

**Part 2A of Form ADV: *Firm Brochure***

**Chelsea Management Company**

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This brochure provides information about the qualifications and business practices of Chelsea Management Company. If you have any questions about the contents of this brochure, please contact us at 213-362-9200 or [Tom.Techentin@chelseamanagement.com](mailto:Tom.Techentin@chelseamanagement.com). The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission.

Additional information about Chelsea Management Company also is available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). You can search this site by a unique identifying number, known as a CRD number. Our firm's CRD number is 110399.

**Item 2    Material Changes**

There have been no recent material changes to report.

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#### **Item 4     Advisory Business**

Chelsea Counsel Company is a SEC-registered investment adviser with its principal place of business located in CA. Chelsea Management Company began conducting business in 1971.

Listed below are the firm's principal shareholders (i.e., those individuals and/or entities controlling 25% or more of this company).

- Frederick John Ruopp, Chairman and CEO

Chelsea Management Company offers the following advisory services to our clients:

##### **PORTFOLIO MANAGEMENT**

Our firm provides continuous advice to a client regarding the investment of client funds based on the individual needs of the client. Through personal discussions in which goals and objectives based on a client's particular circumstances are established, we develop a client's personal investment policy and create and manage a portfolio based on that policy. During our data-gathering process, we determine the client's individual objectives, time horizons, risk tolerance, and liquidity needs. As appropriate, we also review and discuss a client's prior investment history, as well as family composition and background.

We manage these advisory accounts on a discretionary or non-discretionary basis. Account supervision is guided by the client's stated objectives (i.e., maximum capital appreciation, growth, income, or growth and income), as well as tax considerations.

Clients may impose reasonable restrictions on investing in certain securities, types of securities, or industry sectors.

Our investment recommendations are not limited to any specific product or service offered by a broker-dealer or insurance company and will generally include advice regarding the following securities:

- Exchange-listed securities
- Securities traded over-the-counter
- Warrants
- Corporate debt securities (other than commercial paper)
- Commercial paper
- Certificates of deposit
- Municipal securities
- Mutual fund shares
- United States governmental securities
- Options contracts on securities

Because some types of investments involve certain additional degrees of risk, they will only be implemented/recommended when consistent with the client's stated investment objectives, tolerance for risk, liquidity and suitability.

##### **MODEL PORTFOLIO MANAGEMENT**

Our firm provides portfolio management services to clients using model asset allocation portfolios. Each model portfolio is designed to meet a particular investment goal. The investments portfolios offered focus on fixed income (taxable and tax exempt), Equity, Balanced (capital portioned between fixed and equity) and cash management.

## EQUITY - BALANCED MANAGEMENT

The equity investment philosophy of Chelsea Management Company firm is to build portfolios using large capitalization high quality issues with the prospect of above average growth and price/earnings multiples at or below the general market, typically referred to as value investing. Our objective is to achieve consistent total rates of return which reflect the needs of the clients, and a dedication to preservation and sustained growth of capital. Portfolios are structured with industry leaders having good historical records, above-average consistency of earnings and dividends along with intended rates of return. Occasionally a smaller company will be recognized as presenting a superior opportunity and included.

Identifying and forecasting change within sectors of the economy and with specific industry groups while establishing suitable price/earnings ratios before the market adjusts is central to our management style.

## FIXED INCOME MANAGEMENT

Preservation of capital and the compounding of positive returns are the foundation of fixed income management. Experience has demonstrated over many periods that strategies which employ substantial maturity risk are successful only briefly. The negative returns produced as interest rates and volatility increase then tend to overwhelm the positive results achieved earlier. Interest rate forecasting is an important element as is commitment made to the strongest grade credit ratings.

At Chelsea Management Company, it is our belief that optimal results are obtained by correctly forecasting the direction of interest rates and staying with high quality securities. Yield curve and quality spread analysis along with management of duration to moderate maturity risk are also important contributors to positive performance.

We have a long history managing tax – exempt municipal bonds. Individuals and insurance companies are the primary clients. These portfolios can be solely constructed in a single state, or to maximize the after-tax effect, they may encompass all fifty states plus Puerto Rico for the purpose of diversification.

We manage these advisory accounts on a discretionary or non-discretionary basis. Account supervision is guided by the client's stated objectives (i.e., maximum capital appreciation, growth, income, or growth and income), as well as tax considerations.

Through personal discussions with the client in which the client's goals and objectives are established, we determine if the model portfolio is suitable to the client's circumstances. Once we determine the suitability of the portfolio, the portfolio is managed based on the portfolio's goal, rather than on each client's individual needs. Clients, nevertheless, have the opportunity to place reasonable restrictions on the types of investments to be held in their account. Clients retain individual ownership of all securities.

Our investment recommendations are not limited to any specific product or service offered by a broker dealer or insurance company and will generally include advice regarding the following securities:

- Exchange-listed securities
- Securities traded over-the-counter
- Foreign issuers
- Warrants
- Corporate debt securities (other than commercial paper)
- Commercial paper
- Certificates of deposit
- Municipal securities

- Mutual fund shares
- United States governmental securities
- Interests in partnerships

Because some types of investments involve certain additional degrees of risk, they will only be implemented/recommended when consistent with the client's stated investment objectives, tolerance for risk, liquidity and suitability.

