

# Talbot Financial, LLC

## Form ADV Part 2A Brochure

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Date of this Brochure: March 25, 2020

Last Annual Updating Amendment: February 14, 2019

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

This Form ADV Part 2A brochure provides information about the qualifications and business practices of Talbot Financial, LLC. If you have any questions about the contents of this brochure, please contact us at 425-533-0797 ([Jim.Pirak@talbotfinancial.com](mailto:Jim.Pirak@talbotfinancial.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 Talbot Financial, LLC also is available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). Talbot Financial, LLC is a registered investment advisor. Registration as an investment advisor does not imply any certain level of skill or training.

## **Material Changes (Item 2)**

*This section of the brochure helps you quickly identify material changes from the last annual update.*

This section of our brochure is used to identify material changes since our last annual updating amendment. Since the last update in February of 2019, we have made the following material changes:

In Item 4, Item 6, and Item 10, we have provided information about the real estate investments managed by our majority owner and which some Talbot Financial clients invest in. We have also described in Item 15 the surprise examination requirements we are subject to in connection with these real estate investments.

We have added some additional information to Item 5 and Item 6 about our fees and specifically about the assets we do *not* charge advisory fees on. We have also clarified the difference between the fees charged by Talbot Financial and the real estate investments discussed above.

We have also made a number of updates throughout this brochure to improve clarity and more closely conform our responses to the ADV instructions. We encourage you to read the entire brochure and to let us know if you have any questions.

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## **Advisory Business (Item 4)**

*This section of the brochure tells you about our business, including ownership, and a description of the services we offer.*

Talbot Financial, LLC is referred to in this document as “Talbot Financial,” “the Company,” “us,” “we,” or “our.” In this document we refer to current and prospective clients of Talbot Financial as “you,” “client,” or “your.” Talbot Financial was created in 2010 and is primarily owned by its principals, Randall Talbot, and James Pirak.

### **Types of Advisory Services**

#### Investment Supervisory Services

Our clients enter into a written Investment Advisory Agreement, where Talbot Financial and our investment adviser representatives provide asset management services on a continuous and ongoing basis guided by the individual needs of the client. Using the information provided by you, the investment advice provided to you is tailored to your individual situation. We regularly inquire about, and you are responsible for providing, information about your investment goals, time horizon, and risk tolerance. These investment supervisory services are generally not provided to all your holdings or net worth but rather only to assets specifically designated by you and agreed to by us as managed assets.

### **Types of Investments Used**

We consider different types of securities when formulating the investment advice we give to you. We are not restricted in the types of investments we can select for clients, but for the most part we employ individual stocks in building client portfolios. We do not typically manage bonds or fixed income investments. If you come to us with existing investments, we evaluate them with respect to your financial goals, risk tolerance, and investment time horizon.

We also frequently recommend that real estate be part of client holdings. Our majority owner sources commercial real estate opportunities, forms special purpose vehicles (“SPV”) to invest in real estate, and serves as the managing member of these SPVs. Opportunities to invest in the SPVs are made available to our client base in a single communication and investments are permitted on a first-come, first served basis, and in the sole judgment of the SPV’s managing member. The SPVs are unregistered and are available only to accredited investors, as defined under Rule 501 of Regulation D. Investors must also be “qualified clients,” as defined in SEC Rule 205-3 under the Investment Advisers Act of 1940. These SPVs are not liquid and clients who choose to invest in them should assume they will hold them for the long-term. We cannot use our discretionary authority to invest in the SPVs on behalf of our clients. All investors receive offering materials and subscription agreements (collectively, the “Offering Materials”) from the SPV’s managing member, who ultimately decides whether an investor is qualified and whether the investor’s subscription will be accepted. See Item 6 and Item 10, below, for more information.

## Tailored Services and Investment Restrictions

We attempt to tailor your investment portfolio to your situation as you have described it to us. This is why it is so important that you let us know about changes to your financial situation, goals, or investment time horizon. You may impose restrictions on investing in certain securities or types of securities, as long as we believe the operational requirements of the restriction are operationally manageable, and as long we believe the restriction is consistent with our fiduciary duty to you. You must clearly identify any restrictions in writing to us and we must accept them.

## Assets Under Management

As of December 31, 2019, Talbot Financial managed approximately \$321,277,000 on a discretionary basis and approximately \$198,500 on a non-discretionary basis.

## Fees and Compensation (Item 5)

*This section of the brochure describes how we are compensated for the services we offer.*

### Compensation Methodology and Rates

Clients are charged for our asset management services based on a percentage of the assets being managed.

