

**Item 1.       Cover Page**

**Brochure of  
Hawthorn Capital Management, LLC**

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Sebastopol, CA 95472**

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**March 2019**

This brochure provides information about the qualifications and business practices of Hawthorn Capital Management, LLC (“Hawthorn”). If you have any questions about the contents of this brochure, please contact us at (443) 994-1963. 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 Hawthorn also is available on the SEC’s website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

**Item 2.       Material Changes**

The following material change has been made to this Brochure since its last annual update:

AUM reported in Item 4 increased to \$123 million

**Item 3. Table of Contents**

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

Hawthorn is a Maryland limited liability company that has been in business since 2000, and is currently located in Sebastopol, California. It serves as the investment adviser to separately managed accounts. Hawthorn's manager, controlling owner and portfolio manager is Brian Leshner. As of March 1, 2019, Hawthorn had total discretionary assets under management of approximately \$123 million. Hawthorn only manages assets on a discretionary basis.

Hawthorn invests principally in debt and equity securities of companies that Hawthorn believes to be undervalued. These may include U.S. and non-U.S. corporate debt securities, U.S. municipal debt securities, U.S. government and agency debt securities, short-term debt obligations of foreign governments, foreign money-market instruments, common and preferred stock (including convertible preferred stock), partnership interests, business trust shares, interests in REITs, rights and warrants, and depositary receipts. Hawthorn also invests in mutual funds that invest in such securities. Notwithstanding the foregoing, Hawthorn may enter into any type of investment transaction that it deems appropriate to the extent permitted under the terms of the client's account agreement.

Hawthorn selects sub-advisers to manage portions of certain clients' assets. The sub-advisers, like Hawthorn, employ strategies of investing in undervalued securities, but the sub-advisers are typically focused on equity instruments, while Hawthorn focuses on both debt and equity securities.

To tailor its services to the individual needs of each client account, Hawthorn:

- Manages each such account based on the client's financial situation and investment objectives and in accordance with any restrictions that the client imposes on managing the account. Hawthorn obtains this information from a client in a questionnaire or otherwise.
- At least annually, contacts each client (either in person or by telephone) to ask about any changes in the client's financial situation or investment objectives and whether the client desires to impose or modify any restrictions on managing the account.
- Notifies each client quarterly in writing to contact Hawthorn if there are any changes in the client's financial situation or investment objectives, or if the client desires to impose or modify any restrictions on managing the account.
- Makes itself reasonably available to clients for consultation.

Hawthorn provides an annual financial plan to its investment management clients, for no additional fee.

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

Hawthorn's compensation for investment management services is negotiable and varies, but typically, it charges an annual fee of from 0.2% to 1.0% of assets under management, which is

payable in quarterly installments at the beginning of each calendar quarter based on the net market value of each client's account on the date the fee accrues and becomes payable.

Hawthorn typically deducts management fees directly from client accounts but may bill a client for such amounts on request.

Hawthorn may select sub-advisers to manage portions of certain clients' assets. Hawthorn may waive its investment management fees with respect to client assets that are managed by such sub-advisers, so that those clients pay only the sub-advisers' fees. If Hawthorn does not waive its fees in such cases, clients will pay a double level of fees, to both Hawthorn and the sub-adviser.

Client accounts that invest in mutual funds also pay, indirectly, investment advisory fees to the managers of those funds.

Each account is responsible for its own costs and expenses, including custodial fees and trading costs and expenses (such as brokerage commissions, expenses related to short sales, and clearing and settlement charges). Hawthorn bears its own operating, general, administrative and overhead costs and expenses, other than the expenses described above. All or part of these costs and expenses may be paid, however, by securities brokerage firms that execute clients' securities trades, as discussed in Item 12 below.

Hawthorn believes that its investment management fees are competitive with fees charged by other investment advisers for comparable services. Comparable services may be available, however, from other sources for lower fees.

Except as may be otherwise negotiated in particular cases, a client may terminate the account by giving 30 days' prior written notice. Expenses and the pro rata portion of the management fee through the date of termination are charged to the account. All prepaid but unearned advisory fees are refunded on termination of a client's account.

