

# EUREKA INVESTMENT ADVISORS, INC.

A Blueprint for an Independent Investment Subsidiary of  
Sanwa Bank California

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## **1.0 EXECUTIVE SUMMARY**

### **1.1 Regulatory Need**

On November 12, 1999 the President signed into law the Financial Modernization Act of 1999, also known as the Gramm-Leach-Bliley Act, or "GLB." Under GLB, Congress repealed the exemption from registration with the Securities and Exchange Commission (SEC) given to banks and bank holding companies under the Investment Advisers Act of 1940. This exemption had previously allowed banks to act as investment advisers to mutual funds without having to register as a Registered Investment Adviser (RIA) with the SEC.

Under the new law banks which act as investment advisers to mutual funds must either register with the SEC as an RIA or create a subsidiary to register as an RIA and manage the funds. The Legal Department of Sanwa Bank California has recommended, as has outside counsel and other retained consultants, for purposes of minimizing the impact of SEC regulatory intervention on its non-investment activities, that SBCL create and register with the SEC a subsidiary of SBCL for the purposes of providing investment advisory services, principally to SBCL's family of proprietary mutual funds, the Eureka Funds. This activity must be fully achieved by May 12, 2001.

### **1.2 Subsidiary Vision and Structure**

Eureka Investment Advisors, Inc. (EIA) will be an independent company, wholly owned by Sanwa Bank California (SBCL), established for the purpose of providing a unique brand of quantitative investment management services primarily to the Eureka Funds, as well as to institutional and corporate clients in the United States and abroad. Seeded initially with selected personnel and clientele from SBCL, EIA will be expected to grow and expand in its own market niche by relying on a combination of its unique investment style, its strong team of seasoned professionals, and its stable client base. It is anticipated that EIA will provide for most of its own needs, and will operate independently within its own revenue and budget.

EIA will be a C Corporation registered in the State of California whose sole stockholder will be SBCL. EIA will be capitalized initially at approximately \$500,000, with funding for the capitalization provided by the redirection of client revenues for March into the subsidiary at the start of April. EIA will be governed by a three member board, comprised of two senior members of SBCL and the President of EIA. It is anticipated that the two senior members of SBCL to serve on the Board will be Howard Gould and Takashi Muraoka, with Howard Gould serving as Chairman of the Board. Counsel to the EIA Board will be provided by a designated member of the Legal Department of SBCL, presumed to be Bruce Steele at the current time. The President of EIA will be the Bank's current Chief Investment Officer, Bob Bannon, who will serve the Bank in a dual capacity as President of EIA as well as continuing as Chief Investment Officer of SBCL.

For purposes of day-to-day management, the President of EIA will report directly to the Chairman of the Board of EIA. Staff members of EIA other than Bob Bannon will not be dual employees of EIA and the Bank, but will be the sole employees of EIA. EIA staff will provide services to SBCL primarily under specific contractual arrangements. Initial physical location of EIA will be on the 10<sup>th</sup> floor of the Los Angeles Head Office of SBCL, but it is recommended that office space be found eventually that is separate from the current Wealth Management Division in order to provide an additional firewall for SBCL against undesired regulatory intrusion.

### **1.3 Staffing**

The majority of initial personnel for EIA will derive from existing employees of SBCL's Wealth Management Division (WMD). Total staff of EIA is expected to be 14 full-time employees, nine of whom are currently WMD employees, while the remaining five are to be filled in the near-term. Three of the five positions needing to be filled are currently open positions under recruitment in the WMD. Staff will be drawn from the areas of Portfolio Management, Investment Research, and Administration/Sales. All staff of EIA will resign their positions from SBCL and will be the sole and exclusive employees of EIA – no EIA employee will be a dual employee of SBCL (except for the President, Bob Bannon), although service agreements for the provision of services back to SBCL will be utilized as necessary to minimize the disruption to SBCL of the loss of key employees. Employees transferring to the subsidiary will maintain the medical and retirement benefits of the Bank, and will not lose any seniority or vesting in these programs as a result of their move to EIA. A reorganization of SBCL's Investment Management Department will also be required following the subsidiary's creation.

### **1.4 Marketing Plan**

EIA will have as its anchor client the Eureka Fund family. In addition to managing the assets of the Eureka Funds, EIA will assume full responsibility for the marketing, wholesaling, strategic positioning, compliance, reporting, and product development of the Eureka Fund family. In addition to the Eureka Fund family, EIA will assume full management authority of all institutional accounts currently managed by the Wealth Management Division of SBCL, and a to-be-determined number of separate, non-trust, managed agency accounts. EIA will **not** provide direct investment management services for SBCL trust clients, primarily for regulatory reasons, although EIA will provide indirect research and analysis services to such clients. Initial assets under management of EIA will be approximately \$1.3 billion, with an average fee of approximately 35-40 basis points. A detailed description of EIA's plans to grow assets from all three sources – Eureka, institutional accounts, and corporate accounts – is included in section 5.0 of this proposal.

## 1.6 Financial Projections

EIA will assume all revenues from the accounts that are officially assigned to EIA by SBCL, which includes the revenues of the Eureka Funds, current institutional accounts, and any managed agency accounts that are to be initially transferred to EIA. EIA, as an independent subsidiary, will not be required to "I/O" (inter-office transfer) its revenues back to any units of SBCL, but will instead work with FMC to insure that the appropriate departments and divisions of SBCL receive credit towards their goals for having raised assets for EIA. In addition, EIA will have specific service level agreements to pay for direct services received from SBCL support units. At current revenue run rates it is anticipated that EIA will have an annual revenues of \$5.5 million (to be adjusted for a partial first year of operation). Expenses for EIA have been approximated and are included herein.. Annual payroll expense, the largest single anticipated expense, is expected to be \$1.6 million in base salary in the first year (annualized), and \$600,000 in incentive compensation (annualized). EIA is expected to be profitable from its initiation, and to generate almost \$1.8 million per year in earnings before taxes in its first year .

## 2.0 REGULATORY NEED

On November 12, 1999, President Clinton signed into law Senate Bill 900, The Financial Modernization Act, more commonly known as the Gramm-Leach-Bliley Act ("GLB"). This law upended over 60 years of federal legislation guiding the nature of the banking industry's efforts to provide financial services other than traditional banking products. This section contrasts the rules and regulations in existence prior to the passage of GLB with the changes brought about by the passage of GLB. The specific impact of these changes on SBCL is discussed, and a plan is offered that will allow SBCL to comply with the terms of GLB.

### 2.1 Conditions Prior to Gramm-Leach-Bliley

Prior to the passage of GLB, a multiplicity of laws governed bank behavior in the areas of mutual funds and investment management services. The following items represent the key laws that were in existence, governing banks in the area of investment management, prior to the passage of GLB.

Exemptions for Investment Advisory - Banks had a blanket exemption from the definition of "investment adviser" contained in Section 202(a)(11)(A) of the Investment Advisers Act of 1940 ("Advisers Act"). The Advisers Act defined an "investment adviser" as an entity that serves as an adviser to a Registered Investment Company (a RIC, or mutual fund). Based on this exemption, banks could serve as investment advisers to mutual funds without having to register with the SEC as a Registered Investment Adviser (RIA), or to comply with the SEC's rules for RIA's as to disclosure, record-keeping and other requirements.

Sponsorship of Mutual Funds - Section 20 of the Glass-Steagall Act of 1933 ("Glass-Steagall"), effectively prohibited banks from sponsoring, organizing, or controlling mutual funds by prohibiting all *affiliations* between member banks and firms principally engaged in the issuance, underwriting, sale, or distribution of securities (including mutual funds).

Distribution of Mutual Funds - Sections 16 and 21 of Glass-Steagall restricted banks from *directly* acting as underwriters or distributors for mutual funds.

Directorates of Mutual Funds - Section 32 of Glass-Steagall prevented "interlocking directorates," i.e., directors of member banks could not also be directors of mutual funds. This limitation also applied to member bank directors serving as directors of other firms primarily engaged in securities underwriting or distribution. In addition, Section 10(c) of the Investment Company Act of 1940 ("Company Act") prohibits a majority of the directors of a mutual fund from being affiliated with a single bank (member or non-member).

Custodian of Mutual Funds - Under section 17 of the Company Act, banks may act as custodian to, or provide loans to, a mutual fund.

Exemptions for Common Trust Funds - Under Sections 3(a)(12) of the Securities Exchange Act of 1934 ("Securities Act") and under section 3(c)(3) of the Company Act banks have an exemption to organize, manage, and offer Common Trust Funds (CTF's). CTF's, if used solely as an aid to fiduciary account administration, are exempt from the definition of an investment company (i.e., they are not considered to be mutual funds).

## **2.2 Changes Brought About by Gramm-Leach-Bliley**

The passage of GLB in late 1999 put in motion a series of changes and deadlines for the banking industry. Various sections of such critical laws as the Glass-Steagall Act of 1933, the Securities Exchange Act of 1934, the Investment Advisers Act of 1940 and the Investment Company Act of 1940 were either repealed or modified significantly. This section highlights some of the most important changes.

Loss of Exemption for Investment Advisory – Effective May 12, 2001, GLB eliminates the exemption granted to banks under the Advisers Act. As a result of the removal of this exemption, banks which serve as investment advisers to mutual funds must choose one of the following options: (1) Register the entire bank as an RIA with the SEC; (2) Register only a "Separately Identifiable Department or Division (SIDD)" of the bank with the SEC as an RIA (which presumably but not assuredly would limit the SEC's examination authority to just the SIDD and not the entire bank, assuming certain definitions were satisfied); (3) Transfer the functions necessary to serve as an investment adviser into an affiliated subsidiary, and register the subsidiary as an RIA with the SEC; (4) Divest itself of its responsibilities as an investment adviser to mutual funds, by either selling the funds to another adviser or ceasing operations; (5) Convert any mutual funds into Common Trust Funds and obey all necessary procedures to insure that the CTF's remain exempt from the definition of an Investment Company as defined in the Company Act, thereby avoiding any need for the bank or any affiliate to register as an RIA with the SEC.

Sponsorship and Distribution of Mutual Funds – Effective March 11, 2000, GLB repealed Section 20 of Glass-Steagall, allowing banks to affiliate with firms that underwrite or distribute mutual funds. GLB does not repeal Sections 16 and 21 of Glass-Steagall, however, so that banks are still prohibited from directly underwriting or distributing securities such as mutual funds (except within a very narrow list of exempted activities, including the provision of trust activities, sweep accounts, safekeeping, swaps, and certain fixed income underwriting). Banks can enter into third-party networking agreements with affiliates that are registered as broker/dealers with the SEC and NASD, or they can create a broker/dealer subsidiary to do the same.

Allowance of Interlocking Directorates – GLB repeals section 32 of Glass-Steagall, which will allow interlocking directorates between member banks and registered

investment companies. However, GLB does not repeal section 10(c) of the Advisers Act, so a single bank cannot control the majority of seats on the board of an RIC. Also, non-member banks (such as SBCL) were not held to Section 32 of Glass-Steagall, and could place its bank directors on a mutual fund board freely, so long as the bank's directors did not become a majority of the mutual fund's board.

SEC Regulation of Banks as Custodians for Mutual Funds - GLB directs the SEC to develop rules to govern the manner in which banks can act as custodian to mutual funds. Until the SEC issue such rules, however, banks may continue to act as custodians under section 17 of the Advisers Act.

Refinement of the Common Trust Fund Exemption - GLB refines the CTF exemptions such that CTF's will not be considered RIC's so long as the CTF (1) is employed solely as an aid to fiduciary account administration; (2) is not advertised to the general public, except as part of the advertisement of trust services; and (3) charges fees and expenses consistent with violate fiduciary law

### **2.3 Impact of the Passage of GLB on SBCL**

SBCL has established and arranged many aspects of its investment management functions based on a good faith attempt to comply with the laws that were in existence prior to the passage of GLB. In 1997, SBCL sought to convert several of its existing Common Trust Funds in mutual funds, for the purposes of expanding assets under management through channels other than the growth of Trust Department assets. The following actions were taken at that time, in accordance with then-existing banking laws. Comments as to whether these actions are still in compliance with GLB are also included.

- Creation of a Registered Investment Company - In 1997 SBCL created a Registered Investment Company, the Eureka Funds, and established a family of mutual funds by converting existing Common Trust Funds into the Eureka mutual funds. The Board of Trustees for this Registered Investment Company was filled with two senior executive officers of SBCL and three independent directors. One of the two senior executives of SBCL was selected to chair the Eureka Board (neither action was a violation of Section 32 of Glass-Steagall, since SBCL was not a member bank). This arrangement creates no difficulties under GLB, since SBCL continues to comply with the Company Act restrictions on majority control, insofar as the Eureka Board has not and will not have as a majority of its Directors the officers of a single bank. SBCL can continue its relationship with the Eureka Funds company without adjustment.
- SBCL Advisory of the Eureka Funds - The Eureka Funds Board of Trustees selected the Investment Management Department of SBCL to be the hired Investment Advisor to the Eureka Funds. This relationship has been in place since the inception of the Funds, and continues today. This arrangement does in fact cause a conflict with GLB, since GLB requires that all mutual funds be advised by an SEC-registered RIA, and neither SBCL nor its Investment Management Department is an RIA.



- Distribution of the Eureka Funds – The Eureka Funds Board originally selected Bisys Fund Services as the Administrator and Distributor of the Eureka Funds, since SBCL was prohibited under Glass-Steagall from serving directly as either underwriter or distributor of the Eureka Funds. Continued use going forward of Bisys as Distributor of the Eureka Funds is consistent with the changes brought about by GLB, although GLB would also now permit SBCL to engage directly in the distribution of the Eureka Funds if it so chose. The decision as to whether Bisys remains the Administrator/Distributor or SBCL seeks to perform those services is entirely a business matter, and is not affected by the passage of GLB.
- Custody of the Eureka Funds – Originally SBCL chose Bank of New York (BONY) to serve as the Custodian of the Eureka Funds. It was a business decision at the time to use BONY rather than SBCL, primarily due to their superior ability to provide custody services for global securities; however, the passage of GLB does not preclude consideration of Sanwa as a possible custodian for the Eureka Funds in the future. It should be noted, though, that GLB does give the SEC additional rulemaking authority over the ability of banks to serve as custodian to mutual funds, and SBCL should review carefully whether it wishes to incur the potential regulatory scrutiny of the SEC in exchange for providing custody to the Eureka Funds at some future date.

Overall, therefore, it appears that the passage of GLB causes difficulties for SBCL in only one area: its investment advisory relationship with the Eureka Funds.

## **2.4 A Plan to Comply with Gramm-Leach-Bliley**

Unfortunately the passage of GLB threatens to push SBCL out of compliance with now-prevailing banking and securities laws unless certain changes are made. As described in section 2.3 above, the primary difficulty for SBCL is that it has accepted the role as Investment Advisor to a mutual fund and the legal environment now requires all mutual fund advisors to meet certain conditions that SBCL does not currently satisfy. The Investment Management department has devised a plan to bring SBCL into compliance with GLB. This plan is more fully described in the remaining sections of this proposal, but the features of this plan which seek to achieve compliance with GLB are described below:

- Creation of an Investment Management Subsidiary to SBCL – All necessary personnel and resources to provide the full array of investment advisory services for the Eureka Funds should be transferred into a wholly-owned subsidiary of SBCL. This subsidiary will, as its primary purpose, manage the Eureka Funds. Creation of an investment management subsidiary is one of the approved choices within GLB for banks to comply with GLB. However, counsel has advised that the creation of a subsidiary must truly be capable of providing all needed services to the Eureka Funds, and not simply be a “shell” established to evade SEC regulation of the “true” investment advisor to the mutual funds.

