

# **SANDERS MORRIS HARRIS LLC**

## **FOCUS Asset Management Program Wrap Fee Program Brochure**

March 20, 2020

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This wrap fee program brochure provides information about the qualifications and business practices of Sanders Morris Harris LLC. If you have any questions about the contents of this brochure, please contact the Compliance Department at the above telephone number. 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.

Sanders Morris Harris LLC is a registered investment adviser. Registration of an investment adviser does not imply any level of skill or training. The oral and written communications of an adviser provide you with information about which you determine to hire or retain an adviser.

Additional information about Sanders Morris Harris LLC also is available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

## **Material Changes**

The purpose of this page is to inform you of any material changes since the last annual amendment submitted March 2019.

On June 1, 2019 Item 10, Other Financial Industry and Affiliations was updated to reflect the current structure of Tectonic Financial, LLC, a publicly traded entity; (formerly, Tectonic Holdings), which owns the following financial industry affiliates: Tectonic Advisors LLC, Sanders Morris Harris LLC, T Bank N.A. and HWG Insurance LLC.

We review and update our brochure at least annually to make sure that it remains current. If you would like to receive a copy of the most recent version of our ADV Part 2 Brochure, please call us at (713)-224-3100.

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Brochure Supplement(s)

## **Services, Fees, and Compensation**

### **FOCUS Asset Management Program**

FOCUS is a flexible wrap fee advisory program that offers the client the choice of discretionary, non-discretionary, and third-party portfolio manager platforms as selected by the client. When a discretionary arrangement is selected, the Representative selects investments and executes transactions without further consultation with the client. In a non-discretionary arrangement, client authorization must be received prior to executing any transactions in the investments selected by the Representative. In this type of arrangement, the Representative may also execute transactions in securities selected by the client. When a Portfolio Manager platform is utilized, the third-party Portfolio Manager is granted discretion over the account.

SMH serves as the investment adviser for all FOCUS accounts and does not select other portfolio managers or investment advisers to manage client accounts and in some SMH utilizes outside managers albeit SMH is the adviser.

Management services in FOCUS are provided by a Representative selected by the client on either a discretionary or non-discretionary basis. These services include, but are not limited to, portfolio reviews and recommendations with respect to various investments and various administrative services.

A client also has the option to establish a dual contract wrap fee account whereby the client directs SMH to engage the third-party Portfolio Manager(s) selected by the client to invest the account assets on a discretionary basis. SMH assumes no responsibility for the selection of the Portfolio Manager or the suitability of the recommendations made by the Portfolio Manager.

No minimum investment is required to participate in FOCUS; however, minimum requirements may be established by any third-party Portfolio Manager selected by the client.

## **Fees and Compensation**

### **FOCUS Fees**

Within a FOCUS Account, fees are deducted from the account by SMH and are noted on account statements sent to the client by the custodian.

The Total Program Fee for FOCUS includes the Advisor Fee, which is shared by SMH and the Representative, and the Program Administrative Fee paid to the sponsor, administrator, or custodian of the program.

The negotiable Advisor Fee compensates SMH and the Representative for investment advisory services provided, pursuant to the Focus Asset Management Program Agreement. This fee covers the management and other account related services provided by SMH and the Representative, such as investment advice, investment selection, and the allocation and reallocation of investments. The Advisor Fee may be discounted at the discretion of the Representative.

The non-negotiable Program Administrative Fee compensates SMH and Pershing, the program's custodian, for the cost of execution, clearance and custody, fee calculation and deduction, and

performance reporting.

The Total Program Fee is payable quarterly and may be deducted either in advance or in arrears using the following formula:

$$\frac{\text{Account Value} \times \text{Fee Schedule} \times \# \text{ of days in the billing cycle}}{365 \text{ (366 if leap year)}}$$

The account value for fee calculation purposes is based on the market value of the securities held in the account. The calculation excludes illiquid investments such as private placements, non-traded REITs, annuities, investments that include a publicly disclosed selling concession such as underwritten offerings, and any other securities previously designated by the client. The calculation follows a blended (or “not retroactive”) schedule where the fee schedule for each asset level is calculated using the relevant formula above. The fee for each asset level will then be added together to determine the total fee due for the specified period. Under certain circumstances, fees may be negotiated.

