

Supervisory Procedures Manual

Coastal Equities, Inc.

Effective: September 1, 2021

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INTRODUCTION

CEI ("CEI") will conduct its business consistent with the highest standards of commercial honor and just and equitable principles of trade. Keeping our customers' interest foremost is key to CEI's success. The trust of our customers and CEI's reputation are of paramount importance. Effective supervision is an integral part of achieving our goals in serving our customers.

"Compliance" is not a static event; it is a process which evolves in tandem with regulations that govern our industry and the circumstances of each particular interaction. This manual includes CEI's supervisory policies and procedures to provide guidance to designated supervisors in their oversight of the Firm's business. It is a working document and reference for supervisors and will be updated when necessary.

It is recognized that supervision must be a flexible tool for use by those charged with managing the Firm's various activities. While it is generally expected these procedures will be followed, supervisors are encouraged to adapt these procedures to the needs of CEI, their particular department, and the employees and customers of CEI. These procedures are meant to be a basic framework upon which supervisors oversee the Firm's activities.

This manual does not attempt to set forth all of the rules and regulations with which employees must be familiar, nor does it attempt to deal with all situations involving unusual circumstances. When questions arise, refer them to Compliance for assistance.

Supervision may be delegated to others, where appropriate; however, designated supervisors are responsible for ultimate supervision of assigned areas. The term "employee" as used in this manual includes Registered Representatives ("RRs") (and others as identified by CEI) who may be independent contractors for tax and compensation purposes.

This manual is the property of CEI and may not be provided to anyone outside the Firm without the permission of Compliance or the Firm's counsel. Please note this manual is applicable to CEI only; please refer to the manual for Coastal Investment Advisors for procedures applicable to that entity.

Throughout the manual, some supervisory tasks are assigned a frequency (daily, weekly, monthly, annually, or as-needed). Daily and As-needed are used in this manual interchangeably. Furthermore, where regulation or law does not require strict construction of such terminology, Coastal requires only material compliance with those terms, i.e. should a weekly task be completed within 10 days or even two weeks, depending on the circumstances, the firm may deem such an aberration to not rise to the level of non-compliance with this manual.

1 DESIGNATION OF SUPERVISORS AND OFFICES

1.1 Designation of Supervisors

[FINRA Rule 3110(a)]

This section includes CEI's designated supervisors responsible for supervision of the areas of business indicated.

Date: January 2, 2020

Area/ Department Supervised	Name/Title/ Location of Supervisor	Registration Status	Effective Date of Supervision	RRs Supervised
Establish policies and procedures including supervisory controls and testing of those procedures	Francis J. Skinner/Chief Compliance Officer/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Compliance	Francis J. Skinner/Chief Compliance Officer/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Financial Reporting	Charles F. Reiling III/Financial and Operations Principal/Wilmington, DE	FINRA Series 4, 7, 24, 27, 65 and 66	September 2012	N/A
CRD Electronic Filings	Charles F. Reiling III/Financial and Operations Principal/Wilmington, DE	FINRA Series 4, 7, 24, 27, 65 and 66	September 2012	N/A
Financial Reporting	David Monahan/Financial and Operations Principal/Wilmington, DE	FINRA Series 28	February 2017	N/A
Over the counter ("OTC") securities	New Products Committee/Charles F. Reiling, III; Matthew Rakerd/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Corporate debt	Aileen DeFroda /Wilmington, DE	FINRA Series 7, 24, 52, 53 and 63	January 2012	N/A

Underwriting or selling group participant	New Products Committee/Charles F. Reiling, III; Matthew Rakerd/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Mutual fund retailer	New Products Committee/Charles F. Reiling, III; Matthew Rakerd/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Municipal securities	Aileen DeFroda/Municipal Securities Principal/Wilmington, DE	FINRA Series 7, 24, 52, 53 and 63	January 2012	N/A
Variable life insurance and annuities	New Products Committee/Charles F. Reiling, III; Matthew Rakerd/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Real estate syndicator	New Products Committee/Charles F. Reiling, III; Matthew Rakerd/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Oil and gas	New Products Committee/Charles F. Reiling, III; Matthew Rakerd/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Options	Kari March/Registered Options Principal/Roswell, GA	FINRA Series 4, 7, 24, 31, 63 and 65	January 2015	N/A
Tax shelters and limited partnerships in primary distributions	New Products Committee/Charles F. Reiling, III; Matthew Rakerd/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A
Private placements	New Products Committee/Charles F. Reiling, III; Matthew Rakerd/Wilmington, DE	FINRA Series 7 and 24	June 2, 2015	N/A

Correspondence	Designated branch supervisor	FINRA Series 24	Various	All RRs in the branch office
Customer complaints	Francis J. Skinner/Chief Compliance Officer/Wilmington, DE	FINRA Series 7, 24	June 2, 2015	N/A
Internal inspections	Francis Skinner, Wilmington DE	FINRA Series 7, 24	January 2, 2020	N/A

1.2 Designation of Offices

[FINRA Rule 3110(f); MSRB Rule G-27(b)(iii) and G-27(g)]

Coastal Equities, Inc. maintains the following types of office(s):

OSJ = Office of Supervisory Jurisdiction

BR = Branch Office

Non-Branch locations:

NSA = Non-sales location (limited to customer service, back office functions, *etc.*)

NSE = Non-securities location (associated person(s) primarily engaged in non-securities activities)

PR = Primary residence (associated person's primary residence used for securities business)

OPR = Locations other than primary residences (*e.g.*, other location used less than 30 business days/year for securities business)

OC = Office of convenience (location used occasionally and exclusively by appointment to meet with customers)

NON = Location used primarily to engage in non-securities transactions (no more than 25 securities transactions in a calendar year; retail communications (including business cards) must include location of supervising office)

TEMP = Temporary office established because of implementation of business continuity plan

The firm maintains a log of all branch offices and designated supervisors electronically. That document is the official record of the branch offices and their designated supervisors, and is updated regularly. The document is titled the "Supervision Matrix" and on a monthly basis, the matrix is archived to maintain the historical versions of the matrix.

2. REGISTERED REPRESENTATIVES; ASSOCIATED PERSONS; and NON-REGISTERED PERSONS

2.1 Employees

CEI retains employees to serve operational, compliance, administration, and some trading functions. All employees are fingerprinted. When a new position is created within CEI, the position is reviewed by compliance and management to determine mandatory licensing requirements.

Series 99: Individuals with any of the following responsibilities will be required to possess a S99 or S4, S6, S7, S9/10, S14, S16, S24, S26, S27, S28, S51, or S52.

- Customer on-boarding (customer account data and document maintenance)
- Collection, maintenance, reinvestment (i.e., sweeps) and disbursement of funds
- Receipt and delivery of securities and funds, account transfers
- Bank, custody, depository and firm account management and reconciliation
- Settlement, fail control, buy-ins, segregation, possession and control
- Trade confirmation and account statements
- Margin
- Stock loan/securities lending
- Prime brokerage (services to other broker-dealers and financial institutions)
- Approval of pricing models used for valuations
- Financial control, including general ledger and treasury
- Contributing to the process of preparing and filing financial regulatory reports
- Defining and approving business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements
- Defining and approving business security requirements and policies for information technology, including but not limited to systems and data, in connection with the covered functions
- Defining and approving information entitlement policies in connection with the covered functions
- Posting entries to a member's books and records in connection with the covered functions to ensure integrity and compliance with the federal securities laws and regulations and FINRA rules

Firm principals and supervisory personnel are required to maintain the appropriate license for the activity supervised.

Employees are also required to acknowledge receipt of the Employee Handbook, and to abide by its policies and procedures.

2.2 Independent Contractors

CEI is an independent contractor model BD – meaning its sales force is comprised of independent contractor registered representatives. Substantially all of CEI's registered persons ("RR"s or financial professionals) involved in sales activity are independent contractors. It is CEI's policy that it will take no actions which could create and employer/employee relationship. Such actions include, among other things, providing work tools or equipment to an independent contractor free of charge, providing office space or employees, or mandating specific work hours. Each independent contractor registered representative is required to sign a registration agreement with CEI prior to registration. The terms concerning the independent contractor relationship are fully set forth in the registered representative's registration agreement executed and approved by CEI.

Registered Representatives may hire their own employees with notice to and approval by CEI. Employees must be either registered or fingerprinted if they will have access to customer information.

Although certain sections of these WSPs may refer to the "hiring" process, or refer to RRs as "employees", these terms are used in the general and ordinary sense of the words and are not intended to establish an employment relationship with the RR. Notwithstanding anything herein to the contrary, no section of these WSPs should be construed as conferring employment status to any of CEI's RRs.

2.3 Recruiting Procedures: Independent Contractors

[FINRA Regulatory Notice 07-55]

This section outlines basic requirements concerning the recruitment of independent contractor RRs. CEI's employee handbook controls hiring procedures of home office non-sales employees. Parts of this Section will apply to other associated persons ("AP"s) and non-registered fingerprinted ("NRF"s) persons who will be working in the registered representative's branch.

2.4 RR Interview Guidelines

[FINRA Notice to Members 07-06]

The Hiring Manager may vary depending on the source of the referral or recruitment of a prospective RR. The Hiring Manager is typically the CEO or Business Development Personnel. While operational procedures may be overseen by the Hiring Manager, functions which require licensing to perform or to supervise will be conducted by an appropriately licensed principal or supervisor.

At the time an RR is being considered for hire in a sales capacity, the following are areas the hiring manager should consider:

1. Discuss with the applicant the nature of the applicant's prior customers and the types of securities sold while associated with prior employers. If customers' investments include investment company products (mutual funds, variable annuities), determine whether CEI has dealer or servicing agreements in place and, if not and the RR is hired, plan for suitability reviews and notification to customers of investment options and costs of switching investments.
2. Obtain the applicant's explanations regarding any customer complaints and regulatory actions to determine the merit, to the extent practicable, of each before hiring.
3. Ask the applicant about the existence of and nature of any pending proceedings, customer complaints, regulatory investigations, or arbitrations not listed in the CRD.
4. Discuss the reasons for the applicant's frequent change of employers, if applicable.
5. Obtain the RR's prior year W-2.
6. Ask the RR whether he or she signed an employment contract with the present employer and if so, obtain a copy from the RR.

2.5 Hiring/Registration Process

CEI provides all prospective persons who will register with CEI an onboarding package which provides basic information about the firm and other ancillary documents to assist CEI in fulfilling both its business and regulatory obligations. Home Office and other non-sales positions do not require compliance with sales-related sections of this Chapter and certain forms relating to sales activity need not be completed by the prospect. Prospective sales registered representatives are presented by Business Development personnel to the Firm's CEO and Board of Directors for consideration. Hiring decisions are made by the CEO. Approval of a registered representative is evidenced by the signature of an authorized officer of CEI on the Registration Agreement.

2.5.1 Qualification of Prospective Supervisors

[FINRA Rule 3110(a)(6)]

Responsibility	<ul style="list-style-type: none"> • Chief Supervision Officer - confirm qualifications • Compliance - determine registration requirements
Resources	<ul style="list-style-type: none"> • Individuals identified as potential supervisors • Background information on candidate including registration status
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • CSO: <ul style="list-style-type: none"> ○ Evaluate candidate's qualifications including experience and knowledge ○ Arrange for training, if necessary • Compliance: <ul style="list-style-type: none"> ○ Confirm individual has required registration qualifications and, if not, arrange for the individual to complete the required exams ○ Notify the CSO of added qualifications required and remind him/her the individual may not act as a supervisor until necessary registrations are obtained (unless a regulator allows for a grace period to act as a supervisor before registration is completed) ○ Provide supervisory policies/procedures to the candidate if not already available to him/her
Record	<ul style="list-style-type: none"> • CSO's consent to appoint the candidate to a supervisory position • Background and registration information in candidate's file • Record of training (if necessary) including a description of training and when completed • Record of providing supervisory policies/procedures

The CSO is responsible for determining that the individual is qualified for the supervisory position. Individuals included in CEI's business plan filed with FINRA are required to have at least one year of direct experience or two years of related experience in the area to be supervised.

2.5.2 Background Investigation

[FINRA Rule 3110(e)]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Onboarding file • Form U4 • Public records • Outside background check services

Frequency	<ul style="list-style-type: none"> • When new employees are hired
Action	<ul style="list-style-type: none"> • Identify outside services, if any, to conduct background investigations <ul style="list-style-type: none"> ◦ Where an outside service is used, review capabilities and references • Obtain records for review • Within 30 calendar days of filing Form U4, verify information: <ul style="list-style-type: none"> ◦ Contact prior employers for 3 years ◦ Obtain additional information from employee, if necessary, and verify ◦ Review notification from FINRA regarding public records information missing or contrary to filed U4 ◦ Submit revised U4 within 30 days to reflect information received from FINRA public records search • Review CFTC Form 8-T if applicable • Conduct further investigation where reviews reveal patterns of negative information such as customer complaints, bankruptcies, liens, criminal activity, litigation, or other negative information • Internet searches of disclosed names, residential and business addresses, phone numbers, and email addresses to check for negative news, undisclosed OBA activity, and undisclosed social media accounts • Where discrepancies or incomplete information are identified, contact the employee for further information and investigate further, if needed • Evaluate negative information and its impact on the employment of the individual, consulting with the employee's supervisor or principal of the firm
Record	<ul style="list-style-type: none"> • Review of outside services to conduct background investigations • Review of public records (Broker Check/IAPD) • Form U5 and results of review • Form U4 with related reviews and results of reviews including public records • CFTC Form 8-T and results of review • Internet searches • Contact with prior employers for 3 years including contact person and date contacted • Reviews of discrepancies or missing information and action taken including consultation with employee and supervisor • Action taken, if any, after reviews conducted

Background investigations are conducted on all new employees. New employees must be accurate and complete in the information provided to CEI at time of hire. Failure to do so may result in termination.

Records to be provided by a new employee include:

- Driver's license or passport to verify identity
- Completed Form U4 (required for all registered persons)
- Prior firm's Form U5 filed on behalf of a registered person
- CFTC Form 8-T for registered persons previously employed with an FCM (Futures Commission Merchant) or IB (Introducing Broker)
- Other information requested by CEI

Reviews conducted will include:

- Contact with at least the last three years' employers. Contact may be by telephone or by written correspondence.
- Form U5 from prior employer
- Form U4 filed with CEI
- CFTC Form 8-T
- Internet searches of disclosed names, residential and business addresses, phone numbers, and email addresses to check for negative news, undisclosed OBA activity, and undisclosed social media accounts
- Review of public records by FINRA/IAPD for information regarding criminal and bankruptcy records, civil litigation, judgments, and liens
- Other reviews which may include a review of credit records in the discretion of Compliance.

New employees and registered representatives will be required to reconcile discrepancies or missing information which may affect the employee's eligibility for registration or hire. U4s will be updated within 30 days of notice from FINRA regarding public record discrepancies.

2.5.3 Fingerprints

[SEC Securities Exchange Act of 1934 Rule 17f-2; FINRA Rule 1010(d)]

Responsibility	<ul style="list-style-type: none"> • Compliance – registered persons • Operations – non-registered persons
Resources	<ul style="list-style-type: none"> • Notifications regarding registration and other applicants
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • If necessary, identify third parties (local law enforcement officials, <i>etc.</i>) to take fingerprints and: <ul style="list-style-type: none"> ○ Notify the third parties of securities industry fingerprinting requirements including identification verification procedures ○ Provide applicants with a list of acceptable third-party vendors • Submit electronic filing to CRD • Obtain Fingerprint Attestation and fingerprints, compare signatures of applicant and note on Attestation • Submit fingerprints to CRD with barcode • If fingerprints are not received by the CRD within 30 days of filing Form U4, notify appropriate supervisor that activities requiring registration must cease
Record	<ul style="list-style-type: none"> • Registration files for associated persons include records of CRD filings and submission of fingerprints including Fingerprinting Attestation form

Compliance will obtain and submit fingerprints on all registered personnel for receipt by the CRD within 30 days of filing Form U4. Fingerprints for other personnel will be obtained and submitted by the Hiring Manager's designee or Operations. A Fingerprinting Attestation form will be completed for each applicant. CEI may utilize a third-party vendor for fingerprinting services at its sole discretion.

If fingerprints are not received by the CRD within 30 days, the associated person must cease engaging in activities that require registration. Compliance will notify the appropriate supervisor of deficiencies, and the supervisor is responsible for restricting the applicant's activities until fingerprints have been received by the CRD.

2.5.4 Procedures Manuals

At the time of hire or prior thereto, RRs are provided with a current copy of CEI's policies and procedures either in hard copy, PDF copy, or by notifying the RR of the location where policies and procedures may be accessed in electronic form. The RR is required to acknowledge, in writing or electronically, that the policies were received and that the RR is responsible for complying. The RR will attest annually that he or she has a current copy of the policies and procedures and is responsible for complying.

2.6 Recruitment Practices and Account Transfers

[FINRA FAQs: <https://www.finra.org/rules-guidance/guidance/faqs/frequently-asked-questions-regarding-finra-rule-2273>]

Responsibility	<ul style="list-style-type: none"> Hiring Manager or designee (licensed)
Resources	<ul style="list-style-type: none"> Newly-hired RRs RR Log of Delivery of FINRA notice
Frequency	<ul style="list-style-type: none"> As required
Action	<ul style="list-style-type: none"> Instruct responsible persons to provide the required communication to former customers transferring to CEI Monitor accounts transferred within 3 months of the RR's hire to confirm communications are provided
Record	<ul style="list-style-type: none"> New RRs including date of hire Log of communications provided to former customers

When an RR is engaged by CEI, each former customer transferring to CEI will be provided, in paper or electronic form, an educational communication prepared by FINRA. The requirement applies for 3 months following the date the RR begins employment with CEI.

The communication will be provided when:

- The former customer of the RR is contacted by CEI or through a representative to transfer assets; or
- A former customer, without individual contact, transfers assets to an account assigned, or to be assigned, to the RR.

Events that trigger the requirement include oral or written communications by the newly-hired RR:

- informing the former customer that he or she is now associated with the recruiting firm;
- suggesting that the former customer consider transferring his or her assets or account to the recruiting firm;
- informing the former customer that the recruiting firm may offer better or different products or services; or
- discussing with the former customer the fee or pricing structure of the recruiting firm.

Communication with a group of customers via a mass mailing, e-mail, or automated phone calls or voicemails also triggers the requirement to provide the disclosure to the customers.

The educational communication must be provided as follows:

- at the time of first individualized contact regarding transferring assets to The Firm.
 - If first contact is in writing, the disclosure must accompany the written communication.
 - If by electronic communication, a hyperlink to the disclosure must be included.
 - If oral, the RR must notify the customer that an educational communication that includes important considerations about transferring assets will be provided no later than 3 business days after the contact, with follow-up delivery within 3 business days.
- If the customer seeks to transfer assets but there has been no individualized contact with the customer, the communication must be sent to the customer with the transfer approval documentation.

If the former customer states he or she will not transfer assets, the educational communication requirement does not apply. Should the former customer decide to transfer assets within 3 months of the RR's employment, the communication must be provided with the account transfer approval documentation.

New registered representatives should maintain a log of each former customer, date of delivery of the FINRA communication, and method of delivery. This log should be forwarded to the Hiring Manager and Designated Supervisor monthly for the first three months.

Exceptions

"Former customer" includes any customer that had a securities account assigned to a registered person at the representative's previous firm. The term "former customer" does not include a customer account that meets the definition of an "institutional account" as defined in FINRA Rule 4512(c); accounts held by a natural person do not qualify for the institutional account exception.

The Rule does not apply to circumstances where a customer's account is proposed to be transferred to The Firm via a bulk transfer or due to a change of broker-dealer of record. Consult Compliance if you believe this exception might apply.

2.6.1 Considerations Regarding Insurance Products for Newly-Hired RRs

[FINRA Regulatory Notice 07-36; FINRA Notice to Members 07-06]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Information about transferring customers' investments in variable company products
Frequency	<ul style="list-style-type: none"> • As required for proposed switching of investments
Action	<ul style="list-style-type: none"> • Review existing investments against proposed substitute investments with particular review of proposed reinvestment in bonus variable annuity products • Prepare information and provide it to customers regarding options including that the customer may have to hold the existing investment at the prior firm, the cost

	of switching to another investment, and other considerations before changing investments
Record	<ul style="list-style-type: none"> Records of accounts reviewed and suitability determination, action taken including information provided to customers

There are considerations when a newly-hired RR transfers customers who hold variable company products (mutual funds, variable annuities). If Coastal Equities, Inc. cannot or will not service the customer's existing investment (inability to transfer products, Coastal Equities, Inc. does not have a dealer or servicing agreement), the appropriateness and suitability of recommending a new investment company product must be determined by the RR and Coastal Equities, Inc.. Before liquidating existing investments and reinvestment in new products, disclosure must be made to the customer regarding the costs and benefits of any proposed change in investments and proposed replacement investments must be suitable. A change of employment is not by itself a suitable basis for recommending a switch from one product to another.

2.7 Registration and Licensing

[FINRA Corporation By-Laws Article V; FINRA Rule 1200 series; FINRA Regulatory Notice 17-30; FINRA FAQs: <https://www.finra.org/registration-exams-ce/qualification-exams/faq>; NASDAQ Rule 1000 series]

Responsibility	<ul style="list-style-type: none"> Registration Principal
Resources	<ul style="list-style-type: none"> New hire notices Change of status notices Requests for registration CRD Late Filing Fee Report
Frequency	<ul style="list-style-type: none"> Compliance: Quarterly - review CRD Late Filing Fee Report As required for new hires and requests for registration
Action	<ul style="list-style-type: none"> Identify associated persons who require registration by reviewing new hire or change of status records Submit required filings to the CRD Acknowledge electronic filings are on behalf of CEI and its associated persons Request and schedule examinations Ensure associated persons who require registrations obtain them Amend U4s or U5s when there are reportable events Review the CRD Late Filing Fee Report to identify late filings and to take corrective action
Record	<ul style="list-style-type: none"> Registration records including CRD notices, approvals, amendments, and other registration records are maintained in associated person files <ul style="list-style-type: none"> Where the registered person's signature is not required on U4 amendments, CEI may rely on the CRD for recordkeeping

	<ul style="list-style-type: none">• The CRD Late Filing Fee Report is retained in a CRD report file with initials of who reviewed and date reviewed and any action taken
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2.7.1 CRD Electronic Filings

[FINRA Rule 1010]

CEI has designated one or more associated persons with authority over registration functions, as named in CEI's *Designation of Supervisors* chart. Any supervisor of electronic filings is a registered principal or a corporate officer and is responsible for review and approval of electronic filings and acknowledging electronically that the forms are filed on behalf of CEI and its associated persons.

2.7.2 Registration Requirement

All individuals engaged in activities (including selling or trading products such as stocks, bonds, options, insurance, *etc.*) subject to registration requirements of SROs or other regulators must complete the necessary registration and licensing prior to engaging in such activities. Associated persons may not conduct business with public customers until required registrations or licenses are effective.

RRs who assume duties that require registration with FINRA as a principal, have 90 calendar days to pass the appropriate principal's examination.

2.7.3 Requests for Waivers

[FINRA Rule 9600]

Regulators seldom grant waivers of training period requirements or examinations. In those very few instances where waivers are granted, the candidate must be able to demonstrate comparable work experience or other successfully completed examinations that could, in the view of the regulator, constitute satisfying their requirements. Requests for waivers will be submitted by Compliance.

2.7.4 State Registrations

RRs must be registered in the state from which they conduct business and may be required to be registered in other states where customers are domiciled. Most states require successful completion of the Series 63 Uniform State Agent Securities Law Examination. Successful completion of the exam does not automatically confer registered status on the examinee. Application must be made to the CRD to obtain each state registration.

The RR's designated supervisor is responsible for identifying transactions in states where registration may be required.

2.7.5 Parking Registrations

[FINRA Rule 1210.02 and 1210.11]

CEI does not permit individuals to "park" licenses. Parking occurs when CEI maintains a registration on behalf of an individual that does not work for CEI or who does not need that registration for their job function. CEI may, however, maintain registration for legal, compliance, or other non-sales employees as permitted under regulators' rules.

Consistent with the requirements of [Rule 3110](#), members shall have adequate supervisory systems and procedures reasonably designed to ensure that individuals with permissive registrations do not act outside the scope of their assigned functions. With respect to an individual who solely maintains a permissive registration(s), the individual's direct supervisor shall not be required to be a registered person. However, for purposes of compliance with [Rule 3110\(a\)\(5\)](#), a member shall assign a registered supervisor who shall be responsible for periodically contacting such individual's direct supervisor to verify that the individual is not acting outside the scope of his or her assigned functions. If such individual is permissively registered as a representative, the registered supervisor shall be registered as a representative or principal. If the individual is permissively registered as a principal, the registered supervisor shall be registered as a principal. Moreover, the registered supervisor of an individual who solely maintains a permissive registration(s) shall not be required to be registered in the same representative or principal registration category as the permissively-registered individual.

Individuals who hold permissive registrations shall be assigned a direct supervisor who will monitor email and other communications and activity on a periodic basis to confirm the individual is not acting outside his/her assigned function. Evidence to the contrary should be investigated by the supervisor and then reported to Compliance.

2.7.6 Form U4

[FINRA Rule 1010 and 2263]

All applicants for registration are required to complete Form U4. It is the RR's responsibility to include accurate information and promptly notify CEI of any updates that may require amendment to Form U4.

At the time a new or amended U4 is signed, the applicant will be provided the *Form U4 Disclosure To Associated Persons*, which discloses information about the pre-dispute arbitration clause included in Form U4.

2.7.7 Amendments to Form U4 or Form U5

CEI will submit amendments to Form U4 when an RR advises of updates that require amendment. Compliance is responsible for determining whether reportable events or other matters require the filing of an amendment to an RR's Form U4. Compliance is also responsible for identifying disciplinary or complaint matters to be reported on Form U5 termination notices including amendments required after termination. Required reportable events include the receipt of an SEC Wells notice.

2.8 Statutorily Disqualified Persons

[FINRA Rule 9285; FINRA Regulatory Notice 21-09 and 09-19; SEC Securities Exchange Act of 1934 Rule 19h-1 and Section 3(a)(39); FINRA By-Laws Article III Section 3 and Section 4; FINRA FAQs for MCDC firms: <https://www.finra.org/rules-guidance/guidance/faqs/faq-eligibility-proceedings-firms-participating-mcdc-initiative>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • N/A
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Compliance will: <ul style="list-style-type: none"> ○ Complete the required regulatory forms ○ Establish procedures for conducting required supervision

	<ul style="list-style-type: none"> • The designated supervisor will: <ul style="list-style-type: none"> ○ Conduct required supervision ○ Provide Compliance with certifications of supervision, if required
Record	<ul style="list-style-type: none"> • Regulatory applications/forms and related documents are retained in the RR's file in Compliance • Certifications of supervision, if required, are retained in the RR's file in Compliance

2.8.1 Introduction

Individuals may become subject to statutory disqualifications as a result of a felony conviction or regulatory suspension, revocation of registrations or injunctions (including actions by domestic regulators including the CFTC and actions by foreign regulators). The definition of statutory disqualification is included in Section 3(a)(39) of the Securities Exchange Act of 1934. FINRA Regulatory Notice 09-19 includes a chart, in Attachment B, that outlines statutory disqualifications under the Rule.

2.8.2 Hiring A Statutorily Disqualified Person

All prospective associated persons (including those engaged solely in clerical and/or ministerial activities) are subject to background investigations that include identification of potential statutory disqualification. Prior to hiring an individual subject to a statutory disqualification, Compliance should be consulted to review the nature of the statutory disqualification and potential special supervision that may be required upon hiring.

2.8.3 Regulatory Filings

[FINRA Rule 4517]

Compliance is responsible for completion and filing of the appropriate regulatory form or application, which will be signed by a senior officer or partner of CEI. A hearing may be required prior to approval of the individual's association with CEI. The individual may not conduct any activities requiring registration until approval is received from the appropriate regulatory authorities.

2.8.4 Supervision

Compliance will establish procedures to carry out the supervision required under agreement with the SRO reviewing the disqualified person, including records of supervision to be conducted by the designated supervisor. The supervisor assigned to supervise the statutorily disqualified person will be provided a copy of the procedures and will be responsible for carrying them out.

2.8.5 Reporting Statutory Disqualifications

When an associated person becomes subject to a statutory disqualification, Compliance will file the necessary registration updates and, in addition, the required notification on the quarterly complaint report will be made to regulators consistent with those SRO's reporting requirements.

3. COMMISSIONS and OTHER COMPENSATION

3.1 Payment to Registered Persons Only

Except as set forth in this Section below, commissions are payable only to registered representatives or member firms. Payments of commission will not be made to unregistered business entities or in the name of a trade name or DBA.

3.2 Rep Codes

Each sales registered representative will be issued a Representative Code (Rep Code) for trading as well as accounting purposes. An RR number may be assigned internally prior to registration approval when customer accounts are being transferred and the RR number is needed to transfer accounts. However, the number is not approved for conducting business until all registration approvals have been received.

Joint Rep Codes or requests for Overrides must be approved by a principal. Registered Representatives may not share commissions with unlicensed persons, or with limited licensed persons in some cases.

3.3 Payout Grids

[Regulation Best Interest; DOL PTE 2020-2]

Payouts are generally established by agreement between the RR and CEI at one fixed payout percentage, and are product agnostic.

Payout grids, if used, will be product agnostic, meaning that registered representatives are paid the same percentage upon the sales of all product types.

Additionally, where CEI engages a retail sales registered representative with a grid or tiered payout, CEI will establish tiers no greater than 10% apart, and reasonably proportionate production levels between tiers. CEI will avoid grids that could unreasonably incent an advisor to make sales to reach a specified breakpoint, rather than a recommendation in the best interest of a retail client.

CEI does not engage in sales contests of products in a fixed-duration of time.

3.5 Promissory Notes (Forgivable)

CEI may in its discretion offer forgivable promissory notes and transition assistance to prospective registered representatives in order to be competitive in the independent broker-dealer world.

CEI will condition forgiveness on the Notes based upon time with the firm and not based upon production or any other measure which creates a conflict of interest.

The conflict that is created with a forgivable note will be disclosed in the registered representative's Financial Professional Brochure and provided to each customer at or before the first investment or account recommendation is given to the client.

3.6 Continuing Commissions Policy (RR Registrations Retained)

[FINRA Rule 2040(b)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests from retirees to continue commissions
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Obtain signed continuing commissions agreement from retiree • Notify designated supervisor and Accounting of agreement
Record	<ul style="list-style-type: none"> • Signed agreement retained in retiring associated person's file

RRs who retire may be eligible to participate in CEI's continuing commissions policy program. This program provides for the transfer of accounts from the retiring RR to another RR and gives the retiring RR the opportunity to provide support to the receiving RR as well as deal with customer transition issues. Retirees under the program sign a continuing commissions agreement; retain registration and licenses through CEI; and are eligible to earn commissions and other income through the term of the agreement.

The retiring RR continues to be subject to all the rules and regulations governing RRs and is subject to ongoing supervision by the RR's designated supervisor.

3.7 Continuing Commissions Policy (Registration Not Retained)

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests from retirees to continue commissions
Frequency	<ul style="list-style-type: none"> • As required - consider requests; obtain agreements • Annually <ul style="list-style-type: none"> ○ Obtain annual compliance certification from retired RR ○ Contact customers subject to the program
Action	<ul style="list-style-type: none"> • Determine RR's state of domicile permits paying continuing commissions without retaining registrations • Determine eligibility of RR • Obtain signed continuing commissions agreement from retiree • Notify designated supervisor and Accounting of agreement • Obtain annual compliance certification from retired RR

	<ul style="list-style-type: none"> • Contact customers subject to the program to verify the retired RR has not contacted them to discuss securities (sample includes a large percentage of high-net-worth customers) • Terminate arrangement no later than 5 years after retirement
Record	<ul style="list-style-type: none"> • Determination of RR's eligibility to participate • Signed agreement with RR • Annual compliance certification • Annual contact with customers to confirm the RR has not contacted them to discuss securities • Termination of RR's participation

RRs who retire may be eligible to participate in CEI's continuing commissions policy program. This program provides for the transfer of accounts from the retiring RR to another RR and gives the retiring RR the opportunity to provide support to the receiving RR as well as deal with customer transition issues. Retirees under the program sign a continuing commissions agreement and are eligible to earn commissions and other income through the term of the agreement.

The following conditions apply:

- Retirees must have been continuously employed with CEI for at least 3 years. (There are exceptions when an RR dies suddenly and his or her heirs participate in the program.)
- Retirees must have demonstrated professional conduct including a low incidence of customer complaints/arbitrations settlement or decided for more than \$25,000 in the 3 years prior to retirement or pending at retirement. If the retiree has been the subject of such complaints, CEI must determine that the complaints did not require disciplinary action or special supervision and the retiree was not at fault for improper sales practices. The retiree also must not have been subject to statutory disqualification during the 3 years prior to retirement.
- Retirees must contractually agree to cease all securities-related activities (cannot contact customers; cannot remain associated with any broker-dealer or investment adviser except for state registrations required to receive commissions; cannot take a job at a bank or insurance company that involves securities transactions).
- Retirees must obey all securities laws and regulations to the extent they remain applicable and must certify compliance annually.
- Receiving RRs (the RR to whom accounts are transferred) must be approved by the designated supervisor, have been in the industry for 3 years and at CEI for 1 year (with some exceptions) and must not have been subject to statutory disqualification during the prior 3 years.
- Continuing commissions are limited to 5 years after retirement.
- CEI will annually contact a sample of customers whose accounts are subject to the program (including a large percentage of high-net-worth customers) to ensure the retired RR has not contacted them to discuss securities.

3.8 Cash and Non-Cash Compensation Policy

[FINRA Rule 2310, 2320 and 2341; MSRB Rule G-20]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
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Resources	<ul style="list-style-type: none"> • Requests from RRs, managers, or outside firms regarding sponsorship of cash or non-cash compensation relating to the sale of securities
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review request and ensure compensation is consistent with rule requirements and limitations • Obtain Sponsor Request Form • Approve or disapprove compensation in writing • Obtain Reimbursement Form from sponsor with RR payment • Establish and maintain required records of approved compensation programs
Record	<ul style="list-style-type: none"> • Requests • Sponsor Request Forms • Reimbursement Forms • Approval/disapproval of compensation arrangement

Regulators' rules restrict compensation relating to the sale and distribution of debt, equity, direct participation program (DPP), REIT securities, and municipal securities. RRs may not accept (directly or indirectly) cash or non-cash compensation from outside firms or persons. The only exception includes compensation arrangements specifically approved by CEI.

3.8.1 Definitions

Cash compensation is defined as follows:

Any discount, concession, fee, service fee, commission, asset-based sales charge, loan or override, or cash associated person benefit received in connection with the sale and distribution of securities.

Non-cash compensation is defined as follows:

Any form of compensation received in connection with the sale and distribution of securities, other than cash compensation, which includes, but is not limited to, merchandise, gifts and prizes, travel expenses, meals and lodging.

3.8.2 Approval

Any compensation as defined in this section and paid directly to the RR requires sponsor submission of the Sponsor Request Form and approval by Compliance **prior to** accepting compensation. The following section outlines types of non-cash compensation permitted without specific approval, unless otherwise noted.

3.8.3 Types of Permissible Non-Cash Compensation

The following types of non-cash compensation are allowed provided they are **not preconditioned on achieving a sales goal**:

- Gifts amounting in aggregate value not exceeding \$100 annually, per person. All gifts must be reported to Compliance under CEI's Gifts, Gratuities and Entertainment policy.

- An occasional meal, ticket to a sporting event or show, or comparable entertainment that is not so frequent nor so extensive as to raise any question of propriety.
- Payment or reimbursement in connection with training or educational meetings, subject to several conditions. *Note:* Prior approval must be obtained from the designated supervisor before participating in such meetings.
- The location of the meeting is appropriate for its purpose, *e.g.*, a U.S. office of the offeror or member holding the meeting, or a facility located in the vicinity of such office, or a U.S. regional location with respect to meetings of associated persons who work within that region or where a significant or representative asset of a DPP or REIT is located (inspection of real estate, oil and gas production facilities, and other types of assets that will be held and managed by the program). The designated supervisor will determine the appropriateness of the meeting.
- Only expenses incurred by CEI or its associated persons are eligible for payment. Expenses for guests of associated persons (spouse, *etc.*) will not be reimbursed.

Non-cash sales incentive programs **preconditioned on achieving a sales goal** are not permitted by the firm.

4. GENERAL POLICIES CONCERNING REGISTERED AND ASSOCIATED PERSONS

4.1 Standards of Conduct

[FINRA Rule 2010]

Definitions:

The term “Access Person” used throughout this manual means a natural person who has physical or electronic access to CEI confidential information or Personally Identifiable Information (PII) of customers or Associated Persons of CEI.

The term "Associated Person" used throughout this manual means: (1) a natural person registered under FINRA rules; or (2) a sole proprietor, or any partner, officer, director, branch manager of the Applicant, or any person occupying a similar status or performing similar functions; (3) any company, government or political subdivision or agency or instrumentality of a government controlled by or controlling the Applicant; (4) any employee of the Applicant, except any person whose functions are solely clerical or ministerial; (5) any person directly or indirectly controlling the Applicant whether or not such person is registered or exempt from registration under the FINRA By-Laws or FINRA rules; (6) any person engaged in investment banking or securities business controlled directly or indirectly by the Applicant whether such person is registered or exempt from registration under the FINRA By-Laws or FINRA rules; or (7) any person who will be or is anticipated to be a person described in (1) through (6) above. [FINRA Rule 1011] [“Applicant” as used above means “CEI”]

It is CEI's policy and mandate to its Associated Persons to conduct CEI's business under the high standards and principles of the rules governing our industry. Associated persons are expected to deal with customers in a fair and honest way, with the customer's interest of primary concern.

CEI distributes written policies and procedures to all Associated Persons, including a Code of Ethics (herein below) during the on-boarding process and from time to time will issue updates as needed to personnel affected by the updates.

4.2 Outside Business Activities

[FINRA Rule 3270]

Responsibility	<ul style="list-style-type: none"> Registered Representative – Request approval; Disclose on U4 when required. Compliance – Initial requests review Designated Supervisor - Monitoring
Resources	<ul style="list-style-type: none"> Outside Business Activity Request for Approval form Annual certifications
Frequency	<ul style="list-style-type: none"> As needed
Action	<ul style="list-style-type: none"> Registered Representative: Submit OBA requests to Compliance or your Supervisor prior to engaging in the activity; Advise supervisor or Compliance when an OBA ceases activity or you are no longer engaged in the activity; maintain accurate disclosure of OBA activity on your U4 and Financial

	<p>Professional Brochure, and any other communications, advertising, or correspondence referencing the OBA</p> <ul style="list-style-type: none"> • Registered Representative's supervisor: <ul style="list-style-type: none"> ○ Monitor communications for unapproved OBA activity ○ Question associated person regarding potential unapproved outside business activities referenced in correspondence, web searches, social media or other indicators of outside business activity ○ Refer requests to Compliance • Compliance: <ul style="list-style-type: none"> ○ Consider whether the proposed activity will: <ul style="list-style-type: none"> ▪ Interfere with or otherwise compromise the associated person's responsibilities to CEI and its customers ▪ Be viewed by customers or the public as part of CEI's business based upon the nature of the proposed activity and the manner in which it will be offered ○ Determine whether the activity is an outside business activity or if it would be considered a private securities transaction subject to the requirements of the next section ○ Determine any limitations to be imposed prior to approval ○ Document the preceding via a memo to the associated person's file ○ Notify associated person of approval/disapproval and any limitations, in writing
Record	<ul style="list-style-type: none"> • Retention for 3 years, 2 years in a readily accessible location after termination of the Registered Representative: <ul style="list-style-type: none"> ○ Outside Business Activity Request forms including approval/disapproval and any limitations on the activity ○ Written notification to the associated person and his/her supervisor ○ Annual compliance questionnaires ○ Online review notes and printouts during on-boarding process and periodically

Registered Representatives are required to disclose to CEI, in writing, any outside business activities and obtain approval prior to engaging in such activity. Charitable activities are not included in this requirement unless the Registered Representative is being compensated. This policy applies to all Registered Representatives; if an OBA request is determined to be a private securities transaction, the Registered Representative must comply with the procedures relating to private securities transactions which are discussed in the next section.

Outside business activities may include a wide range of activities including but not limited to the following:

- Employment with an outside entity
- Acting as an independent contractor to an outside party
- Serving as an officer, director, or partner
- Acting as a finder
- Referring someone and receiving a referral fee
- Receiving compensation or having the reasonable expectation of compensation from any other person as a result of a business activity outside the scope of employment or other relationship with CEI

Compensation may include salary, stock options or warrants, referral fees, or providing of services or products as remuneration. Generally, remuneration consisting of anything of present or future value for services rendered may be considered compensation.

Procedure: Registered Representatives requesting approval to engage in outside business activities must complete the Outside Business Activity Request form and submit it to Compliance **prior to** engaging in the activity. Compliance will review, approve or disapprove the outside business activity in writing and notify the associated person and the associated person's supervisor. Compliance will evidence its analysis of any OBA that is potentially related to the provision of financial services other than registration through an entity affiliated with the firm by memorandum kept in the associated person's file. If the activity is determined to be a private securities transaction, the Registered Representative will be instructed to submit a PST Request Form pursuant to those procedures.

During the on-boarding process (within 60 days of registration) and periodically thereafter, Compliance will perform an online search using indicators to confirm the Registered Representative has reported all disclosable OBAs. Searches may include: personal and business email addresses, phone numbers, physical addresses, and state business registrations.

4.3 Private Securities Transactions

[FINRA Rule 3280]

<p>Responsibility</p>	<ul style="list-style-type: none"> • Associated Person: Request approval prior to engaging in private securities transactions • Designated Supervisor: Forward requests to Compliance; monitor communications for undisclosed PST activity • Compliance: Review and approve PST Requests
<p>Resources</p>	<ul style="list-style-type: none"> • Private Securities Transaction Request form • Annual Compliance Questionnaires • Other indications of potential "selling away" such as in correspondence
<p>Frequency</p>	<ul style="list-style-type: none"> • As needed
<p>Action</p>	<ul style="list-style-type: none"> • Associated Person: Request approval to engage in PST by submitting a PST request form to your Designated Supervisor or to Compliance • Designated Supervisor: <ul style="list-style-type: none"> ○ Refer requests or indications of private securities transactions to Compliance • Compliance: <ul style="list-style-type: none"> ○ Review requests and certifications ○ Follow up with Associated Person and supervisor regarding indicators of selling away ○ Notify associated person by PST Request Form or memo (with a copy to the associated person's supervisor) that private securities transactions are approved or not permitted

	<ul style="list-style-type: none"> ○ Maintain log of approved PST Requests ○ Take corrective action which may include: <ul style="list-style-type: none"> ▪ Disciplinary action against the Associated Person (letter of reprimand; fine, suspension; termination) ▪ Notification to private securities investors that CEI is not associated with the investment
Record	<ul style="list-style-type: none"> • PST Forms and Memos in associated person's file • Records of transactions and review/action taken

Associated Persons are not permitted to engage in private securities transactions (as defined by FINRA) without written approval of the firm, whether or not there is compensation paid for effecting the transaction. Private securities transactions are defined by FINRA as any securities transaction outside the regular course or scope of a Registered Representative's contract or employment with CEI (sometimes referred to as "selling away"). This does not include outside securities accounts approved by CEI, transactions with immediate family members where the associated person receives no selling compensation, and personal transactions in investment company and variable annuity securities.

Promissory Notes: Associated Persons should note that promissory notes often are securities. Even if a promissory note is not deemed a security, the Associated Person has the obligation to obtain CEI's permission **before** engaging in any outside business activity involving the offer of promissory notes.

Private Securities Transactions in which the Associated Person will earn direct or indirect compensation requires that CEI place the transaction(s) on its books and records as if it were its own transaction, and supervise it accordingly. PSTs, such as passive investments in offerings not offered by CEI, require notice to CEI and approval by CEI, however, such investments need not go on CEI's books and records and require no further supervision in that respect.

RIA activity, specifically trading in customer accounts held away from CEI and First Clearing, is deemed PST activity and requires approval as a PST. Please see section **4.5 Supervision of Unaffiliated Investment Advisers and Investment Adviser Representatives** in this manual.

4.4 Use of Other Names

Associated Persons who are permitted to establish business entities (sole proprietorship, partnership, corporation, *etc.*) under which they conduct business. The use of other business names or entities must be approved by CEI prior to use. Requests for approval are to be directed to Compliance using an OBA Request form and include, among other things:

- the name of the business entity
- description of the type of entity (partnership, corporation, *etc.*)
- description of what types of business will be conducted under the business entity

Compliance is responsible for reviewing requests to establish or conduct business through the business entity and approving or disapproving the request. Compliance may request additional documents including corporate formation or partnership documents, and will retain a record of the requests and approval or disapproval.

4.5 Supervision of Unaffiliated Investment Advisers and Investment Adviser Representatives

[FINRA Notice to Members 96-33, 94-44 and 91-32]

Associated Persons (APs) or their business entities may be independently registered as investment advisers (through CEI's affiliate Coastal Investment Advisors, Inc. or otherwise), however, the investment adviser activities are subject to the supervision of CEI required under FINRA NtM 96-33 and its progeny.

Requests to Engage in Activity as an Investment Adviser:

Request to register with CEI's affiliated RIA should be submitted on an OBA Request form to Compliance for review and approval.

Independent registration as an investment adviser with an unaffiliated RIA requires the approval of CEI prior to engaging in investment adviser activities. Requests for such approval should be submitted to Compliance for review and approval by submitting the Private Securities Transaction Form and include the following:

- the name under which the investment adviser activity will be conducted
- whether the registered representative will be executing trades away from CEI (as opposed to referrals to money managers or acting as a solicitor only)
- a copy of Form ADV for the adviser

Compliance may request other information, as necessary, to complete its review of the request. Individuals who do not trade away from CEI will not require that the firm place the transactions on its books and records. Otherwise, upon approval, Compliance will notify operations in order for CEI to obtain duplicate statements and confirmations, or access to the confirmation blotters of the independent RIA.

Compliance will retain a copy of the request and the approval or disapproval. IA activity should be reported on registered representatives' U4s as Outside Business Activity.

Trade Review

Registered Representatives who engage in trading activity in her/his capacity as an IAR away from CEI are engaged in Private Securities Transactions, and such transactions must be placed on the books and records of CEI and supervised by CEI in accordance with these procedures. However, if the IAR is not trading, but merely placing the account(s) into a portfolio model or with a third-party money manager for example, then the IAR is not engaging in a Private Securities Transaction, and therefore CEI will not be required to obtain trade data or to supervise such data.

Otherwise, when approved, Operations will contact the outside RIA's custodian(s) in order to arrange for download of the IC's trade confirmation blotter (or, notwithstanding the custodian's vernacular, any trade blotter providing substantially the same information as the confirmation blotter) and will ensure that the Outside RIA trade review supervisor ("OTR Supervisor") has access to the blotters.

The OTR Supervisor will on at least a monthly basis review the confirmation blotters of all AP's for suitability. Suitability review will specifically include review of the products purchased to determine whether they are consistent with the investment strategy set forth in the outside RIA's disclosure brochure. The OTR Supervisor may make inquiry regarding the suitability of unusual trading activity by contacting the IC or outside RIA CCO and/or requesting additional account documentation including customer account brokerage agreements and advisory agreements. The OTR Supervisor will evidence her/his review by maintaining a review log, noting the

blotters reviewed and the date reviewed. Any inquiries regarding unusual trading activity will be memorialized in a formal memorandum and forwarded to Compliance.

Communications

All IC email and paper correspondence will be reviewed consistent with the procedures set forth in the Retail Communications chapter of this manual.

RIA Due Diligence

The AP (or the RIA's CCO) will also complete the firm's Annual Compliance Questionnaire for outside RIAs. Compliance will review any reported customer complaints, regulatory investigations, and other items reported to the firm in the Questionnaire, and report any material deficiencies to management for consideration, including whether to increase supervision of the registrant's activities, revocation of permission to engage in the outside activity, to exit the firm, or otherwise.

4.6 Associated Person and Associated Person Related Accounts

4.6.1 Related Accounts Defined

[FINRA Rule 3110(d)(4)]

Associated Person and related accounts ("covered accounts") are subject to review by CEI. Covered accounts include:

- the spouse of a person associated with the member;
- a child of the person associated with the member or such person's spouse, provided that such child resides in the same household as, or is financially dependent upon, the person associated with the member;
- any other related individual over whose account the person associated with the member has control; or
- any other individual over whose account the associated person of the member has control and to whose financial support such person materially contributes.

In addition, accounts subject to review include any account where an employee has a beneficial interest or the authority to make investment decisions (for example, trust accounts, accounts for minors, *etc.*).

4.6.2 Outside Accounts

[FINRA Rule 3210; FINRA FAQs on Rule 3210: <https://www.finra.org/rules-guidance/rulebooks/finra-rules/3210/faq>]

Responsibility	<ul style="list-style-type: none"> • Associated Person: Submit written request to open or maintain outside account on Outside Account Request Form • Compliance: Review and Approve requests • Designated Supervisor: Review transactions
Resources	<ul style="list-style-type: none"> • Requests for outside accounts • Annual certifications • Other
Frequency	<ul style="list-style-type: none"> • As needed

	<ul style="list-style-type: none"> • New Associated Persons: within 30 days of registration
Action	<ul style="list-style-type: none"> • Associated person: <ul style="list-style-type: none"> ○ Submit requests to Compliance • Compliance: <ul style="list-style-type: none"> ○ Review requests ○ Notify associated person of approval or disapproval ○ Notify firm carrying the associated person's outside account by letter regarding to whom duplicate confirmations and statements should be sent, or obtain feed from firm; If the carrying firm is a non-member and the ability to receive confirmations and statements is limited, consider whether the account should be approved. • Associated person's supervisor: <ul style="list-style-type: none"> ○ Review accounts ○ For transactions in restricted securities, contact the associated person and take corrective action which may include cancellation of the transaction ○ For trading activity that may be indicative of law or rule violations, refer to compliance, who will conduct an internal investigation
Record	<ul style="list-style-type: none"> • Approval/disapproval of outside account in associated person's file • Confirmations/statements initialed and dated, and filed in associated person's file; or log of review by supervisor • Record of internal investigation, if applicable • Quarterly report to FINRA of any internal investigations pursuant to this section, if CEI engages in investment banking activities

It is the recommendation of CEI that associated persons maintain their securities accounts at CEI. Otherwise, CEI requires written approval by Compliance prior to opening the account. Compliance will request duplicate confirmations and statements from the other broker-dealer carrying the associated person's account, or a direct feed from the other broker-dealer. This includes accounts with a commodities firm to trade security futures and any accounts where the employee has a beneficial interest.

Accounts where the employee is presumed to have a beneficial interest include the account of:

- a spouse
- a child of the associated person or the associated person's spouse, provided the child resides in the same household or is financially dependent upon the associated person
- any other related individual over whose account the associated person has control
- any other individual over whose account the associated person has control and to whose financial support the associated person materially contributes

There may be exceptions to the presumption if the associated person can demonstrate to Compliance that the associated person derives no economic benefit from, and exercises no control over, the account.

The associated person is also obligated to notify in writing the broker-dealer or other institution prior to opening the account that the person is associated with the Firm. Accounts opened prior to association with the Firm are

subject to the same approval requirement by Compliance and notification to the carrying institution within 30 days of registration or association with the Firm.

These requirements do not apply to accounts limited exclusively to transactions in unit investment trusts and variable contracts or redeemable securities in mutual funds.

4.6.3 Review of Transactions in Outside Accounts

[FINRA Rule 3110(d)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Compliance: internal investigations and FINRA reporting when required
Resources	<ul style="list-style-type: none"> • Statements and confirmations • Blotter or feed from custodian
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Review associated person and associated person related accounts for possible concerns regarding: <ul style="list-style-type: none"> ○ Very active trading ○ Sizeable debit balances ○ Bounced checks ○ High risk trading patterns ○ Transfers between accounts, particularly associated person or related accounts and customer accounts ○ Insider trading ○ Transactions in securities restricted by the Firm ○ Transaction in new issues • Where items of concern are identified, action to be taken depends on the circumstances and may include conducting an internal investigation to identify potential rule/law violations
Record	<ul style="list-style-type: none"> • Record of review of transactions and actions taken, if applicable • Record of internal investigation, if applicable • Record of review of accounts and actions taken, if applicable • Quarterly report to FINRA of internal investigations, if CEI engages in investment banking activities

Transactions in associated person and associated person related accounts are reviewed on an ongoing basis. Associated persons will be contacted about transactions that are potentially contrary to rules or Firm policy.

For transactions in restricted securities, contact the associated person and take corrective action which may include cancellation of the transaction.

For trading activity that may be indicative of law or rule violations, refer to compliance, who will conduct an internal investigation.

4.6.4 Insider Trading

[SEC Securities Exchange Act of 1934 Rule 10b-5 and Section 10]

Associated persons are prohibited from effecting transactions based on knowledge of material, non-public information. The chapter *INSIDER TRADING* explains CEI's policy and all associated persons are expected to be familiar with the policy.

Designated supervisors should review account activity for red flags of insider trading such as:

- Short term trading resulting in large gains.
- Unexplained sales or purchases of securities just prior to favorable or unfavorable news concerning the issuer which was related to non-public information and which significantly moved the market for that security.
- Sales of securities in an insider's account relating to the insider's employer or an affiliate.

4.6.5 Sharing In Accounts

[FINRA Rule 2150]

Responsibility	<ul style="list-style-type: none"> • Associated Person: Submit written requests to Compliance • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New account forms • Requests to open accounts jointly with customers
Frequency	<ul style="list-style-type: none"> • As needed
Action	<ul style="list-style-type: none"> • Associated Person's supervisor: <ul style="list-style-type: none"> ○ When approving new accounts, identify accounts where an Associated Person is potentially sharing in the account ○ Confer with associated person as to the nature of the shared account (what is the relationship between the associated person and the other account owner, allocation of profits and losses) ○ Refer shared accounts or requests to share in an account to Compliance • Compliance: <ul style="list-style-type: none"> ○ Require written request from associated person and written authorization from customer ○ Review and determine whether shared account is appropriate ○ Approve or disapprove the request ○ Notify associated person and supervisor of approval or disapproval
Record	<ul style="list-style-type: none"> • Copies of associated person request, customer's written authorization, and notation of approval or disapproval is retained with the new account records for the account

CEI and its associated persons may not share directly or indirectly in the profits or losses of a customer's account (with the exception of performance-based fees specifically permitted under rules governing investment adviser and other permitted arrangements). As a general policy, associated persons may not participate in an account that includes customers who are not family members of the associated person.

An associated person may be a joint owner in an account with a customer only under the following conditions:

- the associated person submits a written request to Compliance accompanied by signed authorization from the customer
- the associated person is a disclosed owner of the account
- the associated person shares in losses and gains only in proportion to the associated person's monetary contribution to the account (not applicable to accounts shared with immediate family members)
- the associated person receives written approval from Compliance

4.6.6 Prohibition on Purchases of Initial Public Offerings (IPOs)

[FINRA Rule 5130]

Associated persons and their immediate families (parents, spouse, children, in-laws, siblings) are prohibited from purchasing IPOs. This includes sales to anyone materially supported by an associated person or a member of the associated person's immediate family.

4.7 Gifts, Gratuities and Entertainment

[FINRA Rule 2310(c)(2)(A), 2320(g)(4)(A), 2341(l)(5) and 3220]

Responsibility	<ul style="list-style-type: none"> • Associated Person: Submit Requests to Designated Supervisor • Designated Supervisor review and approve gift requests
Resources	<ul style="list-style-type: none"> • Gift Approval Form • Expense reports (if any) Gifts Gratuities and Non-Monetary Compensation Log
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Associated Person's supervisor: <ul style="list-style-type: none"> ○ Review gift requests and approve if compliant ○ Refer requests regarding union gifts and gratuities to Compliance ○ Copy all approved requests to Compliance ○ Review expense reports for reasonableness and compliance with expense policies and approve or disapprove ○ Review and approve or disapprove gifts and gratuities to be given, aggregated on a calendar year basis to determine compliance with the \$100 annual limit • FINOP: <ul style="list-style-type: none"> ○ File Form LM-10 with Dept. of Labor if necessary ○ Review employee expense reports for reasonableness and compliance with this section
Record	<ul style="list-style-type: none"> • Gift Approval Forms are maintained in a branch/department file • Employee expense reports are maintained in Accounting (if any)

	<ul style="list-style-type: none"> • FINOP maintains a file for LM-10 filings
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Gifts, gratuities, and entertainment are subject to regulators' limitations. Failure to comply may result in fines or other regulatory actions against the associated person and CEI. **It is important for all** associated persons to know and comply with this policy. Questions regarding this policy on gifts and entertainment should be referred to Compliance. Key requirements include:

- **Gifts to others are limited to \$100 per year per person** (other than "personal gifts" defined in the policy).
 - Multiple gifts to the same person are aggregated, *i.e.*, the total of all gifts in any year firm-wide cannot exceed \$100 to one person.
 - "Personal gifts" are excluded (as discussed below).
- **Receiving** gifts is limited.
- An **associated person must host entertainment** to avoid entertainment being considered a "gift" subject to limitations.
- **Records of entertainment** must include details of who was entertained and the nature of entertainment.
- **Gifts to labor union** associated persons require prior Compliance approval.
- **Gifts to public officials require prior Compliance approval.**
- **Your supervisor must be notified** of gifts to others.
- **Your supervisor must be notified** of gifts received (other than personal gifts).
- Gift requirements (whether the gift is given or received) **do not apply to personal gifts** to immediate family members (parents, children, grandparents, siblings, spouse, in-laws) who also happen to be customers and where the gift is unrelated to CEI's business. The policy also does not apply to occasional personal gifts to others (such as a wedding gift or a congratulatory gift for the birth of a child).
- **If CEI pays for the gift or reimburses the associated person for the cost of the gift, the gift is subject to the requirements of this policy.**
- **Gifts incidental to entertainment** (*e.g.*, a golf shirt given during a golf outing, *etc.*) are considered gifts subject to reporting to Compliance and the gift limitations.

4.7.1 Gifts to Others

Associated persons are required to submit the Gift Approval Form to their supervisor prior to giving a gift (other than a *de minimis* gift described below). Gifts relating to CEI's business are limited to \$100 per year per person. Gifts of tickets to sporting events or similar gifts where the associated person does not accompany the recipient are subject to the limitations on gifts and gratuities. Such gifts may not be so frequent or so expensive as to raise a suggestion of unethical conduct.

Associated persons of regulators are also subject to rule limitations regarding gifts to them from broker-dealers and their associated persons. Compliance should be contacted for guidance before giving gifts to associated persons of regulators.

Gifts and gratuities are not permitted when given for the purpose of influencing or rewarding the action of a person in connection with the publication of information which has or is intended to have an effect upon the market price of any security.

4.7.1.1 De Minimis and Promotional Items

The policy does not apply to gifts of *de minimis* value (such as pens, notepads, or modest desk ornaments) or to promotional items of nominal value with CEI's logo (*e.g.*, umbrellas, tote bags or shirts). Promotional items must be valued substantially below the \$100 limit to be excluded from the gift policy. Items of higher value (near \$100 or more), even if they include CEI's logo, are considered "gifts" subject to this policy.

FINRA excludes customary lucite tombstones, plaques or other decorative items commemorating a business transaction. This exemption is very limited; other items are considered gifts subject to the policy, even if they commemorate a business transaction.

4.7.1.2 Aggregation of Gifts

The annual gift limitation is the aggregate of all gifts given to any one individual. For example, a gift of a \$75.00 ticket to a football game in November (as a gift and not as entertainment discussed below) and then a holiday gift of a \$50.00 bottle of wine to the same person in the same year would be in violation of the \$100 limitation.

Each recipient is limited to \$100 in **total** gifts during any calendar year.

Supervision will maintain a log of each Associated Person's gifts on a calendar year basis and maintain the log in the Associated Person's home office file. Supervisors should consult the log prior to approving a gift to ensure the limit will not be exceeded. If approved, the supervisor will log the gift.

4.7.1.3 Valuation Of Gifts

Gifts are valued at the higher of cost or market value excluding tax and delivery charges. For tickets, it is the higher of cost or face value. If gifts are given to multiple recipients, the names of all recipients are recorded and the value of the gift is prorated among recipients. For example, a \$250 fruit basket given to an office of three individuals is permitted since the value of the gift prorated is less than the \$100 limitation per person.

4.7.2 Accepting Gifts

Associated persons may not solicit gifts or gratuities from customers or other persons with business dealings with CEI. Associated persons are not permitted to accept gifts from outside vendors currently doing business with CEI or seeking future business without the written approval of Compliance. This policy does not include customary business lunches or entertainment; promotional items (caps, T-shirts, pens, *etc.*); or gifts of nominal (less than \$100.00) value. When accepting gifts from customers or other business-related persons, the associated person is required to submit the Gift Approval Form to his or her supervisor.

4.7.3 Entertainment

Entertainment of customers or prospective customers must be reasonable and not so expensive it raises a suggestion of unethical conduct. All entertainment and related expenses must be detailed on an expense form with receipts attached for expenses over \$25.00. Expense forms should be submitted to the appropriate supervisor within 30 days of incurring the expenses.

The limitation on gifts and gratuities does not apply to usual business entertainment such as dinners or sporting events where the associated person hosts the entertainment, though such expenses should be reasonable. "Entertainment" includes a broad range of activities such as trips, parties, and other activities where an associated person hosts someone related to CEI's business. Questions regarding the reasonableness of proposed entertainment and related expenses should be referred to Compliance.

4.7.3.1 Gifts Incidental to Business Entertainment

Items given in conjunction with entertainment (a golf shirt at a golf outing; a fruit basket delivered to a customer's room during a firm outing) are considered gifts subject to the \$100 limitation.

4.7.4 Gifts, Loans, And Entertainment Involving Unions and Union-Affiliated Individuals

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Compliance: Review gifts and entertainment involving public officials
Resources	<ul style="list-style-type: none"> • Expense reports • Annual Employee Certification
Frequency	<ul style="list-style-type: none"> • Annual
Action	<ul style="list-style-type: none"> • File Form LM-10 within 90 days of fiscal year end • Include reportable gifts, loans, entertainment, <i>etc.</i> excluding de minimis amounts of \$250 or less • Review Annual Employee Certifications to identify union-related gifts, loans, <i>etc.</i> and follow up to include item in annual reporting on Form LM-10
Record	<ul style="list-style-type: none"> • Vouchers, worksheets, receipts, and other records • Filed Form LM-10 (retained for 5 years) • Gift Approval Forms • Annual Employee Certifications with notes of action taken, if any

The Department of Labor (DOL), under a federal act, requires CEI to report any payment or loan, direct or indirect, of money or other things of value (including reimbursed expenses), or any promise or agreement to make such payments, to any labor organization or officer, agent, shop steward or other representative or associated person of a labor organization. This includes entertainment (cost of meals, *etc.*), expenses, or giving gifts or other things that exceed \$250.00 in value where the recipient or beneficiary involves a union or union-affiliated individual.

When reporting gifts, entertainment, loans, and other payments, associated persons must identify when a union or union-affiliated individual is involved. Associated persons are obligated to report such items to CEI regardless of the dollar amount involved.

4.7.5 Gifts or Payments to Public Officials Under State Laws

A "public official" is anyone who is elected or appointed to an office or is an employee of a "public entity" including any teacher or professor employed by a public entity. A "public entity" is broadly defined and includes political bodies, municipalities and their governing bodies (school district, school board, *etc.*), public universities and colleges as well as any other municipal entity. This policy also includes honorarium payments (payments for any speech given, article published, or attendance at any public or private conference, convention, meeting, social event, or similar gathering).

Some public entities are statutorily authorized to charge the cost of inspections of regulated entities. A public official may, therefore, receive payment for statutorily-authorized expenses. For example, if a state securities official appears at an office to conduct an inspection, the state may, if authorized in state statutes, charge Coastal Equities, Inc. for expenses related to conducting the inspection.

Prior approval from Compliance is required for gifts or entertainment involving public officials.

4.8 Privacy Policy

[SEC Regulation S-P]

Information regarding customer accounts for individuals is subject to SEC Regulation S-P "Privacy Of Consumer Financial Information." This section explains associated persons' obligation to maintain the privacy of information. A section *Customer Privacy Policies and Procedures* in the chapter *COMMUNICATIONS WITH THE PUBLIC* outlines firm procedures.

1. Regulation S-P requirements apply to individual and not institutional accounts and include U.S. and foreign accounts.
2. Protected information is termed "nonpublic personal information." This is information obtained by CEI that is not deemed "public information" which is defined as information that may be obtained from three sources: federal, state or local government records; widely distributed media; or disclosures to the general public that are required to be made by federal, state, or local law.
3. At the time an account is opened the customer is provided with CEI's privacy policy and is given the opportunity to opt out of arrangements to share nonpublic information with nonaffiliated third parties. The privacy policy is also provided to customers on an annual basis.
4. Associated persons are prohibited from sharing or releasing nonpublic personal information other than to authorized parties. This includes a prohibition against:
 - o Sending internal reports or other information about firm customers to a non-affiliated 3rd party (unless authorized).
 - o Sending internal or other documents that include customer non-public information to your personal e-mail address.

Questions about providing customer information should be referred to Compliance.

4.9 Reporting Possible Law or Rule Violations

[SEC Securities Exchange Act of 1934 Section 21F; SEC Rule 21F; FINRA Rule 4530(b)]

Responsibility	<ul style="list-style-type: none"> • Chief Compliance Officer (or, if the CCO is involved in the potential wrongdoing, the CEO)
Resources	<ul style="list-style-type: none"> • Reports of possible law or rule violations from associated persons • Referrals from outside sources such as regulators
Frequency	<ul style="list-style-type: none"> • Investigate reports: As required • Associated person education: periodically
Action	<ul style="list-style-type: none"> • Acknowledge the associated person's report and advise confidentiality will be maintained and there will be no retaliation for reporting

	<ul style="list-style-type: none"> • Determine who will be involved in the investigation and notify those persons of the confidentiality of the investigation • Conduct the investigation using tools appropriate to the issue (interviewing associated persons, reviewing internal/external reports, engaging counsel, etc.) • Determine whether there was potential wrongdoing and decide whether a report should be made to regulators • Take internal corrective action, as appropriate • Advise the reporting associated person of the status of the investigation • Include reporting of possible law or rule violations and CEI's process for internal investigations as part of regular associated person education
Record	<ul style="list-style-type: none"> • Report from associated person • Information regarding the investigation including records reviewed, who is involved, what steps taken, reports to regulators (if appropriate), conclusion of investigation • Records of associated person education including how education is conducted (classes, online education, compliance memos, etc.), who participates, subjects included, and when it occurs

It is the intent of CEI to adhere to all laws and regulations that apply to the organization; the underlying purpose of this policy is to support the organization's goal of legal compliance. The support of all associated persons is necessary to achieve compliance with various laws and regulations.

4.9.1 Reporting

Associated persons should report possible crimes or rule violations involving CEI, a department, or an associated person or associated persons as well as outside vendors or service providers. Reporting may be made to any or all of the following, particularly where the associated person's supervisor may be involved in the possible wrongdoing.

1. Your supervisor
2. Chief Compliance Officer
3. General Counsel
4. Chief Executive Officer

4.9.1.1 Ombudsman

CEI has named an ombudsman who is independent and whose responsibility is to investigate possible wrongdoing at any level of CEI. Associated persons may contact the ombudsman as follows:

Francis J. Skinner, Chief Legal Officer, (888) 657-5200 x799 or email fskinner@coastal-one.com.

4.9.2 Confidentiality of Employee Reporting

All reports will be treated as confidential. The associated person's identification will be kept confidential other than to those who need to know such as the compliance officer, counsel or someone else conducting an investigation. Any person identified in the report as a potential wrongdoer will not be provided the name of the person who has filed a report.

4.9.3 Notification of Chief Compliance Officer

A supervisor or other manager who receives a report of possible violations should immediately refer the matter to the Chief Compliance Officer who is responsible for conducting an investigation and overseeing the review until its conclusion, including potential reporting to a regulator. If the Chief Compliance Officer is involved in the potential wrongdoing, the member of management to whom the issue is reported will be responsible for conducting the investigation.

4.9.4 Investigation

CEI will promptly investigate the reported possible wrongdoing and determine what action is required. Outside counsel may be engaged as part of the investigation. The reporting associated person will be advised of the conclusion or resolution of the investigation.

4.9.5 Anti-Retaliation

CEI will not retaliate against an associated person who reports some practice of CEI, a department, or associated person(s) or of another individual or entity with whom CEI has a business relationship that may represent a rule or law violation. CEI will not retaliate against associated persons who disclose or threaten to disclose (to CEI or a public body such as a regulator) any activity, policy, or practice of CEI that the associated person believes is in violation of a law, or a rule, or regulation mandated pursuant to law.

Supervisors and others are prohibited from engaging in discipline, threats, or discriminatory actions against associated persons for engaging in whistleblowing activities.

4.9.6 Federal Whistleblower Laws and Rules

The Securities Exchange Act includes Sec. 21F and the SEC has adopted Rule 21F to implement Sec. 21F that provides for reporting possible violation of federal securities laws and potential rewards for information that leads to successful enforcement of a covered judicial or administrative action where monetary sanctions equal \$1,000,000 or more. The Sarbanes-Oxley Act of 2002 (which governs public companies) and the Foreign Corrupt Practices Act (FCPA) also have whistleblower provisions.

4.10 Solicitation of Charitable Contributions

[FINRA Notice to Members 06-21]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Charitable Contribution Approval Request Form
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Review contribution to identify potential conflicts of interest• Approve or disapprove
Record	<ul style="list-style-type: none">• Charitable Contribution Approval Request forms

When an associated person or an agent of a customer such as a mutual fund, pension plan, or investment manager solicits a substantial charitable contribution from CEI or an RR, there may be a conflict of interest. For example, if an investment manager requests a \$10,000 contribution to a charity, this could be construed as a condition for the investment manager to direct business to CEI. There can be no quid pro quo between contributions and business conducted with CEI.

To avoid potential conflicts of interest, CEI has established the following guidelines for handling such requests.

1. Charitable giving by CEI or foundations created by CEI is subject to review by the CEO or the CEO's designee on a periodic basis.
2. Contributions of \$5,000 or more solicited by an associated person or agent of a customer require completion of the Charitable Contribution Approval Request form and the prior approval of Compliance as well as the approval of someone representing the customer other than the person soliciting the contribution. Requests should be submitted by completing the Charitable Contribution Approval Request form.
3. Contributions cannot be based on the actual or anticipated level of business done by the customer.
4. These requirements do not apply to a retail customer who solicits a charitable contribution when acting in his or her individual capacity.

4.11 Media Contact Is Limited to Certain Authorized Employees

Responsibility	<ul style="list-style-type: none"> • Chief Executive Officer
Resources	<ul style="list-style-type: none"> • Requests to communicate with the media • Indications an unauthorized person has had media contact
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • For requests, determine nature of contact and whether the individual is or should be authorized to engage in the contact • If necessary, notify the associated person whether contact will be permitted and provide guidelines • For unauthorized contact, confer with the associated person (and the associated person's supervisor, if appropriate)
Record	<ul style="list-style-type: none"> • Maintain a list of authorized persons and any limitations on their contact, if appropriate, in these procedures; if exceptions are granted, maintain a list of authorized persons and any limitations on their contact

CEI is sometimes contacted by media representatives (television, radio, newspapers, magazines, and other types of media other than social media posts). Associated persons who are contacted by media representatives are not permitted to comment but must refer the representative to one of the following individuals within CEI:

- Charles F. Reiling, III, President

Individuals authorized to speak to the media are expected to make comments consistent with good taste and CEI's opinion or position on matters discussed.

4.12 Requests for Information from Outside Sources

Responsibility	<ul style="list-style-type: none">• Associated Person and Designated Supervisor: forward request to Legal or Compliance as applicable• Chief Legal Officer• Chief Compliance Officer
Resources	<ul style="list-style-type: none">• Written or oral requests for information• Subpoenas• Other attorney LOAs with document requests
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Compliance/CLO: Provide response, as appropriate
Record	<ul style="list-style-type: none">• Retain record of response in legal, regulatory, or other files

CEI and its associated persons are sometimes contacted by outside parties such as regulators (SEC, FINRA, exchanges, state and other regulators), attorneys and governmental agencies (e.g., the IRS) that request information about customer accounts, CEI activities, or an individual associated person's activities.

Information regarding customer accounts, CEI and its associated persons is considered confidential and may be released only to those authorized to receive it. Any requests from outside parties (other than the principal or authorized person on behalf of an account requesting information on the account) should be immediately referred to the Chief Legal Officer for response. This includes requests received in any form whether written, by phone, or in person. This also includes visits by regulators. Proof of identification should be requested and Compliance immediately notified.

4.13 Internal Reviews and Investigations

If necessary, CEI may conduct an internal review or investigation. Associated persons may be requested for information that may include an associated person's signed written statement. Failure to provide requested information may result in disciplinary action, including termination.

4.14 Internal Disciplinary Actions

CEI's goal in administering discipline is to take measures to maintain the quality of service provided to our customers by encouraging appropriate behavior. The expected result of these measures is the deterrence of inappropriate behavior and, when improper activity occurs, to take corrective action commensurate with the activity.

4.14.1 When Disciplinary Action Is Considered

Although it is impossible to list all circumstances in which discipline may be imposed, disciplinary action will be considered when there is:

- An admitted violation of company policy, regulatory rules or regulations, or federal/state laws.

- A determination of an actual or probable violation of company policy, regulatory rules or regulations, or federal/state laws.

4.14.2 Who Determines Disciplinary Action

Compliance and management personnel, including some or all of the Board of Directors, CEO, COO, FINOP, and CCO, will consult and deliberate upon whether disciplinary action is warranted in any given situation. Although Compliance will not be the primary decision maker in determining disciplinary action, it is **essential** that Compliance be notified **in advance** of all disciplinary actions in order to analyze such actions for regulatory reporting purposes and for adequate recordkeeping of disciplinary information. Compliance may modify the terms of discipline outlined in the action depending on the facts and circumstances of the situation.

4.14.3 Types of Discipline

There is a range of possible disciplinary action; the level of discipline will be determined by Compliance. Compliance will collaborate with the individual's supervisor who will be copied on any communications to the individual regarding the disciplinary action.

Letter of Education (LOE): An LOE is a memorandum concerning any issues which may have arisen in a branch, but not necessarily the FA to whom the LOE is directed, or involving an issue concerning the FA which may be operational or a first-time compliance matter. The LOE will outline the operational process or compliance procedure at issue as well as possible consequences for repeat violations. The LOE requires the recipient's signature certifying his/her receipt of the memorandum and understanding of the matter.

Letter of Caution (LOC): An LOC is a memorandum that specifies a possible violation and/or serves as a warning of inappropriate behavior. The LOC outlines the expected behavior and the possible consequences of future violations similar in nature. The LOC requires the recipient's signature certifying his/her receipt of the memorandum and understanding of the matter.

Admonishment: An Admonishment is a memorandum that formally reprimands an individual based on admitted or determined violations. The Admonishment specifies the admitted or determined violation and the expected behavior. It specifies the possible consequences of future violations similar in nature and may be administered with a **Non-reportable** or **Reportable Fine** (see below). The Admonishment requires the recipient's signature certifying his/her receipt of the memorandum and understanding of the matter.

Non-reportable Fine: A Non-reportable Fine is a monetary sanction that is less in amount than that which is required to be reported to a self-regulatory organization (SRO). Non-reportable fines will usually be attached to an **Admonishment** (see above) and/or **Suspension of Employment**. In any event, the admitted or determined violation will be specified along with the expected behavior and possible consequences of future violations similar in nature.

Non-reportable fines will be withheld from a producing-associated person's commissions. In the case of a non-producing associated person, the fine will be collected in the form of personal or certified check or money order.

Reportable Fine: A Reportable Fine is a monetary sanction that is greater than or equal to the amount that is required to be reported to an SRO. Reportable fines will usually be attached to an **Admonishment** (see above) and/or **Suspension of Employment**. In any event, the admitted or determined violation will be specified along with the expected behavior and possible consequences of future violations similar in nature.

Reportable fines will be withheld from a producing-associated person's commissions. In the case of a non-producing associated person, the fine will be collected in the form of personal or certified check or money order.

Suspension of Employment: An associated person may be suspended for violations of applicable company policy, regulatory rules or regulations, or federal/state laws. Prior to Suspension of Employment, the associated person will be informed of the violation, the expected behavior, and the terms of the suspension.

While under suspension, associated persons may not:

- Have direct or indirect contact with customers
- Act as a registered representative
- Represent oneself as a registered representative
- Give investment advice or counsel
- Receive compensation
- Transact business in any securities account (other than a personal account)
- Have contact with company associated persons except the associated person's supervisor or Compliance
- Enter into any company premises

A Suspension of Employment memorandum will be delivered to the associated person. This document will specify the admitted or determined violation and the expected behavior. It will also specify the possible consequences of future violations similar in nature. The Suspension of Employment memorandum may require the recipient's signature certifying his/her receipt of the memorandum and understanding of the matter. Suspensions will be reported by Compliance to the appropriate SRO(s).

Termination of Employment: An associated person's employment may be terminated for violations of company policy, regulatory rules or regulations, or federal/state laws. The associated person will be informed of the violation and termination of employment.

Termination will be reported by Compliance to the appropriate SRO(s).

4.14.4 Additional Action

The associated person may be subject to Heightened or Special Supervision as outlined in the chapter *EMPLOYMENT, REGISTRATION AND LICENSING*. The associated person may also be subject to added education, re-testing for licensing, title downgrading, or other remedial actions deemed appropriate by Compliance.

4.14.5 Considerations in Determining Type of Discipline

The nature of the inappropriate conduct is important in determining the type of discipline to be imposed. The more serious the conduct, the more severe the discipline. An associated person's prior complaint and disciplinary history will be considered in determining the appropriate level of discipline. The activity's risk to CEI, injury to customers, and the associated person's cooperation may all be factors (among others) in determining the discipline.

4.15 Employee Obligation to Notify the Firm and the Firm's Obligation to Report

[FINRA Rule 4530]

Responsibility	<ul style="list-style-type: none"> • Associated Persons: Report disclosable events and changes to information on U4 to Compliance • Designated Supervisor - Notification of possible reportable events to Compliance
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	<ul style="list-style-type: none"> • Chief Compliance Officer - Determination of whether events are reportable, and applicable reporting
Resources	<ul style="list-style-type: none"> • Information provided by associated persons including information from Annual Employee Certifications • Lawsuits and arbitrations • Regulatory actions • Criminal actions • FINRA compliance reports
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Determine whether information or events are reportable including updating the RR's Form U4 or U5 • File information electronically with FINRA
Record	<ul style="list-style-type: none"> • Record of electronic filings • Records of updates to Form U4 or U5

Regulators require reporting of certain events and updating of Forms U4 and U5 when previously-filed information changes. Associated persons are obligated to notify Compliance if there are changes to Form U4 responses and report other information required by rule or by **CEI**.

The following is an excerpt from FINRA Rule 4530 that outlines events that require reporting:

1. the member or an associated person of the member:
 - has been found to have violated any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body, self-regulatory organization or business or professional organization;
 - is the subject of any written customer complaint involving allegations of theft or misappropriation of funds or securities or of forgery;
 - is named as a defendant or respondent in any proceeding brought by a domestic or foreign regulatory body or self-regulatory organization alleging the violation of any provision of the Exchange Act, or of any other federal, state or foreign securities, insurance or commodities statute, or of any rule or regulation thereunder, or of any provision of the by-laws, rules or similar governing instruments of any securities, insurance or commodities domestic or foreign regulatory body or self-regulatory organization;
 - is denied registration or is expelled, enjoined, directed to cease and desist, suspended or otherwise disciplined by any securities, insurance or commodities industry domestic or foreign regulatory body or self-regulatory organization or is denied membership or continued membership in any such self-regulatory organization; or is barred from becoming associated with any member of any such self-regulatory organization;
 - is indicted, or convicted of, or pleads guilty to, or pleads no contest to, any felony; or any misdemeanor that involves the purchase or sale of any security, the taking of a false oath, the making of a false report, bribery, perjury, burglary, larceny, theft, robbery, extortion, forgery, counterfeiting, fraudulent concealment, embezzlement, fraudulent conversion, or

- misappropriation of funds, or securities, or a conspiracy to commit any of these offenses, or substantially equivalent activity in a domestic, military or foreign court;
 - is a director, controlling stockholder, partner, officer or sole proprietor of, or an associated person with, a broker, dealer, investment company, investment advisor, underwriter or insurance company that was suspended, expelled or had its registration denied or revoked by any domestic or foreign regulatory body, jurisdiction or organization or is associated in such a capacity with a bank, trust company or other financial institution that was convicted of or pleaded no contest to, any felony or misdemeanor in a domestic or foreign court;
 - is a defendant or respondent in any securities- or commodities-related civil litigation or arbitration, is a defendant or respondent in any financial-related insurance civil litigation or arbitration, or is the subject of any claim for damages by a customer, broker or dealer that relates to the provision of financial services or relates to a financial transaction, and such civil litigation, arbitration or claim for damages has been disposed of by judgment, award or settlement for an amount exceeding \$15,000. However, when the member is the defendant or respondent or is the subject of any claim for damages by a customer, broker or dealer, then the reporting to FINRA shall be required only when such judgment, award or settlement is for an amount exceeding \$25,000; or
 - is, or is involved in the sale of any financial instrument, the provision of any investment advice or the financing of any such activities with any person who is, subject to a "statutory disqualification" as that term is defined in the Exchange Act. The report shall include the name of the person subject to the statutory disqualification and details concerning the disqualification; or
2. an associated person of the member is the subject of any disciplinary action taken by the member involving suspension, termination, the withholding of compensation or of any other remuneration in excess of \$2,500, the imposition of fines in excess of \$2,500 or is otherwise disciplined in any manner that would have a significant limitation on the individual's activities on a temporary or permanent basis.

In addition, associated persons are required to promptly report any of the following to Compliance:

- A temporary or permanent injunction issued by any court and involving securities, commodities, insurance, or banking matters
- Any customer complaint (securities or commodities) including a written complaint, civil litigation, or arbitration
- An arrest, indictment, arraignment, conviction, pleading guilty or no contest to any felony or misdemeanor (other than misdemeanor traffic offenses)
- A bankruptcy proceeding or unsatisfied liens or judgments

4.15.1 Reporting Requirements

CEI will report specified events involving the firm or an associated person to FINRA via the Regulatory Filings Application on the FINRA Firm Gateway no later than 30 calendar days after CEI knows of the event. This is in addition to any obligation to update an associated person's U4 or U5 or CEI's Form BD.

CEI will promptly report to FINRA (not later than 30 calendar days after CEI has concluded or reasonably should have concluded) that an associated person of CEI or CEI itself has violated any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body or self-regulatory organization. Conduct reported will be conduct that has a significant monetary result with respect to CEI, customers, or markets, or multiple instances of any violative conduct.

Relating to reported events, CEI will file with FINRA copies of the following. Events already reported on Form U4 with an affirmative request to satisfy Rule 4530 reporting requirements and FINRA findings and actions will not be reported separately.

1. any indictment, information or other criminal complaint or plea agreement for conduct reportable under paragraph (a)(1)(E) of this Rule;
2. any complaint in which a member is named as a defendant or respondent in any securities- or commodities-related private civil litigation, or is named as a defendant or respondent in any financial-related insurance private civil litigation;
3. any securities- or commodities-related arbitration claim, or financial-related insurance arbitration claim, filed against a member in any forum other than the FINRA Dispute Resolution forum;
4. any indictment, information or other criminal complaint, any plea agreement, or any private civil complaint or arbitration claim against a person associated with a member that is reportable under question 14 on Form U4, irrespective of any dollar thresholds Form U4 imposes for notification, unless, in the case of an arbitration claim, the claim has been filed in the FINRA Dispute Resolution forum.

4.16 Money Laundering

[FINRA Rule 3310; Bank Secrecy Act]

Money laundering is a serious crime potentially related to the funding of terrorist activities. It is the subject of extensive federal regulations that impose requirements on financial institutions, such as broker-dealers and their associated persons, to detect and prevent potential money laundering activities. This is an obligation of each associated person of CEI.

Money laundering is the movement of criminally derived funds to conceal the true source, ownership, or use of the funds. The funds are filtered through a maze or series of transactions, so the funds are "cleaned" to look like proceeds from legal activities.

In general, money laundering occurs in three stages. Cash first enters the financial system at the "placement" stage, where the cash profits from criminal activity are converted into monetary instruments, such as money orders or traveler's checks, or deposited into accounts at financial institutions. At the "layering" stage, the funds are transferred or moved into other accounts or other financial institutions to separate further the proceeds from their criminal origin. At the "integration" stage, the funds are reintroduced into the economy and used to purchase legitimate assets or to fund further criminal or legitimate activities.

Engaging in money laundering is a federal crime with severe penalties for those engaged in criminal activities and those who facilitate, intentionally or inadvertently, money laundering. It is important that CEI, as well as all associated persons, remain diligent and active participants in CEI's anti-money laundering (AML) program.

4.16.1 Background

The Currency and Foreign Transactions Reporting Act, also known as the Bank Secrecy Act (BSA), and its accompanying regulation, is a tool the U.S. government uses to fight drug trafficking, money laundering, and other crimes. Congress enacted the BSA to prevent financial service providers (such as banks and broker-dealers) from being used as intermediaries for, or to hide the transfer or deposit of, money derived from criminal activity. Money laundering schemes may include the use of wire transfers, cash, bearer instruments, travelers' checks, money orders, cashiers' checks, and other negotiable instruments.

CEI is required to comply with the reporting, recordkeeping, and record retention requirements of the BSA. The requirements govern the payment, receipt, or transfer of currency within and into and out of the U.S. and foreign financial transactions and accounts.

4.16.2 Shell Companies

[FINCen advisory on shell companies: <https://www.fincen.gov/resources/statutes-regulations/guidance/potential-money-laundering-risks-related-shell-companies>]

Shell companies may represent potential money laundering risks. "Shell company" refers to non-publicly traded corporations, limited liability companies (LLCs), and trusts that typically have no physical presence (other than a mailing address) and generate little or no independent economic value. It is important for associated persons to be aware of the risks involved in dealing with shell companies.

Most shell companies are formed for legitimate business purposes such as to hold stock or intangible assets of another business entity or to facilitate domestic and cross-border currency and asset transfers and corporate mergers. Unfortunately, shell companies have become common tools for money laundering and other financial crimes, primarily because they are easy and inexpensive to form and operate, and ownership and transactional information can be concealed from regulatory and law enforcement authorities. Most states do not collect or require disclosure of ownership information at the formation stage or after.

Agents, also known as intermediaries or nominee incorporation services (NIS), can play a central role in the formation and maintenance of shell companies. Agents and NIS firms offer a wide range of services that may include offering an office address, mail-forwarding services, local telephone listings, and other services that may give the appearance of a locally-established business. Some agents and NIS firms also provide nominee services which can preserve a client's anonymity. Some risk indicators of shell companies potentially engaged in money laundering are:

- An inability to obtain (through Internet searches, commercial database searches, or direct inquiries to the company's foreign correspondent bank) information necessary to identify originators or beneficiaries of wire transfers.
- A foreign correspondent bank exceeds the anticipated volume projected in its client profile for wire transfers in a given period or an individual company exhibits a high amount of sporadic activity that is inconsistent with normal business patterns.
- Payments have no stated purpose, do not reference goods or services, or identify only a contract or service number.
- Goods or services of the company do not match the company's profile based on information previously provided.
- Transacting businesses share the same address, provide only a registered agent's address, or raise other address-related inconsistencies.
- An unusually large number and variety of beneficiaries receive wire transfers from one company.
- Frequent involvement of beneficiaries located in high-risk, offshore financial centers.
- Multiple high-value payments or transfers between shell companies with no apparent legitimate business purpose.

4.16.3 Penalties

Participation in a money laundering scheme or the knowing receipt of proceeds from criminal activities is a crime. CEI and its associated persons are subject to severe criminal, civil, and regulatory penalties if they facilitate or participate in money laundering activities. Violations by associated persons may result in internal disciplinary action including termination.

An associated person may be deemed to be facilitating or participating in money laundering by engaging in a transaction with a customer (accept a deposit, arrange a withdrawal, effect a trade, *etc.*) when he or she is aware of, or willfully ignores, the fact that the customer is engaged in illegal activities.

4.16.4 Treasury Dept. OFAC List

The U.S. Treasury Department's Office of Foreign Assets Control (OFAC) is responsible for publishing sanctions against persons, corporations, and other entities including foreign governments that have been identified by the U.S. Government as engaging in criminal activities including drug trafficking and terrorist activities. CEI is obligated to check its accounts against the lists of blockings to ensure it does not engage in prohibited transactions which include securities transactions and transfer of assets out of a blocked account or to a blocked person or entity.

CEI has procedures to monitor the OFAC lists and comply with requirements to block property and notify OFAC when required. Questions regarding the program should be referred to the AML Compliance Officer. More information is also available at the OFAC web site at www.treas.gov/ofac.

4.16.5 Preventing Money Laundering

There are a number of ways CEI and its associated persons can avoid money laundering schemes.

4.16.5.1 Knowing the Customer

Being familiar with the customer's financial resources, business activities, and sources of funds are avenues for knowing the customer. Knowing the customer occurs at the time an account is opened as well as during the operation of a customer's account.

The identity of customers must be verified when a new account is opened. Procedures for verifying customer ID are explained in the chapter *ANTI-MONEY LAUNDERING PROGRAM* in the section *Customer Due Diligence*.

4.16.5.2 Risk Indicators

[NASD Notice to Members 02-21; FINRA Small Firm AML Template]

The following are examples of risk indicators (red flags) that may suggest potential money laundering.

<i>Customer accounts (opening, other activities related to establishing accounts)</i>
The customer exhibits unusual concern regarding CEI's compliance with government reporting requirements and CEI's AML policies, particularly with respect to his or her identity, type of business and assets, or is reluctant or refuses to reveal any information concerning business activities, or furnishes unusual or suspect identification or business documents.
The customer is reluctant to provide complete information about nature and purpose of business, prior banking relationships, anticipated account activity, officers and directors or business location.
The customer's background is questionable or differs from expectations based on business activities.
The information provided by the customer that identifies a legitimate source for funds is false, misleading, or substantially incorrect or refuses to provide information.
The customer (or a person publicly associated with the customer) has a questionable background or is the subject of news reports indicating possible criminal, civil, or regulatory violations.

The customer appears to be acting as an agent for an undisclosed principal, but declines or is reluctant, without legitimate commercial reasons, to provide information or is otherwise evasive regarding that person or entity.
The customer has difficulty describing the nature of his or her business or lacks general knowledge of his or her industry.
The customer is from, or has accounts in, a country identified as a non-cooperative country or territory by the Financial Action Task Force (FATF).
The customer has no discernible reason for using the Firm's service.
<i>Customer account transactions</i>
The customer exhibits a lack of concern regarding risks, commissions, or other transaction costs.
The customer wishes to engage in transactions that lack business sense or apparent investment strategy or that are inconsistent with the customer's stated business strategy.
The customer engages in suspicious activity involving the practice of depositing penny stocks, liquidates them, and wires proceeds. A request to liquidate shares may also represent engaging in an unregistered distribution of penny stocks which may also be a red flag. [FINRA Regulatory Notice 09-05]
The customer attempts to make frequent or large deposits of currency, insists on dealing only in cash equivalents, or asks for exemptions from CEI's policies relating to the deposit of cash and cash equivalents.
The customer engages in transactions involving cash or cash equivalents or other monetary instruments that appear to be structured to avoid the \$10,000 government reporting requirements, especially if the cash or monetary instruments are in an amount just below reporting or recording thresholds.
For no apparent business purpose or other reason, the customer has multiple accounts under a single name or multiple names (including family members or corporate entities); there may be a large number of inter-account or third-party transfers.
The customer's account shows numerous currency or cashiers check transactions aggregating to significant sums.
The customer requests that a transaction be processed in such a manner to avoid CEI's normal documentation requirements.
The customer's account shows an unexplained high level of account activity with very low levels of securities transactions.
Transactions patterns show a sudden change inconsistent with normal activities.
The customer engages in prearranged or other non-competitive trading, including wash or cross trades of illiquid securities.
Two or more accounts trade an illiquid stock suddenly and simultaneously.
The customer has opened multiple accounts with the same beneficial owners or controlling parties for no apparent business reason.
Customer transactions include a pattern of receiving stock in physical form or the incoming transfer of shares, selling the position and wiring out proceeds.
Customer's trading patterns suggest that he or she may have inside information.

The customer, for no apparent reason or in conjunction with other "red flags," engages in transactions involving certain types of securities, such as penny stocks, Regulation "S" (Reg S) stocks, and bearer bonds, which although legitimate, have been used in connection with fraudulent schemes and money laundering activity. (Such transactions may warrant further due diligence to ensure the legitimacy of the customer's activity.)
Large numbers of securities transactions across a number of jurisdictions.
Buying and selling securities with no purpose or in unusual circumstances (e.g., churning at customer's request).
<i>Penny Stock Company Related Transactions</i>
Company has no business, no revenues and no product.
Company has experienced frequent or continuous changes in its business structure.
Officers or insiders of the issuer are associated with multiple penny stock issuers.
Company undergoes frequent material changes in business strategy or its line of business.
Officers or insiders of the issuer have a history of securities violations.
Company has not made disclosures in SEC or other regulatory filings.
Company has been the subject of a prior trading suspension.
<i>Customer avoidance of reporting and recordkeeping</i>
Reluctant to provide information needed to file reports or fails to proceed with transaction.
Tries to persuade an associated person not to file required reports or not to maintain required records.
"Structures" deposits, withdrawals or purchase of monetary instruments below a certain amount to avoid reporting or recordkeeping requirements.
<i>Transactions involving insurance products</i>
Cancels an insurance contract and directs funds to a third party.
Structures withdrawals of funds following deposits of insurance annuity checks signaling an effort to avoid BSA reporting requirements.
Rapidly withdraws funds shortly after a deposit of a large insurance check when the purpose of the fund withdrawal cannot be determined.
Cancels annuity products within the free look period which, although could be legitimate, may signal a method of laundering funds if accompanied with other suspicious indicia.
Opens and closes accounts with one insurance company then reopens a new account shortly thereafter with the same insurance company, each time with new ownership information.
Purchases an insurance product with no concern for investment objective or performance.
Purchases an insurance product with unknown or unverifiable sources of funds, such as cash, official checks or sequentially numbered money orders.
<i>Customer wire and other transfers or deposits</i>
The customer's account has unexplained or sudden extensive wire activity, especially in accounts that had little or no previous activity.

The customer's account has a large number of wire transfers to unrelated third parties inconsistent with the customer's legitimate business purpose.
The customer's account has wire transfers that have no apparent business purpose to or from a country identified as a money laundering risk or a bank secrecy haven.
The customer's account indicates large or frequent wire transfers, immediately withdrawn by check or debit card without any apparent business purpose.
The customer makes a funds deposit followed by an immediate request that the money be wired out or transferred to a third party, or to another firm, without any apparent business purpose.
The customer makes a funds deposit for the purpose of purchasing a long-term investment followed shortly thereafter by a request to liquidate the position and transfer of the proceeds out of the account.
The customer engages in excessive journal entries between unrelated accounts without any apparent business purpose.
The customer's account has inflows of funds or other assets well beyond the known income or resources of the customer.
Many small, incoming wire transfers or deposits made using checks and money orders almost immediately withdrawn or wired out in manner inconsistent with customer's business or history. May indicate a Ponzi scheme.
Physical certificate is titled differently than the account.
Physical certificate does not bear a restrictive legend, but based on history of the stock and/or volume of shares trading, it should have such a legend.
Customer's explanation of how he or she acquired the certificate does not make sense or changes.
Customer deposits the certificate with a request to journal the shares to multiple accounts, or to sell or otherwise transfer ownership of the shares.
<i>Other indicators</i>
Law enforcement subpoenas.
Payment by third-party check or money transfer without an apparent connection to the customer.
Payments to third-party without apparent connection to customer.
No concern regarding the cost of transactions or fees (<i>i.e.</i> , surrender fees, higher than necessary commissions, <i>etc.</i>).

4.16.6 Cash Deposits Not Accepted

CEI does not accept cash deposits or cash equivalents (money orders, travelers checks). Customers who attempt to deposit cash should be advised to submit a personal check to his or her account.

4.16.7 Reports of AML Non-Compliance and Other Potential Crimes

All associated persons are obligated to promptly report to the AML Compliance Officer any known or suspected violations of anti-money laundering policies as well as other suspected violations or crimes. If the potential

violation implicates the AML Officer, it should be reported to a senior officer of CEI. All reports are confidential and the associated person will suffer no retaliation for making them.

What to report: Crimes or suspected crimes by individuals (whether associated with CEI, a customer, or prospective customer) are required to be reported. This includes suspicion that CEI is being used as a conduit for criminal activity such as money laundering or structuring transactions (discussed below) to evade the Bank Secrecy Act reporting requirements. There is no clear definition of what constitutes a "crime." If you believe some improper or illegal activity is occurring, it is your obligation to report it to CEI's AML Compliance Officer.

SAR reports: Broker-dealers are required to file Suspicious Activity Reports (SARs) for transactions that may be indicative of money laundering activity.

By law, CEI and its associated persons cannot disclose to the customer or anyone other than authorized regulators that it has filed a SAR. Questions regarding SAR filings should be referred to Compliance.

4.16.8 Recordkeeping Requirements

In addition to reporting requirements, broker-dealers are subject to requirements to maintain records of transfers of funds (including wire fund transfers) of \$3,000 or more. This includes transfers between accounts that are not for the same owner and transfers to third parties including banks and other financial institutions. Records of transfers are available for inspection by regulators and other appropriate authorities, when requested.

4.16.9 AML Compliance Officer

CEI has designated an AML Compliance Officer who is responsible for overseeing CEI's anti-money laundering program. The AML Officer may be contacted whenever an associated person has questions about CEI's program, a current or prospective account, or activities or transactions that raise questions about potential money laundering activities. An associated person may also provide information anonymously to the AML Officer. The AML Officer is responsible for investigating suspected money laundering activities and taking corrective action when necessary.

4.16.10 Identity Theft

Identity thieves use someone's personal identifying information to open new accounts and misuse existing accounts. CEI has established an Identity Theft Prevention Program (ITPP) to help detect and prevent identity theft. Many elements of detecting or preventing identity theft are similar to anti-money laundering (AML) requirements that are included in these policies.

The ITPP is based on identifying "red flags" that indicate identity theft may have occurred. ***It is the responsibility of all associated persons to be alert and report to the AML Compliance Officer any new or existing customers who may be engaged in violations of anti-money laundering regulations or identity theft or who have reported identity theft.***

Following is a list of potential identity theft red flags.

Red Flag
Category: Alerts, Notifications or Warnings from a Consumer Credit Reporting Agency
1. A fraud or active duty alert is included on a consumer credit report. An "active duty" alert is an alert a military person may add to his/her credit report to identify potential identity theft.

2. A notice of credit freeze is given in response to a request for a consumer credit report.
3. A notice of address or other discrepancy is provided by a consumer credit reporting agency.
4. A consumer credit report shows a pattern inconsistent with the person's history, such as a big increase in the volume of inquiries or use of credit, especially on new accounts; an unusual number of recently established credit relationships; or an account closed because of an abuse of account privileges.
Category: Suspicious Documents
5. Identification presented looks altered or forged.
6. The identification presenter does not look like the identification's photograph or physical description.
7. Information on the identification differs from what the identification presenter is saying.
8. Information on the identification does not match other information our firm has on file for the presenter, like the original account application, signature card or a recent check.
9. The application looks like it has been altered, forged or torn up and reassembled.
Category: Suspicious Personal Identifying Information
10. Inconsistencies exist between the information presented and other things we know about the presenter or can find out by checking readily available external sources, such as an address that does not match a consumer credit report, or the Social Security Number (SSN) has not been issued or is listed on the Social Security Administration's (SSA's) Death Master File.
11. Inconsistencies exist in the information that the customer gives us, such as a date of birth that does not fall within the number range on the SSA's issuance tables.
12. Personal identifying information presented has been used on an account our firm knows was fraudulent.
13. Personal identifying information presented suggests fraud, such as an address that is fictitious, a mail drop, or a prison; or a phone number is invalid, or is for a pager or answering service.
14. The SSN presented was used by someone else opening an account or other customers.
15. The address or telephone number presented has been used by many other people opening accounts or other customers.
16. A person who omits required information on an application or other form does not provide it when told it is incomplete.
17. Inconsistencies exist between what is presented and what our firm has on file.
18. A person making an account application or seeking access cannot provide authenticating information beyond what would be found in a wallet or consumer credit report, or cannot answer a challenge question.
Category: Suspicious Account Activity
19. Soon after CEI gets a change of address request for an account, we are asked to add additional access means (such as debit cards or checks) or authorized users for the account.
20. A new account exhibits fraud patterns, such as where a first payment is not made or only the first payment is made, or the use of credit for cash advances and securities easily converted into cash.
21. An account develops new patterns of activity, such as nonpayment inconsistent with prior history, a material increase in credit use, or a material change in spending or electronic fund transfers.

22. An account that is inactive for a long time is suddenly used again.
23. Mail CEI sends to a customer is returned repeatedly as undeliverable even though the account remains active.
24. We learn that a customer is not getting his or her paper account statements.
25. We are notified that there are unauthorized charges or transactions to the account.
26. We receive an email that purports to be from the customer but there are misspellings, improper grammar or other red flags that the customer did not send the email. (Phishing)
Category: Notice From Other Sources
26. An outside agency, law enforcement, a clearing firm, or other source notifies CEI that an account has been opened or used fraudulently.
27. CEI is notified of potential unauthorized access to customer personal information due to data loss from an outside provider or a breach of an outside provider's data.
28. Notice from a customer of the loss of information (e.g., loss of wallet, birth certificate, etc.).

Red flags should be reported to the AML Compliance Officer and her/his supervisor for review and instruction. New accounts should not be opened until the review is completed. Money movement and trading activity which creates the red flag should be held pending review. The AML Compliance Officer will maintain a memorandum of the incident reported, the investigation, and result, and maintain the memorandum on file.

4.17 Emergency Business Recovery Procedures

[FINRA Rule 4370]

CEI has a *Business Continuity Plan* that assigns responsibilities and outlines procedures in the event of a disaster or emergency which impacts CEI's ability to continue conducting business (also termed a "significant business disruption"). Examples of a major disruption include a regional power outage; disruption at another company that provides services critical to CEI's business; and destruction of an office or other facilities by natural causes or by other means. The Plan designates associated persons who are responsible for associated person safety and protection of firm property, records, and customer assets.

In the event of a disruption, associated persons will be given instructions by authorized personnel. Depending on the nature of the emergency, it may be necessary to use alternative communication systems; transfer personnel and/or business activities to alternative office space; or transfer CEI's business to other brokerage firms or financial institutions until normal operations can be resumed.

CEI has established procedures for contacting associated persons in the event of an emergency. If CEI conducts a test of its emergency procedures, all associated persons are required to participate as if the emergency were real. Past emergencies affecting the securities industry have shown that preparedness and cooperation are key to maximizing the safety of associated persons and minimizing business interruptions. It is important for all associated persons to follow instructions from senior management and other authorized key personnel during any drill or when an emergency occurs.

Questions regarding CEI's Business Continuity Plan may be referred to Compliance.

4.18 Prohibited Activities

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Various (referral of items, direct identification, review of transactions, correspondence, <i>etc.</i> depending on the nature of the prohibited activity)
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Take corrective action which may include: <ul style="list-style-type: none"> ○ Conferring with the associated person ○ Referring the matter to Compliance ○ Issuing a written warning or admonition ○ Restricting the activities of or transactions handled by the associated person ○ Suspending the associated person ○ Termination
Record	<ul style="list-style-type: none"> • The record of action taken depends on the nature and seriousness of the prohibited activity. Records, if needed, may be in different forms, including the following: <ul style="list-style-type: none"> ○ Designated supervisors may record action taken in supervisory logs, Daytimers, memos to associated persons' files, <i>etc.</i> ○ Compliance may record action by memo to the associated person's file

4.18.1 Use of Firm Name

No associated person may use CEI's name in any manner which could be reasonably misinterpreted to indicate a tie-in between CEI and any outside activity of the associated person.

4.18.2 High Pressure Sales Tactics

CEI and its RRs will not engage in high pressure sales tactics which may include excessive telephone calls, implying that a price may change on a security if the customer does not act immediately, or falsely representing that there is a limited supply of a security at a particular price.

4.18.3 Providing Tax Advice Not Permitted

Associated persons may not give tax advice to customers because CEI and its associated persons are not engaged in the practice of providing tax advice. Customers requiring specific tax guidance should be referred to their personal tax advisers.

This provision does not prohibit associated persons to provide professional tax advice through an unaffiliated outside business if that activity has been disclosed and approved by the Firm, and communications with customers of both CEI and the outside tax-related business are provided disclosures regarding the relationship of the entities.

4.18.4 Rebates of Commission

[FINRA Rule 2040]

Associated persons are prohibited from rebating to anyone, directly or indirectly, any commission or compensation received.

4.18.5 Sharing Commissions or Fees with Non-Registered Persons

[FINRA Rule 2040]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor: Requests to share commissions • Accounting: maintain Joint Rep Code and Override Forms
Resources	<ul style="list-style-type: none"> • Payroll/commissions reports • Requests to share commissions • Joint Rep Code and Override Request Forms
Frequency	<ul style="list-style-type: none"> • Ongoing (payroll/commission reports) • As required (requests)
Action	<ul style="list-style-type: none"> • Designated Supervisor: <ul style="list-style-type: none"> ○ Refer all requests to Compliance for approval ○ Discontinue any unapproved arrangements identified until they are approved • Accounting will ensure commissions are paid to registered persons only, or upon instruction by Compliance • Compliance will notify Accounting/Commissions regarding approved commission sharing arrangements
Record	<ul style="list-style-type: none"> • Joint Rep Code Form/Override Form • Accounting/Commissions will retain a record of Compliance's approval of commission sharing arrangements

With few exceptions, regulations generally prohibit the sharing of commissions or compensation with non-registered persons. Any payment or sharing arrangement to a non-registered person must be referred to Compliance for review.

4.18.6 Settling Complaints or Errors Directly with Customers

Associated persons may not make payments to customers of any kind to resolve an error or customer complaint. Errors and complaints must be brought to the attention of the associated person's designated supervisor.

4.18.7 Borrowing From and Lending to Customers

[FINRA Rule 3240; FINRA Notice to Members 04-14]

Registered associated persons are generally not permitted to borrow from or lend to their own customers. "RR" as used in this policy refers to **any** registered associated person of CEI.

This restriction does NOT apply when an associated person enters into a loan arrangement with a customer who is:

1. an immediate family member (defined as parents; grandparents; in-laws; spouse; siblings; children; grandchildren; cousins; aunts or uncles; nieces or nephews; and any other person whom the RR supports, directly or indirectly, to a material extent);
2. a financial institution in the business of providing credit, financing, or loans AND where the terms of the lending arrangement are those that would also be available to the general public doing business with those institutions;
3. another registered associated person of CEI;
4. someone (or an entity) who has a personal relationship with the RR and the lending arrangement arises from the personal relationship rather than an RR/customer relationship; or,
5. someone (or an entity) that has a business relationship outside the RR/customer relationship.

Any proposed loan with the RR's customer (other than a loan with a family member or financial institution in item numbers 1 and 2 above) requires the PRIOR review and approval by Compliance. RRs requesting exceptions must complete the RR/Customer Lending Arrangement Request form and submit it to Compliance prior to effecting the loan arrangement. Compliance will retain written approvals for at least 3 years after the date that the borrowing or lending arrangement has terminated or for at least 3 years after the RR has terminated employment with CEI.

4.18.8 Personal Funds Deposited in Customer Accounts

In general, associated persons are not permitted to deposit personal funds or securities in customers' accounts or deposit customers' personal funds or securities in associated person accounts. The same prohibitions apply to withdrawals. Exceptions should be reviewed by Compliance.

4.18.9 Prohibition Against Guarantees

[FINRA Rule 2150]

CEI and its associated persons are prohibited from guaranteeing a customer against loss in any securities transaction. Designated supervisors are responsible for identifying prohibited guarantees in correspondence or other written communications with public customers. Options or written agreements that establish the future price of a transaction such as repurchase agreements are not included in this prohibition.

4.18.10 Fees and Other Charges

Associated persons are not permitted to charge fees or assess other charges to customers or customers' accounts unless they are expressly permitted by CEI.

4.18.11 Customer and Other Signatures

Associated persons are not permitted to sign documents on behalf of customers, even when doing so is meant to accommodate a customer's request. Customer signatures must be original by the customer on all documents. Associated persons likewise may not sign documents on behalf of principals or supervisors.

Associated persons must send complete sets of documents to customers for signature – sending a signature page only is impermissible.

Associated persons and customers may not back-date any document submitted to the Firm.

4.18.12 Rumors

[FINRA Rule 6140(e)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Correspondence (electronic or written)
Frequency	<ul style="list-style-type: none"> • Ongoing • Periodically - training
Action	<ul style="list-style-type: none"> • As part of routine reviews of correspondence, look for communications that appear to spread rumors <ul style="list-style-type: none"> ○ Contact RR regarding source of information ○ If false rumors are identified, contact Compliance ○ Corrective action may include contacting recipients of correspondence containing false rumors; enhanced training for RR; disciplinary action appropriate to the offense • For scheduled training, include the prohibition against spreading false rumors
Record	<ul style="list-style-type: none"> • Correspondence with record of reviewer's initials or electronic note, and action taken, if appropriate • Record of training sessions (who attended, dates conducted, subject matter included)

No associated person may spread any rumors or misinformation that the associated person knows to be false or misleading. This includes rumors of a sensational character that might reasonably be expected to affect market conditions. Discussion of unsubstantiated information published by a widely circulated public media is not prohibited providing the source and unsubstantiated nature are also disclosed.

4.18.13 Misrepresentations

Associated persons may not disseminate any information that falsely states or implies guarantees or approval of securities by the government or other institution such as government guarantee of securities that carry no such guarantee. SIPC may not be misrepresented as a guarantor of a customer's account against losses from transactions.

4.18.14 Bribes

No associated person may offer or solicit explicit inducements to or from associated persons or representatives of other institutions or foreign governmental or political officials to obtain business. Entertainment and gifts in reasonable amounts are not included in this prohibition and are discussed in the section *Gifts, Gratuities And Entertainment*.

4.18.15 Acting Without Registration

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New account forms

	<ul style="list-style-type: none"> • Notices of registration status from Compliance • Reports of transactions effected by RRs not licensed in the customer's state of residency
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Review new account forms to identify any out-of-state accounts where the RR may not be registered • Review reports of transactions identifying unlicensed activity and follow up with RR • Immediately refer any RRs requiring state registration to Compliance
Record	<ul style="list-style-type: none"> • Include a notation on the New Account form or report noting action taken • Supervisor's log, Day Timer, or other record, as needed

No associated person may engage in activities that require registration (selling securities, soliciting accounts, trading, etc.) unless registered in the appropriate capacities. Questions regarding the need for registration should be referred to Compliance.

4.18.16 Improperly Influencing Research Analysts

Non-research personnel are prohibited from attempting to coerce research analysts to: (1) alter their views regarding the content of a research report or the timing of its publication; or (2) change the investment conclusions in a research report other than as appropriate to correct factual inaccuracies or verify market information such as prevailing market prices or to ensure consistency with established firm policies.

4.19 Electronic Communications Policy

[FINRA Rule 3110(b)(4), 3110.07, 3110.08 and 3110.09]

This policy governs the use of electronic communications by associated persons including part-time associated persons and independent contractors. It applies during business hours and after-business hours. ***This is an important policy; associated persons will be required to certify annually that they are familiar with and will comply with the policy.***

1. Firm electronic systems or communications devices are for firm business purposes and business communications must conform to accepted business standards and regulatory requirements.

- Inappropriate communications (profanity, obscenity, threats, otherwise offensive content) are prohibited. Report threatening or harassing communications to Compliance.
- Communications must include current and valid information.
- Copyrighted material cannot be sent unless authorized; contact Compliance for assistance.
- Copyrighted software cannot be copied or transmitted to others unless authorized.
- References and/or links to web sites are a form of communications requiring supervisory approval prior to use.
- Communications that must be accompanied by a prospectus may not be sent electronically unless the prospectus is available as an electronic attachment or an electronic link is provided to access the prospectus.

- CEI and its associated persons are prohibited from sponsoring a social media site or using a communication device that includes technology which automatically erases or deletes content.

2. Electronic business communications must be accessed and transmitted only through firm-sponsored systems.

- Regulators require retention of business communications and firm systems are designed to comply with retention requirements.
- **Approved communication systems only include:**
 - E-mail and e-faxes via company approved and archived e-mail addresses
 - Text messages are prohibited, unless communications are made through *Telemessage*, CEI's approved text messaging vendor. Texts through this service are archived through Smarsh and reviewed by the Firm
 - Messaging and mail through Twitter and LinkedIn accounts approved and archived by CEI
 - Other Instant Messaging and electronic communication vehicles such as Facebook messaging, Skype, Slack etc. are not approved and may not be used for communications concerning CEI 'business as such', unless CEI has approved the account for such use and archives the communications
- Encryption of information containing personal identifiers is required by CEI prior to delivery; associated persons must encrypt and password protect such documents on firm systems. The firm recommends Citrix Share File for such purposes. Other options include encrypting and password protecting PDF and Excel attachments that contain PII.
- Home computers or other personal devices and external systems may not be used for business purposes unless specifically approved by Compliance and enrolled with *Entreda* - Please refer to the firm's *Cybersecurity and Personal Information Protection Policy* manual for more information.

3. Consider electronic communications as public communications; protect confidential information.

- Do not confuse phone conversations or face-to-face communications with electronic communications. Your electronic conversation is subject to review and retention and may be the subject of subpoena in a civil or regulatory action.
- Confidential communications must not be sent on portable devices in public places unless encrypted.
- Do not view confidential information where unauthorized persons may have access (elevators, other public places).
- Safeguard portable devices to avoid unauthorized access to firm business.
- Safeguard passwords.
- Close open pages and sign out when the device is not in use.

4. There are restrictions on unsolicited e-mails under the CAN-SPAM Act of 2003.

- Unsolicited "mass" commercial e-mails are prohibited.
- "Commercial" e-mail includes any electronic messages that send a commercial advertisement or promote a commercial product or service. It does not include e-mail where there is an existing business relationship.
- Recipients may "opt-out" of receiving future e-mails. Forward such requests to Compliance.
- "Address harvesting" or "dictionary attacks" may not be used to obtain e-mail addresses off the Internet.
- E-mails sent from firm systems will include required identification of CEI and disclosures or disclaimers.

5. Participation in social media sites, blogs, and other electronic forums or communication systems is permitted with certain requirements and restrictions.

- Participants must receive prior approval from Compliance and, if required, complete training.
- Approved participants will be required to certify annually their understanding of and compliance with CEI's policies and procedures.
- Postings may require the prior approval of a supervisor depending on the type of participation.
- Media and systems used must be able to provide a permanent record of communications for retention by CEI.
- CEI will monitor and review such communications.

Refer to the section *Social Media, Blogs, Web Sites And Other Electronic Communication Systems* in the chapter *COMMUNICATIONS WITH THE PUBLIC* for CEI's policy on social media.

6. Electronic communications will be reviewed, monitored and audited by CEI.

- All electronic communications are subject to review and retention.
- Communications that require pre-use approval may not be transmitted prior to review by a supervisor.
This includes:
 - Retail communications.
 - Communications that must be accompanied by a prospectus.
 - Advertising.

7. Use of the Internet related to CEI's business is subject to restrictions.

- Associated persons are prohibited from posting information to the Internet without prior firm approval.
- Accessing offensive sites is prohibited.
- Please refer to CEI's *Cybersecurity and Personal Information Protection Policy* for further information.

4.19.1 Failure to Comply

Failure to comply with this policy may lead to disciplinary action. Non-compliance may generate one or more of the following:

- Oral and/or written warning
- Letter of Caution or Admonishment
- Education/training
- Fine
- Suspension of electronic communications privileges permanently or for a set period of time
- Regulatory discipline
- Suspension or termination of employment

4.19.2 Consent to Policy

Use of CEI's electronic communications systems represents the associated person's consent to the terms outlined in this Policy, including consent for CEI to monitor and audit content and/or usage.

4.20 Advertising and Publishing Activities

Prior to issuing any advertising or writing any books, articles, newsletters, or other materials to be published in public media (magazines, newspaper, computer bulletin boards, Internet, *etc.*) for public access, associated persons must contact the Advertising Supervisor for review and approval. If unrelated to CEI business, the requested activity may also require an Outside Business Activity Request Form and review as such. Approval is

not required for use of CEI-issued research or other materials approved by CEI and intended for public distribution.

4.21 Employees Acting as Trustees, Executors, or Other Fiduciary Capacities

[FINRA Rule 3241]

Associated persons usually will not act in a fiduciary capacity (*e.g.*, trustee, executor) for a customer's account unless the account is for a relative of the associated person. Exceptions require the approval of your supervisor through submission of the Request to Serve as Trustee, Executor or Beneficiary of Customer Account Form (Beneficiary Request Form).

4.22 Use of Titles

[NASAA Model Rule on the Use of Senior-Specific Certifications and Professional Designations]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • RR requests to use titles • Information regarding outside organizations that confer titles • Correspondence and retail communications
Frequency	<ul style="list-style-type: none"> • As required - review requests • Daily and ongoing - review of correspondence/communications
Action	<ul style="list-style-type: none"> • Review requests for use of special titles/designations: <ul style="list-style-type: none"> ○ Review any outside organization conferring designations for appropriate qualifications such as internal ethics policies, criteria for conferring designations ○ Review the RR requesting the title for qualifications including experience, completion of continuing education with CEI and regulatory/compliance history ○ Determine state requirements that regulate the use of designations • For those approved to use titles, notify the RR's supervisor who is responsible for review of correspondence and retail communications to determine proper use of title • Notify RR and supervisor if approval is withdrawn due to failure to complete necessary education requirements or other requirements
Record	<ul style="list-style-type: none"> • Review of outside organizations • Review of RRs • Approval or disapproval of correspondence and retail communications, other actions taken

RAs may use special titles indicating expertise when dealing with senior investors under the following requirements:

- A request to use a title must be provided to Compliance **prior to use** including the name and address of any outside organization conferring such titles based on meeting the organization's requirements.
- Titles may not be self-conferred, *i.e.*, the title must be based on some criteria or qualification met.
- The RR must be in good standing with the organization that confers the designation.
- The RR must be current on any continuing education requirements of the outside organization.
- The RR must complete firm training specifically relating to dealing with senior investors which may include retirement planning; ethics when working with senior investors; and the proper use of senior designations in correspondence, retail communications and seminars/luncheons.
- Business cards/letterhead are limited to that which is centrally issued by CEI; RRs may not create their own cards or letterhead.
- Compliance will review the request and notify the RR and the RR's supervisor if the request is approved or disapproved.
- Titles may be used only after Compliance approval.
- RRs who use senior designations must attest on the *Annual Employee Certification* their compliance with requirements.

4.23 Annual Compliance Questionnaire and Certification

Responsibility	<ul style="list-style-type: none"> • Chief Compliance Officer or designee
Resources	<ul style="list-style-type: none"> • Annual Compliance Questionnaire (ACQ)
Frequency	<ul style="list-style-type: none"> • Annually
Action	<ul style="list-style-type: none"> • Send Questionnaires to associated persons for completion • Review completed forms • Take appropriate action which may include: <ul style="list-style-type: none"> ○ Inquiring regarding reported outside business activities ○ Inquiring regarding reported outside securities accounts ○ Conferring with the associated person and/or associated person's supervisor for any other reported information requiring follow up ○ Filing updates to the associated person's Form U4, if necessary
Record	<ul style="list-style-type: none"> • Annual Questionnaires are retained in an annual file for associated person certifications

CEI will, on an annual calendar-year basis, ask associated persons to complete an Annual Compliance Questionnaire. The purpose of this form is to ensure CEI's records are current regarding items to be reported to CEI (outside business activities, outside accounts, *etc.*).

Persons who associate with the firm on or after October 1 need not complete a Questionnaire for that calendar year. This policy is based upon the fact that the information has been acquired during the on-boarding process and it is reasonable to assume the information is not stale within three months. Associated Persons have an on-going obligation to notify his or her supervisor of any material changes to the information on his or her U4 and any other information provided to the firm during the on-boarding process.

4.24 Due Diligence on Registered Representatives

Within thirty (30) days of registration and annually thereafter (calendar year) Compliance conducts a social media and internet review of its registered persons. At minimum, compliance will review the registered person by name, office address, home address, office phone number, and office email to review for, among other things, negative news, unreported OBA activity, unreported social media accounts. Compliance may also search by known personal email addresses, personal phone numbers, other known business email addresses, or other information at its discretion in order to detect unreported OBA activity, social media or other negative news.

Searches may be delegated to unregistered personnel. Compliance or a designated principal will evidence review by physical or electronic signature or initials and date on the first page of the internet search in PDF (or other substantially similar format). An Adobe Date Stamp showing the reviewer's name is also acceptable.

5. CODE OF ETHICS

5.1 Introduction

The Code of Ethics is a compilation of basic principles of conduct for which you, as a Firm associated person, are responsible for knowing and following. These principles represent values critical to our customers and others to conduct our business with honesty and integrity. The Code has been adopted to protect the reputation and integrity of CEI and its associated persons and to assist associated persons in following uniform standards of ethical conduct. The term "associated person" in the Code is understood to mean officers, directors, employees, and independent contractors.

The Code of Ethics is intended to govern the actions and working relationships of associated persons with current or potential customers, consumers, other Firm associated persons, competitors, suppliers, government representatives, the media, and anyone else with whom the Firm has contact. In these relationships, associated persons must observe the highest standards of ethical conduct. The success of CEI as a provider of financial services is built upon the trust and confidential relationships maintained between CEI and its customers. Therefore, each associated person is expected in all business matters to place CEI's and its customers' interest above his or her own self-interest and to discuss with Compliance any proposed transaction or relationship that reasonably could be expected to give rise to a conflict of interest.

It is CEI's policy that an associated person maintain no position which (1) could conflict with their performance of duties and responsibilities to CEI, (2) affects or could affect independence or judgment concerning transactions between CEI and its customers, suppliers, or others with whom CEI competes or has existing or pending or potential business relationships, or (3) otherwise reflects negatively on CEI.

Associated persons must resolve any doubt as to the meaning of the Code in favor of good, ethical judgment. **It is the responsibility of each associated person to avoid even an appearance of impropriety.**

Implicit in the Code of Ethics is CEI's policy that both CEI and its associated persons comply with the law. The law prescribes a minimum standard of conduct; the Code of Ethics prescribes conduct that often exceeds the legal standard. Any request made of an associated person by any supervisor carries with it, whether or not articulated, the understanding that the associated person is to comply with the request only to the extent he or she can do so while complying both with the law and this Code of Ethics. In certain instances, areas of CEI have their own unique policies governing subjects covered by the Code of Ethics due to their lines of business. These policies are in addition to the requirements of the Code of Ethics.

5.2 Confidentiality

Non-public information regarding CEI or its businesses, associated persons, customers, suppliers or consumers is confidential. Associated persons may not purposefully access or view such information without a business justification, disclose such information, or use it for trading in securities or for other personal gain during or after employment, except that associated persons may use confidential information to perform their job duties.

5.3 Self-Interest

Associated persons are prohibited from:

1. Accepting employment or engaging in a business (including consulting and similar arrangements or arrangements with competitors) that may conflict with the performance of their duties or CEI's interest. All outside business activities require prior approval by Compliance.
2. Taking for themselves personally opportunities that are discovered through the use of CEI proprietary, non-public information (such as processes, programs, software, and business information and plans) about CEI or its businesses, or position, even if developed by the associated person either within or outside of the associated person's area of responsibility, or using corporate property, information or position for personal gain, or competing with CEI.
3. Taking unfair advantage of any customer, supplier, competitor, or other Firm information through manipulation, concealment, abuse of privileged information, misrepresentation of material fact, or any other unfair dealing or practice.
4. Soliciting or demanding anything of value from any person in conjunction with the performance of their duties to CEI (other than normal compensation received from CEI).
5. Accepting personal fees, commissions, other compensation paid, or expenses paid or reimbursed from others, not in the usual course of CEI's business, in connection with any business or transaction involving CEI.
6. Purposefully viewing or using confidential information about the Firm or its businesses, associated persons, or customers, consumers or suppliers without a valid business reason, for personal benefit or disclosing such information to others outside of job duties.
7. Misusing CEI's information technology and electronic communications system, including accessing or distributing pornographic or other distasteful information or materials containing offensive, sexually explicit or harassing language, sending chain letters, or conducting excessive personal business.
8. Permitting Firm property (including data transmitted or stored electronically and computer resources) to be damaged, lost, used, or intercepted in an unauthorized manner.
9. Making any political contribution of money or other property on behalf of CEI that would violate federal or state law.
10. Borrowing or accepting money from customers or suppliers unless the customer or supplier is a financial institution that makes such loans in the ordinary course of its business.
11. Purchasing property, whether real, personal or intangible, from CEI without the approval of his or her supervisor or other designated senior officer unless CEI makes a general offer of extraneous company property to associated persons on a non-discriminatory basis.
12. Selling property or services to CEI unless approved by Compliance which will ascertain the reasonableness of the selling price.
13. Providing customers with legal, tax, accounting or investment advice not in the usual course of business; or recommending attorneys, accountants, securities dealers, insurance agents, brokers, real estate agents, or other service providers if the advising associated person receives a personal reciprocal benefit for the referral from the service provider. (Note that referrals to service providers are permissible as long as the associated person does not receive a personal reciprocal benefit for that referral.)
14. Engaging or investing in any business that directly or indirectly competes with services provided by CEI or any subsidiary of the Firm, except where such an investment represents insignificant ownership in a publicly traded company.
15. Knowingly benefiting from an error, including but not limited to payment of compensation (including incentive plan payments) or travel and entertainment expense reimbursement, without disclosing that error.
16. Doing any of the above actions indirectly through another person.

5.4 Gifts and Entertainment

Entertainment and the giving or receipt of gifts are governed by CEI's Gifts, Gratuities and Entertainment policy in the chapter *GENERAL POLICIES* of CEI's Written Supervisory Procedures.

Discounts and price reductions not generally available to others are considered gifts. Associated persons are expressly prohibited from soliciting, demanding or accepting anything of value with the intent to be influenced or rewarded in connection with any business transaction or relationship involving CEI.

5.5 Bequests

An associated person must report to Compliance any potential bequest in excess of US\$100 to the associated person under the will or trust instrument of a customer, vendor or supplier of CEI, whether or not CEI is the fiduciary named under such instrument, unless the customer, vendor, or supplier is a member of the associated person's immediate family. Bequests in excess of US\$100 are subject to the approval of the associated person's immediate supervisor and Compliance.

5.6 Privacy

Associated persons may be restricted from accessing, sharing or using certain information across Firm affiliates and from sharing information with external third parties, except as allowed by law. Associated persons must not view or request access to information unless a valid business purpose exists.

For specific information about privacy requirements, see *Customer Privacy Policies And Procedures* in the chapter *COMMUNICATIONS WITH THE PUBLIC*.

5.7 Holding Office/Appointments

- Before an associated person may become a director, officer, or partner of any business organized for profit outside CEI, written approval by Compliance is required.
- Associated persons are encouraged to participate in organizations that are involved in charitable, educational, or community activities, and no approval is needed for involvement with such organizations unless the associated person will receive compensation.
- Associated persons are encouraged to participate in civic and political activities.
- An associated person may hold a part-time elective or appointive office provided the associated person receives the written approval of Compliance and provides full disclosure concerning the time involved and compensation, if any, to be received. When an associated person seeks a political office, the associated person must obtain an opinion from the political entity's legal counsel stating that the associated person's candidacy is not prohibited and that the associated person's election or appointment will not bar the political entity from doing business with CEI.
- Associated persons must avoid appointments, including fiduciary appointments, which may conflict with the performance of their duties for CEI or otherwise interfere with their employment relationship with the Firm. All fiduciary appointments, except those on behalf of the associated person's immediate family members ("Immediate family member" means a person's child, parent, spouse, sibling, and in-laws) must be approved by Compliance which may require execution of a hold harmless agreement by the beneficiary. Associated persons are prohibited from maintaining trusteeships and other fiduciary appointments for their own customers other than immediate family members.

5.8 Internal Accounting Controls

It is the legal responsibility of CEI to develop and maintain systems of internal accounting controls that permit the preparation of its financial statements in accordance with applicable laws, rules, and accounting principles.

No one shall, directly or indirectly, knowingly falsify or cause to be falsified any book, record or account of the Firm. This includes expense accounts, approval of invoices submitted by vendors, records of transactions with customers, records of disposition of company assets, records of consumers, or any other record.

Any associated person who becomes aware, directly or indirectly, of inadequate controls, a failure of controls, or a circumvention of controls, or that transactions or other items are improperly recorded on CEI's books or records, must promptly report the situation to Compliance.

5.9 Reporting Possible Ethics Violations and Disciplinary Action

Associated persons have an obligation to report potential ethics violations to Compliance. Compliance will maintain the confidentiality of the individual reporting the possible violation; the associated person may also report anonymously the identity of the parties involved. Retaliation against associated persons who report possible violations is strictly prohibited and will subject those who retaliate with disciplinary action which may include termination. Those who violate the Code are subject to disciplinary action which may include termination.

For example, if an associated person would feel more comfortable in merely reporting that they suspect several of their co-associated persons are involved in what appears to be falsifying credit reports or that a fellow associated person is involved in a transaction that may be a conflict of interest on his or her part, the associated person need only report the suspected Code violation, the persons involved, and the department in which they suspect the activity is occurring.

5.10 Trading in the Stock of Firm Customers, Suppliers or Vendors

Customer Securities

No associated person may invest in the securities of a customer of CEI if the associated person participates in or is expected to participate in transactions involving, or is responsible for, extensions of credit to the customer or if the customer's securities are publicly traded and the associated person has non-public information concerning the customer at the time of the proposed investment. If the associated person participates in or is responsible for decisions involving non-credit business transactions with the customer, the associated person must comply with any investment policy applicable to the associated person's line of business before making an investment in the customer's securities. In no case may the associated person invest in the customer's securities until after making disclosure of the proposed investment to the associated person's immediate supervisor, to the person approving the transaction with the customer, and Compliance.

Supplier or Vendor Securities

No associated person may invest in the securities of a supplier or vendor if the associated person participates or is expected to participate in or is responsible for decisions involving business transactions with the supplier or vendor or if the securities are publicly traded and the associated person has nonpublic information about the supplier or vendor at the time of the proposed investment. If an associated person has an existing investment in the securities of a supplier or vendor of CEI and such associated person participates or is expected to participate in or is responsible for decisions involving business transactions with the vendor or supplier, the associated person shall promptly disclose the investment to his or her immediate supervisor and Compliance, and shall refrain from

further participation in such decisions unless expressly authorized in writing by his or her immediate supervisor and Compliance.

An associated person may make an insubstantial investment in the publicly traded securities of a supplier or vendor even though such associated person participates or is expected to participate in or is responsible for decisions involving the supplier or vendor if the associated person obtains the prior approval of the associated person's immediate supervisor and Compliance.

5.11 Full and Fair Disclosure

Associated persons are required to make full, fair, accurate, timely, and understandable disclosure in reports and documents that CEI files with, or submits to, the Securities and Exchange Commission, SROs, government agencies, and in other public communications made by CEI.

5.12 Compliance

- Each associated person of CEI shall act on CEI's behalf in a manner that complies with all laws, rules, and regulations under which CEI must operate. Any associated person who becomes aware, either directly or indirectly, of an associated person's violation of a law involving a breach of trust must report the violation promptly to Compliance.
- If an associated person becomes aware of or suspects embezzlement, false entries in CEI's records, false statements to CEI's regulators, false statements by customers or consumers (where the associated person knows that the statement is false or has reason to inquire as to its falseness), or any fraud or potential fraud, or other criminal violation involving CEI, its associated persons or customers, such associated person must immediately contact Compliance.
- An associated person who is convicted of a crime (other than a minor traffic offense) or found liable for an offense that subjects the associated person to a disciplinary or licensure order by a regulatory agency or self-regulatory organization, must promptly report the event to Compliance. In addition, an associated person who is charged with (but not convicted) of a crime involving a breach of trust, dishonesty, substance abuse, money laundering, or a felony, or is charged with (but not found liable) of an offense by a regulatory agency or self-regulatory organization that may result in a disciplinary or licensure order must promptly report the event to Compliance. Failure to report the above is a violation of the Code.
- Each associated person must cooperate fully with a request by CEI to conduct an investigation of the associated person. Failure to do so is a violation of the Code.

5.14 Supervision

It is the responsibility of each supervisor to train and supervise associated persons so that they are able to perform their jobs in a competent manner and in conformity with CEI's policies, including the Code of Ethics. When assigning responsibilities to an associated person, it is the supervisor's responsibility to ensure that the associated person has demonstrated the capability to discharge the assigned responsibility in conformity with the Code of Ethics. It is also the supervisor's responsibility to ensure that all associated person questions concerning the operation and requirements of the Code of Ethics are fully addressed.

5.15 Administration

1. The Chief Compliance Officer is responsible for administration of the Code of Ethics and updating the Code when necessary.

2. All associated persons will receive a printed copy or directed to review an electronic version of the Code upon hire and will certify their compliance annually on the Annual associated person Certification.
3. Disclosures, approvals, or waivers will be reviewed, acted upon, and retained by the Chief Compliance Officer with the exception of requests for waivers by Firm directors which will be reviewed and acted upon by the Board of Directors and/or CEI Audit Committee, if an audit committee exists.
4. The Code will be included in associated person training.

6. Associated Person and Employee Exit Procedures

[FINRA Corporation By-Laws Article V Section 3; FINRA Rule 3110(f); FINRA Regulatory Notice 19-10]

Responsibility	<ul style="list-style-type: none"> • Associated Person/Employee: Written notice of resignation with proposed exit date to Designated Supervisor • Designated Principal • Operations
Resources	<ul style="list-style-type: none"> • Notification of termination to Operations, Accounting, and Compliance
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Immediately notify Compliance of terminating registered associated persons • Immediately notify Compliance of terminating non-registered associated persons where termination was caused by theft or fraud • Immediately notify Home Office of terminating registered and non-registered associated persons • Secure computers and computer files • Retrieve office keys, company credit cards, <i>etc.</i> from terminated associated person • Reassign accounts • Notify customers of newly-assigned RR • Compliance will file Form U5 for terminating RRs • Compliance will provide the terminated RR with a copy of the RR's Form U5 within 30 days of termination
Record	<ul style="list-style-type: none"> • The CRD retains copies of Form U5

6.1 Notification to Compliance

Whenever an associated person terminates employment from CEI, the designated supervisor is responsible for immediately notifying Compliance and Home Office if they have not been directly given notice. Notification to Compliance regarding registered associated persons should include:

- Name of terminated person and RR number(s)
- Type of termination (voluntary, permitted to resign, discharged, *etc.*)
- If the termination is not voluntary, an explanation of the reason for termination
- Date of termination
- Any known compliance problems at the time of termination

6.2 Securing and Retrieving Firm Property

Operations is responsible for retrieving CEI property from terminated employees including office keys, company credit cards, computer files, customer files, and any other items which are the property of CEI. Registered representatives are generally independent contractors who possess no physical CEI property.

6.3 Reassignment of Accounts

Within thirty (30) days of resignation or termination, the accounts of a registered representative will be sent a letter to the customers by the Home Office announcing the exit of the RR, and that accounts will be self-directed. Any accounts remaining after thirty (30) days will be assigned to a house account rep code for administrative purposes.

6.4 Responding to Customer Inquiries

Designated Supervisors should instruct branch or department associated persons, including RRs receiving reassigned accounts, that when asked, to state only that the associated person is no longer with CEI. No details or speculation regarding the departure should be given to customers or anyone else outside CEI unless authorized by Compliance to do so.

6.5 Form U5

Compliance is responsible for filing Form U5 for any terminated registered associated person. Compliance will also send, within 30 days of termination, a copy of Form U5 to the former associated person.

Coastal Equities, Inc. is not registered as an investment adviser to engage in adviser activities (managing accounts, discretionary accounts, *etc.*)

7 OFFICES

This chapter describes the types of offices defined by regulators and requirements for inspections and supervision of offices. **Compliance must be notified:**

- Before a new branch office or other business office is opened (including all types of offices defined in this chapter)
- When an office address changes
- Prior to a change in the types of business conducted in an office
- When an RR changes offices
- Prior to an RR commencing work from a second location, such as a primary residence
- Prior to establishing an office-sharing arrangement with an outside person or entity

7.1 Office Designations

[FINRA Rule 3110]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Information regarding offices including new offices, address changes, office sharing arrangements
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Identify each office as to type to determine regulatory requirements, maintain list of offices and types • Establish and document supervision for non-branch locations • Make required regulatory filings • Review requests for a principal to supervise more than one OSJ considering the following: <ul style="list-style-type: none"> ○ whether the on-site principal is qualified by virtue of experience and training to supervise the activities and associated persons in each location; ○ whether the on-site principal has the capacity and time to supervise the activities and associated persons in each location; ○ whether the on-site principal is a producing registered representative; ○ whether the OSJ locations are in sufficiently close proximity to ensure that the on-site principal is physically present at each location on a regular and routine basis; and ○ the nature of activities at each location, including size and number of associated persons, scope of business activities, nature and complexity of products and services offered, volume of business done, the disciplinary history of persons assigned to such locations, and any other indicators of irregularities or misconduct.
Record	<ul style="list-style-type: none"> • List of offices including types of offices • Regulatory filings

	<ul style="list-style-type: none"> • Approval for one principal to supervise more than one OSJ and document why such a supervisory structure is reasonable
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This section describes different types of offices and related requirements.

7.1.1 Branch Office

[FINRA Rule 3110(a)(3), 3110(a)(4) and 3110(f)(2)]

A branch office is any location where one or more associated persons (*e.g.*, employees, independent contractors) regularly conduct the business of effecting any transactions in, or inducing or attempting to induce the purchase or sale of any security or any location held out as such. Branch offices are required to be registered, and if the "main office" meets the definition of "branch office" (or OSJ) it is required to be registered.

Any office that is responsible for supervising associated persons at one or more non-branch locations is considered to be a branch office.

7.1.2 Offices of Supervisory Jurisdiction (OSJ)

[FINRA Rule 3110(a)(3), 3110(a)(4), 3110(f), 3110.02 and 3110.03]

An office that includes any of the following activities will be designated as an Office of Supervisory Jurisdiction (OSJ) with a resident principal responsible for supervision:

- Order execution and/or market making
- Structuring of public offerings or private placements
- Maintaining custody of customers' funds and/or securities
- Final acceptance (approval) of new accounts
- Review and approval of customer orders
- Final approval of retail communications
- Supervision of RRs at one or more other branch offices

In addition, the following factors will be considered on determining whether an office is an OSJ:

- whether registered persons at the location engage in retail sales or other activities involving regular contact with public customers;
- whether a substantial number of registered persons conduct securities activities at, or are otherwise supervised from, such location;
- whether the location is geographically distant from another OSJ of CEI;
- whether the member's registered persons are geographically dispersed; and
- whether the securities activities at such location are diverse or complex.

Excluded from the definition of OSJ is an office that solely provides final approval of research reports.

An OSJ principal will supervise only one OSJ; exceptions must be approved by Compliance.

7.1.3 Branch Offices Assigned to OSJs

Each branch office that is not an OSJ will be assigned to the supervision of an OSJ. All business transacted by non-OSJ branch offices must be processed through the supervising OSJ. The designated supervisor is responsible for supervision of the branch office's activities. Each branch is responsible for maintaining files for complaints, communications, new accounts, option accounts, advertising, and transactions originating from the branch office.

A branch office may be a "supervisory branch office" that has responsibility to supervise one or more other offices or a "non-supervisory branch office" that has no supervision over other offices.

7.2 Approval of Persons to Operate in Non-Branch Locations

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests for RRs to conduct business at non-branch locations
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review the request considering: <ul style="list-style-type: none"> ○ Business to be conducted ○ RR disciplinary or complaint history ○ Requirements to supervise, including the need for heightened supervision ○ RR engagement in outside activities that may conflict with Firm business ○ Technology requirements • Approve or disapprove request and notify RR's supervisor
Record	<ul style="list-style-type: none"> • Records of request reviews, action taken, notices to RR and supervisor

Because of the remote nature of some non-branch locations, approval is required **prior to** allowing an RR to operate from a non-branch location. Requests must be submitted on the form "Office Locations - Request For Approval."

7.2.1 Primary Residence Offices

[FINRA Rule 3110(f)]

On a case by case basis, an RR's request to conduct business from their primary residence *as an NBL* may be considered provided that, at a minimum, the RR is currently employed by CEI and is in good standing with both CEI and supervising regulatory authorities. Compliance must approve any such arrangement. The form "Office Locations - Request For Approval" must be submitted to Compliance. The RR must submit a signed acknowledgment that he/she has read and understands this policy. If the request is not approved, the location may be approved as a registered branch.

RAs approved for working from their primary residences may do so as long as the residence is not held out to the public as a branch office, and that they adhere to all relevant policies and procedures of CEI. The following requirements must also be met:

- only one Firm RR may conduct business from the location (unless otherwise approved by Compliance)
- the RR does not meet with customers at the location
- customer funds and securities are not handled at the location
- the RR is assigned to a designated branch office, and such office is reflected on all business cards, stationery, advertisements, and other communications to the public

- the RR's outgoing customer communications sent from the primary residence are **pre-approved** by his/her designated supervisor
- all electronic business communications (*i.e.*, e-mails, faxes) are transmitted through Firm systems
- all customer orders are entered through the designated branch office or, if approved, via a Firm-approved system
- all required branch records are maintained at the designated branch office location

Other requirements:

- the RR may not use his/her personal e-mail accounts (*i.e.*, yahoo, gmail, *etc.*) to communicate with existing or potential clients; only Firm electronic systems may be used for customer communications
- all Firm system installations must be supervised by the Information Officer or IT department and in accordance with all Firm policies

7.3 Supervision of Non-Branch Locations

Each non-registered location will be assigned for supervision to a designated supervisor in a registered branch office. Compliance will determine the scope of supervision and notify the designated supervisor considering factors including the number of RRs, types of business conducted, volume of business, qualification and history of on-site personnel (*e.g.*, whether there is a registered supervisor at the location, whether RRs have disciplinary or complaint histories), and the nature and extent of RRs' outside business activities.

The designated supervisor will conduct ongoing reviews and retain records of the reviews at the designated branch location, which is subject to inspection, including records of non-branch office supervision.

7.4 Supervision of Producing Managers

[FINRA Rule 3110(b)(6)(c) and 3110.10]

The customer account activities of managers and other supervisors are subject to supervision. Procedures are included in the chapter *SUPERVISORY SYSTEM, PROCEDURES, AND CONTROLS* in the section *Supervision Of Producing Managers' Customer Account Activity*.

7.5 Office Records

[SEC Securities Exchange Act of 1934 Rule 17a-3 and Rule 17a-4]

Each office is required to maintain or have access to certain records relating to the business conducted in the office. "Office," for records purposes, means any location where an associated person conducts business (not including a home office or the office of a customer that a RR visits regularly). "Conducting business" includes handling funds or securities or soliciting/accepting orders. Each office is required to designate someone who can explain the office records to regulators.

There are two aspects to records requirements: *retention* and *access*. Documents (paper or electronic) regarding CEI's business ("books and records") must be retained for periods of time specified by regulators. Where CEI's required books and records (such as order tickets, communications, *etc.*) are not retained at the office that created the records, there is a requirement that the records must be produced within a reasonable period of time upon request from a regulator that visits the office.

This section describes both types of requirements. All questions regarding books and records should be referred to Compliance.

7.5.1 Retention of Records at the Office

Offices are required to retain the following records:

- Order records (3 years, 2 recent years in an accessible location)
- New account records (6 years after account closing, in an accessible location)
- Communications, incoming and outgoing (3 years, 2 recent years in an accessible location)
- Advertising (3 years, 2 recent years in an accessible location)
- Operations records including records of receipt/delivery of securities or funds (3 years, 2 recent years in an accessible location)
- Complaints (3 years, 2 recent years in an accessible location)

7.5.2 Forwarding Records to Home Office

The following records must be forwarded to home office for retention:

- Communications, incoming and outgoing
- Advertising
- Copies of complaints

7.5.3 Access to Records

For records that are **not** maintained at the office location, the following records for the most recent two-year period will be produced at the office location promptly upon request of a regulator. **Regulators' requests should immediately be referred to Compliance for response.** "Promptly" is generally understood to mean within 24 hours of the request.

- Order records (daily trade blotters, order tickets/memoranda, including for the firm account)
- Receipts/deliveries of securities, receipts/disbursements of cash, all other debits/credits
- Employee records (U4, employment application, compensation agreements, CRD numbers, internal identifying numbers, offices where RR conducts business)
- Customer account records
- Complaints
- Transactions, by RR, including compensation earned, commission schedules, method by which compensation is determined
- Communications with the public: originals of communications received, copies of communications sent; approval of outgoing communications including correspondence, retail communications, and (if applicable) institutional communications
- Record naming the person in the office who can explain records
- Record listing the person responsible for policies and procedures
- Compliance and supervisory manuals, including updates and revisions, until three years after termination of use of the manual

7.5.4 Regulatory Requests for Records

If a regulator (SEC, SRO, state regulator, or other) requests office records (in person or by another means), Compliance should be contacted immediately. CEI is obligated to provide prompt response to regulators' requests for information, therefore it is important the record retrieval process begin immediately or as soon as possible after receipt of the request.