<u>Assets Under Management</u>	<u>Annual Fees</u>
• Equities & Fixed Income	
○ Up to \$30,000,000	0.85%
○ Over \$30,000,000	0.50%
• Cash	0.00%

The firm will, on occasion, choose to charge 0% on some assets due to special situations such as holding restricted stocks for a client. Because we charge no advisory fees on cash but have discretionary authority to manage your allocations to cash, we have a conflict of interest as a result of choosing not to charge on cash. This is because we have a financial incentive to keep you fully invested and to retain as little cash as possible. In general, we advise to keep cash balances needed for ongoing liquidity requirements in accounts outside of our management.

Your specific annual fee arrangement will be described in the written Investment Advisory Agreement entered into between Talbot Financial and you. Investment advisory fees charged by us are negotiable at our sole discretion. All clients do not pay the same fee. The annual fee for our services is billed monthly, in arrears, based on the value of the account at the end of the month. If the management agreement does not span the entire monthly billing period, the fee will be pro-rated based on the number of days the account is open during the billing period. Your account custodian will send client statements, at least

quarterly, showing all disbursements for the account including the amount of the advisory fee, if deducted directly from the account. It is the shared responsibility of Talbot Financial and you to verify the accuracy of the fee calculation as the account custodian will not determine whether the fee has been properly calculated. See Brokerage Practices (Item 12) in this brochure for more information about your account custodian(s).

You may terminate the Investment Advisory Agreement without fee or penalty by providing written notice to Talbot Financial within five (5) business days from the execution of the agreement. Thereafter, either party may terminate the Investment Advisory Agreement by providing written notice.

#### Valuation of Publicly Traded Securities

Publicly traded securities in your account(s) managed by us are held at the custodian that we recommend but is ultimately chosen by you. We use the securities valuation provided by the independent qualified custodian for reporting and billing purposes. Publicly traded securities are usually valued as of the end of business on the last trading day of the calendar quarter. The custodian's valuation policies are typically distributed on account statements.

#### **How Clients Pay Advisory Fees**

Fees are generally deducted directly from your account. You may provide your qualified account custodian with written authorization to have fees deducted from the account and paid to Talbot Financial. This authority is also found in the Investment Advisory Agreement.

#### **Other Types of Fees and Expenses**

In addition to the investment advisory fees you pay to us, you will pay transaction fees (commissions) to your custodian or broker-dealer for executing securities transactions and charges for special services elected by you or Talbot Financial. These fees may include:

- periodic distribution fees
- electronic fund and wire transfer fees
- certificate delivery fees
- reorganization fees
- account transfer fees (outbound)
- returned check fees
- international security transfer fees
- overnight mail and check fees
- Rule 144 transfer fees
- transfer agent fees

This list is not meant to be all inclusive. Any fee on a special service incurred by the client will be fully disclosed. Please refer to Item 12 of this document for an explanation of our brokerage practices.

### Investment Company Fees

Investment company funds (e.g., mutual funds or ETFs) that are held by you will bear their own internal transaction and execution costs, as well as directly compensate their investment managers along with internal administrative services. These fees reduce the net asset value of the fund shares and are indirectly borne by fund shareholders. As described in Item 4, above, we typically use individual stocks, rather than funds in client portfolios. If you transfer assets to our management, we will evaluate whether to hold or sell those assets. We typically liquidate high-expense funds, including those that pay a 12b-1 fee or similar trailing commissions. If we believe that the client will incur significant tax liability or excessive redemption fees, or that the sale is otherwise not in the client's best interest, we will continue to hold the security. In no case, however, does Talbot Financial share in the continuing commissions or otherwise receive transaction-based compensation.

### **Commission Based Compensation**

Neither the firm nor its advisory representatives receive any commissions or transaction-based compensation.

### **Performance-Based Fees and Side-By-Side Management (Item 6)**

*This section of the brochure explains any performance-based fees we may charge you for and how they may be different from other clients' charges.*

Talbot Financial does not charge fees that are based upon a share of capital gains or capital appreciation of client assets (performance-based fees).

As discussed in Item 4, our majority owner, Randy Talbot, also serves as the managing member for real estate SPVs, typically through entities he controls (and in some cases owns with Talbot Financial's other owner and manager, James Pirak) that are formed for the purpose of managing the SPV. While the SPVs are responsible for certain limited expenses described in the offering documents, there are no ongoing management fees charged against the SPVs and Talbot Financial does not charge any advisory fees on these assets. Talbot Financial's own managers do invest in these SPVs personally, consistent with the company's belief in investing alongside clients.

