees are required to safeguard material non-public information in such employee's possession and are prohibited from using such information to such employee's personal benefit. Each employee must treat information belonging to clients as confidential and take care to protect such information from unauthorized access by third parties.

To avoid any potential conflict of interest involving personal transactions, VS requires each employee to notify the Compliance Officer upon opening a personal account, to pre-clear personal transactions and disclose all potential conflicts of interest with regard to such a personal transaction before engaging in the transaction. Employees are also subject to a restricted list and blackout periods. In addition, access persons (defined as employees with access to non-public information regarding VS's purchase or sale of securities and directors, officers and partners) will (i) upon starting employment, provide a complete record of his or her securities holdings to the Compliance Officer and annually thereafter and (ii) provide quarterly reports of personal securities transactions within 30 days following the end of the quarter, unless such information has been provided through other means. All employees are required to inform the Compliance Officer of any violation of the Code of Ethics that comes to his or her notice.

A copy of VS's Code of Ethics will be provided to any client or prospective client upon request.

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

### **C. Investing in Securities That You or a Related Person Recommends to Clients or has a Financial Interest**

Please see Item 10C for a discussion regarding the following items:

- *Trading or Issuing Securities in, or Linked to Securities in, Client Accounts.*
- *Restrictions on Securities Transactions.*
- *Research Reports.*
- *Conflicts Related to Citigroup and MS Research.*
- *Transaction-Related Agreements with MS&Co., Citi and Affiliates.*

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

Please see the paragraph entitled "*Different Advice*" located in Item 10C.

## **Item 12: Brokerage Practices**

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

Funds generally invest directly in an Underlying Fund, and VS will not utilize or pay any broker or dealer in connection with an investment in an Underlying Fund, although affiliates of VS may be compensated by an Underlying Fund and the manager thereof for placing assets in the Underlying Fund and for other reasons.

VS may utilize the services of a broker or dealer, including affiliates of VS, in investing in Temporary Investments or in selling securities received from an Underlying Fund in an in kind distribution. In selecting brokers or dealers to execute transactions on behalf of the Fund, VS will consider factors it deems relevant, including, but not limited to, the breadth of the market in the security, the price of the security, the financial condition and execution capability of the broker or dealer and the reasonableness of the commission, if any, for the specific transaction and on a continuing basis.

#### 1. Research and Other Soft Dollars

VS generally is authorized, under the terms of its Investment Advisory Agreement with each Fund, to consider the brokerage and research services provided to the Fund and/or other accounts over which VS or its affiliates exercise investment discretion. However, VS does not currently have any “soft dollar” arrangements pursuant to which products, research and services are given to VS or an affiliate by brokers in return for effecting Fund transactions through such brokers.

#### 2. Brokerage for Client Referrals

VS does not consider whether it or an affiliate will receive client referrals from a broker-dealer or third party when selecting or recommending broker-dealers.

#### 3. Directed Brokerage

VS does not offer Funds directed brokerage as an option to pay their investment advisory fees.

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

VS does not aggregate the purchase or sale of securities for the Funds.

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

Please see the response to Item 4 for a description of the monitoring and review of the Fund's investments in Underlying Funds.

VS's clients are the Funds, and not the Funds' underlying investors. VS will provide each Fund's general partner with periodic reports concerning the Fund's investment in Underlying Funds and Temporary Investments.

While the Funds' underlying investors are not advisory clients of VS and will not receive reports from VS as advisory clients, such investors will be provided by the Funds with annual audited financial statements of the applicable Fund and periodic investor reports.

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

CGMI and MSSB, which are affiliates of VS, may act as placement agents with respect to interests in the Funds. VS may pay a fee, out of its own resources, to placement agents responsible for subscriptions to the Funds. The placement agents will pay a portion of such placement agent fees to CGMI and MSSB Financial Advisors and other placement agent representatives whose clients purchase interests in the Fund. The placement agents may engage, and pay (to the extent permitted under applicable state and federal law) subplacement or finder's fees to, other financial institutions to assist them in placing interests in the Funds.

