

# Disclosure Brochure

July 2, 2012

## **Nichols Investment Management**

*a Licensed Investment Adviser*

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This brochure provides information about the qualifications and business practices of Nichols Investment Management (hereinafter "NIM"). If you have any questions about the contents of this brochure, please contact James W. Nichols at (207) 942-8737 or fax number (207) 990-1310. 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 Nichols Investment Management is available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

Nichols Investment Management is a licensed investment adviser. Licensure does not imply any level of skill or training.

## Item 2. Material Changes

This Item discusses only the material changes that have occurred since NIM's last annual update dated March 31, 2011.

Since the firm's last annual update, the firm has initiated switching from SEC registration and has applied to become licensed with the State of Maine.

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### Supervised Person Brochure Supplement

## Item 4. Advisory Business

NIM provides financial planning, consulting, and investment management services. Prior to engaging NIM to provide any of the foregoing investment advisory services, the client is required to enter into one or more written agreements with NIM setting forth the terms and conditions under which NIM renders its services (collectively the “*Agreement*”).

NIM has been in business since October 20, 1989. James W. Nichols is the principal owner of NIM.

NIM has \$52,828,691 of discretionary assets under management as of June 1, 2012.

This Disclosure Brochure describes the business of NIM. Certain sections will also describe the activities of *Supervised Persons*. *Supervised Persons* are any of NIM's officers, partners, directors (or other persons occupying a similar status or performing similar functions), or employees, or any other person who provides investment advice on NIM's behalf and is subject to NIM's supervision or control.

### Financial Planning and Consulting Services

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NIM may provide its clients with a broad range of comprehensive financial planning and consulting services. These services include basic estate planning, retirement planning and educational funding assistance.

In performing its services, NIM is not required to verify any information received from the client or from the client's other professionals (e.g., attorney, accountant, etc.) and is expressly authorized to rely on such information. NIM may recommend the services of itself and/or other professionals to implement its recommendations. Clients are advised that a conflict of interest exists if NIM recommends its own services. The client is under no obligation to act upon any of the recommendations made by NIM under a financial planning or consulting engagement or to engage the services of any such recommended professional, including NIM itself. The client retains absolute discretion over all such implementation decisions and is free to accept or reject any of NIM's recommendations. Clients are advised that it remains their responsibility to promptly notify NIM if there is ever any change in their financial situation or investment objectives for the purpose of reviewing, evaluating, or revising NIM's previous recommendations and/or services.

### Investment Management Services

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Clients can engage NIM to manage all or a portion of their assets on a discretionary basis.

NIM primarily allocates clients' investment management assets among individual debt and equity securities in accordance with the investment objectives of the client. NIM also provides advice about any type of investment held in clients' portfolios.

## Nichols Investment Management Disclosure Brochure

NIM also may render non-discretionary investment management services to clients relative to variable life/annuity products that they may own, their individual employer-sponsored retirement plans, and/or 529 plans or other products that may not be held by the client's primary custodian. In so doing, NIM either directs or recommends the allocation of client assets among the various investment options that are available with the product. Client assets are maintained at the specific insurance company or custodian designated by the product.

NIM tailors its advisory services to the individual needs of clients. NIM consults with clients initially and on an ongoing basis to determine risk tolerance, time horizon and other factors that may impact the clients' investment needs. NIM ensures that clients' investments are suitable for their investment needs, goals, objectives and risk tolerance.

Clients are advised to promptly notify NIM if there are changes in their financial situation or investment objectives or if they wish to impose any reasonable restrictions upon NIM's management services. Clients may impose reasonable restrictions or mandates on the management of their account (e.g., require that a portion of their assets be invested in socially responsible funds) if, in NIM's sole discretion, the conditions will not materially impact the performance of a portfolio strategy or prove overly burdensome to its management efforts.

## Item 5. Fees and Compensation

NIM offers its services on a fee basis, which may include hourly fees, as well as fees based upon assets under management.

### **Financial Planning and Consulting Fees**

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NIM may charge an hourly fee for financial planning and consulting services. These fees are negotiable, but are generally \$60 on an hourly rate basis, depending upon the level and scope of the services. If the client engages NIM for additional investment advisory services, NIM may offset all or a portion of its fees for those services based upon the amount paid for the financial planning and/or consulting services.

