



## **FSI GROUP, LLC**

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**August 18, 2017**

Form ADV, Part 2A – Disclosure Brochure as required by the Investment Advisers Act of 1940 is a very important document between clients (you, your) and FSI Group, LLC (us, we, our).

***This Brochure provides information about the qualifications and business practices of FSI Group, LLC. If you have any questions about the contents of this Brochure, please contact us at 513-746-2200. 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.***

***Additional information about FSI Group, LLC is available at the SEC's website [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov) (click on the link, select "investment adviser firm" and type in our firm name). Results will provide you both Part 1 and 2 of our Form ADV.***

We are a registered investment adviser with the Securities and Exchange Commission. Our registration as an Investment Adviser does not imply any level of skill or training. The oral and written communications we provide to you, including this Brochure, is information you use to evaluate us (and other advisers) which are factors in your decision to hire us or to maintain your relationship with us.

## Item 2 – Material Changes

This document was developed in response to requirements adopted and imposed by the Securities and Exchange Commission (SEC) under the Investment Advisers Act of 1940 (IA Act) / 2010 amendments to SEC Form ADV.

This section of the Brochure summarizes material changes that have been incorporated in this document since our last brochure dated March 29, 2017. We note the following:

- Trapeza Capital Management, LLC and Trapeza Management Group, LLC have assigned the collateral management contracts for Trapeza CDOs I-XIII to an unaffiliated third party, thereby exiting the collateral management business and resulting in a material reduction to FSI assets under management as set forth in Item 4 below.

We may, at any time, update this Brochure and either send you a copy or offer to send you a copy (either by electronic means (email) or in hard copy form).

If you would like another copy of this Brochure, please download it from the SEC Investment Adviser Public Disclosure website located at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov) or request a copy by calling us at 513-746-2200.

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## Item 4 – Our Advisory Business

### THE FIRM

FSI Group, LLC (together with its subsidiaries referred to as FSI, the firm, we or us), was founded in 1995. The firm was originally organized as an Ohio corporation, registered as an investment adviser with the SEC in 1997, and reorganized as a Delaware limited liability company in 2008.

As of July 31, 2017, the firm was principally owned by Steven N. Stein and John M. Stein, who each hold their interests directly and through a holding company, FSI Group Holdings, Inc. In April, 2008, Stifel Financial Corp. (NYSE: SF) purchased a note which is convertible into a minority interest in FSI under certain circumstances.

### INVESTMENT SERVICES

FSI operates a multi-strategy investment platform focused primarily on opportunities in the financial services sector. We specialize in financing and investing in financial services companies, including banks and thrifts, insurance companies, asset management firms, real estate investment trusts, real estate operating companies, business development companies, commercial and consumer finance, leasing, brokerage and financial technology businesses and companies providing technology, infrastructure, information, support, and services to any of the foregoing, as well as companies or other business or pass-through entities whose activities are similar or attendant to those of companies which are engaged in the financial services sector. Our investments focus primarily on a long/short equity hedge fund strategy and a private equity strategy.

We provide investment management services primarily to private investment funds and institutional separate accounts. FSI offers equity investment strategies for both public and private securities. (Item 8 provides more information about our investment strategies).

We do not provide financial planning services, and we do not advise our clients in the selection of other investment advisers. Upon request, FSI will work with separately managed institutional accounts and registered investment company accounts to accommodate client-specific restrictions on FSI's equity investment strategies.

Our portfolio strategies may include investments in common stocks, preferred stocks, investment-grade and non-investment grade bonds (including private placements), U.S. Government and agency securities, convertible securities, real estate investments trusts, or other securities, of companies primarily in the U.S. financial services sector.

### WRAP FEE PROGRAMS:

We do not participate in wrap fee programs.

## **ASSETS UNDER MANAGEMENT:**

As of July 31, 2017, FSI managed \$184,505,865 of client assets on a discretionary basis.

## **Item 5 – Fees and Compensation**

### **INSTITUTIONAL SEPARATE ACCOUNTS**

We may provide investment advisory services to institutional separate accounts. Fees for institutional separate accounts that utilize our equity strategies are negotiable and generally are based upon a percentage of assets under management and performance. FSI reserves the right to negotiate all fees. Some clients may pay more or less than others depending on certain factors, including but not limited to, the type and size of the account. The fees that we charge for investment advisory services are specified in written agreements between the firm and our clients.

The fees we charge institutional separate accounts may vary by investment strategy or account; FSI typically receives a fixed fee / base compensation and is eligible to receive incentive compensation. The fees for institutional separate accounts are typically payable monthly or quarterly in arrears and may be calculated based on the value of the assets in the account at the end of each calendar month / quarter. Fees for partial periods may be pro-rated.

### **LIMITED PARTNERSHIPS / PRIVATE INVESTMENT FUNDS:**

Each limited partnership / private investment fund which we manage pays the firm a management fee and a performance-based advisory fee as described below. These fees are described in the fund's investment management or limited partnership agreement. (Item 6 provides more information about performance-based fees, and Item 10 provides more information about our private investment funds).

The fees paid by investors in our private investment funds are not negotiable; provided, however, that certain large or strategic investors, principals, affiliates, or relatives of such persons may purchase or may have purchased interests in FSLP, FSCP IV, and FSCP V which differ with respect to administrative fees and/or performance allocations or fees.

**Financial Stocks Limited Partnership.** Administrative Fee: FSLP pays a fee equal to 1.5% per annum of the limited partners' aggregate net asset value to FSI (its General Partner) on a quarterly basis, in advance.