To ensure that our initial determination of an appropriate portfolio remains suitable and that the account continues to be managed in a manner consistent with the client's financial circumstances, we will:

1. send quarterly written reminders to each client requesting any updated information regarding changes in the client's financial situation and investment objectives;
2. at least annually, contact each participating client to determine whether there have been any changes in the client's financial situation or investment objectives, and whether the client wishes to impose investment restrictions or modify existing restrictions;
3. be reasonably available to consult with the client; and
4. maintain client suitability information in each client's file.

#### **ENVESTNET'S MANAGED ACCOUNT SOLUTIONS PROGRAM**

Through the Envestnet Program, Chelsea's model portfolios are offered to Envestnet clients. Envestnet offers the Chelsea Equity, Balanced and Fixed Income portfolios through their platform.

#### **AMOUNT OF MANAGED ASSETS**

As of 3/31/2012, Chelsea is actively managing \$920,574,353 of clients' assets on a discretionary and non-discretionary basis.

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

##### **INVESTMENT MANAGEMENT FEES**

Our annual fees for Services are based upon a percentage of assets under management.

##### **Equity/Balanced Accounts**

\$0-	\$ 1,000,000	1&1/2% Per Annum
\$1,000,000 -	\$ 3,000,000	1% Per Annum
\$3,000,000 -	\$ 5,000,000	3/4 of 1% Per Annum
\$5,000,000 -	\$10,000,000*	1/2 of 1% Per Annum

##### **Fixed Income Accounts**

\$0	- \$ 1,000,000	1/2 of 1% Per Annum
\$1,000,000 -	\$ 5,000,000	3/8 of 1% Per Annum
\$5,000,000 -	\$10,000,000*	1/4 of 1% Per Annum

\*Fees for accounts in excess of this amount will be negotiated in the light of all relevant account factors.

We also occasionally engage in a closely held security evaluation for a flat fee, which is negotiated and payable upon completion of the evaluation.

A minimum of \$500,000 of assets under management is required for this service. This account size may be negotiable under certain circumstances. Chelsea Management Company may group certain related client accounts for the purposes of achieving the minimum account size and determining the annualized fee.

**Limited Negotiability of Advisory Fees:** Although Chelsea Management Company has established the aforementioned fee schedule(s), we retain the discretion to negotiate alternative fees on a client-by-client basis. Client facts, circumstances and needs are considered in determining the fee schedule. These include the complexity of the client, assets to be placed under management, anticipated future additional assets; related accounts; portfolio style, account composition, reports, among other factors. The specific annual fee schedule is identified in the contract between the adviser and each client.

We may group certain related client accounts for the purposes of achieving the minimum account size requirements and determining the annualized fee.

Discounts, not generally available to our advisory clients, may be offered to family members and friends of associated persons of our firm.

## **ENVESTNET'S MANAGED ACCOUNT SOLUTIONS PROGRAM**

Chelsea's annual fee for services it provides for the Envestnet Program ranges from 0.20% to .25% of the total client assets invested in the Program

Envestnet clients will receive a separate disclosure document (Form ADV Part 2) prepared by Envestnet describing the company and the specific fees charged within the Program, the minimum account requirements, billing arrangements and service termination provisions. Clients are encouraged to review this disclosure document regarding the particular characteristics of the fees charged within the Program.

## **GENERAL INFORMATION**

**Termination of the Advisory Relationship:** A client agreement may be canceled at any time, by either party, for any reason upon receipt of 30 days written notice. As disclosed above, certain fees are paid in advance of services provided. Upon termination of any account, any prepaid, unearned fees will be promptly refunded. In calculating a client's reimbursement of fees, we will pro rate the reimbursement according to the number of days remaining in the billing period.

**Mutual Fund Fees:** All fees paid to Chelsea Management Company for investment advisory services are separate and distinct from the fees and expenses charged by mutual funds and/or ETFs to their shareholders. These fees and expenses are described in each fund's prospectus. These fees will generally include a management fee, other fund expenses, and a possible distribution fee. If the fund also imposes sales charges, a client may pay an initial or deferred sales charge. A client could invest in a mutual fund directly, without our services. In that case, the client would not receive the services provided by our firm which are designed, among other things, to assist the client in determining which mutual fund or funds are most appropriate to each client's financial condition and objectives. Accordingly, the client should review both the fees charged by the funds and our fees to fully understand the total amount of fees to be paid by the client and to thereby evaluate the advisory services being provided.

**Additional Fees and Expenses:** In addition to our advisory fees, clients are also responsible for the fees and expenses charged by custodians and imposed by broker dealers, including, but not limited to, any transaction charges imposed by a broker dealer with which an independent investment manager effects transactions for the client's account(s). Please refer to the "Brokerage Practices" section (Item 12) of this Form ADV for additional information.

**Grandfathering of Minimum Account Requirements:** Pre-existing advisory clients are subject to Chelsea Management Company's minimum account requirements and advisory fees in effect at the time the client entered into the advisory relationship. Therefore, our firm's minimum account requirements will differ among clients.

