



**Kennedy** Capital Management®

## ADV Part 2A

August 28, 2012

Kennedy Capital Management, Inc.

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This Brochure provides information about the qualifications and business practices of Kennedy Capital Management, Inc. If you have any questions about the contents of this Brochure, please contact us at 800-859-5462. The information in this Brochure has not been approved or verified by the United States Securities and Exchange Commission ("SEC") or by any state securities authority.

Kennedy Capital Management, Inc. is a registered investment adviser. Registration with the SEC does not imply any level of skill or training.

Additional information about Kennedy Capital Management, Inc. is also available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). Clients can search this website by using our name or by using a unique identification number known as a CRD number. The CRD number for Kennedy Capital Management, Inc. is 105834.

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## SUMMARY OF MATERIAL CHANGES

### *Annual Update*

On July 28, 2010, the United States Securities and Exchange Commission (“SEC”) published “Amendments to Form ADV” which amends the rules pertaining to the disclosure documents that we provide to clients as required by SEC Rules. This Brochure is prepared according to the SEC’s amended rules. This Section summarizes specific material changes that have been made to the Brochure.

Pursuant to the amended SEC Rules, within 120 days of the close of our firm’s fiscal year (December 31<sup>st</sup>) we will deliver either:

1. a copy of the current (updated) Brochure that includes or is accompanied by the summary of material changes, or
2. a summary of material changes that includes an offer to provide a copy of the current (updated) Brochure.

We may further provide other ongoing disclosure information about material changes as necessary as well as provide you with a new Brochure as necessary based on changes or new information, at any time, without charge.

Currently, our Brochure may be requested by contacting our Client Service Department at 800-859-5462 or [clientservice@kennedycapital.com](mailto:clientservice@kennedycapital.com). Our Brochure is also available on our web site, [www.kennedycapital.com](http://www.kennedycapital.com).

Additional information about Kennedy Capital Management, Inc. is 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 our firm who are registered, or are required to be registered, as investment adviser representatives of Kennedy Capital Management, Inc. (“KCM”).

### *Material Changes Since the Last Update*

This Brochure was first filed with the SEC on March 30, 2011 with the previous filing on March 29, 2012. Material changes to this Brochure since the last update are noted below:

1. Page 3, Sub-Advisory Relationships. KCM has initiated a sub-advisory relationship with Robert W. Baird & Co. Incorporated.
2. Page 4, WRAP Fee Programs. Due to recent contract amendments, the second paragraph under Morgan Stanley Smith Barney was updated to reflect KCM’s responsibility to deliver updates to its ADV Part 2 to applicable clients of Morgan Stanley Smith Barney.
3. Page 6, Assets Under Management were updated as of June 30, 2012.
4. Page 6, The Small Cap Fundamental Growth strategy was added to the Small Cap Strategies Fee Schedule.

5. Page 20, Intern Program. A description of university-level coursework that may be completed by KCM Finance Interns pursuing a degree in Finance was added.
6. Page 21, Research and Other Soft Dollar Benefits. Information was added regarding the number of brokers with which KCM may trade and the general range of commissions per shares paid.
7. Page 30, Economic Benefits Provided by Third Parties for Advice Rendered to Clients. Information was added regarding our gift and entertainment reporting policy.
8. Pages 32 and 33, Clients That Provide Proxy Voting Authority to KCM. Information was added to better explain that certain actions taken by a client's custodian may affect how or if our proxy service provider is able to vote proxies.

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## ADVISORY BUSINESS

### *Description of the Advisory Firm*

Established in 1980 by Gerald Kennedy and Richard Sinise, we are an independent, employee and director-owned advisory firm registered with the Securities and Exchange Commission pursuant to Section 203 of the Investment Advisers Act of 1940, as amended (the Act). We are located in St. Louis, Missouri and are incorporated under the laws of the State of Missouri as an S corporation.

From 1980 to 1992, we managed accounts for high-net-worth individuals, focusing on small cap stocks. In 1993, a program was initiated to market our philosophy to institutional investors. This program was successful, eventually growing the firm in assets and allowing the company to build our investment team, back office, compliance and trading operations to current levels. Since that time, we have supplemented our small cap strategies to include micro cap, mid cap, SMID (combination of small and mid cap), and all cap products.

Firm co-founder Gerald Kennedy passed away in 1999, but Richard Sinise continues to be a part of the firm as a portfolio manager and serves as Chief Portfolio Manager. As of June 30, 2012, we employed 47 full-time people. Our ownership structure is arranged so that our employees and directors own 100% of the firm's total shares outstanding.

As used in this Brochure, the words "we", "our" and "us" or "KCM" refer to Kennedy Capital Management, Inc. The words "you", "your" and "client" refer to you as either a client or prospective client of Kennedy Capital Management, Inc.

### *Advisory Services*

We provide investment management services on a discretionary basis for taxable and tax-exempt institutions, investment companies, and individual clients. We also provide investment sub-advisory services to investment companies, a number of wrap fee programs, and to clients of consultants and other investment advisers as described in further detail later in this section. Discretion means that we have permission to make investment decisions for the account without prior consultation with you, the client. Please refer to the section titled *Investment Discretion* for additional information regarding discretion.

We do not consider our services to be "financial planning" or any similar term, and we do not provide advice in the selection of other investment advisers. To determine your specific needs and financial goals, we encourage you to consult with your broker and/or financial consultant. Furthermore, as we are not tax advisers, we recommend that you consult your legal, financial, and/or tax adviser regarding your particular circumstances.

We primarily invest client funds in domestic equity securities, including common stocks of micro, small, mid, and large capitalization companies. We may also invest client funds in foreign securities. These equity securities may include stocks traded on a national exchange and over-the-counter such as the New York Stock Exchange and the Nasdaq, foreign exchanges or other applicable venues. Additionally, we may invest client funds in other securities such as preferred stock, real estate investment trusts, American depository receipts, American depository shares, exchange-traded funds, corporate bonds, restricted securities and private placements. Please refer to the section titled *Methods of Analysis, Investment*

*Strategies and Risk of Loss* for a discussion of these securities and any additional types of securities that may be purchased in your account along with a discussion of the associated risks.

Although we retain investment discretion over your account as outlined in the section titled *Investment Discretion*, you have the opportunity to place reasonable restrictions or constraints regarding specific conditions or limitations on the types of investments to be made for your account. For example, you may specify that at the time of purchase the investment in any particular stock or industry should not exceed a specified percentage of the value of the portfolio. All such restrictions or constraints, and any modifications to existing restrictions or constraints, are to be agreed upon in writing. We reserve the right to reject or to terminate an account if we believe the restrictions or constraints imposed are not reasonable or prohibit effective management of the account. You should understand that the portfolio restrictions or constraints may affect the performance of your account, either positively or negatively. Furthermore, accounts with restrictions may result in performance dispersion within the portfolio due to portfolio holdings differing from other portfolios in the same strategy. The portfolio manager works to maintain dispersion at a minimum among the accounts; therefore, accounts with restrictions may receive an allocation of a similar non-restricted security.

### ***Sub-Advisory Relationships***

We have been retained to serve as an investment adviser to clients of other unaffiliated registered investment advisers. Clients should understand that we rely on the investment adviser to determine the suitability of our services for their client as we are generally not provided with sufficient information by the investment adviser to perform an assessment as to the client's suitability. We manage these accounts similarly to other separately managed client accounts.

As part of our agreements with other investment advisers, we do not pay them a fee for referring clients to us. We receive an agreed upon percentage of the fees charged by the investment adviser for the sub-advisory services. The agreement between us and the investment adviser states the manner and amount that we will be paid and also describes the services we will provide to the adviser's clients. Clients of these investment advisers compensate their adviser directly and the adviser in turn pays us a fee either quarterly in advance or quarterly in arrears as specified in our agreement with the adviser.

With respect to the assets we manage for clients of these advisers that are employee benefit plans covered under Rule 408(b)(2) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), KCM provides services as an ERISA "fiduciary" (as defined in Section 3(21) of ERISA) and is a registered investment adviser under the Investment Advisers Act of 1940.

Firms with whom we have established sub-adviser management relationships include, but are not limited to, the following:

#### **Convergent Wealth Advisors, LLC - SEC File Number 801-67788**

We may provide investment sub-advisory services to clients of Convergent Wealth Advisors, LLC ("Convergent") as well as individually managed separate account services to Convergent's clients subject to reasonable restrictions.

We will provide our disclosure statement (ADV Part 2A) and Privacy Notice to clients of Convergent at least 48 hours prior to trading such account and will be responsible for voting proxies for the account of Convergent's client unless otherwise instructed. Convergent is solely



responsible for taking all appropriate steps to comply with anti-money laundering requirements for its clients.

Clients of Convergent compensate Convergent directly and Convergent in turn pays us its fee generally quarterly in advance. If our services are terminated, we will refund a pro-rata portion of the fees received from Convergent.

**Windsor Advisory Group, LLC – SEC File Number 801-61372**

We may provide investment sub-advisory services to clients of Windsor Advisory Group, LLC (“Windsor”) as well as individually managed separate account services to Windsor’s clients subject to reasonable restrictions.

Windsor is responsible for providing our disclosure statement (ADV Part 2A) and Privacy Notice to its clients at least 48 hours prior to notifying us that such client’s account is ready to be invested. We are responsible for voting proxies and for responding to corporate actions for the account of Windsor’s client unless otherwise instructed.

Clients of Windsor compensate Windsor directly and Windsor in turn pays us its fee generally quarterly in arrears. If our services are terminated, fees will be calculated on a pro-rated basis.

**Legato Capital Management, LLC – SEC File Number 801-64653**

We may provide investment sub-advisory services to clients of Legato Capital Management, LLC (“Legato”) as well as individually managed separate account services to Legato’s clients subject to reasonable restrictions.

Legato is responsible for providing our disclosure statement (ADV Part 2A) and we will be responsible for voting proxies for the account of Legato’s client unless otherwise instructed.

Clients of Legato compensate Legato directly and Legato in turn pays us its fee generally quarterly in arrears. If our services are terminated, fees will be calculated on a pro-rated basis.

**HighTower Advisors, LLC – SEC File Number 801-69625**

We may provide investment sub-advisory services to clients of HighTower Advisors, LLC (“HighTower”) as well as individually managed separate account services to HighTower’s clients subject to reasonable restrictions.

HighTower is responsible for providing to its prospective clients our disclosure statement (ADV Part 2A) and our Privacy Notice. We are responsible for voting proxies for the account of HighTower’s clients unless otherwise instructed. Annually, we are responsible for providing a copy of our Privacy Notice and for offering or providing a copy of our disclosure statement to HighTower’s clients.