- Registration of the Subsidiary as an Investment Advisor – Once created, officers of the subsidiary will register the subsidiary as a Registered Investment Advisor with the SEC. Once registered, SBCL will transfer all aspects of investment advisory for the Eureka Funds into the subsidiary, and SBCL will relinquish all responsibility for the investment management of the Eureka Funds.
- Establish Additional Firewalls – To help ensure that the SEC favorably respects the distinction between SBCL and its subsidiary, additional steps will be taken including:
  - Avoidance of “dual employees” shared by SBCL and the subsidiary (other than Bob Bannon)
  - Separate investment accounting systems for SBCL vs. subsidiary clients
  - Separate financial accounting for the Subsidiary from SBCL
  - Dedicated compliance officer for the subsidiary
  - Distinct geographic location for the subsidiary
  - Prohibition of the subsidiary from managing bank trust accounts
  - Service level agreements for any services provided to SBCL by the Subsidiary
  - Separate Board of Directors for the subsidiary

While there is no guarantee that the SEC will not try to use SBCL’s connection to the Eureka Funds as a justification to examine SBCL as well as the subsidiary, these steps at creating a firewall provide significant protection against excessive SEC scrutiny.

## **2.5 Implications of a Subsidiary on SBCL’s Relationship with other Regulators**

Creation of an investment management subsidiary has implications for SBCL’s relationship with other regulators, as well as with its parent, Sanwa Bank Limited (SBL). The following describes those implications:

- Implications for SBL – The Policy Manual for SBCL states that the creation of any type of subsidiary for SBCL must be approved not only by Management Committee and the Board of Directors of SBCL, it must also be approved by the Board of Directors of SBL.
- Implications for the Department of Financial Institutions (DFI) – DFI has an approval process for state-chartered institutions that wish to invest in the equity capital of any company, which would include the creation of a subsidiary. In 1988 SBCL originally requested that DFI approve the creation of an investment management subsidiary which was never actually created. However, according to the DFI, that approval still stands, which will significantly reduce the paperwork necessary to create an investment subsidiary at the current time. Given our existing DFI approval to create a subsidiary, we would simply need to submit our business plan, an approved resolution from the SBCL Board, and other minor paperwork within 30 days after the new subsidiary has been capitalized in order to finish the notification process to DFI.

- Implications for the Federal Deposit Insurance Corporation (FDIC) – The FDIC has no formal approval process for state-chartered banks that wish to invest in the creation of a subsidiary. However, it would be advisable to send a similar notice to the FDIC as that which will be sent to the DFI, as a courtesy.
- Implications for the Financial Services Agency (FSA) of Japan – The creation of a subsidiary by SBCL requires Board approval of Sanwa Bank Limited, which in turn requires the approval of the FSA in Japan. The approval process would need to be coordinated with SBL through OOP.

### 3.0 SUBSIDIARY VISION AND STRUCTURE

Eureka Investment Advisors, Inc. (EIA) will be created initially by pushing out existing SBCL employees, fixed assets, clients, and associated client revenue streams into a wholly-owned but independently managed subsidiary corporation. This section defines the broad vision for the subsidiary in terms of its purpose both for the immediate satisfaction of GLB requirements as well as its potential to add a diverse new income stream to SBCL. This section will also discuss specific issues of corporate structure, such as the terms of incorporation, board structure, executive officer duties, and geographic location of the subsidiary. Finally, a discussion of the subsidiary's relationship within the structure of SBCL will be presented. Later sections will detail the staffing and budgetary needs of the subsidiary, the marketing plan for the subsidiary, and the impact of these plans on the existing structure of SBCL's Wealth Management Division.

#### 3.1 A Vision for an Independent Investment Management Subsidiary of SBCL

Eureka Investment Advisors, Inc. (EIA) will be created for two primary purposes: to minimize unnecessary regulatory intrusion into those areas of SBCL not directly related to the management of the Eureka Funds, and to provide a vehicle for SBCL to target a new client base and a new source of revenues – the marketplace for institutional investment management and advisory.

As a method for minimizing regulatory intrusion, the creation of EIA is closely in keeping with the approach which most of SBCL's competitors are taking to comply with the Gramm-Leach-Bliley ramifications described in Section 2.0. While there are no guarantees that the creation of an independent yet wholly-owned investment subsidiary of SBCL will prevent SEC encroachment in banking areas previously not under their purview, multiple legal sources both internal and external to SBCL have provided counsel that the approach of creating an independent subsidiary is the most cautious avenue for protecting SBCL, short of divesting itself from providing investment management services to the Eureka Fund family. It is also important to stress that based on this mandate alone (minimizing regulatory intrusion), the EIA subsidiary is a necessary entity regardless of whether it succeeds in expanding its business line. Indeed, EIA is being created so as to be profitable based simply on its management of the Eureka Fund family (see section 6.0 on the Financial Projections for the subsidiary), assuming the Eureka Funds stay at or exceed current asset and revenue levels.

As a vehicle for SBCL to target a new client base, the creation of EIA is a necessary (albeit not a sufficient) condition for success. The Wealth Management Division of SBCL does not currently manage more than a very small handful of institutional accounts, and those accounts were primarily granted to WMD by other Sanwa affiliates. It is unlikely that WMD would acquire similar non-Sanwa-directed institutional clients on its own going forward, due to the widespread perception in the institutional

marketplace that banks (particularly banks that are perceived to be cater to a regional, middle market, and/or agricultural business base) are generally incapable of providing the quality of investment management services desired by sophisticated institutional investors. Institutional investors have been willing, however, to consider using the investment services of bank investment subsidiaries, and this has occasionally succeeded quite well for the parent bank (witness the creation of Western Asset Management Company, or WAMCO, by First Interstate Bank, or Wells Fargo/Nikko Investment Advisers, now Barclays Global Investors, for Wells Fargo).

### **3.2 Corporate Structure**

This sub-section discusses the various legal and business aspects of the design of EIA as a corporation. More detailed discussions of the staffing and *pro forma* financials appear in sections 4.0 and 6.0.

#### **3.2.1 Terms of Incorporation**

EIA will be incorporated *de novo* in the state of California as a section C corporation. EIA will have as its sole shareholder SBCL. Articles of incorporation and by-laws have been drafted by outside counsel, under the direction of senior counsel from SBCL's Legal Department. Requests to establish a shell corporation for the purpose of shifting assets, personnel, clients, revenues, and expenses from SBCL into the subsidiary have been made to SBCL's Management Committee and Board of Directors, and have been approved. A similar request for approval has been made of SBL's Board of Directors, and has also been approved.

The purpose of housing EIA in a corporate subsidiary is twofold:

- To cement the image of the Registered Investment Advisor to the Eureka Funds as a separate entity from SBCL in the eyes of the SEC
- To create an image for EIA as a non-bank investment "boutique" in the eyes of potential institutional and other sophisticated clients

#### **3.2.2 Board of Directors of EIA**

EIA will be governed by a three member board, comprised of two senior executive officers of SBCL and the President of EIA. It is anticipated that the two senior members of SBCL to serve on the EIA Board will be Howard Gould and Takashi Muraoka, with Howard Gould serving as Chairman of the Board of EIA. Bob Bannon, as President and CEO of the subsidiary, will serve as a member of the Board of Directors. Henry Baltazar, the compliance officer for the subsidiary, will serve as Secretary to the Board but will not be a member of the Board. Counsel to the Board will be provided by a member of SBCL's Legal staff, under a direct service level agreement between SBCL and EIA to provide such advice. Outside counsel may also be used from time to time.

### ***3.2.3 Executive Officers of EIA***

California law only requires that a corporation declare a President and a Chief Financial Officer. Bob Bannon will serve as President and Chief Executive Officer of EIA, while Henry Baltazar will serve as the Chief Financial Officer. For purposes of day-to-day management, the President (Mr. Bannon) will report directly to the Chairman (Mr. Gould) of the Board of EIA. Mr. Bannon will also serve as the Chief Investment Officer of the subsidiary until such time as growth in the subsidiary warrants a separate full-time officer. No other executive officers will be defined or declared at the inception of EIA, either for purposes of registering EIA with the state of California as a corporation, or for the purposes of registering EIA with the SEC as a Registered Investment Advisor. A more complete discussion of the roles and responsibilities of the non-executive officers of EIA is provided in Section 4.0 of this proposal.

### ***3.2.4 Geographic Location of EIA***

Ideally the offices of EIA should be in a separate and distinct location from the offices of the current Wealth Management Division of SBCL, and perhaps even distinct from any current location of SBCL itself. There are three reasons why physical separation of EIA from both SBCL and the WMD would be useful:

- SEC Scrutiny – The most likely triggering event for the SEC to request an examination of SBCL would be a belief on the SEC's part that information from the trading of the Eureka Funds is being used to benefit trust or investment clients of SBCL (so-called "front-running" of client trades). The more physically separate is the trading facility of EIA from any investment management function remaining within SBCL, the less ability the SEC will have to claim possible misuse of Eureka Fund information.
- Image with Potential Clients – For those clients that worry that a bank does not have the expertise to manage institutional assets, physical separation from the facilities of SBCL (or at least from any connection with the more retail-oriented investment functions of the WMD) would be useful.
- Insuring Flexibility of Operations – For EIA to be a success it must be free from excessive bureaucracy and capable of independent self-governance, for example in the area of selection of service providers outside of SBCL channels. Physical separation from SBCL would help establish a sense of independence for EIA, both in the minds of EIA employees as well as SBCL employees.

While complete physical relocation of EIA might be the ideal, the reality is that such a separation is likely not feasible at the inception of the new corporation. At a minimum, to insure minimization of SEC scrutiny of SBCL, personnel and resources drawn from SBCL to form EIA will be rearranged within the 10<sup>th</sup> floor head office location of SBCL's Wealth Management Division so as to concentrate EIA in one area. Additional

efforts to signify the separation of EIA from the other functions of WMD may include the use of separate signage, and possibly glass or drywall enclosures. Relocation of EIA to another floor of the head office building, or perhaps to another physical location altogether, will be reviewed at a later date. Opportunities for relocation may arise as part of the planning process to incorporate Tokai Bank of California within SBCL.

### **3.3 Impact of a Subsidiary on SBCL's Current Corporate Structure**

Creation of a new corporate subsidiary has a number of implications for SBCL. Questions arise both as to where the new subsidiary will "fit" into the SBCL corporate structure, and what type of relationship the subsidiary will have with SBCL's current Wealth Management Division, from which the employees, clients, revenues, and expenses are being taken to form the subsidiary. This sub-section addresses these issues.

#### ***3.3.1 Relationship of EIA to SBCL***

SBCL currently has four subsidiaries on its books, although three of these four subsidiaries have been relatively dormant. The relationship of EIA to SBCL will be defined within the following areas:

- Impact on SBCL Organization Structure – The subsidiary will report into the Bank through the Retail and Community Banking Group. Howard Gould, Vice Chairman for the Group, will be Chairman of the subsidiary and responsible for all of its operations.
- Impact on the Eureka Board – The subsidiary will be the hired Investment Advisor to the Eureka Funds. The Eureka Board voted at its February 2001 meeting to approve the role of EIA as the new investment advisor for the Eureka Funds, contingent on its formation and successful registration with the SEC.
- Impact on SBCL Personnel – As described in Section 4.0, eight current employees of SBCL will transfer into the subsidiary, not counting Bob Bannon. These employees will no longer be employees of SBCL, but will be exclusive employees of EIA. For those employees affected, however, there will be no loss of employment benefits, such as medical or retirement benefits, which will continue to be provided to EIA staff under a service level agreement with SBCL's HR Department.
- Impact on SBCL Client Relationships – Only a small number (less than 10) clients of SBCL will transfer into the subsidiary. It is not anticipated that the SBCL client base will provide a significant source of leads for the subsidiary. On the contrary, if the subsidiary is successful it may open the doors to a new client base for SBCL.
- Impact on SBCL Accounting and Budgeting Procedures – Revenues and expenses of the subsidiary will "roll-up" into SBCL through the payment of a dividend from the subsidiary to SBCL. As an independent company for which SBCL is simply a

shareholder, however, the subsidiary will subject its own budgeting process primarily to the approval of its own Board of Directors, with the caveat that the subsidiary's budgeting schedule must be timed to be consistent for providing all necessary "roll-up" information to SBCL for its own books and budgets in a timely manner.

- Impact on SBCL "Branding" Efforts – By virtue of its different target markets and unrelated name, EIA is not likely to distract from efforts by SBCL to position itself as the best relationship bank in California. However, if EIA is successful, ownership of a successful investment management subsidiary could help position SBCL to move into the tier of financial institutions that are known for providing a full range of financial services.
- Impact on SBCL Efforts to Acquire an RIA – SBCL has been "on the lookout" for a Registered Investment Advisor that it could acquire in an effort to boost its own investment management efforts. Creation and registration of its own RIA will not distract from that effort, and may in fact aid in the process, by convincing potential acquisition targets of SBCL's seriousness in that marketplace. No regulatory restrictions prevent a bank from owning more than one RIA, so SBCL could retain the option to either merge an acquired RIA into its own investment subsidiary or to operate both RIA's as independent and separate entities.
- Impact on SBCL's Relationship with SBL – Creation of an investment subsidiary may cause additional regulatory requirements for SBL as well, as has already been the case with the FSA. However, these regulatory requirements appear to be minor. In addition, the creation of a separate investment subsidiary may help SBCL to regain its Registered Investment Advisor status in Japan as well, a status that SBCL had to relinquish in 2000 due to the complications of listing an organization as large as SBCL as a Japanese investment advisor. Listing EIA as the advisor (which would otherwise be more appropriate than listing SBCL) will be much easier due to its limited staff and simpler corporate structure. This could lead to expansion opportunities in the Japanese market, as well as co-branding opportunities with SBL's investment advisory affiliates, similar to those opportunities that have already been pursued between SBL's affiliates and the Investment Management Department.

### ***3.3.2 Relationship of EIA with SBCL's Wealth Management Division***

By virtue of the fact that all of the personnel, resources, clients, revenues, and expenses for EIA are being drawn from SBCL's Wealth Management Division, clearly the creation of EIA will have a significant impact on the Division. Specific staffing and financial impacts are discussed in more detail in Sections 4.0 and 6.0. A broad overview of the impact on WMD of the creation of EIA are included below. These impacts include:

- Loss of Personnel – Eight of the individuals forming EIA will come from the current WMD. Since these individuals are essentially leaving SBCL to pursue the growth of EIA, they are, for all intents and purposes, being pulled out of the WMD. Five of the eight individuals are being removed from within the current Investment Management



of the WMD, while the other three are being drawn from the administrative support unit within WMD. The impact of the loss of these individuals is discussed in more detail in Section 4.0 and in Table 4.1. In addition, certain open FTE positions currently slated for the WMD, both within the Investment Management Department and in other areas of WMD, will be affected by the new staff requests made for EIA.

