

# **BlueGrass Investment Management, LLC**

## **Form ADV Part 2**

**March 30, 2013**

This brochure provides information about the qualifications and business practices of BlueGrass Investment Management, LLC (the “Adviser”), an investment adviser registered with the United States Securities and Exchange Commission (the “SEC”). Registration with the SEC does not imply a certain level of skill or training. If you have any questions about the contents of this brochure, please contact us at (859) 879-6731 or [andreatew@mindspring.com](mailto:andreatew@mindspring.com). This information has not been approved or verified by the SEC or any state securities authority.

Additional information about BlueGrass Investment Management, LLC is available on the SEC’s website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). You can search this site by our unique CRD number, 149906.

**BlueGrass Investment Management, LLC**  
**910 Aiken Road**  
**Versailles, Kentucky 40383**  
**(859) 879-6731**

## **Material Changes**

The following information has changed materially from our last Form ADV, Part II:

- BlueGrass Investment Management, LLC (the “Adviser” or “BGIM”) has updated Items 4, 7, and 8 to reflect that it provides investment advisory services to individual retirement accounts and to provide disclosure regarding the opportunistic derivatives strategies that it offers to such accounts.

### **Item 3. TABLE OF CONTENTS**

<b><u>Item Number</u></b>	<b><u>Item</u></b>	<b><u>Page</u></b>
Item 1.	Cover Page.....	1
Item 2.	Material Changes.....	2
Item 3.	Table of Contents.....	3
Item 4.	Advisory Business.....	4
Item 5.	Fees and Compensation.....	4
Item 6.	Performance-Based Fees and Side by Side Management.....	5
Item 7.	Types of Clients.....	5
Item 8.	Methods of Analysis, Sources of Information, and Investment Strategy.....	5
Item 9.	Disciplinary Information.....	11
Item 10.	Other Financial Industry Activities and Affiliations.....	11
Item 11.	Code of Ethics, Participation in Client Transactions, & Personal Trading.....	11
Item 12.	Brokerage Practices.....	12
Item 13.	Review of Accounts.....	13
Item 14.	Client Referrals and Other Compensation.....	13
Item 15.	Custody.....	13
Item 16.	Investment Discretion.....	13
Item 17.	Voting Client Securities.....	14
Item 18.	Financial Information.....	14
Item 19.	Requirements for State-Registered Advisers.....	14

#### **Item 4. Advisory Business**

BlueGrass Investment Management, LLC (“BGIM” or the “Adviser”) is an investment advisor with its principal place of business in Versailles, Kentucky. BGIM commenced operations as an investment adviser on April 7, 2009. The principal owners of BGIM are Bernard V. Tew and Andrea B. Tew.

BGIM provides the following advisory services on discretionary basis to its clients, which consist primarily of institutional pension plans and individual retirement accounts: (i) investment supervisory services on a discretionary basis, and (ii) related advice regarding the management and operations of institutional pension plans through consultations not involving investment supervisory services.

With respect to BGIM’s institutional pension plan clients, its services include the following “Master Manager Investment Management Services” provided to institutional pension plans on an on-going basis:

- Determine the effective liabilities of the fund and the "cost" of changes in the liability stream
- Establish the present value of the effective liabilities
- Compare the pension plan's current asset allocations to the current effective liability projections
- Model the effects of changes in the pension plan's effective liabilities on pension plan funding ratio
- Make recommendations concerning changes to asset allocation
- Analyze the asset allocation
- Recommend adjustments in the asset classes to reduce the volatility of the fund's effective funding ratio
- Monitor asset class changes due to changing conditions in the financial markets
- Monitor changes in correlations among asset classes that may increase the volatility of the pension plan's funding ratio
- Manage assets in individual asset classes including listed fixed income investments, privately-placed fixed income investments, core equity investments, quantitative equity investments, privately-placed equity investments, privately-placed real estate investments, and cash and liquidity requirements of the pension plan

All of the above services are individually tailored to meet the specific investment objectives and strategies as defined by a pension plan’s board of trustees and its Investment Policy, which may include or exclude specific securities or types of securities. The advisory services provided to individual retirement accounts are also individually tailored.