When advance billing is selected, the initial Total Program Fee is due in full on the effective date of the advisory agreement. The effective date is defined as the date when the account is accepted by SMH, and the fee is based on the account value on that date. The fee calculation is prorated if the account has been added to the billing system at any time other than the beginning of a billing cycle. Subsequent quarterly fees are determined on the first day of each calendar quarter based on the total value of the account as of the close of business on the last business day of the previous quarter and are due the following day. In the event that the advisory agreement is terminated prior to the end of a period for which a quarterly fee has been paid, fees are recalculated based on the length of service and unearned fees are returned to the client.

When arrears billing is selected, the Total Program Fee is deducted from the account at the end of the calendar quarter. When selecting arrears billing, the client must also elect if billing is to be based upon either the account value on the last day of the calendar quarter or the average daily account value.

If the client elects to be billed in arrears based on account value on the last day of the calendar quarter, subsequent quarterly fees are determined on the last day of each calendar quarter based on the total value of the account as of the close of business on the last business day of the quarter and are due the following day. Accounts added to the billing system during the billing period are charged a pro rata fee at the end of the period.

If average daily balance billing in arrears is elected, fees are charged at the end of the billing period. Daily account value is based on the previous market close. Fees calculated using this method are always final, and no adjustments will be made for any billing period.

In the event the advisory agreement is terminated prior to the end of a period for which an arrears quarterly fee is due, the fee is prorated and is due immediately.

If the account does not maintain sufficient cash or money market balances to cover the Total Program Fee, the client may deposit additional funds by the due date. If no deposit is made, SMH may liquidate securities in the account in amounts sufficient to cover such fees. Any liquidation may cause the client to incur taxes and other costs. For each addition to or withdrawal from the account of \$1,000 or more, the fee is adjusted in the next billing period.

The fee schedule for FOCUS is as follows:

<u>Total Assets</u>	<u>Maximum Total Program Fee as a % of Asset Value</u>
First \$100,000	3.00%
Next \$200,000	2.25%
Next \$200,000	1.90%
Next \$500,000	1.70%
Above \$1,000,000	Negotiable

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Next \$200,000	1.90%
Next \$500,000	1.70%
Above \$1,000,000	Negotiable

### **Payment Method**

Within a FOCUS account, fees are deducted from the account by SMH and are noted on account statements sent to the client by the custodian. If the account does not maintain sufficient cash or money market balances to cover the Total Program Fee, the client may deposit additional funds by the due date. If no deposit is made, SMH may liquidate securities in the account in amounts sufficient to cover such fees. Any liquidation may cause the client to incur taxes and other costs. For each addition to or withdrawal from the account of \$1,000 or more, the fee is adjusted in the next billing period.

### **Changes to Fees**

SMH may change the Program Administrative Fee at any time by giving thirty days prior written notice to the client. Following the 30-day notice period, the new fee schedule will become effective unless the client terminates the FOCUS Agreement. Any changes to the Advisor Fee require written authorization of the client.

## Other Fees and Compensation

The Total Program Fee for FOCUS does not include any fees charged by the third party Portfolio Manager selected by the client, if any. The Portfolio Manager Fee varies per Manager selected by the client. For specific information regarding the fees charged by the Portfolio Manager, the client should refer to the Portfolio Manager's Form ADV. The Portfolio Manager Fee, if any, is reflected as a separate line item on the client account statement.

The Total Program Fees also do not include certain charges associated with securities transactions that may be imposed by regulatory authorities or by broker-dealers other than SMH, including commissions, dealer markups or markdowns in principal transactions by or agency transactions with broker-dealers other than SMH, American Depository Receipts (ADRs) agency processing fees, odd-lot differentials, SEC and exchange fees and transfer taxes, and any other charges imposed by law.

In addition to the Total Program Fees described above, each mutual fund or exchange traded fund in which the client may invest also bears its own fees, including but not limited to short-term redemption fees, and expenses. Complete details of fees can be found in the applicable mutual fund or exchange traded fund prospectus. Other fees, such as SEC fees, Individual Retirement Account custodial fees, wire transfer fees, overnight check fees, account transfer fees or other taxes as required by law may be incurred.

Certain mutual funds may be subject to deferred sales charges. Neither SMH nor the Representative recommends the transfer of such funds into FOCUS accounts. Should the client choose to transfer such funds into the account, the client may incur deferred sales charges upon the redemption of the shares.

