

## Divisar Capital Management, LLC

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This brochure provides information about the qualifications and business practices of Divisar Capital Management, LLC. If you have any questions about the contents of this brochure, please contact us at the telephone number and/or e-mail address above. The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission or any state securities authority.

Divisar Capital Management, LLC is a registered investment adviser. Registration of an investment adviser does not imply any level of skill or training. The verbal and written communications of an investment adviser provide you with information you need to determine whether to hire or retain the adviser.

Please contact us at (415) 418-2201 or steve@divisarmanagement.com if you would like a copy of our updated Part 2. Additional information about Divisar Capital Management, LLC is also available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

## Divisar Capital Management, LLC

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Our previous annual update was dated March 2020. The following material changes have been made to the Part 2 since that amendment.

1. Item 4 has been amended to reflect that as of December 31, 2020, we have \$654.7 million in discretionary regulatory assets under management.

# ITEM 3

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## **ITEM 4: ADVISORY BUSINESS**

### **Who We Are**

Divisar Capital Management, LLC (referred to as “we,” “our,” “us,” the “Firm”, or “Divisar”) has been registered as an investment adviser since February 2009. Our principal officer and sole owner is Steven R. Baughman.

### **Services We Offer**

We provide investment advisory services to Divisar Partners, LP, an investment limited partnership and Divisar Partners QP, LP, an investment limited partnership (herein referred to as the “Funds”). Divisar Capital Management, LLC is currently not accepting new capital into its Funds.

The Funds’ goals are capital appreciation through investing and trading in securities, while attempting simultaneously to preserve capital. Current income is not an objective.

The Funds focus primarily on equity and equity-related securities that are publicly-traded. However, they are permitted to pursue a highly diverse range of investment and trading strategies. In particular, the Funds also sell short equity securities both as an independent profit opportunity and as an attempt to hedge a portion, or the entirety, of the securities held long. The Funds may also use leverage. The Funds may buy or sell (write) options, both publicly-traded and over-the-counter, covered and uncovered, on securities and securities indices. The Funds may also engage in futures and other derivatives transactions, typically for hedging of existing long and short positions, but also, at Divisar’s discretion, as independent profit opportunities. The Funds may also invest in fixed income securities.

Our investments are tailored to comply with the investment guidelines disclosed in the offering materials for the Funds. Each potential investor in each Fund receives a complete set of offering materials prior to investing in that Fund.

We do not provide portfolio management services to a wrap fee program.

### **Assets Under Management**

As of December 31, 2020, we have \$654.7 million in discretionary regulatory assets under management. We do not manage assets on a non-discretionary basis.

## **ITEM 5: FEES AND COMPENSATION**

### **Fees and Compensation**

#### **Divisar Partners, LP**

We receive both an asset-based fee and an incentive allocation. The asset-based fee is 1.5% per year, billed in monthly installments. This fee is billed monthly in advance, based on the value of the assets under management as of the first day of the month.

The incentive allocation is calculated as of December 31 each year. When profits for the current period exceed the accumulated unrecouped net losses for prior periods, we will receive an incentive allocation of 20% of the profits generated. Solely for purposes of computing this fee, net profits and net losses include unrealized gains and losses. If you withdraw capital from the Fund the incentive allocation for the amount withdrawn will be calculated as of the withdrawal date.

For investors who do not meet the minimum requirements to pay an incentive allocation, we will charge an asset-based fee of 1.5%, with no incentive allocation. This asset-based fee will be billed on the same schedule as disclosed above.

With respect to both the asset-based fee and the incentive allocation, Divisar may waive, rebate or otherwise vary the rate charged to an investor.

Investors may make withdrawals as of the last day of any calendar quarter by providing 55 days written notice.

### Divisar Partners QP, LP

We receive both an asset-based fee and an incentive allocation. The asset-based fee is 1.5% per year, billed in monthly installments. This fee is billed monthly in advance, based on the value of the assets under management as of the first day of the month.