7.6 Display of SIPC Symbol

In authorized branch locations, the SIPC symbol will be displayed. Compliance is responsible for identifying the office locations that require the necessary SIPC display.

7.7 Changes in Branch Offices

[FINRA By-Laws Article IV Section 8]

Compliance is responsible for filing the uniform branch office registration form (Form BR) with the CRD to reflect changes to existing offices or to register new offices. Compliance retains records of branch registration filings.

7.8 Closing Offices

When an office is closed (and not just moved to another location), Compliance will forward a letter to the person in charge of the office requesting a copy of all branch files and requesting the return of any Coastal letterhead and business cards, and SIPC sign. The firm may also notify customers of the branch closing if and when necessary to protect customers or to protect the Firm.

7.9 Use of Office Space by Others

[Form BR]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Requests for office-sharing arrangements involving outsiders
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review the potential arrangement to determine that it will be clear to the public which entity they are dealing with, considering the following: <ul style="list-style-type: none"> ○ Amount of customer traffic in the office ○ Physical separation ○ Clearance with the fidelity insurance carrier ○ Posting the name of each entity on the door to their working place ○ The entities' names are not listed under the same telephone number ○ CEI's phone number is not used on the letterhead, business cards, or on any advertising of the outside entity ○ Employees of each organization will wear a badge identifying their employer ○ Any other considerations • When space-sharing involves the dual employment of CEI personnel, include policies and procedures that clearly identify the duties/functions to be performed for CEI and the supervisory reporting lines • File an amendment to Form BR for approved arrangements
Record	<ul style="list-style-type: none"> • Record of review and considerations that allow or disallow the arrangement • Approval/disapproval of the arrangement

	<ul style="list-style-type: none"> • If dual employment is involved, policies and procedures to address duties and supervisory structure if not already addressed in these WSPs • Form BRs filed
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Persons not affiliated with CEI are generally not permitted to conduct business or maintain offices on CEI premises. Office-sharing arrangements require the prior approval of Compliance.

7.10 Office Inspections

[FINRA Rule 3110(c)(1), 3110(c)(2), 3110(c)(3), 3110.13 and 3110.14]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Various reports/information regarding office activities
Frequency	<ul style="list-style-type: none"> • Annual: inspect OSJs and any branch office supervising one or more non-branch locations • Conduct risk-based review to determine inspection cycle of other offices (no less than every 3 years for branch offices) for new branches and when material changes occur in existing branches • Annual: prepare inspection schedule • Annual: assign responsibility for conducting inspections • Per inspection schedule: conduct inspections
Action	<ul style="list-style-type: none"> • Conduct risk-based review to determine inspection cycle for non-supervisory offices • Prepare schedule including an explanation of the factors used in determining inspection cycles for non-supervisory offices • Assign inspection responsibility considering any potential conflicts of interest including economic, commercial, or financial interests in the associated persons or business being inspected and ensuring the person assigned is not assigned to the business unit and is not directly or indirectly supervised by, or otherwise reporting to, an associated person assigned to the unit or location. Where compliance is not possible due to CEI's size or business model (only one office; business model where small or single-person offices report directly to an OSJ-manager who is also considered the office's branch office manager), document in the report both the factors used to make this determination and how the inspection otherwise complies with the requirements of Rule 3110(c)(1) • Conduct inspections • Prepare draft and final reports and provide final report to office supervisor or person in charge • Obtain response from office supervisor/person in charge and follow up regarding corrective action (no later than next inspection) • For an office with significant risk profile changes or regulatory/complaint issues, review the need for an immediate "for cause" inspection or acceleration of the inspection cycle

	<ul style="list-style-type: none"> • Maintain inspection program (and revise, as needed)
Record	<ul style="list-style-type: none"> • The inspection program, schedule of inspections, reports, review of those conducting inspections, reports • Determinations of whether a branch's inspection cycle should be accelerated or a "for cause" inspection should be conducted

All OSJs, branch offices, and non-branch offices are inspected in accordance with FINRA Rule 3110(c). "Non-supervisory office" in this section refers to branch offices that do not supervise other offices and non-branch offices.

7.10.1 Risk-Based Inspection Cycle

CEI will inspect non-supervisory offices based on a risk-based inspection cycle. The frequency of inspections will be determined as follows.

- New Branches will be evaluated using the Review Of Branch Office Risk Factors/Inspection Cycle form to determine whether any factors require the branch to be inspected annually or for a cycle less than three years.
- Consistent with FINRA rules, any office designated as an Office of Supervisory Jurisdiction will be inspected annually, and does not require completion of the form.
- Any branches with YES answers on the Risk-Based Evaluation form will be considered for more frequent inspections.
- For those branches that qualify for inspection less frequently than annually, the Review Of Branch Office Risk Factors/Inspection Cycle form will be completed to consider various risk factors and to determine how frequently the branch will be inspected. (The minimum inspection cycle is every three years.)
- Some offices will be inspected on an unannounced basis.
- Non-Branch locations will by default be inspected every three years. A shorter, or longer inspection cycle may be determined by compliance, and evidenced by completing the Review Of Branch Office Risk Factors/Inspection Cycle form. Factors considered in this evaluation include: the number of RRs, types of business conducted, volume of business, qualification and history of on-site personnel (*e.g.*, whether RRs have disciplinary or complaint histories), and the nature and extent of RRs' outside business activities.

7.10.1.1 "For Cause" Inspections

At any time, a branch office may be identified for an immediate "for cause" inspection, as determined by Compliance. A "for cause" inspection may be initiated considering serious regulatory or disciplinary actions against branch personnel; serious or a pattern of complaints; thefts; fraud; suspected money laundering activities; or other malfeasance by branch personnel.

7.10.1.2 Change of Risk Profile for Offices Inspected Less Frequently Than Annually

Compliance will consider whether a significant change to an office's risk profile triggers a review of the inspection schedule for that branch. Events that may trigger this review include:

- A branch RR comes under SRO/state/Firm heightened supervision requirements.
- A branch that previously did not supervise other offices now supervises another office (requiring annual inspection).
- A branch or branch associated person becomes the subject of a pattern of complaints.

- A branch's level of errors or changes in accounts on orders becomes high compared to other branches.
- Branch personnel become the subject of regulatory action.
- The branch is assigned a new branch manager.
- An existing or newly-hired RR becomes or is subject to a statutory disqualification.

7.10.2 Conducting Inspections

[FINRA Rule 3110(c)(3)(B) and 3110.14]

Inspections must be conducted by someone independent of supervisors of the office being inspected. Inspections may not be conducted by anyone who:

- supervises the office being inspected (branch manager, *etc.*);
- is another supervisor in that office; or
- is directly or indirectly supervised by either of the prior-listed supervisors or someone who directly supervises those office supervisors.

Inspections generally include the following:

- Assignment of inspection responsibilities to a qualified person
- Pre-inspection document/information review including review of prior report(s) for the office
- Scheduling a visit on either an announced or unannounced basis
- For branch offices, scheduling reviews at the supervising office to examine records of supervision
- During a physical inspection, reviewing records and interviewing personnel in accordance with the inspection program
- Preparing a draft report of findings
- Submitting the draft to the appropriate supervisor or person in charge for comment and response if deficiencies are found
- Preparing a final report incorporating the supervisor's responses
- Submission of the final report to management and compliance

If the branch includes RIA activity of its affiliate RIA, then the inspector will review approximately 5% of the household accounts of each RR's advisory book of business. Reviews will include suitability review of the trading in such advisory accounts.

Compliance, at its discretion, initiates unscheduled inspections (when potential significant problems are identified, a change in office management warrants a special review, at the request of senior management, *etc.*).

7.10.3 Reports

[FINRA Rule 3110(c)(2)]

Written reports of inspections will include:

- the name of the person who conducted the inspection and prepared the report
- the date(s) of the inspection
- areas reviewed which will include, at minimum (depending on types of business conducted in the office)
 - safeguarding customer funds and securities;
 - maintaining books and records;
 - supervision of supervisory personnel;
 - transmittals of funds (*e.g.*, wires or checks, *etc.*) or securities from customers to third party accounts; 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; and
- changes of customer account information, including address and investment objectives changes and validation of such changes.
 - for any of the above areas **not** included in the report, an explanation of why they were not included (*i.e.*, the office does not accept funds or securities, the office does not have a producing manager, *etc.*) and a statement that the office may not engage in these activities until policies and procedures for these activities are in place at that location
 - observations and exceptions regarding compliance with policies and procedures
 - the person in-charge or office supervisor's response regarding exceptions and corrective action

Final reports will be distributed to senior management and the branch supervisor if material deficiencies are found.

7.10.4 COVID-19 TEMPORARY RELIEF (Eff. 2020 and 2021)

FINRA has granted relief concerning firm obligations to conduct branch inspections under Rule 3110.

Timing: Coastal will complete its 2020 branch examinations on or before March 31, 2021. In addition, inspections conducted in 2020 and 2021 will be 'remote' inspections.

Documentation Requirement: Inspections conducted remotely will be identified as such on the Branch Office Inspection Schedule maintained by Compliance. If an inspection results in a determination that the branch requires additional supervisory procedures or more frequent monitoring under Rule 3110.17(c), the firm will identify such on the Schedule.

Methodology: The firm's examination process currently includes remote work prior to any physical inspection. This process will remain the same and includes reviews of money movement blotters, trading activity, and direct business blotters as applicable to the branch. The inspector will also review and consider other information itemized on the Office Inspection Form such as: reported OBAs, customer complaints and prior inspection findings as part of her/his risk analysis. The firm's review of the above data provides guidance for a risk-based review of the branch.

Inquiry should be made as to whether the branch physical space is being utilized, or if personnel operate remotely. Photos or live video inspection (via Zoom, GotoMeeting, Facetime, *etc.*) may be requested to observe where documentation containing PII is maintained, shared office spaces, home office spaces or other areas of concern in the inspector's discretion. If the branch is working remotely, inquiry should be made as to the branch process concerning mail, customer checks, and customer complaints.

Inspectors may conduct interviews with branch personnel including financial professionals and their staff. Interviews may be conducted via telephone, or by Zoom or GotoMeeting. Screen sharing may be used, but chat functionality may not be used.

Final Office Inspection Report: The inspector will sign the Office Inspection Form when completed, which is evidence that all of the factors relevant to the branch on the form have been reviewed by the inspector. If there are findings or recommendations, the inspector will provide a formal report to the person in charge of the branch and the branch supervisor. Material findings will be escalated to the CCO.

Documentation: The signed Office Inspection Report, findings, and any response to the findings will be maintained in the Compliance Branch Inspection Folder on the firm's network. Notes and backup materials used by the inspector will also be maintained with the Report.

7.11 Display of Certificates

[SIPC By-Laws Article 10 Section 3]

Branch offices are required to conspicuously display a SIPC sign on their premises. The Home Office will provide such a SIPC sign to the branch upon registering the branch.

7.12 Availability of Rules

Each office that deals with public customers will maintain copies of rules for regulators where CEI is a member. Where Internet access is available, this requirement is satisfied by providing access to the rules published on the regulators' web sites either as a bookmark on an internet browser or a direct link in a document or on a desktop.

Rules are available at www.FINRA.org and www.MSRB.org .

8 TRAINING AND EDUCATION

Coastal provides training in a variety of methods. Training includes material in this manual and any supplements. Training will also be provided through email alerts and newsletters periodically. This chapter describes Coastal policies and procedures concerning its annual compliance meeting, regulatory element, and firm element programs.

8.1 Annual Compliance Meeting

[FINRA Rule 3110(a)(7) and 3110.04]

Responsibility	<ul style="list-style-type: none"> • Chief Compliance Officer
Resources	<ul style="list-style-type: none"> • List of RRs and registered principals by branch, department, or for CEI
Frequency	<ul style="list-style-type: none"> • Annual
Action	<ul style="list-style-type: none"> • Determine appropriate subjects to include in meetings, depending on RRs and principals who are participants • Conduct compliance meetings or interviews with RRs and principals • If electronic media is used to conduct meetings, designate a local supervisor to complete an attendance record to ensure RRs and principals arrive on time and attend the entire meeting • If on-demand webcasts are used: <ul style="list-style-type: none"> ○ Users are assigned a unique user ID and password ○ Records of attendance are maintained electronically in "read-only" format ○ Each user will be advised he or she has the opportunity to e-mail or telephone questions to the presenter and receive answers in a timely manner ○ Each user will be advised of Q As available on Coastal Equities, Inc.'s intranet and Q As will be updated when questions are received ○ The number of minutes the webcast stays on is tracked ○ The webcast is configured as click-as-you-go ○ At the end of the webcast a pop-up box requires the user to attest that the entire webcast was viewed (or a separate attestation will be required) • Ensure all subject RRs and principals complete the required annual meeting or interview • For RRs and principals who do not complete the requirement, take corrective action which may include contact with the RR's or principal's supervisor; limitation on business activities until the requirement is completed; other corrective action determined as appropriate for the circumstances
Record	<ul style="list-style-type: none"> • A record of when and where meetings are conducted, subjects discussed, and who attended is retained by Compliance • A record of corrective action is retained in the RR's or principal's file

As required by FINRA rules, RRs and registered principals are required to attend an annual compliance meeting or interview.

8.2 Continuing Education

[FINRA Rule 1240; FINRA CE web site: <http://www.finra.org/industry/continuing-education>]

Registered associated persons are subject to SRO continuing education requirements composed of two distinct elements. Registered associated persons are required to complete both elements at specified time intervals. The two elements are:

Regulatory Element: This element is a computer-based training program that focuses on compliance, regulatory, ethical, and sales practice standards. Its content is derived from rules and regulations as well as standards and practices widely accepted within the industry. This element is administered at designated testing centers or through an in-firm program.

Firm Element: All registered associated persons dealing with public customers and their supervisors are required to complete continuing education administered by Coastal Equities, Inc.

8.2.1 Regulatory Element

Responsibility	<ul style="list-style-type: none"> • Chief Compliance Officer
Resources	<ul style="list-style-type: none"> • CRD Firm Queues and related reports • CRD e-mail notifications of inactive registrations
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Review CRD Firm queue • Request queue reports • Notify affected persons of requirements • Schedule computer based training • Review CRD e-mail notifications of inactive registrations • Notify designated supervisors of restricted persons
Record	<ul style="list-style-type: none"> • Queue reports, e-mail notices, and records of notifying associated persons are maintained electronically in the Firm's email archive

8.2.1.1 Who Is Subject to The Requirements

All registered persons are subject to the regulatory element.

8.2.1.2 When Requirements Must Be Completed

The regulatory element is to be completed within 120 days of the 2nd anniversary of the individual's original registration date and every three years thereafter. For registered persons who become subject to statutory disqualification or disciplinary action as defined under the rules, the regulatory element must be completed within 120 days of the posting date of the disciplinary action and every three years after that date.

8.2.1.3 Regulatory Element Contact Person

[FINRA Rule 1250(a)(7)]

Compliance or a designated person responsible for registration will notify FINRA of the name and email address of the contact person to receive CRD notices. Changes will be reported within 30 days of the change. Annually, by the 17th business day following the end of the calendar year, the contact person information will be reviewed and updated, if necessary.

8.2.1.4 CRD Notices and Appointments for Training Sessions

Compliance is responsible for notifying associated persons of pending Regulatory Element requirements. CRD notices are received and sent by email and retained electronically in the firm's email archive.

8.2.2 Firm Element

Responsibility	<ul style="list-style-type: none">• Chief Compliance Officer
Resources	<ul style="list-style-type: none">• Information regarding firm products, services, training needs• Guidance from regulators• Current regulatory concerns• Disciplinary actions• Quest CE (approved vendor)
Frequency	<ul style="list-style-type: none">• Annual by calendar year
Action	<ul style="list-style-type: none">• Develop needs analyses; training plans; and training materials• Identify associated persons who are subject to the requirement (covered persons)• Monitor completion of requirements• Restrict covered persons who do not complete requirements
Record	<ul style="list-style-type: none">• Needs analyses; training plans; training materials• Dates of training, contents of training, lists of attendees• Copies of training material used• Certifications• Records (memos, notes, etc.) of actions restricting covered persons

8.2.2.1 Who Is Subject to The Requirements

All registered persons who do business with the public and their supervisors are subject to the firm element. Firm element continuing education is required regardless of the length of registration or employment in the securities industry.

8.2.2.2 Firm Requirements

Coastal Equities, Inc. is required to:

- identify job functions and persons subject to the requirement
- prepare an annual needs analysis including gathering information about products and services and training topics
- implement the training plan
- retain a record of participation
- develop a method of evaluating the effectiveness of the training
- consider the evaluations in developing the next year's needs analysis
- restrict covered persons who do not complete the requirement

Coastal Equities, Inc.'s internal program may include videos, computer training, in-person presentations, and other methods of conveying training material including a combination of methods.

8.2.2.3 Annual Needs Analysis

An annual needs analysis is prepared for covered persons.

In developing the needs analysis, the following methods will be used:

- Feedback from regulators including recent audits, regulatory alerts, and CE feedback will be evaluated
- Customer complaints, arbitrations, and other litigation involving the firm will be evaluated

Needs analyses will be completed by end of first quarter (or shortly thereafter) each year for the upcoming calendar year.

8.2.2.4 Evaluating the Firm Element Program

Written comments by participants will be reviewed and maintained in the Firm Element evaluation file for consideration in the following year's Needs Analysis. Comments and feedback are encouraged and may be submitted to compliance@coastal-one.com.

8.2.3 Registered Persons Who Fail to Complete Requirements

Registered persons who fail to complete the requirements of continuing education cannot conduct any duties that require registration or earn commissions or other compensation related to such activities. Registrations are considered "inactive" until continuing education requirements are completed.

The Chief Compliance Officer or his designee will notify affected persons and their supervisors by e-mail or written memorandum when their registration becomes inactive, and when the requirement is satisfied and inactive status is lifted. Accounting/Commissions also will be notified by e-mail or written memorandum. Copies of notification and memos will be retained electronically in the firm's email archive.

9 INSIDER TRADING

[Insider Trading and Securities Fraud Enforcement Act of 1988; SEC Securities Exchange Act of 1934 Rule 10b-5; FINRA Notice to Members 89-5; SEC Staff Summary Report on Examinations of Information Barriers: <http://www.sec.gov/about/offices/ocie/informationbarriers.pdf>; SEC Guidance on the use of company web sites (application of Regulation FD): <http://www.sec.gov/rules/interp/2008/34-58288.pdf>; <http://www.sec.gov/about/offices/ocie/informationbarriers.pdf>]

<p>Responsibility</p>	<ul style="list-style-type: none"> • Designated Supervisor • Compliance
<p>Resources</p>	<ul style="list-style-type: none"> • Daily Transaction Report • Associated person transactions (see the section <i>Employee, Employee-Related and Proprietary Trading</i>) • Customer and proprietary and affiliate asset management (if applicable) transactions • Restricted and watch lists • Inquiries from regulators • Transactions in securities on CEI's Watch or Restricted Lists (see the sections <i>Watch List</i> and <i>Restricted List</i>) • Questions or transactions referred by managers or other firm personnel • Access controls including key card controls, computer networks
<p>Frequency</p>	<ul style="list-style-type: none"> • Daily and as required • Monthly - Review of controlled access • Annually and ongoing - develop and provide training
<p>Action</p>	<ul style="list-style-type: none"> • Supervisors reviewing trades: refer questioned trades to Compliance • Compliance will review the referred transaction and take appropriate action which may include: <ul style="list-style-type: none"> ○ Determination if further information is necessary ○ Consultation with RR or other firm personnel regarding the nature of the transaction(s) including reason for transaction, solicited vs. unsolicited ○ Review of other transactions by the same customer and/or RR ○ Consultation with in-house or outside counsel ○ Referral of transaction(s) to appropriate regulator • Compliance <ul style="list-style-type: none"> ○ reviews transactions (Associated person/customer/proprietary/affiliate asset management) against restricted and watch lists to identify potential breaches ○ reviews access controls (key cards, network controls) for unauthorized access ○ investigates potential breaches ○ takes corrective action which may include: <ul style="list-style-type: none"> ▪ Contact with affected personnel ▪ Consultation with outside counsel ▪ Disciplinary action

	<ul style="list-style-type: none"> ▪ Added training ▪ Referral to regulators ○ Develop and provide training for all personnel and particularly for those with access to inside information
Record	<ul style="list-style-type: none"> • Initials on Daily Transaction Report by the designated reviewer • Compliance's review of transactions documented to include who conducted the review; when reviewed; identification of the transaction(s) reviewed; copies of the records used to conduct the review; and notation of action taken • Compliance review of controlled access and corrective action taken, if applicable • Compliance and supervisors' records of Associated person training on insider trading

9.1 Insider Trading Policies and Procedures

Broker-dealers are required to establish, maintain, and enforce policies and procedures to prevent the misuse of material non-public information ("inside information"). These requirements are included in the Insider Trading and Securities Fraud Enforcement Act of 1988. CEI has established policies and procedures reasonably designed to prevent the misuse of inside information considering CEI's business, structure, size and other relevant factors.

At the time of hire, Associated persons are provided with the *Firm Policy Memorandum Regarding Insider Trading* included in this chapter. Updates to this policy are provided by Compliance when required.

9.2 Prohibition Against Acting on or Disclosing Inside Information

CEI policy prohibits Associated persons and associated persons from effecting securities transactions while in the possession of material, non-public information. Associated persons are also prohibited from disclosing such information to others. The prohibition against insider trading applies not only to the security to which the inside information directly relates, but also to related securities, such as options or convertible securities.

If associated persons receive inside information, they are prohibited from trading on that information, whether for the account of CEI or any customer, or their own account, any accounts in which they have a direct or indirect beneficial interest (including accounts for family members) or any other account over which they have control, discretionary authority or power of attorney.

9.3 Tippees are Insiders

An associated person may, depending on the circumstances, become an "insider" or "tippee" when obtaining **apparently** material, non-public information by happenstance, including information derived from social situations, business gatherings, overheard conversations, "tips" from "insiders," or other third parties. In these situations, the associated person must, **unless Compliance advises otherwise**, treat the information as inside information and comply with all of the policies on insider trading.

9.4 Misuse Constitutes Fraud

The misuse of material, nonpublic or "inside" information constitutes fraud, a term broadly defined under federal securities laws. Engaging in fraud is subject to civil and criminal penalties (including imprisonment), SEC

administrative actions, disgorgement of profits, penalties from exchanges, and dismissal by CEI. There are no circumstances where any person becomes aware of inside information, for whatever purpose, may use that information to trade for personal benefit, for CEI's benefit, or for the benefit of another. If any associated person believes he or she has received inside information, he or she should immediately advise their supervisor or Compliance.

9.5 Annual Certification

Employees and associated persons are required to annually certify their knowledge of and compliance with CEI's insider trading policy. This certification is included in the Annual Certification form.

9.6 Firm Policy Memorandum Regarding Insider Trading

This policy memorandum is intended to provide information and guidance concerning the restrictions on insider trading, which is an enforcement priority of the Securities and Exchange Commission and the Department of Justice. It also explains policies adopted by CEI to prevent fraudulent or deceptive practices relating to trading on material, non-public information ("insider trading"). Trading in securities on the basis of material, non-public information ("inside information") is prohibited and contrary to firm policy. The penalties for insider trading can be considerable, including loss of profits plus treble damages, criminal sanctions including incarceration, loss of employment and permanent bar from the securities industry. This policy applies to all associates of CEI. Specific departments of CEI may have insider trading policies that supplement this policy.

READ THIS MEMORANDUM VERY CAREFULLY. You will be asked to sign a statement affirming that you have read and understand the policies set forth herein and that you will abide by them.

THE PROHIBITION

The prohibition against insider trading includes the following: if you are in possession of material non-public information about a company or the market for a company's securities, you must either publicly disclose the information to the marketplace or refrain from trading. Generally, disclosure is not an option and the effect is to require an individual to refrain from trading. You also may not communicate inside information to a second person who has no official need to know the information.

Information is considered material if there is a substantial likelihood that a reasonable investor would consider it important in deciding to buy or sell a security. In addition, information that, when disclosed, is likely to have a direct effect on a security's price should be treated as material. Examples include information concerning impending tender offers, leveraged buy-outs, mergers, sales of subsidiaries, significant earnings changes and other major corporate events.

Information is non-public when it has not been disseminated in a manner making it available to investors generally. Information is public once it has been publicly disseminated, such as when it is reported on the Dow Jones or other news services or in widely disseminated publications, and investors have had a reasonable time to react to the information. Once the information has become public or stale (*i.e.*, no longer material), it may be traded on or disclosed freely.

Generally, a person violates the insider trading prohibition when that person violates a duty owed either to the person on the other side of the transaction or to a third party (such as a customer or employer) by trading on or disclosing the information. The insider trading prohibition applies to an issuer's directors, officers and employees, investment bankers, underwriters, accountants, lawyers and consultants, as well as other persons who have entered into special relationships of confidence with an issuer of securities.

Virtually anyone can become subject to the insider trading prohibition merely by obtaining material non-public information by unlawful means or by lawfully obtaining such information and improperly using it. This is known as misappropriation. If you receive material, non-public information as part of your legitimate business dealings on behalf of CEI or its customers and you use that information to trade in securities or if you transmit that information to another person for purposes of trading in securities (so-called "tipping"), you would likely be guilty of insider trading. Insider trading liability may also be derivative. A person who has obtained inside information (so-called "tippee") from a person who has breached a duty or who has misappropriated information may also be held liable.

The foregoing is just a synopsis of the insider trading prohibition. Because the law in this area is complex, CEI has adopted the following guidelines which are designed to prevent violations of the insider trading rules.

WHEN CEI IS AN INSIDER

CEI may be deemed an insider when it comes into possession of inside information through its various activities such as investment banking and research. Research analysts may become insiders (or tippees) upon receiving inside information from a company officer, director or employee. In addition, the intention to update or downgrade a research recommendation might be material information and should not be disclosed, prior to public dissemination, to anyone outside the Research Department (and in some instances to some within the Research Department) unless there is a need to know the information.

CEI will remain an insider as long as it has inside information, regardless whether the prospective banking client decides to engage another investment banking firm or whether CEI declines to accept the proposed engagement.

REGULATION FD (FAIR DISCLOSURE)

SEC Regulation FD governs the release by public companies of information that may reasonably be expected to affect the market price of securities issued by the public company. While obligations under the Regulation fall primarily on public companies, it is equally important for associated persons of CEI to be aware of the requirements and to act appropriately if an associated person becomes privy to inside information about the company.

The goal of the Regulation is to create a "level playing field" so that the dissemination of information that is reasonably likely to affect the market price of a security is released simultaneously to all investors. In general, the issuer, its executive officers, directors, investor relations personnel or other associated persons with similar duties are prohibited from selectively disclosing material, nonpublic information to securities analysts, to other securities professionals, or to a shareholder when it is foreseeable that a recipient of such information will trade on the information. The Regulation requires action by the issuer if there is intentional or unintentional selective disclosure of such information.

Associated persons must not expect or seek to obtain, other than in the normal course of confidential investment banking activities, material non-public information from issuers and their employees.

GUIDELINES

TREATMENT OF CUSTOMER INFORMATION. CEI considers confidential all information concerning its customers including, by way of example, their financial condition, prospects, plans and proposals. The fact that we have been engaged by a company as well as the details of that engagement are also confidential. CEI's reputation is one of its most important assets. The misuse of customer information can damage that reputation as well as customer relationships.

WHAT TO DO IF YOU LEARN INSIDE INFORMATION. It is not illegal to learn inside information. CEI learns material non-public information from its customers and is permitted to use that information in a lawful manner to advise and assist them. It is, however, illegal for you to trade on such information or to pass it on to others who have no legitimate business reason for receiving such information.

If you believe you have learned inside information, other than in the ordinary course of business (such as investment bankers who learn inside information when working on an engagement), contact Compliance immediately so that we may address the insider trading issues and preserve the integrity of CEI's activities. Do not trade on the information or discuss the possible inside information with any other person at CEI. If you become aware of a breach of these policies or of a leak of inside information, advise Compliance immediately.

INVESTIGATIONS OF TRADING ACTIVITIES. From time to time, the Exchanges, FINRA and the SEC request information from CEI concerning trading in specific securities. Requests for information should be referred directly to Compliance. You may be asked to sign a sworn affidavit that, at the time of such trading, you did not have any inside information about the securities in question. Your employment may be terminated if you refuse to sign such an affidavit. CEI may submit these affidavits to the Exchanges, FINRA or SEC.

STEPS YOU CAN TAKE TO PRESERVE THE CONFIDENTIALITY OF MATERIAL NON-PUBLIC INFORMATION.

If you are in a position within CEI to access inside information, the following are steps you must take to preserve the confidentiality of inside information:

1. Material inside information should be communicated only when there exists a justifiable reason to do so on a "need to know" basis inside or outside CEI. Before such information is communicated to persons within CEI, your department, or another person you believe needs to know, contact your department manager or Compliance.
2. Do not discuss confidential matters in elevators, hallways, restaurants, airplanes, taxicabs or any place where you can be overheard.
3. Do not leave sensitive memoranda on your desk or in other places where they can be read by others. Do not leave a computer terminal without exiting the file in which you were working.
4. Do not read confidential documents in public places or discard them where they can be retrieved by others. Do not carry confidential documents in an exposed manner.
5. On drafts of sensitive documents use code names or delete names to avoid identification of participants.
6. Do not discuss confidential business information with spouses, other relatives or friends.
7. Protect electronic information on laptops and other portable devices by encrypting confidential data.
8. Avoid even the appearance of impropriety. Serious repercussions may follow from insider trading and the law proscribing insider trading can change. Since it is often difficult to determine what constitutes insider trading, you should consult with Compliance whenever you have questions about this subject.

YOUR OWN SECURITIES TRADING. Firm policy is to require all associated persons to maintain their securities accounts at CEI except with the approval of Compliance. If you have an account outside of CEI and have not already done so, please advise Compliance immediately. This includes outside accounts in which you have a financial interest or direct the trading.

CONCLUSION

CEI has a vital interest in its reputation, the reputation of its associates, and in the integrity of the securities markets. Insider trading would destroy that reputation and integrity. CEI is committed to preventing insider trading and to punishing any associated person who engages in this practice or fails to comply with the above

steps designed to preserve confidentiality of inside information. These procedures are a vital part of CEI's compliance efforts and must be adhered to.

9.7 Employee, Employee-Related, And Proprietary Trading

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Daily Transaction Report • Confirmations/statements for associated persons' outside accounts
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Identify transactions in securities included on CEI's Restricted or Watch Lists (refer to sections on those procedures)
Record	<ul style="list-style-type: none"> • Notations are included in Compliance's files regarding identified transactions including details of each trade, action taken and initials or signature of reviewer.

Associated person and proprietary trades are reviewed by Compliance for trades contrary to restrictions because of underwriting activities, other restrictions, and potential insider trading. This review includes review of associated persons' outside securities accounts to identify transactions in securities on CEI's Restricted List or Watch List.

9.8 Information Barrier Procedures

[FINRA Rule 5280; FINRA Notice to Members 91-45]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Information regarding confidential investment banking activities
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Investment Banking notifies Compliance regarding confidential investment banking activities • Compliance: <ul style="list-style-type: none"> ○ Maintain records of companies subject to investment banking (also see <i>Restricted List</i> and <i>Watch List</i>) ○ Maintain records of associated persons brought "over the wall" including name, date brought over, and the company the subject of confidential activities ○ Issue restrictions on the "over the wall" associated person's activities (issuing research reports, trading in a particular security, <i>etc.</i>), as appropriate ○ Obtain certifications from affected associated persons

Record	<ul style="list-style-type: none"> • Compliance retains records of Restricted List and Watch List securities • Compliance retains records of associated persons brought over the wall • Certifications filed in associated person's file in Compliance
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9.8.1 Introduction

Information barriers (also known as "Chinese walls") are established within broker-dealers to prevent the flow of material, non-public information. CEI may obtain material, non-public information while engaging in investment banking activities. Effective procedures permit CEI to continue conducting research, trading, and other business activities while another department has knowledge of inside information affecting an issuer of securities. CEI has established procedures to isolate departments and/or associated persons with inside information and permit the conduct of business in other areas.

9.8.2 Departments Subject to Information Barrier Confidentiality Procedures

The firm currently has identified no department subject to CEI's Information Barrier confidentiality procedures:

Compliance will continue to monitor whether the firm develops any departments which should be subject to Information Barrier Confidentiality Procedures and will advise management accordingly. Departments that obtain material, non-public information in the normal course of business must maintain the confidentiality of that information. Other departments potentially affected by inside information (Research, Trading, *etc.*) may continue to conduct normal activities unless they become aware of inside information, in which case they are required to immediately contact Compliance for guidance regarding future activities involving the subject company or companies.

9.8.3 Confidentiality Procedures

Responsibility	<ul style="list-style-type: none"> • Designated Supervisors for Research, Investment Banking • Compliance
Resources	<ul style="list-style-type: none"> • Pending investment banking deals • Research reports and workpapers
Frequency	<ul style="list-style-type: none"> • As required when deals or research are pending
Action	<ul style="list-style-type: none"> • Notify and train department associated persons regarding confidentiality requirements • Secure confidential information by locking paper files; limiting computer access; using codes or deleted names on deals or reports; provide physical separation between departments that maintain confidential information • Monitor communications and password access • Contact Compliance when violations of confidentiality are identified • Compliance: monitor trading of an issue the subject of a deal or report • Compliance: take corrective action when necessary which may include: <ul style="list-style-type: none"> ○ Withdraw research report ○ Delay or suspend an IB deal

	<ul style="list-style-type: none"> ○ Contact counsel ○ Additional training for personnel
Record	<ul style="list-style-type: none"> ● Training of associated persons including subjects covered, who attended, when occurred ● Deal or research files with codes or deleted names ● Assignment of passwords or other methods to limit computer access ● Monitored communications and password usage ● Corrective actions taken

Associated persons in departments with access to inside information or other information where confidentiality is required (e.g., investment banking deals, research reports) are subject to strict confidentiality requirements. Confidential information may only be shared with those outside the department on a need-to-know basis (see *Bringing An Employee Over the Wall* in this chapter) with the supervisor's approval and the participation of Compliance where required (e.g., communications between Research and Investment Banking). Some procedures for maintaining confidentiality include:

- Maintain all paper files in a locked and secured area.
- Access only those computer files authorized using assigned passwords. Do not reveal or share passwords.
- Refrain from discussing in public areas or with others outside the department (including family members, friends, etc.) any activities that are not publicly known.
- Use code names or delete names on sensitive drafts that identify projects or banking clients.
- Report any potential breaches immediately to the supervisor and/or Compliance.

Failure to maintain confidentiality may result in withdrawal from a deal, suspending issuance of reports, or internal or regulatory disciplinary action. Breaches of confidentiality could have serious consequences for CEI and its Associated persons.

9.8.4 Access to Confidential Information Limited to Certain Employees

Access to actual or potential inside information obtained in the normal course of CEI's banking activities is limited to the following employees:

1. Employees within the respective banking department who need to know
2. CEI's chief compliance officer
3. CEI's general counsel
4. The Chief Executive Officer
5. Other employees brought "over the wall" in accordance with the procedure outlined in the next section

9.8.5 Bringing an Employee "Over the Wall"

There may be occasions where investment banking Associated persons require information from an employee in research, sales, trading, or other business areas of CEI. Bringing an employee not employed in the investment banking department into confidential discussions is often termed bringing the employee "over the wall." Doing so may result in restrictions on research, trading, or other business of CEI because the employee is now in possession of material, non-public information and cannot continue to conduct his or her normal responsibilities. Because it is important to both maintain the confidentiality of inside information and consider carefully any action

that might restrict CEI's ability to conduct its business, the manager (or manager's designee) of the investment banking department is required to contact Compliance before bringing another employee over the wall. Compliance will maintain a written record of the:

- date of the action
- name and department of the employee brought over the wall
- the name of the companies which are the subject of the investment banking activity that resulted in bringing the employee over the wall
- name of the person requesting access to the employee

Compliance will also make a determination whether further restrictions on research, trading, or other CEI activities are appropriate because of the action of bringing an employee over the wall.

9.8.6 Notification to Compliance

When CEI is engaged to provide investment banking services to an issuer, and that engagement may result in obtaining inside information, the designated supervisor is responsible for notifying Compliance of the engagement so that the issuer may be included on CEI's Watch or Restricted Lists, if appropriate. This includes notification of any "target" companies that may become part of the investment banking transaction. Refer to the chapter *CORPORATE FINANCE* for more information about activities affecting investment banking activities.

When CEI is engaged to provide municipal finance services to a municipal issuer regarding an advanced refunding, the designated supervisor is responsible for notifying Compliance so the issue may be included on CEI's Watch List.

9.8.7 Monitoring the Information Barrier

Compliance monitors trading activities in issues where CEI may be in possession of material, non-public information through the use of CEI's Watch or Restricted Lists. The sections *Restricted List* and *Watch List* further explain those procedures.

9.8.8 Certification by Affected Employees

Associated persons in departments subject to CEI's Information Barrier confidentiality procedures will be requested to certify, on an annual basis, that they have read and agree to abide by CEI's Information Barrier Procedures and Policy Regarding Insider Trading. The certifications will be maintained by the designated supervisor of the affected department.

9.8.9 Education and Training of Associated Persons

To ensure associated persons are familiar with CEI's Insider Trading policy CEI has established the following procedures:

- Associated persons receive CEI's Insider Trading policy upon hire and certify their receipt and understanding.
- Annually, associated persons complete CEI's Annual Certification which includes their acknowledgment of receipt and understanding of the Insider Trading policy.
- Associated persons in sensitive departments (investment banking) sign an attestation on an annual basis.
- When procedures are revised, associated persons will be notified by memorandum.

- Insider Trading is a subject periodically included in CEI's continuing education and compliance meeting programs.

9.9 Watch List

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Notification of confidential investment banking activities • Notification of pending material research reports/recommendations • Daily Transaction Report • Confirmations/statements for associated persons' outside accounts
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Maintain confidential Watch List • Review transactions to identify trades in securities on the Watch List including debt and derivative securities • For identified trades: <ul style="list-style-type: none"> ○ Evaluate whether there is a potential breach in CEI's Information Barriers considering solicited vs. unsolicited; timing or unusual nature of transaction ○ For pending research reports, determine whether trading activities must be limited or suspended depending on the materiality of the report/recommendation and its likely affect on market prices ○ Take corrective action, if necessary
Record	<ul style="list-style-type: none"> • Compliance maintains records of: <ul style="list-style-type: none"> ○ Watch Lists, including the date and time a company is added or deleted ○ The name of the person adding or deleting the company ○ Identified trades, including date of review; accounts involved; underlying records possibly including memos, analyses, and statements/confirmations; summary of disposition; and initials/signature of reviewer.

Compliance will maintain a confidential Watch List which will include issues where CEI may be in possession of material, non-public information. This includes pending research recommendations which may affect the market price of the security (debt or equity) and its derivatives. The Watch List is available only to specified CEI personnel. Compliance will monitor daily trading to identify transactions in securities on the Watch List and take action as necessary. Compliance will also record the date and time when an issue is added to and removed from the Watch List.

9.10 10b5-1 Plans

[ABA guidance regarding 10b5-1 plans (<http://www.abanet.org/buslaw/blt/2008-05-06/parris.shtml>)]

Responsibility	<ul style="list-style-type: none"> • Compliance
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Resources	<ul style="list-style-type: none"> • RR regarding 10b5-1 plans
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review the request and the nature of the RR's participation/activity • Approve or disapprove • If approved, provide guidance regarding allowable activities/limitations
Record	<ul style="list-style-type: none"> • Requests, approval/disapproval, and communications regarding guidelines and allowable activities/limitations

Under Rule 10b-5 of the '34 Securities Exchange Act, a person can face insider trading liability for trading securities while aware of material, nonpublic information about the issuer or its securities. 10b-5 also provides some affirmative defenses or exceptions to this liability. One of the defenses for executives subject to knowledge of inside information is the use of a pre-existing trading plan (10b5-1 Plan) that complies with the requirements of 10b-5(c). This section only summarizes requirements and guidelines regarding such plans. The executive at risk for 10b-5 liability is ultimately responsible for conferring with legal counsel and assuring himself or herself that such a plan is structured properly for avoidance of liability.

- The written plan must be adopted before the individual becomes aware of any material, nonpublic information.
- The plan must specify either the amount and price and dates of for purchases or sales or a written algorithm or computer program to determine the amount and price of the securities to be purchased or sold and the dates of purchases or sales.
- The plan must not permit the executive to exercise any subsequent influence over how, when, or whether purchases or sales would be effected under the plan.
- It must be demonstrable that purchases or sales actually took place under the plan.
- There cannot be alterations or deviations from the terms of the plan (changing the amount, price or timing) and cannot be alterations to a corresponding or hedging transaction or position.
- The plan must be entered into in good faith and not as part of a scheme to evade the prohibitions of 10b-5.

The plan may have to comply with the issuer's insider trading policies and procedures and public disclosure of such a plan may be necessary. Other guidelines may strengthen the defensibility of the plan and its execution including eliminating communications between the broker and the executive; avoiding multiple plans for one executive; and minimizing modifications to a plan which may call into question the good faith basis for establishing the plan.

Compliance must be contacted prior to engaging in transactions on behalf of a 10b5-1 plan.

10 COMMUNICATIONS WITH THE PUBLIC

[FINRA Rule 2200 Series, 3110(b)(4), 3110.06, 3110.07, 3110.08 and 3110.09; FINRA Regulatory Notice 19-31; FINRA Rule 2210 Q & A: <https://www.finra.org/industry/finra-rule-2210-questions-and-answers>]

10.1 Introduction

[FINRA Rule 2200 Series; FINRA Regulatory Notice 12-29]

This chapter explains regulatory and policy requirements when dealing with the public through a wide range of media including social media. "Communications" consist of correspondence, retail communications and institutional communications.

In general,

- All communications must be truthful and balanced.
- Communications (incoming and outgoing) are subject to review by CEI. Do not expect confidentiality for any communications that are received by you or that you send from CEI.
- CEI's facilities and systems (email, fax, *etc.*) should be used for business purposes only.
- Records of communications (incoming and outgoing) are retained by CEI, are reviewed by CEI, and are subject to review by regulators and subpoena in civil actions.

10.2 Definitions

[FINRA Rule 2210(a)]

There are three broad categories of communications as defined by rule. ***"Written communications" include electronic communications such as email, texting, and social media messaging.***

Retail communication: includes **any** written communication (including advertising, telemarketing and other sales scripts and other written communications) that is published, distributed or made available to **more than 25** retail investors within any 30 calendar-day period. *Requires pre-use approval except that the following do not require pre-use approval and may be supervised like correspondence:*

- *Communications excepted from the definition of "research report" **unless** the communication makes any financial or investment recommendation;*
- *Any retail communication that is posted on an online interactive electronic forum; and*
- *Any retail communication that does not make any financial or investment recommendation or otherwise promote a product or service of CEI.*

Institutional communication: includes written communications that are distributed or made available only to institutional investors. *(Does not require pre-use approval, reviewed consistent with correspondence requirements.)*

Correspondence: Includes any written communication that is distributed or made available to **25 or fewer** retail investors within any 30 calendar-day period. *(Does not require pre-use approval unless indicated otherwise for specific products or services.)*

Additional definitions include:

Retail investor: includes any person other than an institutional investor, regardless of whether the person has an account with CEI.

Institutional investor: includes a:

1. government entity or subdivision thereof;
2. employee benefit plan, or multiple employee benefit plans offered to employees of the same employer, that meet the requirements of Section 403(b) or Section 457 of the Internal Revenue Code and in the aggregate have at least 100 participants, but does not include any participant of such plans;
3. qualified plan, as defined in Section 3(a)(12)(C) of the Exchange Act, or multiple qualified plans offered to employees of the same employer, that in the aggregate have at least 100 participants, but does not include any participant of such plans;
4. FINRA member firm or registered person of such a member; and
5. person acting solely on behalf of any such institutional investor.

Institutional investor also includes [per FINRA Rule 4512(c)] an account for:

1. a bank, savings and loan association, insurance company or registered investment company;
2. an investment adviser registered either with the SEC under Section 203 of the Investment Advisers Act or with a state securities commission (or any agency or office performing like functions); or
3. any other person (whether a natural person, corporation, partnership, trust or otherwise) with total assets of at least \$50 million.

10.3 Retail Communications

Responsibility	<ul style="list-style-type: none"> • Advertising Supervisor
Resources	<ul style="list-style-type: none"> • Retail communications submitted for review
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review proposed retail communications • Make revisions as needed • Provide requestor with approved copy or notify of disapproval • File communication with FINRA, if required; notify requestor of any required delay to receive FINRA approval
Record	<ul style="list-style-type: none"> • Dates of first and (if applicable) last use • Copies of reviewed communications, including the reviewer's approval and date of approval • For communications not requiring pre-approval, the name of the person who prepared or distributed the communication • Information regarding the source of any statistical table, chart, graph or other illustration used in the communication • Copies of communications filed with FINRA (see section <i>FINRA Filing Requirements</i>) and FINRA response/approval (as applicable) • If the communication was prepared by another member firm and filed with FINRA, the name of the firm and a copy of FINRA's review letter

Retail communications, which include advertising, require the **prior approval** of the advertising supervisor (or a designated covering principal) prior to use or distribution. Advertising may be filed with FINRA depending on the content. The person submitting the retail communication for review (and that person's supervisor, if applicable) will be notified of approval or the need to make changes prior to release.

10.3.1 FINRA Filing Requirements

[FINRA Rule 2210(c)]

Some retail communications must be filed with FINRA. The following chart outlines those requirements and the corresponding rule cite.

- Filings must be accompanied by FINRA's Advertising and Sales Literature Filing Cover Sheet.
- Filings should identify the reference number of any communication previously submitted by CEI and already reviewed by FINRA that is similar to the current filing.
- All retail communications to be submitted to FINRA must be approved by the designated supervisor prior to submission to FINRA.
- The actual or expected date of first use or publication and the name and CRD number of the approving supervisor must be included with the FINRA filing. [FINRA Rule 2210(c)(5)]

It is not necessary to file any retail communication which has previously been filed and is used without any changes. FINRA rules should be consulted for specific requirements and some exclusions [Rule 2210(c)(7)] from the requirements.

Retail Communication Content Requiring Filing	When	FINRA Rule
New member firms only: certain broadly disseminated retail communications such as generally accessible websites, print media communications, and TV and radio commercials. Free writing prospectuses are also included other than those exempt from filing with the SEC. The rule also excludes research reports concerning only securities listed on a national securities exchange [other than those that must be filed under Section 24(b) of the Investment Company Act of 1940]	One-year requirement to file at least 10 business days prior to use starting on the date the firm's membership with FINRA becomes effective, per the CRD. Free writing prospectuses may be filed within 10 business days of first use.	2210(c)(1)(A)
Investment company using rankings or performance comparison information that is not generally published or is created by the investment company, its underwriter or affiliate (must be filed with corroborating data)	10 business days prior to first use; cannot use until changes required by FINRA have been made	2210(c)(2)(A) 2212 2214
Research reports concerning unlisted securities	Within 10 days of distribution	2210(c)(7)(O)

Research reports which must be filed under Section 24(b) of the Investment Company Act of 1940	Within 10 days of distribution.	2210(c)(7)(O)
Security futures (with certain exceptions)	10 business days prior to first use; cannot use until changes required by FINRA have been made	2210(c)(2)(B) 2215
Bond mutual funds that include volatility ratings	10 business days prior to first use; cannot use until changes required by FINRA have been made	2210(c)(2)(C) 2213
Options communications used prior to the delivery of the Options Disclosure Document	10 calendar days prior to first use; cannot use until changes required by FINRA have been made	2220(c)
Public direct participation programs	Within 10 business days of first use	2210(c)(3)(B)
Templates for written reports produced by or concerning an investment analysis tool <i>(Retail communications based on templates previously filed with FINRA where the only changes are to update statistical or other non-narrative information do not require re-filing.)</i>	Within 10 business days of first use or publication	2210(c)(3)(C)
Registered CMOs	Within 10 business days of first use or publication	2210(c)(3)(D) 2216
Registered structured products that are derived from or based on a single security, a basket of securities, an index, a commodity, a debt issuance or a foreign currency	Within 10 business days of first use or publication	2210(c)(3)(E)
Television or video where CEI has filed with FINRA a draft version of a "story board"	Within 10 business days of first use or broadcast	2210(c)(4)
Certain 529 Plans communications offering registered investment company products	Within 10 business days of first use or publication	2210(c)(2)(A)
Certain broker-prepared widely disseminated free-writing prospectuses that are required to be filed with the SEC under Securities Act 433(d)(1)(ii) [Excludes those exempt from filing with the SEC]	Within 10 business days of first use or publication	Regulatory Notice 10-52

10.4 Institutional Communications

[FINRA Rule 2210(b)(3)]

Responsibility	<ul style="list-style-type: none"> • Associated Person
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	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Communications sent to institutions
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Supervisor: Communications limited to institutions reviewed after sending: <ul style="list-style-type: none"> ○ Review outgoing branch correspondence ○ Review email on a risk basis using Smarsh • Associated Person: Limit distribution to only institutions by: <ul style="list-style-type: none"> ○ Advising the receiving institution that the material is for institutions only ○ Adding a legend to material; ○ Asking the receiving institution to affirm materials will be distributed to institutional investors only; or ○ Taking other steps to limit distribution • If institutional communications will be distributed to retail customers or CEI becomes aware they are going to retail customers: <ul style="list-style-type: none"> ○ Subject the communication to reviews required for those sent to retail customers (see <i>Outgoing Communications</i>); or ○ Cease providing material to the institution • Include institutional communications in training (approval requirements, requirements when institutions forward communications to retail customers, acceptable content, other subjects)
Record	<ul style="list-style-type: none"> • Institutional communications reviewed including record of who reviewed and date reviewed • Institutional affirmations limiting distribution • Action taken if an institution distributes institutional-only communications to retail investors • Training including subjects covered, who attended, date conducted

Institutional communications (including electronic communications) are subject to review and retention by CEI. Communications sent only to institutions do not require approval prior to sending. Those sent to institutions that also will be sent to retail customers (whether by CEI or forwarded by the institution) require approval described in *Outgoing Communications*, including prior approval for any communication provided to more than 25 retail investors in a 30-day period. Institutions may be asked to provide written affirmation that communications sent to them will NOT be provided to retail customers.

Institutional communications are subject to the general standards that appear below.

10.5 General Standards

[FINRA Rule 2210(d)(1)]

Communications must meet general standards which are summarized below. The rules should be consulted for details.

- Communications must be based on principles of fair dealing and good faith, must be fair and balanced, and must provide a sound basis for evaluating the facts and must not omit any material fact where its omission would make the communication misleading.
- Communications may not contain false or misleading statements or any statement CEI knows to be untrue.
- Information may be placed in a legend or footnote only in the event that such placement would not inhibit an investor's understanding of the communication.
- Statements must be clear and not misleading within the context in which they are made and must provide balanced treatment of risks and potential benefits. Communications must be consistent with the risks of fluctuating prices and the uncertainty of dividends, rates of return and yield inherent to investments.
- The nature of the audience to which the communication will be directed must be considered providing appropriate details and explanations appropriate to the audience.
- Communications may not predict or project performance, imply that past performance will recur or make any exaggerated or unwarranted claim, opinion or forecast. Exceptions include hypothetical illustrations of mathematical principals, investment analysis tools, or research reports subject to certain conditions.

10.5.1 Comparisons

Any comparison in retail communications between investments or services must disclose all material differences between them, including (as applicable) investment objectives, costs and expenses, liquidity, safety, guarantees or insurance, fluctuation of principal or return, and tax features.

10.5.2 Disclosure of The Firm's Name

All retail communications (other than "blind" advertisements used to recruit personnel) and correspondence must:

- prominently disclose the name of the firm, Coastal Equities, Inc.;
- reflect any relationship between CEI and any non-member or individual who is also named; and
- if it includes other names, reflect which products or services are being offered by CEI.

10.5.3 Tax Considerations

- References to tax-free income must indicate which income taxes apply, or which do not.
- Communications must not characterize income or investment return as tax-free or exempt when liability is merely postponed.
- A comparative illustration of the mathematical principles or tax-deferred versus taxable compounding must meet seven specified criteria.

10.5.4 Disclosure of Fees, Expenses and Standardized Performance

[FINRA Regulatory Notice 13-23]

Communications about fees must be accurate and balanced. Representing that fees are not charged in connection with retail accounts and IRAs is inaccurate and a violation of rules when the account is subject to other charges or fees. Investment products have their own associated costs including commissions, management fees, and other product-level expenses. For example, stating that there are no fees charged or highlighting "no fees" and then providing separate, less-prominent disclosure of other fees is misleading. Footnotes do not meet the requirements for disclosure.

Claims regarding fees must be accompanied by clear disclosure of the types of fees that may be charged. A statement that "other account fees, fund expenses, brokerage commissions and service fees may apply" would be consistent with rule requirements. This statement could be hyperlinked to CEI's web site where fees are explained.

Communications that present certain permitted investment company performance data must disclose performance information required by SEC Rule 482 and Investment Company Act Rule 34b-1, among other things. This information must be set forth prominently, and in any print advertisement, in a prominent text box that contains only the required information.

10.5.5 Recommendations

- If a communication includes a recommendation of securities, it must have a reasonable basis and disclose:
 - whether CEI is making a market in the recommended security (or in the underlying security if the recommended security is an option or security future) or the security will be bought or sold on a principal basis;
 - if CEI or any associated person directly and materially involved in the preparation of the content of the communication has a financial interest in the securities of the issuer; and
 - if CEI was a manager or co-manager of a public offering of any securities of an issuer whose securities were recommended within the past 12 months.
- CEI must provide, or offer to furnish upon request, available investment information supporting the recommendation (including, for corporate equity securities, the price at the time the recommendation is made).
- Generally, a communication may not refer to past specific recommendations of CEI that were or would have been profitable; however, it may set out or offer to furnish a list of all recommendations as to the same type of securities made by CEI within the past year if the communication meets certain conditions, including the condition that the communication contain a specified, prominently displayed cautionary legend.
- These requirements do not apply to any communications that meet the definition of "research report" and include required research disclosures.
- The general disclosure requirements for recommendations do not apply to any communication that recommends only registered investment companies or variable insurance products, if such communications have a reasonable basis for the recommendation.

10.5.6 Prospectuses Filed with the SEC

Prospectuses, preliminary prospectuses, fund profiles and similar documents that have been filed with the SEC are not subject to the content standards except for investment company prospectuses published pursuant to Rule 482 and broadly disseminated free writing prospectuses that are filed with the SEC pursuant to Securities Act Rule 433(d)(1)(ii).

10.5.7 Limitations on Use of FINRA's Name and Any Other Corporate Name Owned by FINRA

[FINRA Rule 2210(e); FINRA email address for questions: trademarks@finra.org]

CEI may indicate its FINRA membership in only three ways:

- In a communication that complies with the standards of FINRA Rule 2210 and neither states nor implies that FINRA or any other corporate name or facility owned by FINRA, or any other regulatory organization, endorses, indemnifies or guarantees CEI's business practices, selling methods, the class or

type of securities offered, or any specific security; references are limited to "Reviewed by FINRA" or "FINRA reviewed;"

- In a confirmation statement for an OTC transaction that includes a specified legend; or
- On CEI's website (or any related firm website about securities business), as long as CEI provides a hyperlink to the homepage of FINRA's website in close proximity to CEI's indication of FINRA membership.

Member firms are prohibited from including FINRA's logo on web sites, business cards, stationery, or other marketing materials. The FINRA trademark or references to membership may not be included in any trademark of CEI or associated person. CEI may, however, include "FINRA Member Firm" or "Member of FINRA" on such materials.

10.6 Approval

[FINRA Rule 2210(b)]

Supervisory review and approval requirements are outlined in the following chart.

Type	Approval Required
Retail communications	<p>Must be approved by the designated Advertising Supervisor before the earlier of its first use or filing with FINRA.</p> <p>Prior approval is not required for the following retail communications:</p> <ul style="list-style-type: none"> • Another FINRA member already filed it and received approval and the Firm does not materially alter it or use it inconsistent with FINRA's approval • Retail communications supervised as correspondence where: it is excepted from the definition of "research report" unless it makes any financial or investment recommendation; it is posted on an online interactive electronic forum; and it does not make any financial or investment recommendation or otherwise promote a product or service of the member.
Institutional communications	<ul style="list-style-type: none"> • Reviewed after sending
Correspondence	<ul style="list-style-type: none"> • Reviewed after sending
Seminar materials	Advertising Supervisor prior approval

Advertising	Advertising Supervisor prior approval
Pre-approved form letters, group e-mails, hedge clauses, other pre-approved communications	Require no additional approval if used without change

10.6.1 Coastal Business Cards and Stationery; Email Signatures

Coastal's formatted business card template and letterhead are pre-approved and need not be pre-approved by a principal unless the advisor utilizes professional designations or additional text other than the contact information of the advisor on record and Coastal's standard disclosure language. All other business cards and letterhead must be pre-approved by the Advertising Supervisor prior to first use.

Email should be submitted to the Advertising Supervisor prior to first use with retail investors. Email, from a Coastal-approved email address, should be forwarded to the Advertising Supervisor, including the appropriate disclosure language below the signature. The Advertising Supervisor will reply with corrections or approval. The approval email should be printed as a PDF and placed in the associated person's folder in the home office.

10.7 Testimonials

[FINRA Rule 2210(d)(6)(B); FTC Guides Concerning the Use of Endorsements and Testimonials:
<http://ftc.gov/os/2009/10/091005revisedendorsementguides.pdf>]

There are specific requirements when using testimonials in communications with the public, including disclosure regarding payment of more than \$100 in value paid for the testimonial. Compliance should be contacted before preparing any communications that include testimonials.

10.8 Telemarketing Scripts

All scripts used for telemarketing calls are considered retail communications and require the approval of the designated supervisor prior to use. The section *Cold Callers* includes further information regarding the use of scripts and callers.

10.9 SIPC Membership

[Securities Investor Protection Act of 1970; United States Code Title 15 Chapter 2B-1; SIPC web site at www.sipc.org/how/sipclogo.aspx]

Advertising must include a notation that CEI is a member of SIPC, e.g., "Member, SIPC." If an explanatory statement will be included in advertising explaining what SIPC is, one of the following two standardized phrases must be included:

- Member of SIPC, which protects securities customers of its members up to \$500,000 (including \$250,000 for claims for cash). Explanatory brochure available upon request or at <http://www.sipc.org>.
- Member of SIPC. Securities in your account protected up to \$500,000. For details, please see <http://www.sipc.org>.

The words "Member, SIPC" may be omitted if the official explanatory statement is used in conjunction with the official SIPC symbol.

When SIPC is referenced in CEI's web site, the site will include a hyperlink to the SIPC web site.

"Advertising" is defined under SIPC rules as any promotional material used in or on any newspaper, magazine, or other periodical, radio, television, telephone or tape recording, videotape display, motion picture, slide presentation, telephone directory, sign or billboard, electronic or other public media.

10.10 Recordkeeping Requirements for Retail and Institutional Communications

[FINRA Rule 2210(b)(4)(A); SEC Securities Exchange Act of 1934 Rule 17a-4]

Records of retail and institutional communications must include:

- Originals of all communications received and copies of all communications sent
- While not "retail" or "institutional" communications, records of inter-office memoranda and communications relating to CEI's business [SEC Rule 17a-4(b)(4)]
- The dates of first use and (if applicable) last use
- The name of the registered principal who approved the communication and the date of approval
- For communications not approved by a supervisor prior to first use, the name of the person who prepared or distributed the communication (where clerical staff prepares or distributes the communication, include the name of the person on whose behalf the communication was prepared or distributed)
- The source of statistical tables, charts, graphs and other illustrations
- For a retail communication prepared by another firm and submitted to FINRA, the name of the firm and a copy of FINRA's review letter
- A record that the item was filed with FINRA and when filed (if required)
- Changes recommended by FINRA and approval received from FINRA (if required)

10.11 Outgoing Communications

[FINRA Rule 3110(b)(4), 3110.07, 3110.08 and 3110.09]

This section outlines requirements for outgoing communications which includes written and electronic communications. Electronic communications are subject to specific procedures for review; see the section *Electronic Mail* in this chapter and the section *Electronic Communications Policy* in the chapter *GENERAL EMPLOYEE POLICIES*.

10.11.1 Review and Approval

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor: weekly review • Advertising Supervisor: pre-approval
Resources	<ul style="list-style-type: none"> • Outgoing customer communications
Frequency	<ul style="list-style-type: none"> • Pre-approval as needed • Weekly review
Action	<ul style="list-style-type: none"> • Review communications for appropriateness of language • Pre-approve retail communications that are sent to more than 25 persons in a 30-day period (other than those excluded; see <i>Retail Communications</i> under <i>Definitions</i> in this chapter) • Review other communications after sending

	<ul style="list-style-type: none"> • Identify outgoing communications that may constitute "research" under NASD Rule 2711(a)(g) • Take corrective action, if necessary, which may include consultation with the RR and/or Compliance, sending corrected communications, added training for the RR, restrictions on communications, or other action considered appropriate for the circumstance
Record	<ul style="list-style-type: none"> • Communications including reviewer's initials or other record of review and action taken, if appropriate

Outgoing customer communications are subject to review and approval by the designated supervisor.

- Retail communications sent to more than 25 persons in a 30-day period require the supervisor's approval **before** sending.
- Other communications will be reviewed and approved after sending.
- Some communications (depending on type and other factors) require prior approval (see the section *Approvals*).

Pre-approved form letters and group e-mails **used without change** (other than customer name, address) may be sent to customers or prospective customers without additional approval. Records of to whom form letters and group e-mails are sent must be retained in CEI's records.

10.11.1.1 Risk-Based Reviews

[FINRA Rule 3110.06]

Responsibility	<ul style="list-style-type: none"> • Compliance: Establish risk-based reviews • Designated supervisors: conduct reviews
Resources	<ul style="list-style-type: none"> • Evaluation of CEI's size, types of business, supervisory structure
Frequency	<ul style="list-style-type: none"> • At inception of risk-based procedures and ongoing
Action	<ul style="list-style-type: none"> • Compliance: <ul style="list-style-type: none"> ○ Determine scope of risk-based review (size, what is subject to review, who is subject to review) ○ Develop procedures and update as necessary ○ Provide procedures and education/training to communications reviewers ○ Include communications requirements in RR training ○ Include risk-based procedures in periodic reviews of branches, offices, and supervisory system, controls and procedures ○ Identify RRs with complaint/disciplinary history necessitating review of ALL communications and notify the RR's supervisor ("heightened supervision") • Designated supervisors: <ul style="list-style-type: none"> ○ Review communications for compliance with policies and securities rules/laws

	<ul style="list-style-type: none"> ○ Take corrective action, if necessary, including consulting with RR and/or Compliance, contacting the customer, issuing corrections, <i>etc.</i>
Record	<ul style="list-style-type: none"> • Procedures for risk-based reviews are included in the manual • Updates to procedures are retained by Compliance • Education and training are documented including how conducted, who attended, and dates of education/training including educational memoranda • Designated supervisors: records of reviews and action taken, if any

Supervisors may review written outgoing communications on a risk-based basis using the guidelines that follow, or, if risk-based review is not adopted, review all outgoing communications.

Risk-based guidelines include the following. "Pre-review" refers to review and approval of written communications **before** it is sent. Communications subject to "post-review" may be reviewed after sending. All RRs are subject to review of at least some of their communications on a regular basis. Risk-based review is permitted for the following type(s) of outgoing communications:

- Written (hard-copy) communications
- E-mails
- Faxes
- Interactive electronic communications (social media/blogs)
- Post-review:
 - Communications that are flagged by CEI's lexicon system provided by Smarsh.
- Refer to the section *Content Guidelines* that follows for guidance on acceptable content
- For communications that includes a recommendation, determine that the information presented balances the benefits and risks of the recommendation and, if the subject security is high-risk, determine the recommendation is appropriate for the customer by conferring with the RR and/or reviewing new account information
- If there are problems with an RR's communications that is being minimally sampled, increase the reviews and note the change in the supervisory log.

10.11.2 Content Guidelines

Items to consider when preparing and reviewing outgoing communications (and other forms of written or electronic communications) include:

- Truthfulness and good taste are required.
- Exaggerated, unwarranted, or misleading statements or claims are prohibited.
- Promises or guarantees: past performance may not be used to promise, guarantee, or imply future profits or income from securities.
- Projections and predictions are not permitted.
- Comparisons of personnel, facilities, or charges with those of other broker-dealers should not be made unless supported by the facts, and other firms' names should not be included.
- Communications regarding securities subject to pending distributions (underwritings) are generally not permitted.
- Communications regarding securities sold by prospectus (mutual funds, limited partnerships, *etc.*) must be approved by Compliance prior to sending (except for pre-approved communications where no changes are made).

- Only firm-approved hedge clauses may be used.
- Tax advice must not be provided; the customer should be referred to his or her tax adviser for such issues.
- Photocopying and distributing copyrighted material may violate copyright laws.
- Profit and loss or other portfolio analyses should include a disclaimer that the customer should rely on customer statements provided by CEI and any analysis or calculation is provided for information purposes only.
- The use of firm letterhead should be restricted to firm-related matters.
- Communications regarding options is subject to specific requirements which are discussed in the chapter *OPTIONS*.

10.11.3 Letters and Notes

Copies of letters, notes, and similar communications must be provided to the on-site designated supervisor on the day sent. Otherwise, such communications must be scanned and emailed to the off-site supervisor at least weekly.

10.11.4 Facsimiles

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Outgoing faxes
Frequency	<ul style="list-style-type: none"> • Weekly
Action	<ul style="list-style-type: none"> • Review outgoing faxes as follows: <ul style="list-style-type: none"> ○ Review faxes on a sampling basis (see risk-based techniques in the Outgoing Communications section of this chapter). • For faxes with questionable content: <ul style="list-style-type: none"> ○ Confer with RR ○ Confer with Compliance, if necessary ○ Take corrective action which may include: <ul style="list-style-type: none"> ▪ Sending a revised fax to the recipient ▪ Training for RR ▪ Disciplinary action against RR which may include a reprimand, suspension, or termination
Record	<ul style="list-style-type: none"> • Outgoing paper faxes with reviewer's initials • E-faxes captured by Smarsh are reviewed by lexicon • Records of corrective action taken

Facsimiles are included in the definition of "outgoing communications" and are subject to review by the designated supervisor.

Facsimile transmissions may NOT be used for unsolicited advertising. Refer to the section *Calling (Telemarketing) And Fax Restrictions* in this chapter.

10.11.5 Communications Defined as "Research"

[SEC Regulation AC; FINRA Rule 2241(a)(11)]

RRs are **not** permitted to send communications that may be deemed "research" since there are complex requirements that apply to the issuance of research reports. Federal and SRO rule interpretations define "research" as any written communications (including electronic) that includes an analysis of equity securities of individual companies or industries, and that provides information reasonably sufficient upon which to make an investment decision and that is distributed to at least 15 persons. This applies even if the author does not hold the title of "research analyst" and does not work in a research department.

There are specific exceptions under SRO rules. Questions regarding whether a communication constitutes "research" should be referred to Compliance.

10.12 Incoming Correspondence

[FINRA Rule 3110(b)(4), 3110.07, 3110.08 and 3110.09]

In this section, "correspondence" means written and electronic communications received by CEI.

10.12.1 Review of Incoming Correspondence

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Incoming correspondence, including correspondence marked "personal and confidential"
Frequency	<ul style="list-style-type: none">• Weekly
Action	<ul style="list-style-type: none">• Review all incoming correspondence• Customer securities and checks received in error must be promptly returned to the customer and logged• Refer customer complaints to Compliance• Refer audit letters to Compliance
Record	<ul style="list-style-type: none">• Resident designated supervisor: Initial each piece of correspondence and maintain in branch/department incoming customer correspondence files.• Off-Site supervisor: See section 5.12.2

All incoming written correspondence will be opened and reviewed by the designated supervisor or someone qualified and appointed by the CSO. This review includes letters, facsimiles, courier deliveries, and other forms of written communication. Electronic mail is subject to specific procedures for review; see the section *Electronic Mail* in this chapter and the section *Electronic Communications Policy* in the chapter *GENERAL EMPLOYEE POLICIES*.

The following guidelines for review apply:

- Correspondence identified as "Confidential" will be opened and reviewed.

- Obvious non-customer correspondence (bank statements, advertising, *etc.*) will not be opened and will be forwarded directly to the addressee.
- Audit letters (requests from customers' auditors for verification of account positions) will be forwarded directly to Compliance for response.
- Complaints will be immediately forwarded to the RR's supervisor and to Compliance.
- Checks or securities received erroneously will be immediately returned to the customer, the RR notified of receipt, and an entry placed in the branch log noting the date, customer name, identify the securities or check, and the date and manner of return to the customer.
- Original customer correspondence will be retained for CEI's files; the addressee will receive a copy.
- Original customer correspondence will be forwarded to the designated supervisor for review, initialing, and filing.

10.12.2 Offices without Resident Supervisors

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Incoming customer correspondence
Frequency	<ul style="list-style-type: none"> • Weekly
Action	<ul style="list-style-type: none"> • Supervisors: review incoming correspondence in accordance with CEI's policy • Compliance: require branch reviews to verify procedures are being followed
Record	<ul style="list-style-type: none"> • Incoming correspondence retained by designated supervisor in accordance with CEI's policy on incoming correspondence • Compliance retains records of branch reviews

For offices without a resident registered supervisor, copies of all incoming, written correspondence related to CEI's securities business must be forwarded to the designated supervisor at the end of each week for review.

Compliance with this requirement will be audited during branch reviews.

10.12.3 Personal Mail

Employees should direct all personal mail to their home address. Personal mail is subject to incoming correspondence and electronic mail review policies.

10.13 Legends and Footnotes

[FINRA Rule 2210(d)(1)(C)]

When legends or footnotes are included in public communications, they cannot be placed or sized in a way that limits the investor's ability to read or understand the information. Small fonts may inhibit reading the information or may inappropriately diminish the importance of the information. Bold claims balanced by a footnote may also mislead the reader.

10.14 Internal Communications

[FINRA Rule 3110(b)(4)(B), 3110.06, 3110.07, 3110.08 and 3110.09]

10.14.1 Inter-Office Communications

[SEC Securities Exchange Act of 1934 Rule 17a-4(b)(4)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Inter-office communications
Frequency	<ul style="list-style-type: none"> • On-going
Action	<ul style="list-style-type: none"> • Review of inter-office communications and business-related communications is integrated as part of each supervisor's on-going review of correspondence using the lexicon system • Review for compliance with policy and rule/law requirements • Where questions arise, take follow up action which may include consultation with the RR, consultation with Compliance
Record	<ul style="list-style-type: none"> • Records of inter-office communications • Record of reviews and action taken, if any

You should presume that any inter-office communications may be subject to regulatory review, and therefore must comply with good business practice as well as CEI's policies on communications and securities rules/laws. Inter-office memos and other communications are subject to review and retention requirements. CEI utilizes e-mail for its inter-office communications and has determined that review of such communication shall be conducted utilizing the firm's lexicon flagging system within Smarsh. This review is integrated in all supervisors' on-going review of electronic communications.

10.14.2 Internal Use Only, BD Use only

Printed or electronic information marked "internal use only," "BD Use only," or otherwise indicates that distribution is not permitted or limited, may not be sent or otherwise provided to individuals outside CEI.

10.15 Investment Analysis Tools

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Description of proposed investment analysis tools
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Evaluate efficacy of tool, its source, and its proposed use • Approve tool or return to submitter for changes or disapprove • If required, make filing with FINRA
Record	<ul style="list-style-type: none"> • Review of tool including approval or disapproval

	<ul style="list-style-type: none"> • Vendors approved • FINRA filings, if any are required
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CEI may use investment analysis tools for use by customers either independently or with assistance from an RR. An "investment analysis tool" is an interactive technological tool that produces simulations and statistical analyses that present the likelihood of various investment outcomes if certain investments are made or certain investment strategies or styles are undertaken, serving as a resource to investors in evaluating the potential risks and return of investment choices.

Recommendations based on use of the tool are subject to suitability rule requirements and other rules about fair dealing with customers. **Proposals for investment analysis tools (including methodology, proposed use, types of investors who will use the tool) must be submitted to Compliance for review and approval prior to use unless provided by an already-approved vendor that created the tool. Vendors must be cleared with Compliance prior to using tools provided by them.**

10.15.1 Disclosures

Disclosures are required when using investment analysis tools. Investment analysis tools (including mention in written reports indicating the results generated by such tool and related retail communications) may be used if the tool, written report, or related retail communication:

- describes the criteria and methodology used (including the tool's limitations and key assumptions);
- explains that results may vary with each use and over time;
- if applicable, describes the universe of investments considered, explains how the tool determines which securities to select, and states that other investments not considered may have characteristics similar or superior to those analyzed (*must indicate whether the tool favors certain securities within the universe of securities considered based on Firm revenue from sales of the securities or understandings between CEI and the entity that created the tool and whether the tool is limited to searching, analyzing or in any other way favoring securities in which CEI makes a market, serves as underwriter, or has any other direct or indirect interest*); and
- displays the following additional disclosure: "IMPORTANT: The projections or other information generated by (*name of investment analysis tool*) regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results and are not guarantees of future results."

Disclosures must be clear and prominent and in written (including electronic) narrative form. Refer to FINRA Rule 2214.06 for exceptions to requirements for incidental references to tools in retail communications. Users may not imply that FINRA endorses or approves the use of any tool or any recommendation based on the tool.

10.15.2 Filing Requirements

Within 10 business days of first use, CEI must:

- provide FINRA's Advertising Regulation Department access to the investment analysis tool; and
- file with FINRA any template for written reports produced by, or retail communications concerning, the tool.

A tool offered exclusively to institutional investors [FINRA Rule 2210(a)(4)] is not subject to the post-use access and filing requirement if the communication relating to or produced by the tool meet the criteria for an "institutional communication" [FINRA Rule 2210(a)(3)]. If the tool or any related report will be used with a retail investor [FINRA Rule 2210(a)(6)] (such as an employee benefit plan participant or retail customer), the tool is subject to the filing and access requirements.

10.16 Complaints

[FINRA Rule 3110(b)(5), 4513 and 4530]

Responsibility	<ul style="list-style-type: none"> • Compliance/Legal • Branch Manager/Supervisor
Resources	<ul style="list-style-type: none"> • Customers' complaints (written or electronic) • FINRA reports (Report Center, Risk Monitoring Reports): <ul style="list-style-type: none"> ○ FINRA Sales Practice Complaint Report ○ FINRA Customer Complaint Report
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Branch Manager/Supervisor: <ul style="list-style-type: none"> ○ Resolve complaints of an operational nature such as late dividends, delayed delivery of stock, <i>etc.</i> If written, forward a copy to Compliance with description of resolution ○ Refer all other complaints (mishandling of account by RR, improper transactions, churning, <i>etc.</i>) to Compliance ○ In either case, complete a Customer Complaint Report form and submit with any relevant documentation to Compliance • Compliance: <ul style="list-style-type: none"> ○ Send initial acknowledgment of receipt of written complaint unless the branch has responded and acknowledged in writing ○ Gather needed information and investigate the complaint when needed ○ Provide a response and resolution to the customer with a copy to the RR and RR's supervisor if needed ○ If necessary, amend the RR's U4 (or, in the case of a terminated RR, amend Form U5) ○ File quarterly electronic complaint report with FINRA ○ Maintain central record of complaints ○ For formal civil actions (lawsuits, arbitrations), refer the matter to Coastal Equities, Inc.'s counsel for response ○ Review FINRA reports for trends in complaints
Record	<ul style="list-style-type: none"> • Copies of written complaints and related correspondence (including acknowledgment of receipt of complaint and resolution) are retained in: <ul style="list-style-type: none"> ○ Branch file for complaints (unless Coastal Equities, Inc. makes complaints promptly available to FINRA upon request at the office location)

	<ul style="list-style-type: none"> ○ Compliance central file of Coastal Equities, Inc.'s complaints (retention for 4 years) ● <i>Note:</i> options complaints are retained in separate files both by branches (where records are maintained at branches) and by Compliance ● Central complaint log (MSRB requires electronic format under Rule G-8) ● Record of electronic filings ● Records of updates to Form U4 or U5 ● Reviewed FINRA reports ● FINRA record retention: 3 years with 2 years in a readily-accessible location (Rule 17a-4) ● MSRB record retention: 6 years with 2 years in a readily-accessible location (MSRB Rule G-8)
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10.16.1 Complaint Defined

"Complaint" is defined as a "written grievance". With respect to a person, other than a broker or dealer, with whom the member has engaged in securities activities, the member must report any written grievance by such person involving the member or a person associated with the member pursuant to FINRA Rule 4530. (See below) Notwithstanding anything herein to the contrary, the definition of "Complaint" pursuant to this section shall not be interpreted or construed in such fashion as to expand its definition beyond the scope of its definition as set forth throughout FINRA Rules.

10.16.2 Handling of Customer Complaints

When a written complaint is received, it must be forwarded immediately to Compliance for follow-up.

Oral complaints may be resolved by the designated supervisor if the nature of the complaint is operational such as late check, late dividend, or another type of nominal problem. Oral complaints alleging mishandling of the customer's account (unauthorized trading, improper investments, *etc.*) should be brought to the attention of Compliance for review and resolution.

RRs should not respond to written complaints unless directed to do so by Compliance.

10.16.3 Oral Complaints

Oral complaints should be reported immediately to the designated supervisor for sales practice issues, or to Operations for operational issues. Examples of sales practice issues include complaints regarding losses, improper trades, and other complaints involving the quality of investments or wrongdoing by the RR or CEI. Examples of operational issues include late dividend checks, errors on monthly statements, *etc.* RRs should not make independent decisions regarding whether to report complaints; all oral complaints should be reported either to the designated supervisor or Operations.

10.16.4 Complaints Received by Clearing Firm

As required under SRO rules, whenever CEI's clearing firm receives a customer complaint, the clearing firm will:

- Provide a copy of the complaint to CEI's compliance officer.
- Provide a copy to CEI's designated examining authority (DEA).

- Notify the customer directly that their complaint has been forwarded to CEI for response and to the DEA.

When received by CEI, the complaint will be handled in the same manner as other complaints received directly by CEI.

10.16.5 Records of Complaints

Compliance will maintain a central record of all customer complaints including the following :

- Complainant's name and address
- Account number or municipal advisory number or code, if any
- Date the complaint was received
- Name(s) of employee(s) identified in the complaint
- Description of the nature of the complaint including the date(s) of activity that resulted in the complaint
- Disposition of the complaint

10.16.5.1 Office Records of Complaints

Each office of supervisory jurisdiction (OSJ) will maintain a separate file of all written customer complaints that relate to that office (including complaints that relate to activities supervised from that office) and action taken by CEI, if any, or a separate record of complaints and a clear reference to the office files that contain correspondence regarding complaints. Alternatively, CEI may make complaints promptly available at that office, upon request of FINRA.

10.16.6 Reporting of Customer Complaints

[FINRA Rule 4530]

Responsibility	<ul style="list-style-type: none"> • Chief Compliance Officer
Resources	<ul style="list-style-type: none"> • Complaints received from customers or referred by RRs, supervisors, or others • FINRA Disclosure Timeliness Report Card
Frequency	<ul style="list-style-type: none"> • Statistical Complaint Report: Quarterly • Form BD, U4s, and U5s (if applicable): Promptly after receipt of complaint
Action	<ul style="list-style-type: none"> • Identify reportable complaints and other reportable events • Report to FINRA the events specified in FINRA Rule 4530 within 30 calendar days of knowledge of the event • File electronically the quarterly statistical report by the 15th of the month following the calendar quarter
Record	<ul style="list-style-type: none"> • Quarterly complaint reports are maintained in a file for the reports • Copies of events reported

CEI will file a quarterly statistical report of complaints with FINRA. Complaints reportable in CEI's Form BD and/or an RR's Form U4 (or an amendment to Form U5, if the RR is terminated) will be promptly forwarded to FINRA.

10.17 Customer Privacy Policies and Procedures

[Gramm-Leach-Bliley Act Sections 501-503; SEC Regulation S-AM and S-P; Evolution of a Prototype Financial Privacy Notice: <http://www.ftc.gov/privacy/privacyinitiatives/ftcfinalreport060228.pdf>; FINRA web site Customer Information Protection: <http://www.finra.org/industry/customer-information-protection>; Fair Credit Reporting Act; SEC Risk Alert on Regulation S-P: <https://www.sec.gov/files/OCIE%20Risk%20Alert%20-%20Regulation%20S-P.pdf>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • CEI's Privacy Policy • Customer opt-out requests (if applicable)
Frequency	<ul style="list-style-type: none"> • When accounts are opened - provide copy of Privacy Policy • Annually - send notice of Privacy Policy to all customers • As determined by the designated supervisor: training for employees • As necessary - establish procedures for protecting customer information and ensuring information is only shared when it is allowed • As necessary - when new technologies are adopted
Action	<ul style="list-style-type: none"> • Send annual notice to customers • Code accounts for customers opting out (if applicable) • If "eligibility information" will be received from affiliates, determine that Regulation S-AM requirements are satisfied • Test internal computer systems periodically • Ensure agreements with third parties receiving customer information reflect the third party firm's privacy policies and include a confidentiality agreement • Include maintaining confidentiality of customer information in employee training • When new technologies involving customer information are adopted: <ul style="list-style-type: none"> ○ Contact CEI's chief legal officer to: <ul style="list-style-type: none"> ▪ Determine whether appropriate technological precautions have been taken to protect customer information ▪ Determine whether existing testing/audits will include the new technology and, if not, adjust testing program ○ Review existing policies and procedures to determine if changes/additions are required ○ Determine whether added training of employees is necessary and implement, if required
Record	<ul style="list-style-type: none"> • Current Privacy Policy • Customer opt-out requests (if applicable) • Record of annually providing notice to all customers • Determination that Regulation S-AM requirements are satisfied, if information from affiliates will be used for marketing purposes • Copies of signed agreements with third parties receiving customer information • Records of periodic privacy audits or other reviews conducted of CEI's computer system that retains customer information

	<ul style="list-style-type: none"> • Records of reviews of outsourced services involving the privacy of customer information (see the section <i>Outsourcing</i> in the chapter <i>FINANCIAL AND OPERATIONS PROCEDURES</i>) • Records of review of new technology involving customer information
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10.17.1 Introduction

CEI has adopted a Privacy Policy which is provided to customers at the time a new account is opened. Notice is also sent to all customers on an annual basis. The Privacy Policy explains CEI's policies regarding safeguarding of customer information and records and whether CEI shares information with outside parties. CEI also publishes its Privacy Policy on its web site.

SEC Regulation S-P ("Privacy Of Consumer Financial Information") applies only to accounts for individuals (*i.e.*, institutional accounts are not affected) and differentiates between "customers," where CEI has an established relationship with the individual, and "consumers," where there is no pre-established relationship. For purposes of this section, any individual from whom information is obtained (and their legal representative acting on their behalf) to open an account or to obtain services or products from CEI is considered a "customer." The term "consumer" will be considered synonymous with "customer" for purposes of this section.

The Privacy Policy applies to all individual customers of CEI, whether U.S. residents or foreign residents.

10.17.2 "Public" vs. "Nonpublic" Personal Information About Customers

Generally, information provided to CEI by a customer or potential customer in the normal course of CEI offering a product or service is considered "nonpublic personal information." Identifying whether information is "public" or "nonpublic" is important as to CEI's obligations if CEI shares information with nonaffiliated third parties. Public information is information that CEI reasonably believes may be obtained from three sources:

- federal state or local government records;
- widely distributed media; or,
- disclosures to the general public that are required to be made by federal, state, or local law.

Nonpublic personal information also includes any list, description, or other grouping of customers (and publicly available information about them) that is derived from financial information that is not publicly available.

10.17.3 Sharing Nonpublic Financial Information

In the normal course of business, CEI may share customer nonpublic financial information with service providers such as clearing firms or service bureaus. Agreements with such third parties include assurances regarding the protection of customer records and information. Information sharing with affiliated companies may also occur, and if applicable, is disclosed in CEI's Privacy Policy.

CEI does not share customer nonpublic financial information with non-affiliated companies or non-exempt service providers.

10.17.4 Customer Notification

[12 CFR Federal Reserve System Regulation P; Federal Reserve Privacy of Consumer Financial Information (Regulation P): <http://www.federalreserve.gov/boarddocs/supmanual/cch/consumer.pdf>; Gramm-Leach-Bliley Act Title V Section 503]

CEI will provide notice to customers about CEI's Privacy Policy. The notice is provided as follows:

- At the time an account is opened.
- On CEI's web site.
- Annually, in writing, unless CEI is not required to provide opt-out, as described in the next section.

10.17.4.1 Exception to Annual Notice

If CEI does not share customer nonpublic financial information that triggers the opt-out requirement, CEI will only post the Privacy Policy on its web site in an accessible and conspicuous way. The following conditions apply:

- The content of the notice most recently provided has not changed.
- CEI has another channel for the opt-out disclosure required under the Fair Credit Reporting Act, and CEI uses the Consumer Financial Protection Bureau (CFPB) model privacy notice.
- Customers must be notified in other required notices where to find the online notice; that the notice has not changed; and that the notice will be promptly mailed upon request by calling a telephone number dedicated to that purpose.

10.17.5 Affiliate Marketing

[SEC Regulation S-AM; SEC Small Entity Compliance Guide regarding Regulation S-AM:

<http://www.sec.gov/divisions/marketreg/tmcompliance/34-60423-secg.htm>; Fair Credit Reporting Act Section 624]

Regulation S-AM limits use of certain information received from CEI's affiliates to solicit a consumer for marketing purposes. Consumers may block the use of certain financial information by affiliates of the person the consumer does business with. CEI may use "eligibility information" (*i.e.*, certain financial information such as information regarding the consumer's transactions or experience with the affiliate) if:

- the potential market use of the information has been clearly, conspicuously, and concisely disclosed to the consumer;
- the consumer has been provided with reasonable opportunity to opt out; and
- the consumer has not opted out.

CEI will only use information from affiliates if the above requirements are satisfied. Opt-out notices under Regulation S-AM may be included with Regulation S-P opt-out notices described above.

10.18 Prohibition Against Payments Involving Publications to Influence Market Prices

[FINRA Rule 5230]

Payments of anything of value, directly or indirectly, are prohibited for the purpose of influencing or rewarding someone in connection with the publication or circulation of information in any electronic or other public media for the purpose of influencing the market price of the subject security. This includes any investment service or similar publication; web sites; newspapers, magazines, or other periodicals; radio; or television program. The prohibition does not apply to clearly-identified paid advertising; a communication that discloses the amount and receipt of compensation; or a research report as defined under FINRA rules.

10.19 Calling (Telemarketing) and Fax Restrictions

[FINRA Rule 3230; NASDAQ Rule 2212; NYSE Rule 3230; MSRB Rule G-39; Telephone Consumer Protection Act of 1991; Telemarketing and Consumer Fraud and Abuse Prevention Act of 1994; Junk Fax Prevention Act of 2005; FINRA FAQs on Telemarketing: https://www.finra.org/rules-guidance/guidance/faqs/finra-rule-3230?utm_source=MM&utm_medium=email&utm_campaign=O%5FWeekly%5FUpdate%5F120.419%5FFINAL]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Requests to conduct telemarketing • Third parties contracted for telemarketing • Do not call requests • Federal/state do not call lists
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • For third party telemarketers, confirm compliance with registration requirements and confirm their ability to comply with requirements • Establish and maintain internal do-not-call list • Obtain federal/state do not call lists and make them available to RRs or establish an internal system for automatically checking outgoing calls against lists • For abandoned calls, establish and maintain a method of ensuring compliance with requirements • Train RRs regarding telemarketing prohibitions, use of billing information (if applicable), do-not-call lists, etc.
Record	<ul style="list-style-type: none"> • Third party telemarketer compliance reviews • Internal do-not-call list • Records of technology (if employed) to block calls to restricted numbers • Recorded phone calls where billing information is submitted • Records of compliance with abandoned call requirements • Records of training including training materials, who attended when conducted

This section describes restrictions on telemarketing calls under Federal and FINRA rules and regulations. There may be additional regulations such as state laws and rules. Compliance will communicate any such requirements to RRs.

10.19.1 Introduction

CEI and its employees are subject to restrictions that govern telephone solicitations as well as unsolicited facsimile advertisements to residences.

Key points include the following:

- Telephone and facsimile solicitations are allowed when the target individual has an "established business relationship" with CEI.
- Calls may not be made to individuals included on a Do Not Call List which includes lists maintained by the federal government, state governments, and CEI.
- "Telephone solicitation" is defined as a telephone call initiated for the purposes of encouraging the purchase of or investment in property, goods, or services. The definition exempts calls made by tax-exempt nonprofit organizations.

- "Established business relationship" includes someone who has had a transaction or security position, money balance, or account activity within 18 months preceding the call or fax or has contacted CEI to inquire about a product or service within 3 months preceding the call or fax.

5.19.2 Telephone Calls

General requirements include the following:

- The caller must provide the called party, the name of the caller; the name of the person or entity on whose behalf the call is being made; a telephone number or address at which the caller may be contacted; and disclosure that the purpose of the call is to solicit the purchase of securities or related services.
- Telephone solicitations to residences may not be made before 8:00 a.m. or after 9:00 p.m. in the time zone of the called party's location.
- A "Do Not Call" list must be established that includes the names of individuals who have specifically requested they not be called for solicitations.
- Prerecorded calls to residences are prohibited unless the person has consented in writing to receive such calls and can opt out of future calls and CEI complies with the requirements of FINRA Rule 3230(k).
- The telephone number of the sender may not be a 900 number or other number where the called party will incur a charge for notifying the sender of a desire not to be called. Consumers may not be charged to protect their privacy.
- Caller identification information must be transmitted; blocking caller identification information is prohibited.
- Outbound telemarketing calls may not be "abandoned" which means a person answers the call and the call is not connected to someone at CEI within two seconds of the completed greeting.

The restrictions do not apply to calls to customers for whom CEI carries accounts and where the account has had some activity in the last 18 months (trading, credit of interest earned, *etc.*). Calls to other broker-dealers also are not covered by these restrictions.

10.19.3 Wireless Communications

The rule also applies to outbound telephone calls to wireless telephone numbers.

10.19.4 Outsourcing Telemarketing

At this time, CEI does not engage the services of third-party telemarketers. Compliance must review the use of third-party telemarketers before they are engaged. CEI is responsible for compliance with telemarketing requirements even if the function is outsourced to a third party. Outsource firms may require registration or licensing to conduct telemarketing for CEI.

10.19.5 Unencrypted Consumer Account Numbers

CEI and its associated persons are prohibited from disclosing or receiving, for consideration, unencrypted consumer account numbers for use in telemarketing. "Unencrypted" is defined as not only complete, visible account numbers, whether provided in lists or singly, but also encrypted information with a key to its decryption.

10.19.6 Abandoned Calls

CEI and its associated persons are prohibited from abandoning any outbound telemarketing call. The abandoned calls prohibition is subject to a "safe harbor" which provides that a firm or its associated person will not be liable for violating the FINRA rule if:

1. CEI or its associated person employs technology that ensures abandonment of no more than three percent of all calls answered by a person, measured over the duration of a single calling campaign, if less than 30 days, or separately over each successive 30-day period or portion thereof that the campaign continues;
2. CEI or its associated person, for each telemarketing call placed, allows the telephone to ring for at least 15 seconds or four rings before disconnecting an unanswered call;
3. whenever an associated person is not available to speak with the person answering the telemarketing call within two seconds after the person's completed greeting, CEI or its associated person promptly plays a recorded message stating the name and telephone number of CEI or associated person on whose behalf the call was placed; and
4. CEI retains records establishing compliance with the "safe harbor."

10.19.7 Other Prohibited Activities

The following are prohibited when calling customers or prospective customers:

- threats, intimidation, and the use of profane or obscene language
- calling a person repeatedly with intent to annoy, abuse, or harass the called party
- using an alias

10.19.8 Do Not Call Lists

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • National Do-Not-Call Registry • State do not call lists • Internal do not call list • Other vendor lists
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Add names to CEI's do-not-call list within 30 days of receiving the request • Provide access to do not call lists • Obtain updated national do-not-call registry every 30 days • Include telephone solicitation restrictions in RR education programs
Record	<ul style="list-style-type: none"> • The internal do not call list is maintained by Compliance • Federal and state lists are maintained by the vendor (if a vendor is used) or by Compliance

Phone solicitations may not be made to phone numbers that are included in federal, state, or CEI's do not call list. **Because fines may be substantial for each call that violates a restriction, it is important to comply with these requirements.**

It is permissible to contact someone with whom CEI has an "established business relationship" (described below); the person called has given express written permission to call outside the applicable time; or the person called is a broker or dealer.

If someone has asked to be included on CEI's do not call list, that person may not be called regardless of whether they are a current customer or have an established business relationship. Individual states may impose stricter requirements limiting contact with persons on that state's do not call list.

- An automated system [currently GRYPHON] will screen outgoing calls against do-not-call lists and block prohibited calls.

10.19.9 National Do-Not-Call Registry

The Federal Trade Commission (FTC) and Federal Communications Commission (FCC) established requirements for sellers and telemarketers to participate in a National Do-Not-Call Registry of phone numbers that do not accept phone solicitations. CEI and its employees must avoid solicitation calls to any number on the list unless the person has an "established business relationship" with CEI. The list used must be no older than 31 days prior to the date any call is made.

In general, national do-not-call requirements apply to residential phone numbers. In addition, the FCC includes wireless subscribers in the national registry, presuming these are residential subscribers.

10.19.10 State Restrictions

Certain states have enacted restrictions on telephone solicitations to residences. Florida, for example, has a restrictive policy whereby individuals may ask to be included on a state-wide "do not call" list. It is the telephone solicitor's obligation to be aware of any individuals who are included on that list. Contact Compliance if you have questions regarding state restrictions.

10.19.11 Internal Do Not Call List

Employees are responsible for reporting to Compliance the names of individuals who do not wish to be called. Compliance maintains a Do Not Call List that is periodically distributed to employees with an explanation of CEI's telemarketing policy. It is the RR's responsibility to ensure outgoing calls are not made to anyone appearing on CEI's Do Not Call List.

10.19.12 Facsimile Transmissions

General requirements that apply to faxes include:

- A facsimile transmission must include, in a margin at the top or bottom of each transmitted page or on the first page of the transmission, the date and time it is sent and the identification of the business, other entity, or individual sending the message and the telephone number of the sending machine or of the sender.
- Unsolicited faxes may only be sent to individuals who have an established business relationship with CEI.

10.19.13 Established Business Relationship

Calls and faxes to the following are not subject to do-not-call restrictions:

- a person having made a financial transaction or having a security position, a money balance, or account activity with CEI (or its clearing firm if a clearing firm relationship exists) within 18 months immediately preceding a call or fax; or
- CEI is the "broker-dealer of record" (identified on the customer's account application for accounts held directly at a mutual fund or variable insurance product issuer) for the account of the person within the previous 18 months immediately preceding the date of the call or fax; or
- the person has contacted CEI to inquire about a product or service offered by CEI within the previous 3 months immediately preceding the call or fax.

10.20 Public Appearances

[FINRA Rule 2210(f)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests for public appearances • Outlines of subjects to be included • Charts or other visual aids to be used in conjunction with public speaking • Written materials to be provided to attendees
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Refer requests for contact with media to Compliance • Review outlines of information to be presented and revise, as needed • For product-specific presentations, request review by original product due diligence reviewer, if necessary • For mutual fund presentations, materials provided by wholesalers also require the approval of Compliance • Option presentations require the review and approval of the ROP and Compliance • Review charts and written materials to be presented • As a best practice, attend sales seminars periodically to confirm compliance with requirements • Ensure presentations involving securities being offered by prospectus include provision of prospectuses to attendees • Include public appearance requirements in training or provide training prior to appearances
Record	<ul style="list-style-type: none"> • Maintain approved outline, samples of visual aids, and written materials in a "Public Appearances" file • Signed and dated Public Appearance Request form • Obtain and maintain in the Public Appearances file a list of attendees who received prospectuses (if applicable) • The ROP and Compliance maintain a file of all approved public appearances that includes options • Compliance maintains records of approved wholesaler materials • Records of training including who participated, subjects covered

The following sections outline requirements when RRs engage in public appearances.

10.20.1 General Guidelines

The general concepts of truthfulness, good taste, and a fair presentation apply to employees engaging in public appearances. Public appearances include participation in a seminar, forum (including an interactive electronic forum), radio or television interview, or other public appearance or public speaking activity.

- The general standards explained earlier in this chapter apply to public appearances.
- If a security is recommended in the public appearance, the RR must have a reasonable basis for the recommendation **and** must disclose:
 - If the RR has a financial interest in the securities of the issuer; the nature of the interest (including derivatives such as options, warrants, *etc.*) and any material conflict of interest of the RR or CEI known at the time of the appearance. (*This disclosure does not apply to investment company securities or variable insurance products.*)
- These requirements do not apply to public appearances by research analysts where the appearance complies with the requirements of FINRA Rule 2711.

10.20.2 Seminar Approval

Whether or not the RR is presenting or speaking, all materials to be presented or distributed at the seminar, including power point presentations and all advertising concerning the seminar must be submitted with the *Public Appearance/Seminar/Luncheon Request* form at least four (4) weeks prior to the seminar to the RR's supervisor, and then to Compliance for approval.

Materials to be used at any seminar by a third party product sponsor to which any CEI registered representative wants to invite CEI customers should also be accompanied with evidence that the presentation material has been filed with the Advertising Review Department and the issuer has received a letter from the Department stating that it appears to be consistent with applicable standards. In that case, CEI permits such materials to be used at an event involving CEI customers subject to the representatives' agreement not to materially alter it or to use it in a manner inconsistent with any conditions of the Department's letter. If the material has not been filed with the Department or does not have the accompanying letter, the designated supervisor will conduct an independent review for compliance with Rule 2210, or decline approval of the materials.

10.20.3 Public Speaking Approval

Prior to engaging in public speaking, the RR should prepare an outline and submit a *Public Appearance/Seminar/Luncheon Request* form for approval by the RR's supervisor and Compliance at least four (4) weeks prior to the event to ensure timely review. The Request should also include a copy of any proposed advertising, power point presentations, and handouts to be used/distributed at the event for pre-approval by CEI. A power point presentation may suffice as an 'outline' as required by this section.

10.20.4 Radio, TV, and Other Extemporaneous Presentations

The general standards of communications with the public apply to all public appearances whether scripted or not. The following should be considered when participating in radio, TV, or other non-scripted public appearances. Also refer to the chapter *GENERAL EMPLOYEE POLICIES* and the section *Media Contact Is Limited To Certain Authorized Persons* that explains restrictions on dealing with the media. Most employees are restricted from such contact except with the specific approval of Compliance.

- Specific recommendations of securities must be avoided unless approved by Compliance or the speaker is authorized under CEI's "Media Contact" policy. If a recommendation is made, the speaker is required to disclose material information such as when the registered representative has a financial interest in the stock. The current price and any special risks associated with the security also must be disclosed.
- The firm's name must be clearly disclosed in conjunction with any securities or services offered.
- The speaker cannot assume a specific level of audience knowledge, experience or suitability. High risk securities may not be appropriate for discussion in a broadcast format available to any listener.
- Media presentations should be clear and understandable. Avoid overly complex messages and technical terminology which may not be understood by the general audience.
- Include products only where the speaker is licensed to sell the product.

For RRs who are approved to engage in radio, TV, or other extemporaneous public speaking, Compliance is responsible for periodically reviewing the presentations, either on tape or concurrent with broadcast, contacting the RR if unacceptable material is included, and making a record of the review and any action taken.

10.20.5 Securities Sold by Prospectus

When presentations include discussion of securities sold by prospectus (mutual funds, variable annuities, *etc.*), participants should receive a copy of the prospectus. A list of participants should be prepared and an indication included that prospectuses were provided.

10.20.6 Options

Any presentation that includes a discussion of options must be approved by Compliance prior to the presentation. Compliance will maintain a written record of any such approved presentations including an outline or description of the presentation.

10.20.7 Collateralized Mortgage Obligations (CMOs)

Because of the potential complexity of some CMO investments, review by the designated supervisor of the CMO area is required prior to public speaking on these investments. The chapter *COLLATERALIZED MORTGAGE OBLIGATIONS (CMOs)* should be reviewed for further information.

10.20.8 Mutual Funds

Refer to the section *Seminars and Other Public Presentations* in the chapter *MUTUAL FUNDS* for specifics regarding mutual fund seminars.

10.21 Cold Callers

[FINRA Notice to Members 95-54]

The Company permits its associated persons to contact persons at their residential or wireless phone numbers only if they have an established business relationship or the calls are return phone calls. NO telemarketing (telephone solicitations, also called cold calling) is permitted, except where prior written approval is obtained from the CEO. At present, the branch located at 14 Wall Street has been granted such approval subject to the procedures below. During ongoing reviews of business activity, all designated Principals are required to take note of violations of this policy and must take action to prohibit further non-compliance. Instances of repeated non-compliance must be brought to the attention of the CCO for investigation and possible disciplinary action.

“Person,” when used to indicate the call recipient, includes any individual, group, unincorporated association, limited or general partnership, corporation, or other business entity.

The following guidelines apply to **unregistered** individuals who engage in cold calling at the 14 Wall Street Branch.

10.21.1 Cold Caller Requirements

RRs are responsible for reporting to the branch supervisor and/or the Home Office the names of individuals who do not wish to be called. The branch subscribes to a service that maintains a National Do Not Call List and blocks outbound calls to any number on the list. It is the RR's responsibility to ensure outgoing calls are not made to anyone appearing on the Do Not Call List. RRs are responsible for reporting to the branch supervisor and/or Home Office the names of individuals who do not wish to be called. The branch adds any such names and numbers to the screening service. It is the RR's responsibility to ensure outgoing calls are not made to anyone appearing on the Company's Do Not Call List. Cold callers are supervised by the designated supervisors of their respective departments.

Cold callers will be provided with a copy of CEI's policy regarding cold callers and the calling restrictions policy as well as CEI's Do Not Call list. Cold callers will be asked to acknowledge, in writing, receipt of the policies and the list.

10.21.2 Permissible Cold Caller Activities

Unregistered cold callers are restricted to the following:

- Asking whether a prospect would like to speak to an RR
- Asking whether a prospect would like to receive information about investments

When making a call, the cold caller must identify himself or herself as well as CEI and the purpose of the call.

Prior to making calls, the caller must check CEI's Do Not Call List.

10.21.3 Prohibited Cold Caller Activities

Unregistered individuals may NOT:

- Solicit prospects to open accounts
- Discuss general or specific products or services
- Pre-qualify prospects by inquiring about financial status or investment objectives
- Use an alias when identifying themselves
- Contact persons included on CEI's Do Not Call List

10.21.4 Telemarketing Restrictions

Cold caller activities are subject to the Telephone Consumer Protection Act of 1991 issued by the Federal Communications Commission, as outlined in the section *Calling Restrictions* of this manual.

10.22 Electronic Communications

[FINRA Rule 3110(b)(4) and 3310.06]

The Electronic Communications Policy for all employees is included in the chapter *GENERAL EMPLOYEE POLICIES* and the *Cybersecurity and Personal Information Protection Policy* manual. This section provides additional details of these requirements and concerning oversight of electronic communications.

10.22.1 Education and Training

Employees and access persons are required to acknowledge receipt of and compliance with the Electronic Communications Policy.

- Before employees are permitted to use CEI-sponsored systems or devices, employees are required to read and agree to the Electronic Communications Policy. The Policy is distributed to all new employees who are required to acknowledge receipt in writing.
- Current employees acknowledge their understanding and agreement with the Policy in CEI's annual certification.
- The Firm Element continuing education program and/or annual compliance meeting for registered employees will periodically include training regarding CEI's Electronic Communications Policy.

10.22.2 Commercial E-Mail Procedures

[CAN-SPAM Act of 2003]

E-mails that are "commercial electronic mail" are subject to the CAN-SPAM Act. Commercial electronic mail includes, under federal law, any electronic mail message primarily for the purpose of sending a commercial advertisement or promotion of a commercial product or service. It does not include electronic mail relating to transactions or where there is a relationship between the sender and the recipient. The Act applies to "persons" who include individuals, groups, unincorporated associations, limited or general partnerships, corporations, or other business entities.

CEI's e-mail will comply with the following federal requirements in the event it distributes "commercial electronic mail".

- All e-mails will include clear identification of CEI, its address and the sender's e-mail address.
- E-mails will be sent using CEI's computers or other computers specifically authorized for transmission of CEI e-mails.
- Recipients will be given the opportunity to "opt-out" from receiving future commercial electronic mail. The recipient cannot, as a condition of honoring an opt-out request, be charged a fee, be required to provide information other than the recipient's e-mail address and opt-out preferences, and be required to take any steps other than sending a reply e-mail or visiting a single page on an Internet website. Opt-out requests will be effected within 10 business days of the request, as required by the Act.
- Where CEI e-mails include other marketers (for example, a mutual fund management company), CEI will be considered the "sender" responsible for compliance with the Act unless specifically agreed in advance that another entity included in the e-mail will act as "sender."
- CEI will not use "address harvesting" or "dictionary attacks" to obtain e-mail addresses from the Internet.

10.22.3 Review of Electronic Communications

This section outlines procedures for reviewing electronic communications.

10.22.3.1 Methods of Review

All electronic communications are subject to review. Review is conducted on a risk-based system controlled by Compliance.

A designated supervisor is assigned one or more Registered Representatives and associated branch personnel in general. Approved email and social media accounts for those persons are also assigned to the designated supervisor for review. Those accounts are assigned to the supervisor's queue in Smarsh by Operations. The designated supervisor reviews his or her queue on a weekly basis. Exceptions to the weekly schedule may be made to accommodate sickness or vacations by the VP of Supervision or Compliance.

Review includes:

- Lexicon-based program that identifies words or phrases in communications selected for review; or
- Special or Heightened supervision may impose an additional review of all or sampled communications depending on criteria determined by Compliance on a case-by-case basis.

Lexicon:

Compliance performs an annual review of the Lexicon and adjusts the lexicon as needed to ensure that the firm has a reasonable system in place to capture potentially problematic email such as customer complaints, undisclosed outside business activity, and misrepresentations to customers, among other things.

Supervisors review for the following issues, among other things:

- Evidence of outside business activity or private securities transactions not reported to the firm
- Complaints
- Advertising not previously approved
- Communications regarding errors or account designation changes in orders
- Business email 'cc'd' to a personal email address and vice-versa
- Blank forms sent to clients for signature

Any action taken should be noted in the Notes box in Smarsh. Violative conduct should be escalated to Compliance through Smarsh, and an email should be sent to compliance giving notice of the violation or complaint. The supervisor is responsible for ensuring complaints are processed in accord with the COMPLAINTS procedures within this manual.

10.22.3.1.1 Delegation of Review

The designated supervisor is responsible for reviewing electronic communications and taking necessary actions. The review may be delegated to a qualified reviewer; "qualified" means the individual has been trained in what to review and what items to refer to the supervisor and/or Compliance. Though reviews are delegated, the supervisor is ultimately responsible for compliance with review requirements. The delegated reviewer will refer the following communications:

- Questionable language to the designated supervisor or Compliance
- Objectionable language or content (profanity, *etc.*) to the supervisor or Compliance
- Complaints to the designated supervisor **and** Compliance
- Advertising not previously approved to Compliance
- Communications regarding errors or account designation changes in orders to the supervisor

10.22.3.2 Communications Review Before or After Sending

The following communications require approval by a qualified supervisor **prior to** sending. Other types of communication are subject to post-sending review.

- Advertising (Compliance approval required)
- Communications defined as "research" (see the section Outgoing Communications for further information)
- Form letters (approval of initial form required; subsequent communications may be sent without prior approval if there is no change in previously-approved content)
- Retail communications (communications sent to more than 25 retail investors)

The Firm has enterprise access to Marketing Pro, Emerald, and FMG Suite, each of which is an electronic content provider for financial industry firms. Registered Representatives may engage one or more of these vendors for those purposes. In such case, Compliance may review and approve requested materials or pre-approve materials within the software. In such cases, neither the advertising/retail communication request form nor supervisory review and approval is needed. Evidence of compliance review and approval is maintained in the applicable system. Registered Representatives cannot distribute such materials unless and until Compliance has approved the material.

10.22.3.3 Review of Institutional Customer Communications

Incoming and outgoing customer electronic communications are reviewed, and complaints are referred to Compliance. Like retail communications, supervisors review institutional communications by lexicon system through Smarsh.

10.22.4 Advertising

Electronic advertising is subject to pre-use review by Compliance. Refer to the section *Retail Communications* in this chapter.

10.22.5 Internet

This section outlines procedures for accessing communications systems on the web and posting information to the web, including a firm web site.

10.22.5.1 Social Media, Blogs, Web Sites And Other Electronic Communication Systems

[FINRA Regulatory Notice 17-18, 11-39 and 10-06]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Compliance
Resources	<ul style="list-style-type: none"> • Requests to participate in social networks, other systems • Postings on sites
Frequency	<ul style="list-style-type: none"> • Approval of participants - as required • Annually or as needed - review of sites
Action	<ul style="list-style-type: none"> • Compliance:

	<ul style="list-style-type: none"> ○ Review and approve media for RR participation particularly considering the ability to monitor and retain records of communications ○ Review requests to participate ○ Review an RR's proposed social media site in the form in which it will be launched, or review of existing site when new registrant is on-boarded ○ Approve or disapprove participation ○ Arrange training for approved participants if deemed necessary by CCO ○ When using unknown third-party media providers, perform due diligence including: <ul style="list-style-type: none"> ▪ The provider's reputation in the marketplace ▪ The third party's policies including: <ul style="list-style-type: none"> ▪ collection and handling of customer information ▪ the process and frequency by which the third party's policies may change ▪ what control CEI may have over the third party's policies or actions ● Designated supervisor: <ul style="list-style-type: none"> ○ Review media either: <ul style="list-style-type: none"> ▪ Using lexicon-based reviews; or ▪ Reviewing communications on a sampling basis ○ Review and approve/disapprove static postings ○ Remove inappropriate postings ○ Take corrective action where problems are noted including blocking a 3rd party from posting; disciplining an RR which may include added training, removal of approval for participation, other appropriate action
Record	<ul style="list-style-type: none"> ● RRs approved/disapproved for participation ● Training materials, who participated and when ● Certifications ● Templates, if available ● Approved static postings: using Smarsh portal, Emerald Portal, or print copy of landing page with initials and date ● Records of business communications and corrective action, if appropriate ● Review of media and any corrective action taken

The use of social media (Facebook, LinkedIn, Twitter, *etc.*), blogs, web sites, and other electronic forums (collectively referred to as "media" in this policy) for the purposes of advertising, soliciting business, or in any way communicating about Firm business is subject to the following requirements. "Social media" is a form of interactive online communication in which users can generate and share content through text, images, audio, and/or video. Social media is a dynamic and constantly evolving technology, therefore the definition is meant to be illustrative and not exhaustive.

10.22.5.1.1 Definitions

Static sites or postings: Information that is posted and does not change unless changed by the person or entity that posted the information. Static postings are considered "advertising" under regulatory rules and require **prior approval**.

Interactive sites or postings: Sites where there are spontaneous communications between parties. Considered "public appearances" by regulators requiring post-use approval.

10.22.5.1.2 Permitted Media

The use of specific media requires the approval of Compliance **prior to** access for business purposes. The proposed media must be able to provide access for monitoring and the ability to provide records of an RR's participation and communications. Regulatory rules require supervision and maintaining of records of use for business purposes.

10.22.5.1.3 Permitted Participation

Compliance must approve RRs **prior to** their participating in social media web sites. Approval will depend on the type of participation requested; CEI's ability to monitor participation and retain records of participation; and factors considered regarding the RR including demonstrable ability to comply with rules, regulations and Firm policy (this will include consideration of an RR's past disciplinary history and current compliance with firm policies and procedures).

10.22.5.1.4 Accuracy and Truthfulness

All electronic communications by CEI and its RRs must be accurate and truthful. They must not include misleading statements or claims and language must be fair and balanced.

10.22.5.1.5 Interactive Media

Where RRs are permitted to participate in interactive media, a record must be retained of all interactive "conversations" as part of CEI's records. These records will be reviewed by the designated supervisor in accordance with firm policy on review of electronic communications (either on a sampling basis or review of all communications).

10.22.5.1.6 Static Postings

Where an RR requests to make a static posting to media (such as a biography), a copy of the proposed posting must be provided to Compliance **prior to** posting along with the *Advertising/Retail Communication Submission Form*. If approved, any subsequent proposed changes to a static posting must be provided to Compliance for review and approval prior to posting. A record will be retained of postings and subsequent changes.

10.22.5.1.7 Use of Personal Communication Devices

Personal communication devices (Blackberrys, iPhones, etc.) may be used for business purposes for voice and voice mail communications. All other electronic communications on such devices are subject to the Firm's Cybersecurity and Personal Information Protection Policy and Electronic Communications Policy in this Manual.

10.22.5.1.8 Third Party Sites

Customers or other third parties may be permitted to post to CEI's site or other sites where RRs participate for business purposes. CEI is not required to supervise those postings unless CEI or an employee was involved in the preparation of the content or explicitly or implicitly endorses or approves the content. **RRs are prohibited from participating in or endorsing third-party postings.** CEI's site includes a disclaimer that third party posts do not reflect the views of CEI and have not been reviewed by CEI for completeness or accuracy.

Links to third party sites are prohibited if CEI or an employee knows or has reason to know it contains false or misleading content.

10.22.5.1.9 Prohibition Against Recommendations

RRs are prohibited from making specific recommendations in media. Postings must be only general in nature regarding the RR and CEI's services.

10.22.5.1.10 Complaints

CEI will treat any complaints posted by a customer of CEI on social media as a complaint subject to complaint procedures in this chapter.

10.22.5.1.11 Legal Liability

An employee is legally liable for anything he or she writes or presents online or through social media communications. Employees may be disciplined by CEI for commentary, content, or images that violate this policy including those that are defamatory, pornographic, proprietary, harassing, libelous, or that can create a hostile work environment. Employees can also be sued by co-workers, competitors, and any individual or company for posted comments/views.

10.22.5.2 Firm Web Site

[FINRA Rule 2210; FINRA Notice to Members 07-02; SIPC By-Laws Article 11 Section 4; SEC Guidance for public companies on the use of company web sites: <http://www.sec.gov/rules/interp/2008/34-58288.pdf>]

Responsibility	<ul style="list-style-type: none"> • Advertising Supervisor
Resources	<ul style="list-style-type: none"> • CEI's web site • Requests to include information
Frequency	<ul style="list-style-type: none"> • Approvals - as required • Annual review of the web site
Action	<ul style="list-style-type: none"> • Review proposed materials to be included on the web site and approve or disapprove <ul style="list-style-type: none"> ○ Determine whether filing with FINRA is required and make necessary filings • Review the web site to confirm that only previously approved materials are included • If SIPC is referenced on the site, provide a hyperlink to the SIPC web site • If FINRA is referenced on the site, provide a hyperlink to FINRA's home page • Contact supervisors of departments that have included unapproved materials and take corrective action • Corrective action may include changing or deleting the material and/or reminding the supervisor of the pre-use approval requirement
Record	<ul style="list-style-type: none"> • Approved materials and (if applicable) copies of FINRA filings • Notations regarding periodic reviews and corrective action taken

	<ul style="list-style-type: none"> Record of the appearance of the site over the past 3 years (including all changes)
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CEI has established a web site. Any information to be included on the web site requires the **prior approval** of Compliance.

If CEI's site refers to its membership with FINRA, a hyperlink to the FINRA internet home page will be included. If SIPC membership is included on the site, a hyperlink to SIPC's web site will be shown.

10.22.5.3 RR Web Sites

Responsibility	<ul style="list-style-type: none"> Advertising Supervisor
Resources	<ul style="list-style-type: none"> Prototype web site formats Proposals for sites Changes to sites
Frequency	<ul style="list-style-type: none"> As required - approval Annually - review sites
Action	<ul style="list-style-type: none"> Develop and update prototype sites Review proposed sites submitted by RRs Revise as needed and approve/disapprove proposals Review sites for compliance with Firm requirements Take corrective action if necessary which may include requiring revisions; limiting RRs whose sites fail to comply with pre-established requirements
Record	<ul style="list-style-type: none"> Proposals including revisions, approval, disapproval Record of annual review of approved sites and actions taken - evidence may include electronic notations in Smarsh or Emerald's CRM Record of the appearance of each RR web site over the past 3 years (including all changes)

R Rs are permitted to establish web sites under the following conditions:

- R Rs must obtain Compliance approval to publish a web site.
- Additions or changes to the site must receive the prior approval of Compliance.
- If FINRA or SIPC membership is included, the site will show hyperlinks to FINRA's internet home page and SIPC's web site.

10.22.5.4 Data Feeds

[FINRA Regulatory Notice 11-39]

Any third party data feeds tied to CEI's or an RR's web site must be reviewed by Compliance prior to use. Reviews will identify the proficiency of the data provider to feed accurate and timely information. Compliance will regularly review the data feeds for red flags indicating the data may not be accurate, and will take corrective action as necessary.

Compliance will advise the requestor whether the data provider is approved and will retain records of its review. For purposes of this section Coastal defines 'data feeds' to include data concerning customer data or personal information only.

10.22.5.5 Third-Party Postings

Advertising Supervisor must review and approve any requests to include third-party postings on CEI's web site prior to inclusion of such postings on the site. If third-party postings (including customer postings) are permitted, the following requirements will apply:

- A disclaimer will be included on the web site stating that such posts are not those of CEI; do not reflect the views of CEI; and CEI does not take responsibility for the content of such posts.
- Potential third-party posters must pre-register and will be screened by Compliance before being allowed to post content.
- The site is regularly reviewed and third-party posts will be monitored as part of that review to mitigate any perception that CEI is adopting any post.
- Usage guidelines will be provided to customers or other third parties permitted to post on firm-sponsored sites.
- Compliance may develop standard responses that RRs will be authorized to use in response to third-party postings on social media web sites.

Advertising Supervisor will retain records of registration and screening of third parties allowed to post.

10.22.6 Hyperlinks

[FINRA Interpretation Letter from Thomas M. Selman to the Investment Company Institute, November 11, 1997]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Proposed web site or other material that includes hyperlinks
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Confirm hyperlink conforms to requirements for inclusion
Record	<ul style="list-style-type: none"> • Web site or other material maintained in review file

When hyperlinks to third-party sites are included in CEI communications or on a CEI web site, it is important the hyperlink meets the following conditions to avoid liability for the content or regulatory filing of information included in the third-party site:

- A hyperlink may not be established to a site known (or there is reason to know) to contain false or misleading information.
- The hyperlink must be continuously available to investors who visit the site.
- CEI or its employees cannot have discretion to alter information on the third-party site.
- Investors have access to the hyperlinked site whether or not it contains material favorable to CEI.
- The linked site can be updated or changed by the third party, following which investors would still be able to use the hyperlink.

10.22.7 Prohibition Against Automatic Erasing/Deleting

[FINRA Regulatory Notice 11-39]

CEI and its employees are prohibited from sponsoring a social media site or using a communication device that includes technology which automatically erases or deletes content.

10.22.8 Policy Violations

Responsibility	<ul style="list-style-type: none">• Compliance
Resources	<ul style="list-style-type: none">• Records of communications
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Review the employee's file to determine if there have been prior violations• Notify employee and his/her supervisor• If appropriate action by the supervisor is not forthcoming, contact the supervisor's supervisor• Where violations are recurring, determine whether to audit the employee's computer files• Determine disciplinary action
Record	<ul style="list-style-type: none">• Records of violative communications and action taken

Employees who violate CEI's Electronic Communications Policy are subject to disciplinary action which may range from education, restricting electronic and/or Internet access, to suspension or termination depending on the nature and seriousness of the infraction. Compliance determines the appropriate action to be taken.

10.23 Identification of Sources

When using communications not prepared under the direct supervision of CEI, it is necessary to identify, on the communication, the person or entity that prepared the material. This includes research reports obtained from outside sources.

10.24 Consolidated Statements and Reports

Some RRs may desire to provide reports to their clients identifying all positions held by the client across multiple accounts, including subscription-way/direct business positions not shown on the firm's brokerage statements, i.e. a consolidated statement. The Firm considers any software application which aggregates client assets and permits manual entry of client accounts and assets, as well as manually created reports using Excel or Word for example, to fit within the meaning of 'consolidated report' for regulatory purposes.

1) Manually **Generated Reports**: Each summary or report, whether created in Excel, Word or other 'manually created' document, must be submitted to the designated supervisor for pre-approval by the financial professional. Reports may not be transmitted, published, or used in a client presentation without first obtaining approval. The report must be submitted to the designated supervisor securely by e-mail or Sharefile, along with copies of all

statements upon which the numerical data is based so that the supervisor may review the data for accuracy. The supervisor will evidence approval of the summary or report by stating 'Approved' in a return e-mail. Approval emails and the approved report with backup will be maintained in the Consolidated Reports supervision folder at the Home Office.

2) **Electronic Reports** (Envision, eMoney, Black Diamond, etc.): Financial Professionals must request Compliance approval prior to first use of aggregation software (other than Coastal Enterprise versions of such software) and identify the vendor(s) utilized for such services. If approved, the registered representative must submit a template report showing the cover page and logo of the branch, and the disclosure pages of the report to advertising@coastal-one.com. The advertising review principal will review and approve the template for use by the registered representative. Once approved, any material changes to the template must be submitted to the advertising principal for review and approval. A copy of the approved template will be maintained in the Consolidated Reports supervision folder at the Home Office.

Thereafter, if the registered representative desires to use a report in a presentation with a client, or to deliver to the client, the report must be maintained by the branch with appropriate backup for any assets manually entered by the registered representative. Backup is not required for assets entered by the client, or for which a direct feed to the custodian has been established.

Designated Supervisors will, on a quarterly basis, choose a branch at random from the list of known users of such reporting software and request that the registered representative generate a current report from the software for a random sample of customers showing accounts and other assets. The supervisor may also request copies of reports generated by the branch during the quarter and sample those reports for review. The Supervisor will review the reports for any suspicious external accounts or external investments, and if found, will investigate such accounts or investments in order to determine its veracity and the reported value of the investment. All uncorroborated investments will be reported to management for further action.

Supervisors shall evidence their review of each such report by notating on the report the date of review and initials or signature. (Electronic is acceptable) All reports should be maintained in a Consolidated Report supervision folder on the Home Office network. In addition, Supervisors should identify the branch reviewed for consolidated reports on his or her quarterly supervisors' log.

In the alternative, supervisors may conduct a remote review via Zoom or other video conferencing software, or by being given temporary access to the software. Review in this fashion may be memorialized by a memorandum stating the customer accounts reviewed and notation of any findings and maintained in the Consolidated Report supervision folder on the Home Office network.

3) Disclosure on Consolidated Reports: Each consolidated report must provide a disclosure substantially similar to the following:

This report may contain manually entered assets. The accuracy and authenticity of manually entered assets is reliant solely on the author of the information and not controlled by or attested to by Coastal Equities Inc. nor its affiliates or business partners. Any information represented as manually entered assets should be regarded as informational only and not interpreted as official or legal financial positions. The combined total represents the combination of various sources and types of accounts. This combined total is subject to any error of any of the types of data sources that may be contributing to it, including manual entry errors and data reliability or completeness errors. The cost basis information is subject to the validity of the supplier of cost basis information and should not be used for tax purposes. Consolidated reporting may be provided via third party data aggregator and portfolio performance engine, under contractual agreement with the broker dealer. This consolidated report is based on custodian(s) and/or Financial Representative provided account detail and is reflected here for

informational purposes only, as a customer courtesy. Account information contained within this report has been provided by the custodian directly, your Financial Representative or, in the alternative, via third party data provider. The information herein is from sources deemed to be reliable, but its accuracy cannot be guaranteed. This consolidated report may include assets that the firm does not hold on your behalf ("held away assets") which are not included on the firm's books and records. Assets "held away" are those accounts which have been solicited and/or are held outside of the broker dealer. In most instances, "held away" assets may be non-verifiable by the Broker Dealer. Assets "held away" from the broker dealer may not be covered by SIPC. This report content may supplement, but is not intended to replace, the official customer account statement (hereafter referred to as "source document") provided by the custodian. You are encouraged to review and maintain the official source document(s) provided by the account custodian(s). These source documents may contain notices, disclosures and other important information and may also serve as a reference should questions arise regarding the accuracy of the information in this consolidated report. Always refer to those source documents for lending, legal or tax purposes. Calculations are based on and valuations are stated in US Dollars. If you have any questions as to the values of the assets, please contact the sponsor company directly.

*Coastal Equities Inc. * 1201 N. Orange St., Suite 729 * Wilmington, DE 19801 * Member FINRA SIPC*

11 ACCOUNTS

11.1 New Accounts

[SEC Securities Exchange Act of 1934 Rule 17a-3(a)(17); FINRA Rule 2090; FINRA Information Notice 10/21/08 New Account Application Template]

When opening and maintaining customer accounts, CEI and its RRs are obligated to use reasonable diligence to "know the customer" by obtaining essential facts about the customer and the authority of each person acting on behalf of the customer. Key requirements include the following:

- The new account application (which is designed to include information required by rules) must be complete prior to submission for approval. If the customer refuses to provide certain information, this must be indicated on the new account application.
- Where recommendations will be made to a non-institutional customer, account information includes the customer's financial status, tax status, investment objectives, and other information used or to be considered to determine the suitability of recommendations.
- The new account form must be signed by the RR opening the account, if any.
- New accounts must be accepted by a Principal, evidenced either by signature on the new account application, or by electronic signature in Smart Station. (Principal approval of the new account opening service request.)
- Under anti-money laundering requirements, the customer's identification must be verified.
- Required account documents, which vary depending on the type of account opened, must be obtained. Failure to obtain required documents may result in closure of the account.
- The customer's new account information will be sent to the customer for verification within 30 days of opening the account and every three years thereafter. When account information is changed, the changed information will be sent to the customer for verification within 30 days of the change.

This section provides an explanation of certain requirements that apply to new accounts.

11.1.1 Trusted Contact Person

Among other required new account information, a trusted contact person should be identified for a "specified adult" under FINRA Rule 2165 which includes natural person customers age 65 or older or who have physical or mental impairments the Firm reasonably believes are unable to protect their own interest. At the time of account opening the customer will be notified, in writing (which may include electronic), that the Firm is authorized to contact the trusted contact person and to disclose to the trusted person 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.

11.1.2 Regulation Best Interest (BI)

Regulation BI applies to new accounts in two key ways:

- New customers must be provided with the Form CRS Relationship Summary at the time the account is opened.

- Recommendations to open accounts are subject to Regulation BI requirements and require provision of the Form.

The standards for making account recommendations in the customer's best interest are included in the chapter: *REGULATION BEST INTEREST (BI)*.

11.1.3 Designation of Accounts

[FINRA Rule 3250]

All accounts must be in the name of the customer except that an account may be designated by a number or symbol if the customer provides a written statement attesting to the ownership of the account.

11.1.4 Anti-Money Laundering (AML) New Account Requirements

AML rules apply to the opening of new accounts. This section summarizes the more complete requirements explained in the chapter *ANTI-MONEY LAUNDERING (AML) PROGRAM*.

11.1.4.1 Accounts Requiring Approval By The AML Compliance Officer

The following accounts require review and approval by the AML Compliance Officer at the time of opening. The AML Compliance Officer may require additional information for these accounts.

- **Numbered accounts** (accounts designating a number rather than a name as the account name).
- **Any account requesting confidential handling** of its name, mailing of confirmation and statements, etc.
- **Accounts domiciled in high risk countries.** Accounts domiciled in countries identified by OFAC or the Financial Action Task Force on Money Laundering (FATF) as having inadequate anti-money laundering standards or representing high risk for crime and corruption.
- **Foreign public officials.** Includes individuals in high offices of foreign governments, political party officials and their families and close associates (if known and/or readily identifiable).
- **Correspondent and Private Banking accounts.** See the section *Due Diligence For Correspondent And Private Banking Accounts*.

11.1.4.2 Customer Identification Program (CIP)

[USA PATRIOT Act Section 326; Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart B; FINRA Notice to Members 03-34; FinCEN Frequently Asked Questions: <https://www.fincen.gov/resources/statutes-regulations/guidance/interagency-interpretive-guidance-customer-identification>; FinCEN No-Action position on CIP requirements under clearing arrangements: FIN-2008-G002; Guidance on Obtaining and Retaining Beneficial Ownership Information, FinCEN Guidance, FIN-2010-G001 March 5, 2010]

New customer accounts are subject to CIP reviews mandated under anti-money laundering rules.

11.1.4.2.1 Definition of Customer Under CIP Rule

The definition of "customer" under the CIP rule is different than definitions under other rules. Who is a "customer" under this Rule affects CEI's obligations.

Under the CIP rule and for purposes of this section, "customer" is defined as:

- A person that opens a new account.
- An individual who opens a new account for:
 - An individual who lacks legal capacity; or

- An entity that is not a legal person.

"Customer" does not include a financial institution regulated by a Federal regulator; a bank regulated by a state bank regulator; those exempted under Federal rule include municipalities; or a person with an existing account at CEI providing there is reasonable belief that the true identity of the person is known.

11.1.4.2.2 Accounts Opened by Other Financial Institutions

There are certain accounts opened by financial institutions where the underlying beneficial owners are not subject to customer identification requirements (see *Customer Due Diligence*) or where CEI may rely on the other financial institution to conduct customer due diligence under their own AML program. A key issue is whether the account is a "customer" of CEI. "Customer" accounts are subject to reviews by CEI or by the financial institution opening the account. More detail is included in the AML chapter. CEI is not obligated to conduct due diligence under the Customer Identification Rule in the following circumstances, depending on conditions explained in the AML chapter. Questions should be referred to the AML Compliance Officer.

- Some financial intermediaries such as banks, clearing firms, investment advisers, *etc.* open accounts for their own customers and provide limited information when opening an account to facilitate clearing of transactions or transfer of assets. The beneficial owners of these accounts are not considered "customers" and are not subject to CEI's due diligence reviews.
- CEI may rely on the other financial institutions to conduct reviews of shared customers where it is reasonable to rely on the other institution; the other institution is subject to AML rule requirements; and the other institution enters into a contract attesting to its performance of AML reviews.
- Shared accounts opened by investment advisers are not subject to CEI's review if the investment adviser:
 - is determined to be reasonable to rely upon;
 - is registered with the SEC; and
 - enters into a written agreement with CEI.

11.1.4.3 Master Accounts and Sub-Accounts

[FINRA Regulatory Notice 10-18; SEC National Exam Risk Alert "Master/Sub-accounts:"
<http://www.sec.gov/about/offices/ocie/riskalert-mastersubaccounts.pdf>]

Accounts are sometimes established as "master accounts" that represent multiple sub-accounts. Depending on facts and circumstances (discussed below), master/sub-accounts may be recognized as separate customer accounts subject to CIP reviews.

11.1.4.3.1 Description of Master/Sub-Accounts

A master account may have multiple underlying accounts on behalf of underlying investors; sub-advisers may be authorized to effect transactions without the intermediation of the master account owner. Also, an individual or entity may set up sub-accounts for separate trading strategies or algorithms. Sub-accounts may be used by individual traders or groups of traders. The master account may be another broker-dealer or a partnership that provides its individual partners trading authority over separate sub-accounts.

11.1.4.3.2 Obligations to Conduct CIP Reviews

Except for accounts opened by investment advisers and financial institutions discussed under *Accounts Opened by Other Financial Institutions* and meeting the conditions of that section, when there are separate owners of the

sub-accounts, CEI has an obligation to identify the beneficial owners. Indicators that there may be separate owners requiring CIP review of the sub-accounts include:

- The sub-account owner is entering orders for itself.
- CEI has actual notice the sub-accounts have different owners.
- The sub-accounts are separately documented and/or receive separate reports.
- The sub-accounts are addressed separately in terms of transaction, tax or other reporting.
- The services provided to the sub-accounts engender separate surveillance and supervision of the sub-accounts for compliance with rules or for risk management purposes consistent with the review of separately owned accounts.*
- There are financial arrangements or transactions with the sub-accounts, or separate account terms, that reasonably raise questions concerning whether such accounts represent separate beneficial owners.*
- The sub-accounts incur charges for commissions, clearance and similar expenses, separately, based upon the activity only of that subject sub-account.*
- There is evidence of financial transactions or transfers of assets or cash balances that would reasonably evidence separate beneficial ownership of the sub-accounts.*
- CEI (or RR) is aware of or has access to a master account or like agreement that evidences that the sub-accounts have different beneficial owners.
- There is evidence that a party maintaining a master/sub-account arrangement has interposed sub-accounts that have or are intended to have the effect of hiding the beneficial ownership interest.*
- The number of sub-accounts maintained is so numerous as to reasonably raise questions concerning whether such accounts represent separate beneficial owners.*

*Items above would not apply in the case of accounts opened by a registered BD or a bona fide investment adviser.

11.1.4.3.3 Information Security

CEI has procedures to protect information and information systems from unauthorized access, disclosure, tampering, and other breaches of information security. Where there are master accounts with sub-account access to Firm systems, all participants will be required to participate in training, validate their participant authority to trade in sub-accounts; and use Firm-issued passwords which will be periodically changed.

11.1.4.3.4 Surveillance

Transactions for master and sub-accounts are subject to CEI's surveillance to identify potential insider trading and market manipulation activities.

11.1.4.4 Definitions

[SEC Securities Exchange Act of 1934 Rule 17a-3(a)(17)(i)(A); FINRA Rule 4512]

The regulations should be consulted for more complete definitions.

Legal entity customer: corporation; limited liability company; another entity created by a public filing with a Secretary of State or equivalent; general partnership; limited partnership; business trust created through a state filing; or any similar entity formed under federal law. Does not include sole proprietorships, unincorporated associations, and natural persons opening their own account. Other exclusions are a federal- or state-regulated financial institution; political departments and agencies of the U.S. or a State; various different types of entities registered with the CFTC or SEC; and other entities included in the regulation.

Beneficial owner: any individual who (directly or indirectly) owns 25% or more of the equity of a legal entity customer; a single individual with ability to control, manage, or direct a legal entity (*e.g.*, CEO, CFO), or anyone else who regularly performs these functions. Does not include a nominee or straw man.

11.1.4.5 Required Customer Information

[SEC Securities Exchange Act of 1934 Rule 17a-3(a)(17)(i)(A); FINRA Rule 4512]

Basic information required **prior to opening the account** includes:

- **Name**
- **Date of birth**, for an individual
- **Address:**
 - for an individual, residential or business street address. If no street address exists or is available, an APO or FPO box number or the residential or business street address of a next of kin or another contact individual
 - for a non-individual (corporation, trust, *etc.*) a principal place of business, local office, or other physical location.
- **Telephone number**
- **Employment status** (including occupation and whether the person is associated with a broker dealer)
- **Annual income**
- **Net worth** (excluding value of primary residence)
- Account's investment objectives
- For joint accounts, information on each joint owner (financial information may be combined)
- **Taxpayer identification number** for a U.S. person (U.S. citizen or non-individual established or organized under U.S. or state laws).
- **Identification number for non-U.S. person** which may include a taxpayer ID number; passport number and country of issuance; alien identification card number; or the number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photo or similar safeguard.
- **Beneficial owners** (see the section that follows) including information about the following:
 - the nature and purpose of customer relationships to develop a customer risk profile
 - information sufficient at the time of account opening so customer activity may be assessed for SAR requirements (may include type of customer requesting services; type of account being opened; services or products being used)

In the case of a customer who has applied for a taxpayer identification number but has not yet received it, notation must be made on the new account application that the taxpayer ID has been applied for. The account will be restricted to liquidating transactions if the taxpayer ID number is not received within 30 days of opening the account.

In addition, under FINRA Rule 4512 CEI will retain the name of the RR responsible for the account and, if multiple RRs are assigned to the account, a record indicating the scope of their responsibilities with respect to the account. This requirement does not apply to an institutional account.

See Chapter ANTI-MONEY LAUNDERING (AML) PROGRAM for Customer Identification Program (CIP) requirements

11.1.5 Identity Theft (Red Flags Rule)

[Fair and Accurate Credit Transactions Act (FACT Act) Section 114 and 315; SEC Securities Exchange Act of 1934 Regulation S-ID]

Responsibility	<ul style="list-style-type: none"> • Associated Persons • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New account information • Order and transactions records (including transfers of funds/securities) • Available reports
Frequency	<ul style="list-style-type: none"> • Daily and ongoing
Action	<ul style="list-style-type: none"> • Identify "red flags" when reviewing new accounts, orders, and transactions • If red flags are identified, contact the AML Compliance Officer to consult regarding further action • Include identity theft in training
Record	<ul style="list-style-type: none"> • New account records • Order and transactions records • Referral of red flags to Compliance and notation of action taken • Records of training including when conducted, subject matter, and who attended

Identity thieves use someone's personal identifying information to open new accounts and misuse existing accounts. CEI has established an Identity Theft Prevention Program (ITPP) to help detect and prevent identity theft. Many elements of detecting or preventing identity theft are similar to anti-money laundering (AML) requirements that are included in these policies. A more detailed explanation of the Program is included in the section *Identity Theft Prevention Program (Red Flags Rule)* in the chapter *ANTI-MONEY LAUNDERING (AML) PROGRAM*.

The ITPP is based on identifying "red flags" that indicate identity theft may have occurred. ***It is the responsibility of all associated persons to be alert and report to the AML Compliance Officer any new or existing customers who may be engaged in violations of anti-money laundering regulations or identity theft or who have reported identity theft.***

9.1.5.1 Red Flags

The following two tables include "red flags" that are possible indicators of identity theft or money laundering.

Red Flags indicating potential Identity Theft
Category: Alerts, Notifications or Warnings from a Consumer Credit Reporting Agency
1. A fraud or active duty alert is included on a consumer credit report. An "active duty" alert is an alert a military person may add to his/her credit report to identify potential identity theft.
2. A notice of credit freeze is given in response to a request for a consumer credit report.
3. A notice of address or other discrepancy is provided by a consumer credit reporting agency.

4. A consumer credit report shows a pattern inconsistent with the person's history, such as a big increase in the volume of inquiries or use of credit, especially on new accounts; an unusual number of recently established credit relationships; or an account closed because of an abuse of account privileges.
Category: Suspicious Documents
5. Identification presented looks altered or forged.
6. The identification presenter does not look like the identification's photograph or physical description.
7. Information on the identification differs from what the identification presenter is saying.
8. Information on the identification does not match other information our firm has on file for the presenter, like the original account application, signature card or a recent check.
9. The application looks like it has been altered, forged or torn up and reassembled.
Category: Suspicious Personal Identifying Information
10. Inconsistencies exist between the information presented and other things we know about the presenter or can find out by checking readily available external sources, such as an address that does not match a consumer credit report, or the Social Security Number (SSN) has not been issued or is listed on the Social Security Administration's (SSA's) Death Master File.
11. Inconsistencies exist in the information that the customer gives us, such as a date of birth that does not fall within the number range on the SSA's issuance tables.
12. Personal identifying information presented has been used on an account our firm knows was fraudulent.
13. Personal identifying information presented suggests fraud, such as an address that is fictitious, a mail drop, or a prison; or a phone number is invalid, or is for a pager or answering service.
14. The SSN presented was used by someone else opening an account or other customers.
15. The address or telephone number presented has been used by many other people opening accounts or other customers.
16. A person who omits required information on an application or other form does not provide it when told it is incomplete.
17. Inconsistencies exist between what is presented and what our firm has on file.
18. A person making an account application or seeking access cannot provide authenticating information beyond what would be found in a wallet or consumer credit report, or cannot answer a challenge question.
Category: Suspicious Account Activity
19. Soon after CEI gets a change of address request for an account, we are asked to add additional access means (such as debit cards or checks) or authorized users for the account.
20. A new account exhibits fraud patterns, such as where a first payment is not made or only the first payment is made, or the use of credit for cash advances and securities easily converted into cash.
21. An account develops new patterns of activity, such as nonpayment inconsistent with prior history, a material increase in credit use, or a material change in spending or electronic fund transfers.
22. An account that is inactive for a long time is suddenly used again.

23. Mail CEI sends to a customer is returned repeatedly as undeliverable even though the account remains active.
24. We learn that a customer is not getting his or her paper account statements.
25. We are notified that there are unauthorized charges or transactions to the account.
Category: Notice From Other Sources
26. An outside agency, law enforcement, a clearing firm, or other source notifies CEI that an account has been opened or used fraudulently.
27. CEI is notified of potential unauthorized access to customer personal information due to data loss from an outside provider or a breach of an outside provider's data.
28. Notice from a customer of the loss of information (e.g., loss of wallet, birth certificate, etc.).

Red Flags indicating potential Money Laundering
The customer exhibits unusual concern regarding CEI's compliance with government reporting requirements and CEI's AML policies, particularly with respect to his or her identity, type of business and assets, or is reluctant or refuses to reveal any information concerning business activities, or furnishes unusual or suspect identification or business documents.
The customer wishes to engage in transactions that lack business sense or apparent investment strategy, or are inconsistent with the customer's stated business strategy.
The information provided by the customer that identifies a legitimate source for funds is false, misleading, or substantially incorrect.
Upon request, the customer refuses to identify or fails to indicate any legitimate source for his or her funds and other assets.
The customer (or a person publicly associated with the customer) has a questionable background or is the subject of news reports indicating possible criminal, civil, or regulatory violations.
The customer exhibits a lack of concern regarding risks, commissions, or other transaction costs.
The customer appears to be acting as an agent for an undisclosed principal, but declines or is reluctant, without legitimate commercial reasons, to provide information or is otherwise evasive regarding that person or entity.
The customer has difficulty describing the nature of his or her business or lacks general knowledge of his or her industry.
The customer attempts to make frequent or large deposits of currency, insists on dealing only in cash equivalents, or asks for exemptions from CEI's policies relating to the deposit of cash and cash equivalents.
The customer engages in transactions involving cash or cash equivalents or other monetary instruments that appear to be structured to avoid the \$10,000 government reporting requirements, especially if the cash or monetary instruments are in an amount just below reporting or recording thresholds.
For no apparent reason, the customer has multiple accounts under a single name or multiple names, with a large number of inter-account or third-party transfers.
The customer is from, or has accounts in, a country identified as a non-cooperative country or territory by the Financial Action Task Force (FATF).

The customer's account has unexplained or sudden extensive wire activity, especially in accounts that had little or no previous activity.
The customer's account shows numerous currency or cashiers check transactions aggregating to significant sums.
The customer's account has a large number of wire transfers to unrelated third parties inconsistent with the customer's legitimate business purpose.
The customer's account has wire transfers that have no apparent business purpose to or from a country identified as a money laundering risk or a bank secrecy haven
The customer's account indicates large or frequent wire transfers, immediately withdrawn by check or debit card without any apparent business purpose.
The customer makes a funds deposit followed by an immediate request that the money be wired out or transferred to a third party, or to another firm, without any apparent business purpose.
The customer makes a funds deposit for the purpose of purchasing a long-term investment followed shortly thereafter by a request to liquidate the position and transfer of the proceeds out of the account.
The customer engages in excessive journal entries between unrelated accounts without any apparent business purpose.
The customer requests that a transaction be processed in such a manner to avoid CEI's normal documentation requirements.
The customer, for no apparent reason or in conjunction with other "red flags," engages in transactions involving certain types of securities, such as penny stocks, Regulation "S" (Reg S) stocks, and bearer bonds, which although legitimate, have been used in connection with fraudulent schemes and money laundering activity. (Such transactions may warrant further due diligence to ensure the legitimacy of the customer's activity.)
The customer's account shows an unexplained high level of account activity with very low levels of securities transactions.
The customer maintains multiple accounts, or maintains accounts in the names of family members or corporate entities, for no apparent business purpose or other purpose.
The customer's account has inflows of funds or other assets well beyond the known income or resources of the customer.

11.1.5.2 Notifying the AML Compliance Officer

If an associated person identifies suspicious activity or red flags involving new or existing accounts, it is the associated person's obligation to **immediately** notify his or her supervisor and/or the AML Compliance Officer. Supervisors are responsible for contacting the AML Compliance Officer if notified by an associated person of suspicious activity or red flags or when he or she personally identifies them.

11.1.6 SIPC Disclosure

[FINRA Rule 2266]

When new accounts are opened, new customers will be provided information about the Securities Investor Protection Corporation (SIPC) including SIPC's web site address and phone number. This information is also provided annually in writing to all customers.

11.1.7 Approval

[Exchange Act Rule 17a-3(17)(i)(A); FINRA Rule 4512]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New Account Form
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Review new account form for: <ul style="list-style-type: none"> ○ Completeness ○ Proper styling of account ○ Unacceptable accounts (accounts in name of minor only, fictitious accounts, numbered accounts without disclosure of owner, <i>etc.</i>) ○ Potential improper addresses (post office boxes, addressed to RR or CEI, <i>etc.</i>) ○ Consistency of investment objectives with financial status, prior investment experience, <i>etc.</i> ○ Initial transaction consistent with investment objectives ○ RR registration in state of customer's residency
Record	<ul style="list-style-type: none"> • Supervisor's signature on New Account Form • New account forms are retained by Operations

A completed new account form (written or electronic), signed by the RR, is required for each new account opened. The designated supervisor is responsible for reviewing the new account form for the necessary information and will promptly approve each new account.

11.1.8 Customer Account Information

[SEC Securities Exchange Act of 1934 Rule 17a-3(17)(i)(A)]

Within 30 days of opening an account (or with the next scheduled account statement), the clearing firm will send the customer a copy of new account information for verification. In addition, account information will be verified with the customer every three years. In the event there is a change to the customer's account (including changes in investment objectives), the changed account information will be sent to the customer for verification within 30 days of submission of the change.