Clients of HighTower compensate HighTower directly and HighTower in turn pays us its fees generally quarterly in arrears. If our services are terminated, fees will be calculated through the date of termination.

**Robert W. Baird & Co. Incorporated – SEC File Number 801-7571**

We may provide investment sub-advisory services to clients of Robert W. Baird & Co. Incorporated (“Baird”) as well as individually managed separate account services to Baird’s clients subject to reasonable restrictions.

Baird is responsible for providing to its prospective clients our disclosure statement (ADV Part 2A) and our Privacy Notice. We are responsible for voting proxies for the account of Baird’s clients unless otherwise instructed. Annually, we are responsible for providing a copy of our Privacy Notice and for offering or providing a copy of our disclosure statement to Baird’s clients.

Clients of Baird compensate Baird directly and Baird in turn pays us its fees generally quarterly in arrears. If our services are terminated, fees will be calculated on a pro-rated basis.

***Wrap Fee Programs***

Although we are a sub-adviser to a number of wrap fee programs through wirehouse consultants, we do not sponsor any wrap account arrangements. A wrap account is where one fee (generally determined as a percentage of assets under management) is charged for investment advisory, trade execution and other services provided to a client. Wrap account arrangements, are commonly referred to as separately managed account, directly managed account, unified managed account, wrap account or similarly named arrangements (collectively, “wrap account”). These managed wrap accounts have been created by unaffiliated financial institutions (each a “Sponsor”).

Each program sponsor has prepared a brochure which contains information about its wrap fee program. Copies of each brochure are available from the program sponsor. Each wrap program sponsor has retained us through a separate investment advisory contract.

Clients should understand that we rely on the wrap sponsor to determine the suitability of our services for their client as we are generally not provided with sufficient information by the sponsor to perform an assessment as to the client’s suitability. Absent specific client guidelines, directed brokerage arrangements, and cash flows, we manage these accounts similarly to other separately managed client accounts within the same strategy based on the strategy’s characteristics and the availability of cash in the individual accounts.

The list of wrap sponsors with which we have arrangements includes:

**Morgan Stanley Smith Barney LLC**

We provide investment advisory services to clients of Morgan Stanley Smith Barney LLC (“Morgan Stanley Smith Barney”) as a result of its preexisting relationship with the Smith Barney division of Citigroup Global Markets Inc. (the “Smith Barney Channel”) through two programs offered by the legacy Smith Barney Channel, as well as through two programs offered by the legacy Morgan Stanley Channel: We serve as a sub-manager in the Select Unified Managed Account (“UMA”) program and as a fiduciary manager in the Fiduciary Services program, both offered through the legacy Smith Barney Channel. We also serve as an investment manager in the Personal Portfolio Program (“PPA”) and are available as an investment adviser in the former Access program (rebranded to Fiduciary Services as of March 2011), both offered through the

legacy Morgan Stanley Channel. The PPA program was integrated into the UMA program in July 2011.

Morgan Stanley Smith Barney is responsible for providing our disclosure statement to its clients whose account are to be managed by us either at the time, or before, Morgan Stanley Smith Barney enters into an agreement with such clients. KCM is responsible to deliver to Morgan Stanley Smith Barney clients, updates to its ADV Part 2 as required which may include but is not limited to a summary of material changes, a revised brochure or statements describing material facts in relation to changes in disciplinary information.

### **UMA and PPA**

For the Select UMA and PPA (integrated into the UMA program in July 2011), we offer discretionary investment management services by providing a model Mid Cap Value portfolio to Morgan Stanley Smith Barney which will be implemented for the account of each client who has selected us, subject to client restrictions. Morgan Stanley Smith Barney's decision to purchase, hold or sell securities for the accounts of clients in the Select UMA and PPA programs will be based on the model portfolio that we provide.

Morgan Stanley Smith Barney is responsible for obtaining information from each Select UMA and PPA client regarding the client's investment objectives, financial information, risk tolerance and any reasonable restrictions for determining that the investment portfolio, investment model and investment strategy, provided as part of the Select UMA and PPA programs, is initially suitable and continues to be suitable for the client.

Finally, Morgan Stanley Smith Barney is solely responsible for voting proxies subject to each client's direction and for taking all appropriate steps to comply with anti-money laundering requirements. Clients in the Select UMA and PPA programs compensate Morgan Stanley Smith Barney directly and Morgan Stanley Smith Barney in turn pays us its fee.

### **Fiduciary Services**

For the Fiduciary Services and the former Access programs (the Access program was rebranded to Fiduciary Services as of March 2011), we offer individually managed separate account services to clients who select us to manage a Mid Cap Value account. Clients in the Fiduciary Services and Access programs compensate Morgan Stanley Smith Barney directly and Morgan Stanley Smith Barney in turn pays us its fee.

"Wirehouse consulting accounts" are those referred to us by an investment consultant, financial adviser or broker ("wirehouse consultant") affiliated with a wirehouse brokerage firm (e.g., Morgan Stanley Smith Barney). Wirehouse consulting accounts may either be:

- A. arranged such that all fees are bundles under a wrap arrangement (where the client pays one all-inclusive asset-based fee covering custody, transaction costs, the services of the consultant or adviser and our services – "wrap wirehouse accounts"); or
- B. unbundled where these fees are paid separately by the client ("unbundles wirehouse accounts").

Clients involved in wrap programs or similar directed brokerage arrangements should understand that client transactions generally are expected to be executed only with the broker-dealer providing custodial and other services. No assurance can be provided that transactions executed through the broker-dealer

providing custodial and other services will result in the best execution available to the client. Transactions executed for these accounts may be less favorable in some respects than those accounts whose trades are not executed through the broker-dealer providing custodial services. This is because we have no ability to negotiate price or take advantage of combined orders or volume discounts. Depending on a variety of factors, including the amount of the combined fee, the trading activity and the value of custodial and other services, the combined fee may or may not exceed the total cost of such services if obtained separately. Under certain circumstances, we may direct client securities transactions to a broker or intermediary other than the designated broker or custodian if, in our opinion, we believe that such direction is in the client's best interest.

Investment consultants may recommend to their clients' that their accounts be managed by us. The investment consultant and the client will arrange to open and maintain one or more accounts with a designated custodian. If this type of arrangements is a wrap consulting account or other combined-fee arrangement, the introducing firm (the firm the investment consultant represents) is obligated to make any required disclosures to clients. Clients with these types of arrangement should contact their wrap program sponsor, broker or investment consultant for information regarding the fees for any services other than the investment advisory services provided by us.

### ***Assets Under Management***

We have the following assets under management as of 06/30/2012:

Non-Discretionary Amount:	Discretionary Amount:
\$0.00	\$4,046,373,000

## **FEES AND COMPENSATION**

Approximately 100% of our revenue is generated from advisory fees. Our fees are generally based on a percentage of assets under management, and exclude the costs of brokerage commissions, transaction fees, and other related costs and expenses. In addition to our advisory fee, you may incur certain charges and fees imposed by your custodian, brokers, and other third party managers such as custodial fees, odd lot differentials, transfer taxes, wire transfer and electronic fund fees and other miscellaneous fees and taxes on brokerage accounts and securities transactions. Additionally, securities traded on a non-U.S. exchange may incur additional fees and expenses.

Fees for any particular client or account are negotiable and may be lowered or waived under certain circumstances, in our discretion. When negotiating fees, certain factors may be considered including but not limited to: strategy, capacity size of the strategy, asset size of the account, complexity of the client situation, and similarity of the account to other accounts we manage.

***Fee Schedules***

Strategy	Annual Management Fee
<b>Micro Cap Strategy</b>	
Micro Cap	1.25% on the first \$30 million in assets 1.00% on the balance over \$30 million in assets
<b>Small Cap Strategies</b>	
Small Cap Select	1.00% on the first \$30 million in assets
Small Cap Select SRI	0.90% on the next \$20 million in assets
Small Cap Core	0.80% on the balance over \$50 million in assets
Small Cap Fundamental Growth	
Small Cap Growth	
Small Cap Value	
Small Cap Extended	
Small Cap Opportunistic Value	
<b>Mid Cap and SMID Cap Strategies</b>	
SMID Growth	0.90% on the first \$30 million in assets
SMID Value	0.80% on the next \$20 million in assets
Mid Cap Growth	0.70% on the balance over \$50 million in assets
Mid Cap Value	
<b>All Cap Value Strategy</b>	
All Cap Value	0.70% on all assets

Fees may be paid monthly or quarterly, in advance or in arrears, as provided in the Investment Advisory Agreement (the “Agreement”) with you, based on the value of the account at the close of the applicable billing period.

Annual fees are generally calculated quarterly; thus the annual fee is divided by four. Generally, fees are payable quarterly in arrears based on the average of the assets values including cash under management at the end of each month during the quarter, although in certain instances some accounts are billed quarterly in advance based on the account asset values on the last day of the previous quarter. In certain circumstances, other paying arrangements may be negotiated upon client request. Fees may be prorated for substantial additions to, or withdrawals from, the account during each quarter for each billing period as provided in the Agreement.

In certain situations where we act as a sub-adviser to a commingled fund or pool of assets, fees may be paid monthly in arrears, based on the average of the account’s daily market value during the relevant period.

Related client accounts may be aggregated in order to determine fee breakpoints. Although assets held in the KCM Small Cap Core Fund, LLC and the KCM Mid Cap Value Fund, LLC (the “Funds”) may be included in asset totals for the purpose of such aggregation, the fees charged to clients in the Funds will not be affected by any breakpoints that may be determined to apply to clients for whom we manage separate accounts. Please refer to the Confidential Offering Memorandum or other offering documents for a description of the fees and expenses for the KCM Small Cap Core Fund, LLC and the KCM Mid Cap Value Fund, LLC.

The value of the client's account, as calculated by our client accounting system, Advent APX, is used to compute management fees unless specified otherwise within the Agreement.

Fee arrangements for the sub-adviser management relationships we maintain are as follows:

**Convergent Wealth Advisors LLC**

Clients of Convergent compensate Convergent directly and Convergent in turn pays us its fee in advance. If our services are terminated, we will refund a pro-rata portion of the fee received from Convergent.

**Windsor Advisory Group, LLC**

Clients of Windsor compensate Windsor directly and Windsor in turn pays us its fee quarterly in arrears. If our services are terminated, fees will be calculated on a pro-rated basis.