The incentive allocation is calculated as of December 31 each year. When profits for the current period exceed the accumulated unrecouped net losses for prior periods, we will receive an incentive allocation of 20% of the profits generated. Solely for purposes of computing this fee, net profits and net losses include unrealized gains and losses. If you withdraw capital from the Fund the incentive allocation for the amount withdrawn will be calculated as of the withdrawal date.

With respect to both the asset-based fee and the incentive allocation, Divisar may waive, rebate or otherwise vary the rate charged to an investor.

Investors may make withdrawals as of the last day of any calendar quarter by providing 55 days written notice.

### **Other Costs Involved**

In addition to our advisory fees shown above, expenses associated with making investments on behalf of the Funds and other clients will also be incurred. These fees include:

- management fees for ETFs and mutual funds. These are fees charged by the managers of the ETF or mutual fund and are a portion of the expenses of the ETF or mutual fund.
- brokerage costs and transaction fees for any securities or fixed income trades. These are generally charged by your custodian and/or executing broker.
- Audit, tax preparation services, bookkeeping, other professional fees and legal fees associated with the Funds.

- Governmental fees, taxes, license and registration fees, and costs associated with the ongoing offering and sales of interests in the Funds.

Additional information about brokerage costs and services is provided in “Item 12: Brokerage Practices.”

## General Disclosures

In order to pay an incentive allocation, you must meet certain requirements.

- You have a net worth (or together with your spouse have a net worth) of at least \$2.1 million, excluding your primary residence.
- You have at least \$1,000,000 invested with us.

Investors with initial contributions prior to September 19, 2011, may continue to rely on the exemption available at the time of initial investment.

The subscription documents for the Funds provide additional qualifications standards. All incentive allocations will be made in a manner that complies with applicable rules and regulations.

Incentive allocation arrangements could create an incentive for us to make investments that are riskier or more speculative than would be the case in the absence of the arrangement. In some circumstances, we may receive increased compensation as a result of unrealized appreciation as well as realized gains.

Because the clients may have different fee structures, a conflict of interest exists where the Firm must allocate any limited investment opportunities among the clients, and may have an incentive to allocate to (a) a client with a performance-based fee structure over clients that are not charged a performance-based fee, and (b) clients from which the Firm will receive a greater performance-based fee over clients with a less performance-based fee.

The Firm generally addresses the foregoing conflicts by allocating investment opportunities across the Funds *pari passu*. The clerical splitting of trades is performed at the end of the day and based on mechanical calculations that do not involve discretionary allocations. Although the Funds run *pari passu*, some variations may occur, such as to minimize prospective tracking error or transaction costs for de minimis projected allocations. Additional details are available.

It is critical that investors refer to the relevant confidential private placement memorandum and other governing documents for a complete understanding of how fees are deducted from their assets. The information contained herein is a summary only and is qualified in its entirety by such documents.

## **ITEM 6: PERFORMANCE-BASED FEES AND SIDE-BY-SIDE MANAGEMENT**

We trade the same positions for all eligible accounts, regardless of whether an incentive fee is received. See Item 5 for discussion on asset-based fees and performance-based fees.

## ITEM 7: TYPES OF CLIENTS

We provide discretionary investment advisory services to the Funds, which are private investment funds. Investors in the Funds may include high net worth individuals, trusts, businesses and pension or profit-sharing plans. Generally, investors in the Funds are required to maintain a minimum of \$500,000 invested with the Funds. This minimum may be waived at our sole discretion.

## ITEM 8: METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS

**Value Focus.** In selecting securities for purchase or sale (including short sales), our principal focus is on valuation. Unless a security's price deviates significantly from our perception of fair value, we will not commit our partners' capital. However, we believe that significant under- or over-valuation is only a necessary condition for investment; it is not sufficient alone. Without some catalyst to jolt investors, a cheap stock can languish for years, while an expensive equity, driven by speculative momentum, can rise to unimagined heights.

**Asset Classes.** Divisar generally focuses on small-capitalization equity securities, which we define as those with market capitalizations under US\$1 billion. However, we may choose to invest some or all of the Funds' capital in equities that exceed this market capitalization if we believe that to be the best way to pursue the dual goals of capital appreciation and preservation.