11.1.9 Addresses on Customer Accounts

[SEC Securities Exchange Act of 1934 Rule 17a-3(a)(17)(i)(B)(2)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • RR
Resources	<ul style="list-style-type: none"> • New account forms • Service Requests

Frequency	<ul style="list-style-type: none"> • As needed
Action	<ul style="list-style-type: none"> • Identify improper address on new account forms at time of approval • When approving new accounts, ensure beneficial owner of the account will receive confirmations consistent with the policy • Financial Advisor or designee confirm verbal requests for account changes • Financial Advisor or designee initiate service request for account maintenance • Review and approve address change account maintenance service requests
Record	<ul style="list-style-type: none"> • Supervisor's signature on New Account Form • Service Request record in SmartStation

Confirmations and statements and other account information will be transmitted to the customer at the address requested by the customer. CEI or an associated person may not be the sole addressee for a customer's account unless the account is for the direct benefit of CEI or associated person.

Acceptable addresses include:

- **for an individual:** residential or business street address. If no street address exists or is available, an APO or FPO box number or the residential or business street address of a next of kin or another contact individual
- **for a non-individual (corporation, trust, etc.):** a principal place of business, local office, or other physical location.
- **for a P.O. Box address:** a legal address for the customer must also be provided.

Accounts **may not** be addressed to CEI, an RR or other associated person of CEI with the exception of accounts for the beneficial ownership of the RR or associated person. Accounts **may not** be addressed care/of (c/o) someone else unless the customer provides written authorization requesting such an address.

Address changes: Address changes may be processed through a service request in SmartStation. Each such service request is reviewed and approved by a supervisor prior to execution of the service request. Verbal instruction from the client requires notation that the customer's identity has been verified by two personal identifiers on record in the system (e.g. last four digits of SSN, zip code, birth date, etc.) Written instructions signed by the customer requires verification by contacting the customer by phone at the phone number on record. Upon processing the change of address in SmartStation, a notice will be generated by WFCS and sent to the customer's old address and updated address confirming that an address change has been made to the account. Requests to update an address to a PO box must be in writing and signed by the account holder(s). *See section 9.1.13 Post Office Addresses for further information.* A copy of the service request, and written request from the client if any, shall be kept in the branch Address Change File.

Where the account is opened by a fiduciary such as an investment adviser on behalf of the fiduciary's customer, CEI will provide either confirmations or periodic account statements to the underlying beneficial account holder. CEI will make a good faith effort to obtain the information necessary to send confirmations directly to the beneficial owner; however, if this information is not provided by the fiduciary, CEI will forward confirmations to the owner's custodian or, if there is no custodian or CEI is the custodian, CEI will send the confirmation directly to the fiduciary.

11.1.10 Account Documents

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New account opening documents
Frequency	<ul style="list-style-type: none"> • As needed
Action	<ul style="list-style-type: none"> • Review new account documentation to ensure required account documents are obtained for each new account
Record	<ul style="list-style-type: none"> • Supervisor signature and date on account opening document(s) or electronic approval in SmartStation • New account files (paper) may be maintained in branch file and Home Office • New account files imaged and maintained in SmartStation

Additional account documents may be required depending on the type of account opened. The designated supervisor is responsible for reviewing new account submissions, determining whether additional account documents are required to open the account, and following-up regarding missing documents.

Upon an electronic account opening, where the client is not physically present in the branch, the clearing firm will mail a complete account package to the client within thirty (30) days.

[Effective October 1, 2018] The client must sign and return the Single Signature Page and any other ancillary documents within thirty (30) days of account opening. Accounts for which no Single Signature Page (or other required document) has been returned to the branch and imaged to SmartStation shall be restricted to liquidations only unless and until such documents are received.

11.1.11 Pre-dispute Arbitration Agreements with Customers

[FINRA Rule 2268; FINRA Notice to Members 05-32 and 05-09]

Customers will be provided with copies of any signed agreements that include a predispute arbitration agreement within 30 days of signing; the customer will acknowledge receipt of the arbitration agreement on the agreement itself or on a separate document.

In addition, within 10 days of request by a customer, CEI will provide a copy of any predispute arbitration agreement the customer has signed as well as relevant arbitration forum rules, if requested. The customer will be notified if the signed agreement cannot be located.

11.1.12 Revisions to Customer Agreements

Firm policy does not permit revisions to pre-printed language on customer agreements. Requests for changes should be referred to Compliance for review.

11.1.13 Accounts Requiring Notification to Customer's Employer

[NASD Rule 3050]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
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Resources	<ul style="list-style-type: none"> • New Account Form
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Code account for duplicate confirmations and/or statements as requested by other broker-dealers • For accounts of associated persons of FINRA or the AMEX, code the accounts for duplicate confirmation and statements to FINRA or the AMEX
Record	<ul style="list-style-type: none"> • Record of duplicate confirmations and statements is included with new account records

11.1.13.1 Associated persons of Other Broker-Dealers

When opening an account for a person employed by another broker-dealer (including accounts where the associated person has control or a personal financial interest), the other broker-dealer must be notified. CEI will provide duplicate confirmations, statements, or other information requested by the employing broker-dealer.

11.1.13.2 Transactions Involving FINRA Employees

[FINRA Rule 2070]

When CEI has notice that a FINRA employee has a financial interest in, or controls trading in, an account, CEI will obtain and implement instructions from the employee to provide duplicate account statements to FINRA.

CEI or its Associated persons are prohibited from making a loan of money or securities to any FINRA employee other than disclosed, routine banking and brokerage agreements (or loans originating from a personal or family relationship).

CEI or its associated persons cannot directly or indirectly give anything (other than something of nominal value such as a logo hat, pen, *etc.*) to a FINRA employee who has responsibility for a regulatory matter involving CEI. "Regulatory matter" includes examinations, disciplinary proceedings, membership applications and dispute-resolution proceedings.

11.1.14 Post Office Addresses

If the customer opens an account using a post office address, the street address must also be provided on the new account form. The only exception is for customers who reside in rural areas where the post office address is the only address, which should be noted on the new account form.

11.1.15 Unacceptable Accounts

The following are examples of accounts that are unacceptable. Questions regarding whether new accounts may be opened should be referred to Compliance.

Unacceptable accounts include:

- Fictitious accounts in a name other than the name of the legal owner
- Accounts in the name of a minor
- Margin accounts for minors

11.2 Transferring Accounts

[FINRA Rule 2140 and 11870]

11.2.1 Accounts Transferring In

When new accounts are transferred from another broker-dealer, a transfer form must be completed by the customer authorizing the transfer and provided to the receiving firm. Most accounts transfer via ACATS which expedites validation and transfer from the other BD.

Orders to sell securities to be transferred from the other firm may not be entered until validation is received. RRs should contact Operations to confirm whether the transfer has been validated.

11.2.2 Accounts Transferring Out

When validated instruction has been received to transfer a customer's securities account assets to another firm, the account will be "frozen," *i.e.*, all open orders (with the exception of option positions that expire within 7 business days) must be canceled and no new orders taken.

CEI and its associated persons may not interfere with a customer's request to transfer his or her account unless there is a *bona fide* reason for doing so, such as a lien for money owed.

11.3 Accounts and Securities Subject to Blocking

[Various Treasury Department regulations]

CEI is prohibited from doing business in specific countries or with organizations or individuals the subject of Government sanctions. The U. S. Treasury Department's Office of Foreign Assets Control (OFAC) is responsible for administering and enforcing economic and trade sanctions. Sanctions target foreign countries, terrorism sponsoring organizations, narcotics traffickers, money launderers, and other entities and individuals. Sanctions include the freezing of assets and blocking securities issued by embargoed foreign issuers.

As part of its anti-money laundering program, CEI monitors accounts and securities included on OFAC's lists, available at OFAC's web site at www.treas.gov/ofac. OFAC information is updated whenever the Government issues new sanctions that result in blocking requirements.

Blocking will occur under the following circumstances:

- An account is opened for someone included on an OFAC list.
- The owner of an existing account is added to an OFAC list.
- A security is identified in a customer account where the issuer is the subject of blocking requirements.
- A request is made by a customer to pay or transfer funds or securities to a blocked person or entity.

RRs will be notified if one of their customer accounts; a security held in one of their accounts; or a requested transfer of funds or securities is blocked. In addition to the above, open orders will be cancelled for any account that is blocked.

Compliance with blocking requirements is very important. Violations can result in substantial fines against CEI or persons engaging in prohibited transactions. Questions regarding blocked accounts, transfers, or securities should be referred to Compliance.

11.4 Updating Account Information and Periodic Affirmation

[SEC Securities Exchange Act of 1934 Rule 17a-3(a)(17)]

Responsibility	<ul style="list-style-type: none"> • Registered Representative • Direct Supervisor • Compliance
Resources	<ul style="list-style-type: none"> • Information obtained from customer • Responses from customers
Frequency	<ul style="list-style-type: none"> • As required: update account information based on information provided by customer • Within 30 days of changes: send written information about changes to account • At least every 36 months: send customers a copy of new account information
Action	<ul style="list-style-type: none"> • RR: Record changes to customer information reported by customer • Send information to customers • Compliance: follow up customer responses (contact RR, RR's supervisor, New Accounts)
Record	<ul style="list-style-type: none"> • New account records • Record of furnishing information within 30 days • Notation of action by Compliance for responses received from customers • Copies of approved requests are maintained the the branch file

Registered Representatives should promptly update customer new account information whenever they are informed or become aware of changes. Updates may be recorded by completing new forms. New forms require the approval of the designated supervisor and signature of the customer, where required.

At least every 36 months, the Clearing Firm will provide customers with new account information on record for their accounts and will be asked to advise of any changes or updates. Responses will be forwarded to Compliance. This notification is not required for accounts that have been inactive for 36 months or where no recommendations are made to the customer.

11.4.1 Change of Investment Objective on Accounts

Investment Objective changes are processed through an Account Maintenance service request in Smart Station. Each such service request is reviewed and approved by a supervisor. Verbal instruction from the client requires notation that the client gave instructions in person, and is personally known to the Representative, or that the customer's identity has been verified by two personal identifiers on record (e.g. last four digits of SSN, zip code, birth date, etc.) Within 30 days of changes to a customer's investment objectives, the Clearing Firm will send a copy of the new account information, including the change, to the customer with a request for correction of any inaccurate information. A copy of the service request, and written request from the client if any, shall be kept in the branch Investment Objective Change File.

Accounts custodied outside WFCS: Client address change requests must be submitted in writing on the firm's IO Change Request Form and reviewed and approved by a supervisor. The RR and supervisor must confirm that any account information held with WFCS is updated with the new IO information when necessary.

11.4.2 Change of Customer Address

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Coastal Address Change Form
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Obtain written approval of request by designated supervisor OR • Review/approve electronic Service Request to change address
Record	<ul style="list-style-type: none"> • Copies of approved requests are maintained in the branch file

Accounts custodied at WFCS: Address changes may be processed through a service request in Smart Station. Each such service request is reviewed and approved by a supervisor prior to execution of the service request. Verbal instruction from the client requires notation that the customer's identity has been verified by two personal identifiers on record in the system (e.g. last four digits of SSN, zip code, birth date, etc.) Written instructions signed by the customer requires verification by contacting the customer by phone at the phone number on record. Upon processing the change of address in Smart Station, a notice will be generated by WFCS and sent to the customer's old address and updated address confirming that an address change has been made to the account. Requests to update an address to a PO box must be in writing and signed by the account holder(s). A copy of the service request, and written request from the client if any, shall be kept in the branch Address Change File.

Accounts custodied outside WFCS: Client address change requests must be submitted in writing on the firm's Change of Address Request Form and reviewed and approved by a supervisor. The Firm will notify the associated broker-dealer of the change and will rely upon the account's broker-dealer to mail confirmation of the address change to the current and new addresses on file within thirty days of the address change request.

11.4.3 Undeliverable Mail

When customer mail is returned to CEI as undeliverable, Operations will contact the RR's supervisor to obtain an updated address. When a new address is provided, the customer will be sent a letter at the new address asking for signed confirmation that the new address is correct. When the letter is returned, the customer's signature will be compared to other account documents on file. Signature anomalies will be referred to Compliance for follow up. If the customer fails to return the form, a second letter will be sent notifying the customer his or her account will be frozen unless an affirmation is received.

If a corrected address is not provided, the account will be frozen to preclude securities or money transactions (other than expiration of options or similar passive transactions) until a correct address is provided.

11.4.4 Holding Customer Mail Prohibited

CEI will not hold mail on a customer's behalf, even for a short duration. RRs are **not** permitted to hold customer mail. A customer, who cannot receive mail at the address established on the account, must be instructed to provide a third party mailing address that is not related to CEI or any associate of CEI.

11.5 Sweep Programs

[SEC Securities Exchange Act of 1934 Rule 15c3-3(j)(2)(ii); SEC FAQs regarding financial responsibility rules: <http://www.sec.gov/divisions/marketreg/amendments-to-broker-dealer-financial-responsibility-rule-faq.htm>; FINRA Rule 3260]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Proposed new programs or material changes to existing programs
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Consider net capital/customer protection implications of terminating a program or adopting a new program • Confirm the bank's business continuity program complies with SRO business continuity rule requirements • For programs with banks that allow the customer to make deposits and/or withdrawals, include accounts in AML reviews • Review the new program or changes • Prepare/provide disclosure information for customers • Obtain customer written consents to participate before opening a sweep account • Include required disclosures with quarterly statements • Send 30-day prior notice of program changes • Arrange for RR training, if necessary
Record	<ul style="list-style-type: none"> • Copies of programs, contracts with providers, records of distributing disclosures to customers when new programs are implemented or changes occur • Copy of bank's affirmation regarding compliance with business continuity requirements • Customer written consents and record of providing disclosures

Free credit balances held in a customer's securities account may be transferred to a product in the clearing firm's sweep program or a customer's interest may be transferred between sweep programs. Four conditions regarding customer disclosures apply:

1. The customer must give **prior** written affirmative consent to having free credit balances included in the sweep program after being notified of (a) the general terms and conditions of the Program; and (b) that the firm may change the products available under the Program.
2. Disclosures and notices required by SROs will be provided to customers by the clearing firm.
3. Quarterly notice is included with statements that swept funds or money market shares can be liquidated and remitted to the customer.
4. 30-day prior written notice of any changes to the sweep program and sweep products will be provided by the clearing firm.

11.6 Margin Accounts

[FINRA Rule 4210; Federal Reserve Regulation T]

11.6.1 Opening Margin Accounts

Prior to engaging in margin transactions, the customer's account must have on deposit at least \$2,000 in cash or securities. Customers must sign a margin agreement which must be received within five days from the first margin trade.

11.6.2 Associated Person Accounts

Extensions and prepayments are not permitted in associated person accounts, except under extraordinary circumstances and with approval of the designated supervisor.

11.6.3 Disclosures

11.6.3.1 Margin Disclosure Statement

[FINRA Rule 2264]

Under FINRA rules, all non-institutional customers who open a margin account must be provided with a margin disclosure statement when the account is opened. CEI's disclosure statement must be included when the margin agreement is sent to the customer for signing. In addition, all margin customers will be provided annually with a copy of the disclosure statement or an abbreviated version of the statement. RRs are responsible for providing the initial disclosure statement; CEI (or its clearing firm, if applicable) will send annual disclosures. The margin disclosure statement also appears on CEI's web site.

Under this requirement, the term "**non-institutional customer**" includes all customers **except**:

- A bank, savings and loan association, insurance company, or registered investment company.
- An investment adviser registered either with the SEC or with a state securities commission
- Any other entity (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least \$50 million

The Clearing Firm is responsible for providing the initial and annual disclosure document to new non-institutional margin account customers.

11.6.3.2 Disclosure of Credit Terms

[SEC Securities Exchange Act of 1934 Rule 10b-16]

Upon opening a margin account, the customer will be provided a written statement explaining the operation of a margin account and the calculation of interest charges on debit balances. It is the FINOP's responsibility to establish procedures for providing the required disclosure.

The Clearing Firm is responsible for providing credit disclosures to margin customers.

11.6.3.3 Securities Loan Transactions

[FINRA Rule 4330(a), 4330(b)(2), 4330.04 and 4330.05]

CEI (or its clearing firm) may engage in borrowing and lending customers' fully paid or excess margin securities. The customer's agreement is included in CEI's margin agreement and disclosures will be provided as described in the next section.

There must be reasonable grounds for believing that the customer's loan(s) of securities are appropriate for the customer, including consideration of (but not limited to) the customer's financial situation and needs, tax status, investment objectives, investment time horizon, liquidity needs, risk tolerance, and any other information disclosed by the customer in connection with entering into securities loans. Determining the appropriateness of customer loans of securities is not required for institutional customers under Rules 4512(c) and 2111(b).

11.6.3.4 Other Disclosures

[FINRA Rule 4330(b)(2)(B)]

Prior to entering into a securities borrowing arrangement with a customer, the customer will be provided with written (which may include electronic) notice stating that the provisions of the Securities Investor Protection Act of 1970 may not protect the customer with respect to the customer's securities loan transaction and that the collateral delivered to the customer may constitute the only source of satisfaction of CEI's obligation in the event CEI fails to return the borrowed securities. Other required disclosures (such as loss of proxy voting rights on margined shares and risk of receiving payments-in-lieu of dividends) will be provided in customer margin agreements, by separate notice, in customer monthly statements, and/or on CEI's web site.

11.6.4 Equal Credit Opportunity Act Requirements

CEI will not discriminate in the extension of credit to customers. Where credit is denied, CEI will provide information to the credit applicant in accordance with the provisions of the Equal Credit Opportunity Act.

11.6.5 Arranging Credit

RRs are not permitted to assist a customer in making credit arrangements to purchase securities outside CEI, other than on terms consistent with those permitted by Regulation T and other rule requirements.

11.6.6 Suitability

Margin accounts may involve more risk than cash accounts, depending on a number of factors including leverage used and types of transactions. The RR is responsible for determining the suitability of margin trading in a customer's account including understanding the customer's investment objectives and financial profile.

11.6.7 Margin Requirements

Initial and maintenance requirements are available by contacting Operations.

11.6.8 New Issues

Margin on new issues are not permitted for a period of 30 days from the effective date of the distribution.

11.6.9 Credit on Restricted Securities

Extension of credit or margin transactions in securities for corporate insiders require the prior approval of Operations. If a customer who holds restricted securities wishes to deposit those securities in a margin account, Operations should be notified to determine the marginability of the securities. Operations should confer with the clearing firm in this regard for approval.

11.6.10 Fiduciary Accounts

Margin transactions are permitted for accounts controlled by an administrator, conservator, custodian (not including UTMA/UGMA accounts), executor, guardian or trustee as follows:

- when such person holds explicit power to engage in margin transactions
- after review of the appointment and applicable document (trust agreement, trust certification, will, *etc.*) explaining investment powers and approval by Compliance

RRs should submit the appropriate enabling document (trust agreement, *etc.*) to Compliance prior to engaging in margin transactions.

11.6.11 Portfolio Margin Accounts

[FINRA Rule 4210(g); FINRA Notice 08-41, 07-14 and 07-11]

Customers with portfolio margin accounts must be provided with a special written disclosure describing the nature of, and risks associated with, portfolio margining. Customers must sign and acknowledge that they have read and understand the disclosure statement and agree to the terms of maintaining a portfolio margin account. RRs are responsible for providing the disclosure and obtaining signed acknowledgment which will be retained in the customer's account file.

Portfolio margining is a margin methodology that sets margin requirements for an account based on the greatest projected net loss of all positions in a product class or group using computer modeling to perform risk analysis using multiple pricing scenarios. It is applicable to all margin equity securities, listed options, security futures products, unlisted derivatives, warrants, index warrants and related instruments.

There are eligibility requirements for customers (other than broker-dealers):

- Meet basic standards for having an account approved for uncovered writing
- Have and maintain at all times account net equity of at least \$5 million (waived for accounts solely limited to listed security futures contracts and listed single stock options) aggregated across all accounts under identical ownership at the clearing broker

Portfolio margining generally permits greater leverage resulting in greater risk for loss. The time limit for meeting margin calls is shorter than for a standard margin account. Operations procedures should be consulted for more detailed information regarding portfolio margining requirements.

11.7 Third Party Accounts

When a third party who is not the principal or named person on the account will give instructions regarding orders, disposition of funds, or other actions involving an account, CEI must have a signed third-party trading authorization. The authorization is signed by the principal of the account and the third party, giving the third party authority to act on behalf of the principal. An example of a third party account is an account for a wife whose husband will give instructions regarding his wife's account. The signed trading authorization must be received BEFORE accepting instructions from the third party.

CEI has two types of trading authorizations:

- Limited trading authorizations limit the third party to giving instructions regarding the purchase and sale of securities and does NOT give authority regarding the disposition of funds or securities.
- Full trading authorizations give the third party authority to give instructions regarding purchases and sales as well as the disposition of funds or securities in the account.

11.8 Discretionary Accounts

[SEC Securities Exchange Act of 1934 Rule 17a-3(17)(ii); SEC interpretation re solely incidental exclusion from investment adviser registration: SEC Release No. IA-5249; FINRA Rule 3260 and 4512(a)(3); Investment Advisers Act Rule 202(a); NYSE Rule 408]

CEI is not registered as an investment adviser under the Investment Advisers Act. Some of its RRs are registered in states as adviser agents, where required, to maintain discretionary accounts.

11.8.1 General Requirements

For a discretionary account, an RR is granted written authority to enter orders on behalf of a customer without contacting the customer prior to each transaction. The key elements of discretionary account requirements include:

- Discretionary accounts require specific written authorization from the customer on a designated form, including the date signed.
- A record must be maintained of the manual signature of each named, natural person authorized to exercise discretion in the account.
- A designated supervisor must approve the account as discretionary (including the date approval is granted) prior to effecting discretionary transactions.
- Discretionary authority is NOT effective until the customer has signed the discretionary agreement AND the account has been approved for discretion.
- Option discretionary accounts also require the approval of Compliance. (Refer to the chapter *OPTIONS* for specific requirements regarding discretionary option accounts.)
- Discretion is not permitted over ERISA plan accounts unless specifically permitted under a firm-authorized program such as a managed account program.
- Every discretionary order must be approved promptly, in writing, by the designated supervisor.
- Each order should indicate whether discretion was exercised or not exercised.

11.8.2 Approval

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Discretionary Account Agreement
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Consider whether discretion is appropriate, which may include: <ul style="list-style-type: none"> ○ Knowledge and experience of RR ○ Reasons for requiring discretionary authority ○ Fiduciary accounts (trust, <i>etc.</i>) require Compliance review to determine whether authority may be transferred to a third person ○ Types of transactions anticipated ○ Ensure only limited authority is granted, unless discretion is for the account of a family member of the RR ○ Discretion for option accounts also requires the approval of Compliance

	<ul style="list-style-type: none"> ○ Establish required duplicate confirmations/statements to Branch Manager and Compliance
Record	<ul style="list-style-type: none"> • Branch Manager signature and date of approval on Discretionary Account Agreement.

At the time a discretionary account is established, the designated supervisor shall approve or disapprove the discretionary status of the account. A record of the approval will be included in the account file for the customer's account.

11.8.3 Limited Authority Only Permitted

Discretionary authority is permitted only on a limited basis, *i.e.*, RRs may have authority to purchase and sell securities only. Full authority, which also authorizes the withdrawal of money or securities, is not permitted except for accounts of family members of the RR. Exceptions require the approval of Compliance.

11.8.4 Indication of Discretion Exercised or Not Exercised

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • For discretionary accounts, ensure DE or DNE is marked on each order
Record	<ul style="list-style-type: none"> • Initials on order tickets; notation in electronic order entry system

Orders in discretionary accounts should indicate whether discretion is exercised or not exercised on each order. Such indication is made by marking "DE" for discretion exercised or "DNE" for discretion not exercised. Discretion not exercised means the RR discussed the order with the customer BEFORE entering it.

11.8.5 Trusts and Other Fiduciary Accounts

Some trusts or other accounts governed by a legal instrument such as a trust agreement may not allow the trustee to re-assign authority to a third party. A copy of the trust agreement or other legal document should be provided to Compliance for review prior to approval of a trust or similar account as a discretionary account.

11.8.6 Principal Transactions Not Permitted

Principal transactions are not permitted when discretion is exercised in a discretionary account. Specific approval for the order should be obtained from the customer and the order marked "discretion not exercised" to execute on a principal basis, or the order should be executed on an agency basis if discretion is exercised. This includes syndicate transactions which should be approved by the customer prior to execution and the order marked "DNE."

11.8.7 Distributions of The Firm's or An Affiliate's Securities

Transactions in securities sold in an underwriting and issued by CEI or by a firm affiliate require the prior written approval of the customer. Discretion may not be exercised for such transactions.

11.9 Accounts for Minors

[Uniform Gifts To Minors Act; Uniform Transfers To Minors Act; FINRA Regulatory Notice 20-07]

There are a number of requirements and restrictions that affect minors' accounts:

- A custodian must be named in and handle the account
- Only one custodian is permitted for each account
- Custodians generally may not delegate authority to another person
- Only one minor may be named in each account
- Margin transactions are not permitted
- Gifts to minors are irrevocable, *i.e.*, the custodian may not direct distribution of assets from the account except for the benefit of the minor
- The minor's social security number must be used when opening the account
- Minors may not be a party to a joint account, investment club, or partnership

11.9.1 Custodian and Guardianship for Minor Accounts

[Uniform Gifts to Minors Act (UGMA); Uniform Transfer to Minors Act (UTMA)]

Generally, Coastal may not open an account for any person who has not attained the age of majority. However, custodial accounts may be opened under the following conditions:

- There is only one minor and one custodian for such account;
- The account is opened under the Uniform Gifts to Minors Act (UGMA) or the Uniform Transfer to Minors Act (UTMA) and Coastal verifies which applies;
- Property transferred to the UGMA or UTMA account is a complete and irrevocable transfer of property to the minor (*i.e.*, the transferor gives up all rights to the property); and
- Upon the minor reaching the age of majority in the particular state of residence, the custodian must transfer the custodial property to the minor.

11.9.2 UTMA and UGMA Controls (Age of Majority)

RR Responsibility: It is the Registered Representative's responsibility upon opening a UTMA or UGMA account to take appropriate steps to calendar for the minor's reaching the age of majority in his/her home state, and, when age of majority is imminent, provide guidance to the custodian and/or former minor as requested or as needed by the applicable client in order to transition or liquidate the account assets.

Supervision: Coastal will monitor the age of majority in such accounts on a quarterly basis by running a report of all such accounts showing dates of birth of each account beneficiary. For beneficiaries approaching age of majority within that quarter, Coastal will provide the account custodian written notice of the upcoming age of majority.

11.10 Coverdell Education Savings Accounts

[26 USC §530 - Coverdell Education Savings Accounts]

A Coverdell Education Savings Account (ESA) is an account created as an incentive to help parents and students save for education expenses. An alternative is the 529 College Savings Plan which is included in the *MUNICIPAL SECURITIES* chapter in the section *529 College Savings Plans (Municipal Fund Securities)*. For more information, refer to the IRS site above; plan sponsors; and the customer's tax adviser.

The following summarizes some of the key features of Coverdell accounts.

- The maximum annual contribution is \$2,000 subject to limits on the donor's modified adjusted gross income.
- Contributions are made from after-tax dollars; there is no tax deduction for contributions.
- ESAs are available for beneficiaries (students) who are under the age of 18 when the account is established. There are exceptions for beneficiaries with special needs.
- The funds are controlled by the account owner (*e.g.*, the parent) at all times.
- Investment choices are broad but may not include life insurance contracts.
- Assets may be used for elementary- and secondary-school tuition as well as for higher education.

The following compares some features of Coverdell and 529 plans.

Feature	Coverdell Account	529 Plan
Contribution limits	\$2000 annual	No restrictions up to maximum lifetime contribution
Allowable investments	Allows almost all types of investments including stocks, bonds, and mutual funds (parallels rules for IRAs)	Limited to state-run allocation programs
Distribution of assets	Must be disbursed on qualified education expenses by the beneficiary's 30th birthday or given to another family member below the age of 30	No age limit
	Federal tax-free if used for qualified education expenses; some states offer tax benefits	Same
	Income tax and penalties may apply for ineligible distributions	Same
Qualified education	Elementary and secondary schools; higher education	Does not allow elementary and secondary education expenses
Income limits affecting contributions	Limits on modified adjusted gross income at certain levels	No limits
Ownership of assets	Owned by person establishing the account, not the child	Same

Designation of new beneficiary	Must be eligible family member of the previous beneficiary to avoid taxes or penalties	Same
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11.11 Accounts for Senior Investors

[SEC/NASAA 2008 report on Protecting Senior Investors:

<http://www.sec.gov/spotlight/seniors/seniorspracticesreport092208.pdf>; 2010 addendum to 2008 report:

<http://www.sec.gov/spotlight/seniors/seniorspracticesreport081210.pdf>; SEC web site Senior Investors:

<http://www.sec.gov/divisions/marketreg/seniorinvestors.htm>; FINRA Rule 2165 and 4512; FINRA Regulatory Notice 17-11,

11-52 and 07-43; FINRA FAQs re financial exploitation of seniors: <http://www.finra.org/industry/frequently-asked-questions-regarding-finra-rules-relating-financial-exploitation-seniors>; Senior Safe Act: Sec. 303 of Economic Growth,

Regulatory Relief and Consumer Protection Act; NASAA/SEC/FINRA Senior Safe Act Fact Sheet: <http://www.nasaa.org/wp-content/uploads/2019/05/Senior-Safe-Act-Fact-Sheet.pdf>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New account information • Order records • Daily Transaction Report • Customer monthly transaction records • Advertising targeting senior investors • Seminar materials
Frequency	<ul style="list-style-type: none"> • Training - as scheduled • Ongoing - other actions
Action	<ul style="list-style-type: none"> • Conduct training on dealing with senior investors • When reviewing investments for seniors, take into particular consideration the factors included in the subsection <i>Recommendations To Senior Investors</i> • Review product-specific guidelines when reviewing for suitability of investments • Refer to new account information when necessary to identify investment objectives and other customer information • Review account activity when appropriate • For escalated issues: <ul style="list-style-type: none"> ○ Consider direct contact with the investor ○ Contact the Trusted Person ○ Notify state or other authorities (after conferring with Compliance) regarding potential elder abuse • Confer with RR regarding suitability questions • Confer with Compliance when necessary • Contact customer when necessary to confirm customer's understanding of, and agreement with, transactions • Modify or restrict future transactions, as appropriate
Record	<ul style="list-style-type: none"> • Initials and comments of action taken on order records, Daily Transaction Report, monthly transaction records, and other available account information

11.11.1 General Requirements

When opening and handling accounts for senior investors, there are certain considerations in addition to usual account handling procedures. There is no benchmark for what constitutes a "senior" or "older" investor, but generally these are individuals who are approaching or have achieved retirement.

11.11.2 Opening Accounts for Senior Investors

When opening accounts, the following should be considered when serving senior investors:

- encourage customers to identify a Trusted Contact Person and obtain permission to contact that person in the event there is an issue or event that requires clarification (such as the customer suffers diminished mental capacity in the future); document account information if the customer refuses to identify a contact person
- indicate "retired" on the new account form to assist in evaluating the investor's status as someone potentially withdrawing from investments vs. accumulating assets
- obtain "lifestyle" information such as when the investor plans to retire, if not already retired; how much money will be needed after retirement; whether there are prospects for future employment; whether a dependent is supported by the investor; other expenses including healthcare expenses anticipated by the investor; the existence of a will and financial power of attorney

Accounts must NOT be opened for a senior investor if there is evidence of financial abuse or diminished capacity; orders should not be accepted under such circumstances, either.

11.11.3 Recommendations to Senior Investors

[FINRA Regulatory Notice 07-43]

Suitability considerations are a concern for all types of accounts. While suitability requirements do not specifically refer to age or life stage, these factors should be considered when making recommendations to older investors. Considerations when dealing with senior investors include:

- Current and future prospects for employment
- Primary expenses including whether the customer still has a mortgage
- Sources of income and whether it is fixed or will be in the future
- Income needed to meet fixed or anticipated expenses
- Savings for retirement and how they are invested
- Liquidity needs
- Financial and investment goals (income needs, preservation of capital, accumulation of assets for heirs)
- Health care insurance and future needs to fund health costs

11.11.4 Diminished Mental Capacity

A difficult issue is a customer who appears to be suffering from diminished mental capacity. If a customer's behavior suggests reduced capacity, it is important to take steps to protect the customer, the RR, and CEI. Relatives or estate beneficiaries may file a complaint or lawsuit if they believe the customer was unable to understand what was occurring in his or her account.

There are a number of steps that may be taken to address the issue:

- Contact the Trusted Contact Person
- Have a conversation with the customer with the branch manager or other supervisor present to assist in making a determination.
- Raise the issue with family members and determine if the customer has given power of attorney to another person.
- Document meetings, conversations, and other exchanges with relatives about the situation.
- Document communications with the customer about investments.
- As a final alternative, decide not to continue doing business with the customer.

Contact Compliance with questions about a proper course of action.

11.11.5 Potential Indication of Elder Financial Exploitation

[FinCEN Advisory FIN-2011-A003: <https://www.fincen.gov/news/news-releases/memorandum-financial-institution-and-law-enforcement-efforts-combat-elder>]

This section includes an excerpt from a FinCEN advisory. This information provides guidance to RRs and other associated persons when handling accounts for elderly customers. Questions regarding potential elder abuse should be referred to your supervisor or Compliance.

The following red flags could indicate the existence of elder financial exploitation. This list of red flags identifies only possible signs of illicit activity. Financial institutions should evaluate indicators of potential financial exploitation in combination with other red flags and expected transaction activity being conducted by or on behalf of the elder. Additional investigation and analysis may be necessary to determine if the activity is suspicious.

Financial institutions may become aware of persons or entities perpetrating illicit activity against the elderly through monitoring transaction activity that is not consistent with expected behavior. In addition, financial institutions may become aware of such scams through their direct interactions with elderly customers who are being financially exploited. In many cases, branch personnel familiarity with specific victim customers may lead to identification of anomalous activity that could alert bank personnel to initiate a review of the customer activity.

- Erratic or unusual banking transactions, or changes in banking patterns:
 - Frequent large withdrawals, including daily maximum currency withdrawals from an ATM;
 - Sudden Non-Sufficient Fund activity;
 - Uncharacteristic nonpayment for services, which may indicate a loss of funds or access to funds;
 - Debit transactions that are inconsistent for the elder;
 - Uncharacteristic attempts to wire large sums of money;
 - Closing of CDs or accounts without regard to penalties.
- Interactions with customers or caregivers:
 - A caregiver or other individual shows excessive interest in the elder's finances or assets, does not allow the elder to speak for himself, or is reluctant to leave the elder's side during conversations;
 - The elder shows an unusual degree of fear or submissiveness toward a caregiver, or expresses a fear of eviction or nursing home placement if money is not given to a caretaker;
 - The financial institution is unable to speak directly with the elder, despite repeated attempts to contact him or her;
 - A new caretaker, relative, or friend suddenly begins conducting financial transactions on behalf of the elder without proper documentation;
 - The customer moves away from existing relationships and toward new associations with other "friends" or strangers;
 - The elderly individual's financial management changes suddenly, such as through a change of power of attorney to a different family member or a new individual;

- The elderly customer lacks knowledge about his or her financial status, or shows a sudden reluctance to discuss financial matters.

11.11.6 Escalating Issues Involving Senior Investors

When dealing with senior investors, there may be changes or events that require escalation of an issue to the RR's designated supervisor and/or Compliance. Following are some issues that may require escalation for handling. Any questions regarding dealing with senior investors should be referred to Compliance.

- Suspected elder abuse including financial abuse (contacting appropriate state or other authorities may be necessary; confer with Compliance regarding such referrals)
- Suspected diminished capacity

Having the RR's designated supervisor or Compliance make direct contact with the investor or Trusted Contact Person may be appropriate.

11.11.7 Financial Exploitation - Temporary Holds

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests for temporary holds
Frequency	<ul style="list-style-type: none"> • As required: requests for holds • Within 2 business days of the hold, notify the Trusted Contact Person and all parties authorized to transact business for the account (including the customer)
Action	<ul style="list-style-type: none"> • Immediately review the facts and circumstances surrounding the requested hold including confirming the customer is a Specified Adult • Notify (written or oral) the Trusted Contact Person, the customer, and other authorized persons. No obligation to notify if the Trusted Contact Person or authorized party is unavailable or the Firm believes is engaged in the financial exploitation • Remove the hold no later than 15 business days after placed or extend for 10 additional business days unless subject to a regulatory or court action • Include protection of Specified Adults and account hold requirements/procedures in employee training
Record	<ul style="list-style-type: none"> • Hold requests including internal reviews and action taken and name/title of associated person requesting the hold • Notifications • New account records including required information under Rule 4512.06 • Training records including date, how administered, who attended, content

To protect certain customers, the Firm may place temporary holds on disbursements of funds or securities from the account of Specified Adults. When an RR or other employee suspects potential or ongoing financial exploitation, the designated supervisor (or another supervisor, if the designated supervisor may be involved) should immediately be notified to consider placing a hold on the account.

11.11.7.1 Definitions

"Specified Adult" means: (A) a natural person age 65 and older; or (B) a natural person age 18 and older who the Firm reasonably believes has a mental or physical impairment that renders the individual unable to protect his or her own interests.

"Account" means any account for which a Specified Adult has the authority to transact business.

"Trusted Contact Person" means the person who may be contacted about the Specified Adult's account in accordance with FINRA Rule 4512.06. At time of account opening, this is a person that may be contacted on behalf of the customer to address possible financial exploitation and confirm other information. This applies to accounts for "Specified Adults" defined above.

"Financial Exploitation" means:

- the wrongful or unauthorized taking, withholding, appropriation, or use of a Specified Adult's funds or securities; or
- any act or omission by a person, including through the use of a power of attorney, guardianship, or any other authority regarding a Specified Adult, to:
 - obtain control, through deception, intimidation or undue influence, over the Specified Adult's money, assets or property; or
 - convert the Specified Adult's money, assets or property.

11.11.7.2 Temporary Holds

RRs (or another employee) should forward requests to the designated supervisor in writing including account name, number, age of customer, and reason for requesting the hold. The following guidelines apply.

- A temporary hold on a disbursement may be placed if the Firm reasonably believes that financial exploitation of the adult has occurred or is occurring, has been attempted or will be attempted.
- The Firm will make an attempt to resolve the matter with the customer before placing a hold, unless doing so would cause further harm to the customer.
- The hold may be placed on suspicious disbursements but not on other non-suspicious disbursements.
- Holds do not apply to securities transactions, i.e., a customer's sell order. A hold may be made on the disbursement of the sale proceeds where there is reasonable belief of financial exploitation.
- A customer's objection or information obtained from the Trusted Contact Person may be used in determining whether the hold should be placed or lifted.
- The temporary hold expires no later than 15 business days after first imposed unless terminated or extended by an order of a state regulator or agency or court. The Firm may also extend the hold for an additional 10 business days.

11.11.8 New Accounts for Specified Adults

At the time an account is opened for a Specified Adult, information should be obtained regarding a Trusted Contact Person. The customer will be notified in writing (including electronically) that the Firm or an associated person is authorized to contact the Trusted Contact Person to disclose information about the customer's account and possible financial exploitation. For accounts opened prior to this Rule requirement, notification will be provided when updating account information.

Failure to obtain Trusted Contact Person information does not prevent the opening and maintaining of the account but reasonable efforts must have been taken to obtain the information; failure to obtain the information should be documented in the account records.

11.11.9 Use of Titles Inferring Expertise – Senior Designations

[NASAA Model Rule on the Use of Senior-Specific Certifications and Professional Designations]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • RR requests to use titles • Information regarding outside organizations that confer titles • Correspondence and retail communications
Frequency	<ul style="list-style-type: none"> • As required - review requests • Daily and ongoing - review of correspondence/communications
Action	<ul style="list-style-type: none"> • Review requests for use of special titles/designations: <ul style="list-style-type: none"> ○ Review any outside organization conferring designations for appropriate qualifications such as internal ethics policies, criteria for conferring designations ○ Review the RR requesting the title for qualifications including experience, completion of continuing education with CEI and regulatory/compliance history ○ Determine state requirements that regulate the use of designations • For those approved to use titles, notify the RR's supervisor who is responsible for review of correspondence and retail communications to determine proper use of title • Notify RR and supervisor if approval is withdrawn due to failure to complete necessary education requirements or other requirements
Record	<ul style="list-style-type: none"> • Review of outside organizations • Review of RRs • Approval or disapproval of correspondence and retail communications, other actions taken

RRs may use special titles indicating expertise when dealing with senior investors under the following requirements:

- A request to use a title must be provided to Compliance **prior to use** including the name and address of any outside organization conferring such titles based on meeting the organization's requirements.
- Titles may not be self-conferred, *i.e.*, the title must be based on some criteria or qualification met.
- The RR must be in good standing with the organization that confers the designation.
- The RR must be current on any continuing education requirements of the outside organization.

- The RR must complete firm training specifically relating to dealing with senior investors which may include retirement planning; ethics when working with senior investors; and the proper use of senior designations in correspondence, retail communications and seminars/luncheons.
- Business cards/letterhead are limited to that which is centrally issued by CEI; RRs may not create their own cards or letterhead.
- Compliance will review the request and notify the RR and the RR's supervisor if the request is approved or disapproved.
- Titles may be used only after Compliance approval.
- RRs who use senior designations must attest on the *Annual Employee Certification* their compliance with requirements.

11.11.10 Reverse Mortgages

[FINRA Investor Alert: Reverse Mortgages, Avoiding a Reversal of Fortune]

A reverse mortgage is an interest-bearing loan secured by the equity in a home. Generally the borrower and any other co-borrowers (such as a spouse) must own the home and be 62 or older (some lenders may have other criteria). Home equity may be converted to cash that can be used for any purpose. The homeowner makes no interest or principal payments during the life of the loan; interest is added to the principal. Unless the loan is a fixed-term loan, the loan only becomes due when the homeowner dies, sells the home, or otherwise leaves the home for more than 12 months. If any of these events occur, the borrower or heirs must repay the loan, including compounded interest, in full. Usually the home is sold and the loan is paid from proceeds of the sale.

RRs are not permitted to recommend customers use reverse mortgages to fund investments. If a customer indicates he or she has funds available for investment from the proceeds of a reverse mortgage, the following is required.

1. Provide the customer with a copy of the FINRA Investor Alert *Reverse Mortgages: Avoiding A Reversal of Fortune*. Obtain a letter from the customer acknowledging receipt of the Alert.
2. Consult with the customer about investment objectives and the need for the proceeds as living expenses.
3. Recommend investments consistent with those needs; most investments should be conservative and suitable for someone with a limited lifespan and potentially facing expenses for health issues.
4. Recommendations other than conservative investments must be approved by the designated supervisor **prior to** making the investments. Provide the supervisor with a copy of the new account information and a written explanation of funds available, the needs of the investor, and how they are to be invested.

11.11.11 Luncheon Programs and Seminars

[SEC/NASAA report on free lunch seminars: <http://www.sec.gov/spotlight/seniors/freelunchreport.pdf>]

programs and seminars are a common approach to reach investors and have become particularly popular in soliciting senior investors. These programs, as for all public speaking, require the approval of the Advertising Supervisor including submission of the invitation, any related advertisement, an outline of subjects to be covered and copies of materials to be distributed or shown in presentations (slide shows, Power Point presentations, etc.).

Luncheon programs cannot infer that no products will be sold or mislead invitees as to the purpose of the luncheon. Products offered must be suitable for the target audience and the suitability of any recommendation must be considered for each investor individually.

- Complete the Public Speaking/Seminar/Luncheon Request form and submit to the designated supervisor at least 3 weeks prior to the event, to ensure timely review.
- Attach materials to be provided to attendees as well as proposed advertising of the event.

11.11.12 Advertising Targeting Seniors

Advertising that targets seniors must be balanced and may only include products or services suitable for senior investors. All advertising must be approved by the Advertising Supervisor prior to publication or distribution.

11.12 Incompetent Persons

Accounts for incompetent persons may only be opened with the appropriate authority from a court-appointed guardian. If an RR becomes aware that a customer has become incompetent, the RR should contact the designated supervisor or Compliance for further guidance.

If a customer becomes incompetent while a third-party trading authorization is in effect for his or her account, the authority generally is considered invalid and requires a court order for reinstatement. "Durable" powers of attorney, recognized by some states, remain in effect after a person is declared incompetent. Questions should be referred to Compliance.

11.13 Trust Accounts

New accounts for trusts require a copy of the trust agreement or a trust certification signed by the authorized trustee. The following activities in trust accounts require **prior** approval as follows:

- Margin trading requires approval by Compliance
- Option trading requires approval by Compliance
- Discretionary accounts require approval by Compliance (if CEI permits discretionary accounts)

Fiduciaries (executors, trustees, guardians, administrators, conservators, *etc.*) may not be able to delegate their duties to a third party (whether the RR or an outside person) to manage the account unless the trust or other authorizing instrument specifically permits delegation. Some states require the fiduciary to obtain a court order to delegate authority to a third party.

11.14 Registered Persons (RRs) Being a Customer's Beneficiary or Holding a Position of Trust

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Notices to act in a role subject to Rule 3241• Communications indicating activity subject to Rule 3241
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Review notices considering the information provided by the RR to assess the risks including:<ul style="list-style-type: none">○ whether the activity will interfere with or compromise the RR's responsibilities to the customer○ whether the RR will derive financial gain other than customary fees or other reasonable charges○ whether the RR assuming such status does not present a risk of financial exploitation of the customer○ whether the activity should be approved or disapproved

	<ul style="list-style-type: none"> • Consider whether to discuss the potential beneficiary status or position of trust with the customer • Determine whether to approve or disapprove and, if approved, whether any conditions or limitations will apply • Notify the RR and the RR's supervisor in writing of the determination and any special supervision or conditions or limitations
Record	<ul style="list-style-type: none"> • Request and review on Firm's Rule 3241 Form (Beneficiary Request Form) • Determination whether to disapprove or approve and any conditions or limitations • Retain such record for at least 3 years after the beneficiary status or position of trust is terminated

RRs are limited from being named a beneficiary, executor or trustee, or having a power of attorney or similar position of trust for or on behalf of a customer^{*}. The RR is responsible for immediately notifying his or her supervisor of any such potential designation. The notice requirement includes RRs who hold a beneficiary or position of trust status for an account transferring from a prior employer; the transferring RR must provide notice within 30 days of employment.

These limitations do **not** apply where the customer is a member of the registered person's "immediate family"^{**}. In addition, a registered person who does not have customer accounts assigned to him/her is not subject to these requirements.

Exceptions to this limitation must be requested, in writing, from his/her supervisor using the Firm's Rule 3241 Form (Beneficiary request Form). The request must include the name(s) of the customer's account(s) and in what role the registered person will act (beneficiary, executor, trustee, etc.) as well as the following:

- length and type of relationship between the customer and the registered person
- the customer's age
- the size of any bequest relative to the size of the customer's estate
- any remuneration to be paid to the RR
- any customer mental or physical impairment that renders the customer unable to protect his or her own interests

Registered persons may **not** accept such a role without **prior** approval from his/her supervisor. In addition, a registered person may not instruct or ask a customer to name another person, such as the registered person's spouse or child, to be a beneficiary of the customer's estate or to receive a bequest from that estate.

In the event a registered person unknowingly becomes the subject of these limitations (*e.g.*, notification of receiving a bequest, being named an executor, etc.), the registered person is obligated to decline the role or bequest unless written notice is provided to his/her supervisor and approval is received.

*"Customer" under this Rule includes any customer that has, or in the previous six months had, a securities account assigned to the registered person including a brokerage account, mutual fund account or variable insurance product account and accounts held directly at a mutual fund or variable insurance product issuer. It also includes someone who is a customer of another broker-dealer which subjects the activity to Rule 3241 on limitations explained in this section as well as Rule 3270 regarding outside business activities.

**For purposes of Rule 3241, "immediate family" includes parents, grandparents, in-laws, spouse or domestic

partner, sibling, children, grandchildren, first cousin, aunt or uncle, niece or nephew, and any other person who resides in the same household as the registered person and the registered person financially supports, directly or indirectly, to a material extent, and including step and adoptive relationships.

11.15 Correspondent and Private Banking Accounts and Accounts for Senior Foreign Political Figures

[Bank Secrecy Act 31 CFR Chapter X Part 1010 Subpart F; USA PATRIOT Act Section 312 and 313]

Under anti-money laundering (AML) rules, there are special requirements that apply to "correspondent" and "private banking" accounts as well as to accounts for "senior foreign political figures." Definitions of these and other terms follow the summary of requirements. Questions should be referred to the AML Compliance Officer.

11.15.1 Summary of Requirements

- Correspondent accounts require due diligence to determine ownership of the account.
- Accounts cannot be opened for foreign shell banks.
- When opening an account for a foreign bank, the Foreign Bank Certification form must be submitted to the AML Compliance Officer with the New Account Form for review and approval.
- Every three years foreign banks will be required to re-certify the information in the Foreign Bank Certification.
- When opening an account for a senior foreign political figure, the new account application must be submitted to the AML Compliance Officer for review and approval.

11.15.2 Definitions

Correspondent account: Includes any account established for a foreign financial institution to receive deposits from, or to make payments or other disbursements on behalf of, the foreign institution, or to handle other financial transactions related to such foreign financial institution. This type of account presumes a formal relationship through which the financial institution provides regular services. Due diligence requirements apply to correspondent accounts maintained for the following foreign financial institutions:

- Foreign bank
- Foreign branch of a U.S. bank
- Business organized under a foreign law that, if located in the U.S., would be a securities broker-dealer, futures commission merchant, introducing broker in commodities, or a mutual fund
- Money transmitter or currency exchanger organized under a foreign law

Private banking account: A private banking account is an account that is established or maintained for the benefit of one or more non-U.S. persons, requires minimum aggregate deposit of funds or other assets of not less than \$1,000,000, and is assigned to a bank employee who is a liaison between the financial institution and the non-U.S. person. If the account otherwise satisfies the definition but the institution does **not** require a minimum balance of \$1,000,000, the account does not qualify as a private banking account.

Senior foreign political figure includes:

- a current or former senior official in the executive, legislative, administrative, military, or judicial branches of a foreign government, whether or not they are or were elected officials
- a senior official of a major foreign political party

- a senior executive of a foreign government-owned commercial enterprise (Senior executives are individuals with substantial authority over policy, operations, or the use of government-owned resources.)
- immediate family members of the above, and those who are widely and publicly known (or actually known) close associates of a senior foreign political figure
- a corporation, business, or other entity formed by or for the benefit of one of the above individuals

Proceeds of foreign corruption: any asset acquired by, through, or on behalf of a senior foreign political figure through misappropriation, theft, or embezzlement of public funds, the unlawful conversion of property of a foreign government, or through acts of bribery or extortion, and include any other property into which any such assets have been transformed or converted.

Foreign bank: a bank organized under foreign law, or an agency, branch, or bank office located outside the United States. The term does not include an agent, agency, branch or office within the U.S. of a bank organized under foreign law.

Foreign shell bank: is defined as a foreign bank without a physical presence in any country.

Regulated affiliate: is a foreign shell bank that (1) is an affiliate of a depository institution, credit union, or foreign bank that maintains a physical presence in the United States or a foreign country, as applicable; and (2) is subject to supervision by a banking authority in the foreign country regulating such affiliated depository institution, credit union, or foreign bank.

11.15.3 Prohibition Against Correspondent Accounts for Foreign Shell Banks

CEI is prohibited from establishing, maintaining, administering, or managing a correspondent account in the United States for an unregulated foreign shell bank. The prohibition does not apply to a foreign shell bank that is a regulated affiliate. If an account is inadvertently opened for an unregulated foreign shell bank, the AML Compliance Officer should be notified and the account will be immediately closed.

11.15.4 Foreign Bank Certification

When opening an account for a foreign bank, CEI is obligated to ensure the bank is not a foreign shell bank and must obtain information about the foreign bank's owners and an agent for service of process. The bank must complete the Foreign Bank Certification which must be submitted to the AML Compliance Officer with a copy of the New Account Form for review. Every three years the bank is also required to re-certify the information filed with CEI.

11.15.5 Accounts for Foreign Political Figures

Accounts for foreign political figures (as defined above) are subject to special reviews to comply with Bank Secrecy Act requirements. RRs are required to identify, on the new account application, whether an account for a foreigner falls under the definition. The application must be submitted to the AML Compliance Officer for review and approval by the designated supervisor before he or she approves/accepts the account.

11.16 Collateral/Escrow Accounts

Accounts for customers where the assets in the account are pledged to a third party and CEI is asked to acknowledge it is responsible for holding the assets pending instructions from the third party, must be approved by a principal of the firm after review of the collateralization agreement. Such accounts must be restricted.

CEI will not accept an escrow account wherein CEI undertakes an obligation as escrow agent.

11.17 Wealth Events

Wealth events refer to those situations where an investor faces the decision about what to do with a large amount of money arising from an inheritance, life insurance payout, sale of a business or other major asset, divorce settlement or an IRA rollover, among other events. RRs must consider the following when advising a customer about investing such funds:

- Many wealth events have tax consequences. RRs are prohibited from providing tax advice; the customer should be advised to contact their tax adviser.
- Suitability requirements are important and must be considered by the RR prior to making any recommendation.
- RRs may not infer that the customer's only choice or sound option is rolling funds to an IRA managed by CEI; also, IRAs cannot be represented as "free" or without cost or fees.
- Regulation Best Interest applies to the account recommendation: See Chapter Regulations Best Interest
- If the investor is a Retirement Investor defined by the DOL, a fiduciary obligation will apply
- A Rollover Best Interest Form is required to be completed and signed by the Retirement Investor

11.18 Pension and Retirement Accounts

This section is divided into four areas:

1. A general explanation of ERISA requirements
2. General guidelines when offering retirement plans
3. Individual plans established and funded by the investor
4. Employer-sponsored plans

Because of frequent changes to laws affecting contribution levels and other requirements or limitations, some details are not included in these general explanations; individual plans should be referenced for details.

Questions regarding retirement accounts should be referred to the appropriate marketing specialist or to Compliance.

11.18.1 Employee Retirement Income Security Act (ERISA)

This section provides a general overview of ERISA and how it affects pension and retirement accounts; it does not deal with the complex legal requirements of the Act. Legal counsel should be consulted regarding questions about ERISA and its effect on pension or retirement accounts.

11.18.1.1 Introduction

The Employee Retirement Income Security Act of 1974 (ERISA) is a federal law that sets minimum standards for most voluntarily established pension and health plans in private industry and provides protection for individuals in these plans.

ERISA applies to all Internal Revenue Service-qualified pension and profit sharing plans and employee welfare benefit plans. Most IRA accounts, while not covered by ERISA, are subject to the prohibited transaction penalties. Limited exemptions apply to governmental (public employee) plans and certain offshore and church plans.

This section provides a general overview of ERISA. Because of the technical and legal nature of ERISA, questions should be referred to Compliance or legal counsel.

11.18.1.2 Key Definitions

A "fiduciary" is generally anyone with discretionary authority or control over the management of a plan, the administration of the plan, or the disposition of plan assets. Fiduciaries must comply with certain statutory duties which include prudence and diversification of investments and the duty to act in accordance with the governing instruments of the plan.

A person or entity providing services to an ERISA plan is considered a "party-in-interest" to the plan. This status generally applies to broker-dealers providing traditional brokerage services to ERISA plans. CEI's role in relation to ERISA plan accounts generally is as a party-in-interest unless CEI contracts to provide investment management services or other services where CEI would become a fiduciary to an ERISA plan.

11.18.1.3 Permissible Transactions

Generally, trading in ERISA accounts is subject to the "Prudent Investor Rule" which is discussed in the next section. Allowable transactions are governed by ERISA (and related Department of Labor and IRS rulings), the investment policy of the ERISA plan, and trading guidelines in a managed account program or other trading program if such a program is used.

Some types of transactions (such as margin or certain option transactions) are associated with added risk, and it may be necessary for Compliance to review the plan to determine whether the type of transaction is permissible.

11.18.1.4 Prudent Investor Rule and Diversification

Trading in ERISA accounts is subject to the "prudent investor" rule (also known as the Prudent Man Rule) which is a standard that is generally understood to mean that individuals involved with investment decision-making act with the same care, skill, prudence and diligence as a prudent man in the same capacity. This measure is not judged on the risk of a single investment but by the investment's relationship to the overall portfolio.

ERISA also requires that investments in a covered plan be diversified to minimize the risk of large losses unless it is clearly prudent not to do so.

11.18.1.5 Prohibited Transactions

Federal laws prohibit plan assets from being used by a fiduciary for certain transactions (known as "prohibited transactions"). Fiduciaries are prohibited from dealing in plan assets for their own benefit or for the benefit of a third party with whom the fiduciary is affiliated. The Department of Labor (and other government agencies) have issued exemptions from the prohibited transaction rules which allow plans and broker-dealers to engage in some but not all types of securities transactions. The range of permissible transactions varies depending on whether the broker-dealer is a fiduciary to the plan.

11.18.1.6 General Requirements When Dealing with ERISA Plans

Because of substantial legal liability, RRs are not permitted to become fiduciaries when dealing with ERISA accounts (unless CEI has a specific program designed to meet legal requirements in offering those services). The following summarizes requirements and limitations:

- RRs may not accept responsibilities regarding administration of a plan (other than following instructions for contributions, distributions and investments from authorized persons acting on behalf of the plan).
- RRs may not be named trustees to plans (unless specifically authorized by Compliance).
- Recommendations to ERISA plans must be consistent with investment policies of the plans.
- Trading on margin does not generally occur in ERISA accounts; Compliance approval is required prior to engaging in margin transactions in an ERISA account.

11.18.1.7 Disclosures to Plans

[ERISA Section 408(b)(2); Dept. of Labor Fact Sheet: <https://www.dol.gov/newsroom/releases/ebsa/ebsa20120507>]

Responsibility	<ul style="list-style-type: none"> • Registered Representative
Resources	<ul style="list-style-type: none"> • Plan contracts or arrangements • Information regarding services provided and charges for services
Frequency	<ul style="list-style-type: none"> • Disclosures - reasonably in advance of the date the contract or arrangement is entered into and extended or renewed • Changes or errors in disclosures - as required (see below)
Action	<ul style="list-style-type: none"> • Identify plans and services subject to 408(b)(2) requirements • Assemble information necessary to make required disclosures • Provide disclosures at time of initial contract/arrangement and when changed, errors are identified, or contracts/arrangements are terminated • Respond to fiduciaries/plan administrators when additional information is requested
Record	<ul style="list-style-type: none"> • Covered plans • Disclosures provided including dates provided

Under ERISA, "covered service providers" are required to provide fee disclosures to covered plans to enable the plan fiduciary to make an informed decision about the reasonableness of fees as required under ERISA Section 404(a)(1). CEI's obligation to provide disclosures depends on CEI's role in dealing with a covered plan. This section provides a general explanation of the requirements which are complex; the ERISA section should be consulted for specific requirements.

11.18.1.7.1 Definitions

Covered plan: An ERISA-covered defined benefit and defined contribution pension plan. Does not include simplified employee pension plans (SEPs), SIMPLE retirement accounts, IRAs, employee welfare benefit plans, and certain annuity contracts and custodial accounts described in ERISA Code section 403(b).

Covered service provider: A service provider that enters into a contract or arrangement with the covered plan and expects \$1,000 or more in direct or indirect compensation that is received in connection with providing services defined in Section 408(b)(2) including:

- ERISA fiduciary service providers to a covered plan or to a "plan asset" vehicle in which such plan invests
- Investment advisers registered under Federal or State law
- Record-keepers or brokers who make designated investment alternatives available to the covered plan (e.g., a "platform provider")
- Providers of one or more of the following services to the covered plan who also receive "indirect compensation" in connection with such services:
 - Accounting, auditing, actuarial, banking, consulting, custodial, insurance, investment advisory, legal, recordkeeping, securities brokerage, third party administration, or valuation services

11.18.1.7.2 Required Disclosures

Disclosures include:

- Description of services
- If applicable, that the services are provided in the role of fiduciary
- Compensation, including:
 - Description of all direct compensation either in aggregate or by service to be received
 - Indirect compensation expected to be received
 - Description that compensation will be paid among related parties including identification of payers and recipients of compensation
 - Description of any compensation to be received in connection with termination of the contract or arrangement and how any prepaid amounts will be calculated and refunded upon termination
- Recordkeeping services, if applicable, including direct and indirect compensation related to such services or, if not explicitly compensated, a reasonable and good faith estimate of the cost to the covered plan of such services
- Manner of receipt of the compensation
- Fiduciary services provided and related compensation
- Recordkeeping and brokerage services with respect to each designated investment alternative for which recordkeeping or brokerage services are provided

11.18.1.7.3 Timing of Disclosures

- Required disclosures must be provided reasonably in advance of the date the contract or arrangement is entered into and extended or renewed.
- Changes must be provided as soon as practicable but no later than 60 days from the date on which the covered service provider is informed of the change.
- In the event of an error in a disclosure, the covered service provider must correct the information as soon as practicable but no later than 30 days after knowing of the error or omission.
- Requests for other compensation information from the fiduciary or covered plan administrator must be provided within 30 days following receipt of a written request.

11.18.1.8 Disclosures to Plan Participants

[ERISA Section 404(a)(5); SEC no-action letter to the Department of Labor dated October 26, 2011: <https://www.dol.gov/newsroom/releases/ebsa/ebsa20120507-0>; FINRA Regulatory Notice 12-02]

Responsibility	<ul style="list-style-type: none"> Registered Representative
Resources	<ul style="list-style-type: none"> Plans for participant-directed individual account plans Performance and cost information required to be disclosed
Frequency	<ul style="list-style-type: none"> As required
Action	<ul style="list-style-type: none"> Determine if CEI and any firm-prepared materials for plan participants are subject to disclosure requirements Assemble information necessary to make required disclosures If subject investments are investment companies, contact Compliance to determine whether materials must be filed with FINRA (written materials that conform to the ERISA rule requirements are not required to be filed per the SEC no-action letter) Provide disclosures to participants or to plan administrator for distribution to participants
Record	<ul style="list-style-type: none"> Disclosures provided including when and to whom provided

ERISA Rule 404(a)(5) requires the disclosure of certain plan and investment-related information, including performance information, to participants and beneficiaries in participant-directed individual account plans. Information is required to be presented in a comparative chart format to enable participants to make an informed decision when managing their accounts.

If CEI compiles and/or provides the required information, it will comply with the requirements of Rule 404(a)(5). Where the investment alternatives include investment companies subject to other SEC and FINRA rules regarding communications with the public, the disclosures will comply with those requirements or exemptions to requirements.

11.18.2 General Guidelines when Offering Retirement Plans

Plans differ depending on the law under which they are established. Differences include limits on contributions, tax deductibility, costs, types of plan sponsors (employer or otherwise), and who may participate. The following sections provide general explanations of various types of common retirement accounts. Some of the general guidelines that apply to retirement plan sales include the following. Specific plans should be consulted for limitations and requirements.

- Avoid tax-sheltered investments such as annuities and municipal securities, which generally are not suitable for retirement plans since plans already provide tax benefits.
- Consider the cost of investments recommended for retirement plans vs. the benefits.
- Consider the customer's risk profile and investment objectives when considering securities for recommendation for a retirement plan.
- Consider surrender or exit fees or tax penalties if they apply to the potential transaction.
- Understand the type of plans being discussed or recommended.
- Encourage investors to contact their tax counsel to resolve any tax-related questions.

11.18.3 Individual Retirement Accounts (IRAs)

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Plan applications • New account applications • Transaction reports • Proposed marketing presentations
Frequency	<ul style="list-style-type: none"> • As required - opening accounts • As required - review and approve/disapprove marketing presentations • Daily - review of transactions • Ongoing - provide training
Action	<ul style="list-style-type: none"> • Review applications/new account forms for consistency of investment objectives with proposed investments/rollovers • Review transactions for consistency with investment objectives and take corrective action when necessary which may include contact with RR to discuss transactions vs. objectives; contact with customer; contact with Compliance; adjustments to current or future investments • Review marketing presentations/seminar presentations regarding accuracy of information to be presented, experience/knowledge of RR making presentation and approve (making adjustments if necessary or disapprove) • Provide training when new plans/products are offered to retirement accounts and when 401(k) plan participants will be targeted for marketing efforts
Record	<ul style="list-style-type: none"> • Plan/new account documents • Transactions reviewed including notes of action taken, if any • Marketing presentations/seminars with approval or disapproval • Records of training regarding products/services, who attended, and when training was provided

IRAs are established by individuals through a plan sponsor; following are key features:

- Annual contributions are limited by law
- Older investors have higher contribution limits under a "catch-up" provision
- Contributions may or may not be tax deductible, depending on the IRA owner's income level
- Contributions are from earned income (other than contributions to a non-working spouse's IRA)
- Certain types of investments such as precious metals are not permitted in an IRA
- Early withdrawals (prior to age 59 1/2) may result in tax penalties
- Owners of traditional IRAs are required to begin withdrawing by the year following the year the owner turns 70 1/2

There are multiple types of IRAs including:

- Traditional IRAs; contributions may or may not be tax deductible depending on the IRA owner's income

- Roth IRA:
 - all contributions are in after-tax dollars
 - withdrawals are not taxed at the time of withdrawal if the IRA owner is at least 59 1/2 years old and the Roth IRA has been open 5 years or longer
 - some high wage earners are not eligible to open Roth IRAs
 - no mandatory withdrawals after age 70 1/2
- Individual retirement annuity; a traditional or Roth IRA set up with a life insurance company through the purchase of a special annuity contract
- Simplified Employee Pension (SEP-IRA); a traditional IRA set up by an employer for employees; limitations on contributions apply
- Spousal IRA; traditional or Roth IRA funded by a married taxpayer in the name of a spouse (who has limited earnings)
- Rollover IRA: funded with money that is already in a qualified retirement plan; allows moving the money without owing any tax at the time of the rollover (assuming the requirements for a rollover are met)

11.18.3.1 Rollovers

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Rollovers
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Review rollovers for: <ul style="list-style-type: none"> ○ Conflict of interest earning commissions vs. fees and what is more appropriate for the customer ○ Suitability • Include in training
Record	<ul style="list-style-type: none"> • Review of rollovers and action taken • Rollover Disclosure Form

CEI and its RRs have responsibilities when recommending a rollover or transfer of assets in an employer-sponsored retirement plan to an IRA and when marketing IRAs and associated services. A plan participant leaving an employer has typically four options (which may include a combination of options):

- Leave the money at the employer's plan, if permitted
- Roll over assets to a new employer's plan, if available and permitted
- Roll over to an IRA
- Cash out the account value

When recommending a rollover to an IRA, some considerations include the following:

- Recommendations to open an IRA or rollover workplace retirement plan assets into an IRA rather than keeping assets in a previous employer's workplace retirement plan (or rolling over assets to a new employer's workplace retirement plan) are subject to Regulation Best Interest which identifies many of the following considerations and adds as considerations holdings of employer stock and any special features of the existing account.

- Investment options may be broader in an IRA, but the customer may be satisfied with options under an employer plan.
- Fees and expenses may be higher for an IRA; an employer may pay fees and expenses in its plan; IRA fees may include administrative, account set-up and custodial fees.
- Services may differ between employer plans and various IRAs; such services include planning tools, telephone help lines, workshops, educational material, *etc.*
- Penalty-free withdrawals are available from an employer plan to an employee leaving a job between age 55 and 59 1/2, and it may be easier to borrow from the plan. Such withdrawals may be made from an IRA only after the investor reaches the age of 59 1/2.
- Unlimited protection from creditors and legal judgments is available to plan assets under federal law. IRA assets are protected in bankruptcy only; state laws vary in protecting IRAs in lawsuits.
- Required minimum distributions apply to individuals reaching the age 70 1/2 for both plans and IRAs. However, if the individual continues working past 70 1/2, minimum distributions from the current employer's plans are delayed past 70 1/2.
- Appreciated employee stock in a plan will be subject to negative tax consequences of taxation at ordinary income tax rates vs. long term capital gains if rolled into an IRA. A balancing factor is if the employee is overly-concentrated in the employer stock and is unable to reduce exposure in the plan.
- IRAs cannot be promoted as "no-fees" since the term could mislead investors who typically pay fees in some way to maintain an account. For example, the cost of a "no-fee" account may be subject to higher commissions instead of highlighted as a separate charge. This promotional strategy could attract investors into a rollover that may ultimately be more costly than staying in an employer plan.

RRs have the obligation to consider the suitability of any recommended rollover considering the above factors and others that may apply to the customer and the customer's investment objectives, tax situation, and finances.

Explanation of the reason and justification for a rollover must accompany the rollover transaction. **Furthermore, the RR is required to obtain a client-signed copy of the Rollover Disclosure Form for the file, and supervisors shall not approve new IRA accounts funded by a rollover without a signed copy of the Rollover Disclosure Form. Supervisors shall evidence review of the Form by initialing and dating.**

11.18.4 Employer-Sponsored Plans

Employers may offer different types of plans including traditional pension and profit-sharing plans that are funded entirely by the employer. All eligible employees participate and employer contributions are above and beyond the employee's salary. This section describes other types of employer-sponsored plans that give eligible employees the opportunity to put a portion of current income into a tax-deferred investment account. Participation may be voluntary or mandatory, and employers may make matching contributions.

The following sections provide a general explanation of these various plans.

11.18.4.1 401(k) Plans

- Established by corporations
- Permit their employees to make contributions through payroll deductions from pre-tax income [traditional 401(k) plans]; tax is applied when withdrawals are taken
- Roth 401(k) plans permit employees to make contributions through payroll from after-tax dollars; there is no tax on withdrawals made after age 59 1/2 and if the Roth 401(k) has been open 5 years or longer
- Both traditional and Roth 401(k) plans can be rolled over to an IRA (or a new employer's plan, if the plan permits) if the investor leaves the company

- No mandatory withdrawals for Roth 401(k) plans; mandatory scheduled withdrawals apply to traditional 401(k) plans

11.18.4.1.1 Limitations on Advice

[Pension Protection Act of 2006 Title VI; U.S. Department of Labor Field Assistance Bulletin No. 2007-01]

Providing investment advice to 401(k) plan sponsors and participants is subject to strict limitations and requirements. Providing investment advice places the RR in the role of a fiduciary which creates the legal liabilities associated with fiduciaries.

RRs are limited to offering firm-approved educational material and third-party advisory plans offered through CEI.

11.18.4.2 403(b) Plans

[IRS 403(b) publication: <http://www.irs.gov/publications/p571/cho1.html>]

A 403(b) plan is a salary reduction plan offered by non-profit, tax-exempt employers such as schools and colleges, hospitals, and foundations. Individual accounts in a 403(b) plan invest in two categories of investments:

- An annuity contract provided through an insurance company (fixed or variable)
- Mutual funds

Features include:

- Individuals cannot establish 403(b) accounts; only employers may set up accounts
- For non-Roth plans:
 - Employees make pre-tax contributions and employers sometimes match contributions
 - Tax on contributions and earnings and gains on investments are paid when the investor begins withdrawing funds
 - Mandatory withdrawals after age 72 (70 ½ if you reach 70 ½ before January 1, 2020)
- If the plan is a Roth contribution plan, tax is paid on contributions to the plan but withdrawals are not taxed; no mandatory withdrawals
- Some 403(b) plans impose steep surrender charges

11.18.4.3 457 Plans

These plans are offered by a state or local government or a non-profit organization. A 457 plan is a deferred compensation plan similar to 401(k) or 403(b) plans.

- Pre-tax income is contributed
- No tax on contributions; withdrawals are subject to tax
- Technically the portion of salary contributed to the plan is not owned by the employee; the plan sponsor owns all of the 457 plan assets which are held in trust for the employee in an account set up in the employee's name
- Mandatory withdrawals after age 72 (70 ½ if you reach 70 ½ before January 1, 2020)
- No early withdrawal tax penalties if funds are paid to the employee when leaving the job prior to reaching age 59 1/2; withdrawal is subject to normal income tax
- May be rolled over to an IRA or a new employer's plan to retain tax-deferred status

11.18.4.4 SIMPLEs (Savings Incentive Match Plans for Employees)

- Offered by small companies with 100 or fewer employees who earn at least \$5,000 each during the year
- Less complicated to set up and administer than 401(k) or 403(b) plans
- Two types: SIMPLE IRA and SIMPLE 401(k), both with same contribution limits and catch-up contributions for people 50 or older
- Employer must contribute to the plan in one of two ways, a fixed contribution or a matching contribution
- Account must be open for 2 years before the employee can move the money or take it out; early withdrawal is subject to significant tax penalties

11.19 Foreign Accounts

Responsibility	<ul style="list-style-type: none">• Direct Supervisor
Resources	<ul style="list-style-type: none">• Requests to solicit business in foreign countries• New foreign accounts
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Review requests to solicit business in foreign countries and to open new foreign accounts:<ul style="list-style-type: none">○ Determine whether the account's country of domicile imposes additional requirements such as licensing○ Notify RR and RR's supervisor of special requirements○ If requirements cannot be met, close the account
Record	<ul style="list-style-type: none">• Record of review of requests to do business in foreign countries and new foreign accounts and action taken, if appropriate• List of foreign requirements (or lack of requirements) from information gathered when reviewing accounts or from outside sources

Coastal Equities, Inc. is not registered to do securities business in any foreign jurisdictions, and therefore no registered representatives may solicit foreign prospective customers outside of the United States. Coastal may open accounts for foreign investors in certain circumstances.

Before soliciting investors or opening an account for a person or entity residing in a foreign country, contact Compliance for further information regarding any special restrictions or requirements.

Coastal requires the following before approving an account for a foreign individual or entity:

- A legal address in the country of residence;
- A mailing address in the US; and
- A Power of Attorney located in the US who speaks and understands the English language and will be lawfully responsible for all trading and account decisions.

11.20 Referrals

[SEC Securities Exchange Act of 1934 Section 15(a); FINRA Rule 2040; FINRA Regulatory Notice 15-07]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Compliance
Resources	<ul style="list-style-type: none"> • Requests regarding referral arrangements
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Designated Supervisor: identify unauthorized referrals in reviews of public communications and refer them to Compliance for follow up • Compliance: <ul style="list-style-type: none"> ○ Review requests for referral arrangements and determine compliance with regulatory and firm policy requirements and approve or disapprove; for approved arrangements establish guidelines for arrangements including any compensation ○ For investment adviser referrals: <ul style="list-style-type: none"> ▪ If compensation will be received for referrals, determine whether investment adviser registration is required for CEI and the RR ▪ Maintain a list of approved IAs ▪ Review IAs to be included on the approved list including registration status, investment policies, suitability guidelines for investors ▪ Establish monitoring program and monitor results vs. IA stated performance ▪ Re-evaluate IA participants at least annually • For hedge fund or other investment referrals, the proposed investment is subject to new product review procedures (see the related section in the chapter <i>FINANCIAL AND OPERATIONS PROCEDURES</i>)
Record	<ul style="list-style-type: none"> • Designated Supervisor review of communications and referrals to Compliance • Compliance: <ul style="list-style-type: none"> ○ Review/approval of referral arrangements ○ Reviews of IAs included on approved list ○ Records of monitoring and annual review

Referrals are an important part of our business. Satisfied customers may refer others to CEI and may also seek referrals from associated persons when they need services not provided by CEI. It is important that referrals to others are based on sound knowledge about the other person or company. In addition, FINRA rules restrict compensation to unregistered persons or entities.

Key requirements regarding referrals include the following:

- Associated persons are expected to make referrals involving investments or investment advisory services only to persons or companies included in a firm-sponsored program or on a list of firm-approved providers.
- Associated persons are prohibited from receiving compensation for referrals except through firm-sponsored programs.
- Any proposed compensation, whether for referring or receiving referrals, must be approved **in advance** by Compliance.

- Referrals involving compensation may require disclosure to the customer of potential conflicts of interest.
- Non-cash compensation is subject to the policy described in the chapter *COMMISSIONS*.

11.20.1 Referrals to Others

Associated persons **may not** accept compensation from someone outside CEI for providing referrals.

11.20.1.1 Referrals to Investment Advisers

Other than through firm-approved referrals, RRs should avoid referring customers to investment advisers unless Compliance has been contacted to make a determination regarding the registration status of the IA and to conduct other necessary reviews of the IA **before** making a referral.

11.20.1.2 Referrals to Hedge Funds or Other Outside Investments

RRs are expected to limit their investment recommendations to products or services offered by CEI. Referrals to outside investments not part of a firm program are prohibited.

11.20.1.3 Referrals to Other Departments and Affiliates

Compensation paid by other firm departments because of business referrals must be reviewed and approved by Compliance **in advance**.

11.20.2 Referrals to The Firm

When others outside CEI refer potential customers, referral fees or other compensation may not be paid to the outside person or firm. Questions and requests for exceptions should be referred to Compliance.

11.20.2.2 Referrals from Nonregistered Foreign Persons

FINRA rules provide exceptions (with specific requirements) for referrals from foreign persons who are not registered. Such arrangements require **prior** approval by Compliance.

11.21 Death of a Customer

When a customer dies, the account assets owned by the deceased person may become subject to a will, estate laws, and other governing laws or documents. The assets are, therefore, frozen in the account until necessary documents are received and legal distribution has been determined. Joint accounts and other accounts where the deceased person is a joint owner with others may be subject to certain distribution requirements depending on the styling of the account.

When a customer dies, the RR should:

- immediately notify Operations
- consider assets in the deceased person's account as "frozen" until distribution of assets has been determined, *i.e.*, accept no orders and do not authorize sending of securities or funds from the account
- cancel all open orders

11.22 Active Accounts – Risk Based Account Review Supervision

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Active Accounts in Account Review Tab in Smart Station
Frequency	<ul style="list-style-type: none"> • Monthly
Action	<ul style="list-style-type: none"> • Review Active Accounts flagged for review. Accounts requiring further review may include: <ul style="list-style-type: none"> ○ Fiduciary accounts (trust, pension plans, etc.) ○ Minor's accounts ○ Accounts engaged in higher-risk transactions ○ Accounts with high volume of trading ○ Other accounts by discretion • Further review includes: <ul style="list-style-type: none"> ○ New account documentation for completeness ○ Investment objectives for consistency with trading activity ○ Consulting with the RR regarding account activity • The supervisor may identify selected accounts where further information need be requested from the RR informally or through an account worksheet. The supervisor should: <ul style="list-style-type: none"> ○ ensure completion of the form ○ mark the account reviewed ○ send the original to Compliance • Further action may include branch manager contact with the customer in writing or by phone or in person. A record should be made of any such contact.
Record	<ul style="list-style-type: none"> • Indicate review in Smart Station • Active account letters and/or customer contact forms are filed in the customer account file and forwarded to Compliance • Compliance retains the following records: <ul style="list-style-type: none"> ○ copies of Active Account Questionnaires and memoranda ○ Active Account Reports reviewed including notations of action taken on selected accounts ○ record of supervisor contact

Supervisors will, on a monthly basis, review active accounts for further review flagged by Smart Station in the "Account Review" tab. Items to be reviewed include, depending on the type of account and type of trading activity:

- Review of new account documentation to determine necessary documents are on file and to identify the customer's investment objectives and financial profile
- Review of trading activity in the account including types and size of trades and frequency of trades
- Contact with the RR to determine additional information regarding the customer and trading activity

Additional reviews that may be conducted include:

- Profit and loss or change of equity calculation
- Turnover calculation

- Contact with the customer (written or oral)

Reviews of active accounts may include these items or other items at the discretion of the supervisor.

The designated supervisor of the branch handling the account, will determine whether contact will be made with the customer and whether that contact will be in the form of a letter, telephone call, or face-to-face contact to confirm investment objectives and the customer's knowledge regarding the trading activity in the account. All records of customer contact in conjunction with active account reviews (including telephone conversations and face-to-face meetings) are to be maintained in a file for the customer or an active accounts file.

11.23 Concentrations

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • For Alternative Investments, the AI Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Transaction reports • Margin records • New account records
Frequency	<ul style="list-style-type: none"> • Depending on frequency of available reports
Action	<ul style="list-style-type: none"> • Identify concentrated positions, particularly in margin accounts • If the security is a low-cap or other unknown security, check blue sky status • Review the customer's new account profile, particularly the investment objectives • Confer with the RR about concentrations, if necessary • Confer with the customer, if appropriate • Restrict future purchases for individual or all customers, if appropriate
Record	<ul style="list-style-type: none"> • Reviews of concentrated positions including action taken

Accounts that are concentrated in certain security positions may increase risk for the customer, particularly if the security is purchased on margin. RRs must consider the following factors for concentrated customer accounts:

- Is the concentrated position in a margin account?
- Do trading characteristics (thinly-traded, limited markets) create added risk to the customer?
- If the concentrated position is higher-risk, is the customer aware of this risk and suitable for such a position or positions?
- Should the concentrated position be mitigated by reducing margin exposure or selling off some of the position?

Supervisors should consider all illiquid investments in order to calculate the percentage of such assets versus liquid net worth (LNW). The client's LNW on his or her account profile is a range, and the highest end of the range may be used in making this determination. Generally, a concentration of illiquid securities over 30% may be unsuitable. The supervisor should consider other factors such as age, time horizon, and liquidity needs to determine whether this concentration is suitable. If, after consulting with the RR responsible for the account, the supervisor determines that further review is required, the account should be escalated to the Chief Supervision Officer or other senior firm principle for an exception, or for possible remediation and disciplinary action.

11.24 Money Movement

11.24.1 Customer Purchases

When an order to purchase securities is accepted from a customer, payment from the customer's bank account or other depository must be authorized in writing by the customer. Payment is not acceptable based only on the customer's oral authorization to withdraw funds. Examples of acceptable payment include:

- a check signed by the customer
- written authorization by the customer to draft funds from the customer's bank checking or savings account

Questions regarding proper payments should be referred to Operations or Compliance.

11.24.1 Checks Payable to Clearing Firm

All checks provided by customers must be made payable to CEI's clearing firm only. Registered Representatives are not permitted to take "custody" of customer checks except for subscription-way purchases as set forth below.

If the branch has received approval from CEI to use a check scanner, checks received by the branch must be deposited same day in accordance with Wells Fargo's operational procedures set forth on InfoMax.

Otherwise, customer checks must be forwarded to Coastal's clearing firm, Wells Fargo Clearing Services, LLC, in accordance with Wells Fargo's operational procedures set forth on InfoMax, including, without limitation, notation of the client's account number on the memo line of the check, and if an IRA account, whether the deposit is for the current or prior year. Coastal provides its registered representatives a Check Deposit Instructions form during on-boarding and periodically when the firm updates its procedure or other material information in this regard.

In the event that circumstances require (*e.g.* during exercise of the firm's business continuity plan) that the Registered Representative must forward the check to the Home Office or other check-scanner-approved OSJ, the Registered Representative must obtain written permission from a principal of such branch to accept delivery prior to forwarding the check. Any such check must be sent the ***same day of receipt via priority overnight delivery*** such that the delivery will occur on or before 10:00am. Checks received by the Home Office or approved OSJ shall be deposited promptly (or returned if received in error).

11.24.2 Customer Checks and Securities Received in Error

Customer checks and securities received in error must be immediately returned to the customer. Receipt of the check or security must be kept in a log, identifying the check or security, amount, date received, date returned, and method of delivery. If utilized, a copy of the cover letter returning the check or security must be kept in the customer's file.

11.24.3 Subscription-way Purchases

All checks received from customers concerning direct investments (purchases of a security on a subscription-way basis) should be promptly forwarded to the sponsor/issuer with the subscription agreement upon approval by a registered principal or returned to the customer upon rejection. "Promptly forwarded" means that the check must be transmitted no later than noon of the business day following the registered principal's approval/rejection of the transaction. The registered principal must review the application (and corresponding Complex Product/Direct Investment Disclosure Form) for suitability, among other things. If the registered principal is unable to review

and respond to the customer application that same business day, the procedures of this section apply. The registered principal has seven (7) business days from receipt of a complete and correct application package to accept or reject the application.

Customer checks must be kept in a secured operations area or locked location with access limited only to authorized personnel. At the end of the business day, all customer checks must be locked in a safe or similarly secured area.

The RR must maintain a copy of the check and must log the date the check was received from the customer, and date and time the check was transmitted to the issuer/sponsor or returned to the customer if rejected. In addition, prior to accepting the customer check, the representative must disclose to the customer the firm's process for handling customer checks payable to issuers for subscription-way securities transactions in advance of the transaction. The firm's Complex Product/Direct Investment Disclosure Form includes such disclosure and must be submitted with the customer's application to the registered supervisor.

11.24.2 Transmittals of Customer Funds and Securities

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • Transfers of customer funds or securities • LOAs • Wire Funds Request Form • ACH Request Form • IRA Distribution Request Form • FINRA OFAC Search Tool (ofac.finra.org)
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Conduct training of Operations and Supervision personnel regarding transmittal requirements and controls • Review transactions for possible AML Red Flags
Record	<ul style="list-style-type: none"> • Records of training including who attended, date, training subjects • Records of transmittals, LOAs, other verifications included in procedures

This section describes CEI's procedures for transmitting funds or securities from customer accounts. The following summarizes the CEI's policies:

- All transfers require written letters of authorization (LOAs) when funds and/or securities will be transmitted to a third party, or if by check to an address other than that listed in the account registration. LOAs may be received by mail, fax, delivery, or other means including electronic transmission that provides for written authorization with the customer's verifiable signature.
- If an LOA copy is not presented in person by the customer, the customer's signature will be verified against existing account records.
- Where transfers to a third party are ongoing, a "standing" LOA is permitted. Standing LOAs are good for 12 months from the client signature date.
- Copies of LOAs are retained in the Firm's records.

- Anyone who appears in person to receive assets and who claims to be the customer will be required to present photo identification if the customer is not personally known to the operations personnel releasing funds or securities from the customer's account.
- Any authorized third party receiving a customer's assets in person will be required to present photo ID and the third party authorization (LOA) will be verified.
- Suspicious or questionable activity must be brought to the attention of the AML Compliance Officer who is responsible for determining whether a Suspicious Activity Report must be filed.

General Process for Transmittals of Funds

RR Procedure

- 1- RR receives a request from the Client for a check, journal, ACH, or wire, in person or by phone. If by phone, two factor authentication is required.
- 2- RR and client complete the appropriate form for the type of transmittal, Client and RR sign (In the case of a wire transfer, the RR should alert the client that a supervisor will call the phone number of record to confirm the wire details.)
- 3- RR presents the completed and signed transmittal request form to her/his supervisor and awaits supervisory approval and signature.
- 4- RR contemporaneously enters an Asset Movement Service Request in Smart Station.

Supervision

- 5- Upon receipt of a fully executed transmittal request, Supervisor searches for Third Party Recipient (when applicable) on OFAC List (OFAC.FINRA.ORG) and reviews results
- 6- Supervisor will call client at phone number of record to confirm third party transmittals AND same-name ACH and wires over \$10,000.00
- 8- Supervisor signs transmittal request form to evidence approval and compliance with the above process
- 9- Supervisor locates the Asset Movement Service Request in Smart Station, reviews service request, notes review of OFAC check if applicable to the service request, and may then approve the service request.

11.25.3 ESOP Elections

ESOP Elections are expressly exempted from the firm's WSPs as they pertain to transmittal of funds. Clients electing to fund purchases through an ESOP from their accounts must submit their request directly to Wells Fargo Clearing, LLC ("WFCS") using their required documentation. WFCS is responsible for compliance with their internal procedures concerning third-party asset transfers to the ESOP sponsor or designee. As part of that process all customer documentation submitted to WFCS must be imaged into the client file through Smart Station. Inherent in this section is the Firm's conclusion that it is reasonable to rely upon the custodian, WFCS, in processing such client requests and in providing reasonable controls over the transmittal process to protect the customer. The Firm will monitor this conclusion by reviewing any customer complaints brought to the Firm's attention in this regard on an on-going basis.

11.25.4 Checking Account Safeguards

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • N/A
Frequency	<ul style="list-style-type: none"> • Ongoing • Annual - review of supervisory controls
Action	<ul style="list-style-type: none"> • Train personnel regarding required procedures • Maintain list of authorized check signers and request additional signers as necessary • Review checking account safeguards as part of the annual supervisory controls review (Compliance or other reviewer)
Record	<ul style="list-style-type: none"> • Records of checks issued, including approvals, are retained in files in the Operations area and/or records may be retained by a clearing firm

The following procedures must be followed to safeguard the use of checks.

- Blank checks and check registers must be kept in a secured operations area or locked location with access limited only to authorized personnel.
- At the end of the business day, all blank checks must be locked in a safe or similarly secured area.
- If using a clearing firm's account:
 - Approval must be obtained from the clearing firm prior to writing a check, and approval noted in records retained for checks issued.
 - Transmit to the clearing firm, by the end of the business day, information regarding checks issued that day
- If a clearing firm issues all checks, promptly transmit the customer's request for issuance of a check or sending of securities
- Checks must be used in numerical sequence.
- CEI maintains a list of authorized check signers. Each business location that issues customer checks must have at least 2 designated check signers.
- Checks **must not** be signed in blank, in anticipation of a check signer's absence. The manager of Operations must be contacted if alternate arrangements are necessary in the absence of an authorized check signer.
- When an associated person will personally deliver a customer check, the procedures outlined in the section *Transmittals Between Customers and Registered Representatives* must be followed.

11.25.4.1 Prepayments and Extensions

Prepayments (customer requests payment prior to settlement date on a sale) or extensions of time to make payment must be approved by the designated supervisor.

11.25.4.2 Associated Persons Authorized to Transmit Customer Assets from Accounts

Associated persons who are authorized to release customer funds and/or securities include:

- Authorized Operations personnel who transmit instructions to a clearing firm (if applicable)

- Authorized Operations personnel who issue checks (if applicable)
- RRs authorized under the *Transmittals Between Customers And Registered Representatives* policy below

11.25.4.3 Issuing Checks to Customers

Checks to be paid to customers from their accounts will be paid to the order of the account as it is carried on CEI's books and sent to the address appearing on the account. Exceptions require written authorization by the customer. When checks are to be issued to a third party or funds are transferred to a third party, the following procedures apply.

11.25.5 Persons Receiving Assets in Person

When someone appears in person to receive assets, a photo ID will be required before the assets are released. The person releasing assets is required to note on CEI's records the type of ID presented and the number (driver's license, passport, etc.). If an authorized third party under an LOA is receiving assets, the LOA will be verified before assets are released.

11.25.6 Transmittals to Third Parties

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests to send funds/issue checks to third parties
Frequency	<ul style="list-style-type: none"> • As required - issue transmittals to third parties and send notification to the customer
Action	<ul style="list-style-type: none"> • Obtain required LOA • Issue check/funds in accordance with procedures • Send notification to the customer that funds (or securities) have been sent to a third party
Record	<ul style="list-style-type: none"> • LOAs (in Operations and/or clearing firm's files)

When a customer wishes funds or securities to be paid to a third party in the third party's name, the customer will be required to provide a signed LOA that specifies to whom the funds are to be paid.

When funds are disbursed, CEI (or its clearing firm) will send a notice to the customer confirming that funds were sent to a third party from the customer's account.

General Third-Party Transmittal Process

RR Procedure

1- RR receives a request from the Client for a check, journal, ACH, or wire, in person or by phone. If by phone, two factor authentication is required and must be noted in writing.

2- RR and client complete the appropriate form for the type of transmittal, Client and RR sign (In the case of a wire or ACH transfer, the RR should alert the client that a supervisor may call the phone number of record to confirm.)

3- RR presents the completed and signed transmittal request form to her/his supervisor and awaits supervisory approval and signature.

4- RR contemporaneously enters an Asset Movement Service Request in Smart Station.

Supervision

5- Upon receipt of a fully executed transmittal request, Supervisor searches for Third Party Recipient (when applicable) on OFAC List (OFAC.FINRA.ORG) and prints results

6- Supervisor will call client at phone number of record to confirm third party transmittals AND same-name ACH and wires over \$10,000.00

8- Supervisor signs transmittal request form to evidence approval and compliance with the above process

9- Supervisor locates the Asset Movement Service Request in Smart Station, reviews service request, attaches approved transmittal request form and OFAC report if applicable to the service request, and may then approve the service request.

Supervisors who become familiar with customers who routinely wire or ACH funds to certain third-parties to the same bank account, may, in his or her discretion, waive client contact for up to six months. Supervisors should reconfirm in six months that the requests are still valid. This exception would not apply if the bank or third-party information changes.

11.25.4.7 Letters of Authorization

A Letter of Authorization (LOA) is an important required document whenever a customer asks that funds or securities are to be sent to a third party out of the customer's account. LOAs are an important record for CEI, both to ensure the customer's instructions are followed and to ensure CEI has a written record in the event there is a question in the future about disbursements from an account.

11.25.4.7.1 LOA Instructions

RRs or their assistants are responsible for obtaining completed LOAs, when necessary.

- A completed LOA is required **prior to** disbursements to third parties.
- All blanks must be completed on the LOA.
- The customer's original signature is required. In the case of a joint account, all joint owners must sign the LOA. For corporations, trust accounts, and other accounts, the authorized person must sign the LOA.
- Completed LOAs are submitted to Operations and should accompany the request to disburse funds or send securities to a third party.

11.25.4.7.2 Standing LOAs

Customers who have a need for regular third-party disbursements should be encouraged to apply for a Firm account that provides checking account privileges.

To accommodate customers (on an exception basis), CEI permits standing LOAs for regular disbursements to the same third party under the following procedures:

- The customer's signed LOA must be notarized.

- As a best practice, the standing LOA should be renewed annually, or the customer should be contacted to confirm that the standing LOA is desired with a note to the file. It is the RR's responsibility to ensure standing LOAs are current.

11.25.4.8 Email Instructions

[FINRA Regulatory Notice 12-05]

Email and other electronic communications can be subject to intrusion and compromised by a third party. There have been instances of third parties sending fraudulent requests to broker-dealers to transfer customer funds to an account for the benefit of the third party. To prevent theft from customer accounts, the following apply to email or other electronic requests to transfer funds to a third party:

- The customer will be contacted by phone, mail, or another means independent of the email account to verify the accuracy of the instructions.
- The RR, assistant, or operations person receiving instructions should be aware of "red flags" (*e.g.*, funds to be transferred to an unfamiliar third party, particularly in a foreign country; transfers that appear to be out of the ordinary for the customer; and requests that indicate urgency or otherwise appear designed to deter verification of transfer instructions).
- If CEI processes its transactions through a clearing firm, the clearing firm will have its own procedures to prevent unauthorized third party transmittals.
- The Operations Manager or Compliance should be contacted with any questions about questionable transfer instructions.

11.25.4.9 Authorization Records for Negotiable Instruments Drawn from a Customer's Account

[FINRA Rule 4514]

The customer's written signature is required whenever CEI obtains or submits for payment a check, draft, or other form of negotiable paper drawn on a customer's checking, savings, share or similar account; this may include the customer's signature on the negotiable instrument. Written authorization separate from the instrument must be retained for 3 years following the date the authorization expires. No record is required when the customer signs the instrument (*i.e.*, a check).

11.25.4.10 Transmittals to an Alternate Address

Funds and securities will be sent to the customer's address of record, unless the customer provides **written** authorization to use an alternative address.

11.25.5 Transmittals Between Customers and Registered Representatives

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests to deliver checks • Check Delivery Log
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Approve (or disapprove) the request to deliver a check • Send a letter to the customer on the same day as check delivery, confirming delivery

Record	<ul style="list-style-type: none"> • Initials on Check Delivery Log • Check delivery letter retained in customer account file
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On occasion, a customer may request that the RR or other CEI associated person personally deliver a check to the customer. This is permitted under the following conditions:

- The designated supervisor must approve the check delivery. The designated supervisor should initial a record maintained by Operations.
- A same-day confirmation (letter) will be sent to the customer confirming that a check was delivered and inviting the customer to call if there are any questions.

11.25.6 Suspicious or Questionable Activities

Associated persons are responsible for referring suspicious or questionable activities to their designated supervisor. If the activity involves the designated supervisor, the associated person should bring the activity to the attention of the Compliance Officer. If the Compliance Officer is involved, the activity should be brought to the attention of someone else in senior management. Such activities may include transfers without required authorizations; failure to obtain secondary approvals where required; a pattern of transfers that have no reasonable business basis, or any other activity the associated person considers suspicious.

12 ORDERS

This chapter provides policies and guidelines for the entry and handling of customer orders. References to "order records" in this chapter includes manual order tickets and electronic order records, where appropriate.

12.1 Acceptance and Prompt Entry of Orders

Orders should be accepted only from the beneficial owner of an account or their authorized agent. Authorized agents would include anyone holding third-party power to act on the customer's behalf such as a trustee, court-appointed guardian, authorized investment adviser, *etc.* Orders accepted from an unauthorized third party may result in rescission of the transaction and assigning the loss to the RR. For example, orders should not be accepted from a husband, on behalf of his wife's account, unless the wife has signed a trading authorization giving her husband authority to act on her behalf.

If an associated person receives a telephone order from someone they do not recognize or know to be the owner of the account or person authorized to act on behalf of the account, identity should be requested before accepting the order. Identity verification information would include:

- account number; and
- social security number; or
- other identifying information on record such as mother's maiden name.

RRs are obligated to enter orders in Smart Station, or transmit customer orders to the appropriate order execution desk or order facility, promptly after receipt. Orders cannot be held for future entry; a limit order should be entered if the customer does not want to effect the transaction at the current market price.

12.2 Orders Requiring Pre-Approval

Responsibility	<ul style="list-style-type: none">• Principals and Supervisors
Resources	<ul style="list-style-type: none">• Order records• 'Review and Release' software
Frequency	<ul style="list-style-type: none">• As Needed
Action	<ul style="list-style-type: none">• Review and approve or disapprove orders pending release
Record	<ul style="list-style-type: none">• Electronic approval on Daily Transaction Report• Notes of action taken on Smart Station

Certain representatives, lines of business, or orders require approval because of rule requirements or CEI policy. Those registered representatives affected by such policies may have all or some of their trades restricted, or placed in the clearing firm's 'review and release' module embedded in the trading software. Such registered representative's trades are reviewed by a firm principal or supervisor before the trade is authorized and executed. Orders 'on hold' by the software may be approved by any of the firm principals or supervisors who have been given entitlements to the review and release module by the firm, so long as such principal or supervisor is not releasing his or her own trade order.

Direct business, such as variable annuities and alternative investments, require pre-approval by a supervisor as set forth in the pertinent sections of this manual.

12.3 Solicited and Unsolicited Orders

12.3.1 Definition of Solicited Order

When a transaction is recommended to a customer and the customer enters an order as a result of that recommendation, the resulting order is considered to be solicited. Other actions that may result in an order being deemed solicited include the mailing of a research report or other written communication for the purpose of encouraging the customer to act on the information provided or sending a prospectus on a new issue. Customer orders that are solicited must be so marked on the order ticket for the transaction.

12.3.2 Prohibited Solicitations

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Compliance - ETPs
Resources	<ul style="list-style-type: none"> • Trade blotter • First Clearing ETP report
Frequency	<ul style="list-style-type: none"> • Trade Blotter T+7 • ETP report at least Quarterly
Action	<ul style="list-style-type: none"> • Identify orders contrary to solicitation limitations • If prohibited solicitations are identified, take corrective action: <ul style="list-style-type: none"> ○ Solicitations contrary to CEI's Restricted List may require cancellation; contact supervisor or Compliance for guidance ○ Other exceptions may require different actions including cancellation of the transactions, removal of commissions, reminder to RRs, <i>etc.</i>
Record	<ul style="list-style-type: none"> • Electronic notes on Trade blotter • Records of cancelled trades • Clearing Firm ETP reports • Other records as appropriate (reminder memo to RR, notes to Branch Manager Log, <i>etc.</i>)

RNs may NOT solicit transactions listed below:

- Securities included on the Firm's Restricted List
- ETPs featuring a daily reset, including but not limited to Leveraged or Inverse ETFs

12.4 Suitability of Recommendations

[FINRA Rule 2111; SIFMA Institutional Suitability Certificate: <http://www.sifma.org/services/standard-forms-and-documentation/cross-product/>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New account records • Order records

	<ul style="list-style-type: none"> • Transaction reports • Other available reports • Customer monthly transaction records • Institutional Suitability Certificates
Frequency	<ul style="list-style-type: none"> • Trade Blotter review: T+7 • Daily/Monthly non-trade alerts: 30 days • When required - review/approve new accounts • Periodically - training for RRs
Action	<ul style="list-style-type: none"> • Obtain Institutional Suitability Certificates from institutional customers <ul style="list-style-type: none"> ○ Where an institutional account fails to provide the Certificate, flag the account noting the form is not on file ○ Where the institution does not affirm its independence for all investments, flag the account regarding what investments are or are not affirmed • Review customer orders for suitability (other than those excepted) which includes factors among those listed below and other information known about the customer: <ul style="list-style-type: none"> ○ Customer new account information ○ Other securities held in the customer's account ○ Other information regarding the account such as whether the account is managed by an investment adviser or uses other advisers or consultants in making investment decisions ○ Transaction information from daily transaction reports and monthly transaction records ○ Information obtained from the RR ○ Information obtained by contacting the customer ○ Excessive trading (also see the section <i>Churning</i> in this chapter) ○ Concentration of a security in one account or multiple accounts (also see the section <i>Concentrations</i> in the chapter <i>ACCOUNTS</i>) • Review recommended orders for compliance with Regulation BI [see the chapter <i>REGULATION BEST INTEREST (BI)</i>] • Refer to new account records when necessary to identify investment objectives and other customer information • Review suitability documentation recorded by the RR and pertaining to a recommended investment or strategy • Where investment profile information is incomplete, contact the RR to obtain further information or if none is available, determine whether there is a reasonable basis for making recommendations • For "hold" recommendations, confirm the RR has included adequate documentation • Where there are suitability questions: <ul style="list-style-type: none"> ○ Confer with RR regarding suitability questions ○ Confer with Compliance when necessary ○ Contact customer when necessary to confirm customer's understanding of and agreement with transactions

	<ul style="list-style-type: none"> ○ Modify or restrict future transactions, as appropriate ● Compliance: if CEI uses portfolio or analytic tools or models, review and confirm whether the tools make recommendations subject to the suitability rule, and communicate obligations to RRs ● Train RRs regarding suitability obligations
Record	<ul style="list-style-type: none"> ● Initials or other record of review on order records and reports ● Institutional Suitability Certificates ● Suitability documentation on order records or in RR records ● Compliance: record of reviews of portfolio or analytic tools and communications with RRs about suitability obligations (if applicable) ● Training including who attended, when it occurred, and subjects included

RRs will be required to enter notes into SmartStation Contact Management documenting the suitability and best interest standard for each recommended customer transaction on a risk-basis. For customers who do not hold an account at WFCS, the suitability and best interest information must be documented on the direct business paperwork.

12.4.1 General Requirements

RRs must have a reasonable basis for believing that a recommended transaction or investment strategy involving a security or securities is suitable for the customer. Recommendations should be based on information obtained through reasonable diligence to ascertain the customer's investment profile which is recorded in the account records, generally at the time the account is opened and updated when necessary. The customer's investment profile includes, but is not limited to, the customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information the customer may disclose in connection with the recommendation.

Suitability is only one element of acting in a customer's best interest. Recommendations to retail customers who are natural persons are subject to Regulation Best Interest (BI) which is broader than the suitability requirement. Reg BI includes recommendations for orders; types of accounts; and investment strategies, including recommendations to prospects. It is important to be familiar with those requirements which are included in the chapter *REGULATION BEST INTEREST (BI)*.

There are exceptions to suitability obligations when dealing with certain institutional accounts as discussed in the following section *Institutional Accounts*. Note that FINRA's description of institutional accounts includes certain natural persons under the suitability rule. Regulation BI applies to ALL natural persons.

12.4.1.1 Investment Strategy

[FINRA Rule 2111.03]

"Investment strategy" is defined in FINRA rules to include, among other things, an explicit recommendation to hold a security or securities. However, the following communications are excluded as long as they do not include (standing alone or in combination with other communications) a recommendation of a particular security or securities:

- a. General financial and investment information, including (i) basic investment concepts, such as risk and return, diversification, dollar cost averaging, compounded return, and tax deferred investment, (ii) historic differences in the return of asset classes (*e.g.*, equities, bonds, or cash) based on standard market indices, (iii) effects of inflation, (iv) estimates of future retirement income needs, and (v) assessment of a customer's investment profile;
- b. Descriptive information about an employer-sponsored retirement or benefit plan, participation in the plan, the benefits of plan participation, and the investment options available under the plan;
- c. Asset allocation models that are (i) based on generally accepted investment theory, (ii) accompanied by disclosures of all material facts and assumptions that may affect a reasonable investor's assessment of the asset allocation model or any report generated by such model, and (iii) in compliance with FINRA Rule 2214 (Requirements for the Use of Investment Analysis Tools) if the asset allocation model is an "investment analysis tool" covered by FINRA Rule 2214; and
- d. Interactive investment materials that incorporate the above.

12.4.1.2 Components of Suitability Obligations

[FINRA Rule 2111.05]

As excerpted from the suitability rule, there are three main obligations when making a recommendation: reasonable-basis suitability, customer-specific suitability, and quantitative suitability.

- a. The reasonable-basis obligation requires a reasonable basis to believe, based on reasonable diligence, that the recommendation is suitable for at least some investors. In general, what constitutes reasonable diligence will vary depending on, among other things, the complexity of and risks associated with the security or investment strategy and CEI's or RR's familiarity with the security or investment strategy. Reasonable diligence must provide an understanding of the potential risks and rewards associated with the recommended security or strategy. The lack of such an understanding when recommending a security or strategy violates the suitability rule.
- b. The customer-specific obligation requires a reasonable basis to believe that the recommendation is suitable for a particular customer based on that customer's investment profile which includes the customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information the customer may disclose.
- c. Quantitative suitability refers to avoiding excessive activity and requires a firm or RR who has actual or de facto control over a customer account to have a reasonable basis for believing that a series of recommended transactions, even if suitable when viewed in isolation, are not excessive and unsuitable for the customer when taken together in light of the customer's investment profile. No single test defines excessive activity, but factors such as the turnover rate, the cost-equity ratio, and the use of in-and-out trading in a customer's account may provide a basis for a finding a violation of the quantitative suitability obligation.

Another approach to suitability is portfolio-based that considers the entirety of an investor's investments (or at least those known to the RR). Where a customer has multiple accounts with CEI and those accounts have inconsistent investment objectives, it is necessary to confirm the customer's intent to use different investment profiles or factors for the different accounts. Notation should be made to the customer's account record and on the order record or the recommendation.

12.4.1.3 Customer Financial Ability

[FINRA Rule 2111.06]

Rule 2111 prohibits recommending a transaction or investment strategy involving a security or securities or the continuing purchase of a security or securities or use of an investment strategy involving a security or securities unless the member or associated person has a reasonable basis to believe that the customer has the financial ability to meet such a commitment.

12.4.1.4 Specific vs. General Recommendations

Suitability obligations apply to specific recommendations as opposed to general investment advice (*i.e.*, a recommendation generally to invest in fixed income securities vs. recommending a specific bond). However, recommending a specific strategy (such as use of a bond ladder, day trading, margin, *etc.*) would be subject to suitability obligations. The narrower the scope of the recommendation, the more likely it is subject to suitability obligations.

12.4.1.5 Allocation Models and Educational Materials

To avoid suitability obligations, allocation models or educational materials cannot include recommendations of particular securities such as those comprising the asset allocation model. An explicit recommendation to "hold" specific securities in an asset allocation model constitutes a recommendation. FINRA has indicated that as an allocation recommendation becomes narrower and more specific, suitability obligations may apply. Compliance must review and approve any models or analytic tools **prior to** use.

12.4.1.6 Hold Recommendations

Suitability obligations apply to recommendations to hold a security or securities or to continue to use an investment strategy, even if the RR did not recommend the original purchase. RRs should disclose and document (on the order record or the RR's records) that the hold recommendation is based on relevant factors known at the time of the recommendation only, and that continued monitoring or recommendations will not occur (if that is the case). Some hold recommendations should be documented including those for shorter-term investments; those that have a periodic reset or similar mechanism that could alter the investment's character over time; those that are particularly vulnerable to market conditions; or those that are otherwise potentially risky when the recommendation is made. For example, risky investments may include leveraged ETFs, mortgage REITs, an issuer facing significant financial or other material risks, an over-concentrated position, and a security inconsistent with the customer's investment profile. These hold recommendations should be documented in the RR's records.

12.4.1.7 Complex Products

The suitability of recommendations of complex investments should be documented in the client's file or in Client Dashboard when it is not readily apparent why the investment is suitable for the client. Effective June 30, 2020, recommendations of complex products must be documented as a Note in Client Dashboard (or on disclosure and suitability forms for direct investments) explaining why the investment recommendation is in the best interest of the client, unless the recommendation is objectively in the best interest of the client on its face.

Before any recommendation of a complex product, specifically structured notes and CDs, may be made to a customer, Coastal requires that the customer be qualified for complex product trading by completing the Complex Product Qualification Form. Please see the Chapter *Complex Products* for additional guidance and procedural instructions in that regard.

12.4.1.8 Improper Trading of Long-Term Products

It is improper to recommend the short-term trading of long-term products (such as mutual funds, closed-end funds, variable annuities and UITs). Recommending early UIT rollovers to increase sales credits is a violation of suitability requirements.

12.4.1.9 Documenting Suitability/Best Interest

It is important to document suitability, particularly where there may be differing investment profiles when a customer has multiple accounts and when recommending a complex product. RRs should document the basis of their recommendations on the order record and/or in the RR's records such as Day-timers, electronic records, etc.

Coastal requires notes be placed in Smart Station or other authorized record-keeping system available to the home office on a risk-basis. Notes must be kept to document:

High-Risk Strategies	<i>Examples:</i> Purchases on Margin; Long-term strategy to use margin in account; Options strategies; shorting; Inverse/Leveraged ETF; Selling out of a position short term (<1 year); Selling during a redemption penalty period
Recommendation seems to contradict Retail Customer's IO on its face	<i>Examples:</i> Recommending a high-yield Corporate Bond to a Conservative Growth customer; recommending holding a material portion of an account in cash for an extended duration; investing most of portfolio in treasuries for an Aggressive Growth Retail Customer; Recommending a private placement to a moderate or first-time investor
Recommendation to invest in higher cost security when less costly option is available	<i>Examples:</i> MF A share when C or I share available; MF in same sector and strategy is costlier than similar MF
Product Exchanges	<i>Examples:</i> Recommending sale of fixed annuity and invest some or all of the proceeds in a variable annuity; liquidate 'traditional' assets in portfolio to invest in a private placement
Rollovers	<i>Examples:</i> Recommendation to rollover 401k plan to IRA
Verbal conversations with clients concerning investment recommendations not exercised by the client	<i>Examples:</i> Advice given to client to sell a position but the client declines, etc.
Hold Recommendations	<i>Examples:</i> Express hold recommendations concerning individual securities; Complete portfolio reviews with the client where one or more securities will be a recommendation to hold

As a best practice, notes should be kept to memorialize every conversation with a client regarding investments and the client's accounts.

12.4.1.10 Understanding Recommended Investments

It is important that the RR understands the investment being recommended. CEI offers training and/or other materials to describe the features of certain investments offered by CEI.

If the RR does not understand a security or investment strategy, it is the RR's obligation to contact his or her supervisor, the product manager, or Compliance to receive further information before making a recommendation.

12.4.2 Institutional Accounts

[FINRA Rule 2111(b), 2111.07 and 4512(c); SIFMA Institutional Suitability Certificate:
<http://www.sifma.org/services/standard-forms-and-documentation/cross-product/>]

There is an exemption from customer-specific recommendation obligations when recommendations are made to institutional customers defined by Rule 4512(c). Factors to consider when determining the scope of CEI's suitability obligation when making recommendations to institutional customers include: (1) the customer's capability to evaluate investment risk independently both in general and with regard to particular transactions and investment strategies involving a security or securities, and (2) the institutional customer's affirmation indicating that it is exercising independent judgment in evaluating the recommendations. An institutional customer may indicate that it is exercising independent judgment on a trade-by-trade basis, on an asset-class-by-asset-class basis, or in terms of all potential transactions for its account. Institutional accounts will be requested to provide the Institutional Suitability Certificate to comply with the exemption.

Where an institutional customer has delegated decision making authority to an agent, such as an investment adviser or a bank trust department, these factors are applied to the agent.

Where an RR has reason to believe an institutional investor is not capable of understanding an investment or making an independent decision, the RR is obligated to make a specific suitability determination and should note this action on order records, in the RR's records, or in the account's records.

12.4.3 Recommendations of OTC Equity Securities

[FINRA Rule 2114; FINRA Regulatory Notice 21-03]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Daily Report Tab/Trade Blotter • OTC Equity Securities Suitability Forms
Frequency	<ul style="list-style-type: none"> • Weekly - review "Low-Priced Equity" alerts for potential solicitations in low-priced securities • As required - review Forms
Action	<ul style="list-style-type: none"> • Review alerts to identify solicited transactions in OTC equity securities • For identified transactions, determine whether a Form was required and previously submitted and approved • For non-approved transactions, consult with Compliance regarding corrective action which may include cancellation of transactions • For submitted Forms, review financial statements, determine required information is included with the Form, approve or disapprove, and notify the RR

Record	<ul style="list-style-type: none"> • Records of alert reviews are included on reviews of Daily Transaction Reports including the reviewer's name and date of review and any action taken • Copies of Forms with attachments
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Recommendations to purchase or sell short OTC equity securities require completion of CEI's OTC Equity Securities Suitability Form **prior to** making the recommendation. Securities not subject to this requirement are listed in *Exemptions* at the end of this section. An "OTC equity security" is defined as any non-exchange-listed security and certain exchange-listed securities that do not otherwise qualify for real-time trade reporting.

OTC equity securities as defined in this section often trade at low prices and may represent a higher risk to the purchaser depending on where and how the security trades. For example, a thinly-traded OTC stock may be subject to volatile price changes and may be difficult to liquidate. There is added risk when the security is purchased on margin, since some of these securities may be difficult to liquidate. Customer trading in low-priced and microcap securities may also be an indicator of money laundering, depending on the scope and size of the trading. Any suspicious trading should be reported immediately to Compliance.

12.4.3.1 Low-Priced and Microcap Securities

These securities are subject to scrutiny because of potential risks, including the following. Some of these reviews are included in chapters specific to those activities (trading, research, *etc.*).

- heightened supervision of Firm associated persons who maintain direct or indirect outside business activities associated with microcap and OTC companies;
- heightened supervision of traders involved in trading microcap and low-priced OTC securities;
- ensuring that any research for microcap and low-priced OTC companies produced by CEI is accurate and balanced, and appropriately discloses risks to investors;
- monitoring customer accounts liquidating microcap and low-priced OTC securities to ensure, among other things, that CEI is not facilitating, enabling or participating in an unregistered distribution;
- heightened supervision of Firm activities where an affiliate of CEI is the transfer agent for the microcap or low-priced OTC securities; and
- monitoring RR solicitations of customers to trade microcap and low-priced OTC securities to ensure that any recommendations are balanced and the securities are suitable for the customer.

12.4.3.2 OTC Equity Securities Suitability Determination

RRs have a higher obligation to determine suitability when recommending the purchase or short sale of OTC equity securities. This includes obtaining current financial statements (balance sheet, P&L, *etc.*) and "current material business information" which includes information available that relates to material events that occurred in the 12 months prior to the recommendation. "Current material business information" is defined as information that is ascertainable through the reasonable exercise of professional diligence and that a reasonable person would take into account in reaching an investment decision. If the issuer is delinquent in its filings (SEC, foreign authority, bank, or insurance regulator), an inquiry must be made about the circumstances about the failure to make current filings.

Prior to recommending a security subject to this policy, the RR is required to complete a copy of the OTC Equity Securities Suitability Form and submit the form and the required financial statements and material business information (and information if the issuer is delinquent in its filings) for review and approval by the RR's designated supervisor. Upon approval, the RR may recommend the security to customers. Failure to complete the

Form and obtain the required approval may result in cancellation of the transactions and assessment of resulting losses to the RR.

12.4.3.3 Exemptions

The requirement to submit the form and obtain prior approval does not apply to the following:

- long sales
- transactions meeting the requirements of Rule 504 of Regulation D and transactions with an issuer not involving a public offering under Section 4(2) of the Securities Act
- recommendations to institutional buyers as defined in FINRA Rule 4512(c)
- recommendations to a QIB (qualified institutional buyer) under Rule 144A
- recommendations to a "qualified purchaser" under Section 2(a)(51) of the Investment Company Act
- transactions in the securities of issuers with at least \$50 million in assets and \$10 million in shareholder equity
- transactions in securities of a bank or insurance company subject to regulation by state or federal bank or insurance authority
- transactions in a security that has a bid price published in a quotation medium of at least \$50 per share. If the security is a unit composed of one or more securities, the bid price of the unit divided by the number of shares of the unit that are not warrants, options, rights, or similar securities must be at least \$50.

12.4.4 Investing Liquefied Home Equity

[FINRA Notice to Members 04-89]

Increasing home prices and refinancing have provided homeowners with access to funds, some going into investments. Recommending or facilitating liquefying of home equity to purchase securities is not suitable for all investors. RRs are obligated to consider whether investing these funds is suitable including the following factors:

- How much equity does the investor have in the home?
- What is the level of equity being liquefied for investments?
- How will the investor meet increased mortgage obligations?
- Is the mortgage or home equity loan at a fixed or variable rate?
- What is the investor's risk tolerance with respect to the funds being invested?
- What is the investor's overall debt burden?
- What is the sustainability of the value of the investor's home?

The following is required **prior to** recommending investing home equity funds:

- Provide the Investing liquefied home equity disclosure
- Withdrawal of home equity may not exceed 50% of the home's value
- The RR's supervisor must approve the liquefying of home equity and resulting investment
- Disclose that the firm or an affiliate will earn fees from the refinancing
- Disclose that the firm will earn fees or other remuneration from referring the investor to a third party for liquidation

12.4.5 Proprietary Products

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
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Resources	<ul style="list-style-type: none"> • Proprietary products
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Subject new proprietary products to the new product review procedure • Review transactions in proprietary products for suitability and take corrective action when necessary • Provide training to RRs
Record	<ul style="list-style-type: none"> • Records of training provided to RRs • Daily transaction records including date of review and initials of reviewer

Products developed by CEI, or an affiliate of CEI, may be offered for sale to customers. New proprietary products are subject to the new product review described in the chapter *NEW PRODUCTS AND DUE DILIGENCE*.

RRs are obligated to:

- determine that a proprietary product is suitable for the customer, including consideration of comparable non-proprietary products and related costs to the customer, and
- make recommendations suitable for the customer regardless of the compensation to the RR.

12.5 Fair Prices

[FINRA Rule 2121]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Trade Desk Supervisor; Trade Desk Supervisor's Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Trade blotter • Trade Detail Report from WFCS • Trade Desk Report
Frequency	<ul style="list-style-type: none"> • T+7 for general trading through WFCS • Trade Desk Review Monthly
Action	<ul style="list-style-type: none"> • Review trade blotter, including the green trades, to identify commission or mark-ups/mark-downs that are inconsistent with Firm Guidelines • Where necessary, take corrective action which may include canceling/rebiling the transaction to correct charges, consult with the RR if charges were initiated by him/her, notify trading personnel of inconsistent charges, or consult with Compliance
Record	<ul style="list-style-type: none"> • Trade blotter notations of review and any corrective action taken • Trade Desk Report and evidence of review by email or documentary file

CEI is required to make a reasonable effort to obtain a price for the customer that is fair and reasonable in relation to prevailing market conditions.

12.5.1 Mark-Up Policy

[FINRA Rule 2121.01]

Following is FINRA's Mark-Up Policy in Rule 2121.

12.5.1.1 General Considerations

1. The historical "5% Policy" is a guide, not a rule.
2. A member may not justify mark-ups on the basis of expenses which are excessive.
3. The mark-up over the prevailing market price is the significant spread from the point of view of fairness of dealings with customers in principal transactions. In the absence of other bona fide evidence of the prevailing market, a member's own contemporaneous cost is the best indication of the prevailing market price of a security.
4. A mark-up pattern of 5% or even less may be considered unfair or unreasonable under the "5% Policy."
5. Determination of the fairness of mark-ups must be based on a consideration of all the relevant factors, of which the percentage of mark-up is only one.

12.5.1.2 Relevant Factors

Relevant factors to consider when determining the fairness of a mark-up are as follows:

1. **The Type of Security Involved:** Some securities customarily carry a higher mark-up than others. For example, a higher percentage of mark-up customarily applies to a common stock transaction than to a bond transaction of the same size. Likewise, a higher percentage applies to sales of units of direct participation programs and condominium securities than to sales of common stock.
2. **The Availability of the Security in the Market:** In the case of an inactive security, the effort and cost of buying or selling the security, or any other unusual circumstances connected with its acquisition or sale, may have a bearing on the amount of mark-up justified.
3. **The Price of the Security:** While there is no direct correlation, the percentage of mark-up or rate of commission generally increases as the price of the security decreases. Even where the amount of money is substantial, transactions in lower priced securities may require more handling and expense and may warrant a wider spread.
4. **The Amount of Money Involved in a Transaction:** A transaction which involves a small amount of money may warrant a higher percentage of mark-up to cover the expenses of handling.
5. **Disclosure:** Any disclosure to the customer, before the transaction is effected, of information which would indicate (A) the amount of commission charged in an agency transaction or (B) mark-up made in a principal transaction is a factor to be considered. Disclosure itself, however, does not justify a commission or mark-up which is unfair or excessive in light of all other relevant circumstances.
6. **The Pattern of Mark-Ups:** While each transaction must meet the test of fairness, FINRA believes that particular attention should be given to the pattern of a member's mark-ups.
7. **The Nature of the Member's Business:** FINRA recognizes there are differences in the services and facilities which are needed by, and provided for, customers of members. If not excessive, the cost of providing such services and facilities, particularly when they are of a continuing nature, may properly be considered in determining the fairness of a member's mark-ups.

12.5.1.3 Applicability of Policy

The Policy applies to all securities, whether oil royalties or any other security, in the following types of transactions:

1. A transaction in which a member buys a security to fill an order for the same security previously received from a customer. This transaction would include the so-called "riskless" or "simultaneous" transaction.
2. A transaction in which the member sells a security to a customer from inventory. In such a case the amount of the mark-up would be determined on the basis of the mark-up over the bona fide representative current market. The amount of profit or loss to the member from market appreciation or depreciation before, or after, the date of the transaction with the customer would not ordinarily enter into the determination of the amount or fairness of the mark-up.
3. A transaction in which a member purchases a security from a customer. The price paid to the customer or the mark-down applied by the member must be reasonably related to the prevailing market price of the security.
4. A transaction in which the member acts as agent. In such a case, the commission charged the customer must be fair in light of all relevant circumstances.
5. Transactions wherein a customer sells securities to, or through, a broker/dealer, the proceeds from which are utilized to pay for other securities purchased from, or through, the broker/dealer at or about the same time. In such instances, the mark-up shall be computed in the same way as if the customer had purchased for cash and in computing the mark-up there shall be included any profit or commission realized by the dealer on the securities being liquidated, the proceeds of which are used to pay for securities being purchased.

The Mark-Up Policy is not applicable to the sale of securities where a prospectus or offering circular is required to be delivered and the securities are sold at the specific public offering price.

12.5.1.4 Supervision of Markup Policy through Coastal Trade Desk

Transactions placed with and executed by the Coastal Trade Desk are executed on a riskless-principal basis. Those trades are placed through the trade-desk principal utilizing the firm's inventory account. When securities are transferred from the inventory account, the firm applies a firm markup/markdown. In addition, when the securities are transferred to the customer account, or to another broker-dealer, another markup/markdown may be applied which is paid to the financial advisor.

12.5.1.4.1 Maximum Markup/Markdown; Exceptions

It is the Firm's policy that the maximum gross markup/markdown shall not exceed 2.75%. The factors of Section 12.5.1.2 should be applied when the trade desk supervisor deems it applicable. The Firm recognizes that there may be circumstances in which a larger markup/markdown is justified. In such cases, the Trade Desk Supervisor should complete the Markup Worksheet and forward the same to the appropriate principal (the Trade Desk Supervisor's supervisor) for review and approval. Both the Trade Desk Supervisor and his supervisor shall sign and date the form if approved. The completed form should be forwarded to Compliance for record-keeping purposes.

12.5.1.4.2 Supervision of Markup/Markdown

On a monthly basis, the firm's FINOP, or designee, will obtain the Trade Detail Report from its clearing firm. The Trade Detail Report is a blotter of all of the trading activity for the prior month, including, but not limited to, the Trade Desk.

The firm's FINOP, or designee, will filter from the Trade Detail Report all trading that was not executed by the Coastal Trade Desk. Using the filtered Trade Detail Report, the firm will add a formula that will automatically calculate the markup/markdown percentage for each trade to the report. The formula to calculate markup/markdown is

$ABS[(client\ price) - (firm\ price)] / (firm\ price)$; (ABS means the absolute value of the difference of two variables.)

The FINOP or designee will provide this report ("Trade Desk Report") to the Trade Desk Supervisor's supervisor for review of the markups/markdown for the trade desk transactions that month.

The supervisor will review the Report and memorialize his review by (1) emailing the blotter back to the CCO and his designee(s) stating that the blotter was reviewed and whether any issues were detected concerning markup/markdown, or (2) by printing a hard copy of the blotter, initialing and dating the front page, and maintaining a hard copy file of the reviewed blotters, and otherwise contacting the CCO if there are any detected issues with markup/markdown.

12.5.2 Supervision of Commissions in Fee Billed Accounts

Policy: It is the firm's policy that no sales commissions, concessions, or markup/markdown shall be charged to advisory accounts. This policy does not preclude charging costs such as trade ticket charges and miscellaneous account fees charged by the broker-dealer or custodian.

Procedure:

The firm's designated supervisors of representatives will receive periodic training to consider, when reviewing the Super Vision trade blotter in Smart Station, commissions which may appear in accounts coded for advisory programs.

In addition, the firm shall designate one or more supervisors to perform a risk-based review of the trade blotter on a regular basis. The supervisor will filter the blotter to review accounts coded for advisory fees, and then sort by the commission column largest to smallest to identify possible commissions charged in advisory accounts. The supervisor will at a minimum review all costs in the commission column of the blotter which equal or exceed \$100.00.

For each commission entry equal to or exceeding \$100.00, The supervisor will contact the advisor, trader, or other party with knowledge of the transaction to determine whether the commission was appropriate, such as whether the account was improperly coded or the transaction occurred prior to switching the account to advisory. In cases where the account was not coded properly, the supervisor will instruct the advisor to correct the coding and will document the conversation as a memo in the review file. In cases where the account was changed to advisory the supervisor will determine whether the circumstances justified the commission in light of the switch to advisory, such as notes in Smart Station, length of time between the trade and switch to advisory, etc. If deemed appropriate, the supervisor will document the decision in a memo to the review file.

If the commission is deemed inappropriate, the supervisor will request a correction by the cancel/rebill process.

Frequency: The supervisor will conduct this review at least monthly.

Documentation: PDF of the trade blotter with digital signature to evidence her/his review. The PDF and the reviewed blotter will be maintained in the firm's network Supervision folder, "Trade Blotter Review" subfolder.

12.5.3 Prohibition Against Trading Ahead of Customer Orders

[SEC Regulation NMS Rule 600(b)(30)(ii); FINRA Rule 5320]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Order records/reports
Frequency	<ul style="list-style-type: none">• Reviews: daily, weekly or monthly depending on reports available• Disclosures: when account opened and annually
Action	<ul style="list-style-type: none">• Review for order protection• Provide disclosures (institutional accounts, no-knowledge exception) at account opening and annually thereafter
Record	<ul style="list-style-type: none">• Order records/reports including date reviewed, reviewer's initials, action taken, if appropriate• Records of providing disclosure at account opening and annually• OTC Trading Manager Checklist

A FINRA member firm that accepts and holds an order in an equity security from its own customer or the customer of another broker-dealer without immediately executing the order is prohibited from trading that security on the same side of the market for its own account at a price that would satisfy the customer order, unless it immediately executes the customer order up to the size and at the same price or better price at which it traded for its own account. Pending orders are executed on a first-in/ first-out basis (FIFO). "Customer order" in this section applies to orders for CEI's customers as well as customers of other broker-dealers.

The rule restrictions apply to orders handled during normal market hours and outside normal market hours (if CEI and customer agree to processing the order outside normal market hours).

Exceptions

There are certain exceptions to the prohibition against trading ahead of customer orders.

Large orders and institutional accounts. Regarding orders for institutional accounts [as defined in FINRA Rule 4512(c)] or orders of 10,000 shares or more (unless the orders are less than \$100,000 in value), CEI may trade a security on the same side of the market for its own account at a price that would satisfy the customer order providing CEI has provided clear and comprehensive written disclosure to the customer when the account is opened and annually thereafter that:

- Discloses that CEI may trade proprietarily at prices that would satisfy the customer order, and
- Provides the customer with a meaningful opportunity to opt in to the Rule 5320 protections with respect to all or any portion of the order. If the customer doesn't opt in to the Rule 5320 protections, CEI will presume the customer has consented to the exception. In lieu of written disclosure CEI may provide oral disclosure and obtain the customer's consent on an order-by-order basis, which will be documented on the order for which consent is obtained.

Instead of written disclosure at account opening and annually after, oral disclosure may be made and consent obtained on an order-by-order basis and recorded on the order.

No-knowledge exception. Regarding NMS stocks and where CEI has effective internal controls and information barriers that prevent one trading unit from obtaining knowledge of customer orders held by a separate trading unit, the other trading units may, in a proprietary capacity, continue to trade at prices that would satisfy the customer orders held by the separate trading unit. A description of how customer orders are handled and when CEI's proprietary account may trade at prices that would satisfy the customer's order will be provided at account opening and annually thereafter. For OTC equity securities where CEI has similar controls to prevent a non-market-making trading unit from obtaining knowledge of customer orders held by a separate trading unit, the non-market-making trading unit may trade in a proprietary capacity at prices that would satisfy the customer's order.

Riskless principal exception. Rule 5320 obligations do not apply to CEI's proprietary trades if the trades are for the purpose of facilitating the execution, on a riskless principal basis, of an order from a customer ("facilitated order") providing that CEI:

- Identifies the order as riskless principal when reporting to FINRA (or other SRO); and
- Has written policies and procedures for compliance with FINRA rules regarding riskless principal transactions. Refer to the section *Riskless Principal Transactions* in this chapter.

ISO exception. The restriction against proprietary trades ahead of customer orders does not apply to trading for CEI's account that is the result of an ISO (Intermarket Sweep Order) routed in compliance with Regulation NMS where the customer order is received after CEI routed the ISO.

Odd lot and bona fide error transaction exceptions. The restrictions do not apply to a proprietary trade that is (1) to offset a customer order that is in an amount less than a normal unit of trading; or (2) to correct a bona fide error.

12.5.4 Front Running of Block Transactions

[FINRA Rule 5270]

Knowingly trading ahead of block orders is a manipulative activity that violates securities rules. CEI and its associated persons are prohibited from entering or executing an order to buy or sell a security or related or underlying financial instrument when CEI or associated person has knowledge of material, non-public information about an imminent block transaction in that security or related or underlying financial instrument (stock, option, warrant, *etc.*). The prohibition applies until the information has been made publicly available or has otherwise become stale or obsolete.

This applies to executions in any account where CEI or associated person has an interest, has discretionary authority, or for accounts of customers or affiliates of CEI when the customer or affiliate has been provided the block information by CEI or an associated person.

"Related financial instrument" means any option, derivative, security-based swap, or other financial instrument overlying a security where the value of the security is materially related to, or otherwise acts as a substitute for, the security, as well as any contract that is the functional equivalent of a position in the security.

"Block transaction" means a transaction involving 10,000 shares or more of a security, underlying security, or related financial instrument.

Exceptions include:

- Transactions where CEI has information barriers to prevent disclosure of information
- Transactions in the same security related to a prior customer order in that security

- Transactions to correct bona fide errors
- Transactions to offset odd-lot orders
- Facilitation of block orders (with conditions in the Rule)

Though the Rule specifically applies to block transactions, front running of other orders is not permitted where the interests of CEI or an associated person are placed ahead of the interests of the customer or where misuse of information about an imminent order violates other rules. Refer to FINRA Rule 5270 for specific details regarding the prohibition.

12.5.5 Best Execution

[Exchange Act Regulation NMS; FINRA Rule 5310; FINRA Regulatory Notice 15-46]

CEI has an obligation to provide best execution for its customers' orders, whether executed internally or routed to other broker-dealers. "Best execution" refers to using reasonable diligence to determine the best market to buy or sell a security and obtaining a price as favorable as possible under prevailing market conditions. CEI's obligation to provide best execution also extends to handling and executing orders for customers of other broker-dealers routed to CEI (but not orders that simply execute the order against CEI's quote).

Factors for using "reasonable diligence" include:

- the character of the market for the security, *e.g.*, price, volatility, relative liquidity, and pressure on available communications;
- the size and type of transaction;
- the number of markets checked;
- accessibility of the quotation; and
- the terms and conditions of the order.

The term "markets" is broadly defined, including market centers that are trading a particular security.

12.5.5.1 Orders Involving Securities with Limited Quotations or Pricing Information

Although the best execution requirements in Rule 5310 apply to orders in all securities, markets for securities differ dramatically. One of the areas in which a member must be especially diligent in ensuring that it has met its best execution obligations is with respect to customer orders involving securities for which there is limited pricing information or quotations available.

When there is insufficient pricing information, or less than three available quotations, the firm will execute its best efforts to seek other sources of pricing information such as firms with whom Coastal has traded within the same security, TRACE records in the same or similar security, last quotes or trading price from other broker-dealers, etc.

The Trader will document the process by including screenshots or printouts of the Bloomberg screen, TRACE report, notes of verbal quotations from other broker-dealers (including BD name and individual providing the quote) or other broker-dealer portal screen showing pricing (*e.g.* Mid Atlantic Capital Corp.), for example, and forward those documents to his/her supervisor. The supervisor will initial and date his/her review and maintain the documents in the Home Office as evidence of review.

12.5.5.2 Regular and Rigorous Review of Execution Quality

[FINRA Rule 5310.09]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor (Internalized) • Compliance
Resources	<ul style="list-style-type: none"> • Clearing firm or other agent's report of statistics, review rationale, findings (if applicable)
Frequency	<ul style="list-style-type: none"> • Quarterly
Action	<ul style="list-style-type: none"> • Conduct regular and rigorous reviews of internal executions (if applicable) and order routing to evaluate compliance with best execution responsibilities including: <ul style="list-style-type: none"> ○ Review of data regarding prices and executions ○ Review pre-open orders including single or midpoint pricing as factors to consider ○ Review of aggregate or order-by-order routing of orders to review quality of executions ○ Determine whether to adjust order routing to improve executions ○ Review riskless principal transactions; customer block-sized orders; orders with special pricing terms and conditions; other order types • Where order flow is routed to a BD acting as agent for CEI (clearing firm, other executing BD): <ul style="list-style-type: none"> ○ Obtain other BD's report of statistics, rationale of review, and findings ○ Review data to confirm agent is using reasonable diligence to provide best execution ○ Where deficiencies are noted, consult with agent and, if best execution is determined to be deficient, consider transferring order flow to another BD
Record	<ul style="list-style-type: none"> • Records of reviews of internal or routed customer orders, if applicable • Records of reviews of agent's best execution reviews, action taken, if applicable

CEI conducts regular reviews of its execution quality to determine whether CEI is meeting its obligation for best execution of customer orders. This includes orders that are routed to other broker-dealers on an automated, non-discretionary basis as well as when CEI internalizes order flow.

Where CEI routes its order flow to another broker-dealer that has agreed to handle that order flow as agent for the customer (*e.g.*, a clearing firm or other executing broker-dealer), CEI will rely on that broker-dealer's regular and rigorous review based on the statistical results and rationale of the review disclosed by the broker-dealer and reviewed by CEI.

12.6 Regulation NMS

Regulation NMS was adopted to strengthen the national market system for equity securities. It requires markets to interact in a way that permits orders to seek the best available market. Rule 611, the Order Protection Rule, is the primary rule that affects broker-dealers and requires broker-dealers to prevent "trade-throughs."

12.6.1 Key Definitions

[SEC Regulation NMS Rule 600]

Automated trading center: a trading center that:

- has implemented systems, procedures and rules to display automated quotations in compliance with Regulation NMS;
- identifies all quotations other than automated quotations as manual quotations;
- immediately identifies its quotations as manual quotations whenever it has reason to believe it is not capable of displaying automated quotations; and
- has adopted reasonable standards limiting when its quotations change from automated to manual quotations, and vice versa, to defined circumstances that promote fair and efficient access to its automated quotations.

Directed order: a customer order that the customer specifically instructs the broker or dealer to route to a particular venue for execution.

Intermarket sweep order (ISO): a limit order for an NMS stock that meets the following requirements:

- When routed to a trading center, the limit order is identified as an intermarket sweep order; and
- simultaneously with the routing of the ISO limit order, one or more additional limit orders, as necessary, are routed to execute against the full displayed size of any protected bid, in the case of a limit order to sell, or the full displayed size of any protected offer, in the case of limit order to buy, for the NMS stock with a price that is superior to the limit price of the ISO limit order. These additional routed orders also must be marked "ISO."

An ISO is premised on the condition that the trading center or broker-dealer responsible for routing the ISO will have attempted to access all better-priced protected quotations. This exception facilitates the execution of certain types of orders, such as large block orders.

Market center: any exchange market maker, OTC market maker, alternative trading system, national securities exchange, or national securities association.

NMS security: any security or class of securities for which transaction reports are collected, processed, and made available pursuant to an effective transaction reporting plan, or an effective national market system plan for reporting transactions in listed options.

Protected quotation: a quotation in an NMS stock that:

- is displayed by an automated trading center;
- is disseminated pursuant to an effective national market system plan; and
- is an automated quotation that is the best bid or best offer of a national securities exchange (including NASDAQ) or the best bid or best offer of a national securities association.

To be protected, the quotation must be immediately and automatically accessible.

Trade-through: the execution of a trade as principal or agent during regular trading hours at a price inferior to protected quotations.

Trading center: a national securities exchange or national securities association that operates an SRO trading facility, an alternative trading system, an exchange market maker, an OTC market maker, or any other broker or dealer that executes orders internally by trading as principal or crossing orders as agent.

12.6.2 Trade-Throughs

[SEC Regulation NMS Rule 611; SEC Division of Market Regulation Responses to Frequently Asked Questions Concerning Rule 611 and Rule 610 of Regulation NMS]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Internal or third-party reports on NMS compliance
Frequency	<ul style="list-style-type: none"> • Timeframes (daily, weekly, monthly, other) corresponding to available reports
Action	<ul style="list-style-type: none"> • Review reports for trade-throughs • For trade-throughs <ul style="list-style-type: none"> ○ Review reason for trade-through ○ Consult with trading/order desk personnel ○ Take corrective action which may include: <ul style="list-style-type: none"> ▪ Correcting the trade which may include price improvement or cancellation of trade ▪ Training for trading personnel ▪ Review of order routing/execution systems ▪ Consultation with Compliance regarding other action
Record	<ul style="list-style-type: none"> • Internal or third-party reports with records of action taken

Firms that route orders have the obligation to prevent trade-throughs, i.e., execution of orders at prices inferior to protected quotations. While the purpose of the NMS is to connect markets to afford orders the best available price, broker-dealers have obligations to seek the best available market. Order routers have three tools available to control the handling of orders to comply with Rule 611:

- a limit price (preclude execution at a price inferior to the limit)
- an immediate-or-cancel (IOC) designation (triggers the requirement for automated quotations and particularly that the trading center provide an immediate response to the order)
- an ISO designation (the BD routing the order assumes responsibility)

Exceptions for transactions that trade-through a protected quotation include:

- a transaction effected by the trading center solely to correct a bona fide error (records of facts and circumstances of the error must be maintained and the transaction recorded in the trading center's error account) [SEC Release No. 34-55884]
- an order that meets the terms and conditions of a "Print Protection Transaction" [SEC Release No. 34-55883]
- an order involving one or more NMS stocks that are components of a qualified contingent trade [SEC Releases No. 34-54389 and 34-57620]
- the trading center displaying the protected quotation that was traded through was experiencing a failure, delay or malfunction
- a trade that is not "regular way"

- single-priced opening, reopening, or closing transaction by the trading center
- a trade executed at a time when a protected bid was priced higher than a protected offer in the NMS stock
- an ISO order
- the trade was effected by a trading center that simultaneously routed an ISO order to execute against the full displayed size of any protected quotation that was traded through
- a trade that was not based on the quoted price of the NMS stock at the time of execution and for which the material terms were not reasonably determinable at the time the commitment to execute was made
- the trading center displaying the protected quotation that was traded through had displayed, within one second prior to execution of the trade-through transaction, a best bid or offer for the NMS stock with a price that was equal or inferior to the price of the trade-through
- an order for which, at the time of receipt of the order, the trading center had guaranteed an execution at no worse than a specified price (with conditions)
- transactions in non-convertible preferred securities [SEC Release No. 34-57621]
- other exceptions published by the SEC

12.6.3 Best Execution

Complying with trade-through obligations does not supplant the requirement for best execution. CEI is still obligated to use reasonable diligence to obtain the best execution of customer orders and will continue to conduct best execution reviews of the quality of order routing including orders executed internally.

12.6.4 Intermarket Sweep Orders (ISOs)

When an order is designated as an ISO, the receiving trading center will execute the order without regard to any better-priced protected quotations at other trading centers. When CEI enters an ISO, it is required to route additional ISOs to execute against any better-priced quotations at other trading centers.

12.6.5 Third-Party Vendors

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Contract with third party • Reports available from third party
Frequency	<ul style="list-style-type: none"> • Upon inception and periodically at renewal - contract with third party • Timeframes (daily, weekly, monthly, other) corresponding to available reports • Quarterly - conduct best execution reviews
Action	<ul style="list-style-type: none"> • Review third party's order handling capabilities and ability to comply with Regulation NMS requirements • Execute contract with third party and review contract at time of renewal • Review reports for compliance with NMS • Where compliance is in question: <ul style="list-style-type: none"> ○ Confer with third party ○ Determine corrective action if necessary ○ Make adjustments to trades if necessary ○ Consider alternative third parties if necessary • Conduct best execution reviews to determine quality of executions by third party

Record	<ul style="list-style-type: none"> • Contracts with third party • Reports and records of corrective action • Records of best execution reviews
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If CEI employs a third party to handle orders on its behalf, it will consider the third party's ability to comply with Regulation NMS and regularly review the quality of order executions.

12.7 Orders in Volatile Stocks

[FINRA Notice to Members 99-11; FINRA Regulatory Notice 16-19]

Some securities are characterized by volatility of price and volume. This has, in particular, been a characteristic of some Internet stocks. The RR should know the potential affect of volatility on recommended stocks and discuss these risks when recommending such investments with customers unfamiliar with transactions in these types of securities. Following are some of the conditions potentially affecting volatile stocks:

- High volume in volatile stocks may result in delays in execution at the opening or during the trading day.
- Market orders may be executed at a price significantly different from the current quote. The benefits and risks of market vs. limit orders should be discussed.
- Orders for IPOs in the secondary market may be executed at prices significantly away from the current quote, and, because of "fast market" conditions, the current quote may not be up to date.
- Volatile stocks may be subject to higher margin requirements or not available for purchase on margin.

10.8 Sales of Illiquid Investments

[FINRA Regulatory Notice 08-30]

Customers may contact an RR, on an unsolicited basis, to sell an illiquid investment, and may have a prospective buyer. To effect the transaction, the following is required:

- The RR must have or obtain the required new account information for both the buyer and the seller.
- Both the buyer and the seller must sign a letter confirming that the orders are unsolicited; that CEI is not recommending the transactions or making a suitability determination; and CEI cannot make a determination regarding the sufficiency or competitiveness of pricing of the transactions.
- The RR must have no concerns regarding the ability of both sides to settle the proposed transaction.

The RR may advise the seller of potential buy interest. The letter described above must be signed by both parties and include disclosure that CEI will receive compensation for effecting the transactions.

If orders for illiquid securities are solicited, the RR is responsible for making a suitability determination in addition to obtaining the written acknowledgments.

The RR's designated supervisor must review and approve the transaction for compliance with this procedure.

12.9 Account Designation and Cancels/Rebills [Errors]

[FINRA Rule 4515]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
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Resources	<ul style="list-style-type: none"> • Cancel/Rebill form • Cancel/Rebill Report • FINRA Cancelled and As-Of Trades Report
Frequency	<ul style="list-style-type: none"> • Daily review of forms presented • Monthly review of Report
Action	<ul style="list-style-type: none"> • Review frequent cancellations and cancel/rebills which may be indicative of unauthorized trades • Review and approve or disapprove cancels and rebills. • For cancels from one account to another, particularly review reason for cancel and rebill prior to approval. • Review Cancel/Rebill Report for patterns by customer and/or by RR. • Where patterns appear confer with RR. • Where patterns continue to appear, contact customers whose orders were cancelled to confirm orders were originally authorized. • If customers advise transactions are unauthorized, contact Compliance. • Compliance: Review FINRA report and follow up regarding patterns of cancelled or as-of trades (contact RR and RR's supervisor, customer contact or other appropriate action)
Record	<ul style="list-style-type: none"> • Initials on Cancel/Rebill Form • Initials and date on Cancel/Rebill Report • FINRA Report including notes of action taken retained by Compliance • For patterns of cancellations, notes of review and action taken on reports reviewed or included on supervisor's log, day timer, or other record, if appropriate.

Each order, prior to execution, must include the account name or designation on the order with the exception of investment adviser order allocations explained in the next section.

Whenever an order is cancelled and rebilled to another account (including changes between related or same-owner accounts), the Cancel and Rebill Form must be completed and approved by the designated supervisor and retained with the order record. The supervisor must document the essential facts relied upon to approve the change.

12.9.1 Allocation of Investment Adviser Orders

[FINRA Rule 4515.01]

Orders may be accepted from the investment adviser allowing the investment adviser to later identify the name or designation of the accounts for which the order is to be executed. Specific account designations or customer names must be received by noon of the next business day following the trading session. This exception applies only where there is more than one customer for any particular order.