**Legato Capital Management, LLC**

Clients of Legato compensate Legato directly and Legato in turn pays us its fee quarterly in arrears. If our services are terminated, fees will be calculated on a pro-rated basis.

**HighTower Advisors, LLC**

Clients of HighTower compensate HighTower directly and HighTower in turn pays us its fees generally quarterly in arrears. If our services are terminated, fees will be calculated through the date of termination.

**Morgan Stanley Smith Barney**

1. In the Select UMA our fee is based on the percentage of assets allocated to its Mid Cap Value strategy, as of the date on which the fee is calculated, multiplied by the assets invested in each client account. Select UMA fees are payable quarterly, in advance. Clients in the Select UMA compensate Morgan Stanley Smith Barney directly and Morgan Stanley Smith Barney in turn pays us its fee. If our services are terminated or a client withdraws assets from an account, we will refund a pro-rata portion of the fee received from Morgan Stanley Smith Barney.
2. In the Fiduciary Services and former Access programs our fee is based on the fair market value of client assets invested in its Mid Cap Value strategy, valued as of the last business day of the previous calendar quarter. Fiduciary Services and former Access fees are payable quarterly, in advance. Clients in these programs compensate Morgan Stanley Smith Barney directly and Morgan Stanley Smith Barney in turn pays us its fee. If our services are terminated or a client withdraws assets from an account, we will refund a pro-rata portion of the fee received from Morgan Stanley Smith Barney.
3. In the PPA our fee is paid quarterly in arrears based on the value of the assets in each client account managed by us on the last business day of that client's billing quarter. Clients of the PPA compensate Morgan Stanley Smith Barney directly and Morgan Stanley Smith Barney in turn pays us its fee. If our services are terminated or a client withdraws assets from an account, fees will be prorated.

### ***Payment of Fees***

Unless otherwise instructed in the Agreement, invoices are generated quarterly and at your request may be mailed, faxed or emailed. Upon your authorization, we will provide an invoice containing management fee information to the custodian of your account. The custodian will then remit the management fee directly to us by deducting it from your custodian account. Statements provided to you by your custodian will detail the total amount of the management fees that have been deducted per quarter. Generally, custodians do not confirm the accuracy of our management fee calculation. We encourage you to review the invoice for accuracy and to contact us with regards to any identified discrepancies or questions. The written invoice sent to you itemizes the management fees, including details of the calculation, the time period covered, and the amount of your assets under management upon which the fee is based.

### ***Clients Are Responsible for Third Party Fees***

You are responsible for the payment of all third party fees such as custodian fees, brokerage fees, transaction fees, etc. Those fees are separate and distinct from the fees and expenses charged by us. For additional information, please see the section titled “Brokerage Practices” of this Brochure.

### ***Prepayment of Fees***

We collect fees in advance or in arrears depending upon the terms of the Agreement.

- For new accounts billed in advance, a pro-rata fee is charged based upon the days under management for the quarter and on the initial assets deposited in the account.
- For new accounts billed in arrears, a pro-rata fee is charged based upon the market value of the account at the close of the applicable billing period.

The Agreement may be terminated by providing written notice to the other party. Upon termination, any prepaid management fees relating to the remainder of the calendar quarter will be refunded to you. If the management relationship is terminated prior to the end of the quarter:

- For accounts billed in advance, fees will be refunded based upon the total days remaining in the billing period for which our services were not provided.
- For accounts billed in arrears, a final prorated fee will be calculated according to the number of days for which we provided investment advisory services during the current quarter.

### ***Outside Compensation for the Sale of Securities to Clients***

We do not accept compensation for the sale of securities or other investment products, including asset-based sales charges or service fees from the sale of mutual funds.



## PERFORMANCE FEES AND SIDE-BY-SIDE MANAGEMENT

We may enter into performance-based fee arrangements with selected clients. All such performance fee arrangements are designed to comply with the provisions of Rule 205-3 under the Act. Such performance fees are charged on a minimum time period of one year. To qualify to obtain the performance-based fee, each client must have at least \$1,000,000 under our management, or is a client who we reasonably believe to have a net worth of \$2,000,000 calculated as provided in Rule 205-3 under the Act, or is a qualified purchaser as defined in section 2(a)(51)(A) of the Investment Company Act of 1940 at the time the client enters into the performance fee agreement.

Performance fees are based on a formula which includes the amount of assets under management and the extent to which the growth in the assets exceeds a specific index. For example, we believe that the appropriate index for use in performance fee arrangements for accounts in the small cap strategy is the Russell 2000® Index, as the stocks in this index most closely approximate the small cap market from which investments are selected. However, upon client request and with our consent, another index may be used as a benchmark for performance fee arrangements. For the purposes of determining unrealized gains and losses, the valuation of securities for which market quotations are not readily available is determined using an objective, observable and unadjusted quoted market price for an identical investment in an active market on the measurement date, if available. In the absence of an objective, observable unadjusted quoted market price for an identical investment in an active market on the measurement date, the valuation must represent our best estimate of the fair value.

Clients should understand that the following conflicts of interest are inherent with performance-based fee accounts.

- These accounts create an incentive for us to make riskier, more speculative investments than would be the case in the absence of a performance fee. Due to the inclusion of unrealized appreciation we may receive more compensation than from an account with only an asset based fee.
- It is possible that our portfolio managers simultaneously manage accounts that are charged a performance based fee with accounts that are charged an asset based fee. This may create a conflict of interest in that a performance fee might provide incentive for us to favor the performance fee account creating a disadvantage for other non-performance fee accounts.

We believe these conflicts are mitigated by managing these accounts consistently with that of other asset based fee accounts pursuant to the selected style and are therefore subject to the same aggregation and pro-rata allocation as all other clients in the same style. Please refer to the section titled *Brokerage Practices* for further information.



## TYPES OF CLIENTS

We generally provide investment management services on a discretionary basis to the following types of clients:

- Taxable and tax-exempt institutions;
- High net worth individuals;
- Family offices;
- Banks or thrift institutions;
- Investment companies;
- Pension and profit sharing plans;
- Public/municipal entities;
- Taft-Hartley/Union plans;
- Trusts, estates, and charitable organizations;
- Foundations and endowments;
- Wirehouse consulting accounts; and
- Corporations or business entities other than those listed above.

Prior to opening an account, you will be asked to sign an Agreement which will grant us discretionary investment authority over your account. The Agreement explains the services, strategies, and fees charged, and typically authorizes us to exercise general discretionary authority in the management of your account. Discretionary investment authority includes the investment and reinvestment of your account assets in securities and amounts of such securities to be purchased or sold without prior consultation with you. Unless you have directed us otherwise in writing, discretionary investment authority also allows us to select the broker or dealer to be used and the commission rate to be paid without prior consultation with you.

We will also ask you to complete a Client Information Form that will provide us with additional details and information regarding you and your account. It also provides you the ability to place reasonable restrictions on your account. As an example, a common restriction prohibits us from purchasing specific companies in a client's account. Any client may reasonably specify in the Agreement or otherwise instruct us regarding specific conditions or limitations on the types of investments to be made for an account.

Additionally, upon opening an account and in order to comply with our anti-money laundering policy we may ask you to provide certain identifying documentation such as government issued identification, articles of incorporation, partnership agreement or trust instrument.

We generally do not have absolute minimum requirements regarding the amount of assets needed to open or maintain an account. We do have preferred minimum account sizes, which may be waived or lowered in our discretion, as indicated below based on the character of the account. These minimums will generally not apply to wrap or other wirehouse consulting accounts which tend to have lower thresholds. The preferred initial minimum account size is listed below (if the strategy is open to new investors.)

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**Institutional and Individual Micro Cap Accounts**

\$15,000,000

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**Institutional and Individual Small Cap Core Accounts**

\$5,000,000

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**Institutional and Individual Small Cap Growth Accounts**

\$5,000,000

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**Institutional Small Cap Accounts** *(unless otherwise noted)*

\$20,000,000

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**Individual Small Cap Accounts** *(unless otherwise noted)*

\$1,000,000

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**Institutional and Individual Mid Cap and SMID Cap Accounts**

\$5,000,000

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**Institutional and Individual All Cap Value Accounts**

\$1,000,000

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**Wrap Programs**

The account minimum for wrap programs will vary by program sponsor. Please review the wrap brochure provided by the sponsor for information regarding their program.

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***Anti-Money Laundering Policy***

To help the government fight the funding of terrorism and money laundering activities, the U.S. Patriot Act and Federal law require financial institutions to obtain, verify, and record information identifying each person who opens an account. We support the fight against money launderers and, prior to opening an account, will ask for information and documentation that will allow us to verify your identity. Until the information or documentation we need is provided and until we have verified your identity, we may not be able to open an account or provide services to you. Existing clients' identities will be verified periodically and, if necessary, the account may be closed.

Under certain arrangements, such as the Select UMA offered through the Smith Barney Channel of Morgan Stanley Smith Barney where we are retained as a sub-manager, we will not be responsible for verifying the identities of its clients. While these procedures are not yet required of investment advisers, the development, adoption and implementation of anti-money laundering procedures is clearly considered a best practice for our industry.

The U.S. Patriot Act requires the maintenance of records and periodic updating of identity verification. We recognize the importance of safeguarding clients' non-public personal information and are committed to maintaining the confidentiality of the information clients provide in accordance with our *Privacy Policy*.

## ***Privacy Policy***

We have adopted policies and procedures reasonably designed to:

- i. Collect only the information we need to service your account and conduct our investment advisory business;
- ii. Ensure the security and confidentiality of your records and information;
- iii. Protect against any anticipated threats or hazards to the security or integrity of your records and information;
- iv. Ensure the accuracy of your information; and
- v. Protect against unauthorized access to or use of your records or information that could result in substantial harm or inconvenience to you.

We collect and retain personal information about clients from the following sources:

- i. Information we receive from you on investment advisory agreements, client information forms, or correspondence (written or electronic) - including, but not limited to, your name, address, phone number, tax identification number, assets, income, and date of birth;
- ii. Other information and documentation that we may collect from you to verify identity;
- iii. Custodian account statements; and
- iv. Information about your transactions with independent broker-dealers including, but not limited to, account number and balance, cost basis information, and other financial information.

We do not disclose any non-public personal information about you to anyone, except at your written request, as required or permitted by law, or as described below. We will adhere to our Privacy Policy even if you decide to close your account(s) or become an inactive client. There are times when we must provide specific information to a service company to facilitate the servicing of your account. These organizations have a legitimate business need to see some of your personal information so we can provide service to you. We require that these companies strictly maintain the confidentiality of this information and abide by all applicable laws. We do not sell clients' information.