## **Item 15: Custody**

VS's clients are the Funds, and not the Funds' underlying investors and VS does not act as custodian to the Funds. VS will provide each Fund's general partner with periodic reports concerning the Fund's investment in Underlying Funds and Temporary Investments.

While the Funds' underlying investors are not advisory clients of VS and will not receive reports from VS as advisory clients, the Funds will provide such investors with annual audited financial statements of the applicable Fund and periodic investor reports.

## **Item 16: Investment Discretion**

VS has the authority to determine, without obtaining specific client consent, the Underlying Funds and the Temporary Investments (see response to item 1 above) in which a Fund will invest, subject in each case to the limitations and restrictions described in the Fund's Confidential Private Offering Memorandum and governing documents. A Fund may receive distributions from an Underlying Fund in kind in the form of marketable securities of portfolio companies, some of which may be restricted securities. With respect to such distributions, VS has the discretion to sell such securities and distribute the cash proceeds, distribute such securities in kind or offer the Fund's investors the option, subject to VS's consent, either to receive the securities in kind or to have the Fund sell them and distribute the cash proceeds. While VS will use reasonable efforts either to sell or to distribute marketable securities promptly, a Fund's investors will bear any associated costs or market risks during the disposition process. Affiliates of VS and other proprietary investment accounts may co-invest with the Funds in the Underlying Funds on a side-by-side basis from time to time. The Funds may, from time to time, compete with such other investors for access to potential Underlying Funds. VS and its affiliates will seek to fairly and equitably allocate, based on the particular facts and circumstances, such investment opportunities between or among the Fund(s) and its affiliates and other proprietary investment accounts. However, such allocation will not necessarily be made pro rata based on available assets. There can be no assurance that a particular investment opportunity which comes to the attention of VS's affiliates will be referred to VS and the Funds.

In the event that two or more Funds advised by VS and/or funds advised by its affiliate, PM, have cash available for investment at the same time and an investment opportunity arises that may be appropriate for each such fund but whose availability to VS and its affiliate is limited, VS and its affiliate will seek to fairly and equitably allocate such investment opportunity between or among such funds taking into account such factors as each fund's investment objective, industry and sector focus, size and available cash. Consideration may also be given to whether one of the advisers was primarily responsible for gaining access to the investment opportunity.

Funds generally invest directly in an Underlying Fund, and VS will not utilize or pay any broker or dealer in connection with an investment in an Underlying Fund, although affiliates of VS may be compensated by an Underlying Fund and the manager thereof for placing assets in the Underlying Fund and for other reasons.

VS may utilize the services of a broker or dealer, including affiliates of VS, in investing in Temporary Investments or in selling securities received from an Underlying Fund in an in kind distribution. In selecting brokers or dealers to execute transactions on behalf of the Fund, VS will consider factors it deems relevant, including, but not limited to, the breadth of the market in the security, the price of the security, the financial condition and execution capability of the broker or dealer and the reasonableness of the commission, if any, for the specific transaction and on a continuing basis. VS generally is authorized, under the terms of its Investment Advisory Agreement with each Fund, to consider the brokerage and research services provided to the Fund and/or other accounts over which VS or its affiliates exercise investment discretion. However, VS does not currently have any "soft dollar" arrangements pursuant to which products, research and services are given to VS or an affiliate by brokers in return for effecting Fund transactions through such brokers.

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

VS does not accept proxy-voting authority on behalf of the Funds and their investments in the Underlying Funds. Funds may elect VS to vote proxies or they may vote on their own and VS will send the proxy materials to the Funds. Funds may contact VS with questions about a particular solicitation.

## **Item 18: Financial Information**

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

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

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

## **Item 19: Requirements for State-Registered Adviser**

This item is not applicable to VS.