

Michael K. Davis Investment Services

Firm Brochure

This brochure provides information about the qualifications and business practices of Michael K. Davis Investment Services. If you have any questions about the contents of this brochure, please contact me directly. The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission or by any state securities authority.

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Table of Contents

Advisory Business.....	3-4
Fees and Compensation.....	4
Types of Clients.....	5
Methods of Analysis, Investment Strategies and Risk of Loss.....	5-6
Disciplinary Information.....	7
Other Financial Industry Activities and Affiliations.....	7
Code of Ethics, Conflicts of Interest, and Personal Trading.....	7-8
Brokerage Practices.....	8
Review of Accounts.....	8-9
Client Referrals and Other Compensation.....	9
Custody.....	9
Investment Discretion.....	9
Voting Client Securities and Proxies.....	9-10
Financial Information.....	10

Advisory Business

I have been performing investment management and advisory services as a sole proprietor since the mid-1980's. At the present time I am the only investment professional in my company responsible for investing client assets and giving investment advice.

Background

I am a graduate of Yale University (BA, Philosophy, 1966) and a graduate of the Harvard Business School (MBA, with Distinction, 1971). After my graduation from Harvard I earned my CPA certification in Massachusetts while working with Price Waterhouse and Co. from 1971 to 1973.

From 1973 to 1985 I was a partner and the chief financial officer of Resource Planning Associates, an international management consulting firm specializing in environmental and energy issues for both the public and private sector clients. Over these years I was also actively involved in commercial real estate investment and management.

In my career as an investment adviser I have never been subject to any disciplinary or legal actions related to my professional responsibilities.

Services Provided

My practice consists of two primary services for clients: 1) asset management; and 2) financial planning and investment consulting services.

My asset management practice involves investing client resources in a variety of investment vehicles, including individual stocks and bonds, exchange traded funds ("ETFs"), short-term financial instruments, closed- end funds, and master limited partnerships. To a lesser extent, client funds are invested in actively managed open-ended mutual funds. For some clients, option strategies (typically "covered call" writing), are employed to reduce risk in over-weighted positions or to enhance income.

When appropriate, I may recommend client investments in other alternative investment ideas (such as real estate limited partnerships, or oil and gas partnerships).

Client portfolios are individually structured to account for a client's risk preferences and financial objectives (see Section IV for a discussion of Investment Strategies and related considerations).

My practice is 100% discretionary, but occasionally a client may suggest a specific investment restriction (e.g., no investments in cigarette company stocks), or a more generalized investment restriction (e.g., no sale of a large inherited security without prior client approval). I have always succeeded in obliging these relatively few requests.

As of the end of January 2013 I had approximately \$118,000,000 in discretionary assets under management (excluding my personal and direct family accounts).

In addition to investment management services I provide all my clients with general financial and tax planning advice, as well as more specialized consulting services if requested. (See Section II, Fees and Services).

Fees and Compensation

I am a “fee-only” investment adviser, and accept no compensation or commission, direct or indirect, from any third party for any product or security sold to my clients by a third party.

My fees for investment management services are computed on a percentage of average assets under management. I do not provide investment management services on a “performance-based” fee schedule.

Billings for fees are done in arrears, typically in June and December of each year.

My fees are negotiated directly with clients. As a general guideline, minimum assets under management for a new client is \$1 million. The fee for most clients is .75% *per annum* of average assets under management. My fee includes both investment management services and routine financial and tax planning advice.

In special circumstances a client may need financial advice that is beyond normal financial planning advice. In these circumstances I will bill the client for my services on an hourly basis over and above my asset management charge for the consulting services provided. Consulting is done at a negotiated rate, typically \$250.00 per hour. An example of this kind of extraordinary advice might be the development of a strategy for the sale of a family business. The scope and cost of services to be rendered in these cases are agreed upon in advance with the client.

Clients pay all brokerage and transaction related costs, any mutual fund fees, and any other charges from the custodian for services rendered (e.g., money-transfer fees).

In many cases my fees for services rendered are deducted directly from the client’s account on an annual or semi-annual basis. In other cases I am paid by the client directly.

I offer no *wrap-fee* pricing programs.

Types of Clients

My clients consist primarily of high-net-worth individuals. I manage a wide variety of accounts to service their needs, including retirement plans, trust assets, charitable trusts, and pension plans.

At the present time I am not managing assets for institutional investors or other investment companies or institutions.

Methods of Analysis, Investment Strategies, and Risk of Loss

Basic Management Philosophy

I believe it is virtually impossible to predict future market movements based on past market activity, and as a result do not rely on “technical” analysis as a means of making investment decisions. Instead, I prefer a fundamental approach to investing that focuses on investments that I conclude are intrinsically undervalued or overvalued in relation to their current market prices.

As a professional investor I start with a “top-down” macro-economic assessment of the economy and financial markets in order to assess the major trends that can influence investment opportunities and risk. Important factors that I consider include geo-political events, country-specific investment environments, tax and regulatory constraints, major technological trends, and where we appear to be in the business cycle.