- Reorganization of the Investment Management Department – The IM Department, one of three departments currently within WMD (along with Investment Sales and Personal Financial Services), will need to be restructured as a result of losing five staff members to the subsidiary. A detailed plan for this reorganization is included in Section 4.0, and a revised organization chart is presented in Figure 4.1. Broadly, Bob Bannon will remain the department head of the Investment Management Department, while the department is refocused on separate account portfolio management for the WMD.
- Reporting Structure of the Subsidiary – Since the subsidiary will report directly in to the Chairman of its own Board, who is also the Vice Chairman of SBCL, the subsidiary will effectively be pulled out of the organizational structure of the WMD completely. Mr. Bannon, in his role as President of EIA, will no longer report in to the head of WMD. However, in his capacity as department manager for one of the three departments within WMD, Mr. Bannon will continue to report to the head of WMD for all issues concerning the Investment Management Department, and in his continuing role as Chief Investment Officer for SBCL.
- Reorientation of the Focus of WMD – By placing all responsibility for the marketing and asset management of institutional clients and the Eureka Funds into the subsidiary, and by removing the subsidiary from WMD, this effectively redefines the focus of the WMD to be exclusively in the pursuit of separate and individual clients, rather than institutional clients or commingled vehicles.
- Provision of Services Back to WMD – The subsidiary will be used to provide certain services back to WMD, primarily in the areas of investment research and performance analysis (as well as Mr. Bannon's services as a manager). The WMD will provide direct compensation to the subsidiary for these services, under the provisions of various service level agreements, the terms of which are to be spelled out at a later time.

## **4.0 STAFFING**

### **4.1 Overview**

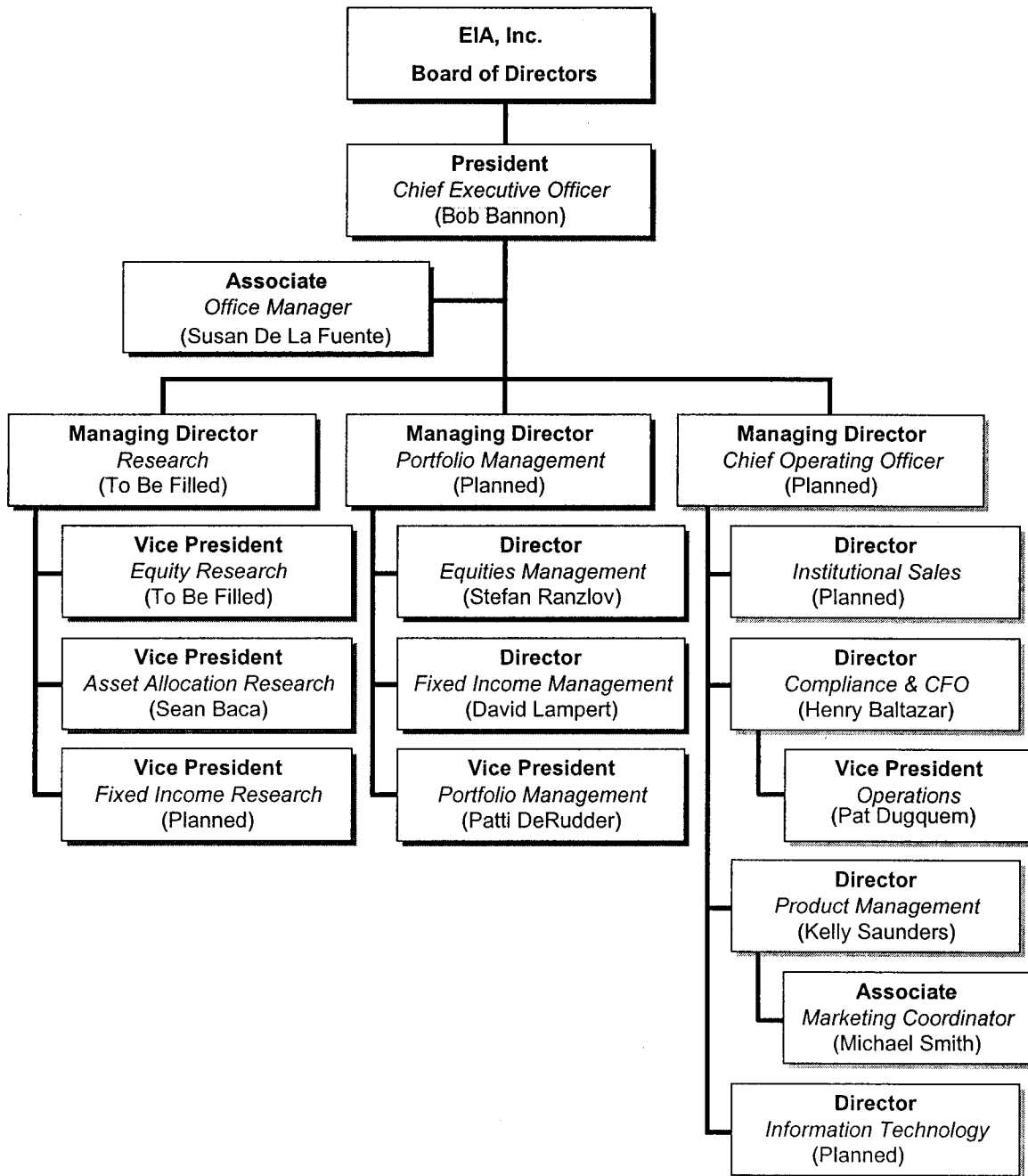
This proposal recommends that Eureka Investment Advisors be allocated an initial staff of 14 individuals to begin operations on April 1, 2001. Six of the 14 positions requested will be filled using SBCL staff members currently working in the Investment Management Department of SBCL, three of the 14 positions will be drawn from SBCL staff members currently working in areas of the Wealth Management Division other than the Investment Management Department, two of the 14 positions will be filled with vacancies currently being recruited for the Investment Management Department, and the remaining three positions are to be hired. An additional three positions are highlighted in this proposal for EIA (bringing the total staffing to 17 full time employees) contingent on sufficient growth in clients and assets over the next two years.

After discussing the broad organizational structure of the subsidiary, this section discusses the specific job functions and titles of the staff members of EIA. An analysis of the impact on the Wealth Management Division, including a suggested reorganization of the Investment Management Department, is also included.

### **4.2 Organization Chart**

Figure 4.1 (following page) provides a complete Organization Chart for Eureka Investment Advisors, Inc. Note that each box on the organization chart contains the corporate title of the position, a brief note of the function, and an indication of who would fill the position. In the event that the position is to be filled with a specific individual currently within SBCL, that individual is identified. For those positions to be authorized and filled immediately, the box indicates "To Be Filled." For those positions that will only be created and filled contingent on sufficient asset and revenue growth over the next two years, the box indicates that the position is "Planned."

**Figure 4.1**  
**Eureka Investment Advisors, Inc.**  
Organizational Chart



#### ***4.2.1 Organizational Functions***

In an effort to match the structures of similar organizations, EIA will have three main business units:

- Research – The Research unit will be headed by a Director of Research and will have as its primary duty providing the Portfolio Management unit with valid inputs, signals, forecasts, and other necessary factors for the Portfolio Management unit to create superior investment portfolios for clients. Research tasks will include equity research, fixed income research, and asset allocation research.
- Portfolio Management – The Portfolio Management unit will be headed by the subsidiary's Chief Investment Officer, and will have as its primary duty creating superior investment portfolios for clients. The Portfolio Management unit will be staffed with portfolio managers who will seek to specialize in a given area of investment expertise (equities, fixed income, money markets, etc), but who will also be cross-trained to offer a mix of programs, or to provide backup to other portfolio managers in the event of client travel, vacation, illness, resignation, etc.
- Operations – The Operations unit will be headed by the subsidiary's Chief Operating Officer, and will have several functions: operational and technological support of the subsidiary, marketing, sales, compliance, and accounting. All subsidiary personnel that are neither research nor portfolio management will fall into the Operations unit.

#### ***4.2.2 A Note on Key Executive Positions***

As can be seen from the Organization Chart in Figure 4.1, none of the three key executive positions heading each of the three business units will be filled at the inception of the subsidiary. Far from being a mistake, this decision was deliberate on several fronts. First, the initial size of the subsidiary, with less than 10 clients, suggests a need to minimize on personnel, particularly management personnel, until growth warrants. Second, leaving these key positions unfilled provides an important incentive to the staff in each of the business units in the subsidiary, insofar as leaving these positions unfilled provides opportunities (and thus incentive) for advancement.

Until such time as each of the positions is filled, Bob Bannon will perform the functions of each unit head, in conjunction with the most senior individuals within the business unit. A search for a Director of Research is currently ongoing, and hopefully will be filled within 3-4 months of the creation of the subsidiary. In the Portfolio Management unit, David Lampert is a seasoned investment professional who will assist Mr. Bannon in the running of the Investment unit (as Mr. Lampert did when he was Mr. Bannon's Deputy Department Manager within SBCL's Investment Management Department). In the Operations unit, Henry Baltazar will work with Mr. Bannon to insure that all areas of support for the subsidiary are functioning smoothly.

### **4.3 Title Structure**

This sub-section discusses the rationale for the corporate titles to be used within the subsidiary, as well as the functional titles of each position. A brief description of the responsibilities of each position is also included.

#### ***4.3.1 Corporate Titles in the Subsidiary***

In order to help the subsidiary compete with other Registered Investment Advisory firms in the business, EIA will not use the corporate titles commonly seen within banks, and widely used within SBCL. Instead, the structure of corporate titles within EIA is patterned after the typical design of a Wall Street investment management firm:

Managing Director – Responsible for a business unit, as well as all the individuals within that unit. The Director of Research, the Chief Investment Officer, and the Chief Operating Officer would typically be Managing Directors. If any area within a business unit were to grow sufficiently large (such as hopefully would be the case with Sales), a new business unit may be created and assigned a new Managing Director as a reflection of that group's success.

Director – Responsible for a product line within a business unit, and may or may not have direct reports. A director of sales, marketing, operations, compliance, equity portfolio management, fixed income research, etc., would all qualify for this title if they had sufficient experience and if the product line warranted.

Vice President – The lowest level of “officer” within a product line, an employee that does not have direct reports but that nevertheless is capable of performing his/her job function without frequent supervision. An equity portfolio manager reporting to the Director of Equity Portfolio Management, for example, would be a vice president.

Associate – A support person within a product line, someone who needs regular direction and supervision. A “catch-all” category for entry-level officers, assistants, office managers, marketing coordinators, junior portfolio managers, etc.

#### ***4.3.2 Functional Titles and Responsibilities***

The following lists all the staff positions described on the Organization Chart in Figure 4.1. The positions are described without regard to which individuals from within SBCL might fill the positions – see Section 4.4 (and Table 4.1 in the Appendix) for a description of those individuals in SBCL who might be best-suited to fill these positions, and the impact on SBCL of transferring those individuals into the subsidiary.

President & CEO - Highest ranking officer in the subsidiary. Member of the Board of Directors of the subsidiary. Has as direct reports all managing directors. Speaks on the subsidiary's behalf at all committee meetings within SBCL and beyond. Responsible for

asset growth, profitability, compliance, client satisfaction, investment performance, and all other goals of the subsidiary.

Managing Director, Research – The overall head of investment research for the subsidiary. Has final authority as to the subsidiary's recommendations on individual securities, as well as the subsidiary's recommendations on market direction, economic outlook, and asset allocation. Has no authority to overrule investment decisions, and does not actively manage assets. Speaks for the subsidiary's market views to the media, at conferences, to clients, and within SBCL.

Managing Director, Portfolio Management – Effectively the subsidiary's Chief Investment Officer, has as his direct and indirect reports all staff in the subsidiary that manage or advise client assets. Responsible for all investment product lines, and ultimately responsible for the subsidiary's composite investment performance.

Managing Director, Chief Operating Officer – The most senior administrative officer of the firm. Responsible for sales, marketing, product development, operations, compliance, finance, budgeting, and human resources. Effectively responsible for all areas of the subsidiary except investment and research.

Vice President, Equity Research – The officer in the research area responsible for recommendations and forecasts on individual equity securities, both domestic and global. Not responsible for recommendations and forecasts on the broad direction of the markets or on the economy.

Vice President, Fixed Income Research – The officer in the research area responsible for recommendations and forecasts on individual fixed income securities, both domestic and global, as well as money market instruments. Not responsible for recommendations and forecasts on the broad direction of markets, the economy, or interest rates.

Vice President, Asset Allocation – Similar in nature to what is often call a Senior Investment Strategist at many investment firms, this individual is responsible for the subsidiary's general market outlook, economic forecasts, asset class forecasts, asset allocation and sector rotation recommendations.

Director, Equities Management – The most senior investment officer directly responsible for equity investments. Responsible for the management of all equity related mutual funds, as well as institutional accounts which have a focus on equities. Will work closely with (but not be in charge of) the Director of Research and any research staff involved in equity research. Will also provide guidance and expertise to any separate account portfolio managers whose mandates include equities in their overall investment responsibilities.

Director, Fixed Income Management – The most senior investment officer directly responsible for fixed income and money market investments. Responsible for the management of all fixed income and money market mutual funds, as well as institutional accounts which have a focus on fixed income or liquidity management. Will work

closely with (but not be in charge of) the Director of Research and any research staff involved in fixed income research. Will also provide guidance and expertise to any separate account portfolio managers whose mandates include fixed income as part of their overall investment responsibilities.

Vice President, Portfolio Manager – This investment officer plays multiple roles as a support individual within the investment area. His/her responsibilities would include (1) serving as a backup portfolio manager for other portfolio managers during vacations, illnesses, and other absences from the office; (2) serving as portfolio manager for those accounts which are neither clearly equity nor fixed income (i.e., balanced or asset allocation programs); (3) Providing client servicing on all accounts. This individual will also serve as co-manager of the money market and liquidity management accounts.

Director, Institutional Sales – The individual responsible for business development of institutional and separate accounts. This individual will have no direct responsibilities for the development or growth of the commingled (mutual) funds. This individual will also be crucial initially in helping the firm become AIMR-compliant, as well as to help the subsidiary gain needed exposure amongst the critical investment management consulting firms through direct contact, conference presentations, media publicity, etc.

Director, Compliance and Finance - The officer responsible for insuring that all activities are in compliance with SEC, bank regulators, the parent bank, and industry standards. Also, the officer in charge of budgeting and financial analysis for the subsidiary.

Vice President, Operations – The individual that will maintain the “back office” systems for client accounts, reconcile trades between brokers, the custodian, and the portfolio manager, and produce all performance reports. Operations will report into the Director of Compliance and Finance.

Director, Marketing and Wholesaling – The individual responsible for the growth of the Eureka Funds, as well as for supervising the production of marketing materials for all products, including funds, institutional accounts and separate accounts. This individual will work closely with (but not be a supervisor of) the Director of Sales. The Marketing Coordinator will report directly into this position.