As of December 31, 2012, BGIM has discretionary authority over approximately \$49,071,695.00 in client assets under management.

#### **Item 5. Fees and Compensation**

The Adviser charges each client an investment management fee based on the value of the client’s assets under management, according to the following schedule:

<u>Assets Under Management:</u>	<u>Annual Fee:</u>
\$0 - \$50,000,000	2.00%
\$50,000,001 - \$100,000,000	1.50%
\$100,000,001 - \$1,000,000,000	1.00%
\$1,000,000,001 +	0.75%

Investment management fees are charged each month in arrears based on the total market value of the assets in the client account (including net unrealized appreciation or depreciation of investments and cash, cash equivalents and accrued interest) on the last day of the month. If a new client account is established during a month or a client makes an addition to its account during a month, the investment management fee will be prorated for the number of days remaining in the month. If a client's investment management agreement is terminated during a month, the fee payable to the Adviser will be calculated based on the value of the assets on the termination date and prorated for the number of days during the month in which the investment management arrangement was in effect. The Adviser instructs the client's custodian to deduct the investment management fee from the client's account each month.

In addition to paying investment management fees, client accounts will also be subject to other investment expenses such as custodial charges, brokerage fees, commissions and related costs; interest expenses; taxes, duties and other governmental charges; transfer and registration fees or similar expenses; costs associated with foreign exchange transactions; other portfolio expenses; and costs, expenses and fees (including, investment advisory and other fees charged by other investment advisers with, or funds in, which the client's account invests) associated with products or services that may be necessary or incidental to such investments or accounts. Client assets may be invested in pooled investment vehicles. In these cases, clients will bear their pro rata share of the underlying fund's operating and other expenses including, in addition to those listed above: sales expenses, legal expenses; internal and external accounting, audit and tax preparation expenses; and organizational expenses. Comparable services may be available from other sources for fees lower or higher than those charged by the Adviser. Fees are negotiable in some special circumstances. The Adviser reserves the right in its sole discretion to charge fees that are less than those the Adviser is entitled to under the terms of the applicable investment advisory agreement.

A client may terminate its Investment Management Agreement with the Adviser under any of the following circumstances: (1) At client's discretion, with or without cause, after ten (10) business days written notice to the Adviser; or (2) immediately upon the Adviser's default or breach of the Agreement. The Adviser may terminate the Investment Management Agreement, with or without cause, after thirty (30) days' written notice to the client. In the event of any termination by either party, the Adviser will cooperate with the client to ensure the orderly transfer of client assets.

#### **Item 6. Performance-Based Fees and Side-by-side Management**

This item is not applicable.

#### **Item 7. Types of Clients**

The Adviser's clients consist primarily of (i) institutional pension and profit sharing plans and (ii) individual retirement accounts. With respect to its institutional pension plan clients, the Adviser generally requires that a client invests a minimum of \$1,000,000 to open an account and to maintain a minimum account size of \$1,000,000 for separate accounts. If the account size falls below the minimum requirement due to market fluctuations only, a client will not be required to invest additional funds with the Adviser to meet the minimum account size. With respect to its individual retirement account clients, the Adviser generally requires that a client invest a minimum of \$5,000 to open an account.

#### **Item 8. Methods of Analysis, Sources of Information, and Investment Strategy**

The Adviser utilizes quantitative methods of investment and portfolio analysis as the foundation of its investment approach. These quantitative methods are based on a rigorous application of financial theory which incorporate impartial statistical and mathematical processes. However, the Adviser is not limited by such quantitative methods in making investment decisions and will make tactical and opportunistic investments in a wide range of transactions when opportunities present themselves. A brief summary of the significant investment strategies employed by the Adviser in managing client assets is set forth below.

## **I. Listed Fixed Income Investment Management**

Fixed income securities generally represent a highly liquid investment instrument for producing income, while providing some diversification versus equity investments. Prior to selecting individual securities, we analyze general economic trends and the prevailing supply/demand for newly-issued securities. This structural information is important in forecasting short- and long-term changes in interest rates, as well as shifts in the yield curve. The Adviser seeks to construct a portfolio of bonds consistent with this outlook. Our domestic and international fixed income selection process engages economic analysis, yield curve assessment, security selection through numerous channels to identify securities and continuous portfolio review.