**ERISA Accounts:** Chelsea Management Company is deemed to be a fiduciary to advisory clients that are employee benefit plans or individual retirement accounts (IRAs) pursuant to the Employee Retirement Income and Securities Act ("ERISA"), and regulations under the Internal Revenue Code of 1986 (the "Code"), respectively. As such, our firm is subject to specific duties and obligations under ERISA and the Internal Revenue Code that include among other things, restrictions concerning certain forms of compensation. To avoid

engaging in prohibited transactions, Chelsea Management Company may only charge fees for investment advice about products for which our firm and/or our related persons do not receive any commissions or 12b-1 fees, or conversely, investment advice about products for which our firm and/or our related persons receive commissions or 12b-1 fees, however, only when such fees are used to offset Chelsea Management Company's advisory fees.

**Advisory Fees in General:** Clients should note that similar advisory services may (or may not) be available from other registered (or unregistered) investment advisers for similar or lower fees.

**Limited Prepayment of Fees:** Under no circumstances do we require or solicit payment of fees in excess of \$1200 more than six months in advance of services rendered.

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

Chelsea Management Company does not charge performance-based fees.

## **Item 7 Types of Clients**

Chelsea Management Company provides advisory services to the following types of clients:

- Individuals (other than high net worth individuals)
- High net worth individuals
- Pension and profit sharing plans (other than plan participants)
- Charitable organizations
- Corporations, LLC or other businesses
- Chartered Schools
- Insurance Companies

As previously disclosed in Item 5, our firm has established certain initial minimum account requirements, based on the nature of the service(s) being provided. For a more detailed understanding of those requirements, please review the disclosures provided in each applicable service.

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

### **METHODS OF ANALYSIS**

We use the following methods of analysis in formulating our investment advice and/or managing client assets:

**Fundamental Analysis.** We attempt to measure the intrinsic value of a security by looking at economic and financial factors (including the overall economy, industry conditions, and the financial condition and management of the company itself) to determine if the company is undervalued (indicating it may be a good time to buy) or overvalued (indicating it may be time to sell).

Fundamental analysis does not attempt to anticipate market movements. This presents a potential risk, as the price of a security can move up or down along with the overall market regardless of the economic and financial factors considered in evaluating the stock.

**Technical Analysis.** We analyze past market movements and apply that analysis to the present in an attempt to recognize recurring patterns of investor behavior and potentially predict future price movement.

Technical analysis does not consider the underlying financial condition of a company. This presents a risk in that a poorly-managed or financially unsound company may underperform regardless of market movement.



**Cyclical Analysis.** In this type of technical analysis, we measure the movements of a particular stock against the overall market in an attempt to predict the price movement of the security.

**Risks for all forms of analysis.** Our securities analysis methods rely on the assumption that the companies whose securities we purchase and sell, the rating agencies that review these securities, and other publicly-available sources of information about these securities, are providing accurate and unbiased data. While we are alert to indications that data may be incorrect, there is always a risk that our analysis may be compromised by inaccurate or misleading information.

## **INVESTMENT STRATEGIES**

We use the following strategies in managing client accounts, provided that such strategy(ies) are appropriate to the needs of the client and consistent with the client's investment objectives, risk tolerance, and time horizons, among other considerations:

**Long-term purchases.** We purchase securities with the idea of holding them in the client's account for a year or longer. Typically we employ this strategy when:

- we believe the securities to be currently undervalued, and/or
- we want exposure to a particular asset class over time, regardless of the current projection for this class.

A risk in a long-term purchase strategy is that by holding the security for this length of time, we may not take advantage of short-term gains that could be profitable to a client. Moreover, if our predictions are incorrect, a security may decline sharply in value before we make the decision to sell.

**Short-term purchases.** When utilizing this strategy, we purchase securities with the idea of selling them within a relatively short time (typically a year or less). We do this in an attempt to take advantage of conditions that we believe will soon result in a price swing in the securities we purchase.

A short-term purchase strategy poses risks should the anticipated price swing not materialize; we are then left with the option of having a long-term investment in a security that was designed to be a short-term purchase, or potentially taking a loss.

In addition, this strategy involves more frequent trading than does a longer-term strategy, and will result in increased brokerage and other transaction-related costs, as well as less favorable tax treatment of short-term capital gains.

**Trading.** We purchase securities with the idea of selling them very quickly (typically within 30 days or less). We do this in an attempt to take advantage of our predictions of brief price swings.

**Margin transactions.** We may purchase stocks for your portfolio with money borrowed from your brokerage account provided we have been provided separate authority from you. This allows you to purchase more stock than you would be able to with your available cash, and allows us to purchase stock without selling other holdings.

**Option writing.** We may use options as an investment strategy. An option is a contract that gives the buyer the right, but not the obligation, to buy or sell an asset (such as a share of stock) at a specific price on or before a certain date. An option, just like a stock or bond, is a security. An option is also a derivative, because it derives its value from an underlying asset.

The two types of options are calls and puts:

- A call gives us the right to buy an asset at a certain price within a specific period of time. We will buy a call if we have determined that the stock will increase substantially before the option expires.
- A put gives us the holder the right to sell an asset at a certain price within a specific period of time. We will buy a put if we have determined that the price of the stock will fall before the option expires.

We will use options to speculate on the possibility of a sharp price swing. We will also use options to "hedge" a purchase of the underlying security; in other words, we will use an option purchase to limit the potential upside and downside of a security we have purchased for your portfolio provided you have given us the authority to invest in this manner.