Director, Information Technology – The officer in charge of all of the subsidiary’s technology needs, including network, PC, software, research vendors, etc.

Associate, Office Manager – An all-purpose individual for the administration of the office, maintaining financial records, providing for human resources issues, establishing policies, monitoring all service level agreements with SBCL, etc.

Associate, Marketing Coordinator – This individual will assist both the marketing director and the director of sales in the production of materials for sales and client servicing. This individual will also coordinate communications with investment management consultants, conference officials, press, etc.

#### **4.4 Staffing Impact on Wealth Management Division**

Since all 14 individuals to be authorized for EIA either currently work in the Wealth Management Division or the functionality of the position is currently performed within the Wealth Management Division, this proposal dramatically affects staffing, budgets, and overall direction of the Division. This sub-section discusses the impact of the creation of the subsidiary on staff and organization, both within the Wealth Management Division overall as well as within the Investment Management Department specifically.

##### ***4.4.1 Overall Staffing Impact on Wealth Management Division***

Table 4.1 (see Appendix) highlights those individuals in the Wealth Management Division that will be affected by the creation of EIA. The table includes the nine individuals that will be transferred into the subsidiary as well as one individual (Don Silva) who will not be transferred into the subsidiary but whose position will be significantly affected nevertheless (see Section 4.4.2 for a fuller discussion of the impact on the management structure of the Investment Management Department).

As Table 4.1 indicates, by and large the staffing impact on the Wealth Management Division is relatively light. This is due to the fact that while a significant number of individuals are being transferred out of WMD and into EIA, those individuals are taking their full functionality with them, thus leaving little or no loss of effective personnel within the WMD. In some cases (Bob Bannon, Sean Baca, Pat Dugquem, Susan De La Fuente, and any future research personnel hired), the individuals will continue to perform most of the same functions for the WMD that they had performed previously, thus causing no loss of functionality for the WMD. Since the costs of those individuals will be transferred in full to the subsidiary, their services will be billed back to the Wealth Management Division through a series of service level agreements.

Other individuals are taking their full tasks with them into the subsidiary, generating no loss of functionality to the Division since the tasks performed will be completely removed as a responsibility of the Division. These tasks include Eureka wholesaling and product management (Kelly Saunders), Eureka Fund Management (David Lampert, Stefan Ranzlov, and Patti DeRudder replacing Don Silva). Don Silva will stay with the WMD to replace both the portfolio management shortfall created by Patti DeRudder's departure, and the departmental management shortfall created by the departure of the Deputy Department Manager (David Lampert).

The only individual whose departure creates a true unfilled shortfall within the Wealth Management Division is Henry Baltazar. While under the WMD, Henry had provided many of the same tasks that he will be providing to the subsidiary (mutual fund and SEC compliance), but he also had managerial responsibility for other areas of compliance (trust and brokerage), as well as managerial responsibility for brokerage operations. It is anticipated that these functions can move to other areas within the WMD without compromising their level of service. The Trust Compliance Officer (Geoff Purdy) who previously reported to Henry Baltazar can (and should) report into the head of Trust, Don



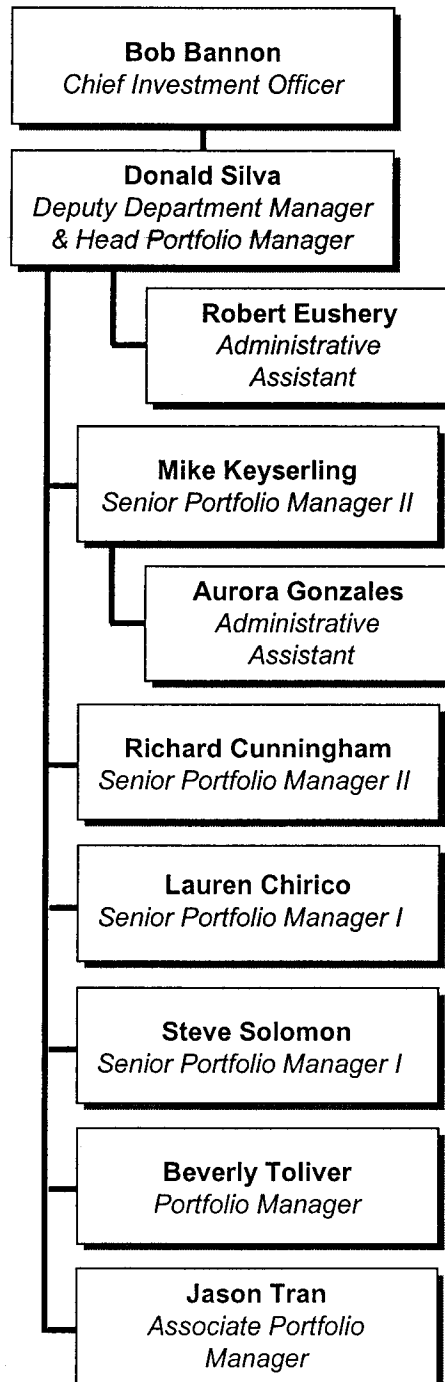
Soucie. The Brokerage Compliance Officer (Bill Conrad) as well as the brokerage operations team (four individuals) will report into either Michael Sessum or James Ely, depending on the direction taken in our efforts to push out a retail brokerage. In any event, the departure of Henry Baltazar will not pose a significant problem to the WMD, and will in fact help accelerate consolidation of areas in the Division (the retail brokerage) which were on track for consolidation nonetheless.

#### ***4.4.2 Reorganization of the Investment Management Department***

The loss of five members of the Investment Management Department, along with two research positions currently under active recruitment, represents a significant reduction of staff for the 17-member Investment Management Department of SBCL. However, many of the responsibilities of the Investment Management Department are also transferring to the subsidiary, so the loss should not necessarily create a productivity shortfall. In fact, the creation of the subsidiary opens the door for a much-needed reorganization and reorientation of the Investment Management Department, as described below.

The Investment Management Department will be reorganized as a result of the creation of the subsidiary to focus more directly on the provision of separate (i.e., trust and managed agency) account management. The only employees remaining in the Investment Management Department after the creation of the subsidiary will be portfolio managers who specialize in managing the traditional types of accounts sought by the Wealth Management Division. Figure 4.2 (following page) provides an organization chart for those individuals who remain in the Investment Management Department following the pushout of the subsidiary. As the org chart clearly indicates, the Investment Management Department will have a very flat organizational structure, comprised of six portfolio managers reporting in to one head portfolio manager, who in turn reports in to the manager of the Investment Management Department (Bob Bannon, who will continue to be SBCL's Chief Investment Officer and Investment Management Department Manager). Two administrative support personnel will also continue to perform their existing functions of administrative support for the entire portfolio management team, and will report in to the two most senior members (Don Silva and Mike Keyserling) of the newly reorganized Investment Management Department.

**Figure 4.2**  
**Investment Management Department**  
Reorganization Following Subsidiary Creation



The advantages of this reorganization are as follows:

- Focus on Core WMD Clientele – The Investment Management Department will no longer be distracted by trying to meet the dual tasks of growth in the commingled funds and growth in the separate accounts. The remaining portfolio managers will be well-suited for working directly with trust officers and business development officers within the WMD, and can concentrate more closely on the customized, personalized relationship management that should be the hallmark of the WMD.
- Defined Role for Don Silva – Due to the fact that Don Silva previously performed many different functions (Eureka Fund Manager, Separate Account Manager, Common Trust Fund Manager, Head of Trading), some of which could not transfer into the subsidiary for legal reasons, it was necessary to have Don relinquish his management of the Eureka Funds and to stay with SBCL. This role fits well for Don, who will be able to absorb more portfolio accounts, concentrate on the common trust funds, and enjoy career advancement to a managerial position after many years with SBCL.

## **5.0 MARKETING PLAN**

The primary purpose for creating Eureka Investment Advisors is to comply with Gramm-Leach-Bliley, but from this stems an opportunity to grow assets. While the subsidiary needs to be created and would be profitable simply through its management of the current Eureka Funds only, the subsidiary represents an opportunity to achieve growth in assets and to diversify SBCL's income stream. This section details the products that will be offered by EIA, the target clients to whom those products will be offered, the distribution channels to be used, and finally, an evaluation of the potential for asset and revenue growth.

### **5.1. Product Offerings of EIA**

#### ***5.1.1 By Strategy***

The products offered by EIA will be based on a slate of quantitative investment management products offered previously by the Investment Management Department of SBCL. These product offerings will fall into three broad categories, and will include:

- Equity Based Products
  - Large Cap Core Domestic US Equity
  - Small Cap Core Domestic US Equity
  - Global Sector Rotation
- Fixed Income Products
  - Investment Grade Domestic Fixed Income
  - Active Liquidity Management
- Balanced Programs
  - Domestic Balanced
  - Global Balanced

Each of these products will use the strategies created and enhanced within the Investment Management Department of SBCL. The same research team and portfolio management team that developed and sustain these products will be transferred into the subsidiary, and will continue to follow the processes already established. The categories listed above are the same descriptions provided in Part II of Form ADV, as filed with the SEC, and which is mandated to be delivered to new clients at the time of their agreement to receive services from the RIA.

#### ***5.1.2 Fee Schedules***

The subsidiary will charge an annualized fee based on a percentage of the net assets managed or advised, valued at market. The fee is payable quarterly in arrears unless

otherwise stipulated. Under certain circumstances, the subsidiary may charge a lower annualized fee in exchange for receipt of a performance-based fee, where performance is measured relative to an agreed-upon benchmark.. Fees will range from 25-40 basis points for money market and fixed income programs, up to 70-90 basis points for equity and balanced programs. All fees are negotiable, depending on the size of the client mandate and the nature of the client relationship.

### **5.1.3 Future Offerings**

While the initial product offerings of EIA will suffice for the clients that are to be transferred into the subsidiary, additional products and services may be offered in the future, subject to the condition that these products are consistent with the quantitative investment philosophy of the subsidiary. Additional products could include:

- Alternative Equity Products – Current equity products are limited to the equity universes of large cap, small cap, and global cap. Additional benchmarks, such as mid cap, active OTC, and value or growth strategies may be pursued.
- Tax Exempt Fixed Income – Expertise (as well as assets) for the management of tax exempt fixed income securities exists within SBCL's Investment Management Department through the management of several tax exempt fixed income Common Trust Funds. As opportunities arise, such strategies may be transferred to, or at least replicated within, the subsidiary.
- Offshore Funds – Certain popular quantitative strategies, such as market neutral and long/short equity programs, gain their advantage through being established within an offshore fund structure. If conditions warrant such strategies and vehicles may be pursued.

## **5.2 Analysis of Potential Markets**

### **5.2.1 The RIA Marketplace**

The new Gramm-Leach-Bliley law will require all mutual funds to be advised by investment managers that are Registered Investment Advisors (RIA's). The following statistics give an indication of the RIA business in the United States:

|                                       |                 |
|---------------------------------------|-----------------|
| Total Number of RIA's                 | 13,500          |
| Total Assets Managed by RIA's         | \$17.4 Trillion |
| Average Assets Managed per RIA        | \$1.3 Billion   |
| Number of RIA's Managing Mutual Funds | 2,800           |
| Median Mutual Fund Assets per RIA     | \$250 million   |

As can be seen by these statistics, the majority of RIA's are not involved in managing mutual fund assets. Most RIA's are single individuals who seek the status of RIA to

assist in marketing themselves as personal financial planners. While the average number of assets managed by RIA's seems significant (\$1.3 billion), the distribution of size for RIA's is very skewed – the vast majority of RIA's manage less than \$100 million in assets, while a much smaller fraction manage very significant sums of assets. Also, it should be noted from these statistics that the typical RIA manages only a very small amount of mutual fund assets – typically an RIA is established to launch a single mutual fund, which grows very slowly.

These statistics paint a very favorable competitive picture for EIA. At its inception, EIA will be far better positioned than the typical start-up RIA. Some of the advantages for EIA will include:

- Initial assets of \$1.3 billion, equal to the industry average
- Mutual fund assets of almost \$1 billion, well in excess of industry median
- A stable anchor client (Eureka Funds, primarily SBCL-directed assets)
- Seasoned group of investment professionals who have worked as a team
- All necessary resources provided at startup by SBCL
- Branded with a unique niche investment style (quantitative investing)
- PROFITABLE FROM ITS DAY OF INCEPTION

Very few start-up investment advisory firms begin with such advantages. The typical start-up RIA begins with two or three investment professionals breaking away from a larger organization, taking one or two tenuous clients. Such a start-up is almost always understaffed, unprofitable, distracted by business initiation needs, and highly dependent on a small set of clients that will not endure for too long any hint of inferior performance from the new firm. Eureka Investment Advisors is being launched under far more stable conditions with a much greater chance for long-term success.

### ***5.2.2 Target Clients for EIA***

EIA will target three broad groups of accounts, as described below. At its inception, EIA will have clients in each of these categories. It is not anticipated that EIA will have individuals as clients within the foreseeable future. There are three reasons for having EIA avoid an individual client base:

- Individual clients are better suited for management within SBCL's WMD
- Individual clients are distracting to an advisor seeking an institutional orientation
- SEC registration procedures increase in complexity when individuals are solicited

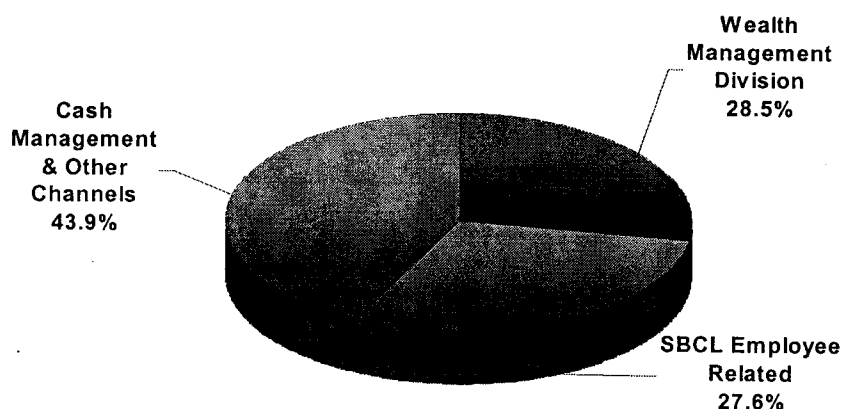
Overall, EIA's quantitative investment style is best suited to, and best appreciated by, a sophisticated client base. With that goal in mind, the following three groups will likely be the primary client focus for EIA.

### 5.2.2.1 Commingled Funds

The primary anchor client for EIA will be the Eureka Funds. Launched as a series of proprietary funds by SBCL in 1997, this fund family has met or exceeded its original goals for revenue and asset growth, as illustrated on the following page in Chart 5.1 and Chart 5.2.

Virtually all of the assets in the Eureka Fund have been directed into the Funds by SBCL channels. As indicated in Chart 5.3, approximately 44% of the Eureka Funds derive from the efforts of SBCL's Cash Management Department, approximately 28% of the assets derive from allocations made to the Funds by SBCL's defined benefit Retirement Plan, and roughly 29% derive from allocations made by SBCL for its fiduciary clients.