Divisar generally will invest a majority of the Funds' capital in securities of companies that are listed or headquartered in the United States. We also expect that a portion of capital may be invested in securities of non-U.S. companies. We may choose to leave the foreign currency exposure of these investments unhedged.

Although Divisar expects to invest the Funds' capital according to the preceding descriptions, the governing documents for the Funds gives Divisar wide latitude, and we expect that there will be times when market conditions will make it advisable to invest outside of these parameters in order to preserve capital or pursue capital appreciation.

**Security Selection.** Divisar selects securities for inclusion in the long and short portfolios using a variety of information sources and methods. These methods include proprietary stock screens that use quantitative criteria that we believe will lead to subsequent stock price appreciation or depreciation. We also source ideas by participating in industry and financial conferences, from buy-side and sell-side contacts, and from close observation of financial markets.

In selecting securities for inclusion in the long portfolio, we look for securities that are cheap based upon a low valuation in comparison to past or future earnings, book value, or our estimation of the value of the intellectual property that the company has developed. We additionally seek to identify a catalyst that could unlock this underappreciated value, which may include a new management or product, an improved economic backdrop, a change in industry structure, improvement in gross and/or operating margins, or other factors that could change investors' opinion of the company and result in share price appreciation. We also expect that, in limited circumstances, the Funds may undertake quiet or public activist stances to unlock the value inherent in a company's balance sheet or business.

Conversely, in identifying securities for the short portfolio, Divisar looks for securities that are expensive compared to current or future earnings, book value, or our estimation of the value of the company's

intellectual property. Catalysts that may result in the Funds selling short a security may include declining margins as competitive forces undermine previously dominant positions, increasing receivables or inventory that may reveal a tougher sales environment or missed internal goals, or other financial statement items that Divisar believes indicate aggressive accounting decisions. Other factors that may result in a decision to sell short a security include untenable business models, capital structures, or elusive future markets that Divisar does not believe will materialize.

**Portfolio Construction and Risk Management.** Divisar constructs the long portfolio and short portfolio to balance the competing goals of diversification, where an unexpected development in a single position does not overwhelmingly affect the Funds' return, and concentration, where the best performing securities have a meaningful impact on the Fund's return. Divisar expects that the long portfolio will normally consist of 25-35 stocks and that the short portfolio will normally consist of 30-45 positions, although market conditions may result in a portfolio with significant deviations from these guidelines.

The investment posture can range widely over time, from significantly net long to predominantly in cash to significantly net short. Divisar measures market risk through gross and net capital exposures as well as through the Funds' hedge ratio, the ratio of capital invested on the short side compared to capital invested on the long side. However, the potential for significant differences in the characteristics and subsequent performance of the long portfolio and short portfolio mean that the hedge ratio is an imperfect measure of future risk and a hedge ratio of even 100% is not assurance that the Funds will not experience significant drawdowns.

Divisar initiates positions with price targets in mind. Although subsequent events can change these estimates of fair value, sometimes dramatically, Divisar generally sells or covers the position when these values are reached. When these targets are reached quickly, this price discipline causes a high proportion of the Funds' realized gains to be short-term capital. Divisar generally considers this trade-off between return and tax treatment to be worthwhile, but the Funds may hold a position across a tax boundary if Divisar deems the risk worth bearing in order to convert the taxable gain to long-term.

While Divisar expects the dominant majority of the Funds' investments to be publicly traded, the Funds may invest a portion of their assets in securities that the Funds may not immediately resell in a ready market, including private investments in public equity securities ("PIPES").

All investing and trading activities risk the loss of capital. While Divisar attempts to moderate these risks, there can be no assurance that Limited Partners will not suffer complete losses. The following discussion sets forth some of the more significant risks associated with the Funds' proposed investment activities.

**General Economic and Market Conditions.** The Funds' investments may be affected by general economic and market conditions, such as interest rates, availability of credit, inflation rates, pandemics, economic uncertainty, changes in laws, developments in governmental regulation and national and international political circumstances. These factors may affect the success of the businesses in which the Funds' portfolio companies are engaged as well as the markets for the securities the Funds hold. Unexpected volatility or illiquidity could impair the Funds' profitability or result in losses.