Prior to engaging NIM to provide financial planning and/or consulting services, the client is required to enter into a written agreement with NIM setting forth the terms and conditions of the engagement. The fees for this service are not charged in advance. Rather, these fees are charged upon completion of hourly services.

### **Investment Management Fee**

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NIM provides investment management services for an annual fee based upon a percentage of the market value of the assets being managed by NIM. NIM's annual fee is exclusive of, and in addition to brokerage commissions, transaction fees, and other related costs and expenses which are incurred by the client. NIM does not, however, receive any portion of these commissions, fees, and costs. NIM's annual fee is prorated and charged quarterly, in arrears, based upon the market value of the assets being managed by NIM on the last day of the previous quarter. The annual fee varies (between 0.40% and 1.00%) depending upon the market value of the assets under management and the type of investment management services to be rendered, as follows:

#### *Equity and Convertible Securities Portfolios*

<b><u>PORTFOLIO VALUE</u></b>	<b><u>BASE FEE</u></b>
First \$100,000	1.00%
Next \$900,000	0.80%
Above \$1,000,000	Negotiable

#### *Municipal and Government Securities Portfolios*

<b><u>PORTFOLIO VALUE</u></b>	<b><u>BASE FEE</u></b>
First \$1,000,000	0.40%
Above \$1,000,000	Negotiable

The Municipal and Government Securities Portfolios are portfolios where at least one investment consists of government or municipal securities. The government or municipal securities typically make up a very small percentage of the Municipal and Government Securities Portfolios.

NIM, in its sole discretion (without the consent of every client), may negotiate with a particular client to charge a lesser management fee based upon certain criteria (i.e., anticipated future earning capacity, anticipated future additional assets, dollar amount of assets to be managed, related accounts, account composition, pre-existing client, account retention, *pro bono* activities, etc.).

## **Fees Charged by Financial Institutions**

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As further discussed in response to Item 12 (below), NIM generally recommends that clients utilize the brokerage and clearing services of TD AMERITRADE Institutional, a division of TD AMERITRADE, Inc. (“*TD Ameritrade*”). *TD Ameritrade* offers to independent investment advisors services which include custody of securities, trade execution, clearance and settlement of transactions. NIM receives some benefits from *TD Ameritrade* through its participation in the program.

NIM may only implement its investment management recommendations after the client has arranged for and furnished NIM with all information and authorization regarding accounts with appropriate financial institutions. Financial institutions include, but are not limited to, *TD Ameritrade*, any other broker-dealer recommended by NIM, broker-dealer directed by the client, trust companies, banks etc. (collectively referred to herein as the “*Financial Institutions*”).

Clients may incur certain charges imposed by the *Financial Institutions* and other third parties such as custodial fees, charges imposed directly by a mutual fund or ETF in the account, which are disclosed in the fund’s prospectus (e.g., fund management fees and other fund expenses), deferred sales charges, odd-lot differentials, transfer taxes, wire transfer and electronic fund fees, and other fees and taxes on brokerage accounts and securities transactions. Additionally, clients may incur brokerage commissions and transaction fees. Such charges, fees and commissions are exclusive of and in addition to NIM’s fee.

NIM’s *Agreement* and the separate agreement with any *Financial Institutions* authorize NIM to debit the client’s account for the amount of NIM’s fee and to directly remit that management fee to NIM. Any *Financial Institutions* recommended by NIM have agreed to send a statement to the client, at least quarterly, indicating all amounts disbursed from the account including the amount of management fees paid directly to NIM.

Pursuant to the Maine Office of Securities Rules (Chapter 515 § 11(8)), investment advisers that have custody by virtue of direct fee deduction, must send the client an invoice at the same time it sends an invoice to the custodian or obtain a waiver from the client. Accordingly, NIM sends the client an invoice at

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the same time the custodian sends an invoice to the client. The invoice includes a statement of NIM's fees as well as the time the management fee will be deducted.



## **Fees for Management During Partial Quarters of Service**

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For the initial period of investment management services, the fees are calculated on a *pro rata* basis.