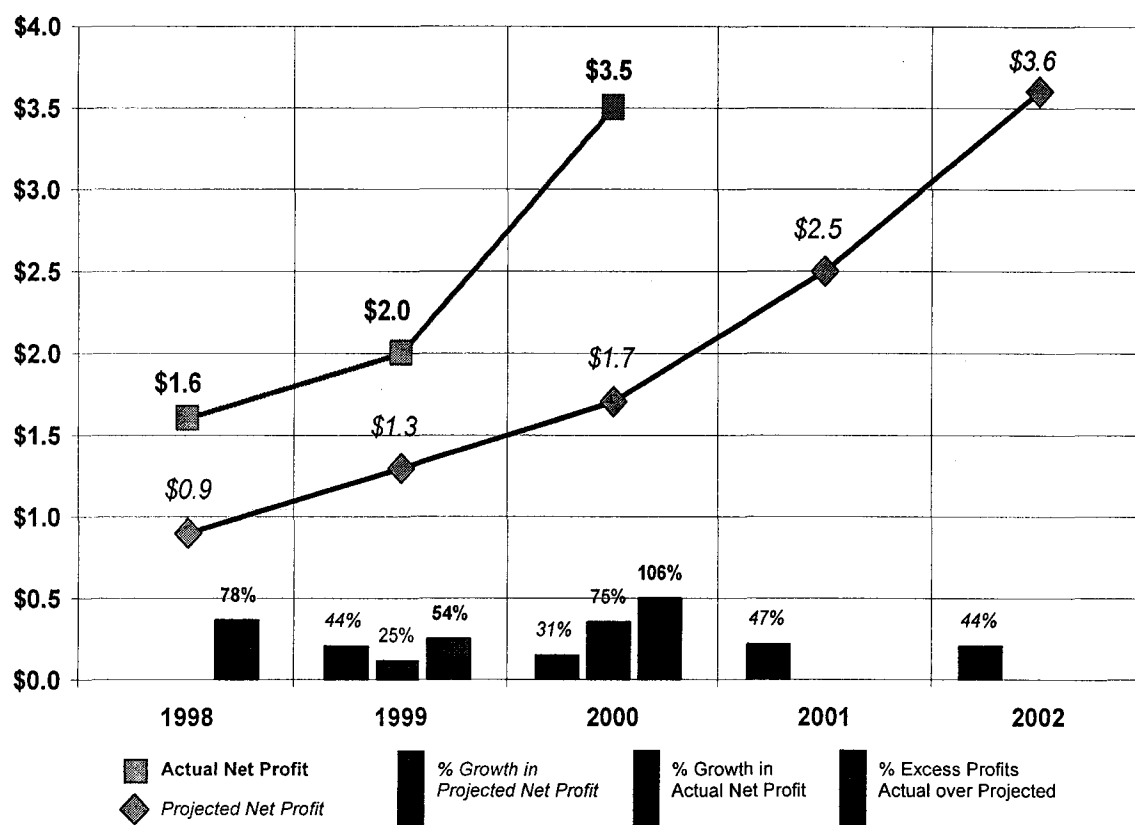
**Chart 5.3 Eureka Funds Average Assets**



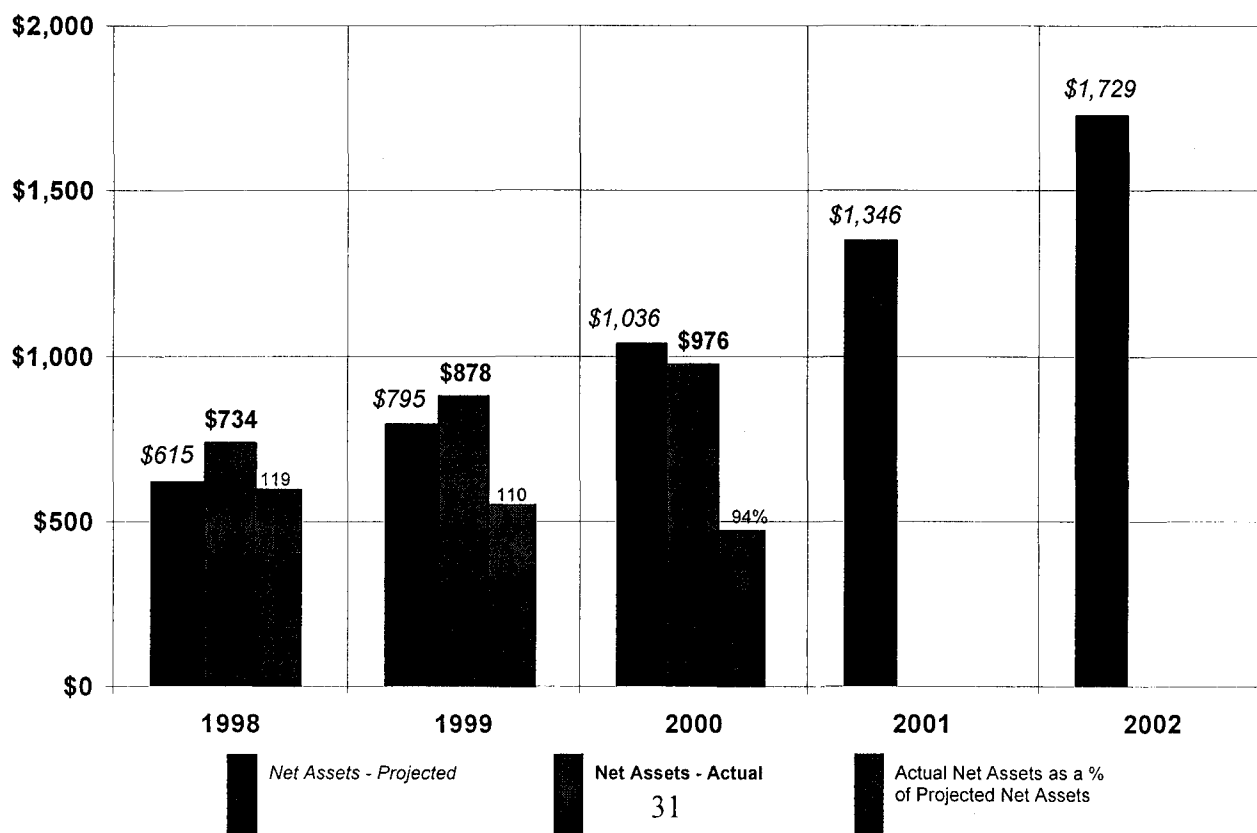
The fact that most Eureka assets have been SBCL-directed is both an advantage and a disadvantage to EIA. On the positive side, the solid relationship between SBCL, the Eureka Funds, and EIA helps insure that the Eureka Funds will be a steady anchor client for EIA. On the negative side, this concentrates too much of the business risk of managing the Funds into one source—a major goal of EIA in its first years of operation will need to be the pursuit of non-SBCL-directed assets. This is particularly true on the fiduciary side, where the concentration of fiduciary assets has drawn unwanted attention from banking regulators.

While the Eureka Funds are obviously a key target client for EIA, other commingled fund vehicles will also be of interest. EIA will pursue opportunities for commingled fund management from two additional sources: subadvisory for other registered investment companies, and the establishment of offshore and onshore funds. Both goals are ambitious, however, given the need to establish EIA as a recognized name in the RIA community before such goals could be attempted. Pursuit of other commingled fund advisory, therefore, will not be an immediate priority of EIA.

### Chart 5.1 Eureka Revenues, Projected vs Actual



### Chart 5.2 Eureka Asset Growth - Projected and Actual





### 5.2.2.2 Institutional Accounts

If EIA is to succeed outside of its management of the Eureka Funds, then it will most likely do so by attracting institutional investors. Typical institutional investors include defined benefit pension plans, unions, foundations, endowments, and government agencies. Some of the salient features of institutional investors include:

- Tax Exempt – The typical institutional investor is exempted from paying taxes on investment income or realized capital gains. This is a significant advantage for the investment advisor to an institutional investor, since it allows the advisor to focus primarily on their investment process, without the distraction or constraint of having to avoid an otherwise preferred investment strategy due to the fear that it might generate unwanted capital gains.
- Infinite Time Horizon – Unlike an individual investor, the typical institutional investor does not have a final termination point for the growth of assets. Most institutions are trying to grow their assets as large as possible *ad infinitum*. This also is an advantage for the investment advisor, since again the advisor's strategy can be implemented without the distraction of knowing that the bulk of the assets will need to be liquidated, transferred, or converted to a different investment objective at the end of a finite time horizon.
- Sophistication – Many institutional accounts are sufficiently large that they have an internal staff of investment professionals to oversee the account. While in some cases these investment professionals actually manage the assets (thus precluding any opportunities for outside investment advisors), in most cases these investment professionals exist only to supervise the search and review the performance of outside managers. Again this is an advantage to the outside investment advisor, since it usually allows for a higher level of communication about the investment process being applied to the account.
- Nature of the Investment Mandate – While most institutional accounts have a balanced mix of assets with an infinite horizon, typically institutional investors allocate only very narrow, homogenous portions of their total institutional assets to an advisor, and usually only for a fixed period of time. If an advisor wins an allocation mandate from an institutional account, typically the mandate will be within a narrow area (e.g., large cap core domestic equities), for only a fraction of the total assets available (e.g., usually between \$25 million to \$100 million, with some mandates as high as \$500 million), and for only a defined period of time (usually 3-5 years). Mandates are renewable, although renewal is largely dependent on investment performance over the original mandate period.
- Preference for the Unique – With so many RIA's competing for the same institutional business, institutional investors are frequently interested in investment strategies that are new and different. Quantitative investment strategies have a particular appeal to institutional investors, both because pure quantitative strategies are relatively rare

(most quantitative managers instill at least some degree of discretion), and also because the sophistication level appeals to the investment professional charged with allocating the institutional assets. Generally a quantitative investment advisor's penchant for risk control and performance attribution feeds directly into main task of the institutional professional, that is, to monitor the risks taken and identify the sources of performance achieved by individual managers.

- Competitive Fees – Since institutional business is so highly prized, fees can be relatively competitive (and much lower than fees that can be charged to individual investors, or inside a commingled fund). A typical active equity mandate might hope to earn between 50 and 75 basis points (higher if it involves an unusual amount of effort, such as with small cap or global equity mandates). A typical active fixed income mandate might hope to earn between 30 and 50 basis points, depending on the level of effort (convertibles, mortgage-backed, and high-yield fixed income mandates earn more than active investment grade government/corporate mandates). However, given the size of the typical mandate and the length of time the account is “secure” with the advisor, a typical institutional client can generate an average of \$100,000 per year in fees for an average of four years.

#### *5.2.2.3 Corporate Accounts*

Corporate accounts will not be the mainstay of EIA, but EIA will be open to managing such accounts. Corporate accounts are those separately managed investment mandates from corporate and commercial investors who are generally taxable, seeking a balanced mandate (or perhaps simply liquidity management), and who are not generally sophisticated investors. The most desirable corporate account for EIA would be that of an incorporated “family office” of a very high net worth individual, seeking a mix of equity and fixed income management. Liquidity management and short-term fixed income management may also be a part of EIA's mandate. Finally, EIA may also solicit as corporate or separate account business mandates to provide services not necessarily directly involving investment management. The advisory work to be performed by EIA in the areas of investment research and performance analysis for SBCL, for example, would be the type of services that might also be pursued with firms other than SBCL if a business opportunity existed.

Unlike its pursuit of commingled fund or institutional account business, the pursuit of corporate accounts by EIA may bring it into direct competition with the asset gathering efforts of SBCL's Wealth Management Division. In particular, the most likely area of overlap would be in the provision of active liquidity management accounts for medium sized corporations. It will be the policy of EIA (as imposed by Bob Bannon, who will serve both as the President of EIA and the manager of SBCL's Investment Management Department) to defer to the Wealth Management Division for most active liquidity management accounts. This will be particularly the case where such accounts have been developed with companies for which SBCL already has a strong business relationship, and which have been uncovered through SBCL's network of commercial or retail banking centers. Active liquidity management accounts, although beneficial in general,

tend to be labor intensive, low profit, and not needing of quantitative investment services. Such accounts are best managed using the economies of scale inherent within SBCL, rather than the more limited resources of EIA. Only if an account desires to be within the subsidiary, or if it requires quantitative investment management, or if it does not have a compelling pre-existing relationship with SBCL, will it be pursued by the subsidiary.

### **5.3 Projected Distribution Channels**

#### **5.3.1 Institutional Sales**

In order for EIA to develop an institutional investment business, the asset gathering effort for institutional accounts must be focused within the subsidiary. SBCL does not currently have an institutional sales effort, and there would be little synergy to creating one and not putting it into the subsidiary. Most of the sales effort currently underway in the WMD is geared towards exploiting existing SBCL client relationships, which do not include any of the institutional accounts that would be sought by EIA. In addition, as described in detail below, the pursuit of institutional investment mandates generally does not involve direct contact with institutional investors, but instead involves an elaborate system of intermediaries that must be cultivated. Expertise in this process does not currently exist within WMD's sales force, and would need to be recruited externally. A brief overview of the institutional sales process is provided below.

##### *5.3.1.1 The Institutional Sales Process*

Institutional investors rarely place assets directly with an institutional investment manager. There are too many managers pursuing too many strategies for the limited investment staff of most institutional accounts to be able to track, review, and recommend the right investment manager for each asset class or investment specialty desired by the institution. Virtually all institutional investors allocate assets to institutional managers through a set of "investment management consultants" that specialize in the tracking, evaluation, and recommendation of institutional managers. By removing the manager search process from the set of tasks that institutional investors must perform, it allows the investor to focus their attentions on the managers they have actually hired, as well as on the overall performance of the entire institutional account.

##### *5.3.1.2 The Role of the Investment Management Consultant*

In the last 25 years an entire cottage industry has arisen within the institutional investment marketplace known as investment management consulting (IMC). There are currently only about ten IMC's in the marketplace covering the majority of institutional investors. These IMC's include Wilshire Associates, Towers Perrin, Frank Russell, Watson Wyatt, RogersCasey, Cambridge Associates, and Callan Associates, amongst other names. Smaller IMC's exist at the fringes, but the top 8-10 provide most of the mandates in the marketplace.