Clients may invest in certain mutual funds that make payments to broker dealers (such as SMH) pursuant to a 12b-1 distribution plan or pursuant to another arrangement as compensation for distribution or administrative services and may be paid out of the fund's assets. Mutual funds with 12b-1 fees are generally more expensive than funds without such fees. There is a conflict of interest when we recommend these products or services since they result in increased compensation to SMH. To mitigate this conflict of interest, SMH credit's back to your account an amount equal to the 12b-1 fees collected in connection with your advisory assets, except for 12b-1 fees generated through the default sweep money market mutual funds available on the Pershing platform, which Pershing remits to SMH and SMH retains. This revenue sharing creates a conflict of interest as the increased revenue generated from the default money market funds is paid to SMH. Because SMH receives and retains these amounts, SMH has an incentive to recommend accounts offering sweep money market funds paying 12b-1 fees, which in turn will negatively impact the amount you earn on cash in your account.

The cost of the services provided through FOCUS may be more or less than if each service was purchased separately. For example, the cost of services provided separately may be less for accounts with infrequent trading activity. Conversely, the cost of services provided separately may be more for an account with more frequent trading activity. Similarly, Representative compensation for FOCUS may be more than what the Representative would receive if the client participated in other available programs or paid separately for advice, brokerage, and other services and, therefore, the Representative may have a financial incentive to recommend FOCUS over other programs and services.

Please refer to the Other Financial Industry Activities and Affiliations section below, in particular the subsection Broker Dealers" Sanders Morris Harris, LLC, for important disclosure as the receipt of certain fees and commissions by the Representative and the conflicts resulting therefrom.

SMH sponsors wrap fee programs other than FOCUS. The complete details of the other programs can be located in the wrap fee program brochure applicable to each program. To obtain a copy of the wrap fee program brochure for another SMH-sponsored program, please contact your Representative.



## **Termination**

Either the client or SMH may terminate the FOCUS advisory agreement upon thirty days written notice to the counterparty.

## **Account Requirements and Types of Clients**

FOCUS is generally offered to individuals who have a need for fee-based services or could benefit from fee-based pricing over that of a traditional commission-based brokerage arrangement. There is no account minimum to participate in FOCUS, however, minimum requirements may be established by any third-party Portfolio Manager selected by the client. SMH primarily provides advisory services to individuals, high net worth individuals, pooled investments, trusts, estates, and corporations and other business entities.

## **Portfolio Manager Selection and Evaluation**

Within FOCUS, the client has the option to establish a dual contract wrap fee account whereby the client directs SMH to engage the third-party Portfolio Manager(s) ("Portfolio Manager") selected by the client to invest the assets of the account on a discretionary basis. SMH does not review Portfolio Manager performance information to determine or verify its accuracy or its compliance with presentation standards. SMH assumes no responsibility for the selection of the Portfolio Manager or the suitability of the recommendations made by Portfolio Manager.

## **Performance-Based Fees and Side-By-Side Management**

SMH (nor MG) does not charge any performance-based fees (fees based on a share of capital gains on or capital appreciation of the assets of a client). SMH does not engage in side-by-side management.

## **Methods of Analysis, Investment Strategies and Risk of Loss**

SMH and its Representatives use a wide variety of methods, including charting, fundamental analysis, quantitative, qualitative analysis and technical analysis to determine investment strategies for clients. The primary sources of information used to conduct these types of analysis are financial newspapers and magazines, inspections, research prepared by third parties, independent sources and affiliated entities, ratings services, press releases, and annual reports, prospectuses and other filings with the SEC. The implementation of these strategies varies based upon the individual client.

Each client's account is managed on the basis of the client's financial situation, sophistication and knowledge, investment objectives (eg. suitability) and instructions. The Representative works with the client to obtain sufficient information to provide individualized investment advice and is reasonably available to consult with the client on an ongoing basis. Clients are permitted to impose reasonable restrictions on the management of the account.

Overall strategies are determined primarily on account size, registration, risk tolerance, objective(s), and the desire to focus on income, yield or volatility. SMH and its Representatives use a wide variety of methods, including charting, fundamental analysis, quantitative, qualitative analysis and technical analysis to determine investment strategies for clients. The primary sources of information used to conduct these types of analysis are financial newspapers and magazines, inspections, research prepared by third parties,

independent sources and affiliated entities, ratings services, press releases, and annual reports, prospectuses and other filings with the SEC. The implementation of these strategies varies based upon the individual client. A quarterly custodial statement, containing a description of all account activity is provided to the client, in electronic or paper form at the direction of the client. The Representative reviews the overall performance of each account on a periodic basis in order to ensure that transactions are suitable based on the client's investment objectives, meet quality expectation of the client and comply with any investment restrictions requested by the client.