The *Agreement* between NIM and the client will continue in effect until terminated by either party pursuant to the terms of the *Agreement*. NIM's fees are prorated through the date of termination and any remaining balance is charged or refunded to the client, as appropriate.

Clients may make additions to and withdrawals from their account at any time, subject to NIM's right to terminate an account. Additions may be in cash or securities provided that NIM reserves the right to liquidate any transferred securities or decline to accept particular securities into a client's account. Clients may withdraw account assets on notice to NIM, subject to the usual and customary securities settlement procedures. However, NIM designs its portfolios as long-term investments and the withdrawal of assets may impair the achievement of a client's investment objectives. NIM may consult with its clients about the options and ramifications of transferring securities. However, clients are advised that when transferred securities are liquidated, they are subject to transaction fees, fees assessed at the mutual fund level (i.e. contingent deferred sales charge) and/or tax ramifications.

If assets are deposited into or withdrawn from an account after the inception of a quarter, the fee payable with respect to such assets will not be prorated based on the number of days remaining in the quarter.

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

NIM does not provide any services for performance-based fees. Performance-based fees are those based on a share of capital gains on or capital appreciation of the assets of a client.

## Item 7. Types of Clients

NIM provides its services to individuals, pension and profit sharing plans, trusts, estates, charitable organizations, corporations and business entities.

### Minimum Account Size

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As a condition for starting and maintaining a relationship, NIM generally imposes a minimum portfolio size of \$40,000. NIM, in its sole discretion, may accept clients with smaller portfolios based upon certain criteria including anticipated future earning capacity, anticipated future additional assets, dollar amount of assets to be managed, related accounts, account composition, pre-existing client, account retention, and *pro bono* activities. NIM only accepts clients with less than the minimum portfolio size if, in the sole opinion of NIM, the smaller portfolio size will not cause a substantial increase of investment risk beyond the client's identified risk tolerance. NIM may aggregate the portfolios of family members to meet the minimum portfolio size.

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

### Methods of Analysis

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NIM's primary methods of analysis are fundamental, technical and cyclical analysis.

*Fundamental analysis* involves the fundamental financial condition and competitive position of a company. NIM will analyze the financial condition, capabilities of management, earnings, new products and services, as well as the company's markets and position amongst its competitors in order to determine the recommendations made to clients. The primary risk in using fundamental analysis is that while the overall health and position of a company may be good, market conditions may negatively impact the security.

*Technical analysis* involves the analysis of past market data rather than specific company data in determining the recommendations made to clients. Technical analysis may involve the use of charts to identify market patterns and trends which may be based on investor sentiment rather than the fundamentals of the company. The primary risk in using technical analysis is that spotting historical trends may not help to predict such trends in the future. Even if the trend will eventually reoccur, there is no guarantee that NIM will be able to accurately predict such a reoccurrence.

*Cyclical analysis* is similar to technical analysis in that it involves the analysis of market conditions at a macro (entire market/economy) or micro (company specific) level, rather than the overall fundamental analysis of the health of the particular company that NIM is recommending. The risks with cyclical analysis are similar to those of technical analysis.

### Investment Strategies

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NIM uses a small-cap value strategy for the majority (90%) of its investment advisory clients. Approximately 10% of NIM clients need income, so NIM recommends more dividend paying and larger company stocks. NIM believes that because small cap stocks are not followed closely on Wall Street, it is able to find stocks with superior financial statistics.

NIM works consistently to make sure all clients own the stocks that it concentrates on. NIM studies these stocks extensively, contacts management, and listens to the conference calls after the quarterly earnings. NIM seeks out stocks that are below book value, low P/E ratio, and low trading volume.

NIM's average holding period for these stocks is generally over 5 years. Often, the stocks that NIM holds in client portfolios get taken over and that is when the positions are sold.

Clients are strongly advised that NIM's investing strategy takes time and patience as NIM will wait for companies to be discovered by others to properly unlock their value.

## Risks of Loss

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### *Market Risks*

The profitability of a significant portion of NIM's recommendations may depend to a great extent upon correctly assessing the future course of price movements of stocks and bonds. There can be no assurance that NIM will be able to predict those price movements accurately.