Investment management consultants seek to assist institutional investors with the fiduciary burdens that fall upon them in the care of the institutional assets that are their responsibility. This is particularly useful for smaller institutional investors, particularly those who do not have the time or the resources to devote full-time to the oversight of institutional assets (such as, for example, the CFO of a medium-sized firm who is charged with managing the firm's defined benefit pension plan but who may be more of a financial analyst or accountant than an investment specialist). IMC's traditionally provide the following three services to institutional investors:

- Strategic Asset Allocation – IMC's will recommend to institutional investors the broad allocations that should be made for periods of 3-7 years. The IMC may recommend just at the asset class level (stocks/bonds/real estate/cash), or they may drill down and recommend allocations to sub-asset classes (small/mid/large cap stocks, government/corporate/high yield bonds, etc). With these allocation targets as guides, the institutional investor can concentrate on rebalancing back to the strategic asset allocation, and on manager selection and performance attribution (unless these tasks are also assigned to an IMC).
- Manager Selection – Once the asset and sub-asset class allocations have been determined, the IMC may also be commissioned to select specific institutional managers to provide the investment service within a sub-asset class. This line of work has traditionally been viewed as the "bread and butter" of the IMC business, due to the highly labor intensive nature of the work. IMC's must maintain substantial databases of all the potential institutional investment managers availables, cataloguing their performance, management, fee structure, product offerings, etc. When commissioned to perform a manager search, an IMC will first sort through its database for a set of 5-10 candidate managers, and then narrow down to two or three recommended managers to present to the institutional investor through a process of RFP's, interviews, and evaluations.
- Performance Measurement and Attribution – While typically the one function that should be performed by the fiduciaries responsible for the institutional assets, in many cases even this task presents more work for the fiduciary than time permits. IMC's will provide performance measurement and attribution services both for the individual managers hired, as well as for the total picture of all the assets that have been allocated. While not a requirement, institutional investors often hire a different IMC to provide performance measurement services from the IMC hired to select managers, due to the inherent conflict of interest.

#### *5.3.1.3 Role of the Institutional Salesperson*

From the point of view of the investment manager, someone in the firm must "quarterback" the process of interfacing with the IMC's. This person is the Institutional Salesperson. The Institutional Salesperson is the point person for all contact between the investment management firm and the IMC. This individual needs to insure that the

investment management firm “stays on the radar screen” of all the important IMC’s. The tasks to be performed by the Institutional Salesperson will include:

- Insuring that the subsidiary is in the database of all important IMC’s
- Insuring that all IMC’s receive regular performance reports of all products
- Providing all IMC’s with a quarterly face-to-face update on conditions at the subsidiary
- Responding to any IMC questionnaire or RFP for specific manager searches
- Coordinating the team that will respond if the subsidiary is chosen to be in the “finals” for an investment search
- Insuring that if a competitive search is won, that all necessary contractual paperwork with the new client is completed and filed satisfactorily
- Insuring that regular performance reports are sent to both the IMC and the institutional investor, and that regular quarterly meetings with the institutional investor are scheduled and attended by appropriate investment personnel

If achieved, an investment management mandate from an IMC can required a long sales cycle (between 1-2 years). In addition, since most IMC personnel (and very often most institutional investors) are highly sophisticated investment professionals, the Institutional Salesperson needs to be of a similar caliber. Successful institutional salespersons are often former portfolio managers or investment strategists, and they often have many of the qualifications (CFA, MBA in finance, etc) to be a successful investment professional. These individuals are usually compensated by providing them a fraction of the revenues received from an institutional account over a series of several years. A pattern of paying 25% of first year revenues, 10% of second year revenues, and 5% of third year revenues directly to the institutional sales person as a sales commission (on top of a base salary) is a reasonable compensation arrangement.

### ***5.3.2 Growth of Eureka Funds***

Mutual funds can be grown through a number of alternative distribution channels. A total of eight distribution channels have been identified and will be utilized to grow the Eureka Funds from within EIA. These channels include, in order of their anticipated importance:

- SBCL’s Cash Management Program – In 2000 the primary source of growth for the Eureka Funds came from SBCL’s Cash Management Department. It is anticipated that the Cash Management Department will continue to be a major source of asset growth for the Eureka Funds, although that growth has been concentrated primarily in the money market mutual funds.
- Growth in PFS – Roughly one-third of the assets currently in Eureka were directed into the Eureka Funds as a result of allocation of separate account (trust and managed agency) assets by the portfolio managers of the Investment Management Department. It is anticipated that this will continue to be an important channel for growth in the Eureka Funds, insofar as aggressive growth targets for separate account assets

continue to be a major part of the mid-term plan for the Wealth Management Division. However, it is important to note that if the WMD achieves the type of success that it seeks, namely larger accounts, growth in the Eureka Funds from this channel are likely to subside, since only the assets of smaller WMD accounts are directed into the Eureka Funds.

- Wholesaling to SBCL's Retail Brokerage – This distribution channel is the most important of all channels for Eureka growth, due to recent changes in the sales load arrangements of the Eureka Funds. All of the Eureka Funds now offer competitive front-end and back-end load payments for SBCL's retail brokers. The Eureka Funds also have comparable performance and attractive risk profiles relative to the products that have previously been sold by SBCL's retail arm, so it is anticipated that the Eureka Funds should be able to share in at least a moderate portion of new sales made within SBCL's retail brokerage unit.
- Third Party Vehicles – EIA will be open to the inclusion of the Eureka Funds into any third party vehicle (wrap program, 401(k) program, variable annuity, etc.) which might be able to grow assets. However, due to the complications involved in constructing such programs, EIA will not proactively seek out such programs. Instead, EIA will rely on the product management team within WMD to identify, design, and incorporate as appropriate the Eureka Funds into any third party vehicles with which WMD wishes to align.
- Wholesaling to Fee-Only Financial Planners – Depending on the investment performance of the Eureka Funds, the Eureka wholesaler may be directed to contact fee-only financial planners directly, in order to convince them to allocate client assets into the Trust share class of the Eureka Funds. Similar to the reasoning used for the institutional sales channel, it is anticipated that the unique quantitative investment approach of the Funds may be attractive to financial planners, many of whom are highly knowledgeable of modern investment theory. Success in this channel is moderately labor intensive, however, and is highly dependent on continuing improved performance in the Funds.
- "Supermarket" Channels – The Eureka Funds wholesaler will be tasked to ensure that the Eureka Funds appear on all of the major supermarket channels for funds, such as Schwab and Fidelity. Successful penetration of the Schwab supermarket can be particularly opportune, given that Schwab provides convenient back office support for fee-only financial planners, as well as convenient conferences and seminars to which properly positioned fund wholesalers can be invited.
- Selling Agreements with Additional Brokerage Channels – The Eureka Funds currently only has a selling agreement with SBCL's retail brokerage arm. There is no reason for this agreement to be the sole agreement in place for the direct brokering distribution of the Eureka Funds. Assuming sufficient performance, additional brokerage selling agreements can be signed with any willing partners, without adverse impact on the current selling agreement with SBCL. Indeed, the current

selling agreement with SBCL would only be enhanced by successful distribution through other brokerage outlets, insofar as SBCL's potential is relatively capped and growth in the Funds would be a positive selling point to SBCL brokerage clients.

- Media Attention and Direct Advertising – Branding of the Eureka Funds name through media attention and, eventually, direct advertising will be the ultimate step in growing assets for Eureka. While direct advertising to establish Eureka as a brand name is not feasible at the moment, media attention can be achieved in the meantime through an aggressive contacting effort. Positive media exposure can also provide useful enhancements to the brokering process through the use of reprints, brochure quotations, etc.

### ***5.3.3 SBCL WMD Referrals***

As discussed in Section 5.2.2.3, acquisition of corporate accounts will be part of the goal of EIA. No direct resources for marketing to corporate channels are planned to be transferred to EIA. As a consequence, the acquisition of corporate accounts will have to come through direct referrals from WMD. The process is described below.

#### ***5.3.3.1 Existing Distribution Channels within WMD***

At the current time the Wealth Management Division of SBCL derives its sales from a variety of sources. Transactional business is generated by the Retail Financial Consultants, working through the retail branch network of SBCL. Fee-based business is generated primarily through a separate network of business development officers known as Wealth Management Consultants. Fee-based business is also generated by the referral networks of the PFS administrators and PFS office managers, although the primary responsibility for sales falls to the Wealth Management Consultants and their manager, James Ely.

Wealth Management Consultants are expected to generate most of their business by marketing to existing clients of SBCL. In particular, these Consultants are expected to develop business through the following four channels:

- Direct solicitation of clients of the Commercial Banking group
- Referrals from Retail Financial Consultants of high net worth clients
- Cross-selling to the existing clients of Wealth Management
- Development of their own non-SBCL book of leads

In order to be successful, these Consultants must gain the support of various relationship managers within SBCL, including the BBC/CBC officers in the Commercial Banking Group, the Retail Financial Consultants and Branch Managers in the Retail Bank, and the Relationship Managers within the Wealth Management Division (primarily the PFS administrators and the IM department portfolio managers).

### *5.3.3.2 The Relationship between WMD and EIA on Sales*

The primary source for new corporate accounts within EIA will be the Wealth Management Consultants. Just as the Retail Financial Consultants are directed to refer "large" clients up to the Wealth Management Consultants, so too will the Wealth Management Consultants be directed to refer certain types of clients to EIA. Specifically, the WM Consultants will be requested to forward to EIA clients that are:

- Managed Agency (i.e., SBCL cannot be a corporate trustee for the client)
- Very high net worth individuals (those who have established family offices)
- Large Active Liquidity Management accounts (\$50 million and above)
- Corporate clients requiring a sophisticated investment mandate
- Accounts that would classify as institutional (tax exempt foundations/endowments)

A compensation arrangement will be developed to insure that the Wealth Management Consultants have the appropriate incentive to refer such business to EIA. In addition, EIA will be alert for referrals that are more appropriate for the Wealth Management Division.

### *5.3.4 Miscellaneous Channels*

EIA may also grow through other channels. Although not expected, these channels could materialize through the right combination of circumstances. Two of the most likely alternative channels for additional distribution would include:

#### *5.3.4.1 Acquisition of Another Registered Investment Advisor*

SBCL has let it be known that it would be willing to purchase an existing investment advisory firm under the right circumstances. In 2000, two purchase opportunities were reviewed, and one was pursued to the point of submitting a non-binding bid (the firm was later purchased by City National Bank). Other opportunities may arise from time to time.

The primary issue when reviewing acquisition opportunities, aside from cost, will be the degree of synergy that is achievable with SBCL's existing investment advisory functions, both in the subsidiary as well as in Wealth Management. Four possible alternatives might arise regarding how synergistic the acquisition might be:

- Absorb the acquisition RIA as a separate subsidiary of SBCL, unaffiliated with either EIA or WMD
- Absorb the acquisition RIA into EIA
- Absorb the accounts and personnel into WMD
- Absorb some of the accounts and personnel into EIA and some into WMD

The choice will depend on the product offerings, investment philosophy, client types, and management strength of the acquisition RIA. If many of the accounts of the acquisition RIA are trust and/or individual accounts, it would make more sense to absorb those



accounts into WMD. If the acquisition RIA was primarily institutional in nature, it might make sense to absorb it into EIA (if the investment philosophy was compatible), or if the management team of the RIA wished to continue, it might make more sense to have a second RIA subsidiary of SBCL. All factors will be reviewed if and when the opportunity arises again.

#### *5.3.4.2 Sale of Ancillary Services*

In order to minimize the impact of lost personnel on the Wealth Management Division, a number of services being transferred into EIA will be provided back to WMD on a fee-for-service basis. These services include investment research and performance reporting. The possibility exists that as these services expand and mature there may be an opportunity to sell those services outside of the SBCL family, particularly the research services. However, this is not a priority goal of EIA, and may not come to pass. It is equally possible that WMD may eventually acquire its own ability to provide these services internally, at which point EIA would cease selling the services to SBCL and would simply use them internally.

### **5.4. Projections for Growth**

This section discusses how successful the various distribution channels might be in raising assets from the target clients identified. Assumptions from this section feed directly into the financial projections presented in Section 6.0.

#### *5.4.1 Growth in Eureka Funds*

After three years of existence the Eureka Funds have almost reached one billion in total assets. The Eureka assets provide a stable stream of income to SBCL that is larger than would have been earned had the previous common trust funds from which the Eureka Funds were developed been left intact. All aspects of product management for the Eureka Funds will be transferred into EIA, and EIA will be wholly responsible for all major measures of success in the Funds, including growth in assets, growth in revenues, and superior investment performance. As referred to previously, original targets for growth and revenues can be found in Charts 5.1 and 5.2.

The outlook for growth in the Eureka funds remains strong. Our forecast is for total revenues from advisor fees to total \$4.5 million in 2001, \$4.9 million in 2002, \$5.4 million in 2003. These figures are similar to growth figures already derived in the three year plan of the Wealth Management Division, and represent approximately 10% growth per year in revenues.

#### *5.4.2 Institutional Growth*

The projections for the acquisition of institutional accounts is a bit aggressive, particularly in light of the fact that an institutional salesperson has not been retained, and

will probably not be retained until the second half of 2001. Nevertheless, growth targets call for the acquisition of one institutional account in 2001, another two in 2002, and another three in 2003. The assumption is that each account will generate an average of 50 basis points per annum on an average account size of \$20 million. If achieved, institutional business will contribute \$1 million in new revenues for EIA from 2001 to 2003. More importantly, however, the acquisition of institutional accounts not otherwise associated with the Sanwa family will establish EIA's reputation in the Investment Management Consulting community as a serious firm.

#### ***5.4.3 Other Sources***

Only a small amount of additional business is assumed to accrue from the efforts of the Wealth Management Consultants, for two reasons: (1) The current group of WM Consultants is still being developed and is not up to full staff; and (2) It is not anticipated that the WM Consultants, in soliciting SBCL clients, will find a large number of clients that are appropriate for the subsidiary – more likely the business will be booked into the Wealth Management Division.

## 6.0 FINANCIAL PROJECTIONS

This section provides an analysis of the revenues, expenses, capitalization, and cash flows of EIA. Section 6.1 focuses on the Income Statement, Section 6.2 discusses the Balance Sheet, and Section 6.3 discusses the impact of removing these budgetary items from the books of the Wealth Management Division.

### 6.1 Income Statement Estimates

Table 6.1 in the Appendix presents the three year *pro forma* Income Statement for EIA. This section discusses the various revenue and expense items on the *pro forma* Income Statement.

#### 6.1.1 Revenue Sources and Estimates

EIA will have three major groups of revenues, coinciding with the three major categories of clients described in Section 5.2.2, *Target Clients for EIA*. These three segments include Mutual Fund Revenue, Institutional Account Revenue, and Separate Account Revenue (adjusted for Selling Expenses). Each category is described in detail below

##### 6.1.1.1 Mutual Fund Revenue

EIA will provide investment advisory services to the Eureka family of mutual funds. Revenues for these services are based on assets under management, and currently are calculated and paid monthly in arrears by the Eureka Funds Administrator (Bisys) to the Wealth Management Division. Following the creation of EIA, these revenues would be directed to the subsidiary and removed from the accounts of the Wealth Management Division. As of the end of December 2000, these revenues totaled \$3.456 million for calendar year 2000 (counting only advisory fees and not 12(b)1 fees). The *pro forma* assumptions for Eureka Fund revenue growth in EIA for 2001-2003 is the same as that put forth in the most recent mid-term plan for the Wealth Management Division.

##### 6.1.1.2 Institutional Account Revenue

EIA will be seeded with three institutional accounts currently managed by the Investment Management Department. Revenues from the three accounts are currently booked within the Wealth Management Division, but will be transferred into the subsidiary. All three accounts originated from Sanwa Bank, and include management of SBCL's Retirement Plan, as well as investment advisory services provided to two affiliates of SBL, Sanwa Asset Management and Partners Investment Management. Combined these accounts will generate about \$650,000 per year in revenues for the subsidiary. The *pro forma* assumption is that these revenues will not grow over the next three years, since there is substantial uncertainty resulting from the merger of SBL with Tokai and Toyo Banks. However, we are hopeful that the parent merger may lead to expanded business

opportunities for the subsidiary, although we do not want to make a forecast for that expanded business until further information is received concerning the merger.

