

## STEWART AND PATTEN Co., LLC

Investment Management

JOHN K. STEWART (1905-1993)

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## DISCLOSURE STATEMENT

The Securities and Exchange Commission requires that all investment managers provide certain information to all existing and potential clients. This statement is to conform to those requirements.

### **Overview -**

The late John K. (Jack) Stewart entered the investment management business in 1942. In 1962, Ronald S. Patten joined Mr. Stewart, and in 1965 they formed Stewart and Patten Company. In 1998, Stewart and Patten Company became a Limited Liability Company (LLC) within the State of California. Investment management is the only business and exclusive source of income for Stewart and Patten. We do not offer or sell any other type of service. We are not registered as a broker nor are we affiliated with any broker, dealer, investment company or other investment adviser. We do not buy or sell securities as principal nor do we share in any compensation with respect to security trades.

Our business consists of managing security accounts, each of which uses as custodian a bank or broker selected by the client. We hold a limited power of attorney that authorizes us to buy or sell securities. Although we do not consult with clients prior to individual security purchases and sales, occasional consultations are held to discuss general matters such as how the account managed by Stewart and Patten relates to the client's other assets and requirements.

Although most of our clients are individuals, there are clients that are trusts, charitable foundations, retirement plans, estates, and corporations. Client portfolios are invested in stocks, taxable and tax-exempt bonds, and short-term instruments such as Treasury bills and money market funds. A separate account is maintained for each client.

### **Investment Philosophy -**

Our investment approach consists of fundamental analysis, as opposed to technical or quantitative strategies. We study company financial statements and reports, industry trends and conditions, and general business conditions. Principal sources of information are (1) the company's annual report, prospectus, Form 10-K and press releases, (2) various trade publications, (3) general business periodicals, newspapers and the internet, (4) brokers' reports, and (5) meetings or phone conversations with company officers.

Common stocks provide the potential for growth and contribute a steadily rising income stream as dividends increase. Typically, we maintain the stock portion of a client's portfolio with a target of 60% of the total value of the account. Other targets are occasionally utilized to meet specific client needs. Our approach to stock selection is conservative and income-orientated, concentrating on financially strong companies with medium to large capitalizations. We generally select stocks paying dividends, where our fundamental analysis suggests good prospects for additional profit and dividend growth. A typical portfolio contains 20 to 25 stocks.

The bonds in a portfolio normally reduce volatility while providing a higher rate of current income and liquidity. We select high quality bonds, mostly U.S. Government issues, with maturities ranging up to 12 years. Usually, about 30 to 35 percent of a portfolio is invested in bonds. When appropriate, we will hold a mixture of U. S. Government issues and municipal bonds in taxable accounts. In tax-free accounts, we sometime utilize high quality corporate bonds. Assets not invested in stocks or bonds are invested in cash equivalents including money market funds and Treasury bills, in order to maximize short-term returns.

The types of securities in which we invest for our clients are limited to common stocks listed on the New York Stock Exchange, American Stock Exchange, or NASDAQ, corporate debt securities, municipal securities and U.S. Government obligations. Securities usually are purchased for the long term and our portfolio turnover tends to be relatively low. We do not use short sales, margin transactions, options or futures.

### **Operations -**

Accounts are not assigned to individual principals or associates. Each member of the firm is familiar with all accounts, and we urge clients to contact any principal or associate whenever they have questions.

The investment committee consists of all the principals and associates. When a committee member reviews an account, he presents his recommendations to the whole committee, which usually meets daily. The committee decides which securities are bought or sold and the quantity. Generally, we will not purchase additional shares in any stock that results in the total holding in that issue exceeding 5% of the total portfolio.

Clients usually select their own broker/custodian. We have made arrangements with several major securities firms for brokerage and custody at commission rates substantially lower than regular "full service" brokerage accounts. On occasion, we help clients choose from one of these alternatives if they have no other preference. Our written Investment Management Agreement with our clients grants us authority to negotiate lower commissions, and we have done so wherever possible. In a limited number of circumstances, we execute trades at a broker other than the client's custodian solely to improve pricing/execution. A few brokers voluntarily send us research reports; however, this is not a factor in our placement of what little discretionary business we have, nor is it a factor in our negotiating lower commissions. We do most of our research ourselves and it applies to all our clients.

