

FIRM SUPERVISORY PROCEDURES MANUAL  
Polar Investment Counsel Inc.  
June 2018

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*FINRA is in the process of converting all old NASD Rules to FINRA Rules. As of the date of this manual, certain rules are “NASD Rules” that have not yet been converted to “FINRA Rules.” The old NASD Rule is referred to as a “NASD Rule”; and when a rule has been adopted by FINRA as a consolidated rule, the new FINRA Rule is referred to as a “Consolidated FINRA Rule.” As rule conversion/consolidation changes are announced, those rule number references are changed herein; eventually all rules will be Consolidated FINRA Rules and the “Consolidated” prefix will be removed.*

**SECTION I: INTRODUCTION**

This manual is intended to set forth the policies, procedures and systems of application by which Polar Investment Counsel Inc. (PICI or Firm) will conduct its operations in compliance with applicable statutes, rules and regulations administered by federal and state regulatory authorities. All associates of PICI are required to review this manual and comply with its terms. Any unexcused failure on the part of any registered representative or administrative personnel of PICI to perform their duties in accordance with these procedures may be grounds for disciplinary action or termination of registration.

The officers and directors of PICI are responsible for the content of this manual, the review and updating of this manual. Questions and comments concerning these matters are encouraged.

**The Firm as Introducing Firm.** The Firm is an Introducing Firm on a fully disclosed basis and its customer transactions are executed through, and its customer accounts are held at, its clearing (carrying) firm, which is also a FINRA member. Certain transactions may not be put through the clearing firm, but rather, go directly to product sponsors or private issuers. Certain accounts may not be held at the clearing/carrying firm, but instead are held at product sponsors or prime brokers.

The firm's clearing firm is: Hilltop Securities Inc. 1201 Elm Street Suite 3500 Dallas TX 75270 214.859.1800

**The Securities Investor Protection Corporation (SIPC):** The Securities Investor Protection Corporation (SIPC) was established to restore public confidence in the securities industry and to protect customers' assets held by members. SIPC provides up to \$500,000 protection per customer for claims of cash and securities with a limit of \$250,000 for claims of cash. The Firm is currently a member of SIPC.

**SECTION 2: SUPERVISORY AUTHORITY and FUNCTION**

**2:1 Supervisory Responsibility:** Supervisory responsibility hereunder shall include all matters relating to the servicing of customer accounts, control and review of the firm's financial affairs, review of representative's compliance, maintenance and review of books and records, records and accounts of the firm and the timely filing of required regulatory reports. Supervisory personnel shall apply the procedures and systems described herein with respect to the above-mentioned functions in such fashion as to prevent and detect violations of state or federal securities law.

Senior Principal Officers shall be responsible for supervision of every aspect of the firm's operations, trading, compliance and supervision of personnel. It shall be the responsibility of the senior principals to see that the policies and procedures set forth herein are applied in such a way as to prevent and detect violation. The Home Office is responsible for all registration and licensing of all registered personnel.

Senior principals of PICI are designated to establish, maintain and enforce supervisory control procedures that will test and verify that PICI's supervisory procedures are sufficient and amend or create additional supervisory procedures where the need is identified by such testing and verification.

The testing and verification will be conducted in a manner that is independent of any business considerations that are countervailing to full compliance with applicable securities laws and regulations and FINRA rules. Testing will be done annually and results discussed between the two senior principals of firm, the firm does not have a board of directors.

The firm has two senior (home office) registered principals which are designated as follows:

**Michael C Jordan, President CEO**

Principal's licenses and effective dates of designation (i.e., test dates):

Series 1 – 1974; Series 3 – 1996; Series 4 – 1997; Series 24 – 1997; Series 28 – 1998; Series 30 – 1996

Series 53 – 1999; Series 63 – 1979

Location: Home Office – Thief River Falls MN

Executive Representative: 1995

Financial and Operations Principal: 2009

MSRB Principal: 1999

Registered Options Principal: 1997

**Sherry Abbott EVP CCO CFO**

Principal's licenses and effective dates of designation (i.e., test dates):

Series 7 – 2006 ; Series 24 – 2011 Series 63 – 2006

Location: Home Office – Thief River Falls MN

Chief Compliance Officer: 2009

Chief Financial Officer: 2009

Sherry Abbott is supervised by Michael Jordan, President, CEO.

**2:2 Persons to Explain Records:** Home Office Senior principals of the firm are responsible for explaining all records and establishing policies and procedures.

**2:3 Registered Principals:** PICI registered principals shall exercise such operational authority and within such function area, as is expressly delegated by the senior principals of the firm. Each registered person will be assigned a registered principal as supervisor. OSJ and branch offices are under the direct supervision of the Home Office senior principals. Each representative signs a Letter of Operational and Supervisory Understanding detailing the authority granted to them to facilitate the day to day activities of their business. The CCO or designee shall inspect each OSJ office annually and each branch office at least once every three years. The firm maintains a separate audit schedule specifying cycles and review criteria.

**2:4 OATS Reporting:** Senior Home Office principals will be responsible for the supervision of OATs reporting. All reporting is currently submitted by our clearing firm. Our clearing firm reports our trades under our MPID number.

**2:5 Producing Managers:** Senior Home Office principals will be responsible for reviewing the activity and transactions of any producing managers. All transactions are reported daily and monthly and are reviewed by a senior principal in a timely manner. If any situation occurs that requires further review, the Home Office may examine various account documents and reports.

**2:6 Heightened Supervision of 20% Producing Managers/Associated Persons:** PICI will review and calculate on a rolling twelve month period the activity of any 20% producing manager. All transactions are reported on a blotter and will be reviewed by a senior home office principal daily.

**2:7 Limited Size and Resource Exception (Rule 3012):** PICI is using the "Limited Size and Resource Exception granted by FINRA as follows:

- PICI is a small broker dealer with a small number of registered reps and staff



- PICI does not have a senior to or otherwise independent person to conduct the reviews of the associated persons. PICI also does not have enough staff or resources to meet the rotation requirement.
- PICI does not have a board of directors; the officers of the firm who are the Home Office senior principals make all firm decisions.

**2:8 Review of Procedures:** The firm's two Home Office senior principals are responsible to review the firm's supervisory practices and procedures and take any appropriate action to achieve member compliance with applicable rules and regulations (Rule 3010).

**2:9 Annual Certification:** The firm's two Home Office senior principals will certify annually that PICI has a process to adopt compliance policies and supervisory procedures reasonably designed to achieve compliance with applicable securities laws and regulations and FINRA rules (Rule 3013).

### **SECTION 3: REGISTERED REPRESENTATIVES**

**3:1 Registration:** The Home Office senior principals supervise the hiring, conduct and actions of Registered Representatives and all other associated persons. All registered representatives must complete a Form U4, fingerprint card, pre-hire questionnaire and pre-hire authorization. If representative was previously registered with FINRA, a copy of their Form U5 must be provided. PICI will make every effort to verify information submitted during the hiring process within 30 days. If any information cannot be verified within the 30 day period, we will make notes and verify as soon as possible. Any amendments that need to be made will be done within this period.

In conducting the pre-hire investigation, the firm may (could not be applicable in all registrations):

- Review U4 and other hiring documents
- Contact previous employers
- Obtain most recent U5
- Conduct OFAC check; and/or
- Conduct a pre-hire check through CRD system
- Background check

The firm may utilize a third party service to conduct a background check and/or the firm may do a public search with a national public records database. Due to the firm's location, all registered persons are required to provide a credit report which they must obtain and forward to the firm to be kept in representatives file and viewed only by Home Office senior principals. All information gathered will be reviewed against documentation presented. Any discrepancies will be amended if need be upon learning of any event.

**3:2 Licensing:** No registered representative shall solicit or receive accounts or orders from any person unless the representative is first registered or licensed in the state in which such person resides or is located, unless a Home Office senior principal approves such action.

**3:3 Fingerprinting:** PICI does not do in-house fingerprinting. Registered representatives are provided a FINRA specific fingerprint card and must go to their local law enforcement agency to have their prints processed. Any fees incurred are the responsibility of the registered person.

**3:4 Sole Registration:** The firm does not generally permit dual registration. No representative of PICI shall at any time represent any other broker dealer or issuer of securities. When a representative terminates their association, they shall notify PICI immediately.

**3:5 Personal/Related Accounts and Trading:** The firm permits with prior written permission of the Home Office, registered representatives to maintain a securities account with an outside broker-dealer. The firm requires duplicate statements and confirms (if applicable) be sent to the Home Office for review. Representatives must observe principles of conduct stated in the manual and elsewhere when transacting business for themselves. Representatives are prohibited from effecting transactions based on knowledge of material and non-public information.

**3:6 Outside Business Activity:** No persons associated with PICI in any registered capacity shall be employed by, contracted to or compensated by or from any other person as a result of any business activity outside the scope of the relationship with PICI unless they have submitted written notice to the firm. Annual review performed with compliance program.

**3:7 Private Securities Transactions:** Prior to participating in any private securities transaction, any associated person shall provide the proper documentation to PICI describing in detail the proposed transaction, proposed role and whether they have received or will receive selling compensation in connection with the transaction. Participation in a private transaction requires the written approval of a Home Office senior principal regardless of compensation or not. If compensated, the transaction shall be recorded on the books and records of the firm and the firm shall supervise the person's participation in the transaction. Unauthorized transactions are grounds for termination.

**3:8 Free Riding and Withholding:** the free-riding and withholding rules state that members of FINRA may not withhold "hot issue" securities for:

- Any of the members accounts or any other member firm
- An officer, director, partner, associate or agent of the member firm or any other member firm, including their immediate families

There is an exception the free-riding and withholding rule for family members of associates of member firms. To qualify for the exception, the buyer and the firm must comply with the following rules:

- Members can sell only an insubstantial amount to the accounts. The amount sold to any one account may not be excessive.
- The securities must be purchased for investment purposes (long term). They cannot be sold for an immediate profit.
- The securities must be in line with the purchaser's normal investment practice.

PICI representatives must have prior written approval in advance of the purchase of any securities which could be considered "hot issues".

**3:9 Professional Responsibility:** Each associated person of PICI shall conduct themselves in accordance with the highest standards of professional responsibility. Each associate shall engage in business activities in conformity with the statutes, rules and regulations of the SEC and each state in which PICI and its representatives are licensed or registered, the NASD Rules of Fair Practice and the provisions of this manual.

**3:10 Receipt of Non-Cash Compensation, Sales Incentives, Gifts and Gratuities:** Non-cash compensation, sales incentives, gifts and gratuity items (including travel bonuses, prizes, and awards offered by any sponsor or program) CANNOT BE PAID DIRECTLY to any associated person of PICI. The Firm, itself, however, is permitted to provide non-cash compensation to its Representatives provided no sponsor, affiliate of a sponsor, or program, including an affiliate, directly or indirectly participates or contributes to providing such non-cash compensation. Note: the firm does not participate in such activity.

All compensation to be received by an associated person that is related to their securities activities or association with the Firm must be paid directly to PICI. PICI shall control distribution of compensation to the associated person and will record the receipt and distribution in its books and records.

Consolidated FINRA Rule 3220 permits associated persons to give or receive gifts that do not exceed an aggregate annual amount of \$100 per person per year. In addition, personal gifts such as wedding, birthday, anniversary or gifts related to other special occasions and de minimis or promotional items with a nominal value are exempted from the Rule. Items that are valued at or near \$100, even if promotional in nature, would not be considered nominal and would need to be included in the aggregate annual value of gifts. All gifts must be reported to the home office.

**3:11 Compliance Meeting:** Each associate of the firm is required to participate in the firm's annual compliance meeting as an element of the firm's continuing education program.

**3:12 Firm Element – Continuing Education:** PICI developed its own continuing education program due to the diverse business mix of its representatives. The firm combined several compliance requirements into its Annual Compliance Certification.

Elements of this program consist of:

- Annual Compliance Certification – acknowledge and attest to regulatory required compliance questions and statements; verify personal, contact and equipment information and agree to various items of compliance nature.
- Annual Compliance Meeting – the firm produces a power point presentation that has review questions upon completion that are submitted to the firm electronically for acknowledgement of participation in the meeting.
- Form U4 Review – the firm provides each register person with a snapshot of their Form U4 to review for any updates, changes or corrections to existing information.
- Outside Business Activity review – the Form U4 snapshot provides current OBA. If any updates are to be made, representatives complete the firms OBS form and Home Office senior principals update CRD.
- PICI Compliance Review – the firm produces a quarterly (quarters may be combined) publication that provides updates to regulatory items, clearing firm items, political and rule items, AML items, firm changes, etc. All associates are required to read all material presented and acknowledge accordingly.

**3:13 Regulatory Element – Continuing Education:** PICI relies on information provided by FINRA (CRD) regarding the personnel that are required to sit for the regulatory element CE session. When PICI receives notification (sent by FINRA 30 days after window opens) they notify the registered person until such time that the session is completed. FINRA provides online access to comply with their regulatory element. A representative logs on to FINRA's website from their computer and completes the program without the use of a testing facility. The firm is notified of complete via email.

If FINRA CE is not completed by window end date, PICI will notify the representative who will be forbidden to do any securities business and shall not receive any compensation during this time until they complete the required CE session.

**3:14 Termination of Registration; Continuing Commissions:** Any registered representative may resign at any time voluntarily as a FINRA associated person of the firm, subject to the provisions of the independent contract between the representative and the firm. Written notice must be provided to the Home Office. The firm may terminate a registered representative at any time, with or without prior notice subject to the provisions of the independent contract between the representative and the firm.

Within 30 days of termination or resignation of a registered person, the Firm's home office senior principal is required to electronically file notice with FINRA on Form U5 disclosing the reasons for termination. Upon receipt of Form U5 in

proper order, FINRA will amend the CRD record of the Representative to reflect the termination. Within 30 days of filing the Form U5, the Representative must be provided with a copy of their Form U5. The Home Office will ensure that a copy of the submitted U5 and evidence it was sent to the individual is maintained in the terminated representative file.

FINRA Rule IM-2420-2 allows the Firm to pay continuing commissions to persons who remain registered representatives and, after they cease to be registered, such persons, their beneficiaries or their estates provided that there is in existence a bona-fide contract for such payment. No arrangement shall cover the solicitation of new business or the opening of new accounts. The provisions of the Rule should be consulted before any arrangements are entered into.

## SECTION 4 CUSTOMER ACCOUNTS

**4:1 Know Your Customer:** The Firm, when opening and maintaining customer accounts, must comply with FINRA's Know Your Customer Rule 2090. Associated persons must use reasonable diligence in order to know the essential facts concerning every customer. Each representative shall be responsible for obtaining and recording sufficient information about their customer and verify that information. The information obtained should be, in all cases, name, address, date of birth, social security number, place of employment, position, annual income, net worth, objectives and bank or other business reference. No order shall be taken from a customer unless the financial condition of that customer has been examined with respect to the relative risk of the investment. PICI must furnish a copy of the account record to the customer within 30 days of account opening and verify every 36 months thereafter.

No account shall be accepted by a representative where the customer refuses to provide information necessary to open an account. In addition, accounts may not be opened for persons under the age of 18 or otherwise legally incompetent except by a duly constituted legal guardian or attorney-in-fact. Margin accounts shall not be opened for administrators, custodians, executors, guardians or trustees, without prior approval of Home Office senior principal.

When doing business with overseas customers, it is important to adhere to the Firm's AML procedures and policy relating to politically-exposed persons and foreign officials, among others. "Knowing your customer" also includes determining whether or not they fall into these categories that require further due diligence and possible additional activity monitoring.