EIA will also seek to expand its business by attracting new institutional business. As described in Section 5.4.2, this type of business has a long sales cycle (upwards of one year or longer), requires the extensive use of intermediaries (investment management consultants), and requires the acquisition of seasoned sales personnel familiar with this niche market. Once acquired, however, the revenue stream is generally "safe" for 3-5 years, and is lucrative. The *pro forma* assumptions are based on the notion that a typical institutional account has an asset value of \$20 million and an annual fee of 50 basis points. One account is assumed to be acquired in 2001, 2 accounts in 2002, and 3 accounts in 2003, for a total increase in revenues for EIA of \$1 million over that period. Each account is assumed to generate revenues for at least three years.

#### *5.1.1.3 Separate Account Revenues*

EIA will also be seeded with a small amount of what are known as "Managed Agency" accounts currently within the Wealth Management Division, but which will be known as "Separate Accounts" or "Corporate Accounts" within the subsidiary. These accounts will generally be corporate or commercial accounts which are too small (or due to the fact that they are taxable) to qualify as institutional, but are more easily accommodated by the subsidiary than by SBCL (the Wealth Management Division will continue to service Managed Agency accounts for affluent individuals and for trust clients, but will generally direct any large corporate Managed Agency accounts to the subsidiary, unless unique circumstances warrant deviation from that rule).

It is anticipated that between 4 to 8 Separate Accounts will initially be transferred from the Wealth Management Division, with annual revenues of approximately \$90,000. Growth rates of 10% and then 15% have been applied to this figures for the outyears, consistent with the notion that the Wealth Management Consultants will begin to drive assets into the EIA.

Two additional line items have been included under Separate Accounts to provide for the provision of research and other advisory and analytical services from the subsidiary to the Bank. Primarily this will include the provision of Recommended Securities lists, tactical asset allocation recommendations, model portfolios, and any other research that might be required by the Investment Management Department in the management of the Bank's trust and managed agency accounts. It will also include an allocation for a portion of the payroll costs for Bob Bannon. Mr. Bannon will be the sole employee of the subsidiary to remain a full-time employee of the Bank, but his personnel costs will be absorbed within the subsidiary and billed back to the Bank for ease of accounting purposes. In addition, the provision of performance analysis services to the Wealth Management Division for the tracking of separate as well as aggregate performance data on the portfolio management services provided to WMD clients will be charged to the Bank under a service level agreement.

Finally, a line item has been included to deduct from revenues the costs of paying the Wealth Management Consultants. It is assumed that a one-time fee of 12% of annualized revenues will be paid to the Consultants as a referral fee.

### **6.1.2 Expense Sources and Estimates**

Table 6.1 categorizes the expenses for EIA into three major categories: personnel expense, other expense, and charge-back expense. Estimates are also included for tax expense and dividend expense. Each category is described in detail below.

#### **6.1.2.1 Personnel Expense**

EIA will have an initial total of 14 authorized positions. Nine of these positions will be filled with existing Wealth Management Division employees, two have been identified from other firms as target candidates willing to join EIA, and three remain yet to be recruited.

For the nine EIA positions to be filled with existing Wealth Management Division employees, the total annualized run rate base salary expense as of 12/31/00 for these nine employees was \$974,000. Market adjustments for some of these nine individuals will be required, which will translate into an annualized 2001 base salary expense of \$1,037,000. Adding the five additional individuals targeted for the startup will increase total annualized 2001 base salary expense to \$1,590,000. Plans call for two additional individuals to be added, one in 2002 and one in 2003, adding an additional \$250,000 per year in salary expenses to EIA if growth of the subsidiary warrants.

Once the initial market adjustments are made to base salary for Bank employees transferring into the subsidiary, the *pro forma* Income Statement includes a 5% annual merit increase to total base salaries. Compensation improvements for employees over time are targeted to derive mainly from incentive compensation, however, which will in turn be tied to revenue growth. The *pro forma* income statement includes an assumption for incentive compensation that is based on an assumed average payout of 37% of salary across the entire employee base in 2001, growing to 40% in 2002 and 42% in 2003.

Benefits and taxes have been calculated as 18% of salary. Other personnel expense, primarily recruitment and retention expenses, have been targeted at 1% of total payroll. These figures are consistent with the historical experience of the Investment Management Department. Other human resource expenses are captured elsewhere in the *pro forma* Income Statement, including through the internal provision of HR services (provided mainly by the Office Manager of the subsidiary), as well as a chargeback expense to SBCL's HR Department for HR services rendered.

#### **6.1.2.2 Other Expenses**

Table 6.1 lists 11 categories of "Other Expenses" expected to be incurred by EIA. In each case these expense items have been estimated either as a percentage of revenues or

based on a specific calculation of amounts that might be needed. Expenses that are not calculated as a percent of revenues are grown at an 8% rate in the outyears, slightly lower than the expected growth rate of revenues (10%) over that time period to account for economies of scale as the subsidiary grows. A description of each expense item follows:

- Marketing – 3% of revenues each year, with an additional \$20,000 estimated for initial development of marketing materials branded under the EIA name.
- Travel & Entertainment – Four individuals travelling domestically for one week each month at \$2000 per week, plus two individuals travelling overseas for a week two times a year at a cost of \$6,000 per trip. Outyears increase at the 8% per year.
- Portfolio Accounting Services – The cost of a front and back office portfolio accounting system to track client accounts has been estimated at an annual cost of \$250,000, increasing at 8% per year.
- Supplies – Estimated for 2001 at the same cost as in 2000, then grown at 8% per year.
- Equipment Depreciation – Assuming \$100,000 in equipment is transferred from SBCL to EIA at the outset with a depreciable life of three years, annual equipment depreciation expense is estimated to be \$33,000.
- External Audit Fees – Audited financials will be a necessary part of marketing to institutional clients. SBCL's audit department estimated a cost of \$35,000 per year.
- Professional Fees – Cost of vendor services other than the portfolio accounting system, grossed up from the estimate for the Investment Management Department in 2000 for the additional use of consultants and other services.
- External Legal – The expense of outside counsel, generally expected to be about \$20,000 per year based on experience, although higher in 2001 due to costs of the initial launch and registration of the subsidiary.
- Operating Loss – A budgeted item for trading errors. While trading errors are not intended or planned they do happen. Based on historical experience, \$50,000 per year is budgeted.
- Interest Expense – A line of credit will be established for EIA, similar to one in place for the Investment Management Department currently. Used to cover failed trades until financing arrives. No cost is budgeted since the line is rarely used.
- Miscellaneous Expense – Estimated from the experience of the Investment Management Department.

#### *6.1.2.3 Chargeback Expenses*

A separate and unique category of expenses has been included on Table 6.1 to allow for the fact that SBCL will continue to provide services to the subsidiary, albeit under a series of fee-for-service service level agreements. Estimates of services expected to be used are included. These estimates are tentative, and subject to negotiation with each of the Division heads within the Bank. Total chargeback expenses each year are estimated to be approximately \$300,000 to \$350,000, with Office Properties accounting for more than half of that cost. Estimates for Office Properties were based on a rental charge of \$1,100 per FTE per month for space in the Los Angeles Head Office of SBCL. Other chargeback estimates were made in consultation with FMC, but are subject to further negotiation with service division heads in SBCL.

## **6.2 Balance Sheet Estimates**

Table 6.2 in the Appendix provides a statement of cash flows and an analysis of the initial balance sheet for EIA, and the changes in the balance sheet over the first year. This section describes the initial capitalization of EIA, and first year cash flows.

### *6.2.1 Initial Capitalization of EIA*

Initial capitalization of EIA is targeted for April 1, 2001. At that time SBCL will provide \$450,000 in capital to initially fund the first month's expenses (itemized under Funding From Parent). After deducting for the first month's expenses for EIA, an ending cash balance of \$250,000 remains. This cash will be split across DDA cash (\$50,000) and short-term investments (\$200,000). Adding in accounts receivable (\$445,000) and adjusting for fixed assets and other prepaid expenses, total assets of EIA begin at \$745,000.

### *6.2.2 Ongoing Cash Impact on the EIA Balance Sheet*

Average cash receipts each month of approximately \$475,000 vs. average monthly disbursements of approximately \$300,000 allow for a cash/investments accumulation throughout the year to allow payment of bonuses and taxes.

## **6.3 Dividend Policy of the Subsidiary**

The dividend policy of the subsidiary remains to be established. The critical assumption in formulating dividend policy is whether the subsidiary can earn a sufficiently high rate of return on retained earnings, or whether SBCL has a more highly valued use for the funds. This policy will be further examined in consultation with SBCL's Chief Financial Officer. However, for the sake of this proposal, all financial calculations have been performed assuming that all earnings after taxes are distributed as dividends to SBCL.

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## 7.0 APPENDICES

**Table 6.1 PRO FORMA INCOME STATEMENT**

**Eureka Investment Advisors, Inc.**

|                                             | Run Rate<br>Dec. 2000 | Calendar<br>Year 2001 | Calendar<br>Year 2002 | Calendar<br>Year 2003 |
|---------------------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| <b>Revenues</b>                             |                       |                       |                       |                       |
| <i>Mutual Fund Revenues</i>                 |                       |                       |                       |                       |
| Eureka Investment Advisory Fees             | \$ 3,456,000          | \$ 4,446,531          | \$ 4,891,184          | \$ 5,380,303          |
| <i>Institutional Account Revenues</i>       |                       |                       |                       |                       |
| Sanwa Retirement Plan(Pen. Fund)            | \$ 208,000            | \$ 208,000            | \$ 208,000            | \$ 208,000            |
| Sanwa Asset Management(Int'l Fund)          | \$ 240,000            | \$ 240,000            | \$ 264,000            | \$ 290,400            |
| SAM UK                                      | \$ 190,000            | \$ 190,000            | \$ 209,000            | \$ 229,900            |
| Partners Investment Management              | \$ 12,000             | \$ 12,000             | \$ 13,200             | \$ 14,520             |
| New Institutional Accounts                  | \$ -                  | \$ 100,000            | \$ 300,000            | \$ 600,000            |
| <i>Separate Account Revenues</i>            |                       |                       |                       |                       |
| Managed Agency Advisory Fees                | \$ 75,000             | \$ 90,000             | \$ 99,000             | \$ 113,850            |
| Performance Analysis Services to WMD        | \$ -                  | \$ 50,000             | \$ 25,000             | \$ -                  |
| Research Services to IMD                    | \$ -                  | \$ 250,000            | \$ 250,000            | \$ 250,000            |
| <i>Selling Expense: Referral</i>            |                       |                       |                       |                       |
| Business Development Commissions            | \$ -                  | \$ (1,800)            | \$ (1,080)            | \$ (1,782)            |
| <b>Total Revenues</b>                       | <b>\$ 4,181,000</b>   | <b>\$ 5,584,731</b>   | <b>\$ 6,258,304</b>   | <b>\$ 7,085,191</b>   |
| <b>Expenses</b>                             |                       |                       |                       |                       |
| <i>Personnel Expense</i>                    |                       |                       |                       |                       |
| Salary                                      | \$ 974,000            | \$ 1,590,000          | \$ 1,789,500          | \$ 1,982,975          |
| Commission -New Institutional Acct          |                       | \$ 25,000             | \$ 60,000             | \$ 100,000            |
| Bonus                                       | \$ 146,100            | \$ 588,300            | \$ 707,800            | \$ 832,850            |
| Benefits & Taxes(Salary,Commission & Bonus) | \$ 175,320            | \$ 296,013            | \$ 330,795            | \$ 371,861            |
| Other Personnel                             | \$ 9,740              | \$ 15,900             | \$ 17,695             | \$ 19,830             |
| <b>Total Personnel Expense</b>              | <b>\$ 1,305,160</b>   | <b>\$ 2,515,213</b>   | <b>\$ 2,885,790</b>   | <b>\$ 3,307,515</b>   |
| <i>Other Expenses</i>                       |                       |                       |                       |                       |
| Marketing                                   | \$ 125,430            | \$ 187,596            | \$ 187,782            | \$ 212,609            |
| Travel & Entertainment                      | \$ 48,000             | \$ 120,000            | \$ 129,600            | \$ 139,968            |
| Portfolio Accounting Services               | \$ 250,000            | \$ 250,000            | \$ 270,000            | \$ 291,600            |
| Supplies                                    | \$ 22,000             | \$ 22,000             | \$ 23,760             | \$ 25,661             |
| Equipment - Depreciation                    | \$ 33,000             | \$ 33,000             | \$ 35,640             | \$ 38,491             |
| External Audit Fees                         | \$ -                  | \$ 35,000             | \$ 35,000             | \$ 35,000             |
| Professional Fees                           | \$ 100,000            | \$ 125,000            | \$ 135,000            | \$ 145,800            |
| External Legal                              | \$ -                  | \$ 40,000             | \$ 20,000             | \$ 21,600             |
| Operating Loss                              |                       | \$ 50,000             | \$ 50,000             | \$ 50,000             |
| Interest Expense                            | \$ -                  | \$ -                  | \$ -                  | \$ -                  |
| Miscellaneous Expenses                      | \$ 10,000             | \$ 10,000             | \$ 10,800             | \$ 11,664             |
| <b>Total Other Expense</b>                  | <b>\$ 588,430</b>     | <b>\$ 872,596</b>     | <b>\$ 897,582</b>     | <b>\$ 972,393</b>     |
| <i>SBCL ChargeBack Expenses</i>             |                       |                       |                       |                       |
| Office Properties                           | \$ 122,800            | \$ 188,800            | \$ 202,000            | \$ 215,200            |
| Human Resources                             | \$ 16,600             | \$ 16,600             | \$ 17,928             | \$ 19,362             |
| Telecommunications                          | \$ 50,000             | \$ 50,000             | \$ 54,000             | \$ 58,320             |
| Internal Audit                              | \$ 5,000              | \$ 5,000              | \$ 5,400              | \$ 5,832              |
| Internal Legal                              | \$ 10,000             | \$ 10,000             | \$ 10,800             | \$ 11,664             |
| OOP/FMC                                     | \$ 5,000              | \$ 5,000              | \$ 5,400              | \$ 5,832              |
| Bank Payment Services                       | \$ 5,000              | \$ 5,000              | \$ 5,400              | \$ 5,832              |
| Mailroom                                    | \$ 5,000              | \$ 5,000              | \$ 5,400              | \$ 5,832              |
| Central Services                            | \$ 5,000              | \$ 5,000              | \$ 5,400              | \$ 5,832              |
| <b>Total Chargeback Expenses</b>            | <b>\$ 224,400</b>     | <b>\$ 290,400</b>     | <b>\$ 306,328</b>     | <b>\$ 333,706</b>     |
| <b>Total Expenses</b>                       | <b>\$ 2,117,990</b>   | <b>\$ 3,678,209</b>   | <b>\$ 4,089,699</b>   | <b>\$ 4,613,615</b>   |
| <b>Earnings Before Tax</b>                  | <b>\$ 2,063,010</b>   | <b>\$ 1,906,522</b>   | <b>\$ 2,168,605</b>   | <b>\$ 2,471,576</b>   |
| Tax Expense                                 | #N/A                  | \$ 800,739            | \$ 910,814            | \$ 1,038,062          |
| <b>Earnings After Tax</b>                   | <b>#N/A</b>           | <b>\$ 1,105,783</b>   | <b>\$ 1,257,791</b>   | <b>\$ 1,433,514</b>   |
| Dividend Expense                            | #N/A                  | \$ 1,105,783          | \$ 1,257,791          | \$ 1,433,514          |
| <b>Retained Earnings</b>                    | <b>#N/A</b>           | <b>\$ -</b>           | <b>\$ -</b>           | <b>\$ -</b>           |
| <b>Capital</b>                              | <b>\$ 450,000</b>     | <b>\$ 450,000</b>     | <b>\$ 450,000</b>     | <b>\$ 450,000</b>     |
| <b>FTE</b>                                  | <b>9</b>              | <b>14</b>             | <b>15</b>             | <b>16</b>             |