**Pandemics.** The impact of epidemics and pandemics could greatly affect the economies of many nations including the United States, individual companies, and the market(s). Pandemics may cause extreme volatility and disruption in both the U.S. and global markets causing uncertainty and risks to economic growth, etc. Health crises caused by the recent coronavirus outbreak may exacerbate other pre-existing



political, social, and economic risks in certain countries and globally. Also, pandemics may result, as this outbreak of coronavirus has resulted, in closing borders, enhanced health screenings, healthcare service preparation and delivery, quarantines, cancellation of travel, disruptions to supply chains and customer activity, as well as general concern and uncertainty.

**Use of Leverage.** The Funds may leverage their investment positions by borrowing funds from securities brokers or dealers, banks, or others. They may also use derivatives to leverage their capital, as discussed below. Leverage increases both the possibilities for profit and the risk of loss. Borrowings (and in some cases guarantees of performance of Funds' obligations) will often be from (or, in the case of guarantees, by) securities brokers and dealers (primarily the prime broker) and are typically secured by the Funds' securities and other assets. Under certain circumstances, such a broker or dealer may demand an increase in the collateral that secures the Funds' obligations, and if the Funds are unable to provide additional collateral, the broker or dealer could liquidate assets held in the Funds' accounts to satisfy the Funds' obligations. Liquidation in that manner could have extremely adverse consequences, including sales at disadvantageous times and prices, and the acceleration of tax consequences.

**Short Selling.** The Funds may sell securities short as a regular part of their investing activities. In a short sale, the Funds sell securities they do not own, in the hope that the market price will decline and that the Funds will be able to buy replacement securities later at a lower price. To accomplish this, the Funds borrow the securities from a broker or other third party. They "close" the position by "returning" the security (buying a replacement security on the lender's behalf). The obligation to replace the borrowed securities does not typically have a specified "maturity" date and the lender generally may require replacement of the securities whenever it chooses. A short sale theoretically involves the risk of unlimited loss: the price at which the Funds must buy "replacement" securities could increase without limit. As collateral for their replacement obligations, the Funds are generally required to leave the proceeds of their short sales with the broker that effected the transactions, and deliver additional amounts of cash or other collateral upon the lender's request if the amount of the Funds' liabilities increase due to increases in a security's price or decreases in the value of the existing collateral. The lender for the Funds' short sales will ordinarily be the Funds' prime broker and, ordinarily, all of the Funds' assets will serve as collateral. Therefore, if the value of those assets were to become inadequate to secure the Funds' obligations under its short positions, it is unlikely that the Funds would be able to provide additional collateral. If that were to occur, the prime broker would likely cause the Funds to "buy in" or "close" some or all of their short positions, likely at a time and on terms that are adverse to the Funds. There can be no assurance that the Funds will not experience losses on short positions or that they will have long positions that appreciate in value enough to offset any such losses.

**Hedging, Generally.** Hedging strategies in general are usually intended to limit or reduce investment risk, but they can also be expected to involve transaction costs and may inherently limit or reduce the potential for profit.

**Small Capitalization Stocks.** The Funds may invest a significant portion of their assets (either directly or through derivative securities) in stocks of companies with relatively small market capitalizations. While these stocks can provide significant potential for appreciation, they can involve higher risks in some respects than investments in stocks of larger companies. For example, prices of small-capitalization and even some medium-capitalization stocks are often more volatile than prices of large-capitalization stocks and the risk of bankruptcy or insolvency of many smaller companies (with the attendant losses to investors) may be higher than for larger, "blue-chip" companies. In addition, due to thin trading in some small-capitalization stocks, an investment in those stocks may be considered less liquid.

**Fixed Income Securities.** The value of fixed income securities (including sovereign debt, corporate, and high yield instruments) in which the Funds may invest will change in response to fluctuations in interest rates. In addition, the value of certain fixed income securities can fluctuate in response to perception of credit worthiness, political stability or soundness of economic policies. Valuations of other fixed income instruments may fluctuate in response to changes in the economic environment that may affect future cash flows. Except to the extent that values are independently affected by currency exchange rate fluctuations, when interest rates increase, the value of fixed income securities generally can be expected to decline. The longer a debt security's duration, the more sensitive such debt security is to this risk.