**4:2 Types of Accounts:** The following types of accounts may be opened with PICI: cash accounts, margin accounts, joint account, custodian account, estate account, options account, partnership account, trust account, ERISA-type accounts, and on a limited basis discretionary accounts. The type of account desired by a customer shall be recorded on the customer new account form.

Cash accounts shall be opened for customers who wish to effect bona fide cash transactions in securities. A cash transaction is one in which the customer agrees to make full cash payment or purchased within trade/settlement following the transactions and not to sell the security prior to making such payment. IF the customer is unable to make payment for purchase in their cash account within the maximum day limit of Reg T, PICI must cancel or liquidate the transaction, unless an extension of time is sought and obtained for extraordinary reasons.

**4:3 New Account Forms:** Each representative is responsible for obtaining and completing customer new account forms for the purpose of permitting the firm to render prompt and efficient service to the customer and to comply with state and federal regulatory requirements. PICI and its clearing firm's new account forms are to include all pertinent customer information that is required. Each new account is reviewed by the representative, their branch manager and/or OSJ manager and final approval is given by the Home Office by a senior principal prior to initial transaction occurring.

**4:4 Margin Accounts:** The Firm offers margin accounts to its customers, however, as it is a fully-disclosed introducing firm, it is the Firm's clearing firm that is extending credit to its customers.

To open a margin account, the client must sign a margin agreement which is a section of the new account document. This agreement states the rules the customer must follow and allows the clearing firm to hypothecate, or pledge the customer's securities, at the bank to secure the call loan. The Firm may hypothecate securities equal to 140% of the customer's debit balance; however, the Firm may borrow only an amount equal to the debit balance. Securities exceeding the 140% figure should be segregated. All margin account securities shall be held in the "street name" of the Firm (or Firm's clearing firm, if applicable) so that it may sell them if the customer cannot meet the margin call.

Trust accounts, estate accounts and other legally created entities may not maintain margin accounts unless the documentation (i.e., trust indentures, wills and corporate resolutions) specifically permit margin transactions. A margin account for any such entity may not be opened unless it is approved in writing by the designated Principal. Short sales in any such account also require the prior written approval of the designated Principal. Custodian accounts for the benefit of a minor or pension or profit-sharing accounts must not, in any case, be maintained on margin. The specific written approval of the designated Principal is required to establish margin accounts for securities industry associates.

**4:5 Discretionary Accounts:** A discretionary account is any account in which a person other than the named accountholder has the power to execute transactions in the account. This power could arise because of a power of attorney, trust agreement, advisory or management agreement or other document. Registered Representatives should take great care to be aware of the discretionary nature of certain relationships and be clear about them both with the customer and with the Firm.

Discretion is the entering of an order by a registered representative without prior specific instructions from the customer. In order for a trade to be considered discretionary, the rep must have the power to determine the following factors:

1. Which security to purchase or sell
2. The amount of the security to be purchased or sold
3. When the security will be purchased or sold
4. The price at which the security will be purchased or sold

The requirements of this section will not apply if the rep has only discretion to time and price. All proposed discretionary accounts should be approved in advance with the designated Principal. The NAF must contain the dated, manual signature of each named, natural person authorized to exercise discretion in the account. If there is more than one, the NAF should identify all such holders of discretion and include their dated signatures. No rep shall exercise any discretionary power in a customer's account unless such customer has given prior written authorization to the rep and the account has been accepted in writing by the firm.

The designated principal shall have the right to place any necessary limits on the discretionary accounts of the firm's reps and may withdraw approval at any time.

**4:6 ACATS:** The Firm does not hold customer accounts or assets. Therefore, its clearing firm will ensure that assets are transferred in accordance with applicable rules and standards. In the event the clearing firm is unable to comply with the customer's request, the designated Principal will receive notification from the clearing firm as to any problems with the request. The designated Principal, and/or the representative for the customer, shall contact the customer to resolve any problems or concerns and will forward corrected instructions to the clearing firm. The registered representatives

shall monitor transfers into or out of accounts held by the Firm's customers to ensure that transfers occur within applicable time frames and will work directly with the Home Office and/or clearing firm to resolve any issues.

**4:7 Customer Account Changes:** Customer account changes should always be brought to the attention of the home office principal. Should a Registered Representative receive notice of a customer's address change, the RR must furnish an updated account information change form to the customer for signature. Complete form should be sent to the home office for updating. The firm's clearing firm will furnish the updated account information to the customer within 30 days of updating the records. Revised account records will be sent to the customer's former address by our clearing firm and need not contain the customer's tax ID number or date of birth.

Ordinarily, it is unacceptable for a customer to change an address to a P.O. Box or other location not indicative of the customer's true street. In accordance with FinCEN guidance, P.O. Boxes used by participants in Address Confidentiality Programs (ACP) are acceptable provided that the Firm also obtains the street address for the state agency or organization through which the program is administered. This street address shall serve as the physical location of the individual in the ACP.

In the event mail is returned after delivery attempt (for instance, as "undeliverable"), the representative on the account or the Home Office will attempt to contact the customer to investigate, and should follow address change procedures if required.

**4:8 Customer Account Statements:** Pursuant to Rule 2340 of FINRA Conduct Rules, the Firm's clearing firm, on behalf of the Firm, provides no less frequently than each calendar quarter a customer account statement showing securities positions, money balances and account activity during the period. The Firm receives copies of customer statements monthly on CD-ROM and online through their system, for review and to meet regulatory requests for such records.

**4:9 Online Accounts Access:** The Firm's website provides to its customers a link to its clearing firm's proprietary online account access system for reviews of account holdings and activities; customers may not set up online accounts or conduct trading on this site. The Firm does not maintain or control this website in any way and therefore has no included online account approval procedures here.

**4:10 Day Trading:** Day trading is the process whereby investors aggressively attempt to profit from intra-day price movements in securities. The ability to engage effectively in "day trading" requires not only sufficient capital but also a sophisticated understanding of securities markets and trading techniques. Day trading rules (see Consolidated FINRA Rule 4210(f)(8)(B)) define terms related to day trading, including day-trading buying power. The firm does not allow its customers to participate in day trading.

**4:11 Death:** Death of a customer automatically freezes all activity in the customer's individual accounts and joint accounts without rights of survivorship until such time as letters testamentary or other evidence of authorization by an executor are presented. Death of a customer should be immediately brought to the attention of the home office.

**4:12 Financial Exploitation of Specified Adults:** Consolidated FINRA Rule 2165 establishes procedures a firm may implement in trying to prevent the financial exploitation of specified adults who are defined as;

- A natural person who is 65 years of age or older, or
- A natural person who is 18 years or older who the firm believes through its business relationship has a mental or physical impairment that renders them unable to protect their own interests.

While the rule does not require a firm to do so, it allows a firm to place a temporary hold on a disbursement of funds or securities as a safe harbor to the firm and its associates from other applicable rules relative to the delivery of funds and

securities when a temporary hold is put in place. A firm may place a temporary hold on a disbursement from the account of a specified adult if the firm:

- Reasonably believes that financial exploitation of the specified adult has occurred, is occurring, has been or will be attempted;
- Provides an oral or written notification within two business days after the date of the temporary hold on the disbursement is placed and that the reasons for the temporary hold to:
  - o All parties authorized to transact business on the account unless a party is unavailable or the firm reasonably believes the party has engaged, is or will be engaged in the financial exploitation of the specified adult;
  - o The Trusted Contact Person, unless the Trusted Contact Person is unavailable or the firm reasonably believes the party has engaged, is or will be engaged in the financial exploitation of the specified adult;
- Immediately initiate an internal review of the possible financial exploitation of the specified adult.

A temporary hold will expire no later than 15 days after it was placed unless terminated or extended by a state regulator or an agency or court of competent jurisdiction. If the firm's review supports the reasonable belief that financial exploitation has occurred, is occurring has been attempted or will be attempted, the temporary hold may be extended for up to an additional 10 days, unless terminated or extended by a state regulator or an agency or court of competent jurisdiction. The CCO or CEO is authorized to place, terminate or extend a temporary hold on behalf of the firm.

The CCO shall be required to ensure the firm maintains records related to compliance with this rule in the event a temporary hold is placed on specified adults account to include:

- The request for disbursement in question of financial exploitation
- The finding of a reasonable belief of financial exploitation
- Name and title of person authorizing temporary hold (only CCO & CEO)
- Notification to relevant parties
- The internal review of facts and circumstances and results

**4:13 Trusted Contact Person:** Amendments to Consolidated FINRA Rule 4512 requires the firm make a reasonable attempt to obtain the name and contact information of a trusted contact person at the time of account opening for non-institutional accounts. A trusted contact person is someone who is 18 years of age or older and can be contacted about the customer's account. The firm's Customer Information Brochure contains the following disclosure that is provided to the account holder at the time the account is opened:

By providing a trusted contact person and their information, you are authorizing the firm and its associates:

- to contact the trusted contact person and disclose information about the customer's account to address possible financial exploitation,
- to confirm the specifics of the customer's current contact information, health status, or the identity of any legal guardian, executor, trustee or holder of a power of attorney, or
- As otherwise permitted by Rule

The absence of the name or contact information for a trusted contact person shall not prevent the firm from opening or maintaining an account for the customer provided the company makes a reasonable effort to obtain trusted contact information.

## SECTION 5 TRADING PROCEDURES

**5:1 Order Tickets:** Order tickets must contain the following information: account registration, registered representative assigned to the account, person who took the order, person who processed the order, whether it is a discretionary trade, time of execution, time of entry, and time the order was taken. All order tickets will be reviewed with the daily blotter by a senior home office principal.

## 5:2 Discretionary Trades

**5:2:1 Transaction Approval and Review:** Rule 3010 of the FINRA Rules of Fair Practice states that members “shall approve promptly in writing each discretionary order entered.” Voice approval is not sufficient.

Every order ticket for a trade in a discretionary account must be marked as discretionary, and only after a trading authorization form has been signed by the customer. The designated principal will assure that the proper written authorization has been obtained from each customer, prior to the acceptance of the account for discretionary trading. Their review and signature will represent the firm’s acceptance of the account.

The senior home office principal will approve and initial each order ticket on the day the order is entered. Copies of monthly statements of all discretionary accounts will be reviewed and noted by the designated principal. The firm does not encourage the opening of discretionary accounts and such accounts will be approved on a limited basis.

**5:2:2 Prohibited Practices:** Discretionary accounts may not be opened for Pension, Profit Sharing and related plans. Under the Associate Retirement Income and Security Act, (ERISA), individuals who execute transactions for pension, profit sharing and related plans on a discretionary basis are subject to certain fiduciary obligations. These duties include, among other things, the responsibility to act with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man in a like capacity and familiar with such matters would use, diversification of investments in the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so, and following the documents and instruments governing the plan.

These obligations and other requirements under the Act are very important and must be scrupulously followed. Under no circumstances will the firm execute discretionary transactions with pension, profit sharing and related plans.

**5:3 Agency Cross Transactions:** All agency cross transactions are reviewed and approved by a senior home office principal. Rep must determine fair trade price by obtaining multiple quotes.

**5:4 Best Execution:** HTS posts on their website quarterly, a disclosure of order routing practices. We will review this report quarterly.

**5:5 Blue Sky Clearance:** It is unlawful for either the firm or its representatives to recommend, offer to sell, or sell to a customer any security that is unregistered and not properly exempt from registration in the state in which the customer resides or is located. Therefore, each representative of PICI shall ascertain, prior to making any recommendation or solicitation, and prior to making any offer to sell, or the sale of, any security, whether that security may be lawfully offered and sold in the state in which the customer resides or is located. No transaction shall be executed by a representative unless/until this information is obtained and verified. The Home Office shall respond promptly to inquiries by the firm’s representatives concerning the registration status of any security.

**5:6 Advertising:** All advertising used or distributed by or on behalf of PICI and/or its representatives shall be approved prior to use, by the firm’s senior home office principal. The Compliance Officer shall be responsible for filing any such advertising when required by law to be filed with one or more regulatory agencies prior to use. Advertising means any circular, prospectus, advertisement, or other material, or any communication by radio, television, pictures or similar means used in connection with a sale or purchase or an offer to sell or purchase any security. No representative may use any materials, documents or sales literature in connection with their activities as a representative for PICI that contains any false or misleading statements. A separate file of all advertisements and sales literature, including the



name(s) of the person(s) who prepared them and/or approved their use, shall be maintained for a period of three years from the date of each use.

**5:7 Electronic Communications.** As with any public communication, advertising electronically is subject to the approval, recordkeeping and filing requirements of the Rules of Fair Practice. Any e-mail used in lieu of written correspondence pertaining to the solicitation or execution of securities transactions must be reviewed and endorsed by a home office principal and must comply with the content standards included in Article III, Section 35 of the Rules of Fair Practice. Communications posted on electronic bulletin boards is considered advertising and must be pre-approved by a home office principal. An identical electronic message (group electronic mail) sent to multiple individuals is considered sales literature and must be pre-approved by a registered principal (sales literature includes form letters, brochures, research reports and market commentary).

**5:8 New Issues:** In connection with the offer and sale of securities which are part of an initial offering or new issue, a representative of PICI shall clearly inform the customer as to the nature of the offering and the fact (if such is the case) that PICI will be taking a mark-up. No representative of this firm shall tell any customer that such a security may be purchased with no commission or no sales charge, without also informing the customer that PICI and the representative will be compensated on the basis of a profit or mark-up realized in selling the customer a security owned by the firm.

**5:9 Riskless Principal Transactions:** The Firm acts as agent, and/or riskless principal in its transactions with customers. At or before completion of a securities transaction, customers must be advised as to the Firm's role in the transaction (i.e. agent or principal). In addition, the Firm's transaction documentation must disclose if it acted as agent for the parties on both sides of a transaction (due to the potential conflict of interest).

When acting as riskless principal, the Firm purchases a security from another firm or customer AFTER it has received an order for such security from its customer. It then sells the security to the customer. A riskless principal transaction is similar to an agency trade due to the fact that the Firm acts as an intermediary only and assumes no market risk. For the Firm's limited role in the transaction, it is compensated by a mark-up or markdown from its cost, based on the price paid to acquire the shares. For riskless principal transactions, the mark-up or markdown must be indicated on internal records and is generally disclosed to customers on confirms.

**5:10 Mark-up Policy:** As noted above, the Firm must adhere to the guidelines under Consolidated FINRA Rule 2121 when pricing securities. Mark-ups/downs in principal and riskless principal transactions in excess of 5% will generally be presumed to be unfair and unreasonable, however a mark-up above 5% may be justified upon a consideration of other permitted factors as described below. It is important to note that a pattern of 5% mark-ups (or downs), or even a pattern of mark-ups/downs less than 5%, may be considered unreasonable based on the circumstances.

It is the policy of PICI not to mark-up or mark-down municipal securities in excess of 2.5%. Any mark-ups in excess of 2.5% requested on trades must be pre-approved by the MSRB Principal of PICI.

**5:11 Approval of Orders:** Where any questions exists with respect to the appropriateness of an order, instructions relating to an order, Blue Sky clearance of the security, licensed status of the representative, suitability, or any other important factors, the Representative shall obtain prior approval of the order from the firm's home office senior principal.

**5:12 4145 Rule 2315 OTC Equity Securities:** This rule requires PICI to review current financial statements and material business information before recommending transactions in low-priced over-the-counter equity securities. All information will be reviewed by the firm's home office senior principal. This rule supplements existing federal and

FINRA rules. The rule applies to securities that are published in a quotation medium and are either (1) not listed on NASDAQ or a national securities exchange or (2) are listed on a regional securities exchange and do not qualify for dissemination of transaction reports via the Consolidated Tape. Current financial statements will include balance sheets, profit and loss statements, and publicly available financial statements and reports.