Terms vary but generally the managing member of the SPV is entitled to carried interest, which represents a share of the SPV's profits. Carried interest is considered a type of performance fee. Details on the carried interest are provided to investors as part of the Offering Materials. Because the managing members of the SPVs are also owners and control persons of Talbot Financial, we have a conflict in recommending that clients invest in these SPVs rather than in real estate investments that are not affiliated with our company. We cannot use our discretionary authority to invest in these on behalf of clients and all investors must receive specific disclosures and complete subscription agreements for each SPV. Mr. Talbot does not manage the equity portfolios of Talbot Financial clients. Similarly, Mr. Pirak is focused on Talbot Financial and not on the day-to-day management of the SPVs.



This limits the ongoing conflict raised by the time and attention needed to run different businesses and the conflict in managing assets that pay a performance fee versus those that do not.

We provide investment advisory services to other clients in addition to you. Not all clients receive the same investment advice, nor do they pay the same fee. We strive to act in the best interests of each of our clients at all times.

## **Types of Clients (Item 7)**

*This section of the brochure describes who we generally provide our services to.*

We provide advisory services to a variety of types of clients including individuals, trusts, individual's pension plan accounts, and retirement plan trustees.

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

*This section of the brochure explains how we formulate our investment advice and manage client assets.*

### **Methods of Analysis**

#### Value Investing

As part of our analysis of investments we currently use a value-oriented method that emphasizes the strength of a company's balance sheet, income statement and statement of cash flows. Factors such as P/E ratio, dividend yield, top and bottom line growth, free cash flow, and strength of the management team are all part of the evaluation process. Talbot Financial does not invest in accordance with a specific asset allocation model, but rather has adopted a value-style investment philosophy that is reflected in the great majority of client portfolios. We attempt to do this by carefully choosing the proportions of various "value" assets in an investment portfolio. Client portfolios that do not reflect this philosophy are a result of the client's expressed wishes to invest in a different manner. We analyze an investment by examining its publicly available financial statements or reports, its management, competitive advantages, competitors, and markets. We attempt to identify investments that are selling for less than their intrinsic worth. Our fundamental analysis method is based upon the assumption that markets may misprice an investment in the short run but that the "correct" price will eventually be reached. A risk of this is that we may be wrong in our assumptions and that the market will never agree with our view of intrinsic worth. We might not be diversified by asset class. Some positions could be concentrated (as defined as a position greater than 5% of the overall portfolio.)

### **Investment Strategies**

We attempt to adjust our asset allocation advice to over-weight or focus on an asset class or sector of the market that we feel will perform better than others. We strive to buy

investments with the goal of holding them as long-term investments, but we might choose to sell a particular investment if, in our opinion, it is no longer in your best interest to hold.

## **Risks**

### General Risks to Investing

Investing is not without risk, and involves the risk of loss of principal which you should be prepared to bear. We use several strategies to try to reduce risk, including diversifying a portfolio across sectors and monitoring the portfolio for changes in fundamentals.

Despite these strategies, historical evidence clearly shows that every asset class has experienced severe declines in value—sometimes sustained over many years—throughout several periods of time in history. In addition, each of our strategies to minimize risk may not achieve that goal as the benefits of diversification decline if asset classes become more correlated. As with any investment, you could lose all or part of your investments managed by Talbot Financial, and your account's performance could trail that of other investments.

### Asset Class Risk

Securities in your portfolio(s) may underperform in comparison to the general securities markets or other asset classes.

### Concentration Risk

To the extent that we recommend portfolio allocations that are concentrated in a particular market, industry or asset class, your portfolio may be susceptible to loss due to adverse occurrences affecting that market, industry, or asset class.

### Equity Securities Risk

Equity securities are subject to changes in value that may be attributable to market perception of a particular issuer or general stock market fluctuations that affect all issuers. Investments in equity securities may be more volatile than other types of investments.

### Growth Securities Risk

Growth companies are companies whose earnings growth potential appears to be greater than the market, in general, and whose revenue growth is expected to continue over an extended period. Stocks of growth companies or "growth securities" have market values that may be more volatile than those of other types of investments. Growth securities typically do not pay a dividend.

### Issuer Risk

Your account's performance depends on the performance of individual securities in which your account invests. Any issuer may perform poorly, causing the value of its securities to decline. Poor performance may be caused by poor management decisions, competitive pressures, changes in technology, disruptions in supply, labor problems or shortages, corporate restructurings, fraudulent disclosures, or other factors. Changes to the financial condition or credit rating of an issuer of those securities may cause the value of the securities to decline.