## **II. Privately-placed Fixed Income Investment Management**

Privately-placed Fixed Income Investments shall include, but not be limited to, PTE85-68 customer notes, as exempted from ERISA Sections 406(a), 406(b)(1) and (2)) and Section 407, and ERISA Code Sections 4975 (a) and (b). Investment Management responsibilities include the following:

- Determine that customer notes are two-party interests, executed with a security agreement for tangible property, accepted in connection with and in the normal course of the creditor's primary business activity.
- After the acquisition of the note, all customer notes will not represent more than 50% of the current value of the Pension Plan's assets, and any one customer note will not represent more than 10% of the current value of the Pension Plan's assets.
- Secure in writing a guarantee for immediate repayment of the outstanding balance of the customer note plus all accrued interest if the customer note is more than 60 days in arrears and the safety of the principal is determined to be impaired.
- File a UCC Article 9 Financing Statement in the name of the Pension Plan.
- Determine that the real property secured by the customer note is insured against loss and the proceeds of such policy are assigned to the Pension Plan.
- Determine that the customer note has met these applicable guidelines:
  1. If secured by heavy equipment, the note duration is no more than 60 months.
  2. If secured by passenger automobiles and light-duty highway motor vehicles, the duration of the customer note is no more than 48 months.
  3. If secured by tangible property not described in Items 1 or 2 above, the duration of the customer note is no more than 36 months.

## **III. Core Equity Investment Management**

Through a rigorous process based upon in-depth analysis, the Adviser seeks to construct a diversified portfolio of companies that have attractive growth or return prospects, or are undervalued relative to their net asset value. We typically evaluate companies based on quantitative metrics as well as qualitatively assessing corporate management, business strategy and macro factors impacting the industry. Importantly, we analyze an investment's risk before addressing the potential return opportunity. Business criteria focuses on profitability, financial resources, the market position of the company, and the historical track record of the management team. Additionally, we intensively assess the competitive landscape within the industry, identifying key macro trends as well as economic, political, and regulatory risks. Valuation is determined utilizing internally generated risk-reward criteria. Price targets typically are developed for each company in the portfolio and reassessed based on business and economic trends. Portfolio positions are eliminated when one of three conditions occurs:

- the company's stock has met our price objective,
- another position offers better risk/reward characteristics, or

- deterioration in the business or industry has made the company susceptible to a permanent impairment.

By creating a diversified portfolio of attractive companies, and performing thorough analysis throughout the lifecycle of each investment, our Core Equity Portfolio is designed to produce consistent results.

#### **IV. Quantitative Equity Management**

The Adviser's Quantitative Equity Management strategy focuses on developing a quantitative driven long-short portfolio. The investment philosophy is a rigorous application of financial theory in which impartial statistical and mathematical processes are the foundation of the portfolio's construction process rather than fundamental or technical methods. The objective of this portfolio is to provide positive total returns over a complete three to five year market cycle. The portfolio construction process begins with an analysis of each security in the benchmark portfolio. This initial collection of securities forms the beginning optimization universe. All securities are screened to eliminate issues that do not have sufficient weekly volume to facilitate trading costs and those that are potential candidates for bankruptcy in the near term. Volatility and co-volatility estimates are calculated for each security. Minimum and maximum potential holding positions are computed for each security in the optimization universe. Optimal portfolio weights are calculated for each optimization universe using a mean-variance, nonlinear optimization method. The portfolio is monitored on a daily basis. Rebalancing activity occurs when positions exceed optimal weights and portions of the holdings are sold to return the positions to optimal weights or when positions are less than optimal and securities are bought to retain optimality. Finally, the entire portfolio construction process is repeated periodically to ensure that the portfolio remains well diversified and displays characteristics that are consistent with the Adviser's investment philosophy.

#### **V. Privately Placed Equity Investment Management**

Private Equity Management seeks to make investments in non-public corporations offering superior return possibilities through capital appreciation in domestic, international, and emerging markets. Opportunities may be in middle market direct investments, middle markets buyouts, distressed private equity securities, and distressed private buyouts.

