

Form ADV Part 2A Brochure

## **Legato Capital Management, LLC**

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This Brochure provides information about the qualification and business practices of Legato Capital Management, LLC. If you have any questions about the contents of this Brochure, please contact us at 415-821-8585 or [info@legatocm.com](mailto:info@legatocm.com).

The information in this Brochure has not been approved or verified by the United States Securities and Exchange Commission or by any state securities authority. Legato Capital Management, LLC is an SEC Registered Investment Adviser. The registration does not imply a certain level of skill or training.

Additional information about Legato Capital Management, LLC is available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

**June 16, 2011**

## Material Changes

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On July 28, 2010, the United State Securities and Exchange Commission published “Amendments to Form ADV” which amends the disclosure document we provide to clients as required by SEC Rules. This Brochure dated March 15, 2011 is a new document prepared according to the SEC’s new requirements and rules. As such, this Document is materially different in structure and requires certain new information that our previous brochure did not require.

In the future, this Item will discuss only specific material changes that are made to the Brochure and provide clients with a summary of such changes. We will also reference the date of our last annual update of our brochure.

In the past, we have offered or delivered information about our qualifications and business practices to clients on at least an annual basis. Pursuant to new SEC Rules, we will ensure that you receive a summary of any material changes to this and subsequent Brochures within 120 days of the close of our business’ fiscal year. We may further provide other ongoing disclosure information about material changes as necessary.

We will further provide you with a new Brochure as necessary based on changes or new information, at any time, without charge.

Currently, you may request our Brochure by contacting Godelieve L. J. (“Lieve”) Mertens, Senior Vice President at 415-821-8585 or [mertens@legatocm.com](mailto:mertens@legatocm.com). Our Brochure is also available on our web site [www.legatocm.com](http://www.legatocm.com), also free of charge.

Additional information about Legato Capital Management LLC (“Legato”) is also available via the SEC’s web site [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). The SEC’s web site also provides information about any persons affiliated with Legato who are registered, or are required to be registered, as investment adviser representatives of Legato.

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### Material Changes

Following is a summary of the material changes since our last annual update of March 22, 2010:

- As of 3/2/2010, Douglas W. Porter, CFA, FRM, CAIA, joined Legato as a member of the Investment Team.
- On June 16, 2011, the Fees and Compensation section was revised

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# Advisory Business

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## Firm Description

Legato Capital Management, LLC ("Legato") is a majority employee-owned institutional investment adviser, specializing in building customized multi-manager equity portfolios across all domestic and international asset classes, styles and capitalization sizes.

On February 11, 2004, Legato filed its Articles of Incorporation with the California Secretary of State. In October 2004, Legato registered with the State of California as an independent registered advisor and, in August 2005, with the Securities and Exchange Commission under the Investment Advisory Act of 1940.

## Principal Owners

Legato is a privately held firm that is majority-owned by its employees. The principal owners are:

- Victor L. Hymes, CEO and Chief Investment Officer, is a majority shareholder and the managing member of Legato
- Forward Management, LLC ("Forward"), is an SEC Registered Investment Advisor controlled by Gordon P. Getty

## Types of Advisory Services

Legato provides investment management and investment consulting services, primarily to institutional clients. Clients have the ability to impose reasonable restrictions on the management of their account, including the ability to instruct us not to purchase certain securities or types of securities.

Legato specializes in building customized multi-manager equity portfolios across all domestic and international asset classes, styles and capitalization sizes. We construct these portfolios by combining strategies managed by independent investment management firms. These strategies have complementary investment styles and we allocate a percentage of the client's portfolio to each of these independent managers. These firms—characterized as Emerging Managers and/or Entrepreneurial Managers—tend to be small, with assets under management of \$2 billion or less. Once these managers are included in a Legato portfolio, we refer to them as "Subadvisor(s)".

In addition, Legato is a manager for Legato Capital Management Ventures, LLC ("LCMV") and Legato Capital Management Investments, LLC ("LCMI"). The principal purpose of LCMV is to locate, analyze and provide capital for, and make investments in, global small and emerging privately-held investment management firms which do or will manage assets of LCMI.

Legato has also entered into a Limited Partnership agreement in which we are the general partner. This partnership has one limited partner and is not open for further investments.

### **Assets Under Management**

All of Legato's assets under management are discretionary. As of March 31, 2011, our assets under management in U.S. Dollars totaled \$1,533,382,643.