### Management Risk

The performance of your account is subject to the risk that our investment management strategy may not produce the intended results.

### Market Risk

Your account could lose money over short periods due to short-term market movements and over longer periods during market downturns. The value of a security may decline due to general market conditions, economic trends, or events that are not specifically related to the issuer of the security or to factors that affect a particular industry or industries. During a general downturn in the securities markets, multiple asset classes may be negatively affected.

### Market Trading Risks

Your investment account faces numerous market trading risks, including the potential lack of an active market for investments held in your account and losses from trading in secondary markets.

### Passive Investment Risk

Talbot Financial may use a passive investment strategy that is not actively managed where we do not attempt to take defensive positions in declining markets.

### Larger Company Securities Risk

Securities of companies with larger market capitalizations may underperform securities of companies with smaller and mid-sized market capitalizations in certain economic environments. Larger, more established companies might be unable to react as quickly to new competitive challenges, such as changes in technology and consumer tastes. Some larger companies may be unable to grow at rates higher than the fastest growing smaller companies, especially during extended periods of economic expansion.

### Leverage Risk

Certain transactions may give rise to a form of leveraging, including borrowing. Such transactions may include, among others, reverse repurchase agreements, loans of portfolio securities, and the use of when-issued, delayed-delivery, or forward-commitment transactions. The use of derivatives may also create leverage. Clients may have access to margin loans against their portfolios through their custodial accounts, which is also a form of leverage and subject to the attendant risks. The use of leverage may cause a portfolio to liquidate portfolio positions when it may not be advantageous to do so. Leveraging may make a portfolio more volatile than if the portfolio had not been leveraged. This is because leverage tends to increase a portfolio's exposure to market risk, interest rate risk, or other risks by increasing assets available for investment. Talbot Financial does not generally use leverage in its discretionary management or recommend the use of margin to clients.

### Liquidity Risk

Liquidity is the ability to readily convert an investment into cash. Generally, assets are more liquid if many traders are interested in a standardized product. For example, Treasury Bills are highly liquid, while real estate properties are not. Certain instruments may have no readily available market or third-party pricing. Private placements, for example, have

virtually no secondary market. Reduced liquidity may have an adverse impact on market price and the ability to sell particular securities when necessary to meet cash needs or in response to a specific economic event, such as the deterioration of creditworthiness of an issuer. Reduced liquidity in the secondary market for certain securities may also make it more difficult to obtain market quotations based on actual trades for the purpose of valuing the security. Clients should invest in illiquid (or relatively illiquid) assets only to the extent they have adequate other liquid assets available to fund current and ongoing cash requirements.

#### Real Estate Risk

We may recommend securities that hold real estate or are focused on the real estate industry. Risks associated with real estate generally include: local, national and international economic conditions; the supply and demand for properties; the financial conditions for tenants, buyers and sellers of properties; changes in interest rates; changes in environmental laws or regulations, planning laws and other governmental roles and fiscal and monetary policies; changes in real property tax rates; negative developments in the economy that depress travel and retail activity; uninsured casualties; force majeure acts, terrorist events, under-insured or uninsurable losses; and other factors that are beyond the reasonable control of the Manager. Other risks include, but are not limited to, tenant vacancies; declining market values; potential loss of entire investment principal; that potential cash flow, potential returns, and potential appreciation are not guaranteed in any way; adverse tax consequences; and that real estate is typically an illiquid investment. In addition, real estate assets are subject to long-term cyclical trends that give rise to significant volatility in values. Investment is disproportionately exposed to the foregoing risks because of its concentration in real estate and real estate-related investments.

#### Regulatory Risk

Changes in government regulations may adversely affect the value of a security. An insufficiently regulated industry or market might also permit inappropriate practices that adversely affect an investment.

#### Smaller Company Securities Risk

Securities of companies with smaller market capitalizations, historically, tend to be more volatile and less liquid than larger company stocks. Smaller companies may have no or relatively short operating histories, or be newly public companies. Some of these companies have aggressive capital structures, including high debt levels, or are involved in rapidly growing or changing industries, or new technologies, which pose additional risks.