Clients who choose a third-party Portfolio Manager are advised to review carefully and should carefully review the third-party firm's Form ADV Part 2 for information on their investment strategy. Investment strategies vary by the Portfolio Manager selected.

Investing in any type of security involves risk of loss that clients should be prepared to bear. SMH does not guarantee the performance of an account or any specific level of performance. Market values of the securities in the account will fluctuate with market conditions. When the account is liquidated, it may be worth more or less than the amount invested.

Some strategies (including those used in some FOCUS accounts) incorporate allocations to alternative investments, including mutual funds or ETFs invested in real estate investment trusts, master limited partnerships, managed futures, commodities, covered calls, long/short strategies, and other non-traditional investments. Investment strategies also include allocation to international/global investments.

Investment in a portfolio that includes alternative investments presents additional risks which the client should consider when making an investment decision. These risks may include adverse market conditions risk, counterparty risk, currency exchange risk, derivatives risk, emerging markets risk, high portfolio turnover, leverage risk, and other risks depending on the investment. Alternative investments are frequently asset classes that are referred to as non-correlated (investments that move contrary to, or without influence from, broader markets). While including non-correlated assets may result in smoother portfolio performance with less volatility, there are no assurances that non-correlated assets will not decline in value.

International investments are subject to risks not associated with domestic investing. In addition to the risks generally associated with domestic investments, international investing is subject to currency, political, economic and social risks.

## **Voting Client Securities**

As a matter of firm policy and practice, SMH has no authority to take action or render any advice with respect to voting proxies on behalf of advisory clients. Clients will receive proxies or other solicitations directly from the account custodian or transfer agent, not from SMH, MG or other affiliated entities. Clients retain the responsibility for voting all proxies for securities maintained in client portfolios.

## **Client Information Provided to Portfolio Managers**

The Representative will obtain information prior to opening an account regarding the client's financial situation, goals and investment objectives, risk tolerance, time horizon and other relevant factors. The Representative will also inquire as to the client's interest in imposing any reasonable restrictions on the management of the account.

If a third-party Portfolio Manager is selected by the client, the client's information and restrictions on investments will be shared as directed by the client in accordance with the parameters of the dual contract arrangement.

The Representative will contact the client at least annually to determine if any changes have occurred that may affect the ongoing suitability of the investments selected and to determine if any new restrictions should be imposed on the account. If any changes have occurred, the Representative will notify the Portfolio Manager.

## **Client Contact with Portfolio Managers**

Clients are generally free to contact SMH and their Representative at any time during normal business hours via telephone, facsimile, mail or email. In-person meetings should be scheduled in advance to ensure that the Representative is available.

## **Additional Information**

### **Disciplinary Information**

Registered investment advisers are required to disclose all material facts regarding any legal or disciplinary events that would be material to the client's evaluation of SMH or the integrity of SMH's management.

SMH is a broker/dealer in addition to its activities as a registered investment adviser. In connection with its broker/dealer business, SMH has been the subject of certain regulatory actions, some of which SMH has determined to be immaterial. Others are summarized below:

On January 8, 2008, SMH entered into a Letter of Acceptance, Waiver and Consent ("AWC") with the NASD (predecessor to FINRA) where SMH neither admitted nor denied the allegations that during the period July 2000 until December 2005, SMH (1) failed to establish, maintain, and enforce adequate procedures and systems that were tailored to ensure that its hedge fund, prime brokerage services, and soft dollar activities were in compliance with federal securities laws and rules, and pertained to supervision of its employees who provided services to funds utilizing the prime brokerage services divisions' platform; (2) allowed improper payment of \$325,000 in soft dollars to one hedge fund manager; and (3) lacked adequate procedures concerning the contents of hedge fund sales materials prepared and disseminated by SMH and distributed sales literature that did not adequately disclose material investment risks to potential investors in accordance with NASD Notice to Members 03-07. During the period January 2003 until December 2004, SMH (1) failed to retain certain e-mails and instant messages sent to and received by certain employees in the prime brokerage services division and (2) permitted an unregistered employee of the prime brokerage services division to engage in activities that required registration. In 2002, SMH modified certain brokers' compensation structure so that they shared in the prime brokerage services profit pool, derived in part from commissions earned on the fund's trading. As a result, contrary to restrictions, from April 2002 to June 2004, the brokers shared indirectly in the commissions SMH earned in the fund's trading but did not amend the fund's offering document to accurately depict the sharing arrangement. SMH was censured, paid a fine in the amount of \$450,000, and entered into an undertaking to have an independent consultant review SMH's systems and procedures.

