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The Strength of Advice®

Crowell Weedon Asset Management Fiduciary Investment Process

- **Why the Fiduciary Investment Process Matters** – See the legal substantiation for why a complete investment process is necessary
- **Definition of those involved in the Fiduciary Investment Process** - Learn about the many roles and responsibilities of all involved
- **Creating a customized Investment Policy Statement** - See the necessary components of an Investment Policy Statement
- **Setting Capital Market Expectations** - Learn about the various forecasting tools & viewpoints used to set capital market expectations
- **Determine your Strategic Asset Allocation** - See how your unique objectives and constraints help determine your asset allocation
- **Implementing the Portfolio Plan** - View the various techniques used to construct a portfolio
- **Performance Evaluation** - Monitor & Evaluate the performance of your entire Investment Process
- **Issues facing the Mid-Size Fiduciary Investor** – Learn more about the challenges facing your investment process
- **Our Services, Investment Philosophy, Fee Schedule & Qualifications** – See how you can improve your Investment Process with CWAM



Crowell Weedon Asset Management

Fiduciary Investment Process

Why This Matters



Personal Liability

When dealing with Fiduciary Accounts (such as foundations, endowments, qualified retirement plans, private trusts, charities, or retirement plans offered to state, county or municipal employees) there are many ethical and procedural requirements as well as applicable laws that must be followed. If not followed, you can be held personally liable.

Taken directly from the Department of Labor's Website:

<http://www.dol.gov/ebsa/publications/fiduciaryresponsibility.html>

"With these fiduciary responsibilities, there is also potential liability. Fiduciaries who do not follow the basic standards of conduct may be personally liable to restore any losses to the plan, or to restore any profits made through improper use of the plan's assets resulting from their actions."



It's About Law

The framework to establish a disciplined investment process is substantiated by legislation, case law, and/or regulatory opinion letters from:

- **ERISA – Employee Retirement Income Security Act (impacts qualified retirement plans)**
- **UPIA – Uniform Prudent Investor Act (impacts private trusts)**
- **UPMIFA – Uniform Prudent Management of Institutional Funds Act (impacts foundations, endowments, & government-sponsored charitable institutions)**
- **MPERS – Uniform Management of Public Employee Retirement Systems Act (impacts state, county, & municipal retirement plans)**

If you read all of these Acts & identified the common fiduciary practices you would discover 7 common practices called “The Global Fiduciary Precepts”.



The Global Fiduciary Precepts

1. Know standards, laws, & trust provisions
2. Diversify assets to specific risk/return profile of client
3. Prepare an Investment Policy Statement
4. Use “prudent experts” and document due diligence
5. Control & account for investment expenses
6. Monitor the activities of “prudent experts”
7. Avoid conflicts of interest and prohibited transactions



Crowell Weedon Asset Management Fiduciary Investment Process

Those Involved in the Fiduciary Investment Process



Those Involved in the Investment Process

Fiduciary – someone acting in a position of trust on behalf of, or for the benefit of, another party.

The vast majority of the world's liquid investable wealth is in the hands of investment fiduciaries. The details of a fiduciary's prudent investment process are critical to the proper implementation of the investment strategy.

Fiduciary can be divided into three groups:

- **Investment Steward – a person who has the legal responsibility for managing investment decisions (trustees and investment committee members)**
- **Investment Advisor – a professional who is responsible for managing comprehensive and continuous investment decisions (financial advisors, trust officers, financial planners, etc.)**
- **Investment Manager – a professional who has discretion to select specific securities for separate accounts, mutual funds, commingled trusts & unit trusts.**



Investment Steward's Primary Responsibilities

Stewards are responsible for the general management of the investments. Stewards may delegate certain decisions to professionals but it does not remove their primary responsibilities:

- **Determining investment goals and objectives**
- **Approving an appropriate asset allocation strategy**
- **Establishing a written Investment Policy Statement consistent with identified goals and objectives**
- **Approving appropriate money managers, mutual funds or other prudent experts to implement the investment policy**
- **Monitoring the activities of the overall investment strategy for compliance with the Investment Policy Statement**
- **Avoiding conflicts of interest and prohibited transactions**