#### Value Style Investment Risk

Value stocks can perform differently from the market as a whole and from other types of stocks. Value stocks may be purchased based upon the belief that a given security may be out of favor. Value investing seeks to identify stocks that have depressed valuations, based upon a number of factors which are thought to be temporary in nature, and to sell them at superior profits when their prices rise when the issues which caused the valuation of the stock to be depressed are resolved. While certain value stocks may increase in value more quickly during periods of anticipated economic upturn, they may also lose value more

quickly in periods of anticipated economic downturn. Furthermore, there is a risk that the factors which caused the depressed valuations are longer term or even permanent in nature, and that there will not be any rise in value. Our assumptions about the company's worth may be inaccurate and the market may never agree with our valuation—what is out of favor today may well continue to be out of favor in the future. Finally, there is the increased risk that such companies may not have sufficient resources to continue as ongoing businesses, which may result in the stock of such companies becoming worthless.

#### Key Man Risk

We are a small firm with James Pirak performing several key functions. This fact leads to “key man risk,” or the risk that we would not be able to manage your portfolios as we have in the past without Mr. Pirak's involvement, including the benefit of his experience and judgment. We now have an additional adviser on the firm's team and believe this helps mitigate some of the key man risk.

### **Disciplinary Information (Item 9)**

*This section of the brochure lists legal and disciplinary information for Talbot Financial, its owners, and management team.*

Investment advisers are required to disclose certain regulatory and legal events. Neither Talbot Financial nor any of our owners or management team members has anything to disclose in response to this item.

### **Other Financial Industry Activities and Affiliations (Item 10)**

*This section of the brochure describes other financial services industry affiliations we may have that could present a conflict of interest with you.*

As disclosed in Item 4 and Item 6, above, our majority owner, Randy Talbot, also serves as the managing member for real estate SPVs, typically through entities he controls (and in some cases owns with Talbot Financial's other owner and manager, James Pirak) that are formed for the purpose of managing the SPV. There are no ongoing management fees charged against the SPVs and Talbot Financial does not charge any advisory fees on these assets. Talbot Financial's own managers do invest in these SPVs personally, consistent with the company's belief in investing alongside clients. Terms vary but generally the managing member of the SPV is entitled to carried interest, which represents a share of the SPV's profits (see Item 6 for more information). Because the managing members of the SPVs are also owners and control persons of Talbot Financial, we have a conflict in recommending that clients invest in these SPVs rather than in real estate investments that are not affiliated with our company.

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

*This section of the brochure describes our code of ethics, adopted pursuant to SEC rule 204A-1, and how we deal with client and related person trading.*

### **Code of Ethics**

We have adopted a code of ethics designed to prevent and detect violations of securities rules by our employees and affiliated persons. Our controls in this area focus upon securities transactions made by our employees that have access to material information about the trading of Talbot Financial. We will provide a copy of our code of ethics to clients or prospective clients upon request.

### **Material Financial Interest and Personal Trading**

From time-to-time the interests of the principals and employees of Talbot Financial may coincide with yours and other clients. Individual securities may be bought, held, or sold by a principal or employee of Talbot Financial that is also recommended to or held by you or another client. If potential insider information is inadvertently provided or learned by a principal or employee, it is our policy to strictly prohibit its use.

It is the policy of Talbot Financial to permit the firm, its employees and investment advisor representatives ("IARs") to buy, sell, and hold the same securities that the IARs also recommend to clients. It is acknowledged and understood that we perform investment services for different types of clients with varying investment goals, risk profiles, and time horizons. As such, the investment advice offered to you may differ from other clients and investments made by our IARs. We have no obligation to recommend for purchase or sale a security that Talbot Financial, its principals, affiliates, employees, or IARs may purchase, sell, or hold. When a decision is made to liquidate a security from all applicable accounts, priority will always be given to client orders before those of a related or associated person to Talbot Financial. In some cases the trades of the clients and advisory personnel will be combined in a single block trade, and all trades will receive the average price. We have procedures for dealing with insider trading, employee-related accounts, "front running" and other issues that may present a potential conflict when buy/sell recommendations are made. These procedures include reviewing employee security transactions and holdings to eliminate, to the extent possible, the adverse effects of potential conflicts of interest on clients.

### **Brokerage Practices (Item 12)**

*This section of the brochure describes how we recommend broker-dealers for client transactions.*

## **Factors Considered When Recommending Charles Schwab & Co., Inc. as Your Qualified Custodian**

Talbot Financial does not maintain custody of your assets that we manage, although we may be deemed to have custody of your assets if you give us authority to withdraw assets from your account (see Item 15 – Custody, below). Your assets must be maintained in an account at a “qualified custodian,” generally a broker-dealer or bank. We recommend that our clients use Charles Schwab & Co., Inc. (“Schwab”), a registered broker-dealer, Member SIPC, as the qualified custodian. We are independently owned and operated and are not affiliated with Schwab. Schwab will hold your assets in a brokerage account and buy and sell securities when we instruct them to. While we recommend that you use Schwab as custodian/broker, you will decide whether to do so and will open your account with Schwab by entering into an account agreement directly with them. We do not open the account for you, although we may help you do so. Even though your account is maintained at Schwab, we can still use other brokers to execute trades for your account as described below (see “Your Brokerage and Custody Costs”).