## **Fees and Compensation**

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### **Investment Management Fees**

Legato provides investment management services on a fee basis. We charge an annual fee based on a percentage of the market value of the assets we manage. The fee is negotiable and varies (between 0.70% and 1.40%) depending upon the type of strategy and the market value of the assets under management, as follows:

#### **DOMESTIC EQUITY**

On all Assets.....	Annual Fee
Small Cap .....	1.00%
SMID Cap .....	0.90%
Large Cap .....	0.70%
All Cap .....	0.75%
Micro Cap.....	1.40%

#### **INTERNATIONAL EQUITY**

On all Assets.....	Annual Fee
Large Cap .....	0.85%

Managing strategies that charge higher fees presents certain conflicts of interest in managing these accounts at the same time. There is an incentive to favor accounts that charge higher fees. Legato's policies and procedures ensure that we treat all clients fairly and equally, and without the influence of fees paid for certain strategies.

### **Fee Billing**

Legato's fee schedule is inclusive of asset management fees for Subadvisors. In addition, the underlying Sub-advisors do not pay fees directly or indirectly to Legato. The majority of our clients make a single quarterly fee payment to Legato, and we then compensate all underlying Subadvisors directly. Legato does not directly deduct fees from the client's account.

Legato prorates the annual fee and charges quarterly, in arrears. We base the fee on the market value of the assets, including interest, dividends, and cash and cash

equivalents as valued by an independent third party. In most cases, the independent third party is the client's Custodian.

### **Investment Management Agreement**

Prior to engaging Legato to provide investment services, we will generally require a written agreement. The agreement sets forth the terms and conditions of the engagement and describes the scope of the services to be provided. Either party may terminate the agreement by written notice to the other. In the event the client terminates our services, the balance of any earned, unpaid fees will be due and payable at the time the account is closed.

When an account is opened other than at the beginning of a quarter, the market value of the account at inception is one of the valuations used and the fee is prorated for that quarter. Similarly, when the management for the account ends other than at the end of the quarter, the closing value of the termination date is one of the valuations used and the fee is prorated.

The terms and conditions under which Legato will engage the Subadvisor(s) will be set forth in separate written agreements between Legato and the designated Subadvisor(s).

### **Investment Consulting Fees**

Legato also provides investment consulting services which do not include the ongoing management of client assets. For these services, we charge a fixed fee and/or an asset-based fee. Our investment consulting fees are negotiable, but generally range from \$5,000 to \$500,000 on a fixed fee basis and/or from 0.02% (2 basis points) to 0.40% (40 basis points) of the assets under advisement. We base this fee on a number of factors, including the level and scope of the services. Legato prorates the annual fee and charges quarterly, in arrears, for both types of fees.

If a client engages Legato for additional investment advisory services, we may offset all or a portion of the fees for those services based on the amount paid for the consulting services.

Legato prorates the annual fee and charges quarterly, in arrears. For an asset-based fee, we calculate the fee on the market value of the assets, including interest, dividends, and cash and cash equivalents as valued by an independent third party. In most cases, the independent third party is the client's Custodian.

### **Other Fees**

Clients may incur certain charges imposed by banks and/or custodians. Such fees may include, but are not limited to custodial fees, charges imposed directly by a mutual fund or exchange traded fund in the account (which will be disclosed in the fund's prospectus), wire transfer and electronic fund fees, and other fees and taxes on brokerage accounts and securities transactions. Additionally, clients may incur

brokerage commissions and transaction fees. Such charges, fees and commissions are exclusive of and in addition to our fee. Legato does not receive any portion of these commissions, fees or costs. Please refer to Section on Brokerage Practices for more information on other fees.

### **Other Compensation**

Legato does not accept compensation for the sale of securities or other investment products.

## **Performance-Based Fees & Side-by-Side Management**

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### **Sharing of Capital Gains**

Legato receives a management fee similar to that described above for providing management services to LCMI and LCMV. In providing services to LCMI, we may be eligible for performance-based compensation in addition to a management fee.

Managing accounts that charge a performance-based fee, and accounts that charge another type of fee, such as a fixed-rate fee, presents certain conflicts of interest in managing these accounts at the same time. There is an incentive to favor accounts from which we receive a performance-based fee. Legato's policies and procedures ensure that we treat all clients fairly and equally, and without the influence of performance-based fees.

## **Types of Clients**

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### **Description**

Legato provides investment advisory services primarily to institutional clients.

### **Account Minimums**

Legato generally imposes a minimum portfolio value of \$5,000,000 for its investment management services. Legato, in its sole discretion, may accept clients with smaller portfolios based upon certain criteria including anticipated future additional assets, dollar amount of assets managed, related accounts, account composition, pre-existing client, account retention, anticipated future earning capacity and pro bono activities. We only accept clients with less than the minimum portfolio size if, in our opinion, the smaller portfolio size will not cause a substantial increase of investment risk beyond the client's identified risk tolerance.

Additionally, certain Subadvisor(s) may impose more restrictive account requirements than Legato. In such instances, we may alter our corresponding account requirements to accommodate those of the Subadvisor(s).