### *General Risk of Loss*

Investing in securities involves the risk of loss. Clients should be prepared to bear such loss.

## Item 9. Disciplinary Information

NIM is required to disclose the facts of any legal or disciplinary events that are material to a client's evaluation of its advisory business or the integrity of management. NIM does not have any required disclosures to this Item.

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

NIM is required to disclose any relationship or arrangement that is material to its advisory business or to its clients with certain related persons. NIM does not have any required disclosures to this Item.

## Item 11. Code of Ethics

NIM and persons associated with NIM (“Associated Persons”) are permitted to buy or sell securities that it also recommends to clients consistent with NIM’s policies and procedures.

NIM has adopted a code of ethics (“*Code of Ethics*”) made up of its personal securities transaction and insider trading policies and procedures. When NIM is purchasing or considering for purchase any security on behalf of a client, no *Covered Person* (as defined below) may effect a transaction in that security prior to the completion of the purchase or until a decision has been made not to purchase such security. Similarly, when NIM is selling or considering the sale of any security on behalf of a client, no *Covered Person* may effect a transaction in that security prior to the completion of the sale or until a decision has been made not to sell such security.

Unless specifically defined in NIM’s procedures (summarized above), neither NIM nor any of NIM’s Associated Persons may effect for himself or herself, for an Associated Person’s immediate family (i.e., spouse, minor children, and adults living in the same household as the Associated Person), or for trusts for which the Associated Person serves as a trustee or in which the Associated Person has a beneficial interest (collectively “*Covered Persons*”), any transactions in a security which is being actively purchased or sold, or is being considered for purchase or sale, on behalf of any of NIM’s clients.

The foregoing policies and procedures are not applicable to (a) transactions effected in any account over which neither NIM nor any of its *Supervised Persons* (as defined in this Form ADV) has any direct or indirect influence or control; and (b) transactions in securities that are: direct obligations of the government of the United States; bankers’ acceptances, bank certificates of deposit, commercial paper, and high quality short-term debt instruments, including repurchase agreements; or shares issued by registered open-end investment companies.

This policy has been established recognizing that some securities being considered for purchase and sale on behalf of NIM’s clients trade in sufficiently broad markets to permit transactions by clients to be completed without any appreciable impact on the markets of such securities. Under certain limited circumstances, exceptions may be made to the policies stated above. NIM will maintain records of these trades, including the reasons for any exceptions.

In accordance with Section 204A of the Advisers Act, NIM also maintains and enforces written policies reasonably designed to prevent the unlawful use of material non-public information by NIM or any of its *Supervised Persons*.

Clients and prospective clients may contact NIM to request a copy of its *Code of Ethics*.

## Item 12. Brokerage Practices

As discussed above, in Item 5, NIM generally recommends that clients utilize the brokerage and clearing services of *TD Ameritrade*.

Factors which NIM considers in recommending *TD Ameritrade* or any other broker-dealer to clients include their respective financial strength, reputation, execution, pricing, research and service. The commissions and/or transaction fees charged by *TD Ameritrade* may be higher or lower than those charged by other *Financial Institutions*.

The commissions paid by NIM's clients comply with NIM's duty to obtain "best execution." Clients may pay commissions that are higher than another qualified *Financial Institution* might charge to effect the same transaction where NIM determines that the commissions are reasonable in relation to the value of the brokerage and research services received. In seeking best execution, the determinative factor is not the lowest possible cost, but whether the transaction represents the best qualitative execution, taking into consideration the full range of a *Financial Institution's* services, including among others, the value of research provided, execution capability, commission rates, and responsiveness. NIM seeks competitive rates but may not necessarily obtain the lowest possible commission rates for client transactions.

NIM periodically and systematically reviews its policies and procedures regarding its recommendation of *Financial Institutions* in light of its duty to obtain best execution.