### How We Select Brokers/Custodians

We seek to recommend a custodian/broker who will hold your assets and execute transactions on terms that are, overall, most advantageous when compared to other available providers and their services. We consider a wide range of factors, including, among others:

- Combination of transaction execution services and asset custody services (generally without a separate fee for custody)
- Capability to execute, clear, and settle trades (buy and sell securities for your account)
- Capability to facilitate transfers and payments to and from accounts (wire transfers, check requests, bill payment, etc.)
- Breadth of available investment products (stocks, bonds, mutual funds, exchange-traded funds, etc.)
- Availability of investment research and tools that help us make investment decisions
- Quality of services
- Competitiveness of the price of those services (commission rates, margin interest rates, other fees, etc.) and willingness to negotiate the prices
- Reputation, financial strength, and stability
- Availability of other products and services that benefit us

### Your Brokerage and Custody Costs

Schwab generally does not charge clients separate for custody services but is compensated by charging you commissions or other fees on trades that it executes or that settle into your Schwab account. Schwab is also compensated by earning interest on the uninvested cash in Schwab’s Cash Features Program or on any margin balance maintained in Schwab accounts, and from other ancillary services.

Most trades no longer incur commissions or transaction fees, though there are exceptions. Schwab discloses its fees and costs to clients and we take those costs into account when

executing transactions on your behalf. Schwab charges you a flat dollar amount as “prime broker” or “trade away” fee for each trade that we have executed by a different broker-dealer but where the securities bought or the funds form the securities sold are deposited (settled) into your Schwab account. These fees are in addition to the commissions or other compensation you pay the executing broker-dealer. Because of this, in order to minimize your trading costs, we have Schwab execute most trades for your account (see “Directed Brokerage, below, for more information).

Certain mutual funds and ETFs are made available for no transaction fee; as a result the confirmation may show “no commission” for a particular transaction. Typically the custodian (but not Talbot Financial) earns additional remuneration from such services as recordkeeping, administration, and platform fees, for the funds and ETFs on their no-transaction fee lists. This additional revenue to the custodian will tend to increase the internal expenses of the fund or ETF. We select investments based on our assessment of a number of factors, including liquidity, asset exposure, reasonable fees, effective management, and low execution cost. Where we choose a no-transaction fee fund or ETF, it is because it has met our criteria in all applicable categories.

#### Products and Services Available to Us From Schwab

Schwab Advisor Services™ (formerly called Schwab Institutional®) is Schwab’s business serving independent investment advisory firms like us. They provide us with access to its institutional brokerage—trading, custody, reporting, and related services—many of which are not typically available to Schwab retail customers. Schwab also makes available various support services. Some of those services help us manage or administer our clients’ accounts, while others help us manage and grow our business. Schwab’s support services generally are available on an unsolicited basis (we don’t have to request them) and at no charge to us as long as our clients collectively maintain a total of at least \$10 million of their assets in accounts at Schwab. If our clients collectively have less than \$10 million in assets at Schwab, Schwab may charge us quarterly service fees of \$1,200. Following is a more detailed description of Schwab’s support services.

#### Services That Benefit You

Schwab’s institutional brokerage services include access to a broad range of investment products, execution of securities transactions, and custody of client assets. The investment products available through Schwab include some to which we might not otherwise have access or that would require a significantly higher minimum initial investment by our clients. Schwab’s services described in this paragraph generally benefit you and your account.

#### Services That May Not Directly Benefit You

Schwab also makes available to us other products and services that benefit us but may not directly benefit you or your account. These products and services assist us in managing and administering our clients’ accounts. They include investment research, both Schwab’s own and that of third parties. We may use this research to service all or a substantial number of our clients’ accounts, including accounts not maintained at Schwab. In addition to investment research, Schwab also makes available software and other technology that:



- Provide access to client account data (such as duplicate trade confirmations and account statements)
- Facilitate trade execution and allocate aggregated trade orders for multiple client accounts
- Provide pricing and other market data
- Facilitate payment of our fees from our clients' accounts
- Assist with back-office functions, recordkeeping, and client reporting

#### Services That Generally Benefit Only Us

Schwab also offers other services intended to help us manage and further develop our business enterprise. These services include:

- Educational conferences and events
- Consulting on technology, compliance, legal, and business needs
- Publications and conferences on practice management and business succession
- Access to employee benefits providers, human capital consultants, and insurance providers

Schwab may provide some of these services itself. In other cases, it will arrange for third-party vendors to provide the services to us. Schwab may also discount or waive its fees for some of these services or pay all or a part of a third party's fees. Schwab may also provide us with other benefits, such as occasional business entertainment of our personnel.