## Methods of Analysis, Investment Strategies and Risk of Loss

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### Methods of Analysis

Legato's research methodology employs both qualitative and quantitative analysis to discover investment managers. The goal of our quantitative analysis is to identify the universe of Subadvisors that have demonstrated the ability to produce excess return in different market environments. Our qualitative and quantitative research focuses on evaluating the investment process, portfolio management team, research capabilities, trade execution, business operations, compliance, risk management, marketing potential, integrity and suitability.

Legato applies fundamental research to construct portfolios. We use publically available financial data to analyze the risk profile of each strategy.

### Investment Strategies

Legato specializes in building customized multi-manager equity portfolios across all domestic and international asset classes and cap sizes. We construct these portfolios by combining strategies managed by independent investment management firms. These strategies have complementary investment styles and we allocate a percentage of the client's portfolio to each of these independent managers. These firms—characterized as Emerging Managers and/or Entrepreneurial Managers—tend to be small, with assets under management of \$2 billion or less. Once these managers are included in a Legato portfolio, we refer to them as "Subadvisor(s)".

Legato generally allocates client assets among Subadvisor(s) for the active discretionary management of those assets based upon the stated investment objectives of the client. In so doing, we will, directly or through the selection of Subadvisor(s), buy, sell, exchange and/or transfer shares of securities based upon the investment strategy.

Clients have the ability to impose reasonable restrictions on the management of their account, including the ability to instruct us not to purchase certain securities or types of securities.

### Risk of Loss

Risks of investing in a Legato Manager of Manager's portfolio includes Subadvisor(s) do not meet our risk and return objectives, resulting in a portfolio with differing risk and

return characteristic expectations. In addition, Legato's constructs portfolios based on assumptions that the underlying fundamental company data is complete and accurate. There is a risk that the market does not price securities based on fundamental company data but on other (e.g., macroeconomic) concepts.

Investing in the securities markets involves risk of loss that each client should be prepared to bear. Investing in foreign securities markets involves additional risks including political, economic and currency risks, as well as risks associated with differing accounting methods.

## Disciplinary Information

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### Legal and Disciplinary

We are required to disclose whether there are any legal or disciplinary events that are material to a client's or prospective client's evaluation of our advisory business or the integrity of our management.

There is no legal or disciplinary information for Legato to disclose.

## Other Financial Industry Activities and Affiliations

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### Affiliations

Forward Management LLC, an SEC registered investment adviser (CRD#109193) ("*Forward*") is currently a principal owner of Legato (more than 25%, less than 50%). Legato has a three member Board of Managers. Victor Hymes, Legato's CEO, is one of the Managers. Legato provides investment consulting services to Forward. We do not anticipate that this relationship poses any potential risk of conflict of interest with our clients. Legato's policies and procedures ensure that we treat all clients fairly and equally, and without the influence of capital investment in the firm.

Legato Employee, LLC, is organized for the sole purpose of facilitating the transfer of Legato ownership profit interests to employees. Victor L. Hymes is the Managing Member of Legato Employee, LLC.

Victor Hymes maintains FINRA Series 7, 24, 63 and 65 license registrations through his affiliation with Forward. Mr. Hymes has elected not to sell securities to clients. If he elects to sell securities in the future, he would be entitled to receive commissions on the sale of those securities. The commissions would be separate from and in addition to any other fees that a client may pay to Legato for investment management services.

## Code of Ethics, Participation or Interest in Client Transactions and Personal Trading

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### Code of Ethics

Legato has adopted a Code of Ethics for all members of the firm ("Access Persons") describing its high standard of business conduct, and fiduciary duty to its clients. The Code of Ethics includes provisions relating to the confidentiality of client information, a prohibition on insider trading, restrictions on the acceptance of significant gifts and the reporting of certain gifts and business entertainment items, and personal securities trading procedures, among other things. All Access Persons at Legato must acknowledge the terms of the Code of Ethics annually, or as amended.

### Personal Trading

Legato also requires that all Access Persons report their personal securities holdings annually and transactions at least quarterly. An Access Person who acquires beneficial ownership of any reportable securities is required to report transaction activity to the Chief Compliance Officer or designated officer within five (5) market-trading days of the trading activity. Written certification that the investment opportunity did not arise by virtue of the access person's activities on behalf of a client is also required.

Clients may contact Legato to request a copy of its Code of Ethics.

## Brokerage Practices

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### Selecting Brokerage Firms

In general, the Subadvisor(s) will recommend or select a broker or dealer most capable of providing the services necessary to obtain the best execution of that transaction. However, upon request of the client, Legato may also make recommendations to certain Subadvisor(s) for broker-dealers on behalf of the client.