Performance allocation: We may also collect a performance fee from FSLP. The performance allocation is computed and made separately with respect to each capital account in the limited partnership. At the end of each quarter following the first anniversary of a capital account, we will determine if the value of the capital account has

increased. If (1) the adjusted capital account of the limited partner interest plus any cash distributions with respect to such interest since the later of the date of purchase and the date of the “previous high peak” is greater than the previous high peak with respect to such limited partnership interest, thus reflecting net capital appreciation with respect to such limited partnership interest, and (2) the adjusted capital account of the limited partnership interest (before consideration of any performance allocation or payment of fees to FSI) has increased to at least the “threshold amount,” then an amount equal to 20% of the net capital appreciation during such period will be reallocated to FSI from that limited partnership interest’s capital account as a “performance allocation.” Accordingly, the performance allocation will be calculated and made on a per-limited partnership interest “peak to peak” basis if the limited partnership interest’s adjusted capital account has increased to at least the threshold amount since the previous high peak. The “threshold amount” means the previous high peak with respect to a limited partnership interest plus an amount equal to simple interest at 8% per annum (2% per quarter) from the date of the previous high peak.

FSLP primarily invests in public companies in the U.S. financial services sector.

**Financial Stocks Capital Partners V L.P. Management Fee:** FSCP V pays Finstocks Capital Management V, LLC (Finstocks V), its General Partner and subsidiary of FSI, a quarterly management fee in advance calculated at a rate of 0.50% (i.e., 2% per annum) of the aggregate capital commitments of all partners for the first four years after the initial closing, and thereafter at a rate of 0.375% (i.e., 1.5% per annum) of the aggregate capital commitments of all partners; provided, however, that the first management fee was paid in advance for the period following the first 12 months after the initial closing and was calculated at an annual rate of 2.0%.

**Performance Allocation:** Net profits and net losses of FSCP V are allocated to all partners in proportion to their respective capital commitments, except that 20% of the cumulative net profits allocable to the limited partners will be reallocated to the “Special Limited Partner” which is an affiliate of Finstocks V.

The purpose of FSCP V is to seek substantial capital appreciation primarily through investment in equity and equity-linked securities of financial services companies.

#### **OTHER FEES AND EXPENSES:**

In addition to management and advisory fees, investors in FSI’s hedge fund, private equity funds, Trapeza and FSI’s institutional separate account clients may indirectly (or in the case of institutional separate accounts utilizing our equity strategies, directly) bear additional expenses, including the following:

- Brokerage commissions;
- Transaction fees;
- Exchange fees;
- SEC fees;
- Custodial Fees;

- Odd-Lot differentials;
- Transfer taxes;
- Wire transfer and electronic fund processing fees;
- Commissions or mark-ups / mark-downs on security transaction;
- Among others that may be incurred.

(Item 12 provides more information on our brokerage practices.)

#### **ADDITIONAL COMPENSATION:**

The firm and our employees do not accept compensation, including sales charges or service fees, from any person for the sale of securities or other investment products.

### **Item 6 – Performance-Based Fees and Side-By-Side Management**

We may receive performance-based fees from our private investment funds (as described in Item 5 above) and institutional separate accounts. A performance-based fee is an advisory fee based on a percent of capital gains on or capital appreciation of assets in the fund/ institutional separate account. Performance-based fees paid to investment advisers may be significantly higher than the asset-based fees paid on traditional accounts.

#### **POTENTIAL CONFLICTS OF INTEREST:**

The receipt of performance-based fees from certain of our clients may create conflicts of interest. We can potentially receive higher fees from accounts with a performance-based compensation structure than from those accounts that pay asset-based fees only. Therefore, we may have an incentive to direct the best investment ideas to the account(s) that pay(s) a performance-based fee or allocate or sequence trades in favor of a particular account. To manage these potential conflicts:

- FSI has adopted a best execution policy and trading procedures.
- FSI has adopted trade allocation policies and procedures designed to ensure that all clients are treated fairly and to prevent this conflict from influencing the allocation of investment opportunities among clients.
- All accounts with substantially similar investment strategies will typically be allocated trades for any eligible securities pro-rata (subject to any account guidelines or limitations, available cash, liquidity considerations, and other factors).
- FSI establishes the monthly allocation percentages for its hedge fund and institutional separate accounts at the beginning of every month; any differences in allocation are noted and reviewed for appropriateness.

- Client portfolios are monitored by the portfolio managers and compliance department for consistency with client investment objectives and any applicable investment restrictions.

## Item 7 – Types of Clients

We generally provide investment advice to the following types of clients:

- Hedge funds and institutional separate accounts
- Private equity and other private investment funds
- Government agencies

Our long/ short hedge funds invest primarily in publicly traded securities of companies in the financial services sector. Our private equity funds make non-controlling investments in financial services companies. Investors in our funds are primarily institutions and high net worth individuals.

The minimum account size for institutional separate accounts is negotiable; we reserve the right to accept or reject any institutional separate account client in our sole discretion. (Item 5 provides more information about advisory fees for institutional separate accounts.)

## Item 8 – Methods of Analysis, Investment Strategies and Risk of Loss

### **FSI FOCUS: FINANCIAL SERVICES SECTOR**

FSI specializes in investing in financial services companies, including banks and thrifts, insurance companies, asset management firms, real estate investment trusts, real estate operating companies, business development companies, commercial and consumer finance, leasing, brokerage and financial technology businesses and companies providing technology, infrastructure, information, support, and services to any of the foregoing, as well as companies or other business or pass-through entities whose activities are similar or attendant to those of companies which are engaged in the financial services sector.

### **METHODS OF ANALYSIS:**

FSI's analytical methods may vary in accordance with types of clients and client objectives. Methods of analysis and investment strategies are more fully set forth in private offering memoranda prepared in connection with each private investment fund managed by FSI, or in separately negotiated institutional account agreements.