**5:13 Penny Stock Rule:** In compliance with SEC Rule 15c2-6, PICI requires that all transactions for customers purchasing designated securities be approved prior to placing an order.

Designated securities covered by this rule are equity securities issued by companies with less than \$2 million in net tangible assets. Transactions in which the price of the security is \$5 or more are exempt. Most penny stock companies are covered by this rule.

Transactions are exempt for non-solicited purchases, established customers and accredited investors. Transactions not meeting one of these exemptions must be discussed in advance with a home office principal and proof of suitability provided on a new account form which has a client signature authorizing the transaction.

All customers receive a copy of the SEC Penny Stock Disclosure statement (provided in our Customer Information Brochure) prior to the first penny stock transactions in their account. PICI requires the completion of its own penny stock documents. These disclosure documents shall not be altered in any manner.

**5:14 Execution:** PICI and its representatives shall comply with all rules and regulations as set forth under Reg. 240.15c3-1.2 of the Securities Exchange Act of 1934 regarding minimum net capital requirements for brokers who do not generally carry customers' accounts.

As a Fully Disclosed Dealer, PICI and its representatives do not receive or hold funds or securities of customers. All cash and securities need to be forwarded directly from the customer to our clearing firm, the mutual fund firm, or in the case of a limited partnership, to the escrow agent. All customers should be given clear instructions concerning where they need to send the cash or securities.

No customer checks should be made payable to PICI.

In the case of a certificate being sent to PICI or one of its branch offices by the customer against our instructions, the certificate will be logged in and immediately sent to our clearing firm. The customer should then be informed that the certificate has been forwarded and again given instructions for proper handling of certificates.

In the case of a customer's check being improperly made payable to PICI, the check should be immediately returned to the customer with instructions for writing a new check. If a check is payable to PICI and the client has a trade that is settling, we will forward the check to Hilltop Securities for deposit. A letter will be sent to the client informing them that the check was deposited, but in the future needs to be made payable to the clearing firm.

Forms are available to assist the customers in making a deposit of their funds or securities to our clearing broker. A suggested form letter is also available should a customer incorrectly send either to PICI.

PICI and its Representatives shall:

- a. Introduce and forward, as broker, all transactions and accounts of customers to firms clearing firm, Hilltop Securities, Inc. who carries such accounts on a fully disclosed basis and will promptly forward all of the funds and securities of customers received in connection with such activities as a broker;

- b. Participate, as broker or dealer, in underwritings on a “best efforts” or “all or none” basis in accordance with the provisions of 17 CFR 240. 15c2 4(b)(2) and promptly forward to an independent escrow agent customers’ checks, drafts, notes, or other evidences of indebtedness received in connection therewith which shall be made payable to such escrow agent;
- c. Promptly forward, as broker or dealer, subscriptions for securities to the issuer, underwriter, sponsor, or other distributor of such securities and receives checks, drafts, notes or other evidences of indebtedness payable solely to the issuer, underwriter, sponsor, or other distributor who delivers the securities purchased directly to the subscriber; or,
- d. Act as broker or dealer with respect to the purchase, sale and redemption of redeemable shares of registered investment companies or of interests or participation in insurance firm separate accounts, whether or not registered as an investment firm, and promptly transmit all funds and deliver all securities received in connection with such activities.

**5:15 Fails and Prepayment:** The firm’s home office personnel shall inform a representative on settlement day of any instance in which a customer has failed to remit funds or deliver securities. It shall be the responsibility of the representative to see that such funds or securities are received by the settlement day following the transaction. In the event an extension is requested, it must be approved by a senior home office principal. Customers are not entitled to receive the proceeds of a sale prior to the settlement date. However, where a customer may justify a prepayment, a representative may submit a request for prepayment which shall be reviewed by a senior home office principal.

#### **5:16 Payment checks**

PICI will not accept checks written on the accounts of representatives or other associates of the firm in payment of customer orders. Payments shall not be accepted by checks drawn on the account of any person other than the customer, or payable to anyone other than the firm’s clearing firm, without prior approval of a senior home office principal.

## **SECTION 6 INSIDER TRADING RULES**

**6:1 Insider Trading:** The Insider Trading and Securities Fraud Enforcement of 1988, required that every broker/dealer firm establish, maintain, and enforce procedures to detect and prevent misuse of materials, non-public information, by such broker/dealer or any person associated with the broker/dealer.

Insider trading is generally defined as trading in securities while in possession of material, non-public information, in violation of a fiduciary responsibility or trust.

**6:2 Who Is An Insider:** An insider is any person who might have access to non-public information about a corporation. A director or officer of a firm is an insider. Also someone owning 10% or more of the outstanding shares of a firm is an insider. If someone owns less than 10% of a corporation shares but is closely related to a 10% or more shareholder, that person is considered to be an insider.

PICI and the registered representative are responsible to determine whether a client is or is suspected to be an insider. Additionally, it is the responsibility of the firm and the registered representative to detect the communication of non-public, confidential, market sensitive information and monitor its dissemination. It is inappropriate to solicit an order on a basis of rumor or to circulate a rumor.

Inside information is material, non-public information concerning a publicly traded corporation or its securities.

Material information is any information which a reasonable investor may view as significant or important in making an investment decision. Therefore, material information could be any information that may effect, either positively or negatively, the market price of publicly traded securities. Examples of material information include, but are not limited to:

- Knowledge pertaining to future mergers or acquisitions
- Anticipated management changes
- Down-grades or up-grades in debt ratings
- Knowledge of important litigation
- Knowledge of future earnings announcements

All associates are required to fully comply with all insider trading laws and prohibitions. If any associate obtains inside information concerning a publicly traded firm, the associate shall not, under any circumstances, buy or sell securities of the firm or initiate any other action to take advantage of, improperly transmit, or otherwise misuse the inside information.

**6:3 Opening Accounts:** Upon opening an account for an insider or someone suspected to be an insider or when an existing client becomes an insider, the representative will notify a home office principal and notations will be made in the client's account.

**6:4 Review of Accounts:** A home office principal must review all account(s) of all representatives under their supervision. The home office principals will review the accounts that are through outside broker/dealers for all associates and registered representatives.

All trades made on behalf of individuals known to be or suspected of being insiders will be approved in advance by a home office principal. A list of securities known to be associated with or related to an insider will be scrutinized for detection of possible violation of the insider trading rules. The representatives of PICI will not use inside information which may be obtained from an insider client in any manner.

**6:5 Definition Chinese Wall Policy:** PICI has established rules and policies designed to prevent material non-public information obtained by PICI and individual agents and associates in the conduct of their securities business from becoming known to the trading personnel or other PICI associates and individual selling registered representatives prior to its public release, and to prevent such information from being used for insider trading.

**Chinese Wall Rules:**

1. PICI associates must not pass non-public information to trading personnel (including registered representatives) until its public release. This includes non-public financial information relating to restructuring, refinancing, mergers or acquisitions, new product discoveries and plans, plans for refunding bond issues, etc.
2. PICI and its agents and associates must keep files, financial statements and other written memoranda controlled until an appropriate announcement is made.
3. PICI is responsible for instructing their personnel on PICI's rules on this matter, and insuring their compliance with such rules. If an associate must be given material non-public information, the subject associate must be cautioned that such information is to be kept confidential. In addition, the home office principal must note in the file the name of the associate and the date the information was given.

4. PICI home office will monitor on any issues in which PICI is involved in a financing that requires placement of issuers names on the Restricted Trading List.
5. Each PICI agent and associate will be required to sign a statement reciting that they understand the Chinese Wall rules, and agree to conduct themselves in compliance with these rules. This is facilitated through the firm's Annual Compliance Certification.

## **SECTION 7 PROHIBITED PRACTICES**

**7:1 Borrowing or Lending:** No Representative of PICI shall borrow money or securities from, or lend money or securities to, a customer.

**7:2 Email:** The firm prohibits the use of any unauthorized email addresses for communication with clients. The firm hosts their firm email with Smarsh Technologies.

**7:3 Text Messages:** The firm prohibits the use of text messaging with clients unless prior arrangements are made to archive and retain all text messages for used phone number.

**7:4 Social Media:** No representative of PICI shall establish any site, page, blog, etc. in social media on behalf of or representing the firm in any way unless prior arrangements are made to archive and retain all social media pages.

**7:5 Acting as Custodian:** No Representative of PICI shall act as a custodian for the money, securities or an executed stock power of any customer.

**7:6 Undisclosed Transactions:** No Representative of PICI shall effect any securities transactions with or for a customer not recorded on the regular books or records of PICI.

**7:7 Fictitious Name:** No Representative of PICI shall effect transactions in securities for an account operating under a name known to the Representative to be fictitious, unless disclosed to, and permitted in writing by, the firm's home office principal.

**7:8 Sharing in Account:** No Representative of PICI shall share, directly or indirectly, in the profits or losses in the account of any customer.

**7:9 Splitting Commissions:** No Representative of PICI shall divide or otherwise split commissions, profits or other compensation receivable in connection with the purchase or sale of securities with any person not also licensed or registered as a Representative for PICI or an affiliate thereof without prior approval of the firm's senior home office principal.

**7:10 Business Advertising:** No Representative of PICI shall use advertising describing or relating to the Representative's securities business, unless the advertising clearly identifies the name and address of PICI and has been approved in advance by the firm's home office principal.

**7:11 Churning:** No Representative of PICI shall induce trading in a customer's account which is excessive in size or frequency in review of the financial resources and character of the account.

**7:12 Suitability:** No Representative of PICI shall recommend to a customer the purchase, sale or exchange of any security without reasonable grounds to believe that the recommendation is suitable for the customer on the basis of

information furnished by the customer after reasonable inquiry concerning the customer's investment objectives, financial situation and needs, and any other information known by the Representative.

**7:13 Unauthorized Transactions:** No Representative of PICI shall execute a transaction on behalf of a customer without proper authority to do so. In the case of a transaction for the account of a customer upon instructions from a third party, the Representative shall first obtain written authorization from the customer.

**7:14 Unregistered, Nonexempt Securities:** No Representative of PICI shall execute orders for the purchase by a customer of securities that are not properly registered, or exempt from registration, in the state in which the customer resides or is located.

**7:15 Financial Planner or Advisor:** No Representative of PICI shall identify himself, herself, or the firm as a financial or investment planner, consultant, or advisor, unless such description accurately reflects the person's qualifications and the nature of the services offered and has been authorized by the firm's senior home office principal.

**FINRA Rules:** No Representative of PICI shall violate any rule of the FINRA or any securities and exchange of which PICI is a member, with respect to any customer or transaction.

**7:16 Referrals:** No Representative of PICI shall recommend to a customer that the customer engage the services of any investment advisor that is not properly licensed or registered to transact business with that customer. In no event shall the Representative receive any fee or remuneration (other than directed business) from an investment advisor for making a referral.

**7:17 Investments of Liquefied Home Equity:** The Firm strictly prohibits its representatives from recommending securities investments using liquefied home equity (proceeds from refinancing's). However, if a representative has not recommended such a strategy, yet knows a customer's source of funds is liquefied equity, they are required to disclose the risks and assess the suitability of the transaction.

**7:18 Unlicensed Activity:** No Representative of PICI shall open a customer account, recommend a security, solicit the purchase or sale of a security, offer or sell a security, accept an order, or otherwise represent or transact business on behalf of PICI, to, from, for, or with respect of a customer residing or located in a state in which the Representative is not properly registered or licensed at the time, without the approval of the firm's home office principal. Licensing or registration of the Representative in such state will be undertaken by PICI upon the request of the Representative, at the Representative's expense.

**7:19 Mutual Fund and Variable Annuity Sales Practice:** All accounts will be reviewed on a regular basis for all accounts showing mutual fund and variable contract activity for the following problems: inappropriate switching, breakpoint sales, improper use of L.O.I., selling dividends, etc.

**7:20 Cold Calling:** While many consider the telephone as one of life's necessities, some feel it inconveniently intrudes. For some time, ordinary citizens have voiced concern about supper-time calls from people selling something or wanting an opinion. But they lacked recourse—until now.

On 12-20-1992, the Telephone Consumer Protection Act of 1991 (TCPA) took effect. This act—the first of its kind on the federal level—gives leverage to individuals who don't want to be solicited over the phone at their homes.

As one who contacts individuals and businesses on behalf of PICI it's important you know about this legislation and how it impacts you and our firm.

The TCPA establishes guidelines that businesses, their associates and associates must meet when using the phone. It also gives individual consumers a way to take action against businesses that violate the act. Violations can result in fines and lawsuits.

The TCPA addresses many aspects of telemarketing. It primarily focuses on calls made by businesses to individuals at their homes. It sets guidelines on such things as:

- When callers can call
- How callers identify themselves
- Using auto dialers, prerecorded voice messages and fax machines

In addition, it requires companies to set up and maintain a “Do Not Call” list and establish procedures for using it. PICI in compliance with the TCPA, has set up a “Do Not Call List” and established guidelines for using the phone in marketing activity. We believe our guidelines are generally consistent with those of other companies.

The following is a summary of our guidelines. Please follow them.

TELEPHONE CONSUMER PROTECTION ACT GUIDELINES	
These rules apply only to telephone sales solicitations. Generally, business-to-business calls are not affected. Also, the rules do not apply to service transactions, or written communications. More restrictive state laws may apply.	
Telephone Solicitation	You cannot call a residence to solicit between 9 p.m. and 8 a.m. (local time of the residence). When calling you must identify yourself, the firm you’re calling for, and the address or phone number where you can be reached.
Automatic Dialing Systems or Prerecorded Voice Machines	Using automatic (random or sequential) dialing systems or prerecorded voice machines in solicitations on behalf of PICI, Inc., is not permitted.
Fax Transmissions	Fax machines cannot be used to transmit advertising material—without prior consent or invitation. the date, time, sender and sender’s phone number must appear on each page or on a cover sheet for all faxes.
Do Not Call List	Consumers or clients may ask PICI Inc., not to solicit them by telephone. Under the TCPA, we must record these requests and honor them. This means unsolicited calls cannot be made to residential households on our “Do Not Call” list.  Certain exemptions apply.
Exemptions	“Do Not Call” provisions do not apply if calling someone with: Prior consent or invitation, or “An established relationship”—formed by a voluntary two-way communication on the basis of an inquiry, application, purchase or transaction regarding products or services, where there has not been a request that future telephone solicitations not be made.
Access to the “Do Not Call” List	Before you make a call which falls under these TCPA rules, please make sure the individual is not on our “Do Not Call” list.
Add to the “Do Not Call” List	If a person indicates he/she does not want any more telephone solicitation calls from PICI, please notify the PICI operations.
Questions	Questions about the law can be directed to your supervisory principal.

**7:21 Financial Exploitation of Specified Adults:** No Representative of PICI shall participate or willingly facilitate or aid in the financial exploitation of specified adults. It is the responsibility of every representative of PICI to alert the Home Office of any activity that could or might lead to the financial exploitation of specified adults.

## SECTION 8 REPRESENTATIVES RECORDS

**8:1 Customer New Account Form:** To comply with our responsibility to know our customers, as well as to provide recommendations regarding the purchase and sale of securities that are suitable in relation to our customers’ investment objectives and financial situation and needs, each representative of PICI is required to prepare and keep

current, a New Account Form setting forth basic information about the customer, including investment objectives. The New Account Form calls for information concerning the customer's annual income and net worth, which information is important in determining the suitability of investments for that account. If the customer refuses to provide such information upon request, however, a notation to that effect should be made on the form, and appropriate limitations with respect to the advice and recommendations given to such a customer should be observed. Every three years, the Representative should review with their customer the information on that customer's New Account Form to make certain of its current accuracy. In addition, the representative should familiarize themselves with that information on a periodic basis when servicing the account.