### Best Execution

As a matter of policy and practice, Legato conducts initial and on-going due diligence on Subadvisor(s) policies, procedures and practices regarding Soft Dollars, Best Execution

and Directed Brokerage. Legato seeks to ensure each Subadvisor comply with client guidelines and observe best practices.

The Subadvisor(s) will act in accordance with its duty to obtain “best execution.” However, a client may pay a commission that is higher than another qualified broker-dealer might charge to effect the same transaction where the Subadvisor(s) determines, in good faith, that the commission is reasonable in relation to the value of the brokerage and research services received. In seeking best execution, the determinative factor is not the lowest possible cost, but whether the transaction represents the best qualitative execution, taking into consideration the full range of a broker-dealer's services, including among others, the value of research provided, execution capability, financial strength, commission rates and responsiveness. While the Subadvisor(s) will seek competitive rates, they may not necessarily obtain the lowest possible commission rates for client transactions.

The client may direct the Subadvisor(s) and/or Legato in writing to use a particular broker-dealer to execute some or all transactions for the client. In that case, the client will negotiate terms and arrangements for the account with that broker-dealer, and neither Legato nor the Subadvisor(s) will seek better execution services, better prices or be able to “batch” client transactions for execution through other broker-dealers with orders for other accounts managed by Legato. As a result, the client may pay higher commissions or other transaction costs or greater spreads, or receive less favorable net prices, on transactions for the account than would otherwise be the case. Subject to its duty of best execution, the Subadvisor(s) and/or Legato may decline a client's request to direct brokerage if, in the Subadvisor(s)' or our discretion, such directed brokerage arrangements would result in additional operational difficulties.

## Review of Accounts

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### Periodic Reviews

Members of Legato's Investment Team periodically monitor portfolios as part of an ongoing process. On a quarterly basis, the Investment Team formally conducts Subadvisor due diligence meetings and reviews portfolio exposures relative to specific benchmarks, along with performance and risk attribution.

At least annually, Legato meets with clients for a formal portfolio review. All investment advisory clients are encouraged to discuss their needs, goals and objectives with Legato and to keep us informed of any changes.

## **Regular Reports**

Legato delivers customized reporting with client-specific requirements for each account. The information we provide includes, but is not limited to, monthly and quarterly reports on the total portfolio and on each Subadvisor in the client's portfolio:

- Legato and Subadvisor organizational updates
- Investment strategy review
- Performance analysis
- Total portfolio and Subadvisor performance
- Portfolio holdings and transactions
- Portfolio characteristics

For those clients to whom we provide investment consulting services, Legato conducts reviews on an "as needed" basis. Those clients will receive reports from us summarizing our analysis and conclusions as requested by the client or otherwise agreed to in writing by Legato.

## **Client Referrals and Other Compensation**

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Legato does not compensate any person, who is not a supervised person, for client referrals—directly or indirectly.

## **Custody**

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### **Account Statements**

Clients should receive at least quarterly statements from the broker-dealer, bank, or other qualified custodian that holds and maintains client's investment assets. Legato urges you to carefully review such statements and compare such official custodial records to the account statements that we may provide to you. Our statements may vary from custodial statements based on accounting procedures, reporting dates, or valuation methodologies of certain securities.

## **Investment Discretion**

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### **Discretionary Authority for Trading**

Legato allocates client assets on a discretionary basis among Subadvisors for the active management of those assets, based upon the stated investment objectives of the client.

In addition, clients may, in writing, place reasonable limitations upon our discretionary authority.

## Voting Client Securities

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### **Proxy Votes**

As a matter of policy and practice, Legato conducts initial and on-going due diligence on Subadvisors policies, procedures and practices regarding proxy voting. Legato seeks to ensure each Subadvisor complies with client guidelines and observes best practices regarding proxy voting.

Generally, Legato delegates proxy voting to the Subadvisor(s) who vote according to their policies. In the event of a conflict of interest between the client and Subadvisor(s), the client will determine by whom and how the shares are voted.

The client may also elect to vote their own proxies and will receive their proxies or other solicitations directly from their custodian or transfer agent.

Clients may obtain their voting records and the Proxy Voting policies and Procedures for Subadvisor(s) upon request.

## Financial Information

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### **Financial Condition**

Legato has never been the subject of a bankruptcy petition and we are not aware of any financial condition that is reasonably likely to impair our ability to meet our contractual commitments to clients.

Legato does not require or solicit prepayment of fees.

## Additional Information

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### **Business Continuity Plan**

As part of our fiduciary duty to our clients and as a matter of best business practices, Legato has adopted policies and procedures for disaster recovery and for continuing our business in the event of an emergency or a disaster. Legato's Business Continuity Plan is available upon request.