In general, we utilize fundamental value analysis and other research methods to identify mispriced securities and securities with the greatest potential for price appreciation. The firm develops and maintains target values for acceptable investments and seeks to buy



available securities at the greatest risk-adjusted discounts to value and sell them as their values approach targets or substantially better alternative investments are identified.

In analyzing securities, FSI strives to:

- anticipate and stay abreast of changes in the financial services industry and the general business and economic environment;
- identify specific companies that will prosper as these operating environments change;
- identify and sponsor strong management teams committed to creating shareholder value; and
- take advantage of special situation opportunities in the industry.

FSI typically examines numerous factors relating to a potential investment, which may include its financial condition, earnings quality, distribution of assets, projected earnings, prospects for dividends, prospects for appreciation of stock price, capitalization, management capability and practices, price/earnings ratios of comparable public companies, diversification of the client's portfolio and the possibilities for corporate restructuring, such as prospects that an issuer could become a target of a tender offer or acquisition candidate. We also consider macro-economic factors, such as current general economic and political outlook and interest and inflation rates.

Notwithstanding FSI's analytical approach, our clients and investors in our funds will bear the risk of significant loss.

### **INVESTMENT STRATEGIES:**

Investment strategies for each affiliated fund and institutional separate account may vary, and are more fully set forth in private offering memoranda prepared in connection with each fund managed by FSI, or in separately negotiated institutional account agreements.

For FSI's equity hedge fund and related separate account strategy, we seek to achieve superior returns by investing in publicly traded equity securities issued by financial services companies. Debts securities may also be acquired, and short selling techniques and leverage may be employed. Although some investments may produce dividends, interest, and other income, current income is not an objective.

FSI seeks to identify companies that have strong management committed to shareholder value, quality franchises, aggressive (but rational) growth plans, and defensible market positioning. Accordingly:

- We invest opportunistically in long/short equity of companies in the financial services sector;
- We may also invest in debt, hybrid, and other securities issued by or related to financial services companies;

- We utilize a combination of top-down macroeconomic analysis with fundamental bottom-up research to identify attractive opportunities in the financial services sector; and
- Shorting is done opportunistically to create alpha.

FSI employs a combination of economic/sector analysis and bottom-up fundamental company research to make investments across all market capitalizations and all financial services sub-sectors. Risk is typically evaluated on an individual name, sector and portfolio basis with respect to liquidity, leverage, and portfolio diversification, including sub-sector diversification. We may also utilize third party risk reports.

For our private equity strategy, the firm seeks capital appreciation primarily through investment in equity or equity-linked securities of financial services companies. Such securities will typically be non-marketable or illiquid at the time of acquisition by an FSI private equity fund.

### **RISK OF LOSS:**

All investments in securities include a risk of loss of principal (invested amount) and any profits that have not been realized (the securities were not sold to “lock in” the profit). Stock and bond markets fluctuate substantially over time. In addition, as recent global and domestic economic events have indicated, performance of any investment is not guaranteed. As a result, there is a risk of loss of the assets we manage that may be out of our control. We cannot guarantee any level of performance or guarantee against loss in connection with our investment advisory services. Investing in securities involves the risk of loss. Our clients and investors in FSI funds must bear this risk.

The specific investment risks affecting our funds are typically disclosed in a private placement memorandum and/or investment management agreement delivered to investors prior to subscription. Below is a summary of certain risks that may impact our client’s investments, or an investment in one of our funds. For a more complete discussion of risks, please consult the private placement memorandum, investment management agreement, or other disclosure document provided in connection with your investment.

### **Financial Services Sector**

FSI concentrates our fund investments in financial services companies and does not diversify by sector. These investments are subject to all the risks of the market in general, and the financial services sector more specifically. As such, the value of your investment or your interest in an FSI fund could shift rapidly due to fluctuations in the financial services sector; such fluctuations could vary dramatically from fluctuations in the overall market.

### **The Banking and Thrift Industry**

The results of operations of banks and thrifts are significantly affected by general economic conditions and the related monetary and fiscal policies of the federal government, particularly as they relate to the level of interest rates. The profitability of many banks and

thrifts is largely dependent upon net interest income, which is the difference between interest income on interest-earning assets, such as loans, mortgage-backed securities and investment securities, and interest expense on interest-bearing liabilities, such as deposits. For an institution with interest-earning assets maturing or re-pricing faster than its interest-bearing liabilities in a given period, an increase in interest rates could have a positive impact on net interest income. A decrease in interest rates, however, could have an adverse effect on such an institution. Changes in the level of interest rates may also affect the amount of loans originated (including refinancings) and loans sold by banks and thrifts. An increase in interest rates may result in lower levels of originations and loan sales, and thus, in the amount of loan and commitment fees and gains on sales of loans. In addition, changes in interest rates may result in disintermediation, the flow of funds away from savings institutions into direct investments, such as corporate securities and other investment vehicles, which, because of the absence of federal insurance premiums and reserve requirements, may pay higher rates of return than savings institutions. Higher interest rates may also have an adverse impact on the market value of banks' and thrifts' interest-earning assets. Furthermore, regulations applicable to banking and thrift institutions will limit our ability to seek to protect our clients' private equity investments in banks or thrifts through the controls typically imposed by venture capital and private equity investors on their portfolio companies.