Management responsibilities in connection with the Private Placed Equity Strategies include:

- Obtaining correct formation and operating agreements and all other articles of organization governing the target investment
- Obtaining relevant minutes for previous members and managers or directors
- Acquiring a list of all members or unit holders and the percentage of membership
- Determining a list of outstanding warrants, options, and other rights to acquire any interest in the target investment company
- Obtaining copies of all shareholder/member agreements and voting trusts
- Obtaining a list of subsidiaries, affiliates, and joint ventures showing ownership percentages or revenue sharing arrangements with the target company
- Determining a list of locations where the company does business, and in any states in which it may be qualified as a foreign company
- Identifying current officers and managers
- Examining audited financial statements for the past three years or, in the event the company does not have audited statements, all unaudited statements for the past three years
- Examining federal, state, and local tax returns and any correspondence with taxing authorities for the past three years

- Examining current financial plans, budgets, projections, and similar materials prepared by current management
- Examining business plans for the company for the past three years, including all marketing and other descriptive brochures and all press releases
- Examining executed or proposed material contracts, including any defaults on previous agreements
- Examining insurance policies covering real or personal property, operations, lives of employees or managers
- Obtaining a list of all liens, charges, and encumbrances
- Evaluating existing environmental reports
- Evaluating employment, management, and consulting agreements including all stock options plans or similar arrangements
- Evaluating confidentiality, non-disclosure, and non-competition agreements
- Evaluating existing litigation or terminated litigation, including all settlements, judgments, and orders to which the target company is subject
- Evaluating licenses and permits, including intellectual property rights owned by the company
- Examining real or leased property used by the company, including leases, mortgages, title insurance, and appraisals
- Evaluating and examining agreements to which the target has acquired security or membership units, including prospectuses and private placements memoranda
- Listing all agreements, transactions, and other business relationships between the target company and any member, manager, or officer of the target company

## **VI. Privately Placed Real Estate Investment Management**

Privately Placed Real Estate Investments, including but not limited to those defined by ERISA Section 407/408(e) as Qualifying Employer Real Property (QERP). The Adviser seeks to secure investment(s) in unique income-producing and value-added properties identified on an opportunistic basis. This management shall include:

- Determining that the real estate is dispersed geographically and that each parcel of real estate and improvements are suitable for more than one use, and that the acquisition of said property is for adequate consideration
- Originating and negotiating a competitive lease agreement and manage all aspects of leasing the property
- Obtaining an independent appraisal to determine that adequate consideration was given and received

## **VII. Derivatives and Opportunistic Transactions**

For individual retirement accounts, BGIM pursues a flexible investment strategy focused on deploying assets in opportunistic transactions. These opportunistic transactions typically focus on unique or limited investment opportunities identified by BGIM. Trades in identified opportunities are often of limited duration and may be expressed through a variety of derivative investments related to equities, debt currencies and other assets traded in markets around the world. Through such limited opportunity transactions, BGIM seeks to provide its clients with discrete opportunities for the generation of returns that share low correlations with other sources of active return. In this regard, participation in these transactions



is not intended to be a complete investment strategy for any portfolio or client, but rather a supplement to a broader investment strategy.

Investing in securities involves significant risks, including the risk of loss of some or all of an investment. Prospective investors should speak with their legal, tax, and financial advisors prior to making an investment with BGIM. The following summary identifies the material risks related to BGIM's significant investment strategies and should be carefully evaluated before making investment with BGIM; however, the following does not intend to identify all possible risks of an investment with BGIM or provide a full description of the identified risks.