We may disclose the personal information that we collect to the following entities:

- i. Unaffiliated service providers (for example, banking institutions that may provide services at our direction);
- ii. Government agencies, other regulatory bodies, and law enforcement officials for reporting suspicious transactions; and
- iii. Other organizations, with your consent or as directed by a client's representative.

We restrict access to your non-public personal and account information to those employees who need to know that information in order to provide investment advisory services to you. We also maintain physical, electronic and procedural safeguards to guard your personal information.

You may obtain a copy of our privacy policy by writing to KCM at 10829 Olive Boulevard, St. Louis, MO, 63141.

## **METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS**

Your assets may be invested in various securities, including (but not limited to) common and preferred stock, American depository receipts, real estate investment trusts, convertible securities, exchange traded funds and/or corporate bonds of domestic or foreign issuers.

### ***Methods of Analysis and Investment Strategies***

Our investment strategy centers around fundamental, “bottom-up” stock picking, meaning that we seek to place investment ideas into the portfolios one stock at a time based on fundamental research of a company’s operations, financials, and our assessment of the valuation potential of that business versus what value the market is assigning.

We seek to invest in securities, primarily domestic equities (“stocks”), which are undervalued and which we believe will appreciate over time (a “long only” approach). We may use procedures (“screening”) to help guide our search and make better and more efficient use of time; however, we do not ‘automatically’ place securities into client portfolios based simply on computer model outputs alone. Each security is evaluated fundamentally by the analysts and/or portfolio managers prior to inclusion in client portfolios.

Our methods of analysis focus on return on investment (“ROI”) and specifically the return on invested capital (“ROIC”) as our preferred measure of corporate performance. ROIC is the net operating profit a business generates expressed as a percentage of the total capital invested in that business. We seek to understand the dynamics of a company’s business as reflected by its earnings potential, ability to use assets, and what kind of cash flows it can generate. Attractive investment candidates typically exhibit characteristics like improving sales and earnings growth, conservative accounting, new product development, high or improving return on invested capital and other strong fundamentals we do not believe to be reflected in the price of the security. Attractive securities may include those with outperforming business models or those that are deemed capable of turning around, but generally feature low market expectations. Our analysis thus seeks to understand why a company’s valuation should improve and what the business is worth economically. We use tools to help guide and define our search but seek to fundamentally understand what return on investment characteristics and market valuations suggest about a security or company before choosing to invest.

In pursuit of these goals, we employ both a large staff of industry-specific research analysts as well as an earnings screening process that seeks to capture positive inflections to business models by reviewing business and financial results on an ongoing basis.

We often find fertile ground in small cap securities (roughly less than \$3 billion in market value), which have historically been our primary focus. However, we believe that our process also applies to mid and larger cap securities. Once ideas have been identified, our analysts and portfolio managers perform fundamental analytical work to ascertain the merits of the idea and the opportunity available for investment.

We also obtain information about potential investment candidates from many types of public information, including, but not limited to, filings with the U.S. Securities and Exchange Commission and other federal and state regulatory agencies, financial publications, discussions with corporate management, public conference calls and presentations, site visits, outside analysts, industry reports, court records, press releases, and research reports. We may periodically purchase stocks based upon the research analysis and recommendations of analysts and brokers at other financial services firms. Employees are encouraged to use our extensive computer-based technology to evaluate information on potential investment candidates. We prohibit our employees from illegally seeking, using, trading upon, or disseminating material non-public information as prescribed by law.

Once a security is purchased for a portfolio, we monitor the security and continue to evaluate if the underlying business is progressing as expected. Where the price of a security does not rise to the level which we believe is appropriate given the company's fundamentals, our analysts and portfolio managers will regularly evaluate the relevant data for signs that the investment thesis is maintaining its original characteristics. We will generally sell a company's security when the price reaches a level consistent with our valuation assessment for that business, if it has grown outside of a specific market capitalization range for a given portfolio, if there appears to be better investment opportunities elsewhere, or if company fundamentals deteriorate from our expectations. Market liquidity and other trading considerations may also affect the timing of sales.

The portfolio managers have final decision making responsibility for their specific portfolios. The analysts seek to provide research ideas from their specific industries across a variety of the Firm's portfolio products, differing in style and market cap range. We implement our investment strategy through a variety of these products designed to address clients' specific needs. Clients may select an investment style such as "growth", "value", or "core" (a combination of growth and value); or target a specific market cap range of "micro", "small", "mid" or sometimes a combination of style and market cap. Equities are chosen using the same process regardless of the size of the client account.

### ***Material Risks Involved***

Past performance is not a guarantee of future returns. Investing in securities involves risk of loss that you, as a client, should be prepared to bear.

**Management Risk** – There is no guarantee that individual securities will perform as we anticipate. Our judgments for an individual security or a particular asset class regarding the attractiveness, value and potential appreciation may be inaccurate. If our investment strategies do not produce the expected results, an investor's investment could be diminished or even lost.

**Equity Market Risk** – Overall stock market risks may affect the value of the investments in equity strategies causing the market value of securities to move up and down, sometimes rapidly and unpredictably. These fluctuations may cause a security to be worth less than the price originally paid for it, or less than it was worth at an earlier time. Market risk may affect a single issuer, an industry, or a sector of the economy or the market as a whole. Equity markets are affected by factors such as U.S. economic growth and market conditions, interest rates, and political events.

**Undervalued Stocks Risk** – Undervalued stocks can react differently to issuer, political, market and economic developments than the market as a whole and other types of stocks. Undervalued stocks tend to

be inexpensive relative to their earnings or assets compared to other types of stock. However, these stocks can continue to be inexpensive for long periods of time and may not realize their full economic value.

**Growth Company Risk** – Growth stocks are expected to increase sales, cash flow and/or earnings faster than the market as a whole and often sell at a premium to stocks of companies with lower expectations. However, these expectations may not be realized and the growth premium may prove to be unjustified.

**Micro, Small and Mid Cap Company Risk** – Investments in micro, small and mid cap companies may be riskier than investments in larger, more established companies. The securities of these companies may trade less frequently and in smaller volumes than securities of larger companies. In addition, micro, small and mid cap companies may be more vulnerable to economic, market and industry changes.

**Foreign Security Risk** – It is important to understand that foreign securities offer different risks from domestic equities as many countries may not have as stringent regulations when dealing with securities and issuers as the U.S. does. As a consequence, the depth of information and disclosure may not be as great in foreign countries. There may also be sovereignty risks in that the government of a foreign company's country may place restrictions on capital and currency flows and may also nationalize firms or industries, expropriate private property and restrict foreign ownership of business and/or markets. Foreign banks and brokerages also recognize separate and additional holidays that may affect trade settlements, the receipt of dividends and income, and all other capital transactions including liquidations. Foreign issues may be subject to withholding taxes on dividends from the country of origin. Moreover, additional custodian costs may be incurred with foreign issues.

### ***Risks of Specific Securities Utilized***

We purchase for client accounts common stock which is a class of security representing equity ownership in a corporation. Holders of common stock have the right to elect directors and collect dividends. Common stock claims are subordinate to bondholder claims, preferred stockholders, and general creditors.

For clients without restrictions, we may also invest in stocks of foreign issuers that are either listed on a US exchange or represented by American Depositary Receipts (ADRs), American Depositary Shares (ADSs), or “ordinary” shares (ORDS), or securities that trade on foreign exchanges.

We may purchase equity securities which are “restricted” within the meaning of Rule 144 under the Securities Act of 1933, as amended (the “Securities Act”), or whose sale is otherwise limited. Unless these limitations are eliminated by registration of a sale transaction under the Securities Act or the availability of an exemption from the registration requirement, the price at which sale transactions are executed may be different than the market price of the same securities whose sale is not restricted.

We may purchase equity securities which are “restricted” within the meaning of Rule 144A under the Securities Act which provides a safe harbor exemption from certain registration requirements and which allows resale of such securities to qualified institutional buyers, under certain conditions.

From time to time exchange-listed master limited partnerships (“MLP”) with operations in various industries may be purchased. An investment in MLP units involves risks that differ from a similar investment in equity securities, such as common stock, of a corporation. Holders of MLP units have the rights typically afforded to limited partners in a limited partnership. As compared to common

shareholders of a corporation, holders of MLP units have more limited control and limited rights to vote on matters affecting the partnership. There are certain tax risks associated with an investment in MLP units.

We may invest in exchange-traded funds ("ETFs"), which own a basket of stocks that track a particular stock market index. Changes in the price of an ETF, before deducting its expenses, track the movement of the associated index relatively closely. ETFs charge their own management fee and other expenses. The principal risks associated with ETFs include the risk that the equity securities in an ETF will decline in value due to factors affecting the issuing companies, their industries or the equity markets generally.

From time to time, we may purchase private placements for selected clients. Private placements (generally, securities which cannot be sold absent registration or an exemption from registration) involve certain risks including the lack of liquidity and objective third party pricing sources. We price equities purchased in private placements and other restricted securities at fair value.

A security may be frequently traded in a portfolio as determined by the portfolio manager. Frequent trading of securities can affect investment performance, particularly through increased brokerage commissions and taxes.

Risks associated with real estate investment trusts ("REITs") include: real estate industry risk which is the risk that REIT share prices will decline because of adverse developments affecting the real estate industry and real property values; real estate values can be affected by a variety of factors, including supply and demand for properties, the economic health of the country or of different regions, and the strength of specific industries that rent properties; investment style risk which is the risk that returns from REITs, which typically are small or medium capitalization stocks, will trail returns from the overall stock market; and interest rate risk which is the risk that changes in interest rates may hurt real estate values or make REIT shares less attractive than other income-producing investments.

## **DISCIPLINARY HISTORY**

We are required to disclose in this Brochure facts about any legal or disciplinary events that have occurred in the last ten (10) years that are material to a client's or prospective client's evaluation of our advisory business or the integrity of our management. We do not have legal or disciplinary information to disclose.

## **OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS**

### ***Registration as a Broker-Dealer or Broker-Dealer Representative***

We are neither registered as a securities broker-dealer nor are we affiliated with a broker-dealer. Additionally, none of our employees are registered or affiliated with a broker-dealer.



***Registration as a Futures Commission Merchant, Commodity Pool Operator, or a Commodity Trading Advisor***

We are not registered as a futures commission merchant, commodity pool operator, or a commodity trading adviser.