Other factors affecting the banking and thrift industry generally:

- the extensive regulation, supervision and examination of banks and thrifts and their holding companies by federal and state law and regulatory agencies, which regulatory framework is subject to changes that may affect materially the operations and results of banks, thrifts and their holding companies; in addition, limitations on control of banks and thrifts will limit our clients' ability to affect management of bank and thrift issuers in which they invest;
- regulatory and charter restrictions applicable to changes in control of certain banks and thrifts, which may limit the potential for acquisitions and the stock appreciation that may arise from such transactions;
- the risks associated with banks' and thrifts' real estate, commercial and consumer loan assets, which may be affected by local and national economic conditions;
- changes in regulation, which may have unforeseen results and in addition to, or instead of, creating investment opportunities, may also create additional risk;
- increasing internationalization of financial and credit markets, which may increase the possible adverse effects on U.S. financial institutions of foreign economic disturbances; and

- increasing competition in the banking and thrift industry, including competition from non-banks such as electronic data processing firms, which may erode the market share and decrease the margins of particular banks and thrifts.

## The Insurance Industry

Certain factors affecting the insurance industry generally:

- the extensive regulation, supervision and examination of insurance companies and their holding companies both by federal and state legislation and by state insurance commissions, including limitations on control of insurance companies that will limit our clients' ability to affect management of insurance companies in which they invest;
- the sensitivity of the insurance industry to catastrophic events beyond its control, such as major terrorism and acts of nature, including earthquakes, floods and storms, which can increase claims as well as decrease the availability and increase the cost of reinsurance;
- regulatory and charter restrictions applicable to changes in control of certain insurance companies, which may limit the potential for acquisitions and the stock appreciation that may arise from such transactions;
- the historically cyclical nature of the insurance industry, which results in significant fluctuations in operating results due to competition, frequency of occurrence or severity of catastrophic events, levels of capacity, general economic conditions and other economic factors, all of which lead to significant fluctuation in premium rates, policy terms and volume of business;
- the performance of the investment portfolios of insurance companies, which are impacted by changes in interest rates and general economic conditions; and
- the highly competitive nature of the insurance industry, resulting in part from continual entry of new competitors and capital into the industry.

## Leverage

Certain FSI strategies may use leverage. Leverage may increase a client's overall return on capital, but may increase the volatility of returns and the risk of loss.

## **Short Sales**

Certain FSI strategies may engage in short sales of securities. Short sales can, in certain circumstances, substantially increase the impact of adverse price movement on client accounts/ investments. A short sale involves the risk of a theoretically unlimited increase in the market price of the particular investment sold short, which could result in an inability to cover the short position and a theoretically unlimited loss.

## **Portfolio Turnover**

The turnover rate in FSI's publicly-traded equity investment portfolios may be extremely high and a high portfolio turnover rate would cause larger brokerage commission to be borne by those clients.

## **Mid and Small-Cap Companies**

Certain FSI funds may investment in mid- and small-cap companies. Those investments may involve greater risk than is customarily associated with larger, more established companies. Smaller companies often have limited markets or financial resources, and they may be dependent upon extremely small management teams. Securities of smaller companies may have limited marketability and may be subject to more abrupt or erratic movements in price than securities of larger companies or market averages in general.

## **Credit Ratings**

Certain FSI funds may invest in securities that have low ratings, are unrated, or are subordinate to other securities / obligations of the issuer. Additionally, our private equity funds may invest in securities that demonstrate high price volatility and risk of principal.

## **Limited Diversification**

FSI private equity funds may invest their assets in relatively few portfolio companies. The limited diversification may provide less protection against market price changes than would a more diversified investment portfolio.

## **Lack of Liquidity**

FSI private equity funds typically invest in securities that are subject to restrictions on resale because they are acquired in private placement transactions. The private equity funds will not be able to sell these securities publicly unless their sale is registered under the Securities Act and applicable state securities laws or unless an exemption from such registration requirements is available. We may also be able to sell such securities in private transactions, but because the securities would remain subject to restrictions on their further transfer, the price at which the securities could be privately sold may be negatively affected.

Our private equity funds may also acquire a substantial amount of publicly-traded securities of an issuer for which there is insufficient market liquidity to permit an orderly and efficient sale of such securities.

### **Reliance on Existing Portfolio Company Management**

Our funds do not have an active role in the day-to-day management of their portfolio companies. The success or failure of the companies in which we invest will depend to a significant extent on their existing management.

In addition, FSI funds individually and in the aggregate seek to hold less than 10% of the voting securities issued by any regulated financial institution.

### **Non-U.S. Investments**

Investing in securities or other financial instruments traded outside the United States ("Non-U.S. Investments") involves considerations and possible risks not typically involved in securities or other financial instruments that trade in the United States ("U.S. Investments"), including instability of some non-U.S. governments, the possibility of expropriation, limitations on the use or removal of funds or other assets, changes in governmental administration or economic or monetary policy (in the United States or abroad) or changed circumstances in dealings between nations. The application of foreign tax laws (e.g., the imposition of withholding taxes on dividend, interest or other payments) or confiscatory taxation may also affect Non-U.S. Investments. Higher expenses may result from Non-U.S. Investment than would from investments in securities because of the costs that must be incurred in connection with conversions between various currencies and foreign brokerage commissions that may be higher than U.S. Investments. Non-U.S. commodity and securities markets also may be less liquid, more volatile and less subject to governmental supervision than in the United States. Non-U.S. Investments could be affected by other factors not present in the United States, including lack of uniform accounting, auditing and financial reporting standards and potential difficulties in enforcing contractual obligations.

### **Reliance on FSI Portfolio Managers**

The success of our affiliated funds depends on the continued services of our portfolio managers, Steven N. Stein and John M. Stein. The death, disability or departure of Steven N. Stein or John M. Stein would adversely affect our business and our affiliated funds. Neither Steven N. Stein nor John M. Stein is precluded from engaging in other business activities, including the management of other funds and other entities that they control, and such other activities could impact their services on behalf of our clients.