- *Equity Securities.* The value of equity securities fluctuates in response to issuer, political, market, and economic developments. Fluctuations can be dramatic over the short as well as long term, and different parts of the market and different types of equity securities can react differently to these developments. For example, large cap stocks can react differently from small cap stocks, and "growth" stocks can react differently from "value" stocks. Issuer, political, or economic developments can affect a single issuer, issuers within an industry or economic sector or geographic region, or the market as a whole. Changes in the financial condition of a single issuer can impact the market as a whole. Terrorism and related geo-political risks have led, and may in the future lead, to increased short-term market volatility and may have adverse long-term effects on world economies and markets generally.
- *Fixed-Income and Debt Securities.* Investment in fixed-income and debt securities such as bonds, notes and asset-backed securities, subject a client's portfolios to the risk that the value of these securities overall will decline because of rising interest rates. Similarly, portfolios that hold such securities are subject to the risk that the portfolio's income will decline because of falling interest rates. Investments in these types of securities will also be subject to the credit risk created when a debt issuer fails to pay interest and principal in a timely manner, or that negative perceptions of the issuer's ability to make such payments will cause the price of that debt to decline. Lastly, investments in debt securities will also subject the investments to the risk that the securities may fluctuate more in price, and are less liquid than higher-rated securities because issuers of such lower-rated debt securities are not as strong financially, and are more likely to encounter financial difficulties and be more vulnerable to adverse changes in the economy.
- *Distressed Situation Risk.* Investment in distressed situations exposes the client to significant risks, including: the difficulty in obtaining information as to the issuer's true condition; regulatory risk, including laws relating to fraudulent conveyances, voidable preferences, lender liability and bankruptcy; litigation risk; liquidity risk; and collection risk.
- *Hedging.* There can be no assurances that a particular hedge is appropriate, or that certain risk is measured properly. Further, while the Adviser may enter into hedging transactions to seek to reduce risk, such transactions may result in poorer overall performance and increased (rather than reduced) risk for the Adviser's investment portfolios than if the Adviser did not engage in any such hedging transactions.
- *Interest Rate Risks.* Generally, the value of fixed-income securities changes inversely with changes in interest rates. As interest rates rise, the market value of fixed-income securities tends to decrease. Conversely, as interest rates fall, the market value of fixed-income securities tends to increase. This risk is greater for long-term securities than for short-term securities.
- *Issuer-Specific Changes.* Changes in the financial condition of an issuer or counterparty, changes in specific economic or political conditions that affect a particular type of security or issuer, and changes in general economic or political conditions can increase the risk of default by an issuer or counterparty, which can affect a security's or instrument's value. The value of securities of smaller, less well-known issuers can be more volatile than that of larger issuers. Smaller issuers can have more limited product lines, markets, or financial resources.

- *Lack of Diversification.* Client accounts may not be diversified among a wide range of types of securities, countries or industry sectors. Accordingly, client portfolios are subject to more rapid change in value than would be the case if the Adviser were required to maintain a wider diversification among types of securities and other instruments.
- *Relative Value Risk.* In the event that the perceived mispricings underlying the Adviser's relative value trading positions were to fail to converge toward, or were to diverge further from, relationships expected by the Adviser, client accounts may incur a loss.
- *Asset-Backed Securities.* Asset-backed securities are subject to interest rate risk and, to a lesser degree, prepayment risk. Asset-backed securities are subject to additional risks in that, unlike mortgage-backed securities, asset-backed securities generally do not have the benefit of a security interest in the related collateral. Each type of asset-backed security also entails unique risks depending on the type of assets involved and the legal structure used. In addition, asset-backed securities experience credit risk. There is also the possibility that recoveries on repossessed collateral may not be available to support payments on these securities because of the inability to perfect a security interest in such collateral.
- *Distressed Securities.* Investments in unrated or low grade debt securities of distressed companies are subject to greater risk of loss of principal and interest than higher-rated debt securities. Also, securities of distressed companies are generally more likely to become worthless than the securities of more financially stable companies
- *Hard Assets.* The production and marketing of hard assets may be affected by actions and changes in governments. In addition, hard assets and hard asset securities may be cyclical in nature. During periods of economic or financial instability, hard asset securities may be subject to broad price fluctuations, reflecting volatility of energy and basic materials prices and possible instability of supply of various hard assets. In addition, hard asset companies may also be subject to the risks associated with extraction of natural resources as well as the risks of the hazards associated with natural resources, such as fire, drought, and increased regulatory and environmental costs. Hard asset securities may also experience greater price fluctuations than the relevant hard asset.
- *Illiquid Instruments.* Certain instruments may have no readily available market or third-party pricing. Reduced liquidity may have an adverse impact on market price and the Adviser's ability to sell particular securities when necessary to meet liquidity needs or in response to a specific economic event, such as the deterioration of creditworthiness of an issuer. Reduced liquidity in the secondary market for certain securities may also make it more difficult for the Adviser to obtain market quotations based on actual trades for the purpose of valuing a fund's portfolio.
- *Mortgage-Backed Securities.* Mortgage-backed securities are subject to credit risk associated with the performance of the underlying mortgage properties. Factors such as consumer spending habits, local economic and competitive conditions, tenant occupancy rates and regulatory or zoning restrictions, or the loss of a major tenant may adversely affect the economic viability of a mortgaged property. In addition, these securities are subject to prepayment risk. Some securities have a structure that makes their reaction to interest rates and other factors difficult to predict, making their value highly volatile.
- *Derivatives.* Swaps, and certain options and other custom derivative or synthetic instruments are subject to the risk of nonperformance by the counterparty to such instrument, including risks relating to the financial soundness and creditworthiness of the counterparty. In addition, investments in derivative instruments require a high degree of leverage, meaning the overall contract value (and, accordingly, the potential for profits or losses in that value) is much greater than the modest deposit used to buy the position in the derivative contract. Derivative securities can also be highly volatile. The prices of derivative instruments and the investments underlying the derivative instruments may fluctuate rapidly and over wide ranges and may reflect