***Relationships Material to this Advisory Business and Possible Conflicts of Interests***

We serve as the manager of the KCM Small Cap Core Fund, LLC (the "Core Fund") and the KCM Mid Cap Value Fund, LLC (the "Mid Cap Fund") (collectively, the "Funds"), limited liability companies organized under the Missouri Limited Liability Company Act. We serve as the investment adviser to each pursuant to investment advisory agreements and receive a fee for managing the investment portfolios. We may recommend subscriptions for units of the Core Fund, and either Class A or Class B units of the Mid Cap Fund (depending on whether or not the investor who proposes to subscribe to the Mid Cap Fund is a "restricted person" as defined under Rule 5130 of the U.S. Financial Industry Regulatory Authority - FINRA) to our clients who are accredited investors. The units have not been registered under federal or state securities laws and are subject to an exemption provided by Rule 506 of Regulation D under the Securities Act. The Core Fund members have the same type of interests and the Mid Cap Fund has both Class A and Class B units, but all current owners (including us) own Class A units. The units are offered only to accredited investors through the means of a private placement memorandum (PPM). We encourage you to review the PPM along with the offering documents prior to investing in either of the Funds for a detailed discussion of risks associated with these Funds.

A conflict of interest may arise as we recommend the Funds to our clients and also own units of the Funds as do several of our employees. We manage our own assets and employee assets along with client assets and may be incented to provide preferential treatment to our employee and internal accounts. To address this potential conflict we have developed procedures that provides for these accounts to be treated similarly to any other client account and in a manner that we believe does not conflict with the interests of any client.

A current member of our board of directors who is not an employee (an outside director) also serves as the general partner of one or more limited partnerships and serves as a board member or trustee of one or more exchange traded funds and closed end funds that may invest directly or indirectly in items such as debt and equity securities, private funds and real estate. While certain of our clients may have invested in one or more of these limited partnerships, exchange traded funds, or closed end funds none of these investments were made by using assets from accounts managed by us and these investments were made without consulting us.

***Selection of Other Advisors or Managers and How This Adviser is Compensated for Those Selections***

We do not select or advise our clients regarding other advisors or third party managers. We manage all client assets entrusted to us.



## ***Other Information***

KCM is not registered with any foreign financial regulatory authority. However, as contractually required in order for KCM to qualify for a sub-advisory relationship, on April 21, 2011 the Central Bank of Ireland (the "Central Bank") responded to an application by stating in writing that it has no objection to KCM acting as an investment manager to Irish authorized collective investment schemes ("Irish Funds"). The Central Bank supervises Irish Funds and any investment manager appointed to advise them must meet certain criteria. KCM is not registered with the Central Bank and the Central Bank does not supervise KCM.

## **CODE OF ETHICS, PARTICIPATION OR INTEREST IN CLIENT TRANSACTIONS AND PERSONAL TRADING**

### ***Code of Ethics***

We permit our employees to engage in personal securities transactions. Conflicts of interest may exist when an employee trades in a security that is considered for purchase or sale by a portfolio manager for a client account. We have adopted a Code of Ethics (the "Code") to establish policies addressing our fiduciary duties to our clients. The Code generally prohibits fraudulent or manipulative practices in connection with client investments. The Code establishes policies regarding personal trading by Access Persons. Specifically, the Code prohibits personal trading in any security (a) being considered for purchase or sale for a client, or (b) which has been purchased or sold for the account of clients in the previous ten (10) business days. In addition, the Code establishes an investment holding period of thirty (30) calendar days, subject to certain exceptions. Under certain circumstances, exceptions may be made to the personal trading policy. Records of these trades, including the reasons for the exceptions, will be maintained by the compliance department.

Procedures have been implemented to ensure compliance with the provisions of the Code, including preapproval of personal securities transactions, quarterly affirmations of compliance and annual holding reports. Our personal trading policy is periodically reviewed in light of industry practices, U.S. Securities and Exchange Commission proposals and rules, and best practice recommendations of organizations such as the Investment Adviser Association. Updates to our personal trading policy may be made with the approval of our Board of Directors. You may obtain a copy of the Code by writing to Kennedy Capital Management, Inc. at 10829 Olive Boulevard, St. Louis, MO, 63141.

### ***Recommendations Involving Material Financial Interests***

Our firm does not buy or sell securities for client accounts in which our firm or a related person has a material financial interest. We have adopted procedures that are reasonably designed to mitigate the potential misuse of material non-public information including the use of restricted lists, internal controls and information barriers.

We serve as manager of the Funds and may recommend them to our clients. A discussion of the Funds may be found in Section titled *Other Financial Industry Activities and Affiliations*. We earn a management fee on the Funds and may be incented to treat them more advantageously than other client accounts. To address this potential conflict we have developed procedures that provides for the Funds to

be treated similarly to any other client account and in a manner that we believe does not conflict with the interests of any client.

We also manage accounts in which we have invested our own seed money. These accounts are treated similarly to any other client account and in a manner that we believe does not conflict with the interests of any client.

### ***Investing in the Same Securities as Clients***

Our employees may hold, buy, or sell the same, similar, or related (i.e. warrants, options) securities in their personal trading accounts that are held, bought, or sold in client accounts. It is our policy that employees must wait ten (10) business days to purchase or sell a security after the security has been bought or sold for client accounts; thus, preventing employees from benefitting from transactions placed on behalf of our clients. However, to reduce any conflicts of interest, procedures have been established so that our clients receive priority for any security that is being considered by an employee in a personal trading account. Additionally, transactions effected in employee personal trading accounts must be executed at the broker-dealer through which they are maintained and as a result are not traded through our firm's trading desk.

Conflicts of interest may arise regarding the actions taken for our own accounts or the accounts we manage for our employees, directors, or affiliates ("Affiliated Persons") or for accounts in which Affiliated Persons may participate, such as a mutual fund for which we serve as the sub-adviser. While certain of our Affiliated Persons may have invested in one or more of these mutual funds for which we serve as sub-adviser, none of these investments were made by using assets from accounts managed by us.

We may buy or sell securities for Affiliated Persons or accounts in which our Affiliated Persons may participate that we also recommend to clients, provided that the account is managed consistently with that of all other client accounts managed in the selected style. In the event Affiliated Persons participate in any of the strategies offered or managed by us, a conflict of interest may arise regarding trade execution and/or allocation. See *Brokerage Practices* for information regarding allocations.

Our investment management services are not offered exclusively to any client and we will expect to continue to serve as investment manager (or in a similar role) for current and future client accounts.

It is our policy that we will not conduct any principal or agency cross transactions between client accounts. Principal transactions are generally defined as transactions where an adviser, acting as principal for its own account or the account of an affiliated broker-dealer, buys from or sells any security to any advisory client. An agency cross transaction is defined as a transaction where a person acts as an investment adviser in relation to a transaction in which the investment adviser, or any person controlled by or under common control with the investment adviser, acts as broker for both the advisory client and for another person on the other side of the transaction.

### ***Trading Securities At or About the Same Time as Clients***

Our Code prohibits employees or related persons from personally purchasing or selling a security (a) being considered for purchase or sale for a client, or (b) which has been purchased or sold for the account of clients in the previous ten (10) business days. Employees with accounts managed by us with full discretion similar to other client accounts are not subject to the personal trading requirements. These

accounts are considered client accounts and are managed consistently with that of other client accounts pursuant to the selected style and are therefore subject to the same aggregation and pro-rata allocation as all other clients.

### ***Intern Program***

KCM supports an active intern program. Students with an interest in pursuing a career or degree in finance will generally complete advanced coursework related to securities analysis, valuation and portfolio management. In some cases, university coursework involves not only securities analysis and valuation studies, but may require students to make recommendations for an actively traded university-sponsored portfolio. KCM interns routinely assist our analysts and portfolio managers with company analysis and have access to the recommendations of our analysts that must be used solely for the benefit of our clients. An intern that makes recommendations for an actively traded university-sponsored portfolio may cause that student's coursework to conflict with the interests of our clients. Such students must advise their KCM supervisor immediately upon registering for such coursework so that their supervisor may place restrictions on the intern's access to information within KCM regarding the specific securities and/or sectors they may be assigned to follow. The student will be prohibited from using KCM proprietary research for purposes of their coursework and written coursework recommending any security for purchase or sale pertaining to the university's portfolio will be reviewed by KCM prior to the student's submission. We believe the procedures in place surrounding the student's activities regarding such coursework are adequate to address any potential conflict of interest with the interests of our clients.

## **BROKERAGE PRACTICES**

### ***Factors Used to Select Broker-Dealers***

In determining which broker-dealers to execute trades for your account, we may consider various factors which we believe are important, such as the quality of trade executions, costs of transactions, quality of client services, execution capability, commission rates and volume discounts, financial responsibility, reputation, ability to integrate with our existing systems, effectiveness of systems for monitoring client investments and regulatory compliance, and responsiveness. While we seek competitive commission rates, we may not necessarily obtain the lowest possible commission rates for client transactions. Broker-dealers may offer us investment research, which may be used to service other accounts we manage.

### ***Research and Other Soft Dollar Benefits***

Certain broker-dealers through whom we execute trades may provide us with research, brokerage products or other services (collectively "Products and Services"). The Products and Services may be useful for all client accounts, and not all research may be useful for the account for which the particular transaction was effected. We may select broker-dealers that may be paid commissions for effecting transactions for our clients that exceed the amounts other broker-dealers would have charged for effecting these transactions if we determine in good faith that such amounts are reasonable in relation to the value of the Products and Services provided by those broker-dealers, viewed either in terms of a particular transaction or in our overall duty to our clients.

Products and Services may be used by KCM for itself and/or in servicing some or all of its clients. In addition, some Products and Services may not necessarily be used for your account even though your commission dollars (or other transaction charges) helped to provide for the Products and Services. You, therefore, may not, in any particular instance, be the direct or indirect beneficiary of the Products and Services provided.

An adviser that uses client brokerage commissions to obtain research (whether proprietary or third-party), products, or services receives a benefit because it does not have to produce or pay for the research, products, or services itself. Consequently, the adviser may have an incentive to select or recommend a broker based on its desire to receive research, products, or services rather than a desire to obtain the most favorable execution, which is in the clients' best interest. We seek to obtain overall best execution for client transactions and in the selection of broker-dealers taking into account the value of the Products and Services of the type contemplated under Section 28(e) of the Securities Exchange Act of 1934, as amended, that are provided by broker-dealers.

KCM generally uses between 100 and 150 brokers. Commissions generally range from \$0.01 to \$0.04 per share and KCM estimates that approximately \$0.02 per share is attributable to soft dollars.