The exception applies to outside registered investment advisers and associated persons who provide investment advisory services on behalf of CEI acting as a registered investment adviser. This does not apply to RRs who have discretionary authority over customer accounts subject to NASD Rule 2510 "Discretionary Accounts."

12.10 Time and Price Discretion

[FINRA Rule 3260 and 4512(a)(3)]

With the customer's consent, time and price discretion may be used for orders for a definite amount of a specific security without written authorization from the customer. The duration of this authority is limited to the end of the business day on which the order was received. Discretion beyond the same day requires establishment of discretionary authority and signed and dated authorization from the customer. Refer to the chapter *ACCOUNTS* and the section *Discretionary Accounts* for procedures for establishing and handling discretionary accounts.

Exercise of time and price discretion should be noted on the order record.

This limitation does **not** apply to time and price discretion exercised in institutional accounts pursuant to valid good 'til cancelled instructions issued on a "not held" basis. "Institutional account" includes a bank; savings and loan association; insurance company; registered investment company; registered investment adviser; and any other entity (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least \$50 million.

12.11 Trading Halts

[FINRA Rule 5260, 6120, 6121 and 6440; NASDAQ Rule 3340, 4120 and 4121]

When trading halts occur, whether they are for specific securities or circuit breakers that close entire markets, orders are handled as follows:

- When trading is resumed on the same trading day, pending and new customer orders are forwarded to the appropriate market for execution upon resumption of trading, unless the customer instructs otherwise.
- When trading is closed for the duration of the trading day, pending and new customer orders are treated as follows:
 - Orders pending at the time of the halt and new orders received after the halt commences are treated as "Good Til Cancelled" and held for execution at the reopening of the next trading session (unless the customer instructs otherwise).
 - "At-the-Close" orders (including "Market-on-Close" orders) pending at the time trading is halted are treated as cancelled orders. No new orders relating to closing prices received during a trading halt are accepted or forwarded to a market.

If CEI maintains a web page, a notice will be promptly posted stating that circuit breaker halts have closed the markets and explaining how pending or new orders will be handled.

12.12 Trade Reporting by Third Parties

[2007 Member Alert: Notice to All TRF, ADF and Other FINRA Facility Participants Regarding AGU and QSR Relationships]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Transaction data• FINRA compliance report cards
Frequency	<ul style="list-style-type: none">• Monthly

Action	<ul style="list-style-type: none"> • Execute agreement(s) with third party ("give up agreement") in the form specified by FINRA and/or a QSR agreement • Review trade data and compliance reports to determine accuracy of third party reporting • If errors are noted: <ul style="list-style-type: none"> ○ Confer with the third party regarding what corrective action will be taken to prevent future errors ○ If errors persist, consider changing third party reporting agents
Record	<ul style="list-style-type: none"> • Transaction data and reports reviewed (including date reviewed, who reviewed, action taken)

When a third party is used for clearing, reporting or locking-in trades, whether under an Automated Give Up (AGU), Qualified Service Representative (QSR) or other arrangement, the third party's reporting will be periodically reviewed for compliance with requirements.

12.13 Trading Systems and Electronic Transmission of Orders

[FINRA Notice to Members 04-66]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Trade data • Operating system procedures
Frequency	<ul style="list-style-type: none"> • Authorizing access persons - as required • Review of errors - daily as required • Testing of system - at least annually
Action	<ul style="list-style-type: none"> • Provide passwords to persons authorized to access trading systems • Provide training to those with authorized access • Review and correct errors in accordance with CEI's trade error procedures described in a section of this chapter • If access is provided to correspondents or other parties, obtain their written control procedures and a written undertaking the other party will abide by the procedures
Record	<ul style="list-style-type: none"> • Errors are documented in accordance with trade error procedures • Testing and/or audits of trading systems is documented in reviews of systems and/or audits of business units • Correspondents' written control procedures and undertaking (if applicable)

This section describes supervisory procedures to prevent errors when entering orders through order-routing and execution systems ("trading systems").

- Only authorized persons are permitted to access trading systems. Access is password-protected.
- Order entry personnel will receive training regarding order entry procedures and proper operation of the system.
- Orders will be validated for accuracy and identification of duplicate or re-transmitted orders.

- Limits on order entry include order size and/or credit limits.
- Errors due to system failure, order entry errors, or other system-related errors will be corrected internally. FINRA's "clearly erroneous transaction" procedures are not available to correct such errors.
- The system will be tested periodically. Testing connectivity to regulators' systems will be conducted using procedures established by the regulator with test orders clearly marked as such and not sent in the guise of an actual order.

12.14 Order Records

[SEC Securities Exchange Act of 1934 Rule 17a-3 and Rule 17a-4; FINRA Rule 5340 and 7440]

Certain information must be recorded for orders accepted by CEI. Orders placed through CEI's clearing firm are placed electronically using Smart Station. Orders processed through CEI's trading desk are memorialized in an Order Memorandum. Information to be recorded includes:

- Identification of the account
- Buy or sell
- If sell, long or short
- If a short sale, an indication the security can be borrowed
- If sell long, an indication that the seller will deliver the security
- If an option, put or call and open or close
- Name of security
- Quantity
- Price (if a limit order)
- Day or GTC (if not a market order)
- Other terms of the order (fill or kill, stop limit, *etc.*)
- If a discretionary account, notation whether discretion is exercised or not exercised (DE or DNE)
- Identity of RR responsible for the account, if any
- Identity of other person(s) who entered or accepted the order
- Date and time order is received and entered (pre-timing of orders for block positions is prohibited)

Other information to be recorded for the order includes:

- If the customer's order is granted a stop (*i.e.*, price protection on an order as negotiated by CEI and the customer), the stop is to be noted on the order
- Any modification to/cancellation of order or instructions
- Execution price
- Date and time of execution or cancellation
- If the customer enters the order on an electronic system, a notation regarding electronic entry

12.14.1 Large Trader Definition

A Large Trader is defined as a person, including a firm or individual, whose transactions in NMS securities equal or exceed (1) 2 million shares or \$20 million during any calendar day or (2) 20 million shares or \$200 million during any calendar month (the "identifying activity level" for filing Form 13H). "Transactions" for purposes of identifying a Large Trader exclude: (1) transactions part of an offering; and (2) sales by a selling shareholder in connection with an IPO or in a secondary offering if the seller is a current or former associated person of the issuer and securities being sold were part of the associated person's compensation.

An ownership level of 25% would generally give a person "control" for purposes of Large Trader designation. Multiple persons within a corporate group may qualify as Large Traders. If a natural person or subsidiary entity

within a large organization independently qualifies as a Large Trader, a parent company of that Large Trader may file on Form 13H and identify itself as the Large Trader on behalf of the group, removing the requirement of the subsidiary to separately identify as a Large Trader.

12.14.2 Identifying Activity Level

It is the identifying activity level that identifies a person as a Large Trader. Offsetting or netting transactions among or within accounts, even for hedged positions, are added to a market participant's activity level in order to show the full extent of a trader's purchase and sale activity. When aggregating transactions, the Large Trader would determine across all accounts over which it has investment discretion:

- The volume or fair market value of transactions in equity securities and the volume or fair market value of the equity securities underlying transactions in options on equity securities, purchased and sold; and
- The fair market value of transactions in options on a group or index of equity securities (or based on the value thereof), purchased and sold.

The rule should be consulted for transactions exempt from the identifying activity level including gifts, journals/bookkeeping entries, issuer offerings, and other exemptions.

12.14.3 Large Trader Identification Number (LTID)

The SEC assigns each large trader an LTID. Large traders are obligated to disclose this number to the registered broker-dealers effecting transactions on its behalf and identify for them each account to which it applies. The LTID is one of the elements to be included in consolidated audit trail reporting.

12.14.4 Filings

Large traders are required to make filings of Form 13H which is a web-based form.

Initial filing: Large Traders are required to identify themselves to the SEC by filing Form 13H [Rule 13h-1(b)]. The initial filing is due within 10 days after the Large Trader meets or exceeds the identifying activity level.

Annual filing: Submit an annual filing of Form 13H within 45 days after the end of each calendar year.

Amended filing: Inaccurate filings must be promptly corrected following the end of the calendar quarter in which the prior filing becomes inaccurate for any reason. For example, changes to the name, business address, *etc.* would require an amended filing.

Inactive status: Form 13H is not required if a person does not meet or exceed the identifying activity level. If the person does not anticipate meeting the level again, it may file for "Inactive Status."

Reactivated status: If a person on Inactive Status meets or exceeds the identifying activity level, it must file for Reactivated Status within 10 days.

Termination filing: Persons may terminate Large Trader status by submitting a Termination Filing. For example, if a person ceases operations, dissolves, or is acquired.

12.15 Conflicts of Interest

12.15.1 Adverse Interest

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Daily Alerts
Frequency	<ul style="list-style-type: none"> • T+7 or monthly for monthly alerts
Action	<ul style="list-style-type: none"> • Review Employee/client alerts for transactions where an RR is on the other side of the trade from the customer • Ensure the customer's confirmation includes a trailer disclosing an associated person was on the other side of the transaction, OR, • Send the customer a disclosure letter
Record	<ul style="list-style-type: none"> • Customer confirmation, OR • Copy of disclosure letter to customer which is maintained in the branch customer file

When an RR is on the opposite side of a transaction from a customer (customer sells a security and the RR is the purchaser, or customer buys a security and the RR is the seller), the RR may be considered to have an "adverse interest" in the transaction. The branch manager or other designated supervisor should require a disclosure on the customer's confirmation or a letter to the customer disclosing that the associated person was on the opposite side of the transaction.

10.15.2 Precedence of Customer Orders

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Daily alerts
Frequency	<ul style="list-style-type: none"> • T+7 or monthly for monthly alerts
Action	<ul style="list-style-type: none"> • Identify orders where the RR has received a better price for a transaction in the same security, on the same day, and on the same side of the market (buy or sell) as the RR's customer • Adjust the customer's order to the better price, if appropriate
Record	<ul style="list-style-type: none"> • Order adjustments are included in records of the day's orders

The customer's interest has precedence over any associated person's personal interest. While there is no standard that applies in every case, in general, RRs will solicit customer orders before entering orders for personal accounts in the same security. When an RR receives a better price in a security the same day the RR's customer executes an order in the same security on the same side of the market (buy or sell), the customer will generally receive the better price unless there are circumstances that justify the RR's better price (time of order entry, inability to reach customer, *etc.*).

12.15.3 Disclosure of Control Relationship

[FINRA Rule 2262]

When a customer effects a transaction in a security where the issuer controls, is controlled by, or is under common control with CEI, CEI will provide the customer with a disclosure in writing at or before completion of the transaction. This is usually accomplished by included disclosure on the customer's confirmation.

12.16 Review of Customer Transactions

12.16.1 Review of Daily Transactions

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Order records/Subscription and disclosure documents• Smart Station alerts
Frequency	<ul style="list-style-type: none">• T+7 or monthly for monthly alerts
Action	<ul style="list-style-type: none">• Review orders for, among other possible items:<ul style="list-style-type: none">○ Completeness of order records○ Suitability of transactions○ Discretionary account orders○ Orders requiring approval○ Excessive commissions○ Unauthorized transactions○ Wash sales/prearranged trades○ Prohibited orders• For orders contrary to CEI policy or rule requirements, take corrective action which may include:<ul style="list-style-type: none">○ Confer with the RR to clarify the transaction, if necessary○ Cancel and rebill the transaction to reflect appropriate charges○ Cancel the transaction to CEI's error account○ Confer with Compliance regarding additional education for the RR and/or disciplinary action
Record	<ul style="list-style-type: none">• Electronic approval or review note on flagged trades, and on order records requiring approval• Signature on direct business records

Orders are reviewed on a risk-based alert system for compliance with order requirements through Smart Station, and on an order-by-order basis for direct business.

12.16.2 Unauthorized Transactions

Reviews of transactions should include identification, where possible, of unauthorized transactions. Potential indicators of unauthorized transactions may include patterns of:

- Cancellations of transactions

- Cancels and rebills between accounts
- Sellouts for failure to pay for purchases
- Numerous extensions

The designated supervisor is expected to take corrective action regarding potential unauthorized transactions. Corrective action may include, depending on the circumstances:

- Confer with the RR
- Contact customers directly to confirm authorization of transactions
- Cancellation of unauthorized transactions
- Confer with Compliance regarding any identified unauthorized transactions

12.16.3 Review of Account Activity by Designated Supervisors

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Customer monthly statements • Posting records • New account forms
Frequency	<ul style="list-style-type: none"> • When active account reviews are triggered, or when further account review is required in Designated Supervisor's judgment
Action	<ul style="list-style-type: none"> • Review customer transactions records for suitability of transactions • Refer to new account forms when necessary to identify investment objectives and other customer information • When reviewing a Smart Station active account review, populate the Account Review Worksheet as prompted • Confer with RR regarding suitability questions • Confer with Compliance when necessary • Contact customer when necessary to confirm customer's understanding of and agreement with transactions • Modify or restrict future transactions, as appropriate
Record	<ul style="list-style-type: none"> • Electronic signature/Initials on Smart Station • Initial and date any paper records reviewed • Supervisor's Log

Designated Supervisors are expected to review customer account activity when an active alert review is populated in Smart Station, and when in the judgment of the supervisor, facts and circumstances warrant a deeper review of an account or book of a registered representative. This may be accomplished by reviewing the monthly statements, posting records, and/or other cumulative transaction information of selected RRs. Smart Station provides a built-in account review worksheet which must be used to review system generated Account Review Alerts. Account Reviews may also be initiated in Smart Station if desired.

12.17 Trade Errors

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Cancel/Rebill Form
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Frequent errors by RRs may indicate poor work habits, insufficient manpower to properly enter orders, deficiencies in understanding proper order entry procedures, or unauthorized trading. It is the Branch Manager's responsibility to minimize trade errors in the branch; take immediate corrective action when an error is identified; and take follow up corrective action as necessary. <ul style="list-style-type: none"> ○ Instruct the wire operator or other order entry person regarding action to correct the error ○ Approve Trade Error Forms ○ Identify patterns of errors by individual RRs ○ Where patterns are identified, confer with the RR regarding any order entry problems and the reasons for frequent errors ○ Take corrective action as appropriate
Record	<ul style="list-style-type: none"> • Initials on Trade Error Forms • Notes regarding corrective action in the RR's file or on the supervisor's log, day timer, or other record, as appropriate

Trade errors are to be immediately reported to the designated supervisor for correction. RRs are not permitted to correct errors themselves.

CEI may not cover losses for investors by treating transactions as errors when, in fact, they are not errors. Some customers may request such an accommodation in exchange for future business. Absorbing losses is a violation of SRO rules and is not permitted.

12.18 Sellouts

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Operations
Resources	<ul style="list-style-type: none"> • Notices from Operations regarding sellouts
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Operations: Notify the RR and supervisor that customer's payment is due • If the customer does not pay for the trade, sell out the customer's position • Remove the transactions from the customer's account through cancel/rebill • Review the circumstances of the sellout • If there is a loss, charge the RR (unless an exception is warranted) • Identify patterns of customer reneges which may reflect: <ul style="list-style-type: none"> ○ Potential unauthorized transactions ○ A customer whose account should be closed

	<ul style="list-style-type: none"> • Take corrective action, if necessary, which may include discussing sellouts with the RR; reviewing new account documentation; contacting the customer; closing the account; contacting Compliance regarding possible disciplinary action against the RR
Record	<ul style="list-style-type: none"> • Sellouts are included in the day's order records • Review of sellout, cancel/rebill of transactions • Investigation of repeat sellouts and corrective action taken

Customers who fail to pay for transactions will be subject to sellouts to close out the unpaid security position. RRs will be charged for any unpaid balance remaining after the sellout.

12.19 Issuer Repurchases of Common Stock

[SEC Securities Exchange Act of 1934 Rule 10b-18]

Rule 10b-18 provides a "safe harbor" when an issuer (or its affiliate) repurchases its own outstanding common stock, including purchases to effect a merger or acquisition or as a "going private" effort. The safe harbor enables the issuer to avoid violations of the anti-manipulation rules. To come within the safe harbor, the issuer must meet four conditions on each day it bids for and repurchases shares of its common stock (manner of entry, timing, pricing, and volume conditions).

Because the Rule is technical and complex, the appropriate trader or Compliance should be consulted regarding questions about the issuer's obligations and CEI's role under the Rule. RRs may not give advice to issuers on 10b-18 compliance; issuers should be encouraged to consult with their own counsel.

The following is a brief summary of Rule 10b-18 conditions. **Other requirements not listed here are included in the Rule.**

- All bids and purchases must be made through or by only one broker or dealer in a single day.
- A purchase may not be the opening reported purchase of the day.
- Purchases may not be made at a price higher than the highest independent bid or transaction price at the time of the purchase.
- For issuers having an average daily trading volume of \$1 million or more and a public float value of \$150 million or more, purchases may be made until the day's last 10 minutes of trading. Other issuers are limited to purchases until the day's last 30 minutes of the primary trading session in the principal market for the security.
- The number of outstanding common shares purchased by an issuer on any single day may not exceed 25% of the average daily trading volume of the stock for the 4 calendar weeks preceding the week purchases are made.
- Issuers are permitted to make "block" transactions once a week on a day when no other 10b-18 purchases are made.
- Issuers are required to make disclosures regarding repurchases in their 10-Q and 10-K filings.

12.20 Short Sales

[SEC Regulation SHO; SEC Division of Market Regulation Responses to Frequently Asked Questions Concerning Regulation SHO:
<http://www.sec.gov/divisions/marketreg/mrfaqregsho1204.htm>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Comply with short sale price test requirements through systems to: <ul style="list-style-type: none"> ○ Determine when a covered security becomes subject to the price test ○ Monitor, on a real-time basis, the national best bid to determine permitted execution or display prices ○ Record a "snapshot" of the national best bid at the time a short sale order is submitted ○ Confirm only orders that are exempt are marked "short exempt" ○ Monitor and address latencies in obtaining data regarding the national best bid • For riskless principal transactions that are marked "short exempt," systems are in place to confirm that: (i) the offsetting transaction occurred after the customer order was received; and (ii) the offsetting transaction is allocated to a riskless principal or customer account within 60 seconds of execution • Take reasonable steps to enforce the policies and procedures, including conducting regular post-trade analysis • Review for: <ul style="list-style-type: none"> ○ compliance with price test requirements ○ sell orders marked "long" or "short" or "short exempt" ○ locate information (affirmative determination) on short sells including who was contacted and the date advised the stock could be borrowed
Record	<ul style="list-style-type: none"> • Record of the national best bid at the time of execution or display of a short sale order (e.g., a "snapshot" of the market) • Records (available in a time-sequenced manner) that enable CEI to accurately and readily reconstruct, in a time-sequenced manner, all orders executed based on the riskless principal exemption • Initials or other record of review on order records and action taken, if any • Locate information on order records

A "short sale" is defined as the sale of a security that the seller does not own or any sale that is completed by the delivery of a security borrowed by or on behalf of the account of the seller. The exercise of a long put by someone who does not own the underlying stock to deliver against the exercise will have engaged in a short sale and the stock must be borrowed and delivered within the required timeframe.

Determination of whether a sale is long or short also requires that the seller must net all positions in the security. This includes netting positions held in accounts that are related or under common control. For example, a customer is long 1,000 shares of Security A in an account. The customer also cross guarantees, for Regulation T and margin purposes, a "short account" for the benefit of a family member who is short 1,000 shares of Security A. The net position would be zero; if the customer sells shares of Security A, the sale would be deemed a short sale.

Accounts are considered related or controlled if the customer:

- exercises discretion over the account;
- cross guarantees the account for Regulation T or margin purposes; or,
- has been granted a power of attorney to execute transactions in the account.

12.20.1 Key Defined Terms

"**Listing market**" means the effective transaction reporting plan for the covered security. While the two reporting plans define the term "listing market" similarly, their treatment of dually listed securities differs. Specifically, the CTA Plan looks to where the security was first listed, while the NASDAQ UTP Plan looks to the market with the highest number of the average of the reported transactions and reported share volume for the preceding twelve-month period. The listing market is responsible for monitoring the trading in stocks listed on its marketplace and for notifying market participants when a circuit breaker has been imposed.

The Short Sale Price Test applies to "**covered securities**" which are "NMS Stocks" as defined under Rule 600(b)(47)[4] of Regulation NMS. The Short Sale Price Test covers all securities, except options, that are listed on a national securities exchange whether traded on an exchange or in the OTC market, but does not include non-NMS stocks quoted on the OTC Bulletin Board or elsewhere in the OTC market.

Rule 201 applies to "**trading centers**," which are defined in Rule 600(b)(78) of Regulation NMS as a "national securities exchange or national securities association that operates an SRO trading facility; an alternative trading system; an exchange market maker; an OTC market maker; or any other broker or dealer that executes orders internally by trading as principal or crossing orders as agent." Consequently, any entity that executes a short sale order in a covered security must comply with the Short Sale Price Test.

12.20.2 Short Sale Price Test

[SEC Regulation SHO Rule 201; SEC FAQ concerning Regulation 201: <http://www.sec.gov/divisions/marketreg/rule201faq.htm>]

Short sales of covered securities are subject to a circuit breaker and uptick rule. When a circuit breaker is triggered by the listing market, short selling is permitted only at a price above the current national best bid. The following requirements apply:

- A short sale order may not be executed or displayed at a price that is less than or equal to the current national best bid if the price of the covered security decreases by 10% or more from the security's closing price determined by the listing market as of the end of regular trading hours on the prior day.
- The above requirements apply for the remainder of the day and the following day when a national best bid for the covered security is calculated and disseminated on a current and continuing basis by a plan processor pursuant to an effective national market system plan.

CEI's systems identify covered securities subject to price test requirements. Traders are responsible for complying with price test requirements.

10.20.2.1 Exemptions to The Short Sale Price Test

There are several exemptions to the Short Sale Price Test. The exemptions apply when the price test circuit breaker is triggered. When relying upon the following exemptions, a broker-dealer must mark the order "short exempt."

- **Broker-Dealer Provision.** Rule 201 permits a broker-dealer to mark certain qualifying sell orders as "short exempt" if the broker-dealer reasonably determines that it is submitting the short sale order to the trading center at a price that is above the current national best bid at the time of submission.

- **Sellers Delay in Delivery.** Orders may be marked "short exempt" when a broker-dealer has a reasonable basis to believe that a seller owns the securities, but is unable to deliver them prior to settlement because of circumstances outside of the seller's control.
- **Odd Lot Transactions.** An odd lot short sale order may be marked "short exempt" by a market maker if it has a reasonable basis to believe that the order offsets a customer odd-lot order or liquidates an odd-lot position that changes such broker-dealer's position by no more than a unit of trading.
- **Domestic and International Arbitrage.** Certain domestic or international arbitrage transactions may be marked "short exempt."
- **Over-Allotments and Lay-Off Sales.** Rule 201(d)(5) permits a broker-dealer to mark as "short exempt" short sale orders by underwriters or members of a syndicate in connection with over-allotments, or in connection with lay-offs by the same persons through a rights or standby underwriting commitment.
- **Riskless Principal Transactions.** Rule 201(d)(6) permits a broker-dealer to mark short sale orders "short exempt" when the broker-dealer facilitates customer buy orders or sell orders where the customer is net long, and the broker-dealer is net short but is effecting the sale as riskless principal. Rule 201(a)(8) defines the term "riskless principal" to mean "a transaction in which a broker or dealer, after having received an order to buy a security, purchases the security as principal at the same price to satisfy the order to buy, exclusive of any explicitly disclosed markup or markdown, commission equivalent, or other fee, or, after having received an order to sell, sells the security as principal at the same price to satisfy the order to sell, exclusive of any explicitly disclosed markup or markdown, commission equivalent, or other fee."
- **Transactions on a Volume-Weighted Average Price Basis.** Orders executed on a volume-weighted average price ("VWAP") may be marked "short exempt" provided that they satisfy several conditions in Rule 201(d)(7).

12.20.3 Marking Orders

[SEC Regulation SHO Rule 200(g)]

All sell orders are required to be identified on the order record as "long," "short," or "short exempt" (if applicable) at the time of entry.

A sell order may be marked "long" when the seller owns the security being sold and the security either is in the physical possession or control of CEI or it is reasonably expected that the security will be in the physical possession or control of CEI by settlement date.

A sell order should be marked "short" when the security being sold is not owned by the seller and will require it to be borrowed to make delivery by settlement date. See the section *Locate And Delivery Requirements* regarding the requirement to borrow securities.

Short sales effected in covered securities when a circuit breaker price test is triggered may be marked "short exempt" if they qualify for the exemption.

12.20.4 Locate and Delivery Requirements

[SEC Regulation SHO Rule 203]

Prior to effecting a short sale in an equity security, there is an obligation to "locate" securities available for borrowing and delivery by settlement date. The "locate" must be determined prior to order entry. Exceptions to this requirement are listed below.

It is the RR's responsibility to contact Operations (or consult a "borrow" list if available) to confirm whether the security being sold short may be borrowed. The borrow list relied upon must be less than 24 hours old. The following locate information must be recorded on the order:

- if obtained from a person, the name of the person and the number of shares to be borrowed and the date
- if obtained from an authorized "borrow list," notation that the list was consulted and the date

If affirmation is obtained from someone outside CEI, the order record must also include the name of the person's employer.

12.20.4.1 Exceptions from the Locate Requirement

The following short sale orders are not required to comply with the locate requirement:

- Orders received from another broker-dealer (the originating broker-dealer has the obligation to comply with the locate requirement)
- *Bona-fide* market making transactions

12.20.5 Close-Out Requirements for Fail to Deliver

"Naked short selling" is an abusive practice where the seller does not intend to deliver securities in time for settlement (including deceiving a broker-dealer about their locate source or ownership of shares). Close-out requirements apply to **all** equity securities. Obligations to close-out fails to deliver are the responsibility of the participant of a registered clearing agency, *i.e.*, a broker-dealer that self-clears its own trades or the clearing firm on behalf of an introducing firm. The SEC's rules apply to "reporting securities" which are issuers registered under Section 12 of the Exchange Act or that are required to file reports under Section 15(d) of the Exchange Act. FINRA requirements apply to securities not covered by SEC Regulation SHO.

Operations (or a clearing firm if orders are introduced to a clearing firm) is responsible for closing out positions.

12.20.5.1 SEC Requirements for Reporting Securities

[SEC Securities Exchange Act of 1934 Rule 10b-21; SEC Regulation SHO Rule 204]

To prevent this abusive practice, the SEC has imposed requirements that **securities must be delivered for short sales of all equity securities by settlement date (T+3)**. If securities are not delivered by settlement day, the broker-dealer is obligated to close out the position by borrowing or purchasing securities by the beginning of regular trading hours on the following settlement day (T+4). **For long sales and bona fide market making activity**, the BD must close out the position no later than the beginning of regular trading hours on the 3rd consecutive settlement day following the settlement date (T+6).

For sales of securities under Rule 144 and other securities the seller is "deemed to own" and intends to deliver (such as securities not yet received after exercising an option or warrant): transactions must be closed out no later than the beginning of regular trading hours on the 35th calendar day following the settlement day for the transaction.

The purchase or borrow of securities does not qualify as a close-out if the BD or participant knows or has reason to know the securities will not actually be delivered by settlement [Rule 204(f)].

When a BD fails to close out a position as required under this rule, the BD may not accept a short sale order in that security from another person or effect an order in its own account until the fail to deliver is closed out.

12.20.5.2 FINRA Requirements for Non-Reporting Securities

[FINRA Rule 4320]

Participants of registered clearing agencies must take action on failures to deliver that exist for 13 consecutive settlement days in certain non-reporting securities. If the fail to deliver position is not closed out in the requisite time period, the participant or any firm for which it clears is prohibited from effecting further short sales in the security without borrowing, or entering into a bona fide arrangement to borrow, the security until the fail to deliver position is closed out.

12.20.6 Short Sales of Securities Subject To A Public Offering

[SEC Regulation M Rule 105; SEC Release No. 34-56206]

A person may **not** purchase a security from an underwriter or broker or dealer participating in a public offering if the person sold the security short during the "Rule 105 restricted period." The Rule 105 restricted period is the shorter of:

- the period beginning five business days before the pricing of the offered securities and ending with such pricing; or
- the period beginning with the initial filing of the registration statement or notification on Form 1-A or Form 1-E and ending with the pricing.

Exceptions to the short sale limitation include the following.

1. **Bona fide purchases:** Restricted period short sellers may purchase offered securities if they make a bona fide purchase of the same security prior to pricing. A *bona fide purchase* must be:

- at least equal in quantity to the entire amount of the Rule 105 restricted period short sale(s);
- effected during regular trading hours;
- reported pursuant to an effective transaction reporting plan; and
- made after the last Rule 105 restricted period short sale and no later than the business day prior to the day of pricing.

In addition, the person may not have effected a short sale that is a reported transaction within 30 minutes before the close of regular trading hours on the business day prior to the day of pricing.

2. **Separate accounts:** A purchase of the offered security may be made in an account that sold short during the Rule 105 restricted period in a separate account if decisions regarding transactions for the account are made separately and without coordination of trading or cooperation among or between accounts.

3. **Investment companies:** An individual fund within a fund complex, or a series of a fund, will not be prohibited from purchasing the offered security if another fund within the same complex or a different series of fund sold short during the Rule 105 restricted period.

There are conditions that apply to these exceptions; Compliance should be consulted for further guidance regarding covering short sales in securities subject to a public offering.

12.21 Sale of Control or Restricted Stock

[SEC Securities Act of 1933 Rule 144 and Rule 145; SEC Rule 144 Guidance: <http://www.sec.gov/divisions/corpfin/guidance/rule144interp.htm>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Proposed 144 or 145 sales
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Determine the seller's status (affiliate or non-affiliate) • Determine eligibility for selling the amount and timing of sale • Assist the customer in preparation of required forms
Record	<ul style="list-style-type: none"> • Records of forms filed and determinations are included in a file for Restricted Stock sales

12.21.1 Introduction

SEC Rule 144 provides a safe harbor method for affiliates (e.g., controlling shareholders, directors, and executive officers) to sell securities of their company (control securities). Rule 144 applies to non-affiliates on only a very limited basis. Rule 144:

- limits the number of shares sold in any three-month period (affiliates only);
- requires current public information about the issuer;
- imposes a holding period on shares prior to sale;
- places restrictions on how shares may be sold; and
- requires affiliates to file Form 144 (Notice of Intent to Sell)

Rule 145 governs the offer or sale of securities received in connection with reclassifications, mergers, consolidations and asset transfers. Rule 145 applies only to affiliates selling securities of a shell company.

Compliance should be consulted for assistance regarding the processing of Rule 144 and Rule 145 sales. This section is provided for quick reference only.

12.21.2 Definitions

Restricted securities: Restricted securities generally are securities which were:

- acquired directly or indirectly from the issuer or from an affiliate of the issuer in a transaction or series of transactions not involving a public offering.
- acquired from the issuer and are subject to the resale limitations of various rules including Regulation D, Rule 144A, Regulation CE, and other rules and regulations providing for resale of unregistered securities [Rule 144(a)(3)].

Debt securities: Any security other than an equity security; non-participatory stock (non-convertible capital stock where holders are entitled to a preference for dividends and a share of assets upon liquidation of the company but not entitled to participate in residual earnings or assets); and asset-backed securities [Rule 144(a)(4)].

Affiliate: A person who, directly or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with the issuer. An affiliate can be an individual, certain relatives, trusts, estates, corporations or other entities in which the seller is a 10% beneficial owner, trustee, executor or one acting in a similar capacity. The term applies for purposes of Rule 144 sales to anyone who had affiliate status within 90 days before the sale and for the 90 days after ceasing to have affiliate status.

Reporting issuer: An issuer who is, and has been for a period of at least 90 days prior to the 144 sale, subject to SEC reporting requirements and has filed all required reports during the 12 months preceding the sale.

Non-reporting issuer: An issuer not subject to SEC reporting requirements but where there is publicly-available information as specified by Rule 144.

Control securities: Securities owned by an affiliate of an issuer; these securities are considered "restricted" and "control" securities.

12.21.3 Summary Chart of Rule 144 And 145 Requirements

Subject	Requirement
<p>Holding period for affiliates and non-affiliates Rule 144(d)</p>	<ul style="list-style-type: none"> • Reporting company: 6 months • Non-reporting company: 1 year <p><i>(To qualify as a reporting company, issuer must be subject to SEC reporting requirements for at least 90 days prior to sale.)</i></p>
<p>Rule 144 restrictions <i>(Affiliate restrictions apply if the person was an affiliate at any time during the period 90 days before the sale and for 90 days after the person ceases to be an affiliate.)</i></p>	<ul style="list-style-type: none"> • Apply to affiliates ONLY; the following limited requirement applies to non-affiliates • For non-affiliates selling securities of a reporting company, Rule 144(c) regarding the current public information requirement applies if securities are held less than 1 year <i>(may not sell under 144 if the issuer is late in filing an SEC report during the second 6 months after the minimum 6-month holding period)</i> • For non-affiliates selling securities of a non-reporting company, after complying with the 1-year holding period, no other Rule 144 restrictions apply
<p>Volume limitations for affiliates <i>(calculated with all sales of restricted and other securities of the same class for the same person within the preceding 3 months)</i> Rule 144(e)</p>	<ul style="list-style-type: none"> • Apply to affiliates ONLY <i>(non-affiliates may make unlimited resales)</i> • Cannot exceed the greater of: <ul style="list-style-type: none"> ○ 1% of the outstanding shares or other units, or ○ the average weekly reported volume on all national exchanges and/or reported through the automated quotation system during the 4 calendar weeks preceding filing of Form 144 (or date of broker's receipt of the order or date of execution by a market maker), or ○ the average weekly volume reported under a transaction reporting plan or national market system plan during the 4-week period explained above. • For debt securities, an amount that does not exceed 10% of a tranche (or class when the securities are non-participatory preferred stock), aggregated with all sales of securities of the same tranche sold for the seller within a three-month period

Subject	Requirement
	<ul style="list-style-type: none"> • For convertible securities, applies to amount of securities into which they are convertible • Other standards apply to sales by pledgees, donees, estates, and acting in concert and exclusions for determining volume limits [Rule 144(e)(3)]
<p>Manner of sale restrictions for affiliates <i>(in essence, require an ordinary marketplace sale with no special selling efforts)</i> Rule 144(f)</p>	<ul style="list-style-type: none"> • Apply ONLY to resales by affiliates • Apply ONLY to equity securities • Seller or broker cannot solicit buyers or arrange to solicit buyers • Agency and riskless principal transactions permitted
<p>Brokers' transactions <i>(applies to affiliate and non-affiliate transactions)</i> Rule 144(g)</p>	<ul style="list-style-type: none"> • Allows inquiries to other broker/dealers who indicated an interest within the preceding 60 days or to customers who indicated an unsolicited bona fide interest within the preceding 10 business days • Broker receives no more than usual and customary broker's commission • Broker may publish quotations in an inter-dealer quotation system if they are incident to usual market making activities and quotations were published at least 12 days within the preceding 30 calendar days with no more than 4 business day in succession without a 2-way quotation • Brokers may insert bid and ask quotations for a restricted security in an alternative trading system if the broker has published bona fide bid and ask quotations for that security on the ATS on each of the 12 preceding business days • Broker should obtain written evidence of indications of bona fide unsolicited interest and when received
<p>Form 144 filing requirements Rule 144(h)</p>	<ul style="list-style-type: none"> • Apply to affiliates ONLY • <i>de minimis</i> filing threshold of 5,000 shares or \$50,000 in value, whichever is lower, within a 3-month period (<i>no filing requirement below these levels</i>) • 3 copies to be filed with SEC; one copy with the exchange if listed on a national securities exchange
<p>Rule 145</p>	<ul style="list-style-type: none"> • "Presumptive underwriter" provision applies ONLY to affiliates of shell companies

Other Notes:

- Non-affiliate: to qualify as a non-affiliate, must not have been an affiliate of the issuer for at least 3 months prior to the sale.

- Various staff positions also apply regarding tacking of the holding period; sales by a pledgee; and other staff opinions.
- Rule 144 is not available to sellers of a shell company's securities whether the company is reporting or non-reporting.

12.21.4 New Account Information Regarding Affiliates

CEI's new account form includes an inquiry whether the customer is an affiliate of an issuer. RRs are responsible for obtaining this information and, if the customer is an affiliate and places an order to sell shares of the issuer, contacting Compliance for instructions on executing the order under Rule 144.

12.21.5 Lending and Option Writing on Control and Restricted Securities

The lending of money, extension of loan value, or use as collateral of restricted securities are subject to specific limitations. Compliance should be contacted prior to any such arrangement.

Covered listed options may be written on underlying control or restricted stock if the stock is saleable when the option is written. Compliance should be contacted to determine the salability of the underlying securities prior to writing covered options.

12.22 Unregistered Resales of Restricted Securities

[FINRA Regulatory Notice 09-05; SEC FAQs <http://www.sec.gov/divisions/marketreg/faq-broker-dealer-duty-section4.htm>; SEC National Exam Program Risk Alert: <http://www.sec.gov/about/offices/ocie/broker-dealer-controls-microcap-securities.pdf>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Operations personnel
Resources	<ul style="list-style-type: none"> • New accounts at opening • Proposed sales of potentially unregistered securities • Order records or transaction reports • Physical certificates
Frequency	<ul style="list-style-type: none"> • When new accounts are opened with a potentially questionable transaction • As required - assist RR in evaluating a potential sale • Daily - review of order records/transaction reports • As required - review certificates
Action	<ul style="list-style-type: none"> • Review for "red flags" listed in this section • If a red flag is identified, contact the RR for more information about the customer and the block being sold; contact the customer if necessary to confirm the securities are not unregistered or restricted • Operations personnel should refer questionable certificates to the designated supervisor for follow up with the RR or customer
Record	<ul style="list-style-type: none"> • Order records/transaction reports • New account records • Records of certificates received • Designated supervisor's record of action taken, if applicable, in a log, on the order record, in a daytimer, or in another record

Broker-dealers are prohibited from selling unregistered securities unless the sale falls within an available exemption such as Rule 144 or Section 4(a)(4) discussed in the prior section. Avoiding such sales is based on knowing the customer and the securities to be sold. The RR should be aware of "red flags" that may indicate a customer is selling unregistered securities, including the following examples:

- A customer opens a new account and delivers physical certificates representing a large block of thinly-traded or low-priced securities.
- A customer has a pattern of depositing physical share certificates, immediately selling the shares and then wiring out the proceeds of the resale.
- A customer deposits share certificates that are recently issued or represent a large percentage of the float for the security.
- Share certificates reference a company or customer name that has been changed or that does not match the name on the account.
- The lack of a restrictive legend on deposited shares seems inconsistent with the date the customer acquired the securities or the nature of the transaction in which the securities were acquired.
- There is a sudden spike in investor demand for, coupled with a rising price in, a thinly-traded or low-priced security.
- The company was a shell company when it issued the shares.
- A customer with limited or no other assets under management at CEI receives an electronic transfer or journal transactions of large amounts of low-priced, unlisted securities.
- The issuer has been through several recent name changes, business combinations or recapitalizations, or the company's officers are also officers of numerous similar companies.
- The issuer's SEC filings are not current, are incomplete, or nonexistent.
- Omnibus accounts are opened for purported stock loan companies which may hold restricted securities of corporate insiders who have pledged the securities as collateral for, and then defaulted on, purported loans, after which the securities are sold on an unregistered basis.
- Accounts are held in the name of a corporate entity (or LLC), either for the company's own use or as a third-party custodian on behalf of other beneficial shareholders or customers, which disguise the unregistered sales of securities owned by corporate insiders of the company and allow for those insiders to withdraw proceeds individually.
- Accounts are held in the names of foreign financial institutions, such as offshore banks and/or broker-dealers that sold shares of the stock on an unregistered basis on behalf of customers, who may have been stock promoters.
- Accounts may use a master/sub-structure, which allows for trading anonymity with respect to the sub-accounts' activity.

When confronted with a customer wanting to sell a block of stock where there may be a question about the registered status of the stock, the following questions should be asked:

- How long has the customer held the securities?
- How did the customer acquire the securities?
- Does the customer intend to sell additional shares of the same class of securities through other means?
- Has the customer solicited or made any arrangement for the solicitation of buy orders in connection with the proposed resale of unregistered securities?
- Has the customer made any payment to any other person in connection with the proposed resale of securities?
- How many shares or other units of the class are outstanding, and what is the relevant trading volume?

12.22.1 Suspicious Activities

Trading in microcap securities may involve suspicious activity subject to the filing of a Suspicious Activity Report under the Bank Secrecy Act. Compliance is responsible for identifying transactions subject to reporting and filing required reports. associated persons who suspect questionable activity should contact Compliance immediately. Also refer to the section *Suspicious Activity Reports (SARs)* in the chapter *ANTI-MONEY LAUNDERING (AML) PROGRAM*.

Activity that has been previously identified by regulators as potential red flags include:

- Atypical trading patterns in the issuers' securities, including trading involving sudden spikes in price and volume;
- Certain patterns of trading activity being common to several customers, including, but not limited to the sales of large quantities of the shares of multiple issuers by the customers;
- Notifications received from a clearing firm that the clearing firm has identified potentially suspicious activity in the securities of certain issuers or certain customer accounts. Such notifications may take the form of alerts, expressions of concern, or actions taken by the clearing firm to restrict trading in certain issuers' securities and/or certain customer accounts;
- The involvement of certain types of accounts, including those that provide anonymity to the beneficial owners in the liquidation of the shares of the microcap issuers;
- Requests received from FINRA for information relating to certain issuers and the broker-dealers' customer accounts;
- Certain types of issuer information, such as nominal assets and low operating revenue, and frequent changes to the type of activity in which the business was engaged, the name of the corporate entity, directors, and/or management; and
- Sales through CEI by individuals known throughout the industry to be stock promoters.

12.23 Reporting of Insider Transactions

[SEC Securities Exchange Act of 1934 Section 16(a); SEC Exchange Act Section 16 and Related rules & Forms (Q & A): <http://www.sec.gov/divisions/corpfin/guidance/sec16interp.htm>]

Under Section 16(a) of the Exchange Act, directors, officers, and >10% holders of equity securities of a publicly-traded company are required to report their purchases and sales of the issuer's securities to the SEC (and, if the security is listed on a national exchange, with the exchange where listed) as follows:

- at the time the security is registered on a national securities exchange or by the effective date of the registration statement
- within 10 days of becoming a 10% beneficial owner, director or officer
- by the end of the second business day following a purchase or sale transaction

Alternate reporting period requirements apply to two categories of transactions in which the insider does not control and may not be able to predict when the transaction will occur:

- Transactions pursuant to a contract, instruction or written plan
- Discretionary transactions pursuant to associated person benefit plans such as fund switching transactions

In these instances, the date the executing broker-dealer or plan administrator notifies the insider of the transaction is deemed the date of execution for reporting purposes, as long as the notification is not later than the

3rd business day following trade date. The SEC may also provide different due dates for limited types of transactions where two-day reporting is not feasible.

If the issuer maintains a corporate website, the issuer is required to post the filing on the site no later than the end of the business day following the filing.

Transactions by directors or officers that result in "short-swing" profits but that are exempt from Section 16(b) are also subject to the two-day reporting requirement.

The obligation to report is the responsibility of the insider. Customers should be encouraged to contact their counsel if they have questions, and Section 16 should be referenced for specifics regarding filing requirements.

12.24 Penny Stocks

[SEC Securities Exchange Act of 1934 Rule 15g-9, Rule 15g-100 and Schedule 15G; FINRA Notice to Members 93-55, 92-42 and 92-38]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New Account Form • Order Records • Daily Transaction Report • Risk Disclosure Documents
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • FINOP: <ul style="list-style-type: none"> ○ Include required disclosures on confirmations • RR's supervisor, for customers who are not "established" customers: <ul style="list-style-type: none"> ○ Determine required signed risk disclosure document is received prior to effecting the first 3 penny stock purchases and the two-business-day cooling-off period has been satisfied ○ Review new account form and determine investment objectives are consistent with penny stock purchases ○ Review and initial signed risk disclosure document ○ Submit document to Compliance or New Accounts
Record	<ul style="list-style-type: none"> • Initials on the Risk Disclosure Document • Risk Disclosure Documents are retained in the customer's new account file

12.24.1 General Requirements

[SEC Securities Exchange Act of 1934 Rule 15g-1 through 15g-6 and Rule 15g-9]

Securities that are identified as "designated securities" (penny stocks) are subject to certain requirements including:

- provision of risk disclosure to a customer other than an "established customer"
- a "cooling-off period" of two business days after the risk disclosure is sent before a penny stock may be purchased
- disclosure of certain price information relating to the customer's purchase
- disclosure of compensation received by the broker or dealer

- inclusion of prices of penny stock positions on the customer's monthly statement and a legend regarding the value assigned to the penny stock

There are five primary exemptions from these requirements:

1. The price of the security is \$5.00 or more per share.
2. The purchaser is either an accredited investor or established customer or is a principal affiliated with the issuer (as defined in the rule).
3. The transactions are not recommended.
4. The broker-dealer's commissions, mark-ups and mark-downs from penny stock transactions did not exceed 5% of total commissions or mark-ups and mark-downs during the 3 months immediately preceding the transaction, AND, the broker-dealer has not been a market maker in the penny stock to be purchased by the customer for the immediate 12 months preceding the transaction.
5. Any other transaction exempted by the SEC.

The following sections outline CEI's requirements for penny stock transactions subject to the rules.

12.24.2 Penny Stock Defined

[SEC Securities Exchange Act of 1934 Rule 3a51-1; SEC Guide to Broker-Dealer Registration Section V(F)]

Penny stocks are equity securities identified as "designated securities" under the SEC's Penny Stock Rule. Penny stocks are low-priced securities (less than \$5.00 per share) with the Rule listing securities that are **not** included in the definition, as follows.

The following are **not** considered penny stocks subject to the requirements outlined in following sections:

- A reported security as defined in Regulation NMS Rule 601.
- The stock is priced at \$5.00 or more per share.
- Shares of investment companies.
- The stock is listed on an exchange.
- Security futures.
- The issuer has net tangible assets in excess of \$2 million, if the issuer has been in continuous operation for at least 3 years, or \$5,000,000 if in continuous operation for less than 3 years; or average revenue of at least \$6,000,000 for the last 3 years.

Penny stocks include the equity securities of private companies with no active trading market if they do not qualify for one of the exclusions from the definition of penny stock.

RRs should assume that any unlisted securities priced less than \$5.00 per share may be subject to the penny stock requirements.

12.24.3 Established Customer Defined

The requirements of the Rule do not apply to penny stock transactions for "established customers." The term established customer includes a customer who:

- has maintained an account (effected a transaction, made a deposit of funds or securities) more than one year previously, or
- has made three purchases of penny stocks that occurred on separate days and involved different issuers.

12.24.4 Suitability Information

RRs are required to obtain information from the customer including prior investment experience, investment objectives, and financial situation. This information is recorded on CEI's new account form which must be completed prior to effecting a transaction in a penny stock. With this information, the RR is required to reasonably determine whether transactions in penny stocks are suitable for the customer.

Prior to effecting a transaction in a penny stock, the new account form must be completed and submitted to the designated supervisor for approval. The designated supervisor should review the information included on the form to confirm the suitability of penny stocks for the customer's account.

12.24.5 Risk Disclosure Document

Prior to effecting a penny stock transaction for a customer, the RR must furnish the customer with a copy of CEI's penny stock disclosure document titled "Important Information On Penny Stocks" and obtain the customer's signature on the disclosure document acknowledging receipt. The disclosure document may NOT be copied on CEI letterhead but must be reproduced on plain paper.

Furnishing this disclosure and obtaining the customer's signature evidencing receipt is required for each of the first three penny stock transactions before orders are entered.

12.24.6 Two-Business-Day Waiting Period

Penny stock transactions may **not** be executed until at least two business days after the suitability statement and agreement to the transaction has been sent either electronically or by mail. These documents must also be signed by the customer and received by CEI.

12.24.7 Disclosure of Quotations and Other Information

Rule 15g-3 prescribes certain required information that must be disclosed to the customer at or prior to the time of effecting a penny stock transaction. The designated supervisor is responsible for establishing procedures to ensure the necessary disclosures are included on customers' confirmations. Traders are responsible for including notations on order tickets that include the required information regarding bids or offers. A copy of Rule 15g-3 will be provided to traders responsible for recording the required information. The designated supervisor is responsible for establishing procedures to ensure the bid or offer information is included with customer confirmations of penny stock transactions.

12.24.8 Disclosure of Compensation

CEI's compensation for penny stock transactions will be disclosed on customer confirmations as follows:

- For agency transactions, the amount of the compensation.
- For riskless principal transactions where CEI is NOT a market maker, the difference between the price to the customer and the contemporaneous purchase or sale price.
- For other principal transactions, the difference between the price to the customer and the prevailing market price.

"Active and competitive" market, for purposes of calculating mark-ups or mark-downs, is defined in the penny stock rules to include a market where the market maker, in the five business days preceding the transaction, executes less than 20% of the aggregate number of all transactions in the penny stock reported to an automated

interdealer quotation system. Where CEI dominates the market, contemporaneous cost will be used to calculate mark-ups or mark-downs.

Traders are responsible for recording the required information on order records. This information is to be transmitted for inclusion on customer confirmations. The designated supervisor is responsible for establishing procedures for ensuring that required compensation disclosures are included on customer confirmations.

12.25 Sales to Military Personnel on Military Installations

[FINRA Rule 2272; Military Personnel Financial Services Protection Act]

The following requirements apply when offering life insurance products and annuities to military personnel and their dependents on military installations:

- Referral fees upon securities sales or solicitations are prohibited unless the fee recipient is both registered with a broker-dealer and appropriately qualified under relevant SRO rules.
- Perform a suitability determination.
- Provide required written disclosures which must be provided at the time of the sale or solicitation.

Disclosures must:

- clearly and conspicuously disclose the identity of the registered broker-dealer offering the securities, and
- inform potential investors that the securities offered are not being offered by or provided on behalf of the federal government and are not sanctioned, recommended, or encouraged by the federal government.

Disclosures required when selling life insurance are included in a corresponding section in the chapter *INSURANCE PRODUCTS*.

12.26 Tax Switching Transactions

Transactions that are effected to accomplish certain tax results (*i.e.*, establishing a gain or a loss) must be handled consistent with prevailing securities and tax rules and laws. Riskless tax switching trades (also known as "wash sales") are not allowed and may represent a violation of rules prohibiting pre-arranged trades.

Under tax laws, a "wash sale" occurs when someone sells a stock, mutual fund, or some other security at a loss and buys the same thing, or something "substantially identical," within 30 days before or after the sale. The seller cannot deduct the loss on that sale on his or her tax return for that year. "Substantially identical" means buying and selling the same security or one that is almost the same, such as selling an index fund and buying another index fund based on the same underlying index. Customers should be referred to their tax advisers when questions arise regarding tax loss strategies and what may be considered a security that is substantially identical.

A cross transaction must represent a beneficial change in ownership of the security sold and purchased. Where a customer wishes to sell a security and buy it back in their own account, this transaction must be effected at the risk of the market with no guarantee of the price at which the security may be repurchased. The prohibition applies to equity and debt securities. The following is an example of this type of transaction.

A customer wishes to sell Company A at year-end to establish a loss for tax purposes. He also ultimately wants to maintain his position in the security in his account. He asks that you sell the shares and buy them back in his IRA account 31 days later at the same price.

Even though the proposed transaction would meet the 30-day test, this transaction would be disallowed by the IRS because there is no beneficial change in ownership of the security and the customer would be guaranteed to sell and repurchase the security at the same price. In this example, an appropriate method of handling these orders would be to enter a sell transaction and, after it has been executed, enter a buy transaction at market risk after 30 days have elapsed. This places both transactions at the risk of the market and does not involve a guaranteed cross.

12.27 Sales Contests

Coastal does not engage in sales contests.

12.28 Prohibited Transactions and Practices

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Super Vision reports • Customer monthly statements
Frequency	<ul style="list-style-type: none"> • Daily review of order records and Daily Transaction Report • Review of customer monthly statements
Action	<ul style="list-style-type: none"> • Reviews of transactions should include consideration of prohibited transactions prescribed in these policies. Action on identified prohibited transactions could include consultation with Compliance to confirm whether transactions in question are prohibited and to identify corrective action. • Some specific guidelines for review include the following. Contact Compliance for guidance regarding corrective action: <ul style="list-style-type: none"> ○ Wash transactions result from cross transactions between two accounts with the same beneficial owner and at no market risk, <i>i.e.</i>, the buy and sell are pre-arranged at a set price. Wash transactions should be cancelled and securities sold at the risk of the market. ○ Cross transactions on a frequent basis particularly in thinly-traded securities may be an indicator of supporting the market. ○ Orders by the same RR frequently marked for "at the opening" or "at the close" may be an indication of an attempt to influence the market. ○ A pattern of purchasing securities in one account and transferring to another account at a later date may indicate parking. ○ Excessive trading may be an indicator of churning. See the section <i>Active Accounts</i> for guidance regarding action on actively traded accounts. ○ RRs trading ahead of customer block orders that may affect the market price of a security may indicate frontrunning.
Record	<ul style="list-style-type: none"> • Initials on order records • Initials on Daily Transaction Report • Supervisor's Log • Notes/memos to RR's file or Super Vision, if appropriate

12.28.1 Introduction

RRs are required to handle customer transactions in compliance with regulators' rules. This section highlights certain types of prohibited transactions.

12.28.2 Unauthorized Trading

No associated person may enter a transaction before contacting the owner of the account (or the authorized agent for the owner) unless the associated person has specific written authorization to act on the customer's behalf. Failure to contact the customer or the customer's agent can result in the customer later rescinding the transaction because it was not authorized. Engaging in unauthorized transactions subjects the associated person to regulatory and Firm discipline which may include fines and/or termination depending on the seriousness of the violation. If CEI determines an RR engaged in unauthorized trading, any related losses will be charged directly to the RR.

RRs must also avoid "inadvertent" unauthorized transactions such as accepting an order from a husband for a wife's account where the wife has not signed a trading authorization giving her husband authority to trade on her behalf. Doing a customer a "favor" by entering an order when he or she cannot be reached may be construed as good customer service by the RR but in reality is a rule violation and subjects the RR and CEI to potential liability for losses from unauthorized transactions.

Supervisors should look for red flags such as a series of cancelled trades by a customer, customer complaints, and frequent trading. Customer contact may be made to determine whether trades were solicited or otherwise authorized by the customer, and a note should be made in Super Vision.

12.28.3 Market Manipulation

[SEC Securities Exchange Act of 1934 Rule 10b-5; FINRA Rule 6140]

CEI and its associated persons may not engage in manipulative activity to artificially affect the price of a security including entering orders at successively higher prices; creating or inducing a false or misleading appearance with respect to the market in a security; trading at the close to influence the price of a security; or participate (directly or indirectly) in the profits of a manipulative operation or knowingly manage or finance a manipulative operation. "Matched trades" where a person buys or sells a stock, with knowledge that a substantially offsetting transaction is going to be entered by someone, in order to mislead others about the extent of activity in, or the market for, a given stock is a form of market manipulation.

12.28.4 Prearranged Trading

An offer to sell coupled with an offer to buy back at the same or a higher price, or the reverse, is a prearranged trade and is prohibited. Options or written agreements such as repurchase agreements are not included in this prohibition.

12.28.5 Adjusted Trading

Adjusted trading is a prohibited practice that involves the sale by a customer of a security to a broker-dealer at a price above the prevailing market price and the simultaneous purchase of a different security at a price greater than its market value. This may be requested in instances where a bank or other fiduciary does not want to realize a loss on their books and engages in a scheme to avoid, disguise, or postpone losses. Federal banking regulators have stated that adjusted trading by federal financial institutions is an unacceptable and unsuitable investment practice.

12.28.6 Overtrading or Undertrading

These are transactions at prices in excess of or below the prevailing market. Customer transactions must be executed at a price reasonably related to the market; overtrading and undertrading are not permitted.

12.28.7 Wash Transactions

[FINRA Rule 6140(a) and 6140(b)]

Firms and individuals are prohibited, for purposes of creating or inducing a false or misleading appearance with respect to the market in such security, from:

- Executing any transaction in a security which involves no change in beneficial ownership;
- Entering any order or orders for the purchase of a security with the knowledge that an order or orders of substantially the same size, and at substantially the same price, for the sale of the security has been or will be entered by or for the same or different parties; or
- Entering any order or orders for the sale of any security with the knowledge that an order or orders of substantially the same size, and at substantially the same price, for the purchase of such security, has been or will be entered by or for the same or different parties.

12.28.8 Cross Transactions

Firms and their associated persons may not engage in a practice of effecting cross transactions for the purpose of supporting or maintaining the market price of a security.

12.28.9 Orders at the Opening or Close

Orders entered at the opening or close of the market for purposes of influencing the price of a security are prohibited.

12.28.10 Parking Securities

"Parking" is a prohibited practice where a trade or series of trades are effected for a person or entity and held in another person's or entity's account to disguise the investment activities of the original person or entity.

12.28.11 Churning

[FINRA Rule 2111.05(c) and 6140(c)]

Churning of a customer's account is prohibited. The term "churning" has a number of elements including:

- Control of the account by the RR
- Excessive transactions
- Intent to defraud which may be defined as the RR acting in the RR's own interest contrary to the customer's interest

An account that is "active" does not necessarily denote churning. An account's activity must be reviewed individually when reviewing for churning including the customer's objectives and the customer's control of the account.

CEI also may not engage in excessive trading in a proprietary account considering CEI's financial resources and/or considering the market for the security.

Velocity and turnover alerts may be used by the supervisor to detect possible churning. The account review alert will trigger in the event that possible excessive trading is detected as well. Those accounts should be reviewed with the RR.

Turnover over 2 is evidence of possible excessive trading, while 6 or higher is usually dispositive of excessive trading. Account performance should be reviewed, and a determination of costs to annualized equity should be calculated. (Both items will be calculated by an account review alert in Super Vision.) Cost to Equity above 8 is usually dispositive of excessive trading.

If excessive trading is detected, the customer should be contacted to review the account activity and sent an activity letter. If the customer is comfortable with the activity then no further action is required. Otherwise, the account should be restricted (or all trades are made at no commission) until turnover and cost to equity reduces to an acceptable level. Remedies and disciplinary actions are at the discretion of the supervisor.

12.28.12 Trade Shredding

[FINRA Rule 5290]

"Trade shredding" (also known as "tape shredding") is the practice of breaking orders into multiple smaller orders for the primary purpose of maximizing commissions or other revenue. For example, a firm may receive a rebate from a particular market center for directing a certain number of transactions to that market center. CEI and its associated persons are prohibited from engaging in breaking up orders for the purpose of maximizing CEI's revenues or for any other prohibited purpose.

12.29 Market Access

[Exchange Act Rule 15c3-5; SEC FAQs concerning market access risk management: <http://www.sec.gov/divisions/marketreg/faq-15c-5-risk-management-controls-bd.htm>; SEC Small Entity Compliance Guide: <http://www.sec.gov/rules/final/2010/34-63241-secg.htm>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order entry systems • Orders
Frequency	<ul style="list-style-type: none"> • Ongoing: oversight of systems • Daily, weekly, annually: provide reports of orders to supervisors for supervision • Annual: review of risk controls and CEO certification
Action	<ul style="list-style-type: none"> • Establish pre- and post-order entry controls • Provide reports to supervisors • Conduct review of risk controls • Obtain CEO certification
Record	<ul style="list-style-type: none"> • Reviews of reports (retained by supervisors receiving reports) • Annual review • Annual certification

SEC Rule 15c3-5 requires broker-dealers (BDs) with market access, including BDs that provide a customer or any other person with market access through use of the BD's market participant identifier or otherwise, to establish appropriate risk management controls and supervisory systems. These requirements are designed to limit the

financial exposure of a BD that could arise as a result of market access, and to ensure compliance with all regulatory requirements that apply to providing market access.

The Rule applies to BDs with market access to trading securities by virtue of being an exchange member, an ATS subscriber, or an ATS operator with non-broker-dealer subscribers. It applies to security-based swaps if they become traded on an exchange and to BDs engaged in proprietary trading.

The Rule prohibits "naked" or "unfiltered" sponsored market access for third parties accessing markets through the BD.

12.29.1 Definitions

Market access: (i) access to trading in securities on an exchange or alternative trading system as a result of being a member or subscriber of the exchange or alternative trading system, respectively; or (ii) access to trading in securities on an alternative trading system provided by a broker-dealer operator of an alternative trading system to a non-broker-dealer.

Regulatory requirements: all federal securities laws, rules and regulations, and rules of self-regulatory organizations, that are applicable in connection with market access.

Sponsored Access System: The practice by a member firm ("Sponsoring Member") of providing access to a market to another person, firm or customer ("Sponsored Participant").

12.29.2 Risk Management Controls

The risk management controls must be under the direct and exclusive control of the BD with market access, with limited exceptions specified in the Rule that permit reasonable allocation of certain controls and procedures to another registered BD that, based on its position in the transaction and relationship to the ultimate customer, can more effectively implement them. There is a limited exception for BDs that provides outbound routing services to an exchange or ATS for the sole purpose of accessing other trading centers with protected quotations on behalf of the exchange or ATS to comply with Reg NMS Rule 611 or the Options Linkage Plan for listed options. Routing brokers still must comply with preventing entry of erroneous orders.

CEI is responsible for establishing and maintaining risk controls for market access, whether for its own access or for access provided to a third party.

12.29.2.1 Financial Controls

The CFO is responsible for establishing financial controls to ensure the financial safety of CEI from undue exposure and errors when orders are entered. These limits are established in conjunction with senior management and committees (if they exist) with responsibility for oversight of specified areas of CEI. Risk exposure is also considered as part of the new product review process described in the chapter *FINANCIAL AND OPERATIONS PROCEDURES* and as part of CEI's risk management controls.

Financial risk controls may include the following:

- trading limits for CEI and/or its customers
- inventory limits
- commitments to and trading in financial instruments that pose a potential risk to CEI
- limits to credit extended to certain customers or on behalf of a trading desk

12.29.2.2 Order Entry Controls

CEI (or its clearing firm) has established controls to prevent the entry of orders that:

- exceed appropriate pre-set credit or capital thresholds
- exceed a customer's trading limit
- appear to be erroneous including duplication of orders
- do not include all required conditions of the order (price, quantity, security, *etc.*)
- the customer is restricted from trading
- is a short sale without the required verification the security may be borrowed
- other controls if determined necessary

12.29.2.3 Post Order-Entry Controls

CEI (or its clearing firm) has established post-entry order controls that:

- identify trades or patterns of trading that may violate firm or regulatory rules or policy
- other controls if determined necessary

12.29.2.4 Authorized Access

Only authorized associated persons have market access. associated persons are designated by the trading manager and are assigned passwords which are periodically changed. Passwords are de-activated when an associated person terminates or is transferred to a position that does not have authorized access.

12.29.2.5 Post-Trade Execution Reports

Reports are provided to designated supervisors through printed or electronic reports that include all transactions or filtered reports to identify potential violations. These are available on a daily, weekly, monthly, or other appropriate interval for the review to be conducted.

12.29.2.6 Annual Review

On an annual basis CEI's systems and controls and its written procedures are reviewed. Refer to the chapter *SUPERVISORY SYSTEM, PROCEDURES AND CONTROLS*. This includes review of the risk management controls for oversight of market access.

12.29.2.7 Annual Certification

The CEO's annual certification regarding CEI's supervisory system and controls includes a certification that the risk management controls and supervisory procedures comply with Rule 15c3-5 and that the regular review has been conducted.

13 CORPORATE FIXED INCOME SALES AND TRADING

13.1 Fair Prices

[FINRA Rule 2121]

Traders are responsible for making a reasonable effort to obtain a price for the customer that is fair and reasonable in relation to prevailing market conditions.

13.2 Best Execution

[FINRA Rule 5310.03; SIFMA Best Execution Guidelines for Fixed-Income Securities: <https://www.sifma.org/resources/submissions/best-execution-guidelines-for-fixed-income-securities/>]

Responsibility	<ul style="list-style-type: none">• Designated Branch Supervisors• Trade Desk Supervisor
Resources	<ul style="list-style-type: none">• Order records including supporting information• Smart Station alerts• Regulators' reports, if available
Frequency	<ul style="list-style-type: none">• Monthly
Action	<ul style="list-style-type: none">• Review transactions to identify:<ul style="list-style-type: none">○ Cancels/rebills - reviewed in Home Office for patterns, and principal approval where required○ Monthly review of Trade Desk monthly blotter by supervisor of Trade Desk Supervisor
Record	<ul style="list-style-type: none">• Order records and/or reports with notations indicating review and action taken, if any

The concept of "best execution" is somewhat different in the fixed income market vs. the equity market. Fixed income securities have a more fragmented market with fewer participants, no central market, and limited published quotations. Traders still have an obligation to determine a fair price by considering the following factors when pricing a debt transaction.

- Accessibility of quotations (either dollar [or other currency] pricing or yield pricing). Quotations may be "indicative" quotes only, indicating a quote relevant for only a short time or interest in buying or selling a particular issue to solicit bids or offers
- The availability of pricing of recent sales in the same, similar, or benchmark securities (*i.e.*, TRACE for corporate bonds)
- Review of multiple market venues, if they are available
- Contact with other dealers
- The liquidity of the bonds
- Size of the transaction
- Internal capabilities to execute large blocks vs. smaller blocks that may not fill an order
- Reasonable mark-ups/mark-downs as discussed in the next section

- The customer's instructions and expectations

Copies of screenshots should be included with orders when available to document pricing.

13.3 Mark-Up Policy

[FINRA Rule 2121]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor of Trade Desk Supervisor • Trade Desk Supervisor
Resources	<ul style="list-style-type: none"> • Orders • Trading reports • Trade Desk blotter
Frequency	<ul style="list-style-type: none"> • Ongoing (Trade Desk) • Monthly (Trade Desk Supervisor's Designated Supervisor)
Action	<ul style="list-style-type: none"> • Traders: <ul style="list-style-type: none"> ○ Ensure mark-ups and mark-downs are within general Firm guidelines ○ For mark-ups and mark-downs that are outside guidelines, include a written justification on the order record • Trade Desk Supervisor's Designated Supervisor review for mark-ups and mark-downs that exceed general Firm guidelines: <ul style="list-style-type: none"> ○ Review monthly Trade Desk Report ○ Review order records for written justification (<i>e.g.</i>, yields on comparable securities) ○ Notify Trade Desk Supervisor of missing justifications and request correction of the deficiency ○ Confer with Trade Desk Supervisor regarding orders where justification does not seem warranted ○ Report issues to compliance
Record	<ul style="list-style-type: none"> • Order records maintained by the Trading Desk. • Trade Desk Report • Trading reports including initials of reviewer and review notes, if any, maintained by supervisors • Compliance reviews if necessary and action taken

13.3.1 Supervision of Markup/Markdown

Supervision of the Trade Desk and the maximum markup/markdown on corporate fixed income trading is set forth in section 12.5.1.4, et seq.

13.3.2 Prevailing Market Price

(1) A dealer that is acting in a principal capacity in a transaction with a customer and is charging a mark-up or mark-down must mark-up or mark-down the transaction from the prevailing market price. The presumptive prevailing market price for a debt security is established by referring to the dealer's contemporaneous cost as incurred, or contemporaneous proceeds as obtained, consistent with FINRA pricing rules. (See, *e.g.*, Rule 5310).

(2) When the dealer is *selling* the security to a customer, countervailing evidence of the prevailing market price may be considered only where the dealer made no contemporaneous purchases in the security or can show that in the particular circumstances the dealer's *contemporaneous cost* is not indicative of the prevailing market price. When the dealer is buying the security from a customer, countervailing evidence of the prevailing market price may be considered only where the dealer made no contemporaneous sales in the security or can show that in the particular circumstances the dealer's *contemporaneous proceeds* are not indicative of the prevailing market price.

(3) A dealer's cost is considered contemporaneous if the transaction occurs close enough in time to the subject transaction that it would reasonably be expected to reflect the current market price for the security. (Where a mark-down is being calculated, a dealer's proceeds would be considered contemporaneous if the transaction from which the proceeds result occurs close enough in time to the subject transaction that such proceeds would reasonably be expected to reflect the current market price for the security.)

(4) A dealer that effects a transaction in debt securities with a customer and identifies the prevailing market price using a measure other than the dealer's own contemporaneous cost (or, in a mark-down, the dealer's own proceeds) must be prepared to provide evidence that is sufficient to overcome the presumption that the dealer's contemporaneous cost (or, the dealer's proceeds) provides the best measure of the prevailing market price. A dealer may be able to show that its contemporaneous cost is (or proceeds are) not indicative of prevailing market price, and thus overcome the presumption, in instances where:

- interest rates changed after the dealer's contemporaneous transaction to a degree that such change would reasonably cause a change in debt securities pricing;
- the credit quality of the debt security changed significantly after the dealer's contemporaneous transaction; or
- news was issued or otherwise distributed and known to the marketplace that had an effect on the perceived value of the debt security after the dealer's contemporaneous transaction.

(5) In instances where the dealer has established that the dealer's cost is (or, in a mark-down, proceeds are) no longer contemporaneous, or where the dealer has presented evidence that is sufficient to overcome the presumption that the dealer's contemporaneous cost (or proceeds) provides the best measure of the prevailing market price, such as those instances described under *Prevailing Market Price*, sub-paragraph (4), a member must consider, in the order listed, the following types of pricing information to determine prevailing market price:

- a. Prices of any contemporaneous inter-dealer transactions in the security in question;
- b. In the absence of transactions described in (a), prices of contemporaneous dealer purchases (sales) in the security in question from (to) institutional accounts with which any dealer regularly effects transactions in the same security; or
- c. In the absence of transactions described in (a) and (b), for actively traded securities, contemporaneous bid (offer) quotations for the security in question made through an inter-dealer mechanism, through which transactions generally occur at the displayed quotations.

[A member may consider a succeeding category of pricing information only when the prior category does not generate relevant pricing information (*e.g.*, a member may consider pricing information under (b) only after the member has determined, after applying (a), that there are no contemporaneous inter-dealer transactions in the same security). In reviewing the pricing information available within each category, the relative weight, for

purposes of identifying prevailing market price, of such information (*i.e.*, either a particular transaction price, or, in (c) above, a particular quotation) depends on the facts and circumstances of the comparison transaction or quotation (*i.e.*, such as whether the dealer in the comparison transaction was on the same side of the market as the dealer is in the subject transaction and timeliness of the information).]

(6) In the event that, in particular circumstances, the above factors are not available, other factors that may be taken into consideration for the purpose of establishing the price from which a customer mark-up (mark-down) may be calculated, include but are not limited to:

- Prices of contemporaneous inter-dealer transactions in a "similar" security, as defined below, or prices of contemporaneous dealer purchase (sale) transactions in a "similar" security with institutional accounts with which any dealer regularly effects transactions in the "similar" security with respect to customer mark-ups (mark-downs);
- Yields calculated from prices of contemporaneous inter-dealer transactions in "similar" securities;
- Yields calculated from prices of contemporaneous dealer purchase (sale) transactions with institutional accounts with which any dealer regularly effects transactions in "similar" securities with respect to customer mark-ups (mark-downs); and
- Yields calculated from validated contemporaneous inter-dealer bid (offer) quotations in "similar" securities for customer mark-ups (mark-downs).

The relative weight, for purposes of identifying prevailing market price, of the pricing information obtained from the factors set forth above depends on the facts and circumstances surrounding the comparison transaction (*i.e.*, whether the dealer in the comparison transaction was on the same side of the market as the dealer is in the subject transaction, timeliness of the information, and, with respect to the final factor listed above, the relative spread of the quotations in the similar security to the quotations in the subject security).

(7) Finally, if information concerning the prevailing market price of the subject security cannot be obtained by applying any of the above factors, FINRA or its members may consider as a factor in assessing the prevailing market price of a debt security the prices or yields derived from economic models (*e.g.*, discounted cash flow models) that take into account measures such as credit quality, interest rates, industry sector, time to maturity, call provisions and any other embedded options, coupon rate, and face value; and consider all applicable pricing terms and conventions (*e.g.*, coupon frequency and accrual methods). Such models currently may be in use by bond dealers or may be specifically developed by regulators for surveillance purposes.

(8) Because the ultimate evidentiary issue is the prevailing market price, isolated transactions or isolated quotations generally will have little or no weight or relevance in establishing prevailing market price. For example, in considering yields of "similar" securities, except in extraordinary circumstances, members may not rely exclusively on isolated transactions or a limited number of transactions that are not fairly representative of the yields of transactions in "similar" securities taken as a whole.

(9) "Customer" does not include a qualified institutional buyer ("QIB") as defined in Rule 144A under the Securities Act of 1933 that is purchasing or selling a non-investment grade debt security when the dealer has determined, after considering the factors set forth in Rule 2111(b), that the QIB has the capacity to evaluate independently the investment risk and in fact is exercising independent judgment in deciding to enter into the transaction. "Non-investment grade debt security" means a debt security that:

- if rated by only one nationally recognized statistical rating organization ("NRSRO"), is rated lower than one of the four highest generic rating categories;
- if rated by more than one NRSRO, is rated lower than one of the four highest generic rating categories by any of the NRSROs; or

- if unrated, either was analyzed as a non-investment grade debt security by the dealer and the dealer retains credit evaluation documentation and demonstrates to FINRA (using credit evaluation or other demonstrable criteria) that the credit quality of the security is, in fact, equivalent to a non-investment grade debt security, or was initially offered and sold and continues to be offered and sold pursuant to an exemption from registration under the Securities Act of 1933.

13.3.3 "Similar" Securities

(1) A "similar" security should be sufficiently similar to the subject security that it would serve as a reasonable alternative investment to the investor. At a minimum, the security or securities should be sufficiently similar that a market yield for the subject security can be fairly estimated from the yields of the "similar" security or securities. Where a security has several components, appropriate consideration may also be given to the prices or yields of the various components of the security.

(2) The degree to which a security is "similar" to the subject security may be determined by factors that include but are not limited to the following:

- Credit quality considerations, such as whether the security is issued by the same or similar entity, bears the same or similar credit rating, or is supported by a similarly strong guarantee or collateral as the subject security (to the extent securities of other issuers are designated as "similar" securities, significant recent information of either issuer that is not yet incorporated in credit ratings should be considered (*e.g.*, changes to ratings outlooks));
- The extent to which the spread (*i.e.*, the spread over U.S. Treasury securities of a similar duration) at which the "similar" security trades is comparable to the spread at which the subject security trades;
- General structural characteristics and provisions of the issue, such as coupon, maturity, duration, complexity or uniqueness of the structure, callability, the likelihood that the security will be called, tendered or exchanged, and other embedded options, as compared with the characteristics of the subject security; and
- Technical factors such as the size of the issue, the float and recent turnover of the issue, and legal restrictions on transferability as compared with the subject security.

(3) When a debt security's value and pricing is based substantially on, and is highly dependent on, the particular circumstances of the issuer, including creditworthiness and the ability and willingness of the issuer to meet the specific obligations of the security, in most cases other securities will not be sufficiently similar, and therefore, other securities may not be used to establish the prevailing market price.

13.3.4 Pricing Disclosure (eff. May 18, 2018)

[FINRA Rule 2232; FINRA Regulatory Notice 17-08; FINRA FAQs: <http://www.finra.org/industry/faq-fixed-income-confirmation-disclosure-frequently-asked-questions-faq>]

The amount of mark-ups and mark-downs will be disclosed on retail customer confirmations. Two additional disclosures include: (1) a reference (or hyperlink if the confirmation is electronic) to a FINRA web page containing publicly-available trading data for the security traded; and (2) the execution time expressed to the second. This function is executed by Coastal's clearing firm.

13.4 Crossing OTC Bonds

Responsibility	<ul style="list-style-type: none"> • Trade Desk Supervisor
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Resources	<ul style="list-style-type: none"> • Order records • Available reports
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Review crossed bond orders for pricing documentation • Take corrective action if pricing is not documented or appears to be incorrect by consulting with the trader, correcting the price, or other appropriate action
Record	<ul style="list-style-type: none"> • Reviews of transactions including corrective action, if appropriate

When crossing OTC bonds, the following must be considered:

- Crossing transactions must represent a change in ownership, *i.e.*, bonds may not be crossed between accounts for the same beneficial owner ("wash transaction").
- Determining a fair crossing price involves one or more of the following, **which must be documented on the order record**:
 - The price relates to the current quoted market price for the bonds. Indicate where they are quoted and the quote at the time bonds are crossed.
 - The price is determined from a recent transaction in the security (indicate when and where the transaction took place).
 - The price relates to a recent transaction in a similar bond (maturity, rating, coupon). Indicate the related transaction including description of the bond, when the transaction took place, and the price.
 - Other documentation for determining a fair price to cross the bonds.

13.5 Errors

All errors in customer orders must be resolved immediately when discovered. No overnight positions should be maintained in the error account. Errors in customer accounts are documented on the Cancel and Rebill/Error Report form which requires a designated principal's approval.

13.6 Cancels and Rebills

[FINRA Rule 4515]

Cancellations and rebills in customer accounts are documented on the Cancel and Rebill/Error Report form which requires a designated supervisor's signature.

13.7 Extended Settlements; Delayed Deliveries

[FINRA Rule 11320]

Extended settlements or delayed deliveries are transactions that should be reviewed by the trade desk supervisor. Variances from normal settlement or delivery should be available only to those customers where the supervisor is reasonably confident regarding the customer's ability and willingness to pay or deliver securities on a timely basis.

Any pattern of extended settlements or delayed deliveries with a particular RR or client could indicate a credit problem, potential unauthorized trading or other improper activity and should be investigated.

13.8 Inventory Positions

Responsibility	<ul style="list-style-type: none"> • Trade Desk Supervisor • FINOP
Resources	<ul style="list-style-type: none"> • Pricing provided by traders • Independent pricing services
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Trade Desk supervisor: <ul style="list-style-type: none"> ○ Review daily pricing, marks ○ If pricing appears unreasonable, contact trader and make necessary adjustments ○ Review requests for exceptions to inventory limits and, in consultation with the FINOP, approve or disapprove ○ Provide training to traders on proper pricing • FINOP: <ul style="list-style-type: none"> ○ Establish inventory limits ○ Review daily inventory to confirm compliance with limits (may be designated to Trade Desk Supervisor) ○ If limits exceeded, contact the trader's supervisor; reduce the position or approve an exception; take corrective action (in conjunction with the designated supervisor) which may include restricting the trader's activities, added training for the trader, or other action as appropriate • <ul style="list-style-type: none"> ○ Monitor intra-day risk (size, exposure, net buys vs. short positions, <i>etc.</i>)
Record	<ul style="list-style-type: none"> • Inventory limits • Daily pricing of inventory • Designated supervisor's review of marks • FINOP review of compliance with inventory limits • Risk management actions when anomalies are detected

CEI does not maintain inventory positions. Traders are responsible for complying with inventory position limits. Exceptions require the approval of the designated supervisor.

13.8.1 Pricing Positions

For positions where automated pricing is unavailable, it is the traders' responsibility to price inventory positions at the end of each trading day. Positions are priced using one or more of the following resources:

- Transactions that day in the security being priced
- If no transactions, transactions in similar securities (rating, maturity, type, *etc.*)

- Index values
- Treasury curve, yield curve changes
- Consideration of overall market
- Conversations with other dealers regarding the market
- Pricing available from Bloomberg, other vendors

Traders should be conservative when pricing positions. Daily pricing of inventory positions is communicated to the FINOP.

13.9 Market Access

[Exchange Act Rule 15c3-5; SEC FAQs concerning market access risk management: <http://www.sec.gov/divisions/marketreg/faq-15c-5-risk-management-controls-bd.htm>; SEC Small Entity Compliance Guide: <http://www.sec.gov/rules/final/2010/34-63241-secg.htm>; NASDAQ Rule 4615]

Responsibility	<ul style="list-style-type: none"> • Trade Desk Supervisor
Resources	<ul style="list-style-type: none"> • Order entry systems • Orders
Frequency	<ul style="list-style-type: none"> • Ongoing: oversight of systems • Daily, weekly, annually: provide reports of orders to supervisors for supervision • Annual: review of risk controls and CEO certification
Action	<ul style="list-style-type: none"> • Establish pre- and post-order entry controls • Provide reports to supervisors • Conduct review of risk controls • Obtain CEO certification
Record	<ul style="list-style-type: none"> • Reviews of reports (retained by supervisors receiving reports) • Annual review • Annual certification

SEC Rule 15c3-5 requires broker-dealers (BDs) with market access, including BDs that provide a customer or any other person with market access through use of the BD's market participant identifier or otherwise, to establish appropriate risk management controls and supervisory systems. These requirements are designed to limit the financial exposure of a BD that could arise as a result of market access, and to ensure compliance with all regulatory requirements that apply to providing market access.

The Rule applies to BDs with market access to trading securities by virtue of being an exchange member, an ATS subscriber, or an ATS operator with non-broker-dealer subscribers. It applies to security-based swaps if they become traded on an exchange and to BDs engaged in proprietary trading.

The Rule prohibits "naked" or "unfiltered" sponsored market access for third parties accessing markets through the BD.

13.9.1 Definitions

Market access: (i) access to trading in securities on an exchange or alternative trading system as a result of being a member or subscriber of the exchange or alternative trading system, respectively; or (ii) access to trading in securities on an alternative trading system provided by a broker-dealer operator of an alternative trading system to a non-broker-dealer.

Regulatory requirements: all federal securities laws, rules and regulations, and rules of self-regulatory organizations, that are applicable in connection with market access.

Sponsored Access System: The practice by a member firm ("Sponsoring Member") of providing access to a market to another person, firm or customer ("Sponsored Participant").

13.9.2 Risk Management Controls

The risk management controls must be under the direct and exclusive control of the BD with market access, with limited exceptions specified in the Rule that permit reasonable allocation of certain controls and procedures to another registered BD that, based on its position in the transaction and relationship to the ultimate customer, can more effectively implement them. There is a limited exception for BDs that provides outbound routing services to an exchange or ATS for the sole purpose of accessing other trading centers with protected quotations on behalf of the exchange or ATS to comply with Reg NMS Rule 611 or the Options Linkage Plan for listed options. Routing brokers still must comply with preventing entry of erroneous orders.

CEI is responsible for establishing and maintaining risk controls for market access, whether for its own access or for access provided to a third party.

13.9.2.1 Financial Controls

The CFO is responsible for establishing financial controls to ensure the financial safety of CEI from undue exposure and errors when orders are entered. These limits are established in conjunction with senior management and committees (if they exist) with responsibility for oversight of specified areas of CEI. Risk exposure is also considered as part of the new product review process described in the chapter *FINANCIAL AND OPERATIONS PROCEDURES* and as part of CEI's risk management controls.

Financial risk controls may include the following:

- trading limits on the Firm or its customers
- inventory limits
- commitments to and trading in financial instruments that pose a potential risk to CEI
- limits to credit extended to certain customers or on behalf of a trading desk

13.9.2.2 Order Entry Controls

CEI (or its clearing firm) has established controls to prevent the entry of orders that:

- exceed appropriate pre-set credit or capital thresholds
- exceed a customer's trading limit
- appear to be erroneous including duplication of orders
- do not include all required conditions of the order (price, quantity, security, etc.)
- the customer is restricted from trading
- is a short sale without the required verification the security may be borrowed
- other controls if determined necessary

13.9.2.3 Post Order-Entry Controls

CEI (or its clearing firm) has established post-entry order controls that:

- identify trades or patterns of trading that may violate firm or regulatory rules or policy
- other controls if determined necessary

13.9.2.4 Authorized Access

Only authorized associated persons have market access. Associated persons are designated by the trading manager and are assigned passwords which are periodically changed. Passwords are de-activated when an associated person terminates or is transferred to a position that does not have authorized access.

13.9.2.5 Post-Trade Execution Reports

Reports are provided to designated supervisors through printed or electronic reports that include all transactions or filtered reports to identify potential violations. These are available on a daily, weekly, monthly, or other appropriate interval for the review to be conducted.

13.9.2.6 Annual Review

On an annual basis CEI's systems and controls and its written procedures are reviewed. Refer to the chapter *SUPERVISORY SYSTEM, PROCEDURES AND CONTROLS*. This includes review of the risk management controls for oversight of market access.

13.9.2.7 Annual Certification

The CEO's annual certification regarding CEI's supervisory system and controls includes a certification that the risk management controls and supervisory procedures comply with Rule 15c3-5 and that the regular review has been conducted.

13.9.3 Sponsored Access

[FINRA Rule 6271, 6281 and 7220A; NYSE Rule 123B]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor• Compliance
Resources	<ul style="list-style-type: none">• Requests for sponsored access
Frequency	<ul style="list-style-type: none">• As required: execute and file agreements• Initially upon sponsoring access: provide training to authorized persons• Ongoing: monitor transactions• Quarterly: verify access of participants• Annual: confirm physical security of equipment
Action	<ul style="list-style-type: none">• Conduct review of potential sponsored participant• Approve or disapprove participation

	<ul style="list-style-type: none"> • Determine limitations on participant's activities (for example, pre-set credit thresholds; price, size or value parameters for orders) • Execute with Sponsored Participant an agreement that outlines conditions for access • Obtain list of persons authorized to enter orders on participant's behalf • Provide training to authorized persons • Verify that access is provided only to authorized sponsored participants • Monitor transactions entered by the sponsored participant to determine compliance with regulators' rules and requirements <ul style="list-style-type: none"> ○ Avoidance of errors ○ Orders represent bona fide trading interest ○ Trading within limitations established by CEI • When problems are identified: <ul style="list-style-type: none"> ○ Confer with participant ○ Provide additional training, if appropriate ○ Terminate agreement, if necessary • Confirm the physical security of any equipment on the participant's premises by annual certification or examination by a firm-authorized person
Record	<ul style="list-style-type: none"> • Records of participant due diligence review prior to approval • Limitations established on participant's activities • Copies of agreement with Sponsored Participant • List of persons who will enter orders for the participant • Record of training authorized persons • Monitoring of sponsored participant activity, notes of action taken • Record of quarterly verification of access only by sponsored participants • Record of confirmation of the physical security of equipment provided to the sponsored participant (annual certification or examination)

CEI may act as a Sponsoring Member that gives access on an agency basis to another firm or customer ("Sponsored Participant") to execute orders on exchanges where CEI is a member. Sponsored access is subject to the risk management controls established for CEI's access to markets. Where the Sponsored Participant is a registered broker-dealer, some supervisory responsibilities may be allocated to the Sponsored Participant under the written agreement.

13.9.3.1 Approval of Sponsored Access

Proposed sponsored access will be reviewed by Compliance which will conduct a due diligence review of the firm or customer that is the potential sponsored participant. Compliance will also establish any credit or trading limits; these limits will be communicated to the participant.

13.9.3.2 Limits and Controls

CEI may establish pre-set credit thresholds for participants and may set price, size, or value parameters that would reject orders that exceed the established parameters. User Agreement must be signed by CEI and the participant and filed with the exchange.

Sponsored Participants are subject to pre-entry order limits and post-entry controls applicable to CEI and may be subject to more stringent limits and controls. The designated supervisor will establish the limits and controls for each participant and notify system personnel to establish those controls in the system.

13.10 Traders' Personal Accounts

Responsibility	<ul style="list-style-type: none"> • Designated Branch Supervisor
Resources	<ul style="list-style-type: none"> • Confirmations • Statements
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Review trader's personal transactions to identify: <ul style="list-style-type: none"> ○ trades in securities in which the trader makes a market ○ trades that were not approved by the Manager prior to entry • Take corrective action for exceptions which may include conferring with the trader; canceling transactions; issuing a formal reprimand; or other appropriate action
Record	<ul style="list-style-type: none"> • Trading Department files for traders' transactions

- Exceptions require the approval of the designated supervisor.

13.11 TRACE

[FINRA Rule 6700 series; FINRA Regulatory Notice 16-38, 13-15 and 12-56; FINRA TRACE web site: <http://www.finra.org/RegulatorySystems/TRACE/index.htm>; TRACE FAQs Reporting Notice /1/13: <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p314034.pdf>]

Responsibility	<ul style="list-style-type: none"> • Trade Desk Supervisor
Resources	<ul style="list-style-type: none"> • TRACE-eligible transactions • TRACE Quality of Markets Report Card • TRACE Entitlement & Contact Report
Frequency	<ul style="list-style-type: none"> • Monthly
Action	<ul style="list-style-type: none"> • If a third-party (such as a clearing firm) is used for TRACE reporting, confirm the agent is reporting as required • Review Report Card to determine whether trades are properly reported • Where exceptions are noted, take corrective action which may include: <ul style="list-style-type: none"> ○ Conferring with person responsible for input ○ Additional training when necessary ○ If a third party is used to report, contact with appropriate person to obtain assurances regarding corrective action

	<ul style="list-style-type: none"> • Review the Contact Report to confirm only authorized persons are accessing TRACE
Record	<ul style="list-style-type: none"> • Review of third-party reporting, if applicable • Copies of TRACE Quality of Markets Report Card with note of action taken, reviewer's initials, and date reviewed • Copies of Trace Entitlement & Contact Report with reviewer's initials and date reviewed and action taken, if appropriate

FINRA requires the reporting of OTC transactions in eligible corporate debt securities to its Trade Reporting and Compliance Engine (TRACE). This section summarizes TRACE reporting requirements. FINRA rules should be consulted for more detailed information, including the information to be reported and timeframes for reporting.

13.11.1 TRACE Eligible Securities and Reportable Transactions

[FINRA Rule 6710; FINRA Regulatory Notice 16-39, 14-23 and 08-75]

"TRACE-eligible securities" include securities that are:

- U.S. Treasury securities (all securities issued by the Treasury Dept. including separate principal and interest components; savings bonds and U.S. Treasury securities bought in an auction are NOT included)
- U.S. dollar denominated debt securities issued by a U.S. or foreign private issuer (and, if a restricted security, sold under Rule 144A);
- Hybrid securities (both debt- and equity-like features) as specified by FINRA;
- A debt security that is U.S. dollar-denominated and issued or guaranteed by an Agency or a Government-Sponsored Enterprise (as defined in Rule 6710);
- FDIC-guaranteed debt securities under the federal "Temporary Liquidity Guarantee Program;" **and**
- Asset- and mortgage-backed securities (as broadly defined in FINRA Rule 6710(a) including CMOs, CDOs, CBOs, and other asset-backed securities) [FINRA Rule 6730(a)(3)].

TRACE eligible securities include unlisted convertible debt, unlisted equity-linked notes and similar securities (those that are listed on a national securities exchange must be reported to the appropriate equity trade reporting facility). A "foreign private issuer" is a foreign issuer that is not eligible to use the SEC's Schedule B for registering a debt offering in the U.S.

Reporting obligations include primary market transactions in TRACE eligible securities.

13.11.1.1 Securities Excluded

"TRACE-eligible securities" (governed by definitions within the Rule) exclude:

- debt issued by a foreign sovereign
- money market instruments

13.11.2 Transaction Reporting

[FINRA Rule 6730; FINRA Regulatory Notice 16-30]

CEI is obligated to report to TRACE any transactions in the securities subject to TRACE requirements. Trace reporting is conducted by the clearing firm. Refer to FINRA Rule 6730 for details of timeframes for reporting and transaction information to be reported.

13.11.2.1 Who Reports

When the buyer and seller are both FINRA members, both members must report to TRACE. For transactions between a member and a non-member, including a customer, the member must report.

13.11.2.2 Transactions Exempt from Reporting

[FINRA Rule 6730(e) and 6732]

The following transactions are not reportable:

- Transfers of TRACE-Eligible Securities for the sole purpose of creating or redeeming an instrument that evidences ownership of or otherwise tracks the underlying securities transferred (*e.g.*, an exchange-traded fund).
- Transactions in TRACE-Eligible Securities that are listed on a national securities exchange, when such transactions are executed on and reported to the exchange and the transaction information is disseminated publicly.
- Transactions where the buyer and the seller have agreed to trade at a price substantially unrelated to the current market for the TRACE-Eligible Security (*e.g.*, to allow the seller to make a gift).
- Provided that a data sharing agreement between FINRA and NYSE related to transactions covered by this Rule remains in effect, transactions in TRACE-Eligible Securities that are executed on a facility of NYSE in accordance with NYSE Rules 1400, 1401 and 86 and reported to NYSE in accordance with NYSE's applicable trade reporting rules and disseminated publicly by NYSE.
- Transactions resulting from the exercise or settlement of an option or a similar instrument, or the termination or settlement of a credit default swap, other type of swap, or a similar instrument.
- Transfers of securities made pursuant to an asset purchase agreement (APA) that is subject to the jurisdiction and approval of a court of competent jurisdiction in insolvency matters, provided that the purchase price under the APA is not based on, and cannot be adjusted to reflect, the current market prices of the securities on or following the effective date of the APA.

13.11.2.3 Underwriter Obligation to Obtain CUSIP And Provide Notice

[FINRA Rule 6760]

The managing underwriter or group of underwriters of a distribution or offering (excluding a secondary distribution or offering) of a TRACE-eligible debt security must obtain the CUSIP number and report required information to FINRA Operations. Information must be provided to FINRA prior to the execution of the first transaction with exceptions under Rule 6760(c) including same-day pricing/trading and CMO issues.

13.11.3 System Outages

[FINRA Regulatory and Compliance Alert Winter 2000]

System outages involving fixed income transactions and TRACE reporting will be reported to FINRA by e-mail to bondreporting@finra.org. The trading supervisor is responsible for determining whether to report outages and will retain copies of e-mail communications sent to FINRA.

13.11.3.1 Information to Be Reported

Information that will be reported includes the following:

- the date(s) the system problem occurred;
- the specific systems that were affected (*e.g.*, internal systems, third party vendor system);

- the exact nature of the problem (*e.g.*, complete outage, slow transmission times);
- the time the problem began;
- the time the problem was first detected;
- the time the problem was resolved and a brief description of the resolution;
- the level of activity impacted (*e.g.*, the approximate number of trades not reported) and a description of how the impact will be addressed (*e.g.*, trade reports to be submitted on an "as of" basis the next business day);
- contact name and telephone number; and,
- any additional information deemed relevant.

13.11.3.2 Independent Contractors

If an independent contractor immediately transmits orders to the trading department, either electronically or manually, the independent contractor is not required to maintain a separate synchronized clock. If there is any delay in transmitting the order, however, the contractor must maintain a synchronized clock.

13.12 Prohibited Activities

Responsibility	<ul style="list-style-type: none"> • Trade Desk Supervisor • Trade Desk Supervisor's Designated Supervisor
Resources	<ul style="list-style-type: none"> • Trading reports • Observation of traders' activities • Monthly trader reviews
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Take corrective action depending on the nature of the prohibited activity
Record	<ul style="list-style-type: none"> • Trading files and/or the Trading Desk Supervisor's Blotter

13.12.1 Inside Information

[SEC Securities Exchange Act of 1934 Rule 10b-5; FINRA Notice to Members 89-15; Insider Trading and Securities Fraud Enforcement Act of 1988]

Traders are prohibited from acting on, passing on, or discussing any inside information regarding any fixed income security issues, including any material non-public information regarding, for example, a credit-rating change, default or advance refunding. Any knowledge of such information must be brought to the attention of the designated supervisor and Compliance. No CEI proprietary account or associated person account may enter a transaction in a security based on material non-public information about that security.

13.12.2 Financial Arrangements

Traders are prohibited from entering into financial arrangements with customers or issuers (*i.e.*, sharing in profits or losses, sharing in commissions, rebating commissions, *etc.*).

13.12.3 Market Manipulation

[SEC Securities Exchange Act of 1934 Rule 10b-3; FINRA Rule 2020]

No purchase or sales order shall be entered or executed that is designed to raise or lower the price of a security or to give the appearance of trading for purposes of inducing others to buy and sell. No purchase or sale order shall be entered or executed with the intent to "corner" a market or create a "squeeze" in a security.

13.12.4 Front Running

[FINRA Rule 5270 and 5320]

No firm proprietary or associated person account may trade a security while in possession of material information about an imminent block-sized transaction in that security or a derivative security or trade ahead of customer orders. Refer to the chapter *ORDERS* and the sections *Prohibition Against Trading Ahead Of Customer Orders* and *Front Running Of Block Transactions*.

13.12.5 Parking Securities

No arrangement may be used to conceal the true ownership of securities through a fictitious sale or transfer to another party or nominee who agrees to later sell or transfer the securities to the true owner (or his agent) at the agreed upon time at essentially the same terms. Legitimate repurchase or "repo" transactions, usually entered into as financing transactions, are not included in this prohibition if they are not entered for a manipulative purpose.

13.12.6 Secret Profits

A trader may not permit the charging of a mark-up or mark-down in addition to a commission on any transaction.

13.12.7 Adjusted Trading

[FINRA Regulatory and Compliance Alert Fall 1993]

Adjusted trading or "overtrading" is a prohibited practice that involves the sale of a security by a customer for a price above the prevailing market price and the simultaneous purchase of a different security at a price lower than the prevailing market price. The purpose of an adjusted trade usually is to assist a customer in avoiding, disguising, or postponing losses.

Other scenarios of adjusted trading include:

- permitting a customer to sell a security at an inflated price and re-selling the security to another customer at the inflated price
- interpositioning the broker-dealer between two customers where the broker-dealer acts as a conduit allowing the two customers to "swap" losing positions by paying an inflated price for each other's securities

All transactions must be executed at prices reasonably related to current market prices and all books and records of CEI must show an accurate price for securities purchased or sold.

13.12.8 Wash Sales

A wash sale occurs when a purchase and sale takes place where there is no change in beneficial ownership. For example, someone sells bonds from their personal account to their IRA account. Wash sales are sometimes effected to create the false appearance of activity in a security. Wash sales sometimes occur when a customer wants to take a tax loss selling the security on one day and then re-purchasing it within 30 days of the sale. The IRS considers such transactions wash sales and disallows the loss as a tax deduction. The firm utilizes "NICE/Actimize" to detect AML activities which include surveillance of potential wash sales, and those alerts are monitored by the AML department.

13.12.9 Daisy Chain/Round Robin Transactions

These transactions represent a fraudulent scheme in which a security is traded in a circular manner among those involved in an attempt to manipulate the price of the security. The circular transactions result in a small profit to those involved and result in artificial pricing of the security.

13.13 High Yield Debt Securities

[FINRA Notice to Members 04-30]

Responsibility	<ul style="list-style-type: none"> • Registered Representative • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Account records
Frequency	<ul style="list-style-type: none"> • As required when transactions in high yield securities are effected
Action	<ul style="list-style-type: none"> • Review that disclosures have been provided to the customer • Review the customer's investment objectives to confirm risk tolerance is part of the customer's profile • Review recommended orders for compliance with Regulation BI [see the chapter <i>REGULATION BEST INTEREST (BI)</i>] • Consult with the RR if questions arise • Consult with customer if necessary • Take corrective action, if necessary, which may include canceling the transaction(s)
Record	<ul style="list-style-type: none"> • Order records with record of review including corrective action taken, if any

High yield debt securities (also known as "junk bonds") generally involve a higher degree of risk and are typically rated BB or less by Standard and Poor's or Ba or below by Moody's. Because of the higher risk, RRs have enhanced suitability and disclosure obligations.

13.13.1 Suitability

[FINRA Rule 2111]

R Rs must consider the following risk factors (and any other factors that may exist) before recommending high yield debt securities to customers:

- The bond may default resulting in loss of investment.
- Markets for such bonds may be relatively illiquid, impacting the investor's ability to sell and the price of the bond.
- In a low-interest, low-yield environment, there may be a compression of risk premium resulting from investors bidding up prices and driving down yields while default rates remain high.

Customers who purchase high yield debt securities must have higher risk tolerance as at least one of their investment objectives.

Suitability is only one element of acting in a customer's best interest. Recommendations to retail customers who are natural persons are subject to Regulation Best Interest (BI) which is broader than the suitability requirement. Reg BI includes recommendations for orders; types of accounts; and investment strategies, including recommendations to prospects. It is important to be familiar with those requirements which are included in the chapter *REGULATION BEST INTEREST (BI)*.

13.13.2 Disclosures

RRs are obligated to disclose the risks listed above to potential purchasers of high risk bonds. Any other known risks particular to the issue must also be disclosed.

13.13.3 Catastrophe Bonds

Catastrophe bonds (also known as cat bonds) are risk-linked securities that transfer a specified set of risks from a sponsor to investors. Cat bonds are linked to specific types of disasters and are issued on the condition proceeds won't be used by the insurer for claims payments until the insurer's claims costs top a set of pre-determined amounts. Catastrophe bonds are typically used by insurers as an alternative to traditional catastrophe reinsurance.

If no catastrophe occurs, the insurance company pays a coupon to the investors. On the contrary, if a catastrophe did occur, then the principal would be forgiven and the insurance company would use this money to pay its claimholders.

These bonds are inherently risky and often have a maturity of three years or less. Investors can lose their entire investment. Cat bonds are suitable only for customers with high risk investment profiles and where the risks have been clearly communicated.

13.13.4 Creditors' Committee

Any associated person that anticipates serving on the creditors' committee should notify Compliance prior to accepting the position. The following will be considered in determining whether the associated person should serve on the committee:

- Whether access to inside information would unduly restrict CEI from issuing research or trading the issuer's securities
- Whether adequate information barrier procedures are in place to permit unrestricted activities in other business areas of CEI while the associated person serves on the creditors' committee
- Whether disclosure of the associated person's role should be included in footnotes on any research reports on the issuer's securities

14 CORPORATE SECURITIES UNDERWRITING

[FINRA FAQ on Public Offering Review: <http://www.finra.org/industry/compliance/regulatoryfilings/publicofferingsystem/faq/>; SEC Securities Offering Reform Questions and Answers November 30, 2005 (www.sec.gov/divisions/corpfin/faqs/securities_offering_reform-qa.pdf)]

14.1 Syndicate Member Procedures

Responsibility	<ul style="list-style-type: none">• Syndicate Supervisor
Resources	<ul style="list-style-type: none">• Invitations to participate as a syndicate group member• Prospectus• Registration statement• Other information provided by the managing underwriter
Frequency	<ul style="list-style-type: none">• As required for each underwriting
Action	<ul style="list-style-type: none">• Review agreement, related documents, and accept or decline• Notify Compliance of proposed deal for consideration whether to add the security to Coastal Equities, Inc.'s Restricted List and notify Compliance when price and trading restrictions are lifted• Notify Research if necessary• Allocate available securities• Provide prospectuses to purchasers, if required• Handle returned shares trading at a premium in the aftermarket by returning them to the Syndicate Manager to offset an existing syndicate short position or, if none exists, allocate to unfilled customer requests or sell them in the market and donate profits
Record	<ul style="list-style-type: none">• The invitation, signed agreements, prospectus, registration, and other information provided by the managing underwriter as well as Compliance and Research notification and tombstone ads are retained in the deal file.• Disposition of returned shares trading at a premium in the aftermarket

When invited to participate as a syndicate member, the syndicate supervisor will review the deal, accept or decline, and oversee the distribution of securities sold by Coastal Equities, Inc..

14.1.1 Returned Shares of an Issue Trading at a Premium

[FINRA Rule 5131(d)(3)]

If new issue shares are returned by a purchaser when the shares trade at a premium in the aftermarket, the returned shares will offset the existing syndicate short position. If no short position exists, Coastal Equities, Inc. will:

- Offer returned shares at the public offering price to unfilled customers' orders using a random allocation methodology, or

- Sell returned shares on the secondary market and donate profits from the sale to an unaffiliated charitable organization with the condition that the donation be treated as an anonymous donation to avoid any reputational benefit to Coastal Equities, Inc.

14.1.2 Tombstone Ads

Coastal Equities, Inc. may publish tombstone announcements of participation as a syndicate member. Tombstone ads must be approved by Compliance prior to publication.

14.1.3 Research

If Coastal Equities, Inc. issues research regarding the subject company, participation as a syndicate member requires compliance with SRO rules regarding research activities. The syndicate supervisor is responsible for notifying the Research Department of pending deals since issuance of research reports may be restricted.

14.2 Selling Group Member Procedures

Responsibility	<ul style="list-style-type: none"> • Syndicate Supervisor
Resources	<ul style="list-style-type: none"> • Invitations to participate as a selling group member • Prospectus • Registration statement • Other information provided by the managing underwriter
Frequency	<ul style="list-style-type: none"> • As required for each underwriting
Action	<ul style="list-style-type: none"> • Review agreement, related documents, and accept or decline • Notify Compliance of proposed deal for consideration whether to add the security to Coastal Equities, Inc.'s Restricted List and notify Compliance when price and trading restrictions are lifted • Notify Research if necessary • Allocate available securities • Return unsold allotment to managing underwriter
Record	<ul style="list-style-type: none"> • The invitation, signed agreements, prospectus, registration, and other information provided by the managing underwriter as well as Compliance and Research notification and tombstone ads are retained in the deal file.

This section describes procedures when Coastal Equities, Inc. participates in an underwriting as a selling group member.

14.2.1 Returning Unsold Allotment

As a selling group member, Coastal Equities, Inc. has no financial commitment to sell underwritten shares and will return unsold allotments, unless the terms of the selling agreement dictate otherwise.

Unsold shares will be returned to the managing underwriter within the timeframe specified by the selling group agreement.

14.2.2 Tombstone Ads

Coastal Equities, Inc. may publish tombstone announcements of participation as a selling group member. Tombstone ads must be approved by Compliance prior to publication.

14.2.3 Research

If Coastal Equities, Inc. issues research regarding the subject company, participation as a selling group member requires compliance with SRO rules regarding research activities. The syndicate supervisor is responsible for notifying the Research Department of pending deals since issuance of research reports may be restricted.

14.3 Special Purpose Acquisition Companies (SPACs)

[FINRA Regulatory Notice 08-54]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Information from sponsors/managers
Frequency	<ul style="list-style-type: none"> • As required when a SPAC will be offered
Action	<ul style="list-style-type: none"> • Review background of SPAC sponsor/managers • Review registration statement • Review/approve proposed marketing materials • Confirm disclosures are provided for potential investors
Record	<ul style="list-style-type: none"> • Review of sponsors/managers/registration statement • Review/approval of marketing materials • Copy of disclosure document(s) provided to prospective investors and record of providing

SPACs are shell companies that raise capital through IPOs for the purpose of merging with or acquiring an operating company. This section outlines the differences between SPACs and traditional equity IPOs. RRs are responsible for understanding the features of a SPAC before recommending purchase to a potential investor and communicating the differences to the investor.

	Traditional IPO	SPAC
Revenue or operating history of issuer	Available and subject to underwriter due diligence	No history

Operates as blank check company	n/a	Yes - no specific business plan or purpose; may have indicated plans to engage in a merger or acquisition with unidentified companies
Due diligence	Underwriter conducts due diligence on issuer	No due diligence on targeted acquisitions since they are not identified at time of offering
Penny stock	n/a	May issue penny stock; if so, investor funds must be held in escrow and returned if an acquisition does not occur within 18 months of the initial registration statement. Most SPACs structure to be exempt from penny stock designation which means escrow does not apply.
Price	Offered at price per share	Offered at unit price
Dissolution	n/a	Typically must complete an acquisition within 18 to 24 months and use at least 80% of its net assets for any acquisition; if it does not, it must dissolve. Upon dissolution, investors receive a pro rata share of the assets in escrow which usually is all of principal invested but without a share of returns on the assets since those are used for operating expenses of the SPAC.
Secondary market trading	Listed or OTC market for shares	SPACs sell as units which typically are comprised of common stock and a warrant which trade separately within weeks of the IPO. Common shares often trade at a discount to cash held in escrow; warrants are exercisable only upon successful completion of any acquisition and will expire worthless if the SPAC is liquidated.
Targeted acquisitions	n/a	Subject to shareholder vote; investors receive proxy materials outlining the proposed acquisition which may or may not be approved. After a target is announced, it may be weeks before audited financial statements regarding the target are available through the preliminary proxy filing. Acquisition terms and arrangements may change during the proxy filing and review period. SPACs typically require 60% shareholder approval of an acquisition; some require as high as 80% of shareholders.
Completed acquisition	n/a	SPAC sponsors may have a conflict of interest to complete acquisitions. They do not receive a pro rata distribution if the acquisition is not completed and are typically prohibited from selling their shares in the secondary market prior to completion of an acquisition. SPAC managers have a strong incentive to buy a company since they will get 20% of the company at a nominal price.

14.3.1 Suitability

RRs must conduct a suitability analysis before offering a SPAC to an investor. This includes understanding the features and risks of the SPAC and communicating them to the investor. Potential investors should have no

current need for the funds invested since SPACs are longer-term investments that tie up funds without any immediate return.

14.3.2 Risk Disclosures

The following risks must be disclosed to potential investors. This may be accomplished by communicating this information directly or through written disclosures/preliminary prospectuses provided at the time of solicitation.

- SPAC managers may be unqualified or incompetent with no history of operations or past performance of the SPAC.
- No acquisition may occur and the SPAC will be liquidated. While investors have some protection since escrowed funds are returned on a prorated basis (with no guarantee of full principal return) and may be able to sell units on the secondary market, there is an opportunity cost of waiting for acquisitions to be completed

14.3.3 Secondary Market

Buying units in the secondary market involve other considerations. The **common stock** value may depend on whether or not an acquisition target has been announced and whether an announced target is an attractive investment. Release of more information about a target sometimes results in decline in the price of the common stock.

Warrants are suitable only for sophisticated investors with speculative investment objectives who are willing to assume the risk the warrants may expire worthless. Buying warrants after a targeted acquisition is announced includes the risk of increased price at the time of the announcement and potential price decline during a period of delay and release of information about the target.

FINRA research indicates SPAC share prices outpace the market on the day an acquisition target is announced and significantly lag the market after the acquisition is completed.

14.4 Communications Around the Time of Registered Offerings

[SEC Securities Act of 1933 Rule 134, Rule 135, Rule 163, Rule 163A, Rule 164, Rule 168, Rule 169, Rule 405 and Rule 433; SEC Release No. 34-52056; FINRA Rule 2210; FINRA Regulatory Notice 10-52; JOBS Act, Title I; SEC JOBS Act Frequently Asked Questions: <http://www.sec.gov/divisions/corpfin/guidance/cfjobsactfaq-title-i-general.htm>]

Issuing communications (other than the prospectus) to investors around the time of an offering may constitute "gun-jumping." Certain types of communications are permitted or are exempt from gun-jumping restrictions under federal rules. This section summarizes key elements of communications about offerings. The rules are complex and technical; questions should be referred to Compliance.

14.4.1 Categories of Issuers

Permitted communications depend, at least in part, on the category of the issuer, summarized below (the rules should be consulted for details regarding eligibility and ineligibility).

Well-known seasoned issuer: An issuer current and timely in its '34 Act reports for at least one year and has either \$700 million of worldwide public common equity float, or has issued \$1 billion of non-convertible securities (other than common equity) in registered offerings for cash in the preceding three years.

Seasoned reporting issuer: An issuer eligible to register as a primary offering of securities on Form S-3 (among other requirements). To be Form S-3 eligible for a primary offering, a company must have an aggregate market value of \$75 million or more of common equity held by non-affiliates.

Non-reporting and unseasoned issuers: An issuer that does not fall within the above categories (this category is subject to specific restrictions).

Ineligible issuers: Issuers that are ineligible as defined in Rule 405 and where communications outside the prospectus are not permitted. Rule 164 regarding free writing prospectuses also excludes investment companies registered under the Investment Company Act of 1940 and offerings involving an issuer registering a business combination transaction.

Emerging growth company ("EGC"): A company that conducts an IPO after December 8, 2011 and had annual gross revenues of less than \$1 billion during its most recent fiscal year. A company will retain EGC status until the earliest of:

- the first fiscal year after its annual revenues reach \$1 billion;
- the first fiscal year following the fifth anniversary of its IPO;
- the date on which the company has, during the previous three-year period, issued more than \$1 billion in non-convertible debt; and
- the date on which the company becomes a "large accelerated filer."

14.4.2 Other Definitions

Free writing prospectus: A written communication (including electronic communications) outside the statutory prospectus that after the filing of the registration statement, may be filed with the SEC, with certain conditions depending on the type of issuer.

Written communications: All methods of communication other than oral communications are defined as "written." Written communications include any communication that is written, printed, a radio or television broadcast, or graphic communication. *Graphic communication* excludes communications that are carried live and in real-time to a live audience, regardless of the method of transmission. All electronic communications (other than telephone and other live, in real-time communications to a live audience) are "written."

Electronic roadshows: Live electronic roadshows, even though transmitted to a live audience via an electronic medium, are not considered "written" material. Electronic road shows that are not live are considered free writing prospectuses. Electronic road shows for IPOs of common equity or convertible equity securities do not have to be filed with the SEC if a version of the bona fide electronic road show is made readily available to an unrestricted audience. No other road shows are subject to filing with the SEC.

14.4.3 Permitted Offering Activity And Communications

The following is an overview of permitted communications.

- Well-known seasoned issuers may engage, at any time, in oral and written communications, including the use of a free writing prospectus.
- Emerging Growth Companies (EGCs) are subject to fewer restrictions than other issuers. Contact Compliance for clarification of permitted communications. Some restrictions or permissible activities involving EGCs include:
 - Any firm subject to the Global Settlement remains restricted by any applicable terms of the settlement.

- When "testing the waters," an underwriter may ask customers for nonbinding indications of interest, including how many shares the customer may seek to purchase, without violating rules requiring the provision of a preliminary prospectus when soliciting orders.
- All reporting issuers may, at any time, continue to publish regularly released factual business information and forward-looking information.
- Non-reporting issuers may, at any time, continue to publish factual business information that is regularly released and intended for use by persons other than in their capacity as investors or potential investors.
- Communications by issuers, more than 30 days before filing a registration statement, are permitted, if they do not reference the securities offering that is the subject of a registration statement.
- All issuers and offering participants may use a free writing prospectus after the filing of the registration statement, subject to conditions. The statutory prospectus has to accompany or precede the free writing prospectus for unseasoned or non-reporting issuers, if the issuer or an offering participant prepares or pays for the free writing prospectus.
- Some routine communications are permitted, including an offering schedule or about account opening procedures.
- Research reports (other than reports on EGCs) may be issued under the safe harbors of Rules 137, 138, and 139. There are no restrictions on issuing research reports on EGCs.
- Media interviews are permitted if they meet the conditions of Rule 433 and conditioned on whether the issuer or participant paid for the media communication.

14.4.4 Social Media

[SEC Securities Act Rules Compliance and Disclosure Interpretations (re applicability of rules to use of social media relating to offerings): <http://www.se.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm>]

The SEC has provided guidance regarding use of social media for certain written communications otherwise subject to SEC regulation, as follows. The Compliance and Disclosure interpretations should be referenced for details.

- Rule 134 announcements
- Free writing prospectuses
- Business combination communications
- Proxy solicitations
- Pre-commencement communications in tender offers

The SEC's guidance addresses legend requirements. Existing rules restricting the permitted content of these communications and/or that impose filing requirements are unchanged. The legend requirement may be satisfied by using an active hyperlink under the following conditions:

- The electronic communication is distributed through a platform that has technological limitations on the number of characters or amount of text that may be included;
- Including the required statements in their entirety, together with the other information, would cause a communication to exceed the limit on the number of characters or amount of text; and
- The communication includes an active hyperlink to the required legend (and other required information) and prominently conveys, through introductory language or otherwise, that important or required information is provided through the hyperlink.

14.4.5 Free Writing Prospectus

Any free writing prospectus distributed in a manner reasonably designed to lead to "broad unrestricted dissemination" [described in Securities Act Rule 433(d)(1)(ii)] is subject to FINRA Rule 2210 (Communications with the Public). Free writing prospectuses are subject to the following:

- Review and approval by a registered principal prior to distribution
- Filing with FINRA within 10 days of first use
- For FWPs provided to institutional investors [defined in FINRA Rule 2210(a)], approval prior to distribution is **not** required.

Unrestricted dissemination includes posting an FWP on an unrestricted website or releasing it to the media. Posting to a restricted website or an FWP sent directly to customers (regardless of the number of customers) does not constitute broad unrestricted dissemination.

14.5 New Issue Allocations and Distributions

[FINRA Rule 5131]

The following sections outline policies and procedures that govern the sale of new issues of equity securities. A "new issue" refers to an initial public offering of an equity security [as defined in Section 3(a)(11) of the Exchange Act] made pursuant to a registration statement or offering circular.

14.5.1 Fixed Priced Offerings

[FINRA Rule 5141]

Offerings must be sold at the stated public offering price to buyers, i.e., preferences cannot be granted to purchasers. A reduced price below the stated price is prohibited other than to those that are a member participating in a selling syndicate or selling group. This prohibition applies until the termination of the offering or until, after making a bona fide public offering of the securities, securities remain unsold.

A member of a selling syndicate or selling group may sell securities in the offering to an affiliated person (subject to restrictions under Rule 5130) if the securities are not sold at a reduced price. The prohibition does not apply to research provided under a soft dollar arrangement under Section 28(e) of the '34 Exchange Act.

A "**reduced price**" includes any direct or indirect offer or grant of a selling concession, discount, or other allowance, credit rebate, reduction of any fee (including any advisory or service fee), any sale products or services below reasonable commercially available rates for similar products and services (except research as described below) or any purchase of or arrangement to purchase securities from the person or account at more than their fair market price in exchange for securities in the offering.

"**Fair market price**" refers to a price or range of prices at which a buyer and a seller, each unrelated to the other, would purchase the securities in the ordinary course of business in transactions that are of similar size and similar characteristics and are independent of any other transaction.

14.5.2 Indications of Interest

Indications of interest are accepted prior to the effective date of the underwriting. Indications of interest are not orders and do not become orders until the syndicate supervisor confirms that securities are available to satisfy indications; RRs are responsible for re-confirming the customer's purchase of the securities at the time the issue is effective and allocated to customers. There is no assurance of an adequate quantity of securities to meet indications of interest.

14.5.3 Conditional Offers

Coastal Equities, Inc. may allow "conditional offers" for an underwriting; RRs will be notified if such orders are allowed and during what period the customer may revoke the order.

14.5.4 Prospectuses and Confirmations To Purchasers

[SEC Securities Act of 1933 Rule 172 and Rule 173]

Responsibility	<ul style="list-style-type: none">• Syndicate Supervisor
Resources	<ul style="list-style-type: none">• Indications of Interest• Record of purchasers
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Provide preliminary prospectuses to RRs when available• Notify Operations to include the required disclosure on confirmations sent to purchasing customers• If a final prospectus is required to be provided to investors, obtain prospectuses and forward to appropriate Operations personnel for sending or establish electronic access to the prospectus and notify purchasers
Record	<ul style="list-style-type: none">• A record of purchasers and sending of prospectuses (if required) is maintained in the deal file or establishment of electronic access and notice provided to purchasers

14.5.4.1 Confirmations and Notices of Allocations of Shares

Written confirmations and notices of allocations of shares offered, may be sent after the effectiveness of a registration statement (for an issue complying with Rule 172) without being accompanied or preceded by a final prospectus. Written communication from a broker-dealer to a customer, or from an underwriter to participating dealers in the selling group, may notify them of the basic terms of the transaction or their allocations of the securities. Notices of allocation may include the identity of the securities; CUSIP number; amount allocated; price; date or expected date of settlement; and incidental information.

When final prospectuses are not required, purchasers will be provided, no later than two business days after the sale a notice that the sale was made pursuant to a registration statement or in a transaction in which a final prospectus would not have been required to have been delivered in the absence of Rule 172.

14.5.4.2 Preliminary and Final Prospectuses

Preliminary prospectuses will be provided to RRs if available. These should be provided to customers submitting an indication of interest in the new issue.

The issuer is not required to print and physically deliver a final prospectus to investors, if the issuer files the prospectus with the SEC within a prescribed period of time and complies with certain other conditions. For issuers that are required to provide prospectuses, copies will be obtained and forwarded to purchasers. In lieu of

sending prospectuses, purchasers may be notified of electronic access to prospectuses if the issue qualifies for this alternative under Rule 172.

An investor may request a physical copy of the final prospectus, but the prospectus is not required to be provided prior to settlement.

14.5.4.3 Purchases During the Post-Effective Period

[SEC Securities Act of 1933 Rule 174 and Section 4(3)]

There is no obligation to provide a prospectus to purchasers in the post-effective period if the issuer is a reporting company under Section 13 or 15(d) of the '34 Act; is a shelf offering (other than the first bona fide offering); or if the registration statement is on Form F-6. This exemption does **not** apply to blank check companies.

For issues not included above, customers who purchase in the post-effective period and where the issue satisfies the requirements of Rule 172, will be provided with the required notice (see *Confirmations And Notices Of Allocations Of Shares*, above) within two business days of the sale. This requirement applies for a period of 25 calendar days after the offering date.

For issues that do not qualify under Rule 172, purchasers during the period of 25 calendar days after the offering date will be sent a copy of the final prospectus.

14.5.4.4 Term Sheets

[SEC Regulation C Rule 421]

Term sheets may be provided to prospective purchasers and will meet the requirements of a plain English summary that includes most material terms of the proposed offering. Bullet points will cross-reference detailed information in the prospectus or other offering document.

Term sheets may also be provided to new issue purchasers who have received a preliminary prospectus. The term sheet is included with the customer's confirmation and supplements the preliminary prospectus to disclose final terms such as price and effective date.

14.5.4.5 Electronic Delivery of Prospectuses

[SEC Securities Exchange Act of 1934 Release No. 37182 (May 1996) and Release No. 36345 (Oct. 1995)]

Where Coastal Equities, Inc. determines to provide prospectuses through electronic media, the following guidelines apply:

- The prospectus itself may be sent to the investor by disk, tape, email, or similar method.
- If a prospectus is posted on Coastal Equities, Inc.'s web site, separate written notice by email or regular mail will be forwarded to the investor.
- Customers must agree to accept electronic delivery and consent retained in the customer's records.
- Delivery must be evidenced (confirmation document has been downloaded, record of hyper link access; *etc.*)
- Current updated versions of the preliminary prospectus may be posted on Coastal Equities, Inc.'s website available to all potential investors. Notice of updates is sent to investors expected to purchase the offered securities.
- Final prospectuses will be posted to the website and written notice mailed to purchasers notifying them how they may access the prospectus.

- When a prospectus is amended, (1) a postcard or email will be sent to investors notifying them of the availability of the amended prospectus or (2) a paper copy of the amendment will be sent to investors.

14.5.5 Restrictions on Purchase and Sale of IPOs of Equity Securities

[FINRA Rule 5130; FINRA Regulatory Notice 19-37]

Responsibility	<ul style="list-style-type: none"> • Syndicate Supervisor
Resources	<ul style="list-style-type: none"> • Indications of interest for IPOs
Frequency	<ul style="list-style-type: none"> • As required, when equity IPOs are offered
Action	<ul style="list-style-type: none"> • Review indications to determine no purchasers are restricted persons • If potential purchasers are restricted, notify RR and offer the shares to a qualified purchaser
Record	<ul style="list-style-type: none"> • Indications of interest and review to identify restricted persons are included in the underwriting file

When selling IPOs, the distribution of shares must be a *bona fide* public offering and fair distribution to the public. This means sales will not be made to benefit insiders in the securities industry or to other closely-related parties that might unfairly benefit at the expense of public customers. This section describes key elements of FINRA rule that limits the types of investors that may purchase equity IPOs.

The Rule should be consulted for specific details. Questions regarding restrictions should be directed to the syndicate supervisor or to Compliance.

14.5.5.1 Restricted Persons

Equity IPOs **may not be purchased** by "restricted persons" as defined in FINRA Rule 5130 including accounts where the restricted person has a beneficial interest. Restricted persons include:

- **FINRA members or other broker-dealers**
- **Broker-dealer personnel**
 - Any officer, director, general partner, associated person or employee of a member or any other broker-dealer;
 - Any agent of a member or any other broker-dealer that is engaged in the investment banking or securities business; or
 - An immediate family member or a person listed above if the above person:
 - Materially supports, or receives material support from, the immediate family member;
 - Is employed by or associated with the member, or an affiliate of the member, selling the new issue to the immediate family member; or
 - Has the ability to control the allocation of the new issue.
- **Finders and fiduciaries**
 - With respect to the security being offered, a finder or any person acting in a fiduciary capacity to the managing underwriter, including, but not limited to, attorneys, accountants and financial consultants; and

- An immediate family member of a person above if the person materially supports or receives material support from the immediate family member.
- **Portfolio managers** (any person who has authority to buy or sell securities for a bank, savings and loan institution, insurance company, investment company, investment advisor, or collective investment account) and their immediate family members if the person materially supports or receives material support from the immediate family member
- **Persons who have ownership in a broker-dealer including:**
 - **Direct owners** (any person listed, or required to be listed, on Schedule A of Form BD) unless ownership is less than 10%
 - **Indirect owners** (any person listed or required to be listed on Schedule B of Form BD) unless ownership is less than 10%
 - **Persons listed** or required to be listed on **Schedule C** of Form BD
 - **Persons that directly or indirectly own 10% or more of a public reporting company** listed or required to be listed in Schedule A or **persons that directly or indirectly own 25% or more of a public reporting company** listed in Schedule B of Form BD (other than reporting companies listed on an Exchange, the NASDAQ National Market, or that is a limited business broker-dealer)
 - **Immediate family members** of the above, with some exclusions in the Rule

Excluded from the definition of "restricted person" is an **employee** or immediate family member of an employee of a "**limited business broker-dealer**" which is defined as any broker-dealer whose business is limited solely to the purchase and sale of investment company/variable contract securities and direct participation program securities.

14.5.5.2 General Prohibitions

The following summarizes the general prohibitions that apply to the sale of equity IPOs.

1. Restricted persons are not allowed to purchase IPOs, unless there is an available exemption.
2. A broker-dealer or associated person (AP) may not purchase an equity IPO in an account where the BD or AP has a beneficial interest.
3. A broker-dealer may not continue to hold new issues acquired as underwriter or selling group member except when the issue is under-subscribed (described in a later section).

14.5.5.3 Certification of Non-Restricted Status Required from All Purchasers

Responsibility	<ul style="list-style-type: none"> ● Syndicate Supervisor ● Compliance - annual negative consent
Resources	<ul style="list-style-type: none"> ● Indications of interest ● IPO certifications
Frequency	<ul style="list-style-type: none"> ● As required, when equity IPOs are offered ● Annual - negative consent letter
Action	<ul style="list-style-type: none"> ● Determine whether proposed purchaser has submitted the IPO certification ● If not, contact RR or otherwise obtain the required certification ● For accounts lacking certification, exclude from IPO purchasers

	<ul style="list-style-type: none"> • Compliance - arrange for annual negative consent and change the customer's eligibility to purchase IPOs if the customer's non-restricted status has changed
Record	<ul style="list-style-type: none"> • Notation that indications have been reviewed for certifications are included in the underwriting file • Certification is noted on the account record and retained in customer records • Record is retained that the annual negative consent has been sent

An IPO may not be sold to an account unless, during the prior 12 months, Coastal Equities, Inc. has received certification that the account is eligible to purchase new issues. This includes certification from conduit accounts (discussed below). Coastal Equities, Inc. or an RR cannot rely on a certification that it has reason to believe is not accurate.

14.5.5.3.1 Initial and Annual Certification

Prior to the first purchase of an equity IPO, the prospective purchaser must sign and submit the IPO Certification form that certifies that the underlying beneficial owners are not restricted persons. The account will be considered non-restricted based on the customer's certification.

After receiving the IPO Certification, Coastal Equities, Inc. will annually send a negative consent letter asking the customer to notify Coastal Equities, Inc. if the initial certification is no longer accurate.

14.5.5.3.2 Conduit Accounts

Certification must be obtained when a potential IPO purchaser is a "conduit" account, which includes, for example, an investment partnership or corporation, a foreign investment company, an investment adviser, and an account for which a bank or trust company is acting as a conduit. The conduit is required to certify that the beneficial owner or ultimate purchaser is not a restricted person.

14.5.5.3.3 Indirect Beneficial Owners

[FINRA Rule 5131.02(b)]

Where it is difficult to identify indirect beneficial owners such as participants in unaffiliated private funds (such as a fund of funds), Coastal Equities, Inc. may rely on a written representation obtained within 12 months by a person authorized to represent an account that does not look through to the beneficial owners of any unaffiliated private fund invested in the account, except for beneficial owners that are control persons of the investment adviser to the private fund. An unaffiliated private fund that qualifies under this exception:

- is managed by an investment adviser;
- has assets greater than \$50 million;
- owns less than 25% of the account and is not a fund in which a single investor has a beneficial interest of 25% or more; and
- was not formed for the specific purpose of investing in the account.

An "unaffiliated private fund" is a private fund defined in Section 202(a)(29) of the Investment Advisers Act, whose investment adviser does not have a control person in common with the investment adviser to the account.

14.5.5.3.4 Third Party Vendor Certifications

Coastal Equities, Inc. may use a third party that obtains certification that potential purchasers are eligible to buy IPOs. Under this approach, the syndicate supervisor is responsible for confirming that the third party has procedures in place that comply with FINRA Rule 5130 and for signing an agreement with the vendor. When a third party is used, Coastal Equities, Inc.'s records will include verification of IPO purchasers' eligibility against the third party's records and at least annual review that the third party's procedures comply with FINRA requirements. Record of third party certifications is retained in the deal file.

14.5.5.4 Exemptions

Equity IPOs **may be sold** to the following types of accounts and are **not subject to** restricted person prohibitions or requirements.

- Registered investment companies.
- Common trust funds with investments from 1000 or more accounts and that do not limit interests in the fund principally to trust accounts of restricted persons.
- Insurance company general, separate, or investment accounts provided that:
 - the account is funded by premiums from 1000 or more policyholders, or, if a general account, the insurance company has 1000 or more policyholders; and,
 - the insurance company does not limit the policyholders whose premiums are used to fund the account principally to restricted persons, or if, a general account, the insurance company does not limit its policyholders to restricted persons.
- *De minimis* exemption for purchase by an account if the beneficial interests of restricted persons do not exceed the aggregate 10% of the account.
- Publicly traded entities listed on a national securities exchange or traded on the NASDAQ Global Market (NGM) or are foreign issuers that meet the quantitative designation criteria for listing on a National securities exchange or NGM. This exemption **does not** include sales to publicly-traded broker-dealers or a publicly-traded affiliate of a broker-dealer.
- Foreign investment companies organized under the laws of a foreign jurisdiction that are listed on a foreign exchange or authorized for sale to the public by a foreign regulatory authority provided that no person owning 5% or more of the investment company is a restricted person.
- ERISA benefit plans qualified under Section 401(a) of the Internal Revenue Code (IRC) provided the plan is not sponsored solely by a BD.
- State or municipal government plans subject to state and/or municipal regulation.
- Tax-exempt charity organized under Section 501(c)(3) of the IRC.
- Church plans described in Section 414(e) of the IRC.

14.5.5.5 Issuer-Directed Securities

[FINRA Rule 5130(d) and 5130.01]

Issuers often direct the underwriter to offer shares to certain persons. Issuer-directed securities may not be sold to:

- a broker-dealer.
- an account in which any restricted person (broker-dealer personnel/immediate family and finders/fiduciaries as defined by the rule) has a beneficial interest. This applies unless such a person or an immediate family member is an employee or director of the issuer, the issuer's parent, or a subsidiary of the issuer or the issuer's parent. A parent/subsidiary relationship exists if the parent has the right to vote

50% or more of a class of voting security of the subsidiary, or has the power to sell or direct 50% or more of a class of voting security of the subsidiary.

The following are exempt from the restrictions on sales of IPOs.

1. Shares are specifically directed by the issuer and are part of an offering in which no broker-dealer:
 - underwrites any portion of the offering;
 - solicits or sells any new issue securities in the offering; and
 - has any involvement or influence, directly or indirectly in the issuer's allocation decisions with respect to any of the new issue securities in the offering.
2. Offering shares are part of a program sponsored by the issuer, or an affiliate of the issuer, that meets four conditions:
 - the opportunity to purchase a new issue under the program is offered to at least 10,000 participants;
 - every participant is offered an opportunity to purchase an equivalent number of shares or will receive a specified number of shares under a predetermined formula applied uniformly across all participants;
 - if not all participants receive shares under the program, the selection of the eligible participants is based on a random or other non-discretionary allocation method; and
 - the class of participants does not contain a disproportionate number of restricted persons.
3. The issuer-directed exemption also applies to new issues directed to eligible purchasers as part of a conversion offering conducted in accordance with the standards of the governmental agency or instrumentality having authority to regulate the conversion offering.

14.5.5.6 Anti-Dilution

A restricted person that is an existing equity owner of an issuer may purchase shares in the IPO in order to maintain its equity ownership position. To qualify for this exemption, the restricted person must meet the following criteria:

- the account held shares for a period of at least 1 year prior to the offering;
- the sale of the new issue does not increase the account's percentage equity ownership in the issuer above the ownership level as of 3 months prior to the filing of the registration statement for the offering;
- the sale of the new issue to the account does not include any special terms; and,
- the new issue is held for at least 3 months following the effective date of the offering.

14.5.5.7 Stand-By Purchasers

Prohibitions on sales of IPOs do not apply if made pursuant to a stand-by agreement that meets four conditions:

1. the stand-by agreement is disclosed in the prospectus;
2. the stand-by agreement is subject to a formal written agreement;
3. the managing underwriter represents in writing that it is unable to find any other purchasers for the securities; and,
4. securities sold under a stand-by agreement are subject to a 3-month lock-up period.

14.5.5.8 Firm Account

Coastal Equities, Inc. is not permitted to retain shares in an initial IPO that is oversubscribed. If a customer cancels his or her indication of interest, the shares will be reallocated to fill another customer's interest. If, in the unusual circumstance another buyer cannot be found, Compliance must be contacted regarding proper placement of the securities which, if retained in a firm account, will be held for a minimum of 60 days.

If Coastal Equities, Inc. is unable to sell all shares for which it has committed and the issue is under-subscribed, Coastal Equities, Inc. may place those shares in a firm account.

14.5.5.9 Definitions Applying to New Issue Allocations and Distributions

[FINRA Rule 5130(i) and 5131(e)]

The following are selected Rule definitions; the Rule should be consulted for other definitions.

Beneficial interest: Any economic interest such as the right to share in gains and losses. This excludes receipt of a management or performance-based fee for operating a collective investment account, or other fees for acting in a fiduciary capacity.

Collective investment account: Any hedge fund, investment partnership, investment corporation, or any other collective investment vehicle engaged primarily in the purchase or sale of securities. This does not include a family investment vehicle or investment club.

Flipped: The initial sale of new issue shares purchased in an offering within 30 days following the offering date of the offering.

Immediate family member: Parents, in-laws, spouse, siblings, and children. The definition also includes anyone else to whom the person provides material support.

Material support: Directly or indirectly providing more than 25% of a person's income in the prior calendar year. Members of the immediate family living in the same household are deemed to be providing each other with "material support."

New issue: Any initial public offering of an equity security as defined in Section 3(a)(11) of the Exchange Act made through a registration statement or offering circular. FINRA Rule 5130(i)(9) excludes a number of offerings from this definition (refer to the rule for details) including sales under Rule 144, 144A, or 506; offerings of exempt securities; commodity pools; rights offerings; exchange offers; investment-grade asset-backed securities; convertible securities; preferred securities; investment companies; ADRs; and DPPs. This list does not include all exempt securities listed in the FINRA rule.

Penalty bid: An arrangement that permits the managing underwriter to reclaim a selling concession from a syndicate member in connection with an offering when the securities originally sold by the syndicate member are purchased in syndicate covering transactions.

Restricted person: Defined at the beginning of this section.

14.5.6 Disclosure of Interest In Distribution

[SEC Securities Exchange Act of 1934 Rule 15c1-6; FINRA Rule 2269]

At or before completion of a transaction in a primary or secondary distribution with managed accounts or other accounts where a fee is charged, the customer will be provided with written notice of the existence of Coastal Equities, Inc.'s participation in the distribution.

14.5.7 State Blue Sky Requirements

The syndicate supervisor is responsible for reviewing purchasers, prior to confirming transactions, to ensure the issue is sold only to purchasers in states where the issue is blue skied or is eligible for sale under an exemption.

14.5.8 Cancellation Policy

Indications of interest are not orders until the customer is contacted and confirms that securities allocated to the customer are accepted. At that point, a confirmation and final prospectus will be provided and the customer will be expected to pay for the transaction.

If the customer then cancels the purchase, Compliance should be contacted to resolve the matter, which may include:

- Consideration of whether the customer received a preliminary prospectus prior to confirming the purchase.
- Determination whether the customer should be held responsible for the purchase or the purchase cancelled.
- If cancelled and all other securities were sold in the underwriting, offer the new issue to another customer whose interest was not filled.
- If no other customer is available to purchase the securities, cancel the purchase to Coastal Equities, Inc.'s account. The RR who sold the shares may be held responsible for any loss incurred due to the cancellation.

14.5.9 Designated Orders

When the firm has been designated by a customer and is not acting as underwriting manager, the following information will be retained for 24 months:

- name of customer making designation
- identity and amount of securities designated
- identity of manager or managers of the offering
- date of commencement of the offering

14.5.10 Flipping

[FINRA Rule 5131(c)]

Customers may be limited or prohibited from purchasing future new issues at the syndicate supervisor's discretion because the customer engages in short-term trading of new issues (selling the new issue immediately or shortly after it becomes effective).

Flipping refers to the practice of selling new issues into the secondary market at a profit within 30 days following the offering date. Coastal Equities, Inc. and its employees are prohibited from directly or indirectly recouping, or attempting to recoup, any portion of a commission or credit paid or awarded to an associated person for selling shares of a new issue that are subsequently flipped by the customer, unless the managing underwriter has assessed a penalty bid on the entire syndicate. Under a penalty bid, Coastal Equities, Inc. itself is required to forfeit its compensation to the managing underwriter(s).

14.5.11 Quid Pro Quo Allocations

[FINRA Rule 5131(a)]

Coastal Equities, Inc. (and its employees) are prohibited from offering or threatening to withhold shares it allocates of a new issue as consideration or inducement for the receipt of compensation that is excessive in relation to the services provided by Coastal Equities, Inc.. The rule prohibits a firm from using an allocation of a new issue as a means of obtaining a "kick back" from the recipient in the form of excessive compensation for services offered by Coastal Equities, Inc.. The prohibition applies not only to trading services but also to any service offered by Coastal Equities, Inc.. The rule does not prohibit providing services where the customer does not pay excessive compensation.

14.5.12 Spinning

[FINRA Rule 5131(b)]

FINRA rule prohibits firms from allocating shares to obtain the investment banking business of a customer. Coastal Equities, Inc. and its employees are prohibited from allocating shares of a new issue to any account where an executive officer or director of a public company or a covered non-public company, or a person materially supported by such executive officer or director, has a beneficial interest:

- If the company is currently an investment banking services customer of Coastal Equities, Inc. or Coastal Equities, Inc. has received compensation from the company for investment banking services in the past 12 months;
- If the person responsible for making the allocation decision knows or has reason to know that Coastal Equities, Inc. intends to provide, or expects to be retained by the company for, investment banking services within the next 3 months; or
- On the express or implied condition that such executive officer or director, on behalf of the company, will retain Coastal Equities, Inc. for the performance of future investment banking services.

These prohibitions do not apply to allocations to any account exempt under FINRA Rule 5130(c) listed in the section *Restrictions On Purchase And Sale of IPOs Of Equity Securities – Exemptions* in this chapter **with the exception** of the *de minimis* exemption if beneficial interest does not exceed 10%. The spinning exception applies to persons materially supported by them in aggregate do not exceed **25%** of such account.

The New Issue Certification includes inquiry whether the potential purchaser is an executive officer or director or person materially supported by them.

14.6 Trading Restrictions While Participating in a Distribution

[SEC Regulation M; FINRA Notice to Members 97-10; FINRA Reg M Frequently Asked Questions: <https://www.finra.org/rules-guidance/faq/regulation-m>]

Responsibility	<ul style="list-style-type: none">• Compliance - Restricted List, review of transactions for compliance• Designated supervisor - Review for prohibited short sales
Resources	<ul style="list-style-type: none">• Notification from the syndicate supervisor regarding pending deals• Customer transaction reports• Available exception reports
Frequency	<ul style="list-style-type: none">• As required

Action	<ul style="list-style-type: none"> • Compliance: <ul style="list-style-type: none"> ○ Add to and remove from the Restricted List securities subject to Regulation M trading restrictions ○ Review transactions for compliance ○ Where exceptions are identified, contact the RR/RR's supervisor regarding the transaction ○ Determine whether the transaction must be cancelled • Designated supervisor: <ul style="list-style-type: none"> ○ Review transactions for five business days before pricing of the offering and ending with pricing; or for the period beginning with the initial filing of the registration statement or notification on Form 1-A and ending with pricing (whichever period is shorter) to identify violating short sales ○ If violating short sales are identified, contact the RR and the RR's supervisor and cancel the transactions or take other corrective action in consultation with Compliance ○ Identify market orders for new issues entered prior to trading of shares in the secondary market and, if found, take corrective action which may include consultation with the RR and the RR's supervisor and cancellation of the transaction
Record	<ul style="list-style-type: none"> • Notification from the syndicate supervisor • Record of orders reviewed including exceptions and corrective action and reviewer's initials and date reviewed

Trading restrictions apply to securities that are the subject of a distribution and also apply to a "reference security," a security into which the distributed security may be converted, exchanged, or exercised or where the terms of the distributed security may determine the value of the reference security. Bids for and purchases of outstanding nonconvertible debt securities are not restricted unless the security being purchased is identical in all terms to the security being distributed. Investment grade nonconvertible debt securities, nonconvertible preferred securities, and asset-backed securities are excluded from restrictions.

14.6.1 Distribution Participant Restrictions

[SEC Regulation M Rule 101]

Orders may not be solicited in the outstanding securities of an issue the subject of an underwriting (and reference securities) under certain conditions of Regulation M:

- No restriction for securities with average daily trading volume (ADTV, as defined in Rule 101) of \$1 million or more and a public float of at least \$150 million
- One business day restriction for securities with ADTV of at least \$100,000 but less than \$1 million and a public float of at least \$25 million
- Five business days for all other securities

The syndicate supervisor will notify Compliance when an issue is subject to these restrictions. Compliance will update Coastal Equities, Inc.'s Restricted List and will monitor daily transactions to inquire whether transactions are solicited or unsolicited, if not included on the order record. If transactions are solicited, Compliance will determine what corrective action is necessary.

The restriction remains in effect until price and trading restrictions are lifted.

14.6.2 Issuer and Selling Security Holder Restrictions

[SEC Regulation M Rule 102]

Issuers, selling security holders, and their affiliated purchasers are restricted from engaging in bidding for, purchasing, or attempting to induce someone else to bid or purchase for a distributed security.

14.6.3 Short Sales

[SEC Regulation M Rule 105; SEC Release No. 34-56206]

A person may **not** purchase a security from an underwriter or broker or dealer participating in a public offering if the person sold the security short during the "Rule 105 restricted period." The Rule 105 restricted period is the shorter of:

- the period beginning five business days before the pricing of the offered securities and ending with such pricing; or
- the period beginning with the initial filing of the registration statement or notification on Form 1-A or Form 1-E and ending with the pricing.

Exceptions to the short sale limitation include the following.

1. Bona fide purchases: Restricted period short sellers may purchase offered securities if they make a bona fide purchase of the same security prior to pricing. A *bona fide purchase* must be:

- at least equal in quantity to the entire amount of the Rule 105 restricted period short sale(s);
- effected during regular trading hours;
- reported pursuant to an effective transaction reporting plan; and
- made after the last Rule 105 restricted period short sale and no later than the business day prior to the day of pricing

In addition, the person may not have effected a short sale that is a reported transaction within 30 minutes before the close of regular trading hours on the business day prior to the day of pricing.

2. Separate accounts: A purchase of the offered security may be made in an account that sold short during the Rule 105 restricted period in a separate account if decisions regarding transactions for the account are made separately and without coordination of trading or cooperation among or between accounts.

3. Investment companies: An individual fund within a fund complex, or a series of a fund, will not be prohibited from purchasing the offered security if another fund within the same complex or a different series of fund sold short during the Rule 105 restricted period.

There are conditions that apply to these exceptions; Compliance should be consulted for further guidance regarding covering short sales in securities subject to a public offering.

14.6.4 Market Order Prohibition

[FINRA Rule 5131(d)(4); FINRA Regulatory Notice 11-29]

Market orders accepted in both NMS stocks and OTC equity securities **are prohibited** when purchasing shares of a new issue in the secondary market prior to commencement of trading of the shares in the secondary market. The market order prohibition applies whether the order is from a customer of Coastal Equities, Inc., a customer of

another broker-dealer, or another broker-dealer. Priced orders such as limit orders are not subject to the prohibition.

"Commencement of trading" in the secondary market is evidenced by the first trade on the listing national securities exchange as indicated by dissemination of an opening transaction in the security by that exchange. For OTC equity securities, commencement is evidenced by the first regular way, disseminated trade reported to the OTC Reporting Facility during normal market hours.

"Not held" orders are not considered "market orders" under this rule. The prohibition applies to "acceptance" of any market order. In the case of a proprietary order, if it is sent directly to an exchange, the prohibition does not apply. If the proprietary order is routed to a member firm, the order is "accepted" by the firm and therefore the restriction applies.

Coastal Equities, Inc. may reject a market order for a new issue at any point within its order management system prior to executing or routing the order. If Coastal Equities, Inc. rejects a previously-accepted customer order that is OATS reportable, Coastal Equities, Inc. must indicate on the OATS report that Coastal Equities, Inc., not the customer, cancelled the order.

14.6.5 Prohibited Conduct

[SEC Release No. 34-51500; SEC Guidance Regarding Prohibited Conduct in Connection with IPO Allocations]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records regarding IPO purchase and aftermarket transactions
Frequency	<ul style="list-style-type: none"> • As required, when issues are over-subscribed
Action	<ul style="list-style-type: none"> • Review purchases of IPOs vs. aftermarket purchases and sales to identify patterns which may indicate prior inducements • Contact supervisors and RRs regarding questionable transactions • If violations are determined, take corrective action in consultation with Compliance regarding disciplinary action against the RR
Record	<ul style="list-style-type: none"> • Transactions reviewed including reviewer, date reviewed, and action taken, if any

Underwriters often engage in "bookbuilding" which involves seeking information from potential investors regarding their interest in the prospective issue including number of shares and price. Bookbuilding helps the pricing and success of the new issue.