Investment Advisor's Primary Responsibilities

Stewards often times use Investment Advisors to assist in the investment process. As professionals & fiduciaries, Investment Advisors have obligations to:

- Be competent
- Place clients' best interests above their own
- Be worthy of the trust placed in them by the investors they serve
- Be current with & conform to best investment practices and legal & regulatory requirements of the profession

The fundamental duty of the Investment Advisor is to manage delegated investment decisions for the exclusive benefit of another party.

The Investment Advisor has a responsibility to employ an objective, independent due diligence process at all times.



Investment Manager's Primary Responsibilities

Investment Manager's are investment fiduciaries who make investment decisions. Examples include money managers who are responsible for separate accounts, mutual funds, commingled trusts, and unit trusts.

When an Investment Advisor recommends an Investment Manager there is an entire due diligence process that should be completed. An example of some items reviewed include:

- **Clear succession plan in place**
- **Effective compliance program in place**
- **A defined business strategy which supports their competitive positioning**
- **Compensation aligned with client interests**
- **The Investment System is defined, focused & adds value in a consistent manner**
- **Research process is defined, focused & documented**



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Fiduciary Investment Process

Investment Policy Statement



What is an Investment Policy Statement (IPS)?

An IPS serves as a blueprint for investing client assets. It identifies:

- **Needs**
- **Goals**
- **Risk Tolerance**
- **Constraints**
- **Expenses**

Once the above items are defined the IPS then formulates an investment strategy to attempt to achieve the desired goals.

A thorough IPS should be:

- **An educational process**
- **Portable**
- **Easily understood by a competent 3rd party**
- **A document of clear definition of roles & responsibilities**



Components of an IPS

Portfolio Objectives

- **Risk Objective:** the ability and willingness to take risk
- **Return Objective:** determine the required & desired returns

Portfolio Constraints

- **Liquidity:** portfolio's ability to meet anticipated & unanticipated demands for cash distributions
- **Time Horizon:** amount of time the bulk of portfolio can remain invested
- **Tax Concerns:** usually a non-issue in Institutional market
- **Legal & Regulatory Factors:** there may be a variety of constraints which can vary by country & type of entity
- **Unique Circumstances:** may include assets restricted from sale, concentrated positions, guidelines for social or special purpose investing, etc.



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Capital Market Expectations



Capital Market Expectations (CME)

Capital Market Expectations

- **Forecasts of risk & return characteristics for various asset classes**
- **These forecasts form the basis for constructing portfolios that maximize expected return for given levels of risk**
- **CME need to be formulated for the permissible asset classes defined in the investor's IPS to develop a strategic asset allocation**



Framework for Developing CME

- **Specify the final set of expectations that are needed**
- **Research the historical record: most forecasts have some connection to the past**
- **Specify the methods and/or models used**
- **Determine the best sources for information needs**
- **Interpret the current investment environment using the selected data and methods applying experience & judgment**
- **Provide the set of expectations that are needed, documenting conclusions**
- **Monitor actual outcomes & compare them to expectations**



Tools Used in Setting CME

- **Historical Ratios**
- **Discount Models**
- **Risk Premium Models**
- **Equilibrium Models**
- **Relative Valuation Methodologies**
- **3rd Party Forecasts**
- **Industry Experience**



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Fiduciary Investment Process

Asset Allocation



Determining your Asset Allocation

- **At this point we combine the objectives & constraints detailed in the IPS with our Capital Market Expectations to determine target asset class weights.**
- **Maximum & Minimum permissible asset class weights are often specified as a risk-control mechanism.**
- **Why is it important? Different asset allocations have different expected returns, risk, & cash flow patterns.**
- **Which asset allocation is most appropriate depends on how well the allocation's characteristics match up with the investment objectives & constraints described in the IPS.**