### **Financial Market Crises**

The year 2007 witnessed the beginning of a liquidity and credit crisis which had a domino effect on financial markets and participants worldwide. As the crisis continued during 2008

and 2009, several prominent financial market participants failed or nearly failed to perform their contractual obligations when due, which contributed further to a period of great uncertainty in the financial markets and resulted in governmental and regulatory authority interventions in certain markets and in the operations of certain failing institutions, severe credit and liquidity contractions, early terminations of transactions and related arrangements, and suspended and failed payments and deliveries. Moreover, the global financial and economic turmoil led certain solvent prime brokers and other lenders to be unwilling or less willing to finance new investments or to only offer financing for investments on less favorable terms than had been prevailing in the recent past. Additionally, both single-strategy and multi-strategy participants in markets that would not ordinarily be expected to be correlated to the mortgage market were forced to liquidate, often at deeply discounted prices, in order to shore up cash reserves. The U.S. Federal Reserve Bank, the European Central Bank, and other countries' central banks injected significant liquidity into markets, and otherwise made significant funds, guarantees, and other accommodations available to certain financial institutions to counter elevated levels of market stress, volatility and impaired liquidity. The events of the past several years continue to have an effect on financial markets, including with respect to liquidity and the availability of credit. It is uncertain how long and to what extent effects of the current liquidity, credit, and economic conditions will continue or what other effects they will have on financial markets and the operations of FSI and our funds and other accounts. In addition, there can be no assurance of an effective coordinated response by central banks or other market participants in the future.

## **Item 9 – Disciplinary Information**

We do not have any legal, financial or other “disciplinary” item to report to you. We are obligated to disclose any disciplinary event that would be material to you when evaluating us to initiate a client / adviser relationship, or to continue a client /adviser relationship with us.

This statement applies to our firm, and every employee.

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

### **WE ONLY PROVIDE INVESTMENT ADVICE:**

FSI is not actively engaged in any business other than giving investment advice and we do not sell products or services other than investment advice to our clients.

### **SOLICITOR FEES:**

We may enter into an agreement with a broker / dealer or registered investment adviser in which our firm would pay a set percentage of our management fee and/ or performance

based fees to the referring broker / dealer. These arrangements, often referred to as solicitor agreements, are more specifically discussed in Item 14.

## **Item 11 – Code of Ethics and Code of Conduct**

### **OUR CODE AND PERSONAL TRADING:**

As required by regulation, we have adopted a Code of Ethics and Code of Conduct (the Code) that governs and seeks to mitigate a number of potential conflicts of interest we have when providing our advisory services to you. This Code is designed to ensure we meet our fiduciary obligation to you, our client (or prospective client); to establish and maintain a culture of compliance within our firm; and to ensure that FSI and our employees adhere to the highest ethical standards.

Our Code is designed to detect and prevent violations of securities laws, including the obligations we owe to you. In recognition of the fiduciary obligations we owe to our clients, the Code contains provisions designed to prevent improper personal trading, prevent the use of insider information in connection with the purchase and sale of securities, and identify and mitigate potential conflicts of interest.

Our Code is comprehensive, is distributed to each employee at the time of hire, and annually thereafter (or more frequently if there are changes). We also supplement the Code with annual training and on-going monitoring of employee / Access Person activity.

Our Code includes the following:

- Requirements related to the confidentiality of our clients / client information;
- Prohibitions on:
  - Insider trading (if we are in possession of material, non-public information);
  - The acceptance of gifts and business entertainment that exceed our policy standards;
  - Engaging in outside business activities without prior approval;
  - Trading securities that are listed on an applicable Restricted List;
  - Seeking to influence adviser selection through political contributions (pay-to-play)
- Reporting of gifts and business entertainment;
- Pre-clearance of all employee personal securities transactions (including participation in any IPO or private placement), unless the security or transaction is specifically exempt from preclearance under the Code;



- Pre-clearance / reporting of political contributions;
- Reporting (on an on-going and quarterly basis) of all personal securities holdings and transactions;
- Prior approval before engaging in any outside business activity;
- On an annual basis, we require all employees to re-certify to our Code, identify any account in which they have a beneficial ownership (they “own” the account or have “control” over the account), and virtually all securities (except open-end mutual funds) they own at that time;
- Reporting (on an on-going basis and from time to time) of any personal or business relationships which may create a conflict of interest for the firm or our clients.

Our Code does not prohibit personal trading by employees (or our firm). In order to prevent insider trading and mitigate potential conflicts of interest, FSI has adopted and implemented a Restricted List Policy and Procedures. To the extent FSI or our Access Persons receive Material Non-Public Information, or contractually agree to any trading restrictions, the securities of such company will be added to FSI’s Restricted List, and the firm and our employees will be restricted from trading such securities. If a publicly traded security is placed on FSI’s Restricted List (or additional watch list maintained for Access Persons engaged on specific institutional client accounts), FSI and/or the relevant Access Persons will not be permitted to trade this security for themselves or our clients, for so long as we have MNPI, or we are otherwise contractually obligated to restrict trading. It is possible that we may hold a restricted security in FSLP, or another client account, or that an Access Person will hold the security in his or her personal securities accounts. When this occurs, FSI or the Access Person will not be permitted to trade the security in violation of FSI’s restriction. This may present a conflict of interest when we are restricted from trading a security for a client because we have received MNPI in connection with a separate engagement. FSI seeks to limit the potential conflicts of interest by attempting to limit our exposure to MNPI.