On June 16, 2008, SMH entered into an AWC with the NASD where SMH neither admitted nor denied the allegations that, during the period December 2002 until April 2004, SMH failed to establish, maintain or enforce a supervisory system and procedures reasonably designed to detect and prevent market timing

activities and that SMH failed to take supervisory action against a Representative who appeared to be market timing. SMH was censured and paid a fine in the amount of \$45,000.

On November 20, 2008, SMH consented to the entry of an Order brought by the Texas State Securities Board (“TSSB”) that alleged the firm failed to require two agents of an independent investment adviser within SMH’s network to be appropriately registered to conduct business in the State of Texas. The TSSB found that SMH failed to enforce a system reasonably designed to supervise the activities of its agents and also found that one of SMH’s agents failed to disclose an outside advisory business activity. The firm was reprimanded and paid a fine in the amount of \$30,000.

On August 7, 2012 SMH entered into an AWC with FINRA where SMH neither admitted nor denied the allegations that (1) failed to reasonably supervise a registered representative who was under a heightened supervision plan, (2) failed to supervise the options trading at a branch office, (3) failed to establish and maintain an adequate AML compliance program and (4) failed to accurately calculate its net capital requirement due to a proposed credit agreement between a bank and SMH’s parent company that pledged its assets, causing inaccurate reporting for more than 18 months. SMH was censured and paid a fine of \$150,000.

On January 2, 2015 SMH entered into an AWC with FINRA which alleged that on December 28, 2012, as a result of an inaccurate deferred tax balance calculation, SMH inaccurately calculated its excess net capital. Based on that, on December 28, 2012 SMH’s board of directors authorized a distribution to its owners, in connection with which it filed with FINRA a notice of withdrawal of equity capital on January 2, 2013. SMH failed to properly accrue this capital distribution as a liability, instead reflecting it as an expense when the distribution occurred on January 4, 2013. When SMH later provided FINRA with an estimated net capital calculation that reflected the correct value for the deferred tax asset and distribution, it showed a net capital deficiency until February 28, 2013. Additionally, from October 1, 2012 to February 28, 2013 SMH failed to maintain books and records that properly reflected the book basis amounts for partnership interests sold in October 2012. Consequently, SMH filed inaccurate FOCUS reports for periods ending October, November and December 2012, as well as January and February 2013. SMH was censured and paid a fine of \$85,000.

## **Other Financial Industry Activities and Affiliations**

SMH is wholly owned by Tectonic Holdings, LLC (“Tectonic”). As such, SMH is managed by the SMH Managers of Tectonic who have the requisite FINRA licenses to manage a SEC registered Investment Adviser and Broker-Dealer. However, SMH exercises its own independent investment and voting discretion in accordance with its investment philosophy, fiduciary duties, client guidelines and policies and procedures as a broker dealer and an investment adviser. In addition to advisory services, SMH offers a broad range of financial services to clients. Currently, the majority of SMH’s revenues are generated by brokerage activities, with the remaining revenues being advisory services and fee-based business. SMH is also registered as a broker dealer and is affiliated with another investment adviser, Tectonic Advisors, LLC, and an insurance agency, HWG Insurance Agency LLC, as described below.

## **Broker Dealers:**

### **Sanders Morris Harris LLC, registered Broker Dealer (CRD No. 20580)**

As a result of the dual registration of SMH as an investment adviser and broker dealer, Representatives, principal executive officers and other related employees of SMH may also be Registered Representatives, managers, and/or officers of the SMH registered broker dealer and FINRA member. SMH may perform and receive compensation for, among other things, brokerage, asset management, underwriting of syndicate and secondary securities offerings, and similar services. The advice given and the action taken with respect to such services may differ from advice given or the timing and nature of action taken with respect to advisory accounts.

Dual registration may present a conflict of interest to the extent that a Representative recommends the purchase of security, which results in commissions being paid to the Representative as a registered representative of the broker dealer. The commissions and fees charged by the broker dealer are in addition to SMH's management fee and other fees and expenses of investment companies in which a client's account may be invested.