#### Research and Other Soft Dollar Benefits

We do not have any traditional "soft dollar" arrangements in place, in which we agree to direct a certain amount of commission dollars to a specific custodian in exchange for research or other services. Rather, the services described in this Item 12 are made available to us simply because we maintain client accounts on the Schwab platform.

Many of these services generally may be used to service all or a substantial number of our accounts, including accounts not maintained at Schwab Advisor Services.

#### Our Interest in Schwab's Services

The availability to us of the foregoing products and services is not contingent upon us committing to Schwab Advisor Services any specific amount of business (assets in custody or trading commissions). In some cases, clients could pay more for custody and execution through the custodian we recommend than through others. We review the capacities and costs of Schwab regularly to ensure that our clients are receiving quality executions and competitive pricing, as well as more intangible service benefits.

#### Directed Brokerage

Because we recommend Schwab and then execute transactions through that custodian on a discretionary basis, we are effectively requiring that clients "direct" brokerage to Schwab, absent other specific instructions as discussed below. Because we are not choosing brokers on a trade-by-trade basis, we may not be able to achieve the most favorable executions for clients and this may ultimately cost clients more money. Not all investment advisers require directed brokerage.

We do not use, recommend, or direct activity to brokers (including Schwab) in exchange for client referrals.

We do not generally permit clients to direct us to use brokers other than the custodian. If we agree to accommodate a request to do this, we will likely have little or no ability to negotiate commissions or influence execution price, and the client will also not benefit from the savings afforded by the occasional trade aggregation we may implement for other clients. This may result in greater costs.

#### Brokerage for Client Referrals

Talbot Financial does not have any agreements in place where securities transactions are directed to particular broker-dealers in exchange for client referrals.

#### Aggregated Orders

When we decide to purchase or sell a specific security for multiple clients at the same time, we will consider aggregating, or combining the orders. This procedure will result in a single average price for all client transactions in the aggregated order. The account custodian charges for each transaction as if it were placed individually.

#### Allocation of Thinly Traded Securities

We may allocate securities among accounts when enough of a particular security or securities cannot be purchased or sold on a given day at a desired price. In this event, we will allocate the shares actually purchased or sold on pro rata basis. We may remove small allocations from the process if we believe it would not be in the best interest of our client(s).

#### Trade Errors Policy

From time-to-time we may make an error in submitting a trade order on your behalf. When this occurs, we may place a correcting trade with the broker-dealer which has custody of your account. If an investment gain results from the correcting trade, the gain will remain in your account unless the same error involved other client account(s) that should have received the gain, it is not permissible for you to retain the gain, or we confer with you and you decide to forego the gain (e.g., due to tax reasons). If the gain does not remain in your account and Charles Schwab & Co. Inc. ("Schwab") is the custodian, Schwab will donate the amount of any gain \$100 and over to charity. If a loss occurs greater than \$100, Talbot Financial will pay for the loss. Schwab will maintain the loss or gain (if such gain is not retained in your account) if it is under \$100 to minimize and offset its administrative time and expense. Generally, if related trade errors result in both gains and losses in your account, they may be netted.

## **Review of Accounts (Item 13)**

*This section of the brochure describes how often client accounts are reviewed and by whom.*

## **Reviews**

Talbot Financial reviews the securities held in its clients' investment supervisory accounts on an ongoing basis. The reviews are conducted by James Pirak and Thomas Swoffer, Investment Advisor Representatives. Your accounts are reviewed at least quarterly for proper asset and sector allocation to assure they comply with your investment objectives and mandates. Reviews may be triggered by changes in a client's personal, tax, or financial status. Macroeconomic and company-specific events may also trigger reviews.

## **Reports**

Talbot Financial sends quarterly written reports to all clients. These are generated through portfolio management system we use and provide performance information as well as position holdings by sector. Your independent qualified account custodian, Schwab, prepares and distribute account statements directly to you. These account statements describe all activity in your accounts including holdings, transactions, and investment advisory fees deducted from the account. The reports we send are never a substitute for the custodial statement. We urge you to compare the custodial statement to the reports we provide and to notify us of discrepancies.