All investments involve different degrees of risk. You should be aware of your risk tolerance level and financial situations at all times. We cannot guarantee the successful performance of an investment and we are expressly prohibited from guaranteeing accounts against losses arising from market conditions.

## **ITEM 9: DISCIPLINARY INFORMATION**

Registered investment advisers are required to disclose any material facts regarding any legal or disciplinary actions that would be material to your evaluation of the investment adviser and each investment adviser representative providing investment advice to you. We have no information of this type to report.

## **ITEM 10: OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS**

We serve as general partner and investment adviser to the Funds. We do not expect to be engaged to advise investors as to the appropriateness of investing in the Funds, and we will not receive any compensation for doing so, or for selling interests in the Funds.

## **ITEM 11: CODE OF ETHICS, PARTICIPATION OR INTEREST IN CLIENT TRANSACTIONS AND PERSONAL TRADING**

### **Code of Ethics**

We have adopted a set of enforceable guidelines (Code of Ethics), which describes unacceptable conduct by Divisar and our associated persons. Summarized, this Code of Ethics prohibits us from:

- placing our interests before yours;
- using non-public information gathered when providing services to you for our own gains; and
- engaging in any act, practice or course of business that is, or might be considered, fraudulent, deceptive, manipulative, or in violation of any applicable law, rule or regulation of a governmental agency.

Please contact us if you would like to receive a full copy of this Code of Ethics.

### **Personal Trading for Associated Persons**

Divisar and associated persons may invest in the same securities that we trade on behalf of the Funds or for a client account. We may buy or sell some of the same securities for the Funds that we already hold in

our personal account. We may also buy for our personal account some of the same securities that are already held in the Funds. Our associated persons may also invest directly in the Funds. It is our policy not to permit our associated persons (or their immediate relatives) to trade in a way that takes advantage of price movements caused by Funds transactions.

Our associated persons must obtain pre-approval before trading in any security. Personal security transactions must be placed after all trades for the clients and the Funds are completed at a given price level. Typically, an associated person may not buy or sell a security for a personal account until two days after orders for clients and the Funds have been filled and there is no buying or selling program in progress.

Divisar and its associated persons may purchase or sell specific securities for their own account based on personal investment considerations without regard to whether the purchase or sale of such security is appropriate for the Funds.

All persons associated with us are required to report all personal securities transactions to us quarterly.

## **ITEM 12: BROKERAGE PRACTICES**

### **Selection of Brokers**

In selecting brokers to execute portfolio transactions, we make a good faith judgment about which broker would be appropriate. We take into consideration not only the available prices and rates of brokerage commissions, but also other relevant factors that may include (without limitation):

- the execution capabilities of the broker/dealer,
- research (including economic forecasts, investment strategy advice, fundamental and technical advice on individual securities, valuation advice and market analysis),
- custodial and other services provided by the broker/dealer that are expected to enhance our general portfolio management capabilities,
- the size of the transaction,
- the difficulty of execution,
- the operational facilities of the broker-dealers involved,
- the risk in positioning a block of securities, and
- the quality of the overall brokerage and research services provided by the broker/dealer.

When we select the broker/dealer for a transaction, we may cause you and/or the Funds to pay a higher commission for effecting a transaction than another broker/dealer would have charged for effecting that transaction. We do this if we determine in good faith that the amount of the commission is reasonable in relation to the value of the brokerage and research services provided by the broker/dealer. The determination is viewed in terms of either the particular transaction or our overall responsibilities with respect to you and the Funds.