unforeseeable events or changes in conditions, none of which can be controlled by the *client* or the Adviser. Further, transactions in derivative instruments are not undertaken on recognized exchanges, and will expose the *client's* account to greater risks than regulated exchange transactions that provide greater liquidity and more accurate valuation of securities.

- *Non-U.S. Securities.* Foreign securities, foreign currencies, and securities issued by U.S. entities with substantial foreign operations can involve additional risks relating to political, economic, or regulatory conditions in foreign countries. These risks include fluctuations in foreign currencies; withholding or other taxes; trading, settlement, custodial, and other operational risks; and the less stringent investor protection and disclosure standards of some foreign markets. All of these factors can make foreign investments, especially those in emerging markets, more volatile and potentially less liquid than U.S. investments. In addition, foreign markets can perform differently from the U.S. market.
- *Regulatory Risk; Changes in the Law.* The regulation of derivative transactions is an evolving area of law and is subject to modification by government and judicial actions. The effect of any future regulatory action or change in the law could be substantial and adverse on the Adviser's ability to pursue its trading strategies, including any opportunistic transactions for the individual retirement accounts.

#### **Item 9. Disciplinary Information**

This item is not applicable.

#### **Item 10. Other Financial Industry Activities and Affiliations**

This item is not applicable.

#### **Item 11. Code of Ethics, Participation in Client Transactions, & Personal Trading**

The Adviser has adopted a Code of Ethics (the "Code") that obligates the Adviser and its related persons to put the interests of the Adviser's clients before its own interests and to act honestly and fairly in all respects in their dealings with clients. All of the Adviser's personnel are also required to comply with applicable federal securities laws. Clients or prospective clients may obtain a copy of the Code by contacting Andrea Tew by email at [andreatew@mindspring.com](mailto:andreatew@mindspring.com), or by telephone at (859) 879-6731.

To avoid any potential conflict of interest involving personal transactions, the Code requires the Adviser's related persons to pre-clear transactions in personal accounts with the Compliance Officer and to disclose all potential conflicts of interest with regard to such a personal transaction before engaging in the transaction. Related persons are also subject to a restricted list and are required to have duplicate copies of personal account statements sent to the Adviser for review.