TREAT

The acronym "TREAT" helps define the key inputs to a client's asset allocation strategy:

T Time horizon of the client

R Risk level of the client

E Expected return necessary to meet client's goals and objectives

A Asset class preferences of the client

T Tax status of the client



Strategic & Tactical Asset Allocation

Strategic Asset Allocation

- **First element of the portfolio management process to focus on selecting investments**
- **A bridge to the execution step of portfolio management**
- **At the broad level of asset classes**
- **The Strategic Asset Allocation should be the appropriate asset mix to be held under long-term or “normal” market conditions**

Tactical Asset Allocation

- **Involves making short-term adjustments to asset-class weights to try and outperform the “normal” asset allocation**
- **Active investment strategy - In exchange for taking active risks the manager hopes to earn positive active returns**



Specifying Asset Classes

Five criteria to help in effectively specifying asset classes:

- **Assets within an asset class should have similar attributes (homogeneous)**
- **Asset classes should be mutually exclusive (no overlap)**
- **Asset classes should be diversifying (low correlation with other asset classes)**
- **The asset classes as a group should make up a majority of world investable wealth**
- **The asset class should have the capacity to absorb a significant part of the investor's portfolio without seriously affecting liquidity**



Optimization

Optimization is the process of converting our asset class inputs into a recommended strategic asset allocation. There are various optimization techniques utilized today and all should be subjected to professional judgment before adoption:

- **Mean-Variance approach – an investor should choose from efficient portfolios. Efficient portfolios offer the maximum expected return for their level of standard deviation of return.**
- **Monte Carlo Simulation – a computer based technique that provides information about the range of possible investment results from a given strategic asset allocation as well as the likelihood that each will occur.**
- **Experience-Based approaches – relying on tradition, experience & rules of thumb. Examples: 60/40 allocation as starting point, Allocation to bonds should increase with increasing risk aversion, Investors with longer time horizons should increase their allocation to stocks**



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Fiduciary Investment Process

Portfolio Implementation



Implementing the Portfolio Plan

For each asset class specified in the Strategic Asset Allocation, we need to select an investment approach. At the broadest level the choices are:

- **Passive Investing – designed to replicate the returns of a broad investable index representing that asset class**
- **Semi-active Investing (Enhanced Indexing) – an investment that permits some under or overweighting of securities to the asset class but with controlled risk**
- **Active Investing – an investment that reflects the investor’s perceived special insights and skill. Makes no attempt to track any asset class index’s performance.**
- **Some combination of the above**



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Fiduciary Investment Process

Performance Evaluation



Performance Evaluation

The feedback step in investment management process. It plays an integral role in assessing manager skills as well as confirming manager compliance with investment policy.

Questions we should answer:

1. What was the account's performance? – Performance Measurement

We utilize Time-Weighted Rate of Return calculations. This method is unaffected by the size and timing of external cash flows.

2. Why did the account produce the observed performance? – Performance Attribution

$$\text{Impact} = \text{Weight} * \text{Return}$$

3. Is the account's performance due to luck or skill? – Performance Appraisal

Our goal is to provide useful information to help make decisions about whether to retain or modify portions of the investment program.



Crowell Weedon Asset Management Fiduciary Investment Process

Issues Facing the Mid-Size Fiduciary Investor



Issues Facing the Mid-Size Fiduciary Investor

- **Investment Strategy not meeting today's Fiduciary Standards**
- **Investment Strategy not in compliance with ERISA & Internal Revenue Code of 1986 in regards to how your Investment Advisor is compensated**
- **Lack of an Investment Policy Statement**
- **High expenses associated with putting together a customized investment program**
- **Pre-packaged investment solutions presented as customized investment plans**
- **Not being provided with appropriate information to make informed investment decisions**
- **Not being provided with appropriate information to evaluate the performance of the investment program**
- **Investment Stewards taking on duties of Investment Advisor with a lack of knowledge and guidance**
- **Dealing with Investment Professionals outside of your local area**



Crowell Weedon Asset Management

Fiduciary Investment Process

**Our Services, Investment Philosophy,
Fee Schedule & Qualifications**



Our Services as an Investment Advisor

We offer the unique ability to assist you as an Investment Advisor or Investment Manager. To avoid any conflicts of interest DA Davidson has internal policies & procedures in place that do not allow the same individual or team to serve as Investment Advisor & Investment Manager to the same client.