The client may direct NIM in writing to use a particular *Financial Institution* to execute some or all transactions for the client. In that case, the client will negotiate terms and arrangements for the account with that *Financial Institution*, and NIM will not seek better execution services or prices from other *Financial Institutions* or be able to "batch" client transactions for execution through other *Financial Institutions* with orders for other accounts managed by NIM (as described below). As a result, the client may pay higher commissions or other transaction costs or greater spreads, or receive less favorable net prices, on transactions for the account than would otherwise be the case. Subject to its duty of best execution, NIM may decline a client's request to direct brokerage if, in NIM's sole discretion, such directed brokerage arrangements would result in additional operational difficulties. Not all investment advisers require their clients to direct brokerage.

Transactions for each client generally will be effected independently, unless NIM decides to purchase or sell the same securities for several clients at approximately the same time. NIM may (but is not obligated to) combine or "batch" such orders to obtain best execution, to negotiate more favorable commission rates, or to allocate equitably among NIM's clients differences in prices and commissions or other transaction costs that might have been obtained had such orders been placed independently. Under this procedure, transactions will generally be averaged as to price and allocated among NIM's clients pro rata to the purchase and sale orders placed for each client on any given day. To the extent that NIM determines to aggregate client orders for the purchase or sale of securities, including securities in which NIM's *Supervised Persons* may invest, NIM generally does so in accordance with applicable rules



promulgated under the Advisers Act and no-action guidance provided by the staff of the U.S. Securities and Exchange Commission. NIM does not receive any additional compensation or remuneration as a result of the aggregation. In the event that NIM determines that a prorated allocation is not appropriate under the particular circumstances, the allocation will be made based upon other relevant factors, which may include: (i) when only a small percentage of the order is executed, shares may be allocated to the account with the smallest order or the smallest position or to an account that is out of line with respect to security or sector weightings relative to other portfolios, with similar mandates; (ii) allocations may be given to one account when one account has limitations in its investment guidelines which prohibit it from purchasing other securities which are expected to produce similar investment results and can be purchased by other accounts; (iii) if an account reaches an investment guideline limit and cannot participate in an allocation, shares may be reallocated to other accounts (this may be due to unforeseen changes in an account's assets after an order is placed); (iv) with respect to sale allocations, allocations may be given to accounts low in cash; (v) in cases when a pro rata allocation of a potential execution would result in a *de minimis* allocation in one or more accounts, NIM may exclude the account(s) from the allocation; the transactions may be executed on a pro rata basis among the remaining accounts; or (vi) in cases where a small proportion of an order is executed in all accounts, shares may be allocated to one or more accounts on a random basis.

Consistent with obtaining best execution, brokerage transactions may be directed to certain broker-dealers in return for investment research products and/or services which assist NIM in its investment decision-making process. Such research generally will be used to service all of NIM's clients, but brokerage commissions paid by one client may be used to pay for research that is not used in managing that client's portfolio. The receipt of investment research products and/or services as well as the allocation of the benefit of such investment research products and/or services poses a conflict of interest because NIM does not have to produce or pay for the products or services.

### **Software and Support Provided by Financial Institutions**

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NIM may receive from *TD Ameritrade*, without cost to NIM, computer software and related systems support, which allow NIM to better monitor client accounts maintained at *TD Ameritrade*. NIM may receive the software and related support without cost because NIM renders investment management services to clients that maintain assets at *TD Ameritrade*. The software and related systems support may benefit NIM, but not its clients directly. In fulfilling its duties to its clients, NIM endeavors at all times to put the interests of its clients first. Clients should be aware, however, that NIM's receipt of economic benefits from a broker-dealer creates a conflict of interest since these benefits may influence NIM's choice of broker-dealer over another broker-dealer that does not furnish similar software, systems support, or services.

There is no direct link between NIM's participation in the program and the investment advice it gives to its clients, although NIM receives economic benefits through its participation in the program that are typically not available to TD Ameritrade retail investors. Additionally, NIM may receive the following benefits from

*TD Ameritrade* through its registered investment adviser division: receipt of duplicate client confirmations and bundled duplicate statements; access to a trading desk that exclusively services its Registered Investment Adviser participants; access to block trading which provides the ability to aggregate securities transactions and then allocate the appropriate shares to client accounts; and access to an electronic communication network for client order entry and account information.