**8:2 Customer Holding Records:** Each Representative of PICI shall have access to Hilltop Securities, Inc. system which provides account holdings, activity, account agreements, and order activity. For accounts held outside of Hilltop Securities, Inc. (PICI's clearing firm), the firm shall keep current statements from companies and any outside custodians. Each representative shall provide the Home Office access to representative's DST account.

**8:3 Transaction Records:** Each Representative of PICI shall have access to all transactions by customers for the current year through Hilltop Securities, Inc. system which provides blotters and views and reports which includes all purchases and sales.

## **SECTION 9      FIRM RECORDS**

**9:1 Registered Representative Assignments:** PICI maintains a listing of registered representative assignments separately. This listing may be obtained from the CCO.

**9:2 Electronic Storage:** PICI maintains its firm/client records pursuant to Rule 17a-3 and 17a-4. The SEC and FINRA have issued general guidelines as to the use of electronic media for delivery of information to customers and recordkeeping. In accordance with these guidelines, the Firm expects to make use of electronic media to the extent appropriate in its business operations.

In general, required records may be maintained and stored electronically by the firm subject to the following conditions:

- Written records shall be maintained and stored where legally required (i.e. original customer signatures, cancelled checks or certificates, other documentation required to be available for legal, evidentiary purposes);
- The Firm shall maintain duplicate "backup" records in electronic form in a secure storage facility to guard against inadvertent erasures, casualties, theft, etc.; and
- Where required by regulatory policies and procedures, all such records shall be immediately accessible and capable of being downloaded and printed out for examination.

Client records are scanned and emailed via an encrypted and secure email for review and final transmission to firm's clearing firm and representative. Our clearing firm maintains all documents electronically in their system where firm's representatives have access to the system, but can make no changes or delete any files. Final approval scanning submitted by PICI home office to clearing firm via an encrypted and secure email for imaging into system.

**9:3 Annual Financial Reports:** PICI shall prepare or have prepared, annually, on a fiscal year basis, financial reports consisting of:

- Financial statements and supporting schedules as described in SEA Rule 17a-5(d)(2)
- A Compliance Report as described in SEA Rule 17a-5(d)(3)
- An Exemption Report as described in SEA Rule 17a-5(d)(4)



A report prepared by a PCAOB-registered independent public accountant covering each of the reports listed above; these reports must be created in accordance with PCAOB standards. The firm shall post on its public website the audited financial report.

Annual financial reports should be filed in the manner required by the recipients:

- The SEC now permits filings to be made either through the EDGAR system or in paper.
- FINRA requires electronic filings via Firm Gateway.
- SIPC permit filings to be made email, fax or in hard copy.
- Most states and other SROs required filings to be made in paper.

**9:4 Daily Blotter:** It is the policy of PICI to access and review a Daily Blotter setting forth an itemized record of all purchases and sales of securities, all receipts and deliveries of securities (including certificate numbers), all receipts and disbursements of cash, and all other debits and credits, relating to the Firm's business. The Blotter is produced by the firm's clearing firm and is to include the account for which each transaction was effected, the name and amount of securities, the unit and aggregate purchase or sale price (if any); the trade date, and the name or other designation of the person from whom purchased or received or to whom sold or delivered. The Daily Blotter is to be reviewed and by a senior home office principal on a regular basis to verify and cross check information concerning transactions effected by the Firm's Representatives and compliance with the requirements of this Manual.

Hilltop Securities, Inc., PICI's clearing firm, handles all cash disbursements from client accounts. A PICI senior home office principal is to process the checks/wires through the appropriate system and/or with the appropriate person named in the Hilltop Securities procedures manual. All requests are verified with the CSS system to ensure the appropriate funds were sent.

All transmittals of funds (e.g., wires or checks, etc.) or securities from customers to third party accounts (i.e., a transmittal that would result in a change of beneficial ownership); from customer accounts to outside entities (e.g., banks, investment companies, etc.); from customer accounts to locations other than a customer's primary residence (e.g., post office box, "in care of" accounts, alternate address, etc.); and between customers and registered representatives, including the hand-delivery of checks; will be monitored by a senior home office principal.

**9:5 Guarantees; Agreements; Powers of Attorney:** It is the policy of PICI, with respect to each account established and maintained with the Firm, that the file of the account shall include copies of all guarantees, all margin and lending agreements, and all powers of attorney and other evidence of the granting of any discretionary authority with respect to the account. In addition, in the case of joint, partnership, and corporate accounts, the file is to include the appropriate documents reflecting the identity and signature of persons authorized to transact business for the account.

**9:6 Customer Correspondence:** It is the policy of PICI to maintain a paper file and/or an electronic file containing copies of all branch office communications, correspondence and other messages from customers (except customer complaints) relating to the securities transactions effected and any other business matters with respect to all accounts of the Firm. Any correspondence received by a branch office is transmitted monthly for review via email. Any correspondence from a Representative to a customer or potential customer is to be approved promptly by the Principal Officer or a designee.

**9:7 Email Correspondence:** PICI uses Smarsh Technologies for hosting and archiving email. Email will be reviewed by a senior home office principal by either a random sampling or need based. The firm may utilize either Smarsh's website for reviewing or the firm may review the CD produced by Smarsh and mailed to the firm. Email is reviewed no less than quarterly.

**9:8 Internal Correspondence:** It is the policy of PICI to maintain a paper file and/or an electronic file containing copies of all internal business communications and correspondence. This correspondence shall be kept for a period of three years.

**9:9 Customer Complaints:** It is the policy of PICI to maintain a separate file for all complaints made or submitted by customers to the Firm or its Representatives relating to securities transactions. Complaint includes any written or oral statement of a customer, or person acting on behalf of a customer, alleging a grievance involving the activities of persons under the control of PICI in connection with the solicitation or execution of any securities transaction or the disposition of securities or funds of that customer. Any Representative who receives a customer complaint shall immediately report and/or deliver such complaint to a home office senior principal.

Effective 10/1/95, an amendment to Article III of the FINRA's Rules of Fair Practice requires member firms to report to the FINRA the occurrence of 10 specific events, called disclosure events immediately and also report on a quarterly basis any complaints that do not fall under these 10 events. The disclosure events include securities law, rule, or regulation violation, customer complaint alleging theft, misappropriation of funds or securities and forgery, regulatory or self-regulatory proceeding, regulatory or self-regulatory membership, criminal offense, association with investment firm that had its registration denied or revoked by any agency, jurisdiction or organization, civil litigation or arbitration, damages claim, statutory disqualification, and disciplinary action. All registered representatives involved in any of the above will notify the home office immediately.

**9:10 Advertising:** It is the policy of PICI to maintain in a separate file containing copies of all advertising published or circulated by the Firm in the conduct of its securities business. Advertising means any circular, prospectus, advertisement, or other material or any communication by radio, television, pictures, or similar means used in connection with a sale or purchase or an offer to sell or purchase, any security.

**9:11 Private Placements:** It is the policy of PICI to maintain in its home office a register relating to each offering of securities in which the Firm participated made in reliance on any exemption from registration for "private placements" or a similar exemption under the securities law of any state. The register shall include information disclosing the name and address of any offeree, the date the offer was made, the control number on any offering circular or other advertising material given to the offeree (if any), the names of persons making the offer, and the date of any sale as a result of the offer.

**9:12 Websites (Firm Maintained Sites):** The home office senior principal will create and monitor all websites (including testing of hyperlinks for correct destinations) on a regular basis to identify and correct any variances from Firm policies and procedures. The firm operates an information only public website. The firm does not allow online trading through its clearing firm.

**9:13 Business Continuity Plan:** The firm maintains its emergency preparedness plan under separate cover. All firm associates are encouraged to periodically review the plan in order to be prepared for unforeseen business disruptions.

**9:14 Offering Due Diligence:** Michael Jordan is the Due Diligence Officer for PICI. Each offering is reviewed by Michael Jordan for firm approval. Once offering is approved, ongoing due diligence shall be performed during entire offering period. All documents provided by the sponsor will be reviewed. The firm will review outside due diligence reports, at the initial approval and all updates made throughout the offering. All documents will be kept by offering in the home office.

During the ongoing review of the offering, if there are any red flags or issues discovered with the offering, the Home Office senior principals will take the appropriate actions depending on the circumstances.

**9:15 New Products Due Diligence:** All new products must be approved by the Due Diligence Officer before use. Representatives may propose new products for review. If approved, the Due Diligence Officer will notify the representatives. If there is any continuing education or other requirements associated with the new product, representatives will need to complete before they can sell the product.

**9:16 Review of Records and Surveillance:** Under the Firm's policy, it is the responsibility of the home office principals of PICI, or a designee, to review the records described in Representative Records section, evidencing such review their initials, and maintain surveillance to prevent and detect violations of the securities laws by the Firm or its Representatives. The home office principals are to review all customer new account forms and blotters on a regular basis, with special attention to transactions or business by representatives who are not properly licensed to service an account, as well as possible sales of unregistered, nonexempt securities. In addition, customer records are to be randomly checked, for the purpose of determining whether trading in any customer's account is excessive in size or frequency in view of the financial resources and character of the account. The Principal will monitor the activity in customer account noted or suspected to be insiders. Trading activity in securities, related to insiders, will be monitored to detect possible trading on non-public or insider information. To the extent the Firm's automated information system can be employed to prepare the records described above and assist in the review of those records, appropriate programming and procedures are to be employed.

**9:17 Clearing Firm Exception Reports:** The Firm should make use of available reports from the clearing/carrying firm to assist in its transaction and account monitoring. The clearing/carrying firm, at the commencement of the relationship and annually thereafter, must provide to the Firm a list of all available exception or other reports. After receiving the list, the Firm must promptly request the reports it requires. On or before July 1 of each year, the Firm's CEO and CCO should expect to receive from the clearing a written list of reports offered to, requested by and supplied to the Firm as of the date of the notice; FINRA will also receive this notice. The senior home office principals should review this information to determine if additional or replacement reports should be received to assist in monitoring.

**9:18 Records Retention:** PICI is required by law to preserve, for a period of not less than six years, all records described above and any other records required by law, except that the records required under section above regarding customer accounts, are to be preserved for a period of not less than six years after closing of the account.

**9:19 Account Reviews by Principals:** Monthly the firm will review accounts utilizing the compliance exception reports available. The principal will review any address or investment objectives changes daily. The Accounts Changed by Entity report will be run and reviewed by the home office principal noting any issues or discrepancies.

**9:20 Consolidated Account Statements:** The firm does not produce consolidated account statements. Should a client request a consolidated account statement, representative must prepare and present the consolidated statement to the home office for approval prior to use.

**9:21 Trading Authorities/POAs:** A blotter of trading authorities/POAs for each account in which discretionary power is exercised will be maintained.

**9:22 Personal Securities Transactions:** A blotter of personal securities accounts will be maintained for all representatives. Transactions are maintained and accessible through the clearing firm system.

**9:23 Privacy Policy:** Pursuant to Regulation S-P, it is the policy of PICI, Inc. to provide each new/prospective client with our privacy policy statement with the initial account opening documents. PICI makes its privacy policy available via its Customer Information Brochure (CIB) located on its public website. Additionally, each client must receive on an annual basis a copy of the privacy statement. Notice of location of our CIB will be provided to them via a statement on their quarter-end brokerage account through Hilltop Securities, Inc. Paper copy will be provided upon request.

Clients who do not have a brokerage account (and have only direct with fund holdings) will receive the privacy policy on an annual basis as well. Each client will receive a letter indicating the electronic location of the privacy statement (CIB) and it will be noted on representative's workbook blotter.

**9:24 AML-CIP and FCPA:** In accordance with Consolidated FINRA Rule 3310 and MSRB G-41, and in an effort to comply with the requirements under the USA PATRIOT Act (in particular, Section 352 of such Act), the Firm has established policies and procedures for the purpose of attempting to deter and detect money laundering activities by customers. The Firm's "Anti-Money Laundering Compliance Program" is not included herein; rather, it is maintained under separate cover. Every associate of the Firm is expected to be familiar with the policies and procedures described in the AML Program and to make reasonable efforts to comply with them. Failure to do so will result in disciplinary action and possible subsequent termination of employment.

In accordance with Section 326 of the USA PATRIOT Act, Registered Representatives are required to attempt to identify any person attempting to engage in transactions. The Firm's AML Program, under separate cover, provides detailed procedures related to this requirement.

Hand in hand with AML CIP efforts is attention to foreign customers and whether they fall into the definition of foreign official as described in the FCPA Policy herein. All new foreign customers must be vetted in an attempt to determine if this definition applies. Subsequent supervision by designated Principals of account activity and gifts/gratuities offered must be attuned to the requirements of the FCPA for the sake of identifying any violations.

**9:25 Foreign Corrupt Practices Act (FCPA) Policy:** It is the Firm's policy that it and all of its associated persons shall fully comply with all applicable provisions of the U.S. Foreign Corrupt Practices Act (the "FCPA"). While these procedures are designed for use by associated persons, this FCPA Policy also pertains to all of the Firm's officers, directors, associates, agents and stockholders who act on its behalf. In general, the FCPA makes it unlawful to bribe foreign officials to obtain or retain business in a foreign country. The firm had established policies and procedures, under separate cover, for the purpose of attempting to deter corrupt practices.

**9:26 Reg. S-ID Identity Theft Prevention:** The Firm will comply with SEC's Regulation S-ID to the extent it is applicable to its business. The firm had established policies and procedures, under separate cover, for the purpose of attempting to deter and detect identity theft.

**9:27 Safeguarding Customer Records and Information:** The Firm has adopted the procedures in addition to those contained within its Identity Protection procedures to comply with Reg. S-ID and related state regulations regarding the protection of confidential client information and the reporting of breaches. These procedures are under separate cover, for the purpose of attempting to protect customer information.

**9:28 Outsourcing:** The Firm has contracted with outside vendors to perform certain required functions for the Firm—or, covered activities. FINRA defines "covered activities" as order taking, handling of customer funds and securities, and supervisory responsibilities under Rules 3110 and 3120.

The following information relates to these contracted services:

Vicki Di Palma	West Bend WI	Accounting Services	Started: September 2009
Smarsh Technologies	Seattle WA	Email Hosting & Archiving	Started: September 2008

## SECTION 10 REPORTING REQUIREMENTS

**10:1 Regulatory Reports:** It is the policy of PICI to file on a timely basis all reports, statements and forms required under the state and federal securities laws, including reports concerning the Firm's annual financial statement, net capital and aggregate indebtedness, material changes in its operation, and other matters. In this regard, all personnel of the firm are to bring to the immediate attention of the home office principals any matters that would require a report under paragraphs below.

**10:2 Criminal or Civil Complaints:** PICI is required by law to file with the appropriate regulatory authorities a copy of any criminal or civil complaint relating to its business, transactions or operations, naming PICI or any of its partners, officers or agents as defendants. Likewise, any complaint filed in connection with an administrative or disciplinary proceeding conducted by any public or private regulatory agency must be filed. Such a filing is to be made within 20 days of the date the complaint is served upon PICI or any of its Representatives.

**10:3 Notice of Securities Disappearance:** PICI is required by law to file with the appropriate regulatory authorities immediate telegraphic or written notice of the theft or mysterious disappearance of any significant amount of securities or funds, stating all material facts known concerning the theft or disappearance.