## Aggregation of Orders

Our policy regarding the aggregation of orders is explained in each Fund's Offering Memorandum. In general, the Funds run *pari passu*. Consequently, each Fund may seek to buy or sell the same security or other financial instrument at the same time. In those cases, we may combine purchase and sale orders on one Fund's behalf with orders for those of the other Funds. When we do so, we will generally allocate the proceeds arising out of those transactions (and the related transaction expenses) on an average price basis among the various Funds in the transactions. We believe combining orders in this way will, over time, be advantageous to all participants. However, the average price could be less advantageous to one Fund than if that Fund had been the only account effecting the transaction or had completed its transaction before the other participants. The clerical splitting of trades is performed at the end of the day and based on mechanical calculations that do not involve discretionary allocations. Although the Funds run *pari passu*, some variations may occur, such as to minimize prospective tracking error or transaction costs for de minimis projected allocations. Additional details are available.

## Soft Dollars

### General Information

We have a fiduciary duty to our clients to obtain best execution, on an overall basis, for any securities transactions. When determining whether we have obtained best execution, we rely on Section 28(e) of the Securities Exchange Act of 1934, as amended (the "Safe Harbor"). A safe harbor is a provision of a statute or a regulation that reduces or eliminates a party's liability on the grounds that the party performed its actions in good faith. Legislators include safe-harbor provisions to protect legitimate or excusable violations.

This Safe Harbor is provided to an investment adviser like us that has "investment discretion" over client accounts. It provides us protection against certain state and federal breach of fiduciary obligation claims (including ERISA claims) because we, the adviser, caused a client to pay more than the lowest available commission when executing a securities trade in exchange for receiving investment research services and products which helped us make investment decisions of benefit to our clients. To rely on the Safe Harbor provision, we must determine in good faith that the amount of the commissions paid is reasonable in relation to the value of the research services we have received. We take into account not only the costs for a specific transaction but also our overall responsibility to you. When we cause an account to pay more than the lowest available commission to a broker/dealer in return for research products and services, these payments are commonly referred to as "soft dollar" benefits. The broker/dealer tracks the soft dollar benefits generated to be used on our behalf. Not all trades generate soft dollar benefits, and we try to limit "soft dollar" trades whenever preferable.

For purposes of the Safe Harbor, "research services" means "advice," "analyses," and "reports" which meet the following criteria:

- The research is related to the market for securities, such as trade analytics (including analytics available through order management systems) and advice on market color and execution strategies; or
- The research constitutes market, financial, economic or similar data.

For the purposes of the Safe Harbor, “brokerage services” are those products and services that relate to the execution of a trade from the point at which the investment manager communicates with the broker-dealer for the purpose of transmitting an order for execution, through the point at which funds or securities are delivered or credited to an account under our management.

We may also use soft dollars generated by trades for the Funds to acquire services and products that provide benefits to us that may not qualify as research and/or brokerage services, or to pay expenses otherwise payable by us. Payments of soft dollars outside the Safe Harbor do not necessarily involve a breach of fiduciary duty.

We did not use soft dollars in 2020 but may do so in 2021.

### Conflicts of Interest

We may have a conflict of interest in allocating the Funds’ brokerage business to certain broker/dealers, including an incentive to cause the Funds to effect more transactions than they might otherwise do in order to obtain soft dollar benefits. The extent of that conflict depends in large part on the nature and uses of the services and products acquired with soft dollars. When a particular service or product provides benefits to the Funds and/or us, we may (but are not obligated to) allocate the cost among the persons receiving the benefits. Our agreements with the Funds may authorize us to use the soft dollars generated by the Funds to acquire a wide range of services and products.

### Prime Brokerage

We obtain certain services for the Funds, including such services as custodial, recordkeeping, clearing and related services, through what is known as a “prime brokerage” relationship. Under this relationship, a single brokerage firm that we generally select provides the following services:

- maintains custody of the Funds’ assets (either directly or through clearing firms),
- provides margin credit,
- locates securities to borrow to facilitate short sales, and
- provides related services but allows the Funds to use other brokers to execute transactions.

This relationship allows us to seek valuable research and to compare execution quality and commission rates, while maintaining only one custodial relationship. By using a brokerage firm, we also may avoid paying custodial fees that banks charge other institutional investors. The prime broker receives interest on credit balances, margin borrowings, stock loans and brokerage commissions as compensation.

Under this arrangement, the prime broker, among other things:

- arranges for the delivery of securities bought, sold, borrowed and lent,
- makes and receives payments for securities,
- maintains custody of cash and securities, and
- provides detailed trading, portfolio and related reports.