As outlined in the paragraph above, non-affiliated brokerage firms - and not Stewart and Patten - always serve as custodians of client accounts. However, Stewart and Patten Principals act as

Trustee for a limited number of client accounts. In these cases, Stewart and Patten would have custody of client assets as defined by the SEC. Nevertheless, client assets are still held at a qualified custodian not affiliated with Stewart and Patten. In addition, co-trustees and/or beneficiaries of these trusts receive all custodial/brokerage reports, quarterly reports from Stewart and Patten, and year-end principal and income accountings from Stewart and Patten. These trusts represent slightly more than \$12.5 million in client assets and 21 separate accounts as of March 31, 2009.

We furnish quarterly portfolio appraisals to each client. We also prepare a year-end schedule of realized capital gains and losses based on the information from the records maintained in our office. Virtually all client records are electronically updated each business day and reconciled monthly. Client account data is retained for at least five years. In addition, each client receives directly from their custodian reports that include monthly summary statements and individual broker confirmations for each purchase and sale.

The frequency of review of a client's account varies. Cash is reviewed almost daily. Copies of quarterly valuations are distributed to each investment committee member, resulting in committee review soon after release. The companies owned by our clients are reviewed whenever earnings or significant news is announced, or after a principal visits the company or its representatives. Other factors which will trigger a review of client accounts include: a significant change in stock prices, a change in a client's personal or financial situation, or a change in emphasis in particular investments such as a new candidate for purchase or sale.

Transactions for clients always have priority over the personal transactions of partners and associates. Personal transactions of partners/associates never operate adversely to clients' interests. Partners and associates occasionally buy or sell securities bought or sold for clients. Partners/associates are required to conduct all aspects of their personal business in such a manner to avoid any actual or potential conflict of interest. Partners/associates are prohibited from placing personal trades for securities when there are open client orders for that security. This effectively means that all trades for partners/associates take place at the end the day after all client trades have been completed. The one exception would be periods when the firm makes a series of transactions in a given security for client accounts over a period of several days. In this case, no personal trades in this security would be allowed until after all client transactions are complete. The company maintains a file (updated quarterly) on all partners' and associates' transactions involving the purchase and sale of equity securities.

We occasionally execute block trades with different brokers because client assets are held at different brokers as directed by clients. We will purchase or sell a security as one block through a selected broker and then allocate that trade among the clients that have selected that broker as their custodian. We then repeat that process for clients who have selected other brokers until the total transaction has been completed for all clients. Although price and transaction costs may vary slightly from broker to broker, within each group of clients who share the same broker, average share price and transactions costs are shared on a pro rata basis. Orders are placed with the small number of retail brokers utilized by some clients first in order to ensure that a connection is made with the broker during the trading day. All other brokers are traded on-line. The sequence in which block trades are placed with each broker group varies based on the size of the order and the liquidity of the security in the marketplace.

## **Fee Structure -**

Annual fees are based on the account valuation as follows:

- .75 of 1% on the first \$5,000,000 of valuation
- .60 of 1% on next \$5,000,000 of valuation
- .40 of 1% on valuations over \$10,000,000

The above schedule pertains to a balanced investment account where a substantial portion of the account is invested in both equities and fixed income assets. The rate schedule would be increased by .25% of 1% at each level for an all equity account. Occasionally, fees are negotiated lower than the schedule shown above.

Semi-annual fees are computed based on the five-month average account balances for the periods ending April 30 and October 31. Bills are prepared during the months of June and December, and mailed to clients in early June and December. On rare occasions, we purchase mutual funds on behalf of clients or hold mutual funds from legacy managers in clients' accounts. In this circumstance, the client will be charged management and other fees by the mutual fund company in addition to Stewart and Patten fees.