We use "covered calls", in which we sell an option on security you own. In this strategy, you receive a fee for making the option available, and the person purchasing the option has the right to buy the security from you at an agreed-upon price.

We may use a "spreading strategy" if so permitted in which case, in which we purchase two or more option contracts (for example, a call option that you buy and a call option that you sell) for the same underlying security. This effectively puts you on both sides of the market, but with the ability to vary price, time and other factors.

**Risk of Loss.** Securities investments are not guaranteed and you may lose money on your investments. We ask that you work with us to help us understand your tolerance for risk.

### **Item 9 Disciplinary Information**

We are required to disclose any legal or disciplinary events that are material to a client's or prospective client's evaluation of our advisory business or the integrity of our management.

Our firm and our management personnel have no reportable disciplinary events to disclose.

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

Our firm and our related persons are not engaged in other financial industry activities and have no other industry affiliations.

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

Our firm has adopted a Code of Ethics which sets forth high ethical standards of business conduct that we require of our employees, including compliance with applicable federal securities laws.

Chelsea Management Company and our personnel owe a duty of loyalty, fairness and good faith towards our clients, and have an obligation to adhere not only to the specific provisions of the Code of Ethics but to the general principles that guide the Code.

Our Code of Ethics includes policies and procedures for the review of quarterly securities transactions reports as well as initial and annual securities holdings reports that must be submitted by the firm's access persons. Among other things, our Code of Ethics also requires the prior approval of any acquisition of securities in a limited offering (e.g., private placement) or an initial public offering. Our code also provides for oversight, enforcement and recordkeeping provisions.

Chelsea Management Company's Code of Ethics further includes the firm's policy prohibiting the use of material non-public information. While we do not believe that we have any particular access to non-public information, all employees are reminded that such information may not be used in a personal or professional capacity.

A copy of our Code of Ethics is available to our advisory clients and prospective clients. You may request a copy by email sent to [tom.techentin@chelseamanagement.com](mailto:tom.techentin@chelseamanagement.com), or by calling us at 213-362-9200.

Chelsea Management Company and individuals associated with our firm are prohibited from engaging in principal transactions.

Chelsea Management Company and individuals associated with our firm are prohibited from engaging in agency cross transactions.

An employee of Chelsea Management Company, Albert S. Dew, is also the principal and General Partner of CQUANT, LLC and PQUANT, LLC, two investment funds. Al is an officer and head trader for Chelsea Management Company. The General Partner has designated Chelsea Management Company as having primary responsibility for investment management and administrative matters, such as accounting tax and periodic reporting, pertaining to the Fund. Chelsea Management Company and our members, officers and employees will devote to the Fund as much time as we deem necessary and appropriate to manage the Fund's business. Chelsea Management Company and our affiliates are not restricted from forming additional investment funds, entering into other investment advisory relationships or engaging in other business activities but do so with the approval of Chelsea's Board of Directors. Chelsea is not required to register funds as an investment company under the Investment Company Act of 1940 in reliance upon an exemption available to funds whose securities are not publicly offered. Chelsea Management Company manages the Fund on a discretionary basis in accordance with the terms and conditions of the Fund's offering and organizational documents.

Our Code of Ethics is designed to assure that the personal securities transactions, activities and interests of our employees will not interfere with (i) making decisions in the best interest of advisory clients and (ii) implementing such decisions while, at the same time, allowing employees to invest for their own accounts.

Our firm and/or individuals associated with our firm may buy or sell for their personal accounts securities identical to or different from those recommended to our clients. In addition, any related person(s) may have an interest or position in a certain securities which may also be recommended to a client.

It is the expressed policy of our firm that no person employed by us may purchase or sell any security prior to a transaction(s) being implemented for an advisory account, thereby preventing such employee(s) from benefiting from transactions placed on behalf of advisory accounts.

We may aggregate our employee trades with client transactions where possible and when compliant with our duty to seek best execution for our clients. In these instances, participating clients will receive an average share price and transaction costs will be shared equally and on a pro-rata basis. In the instances where there is a partial fill of a particular batched order, we will allocate all purchases pro-rata, with each account paying the average price. Our employee accounts will not be included in the pro-rata allocation.

As these situations represent actual or potential conflicts of interest to our clients, we have established the following policies and procedures for implementing our firm's Code of Ethics, to ensure our firm complies with its regulatory obligations and provides our clients and potential clients with full and fair disclosure of such conflicts of interest:

1. No principal or employee of our firm may put his or her own interest above the interest of an advisory client.
2. No principal or employee of our firm may buy or sell securities for their personal portfolio(s) where their decision is a result of information received as a result of his or her employment unless the information is also available to the investing public.
3. It is the expressed policy of our firm that no person employed by us may purchase or sell any security prior to a transaction(s) being implemented for an advisory account. This prevents such employees from benefiting from transactions placed on behalf of advisory accounts.
4. Our firm requires prior approval for any IPO or private placement investments by related persons of the firm.
5. We maintain a list of all reportable securities holdings for our firm and anyone associated with this advisory practice that has access to advisory recommendations ("access person"). These holdings are reviewed on a regular basis by our firm's Chief Compliance Officer or his/her designee.
6. We have established procedures for the maintenance of all required books and records.
7. All of our principals and employees must act in accordance with all applicable Federal and State regulations governing registered investment advisory practices.
8. We require delivery and acknowledgement of the Code of Ethics by each supervised person of our firm.
9. We have established policies requiring the reporting of Code of Ethics violations to our senior management.
10. Any individual who violates any of the above restrictions may be subject to termination.