There are related practices that are prohibited because they constitute attempts to induce aftermarket bids and purchases, which negatively affect the integrity of the distribution process. The following practices are **prohibited**, per the SEC:

1. Agreements to purchase shares in the aftermarket in exchange for an IPO allocation, prior to completion of the distribution. This includes agreements to purchase shares in another less desirable stock to obtain an IPO allocation.
2. Communicating to customers that expressing an interest in or buying shares in the immediate aftermarket would help them obtain allocations of over-subscribed ("hot") IPOs.

3. Soliciting customers before the completion of the distribution about whether and at what price and in what quantity the customer intends to place immediate aftermarket orders for IPO stock where the clear expectation and understanding is that the customer will submit aftermarket orders at the prices and quantities discussed if the customer receives an allocation of shares.
4. Proposing aftermarket prices to customers or encouraging customers who express aftermarket interest to increase the prices at which they are willing to place orders in the immediate aftermarket.
5. Soliciting interest from customers in purchasing aftermarket shares in some fixed proportion to the customer's IPO allocation.
6. Soliciting aftermarket orders from customers before all IPO shares are distributed or rewarding customers for aftermarket orders by allocating additional IPO shares to such customers.
7. Communicating to customers in connection with one offering that expressing an interest or buying in the aftermarket would help them obtain IPO allocations of other over-subscribed IPOs.

14.7 At-The-Market (ATM) Offerings

[SEC Regulation M Rule 100 and Rule 104]

An "at-the-market" offering is a form of shelf registration that allows a company to sell newly-issued shares into the market at prevailing market prices from time to time over a period extending to 36 months rather than through a traditional underwriting offering a fixed number of shares at a fixed price in one event.

The following summarizes key requirements and characteristics of ATM offerings.

- The company files a shelf registration statement on Form S-3 or Form S-3ASR for issuers that qualify as well-known seasoned issuers (WKSI).
- The basic prospectus states that sales of stock may be made from time to time at prevailing market prices by the issuer or through a designated agent.
- The issuer enters into a sales agreement with a broker-dealer that acts as placement agent.
- The issuer may establish terms of sales orders such as minimum required pricing, volume limitations, *etc.* and the terms may be altered at any time. Orders may be executed over an ECN or sold in block trades, private sales, and otherwise.
- Programs may last up to 36 months.
- The issuer will typically disclose aggregate sales and commission amounts on a quarterly basis in a prospectus supplement to update the base prospectus.
- The terms of an ATM offering generally do not restrict an issuer's ability to issue equity securities in traditional underwritten public offerings or PIPE sales.
- Lock-up provisions in a typical underwritten offering will also restrict sales under an ATM offering program, unless otherwise agreed.

14.7.1 Placement Agent Responsibilities

Coastal Equities, Inc. will follow procedures outlined in the section *Managing Underwriter* in this chapter including executing a letter of intent; conducting due diligence; and submitting the deal to the Investment Committee for review. Upon acceptance of the deal, Coastal Equities, Inc. will execute a sales agreement with the issuer.

14.7.2 Restrictions on Purchasers of New Issues

[FINRA Rule 5130]

The restrictions on purchasers of new issues apply to at-the-market offerings. This restricts employees of broker-dealers and others from buying new issue shares. Refer to the section *Restrictions on Purchase and Sale of IPOs of Equity Securities* in this chapter for further details.

14.7.3 Settlement

Coastal Equities, Inc. will submit a trade blotter to the issuer on an agreed-upon basis (which may be daily). The blotter includes all trades made during the preceding period and specifies gross proceeds. Coastal Equities, Inc. will remit proceeds, net of the agreed-upon sales commission, to the issuer on or prior to settlement against electronic delivery of the requisite number of shares.

14.7.4 Program Maintenance

The program may last as long as 36 months. As long as it is effective, Coastal Equities, Inc. will require periodic updates (or "bring downs") of its business and legal due diligence including legal opinions, negative assurance letters, and comfort letters. The frequency of bring-downs will be determined by the designated supervisor and will generally be quarterly, but no less frequent than annually. Material events (a change to the issuer's status including acquisitions or mergers; significant changes in business strategy or financial condition; *etc.*) will trigger an immediate bring-down to re-evaluate the program.

14.7.5 Stabilizing Activities

[SEC Regulation M Rule 104(e)]

Stabilizing is prohibited in an at-the-market offering.

14.8 Structured Finance Product Rating Requests

[SEC Securities Exchange Act of 1934 Rule 17g-5]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests for rating of a structured finance product
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Request rating from an NRSRO • Establish a password-protected web site (accessible to other NRSROs) that includes the information provided to the NRSRO from which a rating is requested
Record	<ul style="list-style-type: none"> • Record of rating request and information provided to NRSRO • Records of password-protected web site and information posted

The Rules for Nationally Recognized Statistical Rating Organizations (NRSROs) impose requirements on broker-dealers (and other entities under the Rule) that seek to obtain a rating for a "structured finance product."

Structured finance product refers broadly to any security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction. This includes (but is not limited to) asset-backed securities such as residential mortgage-backed securities and other types of structured debt instruments

such as collateralized debt obligations (CDOs), including synthetic and hybrid CDOs, or collateralized loan obligations (CLOs).

When a rating is requested for a structured finance product, Coastal Equities, Inc. will establish and maintain a password-protected web site containing the information provided to the NRSRO rating the product.

14.9 Crowdfunding

[Securities Act Section 4(a)(6); JOBS Act Regulation Crowdfunding; FINRA By-Laws Section 15; FINRA Funding Portal Rules; FINRA Rule 4518; FINRA funding portal web site: <http://www.finra.org/industry/funding-portals>; SEC Compliance & Disclosure Interpretations: <https://www.sec.gov/divisions/corpfin/guidance/reg-crowdfunding-interps.htm>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests to participate in crowdfunding
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Qualify Coastal Equities, Inc. as a funding portal through FINRA • Review the potential crowdfunding issue including: <ul style="list-style-type: none"> ○ Conduct due diligence on the issuer including confirming the issuer's compliance with crowdfunding rule requirements • Confirm investors meet rule limitations • Document the deal and investor participation
Record	<ul style="list-style-type: none"> • Funding portal registration records • Deal file including due diligence on the issuer and the issue, records of investors

This section explains the requirements if Coastal Equities, Inc. engages in crowdfunding. "Crowdfunding" generally refers to the use of the internet by small businesses to raise capital through limited investments from a large number of investors.

14.9.1 Introduction

Crowdfunding is an exemption to securities laws requiring registration of an issue. Following is a summary of key features of crowdfunding:

- Offer or sale of securities by an issuer through crowdfunding includes all entities controlled by or under common control of the issuer.
- The aggregate amount sold during the 12-month period preceding the date of the transaction cannot exceed \$1 million.
- The amount sold to any investor cannot exceed:
 - The greater of \$2,000 or 5% of the annual income or net worth of the investor if either the annual income or net worth of the investor is less than \$100,000; and
 - 10% of the annual income or net worth of the investor cannot exceed a maximum aggregate amount or net worth of the investor is equal to or more than \$100,000.
- The transaction must be conducted through a broker or funding portal.
- The issuer must comply with crowdfunding requirements under '33 Act section 4A(b).

14.9.2 Funding Portal Registration

Coastal Equities, Inc. is obligated to notify FINRA if it will act as an intermediary for crowdfunding transactions:

- Prior to the first transaction involving the offer or sale of securities in reliance of the crowdfunding exemption; or
- Within 30 days of directly or indirectly controlling, or being controlled by or under common control with a funding portal.

In addition, Coastal Equities, Inc. may be required to apply for approval of a material change in business operations by filing a continuing membership application (NASD Rule 1017).

14.9.3 Offers to Investors

RRs are responsible for making suitability determinations including confirming the investor qualifies based on limitations on crowdfunding issues.

14.10 Regulation A Offerings

[SEC Regulation A; FINRA Regulatory Notice 15-32]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Information obtained regarding issuer from the issuer or other sources
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Determine issue meets Regulation A requirements and integration issues• Evaluate issuer information and determine Coastal Equities, Inc.'s participation• File offering statement electronically
Record	<ul style="list-style-type: none">• Regulation A and integration issue determinations and issuer information are retained in the deal file• SEC filings

14.10.1 Introduction

This type of offering is available to domestic or Canadian issuers not subject to '34 Act reporting requirement or disqualification under "bad boy" provisions of Rule 262. Not available to investment companies, blank check companies, or issuers of oil, gas or mineral rights. The offering is limited to \$5,000,000 within prior 12 months, but not more than \$1,500,000 by selling security holders.

Regulation A is an amendment to the Securities Act of 1933 and provides for reduced requirements for smaller issuers in limited public offerings of issues up to \$1.5 million. For a Regulation A offering, a limited registration statement is filed with the SEC. In addition, there are further exemptions for small issuers (known as Regulation A+ adopted under the JOBS Act) outlined in the section *Exemptions For Small Issuers* that follows. Key considerations for the syndicate supervisor include:

- whether the issuer is disqualified from distributions under Regulation A
- dollar limitations of the offering
- offers cannot be made prior to the filing of the registration statement and sales may not be effected until the offering statement is qualified

14.10.2 Dollar Limitation of Offering

The syndicate supervisor is responsible for ensuring the issue is not oversold relative to the dollar amount disclosed in the offering document compared to the limitations provided in the rules. The supervisor should consider any "integration" of similar offerings by the same issuer for substantially identical purposes for determining whether the issuer meets the dollar limitation under the exemption within a 12-month period of time. The supervisor's review for integration may include one of the following or another procedure determined adequate by the supervisor:

- Reviewing the issuer's financial statements for the past 12 months and/or contact directly with the issuer
- Obtaining a representation letter from the issuer that states that no other offerings will be distributed in a succeeding 6-month period that would cause the exemption to be lost

The supervisor will retain a written record of this review in the offering's underwriting file.

14.10.3 Initiation of Offers and Sales

The syndicate supervisor is responsible for notifying Firm personnel when a Regulation A offering is available for offering and when the registration statement is qualified to permit sales. A written record of these notices will be retained in a file for the offering.

14.10.4 Exemptions for Small Issuers

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Small offerings
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Determine eligibility for exemption • Conduct due diligence into red flags such as insiders of the issuer with regulatory histories, conflicts of interest among parties, non-compliance with escrow requirements • Confirm issuer is in compliance with requirements • File offering statement electronically; where applicable, submit a draft offering statement to the SEC for non-public review (no less than 21 calendar days before qualification of the offering statement)
Record	<ul style="list-style-type: none"> • Deal file include review for exemption and records of compliance with requirements • SEC filings • Records of solicitation of interest and filing of solicitation materials

There are two tiers of offerings for small issuers that enable them to offer and sell up to \$50 million of securities in a 12-month period. Both tiers are subject to basic requirements with additional requirements for Tier 2 offerings.

- Tier 1 is for offerings of up to \$20 million in a rolling 12-month period with no more than \$6 million in offers by selling security holders that are affiliates of the issuer. These offerings are subject to federal and state registration and qualification requirements.
- Tier 2 is for offerings of securities of up to \$50 million in a rolling 12-month period with no more than \$15 million in offers by selling security holders that are affiliates of the issuer. These offerings are not subject to state requirements but are subject to federal registration and qualification requirements.
- Limits on secondary sales by affiliates limit sales by all selling security holders to no more than 30% of a particular offerings initial Regulation A offering and subsequent offerings for the first 12 months following the initial offering.
- For offerings up to \$20 million, the issuer may choose Tier 1 or Tier 2 requirements.
- Both tiers permit issuers to submit draft offering statements for non-public review by SEC staff before filing, permit the continued use of solicitation materials after filing the offering statement, require the electronic filing of offering materials and otherwise align Regulation A with current practice for registered offerings.
- Tier 2 offerings also require:
 - Annual audited financial statements
 - Annual, semi-annual and current event reports
 - Limitation on the amount of securities non-accredited investors can purchase to no more than 10% of the greater of the investor's annual income or net worth
 - A transfer agent registered with the SEC
- The exemption is limited to companies organized in and with their principal place of business in the U.S. or Canada and is not available to certain companies outlined in the Rule.

14.10.4.1 Solicitation of Interest

Regulation A+ allows eligible issuers and intermediaries to conduct a solicitation of interest in an offering (testing the waters), including solicitation of non-accredited investors, both before or after the filing of the offering statement. Solicitation materials must be filed with the SEC as exhibits to the offering statement.

14.11 Best Efforts Underwritings

[Exchange Act Rule 10b-9 and 15c2-4; FINRA Regulatory Notice 16-08; FINRA Notice to Members 84-7]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Information obtained regarding issuer from the issuer or other sources
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Evaluate issuer information and determine Coastal Equities, Inc.'s participation including: <ul style="list-style-type: none"> ○ Reasonable investigation of the security and the issuer's representations ○ Review of the terms of the contingency, including any agreement and disclosure by the issuer regarding the contingency

	<ul style="list-style-type: none"> ○ Follow up any red flags such as inconsistencies between the escrow agreement and the offering document ● Establish a "separate account" or escrow account ● Confirm purchasers are <i>bona fide</i> purchasers where necessary ● Identify insiders, firm or employee account purchasers and obtain affirmation regarding holding period ● Require subscribers to reconfirm their investments if the issuer extends the offering period ● Return subscriber funds if the issuer changes the contingency by reducing the offering minimum ● Close escrow account and, if contingency met, immediately forward purchaser funds to issuer or, if contingency is not met, immediately return funds to potential purchasers
Record	<ul style="list-style-type: none"> ● Escrow account, issuer information and purchaser information are retained in the deal file

14.11.1 Introduction

Best efforts underwritings may take different forms including "all or none," "minimum-maximum," or other offerings contingent on the sale of a certain amount of the issuer's securities. Two primary concerns are that customer funds be transmitted to the issuer or to an escrow account and that only *bona-fide* purchasers are included in order to meet a stated minimum number of shares or units. Where the minimum is not sold within the deadline specified by the prospectus, all customer funds must be refunded.

Sales will be made only to *bona-fide* purchasers to meet any minimum amount of the securities to be sold.

14.11.2 Handling Investor Funds

Coastal Equities, Inc. will promptly:

- Deposit funds into a "separate bank account" for which Coastal Equities, Inc. is the account holder and is designated as agent or trustee for the investors (only if Coastal Equities, Inc. maintains at least \$250,000 in net capital and is allowed to carry customer accounts); or
- Establish an independent bank escrow account.

Funds will be released to the issuer only after the contingency is satisfied.

14.11.3 Customer Funds - Escrow Account

[Exchange Act Rule 15c2-4]

The designated supervisor is responsible for establishing procedures for the protection of customer funds including the establishment of an escrow account where required.

- Establish an escrow account and execute Coastal Equities, Inc.'s standard escrow agreement with a bank that is not affiliated with Coastal Equities, Inc.. The escrow account may not be controlled by the issuer.
- Maintain copies of bank statements for the escrow account and review the statements when received, to ensure funds are not withdrawn prior to the date the contingency is met.

- Ensure customer funds are promptly deposited to the escrow account.
- Maintain records of all potential purchasers including the quantity to be purchased, when funds are received, and when funds are forwarded to the issuer or escrow account.
- Ensure checks are forwarded to the issuer (where an escrow account is not used) or to an escrow account by noon of the business day following receipt.
- Authorize release of funds to the issuer from an escrow account after the contingency is met and after a review of purchasers, as discussed in the next section, has been conducted.
- If the contingency is not met, promptly refund funds to potential purchasers.
- If the issuer extends the offering period, require investors to reaffirm their investments.
- If the issuer reduces the offering minimum, return funds to investors.

14.11.4 Purchasers

The syndicate supervisor is responsible for establishing procedures regarding purchasers of securities issued through a best efforts underwriting including the following:

- Where the offering is contingent upon the sale of a certain quantity of the issue, confirm that all purchasers are *bona-fide* purchasers. Non-bona fide sales generally include sales of undisclosed purchases by the issuer or broker-dealer, their affiliates or associated persons, or any entities through nominee accounts that are designed to create the appearance of a successful completion of an offering.
- Identify purchases by issuer insiders, Coastal Equities, Inc.'s proprietary account, or employees of Coastal Equities, Inc. and, for those identified, obtain a written affirmation that the purchaser intends to hold the security as an investment or, in conjunction with the issuer, determine restrictions on immediate sale by such accounts.
- Record the review of purchasers in the deal file.

14.12 Asset-Backed Securities (ABS)

[SEC Regulation AB; Dodd-Frank Act Section 621, 941, 942, 943 and 945; SEC release: <http://www.sec.gov/spotlight/dodd-frank/assetbackedsecurities.shtml>]

Asset-backed securities (ABS) are created by buying and bundling loans and creating securities backed by those assets which are then sold to investors. Bundles of loans are often divided into different levels or tranches of risks and returns. Payments on the loans are made first to the holders of lower-risk, lower-interest securities and then to holders of higher-risk securities.

ABS public offerings are often done through shelf offerings and are also sold as private placements exempt from registration and sold to QIBs. There are specific registration, disclosure, and reporting requirements for publicly issued asset-backed securities (ABS) under SEC rules and sections of the Dodd Frank Act, some of which are still in the process of rulemaking. This section summarizes some of the key provisions of Regulation AB which should be consulted for specific requirements.

- An underwriter, placement agent, initial purchaser, sponsor, or any affiliate or subsidiary of any such entity is prohibited from engaging in any transaction that involves or results in a material conflict of interest to any investor in a transaction arising out of such activity for a period of one year after the date of the first closing of the sale of the ABS.
- The securitizer is obligated to retain an economic interest in a material portion of the credit risk. This requirement is pending rulemaking. [Section 941 of Dodd Frank]
- There are specific disclosure and reporting requirements. [Section 942 of Dodd Frank]
- The issuer is required to perform a review of the assets underlying the ABS and disclose the nature of the review. This requirement is pending rulemaking. [Section 945 of Dodd Frank]

14.13 Prohibited Activities

14.13.1 Misrepresentation of Registration with Regulators

[SEC Securities Exchange Act of 1934 Rule 15c1-3]

Coastal Equities, Inc. and its RRs will not misrepresent its affiliation with any regulatory body including an implication that regulatory registration indicates a regulator has passed upon or approved the financial standing, business, or conduct of Coastal Equities, Inc. or the merits of any security or transaction it performs.

Coastal Equities, Inc. and its employees may not:

- make material misstatements or omissions in the registration statement.
- fail to comply with applicable registration requirements.
- fail to provide a final prospectus when required.
- engage in fraudulent transactions.

14.13.2 Anti-Competitive Activities

The following are prohibited anti-competitive activities:

- The exchange of current price information among competitors to influence another firm's pricing of services
- Directing, requesting, or attempting to influence another member to maintain or adjust a price
- Engaging, directly or indirectly, in any conduct that threatens, harasses, coerces, intimidates, or otherwise attempts improperly to influence another firm or employee of another firm

14.13.3 Tying

[FINRA Notice to Members 02-64]

IPOs may not be sold to customers where:

- the purchase is tied to a promise from the customer to buy additional shares once trading begins in the new issue.
- the purchase of a highly desirable IPO is tied to the customer's promise to buy IPOs with less market interest.

14.13.4 Laddering

"Laddering" is another prohibited tying arrangement where an underwriter requires IPO investors to submit orders to buy additional shares of the same stock at higher prices after trading begins.

14.13.5 After-Market Sales

Other prohibited after-market activities include:

- attempts to keep investors from selling IPOs in the aftermarket
- soliciting after-market orders during an IPO
- imposing penalties on retail brokers in connection with immediate "flipping" by retail IPO investors but not by other categories of IPO participants, such as institutions
- requiring customers to sell back IPO shares to Coastal Equities, Inc.

14.13.6 Misrepresenting Pricing

[SEC Securities Exchange Act of 1934 Rule 15c1-8]

When participating in a primary or secondary distribution of a security which is not admitted to trading on a national securities exchange, Coastal Equities, Inc. or any employee cannot make a representation that the security is being offered to a customer "at the market" or at a price related to the market unless Coastal Equities, Inc. is aware of a *bona fide* market for the security which it or any affiliate does not control.

15 INVESTMENT BANKING

15.1 Introduction

These policies and procedures outline requirements for Coastal Equities, Inc.'s Investment Banking ("IB") activities. Questions regarding the policies and procedures outlined in this chapter should be directed to Compliance.

15.2 Information Barrier and Confidentiality Issues

15.2.1 Information Barrier Procedures

In order to control the flow of confidential and material, non-public information, Coastal Equities, Inc. has created Information Barriers to separate the public side employees (*e.g.*, sales, trading and research) from private side employees (*e.g.*, advisory and investment banking).

For more detailed information regarding Coastal Equities, Inc.'s Insider Trading and Information Barriers policies, and the Watch and Restricted Lists policies, refer to the chapter *INSIDER TRADING*.

15.2.2 Origination Meeting Process and Information Sharing

This meeting provides a venue for IB and origination personnel to meet and discuss significant firm opportunities. To that end, open dialogue and communication is crucial, however Compliance guidelines must accompany this open forum in order to address: potential conflict situations; the flow of material, non-public information ("MNPI"); and compliance with Coastal Equities, Inc.'s information barrier policy of sharing information only with those that have a *"need to know."* Separate requirements apply to dealings between IB and Research, outlined in a later section of this Policy titled *"Interaction between Research and Investment Banking."* The following compliance guidelines address information sharing issues other than interaction with Research personnel.

1. As conversations in this meeting will cross industry and product lines, participants will be privy to information that they previously have not been privy to. Senior Origination participants will be held to the same higher standard as Senior Management and above-the-barrier employees.

Participants should always use good judgment when discussing potential transactions or situations and should limit the content and context of the information they present. In the event that MNPI is shared during the meeting, the information should be limited only to essential information (*i.e.*, *"need to know"*).

2. Unlike other forums, project code names are not required. However, if information does not need to be shared or if assistance can be gained by having conversations with colleagues in a separate, smaller venue, this route should be taken.

3. Identifying and discussing common relationships and communication strategies are permissible.

4. Participants should not hand out any materials at the meeting, except for senior management and board of director lists. To the extent that contact lists are handed out or emails are distributed, the documents should:

- have a cover sheet (as applicable),
- be clearly marked Confidential,

- use a project code name in the header or reference field (for emails), and
- be collected and shredded at the end of the meeting by the person handing the material out.

5. At a minimum the use of project code names and limited details should be used as soon as possible, *e.g.*, after the idea comes together and the deal team proceeds with the pitch. Generally, the group should not be updated until the transaction is announced or dead.

6. All MNPI must remain confidential outside the meeting and should be used only for the business purpose it was communicated. Sharing information outside the group should be limited to those with a "*need to know.*"

7. When communicating MNPI outside of the group meeting, individuals should utilize project code names in written and in oral communications when appropriate, *i.e.*, public places, meetings outside the group, e-mail, and broadly disseminated correspondence.

8. Participants should only give their proxy information to other Senior Origination participants in the event they are unable to attend. Participants may not ask members of their industry or origination group to attend as their proxy. Given the above-the-barrier nature of the conversation, it is inappropriate for anyone other than the designated participants to attend the meeting.

15.3 Restricted and Watch Lists

Compliance maintains and monitors a "Restricted List" and a "Watch List" as described in *INSIDER TRADING*. Investment Bankers have an obligation to notify Compliance of pending deals as outlined in the policy.

15.3.1 Watch List

The Watch List is a confidential list of companies and issuers of securities maintained by Compliance for the purpose of monitoring the possession of confidential or material, non-public information obtained by Coastal Equities, Inc. during its normal course of business, usually when it has been retained to advise a customer regarding a transaction, to underwrite an offering, or to provide debt financing. The contents of the Watch List are highly confidential and access to the Watch List is limited to Compliance and persons granted access by Compliance. No person may discuss the contents of the Watch List or any of its information with anyone outside of the immediate deal team and senior management in the respective business unit, where appropriate, without permission of Compliance.

The Watch List is used to review the sales, trading and research activities of Coastal Equities, Inc. and the personal trading activities of employees without restricting such activities. The Watch List helps to ensure the integrity of the Information Barrier and is used to support and monitor compliance of these policies and procedures. For these reasons, Compliance is authorized to break trades in proprietary or employee accounts, restrict trading and research, and prohibit other activities relating to securities or issuers included on the Watch List.

15.3.1.1 Additions to the Watch List

Notification

The Lead Banker is responsible for PROMPTLY informing Compliance when Coastal Equities, Inc. is reasonably likely to be engaged by a customer or they obtain information that is substantially material to the customer and/or Coastal Equities, Inc.. Examples include:

- M&A advisory or fairness opinion

- Underwriting or placement agent activities
- Acquisition finance involving public companies
- Conflict clearance when both the acquirer and target are customers
- Auctions
- Hostile situations

Investment Banking Commitment Committee

The Lead Banker is responsible for notifying Compliance prior to going to the Investment Banking Commitment Committee when Coastal Equities, Inc. is reasonably likely to be buy-side or sell-side advisor for a private or a public company, financial or general advisor, advisor in a going-private transaction, to explore strategic alternatives, to place private equity, or to provide a fairness opinion.

Compliance will place the name of the issuer(s) involved on the Watch List and conduct a firm-wide review in an attempt to identify, manage and resolve potential conflicts of interest arising from Coastal Equities, Inc.'s participation.

Deal Teams

At the time the Lead Banker reports a project for Watch List addition, the Banker should also communicate to Compliance the proposed deal team and a project code name to control the flow of information. The deal team should include employees representing a cross-section of business units and product expertise relevant to the transaction. Those "above the barrier" are not added to a deal team. Compliance will assist with resolving situations where limited resources are available to adequately staff multiple, competing deal teams.

The deal team is required to use the project code name in all communications relating to the transaction to ensure security.

15.3.1.2 Updates to The Watch List

The Lead Banker is responsible for informing Compliance of all material events regarding the transaction. Examples include:

- the approved additions and deletions of employees to and from deal teams
- timing and launching of transactions
- notification prior to a public announcement for an M&A transaction or rendering a fairness opinion
- notification after a shareholder vote is complete or a tender offer expires

15.3.1.3 Deletions from the Watch List

The Lead Banker who added the security or issuer to the Watch List is responsible for PROMPTLY informing Compliance when a security or issuer should be removed from the Watch List. Generally, the removal of a security or issuer from the Watch List is warranted when the information possessed by Coastal Equities, Inc. is no longer deemed confidential, material or non-public in nature or when it has aged to the point where it is no longer relevant. Removal of a security or issuer from the Watch List is also warranted when the project has been abandoned or when the probability of a project occurring is no longer great enough to continue to monitor the sales, trading and research activities of Coastal Equities, Inc. and the activities of employee accounts.

15.3.2 Restricted List

In order to comply with securities laws, to avoid the appearance of impropriety, and to supplement the Information Barrier, Coastal Equities, Inc. maintains a Restricted List. The Restricted List is an internal-use-only list of companies and issuers of securities in which certain restrictions apply in handling customer orders, trading for proprietary accounts, trading for employee and employee-related accounts, and other activities.

The Restricted List is generated, maintained and distributed by Compliance for the exclusive use of Coastal Equities, Inc., and its contents are for internal use only. Distribution or sharing of the list outside Coastal Equities, Inc. is prohibited. It is communicated through Coastal Equities, Inc.'s intranet and is located on the Compliance website. The Restricted List identifies the type of restriction applicable to the security. Restrictions may include legal restrictions (Reg M, 14e-5, etc.) and policy restrictions (no proprietary trades until closing of an M&A transaction in which Coastal Equities, Inc. is serving as a financial advisor) and are assessed and applied by Compliance as required.

15.3.2.1 Prohibitions and Effects of the Restricted List

The Restricted List is most often used in the following situations to restrict the appropriate sales, trading and research activities in the applicable securities of an IB customer. Compliance will determine when one of the following conditions requires addition of a security to the Restricted List.

- When Coastal Equities, Inc. has been retained as a financial advisor in a material public transaction
- When Coastal Equities, Inc. is a participant in a publicly announced offering of securities
- When Coastal Equities, Inc., in some cases, is a provider of debt financing
- In situations where a research analyst, salesperson, or trader is brought over-the-wall
- Prior to the initiation of Equity research coverage with a rating other than hold/market perform
- Prior to dissemination of an equity research report with a material change
- When appropriate, securities of an issuer that is on the opposite side of a material, public transaction with Coastal Equities, Inc.'s customer

The Restricted List generally will not indicate why a particular security or issuer is restricted but will identify what activities are restricted and, conversely, permitted.

15.4 Review of Investment Banking Business

[FINRA Rule 3110(b)(2)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor (IB)
Resources	<ul style="list-style-type: none"> • Proposed and pending IB deals
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review proposed deals working with the Commitment Committee and consulting with outside counsel and others as needed • Oversee assignment of passwords and compliance with confidentiality requirements
Record	<ul style="list-style-type: none"> • Deal file including review of deals, assignment of passwords and imposition of other confidentiality requirements

The supervisor of Investment Banking (IB) is responsible for oversight of IB transactions and compliance with Firm policies and securities rules, laws, and regulations. Compliance reviews IB and other transactions for compliance with insider trading and related requirements (see the chapter *SUPERVISORY SYSTEM, PROCEDURES, AND CONTROLS* and the sections *Review Of Transactions*) and *Internal Investigations*. Individual transactions by investment bankers are subject to requirements explained in the next section.

15.5 Investment Banker Personal Investments

[FINRA Rule 3110(b)(2) and 3110(d)(3)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Compliance
Resources	<ul style="list-style-type: none"> • Requests from Bankers to enter personal transactions
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Check for potential conflicts • Approve or disapprove the request • Compliance: review and monitoring of transactions, initiate an internal investigation if necessary (see section <i>Internal Investigations</i> in the chapter <i>SUPERVISORY SYSTEM, PROCEDURES, AND CONTROLS</i>)
Record	<ul style="list-style-type: none"> • Records of transaction requests/approval or disapproval • Compliance records of reviews, internal investigations

Because investment bankers (Bankers) have access to MNPI, they are subject to specific requirements affecting their personal investments to avoid conflicts of interest and rule violations. Failure to comply with this Policy may result in disciplinary actions up to and including termination of employment.

Bankers are prohibited from trading in securities:

- that they cover.
- for one (1) reporting period after a publicly-announced deal is finalized (but under no circumstances for any period where there is knowledge of material, non-public information).
- in industries where the Banker is aligned.
- where the Banker has knowledge of material, non-public information (this includes a prohibition against passing on such information to others).
- when the Banker is part of a deal team (includes others supporting the deal team and having knowledge of the deal). Includes knowledge of current or proposed deals.
- that are securities of an issuer that is a customer of the Banker.
- when aware of a proposed or pending follow-on offering.
- if currently involved in an underwriting or distribution of securities for the issuer.
- if previously involved in an underwriting or distribution of securities for the issuer, less than one reporting period has elapsed since the close of the underwriting.

- if aware of an ongoing relationship with the issuer/customer of the group you are working in.
- if aware of any current or potential transactions for the issuer as a result of access to financial or other systems, write rights (the ability to view or change information) to shared folders or applications or work on specific projects.
- if aware of any pitches or other communications planned with the issuer.

Pre-clearance of Banker Transactions

Bankers are required to pre-clear all personal transactions with their supervisor or his/her designee.

15.6 Licensing and Registration

[FINRA Rule 1200; NASD Regulatory Notice 09-41]

Bankers are required to pass the SIE, Series 79 (Investment Banking Representative), and Series 63 (Uniform State Law) examinations. Registered personnel should be licensed in each state or jurisdiction (via Series 63) in which they will potentially conduct or solicit securities or investment banking business, unless a specific exemption applies as determined by Compliance.

15.7 Gifts and Entertainment

[FINRA Rule 2310(c)(2)(A), 2320(g)(4)(A), 2341(l)(5) and 3220]

All employees are subject to Coastal Equities, Inc.'s policies on gifts and entertainment (*GENERAL EMPLOYEE POLICIES* chapter). Additional requirements that apply to Bankers are included in this section.

Deal Closing Events

Closing dinners or similar events recognizing a successful transaction are permissible, but are considered "entertainment" for the purpose of the applicable rules and are subject to Coastal Equities, Inc.'s entertainment policy.

Customer Restrictions On Gifts, Gratuities, And Entertainment

Many institutions adopt policies and procedures restricting the receipt of gifts, gratuities and entertaining. Firm personnel should conduct business development activities consistent with such policies and procedures to the extent such policies and procedures are effectively communicated to Coastal Equities, Inc..

Governmental agencies, municipalities, political subdivisions, federally insured deposit institutions, public utilities and bank holding companies typically have adopted policies and procedures or may be subject to state or federal laws and regulations that govern or limit receipt of gifts, gratuities and entertaining. Employees who cover any such customers or sectors should become familiar with the limitations imposed on the receipt of gifts, gratuities or entertainment by the customers themselves or laws applicable to the customer.

Gifts, Gratuities, And Entertainment Provided By Related People

It is not permissible to use spouses or other family members to evade the limitations of the rules. Any gift giving or entertaining of firm customers by a spouse or other family members of an employee will be subject to the rules' limitations except to the extent (i) it solely relates to business development by the spouse's or other family member's employer, or (ii) it is permissible personal gift giving or entertainment to family members and personal friends as provided above and such gift or entertainment is not directly or indirectly paid for by Coastal Equities, Inc..

15.8 Participation in Compliance Meetings, Continuing Education, And Internal Audits/Reviews

[FINRA Rule 1250 and 3110(a)(7)]

Bankers are required to attend an annual compliance meeting, as required by FINRA, at which attendance is mandatory. The meeting provides a forum for education and guidance concerning legal or regulatory requirements and Coastal Equities, Inc.'s internal policies and procedures. Bankers are also subject to continuing education requirements. Registered personnel must complete Regulatory Element continuing education (required every three years) administered by regulators and Firm Element continuing education (required annually) administered by Coastal Equities, Inc.. Compliance will notify employees when they are subject to the requirements; failure to complete the requirements within specified deadlines will result in the employee ceasing business activities until continuing education is satisfied.

IB is subject to reviews to detect and deter violations of applicable legal requirements and internal policies and procedures. Reviews typically include an assessment of the supervisory structure and internal policies and procedures. Bankers and supervisors are expected to cooperate and provide requested materials promptly to auditors.

15.9 Inquiries and Investigations

Coastal Equities, Inc. is subject to supervisory oversight by multiple regulators. When a representative of any of these regulatory bodies contacts or requests information from an employee in IB, the employee must immediately contact Compliance. IB personnel should only communicate with regulators after consultation with Compliance and/or Legal.

15.10 Anti-Money Laundering (AML)

[FINRA Rule 3310]

Money laundering is a serious offense. SROs and federal securities and banking regulators have adopted stringent requirements to prevent and identify money laundering. Failure to comply with AML rules and regulations can result in significant charges and disciplinary action against Coastal Equities, Inc. and/or its employees including charges of aiding and abetting money laundering and/or direct violation of AML laws. Any irregular or suspicious activity needs to be communicated to Compliance in a timely manner. Customer actions that should be viewed with caution include (but are not necessarily limited to) the following:

- using accounts to clear large sums of money without an apparent business purpose,
- conducting transactions with no discernible purpose,
- unnecessary use of an intermediary,
- regular payment of large sums, including wire transfers, that cannot be explained in the context of the customer's normal business,
- customers whose identity proves unusually difficult or expensive to verify,
- use of an address that is not the customer's permanent business address (for example, utilization of a home address for business correspondence),
- customers who purposefully avoid needed contact with firm staff.

Each IB employee is responsible for being familiar with and complying with Coastal Equities, Inc.'s Anti-Money Laundering policies (see the chapter *ANTI-MONEY LAUNDERING (AML) PROGRAM*).

15.10.1 Overview of The Customer Identification Program of The USA PATRIOT Act

Coastal Equities, Inc. has a Customer Identification Program (CIP) as required by AML rules and regulations. Coastal Equities, Inc. is required to obtain certain basic information on any **new customer** (which includes a corporation, LLC, partnership, SPV, *etc.*) who opens an account or otherwise establishes a formal business relationship with Coastal Equities, Inc.. Financial institutions including broker-dealers, industry-wide, are required to implement the following steps as part of their AML program:

1. Obtain and verify the identification of any new customer,
2. Determine whether the person appears on any lists of known or suspected terrorists or terrorist organizations provided to us by any government agency, and
3. Provide notice to the customers that information is being requested about their identity and that the information will be used for verification purposes.

To the extent possible, the verification process has been incorporated into those systems used to open accounts/initiate business relationships, and specific procedures have been developed.

It is the responsibility of the lead or senior banker on a deal team commencing a new business relationship to ensure Coastal Equities, Inc.'s compliance with the CIP. The following describes each component of the rule to be complied with as well as a discussion of the mechanism that will accomplish compliance and the steps that may be required of IB personnel.

Step 1: Obtain and verify the identification of any new customer.

Certain information is required in order to verify the identity of any new customer when entering into a business transaction, relationship, or engagement. Bankers should obtain the following information when a deal moves to "Pitched" status:

- Taxpayer ID number, or alternative government issued ID number for non-U.S. entities
- Full legal name
- Physical address (no P.O. Box) of principal place of business, including city, state, zip, country

When IB introduces or is otherwise involved in an engagement with an issuer's transactions originated by Coastal Equities, Inc., information obtained from the issuer will be the source of information for Coastal Equities, Inc.'s verification.

Step 2: Determine whether the person (or related persons to an organization) appears on any lists of known or suspected terrorists or terrorist organizations provided to us by any government agency.

Operations may be contacted to check customers against lists.

IMPORTANT NOTE: If for any reason an account cannot be verified through the CIP or it has a match on a terrorist listing, the account must be closed immediately.

Step 3: Provide notice to the customers that information is being requested about their identity and that the information will be used for verification purposes.

The verbiage below must be provided to any new IB customer.

Important Information About Opening Your New Account And/Or Entering into a Business Relationship with Coastal Equities, Inc.: To help fight the funding of terrorism and money laundering activities, Federal law requires all financial institutions to obtain, verify and record information that identifies each person or corporation who opens an account and/or enters into a business relationship.

It is the responsibility of the Senior Banker executing an engagement letter on behalf of Coastal Equities, Inc. to ensure the required disclosure is incorporated in the engagement letter or other similar engagement documents executed with issuers and borrowers.

15.11 Communications

IB personnel are subject to Coastal Equities, Inc.'s communications policies (see the chapter *COMMUNICATIONS WITH THE PUBLIC*). Only firm-sponsored communications networks and computers may be used for public communications. Coastal Equities, Inc. is required to review and retain electronic communications. Electronic communications of any type should be considered the equivalent of written communications for purposes of creating a record of communications and should not be considered "conversations" or phone calls.

The following are included in the definition of communications with the public.

- Press Releases
- Single and Multiple Tombstone Advertisements
- Underwriting proposals to issuers
- Pitchbooks, marketing materials
- Research reports
- Recommendations List
- Offering sheets, fact sheets, or prospectus summaries
- Seminar texts
- Any material designed to be published in the public media
- Electronic communications such as e-mail and Bloomberg
- Communications via electronic networks such as instant messaging
- Facsimile ("Fax")

Communications that refer to Coastal Equities, Inc. as a legal entity (in contracts, *etc.*), must state the full legal name of Coastal Equities, Inc. and Coastal Equities, Inc.'s capacity in relation to the product or service offered. Any brand name may be used for marketing purposes, but may not be used in place of the legal entity. If a firm affiliate is mentioned, the relationship between Coastal Equities, Inc. and its affiliate must be clear. If an individual is named in a communication containing the names of Coastal Equities, Inc. and an affiliate, the nature of the relationship of the individual with Coastal Equities, Inc. should be clear.

15.11.1 Prohibited Communications Between Bankers and Customers

Except for Emerging Growth Companies ("EGCs") as discussed in a following section, prior to the effective date of a registered offering, communications mentioning the offering are prohibited including press releases, advertisements, and written communications. There should be **no** written communications (including email or fax) between Bankers and customers during the offering period. Private placements, by their nature, may not be announced prior to the transaction via press releases, advertisements and other media with broad distribution.

"Internal Use Only" material should not be disseminated externally and should be marked "Confidential" to prevent copying or forwarding.

15.11.2 Communication with Other Business Units

This section is intended only to provide general guidelines regarding appropriate levels of communication between IB and other firm business units (other than Research which is discussed in the next section). **If there is any question related to whether or not something can be discussed or shared with other business units, contact Compliance.**

In the event that an employee believes that he or she may have inadvertently signaled that a confidential commitment or project is underway, or may have communicated confidential information about a project to a person not entitled to such information, the employee should immediately contact the senior business person on the transaction, who should then contact Compliance to determine what, if any, actions are advisable or necessary as a consequence of these communications.

15.11.3 "Public Side" Employees (Sales and Trading, etc.)

In the ordinary course of business, IB will possess non-public and potentially material information regarding corporations whose securities are traded by the public side of Coastal Equities, Inc., specifically Trading and Sales. It is the responsibility of Bankers to prevent such information from being shared with the public side of Coastal Equities, Inc.. However, there exists a great deal of information received by IB that is public and of interest to employees on the public side of Coastal Equities, Inc.. To facilitate the sharing of such information the following list of items is pre-approved by Compliance for distribution to the public side of Coastal Equities, Inc. and is considered public information:

- Annual Reports, Press Releases, or other company prepared material which is made available to the public;
- Publicly registered documents, 10Ks, 10Qs, and Credit Agreements filed with the SEC;
- Information from publicly available industry media sources; and
- Publicly distributed research published by other institutions.

Written information **not pre-approved** in the above categories must be reviewed by Compliance before being distributed to the public side of Coastal Equities, Inc..

15.11.4 Interactions Between Research Analysts And Investment Bankers

[FINRA Rule 2241]

Communications and interaction between IB and Research are subject to restrictions by regulatory rules. No Research Analyst may be subject to the supervision or control of any member of Coastal Equities, Inc.'s IB groups. IB will have **no** input into company-specific coverage decisions made by the Research Department (*i.e.*, whether or not to initiate or terminate coverage of a particular company).

No Banker may, directly or indirectly, retaliate against or threaten to retaliate against any research analyst employed by Coastal Equities, Inc. or its affiliates as a result of an adverse, negative, or otherwise unfavorable research report or public appearance written or made by the research analyst that may adversely affect Coastal Equities, Inc.'s present or prospective IB relationship with the subject company of a research report.

There are some Emerging Growth Company exceptions regarding investment banker/research analyst interactions which are discussed in a section that follows.

15.11.4.1 Chaperoning

Most permissible communications between IB and Research require "chaperoning." Chaperoning means that any written or electronic communication between the research analyst and the Banker must be made through Compliance or in a transmission copied to Compliance. Oral communications must be made through Compliance acting as intermediary or in the presence of Compliance; provided that, Bankers may engage in un-chaperoned communications with research administrative personnel and research analysts may engage in un-chaperoned communications with IB administrative personnel only to the extent necessary to schedule an oral communication for which chaperoning is required.

15.11.4.2 Joint Due Diligence

Joint due diligence (*i.e.*, confirming the adequacy of disclosure in offering or other disclosure documents for a transaction) by the research analyst in the presence of investment banking department personnel prior to the selection by the issuer of the underwriters for the investment banking services transaction is prohibited.

15.11.4.3 Prohibited Activities

The following are additional prohibited research/investment banking activities.

15.11.4.3.1 No Solicitation of Investment Banking Business

A research analyst **must not** participate in any efforts to solicit investment or corporate banking business. Accordingly, the analyst **must not** participate in any "pitches" for investment or corporate banking business to prospective customers, or have other communications with companies for the purpose of soliciting investment or corporate banking business.

By the same token, IB personnel must not direct or ask a research analyst to engage in any "pitches" or other communications with companies for the purpose of soliciting investment or corporate banking business. This means that Bankers should **not** ask an analyst to visit a customer or business prospect, or join them on a customer visit or phone call. An analyst may, however, visit or speak with a prospective or current customer as the analyst deems appropriate for purposes of conducting due diligence on a transaction.

Pitch materials may include the fact of coverage and the name of the research analyst if it does not imply favorable coverage. Restrictions on pitches do not apply to Emerging Growth Companies with the prior approval of Compliance.

15.11.4.3.2 No Participation in Deal-Related "Road Shows"

Research analysts **must not** participate in "road shows" related to a public offering or other investment banking transaction. To that end, an analyst may **not** review or comment on "dry run" road show presentations or materials prepared in connection with a road show related to a public offering or other investment banking transaction. By the same token, Bankers must not direct an analyst to engage in marketing or selling efforts to investors with respect to any investment banking transaction.

15.11.5 Emerging Growth Companies (EGCs)

[JOBS Act, Title I; SEC JOBS Act Frequently Asked Questions: <http://www.sec.gov/divisions/corpfin/guidance/cfjobsactfaq-title-i-general.htm>]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
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Resources	<ul style="list-style-type: none"> • Potential EGCs
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Contact Compliance to: <ul style="list-style-type: none"> ○ Verify that an IB customer/potential issuer qualifies as an EGC ○ Obtain pre-approval regarding analyst activities relating to an EGC (meetings, etc.) ○ Compliance will notify the designated supervisor, bankers, and analysts that the issuer qualifies as an EGC and advise as to any applicable restrictions on activities/communications or notify that the issuer does not qualify as an EGC • Provide training for investment bankers regarding permitted activities involving EGCs
Record	<ul style="list-style-type: none"> • Compliance record of review of issuer to determine EGC status and notification to IB supervisor, Research supervisor, and applicable bankers and analysts about permissible activities involving research analysts

The Federal JOBS Act creates a category of issuers known as EGCs that have had total annual gross revenues of less than \$1 billion during its most recently completed fiscal year. An issuer remains an EGC until the earliest of:

1. The last day of the fiscal year during which it had total annual gross revenues of at least \$1 billion;
2. The last day of the fiscal year following the fifth anniversary of the issuer's initial public offering;
3. The date on which it has issued more than \$1 billion in non-convertible debt during the previous three-year period; or
4. The date it becomes a "large accelerated filer."

EGCs receive the following treatment under the Act:

- Confidential filing and review of initial public offerings;
- Permitted publication of research reports at the time of a proposed public offering;
- Permitted broker-dealer public appearances following an IPO and after the expiration of a "lock-up" agreement;
- Limited communications between research analysts and potential investors;
- Limited participation by a research analyst in meetings with management and others regarding securities offerings; and
- Permitted oral and written communications (including offers), both before and after the filing of a Securities Act registration statement, with potential investors that are QIBs or accredited investors.

EGCs also have certain disclosure advantages regarding IPO audited financial statements, less financial information to be filed for IPOs, and fewer disclosures under the Act as well as fewer corporate governance requirements than are imposed on non-EGC issuers.

Compliance must be contacted for review of the potential EGC prior to engaging in activities permissible for EGCs but not permissible for other issuers and prior to involvement with research analysts. Compliance

will notify the banker, analyst, and appropriate supervisors whether the issuer meets EGC status and whether any restrictions apply.

15.12 Prohibition Against Offering Favorable Research to Induce Investment Banking Business

[FINRA Rule 2241(b)(2)(K) and 2242.01; FINRA Regulatory Notice 11-41]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor and/or Compliance
Resources	<ul style="list-style-type: none"> • Notification or indication that an issuer has expressed an expectation of favorable coverage
Frequency	<ul style="list-style-type: none"> • As required - take action when favorable research is expected by potential IB customers • Annually (or more frequently) - train IB personnel regarding prohibited promises of favorable research
Action	<ul style="list-style-type: none"> • When becoming aware of an issuer's expectation for favorable research: <ul style="list-style-type: none"> ○ Provide affected IB personnel with information regarding the prohibition ○ Confirm disclaimer language is included in pitch materials and RFPs ○ Confirm repudiation has been documented ○ Establish heightened supervision to review research materials for objectivity
Record	<ul style="list-style-type: none"> • Repudiation to the issuer • Heightened supervision of research on the subject company • Records of disclaimers

Coastal Equities, Inc. may not agree to provide favorable research to an issuer to obtain the issuer's investment banking business. Pitch materials may not include information about Coastal Equities, Inc.'s research in a manner that suggests, directly or indirectly, that Coastal Equities, Inc. may provide favorable research coverage. FINRA has indicated that the publication in a pitch book or related materials of an analyst's industry ranking will imply the potential outcome of future research because of the manner in which such rankings are compiled. Coastal Equities, Inc. is permitted to include in pitch materials the fact of coverage and the name of the research analyst. Pitch materials and responses to requests for proposals (RFPs) will include disclaimer language that Coastal Equities, Inc. is not, and is unable to, make any promises about research coverage. An example of an inducement would be a CEO of an issuer to requiring candidates for the company's next offering to demonstrate their ability and willingness to follow the company and articulate why investors should own their stock.

If an issuer expresses its expectation, directly or implicitly, that the awarding of investment banking business is conditioned on Coastal Equities, Inc. providing favorable research, the following steps must be taken:

- Notify the IB supervisor or Compliance of the issuer's communication;
- Expressly repudiate to the issuer any expectation with respect to the content of research coverage and document the repudiation;

- Heightened supervision will be implemented regarding solicitation activities, including pitch meetings and materials and other communications with the issuer; and
- Increased oversight of the preparation and content of research on the subject company.

15.13 New Issues

[FINRA Rule 5131(b)]

Firms are prohibited from engaging in "spinning" which is a prohibited practice. Following is the policy regarding spinning as it appears in the chapter *CORPORATE SECURITIES UNDERWRITING*. The IB Manager is responsible for ensuring IB personnel do not participate in allocation of new issues or attempt to influence employees responsible for allocations.

FINRA rule prohibits firms from allocating shares to obtain the investment banking business of a customer. Coastal Equities, Inc. and its employees are prohibited from allocating shares of a new issue to any account where an executive officer or director of a public company or a covered non-public company, or a person materially supported by such executive officer or director, has a beneficial interest:

- If the company is currently an investment banking services customer of Coastal Equities, Inc. or the firm has received compensation from the company for investment banking services in the past 12 months;
- If the person responsible for making the allocation decision knows or has reason to know that Coastal Equities, Inc. intends to provide, or expects to be retained by the company for, investment banking services within the next 3 months; or
- On the express or implied condition that such executive officer or director, on behalf of the company, will retain Coastal Equities, Inc. for the performance of future investment banking services.

These prohibitions do not apply to allocations to any account exempt under FINRA Rule 5130(c) listed in the section *Restrictions On Purchase And Sale of IPOs Of Equity Securities - Exemptions* in the chapter *CORPORATE SECURITIES UNDERWRITING* **with the exception** of the de minimis exemption if beneficial interest does not exceed 10%. The spinning exception applies to persons materially supported by them in aggregate do not exceed 25% of such account.

In addition, spinning prohibitions do not apply to allocations of securities that are directed in writing by the issuer, its affiliates, or selling shareholders, so long as Coastal Equities, Inc. has no involvement or influence, directly or indirectly, in the allocation decisions of the issuer, its affiliates, or selling shareholders with respect to such issuer-directed securities. [FINRA 5131.01]

The New Issue Certification includes inquiry whether the potential purchaser is an executive officer or director or person materially supported by them.

15.14 New Product Approval Process

New products must be presented to the New Product Committee for review and approval prior to offering the new product. A new product or activity can be identified as one that:

- Requires a change or new system or procedure because existing systems or procedures cannot process it;
- Necessitates a new pricing or risk measurement methodology;
- Has unique regulatory, legal, reputation or credit risk characteristics.

Marketing, sales and/or trading activities in the new product may not be commenced until the New Product Committee has given its approval. Request for review should be submitted on the New Product Review Form. Refer to the Chapter *New Products*.

15.15 Pitch Materials

[FINRA Regulatory Notice 11-41 and 07-04]

15.15.1 Definition

"Pitch materials" are defined as any written (electronic or hard-copy) communication prepared in whole or in part by origination professionals that is delivered to the "public" (i.e., customers) for the solicitation of business. This includes "short form" and "follow-up" materials prepared by origination professionals that are sent to customers via hard copy and/or email.

15.15.2 Approval of Pitch Materials

Pitch materials require the supervisor's approval **prior to use**.

15.15.3 Other Disclosures and Guidelines

- Sources for all charts, graphs, etc. are cited (i.e., Bloomberg, FactSet, etc.).
- Information is factual and correct to the best of the preparer's ability.
- Presentation is fair and balanced.
- If research or analyst commentary is included in the pitch material, it must be approved by the Equity Research supervisor and **MAY NOT** include firm research. Quotes must be complete and not out of context, and sources must be cited.
- Pitch materials and response to requests for proposals (RFPs) will include disclaimer language that Coastal Equities, Inc. is not, and is unable to, make promises about research coverage.
- Testimonials from customers regarding the quality of Coastal Equities, Inc.'s advisory/execution capabilities must adhere to the following:
 - Inclusion of the following: *"This testimonial may not be representative of the experience of other customers and is not indicative of future performance or success."*
 - If an amount is paid for the testimonial, the fact that it is a paid testimonial must be included.
 - If the testimonial concerns a technical aspect, the person providing the testimonial must have the experience/knowledge necessary to form a valid opinion.
 - **NOTE: This provision does not pertain to case studies listing only the names and contact numbers of customers as references.**
- Offers of Free Service. Reports, analyses or other services offered as "free" must be furnished entirely free and without condition or obligation.

15.15.4 Pitch Materials: Non-Permissible Items

Pitch Materials may **not** include the following:

- Any item not adhering to the guidelines listed above.
- Pitch materials may not include information about Coastal Equities, Inc.'s research in a manner that suggests, directly or indirectly, that Coastal Equities, Inc. may provide favorable research. Also see the section *Prohibition Against Offering Favorable Research To Induce Investment Banking Business* in this chapter.

- Claims and Opinions - Specifically defined as: "Promises of specific results, exaggerated or unwarranted claims, misleading statements, unwarranted superlatives, opinions for which there is no reasonable basis or forecasts of future events that are unwarranted or that are not clearly labeled as forecasts."
- Hedge Clauses - Specifically defined as: "Cautionary statements or caveats that are misleading or inconsistent with the content of the material."
- "Internal Use Only" Material - not permitted in full or in part.

Research analysts may not participate in pitches, assist with the preparation of specific pitch materials, or review pitch materials prior to use.

Any questions regarding whether pitch material content can be considered as "approved" or as "non-permissible" should be brought to the attention of the appropriate supervisor and Compliance, **prior to the pitch material's use.**

15.15.5 Document Retention

Pitch materials must be retained for three years. Retained materials must include who prepared the material; other business units/individuals who contributed to the materials; and who approved the material, and when.

15.16 Commitment Committee

Responsibility	<ul style="list-style-type: none"> • Commitment Committee
Resources	<ul style="list-style-type: none"> • Requests for review of potential commitments
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review proposed commitments • Approve or disapprove or request more information • Notify the Banker of the Committee's decision
Record	<ul style="list-style-type: none"> • Information submitted for review • Committee action

The Commitment Committee's primary responsibility is to review and approve underwritings of all private or public offerings of taxable and tax-exempt securities in which Coastal Equities, Inc. is the lead or co-manager. The Committee is comprised of __ members representing the following areas of Coastal Equities, Inc.:

- _____

The requirements for presenting proposed issues to the Commitment Committee apply to both negotiated and competitive underwritings.

The Lead Banker must submit each advisory assignment, fixed income, equity, and equity-linked products deals to be undertaken by the Firm to the Commitment Committee for approval prior to entering into any engagement. The Committee proposal must include:

- Summary of issuer's background and business

- Summary of issuer's historical financials
- Summary of the structure of the issue
- Key credit strengths and weaknesses
- Size and name of issue
- Name of the investment banker submitting the deal
- Any conditions attached to the issue

The Committee will notify the Banker of its action, whether approved, disapproved, or a request for more information.

15.17 Commitments

When an investment banking customer has agreed to have Coastal Equities, Inc. represent it in an investment banking transaction, a signed agreement detailing the terms and conditions of the commitment will be obtained and signed by all parties. Copies will be provided to the customer and retained by Coastal Equities, Inc. in the deal file.

15.17.1 Representing Two Sides of A Banking Transaction

In general, Coastal Equities, Inc. will not represent both sides of an investment banking transaction. In those cases where this may be appropriate, the following is required:

1. The proposed dual engagements must be submitted to and approved by the Commitment Committee.
2. The proposed dual engagements must be reviewed and approved by in-house or outside counsel as well as the designated supervisor prior to engagement.
3. Each side must be represented by separate investment banking teams separated physically and separated in their electronic and other communications. Each team will be notified in writing and acknowledge in writing that their activities are separate from the other team, and their activities are confidential and may not be communicated to the other team.
4. The written agreement with the customer must include clear disclosure that Coastal Equities, Inc. is representing both sides of the transaction, and the customer must separately acknowledge in writing their understanding and acceptance of this arrangement.

The designated supervisor is responsible for ensuring that these requirements are satisfied and for retaining records documenting them.

15.18 Fairness Opinions

[FINRA Rule 5150]

Responsibility	<ul style="list-style-type: none"> • IB supervisor • Review committee
Resources	<ul style="list-style-type: none"> • Fairness opinion • Fairness Opinion Review/Approval forms
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Manager:

	<ul style="list-style-type: none"> ○ Review and approve opinion and forward to committee ○ Confirm that required changes are made to the opinion ● Committee: Review and approve opinion or refer back to manager for changes
Record	<ul style="list-style-type: none"> ● Fairness opinions ● Fairness Opinion Review/Approval forms

FINRA Rule 5150 outlines requirements when Coastal Equities, Inc. issues a fairness opinion. The rule requires that investors-shareholders be informed about potential conflicts of interest between Coastal Equities, Inc. and the issuer and addresses specific procedures when issuing fairness opinions. This includes fairness opinions issued to the board of directors and/or any special committee or subset or committee of the board.

Specific requirements are explained below. In summary:

- Required disclosures must be included in the fairness opinion.
- The Fairness Opinion Review/Approval form must be completed.
- The IB supervisor must approve the opinion and forward it, with the form, to the review committee.
- The review committee will review the opinion and notify the manager of approval or required changes.
- Revised opinions must be re-submitted to the committee for review and approval.

15.18.1 Disclosures

Disclosures include "significant" payment or compensation. FINRA does not assign a quantitative number to "significant" but defines it as a payment or compensation that a reasonable person who reads a fairness opinion would have an interest in knowing in order to assess whether Coastal Equities, Inc. has a potential conflict of interest. The receipt of *de minimis* fees (such as trading fees or other small incremental fees from account assets or activity) are not required to be disclosed. Disclosures may be descriptive rather than quantitative.

The fairness opinion must disclose if Coastal Equities, Inc.:

- has acted as financial advisor to any party to the transaction that is the subject of the fairness opinion.
- will receive compensation, contingent on the successful completion of the transaction, for issuing the fairness opinion and/or serving as advisor. *[Includes significant payments or compensation from related transactions (e.g., stapled financings) if such transactions are contingent upon the completion of the transaction for which the fairness opinion was issued.]*
- will receive any other significant payment or compensation contingent upon the successful completion of the transaction.
- has had any material relationships that existed during the past two years or that are mutually understood to be contemplated in which any compensation was received or is intended to be received as a result of the relationship between Coastal Equities, Inc. and any party to the transaction that is the subject of the fairness opinion. *[Includes material relationships between Coastal Equities, Inc. and all parties to the transaction, not just the party requesting the fairness opinion. A fairness opinion issued to a target's board of directors would have to include disclosure of any relationship with the acquirer.]*
- has independently verified information provided by the company requesting the opinion where that information is used for a substantial basis of the fairness opinion. *[If verified, must include a description of the information or categories of information verified and the process or standards for independent*

verification. Where no information provided by the company is verified, include a blanket statement that no independent verification took place.]

- has approved the fairness opinion through a fairness committee or whether approval is required. *["Fairness committee" is deemed by FINRA to include any committee or group that approves a fairness opinion in accordance with Rule 5150(b).]*
- expresses an opinion about the fairness of the amount or nature of the compensation to any of the company's officers, directors or employees, or class of such persons, relative to the compensation to the public shareholders of the company. *[Disclosure is required as to whether or not such an opinion is expressed.]*

15.18.2 Approval

Fairness opinions must be approved prior to issuance.

- Opinions will be approved by a committee comprised of three or more individuals including representation from non-investment banking areas such as Compliance, Operations, or Sales, and representation from Investment Banking personnel who are not involved on the deal team to the transaction. At least two persons must be from non-investment banking departments. All committee members must be sufficiently experienced or knowledgeable in investment banking matters to render approval.
- The deal team must present the complete fairness opinion, including required disclosures and an explanation of valuation analyses used in the fairness opinion, to the manager of Investment Banking for review prior to submission to the committee. The manager is responsible for confirming that all required disclosures are included.
- The committee is responsible for reviewing the opinion (including a determination of whether the valuation analyses used in the opinion are appropriate) and approving or disapproving the opinion. The approval or disapproval and comments regarding necessary changes or other comments will be forwarded to the manager of Investment Banking.
- The manager is responsible for confirming that changes are made consistent with the instructions of the committee. If the fairness opinion is revised, it must be re-submitted to the committee for review.
- The committee will retain records of who is serving on the committee, its reviews, and its actions.

15.19 Origination, Record Retention, Closed Deal Files

15.19.1 Due Diligence

The Securities Act of 1933 can impose substantial civil liability on various parties, including the issuer, the underwriters, and the accountants involved in the preparation of a registration statement or offering document. In particular, these participants are subject to potential liability if any part of the effective registration statement contains an untrue statement of material fact or omits to state a material fact. Moreover, failure to conduct proper due diligence can result in the revocation by the SEC of a broker-dealer's registration.

An underwriter may avoid liability if it can affirmatively demonstrate that it, after a reasonable investigation or "due diligence," had grounds to believe and did believe that the registration statement or offering document did not contain a material misstatement or omission.

15.19.2 Investment Banking's Responsibility

Although the product origination groups have the primary due diligence responsibility, Bankers should work closely with their product origination partners to help ensure a thorough due diligence review has been conducted and documented. Contact Compliance or Legal with any questions.

15.19.3 Required Document Retention

Because an underwriter has the burden of proving its due diligence defense under the securities laws, it is essential that the investigation conducted by Coastal Equities, Inc. be documented. One central "deal file" should be maintained and controlled by the Lead Banker. All other files shall be either merged into the central file or destroyed once the offering has been completed.

The central closed deal file should contain only clean, final copies of deal documents which may include, but not be limited to:

- Final closing documents (any preliminary drafts and all copies with other extraneous records such as handwritten notes should be discarded)
- Investment Committee deal package (where applicable)
- Rating Agency Presentation (where applicable)
- Computational materials provided to investors (where applicable)
- Due diligence questionnaire
- Regulatory filings
- Pitchbooks or other marketing materials
- Other pertinent correspondence

All documentation related to a securities underwriting must be maintained for a period of three years; two years in an easily accessible place.

15.19.4 M&A Closed Deal Files

To comply with federal securities regulations, an M&A Closing File Checklist is designed to assist in collecting and retaining important documents relating to the engagement of Coastal Equities, Inc. as financial advisor to customers in connection with M&A transactions.

This list of documents is not intended to be exhaustive. Given storage space constraints, Coastal Equities, Inc. wishes to keep **final** copies of the **formal** documentation that is necessary to reflect Coastal Equities, Inc.'s relationship with the party or parties to the engagement and our work product. Coastal Equities, Inc. does not want to retain copies of documents that are readily available from other sources, are merely drafts or contain information that is available in other documents that are being retained. Space constraints and the increasing lists involved in the retention of large transaction files make it desirable to retain only those items reflected on the list below or deemed by the deal team leader to be an important record that is in keeping with firm policies.

Promptly upon closing of a transaction or after the expiration or termination of Coastal Equities, Inc.'s engagement, an associate on the deal team, with the guidance of the deal team leader, will compile the documents listed below, as applicable. Upon compilation of the file, the supervisor who supervises the deal team will review the file and include in the file a signed statement signifying that the file is ready for storage. The file will consist of paper documents. Copies of the file may also be kept in "pdf" format in addition to, but not in lieu of, paper documents. Any other electronic copies of documents should be deleted or redacted to remove transaction-specific or confidential information and should be stored in the forms library.

These files will be maintained in a readily accessible central location for a period of three years, with the most recent two years readily accessible.

Compliance and the appropriate supervisor will periodically review these files to ensure that all (and only) appropriate documents are being properly maintained, and that the supervisor has reviewed the files.

Materials required to be maintained (if applicable):

1. **Commitment Committee Materials.**
 - Memorandum.
 - Engagement letter.
2. **Fairness Opinion Materials** (presentation materials vs. engagement letters, contracts or other exhibits).
3. **All board presentations during the engagement (only final).**
4. **Contractual Agreements with Customer and other Parties.**
 - Engagement Letters.
 - Confidentiality Agreements.
 - Indemnity Agreements.
 - Right of Refusal Letters.
 - Amendments or Terminations.
 - Approvals of Marketing Materials or Potential Purchasers, *etc.*
5. **SEC Filings** that refer to Coastal Equities, Inc. and include copies or descriptions of our fairness or adequacy opinions.
 - Proxy statements, information statements, Schedules 14D-9 and TO.
6. **Marketing Materials approved by Customer.**
7. **Substantive Letters to SEC or Other Governmental Agencies from Coastal Equities, Inc. or its counsel.**
 - Consents of Coastal Equities, Inc..
8. **Financing Commitments** (related to the transaction, *i.e.*, to either buyer or seller from Coastal Equities, Inc. or its affiliates [if shared with deal team]).
9. **Opinion Letters or Formal Advice from outside counsel to Coastal Equities, Inc..**
10. **Working Group Lists.**
11. **Other Pertinent Correspondence.**

16 MUTUAL FUNDS

[FINRA Rule 2341]

16.1 Introduction

Mutual funds, for purposes of these policies and procedures, refer to open-end investment companies. In addition to mutual funds, this chapter includes sections on closed-end funds and unit investment trusts (UITs), which also are investment company securities but are not considered "mutual funds."

Key points for consideration when offering mutual funds include the following:

- RRs must consider sales charges when recommending mutual funds and determine the most advantageous cost structure for the customer including class types.
- Customer suitability determination includes consideration of investment objectives, other investments held, financial and tax status, and risk tolerance.
- Fund characteristics to consider include investment objectives, risk, cost structure, and underlying investments and strategies.
- Switching from one fund to another requires the customer's signed acknowledgment.
- RRs cannot "sell dividends" or facilitate customer "late trading" or "market timing."
- Required disclosures are included in prospectuses or summary prospectuses (open-end funds only) which must be provided to purchasers.

16.2 Mutual Funds Offered by The Firm

Responsibility	<ul style="list-style-type: none">• New Product Committee
Resources	<ul style="list-style-type: none">• Prospectuses and other information provided by mutual fund companies or other distributors• Selling agreements• Records regarding commission earned from sales of funds and revenue received from revenue sharing agreements or directed brokerage
Frequency	<ul style="list-style-type: none">• As required - signing selling agreements• As required - review potential revenue sharing agreements for compliance with anti-reciprocal rules• Quarterly - compare mutual fund commissions against revenue sharing or directed brokerage, if applicable• Annually - training for marketing, sales, and trading staff, as appropriate, regarding anti-reciprocal prohibitions, if applicable
Action	<ul style="list-style-type: none">• Review information on mutual funds• Determine which fund companies' products to offer• Review dealer agreements for:<ul style="list-style-type: none">○ restrictions or obligations that may affect CEI's sales of the mutual fund and issue instructions to RRs, if necessary

	<ul style="list-style-type: none"> ○ representation by the mutual fund company that it uses reasonable criteria when selecting Selling Brokers and has reasonable policies and procedures to avoid formal or informal directed brokerage arrangements ● Execute dealer agreements with mutual fund companies ● Provide education regarding mutual fund sales including prohibitions under the anti-reciprocal rule ● Review special sales programs and promotions outside the standard commission schedule to determine compliance with the anti-reciprocal rule ● Review for potential correlation between fund sales and directed brokerage commissions that may indicate violations of anti-reciprocal rules ● Refer potential directed brokerage arrangements to Compliance for review and determination of corrective action ● Review revenue sharing agreements: <ul style="list-style-type: none"> ○ At time of proposal to determine compliance with anti-reciprocal rules ○ To develop and provide disclosure to customers ○ To determine ongoing compliance with anti-reciprocal rules
Record	<ul style="list-style-type: none"> ● Information used to determine which funds to sell ● Signed dealer agreements ● Notices to RRs of special restrictions or requirements included in dealer agreements ● Records of special sales programs and promotions including the date of review, reviewer's signature/initials, and notes of action taken, if appropriate ● Revenue sharing arrangements and disclosures to customers (Initial and quarterly reviews)

Mutual funds with a range of investments and objectives will be available for investment by customers. CEI introduces accounts to Wells Fargo Clearing Services, LLC, which has available to it multiple fund families and their offerings. In addition, CEI offers mutual fund products directly through selling agreements. This chapter applies to all recommendations of mutual funds regardless of the method of purchase or sale.

16.2.1 Dealer Agreements

[FINRA Member Alert November 22 2005]

CEI executes dealer agreements with mutual fund underwriters. Many agreements include restrictions against activities such as late trading or market timing, which are discussed later in this chapter. Any special requirements or restrictions included in dealer agreements and not already covered in this chapter will be communicated to sales personnel.

16.2.2 Anti-Reciprocal Rule

[Investment Company Act Rule 12b-1; SEC Release No. IC-26591; FINRA Rule 2341(k); FINRA Notice to Members 05-04]

CEI is prohibited from favoring the sale of mutual funds based on revenues earned (directly or indirectly) from the investment company issuing the mutual fund. This includes:

- *Directed brokerage*, which is a practice where the investment company directs brokerage business to a broker-dealer to reward or compensate the dealer for selling its funds. This includes, directly referring

brokerage transactions to the dealer that sells its funds and also "step-out" arrangements where brokerage is directed to another firm and then revenue is shared with the dealer selling the funds.

- *Undisclosed revenue sharing*, where the mutual fund company pays incentives to the broker-dealer to secure a prominent place in the selling dealer's distribution network ("shelf space").

If an employee becomes aware of a prohibited activity, it should be reported immediately to Compliance.

The selection and offer of mutual funds will comply with anti-reciprocal prohibitions. Specifically, CEI will not:

- Sell shares of, or act as underwriter for, any investment company where CEI is aware that the investment company or its investment adviser or underwriter have directed brokerage arrangements in place that are intended to promote the sale of investment company securities.
- Favor or disfavor sales of investment companies based on commissions received or expected and tied to sales
- Require such commissions to sell the funds or offer commission to another broker-dealer relating to their sale of funds
- Circulate information about commissions received from an investment company, other than to senior managers for purposes of managing CEI's business
- Sponsor or encourage an incentive campaign or special sales effort of another dealer financed by commissions received related to the sale of the funds
- For retail sales, provide incentive or special compensation based on the amount of commissions expected to be received from the fund or another source
- Establish recommended, selected, or similar preferred lists of investment companies if based on brokerage commissions
- Allow RRs and other sales personnel to participate in commissions received from investment company portfolio transactions
- Use the sale of investment company shares to negotiate the price or amount of brokerage commissions paid on investment company portfolio transactions

These prohibitions do not prevent execution of investment company portfolio transactions that are not tied to sales of the investment company's shares. RRs and managers may be compensated for sales attributable to them including the use of overrides, accounting credits, or other compensation, provided the extra compensation does not violate anti-reciprocal prohibitions.

16.2.2.1 Disclosure Regarding Revenue Sharing

If CEI engages in revenue sharing, it will clearly disclose such an arrangement to retail and retirement customers purchasing the applicable funds.

16.3 Sales Charges

[FINRA Rule 2341(d); FINRA Regulatory Notice 21-07]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Daily Transaction Report • Fund information (<i>i.e.</i>, prospectus, Statement of Additional Information) • Exception reports (as available)

Frequency	<ul style="list-style-type: none"> • Daily/As needed
Action	<ul style="list-style-type: none"> • Review Breakpoint Worksheets for completeness, determination of sales charge discounts available to purchaser • Review order records to determine that discounts and waivers have been considered • Review daily transactions to determine same-day mutual fund purchases are considered for LOI and ROA discounts • Review orders for improper breakpoint sales (near but below common breakpoint levels [\$25,000, \$50,000, etc.]) • Review orders for purchases of multiple funds with similar investment objectives and confer with RR about the suitability of multiple purchases • Letter of Intent (LOI) reviews for: <ul style="list-style-type: none"> ○ Notation on Worksheet/order record whether an LOI will apply (including retroactive LOIs if permitted by the fund) • Rights of accumulation (ROA) review for indication on order record whether ROA applies • Where a customer has not been provided an available discount: <ul style="list-style-type: none"> ○ Confer with the RR ○ Notify the customer and correct the purchase to include the discount • Provide training to RRs on mutual fund purchases and sales charge discounts
Record	<ul style="list-style-type: none"> • Breakpoint Worksheets • Order records • Daily transaction reports • Exception reports (as available)

When investors purchase mutual funds (other than no-load funds), they incur sales charges that may be front-end or back-end charges. Mutual funds offer investors discounts to sales charges, which are explained in the fund's prospectus. This section describes different types of discounts available to mutual fund purchasers.

RRs are responsible for understanding the availability of sales charge discounts to provide the customer the opportunity to purchase a mutual fund under the most favorable terms available. RRs are required to use the Breakpoint Checklist and Worksheet for every mutual fund purchase involving a sales charge. The Checklist and Worksheet are discussed at the end of this section.

16.3.1 Breakpoints

[FINRA Rule 2342; Joint Task Force on Breakpoints: <https://www.finra.org/rules-guidance/guidance/faqs/report-joint-finraindustry-task-force-breakpoints>]

For some mutual funds, front-end sales charges decrease as the dollar amount invested increases. These thresholds for reduced sales charges are called breakpoints. Different fund families establish different opportunities to link accounts, transactions, and share classes to qualify purchasers for reduced sales charges.

The RR has an obligation to disclose the existence of breakpoints to enable the customer to evaluate the desirability of making a qualifying purchase. The RR also must indicate on the mutual fund order if the customer qualifies for a breakpoint because of linked accounts, transactions, or share classes or other basis for meeting a breakpoint by linking the customer's transaction with another.

"Improper 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 is appropriate, but will preclude the customer from qualifying for a breakpoint, the customer should sign a letter acknowledging his or her understanding that a breakpoint is being given up by purchasing multiple funds.

Purchases of mutual funds under a breakpoint are not subject to breakpoint violations if the purchases are made as part of a bona fide asset allocation program sponsored by CEI. Customers who participate in a Firm-sponsored program are notified, as part of the agreement to participate in the program, that they may not receive breakpoint reductions that otherwise would be available.

16.3.1.1 Breakpoint Checklist and Worksheet

When selling a front-end load fund (Class A) to a customer, the RR is required to complete the Breakpoint Calculator in SmartStation (in the Order Entry Menu), or, for direct business, the Breakpoint Worksheet, available at [FINRA Worksheet](#). Worksheets must be submitted along with the Coastal Account Information form to the Financial Advisor's supervisor for direct business.

The purpose of the Worksheet is to document required information about the customer's holdings to determine whether the customer qualifies for a reduced sales charge, including:

- Total holdings at CEI in the fund, or a related fund in the same family
- Total holdings outside CEI in the fund, or a related fund in the same family
- Total holdings of related parties (some funds provide discounts when related persons own the same fund, or funds in the same family of funds)

16.3.1.2 Breakpoint Search Tool

<http://www.finra.org/fundsearch>

A Breakpoint Search Tool is available from FINRA online. The tool provides breakpoint schedules and linkage rules for mutual funds with sales charges.

16.3.2 Letters of Intent

[FINRA Notice to Members 02-85]

A letter of intent (LOI) 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. Some funds allow investors to use an LOI retroactively to include the value of past purchases in the LOI period. The RR should determine whether the customer made a prior purchase within the allowable period and whether the fund allows backdated LOIs.

16.3.3 Rights of Accumulation

[FINRA Rule 2341(d)(1)(B); FINRA Notice to Members 02-85]

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 RR should ask the customer whether the customer has other holdings in the fund or fund family, to determine whether rights of accumulation may be available to the customer.

Mutual funds follow different rules to determine the value of existing holdings and when a customer qualifies for a breakpoint discount. Most funds use current net asset value (NAV) of existing holdings, and a small number of funds use historical cost (cost of the initial purchase). If historical cost is used, it may be necessary for the investor to provide account records to qualify for the breakpoint discount.

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.

16.3.4 Reinstatement Privilege

Some funds offer shareholders a "reinstatement privilege" allowing the shareholder to reinvest some or all of the proceeds from a prior liquidation of the fund within a specified period of time (for example, 180 days) at a reduced sales load or no sales load. The RR should determine whether the customer qualifies for a reinvestment privilege and, if he or she qualifies, note this on the order at time of entry.

16.3.5 Sales Charge Reductions/Waiver or NAV Transfer Program

Some mutual funds waive fees for eligible retirement plans and charities. RRs are obligated to apply waivers where they are available.

A limited number of mutual funds offer a sales charge discount in the form of a waiver or NAV transfer. Investors may purchase Class A shares of a mutual fund without paying a front-end sales charge, if investing some or all of the proceeds from the sale of a mutual fund in a different mutual fund family for which the investor paid a front-end or back-end sales charge within a specified period of time. The period when the discount is available is generally 30 to 90 days from the date the investor purchased the other fund. This type of discount is explained in the fund prospectus and Statement of Additional Information.

Generally, customers will not make short-term sales of mutual funds. In those unusual circumstances, where the customer is making such a sale, the RR should investigate whether a waiver is available on the new purchase.

16.3.6 Deferred Sales Charges

[FINRA Rule 2341(n)]

If a customer purchases shares of a mutual fund that imposes a deferred sales charge on redemption, the front of 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."

16.3.7 Direct Application and Wire Order Accounts

Mutual funds allow investors to purchase funds directly (sometimes called "application way" or "wire order" purchases or accounts). RRs are not permitted to recommend, or to direct, that a customer make a direct purchase of mutual funds unless such purchases are made through CEI.

Direct purchases of Mutual Funds must be submitted to the RR's supervisor with the subscription documents and Coastal New Account Form. Once approved, a copy of the approved documents are forwarded to New Accounts at the Home Office, and the RR will promptly forward the documentation directly to the fund.

16.3.8 Sales Charge Discounts Must Be Marked on Mutual Fund Orders

Because automated mutual fund order processing systems do not generally provide the ability to monitor application of an available sales charge discount, it is important that all pertinent information be recorded on the order and entered to the system, including whether the customer's purchase qualifies for a sales charge discount. Incomplete mutual fund orders will not be accepted and will be returned to the RR for completion of necessary information about available sales charge discounts.

Order entry procedures, including completeness of orders and proper application of available discounts, will be reviewed as part of the periodic review of sales practices in the office.

16.4 Switching

[FINRA Notice to Members 94-16 and 91-39]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Order records• Daily Transaction report
Frequency	<ul style="list-style-type: none">• Daily (As needed)
Action	<ul style="list-style-type: none">• On a risk basis, review mutual fund orders for transactions where the customer sells one mutual fund to buy another mutual fund• When switching is identified, ensure the customer is provided a switch letter
Record	<ul style="list-style-type: none">• Initials on order records; notation of review in Smart Station Supervision module• Switch letters maintained in Smart Station

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 CEI as a result of effecting the switch. As for all recommendations, the RR must have a reasonable basis for believing the switch is in the best interest of the customer.

The customer may incur multiple sales charges by changing from one fund to another or may be subject to an extended holding period, 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 sent to the customer acknowledging an understanding of the consequences of the switch. It is the designated supervisor's responsibility to ensure switch letters are sent for switch transactions. The letter may be sent through Smart Station and retained in Smart Station.

16.5 Market Timing Transactions

[FINRA Notice to Members 95-80]

FINRA has stated that recommendations to fund investors to engage in market timing transactions should be made, if at all, within a single family of funds or where there are no transaction costs associated with the trades. Transactions that do not adhere to this standard may raise suitability questions.

16.6 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.

16.7 Misrepresenting "No-Load" Funds

[FINRA Rule 2341(d)(4)]

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.

16.8 Reinvestment of Maturing Certificates of Deposit in Mutual Funds

[FINRA Notice to Members 93-87]

When funds from maturing certificates of deposit (CDs) are used for the purchase of mutual funds, including money market funds, customers must be advised of the material differences between the two products, particularly the greater risk to the customer's capital and the absence of any federal insurance or guarantee for assets placed into mutual funds.

16.9 Suitability

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Daily Transaction report • Customer monthly statements
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Review mutual fund transactions for suitability with particular attention to the following: <ul style="list-style-type: none"> ○ Funds with high risk objectives: is the investment consistent with the customer's investment objectives?

	<ul style="list-style-type: none"> ○ 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? ○ Large purchases of class B shares that may qualify for lower sales charges if purchased as class A shares ○ Confer with RRs regarding any transactions that raise questions ● Review recommended orders for compliance with Regulation BI [see the chapter <i>REGULATION BEST INTEREST (BI)</i>] ● Follow up action may include: <ul style="list-style-type: none"> ○ Requesting written acknowledgement from the customer that the higher costs are understood ○ Canceling transactions that appear to be inappropriate
Record	<ul style="list-style-type: none"> ● Initials on order records; notation of review in Smart Station supervision module and Daily Transaction Report ● Notes on Daily Transaction report and/or Branch Manager's Log of follow up action, if appropriate ● Customer's signed acknowledgement filed in the customer file, if appropriate

When recommending that a customer purchase, sell, or exchange a mutual fund, the following should be considered:

- Customer information including financial and tax status, investment objectives, other investments including other mutual funds
- Information regarding the fund to be recommended including sales charges, historical performance and volatility, risk, investment objective, and nature of the securities and investment strategies in the fund (use of leverage, investments in hedge funds or derivatives, *etc.*)
- Risk (fund investment risk and customer's risk tolerance)
- Appropriateness of high concentrations in any particular type of fund or investment

Suitability is only one element of acting in a customer's best interest. Recommendations to retail customers who are natural persons are subject to Regulation Best Interest (BI) which is broader than the suitability requirement. Reg BI includes recommendations for orders; types of accounts; and investment strategies, including recommendations to prospects. It is important to be familiar with those requirements which are included in the chapter *REGULATION BEST INTEREST (BI)*.

16.9.1 Multi-Class Mutual Funds

[FINRA Notice to Members 95-80]

Mutual funds often offer three classes of shares that are based on the same mutual fund portfolio but differ regarding costs incurred by the customer.

Class A shares: Generally impose a front-end sales load and no (or a low) ongoing fee to pay for sales and marketing expenses (Rule 12b-1 fees). Usually the front-end sales load will decrease at certain breakpoints depending on the size of the purchase and whether the purchase qualifies for a letter of intent or rights of accumulation which also may result in a lower sales charge. A front-end sales charge means a portion of the customer's funds are not invested and instead pay the front-end charge.

Class B shares: Generally do not impose a front-end sales charge but may impose a contingent deferred sales charge (CDSC) on share redemption and relatively high 12b-1 or other asset-based fees. The amount of the CDSC usually declines the longer the shares are held. Class B shares often automatically convert to Class A shares (with lower asset-based fees) after a period of time, usually after the CDSC declines to zero. All of the customer's funds are invested at the time of purchase. These funds may not be referred to as no-load funds since they impose a back-end contingent charge.

Class C shares: Have different expense features than A and B shares; may include no front or back-end load or a small back-end load; and higher 12b-1 or other asset-based fees. Class C shares are often used for managed accounts and asset allocation purposes.

In addition, some mutual funds offer other classes that impose no front-end or back-end sales charges and relatively low asset-based fees. These may be offered to limited types of purchasers such as retirement plans or institutional investors.

The following are guidelines for determining which class of shares is best for the customer:

- The cost advantages of one class versus another must be considered.
- Class B or C shares generally should not be recommended to customers making purchases in large amounts that may qualify for lower costs because of breakpoints, letters of intent, or rights of accumulation available through the purchase of class A shares.
- Class B shares should not be purchased for a customer if the RR knows or has reason to know that the customer will be purchasing additional shares that would take a purchase over a Class A breakpoint within 13 months of the initial purchase.
- Class B shares should not be purchased if potential additional purchases would qualify for a NAV price.
- Class A shares may be more appropriate for a customer who intends to remain invested in the fund for a longer period of time. Over time the higher continuing sales charges of Class B and C shares may exceed the initial load and smaller 12b-1 fees of Class A shares.
- Class C shares may be appropriate for a customer who does not qualify for a reduced Class A initial sales charge and who does not intend to remain invested in the fund for a period during which the fund's Class B shares are subject to a CDSC.
- Some funds waive the sales charge under circumstances specified in the prospectus (*e.g.*, purchases by employees of broker-dealers and their immediate family members). If a Class A sales charge waiver is available, Class A shares will be less costly than Class B or C shares. A CDSC may be imposed on early fund redemptions of Class A shares where a waiver is granted; the prospectus should be consulted.

16.9.2 Considerations for Newly-Hired RRs

[FINRA Regulatory Notice 07-36; FINRA Notice to Members 07-06]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Information about transferring customers' investments in investment company products
Frequency	<ul style="list-style-type: none"> • As required for proposed switching of investments
Action	<ul style="list-style-type: none"> • Review existing investments against proposed substitute investments

	<ul style="list-style-type: none"> • Prepare and provide information to customers regarding investment options including that the customer may have to hold the existing investment at the prior firm, the cost of switching to another investment, and other considerations before changing investments
Record	<ul style="list-style-type: none"> • Records of accounts reviewed and suitability determination, action taken including information provided to customers

There are considerations when a newly-hired RR transfers customers who hold investment company products (mutual funds, variable annuities). If CEI cannot or will not service the customer's existing investment (inability to transfer products, CEI does not have a dealer or servicing agreement), the appropriateness and suitability of recommending a new investment company product must be determined by the RR and CEI. Before liquidating existing investments and reinvesting in new products, disclosure must be made to the customer regarding the costs and benefits of any proposed change in investments and proposed replacement investments must be suitable. A change of employment is not by itself a suitable basis for recommending a switch from one product to another.

16.10 Late Trading and Market Timing

[FINRA Notice to Members 03-50]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Records of mutual fund transactions • Reports available to track mutual fund transactions
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Review transactions for patterns of late trading • Identify patterns of "as-of" trades in mutual funds that may indicate late trading • Review transactions for indications of market timing (frequent in-and-out transactions in a mutual fund) • Determine whether market timing is permitted for the fund • Consult with Compliance when potential violations of late trading or market timing are identified • Take corrective action which may include contact with the fund, fund sponsor, or other person potentially engaging in the prohibited activities; limiting trading activity; closing the account; or other corrective action appropriate to the situation.
Record	<ul style="list-style-type: none"> • Records reviewed for trading (whether order records or reports) are retained in supervision files including the date reviewed, the initials of the reviewer, and notes of corrective action, if appropriate.

There are two mutual fund trading activities that may violate SRO rules whether initiated by the RR or the RR facilitates the prohibited activity by assisting a fund manager, an investment adviser, a fund sponsor, a customer, or someone else in engaging in these activities.

Late trading is the practice of effecting an after-close mutual fund purchase or redemption at the same day's net asset value (NAV). NAV is usually calculated at 4:00 p.m. E.T., the close of the trading day, and orders received after the close are effected at the next day's closing NAV. Late trading is a violation of fair practices because it potentially permits someone to take advantage of market movements known after the 4:00 deadline and gives the person an advantage in determining whether to buy or sell a fund based on an already established price.

Engaging in late trading or enabling someone else to engage in late trading is prohibited.

Market timing is rapid and repetitive in-and-out trading to take advantage of market movements such as buying an international mutual fund one day and selling it the next day because of movements in foreign markets that impact the fund's value. While trading a mutual fund is not, in itself, illegal or violates a rule, it often violates restrictions established by the fund on short-term market timing trades. **Engaging in market timing or knowingly aiding someone in activity that violates a mutual fund's internal trading guidelines is prohibited.**

There are valid reasons why an occasional mutual fund trade may be entered late and should be processed at the current day's NAV. There may also be funds that do not prohibit market timing. However, RRs must not engage in or assist someone else in engaging in prohibited late trading and market timing. Compliance should be contacted if someone proposes to engage in either activity.

16.11 Block Letter Restrictions

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Compliance
Resources	<ul style="list-style-type: none"> • Mutual fund block letters
Frequency	<ul style="list-style-type: none"> • As required when letters are received
Action	<ul style="list-style-type: none"> • Notify the RR and the RR's supervisor • Monitor the account for potential violations of restrictions • Take corrective action if violations are detected; action will include notifying the RR and the RR's supervisor; potentially closing the account and disciplinary action against the RR as determined by Compliance
Record	<ul style="list-style-type: none"> • Mutual fund block letters • Reviews of blocked accounts and action taken

Mutual fund companies sometimes issue "block letters" that limit the trading activity of a particular customer. This may occur if the fund detects trading that violates trading restrictions imposed by the fund such as late trading or market timing.

When a block letter is received, the RR and the RR's supervisor will be notified, and the RR is responsible for complying with the restriction. Orders may not be entered for the customer in another account that is beneficially owned by the customer to circumvent any restrictions.

16.12 Communications

[FINRA Rule 2210]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Outgoing communications
Frequency	<ul style="list-style-type: none"> • Daily/As needed
Action	<ul style="list-style-type: none"> • Review for the following: <ul style="list-style-type: none"> ○ Use of pre-approved letters without change other than updating data where required ○ 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 CEI) ○ 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 <i>Disclosure Of Material Facts</i>) ○ Performance is represented accurately and consistent with rule requirements regarding yield and return ○ Language that indicates a prospectus is enclosed • Contact Compliance for review of questionable communications • Correct unapproved content
Record	<ul style="list-style-type: none"> • Initials on communications/signed advertising request form/email approval • Compliance retains communications it reviews

RAs should use letters pre-approved by CEI and include a prospectus or limit communications to stating that a prospectus is enclosed and the RA will be in contact with the customer. Questions should be referred to Compliance.

16.13 Disclosure of Material Facts

[FINRA Notice to Members 95-80]

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
- risks of investing in the fund relative to other investments
- 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 generally includes many if not most of these disclosures.

16.14 Disclosure of Fees, Expenses and Performance

[FINRA Rule 2210(d)(5)]

Many firms prohibit generally all written discussion of a fund's performance and simply refer to the prospectus. 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.

Correspondence and retail communications including performance about mutual funds (other than money market funds) must disclose:

- The standardized performance information required by '34 Act Rule 482 and Rule 34b-1; and
- If applicable:
 - The maximum sales charge on purchases or the maximum deferred sales charge included in the current prospectus; and
 - The total annual fund operating expenses, gross of any fee waivers or expense reimbursements, as stated in the fee table of the current prospectus.

This information must be prominent in the communication, and in any print advertisement in a prominent text box that may also include comparative performance and fee data and disclosures required under Rules 482 and 34b-1.

16.15 Prospectuses

RRs should provide a copy of the prospectus when recommending a mutual fund purchase to a customer. A summary prospectus may also be provided (if available from the investment company) for open-end funds. The summary prospectus includes reference to an internet site where the complete statutory prospectus is available along with other required information.

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

16.16 Retail Communications

[FINRA Regulatory Notice 11-49; NASD Notice to Members 93-36]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Firm-approved retail communications
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Review and approve/disapprove retail communications are used in conjunction with sales of mutual funds • Notify RRs/supervisors of approved communications
Record	<ul style="list-style-type: none"> • Records of approved/disapproved retail communications

There are specific requirements for retail communications regarding mutual funds. Advertising must be filed with FINRA within prescribed periods (see the chapter *COMMUNICATIONS WITH THE PUBLIC* and the section *Special Filing Or Approval Requirements* for details). There also are mandated guidelines on representations regarding performance and yield, including specific requirements when retail communications include a TIPS fund's current yield.

RRs may use materials provided by the fund or firm-approved materials. Any other retail communications must be approved by Compliance prior to use.

16.17 Sales Material Provided by Third Parties

[FINRA Rule 2210(b)(1); FINRA Regulatory Notice 08-27 and 08-12]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Proposed sales material from third parties
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • For all third-party sales material review for: <ul style="list-style-type: none"> ○ Clear indication the material is advertising if CEI or the RR paid for it ○ Suggestions or inferences the RR authored the material when in fact that is not the case ○ Acceptable RR titles, if titles are included ○ Pre-determined interviews (written or otherwise) are identified as such and include disclosure the Q&A is pre-determined and not a spontaneous interview • For third-party material previously filed with and approved by FINRA:

	<ul style="list-style-type: none"> ○ Obtain a copy of FINRA approval ○ Allow use if no material changes are made ● For third-party material NOT previously filed with FINRA: <ul style="list-style-type: none"> ○ Review the material for consistency with FINRA standards ○ File with FINRA, if required <ul style="list-style-type: none"> ▪ Upon receipt of review letter, make necessary changes ▪ Indicate approval including date of approval
Record	<ul style="list-style-type: none"> ● Copy of sales material with notations, as necessary ● Copy of FINRA review letter, if one has been obtained ● Record of date first use and (if applicable) date of last use ● Retain for three years from date of last use

Sales material provided by outside (third) parties such as newspaper or magazine articles, books or pamphlets, handouts, and other third-party provided material **must be reviewed and approved by Compliance prior to use**. Materials made available by CEI may be presumed to have been reviewed and approved. When participating in an interview (written or otherwise) where the questions are pre-determined by the third party, disclosure must be made that questions and answers were pre-determined and the interview was not spontaneous. Some sales material requires the prior approval of FINRA.

The following guidelines apply when using third-party sales material:

- RRs may **not** suggest or infer that they authored investment-related books, articles, or other sales material not written by them.
- If CEI or RR has paid for the publication, production, or distribution of any communication that appears to be a magazine, article or interview, then the communication must be clearly identified as an advertisement.
- Sales material may **not** include RR titles other than those normally conferred by CEI (account executive, financial consultant, *etc.*) unless previously approved by Compliance. RRs particularly may **not** use titles inferring expertise in dealing with senior investors.

16.18 Dealer-Use-Only Material

[FINRA Notice to Members 95-80]

Responsibility	<ul style="list-style-type: none"> ● Branch Person in Charge ● Supervisor - communication review
Resources	<ul style="list-style-type: none"> ● Outgoing communications
Frequency	<ul style="list-style-type: none"> ● Daily/As needed
Action	<ul style="list-style-type: none"> ● Ensure the branch does not distribute dealer-use-only materials to the public ● Review communications to identify inclusion of restricted materials

Record	<ul style="list-style-type: none"> • Initials on communications; Global Relay evidence of review
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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 FINRA because it is for internal use only.

All dealer-use-only material will be marked as such with limited distribution.

16.19 Seminars and Other Public Presentations

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Outlines of proposed seminars and other public presentations that include mutual funds
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review outlines for appropriateness of presentation • Make necessary changes and approve (or disapprove, if appropriate) • Remind the RR of the requirement to provide prospectuses and compile a list of attendees who received prospectuses if specific mutual funds will be offered • If wholesaler sales materials will be included, ensure Compliance approves prior to use
Record	<ul style="list-style-type: none"> • Initials on outlines which are retained in the office Public Speaking file • List of attendees who received prospectuses (if appropriate) retained in the office Public Speaking file

The following guidelines apply when an RR or CEI sponsors a seminar for customers or prospective customers and where mutual funds are the subject of the seminar:

- An outline of the seminar must be provided to the designated supervisor prior to conducting the seminar.
- If specific mutual funds are recommended, prospectuses must be provided to those who attend and a list retained of to whom prospectuses were provided. A copy of the list is to be provided to the designated supervisor after the seminar.
- If a wholesaler makes a presentation at the seminar, the sales materials used (*i.e.*, story boards, scripts, handouts, *etc.*) must be approved by Compliance prior to the seminar.

The designated supervisor is responsible for approving and filing the outline of the seminar and the copy of the prospectus list, if applicable. Compliance is responsible for approving any wholesaler sales materials and filing it with FINRA's Advertising Department within 10 days of use.

16.20 Sales Contests and Incentive Programs

The following guidelines apply to sales contests and other incentive programs where mutual funds are the subject of the contest or program. Also refer to the chapter *ORDERS* and the section *Sales Contests* for general guidelines applying to all contests.

- All Sales contests must be approved by Compliance.
- Contests may not be based on the amount of brokerage commissions received or expected to be received from investment companies.
- When CEI acts as underwriter of investment company shares, CEI may not sponsor a contest or other incentive campaign of another broker-dealer with respect to the sale of shares of the investment company.
- RRs may not accept (directly or indirectly) cash or non-cash compensation from outside CEI.

16.21 Prompt Transmission of Applications and Payments

[FINRA Rule 2341(m); FINRA Regulatory Notice 15-23]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Mutual fund/variable annuity applications • Record of when transmitted by the RR such as postmarks on envelopes or check logs
Frequency	<ul style="list-style-type: none"> • Review applications: as required when applications are received • Review delayed transmittals: Monthly
Action	<ul style="list-style-type: none"> • Transmit applications to the payee (underwriter, investment company, or other designee) by: <ul style="list-style-type: none"> ○ the end of the 3rd business day following receipt of the customer's order to purchase; or ○ the end of 1 business day following receipt of the customer's payment, whichever is later • When CEI acts as underwriter and engages in wholesale transactions of shares received from other members, payments will be transmitted by the end of 2 business days following receipt of the payments • Review customer's signature date vs. postmark or other record of transmittal by the RR • Document transmittals more than 2 business days after customer signature date • Review delayed transmittals and: <ul style="list-style-type: none"> ○ for 3 or more occurrences within 12 months, notify the RR's supervisor to meet with the RR ○ for another occurrence within 12 months, assess a fine to the RR
Record	<ul style="list-style-type: none"> • Applications • Documentation of delayed transmittals including record of who reviewed, when reviewed, and action taken

R Rs are obligated to transmit mutual fund (and variable annuity) applications and customer payments to the designated office/application processor **on the same day as they are received**. CEI is obligated, by FINRA rule, to transmit the customer's payment to the underwriter within a short timeframe after receipt from the customer.

Failure to transmit applications and payments promptly is a violation of FINRA rules. RRs who do not comply with prompt transmission requirements may be subject to disciplinary action.

16.22 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 Operations, if required, prior to forwarding the letter to the fund.

16.23 Closed-End Funds

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Transaction reports that include closed-end funds
Frequency	<ul style="list-style-type: none"> • As needed
Action	<ul style="list-style-type: none"> • Review CEF trading for: <ul style="list-style-type: none"> ○ Short-term trading, particularly involving IPOs ○ Suitability of recommendations • Take corrective action, if appropriate, which may include: <ul style="list-style-type: none"> ○ Conferring with the RR ○ Contacting the customer ○ Consulting with Compliance ○ Cancelling trades • Include CEFs in training, particularly the disadvantages of short-term trading
Record	<ul style="list-style-type: none"> • Reviews of flagged transactions including date reviewed, initials of reviewer, and actions taken, if any • Records of training including who attended, date conducted, and subjects included

Closed-end funds (CEFs) are investment companies that issue a finite number of shares that trade in the open market, usually on a stock exchange. Because they trade like other stocks, requirements that apply to open-end mutual funds such as switch letters and prospectuses provided to all purchasers generally do not apply to CEFs. Certain features of mutual funds such as breakpoints, letters of intent, and rights of accumulation are not features of closed-end funds.

Since CEFs trade like stocks, requirements regarding handling orders in the chapter *ORDERS* apply. For example, RRs may not recommend or engage in excessive trading of CEFs, and recommendations are subject to suitability requirements.

Recommendations to purchase an IPO for a CEF may not be appropriate for short-term investors since there is a built-in sales charge. After the offering, CEFs typically trade at a discount from the IPO price. Recommending the sale of a CEF IPO after the penalty bid period (during which the RR would not earn commissions on the purchase) at a loss and then recommending the purchase of another CEF would be unsuitable.

The high distribution rates may be composed of dividends, interest income, capital gains and/or return of capital. RRs should consider and communicate to investors, where it applies, that a high rate of return may be a return of capital and not actual income for the investor and the funds trade at a high premium compared to NAV.

16.23.1 Business Development Companies (BDCs)

BDC funds may represent higher risk that must be considered when recommending them and communicating risks to investors. Following are some of the risk factors that must be considered.

- BDCs primarily invest in the corporate debt and equity of private companies which may offer higher yield through leveraged high credit risk exposure.
- Fueled by the availability of low-cost financing, BDCs may over-leverage illiquid portfolios.
- Non-traded BDCs are illiquid and investors may be limited to selling only through periodic share repurchases by the BDC at high discounts.

16.24 Leveraged Loan Products

Leveraged loans are adjustable-rate loans extended by financial institutions to companies of low credit quality that have a high amount of debt relative to equity. Floating-rate bonds do not trade on an organized exchange, making them relatively illiquid and hard to value. Funds investing in these loans may be marketed as less vulnerable to interest rate fluctuations and offer inflation protection, but the underlying loans held by the fund are subject to significant credit valuation and liquidity risks unclear to investors. RRs must consider and communicate these risks when making recommendations to investors.

16.25 Unit Investment Trusts (UITs)

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Available reports • Information regarding charges and discounts
Frequency	<ul style="list-style-type: none"> • As required when UIT transactions are effected
Action	<ul style="list-style-type: none"> • Review flagged transactions for: <ul style="list-style-type: none"> ○ appropriate sales charges including discounts available ○ Suitability, particularly patterns of sales and switching
Record	<ul style="list-style-type: none"> • Order records including record of review, action taken • Reports reviewed including record of review, action taken

UITs are investment company securities that invest in a fixed portfolio of securities such as corporate, municipal, or government bonds, mortgage-backed securities, common or preferred stock, or other investment company shares. Unit holders receive an undivided interest in both the principal and the income portion of the portfolio in proportion to the amount of money invested.

Unit investment trusts have a finite life that ends when all securities in the portfolio have matured or are liquidated per the terms of the trust.

16.25.1 Suitability

As for other securities, the RR is responsible to making a suitability determination prior to recommending a UIT to a customer. Considerations include the types and safety of securities in the UIT, call features of the trust, and the maturity date for the trust. The length of time the investor intends to hold the investment should be considered when recommending a UIT, since a secondary market for the UIT may not be assured and prices available in the secondary market may vary considerably from the liquidation value of the trust.

16.25.2 Sales Charges

UITs impose sales charges including front-end and back-end loads and management fees. In addition, like mutual funds, discounts may be available through breakpoints, letters of intent, and rights of accumulation. Some UIT sponsors offer rollover and exchange discounts for purchases made with the proceeds from a UIT originally purchased from the same sponsor **as well as UITs purchased from a different sponsor.**

RRs are required to consider charges and discounts available to determine that the customer will receive the best available price.

16.25.3 Primary Offerings

While UITs are not "mutual funds," they have some features similar to mutual funds, particularly in the initial offering of a UIT. The purchaser of a new UIT pays a load or other charges as described in the prospectus. Purchasers are provided a prospectus describing the UIT.

16.25.4 Secondary Market Transactions

A secondary market exists for many UITs. Investors may liquidate or purchase a UIT by placing an order to sell or buy it in the secondary market, if one exists. The price the investor pays to purchase in the secondary market may include a premium based on the market value of the securities in the portfolio. The customer may not recover that amount when the trust matures or is called.

Prospective UIT investors must not be misled regarding the potential return of UITs purchased in the secondary market. Any communication regarding the estimated current return should be accompanied by a quotation of the UIT's long-term yield or internal rate of return.

Secondary market purchasers are provided a copy of the UIT prospectus at time of purchase.

16.26 Funds of Hedge Funds

[FINRA Notice to Members 03-07]

A fund of hedge funds is an investment company that invests in multiple hedge funds and provides some diversification through the underlying investments. A fund of hedge funds allows retail investors who would not otherwise qualify to invest in a hedge fund to do so through the fund.

Because the underlying securities (hedge funds) are generally unregistered, high-risk securities, RRs must consider the risk of the underlying hedge funds prior to recommending the fund to customers.

16.26.1 Characteristics and Risks of Hedge Funds

When recommending a fund of hedge funds, it is important to understand the general characteristics and risks of hedge funds. While a fund of hedge funds provides diversification, the underlying funds represent a higher level of risk that should be considered when making a recommendation to a customer.

Hedge funds have the following general characteristics and risks:

- not registered under the Investment Company Act and exempt from registration under the '33 Act
- high minimum investments, often \$1,000,000 or more
- wide differences in the fees for investments in registered vs. unregistered hedge funds. Managers of unregistered hedge funds may receive both a management fee and a direct percentage in the profits earned.
- often engage in leveraging and other speculative investment practices that may increase the risk of investment loss
- can be highly illiquid
- are not required to provide periodic pricing or valuation information to investors
- may involve complex tax structures and delays in distributing important tax information
- are not subject to the same regulatory requirements as mutual funds
- often charge high fees to their direct investors

16.27 Exchange-Traded Funds (ETFs)

[SEC investor article: <http://www.sec.gov/answers/etf.htm>; FINRA Regulatory Notice 09-31; FINRA Non-Traditional ETFs FAQ: <https://www.finra.org/rules-guidance/key-topics/etf/non-traditional-etf-faq>; NASDAQ Rule 5705]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Descriptions of proposed ETF products to be sold• Transactions and proposed transactions in ETFs• Transaction reports• New account information
Frequency	<ul style="list-style-type: none">• Daily/As needed
Action	<ul style="list-style-type: none">○ Review for suitability of recommended ETFs, particularly non-traditional ETFs○ Consult with RRs, where appropriate, when non-traditional ETFs are sold to individual investors○ Include ETFs in training, particularly for non-traditional ETFs
Record	Order records including notation of action taken, if any

ETFs are open-end investment companies or unit investment trusts (UITs) listed on stock exchanges; they can be bought and sold throughout the trading day at the current market price. A typical ETF is based on specific domestic and foreign market indexes. An index-based ETF tracks the performance of an index by holding in its portfolio either securities replicating the index or a representative sample of the securities in the index. ETFs also

track non-traditional investments such as commodities and currencies. Some ETFs track indexes inversely (*i.e.*, the ETF rises when the index falls) and new ETFs are continually evolving.

Following are considerations when recommending ETFs:

- Purchasers must be provided with a prospectus or "product description." Some ETFs have obtained exemptive relief from the SEC allowing provision of a description instead of a prospectus.
- Purchasers of Portfolio Depository Receipts must be provided with a written description of the terms and characteristics of the securities, no later than the time a confirmation of the first transaction in such series is delivered to such purchaser. The description must also be included with any sales material provided to customers or the public. Any other written materials making specific reference to a series of Portfolio Depository Receipts as an investment vehicle must include a statement: "A circular describing the terms and characteristics of [the series of Portfolio Depository Receipts] has been prepared by [Trust name] and is available from your broker or NASDAQ. It is recommended that you obtain and review such circular before purchasing [the series of Portfolio Depository Receipts]. In addition, upon request you may obtain from your broker a prospectus for [the series of Portfolio Depository Receipts]." Non-NASDAQ members participating in an omnibus agreement are also subject to this obligation.
- Recommendations must consider what the ETF tracks to determine suitability for the proposed investor.
 - Where a commodity such as oil underlies the fund, it is important that the customer understands how the ETF is impacted by changes in price of the underlying commodity.
 - ETFs that track narrow sector or foreign market indexes can be highly concentrated and highly volatile or might fail to track their indexes properly. They also may have higher fees than ETFs based on broader indexes.
 - An ETF that invests in a sampling of the tracked index may not perform consistent with the index.
- Some ETFs sell short, others use leverage, and others use a combination of the two. Some ETFs are more complex financial instruments that offer leverage or are designed to perform inversely to the index or benchmark they track, or both. Leveraged ETFs amplify daily index moves; short selling provides the inverse daily return of market indexes. Targeted leverage levels don't necessarily meet targets over long periods due to compounding returns. Investors in these types of ETFs must be willing to assume higher risk.
- Some inverse ETFs track broad indices, some are sector-specific, and still others are linked to commodities or currencies.
- Most leveraged and inverse ETFs "reset" daily, meaning that they are designed to achieve their stated objectives on a daily basis. The effect of compounding affects their performance over longer periods of time when their performance can differ significantly from the underlying index or benchmark during the same time period. Volatile markets can magnify this effect. **The Firm does not permit the solicitation of leveraged and inverse ETFs to clients. The Firm permits sell orders, unsolicited buy orders, and buy orders in advisory accounts only.**
- ETFs are not suitable for a customer who wants to make regular periodic investments since each transaction will generate a commission cost. ETFs are more appropriate for larger lump-sum investments.
- Some ETFs allow investors to cash out their investment with the issuer.
- ETFs may be subject to temporary price disparities during times of highly volatile markets when ETF shares may trade for significantly less than the value of underlying assets. This risk is of particular concern to short-term traders.
- ETF shares can be sold short and bought on margin.

- For most ETFs, holdings are transparent, *i.e.*, an investor will know what is being held by the ETF by the makeup of the tracked index. However, in the case of an actively-managed ETF, knowledge of investments may not be available to investors.
- ETFs may have lower annual expenses than traditional funds; however, investors incur commission costs for each purchase and sale in the market.
- ETFs may be more tax efficient than regular mutual funds. Since shares are traded in the secondary market, the ETF is not required to liquidate its portfolio to satisfy fund sales and therefore reduces generation of capital gains distributions to investors that result in tax liabilities each year.
- ETFs do not offer dividend reinvestment plans which are available from regular mutual funds.
- Funds of ETFs (complete portfolios of multiple ETFs) may be considerably more expensive than buying the underlying ETFs directly.

16.27.1 Customer Disclosures for Pre- and Post-Market Sessions

[NASDAQ Rule 4631]

Prior to accepting a pre- or post-market session order in ETFs, the customer must be provided with the Extended Hours Trading Risk Disclosure that explains the trading risks associated with extended hours trading.

16.28 Floating-Rate Bank Loan Funds

Floating-rate loans, as opposed to typical debt offerings, are not issued by a firm directly to the public. Instead, banks and similar financial institutions extend loans to firms in need of raising capital and these loans are repackaged for sale to investors. Interest payments on the underlying loans are reset regularly to a reference rate such as LIBOR or the fed funds rate. Floating-rate loans often serve as an alternative method of financing for companies whose credit quality is rated below-investment-grade, or "junk."

RRs must consider and communicate the risks involved in investing in these funds when making recommendations to customers:

- These funds offer some protection from rising interest rates; however, the underlying loans may carry significant default and call risk.
- Interest payments will vary. In a failing interest scenario, returns of traditional bond funds increase while floating-rate funds may be stagnant or decrease.
- The funds may be difficult to value, have longer settlement times than other investments, and are relatively illiquid. Funds invested in these loans could face liquidity challenges when there are significant redemption requests.

16.29 Alternative Mutual Funds

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Funds proposed for sale • Order records
Frequency	<ul style="list-style-type: none"> • As required: review new funds • Ongoing: review orders • Annual or when new products are offered: training

Action	<ul style="list-style-type: none"> • Subject new alternative mutual funds to new product review • Review orders for suitability • Conduct training on alternative mutual funds
Record	<ul style="list-style-type: none"> • Review of new funds (see <i>New Products</i>) • Review of orders including action taken, if appropriate • Records of training

Alternative mutual funds typically employ investment tactics traditionally only found in hedge funds including the use of leverage, derivatives, and short selling. These funds allow investors to gain access to a wide range of traditionally exclusive hedge fund strategies including merger arbitrage, convertible arbitrage, long/short equity, macro trading, leverage, *etc.* They are marketed as a way for retail investors to invest in sophisticated, actively-managed hedge fund-like strategies that may perform well in a variety of market environments. Alternative mutual funds are also represented to reduce volatility, increase diversification, and produce non-correlated returns and higher yields compared to traditional long-only equity and fixed-income funds, all while offering daily liquidity. Alternative mutual funds typically involve non-traditional asset classes, non-traditional strategies or illiquid assets.

These funds have obvious differences and risks from conventional mutual funds. RRs must understand the strategy in which the fund's adviser will engage in various market scenarios. Acceptance of risk must be included in prospective investors' investment objectives.

17 OPTIONS

[FINRA Rule 2360]

This chapter outlines requirements when offering options to customers. Key requirements include the following:

- RRs and supervisors must be registered to sell and supervise options.
- Customers must submit an option agreement, and accounts must be approved for options trading levels.
- Writing uncovered options requires a separate disclosure and approval.
- Customers will be provided with a standard options disclosure document when option trading is approved.
- Customers are subject to position limits and methods of exercise disclosed in the agreement.
- Options communications require inclusion of the special risks associated with options.
- Compliance must approve discretionary accounts that will trade options.

17.1 Option Registration

[FINRA Rule 1220]

RRs must be qualified to engage in the sales of options contracts. Anyone who has successfully completed the Series 7 General Securities Representative examination is qualified to sell options.

RRs engaged in the sale of options are required to be supervised by a qualified Registered Options Principal (ROP). Supervisors are qualified as ROPs by passing prerequisite supervisor exams and the Registered Options Principal examination or by passing the General Securities Sales Supervisor (Series 10) examination.

17.2 Supervision of Option Activities

[FINRA Rule 1220(A)(8), 1220.03 and 2360(b)(20)]

ROPs are responsible for approval of accounts, review of transactions and communications, and other supervision required by rule.

Where secondary approval is required (discretionary accounts, accounts requesting trading levels where the customer does not meet minimum requirements, etc.), a qualified ROP in Compliance will review and approve such accounts.

17.3 Opening Option Accounts

[FINRA Rule 2360(b)(16)]

17.3.1 Option Agreements and Approval of Option Accounts

Responsibility	<ul style="list-style-type: none">• Registered Options Principal• Compliance
Resources	<ul style="list-style-type: none">• Customer Option Agreement• Order records• Daily Transaction Report
Frequency	<ul style="list-style-type: none">• Daily

Action	<ul style="list-style-type: none"> • Review option agreements and approve for appropriate trading level • Ensure option agreements are submitted for approval prior to the customer's first option transaction • Restrict accounts from further opening transactions where the customer's signed option agreement has not been received within 15 days of the first option transaction • Compliance: A qualified ROP will review accounts where the customer does not meet minimum criteria for the level of trading requested and approve or disapprove.
Record	<ul style="list-style-type: none"> • Customer's signed Option Agreement signed and dated by the approving supervisor • Records of providing option disclosure document • Records of providing uncovered short options disclosure • Compliance written justification if an account is approved for a level of trading for which the customer does not meet minimum criteria

Prior to the first option trade, a completed option agreement must be approved by a ROP or qualified sales supervisor (Series 10). In offices where no qualified supervisor resides, a local supervisor may approve the option account but a qualified supervisor must approve the account within 10 days of the local supervisor's approval.

RRs are responsible for obtaining the required information on CEI's customer option agreement. The customer must sign the option agreement confirming the information included on the form and agreeing to abide by the requirements included on CEI's agreement.

The customer's signed option agreement must be submitted to CEI within 15 days of approval. Failure to receive the customer's signed option agreement within 15 days will result in restricting the customer's account to closing option transactions until the agreement is received.

17.3.1.1 Levels of Option Trading

The following guidelines apply to accounts requesting approval to trade at various levels:

- Level 1 - Covered call writing: no minimum requirement
- Level 2 - Puts against long stock positions (married Puts), Put Writing Against Full Deposit of Strike Price (Covered Put): no minimum requirement
- Level 3 - Option Buying, Purchasing Put/Call Warrants: Income \$30,000; LNW \$25,000; NW \$50,000
- Level 4 - Spreads and combinations: Income \$50,000; LNW \$75,000; NW \$75,000; Options Experience 1 year
- Level 5 - Uncovered Put Writing vs. Buying Power: Income \$50,000; LNW \$200,000; NW \$200,000; Options Experience 1 year
- Level 6 - Uncovered Straddles, Uncovered call writing: Income \$100,000; LNW \$250,000; NW \$500,000; Options Experience 3 years

Accounts approved for these trading levels that do not meet the minimum criteria require the review and written notation by Compliance to explain why the account was approved for that level.

17.3.1.2 Requalifying an Account's Approved Option Levels

Responsibility	<ul style="list-style-type: none"> • ROP
Resources	<ul style="list-style-type: none"> • Customer Option Agreement
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review and approve (or disapprove) new option agreements that revise a customer's approved level of trading
Record	<ul style="list-style-type: none"> • Customer's Option Agreement signed and dated by the ROP • Copy of Customer Option Agreement retained in branch customer file and Firm's new accounts file

When a previously-approved option account is to be approved for a higher level of option, a new option agreement is required. The new agreement is to be approved by a ROP or qualified sales supervisor and sent to the customer for verification of account information on the form.

17.3.2 Uncovered Short Options

[FINRA Rule 2360(b)(11)(A)(ii) and 2360(b)(16)(E); FINRA Notice to Members 06-54]

Responsibility	<ul style="list-style-type: none"> • ROP • Compliance
Resources	<ul style="list-style-type: none"> • Customer Option Agreement • Special Statement for Uncovered Option Writers
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Compliance: For accounts not meeting minimum criteria for approval but submitted for approval, review and, if approved, a qualified ROP will document why the account is approved for uncovered short option trading • For accounts approved for uncovered short options, provide the Statement • When the Special Written Statement is revised, provide the revised copy to existing customers approved for uncovered short option trading before or with the confirmation of the next uncovered short option transaction
Record	<ul style="list-style-type: none"> • Copy of customer's acknowledgement of receiving the Statement retained in the customer file • Documentation of approving an account that does not meet minimum criteria is included with option account approval documentation

All accounts that are approved for uncovered short options will be provided with the Special Statement for Uncovered Option Writers ("Statement") before or with the confirmation of the first uncovered short option transaction. If the Statement is revised, the revised version will be provided before or with the confirmation of the next uncovered short option transaction.

Following are the minimum criteria for approval of an account to trade uncovered options:

- 3 years of experience trading options
- Minimum net equity of \$25,000
- Minimum maintenance in the account of \$25,000

If the account does not meet the above criteria and the account wishes to trade uncovered short options, Compliance review and approval is required.

17.3.3 Option Disclosure Document (ODD)

[FINRA Rule 2360(b)(11)(A)]

All customers will be provided the required disclosure document at or prior to the time the account is approved for option trading. The Option Account Agreement form includes an attestation by the client that he/she has received and read the ODD, and the date it was delivered.

In addition, whenever the disclosure document is revised, a revised copy will be provided to customers no later than the time of delivery of a confirmation of a transaction in a category of option the subject of a revision.

17.3.3.1 Options Communications: Hyperlink Delivery of the ODD

[SEC Securities Exchange Act of 1934 Release No. 39356 dated November 25 1997; FINRA Notice to Members 98-03]

- Communications that contain clear and prominent hyperlinks to the ODD are considered to have been preceded or accompanied by the ODD.
- The ODD may be delivered via hyperlink to that document if the customer has consented to receive documents electronically from CEI.

17.3.4 Fiduciary Accounts

Compliance will review trusts, pension plans, and other fiduciary accounts to determine whether options transactions are permitted in the document (trust agreement, *etc.*) governing the account.

17.4 Option Orders

17.4.1 Suitability of Option Transactions

[FINRA Rule 2360(b)(19)]

When recommending opening option transactions, RRs should have a reasonable basis for believing the customer has the knowledge and experience in financial matters that he/she may be reasonably expected to be capable of evaluating the risks of the recommended transaction, and financially able to bear the risks of the recommended position. Suitability determinations are based on the information provided by the customer including the RR's understanding of the customer's ability to evaluate the risk and financial ability to bear the risk.

Suitability is only one element of acting in a customer's best interest. Recommendations to retail customers who are natural persons are subject to Regulation Best Interest (BI) which is broader than the suitability requirement.

Reg BI includes recommendations for orders; types of accounts; and investment strategies, including recommendations to prospects. It is important to be familiar with those requirements which are included in the chapter *REGULATION BEST INTEREST (BI)*.

17.4.2 Orders Requiring Prior Approval

Responsibility	<ul style="list-style-type: none"> • ROP
Resources	<ul style="list-style-type: none"> • Order records • Daily Transaction Report
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Approve (<i>or disapprove</i>) orders requiring prior approval • Identify orders not previously approved as required • Remind wire operator or other order entry person of requirement • Remind RR that order required prior approval
Record	<ul style="list-style-type: none"> • Initials on order records • Initials on Daily Transaction Reports

The following option transactions require the approval of the designated supervisor prior to entry:

- Opening spread transactions greater than 100 contracts in each position

17.4.3 Review of Option Orders and Accounts

[FINRA Rule 2360(b)(20)(C)]

Responsibility	<ul style="list-style-type: none"> • ROP
Resources	<ul style="list-style-type: none"> • Order records • Daily Transaction Report • Customer monthly transaction records • Option Agreements • Other available reports
Frequency	<ul style="list-style-type: none"> • Daily (order records, Daily Transaction Report) • Periodically (customer monthly transaction records)
Action	<ul style="list-style-type: none"> • Review for completeness of orders (open or close, put or call, <i>etc.</i>) • Review for orders requiring prior approval and prohibited transactions • Review daily transactions and customer monthly statements for suitability of option transactions, including the following: <ul style="list-style-type: none"> ○ Compatibility of option transactions with investment objectives and approved trading levels

	<ul style="list-style-type: none"> ○ Size and frequency of option transactions ○ Commission activity ○ Profit or loss in the account ○ Undue concentration in any options class or classes ○ Compliance with Reg T ● Take corrective action which may include consulting with the RR and/or Compliance, requalifying an option account, canceling the order, education for the RR, or other appropriate action
Record	<ul style="list-style-type: none"> ● Initials on order records, Daily Transaction report, and monthly transaction records ● Supervisor's log or other record recording review of accounts

The designated supervisor is responsible for review of option orders to identify transactions inconsistent with policy requirements including incomplete orders and transactions that appear to be unsuitable for the customer. Supervisory offices will have available (electronically or in hard copy) records enabling review of option accounts.

17.4.3.1 Accounts Trading Outside Approved Levels

Responsibility	<ul style="list-style-type: none"> ● ROP
Resources	<ul style="list-style-type: none"> ● Customer Option Agreement ● Order records ● Daily Transaction Report
Frequency	<ul style="list-style-type: none"> ● Daily
Action	<ul style="list-style-type: none"> ● If a customer is trading outside the approved level on the customer's option agreement: ● Confer with the RR regarding whether the customer's trading level should be amended ● If yes, require a new option agreement from the customer and review for higher level of trading ● If no, immediately inform the RR trading outside approved levels must cease ● Consider contacting the customer to determine whether the violative transaction should be canceled, and cancel if appropriate
Record	<ul style="list-style-type: none"> ● Initials on order records and Daily Transaction report ● Notes of action taken on Daily Transaction Report or supervisory log or other written record

CEI has established procedures to identify accounts that trade outside approved option levels. RRs may be required to complete a new option agreement to re-qualify the customer or orders may be canceled if deemed inappropriate for the customer.

17.4.4 Prohibited Trading to Evade Short-Sale Requirements

[SEC Risk Alert: <http://www.sec.gov/about/offices/ocie/options-trading-risk-alert.pdf>]

Responsibility	<ul style="list-style-type: none"> • ROP
Resources	<ul style="list-style-type: none"> • Option transaction reports
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Review option transactions for indicators of attempts to circumvent Regulation SHO: <ul style="list-style-type: none"> ○ Trading exclusively or excessively in hard-to-borrow securities or threshold list securities, or in near-term listed options on such securities ○ Large short positions in hard-to-borrow securities or threshold list securities ○ Large failure to deliver positions in an account, often in multiple securities ○ Continuous failure to deliver positions ○ Using buy-writes, married puts or both, particularly deep in-the-money buy-writes or married puts, to satisfy the close-out requirement ○ Using buy-writes with little to no open interest aside from that trader's activity, resulting in all or nearly all of the call options being assigned ○ Trading in customizable Flexible Exchange (FLEX) Options in hard-to-borrow securities or threshold list securities, particularly very short-term FLEX Options ○ Purported market makers trading in hard-to-borrow or threshold list securities claiming the exception from the locate requirement of Regulation SHO (often these traders do not make markets in these securities, but instead effect trades only to take advantage of the option mispricing) ○ Multiple large trades with the same trader acting as a contra party in several hard-to-borrow or threshold list securities (often traders assist each other to avoid having to deliver shares) • If potential violations are identified, take corrective action which may include consulting with the trader, RR, and/or customer; reversing the transaction; closing the account or restricting dealing with another firm's trader engaged in such activity; consulting with Compliance
Record	<ul style="list-style-type: none"> • Record of transaction reviews, questionable trades, and action taken

Regulation SHO governs short sales to ensure that trades settle promptly, reducing settlement failures. Short sellers who fail to deliver securities are required to close out their position immediately, unless an exception applies. Some options trading strategies have been used to evade those requirements, particularly in hard-to-borrow securities.

Option strategies to circumvent Regulation SHO requirements are prohibited.

17.4.5 Prohibited Transactions

[FINRA Rule 2360(b)(13) and 2360(b)(14)]

The following transaction(s) is/are not permitted:

- Option rules prohibit the entering of a transaction for the sale (writing) of a call option contract for an account of any corporation which is the issuer of the underlying security.
- An opening covered short position in a call option contract may not be established if the underlying stock is restricted and not free to sell.

17.4.6 Disclosure of Option Order Routing

[SEC Regulation NMS Rule 606]

CEI is obligated to publish statistics regarding customer agency orders in options. Procedures for publishing the required information are detailed in the chapter *ORDERS* in the section *Disclosure Of Order Routing*.

17.5 Option Operations Procedures

This section describes some of the operations procedures relating to options. The Operations Department is responsible for these areas.

17.5.1 Reporting Positions

[FINRA Rule 2360(b)(5)]

The designated operations supervisor is responsible for reporting option positions in accordance with SRO requirements.

When CEI is not a member of the options exchange upon which the standardized options are listed and traded, CEI is required to file a report with FINRA regarding the following accounts which have established an aggregate position of 200 or more option contracts (whether long or short) of the put class and the call class on the same side of the market covering the same underlying security or index:

- each account in which CEI has an interest
- each account of a partner, officer, director or employee of CEI
- each customer, non-member broker, or non-member dealer account

Reporting combines long positions in put options with short positions in call options and short positions in put options with long positions in call options.

17.5.2 Position Limits

[FINRA Rule 2360(b)(3)]

Customers are subject to limits on how many contracts may be accumulated in a particular option at any one time. Total positions include all accounts under "common control" by one party. An example of common control would be a registered investment adviser who manages multiple accounts and establishes option positions in accounts under the adviser's management. Position limits also include accounts "acting in concert" to accumulate a position. CEI (or its clearing firm or other firm executing transactions on its behalf) has systems to prevent entry of orders that would violate position limits.

Some qualified hedge strategies and positions are exempt from position limits, including a delta hedging exemption for FINRA members and non-member affiliates. The designated supervisor is responsible for applying the Permitted Pricing Model to all positions in or relating to the security underlying the relevant options position that are owned or controlled by such member or non-member affiliate and providing FINRA with written certification that CEI or its affiliate are using the Permitted Pricing Model and that the affiliate will provide immediate notice to CEI if it ceases to hedge stock positions; CEI is responsible for carrying all option positions relying on the exemption.. CEI is responsible for reporting any positions. [FINRA Rule 2360(b)(A)(vii)]

The designated operations supervisor is responsible for identifying positions that exceed allowable limits under SRO rules. When a position limit violation is identified, the SRO will be notified as required by rule and the customer will be notified and asked to reduce the position to within the permitted levels.

17.5.3 Liquidation of Positions and Restrictions on Access

[FINRA Rule 2360(b)(6)]

When FINRA determines that a person or group of persons acting in concert holds or controls, or is obligated in respect of, an aggregate position in option contracts covering any underlying security or index in excess of position limits, it may direct a member or all members carrying a position in option contracts covering such underlying security or index for such person or persons to liquidate such position or positions, or portions thereof, as expeditiously as possible and consistent with the maintenance of an orderly market, to bring such person or persons into compliance with the position limits. When directed by FINRA, CEI will liquidate positions and will not permit such person or persons to execute an opening transaction and will not accept and/or execute for any person or persons named in such directive, any order for an opening transaction in any option contract, unless in each instance express approval is given by FINRA, the directive is rescinded, or the directive specifies another restriction appropriate under the circumstances.

FINRA will notify the subject person or persons who have the right to appeal the decision.

17.5.4 Exercise of Options

[FINRA Rule 2360(b)(4) and 2360(b)(23)(A)(ii) (vi) and (ix)]

The exercise of options is subject to regulatory rules; the method used for exercising options is disclosed on CEI's option agreement.

The following records will be retained by the designated supervisor regarding exercise of options:

- Memorandums of exercise instructions received from customers showing the time the instruction was received
- Memorandum if CEI receives and acts on exercise instructions after set cut-off times because of some unusual circumstances (including the details explaining the exception), as required under option rules

The designated supervisor is responsible for ensuring the exercise of options does not exceed limitations specified in options rules. If CEI has reason to believe someone acting alone or in concert with others has exceeded or is attempting to exceed position or exercise limits, CEI will promptly contact FINRA.

The exercise cut-off is established by regulators or CEI may establish an earlier time which is communicated to customers trading options. Exercise instructions will not be accepted after the cut-off time. Submission of exercise instructions may be submitted electronically in which case the instructions will include an electronic record of the time it is submitted to comply with the cut-off time. If not submitted electronically, a manual record will be

maintained of the time when the exercise instructions are submitted. Mistakes or errors in submitted exercise instructions will be reviewed and resolved by Operations (at CEI or its clearing firm).

17.5.4.1 Tendering Procedures

[FINRA Rule 2360(b)(A)(ii) (vi) and (ix)]

Special procedures apply to the exercise of standardized equity options on the last business day before their expiration ("expiring options"). Unless waived by The Options Clearing Corporation, expiring standardized equity options are subject to the Exercise-by-Exception ("Ex-by-Ex") procedure under The Options Clearing Corporation Rule 805. This Rule provides that, unless contrary instructions are given, standardized equity option contracts that are in-the-money by specified amounts are automatically exercised. In addition to The Options Clearing Corporation rules, the following FINRA requirements apply with respect to expiring standardized equity options. Option holders desiring to exercise or not exercise expiring standardized equity options must either:

- take no action and allow exercise determinations to be made in accordance with The Options Clearing Corporation's Ex-by-Ex procedure where applicable; or
- submit a "Contrary Exercise Advice" by the deadline.

For both customer and proprietary positions (as well as positions of other firms where CEI has accepted responsibility to exercise options), CEI is responsible for confirming that final exercise decisions are properly indicated to the relevant national options exchange with respect to such positions. CEI may establish a cut-off time prior to FINRA's specified cut-off.

The filing of a final exercise decision, exercise instruction, exercise advice, Contrary Exercise Advice or Advice Cancel does not serve as a substitute to the effective notice required to be submitted to The Options Clearing Corporation for the exercise or non-exercise of expiring standardized equity options.

17.5.5 Adjustments in Terms of Options

The number of shares underlying an option contract and/or the exercise price are subject to adjustments by the Options Clearing Corporation when the underlying shares are subject to dividends (other than cash dividends), distributions, stock splits, recapitalization, or reorganization. Branches are notified and RRs should advise customers who hold option positions in the affected security.

17.5.6 Branch Copies of Account Information and Statements

[FINRA Rule 2360(b)(17)(B)]

For all accounts trading options, each branch office servicing the account and the principal supervisory office having jurisdiction over the branch office will retain copies of background and financial information for approved options accounts and customer statements for the prior 6 months. These records may be in electronic format if readily accessible and promptly retrievable.

17.6 Option Complaints

[FINRA Rule 2360(b)(17)(A)]

Responsibility	<ul style="list-style-type: none"> • Designated Branch Supervisor • Compliance
Resources	<ul style="list-style-type: none"> • Incoming correspondence

	<ul style="list-style-type: none"> • Written complaints
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Immediately provide the original of any written complaint to Compliance • Retain a copy of the complaint for branch files • Compliance (<i>in consultation with the branch manager</i>) will respond to the complaint
Record	<ul style="list-style-type: none"> • Copy filed in branch Option Complaints file • For branch offices that report to an OSJ in another location, the OSJ will retain copies of complaints for branch offices under their supervision • Compliance retains CEI's central complaint files including: <ul style="list-style-type: none"> ○ identification of complainant; ○ date complaint received; ○ identification of RR servicing the account; ○ general description of the matter complained of; and ○ a record of what action, if any, was taken with respect to the complaint

RRs are required to notify their supervisor when a complaint is received. All written option complaints are to be forwarded to Compliance immediately upon receipt.

17.7 Option Communications with the Public

[FINRA Rule 2210 and 2220]

Requirements for options communications (including electronic communications) include the following, which are explained in more detail below:

- The rules governing retail communications, institutional communications and correspondence apply to options communications. Refer to the chapter *COMMUNICATIONS WITH THE PUBLIC* for more information about these policies.
- Retail communications (communications distributed to more than 25 retail investors) require supervisory approval **prior to** distribution.
- Institutional communications (for institutions only) do not require prior approval and are subject to review consistent with correspondence reviews (see the chapter *COMMUNICATIONS WITH THE PUBLIC*). Institutional communications require review by the designated supervisor.
- All options communications (other than institutional communications) must include a statement that supporting documentation for any claims (including claims on behalf of options programs or the options expertise of sales persons); comparisons; recommendations; statistics; or other technical data, will be supplied upon request.
- All advertising requires Compliance approval **prior to** publication.

17.7.1 Definitions

Retail investor: includes any person other than an institutional investor, regardless of whether the person has an account with CEI.

Institutional investor: See the definition in the chapter *COMMUNICATIONS WITH THE PUBLIC*.

Retail communication: includes **any** written communication (including advertising, telemarketing and other sales scripts and other written communications) that is published, distributed or made available to **more than 25** retail investors within any 30 calendar-day period.

Institutional communication: includes written communications that are distributed or made available only to institutional investors.

Correspondence: Includes any written communication that is distributed or made available to **25 or fewer** retail investors within any 30 calendar-day period.

Options [FINRA Rule 2360(a)(20)]: Any put, call, straddle or other option or privilege, which is a "security" as defined in Section 2(1) of the Securities Act of 1933 but not including any tender offer, registered warrant, right, convertible security or any other option in respect to which the writer is the issuer of the security which may be purchased or sold upon the exercise of the option.

Options Disclosure Document (ODD) [FINRA Rule 2360(a)(12)]: The options-market document containing explanatory information relating to the mechanics of buying, writing and exercising options; the risks involved; and other required information about options. The ODD must be provided to all options customers and provided with certain options communications.

Public appearance: Any participation in a seminar, forum (including an interactive electronic forum), radio, television or print media interview, or other public speaking activity, or the writing of a print media article, concerning options.

Standardized Option: Any options contract issued, or subject to issuance, by The Options Clearing Corporation, that has standardized terms for the strike price, expiration date, and amount of the underlying security, and is traded on a national securities exchange registered pursuant to section 6(a) of the Securities Act.

17.7.2 Option Content Standards

- All options communications (other than institutional communications) must include a statement that supporting documentation for any claims (including claims on behalf of options programs or the options expertise of sales persons); comparisons; recommendations; statistics; or other technical data, will be supplied upon request.
- All options communications (other than institutional communications) must include a statement that options are not suitable for all investors.
- Communications including historical and/or performance figures or projections must be preceded or accompanied by the Options Disclosure Document (ODD). For historical performance projections, specific guidelines apply [see FINRA Rule 2220(d)(3) and (4)].

17.7.3 Correspondence and Retail Communications

Responsibility	<ul style="list-style-type: none">• Designated Branch Supervisor
Resources	<ul style="list-style-type: none">• Correspondence and retail communications
Frequency	<ul style="list-style-type: none">• Daily

Action	<ul style="list-style-type: none"> Review to ensure appropriate language and options disclosure document is provided including the required content statement
Record	<ul style="list-style-type: none"> Record of review including any changes required

All communications (written or electronic) are subject to the general requirements of truthfulness and avoidance of language that includes promises of specific results, exaggerated or unwarranted claims. Written communications should avoid hedge clauses which disclaim responsibility for the content of such literature or for opinions included or which are inconsistent with the communication. Statements suggesting the certain availability of a secondary market for options may not be made.

Written communications regarding options should include the following:

- special risks of options and the complexities of certain strategies
- a statement that options are not suitable for all investors
- statements referring to potential opportunities should be balanced by a statement of corresponding risks

Written communications, other than advertising that meets the requirements of SEC Rule 134, must be preceded or accompanied by the options disclosure document.

17.7.4 Communications Regarding Standardized Options Prior to Delivery of the ODD

Prior to providing the ODD, communications are limited to a brief description of options including a statement that identifies the registered clearing agency for options and a brief description of the general attributes and method of operation of the option exchanges including a discussion of how an option is priced. Such pre-ODD communications must include contact information for obtaining a copy of the ODD and must not contain recommendations or past or projected performance figures including annualized rates of return or the names of specific securities. They may include statements required by state law and administrative authority and may include advertising designs and devices, providing such material is not misleading.

17.7.5 Seminars and Public Presentations

Responsibility	<ul style="list-style-type: none"> Designated Branch Supervisor Compliance
Resources	<ul style="list-style-type: none"> Outlines for proposed seminars or public presentations that include options including sales material to be distributed Tapes of radio, TV, newspaper articles, or other public media presentations
Frequency	<ul style="list-style-type: none"> As required
Action	<ul style="list-style-type: none"> Designated Supervisor: review presentation and related sales materials and refer to Compliance for review and approval Compliance: <ul style="list-style-type: none"> ○ Pre-approve radio, TV, newspaper or other public media presentation

	<ul style="list-style-type: none"> ○ Review seminars or other presentations and sales material; approve or disapprove
Record	<ul style="list-style-type: none"> • Compliance: record of presentation and sales material; copies of written materials or tapes of public media presentations; approval/disapproval • Designated Supervisor: <ul style="list-style-type: none"> ○ Copy of presentation and written sales material provided to attendees ○ Record of approval/disapproval ○ List of attendees ○ Confirmation that attendees were provided options disclosure documents

Prior to conducting a seminar or other public presentation regarding options, the outline of the presentation must be provided to the designated supervisor for review. Seminar scripts, handouts, slides, or other visual presentations must be pre-approved and are deemed to be retail communications. All who attend the public presentation should be provided the current options disclosure document. A list of those who attended and received the disclosure document should be prepared and include the date of the meeting.

Appearances in public media (radio, TV, newspapers, other) require the prior approval of Compliance and copies of written material or tapes of the presentation must be provided to Compliance including where published/presented and the type of media (name of newspaper, radio/TV station, other) and date of the appearance or publication.

17.7.6 Filing Requirements

[FINRA Rule 2220(c)]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Proposed communications subject to filing
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review communication and make necessary changes • Submit communication to FINRA for approval at least 10 calendar days prior to first use • Communicate approval or disapproval to originator of the communication
Record	<ul style="list-style-type: none"> • Copies of communications with FINRA approval/disapproval and contact with originator regarding permissible use or restriction on use

Communications that are likely to be widely disseminated such as advertisements and independently prepared reprints are subject to filing with FINRA at least ten calendar days prior to use. If changed or disapproved by FINRA, the originator of the communication will be notified, and the communication will be withheld from distribution until resubmitted to FINRA and approved by them.

Filing with FINRA is not required:

- if the communication is filed with another regulator with standards comparable to FINRA
- for communications which only reference that options are available from CEI
- for the ODD and prospectus
- for targeted communications (such as correspondence) used once the ODD or prospectus has been delivered

17.8 OTC Options (Non-Standardized Options)

ROP approval is required prior to writing OTC non-standardized options. Margin requirements may vary from standardized options.

18 MUNICIPAL SECURITIES

This chapter describes requirements that apply to municipal securities. Rule references (*i.e.*, G-3) refer to Municipal Securities Rulemaking Board (MSRB) rules, unless otherwise noted.

18.1 Administration and Operations

18.1.1 Fees and Assessments

[MSRB Rule A-12, A-13 and A-7]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Data regarding inter-dealer sales transactions in municipal securities and municipal underwriting activity (MSRB Rule A-13)• MSRB Rule A-14 regarding annual fee
Frequency	<ul style="list-style-type: none">• Inter-dealer transactions and underwriting assessments as required• Annual fee - annually by October 31
Action	<ul style="list-style-type: none">• Calculate and pay inter-dealer transaction and underwriting assessment fees• Pay annual fee for receipt by the MSRB by October 31
Record	<ul style="list-style-type: none">• Records of all assessment and fee payments are retained in files by respective subject.

The designated supervisor is responsible for reporting required information and paying assessment fees to the MSRB. The designated supervisor is also responsible for paying the annual fee to the MSRB.

18.1.2 Registration Requirements

[MSRB Rule G-3]

Employees engaged in municipal activities must be registered as outlined in this section. References to "sales" also include the solicitation of sales to and/or purchases from customers.

18.1.3 Municipal Securities Representatives

[MSRB Rule G-3]

Municipal Securities Representatives qualify by completing the Series 52 examination and may engage in a wide range of transactions in municipal securities including sales, trading, underwriting, and other non-supervisory municipal activities.

18.1.4 Limited Representatives

[MSRB Rule G-3]

Municipal Securities Sales Limited Representatives are limited exclusively to handling customer sales and purchases of municipal securities. The term "limited representative - investment company and variable contracts

products" means a municipal securities representative limited exclusively to the sale and purchase of municipal fund securities. Limited representatives may not engage in other municipal activities such as trading or underwriting. For offices where RRs are qualified as Limited Representatives, the designated supervisor is responsible for determining that those RRs do not exceed the limited activities permitted under this registration status.

The Series 7 examination qualifies a Municipal Securities Sales Limited Representative.

The Series 6 examination qualifies an Investment Company/Variable Contracts Limited Representative.

18.1.5 Apprentices

[MSRB Rule G-3]

Individuals who have not previously qualified as municipal securities representatives are required to complete a 90-day "apprenticeship" period during which the individual is prohibited from soliciting or transacting business with the public. This includes a prohibition against soliciting new accounts on behalf of CEI. In addition, apprentices may not be compensated from transactions in municipal securities.

The designated supervisor to whom the apprentice reports is responsible for ensuring apprentices do not solicit or transact business with the public. Compensation to the apprentice will not include remuneration from transactions in municipal securities.

18.1.6 Municipal Securities Sales Supervisors

[MSRB Rule G-3]

Individuals who complete the Series 8 General Securities Sales Supervisor examination are qualified as municipal securities sales supervisors. Supervision is limited to sales of municipal securities to customers.

18.1.7 Municipal Securities Principals

[MSRB Rule G-3]

The Series 53 examination qualifies individuals for the registration status of municipal securities principal which permits the individual to supervise all aspects of CEI's municipal business. Qualified municipal principals will be designated to supervise the areas of underwriting, trading, and pricing of inventories.

18.1.8 General Securities Principals (Series 24)

[MSRB Notice 2011-62]

Individuals with General Securities Principal (Series 24 examination) qualification are limited in what municipal securities activities they may supervise. Those qualified as a General Securities Principal are limited to supervising books and records [G-27(c)(i)(E)], review and approval of the opening of customer accounts [G-27(c)(i)(G)(1)], oversee the gathering of information on associated persons [G-7(b)], and approval of advertising [G-21(f)]. A General Securities Principal may not supervise and review customer transactions, handling customer complaints, or correspondence related to municipal securities. He/she also may not supervise the processing of municipal securities transactions including trade reporting to the MSRB.

18.1.9 Non-Registered Employees

[MSRB Rule G-3 and G-3.03]

Employees who are not registered are limited to clerical and ministerial functions when contacting public customers including:

- the recording and transmission of orders through normal channels;
- the reading of approved quotations; and,
- the giving of reports of transactions.

Non-registered employees, including apprentices, are not permitted to solicit new accounts on behalf of CEI. The designated supervisor to whom the non-registered employee reports is responsible for reasonably ensuring the employee does not exceed the limitations listed above.

18.1.10 Continuing Education (CE)

[MSRB Rule G-3(i)]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Employee records of those engaged in municipal activities • Commission/revenue records of municipal activities
Frequency	<ul style="list-style-type: none"> • Annually: identify those subject to CE • Annually: develop continuing education to be administered • Annually: conduct training
Action	<ul style="list-style-type: none"> • Identify employees subject to the requirement (and those engaged in municipal activities so limited as not to warrant CE training) • Develop CE subjects to be included in training • Conduct training sessions for those subject to the requirements • Restrict activities of those failing to meet the annual requirement; restrictions may include ceasing conduct of business with the public or ceasing other municipal activities
Record	<ul style="list-style-type: none"> • Record of subject employees • Record of employees engaged in limited activities excluded from requirement • Annual CE training program including subjects covered • Record of employees completing CE training • Record of limiting activities for those who do not complete requirements

Employees (including RRs and supervisors) who engage in municipal securities activities are subject to annual Firm Element continuing education on municipal securities. Compliance will notify those employees subject to CE training. This includes anyone engaged in the following municipal activities (except on an infrequent or *de minimis* basis):

- Sales to customers
- Trading
- Financial advisor
- Underwriting

18.1.11 Offices

[MSRB Rule G-27(b)(iii) and G-27(g)]

Compliance is responsible for identifying offices, where municipal business is conducted, and identifying designated supervisors. Designations are included in the chapter *DESIGNATION OF SUPERVISORS AND OFFICES*. The designation of supervisors will consider the following:

- Retail sales or other activities involving public contact with respect to municipal securities
- A substantial number of RRs conduct municipal securities activities at, or are otherwise supervised from, the location
- The location is geographically distant from another municipal OSJ
- RRs are geographically dispersed
- Municipal activities at a location are diverse and/or complex

Office designations include offices of municipal supervisory jurisdiction, branch offices, and other offices as defined in the Rule. MSRB rule definitions track FINRA's office definitions; refer to the chapter *OFFICES* for detailed information about types of offices.

18.1.12 Notifications To MSRB

Compliance will notify the MSRB in writing if CEI ceases to engage in business activities either voluntarily or because of being barred or suspended by a regulator from engaging in securities activities.

Compliance will also promptly notify the MSRB of any change in name or address.