Products and Services may either be provided by a broker-dealer, or paid for by a broker-dealer (either by direct or reimbursement payments - in whatever form - or by commissions, mark-ups, mark-downs or credits or by any other means) to be provided by others. The availability of such Products and Services may create a conflict between the interests of the client in obtaining the lowest cost execution and our interest in obtaining such services. Products and Services may be in any form (e.g., written, oral or on-line) and may include (but are not limited to):

- research products or services;
- clearance;
- settlement;
- on-line pricing and financial information;
- access to computerized data regarding clients' accounts;
- performance measurement data and services;
- portfolio strategy advice;
- market, economic and financial information;
- statistical information;
- data on the pricing and availability of securities;
- publications;
- electronic market quotations;
- document retrieval services;
- analyses concerning specific securities, companies, governments or sectors;
- market, economic, political and financial studies and forecasts; industry and company comments;
- technical data, recommendations and general reports;
- quotation services;
- custody;
- brokerage; and
- computer databases.

In addition, several brokers through whom we execute orders provide proprietary research on general economic trends or particular companies. We also periodically obtain opinions from health care providers or other industry experts on industries in general as well as on specific companies or technologies, and these providers may be compensated by a broker-dealer on our behalf. In many cases, third-party research and other services are provided by means of orders executed through brokers unrelated to the provider of research or other services.

In recommending broker-dealers to clients, we need not solicit competitive bids and do not have an obligation to seek the lowest available transaction cost (e.g., commission cost). It is generally not our practice to negotiate "execution only" transaction costs (e.g., commission rates); thus, our clients may be deemed to be paying for Products and Services provided by the broker-dealer which are included in the transaction charges. When we determine that more than one broker-dealer can offer the brokerage and execution services needed to obtain the best available price and most favorable execution, consideration may be given to recommending those broker-dealers which also supply Products and Services that assist us in fulfilling our investment advisory responsibilities. Products and Services may be used by us or our affiliates and/or in servicing some or all of our clients.

In addition, we have the capability of purchasing over-the-counter (OTC) stocks for our clients directly from a market maker for whom such a transaction would be a principal transaction. We may, alternatively, use brokers to execute orders in OTC stocks on an agency basis, in which case a client may pay both a mark-up or a mark-down and a commission. We will utilize brokers to execute OTC transactions when we believe that it is in the client's best interests to do so, either by maintaining the anonymity of the principal or for other reasons connected with the trading situation at the time the trade is placed. As part of our continuing effort to improve investment performance, we endeavor to use the most appropriate trading mechanism available at the time each trade is placed.

In some instances, we may receive Products and Services that may be used for both research/brokerage and non-research/brokerage purposes. In such instances, we will make a good faith effort to determine the relative proportion of the Products and Services used for research/brokerage purposes and the relative proportion used for non-research/brokerage purposes. The proportion of the Products and Services attributable to research/brokerage purposes will be paid through brokerage commissions generated by client transactions; the proportion attributable to non-research/brokerage purposes will be paid for or reimbursed by us from our own resources. The receipt of "mixed-use" Products and Services and the determination of an appropriate allocation between research/brokerage and non-research/brokerage purposes create a potential conflict of interest between us and our clients. These arrangements are periodically reviewed in relation to Section 28(e) of the Securities Exchange Act of 1934, as amended.

We have entered into an agreement for certain business consulting services with an independent contractor who is also a consultant for one of the broker-dealers we use for trade execution services. In addition, the same broker-dealer provides proprietary research services to us and pays for the consulting fees charged by the consultant which are paid for by means of client commissions. This contractual arrangement has been made by and between the business consultant and Kennedy Capital Management, Inc., and the broker-dealer is not a party to it. This arrangement has not caused us to alter our use of this broker-dealer nor has it caused us to commit to or pay additional commissions for client transactions.

In no event are soft dollar credits to be used to offset losses from trading errors. A copy of our *Trade Error Policy* is available upon request.

## ***Brokerage for Client Referrals***

We do not select broker-dealers for trade execution based on our interests in receiving client referrals from broker-dealers or third parties. However, certain broker-dealers may recommend us to their clients and it is generally expected that trades for these types of accounts will be directed only to that particular broker-dealer.

## ***Directed Brokerage***

You may direct that a portion, or in certain circumstances all, of the transactions for your account (a "directed brokerage account") be executed through one or more broker-dealers (a "directed broker"). In such cases, our policy is that you must negotiate the commissions or other charges and fees for your transactions with the broker-dealer. When you direct the execution of transactions through a particular broker-dealer, we are not responsible for the negotiation of transaction commissions or other related charges or fees. There may be a material disparity in commission charges directed to brokerage accounts and the accounts of other clients. For this reason, clients who direct us to use specified brokers may not receive execution that is comparable to the best execution we might obtain on transactions if we were free to select the executing brokers. Our investment advisory agreements include acknowledgements regarding these issues.

We may be able to include the order of a directed brokerage account with orders of other accounts with the objective of obtaining a better execution for the directed brokerage account if the executing broker will transfer the billing and settlement of the order to the directed broker (generally known as a "step-out"). Reconciliation of the portion of the trade given to a directed broker is done through the clearing process between the two brokers. Under such circumstances you may incur both a transaction cost for the execution of the trade and a transaction cost for the billing and settlement of the trade. We will bunch the trades of directed brokerage accounts only under circumstances in which we consider that executing the order in this manner is in the best interest of the directed brokerage account. Our investment advisory agreements include acknowledgements regarding these issues.

Where directed by a Client (other than in a wirehouse consulting account or similar directed brokerage arrangement) in writing to use a particular broker-dealer for transactions in the Client's account, it is our standard policy to use our reasonable best efforts to execute up to 25% of account securities transactions through the broker-dealer specified, where such securities are listed on a primary exchange ("listed securities"), if we have determined in our sole discretion that the broker-dealer can provide price and execution at least equal to the price and execution offered by other broker-dealers. We cannot commit to direct any specific dollar amount or percentage of trades to any particular broker-dealer due to the nature of our trading, which frequently requires us to trade directly with market makers in order to achieve best execution for our clients. It is important to recognize that 25% of transactions in listed securities could represent well below 25% of transactions placed for an account. Therefore, the 25% best efforts target will apply only to the segment of total account transactions that involves listed securities rather than all account transactions placed during a one-year period.

As a participating manager in various wirehouse consulting programs, we are generally free to place orders in these accounts through brokers of our own choosing. However, since wirehouse consulting clients' fee arrangements generally cover transaction costs only when we place orders in these accounts through the wirehouse consulting program sponsor, in most cases we will place orders for wirehouse



consulting accounts through the sponsor since to do otherwise would likely increase the cost of wirehouse consulting services to the wirehouse consulting clients. When we place orders for wirehouse consulting clients through the sponsoring program broker, we will typically do so in a rotational manner, as described below.

### ***Aggregating Trading for Multiple Client Accounts***

It is our policy to seek overall best execution in all trading activities and to allocate purchases and sales of securities fairly among strategies and individual client accounts.

For the purposes of this section, “percentage ownership” means the percentage of the value of a particular stock in relation to the total asset value of your account. We employ several strategies in managing accounts, and a particular stock may be appropriate for and utilized in more than one strategy. Stocks may be held among different strategies managed by more than one portfolio manager. If one or more portfolio managers decide to sell the stock or purchase more of the stock then, to the extent that there is coordination among the portfolio managers, sales and purchases are allocated:

- first, among strategies in proportion to the amount of stock in the accounts of a strategy relative to the total held by all selling or purchasing strategies, and
- second, within each strategy, as described below.

When initiating a new position, shares purchased are generally allocated pro-rata relative to account assets among the clients for whom the stock is being purchased. Within a strategy, accounts may have approximately the same percentage ownership or different percentage ownerships, depending in part on specific account requirements and the manner in which shares were allocated at the time of purchase. If accounts have different percentage ownerships sales are generally allocated first to the account with the highest percentage ownership and subsequently to other accounts in the order of declining percentage ownership. However, at the discretion of each portfolio manager, additional purchases may be allocated first to accounts with the lowest percentage ownership and subsequently to other accounts in the order of increasing percentage ownership.

If accounts within a strategy have approximately the same percentage ownership, sales and additional purchases are generally allocated pro-rata among the accounts. In the case of sales, the amount of stock initially sold at the target price may be insufficient to liquidate a significant portion of every account which would otherwise be allocated pro-rata. Therefore, in the portfolio manager's discretion, shares sold may be allocated randomly among accounts, with each selected account being allocated shares sold in an amount sufficient to liquidate a specified portion of the position in the account (which may be the entire position) prior to shares being allocated to another account. This may result in positions in selected accounts being completely liquidated while other accounts continue to hold the stock.

Random allocation for purchases and sales is done automatically through the trade order management software system. If in the case of a sale, as a result of such random allocation, only a portion of the position in an account is sold, we may manually allocate shares sold in a subsequent block transaction in a fair and equitable manner to completely liquidate the remainder of such position. The allocation of shares sold may also reflect the judgment of the portfolio manager as to the specific needs of an account, such as the need for cash.

We may be allocated shares of equity securities being sold in an initial public offering (a “new issue”). Under FINRA Rules, as they may be amended from time to time (the “Rules”), each client account or investor in a client account, as applicable, must certify to our satisfaction whether they are a “restricted person,” as defined by the Rules, prior to participating in any new issue profits or losses. If a client fails to provide us with such certification the client will be deemed a restricted person and will only be entitled to participate in new issue profits or losses at a reduced level, if at all. Our policy provides that a new issue will be allocated among client accounts in the same manner as other purchases of securities, to the extent allowed by the Rules. If the allocated new issue position is large enough, it will be allocated among the accounts as a percentage of the assets in our clients' portfolios. Random allocations may be used to allocate small new issue positions and may result in some clients obtaining the benefits of new issues while others do not.

Additionally, we may be allocated other securities in limited offerings, including private placements (each, a “Limited Issuance”). Our policy provides that a Limited Issuance will be allocated among client accounts in the same manner as other purchases of securities, to the extent allowed by applicable securities laws. If the allocated Limited Issuance position is large enough, it will be allocated among the accounts as a percentage of the assets in our clients' portfolios. Random allocations may be used to allocate small Limited Issuance positions and may result in some clients obtaining the benefits of Limited Issuances while others do not.