The Funds' obligations to the prime broker (and its affiliates) may be secured by way of a first priority perfected security interest over all of the Funds' assets held in custody. The prime broker (and its affiliates) may transfer to themselves all rights, title and interest in and to those assets as collateral and may deal with, lend, dispose of, pledge or otherwise use all such collateral for their own purposes.

#### Soft Dollar Procedures

A broker/dealer with whom we have a soft dollar arrangement may establish "credits" relating to brokerage commissions paid in the past that may be used to pay or reimburse the broker/dealer for research or other specified expenses. In other cases, a broker/dealer may provide or pay for a service or product and suggest a higher "commission" level for future business to fully compensate the broker/dealer.

Our actual transactional business with such a broker/dealer may be less than the suggested commission level but can—and likely will—exceed that level. This may be in part because our investment activities generate aggregate commissions in excess of the aggregate suggestions from all broker/dealers providing services and products. It may also be in part because those broker/dealers may also provide superior execution and may therefore be the most appropriate for particular transactions. We will not exclude broker/dealers from transaction business simply because they have not provided research or other services.

We believe the above procedures are consistent with the requirements of the Safe Harbor to the extent the services we acquire otherwise qualify as research or brokerage services. Transactions effected on a principal basis, as most transactions with market-makers in over-the-counter securities are, with a mark-up or mark-down paid to the dealer, do not fall within the Safe Harbor.

### **ITEM 13: REVIEW OF ACCOUNTS**

On a daily basis, Steven Baughman, CEO, performs a review of the appropriateness and advisability of the holdings for the Funds and other clients.

Each month investors and clients receive a performance estimate (via e-mail) and a statement of capital account.

On an annual basis, investors in the Funds receive a K-1 and audited financial statements.

### **ITEM 14: CLIENT REFERRALS AND OTHER COMPENSATION**

We do not pay for client referrals.

### **ITEM 15: CUSTODY**

Rule 206(4)-2 promulgated under the Advisers Act (the "Custody Rule") (and certain related rules and regulations under the Advisers Act) imposes certain obligations on registered investment advisers that have custody or possession of any funds or securities in which any client has any beneficial interest. An investment adviser is deemed to have custody or possession of client funds or securities if the adviser

directly or indirectly holds client funds or securities or has the authority to obtain possession of them (regardless of whether the exercise of that authority or ability would be lawful).

We have implemented the following procedures for the Funds:

- All Fund assets are held by a qualified custodian.
- We provide audited financials for each Fund to each investor in that Fund within 120 days of the Fund's fiscal year end. This audit is performed by an independent CPA that is registered with, and subject to regular inspection, by the Public Company Accounting Oversight Board.

Divisar does not accept physical custody of client assets.

## **ITEM 16: INVESTMENT DISCRETION**

We manage the Funds on a discretionary basis and do not allow for any limitations to be placed on our investment authority. Our investment philosophy is summarized above, and more completely described in the offering materials for the Funds.

## **ITEM 17: VOTING CLIENT SECURITIES**

As a matter of policy and as a fiduciary to our clients we have responsibility for voting proxies with the best economic interests of the Funds and the clients. We maintain policies and procedures as to the handling, research, voting and reporting of proxy voting and make appropriate disclosures about our proxy policies and practices. Our policy and practice include the responsibility to monitor corporate actions, receive and vote client proxies and disclose any potential conflicts of interest as well as making information available to clients about the voting of proxies for their portfolio securities and maintaining relevant and required records. You may not provide direction regarding any particular proxy solicitation.

You may request a copy of our Proxy Policies and Procedures and/or information about how a proxy was voted at any time.

## **ITEM 18: FINANCIAL INFORMATION**

We do not charge or solicit pre-payment of more than \$1,200 in fees per client six months or more in advance. We have never filed for bankruptcy and are not aware of any financial conditions that are reasonably likely to impair our ability to meet our contractual obligations to clients.

## **ITEM 19: REQUIREMENTS FOR STATE-REGISTERED ADVISERS**

Not Applicable.