

# Founders Capital Management, Inc.

## Part 2A of Form ADV

### The Brochure

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This brochure provides information about the qualifications and business practices of Founders Capital Management, Inc. (“FCM” or “Adviser”). If you have any questions about the contents of this brochure, please contact us at 713-877-1188. 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.

Additional information about FCM is also available on the SEC’s website at: [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

## Material Changes

FCM's most recent update to Part 2 of Form ADV was made in March 2014. FCM's business activities have not changed materially since the time of that update. In 2010 the SEC required significant changes to the content and format of Part 2 of Form ADV. This brochure, which reflects those changes, is materially different from brochures used by FCM in prior years.

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## Advisory Business

FCM primarily provides customized investment management services to individuals, high-net-worth individuals and associated trusts and estates, charitable organizations, pension and profit sharing plans, and corporations or other legal entities. FCM provides investment advice on a limited number of securities types, and generally invests client assets in domestic and international stocks, bonds, mutual funds, exchange traded funds ("ETFs"), warrants, certificates of deposit, and options.

FCM works with each client to determine the client's individual needs, including investment objectives, risk tolerance, and desired return parameters, and to establish an appropriate investment profile. Clients choose from growth, balanced, and conservative strategies, and can impose reasonable restrictions on FCM's management of their accounts.

FCM was founded in 1995 and is owned by Grant E. Buce and James L. Walter. As of March 9, 2015, FCM managed \$154,148,031 on a discretionary basis and \$11,288,981 on a non-discretionary basis.

## Fees and Compensation

FCM charges an annual investment management fee based on the following schedule:

<u>Assets under management</u>	<u>Annual Fee</u>
First \$1,000,000	1.25%
Next \$1,000,000	0.80%
Amounts in excess of \$2 Million	0.60%

Based upon certain factors (such as account size, expected future additions, level of trading, and account complexity), fees may be negotiable and vary from client to client. In addition, FCM has waived or negotiated lower fees for certain clients, such as charitable organizations or employees' family members.

FCM charges fees quarterly in arrears based on the account value at the end of the prior quarter, and clients authorize FCM to deduct fees automatically from their brokerage accounts. FCM is the successor advisor for some clients who are charged fees quarterly in advance based upon the account value at the beginning of the quarter.

If a client terminates the investment management agreement with FCM in the middle of a billing period FCM will invoice the client for an amount that is pro-rated based on the number of days that the account was managed. If a client who is billed in advance terminates in the middle of a billing period FCM will return an amount based upon the remaining number of days in the quarter after receiving written notification from the client of the termination.

In addition to FCM's investment management fees, clients bear trading costs and custodial fees. FCM may invest client's funds in mutual funds. To the extent that clients' accounts are invested in mutual funds, these funds pay a separate layer of management, trading, and administrative expenses. Since the mutual funds are generally available to the public on the same basis as they are purchased in FCM's clients' accounts, a client who chooses to research, select, monitor, and manage his own mutual fund investments can avoid paying the advisory fee to FCM for those assets.

The typical mutual fund management fee ranges from 0.20% of assets in the case of some bond funds to a high of 2.00% of assets in the case of some specialized stock funds.

All of FCM's discretionary account clients hold their mutual fund shares in brokerage accounts with Charles Schwab & Co., Inc. ("Schwab") or TD Ameritrade ("Ameritrade"). The brokerage firm may charge a transaction fee to buy or sell shares of such funds. In some cases, the mutual fund and the brokerage firm have agreed to a service fee arrangement in which case the client is not charged a transaction fee.

FCM's fees do not include any bank fees, margin interest, national securities exchange fees, custody fees, wire transfer fees or other costs or fees associated with securities transactions as required by law. Clients' funds awaiting investment may be placed in a money market fund; FCM's fees do not include any internal fees or expenses of any money market fund.

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

FCM does not charge any performance fees. Some investment advisers experience conflicts of interest in connection with the side-by-side management of accounts with different fee structures. However, these conflicts of interest are not applicable to FCM.

## **Types of Clients**

FCM primarily provides customized investment management services to individuals, high-net-worth individuals and associated trusts and estates, charitable organizations, pension and profit sharing plans, and businesses and other legal entities. FCM requires a minimum portfolio size of \$1 million, which can be comprised of multiple accounts. Based upon certain factors (such as account size, expected future additions, level of trading, and account complexity), minimum portfolio requirements may be negotiable and vary from client to client.

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

FCM's Investment Committee is comprised of Grant E. Buce, Scott F. Orr and James L. Walter. Messrs. Buce, Orr and Walter are responsible for account management. FCM uses research reports on economic conditions, industry groups and specific investments from brokerage and research firms. The Investment Committee works together to conduct fundamental analysis on all securities recommended for client accounts. This analysis varies depending on the security in question. For stocks and bonds the analysis generally includes a review of:

- The issuer's management;
- The amount and volatility of past profits or losses;
- The issuer's assets and liabilities, as well as any material changes from historical norms;
- Prospects for the issuer's industry, as well as the issuer's competitive position within that industry; and
- Any other factors considered relevant.