We may be able to obtain better execution and negotiate more favorable brokerage commissions for our clients by “bunching” orders in the same security with the objective of purchasing a block of stock for various clients. Whenever we determine that it is in the client's best interest to bunch client orders, we will attempt to execute the transactions in this manner. Because of prevailing trading activity, it is frequently not possible to receive the same price or execution on the entire volume of securities purchased or sold. When this occurs, the various prices may in our sole discretion be averaged and accounts will be charged or credited with the average execution price as reported to us by the broker-dealer through whom the securities were purchased or sold. In such cases, each client that participates in the bunched transaction will share transaction costs on a pro-rata basis based upon each client's participation in the transaction. The effect of bunching may operate on some occasions to a client account's advantage or disadvantage.

When initiating a new position, shares purchased in bunched transactions are generally allocated pro-rata relative to account assets among the clients for whom the stock is being purchased. Such allocations are subject to adjustment for additional factors, including:

- cash availability within specific accounts,
- consideration of the minimum distribution of shares bought for an account,
- portfolio sector balancing, and
- building the percentage of assets invested in the stock in selected accounts.

Allocations may also reflect the judgment of the portfolio manager as to the specific needs of an account, such as raising cash.

Our portfolio managers generally establish an objective as to the amount of stock in a bunched order to be allocated to each client account, such position generally being expressed as a percentage of the assets in



the client's portfolio. The liquidity of some small cap stocks is limited, and the stock initially purchased at the target price may be insufficient to achieve the minimum position objective established by the portfolio manager. In addition, the portfolio manager may believe that enough additional stock may be purchased at the target price to achieve the portfolio manager's minimum position for each account through additional purchases. Therefore, in the portfolio manager's discretion, shares of a purchased block may be allocated randomly among accounts with each selected account being allocated the minimum percentage position prior to shares being allocated to another account. Random allocation may also be used to allocate small positions obtained in initial public offerings or Limited Issuance positions. This may result in some accounts not receiving any portion of the stock purchased in a bunched transaction, an initial public offering or a Limited Issuance. This random allocation is done automatically through the trade order management software system. If an account receives only a portion of the minimum percentage position set by the portfolio manager, the trader may manually allocate shares purchased in subsequent block trades to fill the minimum percentage position.

Shares allocated in accordance with these procedures are priced based on the average price of the executions as reported to us by the broker-dealer through whom the securities were purchased or sold.

In cases where trading or investment restrictions are placed on a client's account, our traders may not be able to aggregate that client's transaction with others. In this case the client may pay a higher commission rate and/or receive less favorable prices than clients who are able to participate in an aggregated order.

When placing orders to buy or sell a security for all accounts pursuing a specific strategy, we typically cluster all impacted clients into one of two categories:

1. accounts that grant us discretion in selecting how to execute trades ("freely traded"); and
2. accounts that have directed us to use specified brokers, including wirehouse consulting accounts where trades are normally placed through the sponsoring broker ("fully directed").

In the absence of unique circumstances, all freely traded accounts are generally traded together and each broker with which fully directed accounts are traded, are generally traded together. With the exception of the Select accounts, Select SRI accounts, Small Cap Core accounts, and Mid Cap Value accounts, the trader will make best efforts to trade freely traded and fully directed accounts simultaneously to obtain the least disparity among accounts.

An exception exists for accounts in the Select and Select SRI composites, trades for which are rotated between each composite. All Select SRI accounts are freely traded and, in the absence of unique circumstances, are executed together. The Select accounts are grouped as freely traded or by the client's selected custodian. Once it is the Select composite's turn to trade, trades are rotated as determined by the portfolio manager among spots within the trading rotation and (in turn) the freely traded. Select accounts are also rotated among themselves. The portfolio manager will sequence the trades when he determines that the order placed will be filled by the end of the trading day.

An exception also exists for accounts in the Small Cap Core strategy where the client has instructed us to direct its trades to a specific broker, such as the broker the client has selected to custody its account. We intend to trade such fully directed accounts after all trading in the same one or more securities has been completed for all the freely traded accounts, although each broker represented among the fully directed

accounts will have its own spot in the trading rotation for fully directed accounts. While not always the case, trades executed after other clients' trades (including larger bunched orders) may be executed at less favorable prices than those obtained in the earlier orders. Except in rare circumstances, such transactions will not be bunched with the trades of other accounts in the Small Cap Core strategy. Clients may direct us to "step out" transactions; however, fees imposed on these types of trades by a client's selected broker will more than likely be cost-prohibitive. We will not be able to negotiate commissions for clients directing their trades to a specific broker and, therefore, the clients' commissions may be higher than those charged on freely traded orders. In addition, we will not be able to provide assurances that these clients will receive best execution at their selected broker(s).

An exception also exists for accounts in the Mid Cap Value strategy which includes freely traded accounts, fully directed accounts and wirehouse consulting accounts. We will generally trade fully directed accounts and wirehouse consulting accounts after all trading in the same one or more securities has been completed for all the freely traded accounts, although each broker represented among the fully directed accounts and wirehouse consulting accounts will have its own spot in the trading rotation for fully directed accounts and wirehouse consulting accounts (and some brokers with more than one program or platform may have more than one spot in the trading rotation). While not always the case, trades executed after other clients' trades (including larger bunched orders) may be executed at less favorable prices than those obtained in the earlier orders. Except in rare circumstances, such transactions will not be bunched with the trades of other accounts in the Mid Cap Value strategy. Clients may direct or allow us to "step out" transactions; however, fees imposed on these types of trades by a client's selected broker may be cost-prohibitive. We will not be able to negotiate commissions for clients directing their trades to a specific broker and, therefore, the clients' commissions may be higher than those charged on freely traded orders (although commissions may also be included as part of an overall wrap fee). In addition, we will not be able to provide assurances that these clients will receive best execution at their selected broker(s).

### ***How Withdrawals and Small Deposits are Traded for Fiduciary Services and Former Access Accounts***

We define a small deposit as a deposit that results in the cash level of your account remaining under 10% of your account's total market value. When you make a withdrawal or a small deposit to your account, we will generally place trades resulting from the withdrawal or small deposit in the following manner:

#### ***Cash Withdrawal Requests***

At the time you make a withdrawal request from your Fiduciary Services or former Access account, no securities will be sold if the cash is readily available in your account. Immediately after the withdrawal, your cash balance may be lower than that of the other accounts in the composite that did not request a withdrawal. In this circumstance, sale transactions will be executed in your account on a bi-weekly basis to bring your account cash balance back in-line with the other accounts within the composite.

### ***Deposits of Cash***

- When you make a cash deposit to your account that causes your account cash level to exceed 10% of its total market value, we will generally invest the cash upon our receipt of the notification of the deposit.
- When you make a small cash deposit to your account resulting in the cash level of your account remaining under 10% of its total account market value, we will generally invest the cash balance on a bi-weekly basis. However, when a deposit is made for any Fiduciary Services or former Access client account that exceeds 10% of that account's total market value, all Fiduciary Services or former Access account deposits (including any small cash deposit to your account) that were under the 10% threshold and which are pending the bi-weekly investment date will be invested concurrently.

## **REVIEW OF ACCOUNTS**

### ***Frequency and Nature of Reviews***

It is your responsibility to notify us of any changes in your investment objectives and/or financial situation. We encourage you to review investment objectives and account performance with us on an annual basis. We offer to schedule at least one meeting per year with you to review account performance and investment objectives. We believe these meetings, which may be held at our client's office, our office, or via telephone conference, are important in aligning our individualized portfolio strategy with our client's investment needs.

Portfolio managers are responsible for constructing and maintaining the investment strategy of their composite. The portfolio manager is responsible for the day-to-day supervision of your account as well as the review of the securities held in their managed strategy or strategies to determine the likelihood that assets held will continue to achieve the expected investment objective. Account reviews are designed to ensure that transactions for client accounts are consistent with each client's specific investment objectives as indicated in the client's advisory agreement and additional instructions to us. Matters generally reviewed include specific guidelines and the performance of the account on a year-to-year basis.

The Investment Policy Committee performs a periodic assessment of the investment decisions implemented by each portfolio manager. The matters reviewed include diversification, portfolio composition, performance, and factor characteristics relative to the identified benchmarks.

On a monthly basis the account holdings are reviewed against custodial statements by the operations department. Data feeds from many of our clients' selected custodians are obtained through a third party, and are used to compare custodial data to our client account records as frequently as daily. In some instances, variances may exist between final audited custodial information and the information we obtain via such data feeds. We have adopted a de minimis standard whereby such variances are noted and aggregated until each month-end, so long as such aggregated variances amount to less than one percent of the prior month-end market value of the account. All such variances are typically reconciled to the applicable account no later than each month-end. Variances of one percent or more will generally be reconciled to the account promptly upon detection.

The overall performance of each portfolio is reviewed on a monthly/quarterly basis.

Additionally, many of our clients engage third-party consultants to assist with monitoring performance, stated objectives and risk tolerance.

### ***Factors that Trigger a Non-Periodic Review***

Daily compliance checks are applied both pre-trade and post-trade electronically through the order management system to determine compliance with specific client guidelines. Alerts are brought to the attention of the compliance department and if necessary are reviewed in more detail by the portfolio manager and trader. Additionally, the compliance department conducts daily trade surveillance on a post-trade basis to review allocations, pricing, cash levels, foreign holdings, and security position weightings, among other things. Discrepancies are researched to understand the cause and to determine if any changes or corrective actions are needed. A more thorough analysis is undertaken periodically to determine that investments in accounts are consistent with objectives and the client's identified restrictions.

Events that may trigger a review include client requests, a change in a client's financial objectives, and significant world, economic or market events.

### ***Content and Frequency of Regular Reports Provided to Clients***

The nature and frequency of reports are determined by the particular needs of each client. Generally, reports are furnished no less than quarterly. We will furnish reports on a more frequent basis if requested. Reports typically summarize investments in the client's account, including an inventory of account holdings with corresponding market values, and the percentage of each security held relative to the total account along with account performance. Performance is compared to the appropriate Russell index and other relevant benchmarks, where applicable. You may also receive from us periodic letters and commentaries discussing the outlook for the markets and your portfolio. Customized reports are also provided upon request.

You may request to receive transaction confirmation notices directly from the broker-dealer executing the transactions in your account. You should also verify that your qualified third-party custodian or broker-dealer (where your account is maintained) is providing statements to you no less than quarterly. We encourage you to compare the information included with our account statements to the information reflected in the statements you receive directly from your custodian. Our statements may vary from custodial statements based on accounting procedures, reporting dates, or valuation methodologies of certain securities.