## **Item 12 Brokerage Practices**

For discretionary clients, Chelsea Management Company requires these clients to provide us with written authority to determine the broker dealer to use and the commission costs that will be charged to these clients for these transactions.

These clients must include any limitations on this discretionary authority in this written authority statement. Clients may change/amend these limitations as required. Such amendments must be provided to us in writing.

Chelsea Management Company will endeavor to select those brokers or dealers which will provide the best services at the lowest commission rates possible. The reasonableness of commissions is based on the broker's stability, reputation, ability to provide professional services, competitive commission rates and prices, research, trading platform, and other services which will help Chelsea Management Company in providing investment management services to clients. Chelsea Management Company may, therefore recommend (or use) the use of a broker who provides useful research and securities transaction services even though a lower commission may be charged by a broker who offers no research services and minimal securities transaction assistance. Research services may be useful in servicing all our clients, and not all of such research may be useful for the account for which the particular transaction was effected.

Consistent with obtaining best execution for clients, Chelsea Management Company may direct brokerage transactions for clients' portfolios to brokers who provide research and execution services to Chelsea Management Company and, indirectly, to Chelsea Management Company's clients. These services are of the type described in Section 28(e) of the Securities Exchange Act of 1934 and are designed to augment our own internal research and investment strategy capabilities. This may be done without prior agreement or understanding by the client (and done at our discretion). Research services obtained through the use of soft dollars may be developed by brokers to whom brokerage is directed or by third-parties which are compensated by the broker. Chelsea Management Company does not attempt to put a specific dollar value on the services rendered or to allocate the relative costs or benefits of those services among clients, believing that the research we receive will help us to fulfill our overall duty to our clients. Chelsea Management Company may not use each particular research service, however, to service each client. As a result, a client may pay brokerage commissions that are used, in part, to purchase research services that are not used to benefit that specific client. Broker-dealers we select may be paid commissions for effecting transactions for our clients that exceed the amounts other broker-dealers would have charged for effecting these transactions if Chelsea Management Company determines in good faith that such amounts are reasonable in relation to the value of the brokerage and/or research services provided by those broker-dealers, viewed either in terms of a particular transaction or our overall duty to its ('brokerage') discretionary client accounts.

Certain items obtainable with soft dollars may not be used exclusively for either execution or research services. The cost of such "mixed-use" products or services will be fairly allocated and Chelsea Management Company makes a good faith effort to determine the percentage of such products or services which may be considered as investment research. The portions of the costs attributable to non-research usage of such products or services are paid by our firm to the broker-dealer in accordance with the provisions of Section 28(e) of the Securities Exchange Act of 1934.

When Chelsea Management Company uses client brokerage commissions to obtain research or brokerage services, we receive a benefit to the extent that Chelsea Management Company does not have to produce such products internally or compensate third-parties with our own money for the delivery of such services. Therefore, such use of client brokerage commissions results in a conflict of interest, because we have an incentive to direct client brokerage to those brokers who provide research and services we utilize, even if these brokers do not offer the best price or commission rates for our clients.

Within our last fiscal year, we have obtained the following products and services on a soft-dollar basis through Interstate Group: Bloomberg Pricing Information, NYSE Wire Fees, Options Price Reporting, Thompson Reuters Market Sales LLC, Value Line Investment Survey

“We are obliged to direct a minimum amount of clients’ commissions to certain brokerage firms in order for the brokerage firm to pay for research services provided to us by third parties. If we don’t direct the minimum required amount for commission to a brokerage firm supplying us with third party research, then the brokerage firm will not continue to pay for research services provided to us by third parties and we would have to pay those costs directly. In 2011, we directed approximately \$161,572 clients’ brokerage commissions to Morgan Keegan (for credit to The Interstate Group) in order to meet the requirements to receive credit toward the payment of research and brokerage services provided to us by third parties. The total commissions directed to this firm represented approximately 48.4% of all commissions generated from client accounts for which we have discretion to direct brokerage. In addition in 2011, we direct clients transactions to Raymond James & Associates, UBS, Merrill Lynch, Fidelity Investments, Schwab Institutional, Crowell, Weedon and Co., TD Ameritrade and Morgan Stanley Smith Barney Inc., among others, in order to receive their internal research.”

Chelsea Management Company will block trades where possible and when advantageous to clients. This blocking of trades permits the trading of aggregate blocks of securities composed of assets from multiple client accounts, so long as transaction costs are shared equally and on a pro-rated basis between all accounts included in any such block.