**10:4 Currency Transactions:** It is required under the currency and Foreign Transactions Reporting Act of 1970 that broker/dealers create records of currency transactions that may be useful in criminal, tax or other regulatory investigations. Representatives of PICI shall comply with the above mentioned act by notifying a principal officer of PICI and taking the following actions.

Within 15 days following the payment, receipt of transfer of currency of \$10,000 or more, a report must be filed with the Commissioner of the Internal Revenue Service (Department of the Treasury, IRS Form 4789 Currency Transaction Report).

Those who import or export currency or other monetary instruments in an aggregate amount exceeding \$5,000 and those who receive U.S. currency or other monetary instruments in an aggregate amount exceeding \$5,000, on any one occasion from any place outside the United States, are required to file reports with the Commissioner of Customs. In the case of the former, the report is generally required to be filed at the time of entry into the United States or at the time of departure, mailing or shipping from the United States. In the case of the latter, the report is to be filed within 30 days after receipt of the currency or other monetary instruments (Department of the Treasury, Customs Form 4790 Report of International Transportation of Currency of Monetary Instruments).

Any resident or citizen of the United States, or person doing business with the United States, having a financial interest in, or other authority over a bank, securities account or other financial account situated in a foreign country, must report that relationship as well as other pertinent information each calendar year on or before June 30. (Department of the Treasury Form 90 22. 1 Report of Foreign Bank and Financial Accounts).

## SECTION 11 DISTRIBUTION OF SUPERVISORY PROCEDURES

**11:1 Delivery to Representative:** It is the policy of PICI to deliver a copy of this Supervisory Procedures Manual to each Representative of the firm, who shall acknowledge receipt thereof via the Annual Compliance Certification. Delivery is in the form of a notice stating manual is available online on the firm's internal compliance website. Each Representative of PICI shall review this Manual at least annually.

**11:2 Retention:** A complete set of the supervisory procedures and system manual shall be on file and kept current at the PICI home office in Thief River Falls, Minnesota, and on the firm's internal compliance website.

**11:3 Additions and Amendment:** It is expected that additions and amendments to these procedures shall be made from time to time. All such additions and amendments must be approved by the firm's CCO, who shall have the responsibility of disseminating such changes to all affected associates. In the event that any such additions or amendments require an amendment to the firm's Form BD or other regulatory reports or filings, the CCO is to see that such requirements are observed.

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## **SECTION 12 PARTICULAR INVESTMENT PRODUCTS**

### **12:1 Mutual Funds**

**12:1:1 Introduction:** Mutual funds, for purposes of these policies and procedures, refer to open-end investment companies. RRs are responsible for recommending mutual fund transactions in compliance with these policies.

The home office senior principals are responsible for reviewing mutual fund transactions on a daily basis, taking the following areas into consideration.

**12:1:2 Breakpoints:** It is the home office principal's responsibility to review mutual fund purchase transactions on a daily basis. Resources available, but not limited to, are: Order tickets, Daily Blotter (transaction report). Evidence of review is noted on the compliance review cover letter.

The following action may be taken:

- Review mutual fund purchase transactions for potential breakpoint sales. Items to look for include:
  - Purchases near but below common breakpoint levels (\$25,000, \$50,000, \$100,000, etc.)
  - Multiple purchases of mutual funds that, if aggregated, would have qualified the customer for a breakpoint if one or fewer funds were purchased
- For purchases where it appears the customer would have been better served by purchasing an additional amount or where purchasing fewer funds would have qualified for the breakpoint:
  - Confer with the RR to determine the basis for the less than breakpoint purchases
  - If justified, send a letter to the customer to acknowledge their understanding that their purchase(s) did not qualify for a breakpoint
  - If not justified, contact the customer to suggest cancellation of one or more of the purchases or adding additional funds to qualify for a breakpoint
  - Correct transactions accordingly and take corrective action with the RR

For some mutual funds, front-end sales charges decrease as the dollar amount invested increases. These thresholds for reduced sales charges are called breakpoints. Breakpoint sales is a term that denotes selling mutual funds to maximize commissions earned, i.e., selling an amount close to but below a breakpoint. The customer will, therefore, pay a higher sales charge. This practice is prohibited.

Recommending diversification among several funds with similar investment objectives, particularly if sales occur in amounts just below the breakpoints of one or more funds sold, may not be in the best interests of the customer. If multiple purchases of different mutual funds are appropriate but will preclude the customer from qualifying for a breakpoint, the customer should sign a letter acknowledging their understanding that a breakpoint is being given up by purchasing multiple funds.

Note: While the clearing firm's system prompts representative for breakpoints, representatives are reminded to inquire with clients as to any other mutual funds they hold elsewhere that would affect their breakpoints.

**12:1:3 Letters Of Intent:** A letter of intent is an investor's written statement of intent to purchase a specified dollar amount of a single mutual fund or funds within a single fund group over a specific period of time. The aggregate investment over time may qualify for a breakpoint and a lower percentage sales charge.

The mutual fund purchase should indicate if the customer will execute a letter of intent so the lower sales charge will apply. The home office senior principal will be responsible for reviewing order tickets and daily blotters, as well as applications for indication whether a customer will sign a letter of intent. Evidence of review is noted on the compliance review cover letter.

**12:1:4 Rights Of Accumulation:** Aggregating purchases of a particular fund or family of funds by one investor (and sometimes family-related purchases) may qualify for rights of accumulation. A lower sales charge may apply based upon the total dollar amount invested.

The mutual fund purchase should indicate rights of accumulation if available and the customer's desire to aggregate purchases to qualify for a lower sales charge. ROA are limited to spouse and minor children living at same address.

The home office senior principal will review order tickets and daily blotters for indication whether customer will qualify for rights of accumulation. Evidence of review is noted on the compliance review cover letter.

**12:1:5 Switching:** Switching is the selling or redemption of one mutual fund with a sales charge to buy another mutual fund with a sales charge. Recommended switches may not be based on the compensation to be received by the RR or the Firm as a result of effecting the switch. As for all recommendations, the RR must have a reasonable basis for believing the switch is suitable for the customer.

The customer may incur multiple sales charges by changing from one fund to another and there may also be tax consequences because of the switch. The concern is whether the switch is justified and whether the customer understands the consequences of the switch.

Switches between mutual funds that result in potential additional sales charges for the customer (whether front-end or back-end load) require that a letter be obtained from the customer acknowledging an understanding of the consequences of the switch. It is the home office senior principal's responsibility to ensure switch letters are obtained for switch transactions. The letter will be retained with in a file for the customer.

It is the responsibility of the home office senior principal to review mutual fund orders for transactions where the customer sells one mutual fund to buy another mutual fund. When switching is identified, they will ensure the customer provides a signed switch letter. Order tickets and daily blotter will be reviewed for such activity. Evidence of review is noted on the compliance review cover letter.

**12:1:6 Mutual Fund Shares Classes:** All registered representatives must be aware of the choices of share classes available and what is in the best interests of their clients. The RR must consider the following:

1. Conscientiously learn about the choices a given fund offers.
2. Gather relevant information about the customer's intentions, such as length of time the customer will hold the fund and how much the investor intends to invest.
3. Analyze how the fund's various share classes would impact upon the customer's return on the investment and the liquidity of the investment.
4. Explain the available choices to the customer in a complete and forthright manner.
5. Make a recommendation based solely upon the customer's best interest.
6. When additional share classes become available to the firm through HTS or the client qualifies for a new share class, reps may initiate a share class conversion through HTS or directly at the fund firm. Reps are responsible for the accuracy and completeness of these conversions. Conversions should be reviewed in the systems to ensure they were completed correctly.

PICI has provided all registered representatives access to the FINRA Mutual Fund Expense Analyzer. Representatives must complete a B/C share disclosure form for all brokerage B and C shares purchases.

**12:1:7 Suitability:** FINRA Rules require that Registered Representatives inquire as to the suitability of a mutual funds transaction for a customer. The Representative should consider the customer's investment profile before making recommendations on particular funds. If the customer is making a selection of funds, the Representative must ensure that each fund, as well as all the funds in the selection, is suitable, and that the proportions are also suitable.

**12:1:8 Deferred Sales Charges:** If a customer purchases shares of a mutual fund that imposes a deferred sales charge on redemption, the confirmation will include the following legend: "On selling your shares, you may pay a sales charge. For the charge and other fees, see the prospectus."

**12:1:9 Selling Dividends:** Selling dividends is a practice of recommending the purchase of a mutual fund based on an imminent dividend distribution. Since the price of a mutual fund is reduced by the amount of the dividend, there is no benefit to the customer unless there are specific tax or other advantages to the customer. In fact, there may be increased tax liability for the investor. A related concern is representing that distributions of long term capital gains by the mutual fund are or could be viewed as part of the income yield from the mutual fund.

**12:1:10 Misrepresenting "No-Load" Funds:** Certain funds impose a sales charge when the customer redeems or liquidates an investment ("back-end load" or contingent deferred sales charge). These charges are generally on a decreasing basis the longer the mutual fund is held. For example, a mutual fund may charge 5% if the shares are sold prior to being held 5 years, 4% if after 5 but before 6 years, etc. Other funds have a combined asset-based sales charge and/or service fee exceeding .25 of 1% of average annual assets.

Mutual funds with back-end loads or asset-based sales or service fees exceeding .25 of 1% may not be sold as "no-load" funds.

**12:1:11 Suitability:** In the recommendation of mutual funds, the RR should match the customer's objectives with the stated objective and investment strategy of the recommended fund. It is the responsibility of the home office senior principal to review order tickets and daily blotter transactions for suitable mutual fund transactions with particular attention to the following:

- Review mutual fund transactions for suitability with particular attention to the following:



- Funds with high-risk objectives: Is the investment consistent with the customer's investment objectives?
- Purchasing multiple funds in different families that may result in higher sales charges: Is diversifying funds justifiable and does the customer understand the higher cost, if applicable?
- Confer with RRs regarding any transactions that raise questions

Follow up action may include:

- Requesting written acknowledgement from the customer that the higher costs are understood
- Canceling transactions that appear to be inappropriate

Evidence of review is noted on the compliance review cover letter.

**12:1:12 Correspondence:** Correspondence regarding mutual funds is subject to specific restrictions limiting what may be included since they are offered by prospectus. When reviewing correspondence regarding mutual funds, the home office senior principal should watch for the following in addition to the usual considerations when reviewing correspondence:

- Selling dividends (not permitted)
- Representing a back-end load fund as "no-load" (not permitted)
- Representing a fund with an asset-based sales or service fee exceeding .25 of 1% as "no-load" (not permitted)
- Representations regarding yield (there are specific requirements regarding quotation of yields; RRs should use materials provided by the fund or pre-approved by the Firm)
- Recommendations that include switching or appear to recommend unsuitable diversification among funds
- Letters that include excerpts from the prospectus that would be misleading when taken out of context
- Disclosures, as applicable (see explanation in the section titled "Disclosure of Material Facts")
- Performance is represented accurately and consistent with rule requirements regarding yield and return

RRs will include a prospectus. Home office principals review RR-generated correspondence to ensure language only indicates a prospectus is enclosed and the RR will call the customer to discuss the investment further.

**12:1:13 Disclosure Of Material Facts:** The FINRA has stated that there are material facts that should be disclosed to a customer when recommending a mutual fund. Items to be disclosed, if applicable or appropriate, include:

- The fund's investment objective
- The fund's portfolio
- Historical income or capital appreciation
- The fund's expense ratio and sales charges
- The fund's hedging or risk management strategy
- Information regarding the structure of multi-class and master-feeder funds sufficient so the customer may understand and evaluate the structure
- Potential tax consequences including tax on distributions and capital gains subject to tax
- Potential risks if a fund invests in financial derivatives
  - If an expense ratio is represented as an advantage of a particular fund, it is explained in the context of and compared with other mutual fund expense ratios

The mutual fund's prospectus and other sales literature generally include many if not most of these disclosures.

**12:1:14 Performance Information:** When presenting performance information, an explanation of total return should explain that total return measures overall performance while current yield represents only the interest or dividend paid by the fund. Where appropriate, RRs should explain the difference between return of principal and return on principal. When providing information regarding distribution rates, the RR is responsible for explaining the difference between distribution rate and current yield.

**12:1:15 Confirmation Disclosures:** For purchases of shares of an investment firm that charges a deferred sales charge upon redemption, FINRA rules prescribe that the confirmation is required to include a statement that states the following: "On selling your shares, you may pay a sales charge. For the charge and other fees, see the prospectus." The rule states that the legend must appear in at least 8-point type.

**12:1:16 Prospectuses:** RRs should provide a copy of the prospectus when recommending a mutual fund purchase to a customer.

A copy of the fund prospectus will be sent to each purchaser of a mutual fund. The home office is responsible for establishing procedures to ensure a prospectus is provided to each mutual fund purchaser.

**12:1:17 Advertising and Sales Literature:** There are specific requirements for advertising and sales literature regarding mutual funds. Advertising must be filed with the FINRA within prescribed periods. There also are mandated guidelines on representations regarding performance and yield. RRs may use materials provided by the fund. Any other advertising or sales literature must be approved by Compliance prior to use.

**12:1:18 Dealer-Use-Only Material:** Materials provided by fund distributors for dealer-use only may not be provided to customers and must not be displayed in a public area such as a reception area where customers obtain written information regarding investments. Dealer-use-only material is often provided as educational material for dealers and their RRs. There is no requirement to file this material with the FINRA because it is for internal use only.

All dealer-use-only material will be marked as such with limited distribution. Home office senior principals will review correspondence monthly to identify inclusion of restricted materials.

**12:1:19 Sales Contests:** The firm will not run or participate in any contest.

**12:1:20 Market Timing:** The firm will not engage or allow for market timing of mutual fund transactions.

**12:1:21 Redemption Of Outside Funds:** If the customer requests liquidation of an outside open-end mutual fund held by the fund, the RR should obtain the customer's signed letter authorizing liquidation. Required signature guarantees should be obtained from client prior to forwarding the letter to the fund. If the client has telephone redemption, the back office can process mutual fund liquidation by phone and fill out the MF Redemption Form. This form will be kept in the customer file. All telephone redemptions or exchanges must be taken and processed with the fund firm by 3:00 pm central time. Any order received after 3:00 pm central time, will be processed on the next business day.

## 12:2 OPTIONS

**12:2:1 Options General Procedures:** The rules of the Self-Regulatory Organizations (SRO's) require that each customer must be specifically approved for options trading prior to the time that the firm accepts an options order from the customer, and the rules set forth the steps that must be taken in connection with that approval. The fact that a customer had been approved for general securities transactions which may have included non-listed options transactions prior to the time that FINRA rules imposed a specific approval requirement for OTC options, is not sufficient to meet the requirements of these rules. Instead, even if an account has been previously approved for other types of securities transactions, it must be reevaluated and specifically approved for options transactions prior to accepting an option order from the customer.

A customer may be approved for one or more of the following types of options transactions:

Level 1 - Covered Call Writing – writing calls fully covered by underlying stock or security convertible into underlying stocks;

Level 2 - Level 1 plus buying calls and/or puts

Level 3 – Level 1 & 2 plus writing, spreads and straddles. Requires use of margin

Level 4 – Level 1, 2 & 3 plus uncovered call writing. Requires use of margin

However, a customer may not be approved for discretionary transactions.

Level 4 options trading requires a rep to be a registered options principal with the firm. The firm considers this type of strategy too risky and the liabilities too great.