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

Hawthorn does not charge performance-based compensation.

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

Hawthorn provides investment advice to high-net-worth individuals, institutions, trusts, endowments and pension plans. Hawthorn generally requires a minimum of \$10,000,000 to open an account, but may waive this minimum.

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

##### Investment Strategy

Hawthorn's investment strategy is to invest in debt and equity securities of companies that Hawthorn believes to be undervalued, and in mutual funds that invest in such securities. The proportion of client assets invested in these asset classes will vary from time to time based on

Hawthorn's assessment of general market and economic conditions. Hawthorn may invest in and shift frequently among asset classes and market sectors. The fixed-income securities in which Hawthorn invests for its clients include U.S. corporate debt securities, U.S. municipal debt securities, non-U.S. corporate debt securities, U.S. government and agency debt securities, short-term debt obligations of foreign governments, and foreign money-market instruments. Hawthorn may engage sub-advisers to manage portions of certain clients' assets. The sub-advisers also employ strategies of investing in undervalued securities, and focus mainly on equity securities. The equity securities in which Hawthorn or the sub-advisers invest include common and preferred stock (including convertible preferred stock), partnership interests, business trust shares, interests in REITs, rights and warrants to subscribe for the purchase of equity securities, and depositary receipts.

Hawthorn's determination as to whether a company's securities are undervalued is based on Hawthorn's assessment of the value of the company and the priority of the claim of a particular security. Hawthorn's valuations of companies are based on its ongoing research and analysis of investment opportunities in the trading of securities that are, or appear likely to be, in financial reorganization, bankruptcy, receivership or other distressed conditions. Hawthorn analyzes the value of a company in one or more ways: (1) as an ongoing entity; (2) as a partial or complete liquidation; and (3) as an entity seeking to reorganize under the protection of the bankruptcy courts.

The priority of a particular claim is extremely important when a company seeks bankruptcy protection, because of a legal theory generally known as the "priority doctrine." The priority doctrine holds that the highest order, or senior, claim will generally be paid in full before any funds are available for payment of lower order, or junior, claims. Because of the priority doctrine, Hawthorn generally attempts to purchase securities with higher order claims, such as secured debt, senior debt or senior subordinated debt.

Most of the equity securities in which Hawthorn invests are now or were previously traded on the New York Stock Exchange or the American Stock Exchange, or are now or were quoted as NASDAQ National Market System securities. Many of the equity securities in which Hawthorn invests trade in the over the counter market. Some of the debt securities in which Hawthorn invests are now or were previously traded on the New York Bond Exchange or the American Bond Exchange, although most trade in the over the counter market. Although Hawthorn invests primarily in securities of United States issuers, it occasionally invests in securities of foreign issuers.

Hawthorn engages in ongoing research in an attempt to improve its ability to select equity and debt securities of companies meeting its investment objectives, and to identify the most opportune time to open or close investment positions in such securities.

The investment strategies summarized above represent Hawthorn's current intentions, are general in nature and are not exhaustive. Except as specified in a client's investment management agreement with Hawthorn, there are no limits on the types of securities in which Hawthorn may take positions on behalf of its clients, the types of positions that it may take, the concentration of its investments or the amount of leverage that it may use. Hawthorn may use any trading or investment techniques permitted by a client's account agreement, whether or not

contemplated by the investment strategies described above. There are limitations in describing any investment strategy due to its complexity, confidentiality and indefinite nature. Depending on conditions and trends in securities markets and the economy generally, Hawthorn may pursue any objectives or use any techniques permitted by a client's account agreement that it considers appropriate and in the client's interest.

### Risk Factors

Investing in securities involves risk of loss that clients should be prepared to bear. Below are some of the risks that investors should consider before investing in any account that Hawthorn manages. Any such risks could materially and adversely affect investment performance or the value of any account or any security held in the account, and could cause investors to lose substantial amounts of money. Below is only a brief summary of some of the risks that a client may encounter. A potential client should discuss with Hawthorn's representatives any questions it has before opening an account.