In 2007, Edward J. Schneider, III, CFA, joined Stewart and Patten as a Principal of the Firm. Mr. Schneider brought with him client relationships where fees are calculated and paid differently from traditional Stewart and Patten accounts. For accounts that have come to Stewart and Patten with Mr. Schneider, fees are based on the market value of supervised assets at the beginning of each three-month reporting period and are payable in advance.

Stewart & Patten Co., LLC operates under an Investment Management Agreement. Following the initial execution of this agreement, it may be terminated at anytime by either party on five calendar days' written notice delivered to the other without payment of penalty and without liability of either party to the other. After the five-day period this agreement can be terminated on 10 calendar days' written notice. On termination of this Agreement, fees will be prorated. A client account or Agreement may not be assigned to a third party without specific approval from the client. Clients are notified of any change in the structure of Stewart & Patten Co., LLC as soon as practicable after such change.

Minimum dollar valuation for starting an account is \$750,000. Under special circumstances, smaller accounts are occasionally accepted. We believe these fees are similar to those charged by many other investment counseling firms for similar services; however, comparable service may be available from other sources for lower fees.

## **Investment Professionals -**

All Principals and Associates at Stewart and Patten have advanced degrees and / or industry specific credentials. The age, education and recent business background of each of our principals and associates are as follows:

**Principals –**

RONALD S. PATTEN - age 77, B.A. degree Occidental College, M.B.A. degree Stanford University. Entered the investment management business with Mr. Stewart in 1962.

GLEB BELONOGOFF - age 72, B.S. degree San Francisco State College, C.P.A. with Price Waterhouse 1967-1972. Joined Stewart & Patten Co., LLC in 1973.

STEPHEN A. ETHRIDGE - age 50, B.P.A. degree University of Mississippi, M.B.A. degree University of Colorado. Active Duty U.S. Naval Officer 1981-1988. Spare, Kaplan & Bischel, Investment Advisors 1988-1991. BTR Capital Management 1991-1993. Retired from the U.S. Navy in 2005 at the rank of Captain after 24 years of active and reserve service. Joined Stewart & Patten Co., LLC in July 1993.

ROBERT M. GENTRY, CFA - age 47, B.S. degree University of California at Davis, M.S. degree St. Mary's College, Chartered Financial Analyst. Retirement Plans Analyst, Franklin-Templeton Funds 1984-1987. Controller, CR-P Associates 1987-1990. Co-Founder and CFO, DBSS/InterMax Solutions 1990-1997. Joined Stewart & Patten Co., LLC in November 1997.

LORI E. SHERMAN, CPA, CFP® - age 45, B.S. degree California State Polytechnic University, Pomona. C.P.A. with Coopers & Lybrand 1986-1990. Financial Consultant, 1991-1993. Vice President and Controller, Roger Engemann & Associates 1993-2000. Joined Stewart & Patten Co., LLC in April 2000.

**Associates –**

MATTHEW J. SCHMIDT, CFA - age 34, B.A. Georgetown University. Chartered Financial Analyst. Associate Portfolio Manager, Dodge and Cox, 2003-2008. Senior Analyst, State Street Bank, 2002-2003. Analyst, mPower Advisors, 1999-2001. Asst. Trader/Associate, Wentworth, Hauser & Violich 1997-1999. Joined Stewart and Patten in May 2008 as an Analyst.

**Retired Principals –**

JOHN R. GENTRY - B. S. degree Oregon State University, C.P.A. with John Forbes & Co., 1955-1986. Chartered Financial Consultant (CHFC), American College. Joined Stewart and Patten Co., LLC in August 1986.

EDWARD J. SCHNEIDER, III, CFA, CIC –B.A. degree Stanford University 1967, M.B.A. degree Columbia University 1969. Vice-President, Director, CFO & Director of Research, Shuman & Schneider 1980-2005. President, Chairman of the Board of Directors and Chief Compliance Officer, Shuman & Schneider 2005-2007. Joined Stewart and Patten in 2007.

**Stewart & Patten Co., LLC**

Revised:

May 11, 2009