18.1.13 Annual Notifications to Customers

On an annual basis the Firm will provide written or electronic notice to customers including the following:

- the Firm is registered with the SEC and the MSRB;
- the MSRB's website address; and
- a statement about the availability of a brochure available on the MSRB's website describing protections provided by MSRB rules and how to file a complaint with the appropriate regulatory authority.

"Customer" (not limited solely to those customers holding or trading municipal securities) includes any person other than a broker, dealer, or municipal securities dealer acting in its capacity as such or an issuer in transactions involving the sale by the issuer of a new issue of its securities (MSRB Rule D-9). In addition, retail customers, institutional customers and customers that invest in 529 Savings Plans will receive the notice.

18.1.14 Anti-Money Laundering Program

[MSRB Rule G-41]

CEI has established an anti-money laundering program which is described in the chapter *ANTI-MONEY LAUNDERING*.

18.1.15 Fidelity Bonding Requirements

[MSRB Rule G-6]

The designated supervisor is responsible for arranging, maintaining, and verifying the adequacy of appropriate fidelity bond coverage.

18.1.16 Books and Records

[MSRB Rule G-8 and G-9]

CEI complies with MSRB Rules G-8 and G-9 by maintaining and preserving records in accordance with '34 Act Rules 17a-3 and 17a-4 [see MSRB Rule G-8(f) and Rule G-9(g)]. In addition, CEI maintains municipal records specifically identified in G-8 subparagraph (a)(iv)(D); paragraph (a)(viii); and paragraphs (a)(xi) through (a)(xxii).

Procedures on books and records are included in the chapter *FINANCIAL AND OPERATIONS PROCEDURES*.

18.1.17 Confirmations

[MSRB Rule G-15; MSRB Notice 2018-05]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Confirmations or available reports
Frequency	<ul style="list-style-type: none">• Monthly
Action	<ul style="list-style-type: none">• Review a sampling of confirmations to determine whether required information is included• Where omissions are found:<ul style="list-style-type: none">○ Have corrected confirmations issued○ Confirm whether the problem is systemic or human error○ If systemic, contact the appropriate supervisor to make corrections to the system○ If human error, notify the person responsible of the problem and provide added training, if necessary• If CEI relies on its clearing firm to issue confirmations, contact the appropriate person at the clearing firm to issue correct confirmations and to correct the problem
Record	<ul style="list-style-type: none">• Review of confirmations including notation of omissions found, corrective action taken• If a clearing firm is involved, documentation of who was contacted and what corrective action will be taken

The designated supervisor is responsible for establishing procedures regarding the preparation and transmission of customer confirmations, including information required under MSRB Rule G-15.

18.1.18 Control Relationships

[MSRB Rule G-22]

A "control relationship" exists when CEI controls, or is controlled by, or is under common control with the issuer of a municipal security or a person (other than the issuer) who is obligated, directly or indirectly, with respect to debt service on the municipal security.

Where a control relationship exists, CEI will provide disclosure to any customer who effects a transaction in the subject municipal security prior to effecting the transaction. Written disclosure will be provided before or at the time the transaction is confirmed to the customer. In the case of a new issue of municipal securities, disclosure will be made in the official statement. In the case of other transactions, disclosure will be included on the customer confirmation or by separate written disclosure included with the confirmation.

In addition, for discretionary accounts, discretion may not be exercised for a transaction in a security subject to a control relationship. The customer must specifically authorize the transaction before it is entered.

18.1.19 Disclosure of Interest in Distribution

[SEC Securities Exchange Act of 1934 Rule 15c1-6]

Rule 15c1-6 of the Securities Exchange Act of 1934 specifies requirements for disclosures when CEI is involved in a primary or secondary distribution of municipal securities. CEI will provide the required disclosure on or with the customer's confirmation of a transaction in the subject securities.

18.1.20 Reciprocal Dealings

[MSRB Rule G-31]

CEI and its employees are prohibited from soliciting municipal transactions from accounts for investment companies in return for sales of shares in the investment company.

18.1.21 Use of Ownership Information

[MSRB Rule G-24]

CEI 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. CEI 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.

18.1.22 Customer Account Transfers

[MSRB Rule G-26]

18.1.22.1 Transferring Firm Accounts to Another Firm

When a customer wishes to transfer an entire account to another broker-dealer and presents a properly-executed transfer notification, the account will be transferred in accordance with the requirements of MSRB Rule G-26 and other regulators' applicable requirements either by CEI or a clearing firm, if applicable.

18.1.22.2 Transferring an Account from Another Firm

For transfers to CEI from another broker-dealer, operations personnel should be consulted for instructions on completing transfer instructions which will be submitted to the carrying broker-dealer.

18.1.23 Transactions for Employees of Other Municipal Dealers

[MSRB Rule G-28]

When an account is opened for the employee of another municipal dealer, CEI is obligated to notify the other dealer, in writing, and send confirmations and statements to the other dealer. The RR is responsible for

identifying on new account documentation that the customer is employed by another broker-dealer. The RR is responsible for sending written notice to the other firm and coding the account for duplicate confirmations and statements to the other firm.

This requirement does not apply if the account for the employee of the other municipal dealer is limited to transactions in municipal fund securities.

18.1.24 Written Supervisory Procedures

[MSRB Rule G-27(c)]

CEI has established and maintains written supervisory procedures including regular review for changes and updates. Procedures regarding the review, maintenance, and updating of written procedures are included in the chapter *SUPERVISORY SYSTEM, CONTROLS AND PROCEDURES*.

18.1.25 Contact Information

[MSRB Rule A-12]

On an annual basis, Compliance will affirm contact information electronically on Form A-12 regarding the following contact persons:

- Primary regulatory contact (must be a registered municipal principal)
- Master account administrator
- Billing contact
- Compliance contact
- Primary data quality contact

Changes will be filed within 30 days of information becoming inaccurate. CEI may, at its discretion, also provide one or more of the following contacts: optional regulatory contact; data quality contact; or technical contact. Compliance is responsible for making the required filings and retaining records of contact information and filings.

18.1.26 Compliance with Regulatory Requests

[MSRB Rule A-12(h)]

Compliance will respond to regulatory requests for information within 15 days (or a longer agreed-upon period).

18.2 Sales of Municipal Securities

[MSRB Notice 2009-42; FINRA Regulatory Notice 09-35]

This section outlines requirements when selling municipal securities, particularly to retail customers.

18.2.1 Conduct of Municipal Securities Business

[MSRB Rule G-17; MSRB Notice 2007-17]

It is CEI's policy to deal fairly with all persons. Deceptive, dishonest, or unfair practices are prohibited.

18.2.2 Suitability

[MSRB Rule G-19 and G-48; MSRB Notice 2020-13 and 2010-37; FINRA Regulatory Notice 10-41]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Daily Transaction Report • Customer Monthly Statements
Frequency	<ul style="list-style-type: none"> • Daily (order tickets and Daily Transaction Report) • Semi-annually (Customer Monthly Statements)
Action	<ul style="list-style-type: none"> • Review municipal transactions for suitability with particular consideration of: <ul style="list-style-type: none"> ○ Non-rated issues ○ Long-term bonds [>10 years to maturity] ○ Regulation BI Requirements
Record	<ul style="list-style-type: none"> • Initials on order records and Daily Transaction Report

RRs 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. Changes to customer suitability information should be made by amending existing new account information or submitting a new form.

RRs are required to have a reasonable basis to believe recommendations are suitable based both on information available from the issuer and on the facts disclosed or otherwise known about the customer.

Suitability is only one element of acting in a customer's best interest. Recommendations to retail customers who are natural persons are subject to Regulation Best Interest (BI) which is broader than the suitability requirement. Reg BI includes recommendations for orders; types of accounts; and investment strategies, including recommendations to prospects. It is important to be familiar with those requirements which are included in the chapter *REGULATION BEST INTEREST (BI)*.

18.2.2.1 Non-Rated Municipal Securities

Non-rated municipal securities may represent a higher level of risk to the investor. RRs should discuss the risks of purchasing non-rated bonds when such bonds are recommended for purchase. Risks may include less liquidity; more price volatility; and higher risk of default. As required by MSRB Rule G-15, customer confirmations include a disclosure when a municipal security is not rated.

18.2.2.2 Sophisticated Municipal Market Professionals (SMMPs)

[MSRB Rule D-15, G-19 and G-48; MSRB Notice 2020-13 and 2016-29]

Suitability obligations differ for institutional customers that are "sophisticated" and capable of making their own suitability determinations.

The term "sophisticated municipal market professional" or "SMMP" means a customer of a broker, dealer or municipal securities dealer that is:

1. a bank, savings and loan association, insurance company, or registered investment company; or

2. an investment adviser registered either with the Securities and Exchange Commission under Section 203 of the Investment Advisers Act of 1940 or with a state securities commission (or any agency or office performing like functions); or
3. any other entity (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least \$50 million; AND,
4. an institution that the BD has a reasonable basis to believe is capable of evaluating investment risks and market value independently, both in general and with regard to particular transactions and investment strategies in municipal securities.

An SMMP may affirmatively indicate that it is exercising independent judgment in evaluating the recommendations of a BD or municipal securities dealer. This may be documented by the SMMP's oral affirmation recorded in the account's records on a trade-by-trade basis or on an account-wide basis by having the SMMP sign the Institutional Suitability Certificate.

18.2.2.2.1 Reasonable Basis Analysis

As part of the reasonable basis analysis, the amount and type of municipal securities owned or under management by the customer should be considered.

18.2.2.2.2 Disclosures Not Required

[MSRB Rule G-48]

For SMMPs, there are certain disclosures that do NOT have to be made:

- a. *Time of Trade Disclosure* (material information that is reasonably accessible to the market).
- b. *Transaction Pricing* (ensure that transactions meeting all of the following conditions are effected at fair and reasonable prices):
 - i. the transactions are non-recommended secondary market agency transactions;
 - ii. the broker, dealer, or municipal securities dealer's services with respect to the transactions have been explicitly limited to providing anonymity, communication, order matching, and/or clearance functions; and
 - iii. the broker, dealer, or municipal securities dealer does not exercise discretion as to how or when the transactions are executed.
- c. *Suitability*. The Firm has no obligation under Rule G-19 to perform a customer-specific suitability analysis.

18.2.2.2.3 Summary

The following describes how SMMPs are treated differently from other customers under specific MSRB rules. Refer to the interpretation for more explanation of these specific applications of the SMMP concept.

Rule G-13	CEI must apply the same standards to an SMMP's quotation as if the quotation were made by another BD or municipal securities dealer.
Rule G-19	For a recommended security, the dealer is not required to make a suitability determination.
Rule G-30	If a dealer effects non-recommended secondary market transactions for SMMPs and its services have been explicitly limited to providing anonymity, communication, order matching, and/or clearance functions and the dealer does not exercise discretion, the

	dealer is not required to take further actions on individual transactions to ensure that its agency transactions are effected at a fair and reasonable price.
Rule G-48	Time of trade disclosure, transaction pricing, and suitability obligations do not apply

18.2.3 Minimum Denominations

[MSRB Rule G-15 and G-17; MSRB Issue Brief "Minimum Denominations of Municipal Securities" <http://www.msrb.org/~media/Files/Resources/MSRB-Minimum-Denominations-of-Municipal-Securities.ashx?la=en>]

CEI may not sell municipal securities to customers below the minimum denomination for securities issued after June 1, 2002, with limited exceptions explained below. In addition, for securities issued on or before June 1, 2002, sales to customers in amounts below the minimum denomination must include a disclosure that the amount is below the minimum denomination and that this may adversely affect the liquidity of the position.

18.2.3.1 Exceptions for Securities Issued After June 1, 2002

There are two limited exceptions to this rule:

- CEI may purchase a below-minimum denomination position from the customer provided the customer liquidates his or her entire position.
- CEI may sell such a liquidated position to another customer but the purchasing customer must be provided with written disclosure.

18.2.3.2 Written Disclosure

Written disclosure about the potential affect on liquidity will be included on confirmations where a customer buys an amount below the minimum denomination.

If CEI determines to provide a separate written disclosure, records of providing the disclosure will be retained by Operations for a minimum of three years.

18.2.4 Disclosures

[SEC Securities Exchange Act of 1934 Rule 15c2-12; MSRB Rule G-17, G-32 and G-47; MSRB Notice 2018-07, 2017-18, 2016-27, 2014-07, 2011-67, 2010-37 and 2009-42; Interpretive Notice Regarding Disclosure of Material Facts dated 3/20/02; Interpretive Notice "Guidance on Disclosure and Other Sales Practice Obligations to Individual and Other Retail Investors in Municipal Securities" dated July 14, 2009; MSRB 1998 Interpretive Guidance regarding disclosure obligations for new municipal securities; FINRA Regulatory Notice 10-41]

CEI and RRs have disclosure obligations when effecting municipal securities transactions.

18.2.4.1 Underwritings

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Municipal underwritings • EMMA
Frequency	<ul style="list-style-type: none"> • As required

Action	<ul style="list-style-type: none"> • As managing underwriter, review official statement and obtain written assurances from issuers of compliance with Rule 15c2-12 disclosures • As participating underwriter obtain assurance from managing underwriter of compliance with reviews and issuer compliance requirements • Review EMMA for potential disclosures and provide information to customers when appropriate
Record	<ul style="list-style-type: none"> • Reviews of official statements, commitments with issuers • Contract with managing underwriter who agrees to perform the above obligations

As a municipal underwriter, CEI is obligated to comply with disclosure requirements of SEC Rule 15c2-12 that applies to primary offerings of municipal securities with an aggregate principal amount of \$1,000,000 or more (unless an exemption applies). These obligations may be satisfied by the managing underwriter for an underwriting group, though each underwriter remains responsible for compliance.

A summary of requirements includes the following (refer to the Rule for details):

- The final official statement must be reviewed prior to bidding, purchasing, offering, or selling the issue.
- Except for competitive offerings, preliminary official statements must be sent to potential purchasers upon request.
- The issuer must agree by contract to provide sufficient final official statements.
- Execute continuing disclosure agreements with issuers and reasonably determine that the issuer will provide required information to the MSRB including material events such as principal and interest payment delinquencies; defaults; bond calls, *etc.*
- When recommending the purchase or sale of a municipal security subject to the Rule (applies to all BDs and secondary market transactions), material events must be disclosed to the customer. Simply referring the customer to EMMA for material event disclosures is not sufficient. (See the next section.)

18.2.4.2 Primary and Secondary Market Transactions

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Primary and secondary municipal market transactions • EMMA
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Review to determine disclosures are identified and provided
Record	<ul style="list-style-type: none"> • Order records including disclosure requirements

RRs are required to disclose material information to customers about municipal transactions. This requirement applies to purchases and sales and solicited or unsolicited transactions. MSRB Rule G-47 states that all material

information known about a transaction as well as material information about the security that is reasonably accessible to the market must be made to the customer, orally or in writing, at or prior to the time of trade. "Time of trade" refers to at or before the point at which the investor and the dealer agree to make the trade and may be made orally or in writing, though either method must be documented on the order.

18.2.4.3 Definitions

Established industry sources: include the MSRB's Electronic Municipal Market Access ("EMMA") system, rating agency reports, and other sources of information relating to municipal securities transactions generally used by brokers, dealers, and municipal securities dealers that effect transactions in the type of municipal securities at issue.

Material information: Information that is considered to be material if there is a substantial likelihood that the information would be considered important or significant by a reasonable investor in making an investment decision.

Reasonably accessible to the market: means that the information is made available publicly through established industry sources.

18.2.4.4 Manner and Scope of Disclosure

The disclosure obligation includes a duty to give a customer a complete description of the security, including a description of the features that likely would be considered significant by a reasonable investor, and facts that are material to assessing the potential risks of the investment.

Whether the customer is purchasing or selling the municipal securities may be a consideration in determining what information is material.

Simply directing a customer to EMMA or another repository or through advertising materials is not sufficient; specific disclosures are required. The level of inquiry for material information will depend on varying factors such as less inquiry for an AAA general obligation bond and more inquiry for a non-rated conduit issue or a more complex security.

If an RR becomes aware of **non-public** material information, the RR should contact Compliance immediately and maintain the confidentiality of the information.

18.2.4.5 Record of Disclosures

RRs must record on the order record (or other method available) the source and information provided to the customer.

18.2.4.6 Disclosure Obligations in Specific Scenarios

The following examples are provided by the MSRB to describe information that may be material in specific scenarios and require time of trade disclosures to a customer. This list is not exhaustive and other information may be material to a customer in these and other scenarios.

- a. **Variable rate demand obligations.** A description of the basis on which periodic interest rate resets are determined and the role of the remarketing agent.
- b. **Auction rate securities.** Features of the auction process that likely would be considered significant by a reasonable investor and the basis on which periodic interest rate resets are determined. Additional facts

that may also be considered material are the duration of the interest rate reset period, information on how the "all hold" and maximum rates are determined, any recent auction failures, and other features of the security found in the official documents of the issue.

- c. **Credit risks and ratings.** The credit rating or lack thereof, credit rating changes, credit risk of the municipal security, and any underlying credit rating or lack thereof.
- d. **Credit or liquidity enhanced securities.** The identity of any credit enhancer or liquidity provider, terms of the credit facility or liquidity facility, and the credit rating of the credit provider or liquidity provider, including potential rating actions (*e.g.*, downgrade).
- e. **Insured securities.** The fact that a security has been insured or arrangements for insurance have been initiated, the credit rating of the insurance company, and information about potential rating actions with respect to the bond insurance company.
- f. **Original issue discount bonds.** The fact that a security bears an original issue discount since it may affect the tax treatment of a municipal security.
- g. **Securities sold below the minimum denomination.** The fact that a sale of a quantity of municipal securities is below the minimum denomination authorized by the bond documents and the potential adverse effect on liquidity of a customer position below the minimum denomination. See also Rule G-15(f).
- h. **Securities with non-standard features.** Any non-standard feature of a municipal security. Additionally, if price/yield calculations are affected by anomalies due to a non-standard feature, this also may be material information about the transaction that must be disclosed to the customer.
- i. **Bonds that prepay principal.** The fact that the security prepays principal and the amount of unpaid principal that will be delivered on the transaction.
- j. **Callable securities.** The fact that a municipal security may be redeemed prior to maturity in-whole, in-part, or in extraordinary circumstances, including sinking fund calls and bonds subject to detachable call features.
- k. **Put option and tender option bonds.** Information concerning the put option or tender option features.
- l. **Stripped coupon securities.** Facts concerning the underlying securities which materially affect the stripped coupon instruments. The unusual nature of these securities and their tax treatment warrants special efforts to provide written disclosures.
- m. **The investment of bond proceeds.** Information on the investment of bond proceeds.
- n. **Issuer's Intent to Prerefund.** An issuer's intent to prerefund an issue.
- o. **Failure to make continuing disclosure filings.** Discovery that an issuer has failed to make filings required under its continuing disclosure agreements.

18.2.5 Customer Accounts

Customer accounts must be reviewed on a regular basis. The designated supervisor is responsible for reviewing daily transactions as well as patterns of account activity by reviewing monthly statements or comparable reports or electronic records that show cumulative activity. Refer to the chapter *ACCOUNTS* for details of CEI's policies regarding supervision of accounts.

The frequency and scope of the account reviews depend on a number of factors which may include the number of transactions in the account; profitability of the account; types of municipal products being purchased or sold; and the experience of the RR handling the account. The review of cumulative account activity should take into consideration suitability of overall recommendations compared to the customer's investment objectives, the volume of activity; patterns of cancelled transactions; and other factors such as complaints.

18.2.6 Complaints

[MSRB Rule G-8, G-10 and G-17; MSRB Notice 2017-03; MSRB Rule G-10, MSRB FAQs on Investor and Municipal Advisory Client Education and Protection: <http://msrb.org/~media/Files/Resources/FAQ-MSRB-Rules-G-10-G-8-G-9.ashx?la=en>; MSRB Sample Checklist for handling client complaints: <http://msrb.org/Rules-and-Interpretations/MSRB-Rules/General/~media/A96CC106F5BA4E16936941E6661C1431.ashx>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Incoming correspondence • Oral or written complaints
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Immediately refer original copy of complaint to Compliance • Retain copy for office or branch files • Maintain electronic complaint log using standard codes (MSRB-specific requirement) • Contact Compliance regarding oral complaints, if needed • Compliance will respond to the complaint, in consultation with the office supervisor
Record	<ul style="list-style-type: none"> • Electronic complaint log • Compliance retains all written complaints in a central complaint file • Copy of written complaint in office or branch complaint file • Records are retained for six years, two years in a readily accessible location (MSRB-specific requirement)

The handling of customer complaints is described in the section *Complaints* in the chapter *COMMUNICATIONS WITH THE PUBLIC*. Customer complaint procedures cover all types of municipal activities including municipal advisor services and complaints received in writing or electronically.

Upon receipt of a complaint, Compliance will send to the customer a copy of the investor brochure designated by the MSRB, and will record the date when the investor brochure was provided.

18.2.7 MSRB Rules

A copy of the MSRB rules is available in each office where municipal securities business is conducted by accessing the MSRB's Internet site at <http://www.msrb.org> or via software products produced by other companies.

18.2.8 529 College Savings Plans (Municipal Fund Securities)

[MSRB guidance on 529 and ABLE programs: <http://www.msrb.org/Regulated-Entities/Resources.aspx>; MSRB Investor's Guide to ABLE Programs: <http://msrb.org/~media/Files/Education/Investors-Guide-for-ABLE-Programs.ashx?>; FINRA Regulatory Notice 19-04]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Plan applications

Frequency	<ul style="list-style-type: none"> • When applications are received
Action	<ul style="list-style-type: none"> • Include 529 plans in RR training • Review applications for suitability including: <ul style="list-style-type: none"> ○ suitability of underlying investments ○ expected duration of the investments ○ tax considerations ○ out-of-state vs. in-state plan benefits and disadvantages • Confer with RR if necessary • Confer with customer if necessary • Take corrective action, if required, which may include advising the RR to make alternative recommendations; canceling a purchase
Record	<ul style="list-style-type: none"> • Plan applications • Daytimer or other record of review

529 College Savings Plans are higher education savings plans named for Section 529(b) of the Internal Revenue Service Code. Through a 529 Plan, an individual may contribute cash to be invested for the purpose of accumulating savings for qualifying education costs of beneficiaries. Plan investments include pooled investment funds and have features similar to mutual funds or variable annuities.

529 plans established by states or local governmental entities are deemed municipal fund securities subject to MSRB rules. This section addresses requirements for 529 plans that are considered municipal securities.

18.2.8.1 Registration Requirements

The following registrations are required to sell municipal fund securities:

- RRs qualify through a Series 6 or Series 7 examination (Series 6 qualification is limited to municipal fund securities only and not other types of municipal securities).
- To supervise the sale of municipal fund securities, supervisors must have the following principal qualifications:
 - Municipal Securities Principal (Series 53); **or**
 - General Securities Principal (Series 24) prerequisite **and** Municipal Fund Securities Limited Principal (Series 51); **or**
 - Investment Company/Annuity Principal (Series 26) prerequisite **and** Municipal Fund Securities Limited Principal (Series 51).

18.2.8.2 Features Of 529 Plans

General features include the following; specific programs must be reviewed to determine actual features.

- Plan programs are offered by states or other governmental bodies that either oversee plan investments themselves or, more often, hire an outside entity such as a mutual fund company to handle underlying investments.
- The person who establishes a plan for a beneficiary retains control, a form of revocable gift. Plans may also allow a change of beneficiary.
- While plans have cumulative maximum contributions, the limits are usually very high.

- There are no federal taxes on earnings if used for qualifying education expenses.
- Withdrawals that are not used for qualifying educational expenses are subject to Federal taxes as well as a 10% penalty. There may also be state tax implications.
- There is no time limit in many states on when the 529 money must be used.
- Other features vary depending on the state's plan and may include limitations on investment options and ability to change investments and limits on aggregate contributions for all beneficiaries.
- For most state plans, the customer does not have to reside in the state to establish a plan.

18.2.8.3 Disclosures

[MSRB Notice 2006-23, 2006-16 and 2006-07]

There are two primary forms of written disclosure that must be provided to customers when marketing 529 college savings plans. Providing disclosures does not relieve the obligation to make suitable recommendations to the customer.

18.2.8.3.1 Official Statement/Program Disclosure Document

Issuers of 529 plans provide a document to be used in connection with sales of municipal fund securities. This may be an official statement, program disclosure document, information statement, prospectus, or other document provided by the issuer.

18.2.8.3.2 Out-of-State Plans

When marketing out-of-state 529 college savings plans, disclosure will be provided to the customer prior to or at the time of the trade as follows:

1. Depending on the laws of the home state of the customer or designated beneficiary, favorable state tax treatment or other benefits offered by such home state may be available only if the customer invests in the home state's 529 college savings plan.
2. State-based benefits should be one of many appropriately weighted factors to be considered in making an investment decision.
3. The customer should consult with his or her financial tax or other adviser about how such state-based benefits would apply to the customer's specific circumstances and may wish to contact his or her home state or any other 529 college savings plan to learn more about their features.

18.2.8.4 Rollovers

A 529 savings plan may be rolled over and avoid tax consequences and other penalties if the funds are rolled over from one 529 plan to another state's 529 plan for the same beneficiary or to another 529 plan for a different beneficiary, if certain conditions are met. RRs should consider the associated fees and charges assessed to assure such fees are appropriate, and note why those fees are in the best interest of the customer in box 2c. of the 529 College savings Plan Worksheet.

18.2.8.5 NIIDS Filings

[MSRB Notice 2019-21 and 2010-19]

The primary distributor of a 529 College Savings Plan is obligated to file Form G-32 and related documents with NIIDS. Supplements must also be submitted on a timely basis. The primary distributor is also obligated to determine that the issuer has undertaken a written agreement to provide the MSRB with information required under MSRB Rule G-32 and SEC Rule 15c2-12.

If CEI is the primary distributor of an issue, the designated supervisor is responsible for making the required filings and obtaining the issuer's assurance and for maintaining a record of filings and the assurance.

18.2.8.6 Rule G-45 Report

[MSRB Rule G-45]

Each underwriter of a primary offering of municipal fund securities (not interests in local government investment pools) is required to report information on the offering to the MSRB electronically via Form G-45. Filings are due no later than 60 days following each semi-annual reporting period of June 30 and December 31.

The designated supervisor is responsible for submitting Form G-45 and retaining records of filings.

18.2.8.7 Selling Considerations

When recommending 529 plans, the RR has the obligation to determine the suitability of the recommendation, with particular consideration of the plan's underlying investments. RRs should consider the following when discussing 529 plans with prospective purchasers:

- The customer's investment objectives and the types of underlying investments available.
- Tax implications including Federal and in-state vs. out-of-state tax benefits.
- Penalties on withdrawals not used for qualifying higher education costs.
- Limitations in the plan being considered including changing investments; changing beneficiaries; limits on aggregate contributions; time limits for using plan money; or other limitations.
- Associated costs including expenses, enrollment fees, mutual fund load expenses, and maintenance fees.
- Whether out-of-state customers qualify for a particular plan.

18.2.8.8 529 College Savings Plan Checklist

The RR's designated supervisor must approve transactions where an out-of-state plan or replacement of an existing plan is being recommended. RRs are required to complete the 529 College Savings Plan Checklist and submit it to the designated supervisor prior to effecting the transaction.

18.2.8.9 Sales Material For Municipal Fund Securities

Special requirements apply to sales material for municipal fund securities. In addition to MSRB rule requirements, any municipal fund securities sales material that includes the following information about underlying investment company investments must comply with SEC advertising rules and FINRA Rule 2210:

- performance
- investment objectives or investment strategies
- experience or capabilities of the investment adviser or portfolio manager
- potential benefits or risks
- fees and expenses

18.2.8.10 Advertising Municipal Fund Securities

[SEC Rule 482; MSRB Rule G-21(e); MSRB Notice 2017-16]

The following is a summary of requirements for municipal fund securities advertising. Other conditions apply that are not detailed here. Compliance approval is required prior to publication of any municipal fund advertisement.

Subject	Rule	Requirement
General product advertisement disclosures	G-21(e)(i)	<ul style="list-style-type: none"> • investor considerations • more information available in OS • source of OS is a BD underwriter • read the OS carefully
Product specific advertising disclosures	G-21(e)(i)	<ul style="list-style-type: none"> • source of OS if OS available • home state plan benefits • if a money market fund, no guarantees
Performance disclosures	G-21(e)(i)	<ul style="list-style-type: none"> • legend about past performance doesn't guarantee future performance • if total return quoted is not current, a toll-free number or website where more current information is available • if sales load or nonrecurring fee is charged, maximum amount and if not included in performance statements, disclosure is not included • total annual operating expense ratio (except for money market funds)
Format of disclosure	G-21(e)(i)(4)	Differing requirements for print and other advertising
Generic advertising (does not refer by name to any specific investment option or portfolio but includes name of dealer or other sponsor of the advertisement)	G-21(e)(i)(B)(1)	Does not require general disclosures
Blind advertisements (promote an issuer and its public purpose without naming a product or dealer)	G-21(e)(i)(B)(2)	Does not require general disclosures
Annual financial reports or similar information required by state law, rules, or regulations		Not considered an advertisement if provided solely as required by state laws, rules, or regulations
Communications with existing customers	G-21(e)(i)(B)(3)	Permits form letters that omit some or all required disclosures if sent to existing customers who have previously invested in municipal fund securities
Tax-related disclosures	G-21(e)(v)	If a product advertisement discusses tax benefits, include disclosure that benefits

Subject	Rule	Requirement
		may be conditioned on meeting certain requirements and if specific benefits are described, include the factors that may materially limit their availability

18.3 Sponsoring Meetings and Conferences Involving Issuer Officials

[MSRB Notice 2007-13]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests to sponsor meetings or conferences where an issuer official will participate
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review request for sponsorship, including the official's role • Approve or disapprove the event • Send to the issuer official a letter outlining the prohibitions against soliciting political contributions • If, after the event, there is concern about whether contribution solicitations took place, confer with Compliance to review the activity and determine whether a filing is required with the MSRB and a ban on business may result
Record	<ul style="list-style-type: none"> • Request and approval or disapproval • Letter to issuer official

When CEI and/or its employees sponsor a meeting or conference that features an issuer official as a speaker or participant, it is important to avoid activities that could be considered soliciting political contributions for the issuer official. Activities that could be considered solicitation of contributions include (but are not limited to):

- The issuer official solicits contributions at the meeting or conference.
- The issuer uses an attendee list to solicit contributions.

If it is determined that activities constitute solicitation or coordination of political contributions for the participating issuer official, expenses for the meeting or conference may be considered a political contribution reportable to the MSRB and may trigger a ban on business with the issuer for two years.

If an issuer official will participate in a firm-sponsored meeting or conference, the following are required:

- The content of the meeting and participation by an issuer official (including the official's role) must be approved by a municipal principal.
- The issuer official must be notified in writing by the municipal principal, prior to the meeting or conference, of the prohibition against solicitation of contributions either at the event or afterwards (using the attendee list).

18.4 Communications with the Public

[MSRB Rule G-27]

Communications (electronic or written) require the approval of the designated supervisor. Refer to the chapter *COMMUNICATIONS WITH THE PUBLIC* for detailed procedures.

18.4.1 Performance Data

Communications that include performance data is subject to advertising disclosure requirements and requires the approval of Compliance prior to sending. Refer to the section *Advertising Municipal Fund Securities* for more information.

18.5 Telemarketing

[MSRB Rule G-39]

The sale of municipal securities is subject to telemarketing restrictions including prohibitions against contacting individuals on the National Do-Not-Call Registry.

Refer to the chapter *COMMUNICATIONS WITH THE PUBLIC* and the section *Calling Restrictions* for policies affecting telemarketing.

18.6 Advertising

[MSRB Rule G-21; MSRB Notice 2019-07 and 2018-08]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Requests to advertise• Unapproved advertising brought to the supervisor's attention
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Refer all requests and unapproved items to Compliance• Compliance will review and approve/disapprove• Compliance will make required FINRA filings for municipal fund securities advertising/sales literature
Record	<ul style="list-style-type: none">• Compliance retains records of advertising including approval/disapproval and, if applicable, record of filing with FINRA municipal fund securities sales material within 30 days of use

18.6.1 Definitions

Advertisement: any material (other than listings of offerings) published or used in any electronic or other public media, or any written or electronic promotional literature distributed or made generally available to customers or the public, including any notice, circular, report, market letter, form letter, telemarketing script, seminar text,

press release concerning the products or services of the broker, dealer or municipal securities dealer, or reprint, or any excerpt of the foregoing or of a published article. The term does not apply to preliminary official statements or official statements, but does apply to abstracts or summaries of official statements, offering circulars and other such similar documents prepared by brokers, dealers or municipal securities dealers.

Form Letter: any written letter or electronic mail message distributed to 25 or more persons within any period of 90 consecutive days.

18.6.2 Approval

All advertising involving municipal securities must be approved in writing by a Compliance-designated municipal securities principal or general securities principal prior to first use.

Some of the requirements that apply to advertising of municipal securities include:

- Advertising that includes yield is subject to certain requirements regarding disclosing the basis of the yield.
- Advertising regarding new issues are subject to certain disclosures regarding price or yield and must include an indication, if applicable, that securities shown may no longer be available at the time of publication or may be available from the syndicate at a price or yield different from that shown in the advertisement.
- If bonds are subject to the alternative minimum tax, a statement is to be included in the advertisement to that effect.
- Advertising involving municipal fund securities may be subject to additional requirements, including filing advertising with FINRA, if it discusses underlying investment company securities. See the section *529 College Savings Plans (Municipal Fund Securities) - Advertising Municipal Fund Securities* for more information.

Compliance should be consulted regarding questions about advertisements that include municipal securities.

18.7 Supervisory System, Procedures and Controls

[MSRB Rule G-27]

The MSRB has adopted rule requirements that parallel FINRA rule requirements for supervisory controls. Refer to the chapter *SUPERVISORY SYSTEM, PROCEDURES AND CONTROLS* for CEI's procedures addressing these requirements.

18.8 Direct Purchases and Bank Loans

[MSRB Notice 2016-12 and 2011-52; FINRA Regulatory Notice 16-10]

Some state and local governments use "direct purchases" (private placements of their municipal securities with banks) and bank loans as a method of raising funds and as an alternative to public offerings. The MSRB has indicated that certain financings may be municipal securities subject to MSRB rules.

Outside counsel should be consulted when CEI is involved in bank loan transactions or acts as a placement agent for a direct purchase or bank loan to determine whether such transactions or activities would be deemed municipal securities subject to MSRB rule requirements.

18.9 Municipal Advisor (MA) Activities

[MSRB Rule G-42 and G-44; Exchange Act Section 15B; SEC FAQs regarding Registration of Municipal Advisors: sec.gov/info/municipal/mun-advisors-faqs.shtml; FINRA Regulatory Notice 19-28; MSRB Notice 2018-24, 2018-12, 2018-08, 2017-08, 2014-10 and 2009-42; Interpretive Notice Regarding Disclosure of Material Facts dated 3/20/02; MSRB answers to webinar questions: <http://www.msrb.org/News-and-Events/Past-Webinars/MSRB-Answers-to-Webinar-Questions.aspx>; Municipal advisor model documents: <http://www.sifma.org/services/standard-forms-and-documentation/municipal-securities-markets/#MAforms>; MSRB advisory re municipal advisors: <http://www.msrb.org/~media/Files/Resources/Municipal-Advisor-Compliance-Advisory-June-2017.ashx>]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Reviews of municipal activities
Frequency	<ul style="list-style-type: none"> • Initially determine CEI is not engaged in MA activities • Quarterly: reconfirm exemption
Action	<ul style="list-style-type: none"> • Review municipal activities to confirm they are outside MA requirements • Review municipal activities to confirm CEI does not fall under MA requirements
Record	<ul style="list-style-type: none"> • Initial review to determine no MA activities • Quarterly review to reconfirm

CEI does NOT act as a municipal advisor under Rule 15B. Compliance is responsible for confirming CEI is **not** required to register as an MA.

18.9.1 Definitions

Exchange Act Section 15B and the SEC's FAQs should be consulted for more detailed explanations of municipal advisor activities. The following summarizes some key terms.

Municipal advisor: A person (not a municipal entity or employee of one) that provides advice to a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues or undertakes a solicitation of a municipal entity.

The term includes financial advisors, guaranteed investment contract brokers, third-party marketers, placement agents, solicitors, finders, and swap advisors (as described in the rule).

Excluded from the definition:

- Public officials, employees of municipal entities, and obligated persons to the extent they are acting within their official capacity.
- Municipal entities or obligated persons represented by an independent municipal advisor, subject to conditions.
- Broker-dealers and municipal securities dealers serving as underwriters, commencing when the municipal issuer engages the underwriter on a particular transaction and continuing until the end of the underwriting period for the transaction. Included in the underwriter exemption: acting as a private placement agent; providing ancillary advice as described in the rule; and structuring of refunding escrow cash flow requirements necessary to provide for the refunding and defeasance of an issuance of municipal securities.

Municipal entity: any State, political subdivision of a State, or municipal corporate instrumentality of a State (the rule includes further specifics of the definition).

Obligated person: any person, including a municipal issuer, who is either generally or through an enterprise, fund, or account of such person, committed by contract or other arrangement to support the payment of all or part of the obligations on the municipal securities to be sold in an offering of municipal securities.

18.10 Solicitation of Municipal Securities Business

[MSRB Rule G-38]

CEI will not, directly or indirectly, make payment to anyone who is not an affiliated person for the solicitation of municipal securities business on behalf of CEI.

An "affiliated person," for purposes of this policy, includes anyone who is a partner, director, officer, employee, or registered person of CEI, or of an affiliated company of CEI. "Affiliated company" includes any entity directly or indirectly controlling, controlled by, or under common control with CEI, and whose activities are not limited solely to soliciting municipal securities business.

"Solicitation" is defined in Rule G-38 and interpretive notices which exclude certain limited communications with issuers from being defined as a solicitation of business. Limited communications include providing information about general capabilities of the dealer; communications incidental to completing tasks related to business for which the dealer has been engaged (*e.g.*, engaging an outside contractor to provide cash flow expertise); communications with conduit borrowers; and communications with unaffiliated professionals who provide legal, accounting, engineering, or other professional services where the professional is paid for services rather than for soliciting municipal business. Because of the complexity of the definition of "solicitation," Compliance should be contacted regarding questions about activities that may or may not be deemed soliciting municipal business.

18.11 Trading and Handling Customer Orders

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records
Frequency	<ul style="list-style-type: none"> • Daily and Ongoing
Action	<ul style="list-style-type: none"> • Oversee trading and execution activities • Establish procedures for maintaining records of orders • Review fairness of mark-ups and mark-downs • Review daily inventory positions for compliance with firm limits • Review errors and error accounts • Report system outages or technology-related problems that prevent timely reporting of trades to the MSRB
Record	<ul style="list-style-type: none"> • Initials and date reviewed on available transaction reports or order records; notations of action taken where appropriate • Notations in Day Timer or supervisor's log • Record of reporting system outages/technology problems

CEI will handle orders in accordance with MSRB Rule G-18 and will make reasonable efforts to obtain prices for customers that are fair and reasonable in relation to prevailing market conditions.

18.11.1 Quotations

[MSRB Rule G-13]

All quotations must be bona fide quotations other than a nominal quotation which is an indication of the price given solely for information purposes. Quotations must represent the trader's best judgment of the fair market value taking into account factors such as CEI's inventory position and anticipated market movement.

On joint accounts, quotations must not indicate more than one market in the same security.

If quotations are distributed outside CEI in writing, a record of the written quotations will be retained by the designated supervisor including the quotation, the date of the quotation, and the person giving the quotation and to whom the quotation was provided. If quotations are included in firm advertising, records will be retained in accordance with CEI's advertising policy.

18.11.2 Fair Prices

[MSRB Rule G-30]

Traders are responsible for making a reasonable effort to obtain a price for the customer that is fair and reasonable in relation to prevailing market conditions.

18.11.3 Minimum Denominations

[MSRB Rule G-15 and G-17]

CEI may not sell municipal securities issued after June 1, 2002 to customers in amounts below the minimum denomination as explained in the section *Sales Of Municipal Securities*, with limited exceptions. In addition, where municipal securities issued on or before June 1, 2002 are sold to customer below minimum denominations, CEI has an obligation to make written disclosure to the customer regarding the potential affect on liquidity.

Municipal traders are responsible for:

- identifying potential sales to customers in amounts below the minimum denomination
- determining whether the security was issued after June 1, 2002
- if the security was issued after June 1, 2002, refusing the order or inquiring whether the sale represents the customer's entire position in the security, in which instance the order may be accepted and the order must be marked to ensure inclusion of the required disclosure on the customer confirmation
- if the security was issued on or before June 1, 2002, marking the order to ensure inclusion of the required disclosure on the customer confirmation

18.11.4 Official Statements

[MSRB Rule G-32]

Customers who purchase municipal securities during the "primary disclosure period" will be provided copies of official statements (OS's) or information regarding accessing OS information electronically through EMMA. Refer to the section *Underwriting* and the subsection *Providing Official Statements To Dealers, Purchasers, And Others* for details regarding provision of OS's and recordkeeping.

This requirement to provide OS information applies whether or not CEI is an underwriter or participates in the underwriting and applies during the "primary offering disclosure period." "Primary offering disclosure period"

means, regarding a primary offering, the period commencing with the first submission to an underwriter of an order for the purchase of offered municipal securities or the purchase of such securities from the issuer, whichever first occurs, and ending 25 days after the final delivery by the issuer or its agent of all securities of the issue to or through the underwriting syndicate or sole underwriter.

18.11.5 Records of Orders

[MSRB Rule G-8]

The trading department will maintain a record of orders in municipal securities consistent with the requirements of MSRB Rule G-8. The designated supervisor is responsible for daily review of transactions in municipal securities.

18.11.6 Mark-Ups and Mark-Downs

[MSRB Rule G-30; MSRB Notice 2018-05; MSRB Resource on Disclosing Mark-ups and Determining Prevailing Market Price]

The designated supervisor is responsible for reviewing the reasonableness of mark-ups and mark-downs on customer trades. In determining fair and equitable mark-ups or mark-downs, relevant factors may include:

- the best judgment of CEI as to the fair market value of the securities at the time of the transaction and of any securities exchanged or traded in connection with the transaction
- the expense involved in effecting the transaction
- total dollar amount of the transaction
- availability of the security
- the price or yield of the security
- the maturity of the security
- resulting yield to the customer, as compared to the yield on other securities of comparable quality, maturity, coupon rate, and block size then available in the market
- the nature of CEI's business
- any other relevant facts at time of execution

MSRB Rule G-30 also includes the factor that CEI is entitled to a profit on the transaction.

Compliance will review mark-ups and mark-downs on at least a spot-check basis. Transactions deemed excessive will be canceled and rebilled to reflect an acceptable mark-up or mark-down.

18.11.6.1 Pricing Disclosures (Eff. May 18, 2018)

The amount of mark-ups and mark-downs will be disclosed on non-institutional customer confirmations. Two additional disclosures include: (1) a reference (or hyperlink if the confirmation is electronic) to the MSRB's EMMA website containing publicly-available trading data for the security traded; and (2) the execution time expressed to the second.

Coastal's clearing firm is responsible for disclosures on confirmations.

18.11.7 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 CEI

- the amount of any other compensation received by CEI in connection with the transaction
- factors considered in principal transactions
- any other relevant factors at the time of execution

18.11.8 Reports of Transactions

[MSRB Rule G-14; MSRB Rule G-14 RTRS Procedures; MSRB Notice 2016-19; MSRB RTRS Users Manual; MSRB dealer data web site: <http://www.msrb.org/dfs1/default.htm>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Trade data • MSRB dealer data and other available reports • MSRB customer report edit register
Frequency	<ul style="list-style-type: none"> • Weekly and monthly review of MSRB data depending on frequency of reports
Action	<ul style="list-style-type: none"> • Review MSRB data to determine accuracy of clearing firm's reporting, specifically reviewing for trades successfully submitted vs. those with errors • When patterns of errors are detected, contact the clearing firm to determine what corrective action will be taken
Record	<ul style="list-style-type: none"> • Initials and date reviewed on MSRB reports; notations of action taken where appropriate

Inter-dealer and customer municipal transactions are submitted to CEI's clearing firm for reporting transactions in municipal securities to the MSRB's Real-Time Transaction Reporting System (RTRS).

18.11.8.1 Fictitious Reports

[MSRB Rule G-14(a)]

Reports of transactions must represent bona-fide purchases or sales. No dealer may report a trade that it knows or has reason to know is fictitious or misleading.

18.11.8.2 Step Outs

[MSRB Notice 2005-22, 2004-09 and 2003-20; Notice on Certain Inter-Dealer Transfers of Municipal Securities: Rules G-12(f) and G-14 dated June 4, 2004]

A "step out" is the delivery of securities between dealers that is not the result of a purchase-sale transaction between those dealers, *i.e.*, delivery of securities to satisfy an investment adviser allocation instruction or transfer of assets between two DTCC accounts of a dealer. CEI has the obligation to ensure step outs are designated properly for G-14 and comparison reporting purposes to prevent the inadvertent reporting of a purchase/sale transaction that did not, in fact, occur. Incorrect designation of step outs is a violation of G-12 on comparisons and G-14 on trade reporting.

18.11.8.3 System Outages

[MSRB Notice 2012-49]

If CEI experiences a system outage or other technology-related problem that affects the ability to comply with MSRB transaction reporting rules or other reporting requirements such as current interest rates and documents for certain variable rate securities to the MSRB Short-term Obligation Rate Transparency System or information or documents about new issues filed with EMMA, the outage will be reported online through CEI's MSRB Gateway account.

18.11.9 Inventory Positions

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Pricing provided by traders • Independent pricing services • MSRB transaction information
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Designated supervisor: <ul style="list-style-type: none"> ○ Review daily pricing, marks ○ If pricing appears unreasonable, contact trader and make necessary adjustments ○ Review requests for exceptions to inventory limits and, in consultation with the designated supervisor, approve or disapprove ○ Provide training to traders on proper pricing ○ Review daily inventory to confirm compliance with limits ○ If limits exceeded, contact the trader's supervisor; reduce the position or approve an exception; take corrective action (in conjunction with the designated supervisor) which may include restricting the trader's activities, added training for the trader, or other action as appropriate • Risk management: <ul style="list-style-type: none"> ○ Monitor intra-day risk (size, exposure, net buys vs. short positions, <i>etc.</i>)
Record	<ul style="list-style-type: none"> • Daily pricing of inventory • Designated supervisor's review of marks • Review of compliance with inventory limits • Risk management actions when anomalies are detected

CEI has established guidelines for maintaining inventory positions. Traders are responsible for complying with inventory position limits. Exceptions require the approval of the designated supervisor.

18.11.9.1 Pricing Positions

It is the traders' responsibility to price municipal inventory positions at the end of each trading day. Positions are priced using one or more of the following resources:

- Transactions that day in the security being priced
- If no transactions, transactions in similar securities (rating, maturity, type, insured vs. non-insured, *etc.*)
- Index values

- Treasury curve, yield curve changes
- Consideration of overall market
- Conversations with other dealers regarding the market
- MSRB published transactions in the same or like securities
- Pricing available from Bloomberg, other vendors

Traders should be conservative when pricing positions. Daily pricing of inventory positions is communicated to the responsible designated supervisor.

18.11.10 Errors

All errors in customer orders must be resolved immediately when discovered. No overnight positions should be maintained in the error account. Errors in customer accounts are documented on the Cancel and Rebill/Error Report form which requires a designated principal's approval.

18.11.11 Cancels and Rebills

Cancellations and rebills in customer accounts are documented on the Cancel and Rebill/Error Report form which requires a designated supervisor's signature.

18.11.12 Traders' Personal Accounts

Traders are required to maintain their personal securities accounts with CEI. Traders may not effect personal transactions in municipal securities from CEI inventory. Purchases or sales must be made on an agency basis with other dealers. Exceptions require the approval of the designated supervisor.

18.11.13 Prohibited Activities

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Trading reports • Observation of traders' activities
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Take corrective action depending on the nature of the prohibited activity
Record	<ul style="list-style-type: none"> • Trading Dept. files and/or the Trading Manager's Log

18.11.13.1 Inside Information

[Insider Trading and Securities Fraud Enforcement Act of 1988; SEC Securities Exchange Act of 1934 Rule 10b-5; FINRA Notice to Members 89-15]

Traders are prohibited from acting on, passing on, or discussing any inside information regarding municipal issues, including confidential information regarding advance refunding. Any knowledge of such information must be brought to the attention of the designated supervisor and Compliance. No CEI proprietary account or employee account may enter a transaction based on material non-public information about the issuer of that security.

18.11.13.2 Fraud or Misrepresentation

[SEC Securities Exchange Act of 1934 Rule 15c1-2]

CEI and its employees are prohibited from engaging in any activity that may be deemed fraudulent or engaging in misrepresentation. This is a general standard that applies to all securities and prohibits making untrue statements about material facts or omitting to state a material fact that is necessary so information presented is not misleading. This applies when the person has reasonable grounds for knowing a statement is untrue or misleading.

18.11.13.3 Improper Use of Assets

[MSRB Rule G-25]

Rule G-25 provides general prohibitions applicable to municipal securities transactions as well as other types of securities and accounts. The following summarizes the prohibitions under G-25:

- No improper use of municipal securities or funds held on behalf of someone else
- No guarantees against loss
- No sharing by employees, indirectly or directly, in the profits or losses of a customer's account

The chapter *GENERAL EMPLOYEE POLICIES* includes similar prohibitions and limitations on activities.

18.11.13.4 Financial Arrangements

Traders are prohibited from entering into financial arrangements with customers or issuers (*i.e.*, sharing in profits or losses, sharing in commissions, rebating commissions, *etc.*).

18.11.13.5 Market Manipulation

[SEC Securities Exchange Act of 1934 Rule 10b-3]

No purchase or sales order shall be entered that is designed to raise or lower the price of a security or to give the appearance of trading for purposes of inducing others to buy and sell.

18.11.13.6 Parking Securities

No arrangement may be used to conceal the true ownership of securities through a fictitious sale or transfer to an accommodator who agrees to later sell or transfer the securities to the true owner (or his agent) at the agreed upon time at essentially the same terms.

18.11.13.7 Secret Profits

A trader may not permit the charging of a mark-up or mark-down in addition to a commission on any transaction.

18.11.13.8 Adjusted Trading

Adjusted trading is a prohibited practice where a broker-dealer is involved in a swap transaction with a customer at prices not reasonably related to the current market value of the securities. An example is a customer sale to a broker-dealer at a price below market value and the simultaneous purchase and booking of a different security at

a price above the current market value. The purpose of an adjusted trade is to assist one party in avoiding, disguising, or postponing losses.

18.12 Gifts

[MSRB Rule G-20; MSRB Notice 2020-13]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests to give gifts
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review and approve or disapprove gift requests • Maintain record of gifts
Record	<ul style="list-style-type: none"> • Compliance maintains a file of gift requests and gifts given

18.12.1 Introduction

Gifts relating to CEI's business are limited to \$100 per year per person. Gifts of tickets to sporting events, or similar gifts where the employee does not accompany the recipient, are subject to the limitations on gifts and gratuities. Such gifts may not be so frequent, or so expensive, as to raise a suggestion of unethical conduct.

Employees are required to notify Compliance of gifts relating to customers or prospective customers. Compliance is responsible for maintaining a record of gifts; the record is subject to review by regulators.

The MSRB also has limitations on cash and non-cash compensation relating to offerings of municipal securities. CEI's policy is in the chapter *COMMISSIONS*, in the section *Cash And Non-Cash Compensation Policy*.

Also refer to *Gifts, Gratuities And Entertainment* in the chapter *GENERAL EMPLOYEE POLICIES*.

18.12.2 Sales Contests

[MSRB Rule G-20.20]

When a municipal securities broker or dealer sponsors a contest and provides gifts or payments to employees of a different broker-dealer, certain requirements apply **prior to** conducting the contest. The sponsoring dealer must obtain a written agreement between the employing broker-dealer and the person who will perform services subject to the contest including the nature of proposed services, amount of proposed compensation, and the written consent of the person's employer.

All proposed contests must be submitted to Compliance for review and approval. Refer to the section *Conflicts Of Interest* in the chapter *REGULATION BEST INTEREST (BI)* for details regarding conflicts involving compensation.

18.13 Political Contributions

[MSRB Rule G-37 and G-37 Q and A; SEC Risk Alert: <http://www.sec.gov/news/press/2012/2012-173.htm>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests to make political contributions • Quarterly certifications
Frequency	<ul style="list-style-type: none"> • As required (<i>requests</i>) • Quarterly (<i>certifications and filing G-37 report</i>)
Action	<ul style="list-style-type: none"> • Review requests and determine permissibility • Identify municipal securities professionals covered by Rule G-37 • Maintain list of current municipal securities professionals • Request quarterly certifications from municipal securities professionals • Prepare and file Form G-37 • Notify appropriate department managers if CEI's activities must be restricted • Contact Compliance to determine corrective action if prohibited activities using Firm resources are identified
Record	<ul style="list-style-type: none"> • Compliance maintains files for: <ul style="list-style-type: none"> ○ Requests and responses ○ Quarterly certifications ○ Quarterly reports ○ List of municipal securities professionals ○ Restrictions, if appropriate

18.13.1 Introduction

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 CEI from engaging in municipal business for two years with any issuer where contributions subject to this rule are made. Because CEI does not want to be subject to a two-year restriction on its municipal business, employees are required to adhere to the requirements of the rule.

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

18.13.2 Summary of Key Requirements

Some of the key requirements that apply to CEI and CEI employees are summarized below.

- The types of public finance business included in this rule are acting as a negotiated underwriter (as manager or syndicate member), financial advisor or financial consultant, placement agent, and negotiated remarketing agent.
- The rule applies to contributions made by CEI, any PAC controlled by CEI, public finance professionals, municipal traders and professionals, CEI's executive committee, and anyone deemed to be a Municipal Finance Professional (MFP) as defined in the rule.

- Political contributions by CEI or affected employees must be cleared through Compliance prior to making the contribution.
- "Contributions" are defined by rule and the recipient of contributions ("official of the issuer") is also defined. Some minimal contributions (\$250 or less) by affected employees who are contributing to officials for whom they may vote are excluded from the rule.
- CEI and its employees are prohibited from soliciting others to make contributions to an official of an issuer.
- Employees are prohibited from using Firm resources (phones, email, computers, office space, *etc.*) for political activities subject to Rule G-37. This includes (but is not necessarily limited to) fund-raising; drafting speeches or fund-raising solicitations, writing campaign memoranda, contracts, letters, talking points, position papers, and responses to issues; approving campaign invoices and expenditures.
- CEI, its municipal finance professionals (MFPs), and affiliates are prohibited from soliciting any person or political action committee (PAC) to make or coordinate contributions to an official of an issuer with which CEI is engaged in business, or is seeking to engage in business.
- CEI will be required to maintain internal records of affected employees and their contributions and report quarterly to the MSRB.
- CEI cannot pay compensation for soliciting municipal business to anyone who is not affiliated with CEI (see the prior section *Solicitation Of Municipal Securities Business*).

18.13.3 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 financial 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 CEI engages a consultant to secure municipal business, the consultant's contributions will affect CEI'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.

18.13.4 Definition of Municipal Finance Professional

Municipal finance professionals subject to political contribution limitations and reporting requirements include (other than employees whose functions are solely clerical or ministerial) employees engaged in:

- municipal securities representative activities (including sales, except that sales to natural persons are NOT included)
- underwriting or trading
- financial advisory or financial consultant services for municipal issuers
- research or investment advice regarding municipal securities
- soliciting municipal securities business as defined in this section
- supervision of the above activities
- acting as CEO or a similar position
- serving on a dealer's executive or management committee

RRs who sell municipal securities to individual investors are not included in this definition or the restrictions on political contributions.

18.13.5 Definition of Non-MFP Executive Officer

Non-MFP Executive officer is defined as an employee who is NOT deemed a municipal finance professional and is in charge of one of CEI's principal business units, division or department or an employee who performs similar policy making functions for CEI. For purposes of this definition, a "principal" business unit, division or department will be defined as one that generates more than 5% of CEI's annual revenues.

For purposes of MSRB Rule G-37, Non-MFP Executive Officers are required to report their political contributions but their contributions would not result in a prohibition on municipal securities business.

18.13.6 Types of Contributions Included

The following types of contributions made by CEI or affected employees 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 also include those made to bond ballot campaigns which typically occur as a result of a state or local government placing a ballot measure before voters to approve specified municipal borrowing. Contributions to bond ballot campaigns (for or against the ballot issue) include payment of debt occurred in connection with the initiative or payment of the costs of the initiative. In the case of an in-kind contribution, the value and nature of the goods or services provided including any ancillary services provided to, on behalf of, or in furtherance of the bond ballot campaign is reportable including the specific date on which such contributions were made.
- "In-kind" support or services may be regarded as political contributions. Examples include engaging in political activities during working hours such as fundraising, drafting speeches and solicitations, writing/reviewing/approving campaign memoranda, contracts, letters, talking points, campaign position papers, responding to campaign issues; using CEI's resources (administrative employees, phones, office space, and other services); approving campaign invoices/expenditures. In-kind contributions must be valued and generally must be recorded and reported in the same manner as other contributions.
- 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 state-wide executive or legislative officials (including governors) would be included within the rule.
- Indirect contributions by affected employees 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 CEI are used (a political position paper is prepared by CEI personnel, CEI 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.

18.13.7 Contributions Subject to Political Contribution Limitations and Reporting

Covered contributions include those by CEI, any PAC controlled by CEI, and by municipal finance professionals listed above. The rule does NOT apply to other employees, provided that contributions are not made for the purpose of inducing or influencing the obtaining or retaining of public finance business from an issuer.

18.13.8 Look-Back and Look-Forward Provisions

[MSRB Rule G-37(b)(ii)(B)]

Individuals who are employed as municipal finance professionals are subject to rules requiring a "look-back" at their political contributions prior to joining CEI. Prior contributions to issuer officials may restrict CEI's ability to do municipal securities business with that issuer until the "look-forward" period has expired. At the time of hire, new municipal finance professionals will be asked to provide information regarding contributions during the look-back period, and the designated supervisor will determine whether restrictions will apply. The individuals affected and the periods are:

Person Affected	Look-Back	Look-Forward
MFPs primarily engaged in municipal securities representative activities (trading or underwriting, financial advisory or consultant services for municipal issuers)	2 years	1 year
Those soliciting municipal finance business for CEI	2 years	1 year
Supervisors and management-level MFPs	6 months	1 year

18.13.9 Political Action Committees (PACs)

[MSRB Guidance on Dealer-Affiliated PACs Under Rule G-37, 10-21-10]

Responsibility	<ul style="list-style-type: none"> Designated Supervisor
Resources	<ul style="list-style-type: none"> Requests to establish PACs Information regarding PACs established by affiliates
Frequency	<ul style="list-style-type: none"> As required
Action	<ul style="list-style-type: none"> Obtain information from affiliates about PACs related to municipal business Determine whether a PAC is controlled by CEI If controlled by CEI, notify persons responsible for the PAC of the applicability of Rule G-37 Make necessary MSRB filings on behalf of a controlled PAC For affiliate PACs not controlled by CEI or an MFP, establish information barriers and notify affected affiliate and firm personnel of the barriers, including acknowledgement by affected persons
Record	<ul style="list-style-type: none"> Requests and reviews of requests Information regarding affiliate PACs

	<ul style="list-style-type: none"> • Review of PACs to determine whether Rule G-37 applies • G-37 filings, as required • Notification of information barriers for affiliate PACs not under control of CEI or an MFP and acknowledgement by affected persons
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A PAC controlled by CEI is subject to the political contribution requirements of Rule G-37. There are factors that may result in an affiliated PAC being viewed as controlled by CEI; the MSRB's interpretive guidance should be consulted for specifics. **Compliance should be consulted before a PAC is established related to municipal securities business.**

A summary of factors that indicate potential control of a PAC by CEI includes:

- If CEI or one of its MFPs is involved in the creation of a PAC (whether solely or together with others), there is a presumption of control unless there is a complete disassociation in any direct or indirect manner.
- The ability to direct or cause the direction of the management or policies of a PAC are potential indicators.
- The level of funding provided by CEI or a firm MFP may indicate control, including potential leveraging of the contribution activities of affiliated PACs.

To avoid conflicts of interest and to comply with G-37, the following information barriers have been established between CEI, its MFPs, and any PAC that is not controlled by CEI or the MFP, but is controlled by an affiliate of CEI.

- CEI and its MFPs cannot recommend, nominate, appoint, or approve the management of affiliated PACs.
- The PAC's meeting agenda, meeting schedule, or meeting minutes cannot be shared with CEI or firm MFPs.
- There cannot be identification of prior affiliated PAC contributions, planned PAC contributions, or anticipated PAC contributions.
- There is a prohibition on directly providing or coordinating information about prior negotiated municipal securities business, solicited municipal securities business, and planned solicitations of municipal securities business.

Compliance will notify affected affiliate personnel and firm personnel, as necessary. Affected persons will be required to acknowledge in writing their understanding and compliance with the information barriers.

18.13.10 Approval

Responsibility	<ul style="list-style-type: none"> • Compliance Officer
Resources	<ul style="list-style-type: none"> • Requests from employees to make contributions • Proposed firm or firm-controlled PAC contributions
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review proposed contributions for compliance with Rule G-37

Record	<ul style="list-style-type: none"> • Requests and approval and/or action taken are retained by Compliance
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Political contributions by CEI, a firm PAC or an MFP to officials of issuers, PACs, or political parties must be cleared through Compliance prior to making the contribution. In addition, any political activities by MFPs (volunteer work, *etc.*), on behalf of an official of an issuer, must be cleared through Compliance prior to participation.

18.13.11 Prohibited Solicitations and Activities

[MSRB Notice 2005-50]

CEI, its MFPs, and any affiliate may not solicit others, including employees, family members, PACs, and any others outside CEI, to make contributions to an official of an issuer with which the dealer engages or is seeking to engage in municipal securities business, or to coordinate such contributions. This includes a prohibition against soliciting a person or PAC to make or coordinate a payment to a political part of a state or locality where CEI is engaged, or seeking to engage, in municipal securities business.

CEI and municipal finance professionals may not engage in fund-raising activities for officials of issuers.

18.13.11.1 Prohibited Indirect Payments

G-37 prohibitions also extend to "housekeeping," "conference," or "overhead" type political party accounts. CEI, its PAC, or MFPs cannot contribute indirectly to officials of issuers through these types of accounts when they are prohibited from such contributions directly. Making such contributions, with instructions accompanying the payment that the specific payment is not to be used for the benefit of an official of an issuer, does not ensure the contribution complies with G-37.

18.13.12 G-37 Records to Be Maintained by The Firm

CEI is required to maintain information in its files identifying affected employees and the states in which the dealer is engaged or is seeking to engage in municipal securities business; issuers with whom CEI is doing and has done business for the past 2 years; and all contributions made to issuer officials subject to Rule G-37, including contributions of affected employees, CEI, and any PAC controlled by CEI. This does not include the minimal \$250 contributions allowed under the rule. This will be an internal record subject to scrutiny by regulatory authorities. Records are also not required for affiliate companies and their employees, spouses of covered employees, or any other person or entity unless the contributions were directed by persons or entities subject to Rule G-37. These records will be retained for six years per MSRB Rules G-8 and G-9.

18.13.13 Quarterly Report

CEI will file Form G-37 by the last day of the month following each calendar quarter (January 31, April 30, July 31, and October 31), as required. CEI is not required to file a report under the No Business Exemption of MSRB Rule G-37 for the calendar quarter if:

- CEI has not engaged in municipal securities business; and
- there are no reportable political contributions to issuer officials or payments to state and local political parties.

The following procedures apply:

- The designated supervisor is responsible for determining if a report is required or whether the No Business Exemption obviates the need for filing.
- Employees subject to political contribution reporting will complete a quarterly certification regarding their contributions during the quarter to be reported.
- Form G-37 will be completed and signed by the appropriate supervisor.
- Two copies will be sent to the MSRB by certified or registered mail or by some other method where a receipt of sending is retained or required. G-37 information will be submitted electronically.
- A copy of the signed form and proof of sending is retained in a file for Form G-37.

19 Non-Conventional Investments (NCIs)

[FINRA Notice to Members 03-71]

Responsibility	<ul style="list-style-type: none"> • RR • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Non-conventional investments and related information
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Conduct due diligence about the product • Prepare or obtain disclosure information for prospective investors • Supervisor <ul style="list-style-type: none"> ○ Review customer transactions in NCIs for suitability ○ Confirm required disclosure documents were provided ○ When necessary, consult with RR regarding suitability ○ When necessary, contact customer to confirm suitability and/or cancel transaction if purchase is inappropriate
Record	<ul style="list-style-type: none"> • Written disclosures, when available, are retained in the product file. • Written subscription agreements or other investor agreements are retained in the product file or the customer's file. • Records of training material or programs are retained in the product file and/or Continuing Education files or compliance meeting files. • Record of review of transactions is included in order records.

Certain investments may have features and complexities not as easily understood by investors as traditional investments such as stocks or bonds. Non-conventional investments (NCIs) such as asset-backed securities, distressed debt, and derivative products may warrant closer scrutiny to determine suitability of the security for the specific potential investor.

The RR recommending a non-conventional investment is responsible for understanding the features of the NCI and making a suitability determination considering the potential investor's investment objectives and financial background. The RR is also responsible for providing information to the prospective investor, including balanced disclosure of the risks and rewards, so the investor may make an informed decision about the potential investment. Where prospectuses or other disclosure documents are available, it is the RR's responsibility to provide the written disclosure to the prospective purchaser. RRs must also obtain signed subscription or other agreements from NCI investors, where required.

19.1 Blue Sky of Securities

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Daily Transaction Report
Frequency	<ul style="list-style-type: none"> • Daily

Action	<ul style="list-style-type: none"> • Review order records and Daily Transaction Report for patterns of solicited purchase orders in securities that are potentially not blue-skied including: <ul style="list-style-type: none"> ○ securities that are not potentially exempt ○ securities that are low-priced • Compliance: if a violation occurs, determine if rescission is required and offer rescission; assess loss • Consult Compliance regarding transactions in question
Record	<ul style="list-style-type: none"> • Initials on order records • Initials on Daily Transaction Report • Notes of questioned transactions on Daily Transaction Report and/or supervisor's log, daytimer, or other record • Records of rescission offered

"Blue sky" refers to state laws that govern the sale of securities and those who sell securities to residents of individual states. Registration of agents is discussed in the chapter *EMPLOYMENT, REGISTRATION AND LICENSING*. This section discusses blue sky requirements of securities sold by CEI.

Securities must be blue skied in the state of residence of the customer to whom the security is sold. If a security that is not blue skied is sold to a customer in violation of state blue sky laws, the customer likely has a right of "rescission," which means the customer may cancel the transaction and receive a refund of the purchase price. Losses resulting from rescissions will be charged to the RR who sold the security in violation of blue sky requirements. States may also take disciplinary action against firms and individuals for violations of state law.

There are two ways a security may be sold to a state resident under blue sky laws. First, the issuer may register with the state. Second, an exemption may apply. Exemptions generally apply to:

- Securities issued by the federal government and municipalities
- Exchange-listed securities
- NASDAQ Capital Market listed securities
- Securities sold to certain institutions

Because blue sky laws vary from state to state, Compliance should be consulted to determine specific requirements.

19.2 Exchange-Listed Index Warrants, Currency Warrants and Currency Index Warrants

[FINRA Rule 2350 series; FINRA reminder of sales practice rules dated May 14, 2007]

Customer transactions in these securities are generally subject to requirements for trading options (FINRA Rule 2360). The following chart indicates requirements when selling these securities and the corresponding language in options rules that applies.

Rule	Corresponding options rule	Explanation/requirements
2351		General requirements language
2351		Definitions of terms

Rule	Corresponding options rule	Explanation/requirements
2352	2360(b)(16)	Account approval: must be approved in accordance with option account approval requirements
2353	2360(b)(19)	Suitability: reasonable basis required
2354	2360(b)(18)	Discretionary accounts: must be approved by an ROP
2355	2360(b)(20)	Supervision requirements consistent with options supervision
2356	2360(b)(17)(A)	Complaints: respond, retain record of complaint/response
2357	2220	Communications: options standards apply
2358	2360(b)(17)(B)	Records: requirements mirror options requirements
2359		Position limits: cannot exceed established limits
2359		Exercise limits: cannot exceed exercise limits
2359		Liquidation of index warrants positions: May be required when position limits are exceeded

19.3 Auction Rate Securities

[FINRA Regulatory Notice o8-o8; FINRA Investor Alert: Auction Rate Securities: What Happens When Auctions Fail; SIFMA Auction Rate Securities Best Practices: www.sifma.org/services/pdf/AuctionRateSecurities_FinalBestPractices.pdf]

Auction rate securities are bonds that have interest rates periodically reset by auction. Interest reset periods are usually either 7, 14, 28 or 35 days. There are some securities where auctions occur more frequently (sometimes daily) or less frequently (for example, every six months or once over a multi-year period). An auction program employs one or more dealers that solicit orders from investors who wish to own the securities over the next interest reset period. The programs require one "auction agent," typically a bank, that receives orders from the dealers and conducts auctions consistent with procedures in the program documents. This procedure determines the lowest interest rate at which all of the securities offered for sale by current holders of the securities will clear the market (the "clearing rate"). The clearing rate then becomes the interest rate for all of the securities in the issue for the next interest rate reset period.

When recommending auction rate securities to retail investors, the following features and risks must be considered and discussed with the customer.

- features of the auction process including that the securities may or may not be sold at auction; there is no guarantee an auction will take place and securities may lose value as a result; there is no assurance regarding the outcome of auctions
- duration of the interest rate period and whether the period is subject to change
- the securities may have long-term maturities or no maturities at all
- features found in official documents including how "all hold" and maximum rates are determined
- the customer's need for liquidity and the liquidity characteristics of the particular auction rate security being considered

When an initial offering of auction rate securities is being sold, investors must be provided with the prospectus or other official document describing the offering.

19.3.1 Allocations

[FINRA Rule 2010 and 4340; FINRA Regulatory Notice 08-21; FINRA Staff Interpretive Memo 7/9/08]

CEI (or its clearing firm) uses a methodology to allocate partial redemptions that is fair and does not disadvantage any customers. If CEI's method (or the clearing firm's method) varies from the specific provisions of NYSE Rule 402.30, it will confirm that the method is fair including satisfying customer positions before proprietary or associated person positions. The disclosure will be provided in plain English by mail or e-mail; on an accessible page of CEI's web site communicated to customers; and/or included prominently on customer statements. Communications will include examples of the allocation process to illustrate the explanation.

The FINOP is responsible for allocation procedures and providing disclosures to customers.

19.4 Commodity Futures-Linked Securities

[FINRA Regulatory Notice 10-51]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Order records• Available reports
Frequency	<ul style="list-style-type: none">• Training: when a new product is introduced and ongoing• Review of orders: Daily, when trades occur• Review of communications: Daily
Action	<ul style="list-style-type: none">• Provide training including features and risks of the security and how to inform customers when selling the securities• Review transactions for suitability, take corrective action when necessary which may include contact with the RR, the customer, and/or Compliance• Review communications regarding securities to confirm accuracy and completeness of descriptions of features and risks
Record	<ul style="list-style-type: none">• Records of training• Records of communications• Records of order review• Records of corrective action taken regarding communications and/or orders

Commodity futures-linked securities use futures contracts to track an underlying commodity or commodity index. The security will typically roll its position before the contract's expiration and can face differing prices between the contract it sells and the new contract - for more distant delivery - that it buys. The difference is called the roll yield. There are different methodologies for achieving investment objectives, and some may not employ strategies that address roll yield. Some invest in a single futures contract while others invest in multiple contracts. Others track indices in an attempt to optimize roll yield by minimizing the impact of contango (an upward sloping forward curve [as in the normal yield curve]). Such a forward curve is said to be "in contango" [or sometimes "contangoed"]) or maximizing the impact of backwardation (a downward sloping forward curve [as in an inverted yield curve]). FINRA Regulatory Notice 10-51 should be reviewed for a more complete description of commodity futures-linked securities.

As with all recommendations, the RR must understand the security being recommended and ascertain that the investment is suitable for the customer. The RR is obligated to discuss with a retail investor the following features:

- the commodity, basket of commodities or commodities index that a given product tracks;
- the product's goals, strategy and structure;
- that commodities prices, and the performance of commodity futures-linked securities, can be volatile;
- the use of futures contracts can affect the performance of the product as compared to the performance of the underlying commodity or index;
- the product's methodology, including its strategy, if any, for managing roll yield and other factors that may affect performance; and
- the product's tax implications. (Commodity pools have different tax implications than mutual funds or exchange-traded notes.)

19.5 Certificates of Deposit

[FINRA Notice to Members 02-69]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Order records • Transaction reports • Customer information • Information about CDs being offered
Frequency	<ul style="list-style-type: none"> • Daily - review transactions • As required - provide training
Action	<ul style="list-style-type: none"> • Provide training to RRs regarding features of CDs and suitability guidelines when recommending CDs depending on type • Review transactions for suitability considering the type of CD being purchased and the customer's investment objectives and investment profile
Record	<ul style="list-style-type: none"> • Order records/transaction reports include supervisor's initials and date of review and note of action taken • Training materials and records of when training is administered and to whom

CEI offers certificates of deposit (CDs) as one of the products available to customers. Because CDs offered by CEI may be different from traditional bank-issued CDs that carry a fixed interest rate over a fixed duration of time and are insured by FDIC, it is important that RRs understand the features of these CDs before offering them to customers.

19.5.1 General Sales Guidelines

The following guidelines apply to the sale of CDs:

- Only CEI-approved sales material may be provided to customers.

- RRs should be familiar with the features of the CD prior to discussing it with the customer. In particular, it is important to understand FDIC insurance coverage, interest rates, maturity dates, fees or markups, and other terms of CDs.
- RRs must consider suitability when recommending CDs. For example, a 30-year zero coupon CD is not likely to be appropriate for an elderly customer.

19.5.2 Special Characteristics of CDs

Some CDs have unique characteristics which should be understood by the RR and communicated to the potential purchaser. Some of those special characteristics are explained below.

CDs may be securities. Some CDs may be considered securities and must be registered. Whether or not a CD is a security depends on a number of factors and requires individual analysis. CDs should be reviewed by Compliance prior to offering to the public, to determine whether registration as a security is required.

"Brokered" CDs may be significantly different from traditional CDs. Brokered CDs are CDs issued by banks via a "master CD" to deposit brokers (which include broker-dealers) which sell interests to individual investors. The master CD is an aggregation of individual CDs with the same denomination.

- Brokered CDs may have longer maturity dates (in some cases 20 years) than traditional CDs.
- Interest rate terms may differ significantly from simple rates paid by traditional CDs.
- There may be a penalty for withdrawing funds before maturity.
- If a secondary market exists for the CD, the customer may lose principal because of prevailing interest rates at the time of sale.
- FDIC insurance protection may or may not be available to the customer, depending on whether the customer has exceeded the \$100,000 limit at a particular bank, thrift or credit union.
- Brokered CDs may have a call feature.

19.5.3 Disclosures When Selling Brokered CDs

Disclosures must be made to customers in the following areas:

- Potential for loss of principal
- Limitations on secondary markets
- Call features
- Step-up or Step-down features

Loss of Principal: Long-term CDs are subject to market price fluctuations primarily affected by prevailing interest rates. If a customer chooses to sell a CD prior to maturity, the pre-maturity sales price of the brokered CD may be less than its original purchase price. Using the term "no penalty for early withdrawal" is misleading unless the issuer guarantees redemption at full face value for a sale prior to maturity.

Secondary market: The secondary market for long-term CDs may be limited. CEI will make the appropriate disclosure to purchasers of CDs during an initial distribution.

Call features: Callable CDs give the issuer the right to redeem the CD. This typically happens when a long-term CD is trading at a premium to its call price in the secondary market. Purchasers should understand it is the issuer that has the right to call the CD, and it may be redeemed at a time when less favorable interest rates are available for reinvesting the funds. RRs must not predict the likelihood that the CDs will or will not be called.

Discount or zero CDs: Purchasers should understand the maturity date of the CD and that interest and principal are not payable until maturity. Early sales may result in a substantial loss of value.

"Step rate" CDs: A "step-down" CD generally pays an above-market interest rate for a period of time after which it will then "step down" to a lower, predetermined rate that will be paid until maturity. A "step-up" CD generally pays a below-market interest rate for a period of time after which it will then "step up" to a higher predetermined rate that will be paid until maturity. The "step rate" may be below or above then-prevailing market rates. The initial rate cannot be used to calculate yield to maturity.

19.5.4 Market Index/Linked CDs

Some CDs are linked to market indices. Market Indexed/Linked CDs ("MCDs") are hybrid investments that often combine zero-coupon bonds with stock options on the underlying market index. When held to maturity, MCDs are intended to offer return of the initial investment with the potential of upside gain based on the performance of the underlying index. MCDs are insured by the FDIC for up to \$100,000 per account held at each institution.

There are important differences between certificates of deposit and indexed CDs. RRs should understand those differences and disclose key risks and features when recommending purchases.

- Unlike traditional CDs, MCDs are subject to market risk if sold prior to maturity.
- A secondary market is not guaranteed and may not exist; customers may not be able to liquidate MCDs prior to maturity.
- Investors must keep MCDs for the full term of the MCD (often 4-5 years) in order to be guaranteed a return of principal plus earnings.
- Some indexed MCDs have complicated terms that can result in yields that vary greatly from what investors expect.
- Risk and return may have multiple determinants; an indexed MCD may be linked to multiple indexes and issuers can use a variety of averaging methods which, depending on the market environment, could result in no paper gains for the investor, even if the market ended higher at the end of the term.
- Some MCDs have call features that may result in the MCD being called prior to maturity.
- Some MCDs have "barriers" or "knock-out rates." Investors may receive no interest when the barriers are breached, *i.e.*, the index rises above or below the barrier.
- The tax implications of MCDs are different from traditional CDs. Because MCDs include zero coupon bonds, the customer will be required to pay tax on the increase in the accreted value of the MCD on a yearly basis ("phantom" income) even though actual interest is not received until maturity. If held in a taxable account, the investor is taxed on this phantom income.
- Customer should be advised on the method used to derive valuation. The price may or may not be based on the actual closing value of the linked index on the final maturity date. Market value of the MCD may not correspond directly to increases or decreases in the underlying linked index.

19.5.5 Account Statements

When brokered CDs are held in the customer's account, they may be priced at an estimated value. It may be difficult to accurately price brokered CDs and CEI's statements will include appropriate disclosures regarding pricing.

19.6 Cash Alternatives

[FINRA Regulatory Notice 08-82]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor • Compliance
Resources	<ul style="list-style-type: none"> • Retail communications that include content about cash alternatives • Order records
Frequency	<ul style="list-style-type: none"> • Daily - review of order records • Daily - review communications with the public • As required - Compliance review of advertising and retail communications for broad dissemination (brochures, summary sheets, <i>etc.</i>) • Quarterly - review of previously approved retail communications still being used • Periodically - include cash alternatives in training
Action	<ul style="list-style-type: none"> • Designated Supervisor: <ul style="list-style-type: none"> ○ Review orders for suitability of recommendations ○ Review written and electronic correspondence and retail communications for accuracy of representations and suitability of recommendations • Compliance: Review and approve/disapprove proposed advertising and broadly-disseminated communications for accuracy or representations, compliance with regulatory requirements; re-review approved retail communications that continue to be used at least quarterly to confirm conditions have not changed that make the material inaccurate • Include cash alternatives in RR training
Record	<ul style="list-style-type: none"> • Designated supervisor: orders records, retail communications • Compliance: advertising, broadly-disseminated communications • Training records including subjects covered, date of training, and who attended are retained by the person/department conducting the training

In addition to issues about CDs, RRs must be aware of obligations when selling other securities that might be considered "cash alternatives." General obligations include the following:

- Avoid overstating a product's similarities to cash holding and provide balanced disclosure of the risks and returns associated with a particular product;
- Understand the features of the product; and
- Consider suitability before making a recommendation.

Correspondence, retail communications and oral communications regarding cash alternatives must present a fair and balanced representation of the risks, benefits, and limitations of investing in these products. Investments may not be represented as an alternative to cash unless that is accurate. Written and electronic communications must include the following:

- Disclosure, if applicable, that the investment is not federally insured and the customer may lose money.
- Factors that may affect liquidity or price stability or the issuer's ability to repay its obligation in full.

Previously-approved retail communications may not be used where market or economic developments affect the continued accuracy of characterization of a product as a cash alternative.

19.7 Real Estate Investment Trusts (REITs)

[FINRA Rule 2310; FINRA Regulatory Notice 08-35]

REITs invest in different types of real estate or real estate related assets such as shopping centers, apartment buildings, office buildings, hotels, and mortgages secured by real estate. The three types of REITs include:

- Equity REITs that invest in or own real estate with income principally from rents collected
- Mortgage REITs that lend money to owners and developers or invest in financial instruments secured by mortgages on real estate
- Hybrid REITs that combine the investment strategies of equity and mortgage REITs

REITs trade on national exchanges or in the over-the-counter market; some mutual funds specialize in public real estate. Some REITs invest specifically in one area of real estate (for example, apartment buildings) or in one specific geographic region. REITs generally provide ongoing dividend income along with the potential for long-term capital gains.

19.7.1 General Sales Guidelines

- When determining the suitability of recommending a REIT, consider the investor's investment objectives and need for income and the risks of the REIT including the use of leverage
- Apply a volume discount if it is available
- For unlisted REITs, consider liquidity and marketability and advise the investor of such risks [FINRA Rule 2310(b)(3)(D)]
- Customer account statements may include valuations and disclosures regarding certain REITs [FINRA Rule 2310(b), Notice to Members 01-08]
- Requirements regarding sales contests and cash/non-cash compensation apply to REITs (Refer to the chapter *ORDERS* and the section *Cash And Non-Cash Compensation*) [FINRA Rule 2310, Notice to Members 05-40]

19.7.2 Guidelines for New Issue REITs

- Follow new issue requirements for limiting written communications to the offering document
- When discussing the REIT, base information on the offering document including features and risks of the REIT
- Provide the offering document to the prospective investor

19.8 Callable Common Stock

[FINRA Rule 2232]

Callable common stock is common stock that includes a feature where the issuer or a third party may call the stock away from the shareholder. The price at which the stock is called away may be at a premium to the prevailing market price at the time of the call or at a price or schedule of prices established at the time the stock is issued. Customer confirmations for transactions in callable common stock include a disclosure that the security is callable and that the customer may contact CEI for further information.

Because callable common stock may be called away from a shareholder, RRs should consider this factor when making a suitability determination before recommending the purchase of the stock.

19.9 Promissory Notes

[FINRA Notice to Members 01-79]

Promissory notes are a form of debt similar to a loan. Companies sometimes issue them to raise money for a variety of business needs. The company promises to return the buyer's funds (principal) and make interest payments during the life of the note.

Promissory notes often are deemed securities and must be registered with the SEC and/or the state they are sold in, or they must qualify for an exemption from registration.

When sold through CEI, RRs are required to make suitability determinations before recommending purchase. Considerations include the safety of the note and length of the term of the note. Transactions in promissory notes offered by CEI are subject to review by the designated supervisor.

Individuals or entities outside CEI may attempt to sell unregistered promissory notes through licensed RRs. RRs are reminded that they may only sell securities offered by CEI, unless specifically approved by Compliance.

19.10 Complex Products

[FINRA Regulatory Notice 17-32 and 12-03; IOSCO suitability requirements: <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD373.pdf>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Third party distributors • Orders for complex products • Complex Product Qualification Form • Account records
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • When third parties are used to distribute products originated by CEI: <ul style="list-style-type: none"> ○ Review distributor's sales practices, training, investor education efforts, and compliance efforts including how over-concentration or other potential issues are identified • Subject new complex products to the new product review process • Review applications/orders for (depending on the product): <ul style="list-style-type: none"> ○ Age/retirement status of investor for suitability ○ Compliance with Firm-established suitability guidelines ○ Concentration of the investment in the customer's account and compliance with Firm- and state-established guidelines ○ Compliance with state suitability standards and customer's state of residence liquid net worth definition, state concentration limits ○ Effect of early withdrawal fees, taxes or penalties on the customer and his/her liquid net worth calculation ○ Use of most current version of the application form • Provide training to RRs and supervisors regarding the products, suitability standards, and required reviews • Perform post-issuance review after release of a new complex product including an assessment of whether the product performs in accordance with its design and

	whether distributors and other sellers sold the product to the types of investors for which it was intended
Record	<ul style="list-style-type: none"> • Reviews of third-party distributors • New product reviews and post-issuance reviews if needed • Reviews of applications/orders and action taken, if any • Records of training including who attended, when conducted, subjects included

FINRA guidance has indicated that complex products warrant particular care in how they are scrutinized and sold to retail customers. FINRA indicates that a product that is complex is one that "presents an additional risk to retail investors because its complexity adds a further dimension to the investment decision process beyond the fundamentals of market forces." This is only a general description since all the potential variations in products make it difficult to clearly define the term. The last subsection of this section includes examples of complex products from FINRA Regulatory Notice 12-03.

The complexity of products imposes additional obligations on RRs who sell such products, as well as on CEI to supervise their sale. Other sections in this chapter that discuss specific complex products include:

- *Hedge Funds*
- *Exchange-Traded Funds (leveraged and inverse products or featuring a daily reset)*
- *Commodity Futures-Linked Securities*
- *Non-Conventional Investments (NCIs)*
- *Structured Products*
- *Exempt Insurance Products and Equity-Indexed Annuities*

Some Complex products are also considered Alternative Investments by CEI, and are sold by subscription. In those cases, the Alternative Investment Suitability and Disclosure Form and procedure must be followed. Otherwise, complex products such as leveraged and inverse ETFs, structured notes and CDs, and other NCIs may be purchased for accounts qualified using the CPQ Form.

19.10.1 Approval of The Product

New products are subject to CEI's new product review process, and for complex products, there is a heightened level of review. If a complex product is approved for sale, training and other informational materials will be provided to RRs and, if appropriate, to potential investors. The types of investors suitable for the product will also be identified and communicated to RRs.

19.10.2 Knowledge of The Product

If inexperienced with a type of complex product, the RR will be provided training regarding the features of a complex product. Before recommending complex products, RRs must understand the features and characteristics of the product and any reference asset (where applicable) including its historic performance and volatility and correlation with specific asset classes; any interrelationship between multiple reference assets; the likelihood that the complex product may be called by the issuer; and the extent and limitation of any principal protection. Knowledge of these aspects as well as how the product is expected to perform in normal market conditions and the risks are necessary to be able to present accurate information to prospective investors and to be able to make suitable recommendations.

19.10.3 Suitability of Recommendations

Knowledge of the product is key to making a suitable recommendation. The other key aspects of a suitable recommendation include:

- The customer's investment experience
- The customer's risk tolerance
- Whether the customer is of retirement age or is retired
- The percentage of investments (concentration) the investment will represent
- The effect of early withdrawal including fees, taxes or penalties
- State requirements regarding suitability, concentration, other state requirements
- Firm guidelines regarding suitability, concentration, *etc.* for specific products
- A reasonable basis for believing, at the time of recommendation, that the customer has the knowledge and experience in financial matters that he/she may reasonably be expected to be capable of evaluating the risks
- The customer is financially able to bear the risks of the investment

The RR should discuss the features of the product with retail customers including how it is expected to perform under different market conditions, the risks and possible benefits, scenarios in which the product may perform poorly, and the costs of the product. The RR should consider whether it seems the retail customer understands the basic features of the product such as the fundamental payout structure and the nature of underlying collateral or a reference index or asset.

19.10.4 Other Requirements

There may be other requirements related to the sale of a complex product, including:

- Limits or conditions on the sale of the product, such as concentration limits or limits on the types of investors who may purchase the product
- Investor qualification agreements from the issuer to pre-qualify potential purchasers
- Limitation on purchasers to those who have been approved for option trading, which provides a minimum qualification to participate in the investment

19.10.4.1 Complex Product Qualification Procedure

Some products require each purchase to be submitted by subscription agreement, and such purchases require pre-approval using the Alternative Investment Disclosure Form and approval by the Alternative Investment Supervisor.

Other Products may be purchased without pre-approval so long as a principal has approved the account for complex product investments as follows:

Prior to purchasing a Complex Product, the customer is required to complete and submit the Complex Product Qualification Form ("CPQ") to the RR's designated supervisor.

The supervisor must review the CPQ to confirm whether the customer information supports qualifying a customer for trading in complex products, i.e. whether any complex product might be suitable for the client based upon the representations made by the client on the CPQ. Trading in complex products will be reviewed on the trade blotter on an on-going basis in accordance with the procedures set forth in this manual concerning trade review.

In qualifying a customer account or accounts for trading in complex products, the supervisor will evidence her/his review by signing the CPQ and forwarding to newaccounts@coastal-one.com. Home Office Operations will maintain a log of all accounts qualified for complex product trading. All CPQs will be maintained in the customer's file.

19.10.5 Examples of Complex Products

- Asset-backed securities that are secured by a pool of collateral such as mortgages, payments from consumer credit cards or future royalty payments on popular music, may be difficult for retail investors to understand. With these securities, the creditworthiness of the underlying borrowers or the existence of prepayment risks, though critical to the evaluation of the product, may not be readily apparent to retail investors. Similarly, unlisted REITs may present liquidity and valuation issues for a retail investor.
- Products that include an embedded derivative component that may be difficult to understand, such as those:
 - in which repayment of principal or payment of yield depends upon a reference asset, when information about the performance of the reference asset is not readily available to investors. An example is structured notes with an embedded derivative for which the reference asset is a constant maturity swap rate.
 - that provide for different stated returns throughout the lifetime of the product. For example, "steepener" notes typically offer a relatively high teaser coupon rate for the first year, after which they offer variable rates determined by the steepness of a yield curve. Similarly, some firms have offered structured notes with payoffs contingent on whether one or more reference asset performs within a certain range.
 - under which the investor might incur a capital loss as a result of the fall in the value of the reference asset without being able to participate in an increase in its value. So-called "reverse convertible notes" may fall into this category.
 - in which a change in the performance of the reference asset can have a disproportionate impact on the repayment of capital or on the payment of return. For example, "knock in" or "knock out" features associated with reverse convertible notes, in which a drop in the value of the reference asset to a pre-defined level, can affect determination of an investor's gains or losses.
- Products with contingencies in gains or losses, particularly those that depend upon multiple mechanisms, such as the simultaneous occurrence of several conditions across different asset classes. An example is range accrual notes for which the return of principal can depend upon the value of two or more reference assets on certain pre-defined dates.
- Structured notes with "worst-of" features, which provide payoffs that depend upon the worst performing reference index in a pre-specified group. These notes can limit the return of principal at maturity if either the reference index falls by a stated percentage (*e.g.*, 30 percent) or if any of the reference indices decline in value since the date of issue.
- Investments tied to the performance of markets that may not be well understood by many investors. For example, some exchange-traded products offer retail investors exposure to stock market volatility. Some of these products also provide inverse or leveraged exposure. The investable form of volatility may be in the form of futures on the CBOE Volatility Index (VIX) that reflect the market's expectation of volatility. Some investors may not understand that the product's return may not be based on VIX fluctuations actually experienced on a given day, but on the market's expectation of future volatility.
- Products with principal protection that is conditional or partial, or that can be withdrawn by the product sponsor upon the occurrence of certain events. Notes that can lose their principal protection based upon a stated event represent an example of a product with this feature.
- Product structures that can lead to performance that is significantly different from what an investor may expect, such as products with leveraged returns that are reset daily. Leveraged or inverse exchange-

traded funds exemplify this feature. Many leveraged and inverse ETFs "reset" daily, meaning that they are designed to achieve their stated leverage or inverse objectives on a daily basis. Their performance over longer periods of time can differ significantly from what might be expected based on their daily leverage or inverse factor.

- Products with complicated limits or formulas for the calculation of investor gains. For example, some structured notes have a payout structure that tracks the upside performance of a reference asset one-for-four, but if the reference asset's performance exceeds a specified threshold the payoff is reduced to a much lower, pre-set level, regardless of how it performs afterward.

19.10.6 Structured Products

[FINRA Notice to Members 05-59; Interagency Statement on Complex Structured Financial Transactions: <http://www.sec.gov/rules/policy/2007/34-55043.pdf>; SEC Summary Report of Sweep Examination of Structured Products Sold to Retail Investors: <http://sec.gov/news/press/2011/2011-157.htm>; SEC Risk Alert Broker-Dealer controls regarding retail sales of structured securities product: <https://www.sec.gov/about/offices/ocie/risk-alert-bd-controls-structured-securities-products.pdf>]

<p>Responsibility</p>	<ul style="list-style-type: none"> • RR – obtain CPQ from customer for each account structured products will be purchased • Designated Supervisor - reviews of CPQ, accounts and transactions, correspondence and retail communications • New Product Committee or other supervisor designated to review new products - review new structured products proposed for sale
<p>Resources</p>	<ul style="list-style-type: none"> • Information about a product to be sold • Order records/reports • Account records of option approval
<p>Frequency</p>	<ul style="list-style-type: none"> • As necessary - conduct reviews of new products • Weekly- review of correspondence and retail communications • As necessary - review/approval of advertising • As necessary - conduct training regarding products • Approve accounts, review transactions
<p>Action</p>	<ul style="list-style-type: none"> • Submit a new structured product to the new product review process as outlined in the chapter <i>FINANCIAL AND OPERATIONS PROCEDURES - Risk Management - New Products</i> particularly considering necessary disclosures when selling the product • Supervisor/Compliance: <ul style="list-style-type: none"> ○ Review advertising • Train supervisors and RRs regarding structured products in general and about the specifics of individual products to be offered, as needed • Review purchases of structured products <ul style="list-style-type: none"> ○ For retail accounts, conduct reviews for suitability including determination that the structured product meets the customer's stated investment objectives ○ Identify customer concentrations in structured products and determine suitability ○ Confirm necessary disclosures were provided

	<ul style="list-style-type: none"> • If CEI trades structured products, conduct independent reviews of desk prices in the secondary market
Record	<ul style="list-style-type: none"> • New product approval including due diligence reviews and determination of necessary disclosures • Supervisor/Compliance: Advertising reviewed • Customer account review for suitability to purchase structured products • CPQ Forms • Records of training including when conducted, who attended, and subjects included • Reviews of pricing in the secondary market (if applicable)

Structured products generally are securities that are derived from or based on a single security, a basket of securities, an index, a commodity, a debt issuance and/or a foreign security. There are many variations of structured products and different features such as principal protection; payment of interest above market rates; and capping upside participation. Structured products have a fixed maturity and some may be listed while others are thinly traded.

Structured products typically have two components, a note and a derivative (often an option). The note pays interest at a specified rate and interval while the derivative establishes the payment at maturity. Structured products are generally subject to the requirements for public offerings of securities under the '33 Act and are usually offered from a shelf registration.

Principal-protected notes are discussed in a specific subsection.

19.10.6.1 Public Communications

All correspondence and retail communications and oral communications must be fair and balanced regarding risks and benefits. Communications must be clear and not misleading and should enable an investor to evaluate the investment from a risk/reward perspective. If returns are discussed, it should be clearly disclosed how returns are linked to an underlying asset. Advertising and written promotional material (brochures, written presentations provided to multiple investors) must be approved by Compliance prior to distribution consistent with the requirements in the section *Retail Communications* in the chapter *COMMUNICATIONS WITH THE PUBLIC*.

The following are necessary disclosures about principal-protected notes, where appropriate:

- The level of principal protection offered
- The credit-worthiness of the guarantor
- The potential returns and pay-out structure (including any limits on upside potential)
- The investor's ability to access funds pending maturity date or the expiration of a lock-up period
- Any costs or fees that might affect the return of principal
- Description of the derivative component of the product (cannot be represented as ordinary debt securities)
- Statements about the product having a ticker symbol or is approved for listing balanced with risks that an active and liquid trading market may not develop

19.10.6.2 Suitability

Because of the potential complexity of structured products, RRs must determine the suitability of potential purchasers, including the customer's:

- financial situation including income and liquid net worth
- age
- investment experience
- ability to bear the risks involved with the product
- knowledge and experience in financial matters that the customer can be reasonably expected to be capable of evaluating the risks of the recommended transaction

RRs should inform the customer of the features of the structured product being recommended. Recommendations may only be made to eligible customers in accounts approved for complex product purchases.

19.10.6.3 Risk Disclosure

It is important that investors understand the risks involved in structured product investments. If a prospectus or risk disclosure statement is available for the product being offered, it must be provided prior to any purchase. RRs must discuss the following risks with potential individual investors:

- General types of risks associated with structured products
- Any risk not usually associated with a given product, such as risk of loss due to any sale of the product before maturity
- Any material product-specific risk such as risks arising from the underlying asset, liquidity and market risks in relation to the product itself, or specific tax considerations
- Acknowledgment of limitations on available data
- The distinction between the underlying asset and the structured product based on the asset
- For principal-protected products, that the principal protection applies only at maturity and the costs of unwinding the product mean an earlier redemption value which may differ significantly from maturity value
- Availability or lack of availability of a secondary market to liquidate the investment
- Sales in the secondary market may be at significantly discounted value to the original investment
- Tax implications (if applicable) and the potential need to consult with the investor's accountant, tax attorney, or other tax professional

19.10.6.4 Fees and Costs

Fees, costs, commissions, discounts, and any other amounts paid at the time of purchase or for acting as such, over the life of that product, must be disclosed to investors.

19.10.6.5 Credit Ratings

Credit ratings of issuers (or guarantors) may not represent a rating of the structured product. If credit ratings are disclosed to potential investors, disclosure must make clear the significance of the rating in relation to the investment.

19.10.6.6 Tax Implications

Investment in structured products may have tax consequences for individual investors depending on their personal circumstances and jurisdiction of residence. Although certain tax implications may be highlighted in

product documents, investors should be encouraged to discuss the specific tax implications of structured products with their accountant, tax attorney, or other tax professional.

19.10.6.7 Post-Trade Information

Where available, CEI will provide information to RRs and/or investors to enable them to monitor performance of structured products and provide access to information regarding the terms of the product including maturity, pay-out details, secondary market price, and other pertinent information.

19.10.6.8 Features and Risks of Structured Products

Each structured product will have different features and it is the RR's responsibility to understand those features before making a recommendation. Following are some features that must be communicated to the customer (depending on the product) before a structured product is purchased:

- **Principal protection:** Some products offer full upside protection or have a cap; no dividends are paid. Principal protection may mature within one to seven years and investors must hold them until maturity to guarantee the principal's return. Maturities shorter than 5 years usually cap returns.
- **Buffered return-enhanced notes:** Usually linked to the performance of a market index and issued as senior unsecured debt obligations that mature within one to five years and trade in \$1,000 increments. There is no dividend or interest income and gains are taxed as long-term capital gains if the investment is held un-hedged for more than one year. Buffered notes provide partial principal protection with the buffer ranging from 10% to 15%.
- **Return-enhanced notes:** The investor gives up the right to participate in market gains over a period in exchange for a payout at maturity that may be 2 or 3 times the return of a benchmark index. Maturities generally range from 1 to 3 years and trade in \$1,000 increments. They have a cap and provide no protection against market declines, and there is no dividend income.
- **Reverse convertibles:** This product is linked to a particular stock, basket of stocks or index and pay a fixed coupon that provides some protection from loss. The registered notes mature within one year or less and trade in \$1,000 increments. They typically carry a coupon of between 10% and 20% and the upside is limited to the coupon amount. If the underlying stock falls below a set "barrier" level, the investor may get significantly lower-valued stock instead of cash upon maturity. If the underlying stock is volatile, risk is significantly increased. Investors who try to sell a reverse convertible before maturity may lose money since there may not be much demand for the notes, especially in a down market.

19.10.7 Principal-Protected Notes (PPNs)

[FINRA Regulatory Notice 09-73; SEC Investor Alert: <http://sec.gov/news/press/2011/2011-118.htm>]

PPN in this section refers to any structured product that combines a bond with a derivative component and that guarantees a full or partial return of principal at maturity. Sales of PPNs to retail customers are subject to particular considerations explained in this section:

- While products may be described as "guaranteed," principal protection, absolute return, minimum return, the degree of guarantee, protection, risk, and return vary depending on the specific features of the note being sold.
- The suitability of recommendations must take these features into consideration as well as the customer's objectives, needs, and willingness/ability to sustain risk.

19.10.7.1 Features of PPNs

PPNs typically combine a zero-coupon bond with an option or other derivative product with a payoff linked to an underlying asset such as an equities index or basket of indices. There is a guarantee of a return of some or all principal at a maturity date which may be up to 10 years from issuance and participation in a return linked to a specific change in the value of the underlying asset.

RRs should review FINRA Regulatory Notice 09-73 for illustrations of how returns and guarantees may vary depending on how the note is structured.

19.10.7.2 Suitability Considerations

The following are factors to consider when recommending PPNs.

- The credit-worthiness of the guarantor and the nature and terms of guarantees
- The investment's pay-out structure, costs and fees
- The customer's need for access to their money before the maturity date arrives or a lock-up period expires
- The call risk of callable notes
- Tax consequences such as a note invested in zero-coupon bonds which could result in paying tax on imputed interest as it accrues
- Fees and costs
- Lack of inflation protection since principal guarantee generally relates to nominal principal

19.10.8 Reverse Convertible

[FINRA Regulatory Notice 10-09]

A reverse convertible is a structured product that has features that should be communicated to potential retail investors before recommending the security. Relevant features potentially include the following:

- **How the product works** including pay-out structure, relevant information about the reference asset, and, if applicable, that the investor will not participate in any appreciation in the value of the reference asset.
- **Return of principal.** Instead of a full return of principal at maturity, the investor could receive less than a full return of principal if the value of the reference asset has fallen below a certain level, often referred to as the "knock-in" or "barrier" level. Depending on the underlying asset, the investor could receive a predetermined number of shares of common stock (or cash equivalent), which would amount to less than the investor's original investment.
- **Pay-out structure.** Pay-out structures may involve multiple variables that affect risk, cost, and potential benefits. The RR should have an understanding so these variables may be communicated to the investor.
- **Sale of product prior to maturity.** The ability to sell and the potential selling price may depend on the willingness of the issuer or another party to maintain a secondary market.
- **Issuance of research by the Firm.** If applicable, disclose to the investor that CEI has published its own research reports regarding the reference asset, the content of the research and how the research is or is not relevant to a recommendation to purchase or sell the reverse convertible.

Communications, whether directly with a potential investor or through advertising or other communications, must be truthful and not contain any exaggerations. Following are restrictions and guidelines on communications:

- Reverse convertibles should **not** be described as ordinary debt securities.

- Any reference to the product's credit rating cannot suggest that the rating has any bearing on the expected performance of the reference asset, nor may it exaggerate the probability that the investor will receive a full return of principal.
- Annualized yield or coupon information cannot be presented in a misleading manner. For example, a 10% per annum coupon provides an actual return of roughly 2.5% (based on a 360-day year) over a 3-month term. Communications about products that mature in less than a year must balance communication about annualized yield with prominent disclosure of the actual percentage return and the term of the note.

19.10.9 Exchange Traded Notes (ETNs)

[FINRA Investor Alert: <https://www.finra.org/investors/alerts/exchange-traded-notes-avoid-unpleasant-surprises>; NYSE Informed Investor: What You Should Know About Exchange Traded Notes: https://etp.euronext.com/sites/etp.euronext.com/files/etf_informed_investor.pdf]

ETNs are unsecured debt obligations of an issuer which typically is a bank or another financial institution. RRs must be familiar with the features and risks of ETNs before recommending them, and explain features to prospective investors. The complexity of an ETN is a factor to consider before recommending it to an investor.

Features include the following:

- ETNs are sold by prospectus which must be provided to the investor.
- ETNs usually do not pay interest but rather make distributions determined by the performance of an underlying index or benchmark on the ETN's maturity date (which may be 10, 30, or 40 years from issuance) minus fees. An individual ETN may or may not provide for periodic payments or cash distributions prior to maturity.
- Underlying indexes may be familiar and broad-based or less familiar asset classes or complex and sometimes proprietary indexes.
- Some ETNs offer leveraged exposure to the index or benchmark they track.
- Leveraged and inverse ETNs are short-term trading investments not intended for long-term investing.
- The creditworthiness of the issuer is important since the ETN itself is not rated.
- ETNs may have a repurchase feature allowing qualified investors to redeem notes of a minimum denomination or value daily or weekly at a predetermined price. Other investors may sell in an available secondary market (ETNs are often listed), sell if called by the issuer, or allow them to mature.
- The issuer charges an annual fee through the term of the ETN. Fees are explained in the prospectus.
- ETNs trade on exchanges; the sales price in the secondary market is determined by supply and demand. ETNs do not sell at net asset value (NAV).

Risks include:

- As unsecured debt obligations, the issuer may default on the note.
- ETNs are influenced by the value of the underlying index subjecting the investor to market risk.
- A trading market may not develop, even though an ETN is listed on an exchange.
- An ETN's market price may not track the underlying index.
- Some ETNs (particularly some leveraged, inverse and inverse leveraged) are short-term trading tools that may reset daily. The performance of these products over long periods can differ significantly from the stated multiple of the performance (or inverse performance) of the underlying index or benchmark.
- ETNs containing components traded in foreign currencies are subject to foreign currency exchange risk.
- Some ETNs are callable at the issuer's discretion; the notes may be called when the investor may incur a loss.
- The issuer may engage in trading activities at odds with investors who hold the notes.

19.10.10 Training

If a RR who desires to recommend such products is inexperienced in the judgment of the supervisor or any firm principal, training will be provided to RRs regarding the general features of structured products and requirements when making recommendations. Additional training may be provided for individual products.

Training will generally include:

- Risks associated with such products including the credit-worthiness of the guarantor, if applicable
- Terms and conditions, including the pay-out structure
- Underlying indices, assets, or benchmark
- The investment's potential for growth and risks associated with the investment
- Fee structure
- Other features that might impact the product's suitability generally or specific to customers

19.11 Alternative Investments

Alternative Investments include all non-traded direct investment programs, such as BDCs, DPPs, REITs, Equipment Leasing investments, Hedge Funds, Oil and Gas investments, and Private Equity. Specific Alternative Investments are discussed in more detail below and in other sections of CEI's WSPs, including DPPs and NON-TRADED REITS and PRIVATE PLACEMENTS.

RRs must have the customer complete CEI's Alternative Investment Suitability Form ("AISF") after discussing the product's features and risks with the customer. The RR is responsible for determining whether the customer is qualified to purchase the investment, including, but not limited to, whether the investor must be an "accredited investor", whether the investment is suitable for the customer, and whether the investor's liquid net worth meets firm suitability requirements, the issuer's suitability requirements, and the applicable State Law set forth in the product's prospectus or PPM. The RR will then submit the form and subscription documents to the Alternative Products Supervisor for review and approval. Once approved, the signed document will be returned to the RR for submission to the applicable sponsor for purchase.

CEI's policy includes a concentration limit of Alternative Investments which progresses on a sliding scale depending on certain suitability factors. Those factors are identified on the AISF. Investments over \$100,000 in an offering require the Alternative Investment Supervisor to request additional approval from either the COO or CEO, or their designee. Any such designee shall be a firm principal.

Because of the unique nature of certain investments and the strategies inherent in the products, exceptions to the concentration limit on the AISF may be granted by the AI Supervisor, or in consultation with a senior principal of the firm, on a case-by-case basis.

The Alternative Investment Supervisor will review the AISF to confirm the suitability analysis and a "Look-back" review by reviewing the customer's prior AISF's, if any, to review changes in the customer's financial profile and concentration levels.

Approved investments will be maintained in the customer's file, and on the direct business log.

19.11.1 Private and Non-traded REITs

[FINRA Regulatory Notice 13-18]

Responsibility	<ul style="list-style-type: none">• AI Supervisor
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Resources	<ul style="list-style-type: none"> • Private and non-traded REITs
Frequency	<ul style="list-style-type: none"> • As determined by New Product Committee
Action	<ul style="list-style-type: none"> • Subject REITs to new product review when initially to be offered • Periodically conduct due diligence reviews to confirm the types of investors for whom the product is suitable or to discontinue sales
Record	<ul style="list-style-type: none"> • New product review • Periodic reviews and determinations

Private and non-traded REITs are companies whose shares do not trade on a national stock exchange. They generally operate like unit investment trusts by purchasing assets that are held for a fixed amount of time, often 7 to 10 years, and will sell the properties, merge with another entity, or register an IPO in order to provide an exit for the fund and deliver returns to shareholders.

There are features and risks which RRs must be familiar with prior to recommending a private or non-traded REIT.

- Sales costs are deducted from the offering price.
- The investment is illiquid during the term of investment which may be 7 to 10 years. Trying to liquidate the investment earlier is often difficult or costly or may be impossible.
- Many companies offer some form of redemption plan but these are very limited, often limited to 3% of the shares outstanding in a year and involve a significant penalty.
- The fixed portfolio and long-term horizon provide a level of stability since the REIT is not required to sell properties to meet investor liquidation requirements.
- Non-traded REITs pay monthly or quarterly dividends which may be higher than publicly-traded REITs; however, dividends are not guaranteed.
- Dividends may include repayment of principal in early stages of the program.
- Private REITs are not required to provide the same level of quarterly disclosure as publicly-traded REITs.
- They impose minimum income and/or net worth requirements; RRs are obligated to determine the investor meets the requirements and completes any necessary subscription agreements.

Refer to the section *Communications Regarding Unlisted Real Estate Programs* in the chapter *DIRECT PARTICIPATION PROGRAMS AND REITS* for details regarding FINRA guidance on communications about real estate programs.

19.11.2 Hedge Funds and Private Funds

[FINRA Notice to Members 03-07]

Responsibility	<ul style="list-style-type: none"> • AI Supervisor • New Product Committee
Resources	<ul style="list-style-type: none"> • Information from issuer • Subscription agreements • Customer account information and AIDF
Frequency	<ul style="list-style-type: none"> • As required

Action	<ul style="list-style-type: none"> • Conduct due diligence for any proposed hedge fund investment to be offered to customers • Provide information and training regarding hedge fund investments in general and about issues to be sold • Review subscription agreements for completeness and suitability of investment for the customer, considering account information on file with CEI • Approve or disapprove subscription agreements
Record	<ul style="list-style-type: none"> • Due diligence file including record of reviews, references, <i>etc.</i> • Notation and date of approval or disapproval, to offer the securities • Subscription agreement file including signature/initials of reviewer and approval or disapproval

This section describes the RR's obligations when selling hedge funds to customers. Funds of hedge funds are discussed in the chapter *MUTUAL FUNDS*.

19.11.2.1 Definition

A hedge fund includes 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 vary in size and trading strategies, including categories such as: relative value hedge funds, event driven hedge funds, equity hedge funds, global asset allocator hedge funds, short selling hedge funds, sectoral hedge funds, and market neutral hedge funds. Most hedge funds are not registered.

19.11.2.2 Features of Hedge Funds

Many hedge funds have the following features:

- not registered under the Investment Company Act and exempt from registration under the '33 Act
- high minimum investments, often \$1,000,000 or more
- wide differences in the fees for investments in registered vs. unregistered hedge funds. Managers of unregistered hedge funds may receive both a management fee and a direct percentage in the profits earned

19.11.2.3 Promotion of Hedge Funds

Correspondence, retail communications and oral presentations promoting hedge funds must be balanced to include the risks and potential disadvantages of the investment. Specific items that may NOT be included are statements that hedge funds offer:

- superior professional management with more investment flexibility
- protection against declining markets
- better returns due to the imposition of performance fees
- target returns unless sales literature referring to the target provides enough information to substantiate and provide a sound basis for the target

unless these statements are fair, accurate, and without exaggeration.

Risks that must be disclosed are that hedge funds:

- often engage in leveraging and other speculative investment practices that may increase the risk of investment loss;
- can be highly illiquid;
- are not required to provide periodic pricing or valuation information to investors;
- may involve complex tax structures and delays in distributing important tax information;
- are not subject to the same regulatory requirements as mutual funds; and,
- often charge high fees.

Investors must be provided with any prospectus or other disclosure document of the hedge fund.

19.11.2.4 Private Funds

Many other alternative investments take form as a private fund and employ varying strategies. CEI considers those funds Alternative Investments embodying similar risks to hedge funds in that they are non-transparent, illiquid, and high risk investments. Private Funds are usually sold as LP or LLC units. The sections concerning Direct Participation Programs and Private Placements apply to Private Fund offerings.

19.11.2.5 Suitability

19.11.2.5.1 Due Diligence

Unregistered funds are usually offered through private placements. CEI will conduct due diligence prior to offering hedge funds to customers, including the following:

- investigation of the background of the hedge fund manager
- reviewing the offering memorandum
- reviewing subscription agreements
- examining references
- examining the relative performance of the fund
- other due diligence reviews determined by the reviewer

19.11.2.5.2 Customer Suitability

Historically private funds have only been available to high net-worth individuals or institutions. Access to some hedge funds has been expanded to include other investors. Prior to recommending a hedge fund or private fund to a customer, the RR is obligated to:

- Understand the risks and features of the investment.
- Consider the structure and nature of the hedge fund, particularly whether the hedge fund has "side-pocket" accounts that hold hard-to-value investments that may affect liquidity and limit the ability to determine the value of the fund.
- Determine suitability considering the usual factors including financial status, tax status, investment objectives, and other information reasonable for determining suitability. A customer's level of assets does not, in and of itself, meet suitability requirements. The fact that a customer is an "accredited investor" under Regulation D does not, alone, satisfy the obligation.

19.11.2.5.3 Subscription Agreement

A subscription agreement, including suitability requirements, must be completed for each investor prior to purchase. Subscription Agreements will be reviewed by the supervisor for completeness and the appropriateness of the investment for the customer.

19.11.3 Direct Participation Programs (DPPs)

[FINRA Rule 2310]

DPPs are primarily suitable for customers who need tax advantages on passive income. DPPs can be a method of obtaining appreciation of capital. Each DPP has specified suitability standards including information such as the purchaser's net worth. Following are features and requirements of DPPs:

- RRs should reasonably determine that the customer understands the ramifications of not having a high enough tax bracket or not enough passive income to receive benefits of a DPP's partnership flow-through concept.
- RRs are responsible for obtaining the required subscription agreement or, if no agreement is required, determining that the customer meets the standards outlined in the prospectus and completing the Suitability Questionnaire.
- While there may be a secondary market for particular DPPs, they may have limited liquidity and should be considered a long-term investment.
- Secondary market transactions must be recorded in CEI's order records including the time of execution.
- CEI will use FINRA standard transfer forms for secondary market transactions.
- Limited partners in rollup transactions will be provided a disclosure outlining information about the rollup.

19.11.4 Section 1031 Tenants-In-Common Exchanges

[Internal Revenue Code Section 1031; IRS Revenue Procedure 2002-22; FINRA Notice to Members 05-18]

Section 1031 of the Internal Revenue Code allows an investor in income-producing or rental real estate to exchange the investment for another like investment of equal or greater value and defer payment of capital gains tax on the original investment. To qualify for the deferral, the investor must acquire an interest in real estate in exchange, and not an interest in a partnership. TIC exchanges receive favorable tax treatment. A 1031 exchange by TIC would qualify for deferral only if the TIC and the transaction meet 15 IRS conditions outlined in Revenue Procedure 2002-22.

TIC interests offered and sold together with other arrangements generally constitute securities under federal securities laws. FINRA considers TIC interests to be a type of non-conventional investment (NCI) which is subject to due diligence, suitability, training, and internal control requirements. 1031 exchanges facilitated by CEI must comply with requirements in the section *Non-Conventional Investments* in this chapter.

FINRA Notice to Members 05-18 should be referenced for a detailed discussion of tenants-in-common interests.

20 DIRECT PARTICIPATION PROGRAMS AND REITS

[FINRA Rule 2231(c) and 2310; FINRA Regulatory Notice 15-02]

Responsibility	<ul style="list-style-type: none"> • Alternative Investments Supervisor
Resources	<ul style="list-style-type: none"> • Information about the sponsor/issuer • Subscription agreements • Other purchase records/Alternative Investment Suitability Form
Frequency	<ul style="list-style-type: none"> • As required when DPPs are offered
Action	<ul style="list-style-type: none"> • For new issues where CEI may act as underwriter: <ul style="list-style-type: none"> ○ Confirm the sponsor or general partner of the DPP or REIT will make required value disclosures in annual reports to investors ○ Conduct due diligence ○ Confirm expenses and compensation are within guidelines ○ Review agreements for completeness • Determine customer qualifies for purchase depending on suitability standards • Review recommended DPP orders for compliance with Regulation BI [see the chapter <i>REGULATION BEST INTEREST (BI)</i>] • Approve or disapprove purchase • Provide liquidity disclosure, if required
Record	<ul style="list-style-type: none"> • Review for required general partner/sponsor value reports to investors, due diligence, expense/compensation reviews, FINRA no objection opinion, and agreements or other purchase records retained in due diligence file

FINRA defines Direct Participation Programs as any "program which provides for flow-through tax consequences regardless of the legal entity or vehicle for distribution including, but not limited to, oil and gas 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." Direct participation programs are also often called "limited partnership" investments.

This chapter outlines CEI's procedures regarding the sale of Direct Participation Programs (DPPs). It also includes procedures (appearing at the end of this chapter) for real estate investment programs which are DPPs and REITs which are subject to the rules governing corporate underwritings and general underwriting procedures.

DPPs are subject to suitability requirements as well as Regulation Best Interest (BI). Recommendations to retail customers who are natural persons are subject to Reg BI which is broader than the suitability requirement. Reg BI includes recommendations for orders; types of accounts; and investment strategies, including recommendations to prospects. ALL natural persons are included in Reg BI including those deemed "institutional investors" under other FINRA rules.

20.1 New Issues

[FINRA Rule 2310(b)]

New issue requirements apply to DPPs and REITs as well as rollup transactions, in some instances.

20.2.1 Due Diligence

CEI has appointed a Due Diligence Supervisor who is responsible for reviewing prospectuses on any proposed DPP offerings and referring them to management with his/her recommendation and analysis. Prior to participating in a direct participation program:

- CEI must confirm that the general partner or sponsor will disclose a per share estimated value in each annual report, as defined by rule.
- CEI must have reasonable grounds to believe that all material facts are adequately and accurately disclosed and provide a basis for evaluating the program.
- To determine the adequacy of the disclosed facts, CEI will obtain information on material facts relating to (among other things) the financial stability and experience of the sponsor and the program's risk factors. This includes, for an REIT, an inquiry into the amount or composition of a real estate investment program's dividend distributions including the amount of distributions that represent a return of investors' capital and whether the amount is changing.
- For REITs, CEI will also consider whether there are impairments to the real estate investment program's assets or other material events that would affect the distributions and whether disclosure regarding dividend distributions needs to be updated to reflect these events.
- For DPPs, suitability standards must have been established by the program for participants in the program.

Per FINRA rules, the following minimum material facts should be disclosed in the prospectus:

- items of compensation
- physical properties
- tax aspects
- financial stability and experience of the sponsor
- the program's conflicts and risk factors
- appraisals and other pertinent reports

If CEI is a participant in an offering underwritten by another firm, it may rely on the managing underwriter's due diligence under the following guidelines:

- CEI has reasonable grounds to believe that the managing underwriter's inquiry was conducted with due care;
- The results of the other firm's due diligence inquiry were provided to CEI with the consent of the firm or firms that conducted the due diligence inquiry; and,
- The firm that conducted or participated in the inquiry is not a sponsor or affiliated with the sponsor of the DPP.

20.2.2 Expenses and Compensation

Prior to participating in a public offering of a DPP (unless the filing is made by another participant), CEI will make the required filing with the FINRA Corporate Financing Department. Prior to offering the DPP, CEI must receive a "no objections" opinion regarding the proposed terms and arrangements in the offering. The following sections explain key requirements that are considered by FINRA.

20.2.2.1 Organization and Offering Expenses

Organization And Offering Expenses (O&O expenses) are limited to 15% of the gross proceeds of the offering. O&O expenses are comprised of: (1) issuer expenses reimbursed or paid for with offering proceeds; (2) underwriting compensation; and (3) due diligence expenses. These elements are explained in the next three sections.

20.2.2.2 Issuer Expenses

Issuer expenses include:

- assembling and mailing offering materials, processing subscription agreements and generating advertising and sales materials
- legal and account services provided to the sponsor or issuer
- salaries and non-transaction-based compensation paid to employees or agents of the sponsor or issuer for performing services for the issuer
- transfer agents, escrow holders, depositories, engineers and other experts
- registration and qualification of securities under federal and state law, including taxes and fees and FINRA fees

FINRA will consider unaccountable payments to a sponsor or issuer or payments identified as "miscellaneous" as issuer expenses includable in underwriting compensation.

20.2.2.3 Underwriting Compensation

Underwriting compensation from whatever source paid to underwriters, broker-dealers or affiliates is limited to 10% of the gross proceeds of the offering. The 10% limit is included as part of the 15% limit on O&O expenses. Refer to Regulatory Notice 08-35 for a detailed explanation of the types of compensation considered underwriting compensation.

20.2.2.4 Due Diligence Expenses

All bona fide due diligence expenses included on a detailed and itemized invoice detailing such expenses are included as part of the O&O expenses. The amount of due diligence expenses may be treated in the calculation of underwriting compensation as a non-accountable expense provided that, when aggregated with all other non-accountable expenses, the amount does not exceed 3% of the offering proceeds.

20.2.2.5 Allocation of Compensation

Rule 2310 (and Regulatory Notice 08-35) outlines specific requirements for allocating employee compensation as underwriting compensation. The Rule and Notice should be consulted for specific guidance when considering what is included as underwriting compensation.

20.2.3 Suitability

[FINRA Rule 2310]

Each DPP will have specified suitability standards including information such as the purchaser's income and net worth. Offerings that require a subscription agreement that is signed by the purchaser will include an affirmation that the customer meets the minimum suitability standards. For offerings where a subscription agreement is not required, the RR is responsible for ensuring the purchaser meets the standards outlined in the prospectus.

Suitability is only one element of acting in a customer's best interest. Recommendations to retail customers who are natural persons are subject to Regulation Best Interest (BI) which is broader than the suitability requirement. Reg BI includes recommendations for orders; types of accounts; and investment strategies, including recommendations to prospects. It is important to be familiar with those requirements which are included in the chapter *REGULATION BEST INTEREST (BI)*.

The RR will complete an Alternative Investment Suitability Form (AISF) for each purchaser of a DPP. The Alternative Investments Supervisor or designee (must be a firm principal) is responsible for ensuring required AISF has been received prior to approving purchases and returning to the RR for submission to the product sponsor. The approved and signed AISF along with the subscription agreement will be forwarded to the Home Office to log the purchase in the direct business blotter and for filing.

20.2.4 Subscription Agreements

The Alternative Investments Supervisor is responsible for the following:

- Ensuring completed and signed agreements are on file, when required, prior to confirming purchases.
- Retaining copies of the signed subscription agreements in a file for the DPP offering by forwarding them, along with the AISF and any ancillary documents, to the Home Office at newaccounts@coastal-one.com. The documents will be filed electronically in the direct business file.

20.2.5 Prospectuses

Prospectuses or PPMs will be provided to all purchasers of DPP offerings. A prospectus or PPM will be included with the subscription documents and receipt confirmed by the customer on the AISF, including the date provided.

20.2.6 Liquidity Disclosure

Disclosure will be provided to prospective investors if the sponsor has offered prior DPPs for which the prospectus disclosed a date or time period when the program might be liquidated, and whether the prior programs in fact liquidated on or around that date or time period. This information is provided on the AISF.

20.3 Rollups

[FINRA Rule 2310(b)(6); FINRA Notice to Members 94-70]

20.3.1 Introduction

All rollup transactions in which CEI participates will be conducted in accordance with the Limited Partnership Reform Act and applicable FINRA rules. The purpose of the Act and the rules is to ensure fair treatment and protect the rights of limited partners whose partnership interests are proposed for restructuring. Compensation and the rollup's structure must meet fairness requirements included in rule requirements.

The AI supervisor is responsible for ensuring all rollup transactions comply with requirements included in the Act and FINRA rules.

20.3.2 Standard Agreement

The AI supervisor will execute a standard agreement with the general partner of the limited partnership subject to the rollup transaction. The agreement will outline the terms of the rollup including compliance with requirements to protect the rights of the limited partners. The agreement will be retained in a file for the rollup transaction.

20.3.3 Disclosure Letter

The Alternative Investments Supervisor will provide a disclosure letter to limited partners, outlining pertinent information regarding the rollup transaction. A record of to whom and when disclosures were sent will be retained by the designated supervisor in a file for the rollup transaction.

20.4 Secondary Market Transactions

[FINRA Notice to Members 91-69]

20.4.1 Order Records

Each secondary market transaction in a Direct Participation Program will be recorded in order records (written or electronic) that will include the time of execution, which is defined as the time the parties have agreed to the essential terms of the transaction.

20.4.2 Reporting Transactions

[FINRA Rule 6622; FINRA Regulatory Notice 10-24; FINRA Notice to Members 97-8]

Secondary market transactions in non-exchange listed direct participation program (DPP) securities must be reported to FINRA within 30 seconds of execution. The "date of execution" and the "time of execution" are defined as the date and time, respectively, when the parties to a transaction in a DPP have agreed to all of the essential terms of the transaction, including the price and number of units to be traded.

Those required to report are as follows:

- Between two members, the executing party reports
- Between a member and a customer, the member reports

The designated trader is responsible for reporting secondary DPP transactions.

20.4.3 Standard Transfer Forms

[FINRA Notice to Members 96-14]

CEI will use the standard transfer forms prescribed by FINRA when limited partnerships are sold in the secondary market. This requirement does not apply to limited partnership securities which are traded on NASDAQ or a registered national securities exchange.

20.5 Communications Regarding Unlisted Real Estate Programs

[FINRA Regulatory Notice 13-18; SEC Division of Corporate Finance guidance: <http://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic3.htm>]

There are FINRA guidelines for communications concerning unlisted real estate investment programs (real estate programs) which include REITs or DPPs that invest in real estate assets or mortgages and that are not listed on a national securities exchange. Following is a summary of the guidance; refer to FINRA Regulatory Notice 13-18 for details.

- **Disclosure:** When describing real estate programs, communications must accurately and fairly explain how the products operate. Communications must be consistent with the program's current prospectus and must not imply an investment in the program is a direct investment in real estate or other assets. If the program has not yet qualified for REIT status under the U.S. tax code, communications must disclose

that the program has not yet qualified and that it may never qualify for REIT status. Potential benefits must be balanced with disclosure of potential risks, which must be presented in a clear and prominent manner (not in a footnote and not in a separate document such as the prospectus even if the communication is accompanied or preceded by a prospectus).

- **Distribution Rates:** Distributions from real estate programs sometimes include return of capital. The composition of distributions may not be misrepresented or described as a yield comparable to a fixed income investment. FINRA's guidance states that communications should include clear and prominent disclosure (as applicable):
 - That distributions are not guaranteed and may be modified;
 - If the distribution consists of return of principal (including offering proceeds) or borrowings, include a breakdown of the components of the distribution rate that represent cash flows, return of principal, and borrowing;
 - The time period during which distributions have been funded from return of principal (including offering proceeds), borrowings or any sources other than cash flows from investment or operations;
 - That distributions that include return of principal will lessen the money available for the program to invest, which may lower overall returns; and
 - If distributions include borrowed funds, that because borrowed funds were used to pay distributions, the distribution rate may not be sustainable.Communications may not include an annualized distribution rate until the program has paid distributions that are, on an annualized basis, at a minimum equal to that rate for at least two consecutive quarterly periods.
- **Stability/Volatility Claims:**
 - Communications may not assert or imply that the value of a real estate program is stable or that volatility is limited without providing a sound basis to evaluate this claim.
 - Communications may not state that the offering price at par value or at another relatively stable price evidences stability in the value of the underlying assets.
 - Representations that the offering price is stable or volatility is limited must include disclosure that the value of underlying assets will fluctuate, may be worth less than what the program initially paid, and that the investor may not be able to sell the investment.
- **Redemption Features and Liquidity Events:**
 - Restrictions and limitations on redemption features (such as the fact that the real estate program's management may terminate or modify the ability to redeem) must be clearly and prominently explained.
 - Communications must disclose if the real estate program has not satisfied all investor redemption requests in the past.
 - Any discussion about potential liquidity events or the timing of such events should disclose if the date of the liquidity event is not guaranteed if it may be changed at the program's discretion.
- **Performance of Prior Related Real Estate Programs:** Discussions of prior or historical performance of related or affiliated entities should include information about such related entities with equal prominence, may not "cherry pick" those favorable to the current program, and should be clearly differentiated from information regarding the current program.
- **Use of Indices and Comparisons:** Communications about real estate programs sometimes include a real estate index's performance to demonstrate the sector's risk or return characteristics. The use of index performance may be misleading if its underlying components do not correspond with those of the program's portfolio. Communications that compare a real estate program against a real estate index must indicate that the performance of the index does not reflect a particular program and must describe the index's components and any relevant differences between the index and the program's investments.

- **Pictures of Specific Properties:** Where a communication includes pictures or images of properties that are not owned by the real estate program - such as similar properties owned by other programs the sponsor manages or properties that are collateral for mortgages owned by the program - the pictures must include prominent text explaining that the property is not owned by the program.
- **Capitalization Rates:** Communications may include the capitalization rate of an individual property within a real estate program if the rate is based on current information contained in the prospectus, and the communication explains (i) how the rate was calculated, (ii) that the rate applies to the individual property, and (iii) that it does not reflect a return or distribution from the program itself. In general it is misleading to include a blended capitalization rate representing multiple individual properties as the factors that go into such rates will differ between individual properties.

21 PRIVATE PLACEMENTS AND OFFERINGS

[FINRA Rule 5122 and 5123; FINRA Frequently Asked Questions: <https://www.finra.org/rules-guidance/guidance/faqs/private-placement-frequently-asked-questions-faq>; Securities Act Regulation D Rule 504, Rule 506(b) and Rule 506(c)]

This chapter explains the requirements when offering private placements and engaging in private offerings. Private placements and offerings are subject to strict requirements that are imposed on the issuer and those who sell the issue. The requirements for offering a specific private placement will be announced at the time the private placement becomes available for sale. It is important to understand and comply with the requirements for each offering.

Coastal may participate in an offering in one of two ways, or both: as Managing Broker Dealer offering a private placement to an institutional selling group, as a Selling Group Participant selling to both retail and institutional investors. When Coastal acts solely as Managing Broker Dealer, procedures relating to retail investors or retail sales may not be applicable.

21.1 Introduction

This section provides general information about private placements and the regulations that govern their offer and sale. A general understanding of private placements is helpful when considering whether to offer a specific issue to a customer.

There are several general areas of requirements and limitations that affect most private placements.

- No general solicitation of purchasers other than those permitted under Rule 506(c) and 144A
- Limits as to the size of the offering
- No advertising or general public meetings about specific private placements other than those permitted under Rule 506(c) and 144A
- Issuers must provide information to potential investors
- Securities purchased are generally restricted as to resale
- Number of purchasers is restricted

21.1.1 Private Securities Offerings Principal

Principals solely responsible for supervising specified activities relating to private securities offerings may register as Private Securities Offerings Principals, instead of registering as General Securities Principals. Individuals can qualify for registration as a Private Securities Offerings Principal in several ways.

Individuals registering as Private Securities Offerings Principals are required to satisfy the Private Securities Offerings Representative prerequisite registration which includes passing the SIE and the General Securities Principal (Series 24) qualification examinations.

21.1.2 Definition of Terms

The following are common terms included in this chapter.

Accredited investor	An investor who meets certain criteria that are indicative of sophistication (see the section <i>Accredited Investors</i>)
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Letter of Non-Distributive Intent	A letter or form signed by the purchaser of a private placement, affirming that the investor is purchasing the securities for their own account and are not to be resold unless registered or subject to an available exemption.
Non-Disclosure Agreement	An agreement signed by the offeree stating that proprietary information learned about the issuer will not be divulged to third parties.
Offer	An attempt to sell a security to a potential purchaser
Offeree	A prospective purchaser to whom an offer is made
Purchaser questionnaire	A questionnaire completed by an offeree to establish the offeree's suitability to purchase the investment
Purchaser representative	A person (not affiliated with the issuer or the broker-dealer selling the issue) who acts on the purchaser's behalf to evaluate the investment for the purchaser
Subscription agreement	The document signed by the purchaser and evaluated by the issuer prior to the purchase

21.1.3 "Private Placement" Defined

Private placements are unregistered, non-public securities offerings that rely on an available exemption from registration with the SEC under either Sections 3 or 4 of the Securities Act. Most private offerings are sold pursuant to one of three "safe harbors" under Rules 504, 506(b), and 506(c) of Regulation D. Private placements sold by FINRA member firms to individuals generally must file offering documents with FINRA.

21.1.3.1 Section 4(2) Of the Securities Act Of 1933

Some private placements are offered under Section 4(2) which provides an exemption for "transactions by an issuer not involving any public offering." While the section does not specifically outline the requirements for establishing an exemption, the following is a summary of requirements gleaned from SEC interpretations and court decisions.

- There may be no general solicitation of purchasers other than those permitted under Rule 506(c) and 144A.
- Offerees and purchasers must have access to information about the issuer and must be able to comprehend and evaluate the information.
- The issuer, broker-dealer, and others acting for the issuer must conduct due diligence to reasonably insure information given to offerees and purchasers is complete and accurate.
- Offerees must have access to meaningful information concerning the issuer and be able to comprehend and evaluate the information.
- Purchasers must acquire the securities for investment and not for resale.

21.2 Blue Sky Requirements

State securities laws ("blue sky" laws) that apply to private placements vary from state to state. Some states have differing definitions for accredited investors; some states require registration of a securities issue that is otherwise exempt under Federal securities laws.

Coastal Equities, Inc. and its sales personnel are required to comply with any blue sky requirements that apply to a specific private placement issue. Requirements may differ depending on where the issue originates and where it is sold.

21.3 The Firm's Participation in Private Placements

Responsibility	<ul style="list-style-type: none"> • Private Placement Supervisor
Resources	<ul style="list-style-type: none"> • Information provided by the issuer and/or issuer's counsel
Frequency	<ul style="list-style-type: none"> • As required - process the private placement • Within 15 calendar days of the date of first sale - provide submissions to FINRA or confirm contractual designee has filed with FINRA
Action	<ul style="list-style-type: none"> • Execute an agreement with the issuer • Conduct due diligence or engage counsel or other qualified person to conduct due diligence • Document the file regarding due diligence • Provide information to Coastal's New Product Committee for review and approval to proceed with the deal • Determine limitations on the offering, including integration issues and obtain representation letter from issuer if needed • Determine what information to provide to sales personnel • Authorize the sale of the offering • Submit private placement memorandum, term sheet or other document (including material amendments) to FINRA or notify FINRA no offering documents were used
Record	<ul style="list-style-type: none"> • The deal file will include due diligence information; approval/disapproval from the appropriate committee or senior manager; the issuer agreement; issuer representation letter; offering materials; and authorization to sell • Record of submissions to FINRA

21.3.1 Due Diligence

Due diligence will be conducted for each private placement issue to be offered by Coastal Equities, Inc. and is documented in the file for the private placement. Outside counsel or another third party may be engaged to assist in due diligence and other aspects of the private placement offering. If the counsel or third party is affiliated with or somehow associated with the issuer, Coastal Equities, Inc. will conduct additional independent due diligence. Due diligence as a managing broker dealer may include the following reviews, as appropriate for the particular potential offering:

- Review financial reports
- Written company assurances as to the accuracy of records and financial statements
- Determination of the issuer's creditworthiness
- Evaluate the validity and integrity of the issuer's business model and how it fits into its business sector
- Review information available from financial and other publishers

- Independent verification of management's representations (contact with issuer's customers; lenders, vendors, lower-level employees, *etc.*)
- Reviewing news articles and industry publications regarding the issuer, its market, and competition
- Review the company's internal documents such as operating plans, product literature, corporate records, financial statements, contracts and lists of distributors and customers
- Physical inspection of the company's facilities
- Contact with the issuer's auditor and other experts knowledgeable about the company
- Contact with outside directors
- Interviews of key personnel or customers
- Determination of the plausibility of expected rates of return as compared to industry benchmarks, particularly considering complex fee structures associated with many of these types of investments
- Updating due diligence as needed until effectiveness of the offering

Private Placements to be offered by Coastal's retail division will undergo due diligence per its New Product procedures in this manual.

21.3.2 Agreement with the Issuer

Coastal Equities, Inc. will execute an agreement with the issuer to define the terms of Coastal Equities, Inc.'s role in the offering and the issuer's obligations as well as other covenants of the offering.

21.3.3 Dollar Amount of the Offering and Integration Issues

The Private Placement supervisor is responsible for ensuring the issue is not oversold relative to the dollar amount disclosed in the offering document compared to the limitations provided in the rules. The supervisor should consider any "integration" of similar offerings by the same issuer for substantially identical purposes for determining whether the issuer meets the dollar limitation under the exemption within a 12-month period of time. The supervisor's review for integration may include one of the following or another procedure determined adequate by the supervisor:

- Reviewing the issuer's financial statements for the past 12 months and/or contact directly with the issuer
- Obtaining a representation letter from the issuer that states that no other offerings were distributed during the 6-month period prior to the current private placement offering or will be distributed in a succeeding 6-month period that would cause the exemption to be lost

21.3.4 Form D

For issues sold under Regulation D, the issuer is required to make a Form D filing electronically on EDGAR within fifteen days after the first sale of securities in the offering. For ongoing offerings lasting longer than one year, the issuer is required to electronically file an amendment annually.

Some states also require filing of Form D. The issuer (or issuer's counsel) is responsible for Form D filings.

21.3.5 Submissions To FINRA

[FINRA Rule 5123; FINRA Regulatory Notice 13-26 and 12-40]

For private placements sold by Coastal Equities, Inc. (other than those exempt under Rule 5123), filings will be made electronically with FINRA within 15 calendar days of the date of first sale including the private placement memorandum, term sheet or other offering document (including any material amendments). If no offering documents were used, FINRA will be notified.

21.4 Retail Sales of Private Placements

This section applies only to retail sales of private placements to Coastal retail customers.

21.4.1 Due Diligence

Coastal will submit new products to the New Products Review Process described in this Manual.

21.4.2 Regulation Best Interest (BI)

A primary objective when selling a private placement is that all securities will be placed with retail investors consistent with Regulation BI. The RR recommending a private placement is responsible for determining that the recommendation is appropriate for the offeree based on information known about the potential offeree. The RR must consider minimum investor requirements and other suitability standards for each private placement offering.

R Rs must consider, and document, why the investment is in the retail customer's best interest, compare the product to other less expensive products, and consider availability of other, less expensive share classes and account type if the RR is dual registered as an investment adviser.

21.4.2.1 Accredited Investors

[Securities Act Rule 215; Securities Act Regulation D Rule 501]

An accredited investor is defined in Rule 501 as someone who meets certain financial criteria which may include minimum net worth, minimum income levels and other standards set by federal or state laws and regulations. It also includes natural persons holding professional certifications or designations or other credentials; knowledgeable employees of private funds; rural business investment companies; limited liability companies that meet certain criteria; other entities meeting an 'investments owned test' (currently over \$5,000,000); family offices and family clients; and spousal equivalents. The Rule should be consulted for specific criteria. Typically, accredited investors are not counted toward the limitation on the number of purchasers of a private placement.

Information about each private placement (and where it is sold) must be consulted to determine who qualifies as an "accredited investor" for a particular issue.

21.4.2.2 Non-Accredited Investors

Private placements sometimes may be offered to purchasers who do not meet the criteria of accredited investors. The number of allowable non-accredited purchasers will be limited, to preserve the registration exemption and meet requirements specified under federal and state law.

21.4.3 Restricted Nature of Private Placement Securities

Private placement securities are considered "restricted securities," other than those purchased in Rule 504 offerings. Certificates will typically include a legend and securities cannot be resold unless registered or the securities qualify for sale under an exemption.

Purchases must be for investment purposes and not for the purpose of resale. Subscription documents typically include an affirmation that the purchaser is buying the private placement for investment purposes and understands they may not be resold (Letter of Non-Distributive Intent).

RRs must consider the illiquidity of most private placements when making suitability determinations. For example, a private placement would not be a suitable investment for a purchaser who expects to invest his funds on a short-term basis.

21.4.4 Retail Communications

[FINRA Rule 2210; FINRA Regulatory Notice 20-21 and 13-18]

This section includes requirements for retail communications about private placements. FINRA Regulatory Notice 20-21 should be referenced for more detail and guidance.

- Under Rule 2210(d) all communications must be fair, balanced, and not misleading;
- Any promotion of potential rewards must be balanced by disclosure of the associated risks;
- Communications must be accurate and provide a sound basis to evaluate the facts with respect to the products or services discussed; and
- Retail communications must be approved by a registered principal.

This also applies to communications prepared by third parties and used by Coastal Equities, Inc.. If a retail communication is included in the same electronic file with an issuer-prepared private placement memorandum and distributed by Coastal Equities, Inc., it is considered a Firm communication in its entirety subject to FINRA Rule 2210. Retail communications must balance any discussions of benefits with a discussion of related risks and must be in the same retail communication (*i.e.*, cannot be in a separate document or different section of the website).

Supervision of Retail Communications of Private Placements:

Communications provided by a third-party or the issuer will be reviewed and approved by the Private Placement Supervisor.

Communications created by a registered representative of the firm, or the firm, must be reviewed and approved by the Advertising Supervisor. The Advertising Supervisor need not approve materials pre-approved by the Private Placement Supervisor.

Retail Communication Guidance:

Retail communications may not contain any prediction or projection of performance, subject to certain exceptions, as well as any exaggerated or unwarranted claim, opinion, or forecast. Reasonable forecasts of issuer operating metrics, along with a sound basis for evaluating the facts and related risks, would be permitted. FINRA Regulatory Notice 20-21 provides more detailed guidance when including forecasts.

Regulatory Notice 13-18 provides guidance for public and non-public REITs including principles relating to distribution rates which refers to issues where a portion of distributions are funded through return of principal or loan proceeds. Refer to the Notice for details of necessary disclosures.

Internal Rate of Return (IRR) is a measure of performance commonly used in connection with marketing private placements of real estate, private equity and venture capital. A drawback of IRR calculations is an inherent assumption that investors will be able to reinvest distributions at the IRR rate, which is unlikely to occur. In addition, calculations may include holdings that have not yet been sold (or liquidated or matured) resulting in subjective factors and assumptions. IRR may not be used in retail communications regarding privately placed new investment programs with no operations or that operate as a blind pool. IRR may be used for completed investment programs (holdings matured or all sold).

21.4.5 Purchaser Questionnaires

Where necessary, the potential investor will be requested to complete a Purchaser Questionnaire which confirms that the investor meets certain minimum requirements to participate in the private offering. Often, the issuer's subscription application includes a Purchaser Questionnaire.

When Purchaser Questionnaires are required, the RR is responsible for obtaining the completed Questionnaire from the potential purchaser and submitting it for review and approval within the timeframe established for the offering.

21.4.6 Purchaser Representatives

If a purchaser is not sufficiently sophisticated to effectively evaluate the investment opportunity, he or she may have a "purchaser representative" (chosen by the investor and **not** an affiliate of the issuer or broker-dealer) who assists in evaluating the investment. The purchaser representative will be required to sign the offering documents attesting to his or her role acting as purchaser representative.

21.4.7 Retail Suitability

Coastal requires all prospective retail purchasers to complete the Coastal 'Alternative Investment Suitability and Disclosure Form' to confirm current customer suitability information and to provide disclosures of certain risks associated with the investments. Additionally, the firm has a sliding scale concentration limit which may not be exceeded (as an integer calculation rounded off to the nearest integer) without a compliance exception by the AI Supervisor or senior firm principal. This form shall be submitted with the subscription documents to the AI Supervisor for review and approval before it is submitted to the issuer.

21.4.8 Offering Memorandum

Responsibility	<ul style="list-style-type: none">• Financial Professional• Alternative Products Supervisor
Resources	<ul style="list-style-type: none">• Offering memorandum
Frequency	<ul style="list-style-type: none">• As required for each private placement
Action	<ul style="list-style-type: none">• Deliver an offering memorandum to each prospective investor prior to sale• Record effective date of offering memorandum on the Alternative Investment Suitability Form• If changes or corrections are made to the offering memorandum prior to closing, provide copies to each offeree who received the original memorandum and note in the customer file the date of delivery of the updated memorandum
Record	<ul style="list-style-type: none">• A copy of the offering memorandum, corrected/changed memorandum, and the control sheet are retained in the deal file.

An offering memorandum is prepared for each private placement, depending on the specific issue. The offering memorandum includes disclosures of information obtained from the issuer including the nature, character, and

risk factors relating to the offering. Purchasers will be required to acknowledge, in writing, that they have received the offering memorandum.

Financial Professionals must provide an offering memorandum to all offerees. If it is necessary to update or correct information in the private placement memorandum prior to closing of the issue, the revised information will be provided to offerees, in writing.

Financial Professionals must identify the effective date of the offering memorandum provided to the client on the Alternative Investment Suitability Form. The client must subsequently sign the form evidencing receipt of the memorandum. The subscription documents also may require initials or a signature of the client acknowledging receipt of the most current offering memorandum.

The Alternative Products Supervisor will confirm that the customer has been provided the most current offering memorandum by reviewing the date of the memorandum disclosed on the customer-signed Alternative Investment Form prior to approving the sale.

21.4.9 Oral Representations

RRs must not deviate from written private placement memorandum information or other pre-approved information when discussing private placements with potential investors. Written notes of conversations with offerees (and their purchaser representatives) should be made, dated and placed in the customer's file.

21.4.10 Offeree Access To Information

Most private placement memoranda state that it was prepared by counsel from information provided by the issuer and offerees are invited to meet with representatives of the issuer to make an independent investigation and verification of information in the memorandum.