Block trading may allow us to execute equity trades in a timelier, more equitable manner, at an average share price. Chelsea Management Company will typically aggregate trades among clients whose accounts can be traded at a given broker, and generally will rotate or vary the order of brokers through which it places trades for clients on any particular day. Chelsea Management Company's block trading policy and procedures are as follows:

- 1) Transactions for any client account may not be aggregated for execution if the practice is prohibited by or inconsistent with the client's advisory agreement with Chelsea Management Company, or our firm's order allocation policy.
- 2) The trading desk in concert with the portfolio manager must determine that the purchase or sale of the particular security involved is appropriate for the client and consistent with the client's investment objectives and with any investment guidelines or restrictions applicable to the client's account.
- 3) The portfolio manager must reasonably believe that the order aggregation will benefit, and will enable Chelsea Management Company to seek best execution for each client participating in the aggregated order. This requires a good faith judgment at the time the order is placed for the execution. It does not mean that the determination made in advance of the transaction must always prove to have been correct in the light of a "20-20 hindsight" perspective. Best execution includes the duty to seek the best quality of execution, as well as the best net price.
- 4) Prior to entry of an aggregated order, a written order ticket must be completed which identifies each client account participating in the order and the proposed allocation of the order, upon completion, to those clients.
- 5) If the order cannot be executed in full at the same price or time, the securities actually purchased or sold by the close of each business day must be allocated pro rata among the participating client accounts in accordance with the initial order ticket or other written statement of allocation. However, adjustments to this pro rata allocation may be made to participating client accounts in accordance with the initial order ticket or other written statement of allocation. Furthermore, adjustments to this pro rata allocation may be made to avoid having odd amounts of shares held in any client account, or to avoid excessive ticket charges in smaller accounts.
- 6) Generally, each client that participates in the aggregated order must do so at the average price for all separate transactions made to fill the order, and must share in the commissions on a pro rata basis in proportion to the client's participation. Under the client's agreement with the custodian/broker, transaction costs may be based on the number of shares traded for each client.
- 7) If the order will be allocated in a manner other than that stated in the initial statement of allocation, a written explanation of the change must be provided to and approved by the Chief Compliance Officer no later than the morning following the execution of the aggregate trade.

8) Chelsea Management Company's client account records separately reflect, for each account in which the aggregated transaction occurred, the securities which are held by, and bought and sold for, that account.

9) Funds and securities for aggregated orders are clearly identified on Chelsea Management Company's records and to the broker-dealers or other intermediaries handling the transactions, by the appropriate account numbers for each participating client.

10) No client or account will be favored over another.

Chelsea Management Company may recommend that clients establish brokerage accounts with the Schwab Institutional division of Charles Schwab & Co., Inc. ("Schwab"), a FINRA registered broker-dealer, member SIPC, to maintain custody of clients' assets and to effect trades for their accounts. Although we recommend that clients establish accounts at Schwab, it is the client's decision to custody assets with Schwab. Chelsea Management Company is independently owned and operated and not affiliated with Schwab.

Schwab provides Chelsea Management Company with access to its institutional trading and custody services, which are typically not available to Schwab retail investors. These services generally are available to independent investment advisers on an unsolicited basis, at no charge to them so long as a total of at least \$10 million of the adviser's clients' assets are maintained in accounts at Schwab Institutional. These services or not contingent upon our firm committing to Schwab any specific amount of business (assets in custody or trading commissions). Schwab's brokerage services include the execution of securities transactions, custody, research, and access to mutual funds and other investments that are otherwise generally available only to institutional investors or would require a significantly higher minimum initial investment.

For our client accounts maintained in its custody, Schwab generally 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.

Schwab Institutional also makes available to our firm other products and services that benefit Chelsea Management Company but may not directly benefit our clients' accounts. Many of these products and services may be used to service all or some substantial number of our client accounts, including accounts not maintained at Schwab.

Schwab's products and services that assist us in managing and administering our clients' accounts include software and other technology that

- i. provide access to client account data (such as trade confirmations and account statements);
- ii. facilitate trade execution and allocate aggregated trade orders for multiple client accounts;
- iii. provide research, pricing and other market data;
- iv. facilitate payment of our fees from clients' accounts; and
- v. assist with back-office functions, recordkeeping and client reporting.

Schwab Institutional also offers other services intended to help us manage and further develop our business enterprise. These services may include:

- i. compliance, legal and business consulting;
- ii. publications and conferences on practice management and business succession; and
- iii. access to employee benefits providers, human capital consultants and insurance providers.

Schwab may make available, arrange and/or pay third-party vendors for the types of services rendered to Chelsea Management Company. Schwab Institutional may discount or waive fees it would otherwise charge for some of these services or pay all or a part of the fees of a third-party providing these services to our firm.

Schwab Institutional may also provide other benefits such as educational events or occasional business entertainment of our personnel. In evaluating whether to recommend or require that clients custody their assets at

Schwab, we may take into account the availability of some of the foregoing products and services and other arrangements as part of the total mix of factors we consider and not solely on the nature, cost or quality of custody and brokerage services provided by Schwab, which may create a potential conflict of interest.

Chelsea Management Company has an arrangement with National Financial Services LLC, and Fidelity Brokerage Services LLC (together with all affiliates, "Fidelity") FINRA registered broker-dealer, member SIPC, through which Fidelity Investments provides our firm with their WealthCentral services. The services include, among others, brokerage, custodial, administrative support, record keeping and related services that are intended to support intermediaries like Chelsea Management Company in conducting business and in serving the best interests of our clients but that may also benefit us.