A written record of the approval of every options customer must be maintained, noting the date the account was approved, and bearing the signature of the ROP who is responsible for options approval of the account. Information considered in approving an account for options transactions must be reflected in the agreements signed by the customer.

The requirement that all public customers must be specifically approved for options is intended to assure that we have exercised due diligence to determine that options transactions are appropriate for the customer in light of their investment objectives and financial situation, and that the customer has been made aware of the risks of options transactions. For these reasons, we are required to obtain specified minimum information concerning the customer's financial background and investment experience, and to provide the customer with a current OCC Document "Characteristics and Risks of Standardized Options".

With respect to accounts in which options trading authorizations have been granted to a third person who is not an associate of the firm, including a person acting on behalf of an investment partnership or an investment club, we must satisfy ourselves of the agent's authority to act and that such authority relates to options trading. Similarly, before approving accounts of trusts, pension funds, profit sharing plans, or other fiduciaries for options trading, we must satisfy ourselves that the instruments under which the fiduciary is acting permit options trading.

**12:2:2 New OCC Combined Options Disclosure Document:** The Options Clearing Corporation (OCC) and the various option exchanges have combined the four existing option Disclosure Documents ("Understanding the Risks and Use of Listed Options"; "Listed Options on Debt Instruments"; "Listed Options on Foreign Currencies"; and "Listed Options on Stock Indices") into a single booklet entitled "Characteristics and Risks of Standardized Options". This new document became effective on September 15, 1985.

We have posted a link to the disclosure document on our public website and representatives have access to print if client requires a paper copy. This assures that we have the most updated version available to all offices.

**12:2:3 Options Specific Procedures:** The following procedures are not to be taken lightly. They must be followed to the letter. Failure to comply with these procedures WILL result in a fine and/or permanent suspension from placing any future option orders. Options are considered to be very speculative and also very volatile; these requirements, therefore, are set forth for the mutual protection of both Polar Investment Counsel, Inc. and our customers. When an order is taken, you must check if it is an existing option account, or if it is the initial option trade for this customer. Unless this customer has been approved for options trading by the ROP the order WILL NOT be entered. Initial approvals for options trading can come only from the ROP.

The following information will be necessary for obtaining approval for each customer who wishes to transact business in option contracts.

1. Customer must have received the Characteristics and Risks of Standardized Options disclosure document prior to entering an option order. It must be indicated in the new account document, options approval area, that the customer has received and understands the Disclosure Document.
2. Before approval can be granted, we must have signed an on file:
  - New Account form
  - A margin and short account agreement (included in new account document)
3. There must be on file a completed option agreement (included in new account document).
4. Customers must be thoroughly reviewed for suitability, both financial and educational. The customer's net worth and the liquidity of his assets must be known in order to determine financial suitability.
5. No account may deal in options in any way without first signing an option agreement and having it approved by a ROP. Once approved, an account may trade only within the bounds set by the ROP. For example, if a client is approved for covered writing only, no purchase or uncovered writing is allowed. If an option agreement is returned to the representative because of investment objectives, the customer must approve any changes made in the investment objectives. This can be evidenced by having the customer initial any change.
6. If the customer has an existing account, their file should be reviewed in order to determine their investment needs and financial suitability for option trading. The customer must then be approved by the ROP and all documents submitted for final approval.
7. If any documents listed above are received incomplete, they will be returned to the representative and no activity will be permitted in options.
8. Only Representatives who have qualified either by passing the NYSE Series 7 exam, including puts and calls, or by taking and passing the separate put and call exam are authorized to enter options orders and/or introduce managed option accounts. Some option products, foreign currency, interest rate (debt) options and futures require separate exams. If in doubt, please check with the Registrations Department to see if the Representative is qualified for options.
9. Uncovered Call Options: (As specified previously)

In the event an order is entered and executed for a customer who has not been approved, the contract will be closed out the following day, and the net loss will be charged directly to the representative's net commissions. If the representative is unsure whether or not an account has been approved, the representative should check with the ROP, or the Home Office.

If an order is entered and executed for the sale of an uncovered call in an account that has not been approved for such activity, the call will be repurchased to close the position and any loss charged to the representative's net commissions.

**12:2:4 Customer Background & Financial Information:** The following is the minimum background and financial information that the Firm requires before approving a natural person customer (i.e., not a corporation or institution) for options. Ordinarily, this information must be asked for by the representative responsible for the customer's account. Although we request information in addition to the specified minimum, the following must be requested and is on the new account document:

1. Investment objectives, (e.g. safety of principal, income, growth, trading profits, speculations).
2. Employment status (name of employer, self-employed or retired). If retired, the name of the client's most recent employer.
3. Estimated annual income from all sources (including spouse, if married).
4. Estimated net worth (exclusive of family residence).
5. Estimated liquid net worth (cash, securities, other).
6. Marital status number of dependents.
7. Age.

8. Investment experience and knowledge (e. g. number of years, size, frequency and type of transactions for options, stock and bonds, commodities, other).

In addition to the foregoing, the customer's account records must contain the following information, if applicable:

1. Source or sources of background and financial information including the basis of any estimates made by the firm.
2. If the customer has granted discretionary trading authority to any person, a written agreement must be on file and the account records must show the name, relationship to customer and experience of the person holding discretionary trading authority.
3. The date the OCC Options Disclosure Document, as furnished to the customer and any other options disclosure documents that may be applicable.
4. The nature and type of transactions for which the account is approved (i.e., buying, covered writing, uncovered writing, spreading, and whether the account is discretionary).
5. Name of representative handling the account.
6. Name of ROP approving account and date of approval.
7. Dates of verification of currentness of account information (see below).

Since a written record of customer background and financial information must be maintained and in order to assure that all of the required information is asked for, it will be necessary to submit a signed and completed option agreement (included in new account document) for approval prior to engaging in any options activity. If a customer refuses to provide any of the required information this must be noted on the form before it is submitted for approval.

**12:2:5 Verification of Customer Background and Financial Information:** The Options Exchanges requires that the minimum required background and financial information obtained by the firm from a new customer must be sent to the customer for verification within 15 days after the customer has been approved for options. The customer must be given an opportunity to correct or complete the information. Therefore, a copy of the new account documents will be sent to the customer requesting verification or corrections. Additionally, if you become aware of any material change in a customer's financial situation, you are under obligation to send a copy of the new account document and financial information to the customer for updating. Whenever information is sent to a customer, absent from the customer to the contrary, we may consider the information in our file to be correct.

**12:2:6 Disclosure Documents:** Options issued by the Options Clearing Corporation (OCC), are registered under the Securities Act of 1933; the prospectus delivery requirements of the 1933 Act are therefore fully applicable to the offer and sale to customer of these options. Thus, at or prior to the time a customer's account is approved for transactions in any category of listed options (equity, index, foreign currency, debt, etc. ) the customer must be furnished a current copy of the Options Disclosure Document, of which the formal title is "Characteristics and Risks of Standardized Options".

If any PICI Representative conducts an options seminar, it is mandatory under SRO rules to deliver to each participant an Options Disclosure Document at the time such a seminar is held. This practice may also satisfy prospectus delivery requirements under the 1933 Act and SRO rules if the client is subsequently approved for options. However, we must be able to demonstrate satisfactorily that all persons attending such seminars received the Options Disclosure Document. This may be accomplished by preparing a list of persons who attended a conference or seminar, with verification of actual delivery of the Options Disclosure Document to all persons who attended.

**12:2:7 Options - Handling Customer's Options Transactions:** In general, the suitability rules of the SRO's provide that any time a person at a member firm recommends an option transaction to a customer, he must have reasonable grounds for believing that the recommended transaction is suitable for the customer.

Without limiting this general requirement that applies to all recommended options transactions, these rules also provide that no recommendation of an opening transaction in any option contract may be made unless the person making the recommendation has a reasonable basis for believing that the customer has such knowledge and experience in financial matters, and that he may reasonably be expected to be capable of evaluating the risks of the recommended position in the option contract. In order to supervise compliance with these rules, it is necessary to mark order tickets either "unsolicited" or "solicited". Determinations of suitability must be based upon information obtained in response to the inquiry of the customer concerning their investment objectives and financial situation, and other information actually known by the person making the recommendation.

Since the risks involved in the purchase of options depend upon such factors as the relationship between the option's exercise price and the market price of the underlying stock, the time period remaining until the option expires, price volatility and other characteristics of the underlying stock, such factors should be considered and brought to the attention of the customer in connection with making a recommendation.

**12:2:8 Index Options - Sales Practices:** Sales practice rules in regards to Index Options will be the same as those currently governing equity option trading. Some of these rules are:

1. Representatives who have passed the Series 7 Examination and are currently qualified to conduct a public business in equity options are qualified to service index options accounts.
2. Clients who have already been approved to trade in options will not need a separate approval to trade index options.
3. Clients who have not previously traded listed options or who do not have an option agreement on file with the Firm must fill out and sign a new option agreement. No trading will be permitted until the option agreement has been approved by the Senior Registered Options Principal (SROP) or the Registered Options Principal (ROP).
4. Each client, prior to the time his account engages in index options transactions, must receive a current copy of the Characteristics and Risks of Standardized Options.

**12:2:9 Index Options - Suitability Standards:** Suitability standards for index options will be the same as those in place for equity options trading, with one exception;

Those accounts approved for covered call writing and put writing to acquire stock will not be permitted to write index options without prior approval from the ROP. There are various conservative strategies that may be utilized for well diversified portfolios which may qualify some of these accounts for index option trading. However, we must have written approval from the client before we can allow any index option trading for these accounts.

**12:2:10 Permissible Investments For Fiduciary Accounts:**

**12:2:10:1 Pension and Profit Sharing:** No margin, futures, covered/uncovered options transaction, or any other transaction requiring an extension of credit is permissible in these accounts unless specifically authorized in the underlying instrument.

**12:2:10:2 IRA and Pension Accounts:**

- No margin, futures, uncovered options transaction, or any other transaction requiring the extension of credit is permissible in these accounts.
- Covered options writing is permissible only when authorized by the Trustee for the account.
- Trading options (i.e. buying long and selling) is considered highly speculative and is not permitted in these accounts.

### **12:2:10:3 Fiduciary Accounts Including Living and Testamentary Trusts, Estate, Custodial and Guardianship Accounts:**

#### **Living Trusts:**

- Covered option transactions will be permitted where they are either specifically authorized in the governing instrument or where we have a letter from the Grantor indicating that it was his intention for the Trustee's power to include such transactions.
- Uncovered options and futures transactions will be permitted only if specifically authorized in the underlying instrument or in a letter from the Grantor of the Trust. The same standard applies to the purchase of an option except where the transaction is being effected to close out an existing position. Opinions of counsel will not be accepted in lieu of specific authorization either in the instrument or by letter from the Grantor.
- Margin transactions other than those referred to above will be permitted only if specifically authorized in the underlying instrument, or if we are furnished with a letter from the Grantor indicating that it was his intention for the Trustee's power to include such transactions.

#### **Testamentary Trusts and Estates:**

- Covered options and margin transactions will be permitted only where specifically authorized in the underlying instrument, or where we are furnished with a well-reasoned opinion of counsel.
- Uncovered options and the purchase of options and futures transactions will be permitted only where specifically authorized in the instrument. Opinion of counsel will not be accepted.
- In an Administrator situation, where there is no will, none of the transactions referred to in 1 or 2 above will be permitted, as an Administrator's basic function is to liquidate and make distribution of the Estate. In any event, there is no underlying instrument which can authorize such transactions.

**Custodian and Guardianship Accounts:** None of the types of transactions discussed in this manual, including covered options transactions, will be permitted for these accounts (including Uniform Gift To Minor Accounts) which are subject to strict statutory guidelines.

**Amendments to Trust Documents:** Many pension and profit sharing plans do not specifically state they can invest in options and have margin accounts. As a result, we cannot permit any transactions other than those covered writing until we receive an amendment specifically authorizing such investments.

**Procedures for Senior Supervision of Customer Accounts:** Exchange rules require firms to maintain written procedures for the review of their option accounts. Polar Investment Counsel, Inc. not only requires that all options accounts be reviewed by the representative servicing the account but also that selected options accounts be reviewed on a random basis at the home office under the overall direction of the ROP.

The following are examples of the kinds of criteria that may be considered in selecting accounts for review.

1. With respect to margin accounts, an excess of a stated percentage increase in the debit balance compared to the previous month.
2. A decrease in total equity that has exceeded a stated percentage over the preceding one, three and six months.
3. Total commissions for one month that exceed a stated percentage of account equity.
4. Volume of option transactions effected in an account that appear to be excessive in comparison to the customer's financial resources.
5. Unusual patterns of trading.
6. Large or frequent margin Calls and Liquidations.

7. Extensions.
8. Other signs of apparent increase in the risk exposure of the accounts.

Once an account has been selected for review, it will be thoroughly examined, and any problems uncovered will be the subject of a special investigation. The disposition of all such investigations will be fully documented and maintained in a separate file for review during the next regular Exchange examination of the firm. Information concerning accounts selected for review will also be made available to the representative handling the accounts.

#### **12:2:11 Option Margin and Maintenance Requirements**

**12:2:11:1 Long Options:** Must be paid for in full, have no loan value and cannot be considered as equity in an account.

**12:2:11:2 Short Equity and Narrow Based (Industry) Index Options:** The initial requirement is 100% of the sale proceeds plus 20% of the underlying reduced by out of the money amount to not less than the premium plus 5%. The maintenance requirement is current premium plus 15% of underlying reduced by out of the money to not less than premium plus 5%. In addition, the minimum equity for an account doing uncovered equity puts is \$5,000.00. Firm policy does not permit the sale of uncovered equity calls. Minimum equity for an account doing uncovered index options is \$25,000.00.

**12:2:11:3 Short Broad Based Index Options:** The initial requirement is 100% of the sale proceeds plus 7 1/2% of the aggregate value of the underlying index (\$100 x index) reduced by out of the money amount to not less than premium plus 2%.

The maintenance requirement is 100% of the current premium plus 5% of the aggregate value of the index reduced by out of the money amount to not less than premium plus 2%. In addition, the minimum equity for an account doing uncovered indexes is \$25,000.00.

**12:2:11:4 Spreads (Long Side Cannot Expire Before Short):** Initial and Maintenance requirement is the amount by which a long Put (short call) aggregate exercise price is below the short Put (long call) aggregate exercise price; the long side must be paid for in full.

i.e.: Long Jul/30 call short Jul/25 call \$500.00 required or long Jul/70 put short Jul/80 put \$1,000.00 required. Spreads must be done in a margin account and are subject to the \$2,000.00 minimum equity rule.

**12:2:11:5 Options Exercises and Assignments:** All of the Firm's options trades are cleared through its clearing firm via CMTA (clearing member trade assignment). The Firm does not allocate exercise notices and therefore does not have procedures related to allocation. The Firm, in its agreement with its clearing firm, expects it to properly allocate exercise notices and complete all required disclosure/reporting associated with such allocations. The home office Principal will make sure that the Firm maintains work papers, exercise reports, etc., if received, relating to the allocation of exercise assignment and notices.

If a customer wishes to exercise a long option, the Representative should call the Trading Department, giving all information, which in turn will be transmitted to the Option Clearing Corporation. The Trading Department will notify the Representative the following day to confirm the execution that your option has been exercised.

Options are assigned on a random basis as outlined in the following section.



Every morning before 8:30 a.m. our clearing firm sends an email of all option assignments to the home office and representative servicing the account(s) so that they can cancel any orders that they may have entered to close out the position in the option. The representative contacts their customer. On call assignments, the customer must sell the stock. They can either deliver the stock from their long position or stay short. The representative should also notify the clearing firm at this time if there is a commission discount on the assignment. The P&S Department must have this information by noon in order to process the order ticket. If the assignment is a put, the customer must buy the stock. Assignments on short puts are always bought into the margin account.