FSI provides investment advisory services to various clients. Our affiliates, including employees, may act as the investment adviser or investment manager for others, may manage funds or capital for others, may have, make and maintain investments in their own name or through other entities, and may serve as officers, directors, consultants, advisors, stockholders, partners, or members of one or more investment funds, partnerships, securities firms or advisory firms. FSI, our affiliates, and related persons, may have conflicts of interest in allocating their time and activities among FSI’s affiliated funds and institutional separately managed accounts and in allocating investments among our clients. To mitigate the potential conflicts of interest that may be involved in managing multiple accounts or other investment-related activities, the Code requires us to adhere to the highest ethical standards; FSI has also adopted best execution / trading policies and procedures. (Item 12 –Brokerage Practices).

FSI, our affiliated companies, and some of our employees, have invested in our hedge fund and private equity funds. We monitor employee investments in these clients via our Code and do not believe such investments represent a conflict of interest. From time to time our employees / Access Persons may invest in the same securities that we purchase for our clients, including related securities such as options and derivatives, personally or through private funds or entities that they own or control. In addition, Access Persons may hold an interest or position in certain securities that we may also recommend for our client accounts. Such positions may present a conflict of interest between our personnel and our clients. We address this conflict of outside business activities, or other investment activities, through the pre-clearance procedures described above (both in trading and engaging in outside business activities) and otherwise contained in our Code, which procedures are designed to ensure that no client is disadvantaged by trades made by the firm for its own account or our Access Persons or outside business activities, and pursuant to which we may deny any pre-clearance request.

You may request a complete copy of our Code by contacting us at FSI Group, LLC, 441 Vine Street, Suite 1300, Cincinnati, Ohio 45202 Attn: Compliance Department, 513-746-2200. We will provide a copy of our Code to any client or prospective client upon request.

#### **AFFILIATED FUNDS' INVESTMENTS:**

The private equity funds we manage have been generally invested serially, *i.e.*, capital from each partnership was fully invested before capital from subsequently formed partnerships was invested. However, our Portfolio Managers may invest in the same security for different clients. When this occurs, the investment shall be allocated in a manner that is fair and equitable to all participating clients, in order to mitigate any actual or potential conflicts of interest.

#### **PARTICIPATION IN CLIENT TRANSACTIONS:**

Neither the firm, nor our employees, participates in client transactions. However, our affiliated funds may participate in a transaction with institutional separate account clients. Allocation and aggregation of any such transactions would be made in accordance with our policies and procedures (described in Item 12 – Brokerage Practices).

#### **TRADE ERRORS:**

If we make a trade error on behalf of a client account, we will use our best efforts to break or otherwise correct the trade so that our client does not suffer a loss and is not harmed.

## **Item 12 – Brokerage Practices**

### **GENERAL CONSIDERATIONS – SELECTING BROKERS FOR CLIENT TRANSACTIONS AND COMMISSION CHARGES:**

Seeking best execution is an important aspect of our trading platform. FSI has adopted policies and procedures designed to achieve best execution. Our Senior Trader and

portfolio managers select the brokers we use to execute trades and determine the reasonableness of their compensation based on the range and quality of the broker's services (including execution capability), trading expertise, accuracy of execution, commission rates, research provided, reputation and integrity, fairness in resolving disputes, financial responsibility, and responsiveness. All brokers on FSI's list of approved brokers are regularly reviewed / evaluated (at least annually) by the Senior Trader and our analysts.

We use an electronic trade execution management system to ensure proper trade management, including fair order allocation and best execution. We have controls in place for monitoring execution of our clients' portfolio transactions, including regularly reviewing trades for best execution.

While FSI selects brokers based on their perceived ability to obtain best execution, we need not solicit competitive bids and do not have an obligation to seek the lowest available commission cost for every trade. In selecting brokers and negotiating commission rates, FSI will take into account the financial stability and reputation of brokerage firms, the size and type of the transaction, the difficulty of execution, the ability to handle a block order and the research, brokerage or other services provided by such brokers.

When securities are purchased or sold in principal transactions in the over-the-counter market, the transactions take place directly with a principal market maker, without the use of a broker, except in those circumstances where in the opinion of FSI at least as favorable prices and execution will be achieved in an agency transaction using a broker.

FSI may utilize brokers providing research and brokerage services or providing research prepared by third party vendors even though lower commissions may be charged by brokers not offering such services. We limit the use of "soft dollars" to obtain research and brokerage services which constitute research and brokerage within the meaning of Section 28(e) of the Securities Exchange Act of 1934. These research services we receive, which are within Section 28(e) currently include, research reports (including market research); certain financial newsletters and trade journals; software providing analysis of securities portfolios; corporate governance research and rating services; attendance at certain seminars and conferences; discussions with research analysts; meetings with corporate executives; consultants' advice on portfolio strategy; data services (including services providing market data, company financial data and economic data); advice from brokers on order execution; certain proxy services, analysis of portfolio risk, and information regarding political initiatives which may impact the financial services sector, or specific securities in which we may invest our clients' funds. Brokerage services within Section 28(e) may also include, but are not limited to, services related to the execution, clearing and settlement of securities transactions and functions incidental thereto (i.e., connectivity services between an adviser and a broker and other relevant parties such as custodians); trading software operated by a broker to route orders; software that provides trade analytics and trading strategies; software used to transmit orders; clearance and settlement in connection with a trade; electronic communication of allocation instructions; routing settlement instructions; post trade matching of trade information; and services

required by the SEC or a self-regulatory organization such as comparison services, electronic confirms or trade affirmations. Research received from brokers or dealers is supplemental to our own research efforts.

In some instances, FSI may receive a product or service that may be used only partially for functions within Section 28(e). In such instances, we would make a good faith effort to determine the relative proportion of the product or service used to assist us in carrying out our investment decision-making responsibilities and the relative proportion used for administrative or other purposes outside Section 28(e). The proportion of the product or service attributable to carrying out our investment decision-making responsibilities will be paid through brokerage commissions generated by client transactions and the proportion attributable to administrative or other purposes outside Section 28(e) will be paid for from our own resources.