21.4.11 Solicitation

[Securities Act Regulation D Rule 506(b) and Rule 506(c); SEC Compliance & Disclosure Interpretations (C&Ds) on verification methods, see 255.48, 255.49, 260.35, 260.36, 260.37, 260.38: <http://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm#255.48>; SEC explanation of 506(b): <https://www.sec.gov/smallbusiness/exemptofferings/rule506b>; SEC explanation of 506(c): <https://www.sec.gov/smallbusiness/exemptofferings/rule506c>; SIFMA Guidance on Rule 506(c) verification: <http://www.sifma.org/issues/item.aspx?id=8589949595>; SEC Compliance and Disclosure Interpretations 256.23-256.33 8/6/15 re solicitations]

Responsibility	<ul style="list-style-type: none"> • Alternative Investments Supervisor
Resources	<ul style="list-style-type: none"> • Rule 506 offerings
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • For offerings under Rule 506(b): <ul style="list-style-type: none"> ○ Ensure there are no media (including internet) or public event announcements of the offering ○ If there is to be solicitation of investors with a pre-existing, substantive relationship, confirm those to be solicited meet SEC guidance ○ If other exemptions apply, confirm compliance with requirements • For offerings under Rule 506(c): <ul style="list-style-type: none"> ○ Confirm that the issuer has determined that purchasers qualify as accredited investors or conduct verification of purchasers

	<ul style="list-style-type: none"> ○ File forms and pay fees as required
Record	<ul style="list-style-type: none"> ● Record of confirming accredited investor status of all purchasers ● Record of confirming the pre-existing substantive relationship to satisfy Rule 506(b) requirements or other SEC guidance requirements ● Records of filing forms/paying fees

Solicitation of private placement offerings under Rules 506(b) and 506(c) differ as explained below.

21.4.11.1 Offerings Under Rule 506(b)

Companies conducting an offering under Rule 506(b) may raise an unlimited amount of money and may sell to an unlimited number of accredited investors. 506(b) offerings are subject to the following:

- no general solicitation or advertising to market the securities
- may not be sold to more than 35 non-accredited investors subject to the following:
 - must provide disclosure documents; if information is provided to accredited investors, the same must be provided to non-accredited investors
 - must provide financial statement information
 - should be available to answer questions from prospective purchasers

Purchasers receive restricted securities. Notice to the SEC on Form D is required within 15 days after the first sale of securities in the offering. Some states may require notice filings and fees.

506(b) offerings are subject to "bad actor" disqualification provisions (see *Disqualification Of Felons And Other "Bad Actors"* in this chapter).

21.4.11.2 Offerings Under Rule 506(c)

Under Rule 506(c) issuers may broadly solicit and generally advertise an offering subject to the following restrictions:

- All purchasers must be accredited investors as defined under Rule 501.
- The issuer is obligated to take reasonable steps to verify that purchasers are accredited investors under Rule 501 of Regulation D. Depending on Coastal Equities, Inc.'s role, Coastal Equities, Inc. may be responsible for verification.
- Certain other conditions in Regulation D are satisfied.

Purchasers receive restricted securities. The issuer must file notice to the SEC on Form D within 15 days after the first sale of the securities in the offering. Some states may require notice filings and fees.

The SEC has provided a non-exclusive list of methods that issuers (or someone acting on behalf of the issuer) may use to satisfy the verification requirement for individual investors, including:

- Reviewing copies of any IRS form that reports the income of the purchaser and obtaining a written representation that the purchaser will likely continue to earn the necessary income in the current year.
- Receiving a written confirmation from a registered broker-dealer, SEC-registered investment adviser, licensed attorney, or certified public accountant that such entity or person has taken reasonable steps to verify the purchaser's accredited status.

The verification rule does NOT apply if there is no advertising or general solicitation.

20.4.12 Investment Seminars or Meetings

Responsibility	<ul style="list-style-type: none"> • Alternative Investment Supervisor • Advertising Supervisor
Resources	<ul style="list-style-type: none"> • Requests to conduct meetings or seminars
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Request a written outline of the information to be presented, including any written materials to be provided to those attending • Request information about how the seminar or meeting will be publicized • Review the outline, written materials, and method of publication • Approve or disapprove, providing any revisions necessary • Require that all invitees receive copies of the offering memorandum
Record	<ul style="list-style-type: none"> • Include copies of the outline, list of invitees, written materials, and the approver's initials and date of approval/disapproval in the deal file.

Rule 504 offerings may be solicited without limitation. There may be general solicitation for Rule 506 and 144A offerings though the issuer is subject to requirements to verify that purchasers are accredited investors (Rule 506) or QIBs (Rule 144A). See the sections *Solicitations* and *Rule 144A Transactions* for more information.

- Seminars or meetings on specific private placements must be approved by the Advertising supervisor prior to conducting the seminar or meeting. Prior to approval provide the supervisor with:
 - a written outline of information to be presented and any graphic or written materials to be provided to attendees.
 - a description of how the seminar or meeting will be publicized to prospective attendees.
- Attendees must be provided with an offering memorandum. No other written material may be provided, unless previously approved by the Alternative Investment Supervisor or the Advertising Supervisor as applicable.

21.4.13 Subscription Agreements

Responsibility	<ul style="list-style-type: none"> • Financial Professional • Alternative Investments Supervisor
Resources	<ul style="list-style-type: none"> • Subscription agreements and accompanying checks
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Log agreements and checks received onto Sales Blotter and check blotter as applicable • Forward subscriptions and suitability forms to Alternative Investment Supervisor • Supervisor - Review subscription agreements and checks for acceptability

	<ul style="list-style-type: none"> • Supervisor Reject unacceptable agreements or checks and return to RR • Financial Professional - log checks on branch check blotter and forward accepted checks to escrow agent or issuer, retaining a copy in the deal file, or return rejected subscriptions to customer and log on blotter • Supervisor - sign/Initial accepted agreements and suitability form, copy approved package to Coastal New Accounts • Financial Professional - Forward accepted agreements to issuer • Issuer-accepted purchasers receive confirmations from the issuer/sponsor when the purchase is effected
Record	<ul style="list-style-type: none"> • Retain: <ul style="list-style-type: none"> ○ Sales blotter ○ Copies of suitability forms, subscription agreements and checks (if any)

Each potential purchaser will be required to complete the necessary subscription agreement to purchase a private placement. The agreement must be accompanied by a check or other funding information (wire or ACH) for the purchase.

Subscription agreements are processed as follows:

- The RR obtains the signed subscription agreement (and other required offering documents) suitability form, and a check or method of payment from the offeree and submits a copy to the alternative investment supervisor. The RR should log the check in the branch blotter and maintain the check in a safe or other secure location for no longer than seven (7) business days. Checks may not be held longer and must be returned after seven days and logged that the check was returned.
- Subscription agreements are logged into the Sales Blotter for the private placement.
- The supervisor reviews the agreement and suitability form for acceptability. If accepted, the supervisor will sign and return to the RR and copy New Accounts at Coastal.
- The RR will forward approved subscription agreements and checks if any to the issuer in accordance with the instructions on the subscription agreement.
- Rejected agreements/checks are returned to the RR with an explanation for the rejection.
- The issuer reviews and accepts or rejects the agreement.
- A confirmation is sent by the issuer to accepted purchasers when the purchase is effective.

RRs should be aware that **purchasers are not accepted until the issuer accepts them**. Final acceptance rests with the issuer who is responsible for ensuring conditions of the offering are satisfied to qualify under the operative exemption.

21.4.14 Contingency Offerings

[Exchange Act Rule 10b-9 and 15c2-4; FINRA Regulatory Notice 16-08; FINRA Notice to Members 98-4]

Responsibility	<ul style="list-style-type: none"> • Private Placement Supervisor
Resources	<ul style="list-style-type: none"> • Issuer agreement • Subscription agreements

Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Evaluate issuer information and determine Coastal Equities, Inc.'s participation including: <ul style="list-style-type: none"> ○ Reasonable investigation of the security and the issuer's representations ○ Review of the terms of the contingency, including any agreement and disclosure by the issuer regarding the contingency ○ Follow up any red flags such as inconsistencies between the escrow agreement and the offering document • Establish a "separate account" or escrow account • Confirm purchasers are bona fide purchasers where necessary • Identify insiders, firm or employee account purchasers and obtain affirmation regarding holding period • Require subscribers to reconfirm their investments if the issuer extends the offering period • Return subscriber funds if the issuer changes the contingency by reducing the offering minimum • Close escrow account and, if contingency met, immediately forward purchaser funds to issuer or, if contingency is not met, immediately return funds to potential purchasers
Record	<ul style="list-style-type: none"> • Escrow account, issuer information and purchaser information are retained in the deal file

21.4.14.1 Introduction

Best efforts underwritings may take different forms including "all or none," "minimum-maximum," or other offerings contingent on the sale of a certain amount of the issuer's securities. Two primary concerns are that customer funds be transmitted to the issuer or to an escrow account and that only *bona-fide* purchasers are included in order to meet a stated minimum number of shares or units. Where the minimum is not sold within the deadline specified by the prospectus, all customer funds must be refunded.

Sales will be made only to *bona-fide* purchasers to meet any minimum amount of the securities to be sold.

21.4.14.2 Handling Investor Funds

Coastal Equities, Inc. will promptly:

- Deposit funds into a "separate bank account" for which Coastal Equities, Inc. is the account holder and is designated as agent or trustee for the investors (only if Coastal Equities, Inc. maintains at least \$250,000 in net capital and is allowed to carry customer accounts); or
- Establish an independent bank escrow account.

Funds will be released to the issuer only after the contingency is satisfied.

21.4.14.3 Customer Funds - Escrow Account

[Exchange Act Rule 15c2-4]

The designated supervisor is responsible for establishing procedures for the protection of customer funds including the establishment of an escrow account where required.

- Establish an escrow account and execute Coastal Equities, Inc.'s standard escrow agreement with a bank that is not affiliated with Coastal Equities, Inc.. The escrow account may not be controlled by the issuer.
- Maintain copies of bank statements for the escrow account and review the statements when received, to ensure funds are not withdrawn prior to the date the contingency is met.
- Ensure customer funds are promptly deposited to the escrow account.
- Maintain records of all potential purchasers including the quantity to be purchased, when funds are received, and when funds are forwarded to the issuer or escrow account.
- Ensure checks are forwarded to the issuer (where an escrow account is not used) or to an escrow account by noon of the business day following receipt.
- Authorize release of funds to the issuer from an escrow account after the contingency is met and after a review of purchasers, as discussed in the next section, has been conducted.
- If the contingency is not met, promptly refund funds to potential purchasers.
- If the issuer extends the offering period, require investors to reaffirm their investments.
- If the issuer reduces the offering minimum, return funds to investors.

21.4.14.4 Purchasers

The designated supervisor is responsible for establishing procedures regarding purchasers of securities issued through a best efforts underwriting including the following:

- Where the offering is contingent upon the sale of a certain quantity of the issue, confirm that all purchasers are *bona-fide* purchasers. Non-bona fide sales generally include sales of undisclosed purchases by the issuer or broker-dealer, their affiliates or associated persons, or any entities through nominee accounts that are designed to create the appearance of a successful completion of an offering.
- Identify purchases by issuer insiders, Coastal Equities, Inc.'s proprietary account, or employees of Coastal Equities, Inc. and, for those identified, obtain a written affirmation that the purchaser intends to hold the security as an investment or, in conjunction with the issuer, determine restrictions on immediate sale by such accounts.
- Record the review of purchasers in the deal file.

21.5 Regulation D

[SEC Securities Act of 1933 Regulation D; FINRA Regulatory Notice 10-22]

Regulation D is a series of six rules, Rules 501-506, that include exemptions from the registration requirements of the 1933 Act. The specific exemptions are included in Rules 504-506 and differ as to the size of the offering and conditions imposed to qualify for the exemption. The following chart summarizes the three exemptions available under Regulation D. This is only a very general summary of requirements and does not include legal definitions and technicalities that may apply to certain types of private placements.

	Rule 504	Rule 506
Who may invest	Anyone suitable for the investment	Qualified investors
Number of investors	Unlimited	35 non-accredited, unlimited accredited investors

Size of offering sold in any consecutive 12 months	\$5,000,000	Unlimited
Restricted securities?	No	Yes
Public solicitation/advertising allowed?	Yes	Yes
Disclosure document required?	No	Yes*
Opportunity to ask questions of issuer?	No	Yes

*Under the rule, disclosure documents are not required to be given to accredited investors though a note to Rule 502(b) states that an issuer should consider providing such information to accredited investors in view of anti-fraud statutes.

The reference to "unlimited accredited investors" in the section "Number of investors" above does not imply that a private placement will, in fact, have an unlimited number of accredited investors. The issuer and Coastal Equities, Inc. will consider limitations on accredited investors, as appropriate, to preserve the exemption as a private placement and avoid the appearance of a broad solicitation of the issue.

21.5.1 Disqualification of Felons and Other "Bad Actors"

[SEC Regulation D Rule 506(d)(1)]

Rules 504 and 506 are frequently-used exemptions from registration under Regulation D. The exemptions are NOT available if the issuer or any person covered by the disqualification rule had a "disqualifying event." Disqualifying events include certain criminal convictions; SEC and CFTC actions; and other events. Refer to the rule cited above for a list of covered persons and disqualifying events.

There is an exception from disqualification if the issuer can show it did not know, and in the exercise of reasonable care, could not have known that a covered person with a disqualifying event participated in the offering.

21.5.2 Due Diligence

This section includes due diligence guidelines provided by FINRA. Coastal Equities, Inc. will conduct due diligence appropriate for the particular Regulation D offering and document its reviews and investigations in the deal file.

When engaging in a Regulation D offering, due diligence will include, at minimum, reasonable investigation of:

- the issuer and its management;
- the business prospects of the issuer;
- the assets held by or to be acquired by the issuer;
- the claims being made; and
- the intended use of proceeds of the offering (including whether investors' money is likely to be applied according to the stated use of proceeds, and whether the stated use of proceeds is reasonable in light of the issuer's business purpose and prospects).

The scope of investigation may depend on a number of specific factors included in FINRA guidance, described below.

BD affiliation with the issuer. If there is affiliation with the issuer, a BD must not compromise its independence in performing a thorough and independent investigation and must resolve any conflict of interests impairing that responsibility.

BD that prepares the private placement memorandum or other offering document. The BD has a duty to investigate the securities offered and representations made by the issuer. Where a BD assists with preparation of a memorandum or document, the BD is subject to FINRA communications rules. **Retail communications are subject to FINRA rule requirements whether or not the BD assisted in their preparation.**

"Red flags" (such as an issuer's refusal to provide information for the BD to meet its obligation to investigate or inaccurate financial statements) must be reviewed and simple reliance on representations by the issuer's management is not sufficient to meet the BD's investigatory obligations.

The use of counsel or experts to perform an investigation on the BD's behalf must be done by firms and individuals that the BD is satisfied are qualified and competent. When Coastal Equities, Inc. is a member of a syndicate or selling group, it may rely upon the reasonable investigation by the syndicate manager if the BD believes the syndicate manager has the expertise and absence of conflicts to conduct the investigation. Reliance may be substantiated by meeting with the manager; obtaining a description of the manager's reasonable investigation efforts; and inquiry regarding the independence and thoroughness of the investigation.

21.5.3 Investigation Practices

The following are FINRA guidelines for what may be included in a reasonable investigation of a Regulation D offering. Coastal Equities, Inc. will conduct investigation into the issuer as appropriate for the proposed offering.

A. Issuer and Management

Reasonable investigations of the issuer and its management concerning the issuer's history and management's background and qualifications to conduct the business might include:

- For Rule 506 offerings, determine whether the issuer or any covered person under Rule 506(d)(1) has been the subject of a disqualifying event precluding the use of the Rule 506 exemption.
- Examining the issuer's governing documents, including any charter, bylaws and partnership agreement, noting particularly the amount of its authorized stock and any restriction on its activities. If the issuer is a corporation, a BD might determine whether it has perpetual existence.
- Examining historical financial statements of the issuer and its affiliates, with particular focus, if available, on financial statements that have been audited by an independent certified public accountant and auditor letters to management.
- Looking for any trends indicated by the financial statements.
- Inquiring about the business of affiliates of the issuer and the extent to which any cash needs or other expectations for the affiliate might affect the business prospects of the issuer.
- Inquiring about internal audit controls of the issuer.
- Contacting customers and suppliers regarding their dealing with the issuer.
- Reviewing the issuer's contracts, leases, mortgages, financing arrangements, contractual arrangements between the issuer and its management, employment agreements and stock option plans.
- Inquiring about past securities offerings by the issuer and the degree of their success while keeping in mind that simply because a certain product or sponsor historically met obligations to investors, there are no guarantees that it will continue to do so, particularly if the issuer has been dependent on continuously raising new capital. This inquiry could be especially important for any blind pool or blank-check offering.
- Inquiring about pending litigation of the issuer or its affiliates.

- Inquiring about previous or potential regulatory or disciplinary problems of the issuer. A BD might make a credit check of the issuer.
- Making reasonable inquiries concerning the issuer's management. A BD might inquire about such issues as the expertise of management for the issuer's business and the extent to which management has changed or is expected to change. For example, a BD might inquire about any regulatory or disciplinary history on the part of management and any loans or other transactions between the issuer or its affiliates and members of management that might be inappropriate or might otherwise affect the issuer's business.
- Inquiring about the forms and amount of management compensation, who determines the compensation and the extent to which the forms of compensation could present serious conflicts of interest. A BD might make similar inquiries concerning the qualifications and integrity of any board of directors or similar body of the issuer.
- Inquiring about the length of time that the issuer has been in business and whether the focus of its business is expected to change.

B. Issuer's Business Prospects

Reasonable investigations of the issuer's business prospects, and the relationship of those prospects to the proposed price of the securities being offered, might include:

- Inquiring about the viability of any patent or other intellectual property rights held by the issuer.
- Inquiring about the industry in which the issuer conducts its business, the prospects for that industry, any existing or potential regulatory restrictions on that business and the competitive position of the issuer.
- Requesting any business plan, business model or other description of the business intentions of the issuer and its management and their expectations for the business, and analyzing management's assumptions upon which any business forecast is based. A BD might test models with information from representative assets to validate projected returns, break-even points and similar information provided to investors.
- Requesting financial models used to generate projections or targeted returns.
- Maintaining in the BD's files a summary of the analysis that was performed on financial models provided by the issuer that detail the results of any stress tests performed on the issuer's assumptions and projections.

C. Issuer's Assets

Reasonable investigations of the quality of the assets and facilities of the issuer might include:

- Visiting and inspecting a sample of the issuer's assets and facilities to determine whether the value of assets reflected in the financial statements is reasonable and that management's assertions concerning the condition of the issuer's physical plants and the adequacy of its equipment are accurate.
- Carefully examining any geological, land use, engineering or other reports by third-party experts that may raise red flags.
- Obtaining, with respect to energy development and exploration programs, expert opinions from engineers, geologists and others are necessary as a basis for determining the suitability of the investment prior to recommending the security to investors.

21.6 Internet Offerings

Responsibility	<ul style="list-style-type: none"> • Private Placement Supervisor
Resources	<ul style="list-style-type: none"> • Coastal Equities, Inc. web site
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Establish appropriate method for qualifying potential purchasers prior to accessing information about private placements • Include necessary disclaimers and information about the nature of private placement offerings
Record	<ul style="list-style-type: none"> • Copies of the web site pages are retained when revised, on an ongoing basis

Private placements that are offered through Coastal Equities, Inc.'s web site are subject to certain limitations and requirements. The SEC, in a no-action letter, has stated that inclusion of information about private placements will not be considered a "general solicitation" if certain requirements are met, including the following:

- The information on the Web must have limited distribution to those who qualify for investing. Those who view information about private placements will be pre-qualified as accredited or sophisticated investors.
- Access to private placement information will be limited to those pre-qualified investors who are assigned passwords to access the information.

Information about private placements will be included on Coastal Equities, Inc.'s web site only if these conditions are met. In addition, blue sky laws may require the posting of information about states where an issue qualifies for sale.

Coastal Equities, Inc.'s Web site may be used to disseminate offering materials and to facilitate the dissemination, execution, and submission of subscription materials.

21.7 Rule 144A Transactions

[SEC Securities Act of 1933 Rule 144A]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests to purchase securities under 144A • Trader referrals of potential 144A transactions
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Confirm the securities to be sold qualify for sale under Rule 144A • Review potential purchasers to ensure they meet the qualification for Qualified Institutional Buyers (QIB) prior to purchase • Provide written notification to all purchasers disclosing the nature of the 144A transaction and confirming that it is Coastal Equities, Inc.'s understanding that the purchaser is a QIB as defined in Rule 144A

	<ul style="list-style-type: none"> • Notify traders regarding securities that are to be sold only under the restrictions of 144A • When Coastal Equities, Inc. includes 144A securities in its inventory, determine the marketability of the securities for net capital purposes and notify the FINOP of the status of such securities in inventory
Record	<ul style="list-style-type: none"> • Review of securities for qualification for sale under 144A • Review of customers for qualification as QIBs and copies of 144A letters • Notification to traders • Records of the written notification provided to purchasers including the date and to whom provided

Rule 144A permits private placement of securities with certain institutional purchasers that qualify as Qualified Institutional Buyers (QIBs) as defined in Rule 144A. While general solicitation and advertising is permitted for these offerings, all purchasers must qualify as QIBs. The seller (issuer) and anyone acting on behalf of the seller must reasonably believe the purchase meets the qualification of a QIB.

For 144A transactions in TRACE-eligible debt securities, traders are required to comply with TRACE requirements. For more information, refer to the section *TRACE* in the chapter *CORPORATE FIXED INCOME SALES AND TRADING*.

21.8 Private Investment in Public Equity (PIPE)

A PIPE is defined as a privately negotiated sale (*i.e.*, private placement) of securities of an already public company. In a PIPE transaction, a public company sells its unregistered securities (*e.g.*, common stock, preferred stock or convertible securities) in a private placement to a select group of sophisticated individuals or institutions and subsequently files a resale registration statement with the SEC at the completion of the private placement to enable the investors to resell the securities into the public market. Coastal Equities, Inc.'s role in a PIPE transaction is to act as the placement agent for the issuer.

21.8.1 Underwriting

PIPE transactions will be managed by Investment Banking (IB) which is also responsible for:

- Obtaining transaction approval from the Investment Banking Commitment Committee;
- Working with other appropriate personnel/departments, as needed (*e.g.*, Compliance, Legal), to execute an engagement letter; and
- Maintaining a Master Log, which includes among other things an investor log and list of firm employees brought "over the wall."

Non-IB employees approached by an issuer to participate in a PIPE should contact Compliance and/or their supervisor immediately and must handle such information as confidential unless advised otherwise by Compliance or Legal.

21.8.2 Compliance Notification

All PIPE offerings in which Coastal Equities, Inc. is involved, including offerings that are reasonably likely to occur or that Coastal Equities, Inc. is actively pursuing, must promptly be added to Coastal Equities, Inc.'s Watch List. Consistent with Coastal Equities, Inc.'s Information Barrier Policy, the IB manager is responsible for immediately contacting Compliance when there is a reasonable likelihood of receiving a PIPE mandate. Once a company has been added to the Watch List, IB must notify Compliance of any significant developments with respect to the transaction, including intended pricing and announcement dates.

21.8.3 Registration Statement Integration

In order to avoid potential registration statement integration (a risk whenever a public and private offering of an issuer's securities are conducted concurrently or within a short period of time to each other), a PIPE offering must be completed before the related resale registration statement is filed. In the event a registration statement covering the same (and/or similar) securities that will be sold in the PIPE offering has been filed but is not yet effective, the issuer must withdraw the registration statement before the PIPE offering can commence. Note the foregoing restriction is not applicable to offerings structured as a registered direct issuance off of an existing/effective registration statement. IB should work with Compliance to ensure compliance with these rules.

21.8.4 Eligible Investors

In general, companies are prohibited from selling unregistered securities unless an exemption is available under SEC rules. With respect to the private placement phase of a PIPE transaction, issuers normally rely on the exemption from registration contained in Section 4(2) of the Securities Act of 1933, as amended (the "Securities Act"), and the safe harbor provisions of Regulation D. As a general matter, in its role as placement agent, Coastal Equities, Inc. may only offer and sell PIPEs to investors whom Coastal Equities, Inc. reasonably believes to be "accredited investors." Generally, Coastal Equities, Inc. may only solicit potential investors who qualify as accredited investors.

Regulation D does not limit the number of accredited investors who may purchase securities in a private placement.

21.8.5 Marketing Restrictions

This section outlines restrictions on marketing pipe offerings.

21.8.5.1 Prohibition on General Solicitation and Advertising

The federal private placement exemption prohibits the issuer of a PIPE and any person acting on its behalf (including placement agents such as Coastal Equities, Inc.) from offering or selling the securities by any form of general solicitation or general advertising. Contacting potential investors with whom Coastal Equities, Inc. has a **pre-existing, substantive relationship** does not constitute a general solicitation. As a general matter, Coastal Equities, Inc. may only contact investors with whom Coastal Equities, Inc. has such a relationship, and generally, initial contact should be made directly with the customer (*i.e.*, contact must be with the ultimate investor with investment discretion).

The general guideline for establishing that a potential investor has had a pre-existing, substantive relationship with Coastal Equities, Inc. is that such potential investor:

- Has invested in other PIPE offerings where Coastal Equities, Inc. acted as placement agent; or

- Has maintained an investment advisory account with Coastal Equities, Inc. (or an affiliate) or a brokerage account or similar relationship with Coastal Equities, Inc. (or an affiliate) for at least 30 days prior to the distribution of information to such investor concerning the offering; and
- Was not solicited to become a customer of Coastal Equities, Inc. in contemplation of the offering.

Failure to observe restrictions that may be imposed on Coastal Equities, Inc.'s activities in connection with an offering may have severe consequences, including, depending on the timing of the violation, a forced delay in the ability to market or close the offering or civil and criminal penalties and rescission rights for investors. Any questions concerning whether an activity is appropriate in light of the private nature of a PIPE transaction should be directed to Compliance.

After the **final** closing, "tombstone" advertisements and public statements as to the PIPE offering may be permitted. Compliance should review each such advertisement and statement prior to its publication or use.

21.8.5.2 Written Presentation Content

PIPE transactions are generally marketed via an oral presentation. Any written materials used during the presentation must adhere to the content standards specified below and must be collected from attendees at the end of the presentation.

Written materials created for the purpose of marketing a PIPE transaction should never be based on anything other than the issuer's existing publicly available information (typically the 10K) accompanied by the following:

- Offering summary;
- Key investment highlights; and
- Business summary.

Further, the written presentation:

- Must also contain customary legal legends and disclaimers including preamble language related to: (1) forward looking statements; and (2) confidentiality and Regulation FD obligations (to be reviewed by issuer counsel).
- Should always be accompanied by a disclaimer letter from Coastal Equities, Inc. to prospective investors (to be reviewed by issuer's counsel).
- Should never reference Coastal Equities, Inc., except to refer to its role as placement agent, and, when appropriate, to disclose potential conflicts of interest to prospective investors (*e.g.*, a firm employee serving on the issuer's board of directors or a material firm ownership position of securities of the issuer).
- Should never be on firm letterhead or other formats containing the firm logo.
- Should never contain forward-looking projections unless such projections have been publicly disclosed. During the marketing process, if prospective investors ask about projections, they should be directed to existing, publicly available research reports and information.

21.8.5.3 FINRA Filings

IB should discuss the specific facts and circumstances of each PIPE transaction with Compliance, Legal and/or external counsel, as necessary, to determine whether to file documents and information with FINRA or whether the offering is clearly exempt from filing.

21.8.5.4 Regulation M

Upon receiving a PIPE mandate, Compliance should be contacted to preliminarily determine if the proposed transaction is subject to Regulation M. Based on the issuer's float, trading volume and a determination of whether the PIPE transaction constitutes a distribution, the issuer's securities may be subject to restrictions on engaging in transactions and quotation activity with respect to the issuer's stock for the applicable restricted period (*i.e.*, 0, 1 or 5 trading days) as required by Regulation M.

If subject to Regulation M, the designated supervisor will make required submissions to FINRA. Upon receiving the UAR from FINRA, Underwriting will consult with Compliance to determine the appropriate firm market maker status (passive or active) and the applicable Regulation M restricted period. If co-agents are involved, Underwriting will consult with the co-agents to determine their desired market maker status as well.

Underwriting will notify the FINRA Market Regulation Department and Coastal Equities, Inc.'s trading desk of Coastal Equities, Inc.'s and the other co-agents' market making status during the appropriate Regulation M period. Compliance will add the issuer to Coastal Equities, Inc.'s Restricted List.

After the subject transaction has priced, but no later than the market open on the day following pricing, Underwriting will fax a Regulation M Trading Notification Form (*i.e.*, Reg M Wire) to the FINRA Market Watch Department and the FINRA Market Regulation Department. IB is responsible for notifying Compliance, as well as other co-agents, upon the completion of the PIPE transaction. Compliance will un-restrict the security and notify Trading.

21.8.6 Information Flow

This section outlines information flow for PIPE transactions.

21.8.6.1 Treatment of Confidential and Inside Information

Prior to the time that an issuer makes a public announcement of a PIPE transaction, information surrounding the offering is confidential information. As PIPE issuers typically see a drop in their share price following the public announcement of the transaction due to the dilution that results from the issuance of additional shares, a PIPE offering will generally constitute a material transaction for an issuer. Accordingly, knowledge of a PIPE transaction prior to a public announcement by the issuer of the transaction may constitute material nonpublic information ("inside information"). As placement agent for an issuer customer, Coastal Equities, Inc. has an obligation not to breach the customer's trust by misusing any information furnished during the course of an engagement. Thus, firm employees with knowledge of a PIPE transaction must:

- Not act on or give this information to others;
- Not trade or advise others to trade based upon the information, misappropriate the information or tip other customers or third parties; and
- Immediately notify Compliance and take appropriate steps to protect the information.

Persons guilty of misusing inside information may be subject to civil and criminal penalties (including imprisonment), SEC administrative actions, disciplinary action by various self-regulatory organizations, and dismissal by Coastal Equities, Inc..

21.8.6.2 Sharing Transaction Details with Potential Investors

Before a firm employee reveals an issuer's name to a prospective investor, commences discussions concerning the details of a PIPE offering, or otherwise furnishes an investor with material nonpublic information regarding an issuer, such employee should mention that the offering constitutes a private transaction and must ask the prospective investor if he/she is interested in learning more about the PIPE transaction. Firm employees, moreover, should obtain from the prospective investor an agreement that the investor will keep such information confidential, and an acknowledgment that the investor understands how such confidential information must be treated under the securities laws. As soon as is practicable and typically within one (1) business day after receipt of a prospective investor's positive response, Coastal Equities, Inc. will send such prospective investor a follow-up email confirming such prospective investor's receipt of material, nonpublic information and acknowledging such prospective investor's agreement to hold such information in confidence. In addition, the email will remind such prospective investor of his/her obligation not to use any such information in contravention of applicable securities laws.

Investor logs must be maintained by IB during the marketing process and must contain, among other things: (1) the identity of the investors contacted; (2) such investor's level of interest in the subject transaction; and (3) the date that the management presentation was given (in person or via conference call) to such investor. Upon completion of the marketing process, IB must forward to Compliance a copy of the investor log.

21.8.6.3 Sharing Information with Sales and Trading Personnel

Any decision to bring sales personnel "over the wall" must be discussed and approved by the designated sales supervisor in consultation with the IB manager and Compliance. Sales personnel brought "over the wall" may continue to conduct their normal sales activities but may not communicate information related to the PIPE transaction to customers. To the extent that sales personnel are asked to assist in the marketing of the PIPE transaction, sales personnel should make the marketing calls off of the trading floor in an area where their conversation cannot be overheard.

Any decision to bring trading personnel "over the wall" must be discussed and approved by the manager of Trading (NASDAQ or Listed) in consultation with the IB manager and Compliance. Trading personnel brought "over the wall" may not trade or make markets in the securities of the issuer subject to the PIPE transaction. The Trading manager should assign trading responsibilities for such securities to another trader without divulging the details of the PIPE transaction. Trading personnel brought "over the wall" may continue to trade and make markets in other securities pursuant to their normal responsibilities but are prohibited from disclosing information regarding the PIPE transaction to anyone that is not already "over the wall."

21.8.6.4 Sharing Information with Research Analysts

Any decision to bring a firm research analyst "over the wall" must be discussed and approved by the Research manager and Compliance.

21.9 Private Equity Funds

Responsibility	<ul style="list-style-type: none"> • Private Placement Supervisor (MBD business) • Alternative Investment Supervisor (Retail/Selling Group)
Resources	<ul style="list-style-type: none"> • Proposed private equity fund investments • Partnership agreements, suitability documents

Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review proposed funds, conduct due diligence, and determine whether Coastal Equities, Inc. will offer the investment • Review partnership agreements, suitability documents and accept or reject
Record	<ul style="list-style-type: none"> • Due diligence file • Partnership agreements, suitability documents

Private equity funds pool investments from individuals and institutions and invest in businesses. Investors are usually limited partners in a limited partnership controlled by a general partner that determines the investing of funds. There is no public market for private equity funds but there may be a secondary market for interests.

Private equity funds may offer a high rate of return with a corresponding high rate of risk of loss. In a growing economy funds may exit the earliest portfolio investments providing distributions to limited partners, but a slowing economy may restrict the fund's ability to liquidate investments. Most investors are institutions that have the ability to develop a diversified portfolio of private equity funds or that invest through a fund of funds to provide a diversified portfolio.

Features of private equity funds include the following:

- Entry requires a substantial initial investment (which may be \$1,000,000 or more) allowing the fund's manager discretion over the first few years of the fund.
- Funds may provide for obligatory capital contributions throughout the life of the fund obligating the limited partners to make additional contributions. Failure to meet capital calls may result in the defaulting limited partner forfeiting interest in the fund.
- These are illiquid investments that are not publicly traded. An investor's capital is locked up in a long-term investment which may last ten years or more with no redemption rights. Distributions are made only as investments are converted to cash.
- Limited partners typically have a passive role with no say in the actions of the general partner.
- The general partner may not find suitable investments for the fund resulting in the investors' funds remaining uncommitted
- Funds are high risk; the investor may lose all of the investment.

RRs must obtain necessary partnership agreements and any suitability documents required for the investment and submit them to the appropriate supervisor for review.

22 INSURANCE PRODUCTS

Generally, Coastal does not engage in the sale of insurance products but permits same as an outside business activity. However, certain insurance products are, or may be, considered securities products. This chapter describes policies and procedures that apply to the sale of those certain insurance products.

22.1 Sales to Military Personnel on Military Installations

[FINRA Rule 2272; Military Personnel Financial Services Protection Act]

The following requirements and guidelines apply when offering life insurance products (including annuities) to military personnel and their dependents on military installations. "Military installation" means any federally owned, leased or operated base, reservation, post, camp, building or other facility which members of the U.S. Armed Forces are assigned for duty, including barracks, transient housing and family quarters.

- Referral fees upon securities sales or solicitations are prohibited unless the fee recipient is a licensed agent of the issuer of the policy or annuity.
- Life insurance products must not be marketed as investment products.
- A suitability determination must be made for sales of securities (*e.g.*, variable annuities).
- Products that provide very low death benefits for very high premiums that are front-loaded in the first few years are inappropriate for most military personnel.
- Written disclosures must be provided that:
 - state that the federal government provides subsidized life insurance to service members under the Servicemembers' Group Life Insurance (SGLI) program, and the amount and cost of the SGLI coverage available;
 - state that the federal government does not sanction, recommend, or encourage purchase of the life insurance product being sold;
 - fully disclose any terms and circumstances under which amounts accumulated in a savings fund or savings feature under the life insurance product that is the subject of the disclosure may be diverted to pay, or reduced to offset, premiums due for continued coverage under the product;
 - state that no one has received any referral fee or incentive compensation for offering to sell the product, unless the person is a licensed agent of the person issuing the product;
 - are in plain and readily understandable language; and
 - for sales or solicitations on federal land or facilities located outside the U. S. , list the address and phone number at which consumer complaints are received by the state insurance regulator.

22.2 Purchases

The following is a summary of how insurance contracts are purchased and processed. Refer to the section *Replacements* for other procedures if the value of one policy is used to purchase a new policy.

22.2.1 Equity-Indexed Annuities

[FINRA Notice to Members 05-50; FINRA Investor Alert:

<http://www.finra.org/InvestorInformation/InvestorAlerts/AnnuitiesandInsurance/Equity-IndexedAnnuities-AComplexChoice/index.htm>; National Association of Insurance Commissioners' Buyer's Guide to Equity-Indexed Annuities: http://www.idfpr.com/DOI/life_annuities/equityindex.asp]

Insurance companies (and sometimes others) offer equity-indexed annuities (EIAs) which are financial instruments that:

- generally offer a combination of interest income, some protection from loss of principal, and an opportunity to earn additional interest based on the performance of a securities market index.
- may be registered securities or are unregistered.

EIAs are complex investments that require both the RR and the customer to understand the various features to determine whether the particular investment is appropriate for the customer.

Coastal generally treats the sale of EIAs as outside business activity. RRs therefore must make a request to engage in such business as an Outside Business Activity by submitting the Request form to his/her supervisor and Compliance.

FINRA NtM 05-50 describes the possibility for certain EIAs to be deemed a security, and therefore alerts firms of their duty to supervise such securities transactions if any such product is deemed to be a security. **If an EIA product is sold by prospectus, it must be sold by CEI.** Recommendations concerning EIAs sold by prospectus (purchases sales redemptions and exchanges) must be forwarded to the Designated Supervisor with a written explanation of why the recommendation is in the best interest of a retail customer, along with evidence that the commissions and any other compensation to be earned by the RR and CEI have been disclosed to the retail customer.

Recommendations to sell securities to fund the purchase of such products must also be in the retail customer's best interest.

22.3 Variable Products

[FINRA Rule 2320; FINRA variable annuity site: <http://www.finra.org/RulesRegulation/IssueCenter/VariableAnnuities/index.htm>]

Variable products are insurance contracts with underlying investments generally in investment company (mutual fund) securities. They are a hybrid of insurance and securities products. There are different types of variable products with differing requirements. Key requirements are listed below; other requirements follow in sections on specific products.

- RRs must have **necessary licensing** to sell variable products, including:
 - securities licensing with an SRO (*i.e.*, FINRA, NYSE)
 - securities licensing in the state where the customer resides (some states waive securities licensing to sell variable products)
 - insurance licensing in the state where the customer resides
- **Supervisors** of RRs who sell variable products **must have required securities supervisory licenses.**
- RRs must be **familiar with features** of variable products before recommending them and explain the features to the customer. Features may include a death benefit, fees and expenses, subaccount choices, special features, withdrawal privileges, and tax treatment. Each product must be reviewed because features vary considerably.
- **Recommendations must be suitable** considering whether features of the product meet the customer's investment needs.
- **If replacing one annuity with another**, the appropriate section of the VA Disclosure Form must be completed and submitted and the exchange must be justified. Exchanges must be suitable with particular concerns for senior (65+) investors regarding investment objectives and the costs of making the exchange which must be justified in account or order records.
- Purchases or exchanges of deferred variable annuities require completion of the **Variable Annuity Disclosure Form** which is provided to the supervisor with a copy of the purchase contract and new account information about the customer.
- **Customer signed applications** must be forwarded to the designated person on the day of receipt.

- **Applications for deferred variable annuities must be reviewed and approved by a principal** no later than 7 business days after the principal receives a complete and correct application and before sending to the insurance company.
- There are specific **requirements that apply to advertising and other communications** about variable products, particularly regarding yield, dollar cost averaging, and other representations of return.
- When a **customer redeems an annuity**, a signed redemption form must be submitted with the customer's signature guaranteed.

22.3.1 Training

[FINRA Rule 2330(e)]

Variable products are included in RR training on an ongoing basis.

22.3.2 General Sales Guidelines and Suitability Requirements

[FINRA Rule 2111]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Insurance contract or other documentation of a proposed or actual purchase • Records of customer's financial information and investment objectives • Information about the insurance product (features, fees, <i>etc.</i>) • Records of exchanges from internal reports, reports from insurance carriers
Frequency	<ul style="list-style-type: none"> • Daily or as required when variable products are sold
Action	<ul style="list-style-type: none"> • Review variable contract sales for the following: <ul style="list-style-type: none"> ○ Insurance product objectives consistent with the customer's financial situation or investment objectives ○ Objectives of underlying securities investments consistent with the customer's financial situation and objectives ○ Allocation of monies to subaccounts are consistent with the customer's stated needs and objectives ○ Subaccount transfers are suitable (other than those part of an insurance company's automatic asset allocation and rebalancing program) ○ Contract size that is not disproportionate to the customer's overall net worth or liquid assets ○ Customer is retired, unemployed, or lacks investment experience ○ Customer is older (>75 years old) and may not be suitable for a long-term investment ○ Sales to IRAs, retirement plans, or other tax-deferred accounts require review to determine whether purchase is appropriate ○ "Commission specials" on certain products to determine sales of such products meet sales guidelines and suitability standards • Review exchanges for: <ul style="list-style-type: none"> ○ Suitability ○ Reasons given for VA exchange should match up with the features of the purchased VA

	<ul style="list-style-type: none"> ○ The customer is told, and understands, the cost of an exchange and any benefits of the switch ○ Compare all switches done by an RR within a narrow period to determine if the RR differentiated among customers ● Confer with the RR to obtain more information regarding a questioned sale or regarding recommendations inconsistent with sales guidelines or suitability standards and suggest alternatives where appropriate ● Rescind or block purchases where a purchase would be inappropriate
Record	<ul style="list-style-type: none"> ● Signature of supervisor on VA/VUL Disclosure Form ● Subaccount transfers, including those done on a direct-way basis ● Reviews of transactions, subaccount transfers and action taken, if any

There are a number of considerations that should be made when recommending a variable product. Suitability obligations include recommendations to transfer investments in subaccounts (other than those that are part of an insurance company's automatic asset allocation and rebalancing program).

- The RR must obtain and document financial information about the customer and the customer's investment objectives.
- Is the proposed recommendation consistent with the customer's investment objectives, both for the insurance component and the objectives of the underlying investments?
- Are the features of the variable product consistent with the customer's objectives and needs (payout phase, periodic payments, death benefit, tax-deferral, *etc.*)?
- What is the customer's need for liquidity and short-term investment? Is a long-term investment suitable for the customer? Older customers typically would not be candidates for annuity investments and recommendations to these persons must be justified.
- What is the customer's investment experience and ability to understand the variable contract and underlying investments?
- What is the customer's immediate need for retirement income?
- Is the customer willing to invest a set amount on a periodic basis?
- Discuss all relevant facts with the customer including liquidity issues; fees and charges; applicable taxes or penalties and surrender charges; and market risk. Fees and charges include surrender charges, mortality and expense risk charge, administrative fees, underlying fund expenses, and other fees and charges.
- Multiple annuities, resulting in higher cost to the customer, should not be recommended when one annuity, or annuities from a family of funds, would meet the customer's investment needs and result in less cost to the customer.
- Use only sales material provided and approved by Coastal Equities, Inc.

22.3.3 Requirements for Specific Products

This section explains requirements that apply to specific variable products.

22.3.3.1 Deferred Variable Annuities

[FINRA Regulatory Notice 09-32 and 07-53]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Application packages • VA/VUL Disclosure Form • Records of purchases and exchanges
Frequency	<ul style="list-style-type: none"> • Review applications within 7 business days of receipt • Monthly review of VA Blotter
Action	<ul style="list-style-type: none"> • Supervisor: <ul style="list-style-type: none"> ○ Note date when application is received ○ Review application package for completeness ○ Review Disclosure Form and new account information for appropriateness of investment ○ The requirements of Regulation Best Interest (BI) apply to insurance products that are securities; [refer to the chapter <i>REGULATION BEST INTEREST (BI)</i>]. ○ Contact RR for more information if necessary and revise or stop the purchase/exchange, if appropriate ○ Within 7 business days of receipt, approve or disapprove the purchase noting date of action taken ○ For disapproved applications, notify RR • Compliance: <ul style="list-style-type: none"> ○ Review RR activity for patterns of exchanges; review for suitability of exchanges if a pattern is detected ○ Identify potential market timing of investments in sub-accounts ○ Confer with RR's supervisor if necessary ○ Take corrective action if necessary which may include added training for RR, changes to customer investments, limiting RR sales of variable products, or other appropriate activity ○ As part of branch or office reviews, determine timeliness of receipt and review of applications
Record	<ul style="list-style-type: none"> • Supervisor: application packages, VA Disclosure Form with notation of date of receipt and date of review and action taken, where appropriate, signature indicating approval/disapproval • Compliance: reports or other records of purchases and exchanges with notation of action taken, where appropriate; office reviews

A variable annuity is a contract between the purchaser and the insurance company whereby the insurer agrees to make periodic payments to the purchaser, beginning either immediately or at some future date. A variable annuity may be purchased by a single payment or through a series of purchase payments. The underlying investment options typically include mutual funds that invest in stocks, bonds, money market instruments, or some combination of the three.

When offering **deferred variable annuities**, there are specific requirements that apply to the purchase or exchange (not sale or surrender) and the initial subaccount allocations. They also apply to the use of these

products to fund IRAs but not sales to certain tax-qualified employer-sponsored retirement or benefit plans unless recommendations are made to individual participants. **The VA/VUL Disclosure Form form must be submitted** to the designated supervisor with the customer's contract and a copy of the customer's new account information.

The following lists the requirements that apply when recommending these products.

- **Suitability must be determined.** This includes a reasonable basis to believe the customer has been informed about material features such as surrender period and charge, potential tax penalty, mortality and expense fees, charges for and features of enhanced riders, insurance and investment components and market risk. These may be generic disclosure but the RR is also obligated to consider the material features of the specific product.
- **Determine the customer would benefit from certain features** such as tax-deferred growth, annuitization or a death or living benefit. This does not require the customer will benefit from *all* features.
- **The particular deferred variable annuity as a whole and the underlying subaccounts must be suitable.**
- **If the transaction is an exchange from one variable annuity to another, the exchange must be suitable.** Factors that must be considered include whether the customer: (1) would incur a surrender charge, be subject to a new surrender period, lose existing benefits, or be subject to increased fees or charges; (2) would benefit from product enhancements and improvements; and (3) has effected another deferred variable annuity exchange within the preceding 36 months (whether at Coastal Equities, Inc. or another broker-dealer).
- **Make reasonable efforts to ascertain and obtain certain customer information.** This includes the customer's age, annual income, financial situation and needs, investment experience, investment objectives, intended use of the variable annuity, investment time horizon, existing assets (including investment and life insurance holdings), liquidity needs, liquid net worth, risk tolerance, tax status, and other information necessary to make a recommendation.
- **Variable annuities generally are considered to be long-term investments not typically suitable for investors with short-term horizons.** The customer should be aware that withdrawals prior to age 59 1/2 - are subject to tax penalties and many variable annuities assess surrender charges for withdrawals within a specified time period after purchase.
- **Variable annuities cannot be described as "mutual funds."**
- **Variable Annuities are subject to suitability requirements as well as Regulation Best Interest (BI).** Recommendations to retail customers who are natural persons are subject to Reg BI which is broader than the suitability requirement. Reg BI includes recommendations for orders; types of accounts; and investment strategies, including recommendations to prospects. ALL natural persons are included in Reg BI including those deemed "institutional investors" under other FINRA rules.

22.3.3.1.1 Market Timing

RRs may not facilitate or permit customer engagement in market timing in sub-accounts. Market timing is rapid and repetitive in-and-out trading to take advantage of market movements. Variable annuities are intended for longer-term investing and most (if not all) insurance companies do not permit market timing of investments in sub-accounts.

Engaging in market timing or knowingly aiding someone in that activity in a variable annuity is prohibited.

22.3.3.1.2 Transmission, Review, and Approval of Completed Applications

The RR is responsible for promptly forwarding the completed application package to his/her designated supervisor. The completed application must be reviewed and approved by the designated supervisor within 7 business days of receipt by the supervisor. Incomplete applications will be promptly returned to the RR. If an application is not approved, the RR will be notified. Approved applications will be forwarded by the registrant to the insurance company for processing.

22.3.3.2 Group Variable Annuity Contracts

[FINRA Notice to Members 97-27; FINRA Interpretive Letter dated February 3, 2003 to Marilyn Sponzo]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Proposed contracts
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review contract including underlying investments and objectives of the employer's plan
Record	<ul style="list-style-type: none"> • Group variable annuity contracts

Group variable annuity contracts are designed for employer retirement plans. Insurance companies directly or through broker-dealers contract with an employer to provide variable annuity investments for 401(k), 403(b), 408(k), or other types of retirement plans. The plan is sold to the employer typically with no contact with the employees who participate in the retirement plan.

When offering group plans to employers, RRs must consider the underlying investments, terms of the contract, and the needs and investment goals of the retirement plan.

22.3.3.3 Variable Life Insurance

Variable life insurance is a life insurance contract with an underlying investment component in securities investments. Variable life contracts include two types of policies: variable whole-life and variable universal life. Both allow the policyholder to invest part of the premium in mutual fund-like investment pools called sub-accounts which often include a broad selection of funds from major mutual fund companies. Variable whole-life policies require fixed premiums; variable universal life policies allow the policyholder to vary payments. Variable life insurance offers a death benefit, similar to traditional life insurance. The cash value generated by the investment element is not guaranteed by the insurance company and can fluctuate depending on the performance of the investments.

- Customers must be advised of the risks of variable life insurance including the risk of loss in the underlying investments which may result in a cash value of the policy that is either too low to maintain the value of the death benefit or will become too low if the policyholder does not pay higher premiums.
- Disclosure documents available for variable life products must be provided to the customer at the time of recommendation. A record should be made of provision of the disclosure document (when and to who provided).
- For variable life insurance contracts, has the customer's need for life insurance already been met?

- RRs should not recommend that customer finance a variable life insurance policy from the value of another insurance policy or annuity, such as through the use of loans or cash values, unless the transaction is otherwise suitable for the customer. It may be difficult to justify such a financing arrangement and the practice is strongly discouraged.

22.3.3.4 Variable Life Settlements

[SEC Investor Bulletin on Life Settlements: <http://www.sec.gov/investor/alerts/lifeselements-bulletin.htm>; SEC Life Settlements Task Force, Staff Report to the SEC July 22, 2010: <http://www.sec.gov/news/studies/2010/lifeselements-report.pdf>; FINRA Regulatory Notice 09-42; FINRA Notice to Members 06-38]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Proposals from life providers • Life provider contracts including confidentiality policies • Variable life settlement transactions
Frequency	<ul style="list-style-type: none"> • As required - review a potential life provider • As required - review life provider's promotional material • Daily - review variable life settlement transactions • Annual and ongoing - provide training
Action	<ul style="list-style-type: none"> • Due diligence of potential life provider: <ul style="list-style-type: none"> ○ Review contracts and confidentiality policies ○ Determine whether licensing is required and, if required, confirm the provider is licensed ○ Review other available information about the life provider's background, dealings with other firms • Review commissions to be charged and subject any above 5% to heightened scrutiny including a written justification of higher commissions • Compliance review of sales/promotional materials: <ul style="list-style-type: none"> ○ Review for reasonableness and avoidance of unwarranted promises or high-pressure sales ○ Submit to FINRA within 10 days of first use • Submit proposed related products (derivatives based on life settlements) to the new product review process prior to offering • Review of life settlements offered: <ul style="list-style-type: none"> ○ Review for suitability ○ Determine 2 or more bids have been obtained and best price provided to customer • Review of sales of derivative life settlement products: <ul style="list-style-type: none"> ○ Review for suitability
Record	<ul style="list-style-type: none"> • Due diligence file includes review of life providers • Records of heightened scrutiny of proposed commissions exceeding 5% • Compliance retains copies of sales/promotional materials and record of filings with FINRA • Copies of life settlement transactions

- | | |
|--|---|
| | <ul style="list-style-type: none"> • Records sales of derivative products and action taken, if appropriate |
|--|---|

"Life settlements" are the sale of existing life insurance policies to third parties. This secondary market for life insurance policies provides a policyholder the opportunity to sell a policy to a third party for less than the net death benefit but more than the cash surrender value. This market provides available cash to individuals who can no longer make premium payments or who need immediate cash. The value of a life settlement depends on different factors including life expectancy and the nature and terms of the policy. Usually the insured sells the policy to a life settlement provider which holds it until the death of the original policy owner and collects the benefits or sells the policy or bundled policies to other investors. Variable life insurance policies are securities subject to the rules and standards that apply to the sale of securities.

There is also a market for "related products" which are derivatives of life settlements that provide an opportunity to investors to purchase derivative securities that invest in life settlements.

22.3.3.4.1 Obligations Involving the Offer Of Life Settlements

The following are obligations when recommending or facilitating the sale of an existing variable life insurance policy to a third party.

- **Sales may be made only to Firm-approved life settlement providers and brokers.** Some jurisdictions require licensing of providers and confidentiality policies may vary. Coastal Equities, Inc. conducts due diligence on accepted life providers to determine they meet standards consistent with customer protection and needs. Sales may only be made through Coastal Equities, Inc..
- **Understand the product.** As for all products recommended to customers, it is important to understand features of the life settlement being offered and obligations imposed on policyholders such as the requirement to provide notification to the provider of significant medical developments.
- **Use only approved promotional material.** Compliance reviews life provider promotional material prior to use and approves it for distribution to customers.
- **Suitability requirements apply.** A variable life settlement may not be suitable for the customer even if the settlement price exceeds the policy's surrender value. Factors to be considered include:
 - The policyholder's need for continued coverage
 - If the policy is to be replaced with another policy, the availability, adequacy, and cost of comparable coverage
 - The customer's financial needs and objectives
 - Tax considerations
- **Explain the product to the customer.** After understanding the product and making a suitability determination, explain the potential life settlement to the customer. Risks and considerations for an investor considering a life settlement transaction include (but are not necessarily limited to):
 - There may be unexpected tax liabilities (tax treatment of a cash payment may be less favorable than tax treatment of a death benefit paid to a beneficiary).
 - Transaction-related costs may be high, particularly where there are multiple intermediaries.
 - Balancing the need for current income vs. the future financial needs of a beneficiary may be a consideration.
 - The individual may have decreased access to insurance coverage, if needed.
 - The individual's private medical information will be released to intermediaries considering the life settlement.
 - A variable life settlement transaction takes a longer time to complete than a typical securities transaction (weeks vs. days).

- A transaction may affect eligibility for public assistance programs such as Medicaid.
- **Obtain bids from multiple approved providers.** To obtain the best price for the customer, reasonable effort should be made to obtain two or more bids and document those bids. If two or more bids cannot be obtained, document the reason why.
- **Compensation may only be received from Coastal Equities, Inc..** Under no circumstances may an RR receive compensation from an insurance company, a life provider, or other outside person or entity.

22.3.3.4.2 Sales of Related Products

Investment products offer investors the opportunity to purchase securities based on life settlements. RRs are obligated to understand and communicate the risks to prospective purchasers who may be attracted by a relatively higher yield.

- Related products are generally illiquid and the investor may not be able to sell it.
- The yield may be adversely affected by the parties structuring the related product by an inexperienced or incomplete actuarial analysis or an incomplete assessment of the medical conditions of any insured(s) covered by any policy in which an investor has an interest, or by failure to follow applicable law regarding life settlements that may result in legal challenges at the time a death benefit is payable.
- External developments such as advances in medical research may reduce the yield of related products.
- Any guarantees depend on the creditworthiness of the firm that structured the product or of a third-party guarantor whose creditworthiness may be unknown.

22.3.3.5 Bonus Products

[FINRA Notice to Members 02-70; FINRA Regulatory and Compliance Alert Summer 2000]

Some insurance contracts offer a bonus credit feature where the insurance company promises to add a bonus to a variable annuity policyholder's contract value based on a specified percentage (typically 1% to 5%) of purchase payments. RRs must be aware there may be disadvantages and added costs may more than offset the benefit to the customer. For example, as compared to a variable annuity that does not have a bonus feature, there may be higher surrender charges; longer surrender periods; and higher mortality and expense risk charges or other charges. The RR is responsible for understanding the benefits and disadvantages of a bonus product before making a recommendation to a customer.

As part of the designated supervisor's suitability review, bonus products should be considered regarding their overall benefit to the purchasers.

22.3.4 Customer Applications, Payments, And Contracts (Other Than Deferred Variable Annuities)

Responsibility	<ul style="list-style-type: none"> ● Designated Supervisor
Resources	<ul style="list-style-type: none"> ● Variable annuity applications ● VA Disclosure Form ● Contracts received from issuers
Frequency	<ul style="list-style-type: none"> ● As required when applications and payments are received for processing
Action	<ul style="list-style-type: none"> ● Indicate received date when application is received ● Review application/VA Disclosure Form for completeness

	<ul style="list-style-type: none"> • Return application to RR or contact RR to obtain missing information, retaining the customer's check in a pending file • Confirm payment is correct for product being purchased • Upon approval, RR to Promptly transmit complete application and customer's payment to the issuer • Forward customer contracts to the customer if received from the issuer
Record	<ul style="list-style-type: none"> • Maintain record of any applications returned to the RR or requests for additional information forwarded to the RR

Applications must be complete and accurate. Upon receipt of an application and payment from the customer, the application must be immediately forwarded to the designated supervisor for review and payment must be immediately transmitted to the designated person upon supervisory approval.

22.3.5 Communications with The Public Regarding Variable Products

[FINRA Rule 2210 and 2211; FINRA Regulatory Notice 08-12]

Some public communications require the prior approval of Compliance. Communications that include dollar cost averaging, effective yield, and performance illustrations must meet regulatory guidelines for presenting such information.

22.3.5.1 Retail Communications

Only Firm-approved vendor material may be provided to customers. Compliance is responsible for reviewing vendor materials and confirming FINRA approval has been obtained, where necessary, by the vendor. Copies are retained by the Compliance Department including the date of approval and initials of the reviewer.

Firm-developed retail communications regarding insurance products require the approval of Compliance prior to issuance. Compliance is responsible for filing such material with FINRA and retaining a record of filings.

Depending on the content, some material may require providing a prospectus prior to or with the advertising or sales literature.

22.3.5.1.1 Sales Material Provided by Third Parties

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Proposed sales material from third parties
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • For third-party material previously filed with and approved by FINRA: <ul style="list-style-type: none"> ○ Obtain a copy of FINRA approval ○ Review the material for consistency with FINRA standards and approval • For third-party material NOT previously filed with FINRA: <ul style="list-style-type: none"> ○ Review the material for consistency with FINRA standards ○ File with FINRA, if required <ul style="list-style-type: none"> ▪ Upon receipt of review letter, make changes, if necessary

	<ul style="list-style-type: none"> ▪ Indicate supervisor's approval including date of approval
Record	<ul style="list-style-type: none"> • Copy of sales material with notations, as necessary • Copy of FINRA review letter • Record of date first use and (if applicable) date of last use • Retain for three years from date of last use

When sales material (advertising, sales literature, independently prepared reprints) is provided by a third party, the sales material may require FINRA approval prior to use depending on the subject of the sales material. Requests to use outside sales material should be submitted to Compliance for review and approval.

22.3.5.2 Communications

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Outgoing communications
Frequency	<ul style="list-style-type: none"> • Daily
Action	<ul style="list-style-type: none"> • Review for the following: <ul style="list-style-type: none"> ○ Use of pre-approved letters without change other than updating data where required ○ 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 Coastal Equities, Inc.) ○ 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 <i>Disclosure Of Material Facts</i> in the chapter <i>MUTUAL FUNDS</i>) ○ Performance is represented accurately and consistent with rule requirements regarding yield and return ○ Language that indicates a prospectus is enclosed • Contact Compliance for review of questionable communications • Correct unapproved content
Record	<ul style="list-style-type: none"> • Communications with reviewer's initials and notes of changes • Compliance retains communications it reviews

RRs should use letters pre-approved by Coastal Equities, Inc. and include a prospectus or limit communications to stating that a prospectus is enclosed and the RR will be in contact with the customer. Questions should be referred to Compliance.

22.3.5.3 Sales Seminars and Public Presentations

Seminars and presentations including variable products require the prior approval of Compliance. An outline of subjects to be covered and any handouts or copies of slides or other presentation materials must be provided for review. Compliance will retain records of materials reviewed including date of review and initials of the reviewer and any changes to be made.

22.3.6 Replacements

It is inappropriate to recommend replacing an existing annuity with a new annuity when there is no reasonable basis or economic justification for making that recommendation (churning) or make misrepresentations to encourage someone to replace an existing contract ("twisting"). RRs are obligated to obtain signed replacement letters or other required disclosure forms when replacing one variable annuity contract with another.

22.3.7 Redemptions

When a customer redeems a variable annuity, the following procedures must be followed:

- Obtain the customer's signature on any required redemption forms
- Follow the "replacement procedures" described earlier, if one annuity is being redeemed to buy another
- Have the customer's signature guaranteed by Operations or have the customer obtain a signature guarantee from a bank or other financial institution

22.3.8 Annuity Buybacks

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Transaction records
Frequency	<ul style="list-style-type: none"> • Dependent on availability of reports
Action	<ul style="list-style-type: none"> • Identify buybacks and review alternative investment product for suitability • If less favorable, determine if customer was notified • Cancel or otherwise correct inappropriate transactions
Record	<ul style="list-style-type: none"> • Record of reviews and action taken

Insurance companies sometimes offer to buy back an investor's variable annuity product. RRs may not recommend the customer accept the buyback unless the customer understands if an alternative variable product has less favorable terms and those terms are disclosed to the customer.

22.3.9 Considerations for Newly-Hired RRs [Repeated from Chapter 2]

[FINRA Regulatory Notice 07-36; FINRA Notice to Members 07-06]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Information about transferring customers' investments in variable company products
Frequency	<ul style="list-style-type: none">• As required for proposed switching of investments
Action	<ul style="list-style-type: none">• Review existing investments against proposed substitute investments with particular review of proposed reinvestment in bonus variable annuity products• Prepare information and provide it to customers regarding options including that the customer may have to hold the existing investment at the prior firm, the cost of switching to another investment, and other considerations before changing investments
Record	<ul style="list-style-type: none">• Records of accounts reviewed and suitability determination, action taken including information provided to customers

There are considerations when a newly-hired RR transfers customers who hold variable company products (mutual funds, variable annuities). If Coastal Equities, Inc. cannot or will not service the customer's existing investment (inability to transfer products, Coastal Equities, Inc. does not have a dealer or servicing agreement), the appropriateness and suitability of recommending a new investment company product must be determined by the RR and Coastal Equities, Inc. Before liquidating existing investments and reinvestment in new products, disclosure must be made to the customer regarding the costs and benefits of any proposed change in investments and proposed replacement investments must be suitable. A change of employment is not by itself a suitable basis for recommending a switch from one product to another.

22.4 Buyout Offers

A buyout offer refers to an offer by an insurance company to either: (1) increase your contract value in exchange for giving up a benefit; or (2) increase your cash surrender value in exchange for surrendering your variable annuity. When consulting with the customer, the RR must include the following considerations:

- Buyout offers are optional. The customer has no obligation to accept.
- The customer will lose a particular benefit.
- Buyout offers may include:
 - surrendering the contract for a cash equivalent where the customer may receive an increased surrender value, waiving of penalties, removing the death benefit, reducing the guaranteed minimum income benefit, or tax reduction (with taxes due if the cash equivalent is more than the customer paid for the contract)
 - swap the product for other types of annuities
- The amount of the offer may fluctuate. The insurance company can advise of the current value.
- Is the buyout in the customer's best interest considering age, financial status, and investment objectives?
- Will the customer be subject to a surrender charge?

- If the customer will transfer the cash surrender value to another annuity, will there be a new sales charge, other fees, or new surrender charge period?

An RR's recommendation to reject a buyout and rationale must be documented and delivered to the customer in writing by mail or by email.

Acceptance of customer buyout offers requires documentation of the above considerations justifying the buyout and any replacement and the prior written approval of the RR's designated supervisor. Designated supervisors should review the recommendation for suitability or to determine whether the recommendation and replacement, if any, is in the best interest of the client.

23 New Products and Due Diligence

[FINRA Notice to Members 05-26]

Responsibility	<ul style="list-style-type: none"> • New Product Committee • Product Due Diligence Supervisor or designee
Resources	<ul style="list-style-type: none"> • New Product Review Checklist or Product Summary Sheet • Other information available about the new product
Frequency	<ul style="list-style-type: none"> • As required when new products are proposed
Action	<ul style="list-style-type: none"> • Conduct a review to: <ul style="list-style-type: none"> ○ Determine the product is beneficial for customers ○ Determine the types of customers that are the target market ○ Conduct appropriate due diligence about features and risks of the product ○ Determine whether written disclosures or educational information should be provided to potential purchasers ○ Determine what information should be provided to RRs and supervisors, including any additional training ○ Consult appropriate product specific guidelines in the WSP manual for additional reference material • Approve or disapprove the product for distribution
Record	<ul style="list-style-type: none"> • Approved New Product Review Checklists are retained in a file for the product • Other reviewed Checklists are retained in a New Product Review Checklist file

All new products require review and approval prior to offering new products to customers. If there is a question whether a product may be a "new" product, it should be submitted for the new product review. In general, market securities and products currently offered by Coastal's clearing firm are not considered New Products.

FINRA states:

What is the definition of a new product? What is considered a material change?

The definition is:

New Product Manufactured:

New or innovative products that your firm has developed:

- Products that are new to the industry, or that the firm is one of the first to introduce to the market (including indices);
- Existing products with novel and/or material modifications, such as the addition of innovative structural elements (e.g., protection features, novel asset class), a conversion of a traditional institutional product for sale to retail investors, etc.

New Product Distributed:

New products that your firm has started selling:

- "New" products that your firm is selling for the first time.
- Existing products that have gone through a novel and/or material modification, such as: the addition of innovative structural elements (i.e., protection features, novel asset class), a conversion of a traditional institutional product for sale to retail investors, etc.

We are not seeking to collect information on every product that your firm offers. For instance, in the case of mutual funds, we are not asking you to list every new mutual fund that your firm makes available to investors. If you have been offering, for example, emerging markets funds we do not want you to include a newly-added emerging markets fund that is substantially similar to those already on your platform. We are interested in learning about new *types* of products that your firm is distributing for the first time, such as a new type of mutual fund that entails different risks or offers exposure to new strategies or asset classes than the funds you currently offer. Floating-rate senior loan funds, mutual funds investing in private company shares, or managed futures mutual funds may be examples of funds that meet the "new" criteria. [New Product Inquiry - Frequently Asked Questions \(finra.org\)](#)

23.1 New Product Review Checklist/Product Summary

Individuals and departments wanting to offer new products are required to prepare information for the review by completing the New Product Review Checklist. Information to be provided includes a description of the product, to whom the product would be offered, and economic justification of the product. The requestor will be notified regarding approval/disapproval or the need for modifications or additional information.

When conducting internal due diligence, the firm may utilize another product summary form or the New Product Review Checklist at his or her discretion, so long as the format is acceptable to the New Product Committee and the form substantially addresses the information required by this section.

23.2 Review Process

The New Product Committee will consider product specific factors raised by the New Product Review Checklist and factors identified in this manual raised in a product-type's 'due diligence' section as appropriate by reviewing issuer materials, and may also review third-party materials such as reports and searches for negative news. Private Placements and DPPs require heightened due diligence as described in each respective Chapter.

The Product Due Diligence Committee will vote to approve or not approve each product and any restrictions thereto.

23.3 Training

A determination will be made by the committee or due diligence officer reviewing the new product regarding the need for training before the product is made available for sale. Considerations include:

- Whether RRs are already knowledgeable about the product including pre-existing training
- Sophistication of targeted investors
- Complexity of the product

24 SOFT DOLLARS

[Exchange Act Section 28(e); SEC Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934 - Release No. 34-54165; SEC Brokerage and Research Activities Release No. 34-23170; SEC Inspection Report on the Soft Dollar Practices of Broker-Dealers, Investment Advisers and Mutual Funds: <http://www.sec.gov/news/studies/softdollar.htm>]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Soft Dollar Arrangement Request Form
Frequency	<ul style="list-style-type: none"> • As required - review and approve/disapprove arrangements and send Soft Dollar Letter to adviser • Quarterly - review accounts • Annually - provide statements to advisers
Action	<ul style="list-style-type: none"> • Review requests for soft dollar arrangements and approve or disapprove • Maintain a list of soft dollar arrangements including advisers and products/services provided • For third party soft dollar arrangements, review and approve payments to vendors directly billed to the Firm (do not accept invoices from the adviser for payment) • Review accounts and commission paid for consistency with soft dollar arrangement and contact adviser if there is a material imbalance • Prepare and provide annual statement to adviser
Record	<ul style="list-style-type: none"> • Soft Dollar Arrangement Request Forms • Soft Dollar Letters • Account review including notations of action taken • Annual statements to advisers • Vendor bills paid directly by the Firm • Master list of soft dollar arrangements

This chapter provides a summary of key requirements for soft dollar arrangements between Coastal Equities, Inc. and an adviser or customer. References to "adviser" include money managers and other fiduciaries with investment discretion over their client accounts. Because of the complex legal nature of this subject, this chapter should not be used to determine compliance of any arrangement since each arrangement must be reviewed on a case-by-case basis. While compliance with soft dollar rule requirements is primarily the responsibility of the adviser, Coastal Equities, Inc. has procedures for review of these arrangements to facilitate compliance with the rules.

All proposed soft dollar arrangements require the **prior approval** of Compliance. Advisers will be provided with a letter explaining some basic understandings regarding their obligations in the arrangement (see the *Soft Dollar Letter*).

24.1 Background

In 1975, the system of fixed commission was abolished and replaced with negotiated rates. Fiduciaries such as money managers and advisers were at risk of breaching their fiduciary duty if they caused their clients to pay more than the lowest commission rates to pay for services "provided by" (but not necessarily produced or created

by) broker-dealers. Section 28(e) of the '34 Exchange Act was adopted to provide a "safe harbor" for these fiduciaries.

The safe harbor provides that "a person who exercises investment discretion with respect to an account shall not be deemed to have acted unlawfully or to have breached a fiduciary duty solely by reason of his having caused the account to pay more than the lowest available commission if such person determines in good faith that the amount of the commission is reasonable in relation to the value of the brokerage and research services provided." In simpler terms, an adviser may pay higher commissions for services provided by the broker-dealer if the commission paid is reasonable in relation to services provided. Soft dollars arrangements must be for the benefit of the adviser's clients and not for the benefit of the adviser's business.

24.2 Soft Dollars Defined

The SEC defines soft dollar practices as arrangements under which products or services (other than executions of securities transactions) are obtained by an adviser from or through a broker-dealer in exchange for the adviser directing client brokerage transactions to the broker-dealer. An individual or firm must exercise investment discretion over an account in order to use client commissions to obtain research under Section 28(e).

Permissible services under a soft dollar arrangement are included in Section 28(e); the SEC issues additional guidance through interpretive releases, no-action letters, and reports. Services and products outside the 28(e) safe harbor do not automatically place the adviser in violation of fiduciary responsibilities, however, most firms rely on the safe harbor to avoid potential violations.

24.3 General Definitions

Providing research: Broker-dealers "provide" research if they (i) prepare the research; (ii) are financially obligated to pay for the research; or (iii) are not financially obligated to pay but their arrangements have certain attributes.

Brokerage services: Those products and services that relate to the execution of the trade from the point at which the money manager communicates with the broker-dealer for the purpose of transmitting an order for execution through the point at which funds or securities are delivered or credited to the advised account.

Lawful and appropriate assistance: The adviser must determine that the research or brokerage service provides "lawful and appropriate assistance" in performing decision-making responsibilities. What constitutes lawful and appropriate assistance in any particular case will depend on the nature of the relationship between the various parties involved and is not subject to hard and fast rules.

Mixed or multiple use: The manner in which a service or product provided to a fiduciary by the broker-dealer through a soft dollar arrangement may be used for both brokerage and research services and for other purposes.

24.4 Agency and Riskless Principal Transactions

[Commission Guidance on the Scope of Section 28(e) of the Exchange Act: SEC Release No. 34-45194]

The SEC has interpreted Section 28(e) to apply only to securities transactions executed on an agency basis and to certain riskless principal transactions. Principal transactions do not fall within the safe harbor.

24.5 Research Services

The types of services permitted under the safe harbor include research that:

- constitutes "advice," "analysis," or a "report"* concerning issuers, industries, securities, economic factors and trends, portfolio strategy, and the performance of accounts;
- provides appropriate assistance for the purpose of investment decision-making (for example, advice on portfolio strategy vs. advice on the adviser's management or operations);
- is not "mass-marketed" to the general public (such as daily or weekly newspapers); and
- the amount paid is reasonable in view of the services provided.

*To qualify as advice, analysis, or a report, products or services must be substantive in nature and contain an "expression of reasoning or knowledge" on an appropriate subject matter (which would include issuers, industries, securities, economic factors and trends, portfolio strategy and the performance of accounts).

Products and services which **may** (or may not) qualify as research (judged on a case-by-case basis) include:

- Traditional research reports on particular issuers or securities
- Discussions with research analysts
- Financial newsletters and trade journals that are not mass-marketed and that relate to investment decision-making
- Quantitative analytical software and software that analyzes securities portfolios, in each case reflecting an expression of reasoning or knowledge
- Meetings with corporate executives to obtain oral reports on the performance of a company
- Fees for seminars and conferences on appropriate subject matter (but not related expenses, such as travel)
- Consultants' services relating to portfolio strategy
- Market data that serve a legitimate pricing function or that serve to keep an adviser informed of market developments
- Advice on market color, execution strategies and potential buyers and sellers

24.5.1 Research Services NOT Permitted Under the Safe Harbor

- Travel expenses, entertainment and meals associated with attending seminars or conferences
- Publications that are mass-marketed
- Physical products, including telephone lines, office furniture and equipment and business supplies ("overhead" items)
- Internal expenses and overhead and administrative expenses of the adviser, such as salaries (including research staff), rent, accounting fees and software, website design, e-mail software, internet services, legal expenses, personnel management, marketing, utilities, membership dues, professional licensing fees, and software to assist with administrative functions such as managing back-office functions, operating systems, and word processing
- Computer hardware and computer accessories, including the peripherals and delivery mechanisms associated with computer hardware, including telecommunications lines and computer cables
- Advice relating to a manager's internal management or operations

24.6 Brokerage Services

Brokerage services that qualify for the 28(e) safe harbor are limited to those that assist order execution in the time between the transmission of an order and the time that the trade is cleared and settled. Products and services used by the adviser for pre-order entry functions generally are not eligible for 28(e) payments.

Examples of eligible brokerage products or services include:

- Communications services related to the execution, clearing, and settlement of securities and other incidental functions, relating to connectivity, such as dedicated lines between the broker-dealer and the money manager's order management system; lines between the broker-dealer and order management systems operated by a third-party vendor; dedicated lines providing direct dial-up service between the money manager and the trading desk at the broker-dealer; and message services used to transmit orders to broker-dealers for execution
- Trading software operated by a broker-dealer to route orders to market centers and algorithmic trading software
- Incidental brokerage services associated with clearance, settlement and short-term custody services
- Post-trade matching; comparison services required by the SEC or another regulator (for example, the use of electronic confirmation and affirmation of institutional trades)

24.6.1 Brokerage Products and Services NOT Eligible

- Order management systems and hardware, such as telephones or computer terminals, trade analytics, surveillance systems, or compliance mechanisms
- Error correction trades or related services in connection with errors made by money managers
- Services used to fulfill compliance requirements
- Long-term custody provided post-settlement

24.7 Mixed Use Products and Services

When an amount covers items that qualify under 28(e) as well as items that do not, only the eligible amount may be paid and the adviser must maintain documentation for mixed use products or services.

24.8 Investment Adviser Obligations

As fiduciaries, investment advisers must act in the best interest of their clients and may not use client assets for their own benefit without consent; advisers are also obligated to seek best execution of client transactions. Advisers generally may not use commissions to obtain products or services outside the Section 28(e) safe harbor.

The adviser has the obligation to determine:

- whether a brokerage or research service falls within the limits of Section 28(e);
- whether the product or service actually provides "lawful and appropriate assistance" to the adviser in the performance of investment decision-making responsibilities; and
- based on a good faith determination, the amount of client commissions paid is reasonable in relation to the value of products or services provided by the broker-dealer.

Where a product or service has a "mixed use" the adviser must make a reasonable allocation of the costs of the item according to such use.

As fiduciaries, advisers are required to disclose any material conflicts of interest and how they mitigate those conflicts. Soft dollar arrangements are disclosed in Form ADV, Part II, which advisers must provide to clients. If the value of research products or services plays a role in an adviser's decision to use certain broker-dealers, the adviser must describe (i) the research products and services; (ii) whether clients may pay higher commissions than those available from other BDs in return for those products and services; (iii) whether the research is used to service all of the adviser's clients or just those accounts whose commission dollars are used to acquire research products or services and (iv) any procedures the adviser has used to engage in soft dollar arrangements.

24.9 Broker-Dealer Obligations

For Section 28(e) to be available, the broker-dealer to which the adviser pays higher commissions must "provide" the relevant research or brokerage. Broker-dealers receiving soft dollar commissions must satisfy two tests:

1. that they be involved in "effecting" the trade; and
2. that they "provide" the research.

Effecting: A broker-dealer is deemed to be "effecting" a trade if it:

- was financially responsible for all customer trades until the trades settled;
- made and/or maintained records relating to its customer trades, including blotters and memoranda of orders;
- monitored and responded to customer comments concerning the trading process;
- generally monitored trades and settlements; or
- executed, cleared or settled the trade.

Provides: A broker-dealer could continue to satisfy the provide requirement by actually preparing the research or by being responsible for paying for the research. Also see the section that follows: *Third Party Services*.

24.10 ERISA Plans

[Pension and Welfare Benefits Administration (PBWA) of the Department of Labor: ERISA Technical Release 86-1]

Where soft dollar arrangements involve ERISA (pension and other defined benefit) plans, the rules of ERISA also govern (see the chapter *ACCOUNTS* and the section *Pension And Retirement Accounts* and the subsection on *ERISA*). An adviser cannot accept soft dollar services if these services reduce the manager's cost of doing business in managing a wide range of assets outside the ERISA plan(s). The service must benefit the plan on whose behalf the soft dollars are paid. The Department of Labor has oversight over ERISA plans and will, on occasion, examine the investment manager's activities if it appears there has been a violation of ERISA, including soft dollar arrangements.

Advisers generally may not use plan commissions to obtain products or services outside the Section 28(e) safe harbor.

24.11 Third Party Services

[SEC No-action letter dated January 17, 2007 to Steven Stone, Morgan, Lewis and Bockius regarding Status of Service Providers in Goldman, Sachs and Co.'s Research XPRESS Program]

Advisers are not limited to receiving proprietary research (produced by the broker-dealer party to the soft dollar arrangement) to benefit from the 28(e) safe harbor. Research may be produced by a third party and still be eligible for the safe harbor if it is "provided by" the broker-dealer. The research may be delivered directly to the adviser but the BD must be obligated to pay for the service. Whether the third-party research qualifies for the safe harbor depends on the nature of the product or service, how the adviser uses it, and the adviser's good faith determination that the commissions paid are reasonable in relation to the research and brokerage received.

Attributes that assist in determining whether the research is "provided by" the broker-dealer include:

- the broker-dealer pays the research preparer directly;

- the broker-dealer reviews the description of services to be paid for with client commissions under the safe harbor for red flags indicating the services are not within Section 28(e) and agrees with the adviser to use client commissions only to pay for those items that reasonably fall within the safe harbor; and
- the broker-dealer develops and maintains procedures so that research payments are documented and paid for promptly.

All services provided under a third party soft dollar arrangement will be charged at the amount billed by the vendor for purposes of calculating soft dollar commissions, *i.e.*, Coastal Equities, Inc. will NOT mark up the vendor's bill.

24.12 Commission-Sharing Arrangements

In order for an adviser to use the safe harbor in a commission sharing arrangement, the broker-dealer effecting the adviser's client transactions must perform at least one of the four functions below and take steps to determine that other functions have been allocated to other broker-dealer(s) in the arrangement:

1. Be financially at risk to the clearing broker-dealer for its customers' failure to pay;
2. Keep records of customer trades in accordance with SEC and SRO rules;
3. Monitor and respond to customer comments concerning the trading process; and
4. Generally monitor trades and settlements.

24.13 Approval of Soft Dollar Arrangements

When requesting a soft dollar arrangement, the *Soft Dollar Arrangement Request Form* must be completed and provided to Compliance which must approve the arrangement **before** it becomes effective.

24.14 Statements

Coastal Equities, Inc. will provide the adviser with a statement, at least annually, of the services provided and the soft dollar commitment to pay for those services.

24.15 Commission Recapture Programs

Responsibility	<ul style="list-style-type: none"> • Compliance: review/approval • Other reviews: Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests for commission recapture
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Compliance: Review requests and approve or disapprove • Obtain written agreement signed by the investor and Coastal Equities, Inc. • Review quarterly statements for consistency with agreement • Take corrective action if discrepancies are identified which may include review with the RR, customer, and any necessary adjustments
Record	<ul style="list-style-type: none"> • Review and approval or disapproval

	<ul style="list-style-type: none">• If approved, obtain written agreement• Quarterly statements summarizing commission payments
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Commission recapture is a process where an institutional investor receives a rebate resulting from brokerage transactions incurred through the investor's investment manager. This rebate represents a portion of commissions or markups/markdowns on these investment transactions. "Directed brokerage" is where plan sponsors direct investment managers to execute a portion of their trades through a selected brokerage firm to the extent the brokerage firm is competitive in price and trade execution. The rebate is paid directly to the investor, usually as hard-dollar payments sent to the investor's custodian. The overriding requirement is that recaptured commissions must benefit the fund or pension plan which may reinvest the funds or pay for authorized expenses. The net effect is to save money for the investor by lowering transaction costs.

Where Coastal Equities, Inc. offers commission recapture, the following procedures apply:

- Review and approval of each program by Compliance.
- When approved, an agreement will be executed between Coastal Equities, Inc. and the investor outlining the terms of the recapture program including how rebated commissions will be paid.
- Coastal Equities, Inc. will provide quarterly statements to the investor summarizing commission recapture payments.

25 REGULATION BEST INTEREST (BI)

[SEC final rule: <https://www.sec.gov/rules/final/2019/34-86031.pdf>; SEC small entity compliance guides: <https://www.sec.gov/info/smallbus/secg/regulation-best-interest> and <https://www.sec.gov/info/smallbus/secg/form-crs-relationship-summary>; SEC release announcing adoption of Reg BI with a link to the entire regulation: https://www.sec.gov/news/press-release/2019-89?mod=article_inline; FINRA Reg BI and Form CRS Checklist: <https://www.finra.org/sites/default/files/2019-10/reg-bi-checklist.pdf>; FINRA Regulatory Notice 19-26; FINRA website re Reg BI: <https://www.finra.org/rules-guidance/key-topics/regulation-best-interest>]

Regulation BI is an SEC regulation that requires a broker-dealer (BD) and its associated persons (RRs in this chapter) to act in the best interest of the retail customer at the time the recommendation is made, without placing the financial or other interest of the broker-dealer or RR ahead of the interest of the retail customer. The purpose of this Chapter is to provide an overall view of Reg BI and to explain how CEI complies, while other Chapters of this manual have been updated where appropriate to comply with the requirements of Regulation Best Interest even though they do not appear in this Chapter.

25.1 Summary of Key Requirements

1. Regulation BI applies only to recommendations to natural persons who are retail customers. Reg BI **also** applies to recommendations to natural persons who are considered "institutional accounts" under FINRA rules.
2. Recommendations include those for orders; types of accounts (*e.g.*, brokerage vs. advisory, whether or not tied to a securities transaction); and investment strategies. Also included are recommendations to prospects.
3. The "best interest" standard goes beyond suitability requirements for recommendations; it requires acting in the customer's best interest and not the RR's or BD's interest including consideration of available alternatives and cost/risk rewards.
4. Compliance with Reg BI requires meeting four obligations: disclosure, care, conflict of interest, and compliance.
5. If the BD agrees to monitor a customer's account, Reg BI applies to explicit and implicit recommendations to hold. Reg BI does not impose a duty to monitor customer accounts.
6. Form CRS must be provided to customers when an account is opened (including additional accounts for existing customers) and when a recommendation is made (as defined in this chapter). Form CRS is posted on the Firm's website and updates must be provided to customers within 60 days of material updates.
7. BDs and their professionals are not permitted to use the titles "advisor" or "adviser" unless the RR is also a supervised person of a registered investment adviser.
8. Incentive programs (sales contests, non-cash compensation, *etc.*) may not be limited to certain securities or types of accounts over a period of time.
9. Communications for education purposes (listed below) that do not include a recommendation of a particular security or strategy involving securities are not considered recommendations:
 - o General financial and investment information which encompasses basic investment concepts.
 - o Descriptive information about an employer-sponsored retirement or benefit plan.
 - o Certain asset allocation models based on generally accepted investment theory accompanied by necessary disclosures.

25.2 General Obligations

Compliance with each of the following four component obligations is necessary to comply with Regulation BI.

25.2.1 Disclosure

[SEC FAQs on Form CRS: <https://www.sec.gov/investment/form-crs-faq>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor - confirmation of Form CRS delivery • Conflicts and Risk Management Committee
Resources	<ul style="list-style-type: none"> • New product reviews and information • Form CRS • Other resources regarding securities and accounts
Frequency	<ul style="list-style-type: none"> • Form CRS and Reg BI Disclosure: at or before the time an account recommendation is made or an account is opened for a new customer • Financial Professional Brochure: at time of account opening or at or before first recommendation • Conflicts and Risk Management Committee annually: <ul style="list-style-type: none"> ○ Review products and services to confirm necessary disclosures are provided to retail customers including possible standardized disclosures ○ Consider the need for specific training • Within 30 days after a material change - update disclosures • Other disclosures: as required or supplemented by prospectus and/or confirms
Action	<ul style="list-style-type: none"> • Identify necessary disclosures and other requirements for new securities or services • Identify necessary disclosures as part of a review of current products and services • Update disclosures if there have been any material changes • Provide Form CRS to retail investors at time of a recommendation/account opening and within 60 days of material changes • Include review of disclosures in annual review of firm's procedures
Record	<ul style="list-style-type: none"> • Reviews of products and services and actions taken for disclosure • Tracking of providing disclosures including version, date provided, to whom provided including Form CRS • Various other methods of disclosure (confirmations, monthly statements, account agreements, prospectuses, <i>etc.</i>)

The obligation to provide full and fair disclosure should give sufficient information to enable a retail investor to make an informed decision with regard to a recommendation.

The disclosure obligation requires a BD or RR, prior to or at the time of the recommendation, to provide the retail customer, in writing, full and fair disclosure of:

- All material facts relating to the scope and terms of the relationship with the retail customer, including:
 - That the BD or associated person is acting as a BD or an associated person with respect to the recommendation;

- The material fees and costs that apply to the retail customer's transactions, holdings, and accounts;
- The type and scope of services provided to the retail customer, including any material limitations on the securities or investment strategies involving securities that may be recommended to the retail customer; and
- Material facts relating to conflicts of interest that are associated with the recommendation. "Material facts" are facts a retail customer would consider important in making an investment decision. For example, material facts relating to conflicts of interest including, but not limited to, how RRs are compensated and the benefits to a BD from recommending a proprietary product.
- Other material facts relating to the scope and terms of the relationship with the retail customer which include:
 - The general basis for a recommendation (*i.e.*, what might commonly be described as investment approach, philosophy, or strategy); and
 - Risks associated with recommendations in standardized terms.
- If necessary, other material facts relating to the scope and terms of the relationship.

Disclosures are provided in a variety of ways, including (but not necessarily limited to) the following:

- Electronic mailings to those who have consented to receive electronic delivery
- Form CRS Relationship Summary
- Confirmations
- Monthly statements
- Account opening documents and account agreements
- Disclosures specific to types of accounts (e.g., margin, option, IRAs, minimum size or investment)
- Firm's website
- Hyperlinks
- Standardized disclosures
- Disclosures specific to certain securities or products (e.g., risk, conflicts of interest, material limitations)
- Agreements for services including costs
- Fee schedules
- Prospectuses
- Personalized account portals

While disclosures must be in writing, in certain circumstances oral disclosures (no later than the time of the transaction) to supplement facts not reasonably known at the time written disclosure is made (a record of oral disclosures) must be maintained with the order record.

Coastal satisfies its Disclosure Obligation in a layered fashion:

- Coastal's Form CRS with hyperlinks provides the high-level disclosures required under Regulation Best Interest
- Coastal supplements its Disclosure Obligation by delivering to each retail customer its Regulation Best Interest Disclosure document
- The above documents will reference hyperlinks to the firm's current brokerage services, service models and products, brokerage fees and compensation, conflicts of interest and additional resources, including where information may be disclosed post-recommendation as permitted by Regulation Best Interest
- Individual Financial Professionals ("FP") will maintain and deliver a Financial Professional Brochure to supplement disclosure of material information unique to the FP

Records of delivery will be maintained in an electronic log for items delivered by email, and a branch delivery log for items delivered in paper form to retail customers, to include customer name, document delivered, and date of delivery.

New Customers to the Firm: Supervisors will not approve a new customer account opening without first verifying delivery of Form CRS, Reg BI Disclosure, and FPB, unless the account is an advisory account or non-retail customer. A "new customer" is defined herein for purposes of this section to mean a customer to whom the Firm's Form CRS has not been delivered. Approval of the account in Smart Station, or by signature on direct business when a direct business customer has not opened a First Clearing brokerage account, shall be evidence that the supervisor verified delivery.

25.2.2 Care

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Customer account information • Information about securities • Available reports
Frequency	<ul style="list-style-type: none"> • When recommendations are made • Other: as required
Action	<ul style="list-style-type: none"> • Communicate risks, costs, and other necessary information to RRs • Review recommendations of transactions and opening of accounts • Confirm recommendations are documented in Smart Station Contact Management
Record	<ul style="list-style-type: none"> • Trade records • Account records • Risk-based reviews of trade and account recommendations with supervisor's record of supervision and actions taken, if any

The care obligation is broader than the existing suitability standard because it: (1) explicitly requires that the recommendation be in the customer's best interest and that the BD and RRs do not place their interests ahead of the customer; (2) explicitly requires that cost be a consideration; (3) applies the quantitative suitability requirement (recommending a series of transactions, avoiding excessive activity); and (4) requires the BD and RRs to consider "reasonably available alternatives" as part of having a "reasonable basis to believe" that the recommendation is in the best interests of the customer.

The RR must exercise reasonable diligence, care, and skill to:

- understand the risks, rewards, and costs associated with the recommendation;
- have a reasonable basis to believe the recommendation is in the customer's best interest; and
- have a reasonable basis to believe that recommended transactions are in the customer's best interest based on the customer's investment profile and doesn't place the interests of the BD ahead of the customer. This includes avoiding transactions that are excessive.

In particular, the BD and RR must have an understanding of complex products, and recommendations of complex investments should be documented, particularly where a recommendation may seem inconsistent with a retail customer's objectives on its face. The care obligation applies to a series of recommended transactions (quantitative suitability) whether or not the BD exercises actual or *de facto* control over the account.

The RR is responsible for documenting each recommendation to his/her client in Smart Station Contact Management. For any customers who do not hold a brokerage account at First Clearing, the RR must open a 'Prospect' in Smart Station Contact Management in order to maintain such notes.

25.2.2.1 Factors to Consider

When making recommendations, the following non-exclusive list of factors (depending on the particular product or strategy recommended) may be considered:

- What are the characteristics (including any special or unusual features) of the security or strategy?
- What are the initial and subsequent costs (if any, *e.g.*, surrender or redemption costs) of the security or strategy?
- How liquid is the security?
- What are the risks, volatility, and likely performance in a variety of market conditions (normal or stressed)?
- What is the expected return of the security?
- What are the financial incentives to recommend the security or investment strategy?
- Are there alternative investments or strategies, at lower cost, that may meet the customer's needs? More costly products may be recommended provided there is a reasonable basis to believe they are in the best interest of the customer. There is no obligation to recommend the "best" of all possible alternatives.

25.2.2.2 Recommending Types of Accounts

RRs must have a reasonable basis for recommending accounts (margin, brokerage or advisory, IRAs, *etc.*). This includes the following considerations:

- services and products provided in the account;
- projected cost of the account;
- alternative account types available;
- services the retail customer requests; and
- the retail customer's investment profile. Profile elements include age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information disclosed by the customer.

Additional considerations when recommending IRAs (including rollovers or transfers of assets in a workplace retirement plan account to an IRA) include:

- customer's current financial situation and liquidity needs;
- fees and expenses;
- level of services available;
- ability to take penalty-free withdrawals;
- application of required minimum distributions;
- protections from creditors and legal judgments;
- holdings of employer stock; and
- any special features of the existing account.

The New Account Opening Wizard provided by WFCS incorporates questions to be answered relating to account type selection and factors considered in light of Regulation Best Interest. Supervisors shall consider the responses thereto in determining whether to approve the account recommendation, and the supervisor's signature shall be evidence of that review.

25.2.2.3 Costs

The RR should understand and consider the potential costs associated with the recommendation and have a reasonable basis to believe that the recommendation does not place the financial or other interest of Coastal Equities, Inc. or the RR ahead of the interest of the retail customer. While cost must be considered, it should never be the only consideration. Cost is only one of many important factors to be considered regarding the recommendation and that the standard does not necessarily require the "lowest cost option." RRs need to consider costs in light of other factors and the retail customer's investment profile.

25.2.2.4 Alternatives

Alternatives should be considered before making recommendations to a particular retail customer. This does not mean customers must be offered all alternatives or necessarily the lowest-cost alternative or the "single best" alternative. Reasonably available alternatives include considerations of, for example:

- An RR's customer base (including the general investment objectives and needs of the customer base)
- Investments and services available to the RR to recommend (including limitations due to the RR's licensing)
- Specific limitations on the available investments and services with respect to certain retail investors (*e.g.*, product or service income thresholds; product geographic limitations; or product limitations based on account type, such as those only eligible for IRA accounts)

25.2.2.5 Quantitative Suitability

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Records of transactions • Available reports • Customer account records
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Identify active accounts and review non-trade alerts and account review population in Super Vision, which may include review for: <ul style="list-style-type: none"> ○ turnover rate (dividing the aggregate amount of purchases by the average monthly investment) ○ velocity or cost-to-equity ratio (percentage of return on the customer's average net equity needed to pay commissions and other expenses) ○ in-and-out trading (sale of newly-acquired investments) • Take action which may include: <ul style="list-style-type: none"> ○ Review of new account records ○ Consult with RR

	<ul style="list-style-type: none"> ○ Contact the customer
Record	<ul style="list-style-type: none"> ● Review of active accounts including action taken by using account review worksheet in Super Vision ● Documentation of contact with customers in Super Vision

RRs may not make recommendations that result in transactions excessive for the customer considering the customer's investment objectives (also known as "churning"). A series of recommended transactions must be in the customer's best interest. The customer may be contacted by Coastal Equities, Inc. to confirm that active trading is appropriate.

25.2.3 Conflict of Interest

[FINRA website on conflicts of interest: <https://www.finra.org/rules-guidance/key-topics/conflicts-of-interest>]

Responsibility	<ul style="list-style-type: none"> ● Designated Supervisor ● Conflicts and Risk Management Committee ● New Product Review Committee
Resources	<ul style="list-style-type: none"> ● Reviews of products and services ● Review of incentive programs, if any
Frequency	<ul style="list-style-type: none"> ● As required when revised or adopted: review incentive programs ● When new products or services are proposed ● At least annually: review current products and services to review for potential conflicts of interest
Action	<ul style="list-style-type: none"> ● Identify potential conflicts of interest using a risk-based approach ● Review products and services for potential conflicts regarding compensation including, but not limited to: <ul style="list-style-type: none"> ○ Proprietary products/services ○ Third-party products/services where Coastal Equities, Inc. receives payment from the third party ○ Non-cash compensation where RRs are provided incentives to sell a product or service ○ Differential or variable compensation, incentives tied to appraisals or performance reviews ○ Compensation practices for new or existing RRs ○ Generally: overarching firm-wide conflicts; associated person related conflicts; material limitations ● Document conflicts reviews including whether to mitigate, disclose and/or eliminate ● Develop written disclosures for providing to customers ● Mitigation consideration for compensation issues include the following: <ul style="list-style-type: none"> ○ avoiding compensation thresholds that disproportionately minimize compensation incentives for employees to favor one type of account over another, or to favor one type of product over another, proprietary or

	<p>preferred provider products, or comparable products sold on a principal basis, for example, by establishing differential compensation based on neutral factors</p> <ul style="list-style-type: none"> ○ eliminating compensation incentives within comparable product lines ○ implementing supervisory procedures to monitor recommendations that are near a compensation threshold for firm recognition; involve higher compensating products, proprietary products or transactions in a principal capacity; or involve the rollover or transfer of assets from one type of account to another ○ adjusting compensation for RRs who fail to adequately manage conflicts of interest ○ limiting the types of retail customer to whom a product, transaction or strategy may be recommended ○ eliminating sales contests, sales quotas, bonuses, and non-cash compensation based on the sales of specific securities or specific types of securities within a limited period of time ○ modifying or eliminating certain compensation practices <ul style="list-style-type: none"> ● Include conflict reviews in annual audits/reviews
Record	<ul style="list-style-type: none"> ● Conflicts reviews and mitigation/disclosures ● New product and service reviews ● Records of training including when, who attended, and subjects

A conflict of interest is an interest that might incline a BD or an RR - consciously or unconsciously - to make a recommendation that is not disinterested. Conflicts may exist between the BD and the retail customer; between the RR and the retail customer; and between the BD and the RR. Additional conflicts may exist between customers (e.g., IPO allocations or proprietary research or advice among different types of customers).

Coastal Equities, Inc. has an obligation to avoid or mitigate conflicts of interest where possible and provide disclosure where conflicts may exist.

Coastal Equities, Inc. will identify conflicts and, where appropriate, identify material limitations placed on the investment product or strategy and any conflicts associated with such limitations (e.g., limited product menu, proprietary products only, etc.) and make necessary disclosures.

Incentive programs (whether provided by Coastal Equities, Inc. or a third party) such as sales contests, sales quotas, bonuses, non-cash compensation, etc., within a limited period of time are prohibited if they are based on:

- a specific product; or
- types of securities.

RAs have an obligation to avoid conflicts of interest when dealing with retail customers; some examples are listed below.

1. Recommending proprietary products because they result in higher compensation without considering the customer's needs and alternative investments.
2. Recommending other products or services based on compensation/incentives from Coastal Equities, Inc. or third parties.

25.2.4 Compliance

Responsibility	<ul style="list-style-type: none"> • Compliance • Conflicts and Risk Management Committee
Resources	<ul style="list-style-type: none"> • Sources of revenue • Training program
Frequency	<ul style="list-style-type: none"> • Annual: review conflicts of interest, compliance with Reg BI • Annual or as required: training
Action	<ul style="list-style-type: none"> • Conduct reviews of new product reviews, new types of accounts/services to confirm conflicts of interest have been identified and necessary actions taken (eliminate, mitigate, disclosure) and identify types of accounts and customers suitable for the investment or product • Confirm policies and procedures comply with Regulation BI as part of on-going review of procedures • Take corrective action which may include new disclosures, contact with RR and/or RR's supervisor, contact with customer, <i>etc.</i> • Confirm Form CRS and Reg BI Disclosure document is current and accurate and provided to customers and posted on Coastal Equities, Inc.'s website
Record	<ul style="list-style-type: none"> • Record of policy/procedure reviews and action taken, if any • Records of training including when, who attended, subjects

Coastal Equities, Inc. conducts ongoing and annual reviews and training to achieve compliance with Regulation BI. It is the responsibility of RRs to be familiar with these requirements and act in the customer's best interest at all times. Questions should be referred to Compliance.

25.3 Form CRS

[SEC Form CRS instructions: <https://www.sec.gov/rules/final/2019/34-86032-appendix-b.pdf>; SEC FAQs on Form CRS: <https://www.sec.gov/info/smallbus/secg/form-crs-relationship-summary>; SEC Form CRS Relationship Summary Small Entity Compliance Guide: <https://www.sec.gov/info/smallbus/secg/form-crs-relationship-summary>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor - Delivery • Compliance - Content of Form CRS and material updates • Operations - Delivery
Resources	<ul style="list-style-type: none"> • Delivery records • Information about securities and types of accounts and services offered by the firm • New product and services reviews

Frequency	<ul style="list-style-type: none"> • When recommendations are made (as defined in this chapter) • Update and file with CRD as required
Action	<ul style="list-style-type: none"> • Provide Form CRS to retail customers when a recommendation is made and within 60 days of a material change to the Form • Post Form CRS to Coastal Equities, Inc.'s website and update as necessary • File Form CRS with the CRD and update within 30 days when required • Include Form CRS in reviews/audits to confirm the form is being kept up to date; posted to the website; filed with the CRD; and sent to customers when there are material changes
Record	<ul style="list-style-type: none"> • Website postings • Providing Form CRS to customers including when delivered; version provided; consent to e-delivery if delivered electronically • Records of updates, changes provided to customers, updates to website • CRD filings • Records of reviews/audits

Form CRS is a relationship summary intended to clarify the relationship between the BD and the customer. Firms without retail customers (as defined under Regulation BI) are not required to provide the form to customers or submit it to regulators. The form is required upon the first event that triggers the requirement.

Form CRS must be provided before or at the earliest of (i) a recommendation of an account type, a securities transaction, or an investment strategy involving securities; (ii) placing an order for the retail investor; or (iii) the opening of a brokerage account for the retail investor including, for example, when:

- An order is placed for the retail customer
- A new account is opened for a new customer
- A new account is opened for an existing customer
- A securities transaction or investment strategy is recommended
- A rollover is recommended from a retirement account into a new or existing account or investment
- An RR recommends or provides a new advisory service or product that does not necessarily involve opening a new account or would not be held in an existing account, for example, the first-time purchase of a direct-sold mutual fund or insurance product that is a security through a "check and application" process, *i.e.*, not held directly within an account
- A retail investor requests a copy (provide within 30 days)

Updates will be made and filed with the CRD within 30 days of material changes. Updated summaries will be provided to customers within 60 days after material updates with changes highlighted. Updates may be provided electronically to customers who have consented to electronic delivery.

25.4 Training

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • In-house training materials

	<ul style="list-style-type: none"> • Outside vendors or materials
Frequency	<ul style="list-style-type: none"> • As appropriate in the discretion of Compliance
Action	<ul style="list-style-type: none"> • Provide training on acting in a customer's best interest, Coastal Equities, Inc.'s culture, the Code of Conduct, and conflicts of interest in their mitigation and management
Record	<ul style="list-style-type: none"> • Record of subjects included in training, who attended, and when administered

RRs will receive training on "best interest" requirements and communicating Firm culture, specific requirements of Coastal Equities, Inc.'s code of conduct and its conflicts management framework.

25.5 Monitoring Accounts

Coastal Equities, Inc. does not offer account monitoring services.

25.6 Dual Registrants

Dual registrants and affiliates (as defined at the end of this chapter) are required to provide a Form CRS for both the broker-dealer and advisory relationships; the forms may be combined. Broker-dealers have an obligation to file Form CRS with FINRA's CRD and advisers are required to file with IARD.

If two separate relationship summaries are provided, they will reference and facilitate access to the other with equal prominence and at the same time, without regard to whether the particular retail investor qualifies for those retail services or accounts.

25.7 Recordkeeping

[Exchange Act Rule 17a-3(a)(35); SEC Use of Electronic Media: <https://www.govinfo.gov/content/pkg/FR-1996-05-15/pdf/96-12176.pdf>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Provision of Form CRS to prospects, customers
Frequency	<ul style="list-style-type: none"> • As required under Form CRS requirements, obtaining consent
Action	<ul style="list-style-type: none"> • Obtain recipient's informed consent for electronic delivery • Track delivery of Form CRS which may include electronic return-receipt or by confirmation that information was accessed, downloaded, or printed and/or disseminating information through facsimile methods • Review branch delivery log of Form CRS (for paper delivery) as needed before opening an account for a new customer
Record	<ul style="list-style-type: none"> • Branch delivery log

	<ul style="list-style-type: none"> • Tracking records of delivery • Records of Form CRS and updates to the form • Record of filing with FINRA CRD • Record of audits/reviews of providing Form CRS
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Records of all information collected from and provided to the retail customer are maintained in accordance with recordkeeping rules. Records are not required to evidence best interest determinations on a recommendation-by-recommendation basis. Coastal Equities, Inc. also is not required to provide information regarding the basis for each particular recommendation. Records of Form CRS will be retained for six years after the earlier of the date that the account was closed or the date on which the information was collected, provided, replaced or updated.

25.8 Definitions

Affiliate: Any persons directly or indirectly controlling or controlled by Coastal Equities, Inc. or under common control with Coastal Equities, Inc..

Best interest: The term "best interest" is explained through SEC guidance and interpretations and is not expressly defined. Whether a broker-dealer has acted in the retail customer's best interest in compliance with Regulation BI will turn on an objective assessment of the facts and circumstances of how the specific components of Regulation BI - including its Disclosure, Care, Conflict of Interest, and Compliance Obligations - are satisfied at the time that the recommendation is made (and not in hindsight).

Conflict of interest: A conflict of interest is an interest that might incline a BD or RR, consciously or unconsciously, to make a recommendation that is not disinterested.

Dually licensed financial professional: A natural person who is both an associated person of a broker-dealer registered under section 15 of the Exchange Act, as defined in section 3(a)(18) of the Exchange Act, and a supervised person of an investment adviser registered under section 203 of the Advisers Act, as defined in section 202(a)(25) of the Advisers Act.

Dual registrant: A firm that is dually registered as a broker-dealer under section 15 of the Exchange Act and an investment adviser under section 203 of the Advisers Act and offers services to retail investors as both a broker-dealer and an investment adviser. There are exceptions; for example, if a BD dually registered offers investment advisory services to retail investors, but offers brokerage services only to institutional investors, the BD is not a dual registrant for purposes of Form CRS.

Full and fair: Sufficient information to enable a retail customer to make an informed decision with regard to a recommendation.

Implicit or explicit recommendations: For accounts where there is agreed-upon account monitoring, if the BD makes no recommendation in a periodic review, it is an implicit "hold" recommendation subject to Regulation BI just as would an explicit "hold" recommendation. Absent an agreement to monitor an account, Regulation BI does not apply to implicit hold recommendations.

Investment Strategy: Interpreted in a manner consistent with current BD regulation under federal securities laws and FINRA rules.

Legal Representative: includes the non-professional legal representatives of a natural person, *e.g.*, a non-professional trustee that represents the assets of a natural person. Regulation BI would not apply when the legal

representative is acting in a legal capacity as a regulated financial services industry professional retained to exercise independent professional judgment. Therefore, recommendations to registered IAs and BDs or corporate fiduciaries would not trigger Regulation BI. On the other hand, recommendations to non-professional trustees, executors, conservators and persons holding power of attorney that represent natural persons are covered. The definition does not apply to financial industry professionals.

Material facts (under Regulation BI): Information is material if there is a substantial likelihood that a reasonable shareholder would consider it important.

Monitoring accounts: An agreement between the BD and the customer to provide account monitoring services. Monitoring may be incidental reviews of accounts to make recommendations and does not require IA registration. Through Form CRS firms are required to advise customers if they provide account monitoring services. BDs do not have a duty to provide account monitoring.

Non-cash compensation: Non-cash compensation includes any form of compensation, including but not limited to merchandise, gifts and prizes, travel expenses, meals and lodging.

Personal, family, or household purposes: The phrase "primarily for personal, family or household purposes" covers any recommendation to a natural person for his or her account, other than recommendations to a natural person seeking these services for commercial or business purposes. Regulation BI would not cover, for example, an employee seeking services for an employer or an individual seeking services for a small business or on behalf of another non-natural person entity, such as a charitable trust.

Receives and Uses: The SEC has stated that "use" means when, as a result of the recommendation: (a) the retail customer opens a brokerage account with the BD regardless of whether the BD receives compensation; (b) the retail customer has an existing account with the BD and receives a recommendation from the BD, regardless of whether the BD receives or will receive compensation, directly or indirectly, as a result of the recommendation; or (c) the BD receives or will receive compensation, directly or indirectly, as a result of that recommendation even if that retail customer does not have an account at the firm.

Recommendation: Interpreted in a manner consistent with current BD regulation under federal securities laws and FINRA rules.

Relationship summary: A written disclosure statement (Form CRS) that must be provided to retail investors when a recommendation is made (as defined in Reg BI).

Retail customer: A natural person (regardless of their financial status, including those previously qualifying as "institutional accounts" under FINRA's suitability rule) or the legal representative of such person who: (a) receives a recommendation for any securities transaction or investment strategy from a broker-dealer or associated person (whether or not the recommendation results in a securities transaction); and (b) uses the recommendation primarily for personal, family, or household purposes.

26 SUPERVISORY SYSTEM, PROCEDURES, AND CONTROLS

[SEC Securities Exchange Act of 1934 Section 15(f); FINRA Rule 3110, 3120 and 3130; FINRA web page: <http://www.finra.org/RulesRegulation/IssueCenter/SupervisoryControl/index.htm>; MSRB Rule G-27; NASDAQ Rule 3010]

26.1 Introduction

CEI has established a supervisory system, procedures and controls reasonably designed to comply with regulators' rules.

Supervisory system: The internal system to oversee business includes the designation of supervisors and allocation of responsibilities; assignment of RRs to appropriate supervisors; identification of areas of business and rules that govern those businesses; and development of procedures.

Supervisory procedures: Procedures in this manual (and in other policies or manuals, if referenced in specific chapters) include:

- compliance procedures for RRs and others that explain rule requirements and prohibitions as well as internal policies when conducting sales and other activities; and,
- supervisory procedures that explain how supervisors are to conduct their ongoing responsibilities. Most supervisory procedures are explained in "matrixes" that appear throughout this manual and include the following:

Responsibility	<ul style="list-style-type: none">• Who is the responsible supervisor? <i>Supervisors are sometimes referenced by name, sometimes by title or as "designated supervisor" which is cross-referenced to the "Designation Of Supervisors" table that appears in this manual.</i>
Resources	<ul style="list-style-type: none">• The information / reports / documents that supervisors use to conduct supervision.
Frequency	<ul style="list-style-type: none">• How often are supervisory reviews to be conducted (daily, weekly, etc.)?
Action	<ul style="list-style-type: none">• How supervision is to be conducted (<i>i.e.</i>, review a report, read correspondence, interview RR or customer, etc.).
Record	<ul style="list-style-type: none">• What record is made that supervision was conducted? <i>Generally supervisors are expected to initial and date reports or other records, note any action taken, and retain that information in their files.</i>

Supervisory Controls: Controls refer to testing and evaluation of systems and procedures to measure and maintain their effectiveness. Internal controls typically involve sampling of functions to test effectiveness and identify shortcomings, gaps, or other inefficiencies in supervisory systems and procedures. Internal controls also involve the ongoing reassessment of these functions to determine whether they are serving their intended purpose.

26.2 Responsibility

Responsibility for CEI's supervisory system, policies, and controls includes the following:

- Designated supervisors are responsible for enforcing policies and procedures in their respective business areas.
- The Chief Compliance Officer (CCO) is responsible for establishing and maintaining the supervisory system, policies and procedures other than financial and operations procedures.
- The Financial and Operations Principal (FINOP) is responsible for establishing and maintaining systems, policies and controls regarding financial and accounting procedures and reporting.

26.3 Controls

26.3.1 Verification and Testing

CEI periodically conducts reviews to test and verify its supervisory system and controls. CEI conducts its own reviews and also enlists an outside vendor to conduct annual testing and reporting.

Testing and verification generally include:

- Identifying areas to be reviewed at least annually
- Retention of an outside auditing company and definition of scope of review annually
- Developing reviews and a schedule for conducting the reviews
- Assigning responsibility for conducting reviews
- Preparing reports of reviews
- Providing reports to management and other appropriate personnel for potential corrective action
- Following up regarding deficiencies in subsequent reviews

Records of testing are maintained by Compliance.

26.3.2 Risk Management

[FINRA Notice to Members 99-92]

CEI has established risk management procedures which are outlined in the chapter *FINANCIAL AND OPERATIONS PROCEDURES*, in the section *Risk Management*.

26.3.3 Outside Auditors

CEI's outside auditors conduct an annual review of internal financial and operational controls as well as compliance with selected rules and regulations. The FINOP (and other personnel, as required) is responsible for working with the outside auditors and providing them with requested information. The auditors' report is provided to senior management and CEI's audit committee (if an audit committee has been established) who are responsible for delegating responsibility for taking corrective action on exceptions noted in the report.

The FINOP retains records of outside audits and reports.

26.4 Written Compliance and Supervisory Procedures

[SEC Securities Exchange Act of 1934 Rule 17a-4(e)(7); FINRA Rule 3110(b)(7) and 3110.11]

Compliance is responsible for maintaining and updating CEI's compliance and supervisory procedures which are included in this manual.

This manual is updated and policies distributed as follows:

- New and amended rules and releases from regulators are reviewed on an ongoing basis and changes considered for written procedures and incorporated where necessary. Changes are considered at least annually.
- Changes are incorporated in written procedures
- Prior versions of the manual are archived for books and records purposes.
- When policy and procedure changes affect personnel, Compliance will distribute new or revised policies by email, and maintaining the most current version on its advisor portal at www.coastal-one.com
- Compliance provides manuals to newly associated persons and obtains annual attestations of receipt that are maintained in associated person or other compliance files.
- Policies may be made available to associated persons in electronic format.
- Electronic versions are protected to prevent changes by unauthorized persons by compliance archiving versions of the manuals in Share File. As an additional backup, prior versions delivered via email are archived in Smarsh for at least three years.

26.10 Supervisory Quarterly Reports

Responsibility	<ul style="list-style-type: none"> • Supervisors
Resources	<ul style="list-style-type: none"> • Order Records • Daily Transaction Report • Customer Monthly Statements • Communications • Reg T records including margin calls, prepayment requests, <i>etc.</i> • Other various records reviewed by the Supervisor
Frequency	<ul style="list-style-type: none"> • Quarterly
Action	<ul style="list-style-type: none"> • Complete the checklist and forward to Chief Supervision Officer
Record	<ul style="list-style-type: none"> • CSO to retain at least three years' Checklists

Supervisors will complete a quarterly checklist to be submitted to the CSO by the 15th of the month following the month reported. The checklist summarizes many of the reviews conducted by the supervisor over the quarter.

26.5 Chief Compliance Officer (CCO)

[FINRA Rule 3130(a)]

CEI has designated a CCO who is listed on the *Designation of Supervisors* chart and Schedule A of Form BD which is filed with regulators.

26.6 Internal Inspections

[FINRA Rule 3110(c)]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Records, reports, policies and procedures
Frequency	<ul style="list-style-type: none"> • Annual (or more frequently for certain high-risk areas)
Action	<ul style="list-style-type: none"> • Identify business areas subject to review • Prepare schedule of inspections considering the risk profile of each business area • Assign inspection responsibility considering any potential conflicts of interest including economic, commercial, or financial interests in the associated persons or business being inspected and ensuring the person assigned does not work in the business unit and is not directly or indirectly supervised by, or otherwise reporting to, an associated person assigned to the unit or location. Where compliance is not possible due to CEI's size or business model, document in the report both the factors used to make this determination and how the inspection otherwise complies with the requirements of Rule 3110(c)(1) • Prepare draft report of review and provide to appropriate supervisory personnel for comment • Prepare final report and send to supervisor of the business area and senior management • Obtain response regarding corrective action from the supervisor • Follow up regarding deficiencies (at the latest at the next inspection)
Record	<ul style="list-style-type: none"> • Records of internal inspections including when conducted, who conducted them, and reports and responses

CEI reviews, at least annually on a calendar-year basis, the businesses in which it engages to identify potential non-compliance with Firm policies and procedures and regulatory rules, laws, and regulations.

Reviews may be conducted through a number of resources including (but not necessarily limited to):

- Compliance
- Clearing firm (for those areas that are the clearing firm's responsibility)
- Internal audit
- Outside auditors
- Outside consultants
- Risk management

Reviews conducted internally may use different approaches:

- Review of a specific period of time
- Review based on a sampling of the activity
- Other reviews appropriate to the area of business

OSJ and branch office inspections are described in the chapter *OFFICES* in the section *Office Inspections*.

26.7 Review and Testing of Procedures and Controls

[FINRA Rule 3120(a)]

Responsibility	<ul style="list-style-type: none">• Compliance
Resources	<ul style="list-style-type: none">• Records, reports, policies and procedures
Frequency	<ul style="list-style-type: none">• Annual
Action	<ul style="list-style-type: none">• Test procedures/controls• Identify gaps in procedures and document• Revise procedures where necessary
Record	<ul style="list-style-type: none">• Documentation of reviews and testing• Revised policies and procedures, as appropriate

CEI conducts reviews of its supervisory procedures and controls at least annually to confirm procedures are current and include all areas of business. Procedures and controls are also tested to determine they achieve the necessary levels of compliance. Findings from internal inspections are also considered in this review.

Reviews and testing may be conducted through a number of resources including (but not necessarily limited to):

- Compliance
- Outside auditors

26.7.1 Conducting Risk-Based Reviews and Testing

Reviews and testing will be documented on the *Supervisory Policies, Procedures, And Controls Review & Testing* form or through similar types of reports or forms. This includes identifying who is conducting the review/testing and assigning risk levels to different areas of business. Areas of higher risk will be subject to more frequent and/or more extensive reviews which may include look-backs, larger samples and/or longer time periods for review, certifications by supervisors, or other reviews determined by the reviewer(s).

26.7.2 Findings and Follow-Up

Findings from reviews and testing are included in the CEO report and annual certification discussed in the next section. Compliance is responsible for:

- Amending policies and procedures to address gaps
- Reporting deficiencies (found in testing) to supervisors of appropriate business areas
- Follow up to determine deficiencies have been addressed
- Assembling findings for inclusion with the CEO report and annual certification (next section)

26.8 Internal Investigations of Transactions

[FINRA Rule 3110(d)]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Orders identified as requiring further review regarding potential insider trading including proprietary and employee trading (see <i>Review Of Transactions</i> in the chapter <i>GENERAL EMPLOYEE POLICIES</i> and the chapter <i>INSIDER TRADING</i>)
Frequency	<ul style="list-style-type: none"> • Ongoing: review of transactions
Action	<ul style="list-style-type: none"> • Review transactions for potentially violative trades • Investigate trades as needed: <ul style="list-style-type: none"> ○ Refer investigation to outside counsel or others, if appropriate • Determine whether corrective action should be taken which may include: <ul style="list-style-type: none"> ○ Cancellation of transactions ○ Education of personnel ○ Disciplinary action depending on the nature of the violation • Within 5 business days of completing an internal investigation where it is determined a violation has occurred, file written report with FINRA
Record	<ul style="list-style-type: none"> • Records of internal investigations and action taken

CEI reviews securities transactions to identify trades that may violate provisions of the Exchange Act and its rules, rules of exchanges, or FINRA rules prohibiting insider trading and manipulative and deceptive devices. The accounts subject to these reviews include:

- accounts of CEI, if any;
- accounts introduced or carried by CEI in which a person associated with the firm has a beneficial interest or the authority to make investment decisions;
- outside accounts of a person associated with CEI (see *Outside Accounts* in the chapter *GENERAL EMPLOYEE POLICIES*); and
- covered accounts (see definition below).

"Covered accounts" include any account introduced or carried by CEI that is held by:

- the spouse of a person associated with the member;
- a child of the person associated with the member or such person's spouse, provided that the child resides in the same household as or is financially dependent upon the person associated with the member;
- any other related individual over whose account the person associated with the member has control; or
- any other individual over whose account the associated person of the member has control and to whose financial support such person materially contributes.

For questioned trades, a prompt internal investigation will be conducted to determine whether a violation of laws or rules has occurred.

26.8.1 Internal Investigation Reports

CEI is engaged in investment banking services as defined in FINRA Rule 3110(d)(4)(B) and is required to file with FINRA reports of internal investigations.

CEI uses a risk-based approach to monitoring transactions in all of its customer accounts by supervisory review of excepted (flagged) transactions identified by CEI's clearing firm's computer platform, Smart Station. Outside accounts are reviewed manually by reviewing a sampling of duplicate statements and confirmations of covered accounts and evidencing review of same by notation of the reviewer's initials and date.

If a supervisor detects a flagged exception or other suspicious activity on an outside account, the supervisor shall make inquiry into the facts and circumstances of the trade which may include, but is not limited to, review of the account and household accounts, contact with the registered representative, and/or contact with the customer. The supervisor must evidence the review through Smart Station, or by written memorandum, the original of which to be maintained in the supervisor's file and scanned and emailed to compliance@coastal-one.com for archiving.

If the supervisor is satisfied that there is no violation pursuant to his/her review, the transaction may be cleared through Smart Station, or otherwise evidenced by written memorandum to the supervisor's file and copied electronically to compliance. Otherwise, the supervisor must escalate the review by reporting the suspicious transaction to compliance and, if not evidenced through Smart Station, forwarding his memorandum of review to compliance.

Compliance will evaluate the transaction and make its own determination as to whether the trade requires a formal internal investigation. Should Compliance determine no investigation is required, it will memorialize the determination by e-mail to the supervisor with its rationale and will instruct the supervisor that he or she may clear the transaction or suggest other action deemed reasonable.

Should Compliance determine that a formal internal investigation is required, the firm will conduct additional inquiry as required of the associated person(s) involved, the customer(s), and all account information available to it. If necessary, the firm may retain outside counsel to conduct additional investigation. After investigation, the firm will report its findings to the associated person(s) responsible for the transaction in question in order to permit the associated person to respond in writing to the firm's findings. The firm will then determine what action, if any, it will take including disciplinary action and reporting requirements to applicable SROs and other agencies.

Compliance is responsible for reporting all internal investigations under Rule 3110(d) on a quarterly basis. The firm must report the commencement date of each internal investigation, the status of each open internal investigation, the resolution of any internal investigation reached during the previous calendar quarter, and, with respect to each internal investigation, the identity of the security, trades, accounts, firm's associated persons or family members of such associated person holding a covered account under review, and a copy of the firm's insider trading review policies and procedures. If the firm did not have an open internal investigation, or either initiate or complete an internal investigation during a particular calendar quarter, the firm is not required to submit a report for that quarter.

If the firm determines after an internal investigation that a trade has violated provisions of the Exchange Act, its regulations or FINRA rules prohibiting insider trading and manipulative and deceptive devices, the firm must, within five business days of the internal investigation's completion, file a written report with FINRA. The report must detail the completion of the investigation, including the results of the investigation, any internal disciplinary action taken, and any referral of the matter to FINRA, another SRO, the SEC or any other federal, state or international regulatory authority.

26.9 Annual Report and Certification of Compliance and Supervisory Processes

[FINRA Rule 3120 and 3130]

Compliance prepares an annual compliance report for the CEO (or equivalent officer).

26.9.1 Meetings Between CEO and CCO

The CEO meets once or more annually with the CCO to review compliance matters the subject of the annual certification.

26.9.2 Annual Report to CEO

The CCO will prepare and provide the CEO (or equivalent officer) with an annual report that includes a review of CEI's supervisory system and procedures and key compliance issues. The report will also include a summary of testing results including significant identified exceptions and any amended supervisory procedures adopted in response to the test results. The CCO will meet with the CEO to discuss and review the report and will meet at other times, as needed, to discuss other compliance matters. If CEI has designated multiple CCOs, each CCO will meet with and prepare a report for the CEO annually.

The annual report will be provided to members of the board of directors (or equivalent senior management) and the audit committee, if one has been established. The report will be provided to these governing bodies at the earlier of their next scheduled meetings or within 45 days after execution of the certification.

26.9.2.1 Firms with Annual Gross Revenue Of \$200 Million Or More

[FINRA Rule 3120(b)]

If CEI has reported \$200 million or more in gross revenue in the previous calendar year, the report to the CEO must include the following, to the extent applicable to CEI's business. Compliance is responsible for confirming whether this requirement applies.

- (1) a tabulation of the reports pertaining to customer complaints and internal investigations made to FINRA during the preceding year; and
- (2) discussion of the preceding year's compliance efforts, including procedures and educational programs, in each of the following areas:
 - trading and market activities;
 - investment banking activities;
 - antifraud and sales practices;
 - finance and operations;
 - supervision; and
 - anti-money laundering.

For purposes of this requirement, "gross revenue" means:

- (1) total revenue as reported on FOCUS Form Part II or IIA (line item 4030) less commodities revenue (line item 3990), if applicable; or
- (2) total revenue as reported on FOCUS Form Part II CSE (line item 4030) less, if applicable, (A) commissions on commodity transactions (line item 3991); and (B) commodities gains or losses (line items 3924 and 3904).

26.9.2.2 Certification

Annually (after receipt and review of the report), the Chief Executive Officer (or equivalent) will certify that CEI has in place processes to establish, maintain, review, test, and modify written compliance policies and written supervisory procedures reasonably designed to comply with regulators' rules. Certification does not, by itself, establish line supervisory responsibility for those involved in the certification process. If CEI has co-CEOs, each CEO will certify as if he/she were acting as sole CEO.

26.10 Supervision of Supervisors

[FINRA Rule 3110(b)(6)(c) and 3110.10]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Designation of supervisors
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Identify and designate supervision of supervisors and include in the "<i>Designation Of Supervisors</i>" chart, confirming supervision complies with the requirements of this section ensuring supervisors do not report to someone they supervise or have compensation determined by such a person • Identify producing managers and establish supervision of accounts and account transactions • Where compliance with these requirements is not possible because of the size of CEI or a supervisor's position in CEI, document the factors used in making such a determination and how an alternative arrangement complies with the requirements • Ensure designated supervisors are aware of the designation and their responsibilities • Include review of supervision in inspections of offices
Record	<ul style="list-style-type: none"> • Designation of supervisors confirmation such designations do not conflict with requirements to exclude supervision by those reporting to the supervisor or who determines the supervisor's compensation • Documentation of exceptions • Reviews of producing managers' accounts and transactions maintained by the designated supervisor • Review of supervision as part of inspection reports

Supervisors are subject to supervision of their activities by other designated supervisors. Supervisors are not permitted to:

- supervise their own activities; and
- report to, or have their compensation or continued employment determined by, a person or persons they are supervising.

Where it is not feasible to comply with these requirements, CEI's records will be documented justifying the exception and how supervisory requirements will be met. Rule exceptions include instances where:

- CEI is a sole proprietor in a single-person firm;
- a registered person is CEI's most senior executive officer (or similar position); or
- a registered person is one of several of CEI's most senior executive officers (or similar positions).

26.10.1 Supervision of Producing Managers' Customer Account Activity

Responsibility	<ul style="list-style-type: none"> • Compliance • Designated supervisor of producing manager
Resources	<ul style="list-style-type: none"> • Various for supervision of producing managers (listed in supervisory matrixes in appropriate chapters, by subject)
Frequency	<ul style="list-style-type: none"> • Compliance: Ongoing - maintain designations of producing manager supervisors • Designated supervisor of producing manager: Various for ongoing reviews depending on type
Action	<ul style="list-style-type: none"> • Compliance: <ul style="list-style-type: none"> ○ Identify producing managers ○ Identify supervisors ensuring independence (does not report to producing manager, determine manager's compensation or have his/her compensation determined by the supervisor with particular review if the proposed supervisor is located in the same physical office as the producing manager) ○ Identify reviews to be conducted ○ Identify producing managers subject to heightened supervision and notify designated supervisor • Designated supervisor: conduct reviews of producing manager customer account activity
Record	<ul style="list-style-type: none"> • Compliance records of producing managers and who supervises them • Designated supervisor: records of reviews conducted

Day-to-day customer account activity conducted by office managers, sales managers, regional or district managers or anyone performing similar supervisory functions ("producing managers") is subject to review and supervision by someone senior to or independent of the producing manager. Any level of customer account activity qualifies for designation as a producing manager, including only handling family accounts.

26.10.1.1 Designation of Supervisors

Compliance is responsible for identifying producing managers subject to these supervisory procedures and designating supervisors to oversee their customer activity. Supervisors must be senior to or "otherwise independent" of the producing manager.

A person "senior to" the producing manager is understood to be someone who does not report to the producing manager; whose compensation is not determined in whole or part by the producing manager supervised; who is not in the same chain of authority; and who has the authority to oversee, direct, and correct the activities of the producing manager and take necessary remedial actions, including termination, if and when necessary.

"Otherwise independent" means a person who does not report either directly or indirectly to the producing manager under review; who is situated in an office other than the office of the producing manager; and must not otherwise have supervisory responsibility over the activity being reviewed (including not being directly compensated based in whole or part on the revenues accruing for those activities).

26.10.1.2 Reviews to Be Conducted

The reviews to be conducted by the producing manager's supervisor are determined by Compliance depending on the nature of the customer account activity. Supervision will be substantially comparable to areas supervised for other RRs engaged in similar customer account activity. Those reviews are described throughout this manual.

26.11 Conflicts of Interest

[FINRA Report on Conflicts of Interest October 2013]

CEI has an obligation to mitigate potential conflicts of interest and put the customer's interest before its own. Potential conflicts are addressed in the following sections which also address supervision of these potential conflicts.

1. CEI's Code of Ethics addresses the following issues:
 - Confidentiality of CEI's business, its associated persons, customers, suppliers or consumers
 - Actions constituting acting in self-interest
 - Gifts and entertainment
 - Bequests
 - Privacy of customer information and requests for information from affiliates
 - Holding outside offices or appointments
 - Internal accounting controls
 - Reporting ethics violations and disciplinary action
 - Trading in the stock of Firm customers, suppliers, or vendors
 - Full and fair disclosure regarding documents filed on behalf of CEI
 - Associated person compliance with Firm policies and rule requirements, obligations to report
 - Contacts regarding ethics issues
 - Supervision vested in supervisors
 - Administration of the Code of Ethics
2. Insider trading (*see the chapter INSIDER TRADING*)
3. Policies regarding associated person outside business activities, outside accounts (*see the chapter GENERAL EMPLOYEE POLICIES*)
4. Customer privacy policies and procedures (*see the chapter COMMUNICATIONS WITH THE PUBLIC*)
5. Identity theft (*see the chapter ACCOUNTS*)

26.12 Cross Reference to Other Supervisory Control Subjects

The purpose of this section is to identify SRO supervisory control rule subjects that do not appear in the chapter *SUPERVISORY SYSTEM, CONTROLS AND PROCEDURES* and that appear in other chapters of this manual.

Subject	CHAPTER	Section / Subsection(s)
Transmittals of customer funds and securities to:	FINANCIAL AND OPERATIONS PROCEDURES	Transmittals Of Customer Funds And Securities

<ul style="list-style-type: none"> • Third parties • Outside entities (banks, investment companies, etc.) • Post office or c/o addresses • Customer by RRs 		
Customer changes of address	ACCOUNTS	<ul style="list-style-type: none"> • Addresses On Customer Accounts • New Accounts - Post Office Addresses
Customer changes of address	FINANCIAL AND OPERATIONS PROCEDURES	Customer Confirmations And Statements - Change Of Customer Addresses On Accounts
Confirming changes in customer investment objectives ['34 Act Rule 17a-3(17)(i)(A)]	ACCOUNTS	<ul style="list-style-type: none"> • New Accounts - Customer Account Information • Updating Account Information And Periodic Affirmation
Time and price discretion for orders [NASD Rule 2510]	ORDERS	Time And Price Discretion
Account designation changes on orders [FINRA Rule 4515]	ORDERS	Account Designation And Cancels/Rebills
Holding customer mail	FINANCIAL AND OPERATIONS PROCEDURES	Customer Confirmations And Statements - Hold Mail Instructions
Office inspections	OFFICES	Office Inspections

26.7 Special Supervision/Heightened Supervision

[FINRA Regulatory Notice 18-15]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Form U4 information • CRD • Customer complaints • Regulatory actions • Other activity that may warrant special supervision, at the discretion of Compliance

Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Compliance: <ul style="list-style-type: none"> ○ Identify associated persons subject to special supervision ○ Determine the scope of special supervision ○ Notify the associated person's supervisor of required supervision ○ Collect certifications from supervisor • Designated supervisor: <ul style="list-style-type: none"> ○ Conduct required special supervision ○ Prepare and send certifications to Compliance
Record	<ul style="list-style-type: none"> • Reviews of associated persons for potential special supervision are retained in a "Heightened Supervision" file in Compliance • Memos and certifications pertaining to a specific associated person are retained in Compliance's file for the associated person

26.7.1 Introduction

CEI will institute special supervision for RRs or other associated persons when appropriate. The following sections describe CEI's procedures for identifying those subject to special supervision and the types of supervision that may be conducted. Reference to "employees" also includes independent contractors affiliated with CEI.

States and other regulatory bodies may require RRs to comply with a program of Heightened Supervision as a condition of licensing. If CEI agrees to maintain the RR it will comply with the terms of the Heightened Supervision program by requiring the RR's assigned supervisor to supervise the program.

26.7.2 Identifying Employees for Special Supervision

It is the responsibility of Compliance to identify associated persons for potential special supervision. Associated persons will be identified at the time of hire or when an associated person becomes subject to regulatory action and/or a pattern of customer complaints. Unregistered individuals who were previously registered and the subject of customer or regulatory complaints are also subject to consideration for special supervision.

26.7.3 Criteria for Identifying Candidates for Special Supervision

The following are criteria that will trigger a review by Compliance to determine whether an associated person should be subject to special supervision. Pending as well as resolved matters will be considered. The criteria are subjective and the details of complaints and/or regulatory actions must be considered in determining whether special supervision is necessary.

- Three or more customer complaints alleging sales practice abuse within the past two years (complaints include written complaints, arbitrations, other civil actions)
- Complaint filed by a regulator
- Injunction in connection with an investment-related activity
- Termination for cause or permitted to resign from a former employer where the termination appears to involve a significant sales practice or regulatory violation
- Employment with three or more broker-dealers in the past five years

- Direct or indirect outside business activities associated with microcap and OTC companies (see the section *Low-Priced And Microcap Securities* in the chapter *ORDERS*)
- Traders involved in trading microcap and low-priced OTC securities (determined by Trading Supervisor)

26.7.4 Special Supervision Memorandum

When a candidate is identified for possible special supervision Compliance, in consultation with the RR's supervisor, will consider whether special supervision will be established. After the determination is made, Compliance will prepare a memorandum outlining action taken (or not taken).

Where it is determined that CEI's existing supervision is adequate to address oversight of the candidate, Compliance will document in the memorandum the reasons why existing supervision is adequate. Where it is decided special supervision will be conducted, Compliance will outline the supervision to be conducted (including type, frequency, time period of special supervision, and how supervision should be documented) and provide copies of the memorandum to the subject RR and the RR's supervisor outlining the terms of the special supervision.

26.7.5 Scope of Potential Special Supervision

Heightened supervision will be established after considering the specifics that apply to the RR. Heightened supervision may take many forms and may include some of the following, to be determined by Compliance. This list does not limit or prescribe how special supervision should be structured for any one RR, since each case must be reviewed individually.

- Limits on type of business (option, futures, *etc.*)
- Limits on types of accounts (discretionary, certain age groups or other demographics, *etc.*)
- Verification with customers of new account information when accounts are opened
- Pre-approval of some or all trades entered
- Pre-approval of certain types of accounts
- Contact with customers by the RR's designated supervisor
- Pre-approval of all written public communications originated by the RR
- Extra training or continuing education in areas subject to special supervision
- Assignment of the RR to a "mentor" or partner

26.7.6 Certification by RR's Supervisor

During the term of special or heightened supervision, the RR's supervisor will certify to Compliance, in writing, that the special or heightened supervision has been conducted. The form and frequency of certification will be determined by Compliance and will be explained in the Special Supervision Memorandum provided to the supervisor, or in writing with delivery of the heightened supervision program to the RR's supervisor.

27 FINANCIAL AND OPERATIONS PROCEDURES

This chapter provides key policies and procedures affecting the financial and operations areas of CEI. Detailed operations procedures are included in CEI's (or a clearing firm's) operations procedures manuals.

CEI has designated a Financial and Operations Principal who is responsible for general oversight of financial and operations areas of CEI. Supervisors of specific financial or operations areas are responsible for day-to-day procedures.

27.1 Qualification of Operations Personnel

[FINRA Rule 1230(b)(6)(A) and 1250; FINRA Regulatory Notice 11-33]

Certain operations personnel are considered "covered persons" under FINRA Rule 1230 because of their responsibilities for "covered functions" as defined in the Rule. These personnel are required to qualify as "Operations Professionals" by completing the Series 99 qualification examination or by qualifying for an exception because of the person's other registration qualifications. In general the requirements apply to senior management responsible for covered functions; persons designated by senior management to supervise, manage, or approve or authorize work relating to the covered functions; and persons with authority or discretion materially to commit CEI's capital relating to covered functions. The Rule should be consulted for definitions of covered persons and covered functions.

In addition, covered persons are required to participate in Regulatory Element and Firm Element continuing education. Refer to the chapter *TRAINING AND EDUCATION* for procedures regarding continuing education.

The Operations designated supervisor is responsible for confirming that covered persons complete the necessary requirements for registration and continuing education and to restrict an associated person's activities if either requirement is not completed within required timeframes.

27.2 Books and Records

[SEC Securities Exchange Act of 1934 Rule 17a-3 and Rule 17a-4; FINRA Rule 4510, 4511 and 4512; FINRA New And Amended Recordkeeping Checklist: <http://www.finra.org/industry/books-and-records>; MSRB Rule G-8 and G-9]

27.2.1 Introduction

SEC Rule 17a-3 identifies the types of books and records to be retained by CEI and 17a-4 identifies the period these records are to be retained. SROs also specify certain record requirements. Designated supervisors are responsible for retaining required records for areas under their supervision. The FINOP is responsible for establishing and maintaining CEI's record retention schedule.

For accounts and other business introduced to a clearing firm, the clearing firm is responsible for retaining certain records as outlined in the clearing agreement.

27.2.2 Electronic Storage of Records

[SEC Securities Exchange Act of 1934 Rule 17a-4(f); FINRA Regulatory Notice 18-31]

Responsibility	<ul style="list-style-type: none">• FINOP
Resources	<ul style="list-style-type: none">• Records required to be retained under SEC and SRO rules

Frequency	<ul style="list-style-type: none"> • Ongoing record keeping, as required by rule • Audit system - ongoing and periodic
Action	<ul style="list-style-type: none"> • Develop internal system or choose a vendor or other third party that meets rule requirements • Contract with an independent third party download partner, if appropriate • Notify DEA when initiating electronic storage and provide third party representation • Provide revised notifications to DEA if necessary • Obtain senior management approval of system configuration to store records and subsequent changes • Issue passwords to authorized personnel and disable passwords for terminated associated persons or those no longer requiring access • Take corrective action internally or with outside vendor if anomalies are detected • Establish audit system for accountability regarding the input of records into the storage system
Record	<ul style="list-style-type: none"> • Contracts with vendors or other third parties • Notification(s) to DEA • Written approval from senior management regarding system configuration • Record of corrective action taken, if necessary, when anomalies are detected • Record of passwords issued and disabled • Audit system and anomalies detected including corrective action taken

CEI utilizes electronic storage media and/or micrographic media for certain records.

CEI continues to utilize paper storage for all other record retention requirements. CEI may utilize electronic storage for the same documents as a matter of firm convenience, for backup, and to expedite operations.

27.2.2.1 Notification to Examining Authority

[SEC Securities Exchange Act of 1934 Rule 17a-4(f)(2)(i)]

CEI has provided the required notification to its designated examining authority (DEA) prior to employing electronic storage media. The independent third party with download access is also required to submit an undertaking indicating it agrees to promptly furnish information to regulators.

27.2.2.2 Conditions

[SEC Securities Exchange Act of 1934 Rule 17a-4(f)(2)(ii)]

As required by rule, CEI's electronic storage media meets the following conditions:

- non-rewritable, non-erasable format
- automatic verification of the quality and accuracy of the process
- serialize original (and duplicate units) and time-date for required retention period
- capacity to readily download indexes and records

27.2.2.3 Ability to Retrieve and Reproduce

[SEC Securities Exchange Act of 1934 Rule 17a-4(f)(3)]

CEI's electronic or micrographic storage will also meet the following requirements:

- facilities for immediate, easily readable production of records
- ability to provide facsimile enlargements
- duplicate copies stored separately from the originals
- organized and indexed accurately
- current information necessary to access records and indexes
- independent third party who has access and the ability to download records

27.2.2.4 Audit System

The third party that provides electronic storage services has an audit system to test, on an ongoing basis, the integrity of the Firm's records retained in electronic storage media. Anomalies reported by the third party will be reviewed by the FINOP or another designated person on the FINOP's behalf to ensure corrective action has been taken and records are retained as required.

27.2.2.5 Confidentiality of Electronic Records

CEI (in conjunction with any vendor) protects against unauthorized access to or use of customer records by use of a password system. Passwords will be changed periodically and disabled for terminated associated persons or associated persons no longer requiring access.

27.2.3 Availability of Records in Offices

Required records under Rules 17a-3 and 17a-4 are available in office locations. The FINOP is responsible for establishing a method for producing required records at office locations upon the request of a regulator. The section *Office Records* in the chapter *OFFICES* discusses this subject in more detail.

27.3 Calculation and Reporting of Net Capital

[SEC Securities Exchange Act of 1934 Rule 15c3-1, Rule 17a-5 and Rule 17a-11; FINRA Rule 4110, 4120, 4130, 4140, 4521 and 4524]

Responsibility	<ul style="list-style-type: none"> • FINOP
Resources	<ul style="list-style-type: none"> • Financial and transaction records
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Maintain ongoing calculation of CEI's net capital • Report net capital as required • Report net capital deficiencies as required, when necessary
Record	<ul style="list-style-type: none"> • Records retained by the FINOP include: <ul style="list-style-type: none"> ○ FOCUS reports ○ Other net capital calculations

The calculation and monitoring of net capital is the responsibility of the FINOP who also is responsible for ensuring the accurate and timely reporting of periodic net capital reports. Some of the FINOP's specific responsibilities include:

- Review and filing of CEI's financial reports and periodic review of accounting records

- Periodic consideration of whether CEI's minimum net capital requirements have changed because of changes in CEI's business
- Supervising additions to, and withdrawals from, the equity capital of CEI
- Reporting borrowings and subordinated loans for capital purposes
- Establishing procedures for retention of required financial books and records

If CEI becomes deficient in its net capital position, the FINOP is responsible for making the necessary reports to regulators and communicating any restrictions in business that may result.

27.4 Reports

Responsibility	<ul style="list-style-type: none"> • FINOP
Resources	<ul style="list-style-type: none"> • Data regarding capital, sending of statements, compliance with protection of customer assets
Frequency	<ul style="list-style-type: none"> • Monthly: Risk reports (if applicable) • Quarterly: Custody Report • Annually: Audit Report; Exemption or Compliance Report (whichever applies)
Action	<ul style="list-style-type: none"> • File required reports
Record	<ul style="list-style-type: none"> • Records of reports and when filed

CEI is obligated to file certain reports with regulators.

27.4.1 Annual Audit Report

[Exchange Act Rule 17a-5(d); FINRA Regulatory Notice 16-05 and 11-46]

The FINOP is responsible for filing of CEI's annual audited financial statements with regulators, not more than 60 days after the date of the statements, including the oath and affirmation page. Filing is made electronically with FINRA and hard copies are filed with the SEC's Washington office and CEI's regional SEC office. The FINOP will retain records of the filings including the filings themselves, names of regulators, and date of filing.

Reports will be as of the same fixed or determinable date each year, unless a change is approved in writing by FINRA. A copy of FINRA's written approval will be sent to CEI's SEC regional office.

27.4.2 Risk Reports

If CEI computes capital charges under 15c3-1e (limitations on the withdrawal of equity capital) it is required to file additional reports with the SEC. Reports are required within 17 business days after the end of each month that is not a quarter and within 17 business days after the end of each quarter. Refer to Rule 17a-5(a)(6) for details of what must be reported.

27.4.3 Custody Report and Requirements

[SEC Securities Exchange Act of 1934 Section 17(b); FINRA web page: <https://www.finra.org/media/document/8365>]

CEI is required to file a quarterly Form Custody report that contains information about whether and how CEI maintains custody of customer assets.

CEI is also required to allow staff of the SEC and SROs to review working papers of CEI's PCAOB-registered independent public accounting firm if requested in writing as part of an examination and allow regulators to discuss the findings of CEI's accounting firm with the accounting firm's representatives. The FINOP is responsible for facilitating regulators' access.

27.4.4 Exemption Report

[SEC Securities Exchange Act of 1934 Rule 17a-5]

CEI will annually file with the SEC the Exemption Report (within 60 calendar days after the fiscal year-end as part of CEI's annual compliance audit).

27.5 Reconciliations and Bank Records

Responsibility	<ul style="list-style-type: none"> • FINOP
Resources	<ul style="list-style-type: none"> • Bank records
Frequency	<ul style="list-style-type: none"> • Monthly
Action	<ul style="list-style-type: none"> • Reconcile bank accounts against CEI's records
Record	<ul style="list-style-type: none"> • Bank statements and other bank records, retained by FINOP

The FINOP is responsible for establishing procedures for the periodic reconciliation of bank statements, clearing and depository accounts, and other accounting and business records. Records of bank accounts and other reconciled accounts will be maintained in accordance with regulatory requirements.

27.6 Designation of Accountant

[SEC Securities Exchange Act of 1934 Rule 17a-5(f)]

The FINOP is responsible for filing notice of the designation of its accountant by December 10 of each year with FINRA, the SEC's principal office, and CEI's SEC regional office. If the agreement with the accountant is continuous providing for successive annual audits, notice is not required annually. The following additional requirements apply:

- An agreement must exist with an independent public accountant by December 1 covering a contractual commitment to conduct CEI's annual audit during the following calendar year.
- If the agreement is for a single audit or if the continuing agreement is terminated or amended, a filing is required by December 10.
- If CEI is exempt from filing an annual audited financial statement, notice must still be filed indicating the date as of which an unaudited report will be prepared.
- Notice must be filed with FINRA and the two SEC offices within 15 days after:
 - CEI notifies the accountant that its services will be terminated;
 - the accountant notifies CEI it will not continue its engagement; or
 - a new accountant has been engaged without notice to or by CEI's current accountant.