**Table 6.2: Pro Forma Balance Sheet & Cash Flow Statement for 2000**  
**Eureka Investment Advisors, Inc.**

|                                   | January | February | March | April   | May     | June      | July      | August    | September | October   | November  | December  | Year To Date |
|-----------------------------------|---------|----------|-------|---------|---------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|--------------|
| Beginning Balance                 | -       | -        | -     | -       | 250,506 | 408,896   | 516,286   | 726,427   | 947,817   | 1,118,207 | 1,412,538 | 1,670,620 |              |
| <b>Cash Receipts:</b>             |         |          |       |         |         |           |           |           |           |           |           |           |              |
| Arrears Billings                  | -       | -        | -     | 24,999  | 459,883 | 408,883   | 437,883   | 522,883   | 411,883   | 535,824   | 525,824   | 414,936   | 3,742,998    |
| Interest Earned                   | -       | -        | -     | -       | -       | -         | -         | -         | -         | -         | -         | -         | -            |
| Funding from Parent Co.           | -       | -        | -     | 450,000 | -       | -         | -         | -         | -         | -         | -         | -         | 450,000      |
| Other Income                      | -       | -        | -     | -       | -       | -         | -         | -         | -         | -         | -         | -         | -            |
| <b>Total Cash Receipts</b>        | -       | -        | -     | 474,999 | 459,883 | 408,883   | 437,883   | 522,883   | 411,883   | 535,824   | 525,824   | 414,936   | 4,192,998    |
| <b>Cash Disbursements:</b>        |         |          |       |         |         |           |           |           |           |           |           |           | Year To Date |
| Payroll                           | -       | -        | -     | 132,500 | 132,500 | 132,500   | 132,500   | 132,500   | 132,500   | 132,500   | 132,500   | 132,500   | 1,192,500    |
| Payroll-Commission                | -       | -        | -     | -       | -       | -         | 6,249     | -         | -         | -         | 6,249     | -         | 12,498       |
| Payroll-Bonus                     | -       | -        | -     | -       | -       | -         | -         | -         | -         | -         | -         | 441,225   | 441,225      |
| Payroll-Other                     | -       | -        | -     | 25,993  | 25,993  | 25,993    | 25,993    | 25,993    | 25,993    | 25,993    | 25,993    | 25,993    | 233,937      |
| Paid Invoices                     | -       | -        | -     | 63,000  | 140,000 | 140,000   | 60,000    | 140,000   | 80,000    | 80,000    | 100,000   | 100,000   | 903,000      |
| Paid Dividend                     | -       | -        | -     | -       | -       | -         | -         | -         | -         | -         | -         | 829,337   | 829,337      |
| Fixed Asset Purchases-Comp. E     | -       | -        | -     | 3,000   | 3,000   | 3,000     | 3,000     | 3,000     | 3,000     | 3,000     | 3,000     | 3,000     | 27,000       |
| Furniture                         | -       | -        | -     | -       | -       | -         | -         | -         | -         | -         | -         | -         | -            |
| Adjustments:                      |         |          |       |         |         |           |           |           |           |           |           |           |              |
| <b>Total Disbursements</b>        | -       | -        | -     | 224,493 | 301,493 | 301,493   | 227,742   | 301,493   | 241,493   | 241,493   | 267,742   | 1,532,055 | 3,639,497    |
| <b>Ending Cash Balance</b>        | -       | -        | -     | 250,506 | 408,896 | 516,286   | 726,427   | 947,817   | 1,118,207 | 1,412,538 | 1,670,620 | 553,501   |              |
| <b>Balance Sheet</b>              |         |          |       |         |         |           |           |           |           |           |           |           |              |
| Cash                              | -       | -        | -     | 50,000  | 50,000  | 50,000    | 50,000    | 50,000    | 50,000    | 50,000    | 50,000    | 50,000    |              |
| S/T Investments                   | -       | -        | -     | 200,506 | 358,896 | 466,286   | 676,427   | 897,817   | 1,068,207 | 1,362,538 | 1,620,620 | 503,501   |              |
| Accounts Receivable               | -       | -        | -     | 445,234 | 455,583 | 517,933   | 552,283   | 502,632   | 564,982   | 504,332   | 454,681   | 517,035   |              |
| Fix Assets                        | -       | -        | -     | 53,000  | 56,000  | 59,000    | 62,000    | 65,000    | 68,000    | 71,000    | 74,000    | 77,000    |              |
| Other-Depr/Prepaid                | -       | -        | -     | (2,750) | (5,500) | (8,250)   | (11,000)  | (13,750)  | (16,500)  | (19,250)  | (22,000)  | (24,750)  |              |
| <b>Total Assets</b>               | -       | -        | -     | 745,990 | 914,979 | 1,084,969 | 1,329,710 | 1,501,699 | 1,734,689 | 1,968,620 | 2,177,301 | 1,122,786 |              |
| Accounts Payable                  | -       | -        | -     | 135,883 | 144,766 | 153,649   | 236,284   | 245,167   | 314,050   | 382,934   | 425,568   | 33,248    |              |
| Accrued Tax Liability             | -       | -        | -     | -       | -       | -         | -         | -         | -         | -         | -         | 616,927   |              |
| <b>Total Liabilities</b>          | -       | -        | -     | 135,883 | 144,766 | 153,649   | 236,284   | 245,167   | 314,050   | 382,934   | 425,568   | 650,175   |              |
| Paid in Capital                   | -       | -        | -     | 449,000 | 449,000 | 449,000   | 449,000   | 449,000   | 449,000   | 449,000   | 449,000   | 449,000   |              |
| Common Stock                      | -       | -        | -     | 1,000   | 1,000   | 1,000     | 1,000     | 1,000     | 1,000     | 1,000     | 1,000     | 1,000     |              |
| Retain Earning                    | -       | -        | -     | 160,106 | 320,213 | 481,319   | 643,425   | 806,532   | 970,638   | 1,135,685 | 1,301,733 | 851,947   |              |
| Dividend                          | -       | -        | -     | -       | -       | -         | -         | -         | -         | -         | -         | (829,337) |              |
| <b>Total Stockholder's Equity</b> | -       | -        | -     | 610,106 | 770,213 | 931,319   | 1,093,425 | 1,256,532 | 1,420,638 | 1,585,685 | 1,751,733 | 472,610   |              |
| <b>Total</b>                      | -       | -        | -     | 745,990 | 914,978 | 1,084,968 | 1,329,710 | 1,501,698 | 1,734,688 | 1,968,620 | 2,177,300 | 1,122,785 |              |

| <b>TABLE 4.1: ANALYSIS OF IMPACT OF EMPLOYEE TRANSFER FROM WMD TO EIA</b> |                                                                                                                                                                                                                         |                                                                                                                                                                                                                                                       |                                                                                                                                                                                                                                       |
|---------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>WMD Employee</b>                                                       | <b>Current Tasks in WMD</b>                                                                                                                                                                                             | <b>Anticipated Tasks in EIA</b>                                                                                                                                                                                                                       | <b>Impact of Employee Shift from WMD to EIA</b>                                                                                                                                                                                       |
| Bob Bannon                                                                | <ul style="list-style-type: none"> <li>Chief Investment Officer for SBCL</li> <li>Head of Investment Management Dept. within Wealth Management Division</li> </ul>                                                      | <ul style="list-style-type: none"> <li>President and CEO of subsidiary</li> <li>Will serve as CIO, COO until expansion warrants filling these positions.</li> </ul>                                                                                   | None. Bannon will retain all current duties within SBCL (CIO and IM Dept head) while also serving as head of the subsidiary.                                                                                                          |
| David Lampert                                                             | <ul style="list-style-type: none"> <li>Deputy department manager, IM Dept.</li> <li>Eureka Bond Fund manager</li> <li>Eureka money market funds co-manager</li> <li>Manager of 20 separate accounts.</li> </ul>         | <ul style="list-style-type: none"> <li>Fund manager for all Eureka fixed income fund offerings</li> <li>Fixed income account manager for separate accounts</li> </ul>                                                                                 | Transfer of deputy department manager duties to Silva (primarily management of 6 trust portfolio managers), Silva would give control of his Eureka Funds to Lampert.                                                                  |
| Patti DeRudder                                                            | <ul style="list-style-type: none"> <li>Senior trust portfolio manager for 225 managed agency/trust accounts</li> </ul>                                                                                                  | <ul style="list-style-type: none"> <li>Backup Fund manager (vacation &amp; illness) for all Eureka Funds</li> <li>Manager for separate balanced accounts</li> <li>client servicing/relationship mgmt</li> <li>Co-manage Eureka money funds</li> </ul> | DeRudder would relinquish all her current accounts, which would be re-allocated to existing trust portfolio managers (esp. Silva, who will need more accounts after giving up the Eureka Funds).                                      |
| Don Silva                                                                 | <ul style="list-style-type: none"> <li>Co-Manager, Eureka Money Funds</li> <li>Fund Manager, municipal bond common trust funds</li> <li>Portfolio manager of 70 separate managed agency &amp; trust accounts</li> </ul> | None                                                                                                                                                                                                                                                  | Don would become head portfolio manager for the portfolio managers staying with the Bank; he would expand his separate account base; he would become deputy department manager for the Investment Department that remains in the Bank |
| Stefan Ranzlov                                                            | Fund manager for Eureka Equity and GAA funds, and for Small Cap Equity common trust fund. Manages SAM relationship.                                                                                                     | Same as current, except Small Cap fund will be converted to Eureka fund. Also, will manage all equity separate accounts.                                                                                                                              | None. Stefan would perform the same role in EIA that he does in WMD.                                                                                                                                                                  |
| Henry Baltazar                                                            | Compliance manager for all issues related to trust, mutual funds, and brokerage; head of brokerage operations                                                                                                           | Compliance manager for mutual funds and RIA compliance; head of operations for EIA; Chief Financial Officer                                                                                                                                           | Brokerage operations transferred to Sessum; compliance officers transferred to Sessum and Soucie.                                                                                                                                     |
| Kelly Saunders                                                            | Product manager for the Eureka funds.                                                                                                                                                                                   | Wholesaler for the Eureka funds; head of marketing.                                                                                                                                                                                                   | None. Perform same role in EIA as in WMD, expanded for unique EIA tasks.                                                                                                                                                              |
| Pat Dugquem                                                               | Recently hired as a performance analyst.                                                                                                                                                                                | Performance analyst and operations director for the subsidiary.                                                                                                                                                                                       | None. Perform EIA tasks as well as tasks for WMD, billed back to WMD                                                                                                                                                                  |
| Susan De La Fuente                                                        | Assistant to Bob Bannon.                                                                                                                                                                                                | Office Manager for the subsidiary.                                                                                                                                                                                                                    | None. Perform additional services.                                                                                                                                                                                                    |
| Sean Baca                                                                 | Research analyst specializing in asset allocation and global sector rotation; manager of the SBC retirement plan                                                                                                        | Research analyst specializing in asset allocation and global sector rotation; manager of the SBC retirement plan                                                                                                                                      | None. His services will be sold back to WMD bundled up with the other research personnel as a research product.                                                                                                                       |

## TIMELINE FOR CREATION OF AN INVESTMENT SUBSIDIARY

| Item Number | Task                                                 | Date of Completion | Performed by           | Approvals Needed       |
|-------------|------------------------------------------------------|--------------------|------------------------|------------------------|
| 1           | Deliver RIA details to consultants (Bisys)           | 01/05/01           | Bob Bannon             | None                   |
| 2           | Select subsidiary Board members                      | 01/12/01           | Howard Gould           | OOP                    |
| 3           | Deliver subsidiary Board member backgrounds to Bisys | 01/15/01           | Bob Bannon             | Legal Department       |
| 4           | Request/Receive SBCL approval to file corporation    | 01/17/01           | Bob Bannon             | Management Committee   |
| 5           | Request SBL approval to file corporation             | 01/19/01           | Jun Kaneda             | SBL Board of Directors |
| 6           | Receive SBL approval to file corporation             | 01/26/01           | Jun Kaneda             | SBL Board of Directors |
| 7           | Receive SBL disciplinary information                 | 01/31/01           | Jun Kaneda             | None                   |
| 8           | Select a corporate name                              | 02/01/01           | Madeline Sell          | Howard Gould           |
| 9           | File articles of incorporation with California       | 02/05/01           | Bruce Steele           | Stephen Weiss          |
| 10          | Request FSA approval                                 | 02/09/01           | Jun Kaneda             | SBL Board of Directors |
| 11          | File Form ADV with SEC                               | 02/09/01           | Janaya Moscony (Bisys) | Howard Gould           |
| 12          | File for approval with DFI                           | 02/16/01           | Bruce Steele           | Stephen Weiss          |
| 13          | SBCL approves RIA business plan                      | 02/21/01           | Bob Bannon             | Management Committee   |
| 14          | Establish by-laws of subsidiary corporation          | 02/28/01           | Bruce Steele           | Stephen Weiss          |
| 15          | Receive approval of DFI                              | 03/09/01           | Bruce Steele           | Stephen Weiss          |
| 16          | First meeting of subsidiary Board                    | 03/15/01           | Howard Gould           | Howard Gould           |
| 17          | Receive RIA approval from SEC                        | 03/30/01           | Janaya Moscony (Bisys) | SEC                    |
| 18          | Transfer WMD employees into subsidiary               | 04/01/01           | Bob Bannon             | HR Committee           |
| 19          | Relocate subsidiary employees                        | 04/01/01           | Bob Bannon             | Howard Gould           |
| 20          | Notify FDIC                                          | 04/13/01           | Bruce Steele           | Stephen Weiss          |
| 21          | Receive FSA approval                                 | 04/13/01           | Jun Kaneda             | FSA                    |
| 22          | Commence hiring any new staff                        | 05/01/01           | Bob Bannon             | Subsidiary Board       |
| 23          | Gramm-Leach-Bliley deadline for RIA operation        | 05/12/01           | Bob Bannon             | None                   |