Although FSI will make a good faith determination that the amount of commissions paid is reasonable in light of the products or services provided by a broker, commission rates are generally negotiable and thus, selecting brokers on the basis of considerations that are not limited to the applicable commission rates may result in higher transaction costs than would otherwise be obtainable.

#### **RESEARCH AND OTHER SOFT DOLLAR BENEFITS:**

FSI does not enter into agreements with any brokers regarding the placement of securities transactions because of the research services they provide. We do, however, have an internal procedure for allocating transactions in a manner consistent with our execution policy to brokers which we have identified as providing superior execution and research, research-related products or services of a particular benefit to our clients.

Receipt of research, products or services from brokers who execute client trades or other third party providers involves conflicts of interest. When we use client brokerage commissions to obtain research, products, or services, we receive a benefit because the firm does not have to produce or pay for the research, products or services. Consequently, we may have an incentive to select a broker based on our desire to receive research, products or services, rather than a desire to obtain most favorable execution, which is in the clients' best interest.

The client commissions used to acquire brokerage and research, products or services are known as "soft dollars." We seek to comply with Section 28(e) of the Investment Advisers Act of 1934, which provides a safe harbor that allows investment advisers to pay more than the lowest commission for brokerage and research services if it determines in good faith that: (1) the brokerage or research services fall within the definitions set forth in Section 28(e); (2) the brokerage or research services fall provide lawful and appropriate assistance in the investment decision-making process; and (3) the commission paid is reasonable in relation to the brokerage and research services provided.

The brokerage and research services that we obtain with soft dollars are not necessarily utilized for the specific client account that generated the soft dollars. Some clients may

benefit from the research obtained from soft dollars despite the fact that they have not generated the trade commissions used to pay for such services. We do not attempt to allocate the relative costs or benefits of brokerage and research services among all client accounts because we believe that, in the aggregate, the brokerage and research services we receive benefit our clients and assist FSI in fulfilling our overall duties to our clients.

Accordingly, broker / dealers selected by FSI may be paid commissions for effecting portfolio transactions for client accounts in excess of the amounts other brokers would have charged for effecting similar transactions if we determine in good faith that such amounts were reasonable in relation to the value of the brokerage / research services provided by those brokers, viewed either in terms of a particular transaction or our overall duty to discretionary accounts.

### **BROKERAGE NOT SELECTED BASED UPON CLIENT REFERRALS:**

If otherwise consistent with seeking best execution, and provided that FSI is not selecting the broker in recognition of the opportunity to participate in capital introduction events or for client referrals, we may place transactions with a broker that:

- provides FSI with the opportunity to participate in capital introduction events sponsored by the broker; or
- refers clients to FSI or investors for our affiliated funds.

Because we have an obligation to obtain best execution for our clients, FSI has a potential conflict of interest with respect to clients / fund investors that are referred by registered representatives of brokerage firms, as such referrals may create an incentive for us to steer brokerage to those brokers. However, we select brokers using factors unrelated to client referrals, as discussed above.

To further mitigate this potential conflict of interest, we may refrain from using the referring broker on trades for that particular client and the clients (or investors in our funds) are provided and asked to execute a disclosure form that provides information regarding any referral fees we pay to such broker.

### **PRIME BROKER:**

Wells Fargo Prime Services, LLC serves as the prime broker for Financial Stocks Limited Partnership. FSI may at any time obtain additional or different prime brokers. Institutional separate account clients may also specify a prime broker for use by FSI in managing its account. Each prime broker has certain administrative responsibilities, including custody of the account assets, the issuance of account statements and information with respect to securities transactions effected through other brokers. A client's prime broker may also be allocated a portion of its securities transactions. The selection of a prime broker may cause FSI to pay higher than the lowest available commissions. FSI designates the prime brokers for its hedge funds; prime brokers for institutional separate accounts are typically designated by the client.

## **TRADE ALLOCATION AND AGGREGATION PROCEDURES:**

As a general policy, we seek to allocate the purchase and sale of securities among potentially eligible clients in a manner that is fair and equitable to all clients. FSI evaluates the appropriateness of the purchase or sale of particular securities for each client, taking into account all relevant factors, including (i) restrictions placed on the account by the client, by agreements or by applicable law; (ii) the size of the account; and (iii) the nature and liquidity of the security to be allocated. Although these factors may lead us to allocate securities to clients in varying amounts, we generally seek to allocate securities to clients using substantially similar investment strategies on a pro rata basis (based on account size).

With respect to liquid securities (such as listed equities and certain fixed income products), FSI may, but shall not be obligated to, aggregate or “batch” orders for the purchase or sale of those securities for all participating client accounts to the extent consistent with best execution and the terms of our agreements with the participating clients. Such combined or “batched” trades may be used to facilitate best execution, including negotiating more favorable prices, obtaining more timely or equitable execution or reducing overall commission charges. In such case, we will place an aggregated order with the broker on behalf of all participating accounts in order to ensure fairness for all accounts. However, in some cases, this policy may cause you to receive a less favorable price than if the order had not been aggregated.