Exercises or Assignments are always done by the Option Clearing Corporation after the close of trading for the day. Therefore, when the P&S Department calls the Representative on an assignment or exercise, the trade date is always the previous day. Settlement is regular way from that date rather than from the day we call the Representative. This is important to understand for dividend purposes, as your client may not be entitled to their dividend because of an assignment of a short call.

A confirmation of the trade will be mailed to the customer and to the branch on the day the Representative is notified of the Exercise of Assignment.

The procedures for exercising stock index options and for assignments of exercises are essentially the same as for stock options except for:

1. Settlement of index option exercises takes place on the business day following the day of exercise.
2. Exercises of index options are settled through the payment of cash rather than the delivery of securities. Cash settlement amount is the difference between the exercise price of the option and the current index value at the close of trading on the day of exercise, multiplied by the applicable index multiplier.

**12:2:11:6 Limitations on Exercise Options are exercisable at any time prior to their expiration, except as follows:**

1. Each of the Exchanges has advised the Clearing Corporation that it has established limits on the aggregate number of Options in each class which may be exercised by a holder or group of holders acting in concert within any five consecutive business days, and that under the rules of the Exchange, customers are required to agree not to violate such limits. Puts and calls covering the same underlying security are separate classes of Options, and are not aggregated for purposes of these limits. The exercise limits established by each exchange are 4,000 or 2,500 options for each class of Options, regardless of whether the Options were purchased on the same or different Exchanges or are held in one or more accounts or through one or more brokers. Any Exchange may establish different limits from time to time either across the board for all classes of Options traded on that Exchange or in respect to particular classes of Options. AMEX, MSE, PHLX, NYSE and PSE have further advised the Clearing Corporation that under their rules, exceptions may be made to their exercise limits in particular instances involving highly unusual circumstances. Representatives should determine the exercise limits to which they will be subject before engaging in an option transaction.
2. Each Exchange is empowered to restrict, wholly or partially, the exercise of particular Options within a class of Options traded on that Exchange, if in its judgment such action is advisable in the interest of maintaining a fair and orderly market in the Options or in the underlying security or securities, or is otherwise deemed advisable in the public interest or for the protection of investors. For the duration and to the extent of any such restrictions, the holder of an Option subject to such a restriction will be unable to exercise it in contravention thereof, if his position is maintained with a member of the exchange imposing the restriction. However, commencing ten business days prior to an Option's expiration, no such restriction will remain in effect.
3. The Clearing Corporation is also empowered to restrict the exercise of particular Options except during the ten business days prior to the Option's expiration. For the duration and to the extent of any restriction, the holder of such an Option will be unable to exercise it in contravention of the terms of the restrictions. During the ten

business days prior to an Option's expiration or thereafter, the Board of Directors may impose a restriction on delivery of underlying securities not owned by a writer of a call to whom an exercise notice is assigned or by a holder of a Put who has exercised it. In the event such a restriction is imposed on writers of Calls, the Clearing Corporation shall and in the event such a restriction is imposed on holder of Puts, the clearing Corporation may, fix a daily settlement value (which may be zero) for the option subject to the restriction, based on its then estimate of the value of the underlying security. If daily settlement values are fixed, the parties to the exercise will be obligated to pay and accept the settlement value fixed for the day the exercise notice is assigned, in lieu of receipt of delivery of the underlying security. The kinds of circumstances that could cause the Clearing Corporation to impose restrictions on the delivery of underlying securities would be if trading in the underlying security were enjoined or ordered suspended by a court, the SEC, or another regulatory or self-regulatory authority having jurisdiction over trading in that underlying security, or if the available supply of the underlying security were limited by a tender offer or similar events. Since it is within the Clearing Corporation's discretion to fix a daily settlement value when delivery restrictions are imposed on holders of Puts, or if a daily settlement value is not fixed, the restriction on Put holders may remain in effect so long as trading in the underlying securities remains suspended. However, the Clearing Corporation may fix a settlement value at any time after delivery restrictions are imposed on holder of Puts, and it will fix a settlement value whenever it is determined that the underlying securities have no value.

4. Each Exchange is also empowered to restrict wholly or partially the exercise of particular Options if it determines that the holder thereof (or a group of holder acting in concert) is in violation of the position limits established by that Exchange.

## 12:3 MUNICIPAL SECURITIES

**12:3:1 Administration and Fees:** The home office principal is responsible for reporting required information and paying the annual fee to the MSRB.

**12:3:2 Municipal Securities Representatives:** All representatives who solicit orders or sell municipal securities will be qualified as Municipal Securities Representatives. Generally, individuals who successfully complete the Series 7 General Securities Sales examination will satisfy this requirement.

**12:3:3 Municipal Securities Principal:** The Series 53 examination qualifies individuals for the registration status of Municipal Securities Principal, which permits the individual to supervise all aspects of the Firm's municipal business. Qualified Municipal Principals will be designated to supervise all areas of municipal securities sales. The municipal principle will be responsible for monitoring municipal transactions sold away from the clearing firm, as well as all aspects of transaction reporting. The principal will monitor the account as well as the customer tickets to ensure the accuracy and timeliness of reporting.

**12:3:4 Fidelity Bonding Requirements:** The home office senior principal is responsible for arranging, maintaining, and verifying the adequacy of appropriate fidelity bond coverage.

**12:3:5 Recordkeeping:** There will be an order ticket created for every municipal trade, including dealer trades. The ticket is transmitted to the home office with the appropriate approval cover form and matched with the affirmation email from reporting. Any discrepancies are noted. A copy of the affirmed and approved trade is emailed to the representative.

**12:3:6 Disclosure of Interest in Distribution:** Rule 15c1-6 of the Securities Exchange Act of 1934 specifies requirements for disclosures when the Firm is involved in a primary or secondary distribution of municipal securities. The Firm will provide the required disclosure on or with the customer's confirmation of a transaction in the subject securities.

**12:3:7 Use of Ownership Information:** The Firm is prohibited from using information regarding the owners of municipal securities obtained in a fiduciary or agency capacity (i.e., as paying agent, transfer agent, registrar, indenture trustee, safekeeping agent, correspondent of another municipal dealer, etc.) for the purpose of soliciting purchases, sales or exchanges of municipal securities. The Firm is also prohibited from using the information for financial gain except with the consent of the issuer or other broker or dealer or the person on whose behalf the information was given.

**12:3:8 Suitability:** Representatives are required to obtain pertinent information about customers (depending on the type of customer) regarding financial background, tax status, investment objectives, and other information to assist in the evaluation of suitability of recommendations. If the customer refuses to provide the requested information, the new account form should be so marked.

RRs are required to have a reasonable basis to believe recommendations are suitable.

**12:3:9 Issuer Disclosures:** Rule 15c2-12 of the Securities Exchange Act of 1934 imposes certain requirements on municipal underwriters and issuers to disclose "material events" and financial information regarding the municipality. This information is available through data providers called Nationally Recognized Municipal Securities Information Repositories (NRMSIRs). Hilltop Securities, Inc. (PICI clearing firm) subscribes to four NRMSIRs, which is available to representatives to access information about municipal issues prior to recommendation.

If an RR becomes aware of a considered change by a rating agency in the issuer's rating or a material event as would be reported to a NRMSIR, the representative should include consideration of this information in any anticipated recommendation and advise the customer, where appropriate.

**12:3:10 Advertising and Sales Literature:** All advertising involving municipal securities will be approved by a home office Municipal Securities Principal. General requirements included in the section of this manual titled "Advertising and Sales Literature" apply to municipal advertising.

**12:3:11 Records of Orders:** PICI will maintain a record of orders in municipal securities consistent with the requirements of MSRB Rule G-8. The home office principal is responsible for daily review of transactions in municipal securities.

**12:3:12 Commissions on Agency Transactions:** The designated supervisor is responsible for reviewing the reasonableness of commissions on agency transactions. Relevant factors in determining the reasonableness of commissions may include:

- The expense of executing and filling the customer's order
- The value of the services rendered by the Firm
- The amount of any other compensation received by the Firm in connection with the transaction
- Any other relevant factors at the time of execution

**12:3:13 Agency Cross Transactions:** All agency cross transactions are reviewed and approved by the home office senior principals. Representative must determine fair trade price by obtaining multiple quotes.

**12:3:14 Reports of Purchases and Sales:** Hilltop Securities, Inc. reports transactions to the MSRB or its designee per MSRB Rule G-14 on behalf of PICI. Effective January 31, 2005 all municipal securities must be submitted for real time reporting and comparison.

**12:3:15 Gifts:** MSRB rules require that the Firm and its Municipal Securities Professionals maintain a record of any gift or gratuity, which includes anything of value in excess of \$100 in relation to municipal securities activities. This does not include occasional gifts of meals or tickets to theatrical, sporting, and other entertainment, reminder advertising, and the sponsoring of legitimate business functions. Gifts cannot be so frequent or so expensive that unethical conduct may become an issue.

Associates are required to notify the home office of any gifts in excess of \$100. The home office senior principal is responsible for maintaining the Firm's Gift Recordkeeping Log, which may be reviewed periodically by regulators.

**12:3:16 Political Contributions:** MSRB Rule G-37 specifies restrictions and requirements regarding political contributions to individuals who may influence the placement of municipal securities business as defined in the rule. The purpose of the rule is to sever any connection between political contributions and the awarding of municipal business. The rule does not prohibit political contributions; it does, however, prohibit the Firm from engaging in municipal business for two years with any issuer where contributions subject to this rule are made. Because the Firm does not want to be subject to a two-year restriction on its municipal business, associates are required to adhere to the requirements of the rule. Rule G-38 requires the disclosure of consultants retained by the Firm to obtain municipal securities business.

Because the rules are extensive and there may be different interpretations depending on the circumstances, it is important to consult with the home office regarding any questions about the effect of the rule.

**12:3:17 Definition of Municipal Securities Business:** The types of business subject to the rule include acting as a negotiated underwriter (as manager or syndicate member), financial advisor or consultant (on a negotiated underwriting), placement agent, and negotiated remarketing agent. The rule does NOT apply to acting as a competitive underwriter or competitive remarketing agent. Note that if the Firm engages a consultant to secure municipal business, the consultant's contributions will affect the Firm's ability to handle municipal business on behalf of the issuer. "Seeking to engage in municipal securities business" is also included under the rule and includes responding to Requests for Proposals, making presentations of public finance capabilities, and other soliciting of business with issuer officials.

**12:3:18 Definition of Municipal Finance Professional:** Municipal finance professional is defined as an associate primarily engaged in municipal underwriting, trading or sales of municipal securities, financial advisory or consultant services for issuers in connection with the issuance of municipal securities, and research or investment advice with respect to municipal securities. It also includes anyone else primarily engaged in any other activities, which involve communication, directly or indirectly, with public investors in municipal securities.

The definition also includes direct supervisors of municipal finance professionals including branch managers; the CEO or similarly situated official; and members of the executive or management committee or similarly situated official.

**12:3:19 Types of Contributions Included:** The following types of contributions made by the Firm or affected associates are subject to the Rule. Those excluded are also explained below.

- Contributions include any gift, subscription, loan, advance, or deposit of money or anything of value made: (i) for the purpose of influencing any election for federal, state or local office; (ii) for payment or reduction of debt incurred in connection with any such election; or (iii) for transition or inaugural expenses incurred by the

successful candidate for state or local office. "State" includes any state of the United States, the District of Columbia, Puerto Rico, the Virgin Islands, or any other possession of the United States.

- Contributions to an "official of an issuer" are subject to the rule. An "official of an issuer" is defined as any incumbent, candidate or successful candidate for elective office of the issuer, which office is directly or indirectly responsible for, or can influence the outcome of, the hiring of a dealer for municipal securities business. This includes any issuer official or candidate (or successful candidate) who has influence over the awarding of municipal securities business so that contributions to certain statewide executive or legislative officials (including governors) would be included within the rule.
- Indirect contributions by affected associates are also subject to the rule, including contributions to a local political party who is soliciting contributions to specifically support an issuer official.
- Specifically excluded from this requirement are contributions by municipal finance professionals that do not exceed, in total, \$250 to each official, per election, but only if the municipal finance professional is entitled to vote for such official. The MSRB has defined "entitled to vote" to mean the municipal finance professional's principal residence is in the locality in which the issuer official seeks election.
- The definition of "contribution" does not restrict the personal volunteer work of municipal finance professionals in political campaigns other than soliciting or coordinating contributions. However, if the resources of the Firm are used (a political position paper is prepared by Firm personnel, Firm supplies or facilities are used, etc.) or expenses are incurred by a municipal finance professional in the course of the volunteer work, the value of the resources or expenses would be considered a contribution and could trigger the restriction on business.

**12:3:20 Whose Contributions Are Affected:** Covered contributions include those by the Firm, municipal finance professionals, the management of the Firm, and anyone who solicits public finance business for the Firm. The rule does NOT apply to other associates, provided that contributions are not made for the purpose of inducing or influencing the obtaining or retaining of public finance business from an issuer.

At the Firm, the following are subject to the restrictions under Rule G-37:

- The Firm itself
- All public finance professionals (clerical staff is excluded)
- The Firm's Executive or Management Committee
- Municipal trading personnel including:
- Municipal Registered Representatives
- Other municipal trading professionals (clerical staff is excluded)

**12:3:21 Approval:** Political contributions to officials of issuers must be cleared through a home office senior principal prior to making the contribution. In addition, any political activities (volunteer work, etc.) on behalf of an official of an issuer must be cleared through Compliance prior to participation.

**12:3:22 Quarterly Report:** G-37 and G-38 require the filing of a quarterly report with the MSRB within 30 days of the end of each calendar quarter in which a contribution has been made. As required by the MSRB, the Firm will send the report via registered or certified mail or by some other means that provides a record of sending. This information will be available to the public from the MSRB.

The home office is responsible for making the quarterly Form G-37/G-38 filing and retaining copies of filed reports in which a contribution has been made. Affected associates will be requested to submit a quarterly certification regarding their political contributions.

**12:3:23 Municipal Customer Complaints:** The Home Office is responsible for keeping and preserving a either a separate file of all written complaints and actions taken by the firm, if any, for municipal customers. In addition, the HO muni principal must confirm that investor complaint brochures have been sent to all muni customers upon receipt of complaints, per Rule G-10. Effective 10-13-17, the HO principal shall ensure an electronic record of all written municipal customer complaints are maintained and preserved for a period of 6 years.

## **12:4 FIXED INCOME**

### **12:4:1 Corporate Bonds**

**12:4:1:1 Introduction:** The Firm conducts sales of the following types of corporate bonds: secured bonds, unsecured bonds, high yield bonds, income bonds, guaranteed bonds, and zero-coupon bonds. The home office senior principal is responsible for reviewing corporate bond transactions on a daily basis, taking the following areas into consideration.

**12:4:1:2 Trade Reporting:** All corporate trades will be monitored by the home office senior principal for accuracy and timeliness of reporting by our clearing firm.

**12:4:1:3 Order Tickets:** All corporate bond transactions will create an order ticket generated by the clearing firm that will be reviewed daily by the home office senior principal. Evidence of review is noted on the compliance review cover letter

**12:4:1:4 Suitability:** Representatives are required to obtain pertinent information about customers (depending on the type of customer) regarding financial background, tax status, investment objectives, and other information to assist in the evaluation of suitability of recommendations. If the customer refuses to provide the requested information, the new account form should be so marked.