When working as Investment Advisors we can provide the following:

- **Creation of a customized Investment Policy Statement**
- **Historical data and forecasts for permissible asset classes**
- **Recommended Strategic Asset Allocation**
- **Recommended Investment Managers**
- **Performance Evaluation**
- **Local support**



Our Services as an Investment Manager

We offer the unique ability to assist you as an Investment Advisor or Investment Manager. To avoid any conflicts of interest DA Davidson has internal policies & procedures in place that do not allow the same individual or team to serve as Investment Advisor & Investment Manager to the same client

When working as Investment Managers we provide the following:

- Separately Managed account strategies – Montecito Investment Portfolios

Model Portfolios

- *Income*
- *Income & Growth*
- *Growth & Income*
- *Growth*
- *Strategic Equity*
- *Enhanced Equity*

- Mutual fund strategy – Two Oaks Diversified Growth & Income Fund (TWOAX – Class A)

- *Balanced Asset Allocation*



Investment Philosophy

“Pursuing growth & income from diverse asset classes by utilizing common-sense investment disciplines”

Diversification

- **We primarily utilize the following asset classes when constructing portfolios: stocks, fixed income & real estate/asset based securities**
- **Over long-term investment periods our goal is to achieve reduced volatility while increasing capital and income**

Potential Cash Flow

- **We screen potential investments for dividends & income**
- **Investments must fit our proprietary investment strategy and show the potential to grow income over time**
- **We believe income streams can allow greater flexibility to weather market volatility**

Seeking Quality

- **Our investments must meet stringent fundamental disciplines based on various metrics such as revenues, free cash flow, earnings & profitability measures to be considered for investment**



Rationale for Fee Based

Effective as of December 27, 2011 according to Paragraph (b)(3)(i)(D) of ERISA:

"The final rule requires that no fiduciary advisor (including any employee, agent, or registered representative) that provides investment advice receives from any party (including an affiliate of the fiduciary adviser), directly or indirectly, any fee or other compensation (including commissions, salary, bonuses, awards, promotions, or other things of value) that varies depending on the basis of a participant's or beneficiary's selection of a particular investment option."

Our recommended policy:

- **Even if your investment program is not subject to ERISA, implement their required fee based compensation rules to avoid the potential conflict of interest charging commissions or varied compensation schedules can create**



Our Fee Schedule

Fees are negotiable dependent upon the roles & services needed. To summarize, we offer the following:

- **Investment Management (with or without custody of assets)**
- **Investment Advisory**
 - **Creation of a customized Investment Policy Statement**
 - **Review of existing Investment Policy Statement**
 - **Historical data and forecasts for permissible asset classes**
 - **Recommended Strategic Asset Allocation**
 - **Review & Recommendation of Investment Managers**
 - **Performance Reporting**
 - **Performance Evaluation**
 - **Local support**



Our Team & Qualifications



Blake Todd, CWS®

- **Portfolio Manager – Crowell Weedon Asset Management**
- **Senior Vice President, Financial Advisor – DA Davidson & Co.**
- **Chief Executive Officer – Two Oaks Investment Management, LLC**
- **Portfolio Manager – Two Oaks Diversified Growth & Income Fund (TWOAX - Class A)**
- **Industry Experience: 39 years**



Jarrett Perez, CFA

- **Associate Portfolio Manager – Crowell Weedon Asset Management**
- **Senior Financial Advisor – DA Davidson & Co.**
- **Chief Compliance Officer – Two Oaks Investment Management, LLC**
- **Associate Portfolio Manager – Two Oaks Diversified Growth & Income Fund (TWOAX – Class A)**
- **Industry Experience: 16 years**