For mutual funds and ETFs the analysis generally includes a review of:

- The fund's management team;
- The fund's historical risk and return characteristics;
- The fund's exposure to sectors and individual issuers;
- The fund's fee structure; and
- Any other factors considered relevant.

The Investment Committee generally meets weekly to discuss existing and prospective investments. Investments are evaluated independently, as well as in the context of clients' existing holdings and sector exposures.

FCM primarily invests for relatively long time horizons, often for a year or more. However, market developments could cause FCM to sell securities more quickly.

Depending on a client's investment objectives, FCM might engage in short selling or option writing. The use of short selling and option writing poses additional risks that are discussed in detail with any clients who are considering the use of these investment vehicles.

All investing involves a risk of loss and any investment strategy offered by FCM could lose money over short or even long periods. Performance could be hurt by a number of different market risks including, but not limited to:

- Stock market risk, which is the chance that overall stock prices will decline. Stock markets tend to move in cycles, with periods of rising prices and periods of falling prices.
- Sector risk, which is the chance that significant problems will affect a particular sector, or that returns from that sector will trail returns from the overall stock market. Daily fluctuations in specific market sectors are often more extreme than fluctuations in the overall market.
- Interest rate risk, which is the chance that interest rates will rise, causing the prices of fixed income securities to fall since the price of most fixed income securities move in the opposite direction of the change in interest rates. If clients hold a fixed income security to maturity, the change in its price before maturity may have little impact on the performance; however, if the client has to sell the fixed income security before the maturity date, an increase in interest rates could result in a loss.
- Inflation risk, which results from the variation in the value of cash flows from a security due to inflation, as measured in terms of purchasing power. For example, if a client purchases a 5-year bond in which it can realize a coupon rate of 5%, but the rate of inflation is 6%, then the purchasing power of the cash flow has declined. For all but inflation linked bonds, adjustable bonds or floating rate bonds, clients are exposed to inflation risk because the interest rate the issuer promises to make is fixed for the life of the security. To the extent that interest rates reflect the expected inflation rate, floating rate bonds have a lower level of inflation risk.

## **Disciplinary Information**

FCM and its employees have not been involved in any legal or disciplinary events in the past 10 years that would be material to a client's evaluation of the company or its personnel.

## **Other Financial Industry Activities and Affiliations**

FCM and its employees do not have any relationships or arrangements with other financial services companies that pose material conflicts of interest.

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

FCM has adopted a written code of ethics that is applicable to all employees. Among other things, the code requires FCM and its employees to act in clients' best interests, abide by all applicable regulations, avoid even the appearance of insider trading, and pre-clear and report on many types of personal securities transactions. FCM's restrictions on personal securities trading apply to employees, as well as employees' family members living in the same household. A copy of FCM's code of ethics is available upon request.

FCM and its related persons are generally permitted to trade alongside client accounts as long as the orders are entered in a manner calculated to give the client the advantage. For example, in the purchase or sale of securities, client orders are entered and executed prior to those of FCM or a related person. In general, investment accounts of the Adviser and its related persons are of insufficient size to materially affect the securities market.

## **Brokerage Practices**

For ease of account administration, FCM generally recommends that clients arrange for their assets to be held with Schwab or Ameritrade; however clients are free to choose another broker/custodian. Schwab and Ameritrade generally charge a transaction fee to buy and sell securities. The main factors FCM considers in recommending Schwab or Ameritrade are substantially discounted commissions and FCM's ability to electronically download client account data from Schwab and Ameritrade each day. FCM has managed client assets held at Schwab and Ameritrade for many years and has found Schwab and Ameritrade to offer good services at competitive prices.

### Soft Dollar Benefits

FCM receives certain products and services from Schwab and Ameritrade for free or at discounted rates. These products and services include:

- The receipt of duplicate client confirmations, statements, and other account information;
- Direct advisory fee debiting capabilities;
- Access to an electronic network for order entry, including the simultaneous entry of trades on behalf of multiple client accounts;
- Morningstar, Inc. software that supports FCM's research processes for mutual funds and individual securities.

Morningstar, Inc. is not affiliated with FCM or Schwab. However, Morningstar, Inc. offers discounts on their annual subscriptions to investment advisers whose clients maintain custody of their assets at Schwab. FCM is unaware of any minimum requirements regarding the amount of commissions, trading, or assets in custody that are necessary to take advantage of these discounts. It is difficult to determine the exact economic benefit to FCM from these discounts related to Schwab because Morningstar, Inc. regularly offers discounts of various types in order to attract and maintain business. FCM estimates that the total economic benefit from discounts at Morningstar, Inc. is less than \$1,000 per year.

FCM does not believe that clients whose accounts are held by Schwab bear any additional costs in connection with FCM's receipt of the products and services. Furthermore, Schwab's provision of these products and services is not contingent upon FCM formally committing any specific amount of business to Schwab. However, FCM would not receive these products and services if client accounts were not held in custody and traded by Schwab. FCM's receipt of these products and services creates a conflict of interest in connection with FCM's recommendation of Schwab. Also, some of the products and services listed above benefit clients whose accounts are held by

other custodians, which could create a conflict of interest between the clients at Schwab, who are indirectly paying for the products and services, and the clients at other custodians who may benefit from the products and services.