- Client accounts may not achieve their investment objectives. Hawthorn's investment strategy may not be successful and clients may lose some or all of their investment.
- Hawthorn determines the value of securities held in client accounts, whether or not an active public market exists for such instruments. Debt securities can be particularly hard to value. If Hawthorn's valuation is inaccurate, it might receive more compensation than that to which it is entitled.
- Investor sentiment on the market, an industry or an individual stock, fixed income or other security is not predictable and can adversely affect an account's investments.
- Hawthorn may not be able to obtain complete or accurate information about an investment and may misinterpret the information that it does receive. Hawthorn also may receive material, non-public information about an issuer that prevents it from trading securities of that issuer for a client when the client could make a profit or avoid losses.
- Hawthorn may engage in hedging, which may reduce profits, increase expenses and cause losses. Price movement in a hedging instrument and the security hedged do not always correlate, resulting in losses on both the hedged security and the hedging instrument. Hawthorn is not obligated to hedge a client's portfolio positions, and it frequently may not do so.
- An account may have higher portfolio turnover and transaction costs than a similar account managed by another investment adviser. These costs reduce investments and potential profit or increase loss.
- Hawthorn may sell securities short for clients, resulting in a theoretically unlimited risk of loss if the prices of the securities sold short increase.
- Hawthorn may borrow on margin and trade derivatives, which increase volatility and risk of loss.

- Hawthorn may sell covered and uncovered options on securities. The sale of uncovered options could result in unlimited losses.
- Counterparties such as brokers, dealers, custodians and administrators with which Hawthorn does business on behalf of clients may default on their obligations. For example, a client may lose its assets on deposit with a broker if the broker, its clearing broker or an exchange clearing house becomes bankrupt.
- Hawthorn may cause clients to invest in securities of non-U.S., private and government issuers. The risks of these investments include political risks; economic conditions of the country in which the issuer is located; limitations on foreign investment in any such country; currency exchange risks; withholding taxes; limited information about the issuer; limited liquidity; and limited regulatory oversight.
- Changes in economic conditions can adversely affect investment performance. At times, economic conditions in the U.S. and elsewhere have deteriorated significantly, resulting in volatile securities markets and large investment losses. Government actions responding to these conditions could lead to inflation and other negative consequences to investors.
- Hawthorn may acquire for a client a large position in an issuer's securities but the client nevertheless is unlikely to have any control over the issuer's management. In addition, if Hawthorn's clients hold a large position in an issuer's securities, that could depress the market for those securities.
- Hawthorn may acquire for a client restricted securities that are subject to long holding periods or that are not traded in public markets. These securities are difficult or impossible to sell at prices comparable to the market prices of similar publicly-traded securities and may never become publicly traded.
- An account's investments may not be diversified. Therefore, a loss in any one position, industry or sector in which the fund has invested may cause significant losses.
- The client, and not Hawthorn, is responsible for any trade errors that Hawthorn makes, even when the error hurts the client.
- Hawthorn and its affiliates and agents generally are not responsible to any client for losses incurred in an account unless the conduct resulting in such loss breached Hawthorn's fiduciary duty to the client.
- If the assets that Hawthorn manages grow too large, it may adversely affect performance, because it is more difficult for Hawthorn to find attractive investments as the amount of assets that it must invest increases.
- No client has been represented by separate counsel. The attorneys who represent Hawthorn or its manager do not represent clients. Clients must hire their own counsel for legal advice and representation.



- Hawthorn or any government agency may freeze assets that any of them believes a client holds in violation of anti-money laundering laws or rules or on behalf of a suspected terrorist, and may transfer such assets to a government agency. Hawthorn will not be liable for losses related to actions it takes in an effort to comply with anti-money laundering regulations.
- Federal, state and international governments may increase regulation of investment advisers and derivative securities, which may increase the time and resources that Hawthorn must devote to regulatory compliance, to the detriment of its investment activities.
- Hawthorn's activities could cause adverse tax consequences to clients, including liability for interest and penalties.
- Hawthorn's activities may cause an account that is subject to the Employee Retirement Income Security Act of 1974 to engage in a prohibited transaction under that Act.
- Hawthorn and its affiliates may spend time on activities that compete with a client without accountability to that client, including investing for other clients and their own accounts. If Hawthorn receives better compensation and other benefits from managing some client accounts than others, it has incentive to allocate more time to the more profitable activities. These factors could influence Hawthorn not to make investments on a client's behalf even if such investments would benefit the client.
- Hawthorn may provide certain clients more frequent or detailed reports or special compensation arrangements that it does not provide to other clients.