From this overview of the investment landscape I then draw conclusions about the relative attractiveness of different investment asset categories to determine appropriate diversification strategies for my clients. These strategies will be customized for each client based on their investment goals, specific liquidity needs, and risk preferences.

Diversification

Because it is impossible to predict the future, *diversification* is an essential element of any investment plan. No investments are truly “risk-free.” However, proper diversification will in many cases reduce the extent of portfolio volatility and the resulting magnitude of loss in adverse market conditions.

Diversification includes allocating investments to broadly different asset categories (e.g., fixed income, equities, money-market funds), and further diversifying among specific investment vehicles within each category.

Example: Assume a client has a primary growth objective for her portfolio. This would generally imply a heavy proportion of equities in her portfolio mix. But proper diversification might require further steps to diversify her equity holdings into international and domestic equities, small-cap and large-cap equities, and “value” and “growth” equities.

Return versus Risk

It is an axiom of investing that asset classes offering higher expected returns entail more risk. This is neither a good thing or a bad thing. But investors seeking higher returns must be prepared for the volatility and risk of loss associated with these investments. On the other hand, an investor must appreciate that investments in common stocks over long periods of time have yielded higher returns than fixed-income investments, and that bonds correspondingly have done better than low-risk money-market funds.

The amount of risk a client should assume is a function of a number of considerations, among them liquidity needs, life style, employment status and security, years to retirement or life expectancy, and total net worth. Another important consideration is a client's *psychological comfort* with risk.

An important role of the investment adviser is to help each client think through these issues to develop investment goals and strategies that balance portfolio risk and potential returns appropriately. No two clients are absolutely alike, and I attempt to tailor each client's investment strategy to meet individual needs and objectives.

Long-Term Investment Perspective

My investment inclination is to hold on to good investments unless circumstances (liquidity needs, tax considerations) warrant liquidation. Reasons for selling include: 1) my investment thesis is no longer valid or the investment strategy is being modified; 2) the specific investment appreciates to the point where valuation no longer makes sense or the security is over-weighted in relation to the desired asset allocation; or 3) I have a better idea for the client. I generally don't sell an investment I believe in just because the price drops; indeed, a falling market is often an opportunity to buy at a better price. And as a general rule I do not believe in taking a "quick profit" in a security; in my experience the best investment ideas pay off over multiple years of steady appreciation.

Tax-Efficiency

Tax effects can have a significant impact on a client's effective net total returns. As just one example, the current difference between Federal short-term and long-term capital gain rates can be as much as 20-25% for high net worth individuals. To minimize the effective taxes on clients' taxable portfolios a number of strategies may be employed:

- Use of tax-free municipal bonds in lieu of taxable bonds in taxable accounts
- Use of exchange traded index funds in lieu of actively managed mutual funds to minimize portfolio turnover and realized capital gains
- Avoidance of frequent trades and rapid portfolio turnover to minimize short-term capital gains and transaction costs
- Balancing capital gains against losses when appropriate to minimize net realized capital gains

Disciplinary Information

I have no professional disciplinary events or actions to report, nor are there any legal proceedings relating to my professional practice of any kind.

Other Financial Industry Activities and Affiliations

None.

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

Clients look for two essential qualities in their investment advisor. The first is *competence*, meaning the advisor has the necessary combination of educational background, experience, maturity, and talent to give clients good advice and manage their investments effectively. The second quality is *integrity*, providing assurance that the advisor is putting his clients' interests before his own, and that the representations he makes to clients are complete and accurate.

How do I assure a client that I am acting in her best interest? The most important thing in my mind is to avoid any serious conflict of interest. Compensation is perhaps the area with the most obvious potential conflicts of interest for investment advisors. *As a "fee only" investment advisor I do not accept compensation from anyone other than my client.* For example, I may recommend that clients purchase or refinance a home, or buy insurance or annuity products. I may if requested recommend an attorney, a mortgage broker, a banker, or tax advisor. I may suggest that a client invest in a private offering or other alternative investment. But in no case do I accept any third-party compensation, direct or indirect, for any of these recommendations.

I do not compensate anyone, directly or indirectly, for a client referral. This assures the prospective client that any third-party recommendation to work with me is not made for reasons of financial gain. In reality, most of my referrals come unsolicited from existing clients.

I do not buy securities from clients for my own account, nor sell securities to clients from my own account.

On rare occasion I have invested personally in a client business venture on the same terms and conditions being offered to other investors. If I were to be the general partner in an investment venture in which I would invite suitable clients to participate as investors, I would recommended the client review the suggested investment with an independent tax or legal advisor. *I have no interest in any investment partnerships or other ventures at the present time in which I am a general partner or managing officer.*

I do invest for my own personal accounts in most of the same securities and investments that are in my clients' portfolios. And it is common for me to be buying and selling securities for my own personal accounts at the same time that I am buying and selling the same securities for my clients' accounts. Most of the securities held in both my personal accounts and those of my clients are marketable securities that are highly liquid

and have daily trading volumes that dwarf the trades made for myself and my clients. As a result, the timing of my personal trades in relation to my clients trades would have no material impact on trade execution or pricing. In these cases I am indifferent to the timing of my personal trade relative to a client's trade.