Additionally, investors in the KCM Small Cap Core Fund, LLC and the KCM Mid Cap Value Fund, LLC receive an annual K-1 and a copy of the annual Fund audit.

Wrap program relationships authorize us to offer continuous investment management services to wrap program clients. Wrap program clients generally receive quarterly performance reports from the wrap program sponsor.

## CLIENT REFERRALS AND OTHER COMPENSATION

### *Economic Benefits Provided by Third Parties for Advice Rendered to Clients*

Our revenues are derived from advisory fees. Our employees may from time to time give or receive gifts from clients, broker-dealers, and other unaffiliated third parties. Additionally, our employees may host a client, broker-dealer, and/or unaffiliated third party or be the recipient of entertainment provided by a client, broker-dealer, and/or other unaffiliated third party. We maintain a gift and entertainment policy that limits gifts and entertainment that employees may receive without approval to \$250 and requires internal reporting of any gifts valued at \$10 or greater. Neither KCM, nor our employees, receive sales awards or other prizes, directly or indirectly from any third party as an incentive for providing advice to our clients.

### *Compensation to Non-Advisory Personnel for Client Referrals*

From time to time we may compensate persons not affiliated with us for client solicitation and referral. We have an agreement with certain brokerage firms under which the broker-dealer may solicit clients.

We may enter into contractual arrangements with non-affiliated individuals or firms ("solicitor") to solicit on our behalf and to refer clients to us. The arrangements are made in writing pursuant to Rule 206(4)-3 under the Act. Our agreements with any such solicitors require that clients receive disclosure of such solicitation and client referral activities as provided by Rule 206(4)-3. The solicitor must, at the time of his solicitation, provide the client with a copy of this Brochure and must also provide the client with a separate document describing the solicitation arrangement, disclosing any affiliation between us and the solicitor, the compensation for solicitation, and whether advisory fees for solicited clients are higher than those for other clients due to compensation paid to the solicitor.

In some circumstances, payments to third party solicitors may create an incentive for the solicitor to recommend to their clients our advisory services.

## CUSTODY

We do not accept physical custody of your assets, including the receipt of securities, cash or checks at any time. The decision to select a qualified third-party custodian remains solely with you. With the exception of the pooled investment vehicles managed by us, you must contract directly with your selected qualified third-party custodian or registered broker-dealer for custodian services.

If you are invested in either of the two pooled investment vehicles managed by us, your account will be maintained with BNY Mellon. BNY Mellon serves as custodian to the KCM Small Cap Core Fund, LLC and the KCM Mid Cap Value Fund, LLC (collectively "the Funds"). BNY Mellon is a national bank subject to the jurisdiction of the Office of the Comptroller of the Currency and is a qualified third-party custodian. Services performed by BNY Mellon include (but are not limited to) executing purchases and redemptions of interests of the Funds, determining the net asset value per unit of the Funds in accordance with generally recognized valuation procedures, custody of the assets of the Funds, various recordkeeping functions and generating periodic fund statements to our clients who are investors in either of the Funds.

You should receive at least quarterly statements from the broker-dealer, bank or other qualified third-party custodian that holds and maintains your investment assets. We encourage 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.

Wrap accounts will be held by the Sponsor of the wrap program.

## INVESTMENT DISCRETION

Discretion means we may make investment decisions without consulting you first, regarding the selection of securities to buy or sell, the amount of securities to buy or sell, the broker-dealer to use, and the commission rates to pay, subject to reasonable investment objectives and guidelines that are generally established by an agreement at the time of account inception. Prior to assuming discretionary authority, an Investment Advisory Agreement (the “Agreement”) will be executed. By signing the Agreement, discretionary investment authority over your account per the terms of the Agreement is granted to us. The Agreement provides us with authorization to give instructions to your custodian regarding the investment decisions for the purchase, sale, conversion, redemption, exchange or retention of any security, cash, or cash equivalent or other investment for your account.

The wrap program relationships outlined in the section entitled *Advisory Business* authorizes us to offer continuous investment management services to wrap program clients. Generally, each wrap program client enters into an investment advisory contract with a wrap program sponsor, and in turn the wrap program sponsor has a separate investment advisory agreement with us. We generally maintain discretion as to which securities shall be purchased or sold in a wrap program account in a manner consistent with the client’s selected strategy, investment objectives, policies and any reasonable restrictions. In order to avoid incurring the incremental costs created by using other brokers, transactions for wrap program clients are typically executed through the wrap program sponsor. In most cases, as part of the wrap program arrangement, we have been directed to execute orders with the wrap program sponsor.

Generally, it is our policy to not accept unsupervised assets. An unsupervised asset is an asset managed by you, the client.

## VOTING CLIENT SECURITIES

### ***Clients That Provide Proxy Voting Authority to KCM***

We will accept authority from you to vote your proxies and will vote according to our proxy policy as outlined below.

Rule 206(4)-6 and rule amendments under the Investment Advisers Act of 1940, which became effective August 6, 2003, are designed to ensure that investment advisers fulfill their fiduciary obligation when voting client proxies. Disclosure requirements include:



- (i) investment advisers that exercise proxy voting authority for clients must describe the firm's proxy policies and procedures, and upon request, provide clients with a copy of those policies and procedures; and,
- (ii) advisers must describe how clients may obtain information on how their securities were voted.

We generally vote proxy ballots for our clients using a proxy voting service to help fulfill our voting obligations, although some clients may choose to retain voting responsibility. Unless otherwise instructed by you, we will undertake to vote proxies for your account. Under certain arrangements, such as the Select UMA offered through the Smith Barney Channel of Morgan Stanley Smith Barney, where we have been retained as a sub-manager, and the sub-advisory arrangement with Legato Capital Management, LLC, we will not vote proxies for their clients. We must make proxy voting decisions solely in the best interests of our clients and will place our clients' interests above our own interest.

You may select among two voting platforms which are; General Policy or Socially Responsible Investment Policy. The General Policy will be used for voting proxies for all clients (both ERISA and non-ERISA) unless you specifically select the Socially Responsible Investment Policy.

Broadridge Investor Communication Solutions, Inc. ("Broadridge") has been retained to provide access to a selection of third-party providers who are available to provide proxy vote recommendations and research. Generally, votes are cast through the Broadridge ProxyEdge® platform ("ProxyEdge®") which provides access to proxy voting recommendations, research and historical voting information. With the assistance of Broadridge, Egan-Jones Proxy Services ("Egan-Jones") has been selected to provide vote recommendations based on its own internal guidelines. The services provided to us through ProxyEdge® include access to research provided by Egan-Jones and access to the analysis and voting recommendations of Egan-Jones as well as reporting, auditing, recordkeeping and consulting assistance for the handling of proxy voting responsibilities. Generally, we follow the recommendation of Egan-Jones, which then forwards the voting recommendation to Broadridge to process.

We may direct that proxies be voted in a manner different from that recommended by Egan-Jones. However, when our interests conflict with the interests of our clients, we will follow the recommendation of the proxy voting service. Additionally, we may seek guidance from our Proxy Voting Committee to resolve material conflicts of interest.

You may elect to participate in a securities lending program through your selected custodian. Under typical securities lending arrangements, securities on loan to a borrower on a proxy record date may not be voted by the lender. Therefore, we will not vote securities that are on loan as the responsibility to vote proxies will typically reside with the borrower of the shares.

Although it is our policy to seek to vote all proxies for the securities held in your account(s) for which we have proxy voting authority, in the case of non-U.S. issuers proxies are voted on a best efforts basis. Generally, research coverage of non-U.S. issuers is issued through Egan-Jones. Voting recommendations are not always provided with research; therefore, ballots for non-U.S. issuers are generally voted according to the chosen policy.

A custodian may, in its discretion, determine that it will provide proxies to Broadridge for U.S. domestic companies, but not for foreign or global companies. Or, custodians may determine to provide proxies for

non-U.S. companies to their selected proxy voting provider. In these instances, Broadridge is generally not able to vote non-U.S. proxies for your account.

It is within each custodian's discretion as to whether it will provide ballots to Broadridge for issuers whose stocks are held in your account. Instead, a custodian may select its own proxy voting provider and choose not to provide proxy ballots to Broadridge. In these instances, Broadridge is generally not able to vote proxies for your account and KCM generally will not be able to accept voting authority for your accounts.

When voting ballots, it is the custodian's discretion as to whether it will aggregate shares, held on behalf of its various clients, in an omnibus account instead of submitting individual ballots for segregated accounts. In these cases, custodians must rely on their own internal records to differentiate the various underlying holdings. In these instances, Broadridge will generally not be able to provide us with a detailed history of voting records at the individual client account level.

You may obtain a copy of our proxy voting policy and procedures or information on your voting history by writing KCM, 10829 Olive Boulevard, St. Louis, MO, 63141.

### ***Clients That Retain Proxy Voting Authority***

If you do not grant us proxy voting authority, you will receive proxies and other solicitations directly from your custodian or a transfer agent. Generally, we do not provide advice on proxy voting issues when a client retains authority to handle such matters.

### ***Class Action Lawsuits***

From time to time, we may receive notification that securities held in your account may be the subject of a class action lawsuit. If you are an existing client, we will make our best efforts to determine if securities held by you in your custodial account are subject to a pending or resolved class action lawsuit. We will make our best efforts to evaluate your eligibility and, if eligible, we will submit a claim on your behalf to participate in the proceeds of a securities class action settlement or verdict. Eligibility is generally based on the accounts for which purchases and sales of the affected security were executed during the class action period while under our management. However, if we do not receive the claim forms or other necessary documentation in a timely manner, we may not be able to file a claim on your behalf. Moreover, we will not submit claims for securities purchased by a prior manager as we will not have the transaction information pertaining to your account that is needed in order for us to file a proof of claim on your behalf.

If you have assigned your custodian or another third-party the responsibility of filing class action claims on your behalf, please advise us so that we do not duplicate any filings. If you instruct us not to file class action lawsuits on your behalf, we will forward to you on a best efforts basis any information we receive regarding class action legal matters for the securities held in your account.



## FINANCIAL INFORMATION

### ***Balance Sheet***

We do not require prepayment of more than \$1,200 in fees per client, six months or more in advance; therefore, a balance sheet is not required to be included with this Brochure.

### ***Financial Conditions Reasonably Likely to Impair Ability to Meet Contractual Commitments to Clients***

We do not currently believe nor foresee any financial condition that is reasonably likely to impair our ability to meet our contractual commitments to clients.

### ***Bankruptcy Petitions in Previous Ten Years***

We have not been the subject of a bankruptcy petition in the last ten years.