The above is only a brief summary of some of the important risks that a client may encounter.

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

Hawthorn has no reportable disciplinary information.

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

Hawthorn has no reportable other financial industry activities or affiliations.

#### **Item 11. Code of Ethics, Participation or Interest In Client Transactions and Personal Trading**

Hawthorn has adopted a Code of Ethics in compliance with Rule 204A-1 under the Investment Advisers Act of 1940, that establishes standards of conduct for Hawthorn's supervised persons. The Code of Ethics includes general requirements that Hawthorn's supervised persons comply with their fiduciary obligations to clients and applicable securities laws, and specific requirements relating to, among other things, personal trading, insider trading, conflicts of interest and confidentiality of client information. It requires supervised persons to comply with the personal trading restrictions described below and periodically to report their personal securities transactions and holdings to Hawthorn's Compliance Officer, and requires the

Compliance Officer to review those reports. It also requires supervised persons to report any violations of the Code of Ethics promptly to the Compliance Officer. Each supervised person of Hawthorn receives a copy of the Code of Ethics and any amendments to it and must acknowledge in writing having received those materials. Annually, each supervised person must certify that he or she complied with the Code of Ethics during the preceding year. Clients and prospective clients may obtain a copy of Hawthorn's Code of Ethics by contacting Brian Leshner.

Under Hawthorn's Code of Ethics, Hawthorn and its manager, members and employees may personally invest in securities of the same classes as Hawthorn purchases for clients and may own securities of issuers whose securities that Hawthorn subsequently purchases for clients. This practice creates a conflict of interest in that any of such persons can use his or her knowledge about actual or proposed securities transactions and recommendations for a client account to profit personally by the market effect of such transactions and recommendations. To address this conflict, except as described in Item 12 regarding aggregating securities transactions, if Hawthorn purchases or sells a security for clients and any of Hawthorn and its manager, members and employees on the same day, either the clients and Hawthorn and its manager, members and employees pay or receive the same price, or the clients receive the more favorable price. Hawthorn and its manager, members and employees may also buy or sell specific securities for their own accounts based on personal investment considerations aside from company or industry fundamentals, which Hawthorn does not believe appropriate to buy or sell for clients.

Because Hawthorn manages more than one account, there may be conflicts of interest over its time devoted to managing any one account and allocating investment opportunities among all accounts that it manages. For example, Hawthorn selects investments for each client based solely on investment considerations for that client. Different clients may have differing investment strategies and expected levels of trading. Hawthorn may buy or sell a security for one type of client but not for another, or may buy (or sell) a security for one type of client while simultaneously selling (or buying) the same security for another type of client. Hawthorn attempts to resolve all such conflicts in a manner that is generally fair to all of its clients. Hawthorn may give advice to, and take action on behalf of, any of its clients that differs from the advice that it gives or the timing or nature of action that it takes on behalf of any other client so long as it is Hawthorn's policy, to the extent practicable, to allocate investment opportunities to its clients fairly and equitably over time. Hawthorn is not obligated to acquire for any account any security that Hawthorn or its manager, members or employees may acquire for its or their own accounts or for any other client, if in Hawthorn's absolute discretion, it is not practical or desirable to acquire a position in such security for that account.

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

Unless otherwise instructed by a client, Hawthorn has complete discretion in selecting the broker that it uses for client transactions and the commission rates that clients pay such brokers. In selecting a broker for any transaction or series of transactions, Hawthorn allocates to brokers for execution at such prices, and at such commission rates (which may be in excess of the prices or commission rates that might have been charged for execution on other markets or by other brokers) that Hawthorn believes in good faith to be appropriate. Hawthorn may consider a number of factors, including, for example:

- net price, clearance, settlement and reputation;
- financial strength and stability;
- efficiency of execution and error resolution;
- block trading and block positioning capabilities;
- willingness to execute related or unrelated difficult transactions in the future;
- special execution capabilities;
- order of call

In addition to execution, clearance and settlement, brokers may offer Hawthorn products and services that assist it in managing and administering clients' accounts, such as research, pricing and market data, and recordkeeping and client reporting services.