Important Disclosures

- DA Davidson is a dually registered Broker Dealer and Investment Adviser, member FINRA/SIPC.
- Crowell Weedon Asset Management (CWAM) – Montecito Investment Portfolios: Montecito investment Portfolios is a fee-only investment advisory program introduced through DA Davidson. The mission of Montecito Investment Portfolios is to provide diversified, disciplined, long-termed investment solutions, and service and guidance to help our clients. Assets are generally allocated amongst ownership of corporate stock, income securities, and income producing real estate and asset based securities. Using these asset classes and rebalancing to a client’s allocation range generally creates a strategy for clients to endure change over economic cycles. Additionally, over the long term, rebalancing helps provide the discipline for assets to be purchased at lows vs. highs; and usually reduces the overall volatility of a portfolio. Eligible securities include individual debt and equity securities, mutual funds, index funds, exchange-traded funds, master limited partnerships, and other eligible securities the manager deems appropriate. Options and futures are prohibited.
- For more information about CWAM, as well as DA Davidson’s products, fees, and services, please refer to DA Davidson’s Form ADV, Wrap Fee Program Brochure, which you should have received at the end of this presentation. The Wrap Fee Program brochure may also be obtained by writing to DA Davidson at:
7110 N. Fresno St., Suite 450, Fresno CA 93720 or by calling (888) 833-2777.
- Investment diversification does not ensure profit or eliminate the risk of loss. All investments involve risk. There is no guarantee of successful results.
- For additional information regarding the Department of Labor’s ERISA Regulation, visit the website: www.dol.gov/ebsa



Important Disclosures, cont'd

- Both Blake Todd and Jarrett Perez are dually employed with DA Davidson and Two Oaks Investment Management, LLC. Two Oaks is an investment advisor registered with the United States Securities and Exchange Commission ("SEC") and is a Limited Liability Company ("LLC") formed under the laws of the State of California. Two Oaks is an advisor to the Two Oaks Diversified Income Fund Class A. The funds are a part of the Northern Lights Fund Trust II, an open-end management investment company, which Two Oaks has an Investment Advisory Agreement with.
- Mr. Todd and Mr. Perez are the Funds' portfolio managers and the Managing Members and owners of Two Oaks Investment Management, LLC. DA Davidson does not maintain an ownership interest in Two Oaks. In their capacity as Financial Advisers to Davidson's clients, Mr. Todd and Mr. Perez are presented with some conflicts of interest. Among those conflicts of interest are the following and how they are managed:
 - As Registered Representatives of DA Davidson, Mr. Todd and Mr. Perez may direct trades for the fund through DA Davidson and DA Davidson may profit from that trading activity. To eliminate this conflict of interest, Two Oaks mutual funds trades are not directed through DA Davidson.
 - Mr. Todd and Mr. Perez could place shares of the Mutual Fund, Two Oaks in discretionary accounts that they manage and get paid a management fee for such discretionary account management, and also receive a fund Advisory fee on the same moneys. To remove this conflict of interest for Mr. Todd's and Mr. Perez's discretionary accounts at DA Davidson, these accounts are prohibited from owning any shares in the Two Oaks Mutual Fund.



Important Disclosures, cont'd

- In their capacity of advising clients on the placement of their investments Mr. Todd and Mr. Perez are compensated as the broker of record and receive any sales commission for the placement of moneys into the Two Oaks Mutual Fund. As such, they may also receive any ongoing 12b1 servicing fees for those clients they are the broker of record for. To address this conflict of interest all clients are informed of the dual role Blake Todd and Jarrett Perez maintain and how they are compensated prior to their purchase of fund shares. Clients could also choose to invest in shares of the fund through another broker to remove this potential conflict of interest. For both Blake Todd and Jarrett Perez over 50% of their compensation comes from the commission and fees that their individual clients pay to them.