#### *Inside Information*

In addition, the Adviser has adopted procedures to guard against insider trading. The Adviser, in the course of its investment management and other activities, may come into possession of confidential or material nonpublic information about issuers, including issuers in which the Adviser or its related persons have invested or seek to invest on behalf of clients. For example, the Adviser or a related person could learn of material, non-public information about an issuer while serving as a Director of an unrelated entity that is considering a transaction with that issuer. The Adviser is prohibited from improperly disclosing or using such information for its own benefit or for the benefit of any other person, regardless of whether such other person is a client. The Adviser maintains and enforces written policies and procedures that prohibit the communication of such information to persons who do not have a legitimate need to know such information and to assure that the Adviser is meeting its obligations to clients and remains in compliance with applicable law. In certain circumstances, the Adviser may possess certain confidential or material, nonpublic information that, if disclosed, might be material to a decision to buy, sell or hold a security, but

the Adviser will be prohibited from communicating such information to the client or using such information for the client's benefit. In such circumstances, the Adviser will have no responsibility or liability to the client for not disclosing such information to the client (or the fact that the Adviser possesses such information), or not using such information for the client's benefit, as a result of following the Adviser's policies and procedures designed to provide reasonable assurances that it is complying with applicable law.

#### *Interest in Client Transactions*

The Adviser may recommend securities in which it or its related persons directly or indirectly have a financial interest. Such practices may present a conflict of interest where the Adviser is in a position to trade in a manner that could adversely affect clients (e.g., place its own trades before or after client trades are executed in order to benefit from any price movements due to the clients' trades). The Adviser will seek to avoid such situations. If necessary, however, the Adviser will aggregate its trades with client trades so that the Adviser does not receive a better price than the client.

#### **Item 12. Brokerage Practices**

Each of the Adviser's clients directs it to execute the client's trades with a specified broker-dealer. Accordingly, the Adviser treats the client's direction as a decision by the client to retain, to the extent of the direction, the discretion the Adviser would otherwise have in selecting broker-dealers to effect transactions and in negotiating commissions for the client's account. Transactions in the same security for accounts that have directed the use of the same broker generally will be aggregated. When the directed broker-dealer is unable to execute a trade, the Adviser will select broker-dealers other than the directed broker-dealer to effect client securities transactions. In such cases, when selecting a broker-dealer to execute transactions (or series of transactions) and determining the reasonableness of the broker-dealer's compensation, the Adviser need not solicit competitive bids and does not have an obligation to seek the lowest available commission cost. It is not the Adviser's practice to negotiate "execution only" commission rates, thus a client may be deemed to be paying for research, brokerage or other services provided by a broker-dealer which are included in the commission rate.

A client who directs the Adviser to use a particular broker-dealer to effect transactions should consider whether such direction may result in certain costs or disadvantages to the client. Such costs may include higher brokerage commissions (because the Adviser may not be able to aggregate orders to reduce transaction costs), less favorable execution of transactions, and the potential of exclusion from the client's portfolio of certain foreign ordinary shares and/or small capitalization or illiquid securities due to the inability of the particular broker-dealer in question to provide adequate price and execution of all types of securities transactions. By permitting a client to direct the Adviser to execute the client's trades through a specified broker-dealer, the Adviser will make no attempt to negotiate commissions on behalf of the client and, as a result, in some transactions such clients may pay materially disparate commissions depending on their commission arrangement with the specified broker-dealer and upon other factors such as number of shares, round and odd lots and the market for the security. The commissions charged to clients that direct the Adviser to execute the client's trades through a specified broker-dealer may in some transactions be materially different than those of clients who do not direct the execution of their trades. Client's that direct the Adviser to execute the client's trades through a specified broker-dealer may also lose the ability to negotiate volume commission discounts on batched transactions that may otherwise be available to other clients of the Adviser.

The Adviser often purchases or sells the same security for many clients contemporaneously/at or near the same time and using the same executing broker. It is generally the Adviser's practice, where possible, to aggregate client orders for the purchase or sale of the same security submitted contemporaneously/at or near the same time for execution using the same executing broker. When an aggregated order is completely filled, the Adviser allocates the securities purchased or proceeds of sale pro rata among the participating accounts, based on the purchase or sale order. Adjustments or changes may be made under certain circumstances, such as to avoid odd lots or excessively small allocations. If the order at a particular broker is filled at several different prices, through multiple trades, generally all such participating accounts

will receive the average price and pay the average commission, subject to odd lots, rounding, and market practice. If an aggregated order is only partially filled, the Adviser's procedures provide that the securities or proceeds are to be allocated in a manner deemed fair and equitable to clients. Depending on the investment strategy pursued and the type of security, this may result in a pro rata allocation to all participating clients.