SMH may purchase or sell securities in which SMH or its Representatives directly or indirectly have or may acquire a position or interest. In some circumstances SMH and its Representatives may receive customary compensation from mutual fund companies, including 12b-1 fees for performing certain administrative and/or shareholder servicing related tasks associated with SMH clients' investments in such securities. SMH and its Representatives may also be compensated for referral activity.

### **Related Persons: Tectonic Advisors, LLC ("Tectonic")**

Relationships and arrangements with related persons: Tectonic is under common ownership with SMH. Employees of Tectonic may also be Registered Representatives of SMH, the dual registrant. Those Registered Representatives may receive compensation from the sale of investment companies (mutual funds), insurance, and other investments and services to various clients. Certain officers and directors of Tectonic may also serve as officers and directors of SMH.

## **Insurance Agency:**

### **Related Persons: HWG Insurance Agency, Inc.**

Relationships and arrangements with related persons: SMH Representatives may also be licensed insurance agents for HWG Insurance Agency, Inc., a subsidiary of SMH. If a client elects to purchase an insurance product through an SMH employee or Representative, which may include life, accident, disability insurance and annuities, the Representative may receive a commission from those sales. This presents a conflict of interest to the extent that the Representative recommends the purchase of an insurance product resulting in a commission being paid to the Representative as an insurance agent.

Through Tectonic Holdings LLC, we are also affiliated with the following investment advisers and operating entities – Sanders Morris Harris LLC, Tectonic Advisors, LLC, HWG Insurance Agency, Inc., (insurance). Sanders Morris Harris LLC is both an investment adviser and a registered broker-dealer. Through common ownership of Tectonic Holdings, LLC. Additionally, SMH is also affiliated with Cain Watters & Associates, an SEC registered investment adviser. SMH is also affiliated with National Bank, T Bank, NA.

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

SMH has adopted a Code of Ethics for all Representatives and employees of the firm describing its high standard of business conduct and its fiduciary duty to its clients. The Code of Ethics includes provisions relating to the confidentiality of client information, insider trading, gifts and entertainment, and personal securities trading, among other things. All Representatives and employees at SMH must acknowledge the terms of the Code of Ethics annually, or as amended. SMH's Representatives and employees are required to follow SMH's Code of Ethics.

SMH's clients or prospective clients may request a copy of the firm's Code of Ethics by contacting us using the contact information on the cover page.

SMH anticipates that from time to time, SMH may recommend and effect the purchase or sale of securities in which SMH, its affiliates and/or clients, directly or indirectly, have a position of interest. As such, this could present the appearance of or an actual conflict of interest. Officers, directors and employees of SMH and its affiliates may trade for their own accounts in securities which are recommended to and/or purchased for SMH's clients. While permitted under the Code of Ethics and applicable laws, this does present a potential conflict of interest. The Code of Ethics is designed to ensure that the personal securities transactions, activities and interests of the employees of SMH will not interfere with: (i) making decisions in the best interest of advisory clients; and (ii) implementing such decisions while, at the same time, allowing employees to invest for their own accounts.

The Code of Ethics requires pre-clearance of certain transactions. It also restricts trading in close

proximity to client trading activity. As mentioned above, employees and other access persons may be permitted to invest in the same securities as clients. As a result, there is a possibility that employees might benefit from market activity by a client in a security held by an employee. Employee trading is continually monitored to reasonably prevent conflicts of interest between SMH and its clients.

Certain affiliated accounts may trade in the same securities with client accounts on an aggregated basis to obtain best execution and avoid price differential. In such circumstances, the affiliated and client accounts will share commission costs equally (if applicable) and transactions are executed on an average price basis.

SMH prohibits principal transactions that involve it or its representatives in advisory client accounts. Principal transactions are generally defined as transactions where an adviser, acting as principal for its own account or the account of an affiliated broker dealer, buys from or sells any security to any advisory client. A principal transaction may also be deemed to have occurred if a security is crossed between an affiliated hedge fund and another client account.

Although occurring on an infrequent basis, SMH or its Representatives may execute transactions in which the client's securities are sold to or bought from an SMH brokerage customer (i.e., an agency cross transaction). Agency cross transactions are only executed for those clients who have provided written consent. Written consent is obtained only after the client has received full written disclosure that SMH or the Representative may act as broker, receive commissions from, and potentially have a conflicting division of loyalties and responsibilities regarding both parties to such transaction.