Fidelity charges brokerage commissions and transaction fees for effecting certain securities transactions (i.e., transactions fees are charged for certain no-load mutual funds, commissions are charged for individual equity and debt securities transactions). Fidelity enables Chelsea Management Company to obtain many no-load mutual funds without transaction charges and other no-load funds at nominal transaction charges. Fidelity's commission rates are generally considered discounted from customary retail commission rates. However, the commissions and transaction fees charged by Fidelity may be higher or lower than those charged by other custodians and broker-dealers. As part of the arrangement, Fidelity also makes available to our firm, at no additional charge to us, certain research and brokerage services, including research services obtained by Fidelity directly from independent research companies, as selected by Chelsea Management Company (within specified parameters). These research and brokerage services presently include services such as technology and is used by our firm to manage accounts for which we have investment discretion.

Chelsea Management Company may also receive additional services which may include a referral program. Without this arrangement, we might be compelled to purchase the same or similar services at our own expense.

As a result of receiving such services for no additional cost, we may have an incentive to continue to use or expand the use of Fidelity's services. We examined this potential conflict of interest when we chose to enter into the relationship with Fidelity and have determined that the relationship is in the best interests of Chelsea Management Company's clients and satisfies our client obligations, including our duty to seek best execution. Chelsea Management Company participates in the institutional customer program offered by TD Ameritrade Institutional. TD Ameritrade Institutional is a division of TD Ameritrade Inc., member SIPC ("TD Ameritrade"), an unaffiliated SEC-registered broker-dealer and FINRA member. TD Ameritrade offers services to independent investment advisers which include custody of securities, trade execution, clearance and settlement of transactions. Chelsea Management Company receives some benefits from TD Ameritrade through our participation in the program.

Chelsea Management Company participates in TD Ameritrade's Institutional customer program and we may recommend TD Ameritrade to our clients for custody and brokerage services. There is no direct link between our firm's participation in the program and the investment advice we give to our clients, although we receive economic benefits through our participation in the program that are typically not available to TD Ameritrade retail investors.

These benefits include the following products and services (provided without cost or at a discount): duplicate client and statements confirmations; research related products and tools; consulting services ; access to a trading desk serving adviser participants; access to block trading (which provides the ability to aggregate securities transactions for execution and then allocate the appropriate shares to client accounts); the ability to have advisory fees deducted directly from client accounts; access to an electronic communications network for client order entry and account information; access to mutual funds with no transaction fees and to certain Institutional money managers; and discounts on compliance, marketing, research, technology, and practice management products or services provided to Chelsea Management Company by third party vendors. TD Ameritrade may also pay for business consulting and professional services received by Chelsea Management Company's related persons and may also pay or reimburse expenses (including travel, lodging, meals [and entertainment] expenses) for Chelsea Management Company's personnel to attend conferences or meetings relating to the program or to TD Ameritrade's adviser custody and brokerage services generally.

Some of the products and services made available by TD Ameritrade through the program may benefit Chelsea Management Company but may not benefit our client accounts. These products or services may assist us in managing and administering client accounts, including accounts not maintained at TD Ameritrade. Other services made available by TD Ameritrade are intended to help us manage and further develop our business enterprise. The benefits received by Chelsea Management Company through participation in the program do not depend on the amount of brokerage transactions directed to TD Ameritrade. Clients should be aware, however, that the receipt of economic benefits by Chelsea Management Company or our related persons in and of itself creates a potential conflict of interest and may indirectly influence our recommendation of TD Ameritrade for custody and brokerage services.

Chelsea Management Company also receives from TD Ameritrade certain additional economic benefits ("Additional Services") that may or may not be offered to any other independent investment advisers participating in the program. TD Ameritrade provides the Additional Services to our firm in its sole discretion and at its own expense, and Chelsea Management Company does not pay any fees to TD Ameritrade for the Additional Services. Chelsea Management Company and TD Ameritrade have entered into a separate agreement ("Additional Services Addendum") to govern the terms of the provision of the Additional Services.

Chelsea Management Company's receipt of Additional Services raises potential conflicts of interest. In providing Additional Services to our firm, TD Ameritrade most likely considers the amount and profitability to TD Ameritrade of the assets in, and trades placed for, our client accounts maintained with TD Ameritrade. TD Ameritrade has the right to terminate the Additional Services Addendum with Chelsea Management Company, in its sole discretion, provided certain conditions are met. Consequently, in order to continue to obtain the Additional Services from TD Ameritrade, we may have an incentive to recommend to our clients that the assets under management by us be held in custody with TD Ameritrade and to place transactions for client accounts with TD Ameritrade.

Chelsea Management Company's receipt of Additional Services does not diminish our duty to act in the best interests of our clients, including seeking best execution of trades for client accounts.

### **Item 13    Review of Accounts**

#### **PORTFOLIO MANAGEMENT**

**REVIEWS:** While the underlying securities within individual portfolios are continually monitored, these accounts are reviewed at least quarterly. Accounts are reviewed in the context of each client's stated investment objectives and guidelines. More frequent reviews may be triggered by material changes in variables such as the client's individual circumstances, or the market, political or economic environment.

**These accounts are reviewed by:** Thomas Techentin, Chief Compliance Officer along with the portfolio managers and investment committee.

**REPORTS:** In addition to the monthly statements and confirmations of transactions that clients receive from their broker-dealer, we provide quarterly reports summarizing account performance, balances and holdings.