Hawthorn may pay to a broker commissions and mark-ups that exceed those that another broker might charge for effecting the same transaction because of the value of the brokerage services that such broker provides. Hawthorn determines in good faith that such compensation is reasonable in relation to the value of such brokerage services, in terms of either the specific transaction or Hawthorn's overall fiduciary duty to its clients. An account may, however, pay higher commissions and mark-ups than are otherwise available or may pay more commissions or mark-ups based on account trading activity.

The products and services available from brokers create a conflict of interest for Hawthorn in allocating client brokerage business among firms that provide such products and services, and those that do not. In evaluating whether to recommend that clients custody their assets at a particular broker, or whether to use a particular broker to execute a client transaction, Hawthorn may take into account the availability of the foregoing products and services and other arrangements, rather than considering only the nature, cost or quality of custody services or transaction-specific execution services provided by the broker. In some cases, the commissions charged by a particular broker for a particular transaction or set of transactions may be greater than the amounts another broker who did not provide brokerage or research services or products might charge. In some cases, a client's transaction may be executed by a broker in recognition of services or products that are not used in managing that client's account. Hawthorn may not only consider that client's particular transaction or transactions, and not only the value of brokerage and research services and products to a particular client, but also the value of those services in Hawthorn's performance of its overall investment responsibilities to all of its clients. The conflict of interest for Hawthorn in selecting brokers is particularly strong to the extent that brokers provide products and services that Hawthorn would otherwise be required to pay for itself.

Currently, unless otherwise directed by a client, Hawthorn recommends that most of its clients maintain their investment accounts managed by Hawthorn at Charles Schwab & Co. ("Schwab"). Schwab is the custodian of the assets in those accounts. Schwab does not charge separately for custody services but is compensated by account holders through commissions and other transaction-related or asset-based fees for securities trades that are executed through Schwab or that settle into Schwab accounts. Hawthorn executes the majority of its trades through Schwab. Schwab provides Hawthorn with research, pricing and recordkeeping services as described above, which are also available to retail investors. Although many firms provide similar services to

investment advisers in exchange for brokerage, custody and clearance fees and other charges, Hawthorn would have to pay those these services if it did not receive them from Schwab. Although client accounts benefit from these services, Hawthorn does as well, particularly to the extent that it would otherwise be required to pay for them itself. Hawthorn is not required a particular number of trades to Schwab or to continue to maintain accounts with Schwab, but it has an incentive to do so based on Schwab's prior and continued services.

Hawthorn addresses these conflicts of interest by annually evaluating the trade execution services that it receives from the brokers that it uses to execute trades for clients. Such evaluation includes comparing those services to the services available from other brokers. Hawthorn considers, among other things, alternative market makers and market centers, the quality of execution services, the value of adding or removing brokers, and the appropriate level of commission rates.

Hawthorn does not use direct commission dollars generated by its clients' accounts to pay for research or other goods and services. Although Hawthorn does not engage in traditional soft dollar practices tied to levels of business it generates for brokers, Hawthorn nevertheless uses as a guide the safe harbor provided by Section 28(e) of the Securities Exchange Act of 1934 in considering which products and services to accept from brokers. Section 28(e) provides a "safe harbor" for an investment manager who uses commissions or transaction fees paid by its client accounts ("soft dollars") to obtain brokerage and research services that provide lawful and appropriate assistance to the manager in discharging its investment decision-making responsibilities, as long as the manager determines that the commissions paid are reasonable in relation to the value of the brokerage and research products and services provided by the broker.

Hawthorn may aggregate securities sale and purchase orders for a client with similar orders being made contemporaneously for other accounts that Hawthorn manages or with accounts of its affiliates. In such event, Hawthorn may charge or credit a client the average transaction price of all securities purchased or sold in such transactions. As a result, however, the price may be less favorable to the client than it would be if Hawthorn were not executing similar transactions concurrently for other accounts. Hawthorn may also cause a client to buy or sell securities directly from or to another client, if such a cross-transaction is in the interests of both clients.

