

# IS YOUR PORTFOLIO WAVING RED FLAGS?


Financial statements could be considered the ultimate language of business and investing. Unfortunately, some companies have used “red flag” tactics such as aggressive accounting to make their financial statements appear significantly better than the current state of their underlying business. This distortion can potentially put investors at risk.

Forensic accounting attempts to pull back the curtain on these tactics and assess the true health of an underlying business. In doing so, financial red flags and high quality financial statements may be identified from stock to stock. This valuable information can be used to potentially avoid certain stocks and highlight those with high quality earnings.

The **Forensic Accounting ETF (FLAG)** seeks to track the DelVecchio Earnings Quality Index. This index performs a forensic accounting analysis of the 500 largest U.S. stocks and selects holdings based on the results of the analysis.

## THE 5 STEP INVESTMENT APPROACH:

- 1. DEFINE:** Universe consists of the 500 largest capitalized US stocks.
- 2. ANALYZE:** Perform a forensic accounting analysis of each stock’s key financial statements: the balance sheet, cash flow statement, and income statement as prioritized in the graphic to the right.
- 3. GRADE:** Each stock receives an overall grade of “A-F”.
- 4. AVOID:** Firms receiving a grade of “F” are avoided due to red flag risk.
- 5. INVEST:** The remaining companies comprise index. Companies graded “A” make up 40% of the portfolio while all other grades make up 20% of the portfolio respectively.

INCOME STATEMENT		Most Critical  Least Critical
METRIC	CONCERN	
Revenue	Aggressive Revenue Recognition	
Cost of Goods Sold	Inventory Issues	
Gross Profit	Reserve Concerns	
Operating Expenses Research & Development Sales, General & Administrative	Large Changes	
Operating Income	Large Changes	
Taxes	Tax Issues	
Net Income		

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## POTENTIAL INVESTOR BENEFITS FOR FLAG INVESTORS

Discipline	Risk Mitigation	Diversification
A rule-based index methodology eliminates emotion	May reduce the risk of financial fraud in the underlying securities comprising the ETF	May reduce overall portfolio investment risk due to unique investment approach, number of securities and sectors

## POTENTIAL USES OF FLAG WITHIN A PORTFOLIO

- ❏ An alternative approach to short selling stocks with financial red flags.
- ❏ A complement to existing equity positions not incorporating forensic accounting analysis.
- ❏ A replacement for equity funds without a stated risk reduction bias.

***Carefully consider the Fund's investment objectives, risk factors, charges and expenses before investing. This and additional information can be found in the Fund's prospectus, which may be obtained by visiting [www.flagetf.com](http://www.flagetf.com). Read the prospectus carefully before investing.***

Investing involves risk, including the possible loss of principal. The Index may include REITs. Adverse economic, business or political developments affecting real estate could have a major effect on the value of the Fund's investments in REITs. Investing in REITs may subject the Fund to risks associated with the direct ownership of real estate, such as decreases in real estate values, overbuilding, increased competition and other risks related to local or general economic conditions, increases in operating costs and property taxes, changes in zoning laws, casualty or condemnation losses, possible environmental liabilities, regulatory limitations on rent and fluctuations in rental income. In addition, REITs are subject to the possibility of failing to qualify for tax-free pass-through of income under the Internal Revenue Code and maintaining exemption from the registration requirements of the Investment Company Act of 1940, as amended. There is no guarantee that the Fund or the index will achieve its investment objective.

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