#### The Selection of Trading Counterparties

FCM can typically trade accounts held at Schwab using other broker/dealers. However, Schwab charges clients trade-away fees that FCM believes outweigh any benefits from trading stocks, mutual funds, or ETFs with other brokers. The availability and pricing of bonds varies more widely, so prior to placing a bond trade FCM solicits bids from several dealers and then executes the trade with the dealer that offers sufficient liquidity and the most favorable pricing.

For clients who elect to have their accounts held by firms other than Schwab or Ameritrade, FCM's approach is generally to trade stocks, mutual funds, and ETFs with the chosen custodian, and to trade bonds with the dealer that offers sufficient liquidity and the most favorable pricing.

Some clients' accounts are relatively small, in which case the custodian may not allow FCM to trade through other firms. Other clients may specifically request that their accounts only be traded through a particular broker/dealer. FCM trades these accounts through the firm chosen by the client, which limits FCM's ability to seek best execution. Trading restrictions may result in materially higher trading costs and reduced returns.

#### Aggregated Trades

At times FCM may aggregate client trades in an effort to treat all clients fairly. Clients participating in a bunched order receive the same average price and incur trading costs that are the same as would be paid if they were trading individually. Employees may be included side-by-side in bunched client trades. In regard to bonds, where an order is partially filled, clients will have their orders fully filled on a randomized basis; FCM will seek to complete any unfilled client orders in the next bunched order of bonds. Employees are excluded from bunched trades whenever client orders are only partially filled.

#### Client Referrals

FCM does not compensate Schwab, Ameritrade or any other custodian or broker/dealer for referring client accounts.

### **Review of Accounts**

Accounts under FCM's management are monitored on a weekly basis by the Investment Committee. Reviews are made with regard to current financial market conditions, investment criteria, and each client's particular investment requirements. Reviews of client accounts will also be triggered if a client changes his or her investment objectives, or if the market, political, or economic environment changes materially.

FCM provides quarterly written reports to clients which show the present position of the portfolio and which summarize interest and dividends received for the quarter. At year end, the client is provided a written report of realized gains and losses. Clients also receive account statements directly from their chosen custodian, typically on a monthly basis and detail transaction activity and month end positions.

## **Client Referrals and Other Compensation**

FCM pays a portion of its advisory fees to another registered investment adviser in connection with that adviser's referral of a client to FCM. The referral fee is a percentage of the advisory fee earned by FCM and is negotiable based upon specific situations. The management fee paid by the client is not increased as a result of any referral fees paid to the solicitor. The referral in question came more than 20 years ago, and since that time no other referrals have been made, nor will any occur in the future, for which FCM shares a portion of its advisory fee.

Other than the previously described products and services that FCM receives from Schwab and Ameritrade, FCM does not receive any other economic benefits from non-clients in connection with the provision of investment advice to clients.

## **Custody**

All clients' accounts are held in custody by unaffiliated broker/dealers or banks, but FCM can access many clients' accounts through its ability to debit advisory fees. For this reason FCM is considered to have custody of client assets. Account custodians send statements directly to the account owners on at least a quarterly basis. Clients should carefully review these statements, and should compare these statements to any account information provided by FCM.

## **Investment Discretion**

FCM has investment discretion over all clients' accounts. Clients grant FCM trading discretion through the execution of a limited power of attorney included in FCM's portfolio management agreement.

Clients can place reasonable restrictions on FCM's investment discretion. For example, some clients have asked FCM not to buy securities issued by companies in certain industries, or not to sell certain securities in which the client has a particularly low tax basis.

## **Voting Client Securities**

In accordance with its fiduciary duty to clients and Rule 206(4)-6 of the Investment Advisers Act, FCM has adopted and implemented written policies and procedures governing the voting of client securities. All proxies that FCM receives will be treated in accordance with these policies and procedures.

FCM considers the reputation, experience, and competence of a company's management and board of directors when it evaluates a prospective investment. In general, FCM votes in favor of routine corporate matters, such as the re-approval of an auditor or a change of a legal entity's name. FCM also generally votes in favor of compensation practices and other measures that are in-line with industry norms, that allow companies to attract and retain key employees and directors, that reward long-term performance, and that align the interests of management and shareholders. FCM may supplement its evaluation of client proxies with guidance from an independent corporate governance consulting firm.

FCM has not identified any material conflicts of interest in connection with past proxy votes. Such a conflict could arise if, for example, a client was a senior executive with a publicly traded company and other clients held securities issued by that company. Absent specific client instructions, if FCM identifies a material conflict of interest it may retain an independent



corporate governance consulting firm and will follow the voting recommendation of the independent corporate governance consulting firm that it has retained.

A copy of FCM's proxy voting policies and procedures, as well as specific information about how FCM has voted in the past, is available upon written request. Upon written request, clients can also take responsibility for voting their own proxies, or can give FCM instructions about how to vote their respective shares.

## **Financial Information**

FCM has never filed for bankruptcy and is not aware of any financial condition that is expected to affect its ability to manage client accounts.