However, there are occasionally securities in client portfolios that are relatively thinly traded. Some individual municipal and corporate bonds and some relatively small closed-end mutual funds fall into this category. In these cases the trades I execute could have some impact (usually relatively small) on short-term market prices. *My policy on thinly traded securities is to execute trades (buys or sells) for my clients before I would execute a trade on my own behalf.*

Brokerage Practices

Unless a client has a strong preference for a particular brokerage institution, I recommend that my clients use the Charles Schwab Institutional Services Group for custody and brokerage services. There are many other institutions (for example, Fidelity Investments, Vanguard) that are excellent firms and could serve this function equally well. Had I not started a relationship with Schwab Institutional a number of years ago, I might well have established a relationship with a different broker-dealer oriented to serving the needs of the professional investor.

Selecting one institution to concentrate my investment activities is essentially a convenience for me, allowing me to execute trades and track client information on one platform. All the major firms offer competitive commission schedules and comparable services. Having one primary broker-dealer to custody most of my assets under management helps me manage my business efficiently, and allows me to keep my fees competitive in relation to other advisors.

Clients may select a different custodian if they wish. About 20% of my assets under management are with a diverse group of other institutions. I will always accommodate clients who have a good reason for selecting their own brokerage firm for custody. In cases where a client might select a "full-service" broker I will advise them if the commission fee schedule is not competitive, but in the end it is the client's choice.

I do not receive any "soft-dollar" or any other economic benefit from placing client assets with any broker-dealer (see Code of Ethics section above). None of the research or other products available to me through the broker-dealers I work with is related in any way to client commission rates or levels of commissions paid.

Review of Accounts

I review client investment portfolios and holdings both regularly and as circumstances warrant. Formal written communications with performance reports occurs at least once a year, and for a number of accounts twice a year. Informal communications with clients about market conditions, tax issues, financial advice, and their specific portfolios typically occur multiple times per year, and is done by telephone, email, and in informal meetings. During periods of market turbulence or uncertainty these informal communications tend to increase significantly. There is no formal schedule for client meetings, but the small number of individuals and families (approximately 50) that I work with insures close personal attention and no shortage of interactions.

Clients also directly receive their monthly brokerage reports and all trade advices for their portfolios, and have the ability to access and review their portfolios online at any time.

Client Referrals and Other Compensation

I do not pay for client referrals from third parties, as explained in more detail in the Code of Ethics section above. I am not compensated by a third-party for any recommendations that my clients use a third-party for any service.

Custody

All client portfolios are in maintained in their own accounts in their own name. As the investment advisor I am authorized by my clients through a limited power of attorney to trade for their accounts and in most cases to vote proxies for their accounts.

All clients receive monthly brokerage statements directly from the custodian in either hard copy or electronic form, as well as trading advices whenever a trade has been executed. Other than my management fees, which many clients authorize the custodian to pay me directly, clients control all withdrawals or transfers from their accounts.

As a general rule I limited my activities to being the investment advisor for a client. However, there are a few exceptional circumstances where I have agreed to act as a co-trustee for family members or life-long personal friends. As in all other cases, assets are maintained in trust name with an independent custodian, and all statements and trading advices are sent to the other co-trustee.

I do not have and never have had any pooled or commingled client assets, which would violate my policy of always maintaining client assets in client name with an independent custodian.

Investment Discretion

As explained in Section I above, I have investment discretion over virtually 100% of client assets under management. Clients execute a limited power of attorney satisfactory to the independent custodian authorizing my authority to trade on their behalf.

Voting Client Securities

In many cases clients authorize me to vote their proxies for mutual funds and other securities owned. I have never had a client request that I vote a proxy a certain way, but if I did receive such a request I would accommodate my client's wishes.

The vast majority of proxies involve the routine election of board of directors and similarly uncontroversial matters. Because my clients' cumulative ownership of most securities is inconsequential relative to the shares outstanding, these routine proxies are reviewed but usually not voted. Where matters might be consequential to my clients' interests, proxy materials are reviewed in more depth and voted appropriately to reflect my judgment of my clients' best interests.

Since my personal investments are aligned with my clients' investments (i.e., we might both own the same security, but I would never be "short" a stock that a client owns), there are no circumstances I can envision where a conflict of interest would arise between my interests and my clients in voting proxies.

Financial Information

I have never been subject to a bankruptcy petition. There are no financial issues pending that impair my ability to meet any contractual obligations to clients.

I always bill my clients in arrears, not in advance. A client may elect to terminate their relationship with me at any time without penalty, with the client obliged to pay only the fees accrued from the time of my last billing through the termination date.