FSI allocates securities among accounts managed with substantially similar investment criteria which are participating in an aggregated or “batch” order on a pro rata basis (based on account size, generally as set forth and determined at the beginning of each month) in a manner that is fair and equitable based upon the overall investment strategy for, restrictions on, and other investment parameters for such account. The portfolio managers determine the appropriate allocation among all participating accounts prior to executing an aggregated order. If an aggregated order is only partially filled as of the end of the trading day, then, to the extent practicable, the quantity of securities allocated to each participating account will generally be allocated on a pro rata basis using available capital, based on the size of the original allocation to such account, subject to adjustments for rounding, odd lots and certain other allocation considerations, such as: (i) the extent to which the order specifies a priority allocation to one or more accounts, (ii) the extent to which an allocation would be too small to justify processing or custodial charges associated with the transaction, (iii) the extent to which an account may be over-invested or under-invested with respect to a particular security, industry or sector in comparison to other accounts in the order, (iv) the availability of, or need for, cash, and/or (v) for bond trades, street convention and good delivery may dictate the minimum size and par amounts. If an order must be allocated in a different manner, we seek to provide all clients fair and equitable treatment. The price at which a security was purchased or sold will be determined by calculating the average price of all executions for such security taken on all orders entered through the same broker on any given day, with transaction costs shared pro rata based on participation.

We may participate in Initial Public Offerings (each an “IPO”). We allocate such IPOs among those clients permitted to participate in IPOs where we believe that, based on the account’s investment restrictions, risk profile, asset composition and cash levels, the IPO is an appropriate investment for such client. If the order for securities issued in an IPO is only partially filled, FSI allocates securities to the participating accounts on a pro rata basis, in accordance with the intended allocation, as determined by our portfolio managers based upon the factors we consider for any allocation. Exceptions may occur if the allocation would result in a client receiving only a de minimus amount of securities.

**NO DIRECTED BROKERAGE:**

We do not intend to participate in any directed brokerage arrangements.

**NO PRINCIPAL TRADING:**

We do not engage in, nor do we intend to engage in, principal transactions (buying securities from or selling securities to our clients). However, we would effect any principal transactions in accordance with Section 206(3) of the Investment Advisers Act of 1940, and provide written disclosure to the client for approval before completing any such transaction.

In the case of a principal transaction, we would seek execution consistent with our fiduciary obligations. If similar transactions are considered on behalf of one client that would be appropriate for other clients, at or about the same time, any such transactions would be allocated in a manner believed to be fair and equitable.

**NO CROSS TRANSACTIONS / AGENCY CROSS TRANSACTIONS:**

We do not engage in agency cross transactions and do not anticipate doing so.

## **Item 13 – Review of Accounts**

**PRIVATE INVESTMENT FUNDS:**

Developments in our affiliated fund portfolios / private investment funds are monitored by our analytical team led by the firm’s portfolio managers on a daily basis. Hedge fund investors receive monthly and quarterly reports and private equity investors receive quarterly reports. The performance of each company in each portfolio is reviewed not less than quarterly.

Investors in our funds receive update letters and account value statements not less than quarterly, and audited financial statements and tax data annually.

## **INSTITUTIONAL SEPARATE ACCOUNTS:**

Daily surveillance is maintained for these portfolios by the portfolio managers and analyst team. Account information and statements are provided directly to the client by the custodian and/or prime broker retained by the client.

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

We currently maintain arrangements pursuant to which registered broker-dealers may be compensated for referring clients or investors in FSI's private funds. This arrangement and any such arrangements that may be established from time to time are set forth in written agreements; they may include an initial placement fee and trailer fees which are based on management fees or performance fees that we earn.

Neither FSI nor its related persons is party to any arrangement where it is paid cash or receives some economic benefit (including equipment or non-research services) from a non-client in connection with giving advice to clients.

### **Item 15 – Custody**

For each of FSI's respective funds, we receive statements at least quarterly from the prime broker, bank, or other qualified custodian which holds and maintains the fund's assets. Likewise, the prime broker, bank, or other qualified custodian which holds and maintains client assets for each institutional separate or registered fund account sends statements at least quarterly to those clients.

### **Item 16 – Investment Discretion**

FSI accepts discretionary authority to manage the assets in client accounts. Unless otherwise set forth in written agreement or as you otherwise instruct, we generally have the authority to determine directly or through our subsidiaries: (i) the securities to be purchased and sold (subject to any written investment objectives, policies, consents, and restrictions set forth in the offering memoranda, investment management agreement, or other related agreements); (ii) the amount of securities to be purchased or sold for your account; (iii) the broker to be used to effect securities transactions; and (iv) the commission rates to be paid in connection with your securities transactions. In all cases, we exercise discretion in a manner consistent with your stated investment objectives and we observe the investment limitations and restrictions that are outlined in your investment management agreement.



## **Item 17 – Voting Client Securities (i.e., Proxy Voting)**

FSI has adopted proxy voting policies and procedures that are designed to ensure that we vote proxies with respect to client securities in the best interests of our clients. These procedures require that we identify and address any conflicts of interest between the firm and our clients with respect to such proxies. If a material conflict of interest exists, we will determine whether voting in accordance with the guidelines set forth in the procedures is in the best interests of the client, or take some other appropriate action. Certain institutional separate account clients have provided us with their own proxy voting guidelines.

We generally vote in favor of routine corporate housekeeping proposals, including election of directors (where no corporate governance issues are implicated). For all other proposals, we determine whether a proposal is in the best interests of our clients, in doing so we may consider all relevant factors, including: (i) whether the proposal was recommended by management and our opinion of management; (ii) whether the proposal acts to entrench existing management; and (iii) whether the proposal fairly compensates management for past and future performance.

You may request a copy of our Proxy Voting Policy and Procedures and obtain information about how we voted your proxies by contacting FSI Compliance at (513) 746-2200.

## **Item 18 – Financial Information**

In certain circumstances, registered investment advisers are required to provide you with financial information or disclosures about their financial condition in this Item. FSI has no financial commitment that impairs its ability to meet contractual and fiduciary commitments to clients and has never been the subject of a bankruptcy proceeding.