The FINOP is responsible for maintaining a record of filing the required notices.

27.7 Guarantees by, or Flow Through Benefits for, Members

[FINRA Rule 4150]

Whenever CEI guarantees, endorses, or assumes, directly or indirectly, the obligations or liabilities of another person (including an entity), a written request will be made to FINRA. Prior written approval from FINRA is required whenever CEI receives flow-through capital benefits in accordance with Appendix C of SEC Rule 15c3-1. The FINOP is responsible for filing necessary requests for such arrangements; responding to subsequent FINRA requests for information; complying with FINRA rule requirements; and maintaining records regarding such arrangements.

The requirements when entering into such an arrangement include the following:

- CEI must have the authority to make available to FINRA the books and records of the other person or entity for inspection in the U.S. The other person's books and records must be kept separately from those of CEI.
- CEI is required to provide FINRA with the person's FOCUS reports simultaneous with their being filed with the person's designated examining authority (DEA), unless the person's DEA is FINRA. If the person is not a registered broker-dealer, CEI will submit financial and operational statements in a format and for time periods required by FINRA.
- Guarantees executed in the normal course of business (trade guarantees, signature guarantees, endorsement of securities and the writing of options) are not subject to these requirements. Guarantees regarding the writing of options are not subject if appropriately recorded in CEI's books and records and reflected in net capital computations.

27.8 General Ledger and Suspense Accounts

[FINRA Rule 4523]

Responsibility	<ul style="list-style-type: none">• FINOP
Resources	<ul style="list-style-type: none">• Ledger and suspense accounts
Frequency	<ul style="list-style-type: none">• Ongoing - oversee entries• Monthly or more frequently - review of accounts
Action	<ul style="list-style-type: none">• Oversee entries• Determine accounts are current and accurate• Review accounts to determine they are accurate and any aged or unresolved are promptly identified for research and possible transfer to suspense account(s)
Record	<ul style="list-style-type: none">• General and suspense accounts• Resolution of aged or unresolved items• Record of reviews including reviewers initials, date reviewed, notes of action taken, if any

The FINOP (or supervisors, if accounts are assigned to multiple persons) is responsible for oversight of general ledger and suspense accounts. Suspense accounts must be clearly identified as such and record money charges or

credits and receipts or deliveries of securities whose ultimate disposition is pending determination. The record must include all information known for each item recorded.

27.9 Financial Reporting

[SEC Securities Exchange Act of 1934 Rule 17a-5 and Rule 17a-11; SEC FAQs regarding financial responsibility rules: <http://www.sec.gov/divisions/marketreg/amendments-to-broker-dealer-financial-responsibility-rule-faq.htm>; FINRA Rule 4520 Series]

The FINOP is responsible for financial reporting and payment of fees and assessments and maintaining records of reporting and payment. Some of the requirements include:

- Filing net capital reports
- Reporting net capital deficiencies
- Reporting notice of books and records deficiencies [17a-11(d)]
- Preparation and filing of unaudited financial statements
- Engaging outside accountants to conduct CEI's annual audit and notifying regulators when there is a change of accountant
- Filing audited financial statements with regulators and providing to customers, as required
- Notifying regulators of any change in CEI's fiscal year
- Payment of assessments and fees to regulators

27.9.1 Preparation of Financial Reports

The FINOP is responsible for preparing and reviewing financial reports. While the FINOP may delegate responsibility for gathering information and preparing the reports, the FINOP is ultimately responsible for reporting accurate information.

Preparation of reports will include the following procedures:

- Gathering information through CEI's records and systems to compile financial information.
- Working with outside auditors, when appropriate.
- Drafting reports.
- Determining the accuracy of calculations and information included in the report.
- Providing information to senior management and others, as appropriate.
- Sending reports to designated regulators.
- Providing information for publication to customers, where required by rule.

The FINOP will maintain files including calculations and other information utilized for preparing financial reports and records of internal, regulatory, and other external distribution of reports, as required.

27.9.2 Notification Rule ("Early Warning Rule")

[SEC Securities Exchange Act of 1934 Rule 17a-11]

The FINOP is responsible for notifying (within 24 hours) the SEC and other securities regulators upon the occurrence of certain events (insolvency, decrease of net capital below required minimum, or CEI's repurchase and securities lending activities exceed 25 times its tentative net capital). As an alternative to notification regarding repurchase and securities lending activities, CEI may report monthly as to its stock loan and repurchase activities to its DEA. The FINOP is responsible for maintaining records of any early warning notifications (or monthly reports).

27.9.3 Compliance with Regulation T

It is the responsibility of the FINOP to establish operating procedures to ensure compliance with Regulation T regarding the settlement of customer transactions.

27.9.4 Customer Margin Balance Report

[FINRA Rule 4521(d)]

If CEI carries customer margin accounts, the FINOP is responsible for filing the Customer Margin Balance Form on a settlement date basis, as of the last business day of the month. For any month where there is no information to submit, a report will be filed indicating such. The report is due as promptly as possible after the last business day of the month, but in no event later than the sixth business day of the following month and is filed through the FINRA Firm Gateway.

The FINOP is responsible for retaining records of filings.

27.10 Fees and Service Charges

[FINRA Rule 2122; NASD Notice to Members 92-11]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor
Resources	<ul style="list-style-type: none">• Schedule of fees and charges• Information regarding changes
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Include notification to new customers when accounts are opened• Arrange for written notification to customers• Update website as needed
Record	<ul style="list-style-type: none">• Notice provided to new customers• Copy of written notification sent to customers including date sent• Records of website changes and information posted

Broker-dealers are obligated to disclose fees and service charges to customers. In general, fees and charges are required to be reasonable and not unfairly discriminatory between customers.

If a fee or commission will be charged to redeem a mutual fund and the fund could be sold through the fund company itself without cost, the customer should be notified that the fund could be redeemed without cost by liquidating directly through the mutual fund.

27.10.1 Notification to Customers

Customers will be notified of fees and changes to fees and service charges as follows:

- At the time an account is opened.

- When there is an increase in fees, at least 30 days prior to the increase to the last known address of every customer whose account is subject to the fees.
- If notification is by a method other than a letter (*i.e.*, statement stuffers, newsletters, *etc.*) notification of a fee increase will be clear and conspicuous and in plain English.
- Where a website is used to communicate or interact with customers, all fees will be posted (and kept current) including changes and the projected date of changes.
- For extensive fee changes, a letter may be sent to customers referring them to a website where complete information may be obtained.

27.11 Fidelity Bonding

[FINRA Rule 4360]

As required, CEI is a member of SIPC and maintains required blanket fidelity bonding coverage based on CEI's net capital requirement. The FINOP is responsible for obtaining and maintaining fidelity bonding as required by rule and verifying the adequacy of coverage and making necessary adjustments on at least an annual basis on the anniversary date of the issuance of the fidelity bond.

27.12 Independent Verification of Assets

[FINRA Rule 4160]

CEI may custody assets (customer or proprietary) at financial institutions that are not members of FINRA. FINRA may request written verification of Firm assets held by that institution. If FINRA notifies CEI that the institution has failed to respond to FINRA, CEI will withdraw its assets promptly and transfer them to another financial institution. This requirement does not apply to:

- proprietary assets that are treated as non-allowable assets under Exchange Act Rule 15c3-1; or
- instances where FINRA determines there is no independent custody or record ownership of assets

The FINOP is responsible for withdrawing affected assets when notified by FINRA. Contracts with non-member financial institutions may include the obligation that the financial institution comply with FINRA requests for verification of assets. The FINOP controls records of custody arrangements and contracts.

27.13 Cash Deposits Not Accepted

CEI does not accept cash or currency from customers. If a customer attempts to deposit cash or currency, the associated person receiving the deposit is responsible for refusing the deposit and advising the customer CEI will only accept checks.

In the event cash is inadvertently accepted, the following steps must be followed:

- Immediately provide the cash to the cashier or other authorized Operations personnel.
- The cashier or Operations is responsible for counting the cash (2 people must be present to verify the amount) and entering the amount into CEI's customer account system for credit to the customer's account.
- Immediately thereafter the cash must be walked to CEI's bank for credit to the account maintained for the benefit of customers or, if no account exists, obtain a cashier's check or money order made payable to CEI (or its clearing firm if applicable) and then deposit or send the check/money order to the bank account for customers the same day.

- The Operations Manager is responsible for filing Form 104 (Currency Transaction Report) with the IRS by the 15th calendar day after receipt for cash in excess of \$10,000 for one person on any one day.
- The designated supervisor of Operations is responsible for retaining a file of forms filed with the IRS.

27.14 Cash Equivalents

CEI also does not accept deposits of cash equivalents such as travelers checks, money orders, or cashier's checks. Customers attempting to deposit cash equivalents should be advised to instead provide a personal check for deposit to their account.

27.15 Risk Management

[FINRA Notice to Members 99-92; SEC Securities Exchange Act of 1934 Rule 17a-3(a)(23), Rule 17h-1T and Rule 17h-2T]

Responsibility	<ul style="list-style-type: none"> • FINOP • Internal Audit • Outside auditors • Designated committees, if appointed: <ul style="list-style-type: none"> ○ Credit committee ○ Risk management committee ○ Audit committee
Resources	<ul style="list-style-type: none"> • Internal reports • Regulatory reports • Financial statements
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Establish risk guidelines including inventory limits, counterparty trading limits, etc. • Review regulatory risks • Evaluate risk exposure of business lines • Report to senior management (and holding company, if appropriate) as required • Take corrective action to reduce risk
Record	<ul style="list-style-type: none"> • Review of internal and regulatory reports • Audit reports (internal and external) • Minutes of committees designated to oversee risk • Corrective action taken

This section generally outlines CEI procedures designed to address "risk management." Because these procedures address various lines of business that operate in a constantly changing market environment, they are not static and should be adapted by the designated supervisor to meet the needs of CEI on an ongoing basis.

27.15.1 Risk Practices Regarding Employment and Associated Persons

CEI has established procedures regarding the hiring of personnel; conduct and review of associated person accounts; granting of authority to act in various capacities on behalf of CEI; and the integrity of CEI's systems and financial reporting.

27.15.1.1 Background Checks

One of CEI's first lines of defense is the hiring of qualified people who do not bring high-risk behavior to their positions. CEI conducts background checks on all applicants for employment with CEI. All offers of employment are considered conditional pending the outcome of the background checks. These background checks include contact with the applicant's prior employers for at least the past three years. Any adverse information is referred to the hiring manager for consideration prior to finalization of employment.

Also refer to the section *Hiring Procedures* in the chapter *EMPLOYMENT, REGISTRATION AND LICENSING* for more information about hiring procedures.

27.15.1.2 Associated Person Accounts

Associated persons are subject to policies governing the conduct of their personal securities accounts. Refer to the section *Employee and Associated Person Related Accounts* in the chapter *GENERAL POLICIES* as well as the chapter on *INSIDER TRADING*.

27.15.1.3 Authority

Associated persons may only act on behalf of CEI within the boundaries of authority granted them by CEI. The following generally outlines the authority of certain associated persons or committees and their respective responsibilities.

27.15.1.3.1 Board of Directors

CEI's Board of Directors meets regularly to take necessary action on behalf of CEI. On at least an annual basis, the Board of Directors will affirm the authority of designated Board committees as well as certain associated persons granted specific powers by the Board.

27.15.1.3.2 Chief Financial Officer

The Chief Financial Officer (or his/her designee) is responsible for the following on behalf of CEI:

- Establishing accounting procedures in accordance with generally accepted accounting principles
- Ensuring the accurate and timely filing of CEI financial reports with regulators and others where financial reports are required
- Establishing bank accounts and designating associated persons authorized to sign checks and transfer funds on behalf of CEI
- Interacting with CEI's public accounting firm and coordinating the providing of information requested during CEI's annual audit
- Follow up regarding exceptions or recommendations referred by the outside public accounting firm

27.15.1.3.3 Department/Business Unit Managers

Department and business unit managers are responsible for oversight of the activities within their respective department or business unit, with the interests of customers and CEI as foremost considerations. The general scope of responsibility includes, among other responsibilities, the following:

- Hiring and termination recommendations to senior management of department/business unit personnel
- Supervision of department/business unit personnel including periodic reviews
- Creating a safe and positive work environment for personnel

- Recommending a budget to conduct the activities of the department/business unit if requested by senior management
- Ensuring only authorized personnel act on behalf of CEI (check signing, purchasing supplies, *etc.*)

27.15.1.3.4 Supervisors

In addition to the responsibilities listed above, Supervisors are charged with the supervision of RRs and support staff in their dealings with CEI's customers.

27.15.2 New Accounts

In addition to review and approval by the designated supervisor, new accounts are subject to CEI's Customer Identification Program (described in the Anti-Money Laundering Program) and verification against the OFAC database of potential "problem" accounts.

27.15.3 Cybersecurity

CEI maintains a separate and stand-alone manual to address Cybersecurity policies and procedures titled "Cybersecurity and Personal Information Protection Policy" Effective July 1, 2019.

27.15.3.1 Assignment of Responsibility

The Chief Compliance Officer is responsible for maintaining the Cybersecurity and Personal Information Protection Policy ("CPIP" or the Manual) in conjunction with others as set forth more fully in the CPIP.

Implementation of the Cybersecurity Policy will be managed by the Chief Technology Officer.

Distribution of the Cybersecurity Policy is the responsibility of Operations: a copy of the Policy or link thereto is provided upon on-boarding of new registered representatives, and annually with CEI's annual compliance questionnaire, wherein registered representatives acknowledge receipt of the Policy.

The on-site Branch Manager, or Person(s)-in-Charge of the branch if there is no such Branch Manager, is responsible for the distribution, education, and compliance with the Policy for all other registered and unregistered employees located in the branch. The Branch Manager or Person-in-Charge of the branch is responsible for reporting all cybersecurity incidents and compliance matters to the Home Office in accordance with the Manual.

27.16 Business Continuity Plan

[FINRA Rule 4370; FINRA Regulatory Notice 13-25; FINRA Notice to Members 06-74 and 04-37; NASDAQ Rule 3510; SIFMA Business Continuity Planning website: <https://www.sifma.org/resources/general/bcp/>]

CEI has developed a Business Continuity Plan to provide procedures for response and recovery in the event of a significant business disruption. The purpose of the Plan is to identify responsible personnel in the event of a disaster; safeguard associated persons' lives and firm property; evaluate the situation and initiate appropriate action; recover and resume operations to allow continuation of business; provide customers with access to their funds and securities; and protect books and records. The Plan was developed considering the types of business conducted, systems critical to support business, and geographic dispersion of offices and personnel.

27.16.1 Designation of Responsibilities

The following is a list of those responsible for CEI's Business Continuity Plan.

Responsibility	Names or Titles
Maintain and update Plan	Chief Compliance Officer
Approve Plan and Plan revisions; conduct annual review	<i>Chief Executive Officer, Charles F. Reiling, III</i>
Annual testing of Plan	<i>Chief Executive Officer, Charles F. Reiling, III</i>
Implementation of Plan when a disruption occurs	Emergency Response Team
Quarterly review of Emergency Contact Persons and report changes to regulators	Chief Compliance Officer
Maintain and distribute Emergency Contact List and provide updates, when necessary	Chief Executive Officer or designee
Maintain and update Books and Records Chart	FINOP
Provide Plan information to customers: <ul style="list-style-type: none"> • At time of account opening • Upon request 	Registered Representative and Supervisor
Post Plan disclosure on CEI's web site and update, as required	Chief Compliance Officer
Review critical third-party assurances or disaster plans or plan summaries: <ul style="list-style-type: none"> • At initial engagement of third party • Annually when CEI's Plan is reviewed 	Chief Legal Officer and/or Chief Compliance Officer

27.16.2 Retention and Location of The Plan

Copies of the current and prior versions of the Business Continuity Plan are retained as follows. Copies are dated as of the effective date of the version of the Plan.

- A current hard copy is retained by Compliance with a record of the senior manager's approval.
- A current hard copy is retained by the CEO at his residence.
- An electronic copies of the current and archived versions are retained on the firm's NAS in the Compliance Folder.

27.16.3 Implementation of The Plan

The Plan has been designed to be implemented in the event of a disaster that results in a significant business disruption. Whether all or only parts of the Plan are implemented depends on the nature of the disruption. Generally, a significant business disruption would include:

- Destruction of one of CEI's offices or facilities, whether by natural causes or by other means

- Loss of life or major injuries to personnel in an office location that disables that office's ability to conduct business
- Disruption of service from a critical service provider
- Disruption of service due to wide-ranging regional outages such as a power outage

27.16.4 Emergency Response Team

CEI has designated an Emergency Response Team that is responsible for implementing necessary procedures included in this Plan. The Response Team's action will depend on the nature and scope of the disruption. The "first responder" has the primary responsibility for taking action, and the "secondary responder" acts as a back-up in the event the first responder is unable to act. Where feasible, the two responders are located in different office locations.

Action	First Responder/Location	Secondary Responder/Location
Contact emergency services such as police, fire department	Charles F. Reiling/DE	Matthew Rakerd/PA
Establish off-site command center and notify associated persons	Charles F. Reiling/DE	Matthew Rakerd/PA
Account for associated persons in affected areas	Charles F. Reiling/DE	Matthew Rakerd/PA
Contact associated persons regarding Plan initiatives	Charles F. Reiling/DE	Matthew Rakerd/PA
For affected offices, evaluate business disruption and transfer associated persons and business operations to other locations	Charles F. Reiling/DE	Matthew Rakerd/PA
Initiate alternative market entry points when the Firm's normal access is disabled	Charles F. Reiling/DE	Matthew Rakerd/PA
Appoint individuals to manage business areas where needed	Charles F. Reiling/DE	Matthew Rakerd/PA
Assess financial and operations capabilities	Charles F. Reiling/DE	Francis J. Skinner/DE
Determine financial and credit risk and contact banks and other counter-parties, if necessary, to secure financing to continue operations	Charles F. Reiling/DE	Francis J. Skinner/DE
Notify regulators in the event of a capital deficiency	Charles F. Reiling/DE	Francis J. Skinner/DE
Interface with SIPC if liquidation of business is initiated	Charles F. Reiling/DE	Francis J. Skinner/DE
Contact critical service providers	Charles F. Reiling/DE	Matthew Rakerd/PA
Transfer mission critical functions that are disrupted	Charles F. Reiling/DE	Matthew Rakerd/PA

Initiate alternative customer communications systems or procedures	Charles F. Reiling/DE	Matthew Rakerd/PA
Update the Firm's web site to include information about operations and contact information	Francis J. Skinner or designee/DE	Charles F. Reiling/DE
Notify customers regarding alternative access to funds and securities	Charles F. Reiling/DE	Matthew Rakerd/PA
Notify trading counterparties of operations and contact information	Charles F. Reiling/DE	Matthew Rakerd/PA
Recover back-up records when primary records are destroyed or inaccessible	Francis J. Skinner/DE	Charles F. Reiling/DE
Contact regulators and notify them of contact persons and recovery plans	Francis J. Skinner/DE	Charles F. Reiling/DE
Identify time-sensitive regulatory requirements and filings	Francis J. Skinner/DE	Charles F. Reiling/DE
<i>[insert other actions]</i>		

27.16.5 Emergency Contact List

CEI has established an Emergency Contact List that includes the names, phone numbers (cell and land lines), e-mail addresses, and other contact information for individuals critical to CEI's business including key associated persons, key vendors or service providers, regulators, insurance carriers, banks, attorneys, and other key contacts. A copy of the List is provided to each member of the Response Team and other key personnel. This list will be reviewed and updated on at least an annual basis.

27.16.6 Alternative Business Locations

In the event associated persons can no longer conduct business at one of CEI's office locations, the following actions may be taken:

- Transfer associated persons to the closest unaffected office location and notify personnel
- Transfer critical systems to another office or a back-up firm or system
- Transfer business operations to another CEI office unaffected by the disruption
- Transfer business operations to a different broker-dealer or other entity

Considerations that will be made include:

- Geographic diversity in the event of regional service outages
- Accessibility of alternative sites and the ability of associated persons to travel to the site and methods of relocating associated persons and living arrangements, if needed
- Number and composition of staff needed and supervisors for alternative sites
- Generator and other back-up sources at alternative sites
- Resources needed at alternative sites (desks, chairs, telephones, equipment, and supplies, etc.)
- Moving staff in advance of a significant BCP event, if it can be anticipated
- Whether associated persons should work from home and what resources they would need

27.16.7 Data Back-Up and Recovery

CEI maintains its books and records in both hard copy and electronic format. The Books and Records chart (Appendix A to the Plan) indicates whether records are maintained in hard copy or electronic form; location of primary records; and back-up site for records.

In the event of an internal or external significant business disruption that causes the loss of CEI's records (whether hard copy or electronic records), back-up records will be recovered from the back-up site.

27.16.7.1 Clearing Firm Back-Up and Recovery

The clearing firm maintains records for CEI under the terms of the clearing agreement. The clearing firm has developed a disaster and recovery plan to recover and retrieve records lost in a disaster affecting CEI and/or the clearing firm. Records retained by the clearing firm are included on CEI's Books and Records chart.

CEI has received assurance from the clearing firm that its plan is consistent with SRO rule requirements and provides adequate protection of customer funds and securities held on behalf of CEI customers and back-up and recovery systems for records retained by the clearing firm. Compliance (or another person designated to review critical third-party plans) will review the clearing firm plan or a summary of the plan at least annually when CEI's Plan is reviewed.

27.16.8 Mission Critical Systems

Mission critical systems are systems that are necessary to ensure prompt and accurate processing of securities transactions including order taking, entry, execution, comparison, allocation, clearance and settlement, maintaining customer accounts, and providing access to customer funds and securities.

The Mission Critical Systems chart (Appendix B to the Plan) identifies systems (or generally describes procedures) that are critical to the operation of CEI's business; identifies third parties that provide those systems; and potential alternate procedures or systems for handling these critical functions in the case of a disruption.

27.16.9 Financial and Operational Assessments

The following describes procedures for assessing changes in operational, financial, and credit risk exposures in the event of a significant business disruption.

27.16.9.1 Operational Risk

In the event of a significant business disruption, alternative systems will be implemented to communicate with customers, associated persons, critical business constituents (banks, counter-parties, *etc.*), regulators, and other key parties depending on the nature and impact of the disruption. Communication systems are described in the section *Alternative Communications*.

27.16.9.2 Financial and Credit Risk

In the event of a significant business disruption, CEI's financial status will be evaluated to determine the need for additional financing or identify capital deficiencies including the following:

- Review the impact of the disruption on CEI's ability to conduct business
- Identify inability to satisfy obligations with counter-parties
- Contact banks or other counter-parties to secure needed additional financing

- Notify regulators of capital deficiencies
- Reduce or cease business as may be required due to capital deficiencies or inability to conduct business
- Transfer business to other financial institutions until CEI may resume conducting business

27.16.10 Alternative Market Entry

CEI may use its clearing firm (if applicable) or other broker-dealers as alternative market entry points when CEI cannot access markets through its own systems.

27.16.11 Alternative Communications

CEI may use a wide range of communication systems to communicate with its customers, associated persons, counter-parties, and regulators including telephone; mail; fax; e-mail; vendor systems (such as Bloomberg); and personal meetings. CEI may establish contracts with multiple telecommunications carriers to provide redundant systems and devices and to provide key associated persons with technology at remote locations, including home locations. Procedures for instituting alternative communications in the event of a significant business disruption include the following, depending on the nature of the disruption:

- Identify the most expedient remaining means of communication
- Notify associated persons if an off-site command center has been activated
- Notify associated persons of alternative communication systems to be used
- Transfer communications to another firm

Determination of what communication system will be used depends on the nature of the disruption and which communication systems (electronic mail, telephone calls, *etc.*) are functional and the availability of personnel in the event telephone contact is necessary.

27.16.11.1 Between Customers and the Firm

In the event of a significant business disruption that disables communications systems, alternative system procedures will be implemented, including the following:

- Identify the most expedient remaining means of communication
- Notify associated persons regarding how to contact customers
- Contact customers about how to enter orders, how to access accounts and account assets, and other alternative business operations

27.16.11.2 Between the Firm and its Associated Persons

In addition to the above, CEI has developed a system to enable senior management to contact associated persons in the event of an emergency. The system may include, depending on geographic dispersion of associated persons:

- A central list of all personnel and their contact information

27.16.11.3 Between the Firm and Trading Counterparties

Communications between CEI and its trading counterparties regarding conduct of business will be implemented by alternative systems which may include:

- Via a clearing or other alternative business partner
- Phone

- Electronic communications
- Web site postings
- Other alternative means of communicating

27.16.11.4 Firm's Web Site

CEI has established an alternative means of maintaining its web site in the event servers and other systems regularly used are unavailable. The web site will be used to communicate information to customers, counterparties, and others needing access to CEI. It will include information about operations and contact information, including contact information at a clearing firm or other alternative business partner.

27.16.11.5 Between the Firm and Regulators

Communications with regulators will be conducted using the most expedient available communication system. The designated Response Team person will contact regulators regarding any major business disruption and plans for continuing business.

27.16.12 Regulatory Reporting

In the event of a significant business disruption affecting offices responsible for regulatory reporting, regulators will be contacted to determine which means of filing are available under the circumstances to meet filing requirements. In the event CEI cannot contact regulators, required reports will be filed using communications means available.

27.16.13 Business Constituent, Bank, And Counter-Party Impact

This section describes business continuity procedures regarding third parties that are critical to the conduct of CEI's business. In most instances, contracts with critical third parties will include assurances regarding the third party's disaster recovery plans. A disruption impacting CEI's ability to conduct business may occur either at CEI itself or at the third party.

The Business Constituent, Bank, And Counter-Party chart (Appendix C to the Plan) identifies key parties and potential alternatives in the event of a disruption.

27.16.13.1 Business Constituents

- Determine whether the third party is able to continue providing critical services.
- If not, identify and contact an alternate third party to provide services.

27.16.13.2 Banks and Other Financial Institutions

- Determine whether the bank/financial institution is able to continue providing financing.
- If not, identify and secure alternative financing.

27.16.13.3 Critical Counter-Parties

- Determine whether transactions may be completed with counter-parties.
- If not, contact counter-parties directly (or CEI's clearing firm, if business is introduced) to make alternative arrangements to complete transactions.

27.16.14 Other Obligations to Customers

27.16.14.1 Accepting Customer Orders

In the event CEI's systems for accepting customer orders are disrupted, alternative systems will be communicated to customers and to associated persons including, where appropriate:

- Accepting orders by telephone or other alternative means
- Communicating orders to trading desks (internal or external) or order execution systems by telephone or other alternative means

27.16.14.2 Prompt Access to Funds and Securities

When customer access to funds and securities is impacted by a significant business disruption, customers will be notified by whatever expedient means is available (telephone, e-mail, *etc.*) regarding who may be contacted to request funds or securities. If CEI is unable to continue business operations, customers will be notified of an alternative financial institution where they may conduct business and access their funds and securities.

27.16.14.2.1 SIPC Liquidation

In the event SIPC liquidation of CEI's business is required, designated personnel will work with the SIPC-appointed trustee to wind down CEI's operations and transfer customer funds and securities.

27.16.14.3 Disclosure of Business Continuity Plan

[FINRA Rule 4370(e)]

Information about CEI's Business Continuity Plan is provided to customers as follows:

- At the time of account opening
- On CEI's web site
- Upon request, by mail

27.16.15 Emergency Contact Information

[FINRA Rule 4370 and 4517]

CEI has provided FINRA with the names of two emergency contact persons, one who must be a registered principal and member of senior management and a second who may be unregistered (such as CEI's attorney, accountant, or a clearing firm contact) and who has knowledge of CEI's business.

Emergency contact information will be promptly updated, when necessary. Contact information will be reviewed by Compliance (or someone else designated) within 17 business days of the end of each calendar year and a written record of the review will be retained.

27.16.16 Widespread Health Emergencies

[Federal government Business Pandemic Influenza Planning Checklist:

<http://www.pandemicflu.gov/plan/pdf/businesschecklist.pdf>; FINRA Regulatory Notice 20-16, 20-08 and 09-59; FINRA Information Notice 3/26/20 Cybersecurity Alert]

A widespread pandemic or any biologically based threat could have significant impact on the ability of CEI to continue conducting business. This section outlines the steps CEI has taken and will take in the event of a widespread pandemic.

27.16.16.1 Preparatory Steps

- Document government resources for information about a pending pandemic
- Identify and document an alternative firm or firms to handle CEI's business for extended periods of time
- Identify and document medical resources to assist associated persons, including administering vaccinations or other medications
- Stock antibacterial and other hygiene products for use by associated persons
- Identify associated persons that can telecommute and establish a list of those associated persons and what computers and technology will be necessary

27.16.16.2 Action if a Pandemic Occurs

The following procedures will be followed in the event of a threatened health emergency.

1. The Emergency Response Team will meet to determine the potential seriousness of the threat and what action to be taken as the threat escalates.
2. Notify associated persons of:
 - available vaccinations or other medication and whether they are mandated
 - necessary conduct such as avoiding personal contact such as handshaking
 - access to antibacterial or other hygiene products to reduce infections and transmission of communicable diseases
 - requirement to stay home and telecommute
 - transfer of business/functions to other firms
 - contact list of key personnel
3. Restrict access to CEI by outsiders (customers, vendors, *etc.*).
4. The Emergency Response Team will meet or communicate regularly to determine steps to be taken.

27.16.17 Education of associated persons

The Business Continuity Plan is communicated to associated persons as follows:

- A summary is included in the chapter GENERAL EMPLOYEE POLICIES in the section *Emergency Business Recovery Procedures* and is provided to all associated persons.
- A current copy of the Plan is provided to the Emergency Response Team and key associated persons with responsibilities for aspects of the Plan. When changes are made to the Plan, new copies will be distributed to these associated persons.
- The most recent Emergency Contact List is provided to key associated persons.

27.16.18 Updating, Annual Review, and Testing

The Plan will be reviewed on at least an annual basis and revised as needed. Each revision will be approved by the designated senior manager and copies of the revised Plan distributed to the Emergency Response Team and key associated persons. Some material events require updating the Plan when they occur, including:

- Material changes to CEI's business
- A change in CEI's main office location

- Added office locations
- A change in a major service provider

When the Plan is reviewed, the procedures and accompanying lists and charts will be reviewed and updated as needed including the:

- Plan itself
- Emergency Response Team list
- Emergency Contact List
- Books and Records chart (Appendix A)
- Mission Critical Systems chart (Appendix B)
- Business Constituent, Bank, and Counter-Party chart (Appendix C)
- *Designation Of Offices* section of the chapter *DESIGNATION OF SUPERVISORS AND OFFICES*
- Any other charts or information related to the Plan

When appropriate, CEI will participate in industry-wide testing programs. A written record of the annual review including the date reviewed and name and signature of the reviewer will be retained by Compliance.

27.19 Customer Protection

[SEC Securities Exchange Act of 1934 Rule 8c-1, Rule 15c2-1, Rule 15c3-3 and Rule 17a-13; FINRA Rule 1020; NYSE Rule 402]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Customer cash and security balances and other operations records
Frequency	<ul style="list-style-type: none"> • Ongoing
Action	<ul style="list-style-type: none"> • Establish special reserve bank account • Obtain letter from bank holding special reserve account • Establish operations procedures to comply with Rule 15c3-3 and related SRO rules • Assign responsibilities to appropriate operations personnel • Train operations personnel
Record	<ul style="list-style-type: none"> • Bank records including letter regarding special reserve account for each bank maintaining such account for the benefit of customers • Reserve formula computations • Records of quarterly security counts • Records of buy-ins and close-outs • Records of daily determination of fully paid/excess securities • Other operations records

The procedures in this section generally outline some key requirements under Rule 15c3-3 and related regulations. The FINOP (or the clearing firm) is responsible for developing detailed procedures for complying with SEC and SRO requirements.

27.19.1 Introduction

SEC Rule 15c3-3 specifies requirements for broker-dealers to protect customers' funds and securities. Two significant elements of the Rule are:

1. a formula for a cash reserve which restricts a broker-dealer from using customer funds and securities in their own business; and,
2. a requirement that brokers or dealers maintain and obtain physical possession or control, as defined in the Rule, of fully paid and excess margin securities.

27.19.2 Exemptions

[SEC.gov | Frequently Asked Questions Concerning the Amendments to Certain Broker-Dealer Financial Responsibility Rules Question #18]

Because of the nature of CEI's business, CEI qualifies for an exemption under Rule 15c3-3(k) or is a "non-covered firm." The FINOP is responsible for determining that CEI qualifies for one of the following exemptions.

27.19.2.1 Exemption Under (k)(2)(ii)

[SEC Securities Exchange Act of 1934 Rule 15c3-3(k)(2)(ii)]

CEI clears all transactions with and for customers on a fully disclosed basis with its clearing firm which carries all of CEI's customer accounts and maintains books and records related to carrying the accounts. CEI promptly transmits customer funds or securities to its clearing firm.

27.19.2.2 Exemption as a Non-Covered Firm

As a "Non-Covered Firm" the Firm is not required to make a daily possession or control determination because the requirement applies only to broker-dealers that carry accounts of or for customers. The Firm is also not required to make the customer reserve or PAB reserve computations because the Firm is only required to make these computations to the extent it has amounts required to be deposited in the customer reserve account or the PAB reserve account.

The Firm will update its FINRA membership agreement when it adopts the Non-Covered Firm exemption. When filing its FOCUS Report the Firm may include a statement that "The firm has no possession or control obligations under SEA Rule 15c3-3(b) or reserve deposit obligations under SEA Rule 15c3-3(e) because its business is limited to [list of activities]."

27.19.2.3 Inadvertent Receipt of Customer Funds or Securities

CEI does not hold funds or securities for, or owe money or securities to, its customers. In the event that funds or securities are inadvertently received by CEI, an entry will be made in a log maintained for that purpose recording the date, the amount, and, in the case of securities, a description of the securities received, and the action taken to return such funds or securities to their rightful owner.

No later than the next business day, CEI will return the funds or securities to the sender. If the sender cannot be immediately determined, CEI will open a separate bank account, to be designated as "Special Account for the Exclusive Benefit of the Owner of Funds and Securities," into which the funds or securities will be deposited and held until the rightful owner has been identified.

27.20 Confirmations

[FINRA Rule 2231 and 2232]

Responsibility	Designated Supervisor Trading managers Clearing firm (if transactions are introduced)
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Resources	Transactions Trading desk records Confirmations records or available reports
Frequency	Annual: audit reviews
Action	The clearing firm is responsible for establishing procedures to include required disclosures Review sampling of confirmations to determine whether required information is included Contact clearing firm if errors or omissions are identified Include confirmation disclosures in audit procedures
Record	Confirmations, trading or other records, available reports Audit records Documentation of corrective action Training records

Confirmations are issued for every trade executed for a customer and include required information, some of which is listed below. This section does not duplicate applicable rules which should be referenced for details.

- SEC Rule 10b-10 and 15g-3, FINRA Rule 2132, and MSRB Rule G-15 include details of required disclosures on customer confirmations
- Transaction information includes (among other information) the name of the security; quantity; price; markups/markdowns the time of execution (in minutes and seconds); the firm's role (agent, principal, riskless principal)
- Other types of disclosures (among others) include:
 - non-rated taxable debt securities (other than U.S. government securities) including a statement that rating information is based on a good faith inquiry of selected sources
 - control relationship with the issuer
 - call features
 - for principal transactions, the reported trade price, the net price to the customer, and the difference between the reported price and the price to the customer, the difference between the reported price and the customer's price (markup/markdown)
 - for municipal securities call features, primary revenue source for revenue bonds, securities sold as "original issue discount" (OID) bonds, yield information
 - for penny stocks bid or offer, compensation, and other disclosures (see Rule 15g-3 and the section Penny Stocks in the chapter *ORDERS*)
 - payment for order flow
 - Markups/markdowns in municipal securities for non-institutional customers (MSRB Rule G-15) (See the section *Mark-ups and Mark-Downs* in the chapter *MUNICIPAL SECURITIES*)

27.21 Lost Securityholders and Unresponsive Payees

[SEC Securities Exchange Act of 1934 Rule 17Ad-17]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Customers with returned undeliverable correspondence • Customer checks not negotiated

Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Identify returned correspondence and checks not negotiated <ul style="list-style-type: none"> ○ (Notify the clearing firm, if applicable, and skip the following steps) • For returned correspondence: <ul style="list-style-type: none"> ○ Conduct searches ○ Update the customer's record if an address is found • For checks not negotiated: <ul style="list-style-type: none"> ○ Send written notification to customer ○ Issue a new check if the original was lost or not received by the customer
Record	<ul style="list-style-type: none"> • Undeliverable correspondence • Unnegotiated checks* • Searches conducted and results* • Notice sent to customers regarding unnegotiated checks* • Action taken pursuant to searches and notification* <p>*These records are retained by the clearing firm, if applicable</p>

CEI (and/or its clearing firm) is required to search for holders of securities with whom it has lost contact and to provide notifications to persons who have not negotiated checks that have been sent to them. "Lost securityholders" are customers to whom any correspondence was sent and returned as undeliverable and for whom an updated address has not been received or is not obtainable from the customer. **The requirement does not apply when the securityholder is not a natural person.**

27.21.1 Searches for Lost Securityholders

Searches will be conducted through an information database service that contains addresses for the entire U.S. including the names of at least 50% of the U.S. adult population, is indexed by taxpayer ID number or name and is updated at least four times a year. The search will be conducted by taxpayer ID number or, if that search is not likely to locate the person, by name. Securityholders will not be charged for searches.

Searches will be conducted between three and twelve months from the later of:

- the date upon which correspondence is returned as undeliverable or
- if returned correspondence is re-sent within one month from the date it was returned and is again returned as undeliverable, the date on which the re-sent item is returned as undeliverable.

A second search will be conducted between six and twelve months after the first search.

Searches will not be conducted when (i) CEI receives documentation the securityholder is deceased or (ii) the total value of assets in the account is less than \$25.

27.21.2 Unnegotiated Checks

Written notice will be provided to customers who do not negotiate checks sent to them within 6 months of sending. This policy does not apply to checks worth less than \$25.

27.22 Subordination Agreements with Investors

[SEC Securities Exchange Act of 1934 Appendix D to Rule 15c3-1; FINRA Notice to Members 02-32 and 02-04; FINRA web site: <https://www.finra.org/filing-reporting/regulatory-filing-systems/subordination-agreements>]

If CEI enters into a subordination agreement with an investor, it will provide the investor with a copy of FINRA Subordination Agreement Investor Disclosure Document and obtain the investor's signature on a copy of the Document. A copy of the signed Disclosure Document will be submitted to FINRA with the subordination agreement, for approval.

The FINOP is responsible for obtaining and submitting the required documents for subordination agreements.

27.23 Expense-Sharing Agreements

[SEC Letter July 11, 2003 to FINRA and NYSE Regarding Recording Certain Broker-Dealer Expenses And Liabilities; FINRA Notice to Members 03-63]

The SEC specifies requirements for incorporating an expense-sharing agreement into a broker-dealer's operations and how these agreements are recorded in the broker-dealer's financial records. The FINOP is responsible for ensuring CEI complies with the SEC's guidelines if it enters into any such agreements.

In addition, the FINOP is responsible for notifying CEI's Designated Examining Authority (DEA) if it enters into an expense-sharing agreement and does not record each of the expenses it incurs relating to its business on the reports it is required to file with the SEC or with the DEA. The notice will include the date of the agreement and the names of the parties to the agreement; a copy of the agreement will be provided to the DEA upon request.

27.24 Electronic Delivery and Signatures

[Electronic Records and Signatures in Global and National Commerce Act; SEC Release No. 34-42728; SEC Interpretive Release No. 33-7233, 33-7856 and 33-36345; NASD Notice to Members 98-3; NASD Regulatory and Compliance Alert March 1998; SIA Legal Alert 00-12]

Federal securities law through the Electronic Signatures in Global and National Commerce Act of 2000 regulates the use of electronic media for transmitting documents and the recording and accepting of electronic signatures. This section outlines requirements when CEI uses electronic methods of delivery between CEI and its customers and the use of electronic signatures for internal purposes such as approval of new accounts.

27.24.1 Electronic Delivery to Customers

[SEC Release No. 34-42728]

If CEI electronically transmits documents to customers and/or accepts electronic signatures from customers, the following requirements will apply:

- The customer's consent will be obtained.
- Notice will be provided to customers that the information is available electronically.
- Customers who are provided electronic delivery have access to the information substantially equivalent to the access that would be provided if the information were delivered in paper form (*i.e.*, the electronically transmitted document will convey all material and required information). Customers will have ready access to the electronic document either through downloading or ongoing access online.
- CEI will evidence satisfactory delivery through the customer's informed consent agreeing to delivery of certain documents or obtaining actual confirmation the customer received the information.

- Electronic delivery is subject to CEI's policies and procedures to protect confidential customer information and ongoing review of CEI's security systems.

27.24.2 Electronic Signatures

[SEC Release No. 34-42728]

Electronic signatures may be used by customers and RRs, and by designated supervisors to indicate approval/review of new accounts, orders, and other ongoing supervisory reviews.

27.25 Transfer of Accounts

For accounts introduced to a clearing firm, the clearing firm is responsible for timely transfer.

27.26 Solicitation of Proxies

[SEC Securities Exchange Act of 1934 Section 14]

RRs are not permitted to solicit proxies from customers. Federal securities rules prohibit solicitation of proxies except in very limited situations. Questions should be referred to Compliance.

27.27 Customer Requests for References

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Requests from customers or prospective customers for reference letters
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Forward requests to Compliance • Review requests and determine what, if any, reference letter may be issued • If appropriate, write reference letter with a copy to the RR
Record	<ul style="list-style-type: none"> • Letters retained by Compliance

Customers or prospective customers sometimes request letters of reference from broker-dealers regarding their accounts or future business to be done. Some of these requests in the past have been scams by unscrupulous individuals seeking to capitalize on a broker-dealer's good name. Any such requests should be referred to Compliance for handling.

27.28 Audit Letters

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Letters from auditors requesting verification of balances in customer accounts
Frequency	<ul style="list-style-type: none"> • As required

Action	<ul style="list-style-type: none"> • Forward requests to Operations for response
Record	<ul style="list-style-type: none"> • Operations will maintain copies of responses in customer account files

Auditors sometimes send letters asking CEI to verify funds and securities on behalf of their customers who also have accounts with CEI.

All requests should be forwarded to the manager of Operations for response. In no instance should an RR or other branch personnel respond to these requests.

6.29 Annual Disclosure of FINRA Broker Check

[FINRA Rule 2267]

As required by FINRA rule, at least annually customers will be provided with the following information in writing about FINRA Broker Check (formerly known as FINRA Public Disclosure Program):

- the hotline number
- the Web Site address
- a statement regarding the availability of an investor brochure regarding FINRA Broker Check

27.30 Carrying Agreements

[FINRA Rule 4311; NASDAQ Rule 3230]

CEI introduces its accounts and customer transactions to its carrying firm. CEI has executed a carrying agreement consistent with regulators' requirements and will amend its carrying agreement when necessary. Any new carrying agreement or amendment will be submitted to its designated SRO for review and approval. A carrying agreement where accounts are carried on a fully disclosed basis will include the responsibilities of each party to the agreement as required by rule. Accounts introduced on a fully disclosed basis will be notified in writing at the opening of the account of the existence of the carrying agreement and the responsibilities allocated to the respective parties.

If CEI has an agreement to act as an intermediary for another introducing firm ("piggybacking" arrangement), it will notify the carrying firm of the existence of the arrangement with the other introducing firm and disclose the identity of the firm. The carrying agreement will identify and bind every direct and indirect recipient of clearing services as a party to the agreement.

The FINOP is responsible for executing required carrying agreements; providing required notices; and retaining records.

27.31 Clearing Firm Exception Reports

[FINRA Rule 4311(h); FINRA web site:

<http://www.finra.org/Industry/Compliance/RegulatoryFilings/ClearingNotifications/index.htm>; NYSE Rule 382]

Responsibility	<ul style="list-style-type: none"> • Compliance
Resources	<ul style="list-style-type: none"> • Clearing firm lists of reports available and currently received
Frequency	<ul style="list-style-type: none"> • Annually, at or around July 31 of each year

Action	<ul style="list-style-type: none"> Review list of reports available from clearing firm and adjust list of reports received, if appropriate
Record	<ul style="list-style-type: none"> Notice from the clearing firm and request for change to reports received are retained in a file for clearing firm exception reports.

In compliance with SRO rules, CEI's clearing firm is required to provide annual notice, by July 31 of each year, as follows:

- Notice to CEI of:
 - exception reports available, and,
 - exception reports currently supplied to CEI.
- A copy of this notice is forwarded to CEI's designated examining authority or other appropriate regulator by the clearing firm.

When the list of available reports is received, Compliance will review the list and contact the clearing firm regarding changes to the list of reports currently received.

27.34 Regulatory Fees and Assessments

[SEC Securities Exchange Act of 1934 Section 31; FINRA By-Laws Schedule A; FINRA Notice to Members 05-11 and 04-63]

The FINOP is responsible for paying fees and assessments required by regulators. A record of information reported and fees or assessments paid are retained in the FINOP's files.

27.35 Regulatory Requests

[FINRA Rule 8210; State Regulations]

Responsibility	<ul style="list-style-type: none"> Compliance
Resources	<ul style="list-style-type: none"> Regulatory requests received from regulators
Frequency	<ul style="list-style-type: none"> As required
Action	<ul style="list-style-type: none"> Process the inquiry including the following: <ul style="list-style-type: none"> ○ Record date of receipt ○ Flag due date in a log or other record ○ Assemble and review response ○ Encrypt responses prior to sending where required ○ Request and record any extension of due date, if necessary ○ Forward response, retaining a copy
Record	<ul style="list-style-type: none"> Copy of request, response, and notations of when received, extensions, and when response was sent

Responses to regulatory requests may only be provided by authorized associated persons or departments such as Operations or Compliance. Requests received by associated persons other than those authorized must be referred to Compliance.

27.35.1 Information Provided Via Portable Media Device

[FINRA Regulatory Notice 10-59]

Typically, the firm will receive requests and provide responses through FINRA Gateway. If this is unavailable, CEI will request to provide by an acceptable encrypted vendor such as Citrix Share File, Zix, or Kite Works so long as the requestor is agreeable.

Otherwise, information provided to FINRA or another regulator by portable media device in response to requests under FINRA 8210 (Provision of Information and Testimony and Inspection and Copying of Books) will be encrypted using a method that meets industry standards for strong encryption. FINRA staff will be provided with the confidential process or key regarding the encryption in a communication separate from the encrypted information itself (separate email, fax, letter, *etc.*).

27.36 Outsourcing and Vendor Due Diligence

[FINRA Notice to Members 05-48]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • Third party vendors • Reviews of vendor performance • Customer complaints
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Identify areas of CEI's business where outsourcing is appropriate • Identify third party vendors that provide the needed services • Evaluate potential third parties and determine whether to engage using the Outsourcing Review Worksheet • Execute contract • Establish procedures to determine periodically that outsourced services are fulfilling CEI's requirements and complying with applicable rules • When problems with outsourced services are identified through customer complaints, monitoring of services, or from the vendor itself: <ul style="list-style-type: none"> ○ Review the problem to determine whether the source is the vendor or is internal ○ Take corrective action which may include the following: <ul style="list-style-type: none"> ▪ Contact the vendor and determine what corrective action will be taken and follow-up to determine corrective action has been taken ▪ If the problem continues or is significant, determine whether vendor should be replaced ▪ If the problem is internal, contact the appropriate supervisor to determine corrective action ○ Consult with Compliance when necessary to determine action to be taken
Record	<ul style="list-style-type: none"> • Outsourcing Review Worksheet or memorandum • Contracts with third parties • Records of third party vendor reviews

	<ul style="list-style-type: none">• Records of corrective action taken
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Some services may be outsourced to third parties (vendors). While third parties are responsible for providing agreed-upon services in an accurate manner, regulators have stated that firms remain responsible for ultimate compliance with rules governing the outsourced activity.

When choosing an outside vendor, a number of factors will be considered depending on the type of service provided. Factors that may be considered when engaging a third party include:

- Length of time in business
- Financial stability
- Prior knowledge of the vendor
- Other users of the vendor's services
- Technology and ability to deliver services
- Security of customer or other financial information, if applicable
- Who at CEI is responsible for monitoring the vendor's services

An Outsourcing Review Worksheet or other memorandum will be completed when a new vendor is considered.

28 Broker-Dealer Registration

Responsibility	<ul style="list-style-type: none">• Compliance
Resources	<ul style="list-style-type: none">• Information regarding reportable items including civil and regulatory actions• Records regarding officers and directors to be included on Form BD• Other information as required by Form BD
Frequency	<ul style="list-style-type: none">• As required - updates
Action	<ul style="list-style-type: none">• Prepare updates as required; consult with in-house or outside counsel, as required• File Form BD updates
Record	<ul style="list-style-type: none">• File of BD amendments

Compliance is responsible for updating Form BD when necessary and filing with the required SROs and other regulatory agencies.

28.1 Member Application and Associated Person Registration (MAP Rules)

[FINRA Rule 1017; [FINRA Regulatory Notice 21-09](#)]

When CEI anticipates a material change in its business, Compliance will file requests for approval by the appropriate SROs.

Events Requiring Approval

Events that require approval include merger with or acquisition of another broker-dealer or acquisition of 25% or more of the assets of another dealer; a change in ownership or control; and a material change in business operations. In addition, material changes include removing or modifying a membership agreement restriction; market making for the first time; adding business activities that require a higher level of minimum net capital; and engaging in activities beyond proprietary trading as defined in NASDAQ rules.

Certain types of expansions are presumed to not be a "material change in business operations" and do not require FINRA approval. However, this safe harbor is not available to firms that, among other things, have a "disciplinary history" as defined in IM-1011-1. The interpretation must be consulted to determine what changes are not material and what constitutes disciplinary history precluding use of the safe harbor.

If the Firm operates under a Restriction Letter, it will conduct business consistent with the Letter and Compliance will contact FINRA if a change is necessary.

Employment (New or Continuing) Of A Natural Person Subject to Criminal Matters or Risk Events

The Firm must file a Continuing Membership Application (CMA) when a person who, during the past five years, becomes subject to one or more "final criminal matters" or two or more "specified risk events" and seeks to become an owner, control person, principal or registered person of the Firm. As an alternative, the Firm may submit a written request to FINRA for a materiality consultation for the contemplated activity. This does not apply to an existing RR or principal of the Firm who seeks to add an additional RR- or Principal-level registration, respectively.

28.2 Regulatory Contact Information

[FINRA Rule 4517; FINRA Contact System web page:<http://www.finra.org/Industry/Compliance/RegulatoryFilings/FCS/>]

CEI is obligated to maintain current contact information with regulators. Updates to contact information will be made within 30 days following any change. In addition, by the 17th business day after the end of each calendar year, CEI's SAA is required to verify contact information through the FINRA Contact System.

Compliance will update the following information through FINRA's Contact System when necessary and will conduct the mandatory annual verification:

- Executive Representative [NASD By-Laws Article IV, Section 3, FINRA Rule 4517; NASDAQ Rule 1150]
- Regulatory Element Continuing Education Contact Person [FINRA Rule 1250]
- Emergency contact persons [FINRA Rule 4370]
- AML contact person(s) [FINRA Rule 3310.02]
- Other contacts mandated by FINRA rules

Contact information will be provided promptly to FINRA upon request, but no later than 15 days after the request.

28.3 Regulatory Filings

[FINRA Rule 4517]

CEI will submit regulatory filings electronically where required. Filing procedures are included in appropriate sections of this manual.

28.4 Reporting Requirements

[FINRA Rule 4530; FINRA Regulatory Notice 11-32; FINRA FAQs on Rule 4530: <https://www.finra.org/filing-reporting/regulatory-filing-systems/rule-4530/faq>]

Responsibility	<ul style="list-style-type: none">• Chief Compliance Officer
Resources	<ul style="list-style-type: none">• Criminal, civil, and arbitration actions against CEI
Frequency	<ul style="list-style-type: none">• As required
Action	<ul style="list-style-type: none">• Determine whether information or events are reportable• File information [specified in Rule 4530(f)(1)] with FINRA; information will be filed within 30 calendar days after knowing of the event; copies of documents will be filed promptly
Record	<ul style="list-style-type: none">• Record of filings

CEI will file information with FINRA for reportable events involving CEI under FINRA Rule 4530 within 30 calendar days of becoming aware of the reportable event. When CEI concludes CEI has violated any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body or self-regulatory organization, such reported violations will include only conduct that has widespread or potential widespread impact to CEI, its customers or markets, or conduct that arises from a material failure of CEI's systems, policies or practices involving numerous customers, multiple errors or significant dollar amounts.

Refer to the section *Reporting Possible Law Or Rule Violations* in the chapter *GENERAL EMPLOYEE POLICIES* for procedures addressing the identification of violations, escalation of internal reporting, and reporting of internal conclusions.

29 ANTI-MONEY LAUNDERING (AML) PROGRAM

[FINRA Rule 3310; NASD Notice to Members 02-21; FINRA web site AML page <http://www.finra.org/RulesRegulation/IssueCenter/Anti-MoneyLaundering/index.htm>; Bank Secrecy Act; Office of Foreign Assets Control (OFAC) web site <http://www.treas.gov/offices/enforcement/ofac>; SEC web site AML page <http://www.sec.gov/spotlight/moneylaundering.htm>; SEC Anti-Money Laundering (AML) Source Tool: <http://www.sec.gov/about/offices/ocie/amlsourceool.htm>; NASDAQ Rule 3011; SIFMA Anti-Money Laundering Resource Center: <http://www.sifma.org/issues/legal-compliance-and-administration/anti-money-laundering-compliance/resources/>; Regulatory Joint Statement on Digital Assets: <https://www.sec.gov/news/public-statement/cftc-fincen-secjointstatementdigitalassets>]

29.1 Introduction

This chapter explains CEI's Anti-Money Laundering (AML) Program. An explanation of money laundering and guidance for all associated persons to detect money laundering is included in the chapter *GENERAL EMPLOYEE POLICIES* in the section *Money Laundering*.

These policies will be updated and appropriate procedures and action effected when new rules are adopted.

29.1.1 Definitions

[Bank Secrecy Act 31 CFR Chapter X Part 1023.100 Subpart A]

Monetary instruments:

1. Currency;
2. Traveler's checks in any form;
3. All negotiable instruments (including personal checks, business checks, official bank checks, cashier's checks, third-party checks, promissory notes (as that term is defined in the Uniform Commercial Code), and money orders) that are either in bearer form, endorsed without restriction, made out to a fictitious payee (for the purposes of Section 103.23), or otherwise in such form that title thereto passes upon delivery;
4. Incomplete instruments (including personal checks, business checks, official bank checks, cashier's checks, third-party checks, promissory notes (as that term is defined in the Uniform Commercial Code), and money orders) signed but with the payee's name omitted; and
5. Securities or stock in bearer form or otherwise in such form that title thereto passes upon delivery.
6. Monetary instruments do not include warehouse receipts or bills of lading.

29.2 AML Compliance Officer

[FINRA Rule 3310(d) and 3310.02]

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • AML Detection software (WFCS-SAS) • Internal audits or outside audits of the Program • Regulations and rules for broker-dealer anti-money laundering programs • OFAC web site • Other sites and resources available
Frequency	<ul style="list-style-type: none"> • As needed - review policies and procedures • As needed - develop and schedule AML education for associated persons • As needed - update program and provide revisions to senior management for review and approval • Annually - review AML contact information on file with FINRA

	<ul style="list-style-type: none"> • Ongoing - review new regulations • Ongoing - monitor activity
Action	<ul style="list-style-type: none"> • Develop and update CEI's anti-money laundering program • Obtain senior management approval for the program and any changes to the program • Monitor (or designate monitoring) the activity of CEI, its associated persons, and customers to reasonably detect and prevent money laundering activities • Develop AML education program for associated persons and schedule training • File required reports • Retain required records • Provide contact information to FINRA and update contact information if necessary
Record	<ul style="list-style-type: none"> • Designation of AML Compliance Officer • Current and past copies of anti-money laundering program with senior management approval • Records of AML education including who attended, date of training, and material covered • Reports filed • Other records to be retained, as listed in the Program

CEI has designated an AML Compliance Officer who is responsible for developing policies, procedures, and internal controls reasonably designed to achieve compliance with AML rules and regulations.

29.3 Independent Testing

[FINRA Rule 3310.01]

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • Policies and procedures • Independent testing results
Frequency	<ul style="list-style-type: none"> • Annual - schedule, conduct, and follow up testing (unless the firm qualifies for testing every two years)
Action	<ul style="list-style-type: none"> • Identify person(s) to conduct testing • Conduct testing • Report results to CEO in annual compliance report • Revise policies and procedures as necessary • Conduct follow-up to determine corrective action has been taken
Record	<ul style="list-style-type: none"> • Independent testing results including who conducted and dates of review • Report to CEO • Record of changes to policies and procedures resulting from testing • Record of follow-up actions

The AML Compliance Officer will arrange for annual (on a calendar-year basis) independent testing of CEI's policies and procedures regarding money laundering and the effectiveness of the program. The review is conducted by member personnel or a qualified outside party. More frequent reviews will be conducted, if necessary, as determined by the AML Compliance Officer.

Independent testing must be conducted by someone with a working knowledge of the Bank Secrecy Act and implementing regulation requirements. Independent testing may not be conducted by:

- A person who performs the functions being tested;
- The designated AML Compliance Officer; or
- A person who reports to a person described in the above two items.

29.4 Training Program

All associated persons are provided with CEI's Money Laundering policy when they are hired. The policy is included in the chapter *GENERAL EMPLOYEE POLICIES*.

In addition, ongoing education will include the firm element continuing education program, periodic circulation of CEI's policy, and other educational programs directed at specific employees such as operations personnel. Training will be delivered periodically and as needed by video, intranet systems, in-person lectures, compliance & operations alerts distributed by email, and other methods including third parties who deliver AML training.

Training will include the following, as well as other subjects identified by the AML Compliance Officer:

- How to identify red flags and signs of money laundering
- What to do once the risk is identified (how, when and to whom to escalate unusual customer activity or other red flags)
- Associated persons' roles in CEI's compliance efforts and how to perform them
- CEI's record retention policy
- Disciplinary consequences (including civil and criminal penalties) for non-compliance

The AML Compliance Officer is responsible for retaining records of associated persons trained, the dates of training, and the subjects included in training.

29.5 Bank Secrecy Act (BSA) Filings

[BSA E-Filing System: <http://bsaeiling.fincen.treas.gov/main.html>; FinCEN web site for Adobe forms: <https://www.fincen.gov/legal-reference-bank-secrecy-act-forms-and-filing-requirements>]

The BSA E-Filing System web site provides a list of forms supported for electronic filing, and include the following (refer to the web site for the most current list of forms):

- Currency Transaction Report (FinCEN Form 112)
- Designation of Exempt Person (FinCEN Form 110)
- Suspicious Activity Report by the Securities and Futures Industries (FinCEN Form 111)
- Report of Foreign Bank and Financial Accounts (Form 114)

29.6 OFAC List and Blocked Property

[Dept. of Treasury, various statutes; OFAC web site <http://www.treas.gov/offices/enforcement/ofac/>; Foreign Assets Control Regulations For The Securities Industry: <https://www.treasury.gov/resource-center/sanctions/Documents/facbk.pdf>]

The property of sanctioned persons or entities will be blocked and transfer of assets prevented for persons or entities included on the OFAC list of blocked persons or entities. In addition, securities issued by sanctioned countries and other sanctioned issuers will be blocked. OFAC (the Office of Foreign Assets Control of the U.S. Treasury Department) enforces the sanctions and publishes, on its web site (www.treas.gov/ofac), information about sanctions. The information is divided into several categories including:

- Persons and entities subject to sanctions, *Special Designated Nationals and Blocked Persons* (SDN list)
- Persons and entities engaged in drug trafficking, *Specially Designated Narcotics Traffickers* (SDNTKs)
- Terrorists and terrorist organizations, *Specially Designated Terrorists* (SDTs)
- Countries, governments, and other entities subject to sanctions

OFAC requirements apply to all persons and entities under U.S. jurisdiction, including foreign branches of U.S. institutions. This also includes foreign institutions that operate in the U.S.

The term "OFAC list" in this section includes all sanctions published by OFAC even though the information may appear in multiple lists. Upon opening a brokerage account, but in no event more than 30 days after approval of account opening, the Supervisor of the registered representative of record on the account (or designee if absent) will conduct a name search in the OFAC database, print a copy of the results, and attach to the customer file to evidence the OFAC check. For self-directed or third-party platform users (e.g. RIA customers) the principal reviewing the account for account opening is responsible for the check.

To confirm existing customers are not on the OFAC list, Coastal's client list is compared to the OFAC list on a semi-annual basis to detect property of sanctioned persons or entities. In the event that an account is identified as being owned or controlled by a sanctioned person or entity, the account(s) will be restricted, and Coastal will file the necessary reports. This testing is conducted by the AML Officer or her designee under her supervision. Records of each check are maintained by the AML Officer on Coastal's server or designated document repository.

29.6.1 Prohibited Transactions

CEI is prohibited from conducting transactions in any account on behalf of a sanctioned party or in certain blocked securities. Securities and funds may not be released and securities transactions may not be executed. Securities and funds may be deposited to a blocked account, but no securities or funds will be released until the account is no longer subject to sanctions. Funds or securities may not be transferred to sanctioned parties.

Because transactions are prohibited, all open orders for a blocked account will be cancelled.

29.6.2 Risk Factors

<https://www.treasury.gov/resource-center/sanctions/Documents/facbk.pdf>

Following are risk factors identified by OFAC that may warrant a heightened level of scrutiny.

International transactions, including wire transfers:

- a) High number of international transactions, cross-border transactions, or investments in a foreign investment fund or on a foreign exchange;
- b) Presence of overseas branches or multiple correspondent accounts with foreign financial institutions, including correspondent accounts subject to enhanced due diligence under Section 312 of the USA PATRIOT Act.

Foreign customers/accounts:

- a) A large, fluctuating client base across a number of foreign jurisdictions involving a large number of security transactions;
- b) Customers located in or having accounts in high-risk jurisdictions, such as countries found to be of "primary money laundering concern" pursuant to Section 311 of the USA PATRIOT Act;
- c) Customers located in or having accounts in countries that are havens for money laundering or are inadequately regulated, including countries identified by the Financial Action Task Force as maintaining an inadequate AML/CFT regime;
- d) Customers located in or having accounts in countries where local laws, regulations, or provisions (such as privacy laws) prevent or limit the collection of client identification information;
- e) Customers located in an offshore financial center as identified by the U.S. Department of State;
- f) Accounts for senior political or government officials ("politically exposed persons") of a foreign government;
- g) Accounts of closely held corporations;
- h) Accounts for unregistered or unregulated investment vehicles;
- i) Accounts for non-resident aliens;
- j) Accounts maintained at an offshore bank.

Foreign broker-dealers who are not subject to OFAC regulations:

- a) Lack of information regarding beneficial owners of securities; and
- b) Foreign broker-dealers that act as introducing brokers.

Risks of Investments in Foreign Securities:

Practical exposure increases when investing in a foreign investment fund or foreign exchange, because of the risk that the securities are issued by a sanctioned country or party or otherwise in violation of OFAC sanctions, *e.g.*, securities of an issuer that provides financing for a sanctions target. Other risk factors include:

- a) Cross-border settlements involving the interaction of different settlement systems and laws in different countries;
- b) Foreign securities that may be more prone to misidentification in the course of a trade, *e.g.*, similar names between two foreign issuers;
- c) Foreign companies that issue shares in bearer form.

Personal Investment Corporations or Personal Holding Companies:

Beneficial ownership by a non-U.S. person that maintains a private banking account with a U.S. financial institution.

Very High Net Worth Institutional Accounts, Hedge Funds, Funds of Hedge Funds and Other Alternative Investment Funds (Private Equity, Venture Capital Funds) and Intermediary Relationships:

- a) Lack of transparency regarding securities/investments and beneficial owners;

- b) U.S. hedge fund with an offshore related fund where beneficial owners are offshore investors; and
- c) Subscription funds that originate from or are routed through an account maintained at an offshore bank, or a bank organized or chartered in an inadequately supervised and poorly regulated jurisdiction, or a foreign shell bank.

Omnibus Accounts/Use of Intermediaries:

- a) Potential for the use of code names to invest funds in the United States on behalf of sanctions targets, concealing the identities of the beneficial owners;
- b) Accounts for intermediaries held in street name that trade on behalf of third parties, such as other broker-dealers, banks, and mutual funds; and
- c) Cross-border trades executed for unregulated investment vehicles, *e.g.*, hedge funds, private equity funds, and other private pools of capital.

Third-Party Introduced Business:

Business introduced by an overseas bank, affiliate, or other investor based in high risk or inadequately regulated countries.

Confidential Accounts:

Private banking accounts established or maintained for non-U.S. persons or services, including financial and related services, to wealthy clients who use offshore accounts for tax avoidance purposes.

29.6.3 Blocking Requirements

Blocking requirements are generally triggered under the following circumstances:

- An account is opened for someone included on an OFAC list.
- The owner of an existing account is added to an OFAC list.
- A security is identified in a customer account where the issuer is the subject of sanctions.
- A request is made by a customer to pay or transfer funds or securities to a blocked person or entity.

While title to blocked property remains with the blocked person or entity, transactions affecting the property (including transfer of the assets) cannot be made without authorization from OFAC. Debits to blocked accounts are prohibited, but credits may be accepted. Cash balances in blocked accounts must earn interest at commercially reasonable rates. Blocked securities may not be paid, withdrawn, transferred (even in book transfer), endorsed, guaranteed, or otherwise dealt in.

It is not a violation to open an account for a blocked person. The violation occurs when the account is not frozen and assets are allowed to transfer out of the account. In addition, OFAC restrictions may vary depending on the blocked person or entity; details of blocking requirements are explained on the OFAC web site.

29.6.4 Monitoring Procedures

Monitoring is to be conducted as follows:

- Operations personnel should be aware of the countries included on the OFAC list, to watch for new accounts to be opened for or requests to transfer funds or securities to residents of those countries.

- CEI and its clearing firm have procedures to monitor new accounts, existing accounts, security positions, and potential disbursements of funds or securities.
- New customers are screened against the OFAC list upon account opening, or within 30 days of account opening, by the designated supervisor of the registered representative responsible for the account.
- Existing customers are continually screened against the OFAC list on a semi-annual basis. The AML Compliance Officer maintains documentation in a spreadsheet to evidence screenings conducted, potential matches, and the results of investigating the potential matches, if applicable. This spreadsheet will be dated to show when the review was completed.
- CEI will screen all recipients of third-party (non-customer) disbursements, prior to approval of the disbursement. The supervisor approving the disbursement is responsible for ensuring OFAC screening documentation is maintained with the service request. The AML Compliance Officer will periodically review third party disbursements to ensure this procedure is being followed.

29.6.5 Other Requests to Monitor Accounts

Regulators or law enforcement agencies may ask the industry's cooperation in identifying accounts for individuals or entities under investigation or suspected of criminal activities.

The AML Compliance Officer is responsible for responding to such requests; providing the necessary information; and retaining records of requests, reviews conducted pursuant to requests, and information provided to authorities.

29.6.6 Blocking Property and Disbursements

Any blocked account will not be permitted to engage in transactions other than the acceptance of deposits of funds or securities. Open orders of blocked accounts will be cancelled.

Disbursements of funds or securities may not be made to sanctioned parties. CEI is responsible for monitoring requests for disbursements.

29.6.7 Reporting Blocked Property and Legal Actions

When an account or disbursement is blocked or a blocked security is identified, OFAC will be notified within 10 days of blocking. If CEI blocks an account or security, it will file the necessary report with OFAC. Reports filed by CEI will be retained in a file of blocked accounts or securities. Information to be reported includes:

- Owner or account party
- Property and property location
- Existing or new account number
- Actual or estimated value
- Date property was blocked
- Copy of the payment or transfer instructions
- Confirmation that funds have been deposited in a blocked account that is identified as blocked
- Name and phone number of contact person at CEI

For rejected disbursements, the following information is to be filed:

- Name and address of the transferee financial institution
- Date and amount of the transfer
- Copy of the payment or transfer instructions

- Basis for rejection
- Name and phone number of contact person at CEI

7.6.7.1 Annual Report of Blocked Property

On an annual basis by September 30th, Form TDF 90-22.50 will be filed with OFAC for any blocked property held as of June 30. The AML Officer is responsible for filing Form TDF 90-22.50 when necessary.

29.6.7.2 Legal Actions Involving Blocked Property

U.S. persons involved in litigation, arbitration, or other binding alternative dispute resolution proceedings regarding blocked property must provide notice to OFAC. Copies of all documents associated with the proceedings will be submitted by Compliance to the OFAC Chief Counsel at the U.S. Treasury Department within 10 days of their filing. In addition, information about the scheduling of any hearing or status conference will be faxed to the Chief Counsel.

29.6.8 Role of Operations Personnel

Operations personnel are an important first line of defense in preventing transactions with sanctioned parties. The following guidance is provided to assist Operations personnel in identifying blocked parties. Any questioned accounts or transactions should be referred to Compliance.

- Be familiar with countries included on the OFAC list. These are countries considered potential havens for money laundering, drug trafficking, or terrorist activities. Information is included on the OFAC web site at www.treas.gov/ofac.
- When processing the opening of accounts, question accounts for residents of countries included on the OFAC list.
- Question requests to transfer funds or securities to residents or entities domiciled in any country included on the OFAC list.

29.7 Currency Reporting Requirements

[SEC Securities Exchange Act of 1934 Rule 17a-8; Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart C]

The following summarizes the reporting requirements under the Bank Secrecy Act. CEI's designated supervisor of Operations is responsible for maintaining records of any currency reports required to be filed by CEI and retaining them for five years.

29.7.1 Transactions Involving Currency Over \$10,000

If CEI accepts a currency deposit exceeding \$10,000, it is required to electronically file a Currency Transaction Report (CTR, Form 112) with the Financial Crimes Enforcement Network (FinCEN). Multiple transactions by the same person equaling over \$10,000 in any one day must also be reported.

"Currency" is defined as the coin and paper money of the U.S. or legal tender of other countries. Currency also includes U.S. silver certificates, U.S. notes, federal reserve notes, and official foreign bank notes customarily used and accepted as a medium of exchange in a foreign country. CTRs must be filed by the 15th calendar day after the day of the transaction and kept for 5 years.

29.7.2 Transactions Involving Currency or Bearer Instruments Over \$10,000 Transferred Into Or Outside The U.S.

Broker-dealers are required to file a Currency and Monetary Instrument Transportation Report (CMIR, Form 105) with the U.S. Customs Service to report transactions in currency and/or bearer instruments which alone or in combination exceed \$10,000 and which are shipped or transported into or outside the U.S. This filing is not required for currency or other monetary instruments mailed or shipped through the postal service or by common carrier. CEI (or clearing firm or other third party) is responsible for filing these reports and maintaining records of them. CMIRs must be filed within 15 days after the receipt of the currency or monetary instruments.

29.7.3 State Reporting Requirements

States have adopted various currency and suspicious activity reporting requirements. Most states have entered into an agreement with FinCEN to provide them with duplicate copies of forms filed by broker-dealers. Some states, however, require duplicate filing with the states themselves at the time the broker-dealer files with a federal agency. CEI will file reports as required under state requirements.

29.8 Foreign Financial Account Reporting Requirements and Recordkeeping (FBAR)

[Bank Secrecy Act 31 CFR Chapter X Part 1010 Subpart C; FinCEN Notice 2012-1]

Certain "United States persons" that maintain accounts (including any account where the person has a financial interest in, or signature or other authority over) in foreign jurisdictions and with aggregate balances exceeding \$10,000 are required to electronically file the Foreign Bank Account Report Form 114 with FinCEN on or before June 30th of each calendar year for accounts maintained during the previous calendar year. The FINOP is responsible for filing the annual report if it is required for CEI.

The filing requirement applies to:

- Non-resident aliens and foreign entities "in and doing business" in the U.S.
- All forms of U.S. business entities, trusts, estates with foreign accounts.
- U.S. citizens and residents with signature or other authority over a foreign account.
- Trust beneficiaries with a greater than 50% beneficial interest in a trust with a foreign account.
- U.S. citizens and resident stockholders with greater than 50% of the value or vote of the shares of a corporation with foreign accounts.
- Entities that are disregarded for tax purposes, such as limited liability companies.

The filing requirement does not apply to certain entities or situations. The regulation should be consulted for specific exemptions or conditions of exemptions.

- If the account is maintained in the United States, it is not considered a foreign account even if it holds foreign assets.
- An omnibus account held by a custody bank that holds assets both in the U.S. and outside the U.S. is not considered a foreign account unless the customer has direct access to its foreign holdings maintained at the foreign institution.
- Certain entities are excluded including: foreign hedge funds, venture capital funds, or private equity funds; tax-exempt investors that own offshore "blocker corporations;" government pension funds; pension plan participants and IRA owners (provided the trustee files a FBAR); investment advisers and employees of such advisers that provide advice to SEC-registered entities; remainder interests in trusts

and beneficiaries of discretionary trusts; employees of a U.S. or foreign entity that issued a class of foreign equity (including ADRs) registered with the SEC.

There also are exemptions for officers or employees with signature or other authority over certain foreign financial accounts but no financial interest in the reportable account. The regulation should be consulted for details regarding who is not required to notify FinCEN regarding signature or other authority over such an account.

29.9 Recordkeeping Requirements (Joint Rule and Travel Rule)

[Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart D]

In addition to maintaining records of reports filed with the IRS or other authorities, broker-dealers are obligated to maintain records of certain transactions, for potential inspection by regulators and other authorities. These records must be retained for five years.

29.9.1 Fund Transfers and Transmittals

[Bank Secrecy Act 31 CFR Chapter X Part 1010 Subpart D; FINRA Notice to Members 97-13, 96-67 and 95-69; SEC Q&As:

<http://www.sec.gov/about/offices/ocie/aml2007/fincen-advissu7.pdf>; SEC Q&As: <http://www.sec.gov/about/offices/ocie/aml2007/fincen-advsiiii.pdf>]

Broker-dealers are required to collect and retain information (such as name, address, account number of customer, date and amount of wire, payment instructions, name of recipient institution, and name and account information of wire payment recipient) and maintain records for domestic and international funds transfers (including wire fund transfers) of \$3,000 or more, with certain exceptions.

CEI (and its clearing firm or other third party, if applicable) is responsible for complying with the requirements to record information regarding fund transfers and, when required, verifying information regarding transmitters and recipients who are not established customers. Examples of verification information include:

- Name and address
- ID reviewed (type and number on the ID)
- Taxpayer ID number (or alien ID or passport number including country of issuance)
- Copy or record of method of payment (e.g., credit card, check)

29.9.2 Other Recordkeeping Requirements

[Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart D 1023.410]

The Bank Secrecy Act incorporates other records requirements that include records covered by *Books And Records* in the chapter *FINANCIAL AND OPERATIONS PROCEDURES*. CEI will retain all of the following required records:

1. Trading authorizations which are addressed in the chapter *ACCOUNTS*
2. Records under 17a-3 which are addressed in the chapter *FINANCIAL AND OPERATIONS PROCEDURES*
3. A record of each receipt of currency, other monetary instruments, checks, or investment securities and of each transfer of funds or credit, of more than \$10,000 received on any one occasion directly and not through a domestic financial institution, for any person, account or place outside the United States.

29.10 DVP/RVP Accounts

DVP/RVP accounts that use brokers to liquidate large volumes of low-priced securities may be a red flag for AML concerns. Such accounts should be the subject of reasonable inquiry to determine the source of the securities and

to identify potential money laundering and registration issues. CEI is responsible for AML inquiries unless there is a formal undertaking by the customer's prime broker.

29.11 Detecting Potential Money Laundering

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer • Other designated supervisor for review of AML Compliance Officer accounts
Resources	<ul style="list-style-type: none"> • Internal reports of transactions, available exception reports • WFCS AML Detection Software Alert System • WFCS Core AML Review Report
Frequency	<ul style="list-style-type: none"> • Monthly
Action	<ul style="list-style-type: none"> • Review reports of transactions (cash and security transactions) to identify potential money laundering (including associated person accounts) • Another designated supervisor will review the AML Compliance Officer's accounts • Report suspicious activity (see the policy in this chapter) • Notify RRs, supervisors, and close accounts when necessary
Record	<ul style="list-style-type: none"> • Reports reviewed • Action taken, when necessary • Suspicious activity reports

CEI has an ongoing program to identify potential money laundering. Monitoring will be conducted using available exception reports or review of a sufficient amount of account activity to permit identification of patterns of unusual size, volume, pattern or type of transactions, geographic factors such as whether jurisdictions designated as "non-cooperative" are involved or involve "red flags" (indicators of potential money laundering) which are included in the *Money Laundering* policy in the chapter *GENERAL EMPLOYEE POLICIES*. Items reviewed include trading and wire transfer transactions in the context of other account activity to determine if a transaction lacks financial sense or is suspicious because it is an unusual transaction or strategy for that customer. Among the information used to determine whether to file a suspicious activity report are exception or transaction reports that include transaction size, location, type, number, and nature of the activity.

Trading accounts will be identified and monitored where a series of financial transactions may help obscure the origins of the funds. This may include effecting securities transactions, closing the account, and transferring funds to a bank or other account, particularly to an offshore location. Trading penny stocks (which may involve unregistered distributions) or engaging in retail forex trading will, in particular, be monitored when they occur.

CEI has included an educational policy (*Money Laundering*) in the chapter *GENERAL EMPLOYEE POLICIES* to educate associated persons on money laundering and guidelines for detecting money laundering activities. Periodically detection of money laundering and the obligation to report suspicious activities will be included in continuing education and other educational programs for associated persons.

29.11.1 Clearing Firm AML Procedures/SAS Alert Program

CEI will work with the clearing firm to exchange information, records, data and exception reports as necessary to comply with AML laws. Required certifications for information sharing are on file. As a general matter, the

clearing firm will monitor CEI's customer activity, and the clearing firm will be provided with proper customer identification information as required to successfully monitor customer transactions.

CEI utilizes its clearing firm's AML detection software ("SAS") to assist in flagging and reviewing activity for AML compliance. The AML Compliance Officer reviews SAS at least monthly.

CEI's and the clearing firm's responsibilities are included in the clearing agreement and each firm is responsible for its own independent compliance with AML laws. CEI and the clearing firm cannot disclaim their respective responsibilities to comply with AML requirements.

29.11.2 Core AML Review

As part of CEI's AML program, the AML Compliance Officer will review the Core AML Review Report provided through Smart Station on at least a monthly basis:

In Smart Station Go To:

- Resources & Tools
- Resources & Tools Rpts
- Ops & Admin Rpts
- Core Brokerage Data/Shared Reports/Validated Reports/First Clearing/Activity
- **Run Activity – ACH Checks & Wires** Report for desired time period. Need not pick any other filters. This report pulls Wires, ACH, checks and money card checks.
 - Export to Excel (Dark grey ribbon at top, looks like a piece of paper with a grid in front)
 - Filter
 - Search states column to identify foreign activity if any
 - Review large transactions (>\$10,000) for suspicious activity
 - Sort by account name to group same-titled accounts to review high frequency transactions in same account(s)
 - Review other suspicious activity, e.g. layering multiple small deposits to evade systems, etc.
 - Store spreadsheet titled **YYYYDDMM_CoreAMLReview**
 - Log review by noting name of reviewer, date, and any action taken. Keep log with spreadsheets in Share File AML Folder

29.11.3 Foreign Currency Transactions

Foreign financial institutions may purchase U.S.-denominated bonds, generally issued by foreign governments, with the local currency, which are then transferred to a U.S. broker-dealer and sold, with proceeds then transferred offshore. U.S. broker-dealers act as intermediaries in these transactions and may receive foreign bonds or other securities worth millions of U. S. dollars without knowing who or how many underlying customers may be involved.

CEI prohibits the receipt of currency.

Nevertheless, if we discover currency has been received, we will file with the Commissioner of Customs within fifteen (15) days of

the transaction or, in the case of a filing resulting from a series of or multiple transactions, the last transaction a CMIR whenever the firm transports, mails, ships or receives or causes or attempts to transport, mail, ship or receive monetary instruments of more than \$10,000 at one time (on one calendar day or, if for the purpose of evading the reporting requirements, on one or more days) in or out of the U.S. We will file a CMIR for all such shipments or receipts of monetary instruments, except for currency or monetary instruments shipped or mailed through the postal service or by common carrier. We will, however, file a CMIR for such receipts of currency and monetary instruments and for shipments and deliveries made by the firm by means other than the postal service or common carrier, even when such shipment or transport is made by the firm to an office of the firm located outside the U.S. We will use the CMIR Form at: http://www.fincen.gov/forms/fin105_ctr.pdf

29.12 Information Sharing Between Financial Institutions

[USA PATRIOT Act Section 314(b); Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart E; Section 314(b) Fact Sheet: Section 314(b) Fact Sheet (fincen.gov)]

Under an AML regulation, financial institutions are permitted to share information regarding those suspected of terrorist or money laundering activities. Information sharing is not required but is permitted solely for the purpose of facilitating identification and reporting. The regulation provides immunity from other laws restricting information sharing if certification and confidentiality requirements of the regulation are satisfied.

Institutions that share information are required to provide FinCEN with annual certification that confirms, among other things, the name of the institution; that the institution will maintain adequate procedures to protect the security and confidentiality of the shared information; that the information will be used only for the authorized purpose; and the identity of a contact person at the institution.

CEI will share information about those suspected of terrorist financing and money laundering with other financial institutions for the purpose of identifying and reporting activities that may involve terrorist acts or money laundering activities and to determine whether to establish or maintain an account or engage in a transaction. The AML Compliance Officer will file the required certification with FinCEN and re-certify annually. All information will be treated as confidential and will be maintained in the AML Compliance Officer's files which may either be hard-copy files or password-protected electronic files.

In addition, the AML Officer will verify that any financial institution with which CEI shares information (including affiliates) has itself filed the requisite certification. A written letter or attestation will be required from the other financial institution and maintained in the AML Officer's files or a list provided by FinCEN will be consulted and a record made that the other institution has filed the required certification.

29.13 Suspicious Activity Reports (SARs)

[Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart B; USA PATRIOT Act Section 356; FINRA Notice to Members 02-47; FinCEN Guidance FIN-2008-Go05; FinCEN FAQs: Answers to Frequently Asked Questions Regarding Suspicious Activity Reporting and Other Anti-Money Laundering Considerations | FinCEN.gov; SEC Risk Alert 3/29/21: aml-risk-alert.pdf (sec.gov)]

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • Reports from associated persons of crimes or suspected crimes • Suspicious activities detected through ongoing reviews • Other available information

Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review and investigate suspicious transactions referred by associated persons • Determine whether CEI (or its clearing firm, if applicable) will file a SAR • If appropriate, file Form SAR-SF with FinCEN and state authorities • Notify senior management, as appropriate, of forms filed • Provide copy to parent company, if applicable • File SARs jointly with other financial institutions, if applicable
Record	<ul style="list-style-type: none"> • Notes and other documented reviews are retained in a suspicious activity file • Copies of SARs filed by CEI are retained in the SAR file with notation of when and to whom sent

CEI will file Suspicious Activity Reports (SARs) for transactions that may be indicative of money laundering activity. Suspicious activities include a wide range of questionable activities; examples include trading that constitutes a substantial portion of all trading for the day in a particular security; trading or journaling between/among accounts, particularly between related owners; late day trading; heavy trading in low-priced securities; unexplained wire transfers, including those to known tax havens; unusually large deposits of funds or securities. For business introduced to a clearing firm, CEI will utilize information and reporting from the clearing firm to conduct reviews in order to identify red flags and suspicious activity, and make filing determinations as appropriate.

29.13.1 Identifying Potential Suspicious Activity

CEI uses a number of tools to identify potential suspicious activity including:

- Transaction information including disbursement of funds or securities
- Education of firm personnel
- Associated person reports of potential suspicious activity forwarded to the AML Compliance Officer
- Information or alerts generated by the clearing firm's AML software for business introduced to a clearing firm:
 - On the 15th of each month, the clearing firm populates a report (WFC-SAS) which displays exceptions that meet certain parameters which could identify potential suspicious activity, which have occurred within the reporting period. The AML Compliance Officer analyzes each exception utilizing account notes and conversations with the Representative, if needed. The AML Compliance Officer makes notes on each exception and marks exceptions as "cleared" when resolved to his or her satisfaction. If necessary, additional actions as outlined in this document will be taken.
 - The AML Officer also runs and reviews the AML Core Compliance Report monthly report through Smart Station Core Data as set forth above in section 29.11.2.

29.13.2 When a Report Must Be Filed

A SAR must be filed for any transaction that, alone or in aggregate, involves at least \$5,000 in funds or other assets, if CEI knows, suspects, or has reason to suspect that the transaction (or a pattern of transactions of which the transaction is part) falls into one of the following categories:

- Transactions involving funds derived from illegal activity or intended or conducted to hide or disguise funds or assets derived from illegal activity.
- Transactions designed, whether through structuring or other means, to evade the requirements of the Bank Secrecy Act (BSA).
- Transactions that appear to serve no business or apparent lawful purpose or are not the sort of transactions in which a particular customer would be expected to engage, and for which CEI knows of no reasonable explanation after examining the available facts.
- Transactions that involve the use of CEI to facilitate criminal activity.

Excluded from the filing requirement are violations otherwise reported to law enforcement authorities such as:

- a robbery or burglary that is reported to law enforcement authorities
- lost, missing, counterfeit, or stolen securities reported pursuant to 17f-1
- a violation of federal securities laws or SRO rules by CEI, its officers, directors, employees, or RRs that are reported to the SEC or SRO, except for violations of Rule 17a-8 (filing of Currency and Transaction Reports) which must be reported on a SAR

29.13.3 Filing A Report and Emergency Notification

If CEI determines to file a SAR with FinCEN, the AML Compliance Officer will file:

- within 30 days of becoming aware of the suspicious transaction; or
- if no suspect has been identified within 30 calendar days of detection, reporting may be delayed an additional 30 calendar days or until a suspect has been identified, but no later than 60 days from date of initial detection.

In situations involving violations that require immediate attention (such as terrorist financing or ongoing money laundering schemes), the AML Compliance Officer will immediately notify by telephone an appropriate law enforcement agency. Suspicious transactions that may relate to terrorist activity may also be reported to FinCEN's Financial Institutions Hotline. In either event, a SAR will be filed.

29.13.3.1 Emergency Notification

[FINRA Notice to Members 02-21]

When conducting due diligence or opening an account, Federal authorities will be notified immediately by the AML Compliance Officer, when necessary, in the following situations:

- A legal or beneficial account holder or person is engaged in a transaction listed on or located in a country or region listed on the OFAC list.
- An account is held by an entity that is owned or controlled by a person or entity listed on the OFAC list.
- A customer tries to use bribery, coercion, or similar means to open an account or carry out a suspicious activity.
- There is reason to believe a customer is trying to move illicit cash out of the government's reach.
- There is reason to believe the customer is about to use funds to further an act of terrorism.

Emergency contacts include:

- OFAC Hotline (1-800-540-6322)
- Financial Institutions Hotline (1-866-556-3974)
- Local U.S. Attorney's office
- Local FBI office

- Local SEC office

29.13.4 Retention of Records

The AML Compliance Officer maintains a file of copies of SARs filed with FinCEN and all related documents for a period of 5 years from the filing date.

29.13.5 Providing SARs Information to SROs

[SEC letter to CEOs: <http://www.sec.gov/about/offices/ocie/brokerdealerletter.htm>]

While SARs are to be treated as confidential, CEI will provide SARs and supporting documentation available to any self-regulatory organization (SRO) that examines CEI for compliance with the SAR Rule. The request may be part of a routine examination, an investigation, or part of the SRO's risk assessment effort within its examination program.

29.13.6 Prohibition Against Disclosure

By statute and regulation, CEI may not inform customers or third parties that a transaction has been reported as suspicious. U.S. Treasury and Federal Reserve Board regulations also require CEI to decline to produce SARs in response to subpoenas and to report to FinCEN and the Federal Reserve Board the receipt of such requests and CEI's response. Failure to maintain the confidentiality of SARs may subject an associated person to civil and criminal penalties under Federal law. Violations may be enforced through civil penalties of up to \$100,000 for each violation and criminal penalties of up to \$250,000 and/or imprisonment not to exceed five years. CEI may also be liable for civil money penalties resulting from AML deficiencies that led to improper SAR disclosure up to \$25,000 per day for each day the violation continues.

Procedures to protect the confidentiality of SARs include the following:

- Access to SARs is limited to associated persons on a "need-to-know" basis
- SARs will be maintained in locked physical or electronic files
- SARs may not be left on desks or on open computer files and must be viewed without access by unauthorized persons
- SARs shared with others will be clearly marked "Confidential"

Compliance (or CEI's counsel) is responsible for responding to subpoena requests and Compliance will notify FinCEN and the Federal Reserve Bank of any subpoenas for SARs.

29.14 Requests and Written Notices from Regulators, Enforcement Agencies, and Other Authorized Persons

Under the Bank Secrecy Act, financial institutions are required to respond to federal banking agency requests for information relating to anti-money laundering compliance. The Rule requires provision of information and account documentation for any account opened, maintained, administered or managed in the U.S. The AML Compliance Officer maintains records of information provided in response to regulators' requests including the request, date of response, and information provided.

29.14.1 Federal Banking Agency Requests -- 120-Hour Rule

[USA PATRIOT Act Section 319(b)]

Upon receiving a request from a Federal banking agency, the AML Compliance Officer will provide the requested information within 5 days (120 hours) of receiving the request or will make available the information for inspection by the banking agency.

29.14.2 Information Sharing with Enforcement Agencies

[Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart E; USA PATRIOT Act Section 314]

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • Deposit records, purchase/sale records, account records, other records as required
Frequency	<ul style="list-style-type: none"> • Upon request
Action	<ul style="list-style-type: none"> • Conduct a search of the required records • If a match is found, submit the information to the requesting agency
Record	<ul style="list-style-type: none"> • Copies of the request, notation of records searched, and information submitted (if a match is found)

Enforcement agencies (FinCEN, state, local, and certain foreign law enforcement agencies eligible to make requests) send requests to financial institutions under Section 314 of the USA PATRIOT Act.

Requests for information will be forwarded to the AML Compliance Officer for response. CEI will respond to FinCEN's request by the due date, which is typically two weeks from the date of transmission. For FinCEN requests, the Subject Information Form (included with FinCEN's request) will be forwarded to FinCEN by electronic mail to sys314a@fincen.treas.gov or, if e-mail is not available, by fax at 703-905-3660.

Enforcement agency requests are confidential and may not be disclosed to the subject of the request. CEI will not use information provided to enforcement agencies for any purpose other than (1) to report to an agency as required under Section 314; (2) to determine whether to establish or maintain an account, or to engage in a transaction; or (3) to assist CEI in complying with any requirement of Section 314.

29.14.3 National Security Letters

[FinCEN SAR Activity Review, Trends, Tips & Issues, Issue 8 (National Security Letters and Suspicious Activity Reporting) (4/2005)]

National Security Letters (NSLs) are written investigative demands that may be issued by the local Federal Bureau of Investigation and other federal government authorities conducting counterintelligence and counterterrorism investigations to obtain, among other things, financial records of broker-dealers. **NSLs are highly confidential. CEI and its employees are barred from disclosing to any person that a government authority or the FBI has sought or obtained access to records.**

The AML Compliance Officer is responsible for responding to an NSL and maintaining the confidentiality of the letter and the response. If an SAR-SF is filed after receiving an NSL, the SAR-SF cannot make reference to the receipt or existence of an NSL. The SAR-SF will only contain detailed information about the facts and circumstances of the detected suspicious activity.

29.14.4 Grand Jury Subpoenas

[FinCEN SAR Activity Review, Trends, Tips & Issues, Issue 10 (Grand Jury Subpoenas and Suspicious Activity Reporting) (5/2006)]

The receipt of a grand jury subpoena concerning a customer does not in itself require the filing of a Suspicious Activity Report (SAR-SF). When a grand jury subpoena is received, the AML Compliance Officer will:

- Conduct a risk assessment of the customer subject to the subpoena as well as review the customer's account activity.
- If suspicious activity is identified during the risk assessment and review, the risk assessment will be elevated and an SAR-SF will be filed. The SAR-SF will not contain any reference to the receipt or existence of the subpoena. The SAR-SF will only contain detailed information about the facts and circumstances of the detected suspicious activity.

The existence of a subpoena and any response are confidential and may not be disclosed directly or indirectly to the person who is the subject of the subpoena. The AML Compliance Officer will maintain the subpoena and any response in a confidential file and will only share information with those authorized.

29.14.5 Foreign Bank Correspondent Accounts

[USA PATRIOT Act Section 313]

Upon receipt of a written request from a Federal law enforcement officer for information about a foreign bank correspondent account, the AML Compliance Officer will provide the requested information no later than 7 days after receipt of the request.

Compliance will terminate any correspondent relationship with a foreign bank within 10 business days of receiving a notice from the Treasury Dept. or the U.S. Attorney General that the foreign bank failed either to comply with a summons or subpoena or to contest it in a U.S. court.

29.14.6 Requests by Law Enforcement to Maintain Accounts

Law enforcement agencies may have an interest in having accounts remain open in spite of suspicious or potential criminal activity in connection with the account. The AML Compliance Officer will consider such requests and, if the account will remain open, require the federal law enforcement agency to provide a written request issued by a supervisory agent or by an attorney within the U.S. Attorney's Office or another office of the Department of Justice. If requested by a state or local law enforcement agency, the letter must be issued by a supervisor or local prosecutor's office.

The written request must include:

- the agency's request that the account remain open;
- the purpose of the request; and
- the duration of the request (not to exceed 6 months).

The request will be retained for 5 years.

If CEI is aware the account is under investigation (because of a subpoena, 314[a] request, National Security Letter, or similar communication), the requesting law enforcement agency will be advised before making a decision about the status of the account.

29.15 Accounts Requiring Approval by the AML Compliance Officer

The following accounts require review and approval by the AML Compliance Officer at the time of opening. The AML Compliance Officer may require additional information for these accounts.

- **Numbered accounts** (accounts designating a number rather than a name as the account name).
- **Any account requesting confidential handling** of its name, mailing of confirmation and statements, *etc.*
- **Accounts domiciled in high risk countries.** Accounts domiciled in countries identified by OFAC or the Financial Action Task Force on Money Laundering (FATF) as having inadequate anti-money laundering standards or representing high risk for crime and corruption.
- **Foreign public officials.** Includes individuals in high offices of foreign governments, political party officials and their families and close associates (if known and/or readily identifiable).
- **Correspondent and Private Banking accounts.** See the section *Due Diligence For Correspondent And Private Banking Accounts.*

29.16 Customer Identification Program (CIP)

[USA PATRIOT Act Section 326; Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart B; FINRA Notice to Members 03-34; FinCEN Frequently Asked Questions: <https://www.fincen.gov/resources/statutes-regulations/guidance/interagency-interpretive-guidance-customer-identification>; FinCEN No-Action position on CIP requirements under clearing arrangements: FIN-2008-G002; Guidance on Obtaining and Retaining Beneficial Ownership Information, FinCEN Guidance, FIN-2010-G001 March 5, 2010]

The opening of customer accounts is subject to customer identity verification requirements under CEI's Customer Identification Program (CIP). Requirements for associated persons opening accounts as explained in the chapter *ACCOUNTS* are duplicated in this section to consolidate all AML requirements within this chapter.

29.16.1 Definition of Customer Under CIP Rule

The definition of "customer" under the CIP rule is different than definitions under other rules. Who is a "customer" under this Rule affects CEI's obligations.

Under the CIP rule and for purposes of this section, "customer" is defined as:

- A person that opens a new account.
- An individual who opens a new account for:
 - An individual who lacks legal capacity; or
 - An entity that is not a legal person.

"Customer" does not include a financial institution regulated by a Federal regulator; a bank regulated by a state bank regulator; those exempted under Federal rule include municipalities; or a person with an existing account at CEI providing there is reasonable belief that the true identity of the person is known.

29.16.2 Accounts Opened by Other Financial Institutions

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • Other financial institution's CIP • Contract with other financial institution
Frequency	<ul style="list-style-type: none"> • Initially when an institution opens accounts and updated as needed - evaluate institution's CIP • Annual - obtain certification
Action	<ul style="list-style-type: none"> • Where required:

	<ul style="list-style-type: none"> ○ Confirm institution is subject to AML rules/requirements ○ Evaluate other institution's CIP ○ Contract with other institution regarding compliance with CEI's CIP requirements ○ Obtain annual certification
Record	<ul style="list-style-type: none"> ● Evaluation of other institution's CIP ● Contract with other financial institution ● Annual certifications from the financial institution

29.16.2.1 Financial Intermediaries as Customers Vs. Beneficial Owners

[Guidance from Dept. of Treasury and SEC regarding broker-dealer CIP rule: <http://www.sec.gov/divisions/marketreg/qa-bdidprogram.htm>]

Financial institutions (such as banks, clearing firms, investment advisers, *etc.*) act as intermediaries opening accounts including master and omnibus accounts. The SEC has stated that the underlying beneficial owners are **not** "customers" subject to CIP requirements under the following circumstances outlined in the SEC's guidance:

1. the omnibus account or relationship is established by or on behalf of a financial intermediary for the purpose of executing transactions that will clear or settle at another financial institution, or the omnibus account holder provides limited information to CEI solely for the purpose of delivering assets to the custody account of the beneficial owner at another financial institution;
2. the limited information given to CEI about the beneficial owner is used primarily to assist the financial intermediary with recordkeeping or to establish sub-accounts that hold positions for a limited duration to facilitate the transfer of assets to another financial institution;
3. all transactions in the omnibus account or sub-accounts at CEI are initiated by the financial intermediary; and
4. the beneficial owner has no direct control over the omnibus account or sub-accounts at the broker-dealer.

CEI is not obligated to look through the intermediary financial institution to the underlying beneficial owners if the intermediary identifies itself as the account holder. Even if CEI has some information about beneficial owners, the intermediary (not the beneficial owner) is treated as the customer for purposes of the CIP rule under these circumstances.

29.16.2.2 Reliance on Other Financial Institutions

[CIP Rule paragraph (b)(6)]

CEI may rely on another financial institution (such as a bank, clearing firm, another broker-dealer, *etc.*) to conduct CIP reviews with respect to dual customers of both CEI and the financial institution that is opening an account or has established an account or a similar business relationship between the customer and the other financial institution to provide or engage in services, dealings, or other financial transactions. CEI may rely on the other financial institution if the following conditions are met:

- Reliance on the other institution is reasonable (knowledge of the other institution's AML program);
- The other institution is subject to AML requirements; and
- The other institution enters into a contract with CEI requiring annual certification to CEI that it has implemented its AML program and will perform (or its agent perform) requirements of CEI's CIP.

29.16.2.3 Registered Investment Adviser Accounts

[SEC Division of Market Regulation No-Action Letter to SIFMA dated January 9, 2015: <http://www.sec.gov/divisions/marketreg/mr-noaction/2015/sifma-010915-17a8.pdf>]

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • New investment adviser accounts
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • For each SEC-registered adviser opening accounts with CEI where CEI will rely on the adviser for CIP compliance: <ul style="list-style-type: none"> ○ Conduct due diligence to review adviser including confirming adviser's SEC registration and update as needed ○ Obtain the adviser's written agreement to comply with CIP requirements ○ Obtain annual certification
Record	<ul style="list-style-type: none"> • Due diligence review • Written agreement of CIP compliance • Annual certifications

CEI may rely on an SEC-registered investment adviser to perform some or all of the CIP obligations related to customers where CEI and the investment adviser have a customer relationship, under the following conditions.

- it is reasonable to rely on the adviser's assurances;
- the investment adviser is a U.S. investment adviser registered with the SEC under the Investment Advisers Act of 1940; and
- the adviser enters into a written agreement with CEI in which the adviser agrees that:
 - it has implemented its own AML Program consistent with the requirements of 31 U.S.C. 5318(h) and will update such AML Program as necessary to implement changes in applicable laws and guidance;
 - it (or its agent) will perform the specified requirements of CEI's CIP in a manner consistent with Section 326 of the PATRIOT Act;
 - it will promptly disclose to the broker-dealer potentially suspicious or unusual activity detected as part of the CIP being performed on the broker-dealer's behalf in order to enable CEI to file a Suspicious Activity Report, as appropriate based on CEI's judgment;
 - it will certify annually to CEI that the representations in the reliance agreement remain accurate and that it is in compliance with such representations; and
 - it will promptly provide its books and records relating to its performance of CIP to the Commission, to an SRO that has jurisdiction over CEI, or to authorized law enforcement agencies, either directly or through CEI, at the request of (i) CEI, (ii) the SEC, (iii) an SRO that has jurisdiction over the broker-dealer or (iv) an authorized law enforcement agency.

29.16.3 Master Accounts and Sub-Accounts

[FINRA Regulatory Notice 10-18; SEC National Exam Risk Alert "Master/Sub-accounts:" <http://www.sec.gov/about/offices/ocie/riskalert-mastersubaccounts.pdf>]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
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Resources	<ul style="list-style-type: none"> • New master/sub-accounts
Frequency	<ul style="list-style-type: none"> • As required when master/sub-accounts are established
Action	<ul style="list-style-type: none"> • Except for those accounts meeting the requirements of the prior subsections regarding financial institution intermediaries, determine, where possible, sub-account ownership including whether persons associated with the master account customers are not themselves customers. Where sub-account holders directly effect transactions, subject the holders to CIP verification. • Conduct CIP reviews • Include master/sub-accounts in reviews of transactions to identify potential insider trading
Record	<ul style="list-style-type: none"> • Records of master and sub-account ownership (where applicable) • AML/CIP reviews • Review of transactions including record of action taken, if any

Accounts are sometimes established as "master accounts" that represent multiple sub-accounts. Depending on facts and circumstances (discussed below), master/sub-accounts may be recognized as separate customer accounts subject to CIP reviews.

29.16.3.1 Description of Master/Sub-Accounts

A master account may have multiple underlying accounts on behalf of underlying investors; sub-advisers may be authorized to effect transactions without the intermediation of the master account owner. Also, an individual or entity may set up sub-accounts for separate trading strategies or algorithms. Sub-accounts may be used by individual traders or groups of traders. The master account may be another broker-dealer or a partnership that provides its individual partners trading authority over separate sub-accounts.

29.16.3.2 Obligations to Conduct CIP Reviews

Except for accounts opened by investment advisers and financial institutions discussed under *Accounts Opened By Other Financial Institutions* and meeting the conditions of that section, when there are separate owners of the sub-accounts, CEI has an obligation to identify the beneficial owners. Indicators that there may be separate owners requiring CIP review of the sub-accounts include:

- The sub-account owner is entering orders for itself.
- CEI has actual notice the sub-accounts have different owners.
- The sub-accounts are separately documented and/or receive separate reports.
- The sub-accounts are addressed separately in terms of transaction, tax or other reporting.
- The services provided to the sub-accounts engender separate surveillance and supervision of the sub-accounts for compliance with rules or for risk management purposes consistent with the review of separately owned accounts.*
- There are financial arrangements or transactions with the sub-accounts, or separate account terms, that reasonably raise questions concerning whether such accounts represent separate beneficial owners.*
- The sub-accounts incur charges for commissions, clearance and similar expenses, separately, based upon the activity only of that subject sub-account.*

- There is evidence of financial transactions or transfers of assets or cash balances that would reasonably evidence separate beneficial ownership of the sub-accounts.*
- CEI (or RR) is aware of or has access to a master account or like agreement that evidences that the sub-accounts have different beneficial owners.
- There is evidence that a party maintaining a master/sub-account arrangement has interposed sub-accounts that have or are intended to have the effect of hiding the beneficial ownership interest.*
- The number of sub-accounts maintained is so numerous as to reasonably raise questions concerning whether such accounts represent separate beneficial owners.*

*Items above would not apply in the case of accounts opened by a registered BD or a bona fide investment adviser.

29.16.4 Customer Due Diligence

[USA PATRIOT Act Section 326; Bank Secrecy Act 31 CFR Chapter X Part 1010, Part 1020, Part 1023, Part 1024 and Part 1026; FinCEN 2016 FAQs: <https://www.ffiec.gov/press/pdf/Customer%20Due%20Diligence%20-%20Overview%20and%20Exam%20Procedures-FINAL.pdf>; FinCEN 2018 FAQs: <https://www.fincen.gov/resources/statutes-regulations/guidance/frequently-asked-questions-regarding-customer-due-o>; FINRA Rule 3310; FINRA Regulatory Notice 18-19 and 17-40]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New account application and other customer ID information
Frequency	<ul style="list-style-type: none"> • When accounts are opened
Action	<ul style="list-style-type: none"> • Before approving an account, determine that customer identification (ID) verification information is included with the new account application and meets CEI's requirements • Obtain beneficial ownership certifications from customers • For non-documentary verification, check the information included with the new account application for completeness and consistency with other customer-provided information (name, address, phone number, taxpayer ID number, etc.) • For unacceptable verification information (incomplete, inconsistent), return the application to the RR for further information or disapprove the account; if the account has been opened and non-documentary review is unacceptable, restrict the account to liquidating transactions only • Identify accounts where the Firm may rely on other financial institutions to satisfy CIP requirements and confirm eligibility to rely on exception • Obtain annual certification from other financial institutions • Include beneficial owners in AML monitoring
Record	<ul style="list-style-type: none"> • New account records include customer ID verification as well as the supervisor's approval and customer certifications • Identification and verification of reliance on other financial institutions • Annual certifications from other financial institutions

When opening new accounts, the customer's identity must be verified, as required by federal law. Customer identification (ID) information must be completed on the new account application. This includes, under FinCEN's requirements:

1. customer identification and verification;
2. beneficial ownership identification and certification;

3. understanding the nature and purpose of customer relationships; and
4. ongoing monitoring for reporting suspicious transactions and, on a risk basis maintaining and updating customer information.

Customer ID verification does NOT apply to accounts for:

- persons with an existing account at CEI (unless the account requires approval by the AML Compliance Officer)
- banks
- governmental entities
- issuers of listed equity securities
- other financial institutions subject to regulation by the SEC, CFTC, Federal Reserve Board, OCC, FDIC, Office of Thrift Supervision, or the National Credit Union Administration
- persons opening accounts to participate in an ERISA plan

29.16.4.1 Definitions

[Exchange Act Rule 17a-3(a)(17)(i)(A); FINRA Rule 4512]

The regulations should be consulted for more complete definitions.

Legal entity customer: corporation; limited liability company; another entity created by a public filing with a Secretary of State or equivalent; general partnership; limited partnership; business trust created through a state filing; or any similar entity formed under federal law. Does not include sole proprietorships, unincorporated associations, and natural persons opening their own account. Other exclusions are a federal- or state-regulated financial institution; political departments and agencies of the U.S. or a State; various different types of entities registered with the CFTC or SEC; and other entities included in the regulation.

Beneficial owner: any individual who (directly or indirectly) owns 25% or more of the equity of a legal entity customer; a single individual with ability to control, manage, or direct a legal entity (*e.g.*, CEO, CFO), or anyone else who regularly performs these functions. Does not include a nominee or straw man.

29.16.4.2 Required Customer Information

[Exchange Act Rule 17a-3(a)(17)(i)(A); FINRA Rule 4512]

Basic information required by law **prior to opening the account** includes:

- **Name**
- **Date of birth**, for an individual
- **Address:**
 - for an individual, residential or business street address. If no street address exists or is available, an APO or FPO box number or the residential or business street address of a next of kin or another contact individual
 - for a non-individual (corporation, trust, *etc.*) a principal place of business, local office, or other physical location.
- **Taxpayer identification number** for a U.S. person (U.S. citizen or non-individual established or organized under U.S. or state laws).
- **Identification number for non-U.S. person** which may include a taxpayer ID number; passport number and country of issuance; alien identification card number; or the number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photo or similar safeguard.

- **Beneficial owners** (see the section that follows) including information about the following:
 - the nature and purpose of customer relationships to develop a customer risk profile
 - information sufficient at the time of account opening so customer activity may be assessed for SAR requirements (may include type of customer requesting services; type of account being opened; services or products being used)

In the case of a customer who has applied for a taxpayer identification number but has not yet received it, notation must be made on the new account application that the taxpayer ID has been applied for. The account will be restricted to liquidating transactions if the taxpayer ID number is not received within 30 days of opening the account.

29.16.4.3 Accounts for Individuals

When opening an account for an individual, the following information is required:

When the Customer Appears in Person:

- An unexpired government-issued identification including a photo and nationality or residence such as a driver's license or passport. The associated person shall record information from it on the new account application and mark the application appropriately

If the customer has not appeared in person at a CEI branch or cannot produce the required photo ID, "non-documentary" information will be required, as explained in Section 7.16.4.11 below.

29.16.4.4 Obtaining and Retaining Beneficial Ownership Information

[SEC Release No. 34-61651: Policy Statement on Obtaining and Retaining Beneficial Ownership Information for Anti-Money Laundering Purposes]

For some accounts, beneficial owner information may not be immediately identified when an account is opened. Under AML requirements, firms have an obligation to identify and verify customer accounts and relationships and enhanced due diligence may be necessary depending on the risk profile of the account. Exceptions apply where the customer opening the account is subject to AML rules, such as registered investment advisers and registered broker-dealers.

General obligations when opening accounts that include underlying owners or beneficiaries include:

- Determining whether the customer is acting as an agent for or on behalf of another, and if so, obtaining information regarding the capacity in which and on whose behalf the customer is acting.
- Where the customer is a legal entity that is not publicly traded in the United States, such as an unincorporated association, a private investment company (PIC), trust or foundation, obtaining information about the structure or ownership of the entity so as to allow CEI to determine whether the account poses heightened risk.
- Where the customer is a trustee, obtaining information about the trust structure to allow CEI to establish a reasonable understanding of the trust structure and to determine the provider of funds and any persons or entities that have control over the funds or have the power to remove the trustees.

If CEI has affiliates with public customers, information may be shared across the enterprise to cross-check beneficial ownership information.

29.16.4.5 Beneficial Owners

Coastal Equities, Inc. is required to identify and verify the identity of the beneficial owners of all legal entity customers (defined above) when a new account is opened. Coastal Equities, Inc. may rely (if the reliance is reasonable) on beneficial ownership provided by a customer but must verify the identity of the beneficial owners. Coastal Equities, Inc. must also conduct "ongoing monitoring" on a risk basis to maintain and update customer information.

Customers must certify beneficial owners using First Clearing's Beneficial Owners form included in the account paperwork. For direct business, customers must complete FinCEN's Certification Form (or similar method developed by Coastal Equities, Inc.).

[Effective Date June 1, 2019] As part of Coastal Equities, Inc.'s monitoring for Suspicious Activity Reporting purposes, beneficial ownership must be considered. The customer's Control Person must complete the Risk Profile Questionnaire. The AML Officer will review the Questionnaire and assign a Risk Score, which will determine whether the account warrants additional review by the AML Officer on either a quarterly (Medium Risk) or monthly (High Risk) basis. The Risk Profile Questionnaire must be completed for all new accounts owned by legal entity customers upon account opening or promptly thereafter. If the Questionnaire is not completed, the account will not be opened, or if already opened, will be restricted until which time that Questionnaire is received in good order by the AML Officer.

Beneficial owner information will be retained for five years from the date of account closing.

29.16.4.6 Enhanced Due Diligence (EDD)

Some types of accounts, because of the potential risk for hiding the identity of underlying beneficial owners or money laundering activities, are subject to enhanced due diligence. The AML Compliance Officer will determine which accounts are subject to EDD and what reviews are necessary. Procedures for correspondent and private banking accounts are included in a separate section of this AML program. Certain trusts, corporate entities, shell entities, and private investment companies are examples of customers that may pose heightened risk.

EDD may include steps, in accordance with the level of risk presented, to identify and verify beneficial owners, to reasonably understand the sources and uses of funds in the account, and to reasonably understand the relationship between the customer and the beneficial owner. EDD information may be used for monitoring purposes and to determine whether there are discrepancies between information obtained regarding the account's intended purpose and expected account activity and the actual sources of funds and uses of the account.

29.16.4.7 Third Party Accounts

Customer ID required for third party accounts includes the following:

On behalf of an incompetent person: Obtain customer ID of the person holding power of attorney.

With power of attorney or trading authorization held by a third party: Obtain customer ID of the owner of the account. Customer ID is not necessary for the individual with authority over the account unless that person is unfamiliar to the RR or the circumstances regarding the opening of the account raises questions (customer requires wiring funds to an offshore address; third party is a foreign citizen; *etc.*).

29.16.4.8 Reliance on Other Financial Institutions

[C.F.R. 1023.220(a)(6)]

Although CEI does not currently rely upon others for CIP purposes, it may in the future rely for CIP purposes upon another financial institution (including an affiliate) that opens a customer account provided that:

- reliance is reasonable under the circumstances;
- the other financial institution is subject to anti-money laundering requirements [U.S.C. 5318(h)] and is regulated by a Federal regulator; and
- the other financial institution enters into a contract requiring it to annually certify that it has implemented its AML program and it will perform (or its agent) specified requirements of Coastal Equities, Inc.'s CIP.

29.16.4.9 Intermediated Account Relationships

[Various guidance from the U.S. Treasury and SEC regarding mutual fund CIP rule, BD CIP rule, FAQs regarding FCMs and introducing brokers, and foreign accounts]

If an intermediary is the customer and Coastal Equities, Inc. has no CIP obligation regarding the intermediary's underlying customers under existing guidance, Coastal Equities, Inc. will treat the intermediary as its legal entity customer. For example, the intermediary may be treated as the customer for transactions through omnibus accounts if:

- the omnibus account was established to execute transactions for settlement at another institution or the intermediary provides limited customer information to Coastal Equities, Inc.;
- the limited information provided is used primarily for recordkeeping purposes or to establish sub-accounts that hold positions for limited durations;
- all transactions in the omnibus account are initiated by the intermediary; and
- the beneficial ownership has no direct control over the omnibus account.

29.16.4.10 Accounts for Non-Individuals

Account documents usually obtained for non-individual accounts (trust instruments, articles of incorporation, partnership agreements, government-issued business license, *etc.*) will usually satisfy customer ID requirements. In the case of corporations, a certified copy of the articles of incorporation is required. These documents must be obtained within 30 days of account opening to satisfy the requirement.

29.16.4.11 Non-Documentary Methods of Verifying Customer Identification

Coastal Equities uses information from a consumer reporting agency to verify the identity of new customer accounts using the non-documentary method, at the time of account opening,

Non-documentary methods must be used in the following circumstances:

- An individual is unable to present acceptable photo ID.
- The documents presented are unfamiliar.
- The account is opened without obtaining documents.
- The customer opens the account without appearing in person at CEI.
- Other circumstances, at the discretion of the RR's supervisor, New Accounts, and/or the AML Compliance Officer, where CEI is unable to verify the customer's identity.

In the event that a customer's identity cannot be verified using documentary evidence or information from a consumer reporting agency, Coastal may rely on one or more of the following:

- Direct customer contact information
- References from another financial institution
- Obtained a financial statement

29.16.4.12 Additional Verification for Certain Customers

For the following types of customers, a minimum of TWO forms of customer ID are required in addition to review and approval by the AML Compliance Officer **prior to** opening the account:

- Numbered accounts
- Accounts domiciled in high-risk countries included on the Treasury Dept. OFAC list (check with Operations personnel for a list of those countries or go to <http://www.treas.gov/offices/enforcement/lists/>)
- Accounts for foreign public officials (individuals in high office in other countries, their families and close associates, political party officials)

29.16.4.13 Lack of Customer ID Verification

For **accounts where non-documentary verification results in substantive, unresolved discrepancies** (information that is inconsistent such as name, address, taxpayer ID number, *etc.*), the customer will be required to provide documentary evidence to resolve those discrepancies. If any discrepancies remain outstanding 30 days after account opening, the account will be restricted to liquidating transactions only until those discrepancies are resolved.

Where inability to verify raises questions about the customer, filing a Suspicious Activity Report will be considered (see the section *Suspicious Activity Reports*).

Questions regarding accounts that do not comply with requirements to verify customer ID should be referred to the AML Compliance Officer.

29.16.4.14 Customer Notice

Customers are provided notice, prior to opening an account, that their identification will be verified. This notice may be on CEI's web site, on new account applications, or in other disclosures provided at the time of account opening.

29.16.5 CIP Records

Customer identification verification records are retained with new account application records in accordance with rule recordkeeping requirements and the terms of the other financial institution's CIP including:

- all identifying information recorded on the new account application
- documentary verification including information from or copies of government-issued IDs or passports
- non-documentary verification
- account approval or disapproval
- resolution of discrepancies
- referral of the account to the AML Compliance Officer
- closing of an account that fails to meet CIP requirements
- other records as may be required

Records are retained for at least 5 years after the account is closed.

29.16.6 Comparison with Government Lists

As required by law, CEI compares customer information against government lists. The section *OFAC List And Blocked Property* in the Anti-Money Laundering Program describes comparison of accounts with lists published by the Treasury Dept.

29.17 Identity Theft Prevention Program (Red Flags Rule)

[Exchange Act Regulation S-ID; Fair and Accurate Credit Transactions Act (FACT Act) Section 114 and 315; FINRA Regulatory Notice 19-18; FINRA Red Flags Rule web site: <https://www.finra.org/rules-guidance/key-topics/customer-information-protection/ftc-red-flags-rule>; Interagency Guidelines on Identity Theft Detection, Prevention, and Mitigation: <http://www.govcollect.org/files/Appendix%20A%20to%20Part%20681.pdf>]

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • New account information • Order records • Transaction information about cash or security transfers • Information reported by associated persons • Information from third party providers, customers, victims of identity theft, law enforcement agencies or others about potential identity theft
Frequency	<ul style="list-style-type: none"> • When new accounts are opened • When account addresses are changed • Ongoing - review of order records and transaction information • As received - associated person information • As required - when a third party is engaged, confirm third party providers (including clearing firms) have identity theft program procedures which may be included in an affirmation in the third party's contract with CEI • Annually - review of controls and procedures • As required - provide revised procedures to the Board, Board committee, or CEO • Annually - report to CEO • Annually (or more frequently) - provide training for associated persons
Action	<ul style="list-style-type: none"> • Establish and maintain the Identity Theft Program <ul style="list-style-type: none"> ○ Provide initial Program and subsequent material changes to the Board, a Board Committee or CEO (if no Board exists) for review and approval ○ Review controls and procedures annually as part of the annual testing described in the chapter <i>SUPERVISORY SYSTEM, PROCEDURES AND CONTROLS</i> • Conduct reviews of orders and transactions to identify red flags • When red flags are identified, take corrective action which may include: <ul style="list-style-type: none"> ○ Consultation with the RR and/or supervisor ○ Monitoring the account ○ Contacting the customer ○ Changing passwords, security codes, or other security devices that permit access to an account ○ Reopening an account with another account number ○ Not opening a new account ○ Closing an existing account ○ Filing a Suspicious Activity Report ○ Notifying law enforcement ○ Taking no action if warranted

	<ul style="list-style-type: none"> • Conduct other reviews which may include: <ul style="list-style-type: none"> ○ Periodic use of internet search engines to identify web sites using CEI's or an RR's name ○ Review online advertising to identify web sites for unauthorized links to promote stock fraud or that appear to be illegitimate • If CEI's or an RR's identity is being used in a scam, take action which may include notifying regulators and the FBI, lodging a complaint at www.ftc.gov, and if it involves email solicitation or spoofing, forwarding email to spam@uce.gov • If a customer's account has been compromised, take action (described in a section that follows) • Include Identity Theft Prevention Program in the annual report to CEO (see the chapter <i>SUPERVISORY SYSTEM, PROCEDURES AND CONTROLS</i>), reporting: <ul style="list-style-type: none"> ○ Effectiveness of the policies and procedures in addressing the risk of identity theft ○ Third party provider arrangements ○ Significant incidents involving identity theft and management's response ○ Recommendations for material changes to the Program • Review third party providers (including clearing firms) for adequacy of identity theft programs <ul style="list-style-type: none"> ○ Contractually require them to have policies and procedures to detect Red Flags included in firm policies and report them to CEI and/or take appropriate steps of their own to prevent/mitigate identity theft • Send confirmation of address change to the customer's old address when a change of address is made (see the section <i>Change Of Addresses On Accounts</i> in the chapter <i>FINANCIAL AND OPERATIONS PROCEDURES</i>) • Training: <ul style="list-style-type: none"> ○ Include identity theft in AML training ○ Develop training, identify target associated persons, and administer training
Record	<ul style="list-style-type: none"> • Policies and procedures and revisions • Reviews of orders and transactions with record of action taken • Red flags identified and record of action taken • Annual testing of procedures (see <i>SUPERVISORY SYSTEM, PROCEDURES AND CONTROLS</i>) • Annual report to CEO (see <i>SUPERVISORY SYSTEM, PROCEDURES AND CONTROLS</i>) • Confirmation that third party providers (including clearing firms) have adequate ITPPs and include in the contracts with third parties • Records of training including subjects included, date, who administered and who attended

29.17.1 Introduction

Under Regulation S-ID, financial institutions with "covered accounts" are required to establish an Identity Theft Prevention Program (ITPP) to prevent, detect, and act on the theft of customers' identity. "Covered accounts" include accounts for individuals (vs. institutions) and accounts where credit is extended. Because CEI has individuals as customers or it offers credit to customers, CEI is subject to the FACT Act requirements.

CEI has established an ITPP which incorporates the Customer Identification Program as a tool for recognizing identity theft. Related policies and procedures include the responsibilities of all associated persons (and designated supervisors, in particular) as listed below. The chapter is in upper case and the section is in lower case.

- *GENERAL EMPLOYEE POLICIES - Money Laundering*
- *GENERAL EMPLOYEE POLICIES - Identity Theft*
- *COMMUNICATIONS WITH THE PUBLIC - Customer Privacy Policies And Procedures*
- *FINANCIAL AND OPERATIONS PROCEDURES - Risk Management - Firm Computers And Computerized Data*
- *ANTI-MONEY LAUNDERING (AML) PROGRAM - Customer Identification Program (CIP)*
- *ACCOUNTS - Customer Account Information*
- *ACCOUNTS - Identity Theft*

29.17.2 Establishment, Administration, and Updates of the ITPP

The Board or a Board committee (or CEO if no Board exists) has approved the ITPP and receives updates from the AML Compliance Officer. The ITPP will be included in the annual report to the CEO (see the chapter *SUPERVISORY SYSTEM, PROCEDURES AND CONTROL* and the section *Annual Report to CEO*).

The AML Compliance Officer is responsible for:

- Establishing the program and obtaining Board, Board committee, or CEO approval
- Updating the program when necessary and communicating changes to appropriate personnel including the Board/CEO
- Administering the program including:
 - identifying supervisors' responsibilities and communicating those responsibilities to respective supervisors
 - monitoring regulatory changes and industry trends
- Establishing training for supervisors and RRs
- Maintaining records of the ITPP and any updates
- Maintaining records of training or delegation of training to supervisors; records include subjects covered, who administered the training, date of training, and who attended

29.17.3 Red Flags

The ITPP is based on identifying "red flags" that indicate identity theft may have occurred. This section describes CEI's methods of identifying red flags and responding to them. Regulators have identified red flags as potential indicators of identity theft. All of the red flags may not apply to CEI because of the nature of its business and types of customers. The following section identifies red flags, how they are detected, and potential action when red flags are identified.

The following factors were considered in establishing the ITPP and are assessed in annual reviews of the program in determining identity theft risks at CEI:

- Types of accounts offered by CEI
- Methods to open and access accounts
- Prior experience with identity theft
- Regulatory/industry releases and industry experience with identity theft
- Technology/reports available to identify red flags
- Use of third parties (including clearing firms) for processing accounts and/or transactions

- Sources of red flags including: reports from credit agencies; suspicious documents; suspicious personal identifying information; suspicious account activity; and notice from other sources, including the customer himself/herself

This list is not intended to be an exhaustive or mandatory list of items but provides guidelines for where risks may appear. Some areas may not be relevant to CEI's business at a particular time.

29.17.4 Identifying and Responding to Red Flags

The following chart identifies identity theft red flags and potential responses which depend on the nature and seriousness of the red flags.

Red Flag	Action
Category: Alerts, Notifications or Warnings from a Consumer Credit Reporting Agency	
1. A fraud or active duty alert is included on a consumer credit report.	Verify that the fraud or active duty alert covers an applicant or customer and review the allegations in the alert.
2. A notice of credit freeze is given in response to a request for a consumer credit report.	Verify that the credit freeze covers an applicant or customer and review the freeze.
3. A notice of address or other discrepancy is provided by a consumer credit reporting agency.	Verify that the notice of address or other discrepancy covers an applicant or customer and review the address discrepancy.
4. A consumer credit report shows a pattern inconsistent with the person's history, such as a big increase in the volume of inquiries or use of credit, especially on new accounts; an unusual number of recently established credit relationships; or an account closed because of an abuse of account privileges.	Verify that the consumer credit report covers an applicant or customer, and review the degree of inconsistency with prior history.
Category: Suspicious Documents	
5. Identification presented looks altered or forged.	Scrutinize identification presented in person to make sure it is not altered or forged.
6. The identification presenter does not look like the identification's photograph or physical description.	Determine that the photograph and the physical description on the identification match the person presenting it.
7. Information on the identification differs from what the identification presenter is saying.	Determine that the identification and the statements of the person presenting it are consistent.
8. Information on the identification does not match other information our firm has on file for the presenter, like the original account application, signature card or a recent check.	Determine that the identification presented and other information we have on file from the account are consistent.
9. The application looks like it has been altered, forged or torn up and reassembled.	Scrutinize each application to identify alterations or forgery (for example, a form that has been cut up and reassembled).

Category: Suspicious Personal Identifying Information	
10. Inconsistencies exist between the information presented and other things we know about the presenter or can find out by checking readily available external sources, such as an address that does not match a consumer credit report, or the Social Security Number (SSN) has not been issued or is listed on the Social Security Administration's (SSA's) Death Master File.	Check personal identifying information to determine that the SSN given has been issued but is not listed on the SSA's Master Death File. If we receive a consumer credit report, check to see if the addresses on the application and the consumer report match.
11. Inconsistencies exist in the information that the customer gives us, such as a date of birth that does not fall within the number range on the SSA's issuance tables.	Check personal identifying information to confirm that it is internally consistent by comparing the date of birth to see that it falls within the number range on the SSA's issuance tables.
12. Personal identifying information presented has been used on an account our firm knows was fraudulent.	Compare the information presented with addresses and phone numbers on accounts or applications that were reported to be fraudulent.
13. Personal identifying information presented suggests fraud, such as an address that is fictitious, a mail drop, or a prison; or a phone number is invalid, or is for a pager or answering service.	Validate the information presented when opening an account by looking up addresses on the Internet to ensure they are real and not for a mail drop or a prison; call the phone numbers given to ensure they are valid and not for pagers or answering services.
14. The SSN presented was used by someone else opening an account or other customers.	Compare the SSNs presented to see if they were given by others opening accounts or other customers.
15. The address or telephone number presented has been used by many other people opening accounts or other customers.	Compare address and telephone number information to see if they were used by other applicants and customers.
16. A person who omits required information on an application or other form does not provide it when told it is incomplete.	Track when applicants or customers have not responded to requests for required information and follow up with the applicants or customers to determine why they have not responded.
17. Inconsistencies exist between what is presented and what our firm has on file.	Verify key items from the data presented with information we have on file.
18. A person making an account application or seeking access cannot provide authenticating information beyond what would be found in a wallet or consumer credit report, or cannot answer a challenge question.	Authenticate identities for existing customers by asking challenge questions that have been prearranged with the customer and for applicants or customers by asking questions that require information beyond what is readily available from a wallet or a consumer credit report.
Category: Suspicious Account Activity	
19. Soon after CEI gets a change of address request for an account, we are asked to add additional access	Operations (or the clearing firm) verifies change of address requests by sending a notice of the change to

means (such as debit cards or checks) or authorized users for the account.	both the new and old addresses so the customer will learn of any unauthorized changes and can notify CEI.
20. A new account exhibits fraud patterns, such as where a first payment is not made or only the first payment is made, or the use of credit for cash advances and securities easily converted into cash.	Review new account activity to ensure that first and subsequent payments are made, and that credit is primarily used for other than cash advances and securities easily converted into cash.
21. An account develops new patterns of activity, such as nonpayment inconsistent with prior history, a material increase in credit use, or a material change in spending or electronic fund transfers.	Review accounts on at least a monthly basis and check for suspicious new patterns of activity such as nonpayment, a large increase in credit use, or a big change in spending or electronic fund transfers.
22. An account that is inactive for a long time is suddenly used again.	Review our accounts on at least a monthly basis to see if long inactive accounts become very active.
23. Mail CEI sends to a customer is returned repeatedly as undeliverable even though the account remains active.	Note any returned mail for an account and immediately check the account's activity.
24. We learn that a customer is not getting his or her paper account statements.	Record on the account any report that the customer is not receiving paper statements and immediately investigate them.
25. We are notified that there are unauthorized charges or transactions to the account.	Verify if the notification is legitimate and involves a firm account, and then investigate the report.
26. We receive an email that purports to be from the customer but there are misspellings, improper grammar or other red flags that the customer did not send the email. (Phishing)	Contact the client at the phone number of record, in person, or by other reliable means to confirm that the email is genuine.
Category: Notice From Other Sources	
27. An outside agency, law enforcement, a clearing firm, or other source notifies CEI that an account has been opened or used fraudulently.	Verify that the notification is legitimate and involves a firm account, and then investigate the report.
28. CEI is notified of potential unauthorized access to customer personal information due to data loss from an outside provider or a breach of an outside provider's data.	In consultation with the outside provider, determine the extent of the loss of data or breach of the provider's systems and determine action to be taken which may include notification of customers and notification of regulatory authorities including states depending on state requirements.
29. Notice from a customer of the loss of information (e.g., loss of wallet, birth certificate, etc.).	Contact the customer to learn the details of the unauthorized access to determine if other steps are warranted.

29.17.5 Compromised Accounts

[FINRA Checklist for Compromised Accounts: <https://www.finra.org/rules-guidance/key-topics/customer-information-protection/firm-checklist-compromised-accounts>]

If an unauthorized person may have gained entry or attempted entry to a customer's account, the AML Compliance Officer will take the following actions, depending on the nature and scope of the intrusion.

- Monitor, limit, or temporarily suspend activity in the account
- Contact the customer using CIP information on file for him/her, describe what has been found, and verify that there has been an attempted or actual identity theft
- Determine if there is a heightened risk of ease of access such as a customer's lost wallet, mail theft, a data security incident, or the customer gave account information to an imposter claiming to represent CEI or the customer gave information to a fraudulent web site
- Check similar accounts where there may be unauthorized access
- Collect incident information including (if available):
 - Firm information (both introducing and clearing firms: firm name, CRD number, contact name and telephone number)
 - Dates and times of activity
 - Securities involved (name and symbol)
 - Details of trades or unexecuted orders
 - Details of wire transfer activity
 - Customer accounts affected by the activity including name and account number
 - Whether the customer will be reimbursed and by whom
- Alert other appropriate firm personnel to be aware of unusual activity in other customer accounts and notify the AML Compliance Officer of any such incidences
- Identify, to the extent possible, the cause of the account intrusion (*i.e.*, the firm's system was compromised; individual account was hacked); whether the customer has been subject to identity theft; whether intrusion is limited to one account or whether it involves multiple accounts
- Notify clearing firm, if applicable
- Contact the SEC, FINRA, and state regulators
- If appropriate, contact law enforcement such as the FBI or the U.S. Postal Inspector, if mail is involved
- Determine whether CEI must provide a specific type of notification to the customer or others under state law
- Determine whether a SAR should be filed
- Review CEI's insurance policy which may require timely notice or prior consent for any settlement
- Provide customer assistance to minimize the impact of potential or actual identity theft, as applicable and determined by the AML Compliance Officer:
 - Consider changing passwords, security codes or other ways to access threatened accounts
 - Offer to close the account and reopen with a new account number
 - Consider not collecting on the account or selling it to a debt collector
 - Advise the customer to go to the FTC Identity Theft Web Site (<http://www.ftc.gov/bcp/edu/microsites/idtheft>); calling the FTC's Identity Theft Hotline (877-438-4338); or writing the Identity Theft Clearinghouse (FTC, 6000 Pennsylvania Avenue, NW, Washington, D.C. 20580)

29.18 Due Diligence for Correspondent and Private Banking Accounts

[Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart F; USA PATRIOT Act Section 312 and 313]

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • New account application • Foreign bank certification

	<ul style="list-style-type: none"> Information about a foreign bank subsequent to opening that indicates it is a foreign shell bank where an account may not be maintained
Frequency	<ul style="list-style-type: none"> As required when accounts are opened Monthly - review of accounts identified for due diligence reviews
Action	<ul style="list-style-type: none"> Conduct due diligence for correspondent and private banking accounts Review selected accounts for potential money laundering activity and, if potential activities are identified, take corrective action which may include: <ul style="list-style-type: none"> Restricting activity in the account Closing the account Filing an SAR For foreign bank accounts: <ul style="list-style-type: none"> Review certification to determine: <ul style="list-style-type: none"> All required information is included Inconsistencies (<i>i.e.</i>, location of the foreign bank's regulated affiliate is consistent with the designated banking authority that supervises the foreign bank and its regulated affiliate) Ensure procedures are in place to restrict transactions in accounts that do not provide certification within 30 days of opening the account Close existing prohibited accounts for foreign shell banks Review re-certifications Ensure procedures are in place to re-certify foreign banks within three years of original certification
Record	<ul style="list-style-type: none"> Record of the AML Officer's review is maintained in new account records on the applicable form: <ul style="list-style-type: none"> New account application Certification form Re-certification form Records of account reviews including corrective action taken Records of closing or restricting accounts are retained with new account records

Due diligence requirements apply when opening and handling correspondent and private banking accounts that are maintained in the U.S. for non-U.S. persons. "Enhanced due diligence" is required for:

- Correspondent accounts for foreign banks in jurisdictions of money laundering concern or operating under an off-shore license
- Private banking accounts for senior foreign political figures

The purpose of these requirements is to detect and report known or suspected money laundering activity.

29.18.1 Definitions

Correspondent account: Includes any account established for a foreign financial institution to receive deposits from, or to make payments or other disbursements on behalf of, the foreign institution, or to handle other financial transactions related to such foreign financial institution. This type of account presumes a formal relationship through which the financial institution provides regular services.

Private banking account: A private banking account is an account that is established or maintained for the benefit of one or more non-U.S. persons, requires minimum aggregate deposit of funds or other assets of not less than \$1,000,000, and is assigned to a bank employee who is a liaison between the financial institution and the non-U.S. person. If the account otherwise satisfies the definition but the institution does **not** require a minimum balance of \$1,000,000, the account does not qualify as a private banking account.

Senior foreign political figure ("politically exposed person") includes:

- a current or former senior official in the executive, legislative, administrative, military, or judicial branches of a foreign government, whether or not they are or were elected officials
- a senior official of a major foreign political party
- a senior executive of a foreign government-owned commercial enterprise (Senior executives are individuals with substantial authority over policy, operations, or the use of government-owned resources.)
- immediate family members of the above, and those who are widely and publicly known (or actually known) close associates of a senior foreign political figure
- a corporation, business, or other entity formed by or for the benefit of one of the above individuals
- a person "widely and publicly known" as a close associate of such a person

Proceeds of foreign corruption: any asset acquired by, through, or on behalf of a senior foreign political figure through misappropriation, theft, or embezzlement of public funds, the unlawful conversion of property of a foreign government, or through acts of bribery or extortion, and include any other property into which any such assets have been transformed or converted.

Foreign bank: defined under the Bank Secrecy Act as a bank organized under foreign law, or an agency, branch, or bank office located outside the United States. The term does not include an agent, agency, branch or office within the U.S. of a bank organized under foreign law.

Foreign shell bank: a foreign bank without a physical presence in any country.

"Owner" of a foreign bank for purposes of enhanced due diligence: Any person who directly or indirectly owns, controls, or has the power to vote 10% or more of any class of securities of the bank.

Payable-through account: A correspondent account maintained by a covered financial institution for a foreign bank by means of which the foreign bank permits its customers to engage, either directly or through a subaccount, in banking activities usual in connection with the business of banking in the U.S.

Regulated affiliate: a foreign shell bank that (1) is an affiliate of a depository institution, credit union, or foreign bank that maintains a physical presence in the United States or a foreign country, as applicable; and (2) is subject to supervision by a banking authority in the foreign country regulating such affiliated depository institution, credit union, or foreign bank.

29.18.2 Due Diligence for Correspondent Accounts for Foreign Financial Institutions

Due diligence requirements apply to the following types of foreign financial institutions:

- Foreign bank
- Foreign branch of a U.S. Bank
- A business organized under a foreign law that, if located in the U.S., would be a securities broker-dealer, futures commission merchant, introducing broker in commodities, or a mutual fund
- A money transmitter or currency exchanger organized under foreign law

The Dept. of Treasury has established the following minimum due diligence requirements:

- determine whether the account is subject to enhanced due diligence
- assess the money laundering risk posed, based on risk factors. Potential risk factors include:
 - the nature of the foreign financial institution's business and the markets it serves
 - the type, purpose, and anticipated activity of the correspondent account
 - the nature and duration of CEI's relationship with the foreign financial institution
 - the AML and supervisory regime in which the foreign financial institution is chartered or licensed
 - information known or reasonably available to CEI about the foreign financial institution's AML record
- apply risk-based policies, procedures and controls to each account, including periodic review of activity

Factors considered in determining due diligence include:

- nature of services provided to the account
- length of relationship
- the AML supervisory regime in the account's home country
- any information known or reasonably available about the account's AML record

Due diligence procedures include the following:

Correspondent accounts for foreign financial institutions are forwarded to the AML Compliance Officer, at the time of opening, for review.

- Review the account's home country vs. OFAC lists of jurisdictions of money laundering concern and blocked persons.
 - If identified on an OFAC list, report the account and close it.
- Review new account information about the account including source of revenue and assets, whether the person/entity has existing accounts with CEI, length of time the RR has known the account, who referred the account, and other available information about account background and how the account came to CEI.
- Conduct a risk-based assessment considering factors listed above.
- If there is inadequate information or due diligence procedures cannot be performed, refuse to open the account or close an existing account.
 - File a SAR, if appropriate.
- If the account is approved for opening, determine whether ongoing review is necessary.
 - If ongoing review is appropriate, establish duplicate statements or another method for review of account activity by the AML Officer.
 - Review will include identifying patterns of securities transactions and securities/money transfers that may be indicative of money laundering activity, and report such activity if necessary and close the account.

29.18.2.1 Enhanced Due Diligence for Some Foreign Banks

Enhanced due diligence is required for a correspondent account for a foreign bank that is operating:

- under an offshore license;
- under a license issued by a country that has been designated as being non-cooperative with international anti-money laundering principles or procedures by an intergovernmental group or organization of which the U.S. is a member and with which the U.S. concurs regarding the designation; or
- under a license issued by a country designated by the Secretary of the Treasury as warranting special measures due to money laundering concerns.

Such accounts are subject to risk-based enhanced due diligence, including the following:

- Compliance is responsible for identifying and monitoring such accounts.
- If the bank's shares are not publicly traded, identify the owners of the bank and verify they do not appear on U.S. lists of restricted individuals or companies.
- Obtain and consider information about the bank's AML program to assess money laundering risk.
- Obtain information from the bank about the identity of any person with authority to direct transactions through any correspondent account that is a payable-through account and the sources and beneficial owner of funds or other assets in the payable-through account.
- Determine whether the foreign bank for which the correspondent account is established or maintained in turn maintains correspondent accounts for other foreign banks that use the foreign correspondent account established or maintained by CEI and, if so, take reasonable steps to obtain information relevant to assess and mitigate money laundering risks associated with the foreign bank's correspondent accounts for other foreign banks, including, as appropriate, the identity of those foreign banks.
- Monitor such accounts for potential money laundering, either manually or electronically depending on available information.
- Report the account, upon initial review or in the course of monitoring, if necessary.

If enhanced due diligence cannot be performed, the account will be not be opened, trading will be suspended, a suspicious activity report will be filed, and/or the account will be closed.

29.18.2.2 Prohibition Against Correspondent Accounts for Foreign Shell Banks

[Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart F; USA PATRIOT Act Section 313]

CEI is prohibited from establishing, maintaining, administering, or managing a correspondent account in the United States for an unregulated foreign shell bank. The prohibition does not apply to a foreign shell bank that is a regulated affiliate. If an account is inadvertently opened for an unregulated foreign shell bank, the AML Compliance Officer must be notified and the account will be immediately closed.

29.18.2.3 Foreign Bank Certification

[FinCEN Frequently Asked Questions re Certification: <https://www.fincen.gov/resources/statutes-regulations/guidance/frequently-asked-questions-foreign-bank-recertifications>]

When opening an account for a foreign bank, CEI is obligated to ensure the bank is not a foreign shell bank and must obtain information about the foreign bank's owners and an agent for service of process. The bank must complete the Foreign Bank Certification which must be submitted to the AML Compliance Officer with a copy of the new account application for review. Every three years the bank is also required to re-certify the information filed with CEI.

29.18.2.4 Special Measures

[USA PATRIOT Act Section 311; Bank Secrecy Act 31 CFR Chapter X Part 1010 Subpart F; FINRA Notice to Members 06-41]

Some foreign jurisdictions, foreign financial institutions, international transactions, or types of accounts are designated to be of "primary money laundering concern" by the Secretary of the Treasury. This designation obligates CEI to take certain "special measures" against the primary money laundering concern. The Secretary of Treasury announces when an entity is considered to be a primary money laundering concern. These special measures include:

- A prohibition against opening or maintaining a correspondent account in the U.S. for or on behalf of the primary money laundering concern including at the time of announcement, review of existing account records to identify any prohibited accounts
- Notification to correspondent account holders that the account may not be used to provide the primary money laundering concern with access to CEI [sample notification is included in Notice to Members 06-41 and may be transmitted by a one-time notice by mail, fax, or e-mail or by including the information in the next regularly occurring transmittal to the account, such as an account statement]
- Reasonable steps to identify an indirect use of correspondent accounts by the primary money laundering concern by review of transaction-based records

The clearing firm is responsible for complying with special measures including notification of correspondent accounts and retaining records of compliance.

29.18.3 Due Diligence for Private Banking Accounts

[Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart F]

Private banking accounts:

- include accounts established for a non-U.S. beneficial owner.
- include accounts where the beneficial owner is an individual:
 - who has a level of control over, or entitlement to, the funds in the account
 - who directly or indirectly controls, directs, or manages the account
 - for whom an account is established, maintained, or administered in the U.S.
- exclude accounts for hedge funds (and other pooled vehicles) and corporations (that are not personal investment companies ["PICs"]).
- include accounts for PICs and trusts for the benefit of individual owners.

Requirements for due diligence:

- Determine the identity of all nominal and beneficial owners of the private banking account.
- Determine the purpose and expected use of the account.
- Determine whether any such owner is a senior foreign political official.
- Determine the source(s) of funds deposited into the private banking account and the purpose and expected use of the account.
- Review the account activity:
 - to ensure consistency with information about the account.
 - to report suspected money laundering activity.

Factors considered in determining due diligence include:

- Is the client from a jurisdiction identified by the federal government as a jurisdiction subject to OFAC restrictions or as having weak AML controls?
- Is the customer's business cash intensive?

CEI cannot rely on foreign institutions to perform due diligence for private banking accounts, and due diligence obligations are ongoing. If appropriate due diligence cannot be performed for the account, the account will be closed.

29.18.4 Enhanced Scrutiny for Accounts of Senior Foreign Political Figures

Accounts for senior foreign political figures (including persons and entities defined in this section) are subject to enhanced scrutiny:

Prior to opening, the account is referred to the AML Officer for review and approval.

- Review the account's home country vs. OFAC lists of jurisdictions of money laundering concern and blocked persons.
 - If identified on an OFAC list, report the account and close it.
- Review new account information about the account including employment history, sources of income and assets, whether the person/entity has existing accounts with CEI, length of time the RR has known the account, who referred the account, and other available information about account background of the account and how the account came to CEI.
- If there is inadequate information or due diligence procedures cannot be performed, refuse to open the account or close an existing account.
 - File a SAR, if appropriate.
- If the account is approved for opening, determine whether ongoing review is necessary.
 - If ongoing review is appropriate, establish duplicate statements or another method for review of account activity by the AML Officer.
 - Review will include identifying patterns of securities transactions and securities/money transfers that may be indicative of money laundering activity, and report such activity if necessary and close the account.

29.19 Shell Companies

[FINCen advisory on shell companies: <https://www.fincen.gov/resources/statutes-regulations/guidance/potential-money-laundering-risks-related-shell-companies>]

Shell companies can represent a potential money laundering risk. Most shell companies are formed for legitimate business reasons, but some have been used for illicit purposes.

"Shell company" refers to non-publicly traded corporations, limited liability companies (LLCs), and trusts that typically have no physical presence (other than a mailing address) and generate little or no independent economic value. Legitimate purposes including holding stock or intangible assets of another business entity (such as subsidiary company shares) but are not engaged in active business operations or facilitating domestic and cross-border currency and asset transfers and corporate mergers. State laws allow shell companies to obscure company structure, ownership, and activities, so there is little transparency to enable CEI to understand with whom they are dealing.

Agents that act as intermediaries or nominee incorporation services (NIS) can play a central role in creating, maintaining, and supporting shell companies. Some agents and NIS firms also provide individuals and businesses with nominee services that preserve the anonymity of underlying officers, directors, and stockholders.

Shell companies are subject to review which may include:

- Checking accounts and owners (if information is available) against OFAC restrictions (applies to all accounts)
- Obtaining information about underlying owners
- Obtaining assurances from the shell company representative that principals have been screened

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