If a client directs Hawthorn to use a specific broker, Hawthorn has not negotiated the terms and conditions (including, among others, commission rates) relating to the services provided by such broker. Hawthorn is not responsible for obtaining from any such broker the best prices or particular commission rates. A client that directs Hawthorn to use a specific broker may not be able to participate in aggregate securities transactions and may trade after such aggregate transactions and receive less favorable pricing and execution. The client may pay higher commissions and mark-ups than it would pay if Hawthorn had discretion to select broker-dealers other than those that the client chooses.

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

Brian Leshner, Hawthorn's Manager, reviews all accounts weekly. Those reviews take into account such matters as asset allocation, cash management, the prospects of individual securities, changes in issuer earnings, industry outlook, market outlook and price levels. Each account

receives a quarterly letter stating performance for the quarter and an annual letter discussing annual performance and investment outlook.

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

Hawthorn does not compensate any party for client referrals and does not receive any economic benefit from any non-client for providing investment advisory services to clients.

#### **Item 15. Custody**

The custodian of each client account sends account statements at least quarterly to the client. Each client should carefully review those statements and compare them with the statements that such client receives directly from Hawthorn, if any.

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

Hawthorn has discretionary authority to manage investment accounts on behalf of clients pursuant to a limited power of attorney in each client's account agreement. Such discretion is limited by the requirement that clients advise Hawthorn of:

- the investment objectives of the account;
- any changes or modifications to those objectives; and
- any specific investment restrictions relating to the account.

A client must promptly notify Hawthorn in writing if the client considers any investments recommended or made for the account to violate such objectives or restrictions. A client may at any time direct Hawthorn to sell any securities or take such other lawful actions as the client may specify to cause the account to comply with the client's investment objectives. In addition, a client may notify Hawthorn at any time not to invest any funds in the client's account in specific securities or specific categories of securities.

#### **Item 17. Voting Client Securities**

Hawthorn decides whether to vote proxies on behalf of each account over which Hawthorn has proxy voting authority after considering whether the proposal will have a material effect on the account's investment strategy. This analysis frequently leads Hawthorn to not vote proxies. In determining whether a proposal serves an account's best interests, Hawthorn considers a number of factors, including:

- the proposal's economic effect on shareholder value;
- the threat that the proposal poses to existing rights of shareholders;
- the dilution of existing shares that would result from the proposal;
- the effect of the proposal on management or director accountability to shareholders; and
- if the proposal is a shareholder initiative, whether it wastes time and resources of the company or reflects the grievance of one individual.

Hawthorn abstains from voting proxies when Hawthorn believes that it is appropriate to do so.

If a material conflict of interest over proxy voting arises between Hawthorn and a client, Hawthorn will vote all proxies in accordance with the policy described above. If Hawthorn determines that this policy does not adequately address the conflict of interest, Hawthorn will notify the client of the conflict and request that the client consent to Hawthorn's intended response to the proxy solicitation. If the client consents to Hawthorn's intended response or fails to respond to the notice within a reasonable time specified in the notice, Hawthorn will vote the proxy as described in the notice. If the client objects in writing to Hawthorn's intended response, Hawthorn will vote the proxy as the client directs.

A client can obtain a copy of Hawthorn's proxy voting policy and a record of votes cast by Hawthorn on behalf of that client by contacting Brian Leshner.

**Item 18. Financial Information**

Hawthorn is not required to report financial information.

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

Not applicable.

## **Privacy Policy**

Hawthorn:

- collects non-public personal information about its clients from the following sources:
  - information received from clients on applications or other forms, and
  - information about clients' transactions with Hawthorn, its affiliates or others;
- does not disclose any non-public personal information about its clients or former clients to anyone, except as permitted by law;
- restricts access to non-public personal information about its clients to its employees who need to know that information to provide services to clients; and
- maintains physical, electronic and procedural safeguards that comply with federal standards to guard clients' personal information.