RRs are required to have a reasonable basis to believe recommendations are suitable.

**12:4:1:5 Commissions on Agency Transactions:** The home office senior principal is responsible for reviewing the reasonableness of commissions on agency transactions. Relevant factors in determining the reasonableness of commissions may include:

- The expense of executing and filling the customer's order
- The value of the services rendered by the Firm
- The amount of any other compensation received by the Firm in connection with the transaction
- Any other relevant factors at the time of execution

### **12:4:2 Government Securities**

**12:4:2:1 Introduction:** In conducting its government securities business, the Firm's associates will comply with all applicable requirements under the Government Securities Act Amendments of 1993, sections 102 to 107 (relating to FINRA's authority to apply sales practice rules to transactions in government securities the risk assessment rules outlined in Notice 95-48 (relating to recordkeeping and reporting designed to provide warning of situations that can affect significantly the functioning of the markets and investors in general), and the general sales practice guidelines discussed below.

Further, the Firm will ensure that mark-up and commissions on transactions in government securities adhere to the policies set forth in Consolidated FINRA Rule 2121. The Government Securities Principal is responsible for ensuring compliance with these policies.

**12:4:2:2 Trade Reporting:** : All government securities trades will be monitored by the home office senior principal for accuracy and timeliness of reporting by our clearing firm.

**12:4:2:3 Order Tickets:** All government securities transactions will create an order ticket generated by the clearing firm that will be reviewed daily by the home office senior principal. Evidence of review is noted on the compliance review cover letter

**12:4:2:4 Suitability:** Representatives are required to obtain pertinent information about customers (depending on the type of customer) regarding financial background, tax status, investment objectives, and other information to assist in the evaluation of suitability of recommendations. If the customer refuses to provide the requested information, the new account form should be so marked.

RRs are required to have a reasonable basis to believe recommendations are suitable.

**12:4:2:5 Commissions on Agency Transactions:** The home office senior principal is responsible for reviewing the reasonableness of commissions on agency transactions. Relevant factors in determining the reasonableness of commissions may include:

- The expense of executing and filling the customer's order
- The value of the services rendered by the Firm
- The amount of any other compensation received by the Firm in connection with the transaction

Any other relevant factors at the time of execution

### 12:4:3 MBS/CMOs

**12:4:3:1 Introduction:** Mortgage-Backed Securities or Collateralized Mortgage Obligations, MBS or CMOs, are multi-class bonds backed by a pool of mortgage pass-throughs or mortgage loans, including REMIC's. MBS/CMOs may be collateralized by 1) Ginnie Mae, Fannie Mae or Freddie Mac pass-throughs, 2) unsecuritized mortgage loans backed by the FHA or guaranteed by the Department of Veteran Affairs, 3) unsecuritized conventional mortgages, or 4) any combination of the above. The firm's business in MBS and CMOs is limited to institutional customers.

**12:4:3:2 Trade Reporting:** : All MBS/CMO trades will be monitored by the home office senior principal for accuracy and timeliness of reporting by our clearing firm.

**12:4:3:3 Order Tickets:** All MBS/CMOs transactions will create an order ticket generated by the clearing firm that will be reviewed daily by the home office senior principal. Evidence of review is noted on the compliance review cover letter

**12:4:3:4 Suitability:** Representatives are required to obtain pertinent information about customers (depending on the type of customer) regarding financial background, tax status, investment objectives, and other information to assist in the evaluation of suitability of recommendations. If the customer refuses to provide the requested information, the new account form should be so marked.

RRs are required to have a reasonable basis to believe recommendations are suitable.

**12:4:3:5 Commissions on Agency Transactions:** The home office senior principal is responsible for reviewing the reasonableness of commissions on agency transactions. Relevant factors in determining the reasonableness of commissions may include:

- The expense of executing and filling the customer's order
- The value of the services rendered by the Firm
- The amount of any other compensation received by the Firm in connection with the transaction

Any other relevant factors at the time of execution

#### **12:4:4 Cash Alternatives**

**12:4:4:1 Introduction:** The Firm may conduct transactions with customers in certain investments that are loosely referred to as cash alternatives, including: bank CDs, bank money market accounts, banker's acceptances, commercial paper, federal agency short-term securities, fixed rate and step-up callable corporate securities, money market mutual funds, municipal notes, treasury bills, ultra-short bond mutual funds or exchange-traded funds. Transactions in these products are subject to the general supervisory procedures and requirements (for instance, concerning account opening procedures and recordkeeping obligations) contained throughout this Manual; some products are subject to the specific requirements in earlier, dedicated sections herein. The following procedures must be understood and followed by personnel engaging in any and all cash alternative transactions.

In general, cash alternative investments offer lower rates of return than longer-term equities and fixed-income securities. They also generally provide higher liquidity and greater price stability. Some well-known cash alternatives, such as bank CDs, are insured by the FDIC; others, such as T-Bills, are backed by the full faith and credit of the US government. Other investments are less understood and less secure: the Firm has included these procedures to remind its RRs to distinguish between the differing types of cash alternatives and to not overstate their relative safety as an alternative to cash.

**12:4:4:2 Trade Reporting:** All cash alternative trades will be monitored by the home office senior principal for accuracy and timeliness of reporting by our clearing firm.

**12:4:4:3 Order Tickets:** All cash alternative transactions will create an order ticket generated by the clearing firm that will be reviewed daily by the home office senior principal. Evidence of review is noted on the compliance review cover letter

**12:4:4:4 Suitability:** Representatives are required to obtain pertinent information about customers (depending on the type of customer) regarding financial background, tax status, investment objectives, and other information to assist in the evaluation of suitability of recommendations. If the customer refuses to provide the requested information, the new account form should be so marked.

RRs are required to have a reasonable basis to believe recommendations are suitable.

**12:4:4:5 Commissions on Agency Transactions:** The home office senior principal is responsible for reviewing the reasonableness of commissions on agency transactions. Relevant factors in determining the reasonableness of commissions may include:

- The expense of executing and filling the customer's order
- The value of the services rendered by the Firm
- The amount of any other compensation received by the Firm in connection with the transaction

Any other relevant factors at the time of execution



## 12:5 INSURANCE PRODUCTS

**Registration:** Only registered representatives who are qualified to sell variable contracts will be permitted to do so. Qualification generally includes a securities license, an insurance license. A registered principal is responsible for reviewing the applications to ensure only properly-registered RRs are selling variable contract products.

**12:5:1 Communications with the Public:** Variable contracts are subject to the requirements of Investment Firm advertising rules. Refer to section titled “Mutual Funds” and subsection “Advertising and Sales Literature” for further information regarding these requirements.

FINRA rules also specify other requirements regarding advertising and other communications with the public, including the following:

- The product must be identified either as a variable life insurance policy (VLI) or variable annuity (VA).
- There may be no indication or implication that the product or its underlying account is a mutual fund.
- There may be no implication that VLI's or VA's are short-term, liquid investments.
- Presentations must be balanced by discussions of the negative impact of early redemptions, loans, or withdrawals.
- There may be no exaggeration of the safety of the guarantee since the guarantee depends on the issuing firm.
- There may be no implied guarantee about investment return or principal value.

**12:5:2 Suitability Requirements:** A home office senior principal is responsible for the review of all variable annuity business. The registered principal shall review the application, new account form, the variable annuity disclosure and switch form (if applicable). The Registered Principal is to review the above information for completeness, suitability, and to monitor annuity exchanges such as 1035 exchanges, replacements, improper twisting, and other exchanges that may be detrimental to the client. The Registered Principal should also review the applications for contracts with multiple issuers. The review will be documented/signed by the Registered Principal.

**12:5:3 Non-Cash Compensation:** Registered representatives are not allowed to accept non-cash compensation except as provided under the provision of FINRA Rule 2830(h). Representatives are instructed to notify the Compliance department regarding any non-cash compensation arrangement.

**12:5:4 Sales Agreements:** PICI will execute a sales agreement with the underwriters of any variable contract products offered by PICI. The Compliance Department will retain copies of sales agreements.

**12:5:5 Approved Issuers of Variable Contract:** The home office senior principals are responsible for approving issuers and variable contracts to be offered by the Firm. Contact the Home Office for a list of approved issuers.

**12:5:6 Applications and Purchase Payments/Delivery:** A home office senior principal is responsible for reviewing applications for completeness and suitability and for promptly transmitting the customer's application and purchase payments to the issuer. Customers will be instructed to make checks payable directly to the issuer. All documents will be reviewed, accepted, and mailed to the issuer with seven days of the customer signing. All contracts will be sent to PICI home office for review and to forward on to the client.

**12:5:7 Exchanges:** A home office senior principal shall review all exchanges. As part of the review, reps are required to complete the Variable Annuity Recommendation Worksheet Exchange Addendum. The principal must review the customer, as well as the rep for appropriate rate of exchanges. Any exchange that is inappropriate, will not be

processed. The client will be notified and the exchange will be discussed with the client and appropriate actions will be taken. The representative will also be notified and disciplined.

**12:5:8 Training:** Training is provided to all firm associates regardless of licensing or if they sell annuity products. Training is provided via the firm's compliance program.

## 12:6 ALTERNATIVES

**12:6:1 Introduction:** The firm conducts transactions with customers in certain investments that are alternatives to conventional equity and fixed-income investments. These products are "complex," in that they present an additional risk to investors because their characteristics add a further dimension to the investment decision process beyond the fundamentals of market forces. Their complexity arises from qualities such as embedded derivative-like features or a structure that produces different performance expectations according to price movements of other financial products or indices. The intricacy of these products can impair the ability of registered representatives or their customers to understand how the product will perform in a variety of time periods and market environments, and may lead to inappropriate recommendations and sales.

Examples of complex products offered by the Firm may include: asset-backed securities, non-traded (unlisted) REITs, publicly-traded REITs, UITs, publicly-traded (application way) LP's, multi-callable step up notes, redeemable secured notes, auction rate preferred securities, principal protected index-linked CDs, principal protected notes and other structured products, derivatives, exchange-traded funds (ETFs), emerging market debt securities, commodity futures-linked securities and reverse convertibles (collectively referred to as non-conventional investments (NCIs) or complex products).

As with all products offered by the Firm, RRs may not offer complex products to customers before the Firm has approved, in general, of such products. Transactions in these products are subject to the supervisory procedures and requirements (for instance, concerning account opening procedures and recordkeeping obligations) contained throughout this Manual.

### 12:6:2 Product Approval and Due Diligence

*Only approved products may be offered to customers by RR's.* No unapproved products must be offered or sold to customers. RR's with questions about certain products should consult the home office senior principals PRIOR to discussing any complex security with customers. The home office senior principal has final approval on products.

Due diligence will be performed by representative prior to discussion with a client and forwarded to the home office for senior principal review and approval. Ongoing due diligence will be performed on a need to basis by the representative and/or home office senior principal.

**12:6:3 Filing and Record Keeping:** All alternative transactions will be monitored by the home office senior principal for accuracy and timeliness of reporting, if applicable.

**12:6:4 Order Tickets:** All alternative transactions will be entered on the firm's workbook blotter and reviewed monthly by the home office senior principals. Evidence of review is noted on the compliance review cover letter

**12:6:5 Suitability:** Representatives are required to obtain pertinent information about customers (depending on the type of customer) regarding financial background, tax status, investment objectives, and other information to assist in

the evaluation of suitability of recommendations. If the customer refuses to provide the requested information, the new account form should be so marked.

RRs are required to have a reasonable basis to believe recommendations are suitable.

**12:6:6 Direct Participation Programs and Unlisted REITs:** The Firm may offer unlisted real estate investment trusts (REITs) or direct participation programs (DPPs). REITs are pass-through entities that offer investors an equity interest in a pool of real estate assets, including land, buildings, shopping centers, hotels and office properties, and, in some cases, mortgages secured by real estate. DPPs are programs which provide for flow-through tax consequences regardless of the structure of the legal entity or vehicle for distribution, including, but not limited to, oil and gas programs, real estate programs, agricultural programs, cattle programs, condominium securities, Subchapter S corporate offerings and all other programs of a similar nature, regardless of the industry represented by the program, or any combination thereof. DPP's are excluded from the definition of "new issue" under Consolidated FINRA Rule 5130, which describes restrictions on offerings of new issues. Rule 2310 governs the underwriting terms and arrangements of DPP's and REITs, whether registered or unregistered, but which are not listed on a national securities exchange.

The current prospectus or other offering memorandum of each DPP/REIT should be delivered to the customer prior to, or at the time of, the sales presentation. The customer should be encouraged to read the prospectus prior to making an investment decision and should be reminded that there is no assurance that the program's objectives will be met. Outdated prospectuses should not be used and amendments to prospectuses should be provided promptly to customers. Information and objectives provided outside of the prospectus should not conflict with those in the prospectus.

Registered representatives are required to disclose all pertinent facts regarding the liquidity and marketability of the DPP or REIT during the term of the investment, including whether the sponsor has offered prior programs and if so, whether;

- the prior program included a date or time period when it might be liquidated; and
- the program was indeed liquidated on or about the published dates or time period.

(This prior program information is not required for certain DPPs that are either listed or reasonably expected to be listed on a national securities exchange.)

**12:6:7 Limited Partnerships/Hedge Funds:** The Firm may act as placement agent in select private offerings of interests in limited liability companies (LLC), limited partnerships (LP) and/or hedge funds. An LP or LLC offering is a type of investment whereby the income would generally flow through to the investors (members or limited partners) who are viewed as passive investors with little or no say in the managerial decision-making (examples of such offerings include real estate syndications and oil and gas programs; REITs are included in the section below entitled, "Non-Conventional Investments"). A hedge fund is defined as a private and unregistered investment pool that accepts investors' money and employs sophisticated hedging and arbitrage techniques using long and short positions, leverage and derivatives, and investments in many markets. Hedge funds are typically organized as LP's or LLC's, with the general partner or managing member managing the fund's portfolio. The procedures in the section are also relevant to the offering of interests in other types of private investment funds, such as private equity funds.

Representatives must examine carefully the suitability of these investments since they may not be appropriate if an individual does not meet certain accredited or sophisticated investor requirements. LP/LLC's and hedge funds are not extremely liquid investments and should be viewed as more long-term investments.

**12:6:8 Private Equity Funds—Primary Placement:** The Firm may engage in “primary fund placement” services, whereby it assists private equity firms in raising capital. Specifically, the Firm assists the general partners (GPs) of private equity (PE) funds in finding limited partners (LPs). The private equity funds are unregistered limited partnerships consisting of ownership interests in private operating companies. When acting in this capacity, the Firm has a contractual relationship with the GP, whereby it:

- assists in the preparation of marketing materials,
- contacts potential investors (which become LPs in the fund upon investment),
- organizes meetings between potential investors and the representatives of the GP,
- facilitates on-going discussions between the parties, and
- assists in the negotiations of the terms of investment.

In essence, the Firm is acting as placement agent in private offerings of limited partnership interests on a negotiated basis. The role of the Firm is strictly limited to advising the GP--its client--and assisting in its capital raising efforts. The Firm does not provide advice to potential investors (LPs) beyond presenting investment opportunities and related information. It is generally understood that the Firm is not recommending securities purchases to investors; however, the Firm intends to comply with FINRA’s suitability rule to the extent it is deemed applicable in each circumstance.

All firm associates are required to read the firm’s written supervisory procedures manual upon association with the firm and when presented with updates. Annual, all firm associates attest to having read the manual and any updates presented through the firm’s annual compliance certification which is an element of the firm’s compliance program/continuing education program.