### **Item 13. Review of Accounts**

Each client account is reviewed by the managing director of the Adviser, on a no less than quarterly basis to determine whether securities positions should be maintained in view of current market conditions. Matters reviewed include specific securities held, adherence to investment guidelines and the performance of each client account. Significant market events affecting the prices of one or more securities in client accounts or changes in the investment objectives or guidelines of a particular client may trigger reviews of client accounts on other than a periodic basis. Each client that is a separate account will receive quarterly reports from the Adviser. Such reports may be delivered electronically to the client in accordance with the client's agreement with the Adviser.

### **Item 14. Client Referrals and Other Compensation**

This item is not applicable.

### **Item 15. Custody**

The Adviser is deemed to have custody of many of the assets it manages for clients, and it will comply with all applicable custody requirements. Some of those assets are maintained by the Adviser with broker-dealers, banks, or other qualified custodians. These qualified custodians send account statements, which should be carefully reviewed, directly to each client at least quarterly. In addition, the Adviser sends monthly statements to each client that describe all of that client's assets, regardless of where they are maintained. Clients should compare any statements they receive from the qualified custodian with those received from the Adviser.

### **Item 16. Investment Discretion**

The Adviser provides investment advisory services on a discretionary basis to clients. Prior to assuming full discretion in managing a client's assets, the Adviser enters into an investment management agreement or other agreement that sets forth the scope of the Adviser's discretion. Unless otherwise instructed or directed by a discretionary client, the Adviser has the authority to determine (i) the securities to be purchased and sold for the client account (subject to restrictions on its activities set forth in the applicable investment management agreement and any written investment guidelines) (ii) the amount of securities to be purchased or sold for the client account. Because of the differences in client investment objectives and strategies, risk tolerances, tax status and other criteria, there may be differences among clients in invested positions and securities held. The Adviser may consider the following factors, among others, in allocating securities among clients: (i) client investment objectives and strategies; (ii) client risk profiles; (iii) tax status and restrictions placed on a client's portfolio by the client or by applicable law; (iv) size of the client account; (v) nature and liquidity of the security to be allocated; (vi) size of available position; (vii) current market conditions; and (viii) account liquidity, account requirements for liquidity and timing of cash flows. Although it is generally the Adviser's policy to allocate investment opportunities to eligible client accounts on a pro rata basis (based on the value of the assets of each participating account relative to value of the assets of all participating accounts), these factors may lead the Adviser to allocate securities to client accounts in varying amounts. Even client accounts that are typically managed on a pari passu basis may from time to time receive differing allocations of securities based on total assets of each account eligible to invest in the particular investment type (e.g., equities) divided by the total assets of all accounts eligible to invest in the particular investment.

**Item 17. Voting Client Securities**

To the extent the Adviser has been delegated proxy voting authority on behalf of its clients, the Adviser complies with its proxy voting policies and procedures that are designed to ensure that in cases where the Adviser votes proxies with respect to client securities, such proxies are voted in the best interests of its clients.

The Adviser's clients are permitted to direct their votes in a particular solicitation. A client that wishes to direct its vote in a particular solicitation shall give reasonable prior written notice to the Adviser indicating such intention and provide written instructions directing the Adviser's vote in regard to the particular solicitation. Where such prior written notice is received, the Adviser will vote proxies in accordance with such written instructions received from a client, provided that such instructions are provided to the Adviser in a timely manner.

If a material conflict of interest between the Adviser and a client exists, the Adviser will determine whether voting in accordance with the guidelines set forth in the proxy voting policies and procedures is in the best interests of the client or take some other appropriate action. The Adviser does not make any qualitative judgment regarding its client's investments.

Clients may obtain a copy of the Adviser's proxy voting policies and procedures and information about how the Adviser voted a client's proxies by contacting Andrea Tew by email at [andreatew@mindspring.com](mailto:andreatew@mindspring.com) or by telephone at (859) 879-6731.

**Item 18. Financial Information**

This item is not applicable.

**Item 19. Requirements for State-Registered Advisers**

This item is not applicable.