These products or services may assist NIM in managing and administering client accounts, including accounts not maintained at *TD Ameritrade*. Other services made available by *TD Ameritrade* are intended to help NIM manage and further develop its business enterprise. The benefits received by NIM's 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 NIM or its related persons in and of itself creates a potential conflict of interest and may indirectly influence NIM's recommendation of *TD Ameritrade* for custody and brokerage services.

## Item 13. Review of Accounts

For those clients to whom NIM provides investment management services, NIM monitors those portfolios as part of an ongoing process while regular account reviews are conducted on at least a quarterly basis. For those clients to whom NIM provides financial planning and/or consulting services, reviews are conducted on an “as needed” basis. Such reviews are conducted by the Principal of NIM, James W. Nichols. All investment advisory clients are encouraged to discuss their needs, goals, and objectives with NIM and to keep NIM informed of any changes thereto. NIM contacts ongoing investment advisory clients at least annually to review its previous services and/or recommendations and to discuss the impact resulting from any changes in the client’s financial situation and/or investment objectives.

Unless otherwise agreed upon, clients are provided with transaction confirmation notices and regular summary account statements directly from the broker-dealer or custodian for the client accounts. Those clients to whom NIM provides investment advisory services will also receive a report from NIM that may include such relevant account and/or market-related information such as an inventory of account holdings and account performance on a monthly basis. Clients should compare the account statements they receive from their custodian with those they receive from NIM.

Those clients to whom NIM provides financial planning and/or consulting services will receive reports from NIM summarizing its analysis and conclusions as requested by the client or otherwise agreed to in writing by NIM.

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

NIM is required to disclose any relationship or arrangement where it receives an economic benefit from a third party (non-client) for providing advisory services. In addition, NIM is required to disclose any direct or indirect compensation that it provides for client referrals. NIM does not have any required disclosures to this Item.

## Item 15. Custody

NIM's *Agreement* and/or the separate agreement with any *Financial Institution* may authorize NIM through such *Financial Institution* to debit the client's account for the amount of NIM's fee and to directly remit that management fee to NIM in accordance with applicable custody rules.

The *Financial Institutions* recommended by NIM have agreed to send a statement to the client, at least quarterly, indicating all amounts disbursed from the account including the amount of management fees paid directly to NIM. In addition, as discussed in Item 13, NIM also sends periodic supplemental reports to clients. Clients should carefully review the statements sent directly by the *Financial Institutions* and compare them to those received from NIM.

## Item 16. Investment Discretion

NIM is given the authority to exercise discretion on behalf of clients. NIM is considered to exercise investment discretion over a client's account if it can effect transactions for the client without first having to seek the client's consent. NIM is given this authority through a power-of-attorney included in the agreement between NIM and the client. Clients may request a limitation on this authority (such as certain securities not to be bought or sold). NIM takes discretion over the following activities:

- The securities to be purchased or sold;
- The amount of securities to be purchased or sold; and
- When transactions are made.

### Item 17. Voting Client Securities

NIM is required to disclose if it accepts authority to vote client securities. While, NIM does not vote client securities on behalf of its clients, clients may contact NIM with questions about a particular solicitation. Clients receive proxies directly from the *Financial Institutions*.

## Item 18. Financial Information

NIM does not require or solicit the prepayment of more than \$500 in fees six months or more in advance. In addition, NIM is required to disclose any financial condition that is reasonably likely to impair its ability to meet contractual commitments to clients. NIM has no disclosures pursuant to this Item.

## Item 19. Requirements for State Licensed Investment Advisors

### Principal Executive Officers and Management Persons

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Below is the formal education and business background of NIM's principal executive officer and management person:

#### James W. Nichols

Born 1952

#### Post-Secondary Education

University of Maine | MBA, Business | 1976

Franklin and Marshall College | BA, Economics | 1974

#### Recent Business Background

Nichols Investment Management | Owner | October 1989 - Present

None of the *Supervised Persons* of NIM are compensated for advisory services with performance-based fees. In addition, neither NIM nor its management persons have been the subject of the type of disciplinary event in the instructions to Item 19. Neither NIM nor any of its *Supervised Persons* have a relationship or arrangement with any issuers of securities not disclosed in response to Item 10 (above).



## **Nichols Investment Management**

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Prepared by:



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