## **Client Referrals and Other Compensation (Item 14)**

*This section of the brochure discloses our arrangements with people who are compensated for referring us business.*

Talbot Financial has not entered into any agreements with third parties to give or receive referrals for compensation.

## **Custody (Item 15)**

*This section of the brochure encourages you to check the statements sent to you by your account custodian to ensure the accuracy of the fee calculation.*

You have authorized us to deduct periodic investment advisory fees directly from one or more of your accounts managed by Talbot Financial. These deductions from your account are shown on the periodic statements sent by your qualified custodian. You are encouraged to review these statements carefully and compare the amounts on the custodian statements with any statements we send and the fee schedule outlined in your Investment Advisory Agreement.

When our clients enter agreements with their custodian where the client requests the custodian transfer funds to a third-party, we are considered to have custody of client funds. To assure that our client's funds are safeguarded we take the following steps:

1. The client provides an instruction to the qualified custodian, in writing, that includes the client's signature, the third party's name, and either the third party's

address or the third party's account number at a custodian to which the transfer should be directed.

2. The client authorizes us, in writing, either on the qualified custodian's form or separately, to direct transfers to the third party either on a specified schedule or from time to time.
3. The client's qualified custodian performs appropriate verification of the instruction, such as a signature review or other method to verify the client's authorization, and provides a transfer of funds notice to the client promptly after each transfer.
4. The client can terminate or change the instruction to the client's qualified custodian.
5. We don't have the authority or ability to designate or change the identity of the third party, the address, or any other information about the third party contained in the client's instruction.
6. We maintain records showing that the third party is not a related party of ours or located at the same address as us.
7. The client's qualified custodian sends the client, in writing, an initial notice confirming the instruction and an annual notice reconfirming the instruction.

We are deemed to have custody of client assets due to Randy Talbot's role in managing the real estate SPVs described in Item 4, Item 6, and Item 10. Talbot Financial does not manage or control those SPVs, but because Mr. Talbot has control of both the SPVs and Talbot Financial, and some of our clients invest in the SPVs, we comply with the SEC's custody rule and obtain an annual surprise examination of the SPVs, in accordance with SEC guidance on this issue. The SPVs invest in real estate and do not trade in securities or other assets, and the surprise examination is therefore focused on cash flows in and out of the SPVs.

## **Investment Discretion (Item 16)**

*This section of the brochure discloses the power we have to make trades in your account.*

You grant Talbot Financial a limited power of attorney to select, purchase, or sell securities without obtaining your specific consent within the account(s) you have under our management. The limited powers of attorney are granted in the written Investment Advisory Agreement entered into between us. You may also need to execute additional documents from the account custodian granting us trading authority over your custodial accounts. There are no restrictions upon the securities that may be purchased, sold, or held in your account unless you provide these restrictions to us in writing and we agree to the restrictions.

## **Voting Client Securities (Item 17)**

*This section of the brochure explains our proxy voting policy and your ability to get proxy voting information from us.*

We do not vote client proxies. Clients will receive proxy information through their custodian based on the preferences selected at the time the custodial account is opened. We are happy to discuss questions clients may have about a particular proxy solicitation.

## **Financial Information (Item 18)**

*This section of the brochure is where investment advisors that collect more than \$1200 in fees per client and six months or more in advance would include a balance sheet.*

Talbot Financial is not aware of any circumstance that is reasonably likely to impair our ability to meet contractual commitments to you or our other clients. We do not require pre-payment of investment advisory fees of greater than \$1200 and more than six months in advance.

## Privacy Statement

*We, like other professionals who advise on personal financial matters, are required by federal law to inform our clients of their policies regarding the privacy of client information.*

In the course of providing our clients with certain advice, we may receive nonpublic personal financial information such as financial statements, account statements, and tax returns from our clients, their accountants and other representatives. All nonpublic personal information that we receive regarding our clients or former clients is held in strict confidence in accordance with our professional obligations, and is not released to people outside Talbot Financial, except with your consent, as required by law or to explain our actions to professional organizations that we are members of. We may share certain information with third parties who assist us in providing our services to you (such as administrative and client service functions) or marketing services, as permitted by law, subject to the obligation of these third parties not to use or disclose such information for any other purpose.

We retain records relating to professional services that we provide so that we are better able to assist you with your professional needs and, in some cases to comply with professional guidelines. In order to guard your nonpublic personal information from unauthorized disclosure, we maintain physical, electronic, and procedural safeguards.