#### **MODEL PORTFOLIO MANAGEMENT**

**REVIEWS:** While the underlying securities within Model Portfolios are continually monitored, these accounts are reviewed at least quarterly. Accounts are reviewed in the context of the investment objectives and guidelines of each model portfolio as well as any investment restrictions provided by the client. More frequent reviews may be triggered by material changes in variables such as the client's individual circumstances, or the market, political or economic environment.

**These accounts are reviewed by:** Thomas Techentin, Chief Compliance Officer along with the portfolio managers and investment committee.

**REPORTS:** In addition to the monthly statements and confirmations of transactions that clients receive from their broker-dealer, we provide quarterly reports summarizing account performance, balances and holdings. These reports will also remind the client to notify us if there have been changes in the client's financial situation



or investment objectives and whether the client wishes to impose investment restrictions or modify existing restrictions.

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

##### **CLIENT REFERRALS**

Our firm may pay referral fees to independent persons or firms ("Solicitors") for introducing clients to us. Whenever we pay a referral fee, we require the Solicitor to provide the prospective client with a copy of this document (our *Firm Brochure*) and a separate disclosure statement that includes the following information:

- the Solicitor's name and relationship with our firm;
- the fact that the Solicitor is being paid a referral fee;
- the amount of the fee; and
- whether the fee paid to us by the client will be increased above our normal fees in order to compensate the Solicitor.

As a matter of firm practice, the advisory fees paid to us by clients referred by solicitors are not increased as a result of any referral.

It is Chelsea Management Company's policy not to accept or allow our related persons to accept any form of compensation, including cash, sales awards or other prizes, from a non-client in conjunction with the advisory services we provide to our clients.

#### **Item 15 Custody**

We previously disclosed in the "Fees and Compensation" section (Item 5) of this Brochure that our firm, at the direction of the client, directly debits advisory fees from client accounts.

As part of this billing process, the client's custodian is advised of the amount of the fee to be deducted from that client's account. On at least a quarterly basis, the custodian is required to send to the client a statement showing all transactions within the account during the reporting period.

Because the custodian does not calculate the amount of the fee to be deducted, it is important for clients to carefully review their custodial statements to verify the accuracy of the calculation, among other things. Clients should contact us directly if they believe that there may be an error in their statement.

In addition to the periodic statements that clients receive directly from their custodians, we also send account statements directly to our clients on a quarterly basis. We urge our clients to carefully compare the information provided on these statements to ensure that all account transactions, holdings and values are correct and current.

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

Clients may hire us to provide discretionary asset management services, in which case we place trades in a client's account without contacting the client prior to each trade to obtain the client's permission.

Our discretionary authority includes the ability to do the following without contacting the client:

- determine the security to buy or sell; and/or
- determine the amount of the security to buy or sell

Clients give us discretionary authority when they sign a discretionary agreement with our firm, and may limit this authority by giving us written instructions. Clients may also change/amend such limitations by once again providing us with written instructions.

## **Item 17 Voting Client Securities**

We vote proxies for all client accounts; however, you always have the right to vote proxies yourself. You can exercise this right by instructing us in writing to not vote proxies in your account.

We will vote proxies in the best interests of its clients and in accordance with our established policies and procedures. Our firm will retain all proxy voting books and records for the requisite period of time, including a copy of each proxy statement received, a record of each vote cast, a copy of any document created by us that was material to making a decision how to vote proxies, and a copy of each written client request for information on how the adviser voted proxies. If our firm has a conflict of interest in voting a particular action, we will notify the client of the conflict and retain an independent third-party to cast a vote.

Clients may obtain a copy of our complete proxy voting policies and procedures by contacting Thomas Techentin by telephone, email, or in writing. Clients may request, in writing, information on how proxies for his/her shares were voted. If any client requests a copy of our complete proxy policies and procedures or how we voted proxies for his/her account(s), we will promptly provide such information to the client.

We will neither advise nor act on behalf of the client in legal proceedings involving companies whose securities are held in the client's account(s), including, but not limited to, the filing of "Proofs of Claim" in class action settlements. If desired, clients may direct us to transmit copies of class action notices to the client or a third party. Upon such direction, we will make commercially reasonable efforts to forward such notices in a timely manner.

With respect to ERISA accounts, we will vote proxies unless the plan documents specifically reserve the plan sponsor's right to vote proxies. To direct us to vote a proxy in a particular manner, clients should contact Thomas Techentin by telephone, email, or in writing.

You can instruct us to vote proxies according to particular criteria (for example, to always vote with management, or to vote for or against a proposal to allow a so-called "poison pill" defense against a possible takeover). These requests must be made in writing. You can also instruct us on how to cast your vote in a particular proxy contest by contacting us at 213-362-9200.

## **Item 18 Financial Information**

As an advisory firm that maintains discretionary authority for client, we are also required to disclose any financial condition that is likely to impair our ability to meet our contractual obligations. Chelsea Management Company has no adverse financial circumstances to report.

Under no circumstances do we require or solicit payment of fees in excess of \$1200 per client more than six months in advance of services rendered. Therefore, we are not required to include a financial statement.

Chelsea Management Company has not been the subject of a bankruptcy petition at any time in its history.