Client's written consent approving agency cross transactions may be revoked at any time by written notice to SMH. Each client will receive a written confirmation at or before the completion of each such transaction.

The confirmation will include a statement of the nature of such transaction and the date the transaction took place. The confirmation must also contain an offer to furnish, upon request, the time the transaction took place and the source and amount of any other remuneration received or to be received by the SMH or the Representative in connection with the transaction. An annual disclosure statement identifying the total number of such transactions and the total amount of all commissions or other remuneration received in connection with such transactions during the period must also be provided. Under no circumstances will SMH or a Representative make recommendations to parties on both sides of the transaction.

Representatives may buy or sell for themselves securities that they also recommend to clients. Securities purchased and sold for the account of a Representative or employee are purchased and sold on the same basis for the client according to the client's stated goals and investment objectives. In all instances, the positions would be so small as to have no impact on the pricing or performance of the security.

Representatives may hold positions in securities held by or recommended to clients but may not front-run or otherwise benefit from these positions. Internal procedures have been instituted to ensure that the client is treated fairly in execution of all trades.

To avoid conflicts of interest, SMH directors, officers or employees are prohibited from buying or selling securities for their personal portfolio(s) where their decision is substantially derived, in whole or in part, by reason of their employment unless the information is also available to the investing public on reasonable inquiry. No associated person of SMH shall place their own interests over those of the advisory client. Further, all Representatives must comply with all applicable federal and state regulations governing registered investment advisory practices.

## **Review of Accounts**

SMH Representatives monitor investment strategies on a periodic basis. Changes affecting a particular investment strategy may trigger changes to all client portfolios following that strategy. Portfolios not following a particular strategy may also be reviewed periodically by the Representative for investment opportunities. In addition, not less than annually, accounts are reviewed with clients by Representatives to ensure that the strategy continues to meet the client's investment objectives and to determine if the client wishes to impose any new restrictions or revisions to the investment objectives on the management of the account.

The overall performance of each portfolio is reviewed on a periodic basis by the Representative. Portfolio transactions are reviewed to ensure that each transaction: (1) is suitable to the client's investment objectives, (2) meets the client's investment objectives, and (3) complies with the client's investment restrictions, if any.

The nature and frequency of reports to clients are determined primarily by the particular needs of each client. Generally, SMH issues quarterly performance reports detailing account holdings. Clients also receive account statements from the custodian at least quarterly detailing all activity in the client's managed account.

Clients may contact and consult with the Representative that is responsible for the client's account at any time. Accounts are valued by the account custodian who utilizes a third party pricing service. If third party pricing is unavailable, valuations are provided on at least a quarterly basis and are summarized in a portfolio performance report detailing assets, transactions, receipt and disbursement of funds, interest and dividends received and gain or loss by security and for the overall account. Illiquid investments, such as private placements, non-traded REITs, and annuities may be included at the client's election on custodial statements for informational purposes only where permitted by the custodian. Illiquid investments are valued by third parties, such as the issuer or others possessing the requisite knowledge of the investment of the security. Such

values are provided for informational purposes only and are intended to reflect an estimate of the interest in the illiquid investment and the value may not be realized when liquidated.

Third party portfolio managers, if applicable, will also review and monitor accounts on a periodic basis. A detailed explanation of the portfolio manager's review can be found in the manager's Form ADV Part 2A.

## **Client Referrals and Other Compensation**

From time to time, SMH may enter into solicitation agreements with individuals or entities whereby investment advisory accounts or private fund investors are solicited by SMH and referred to another state or SEC-registered investment adviser. In these situations, SMH may be compensated for the referral activity. Similarly, SMH may enter into solicitation agreements where investors are solicited by another individual or entity and referred to SMH. In these situations, the individual or entity may be compensated by SMH for the referral activity.

Solicitation agreements require the solicitor to perform his duties in accordance with the Investment Advisers Act of 1940 and appropriate state regulations. Under the agreement, the solicitor must also provide each prospective client with Part 2 of Form ADV for the firm receiving the referral and SMH's separate written disclosure document.

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## **Financial Information**

Registered investment advisers are required to provide clients with certain financial information or disclosures about its financial condition. Currently, SMH has no financial condition that is reasonably likely to impair its ability to meet contractual and fiduciary commitments to clients. SMH has not been the subject of any bankruptcy proceeding.