

DIAMOND HILL INVESTMENT GROUP INC

Form 10-Q

May 08, 2009

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**U.S. Securities and Exchange Commission**  
**Washington, D.C. 20549**  
**Form 10-Q**  
**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE**  
**SECURITIES EXCHANGE ACT OF 1934**  
**For the quarterly period ended March 31, 2009**  
**Commission file number 000-24498**  
**DIAMOND HILL INVESTMENT GROUP, INC.**  
(Exact name of registrant as specified in its charter)

Ohio

65-0190407

(State of incorporation)

(I.R.S. Employer Identification No.)

325 John H. McConnell Blvd, Suite 200, Columbus, Ohio 43215

(Address, including Zip Code, of principal executive offices)

(614) 255-3333

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. Yes:  No:

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes:  No:

The number of shares outstanding of the issuer's common stock, as of the latest practicable date, May 8, 2009 is 2,595,158 shares.

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**Table of Contents****PART I: FINANCIAL INFORMATION****ITEM 1: Consolidated Financial Statements****Diamond Hill Investment Group, Inc.****Consolidated Balance Sheets**

	3/31/2009 (Unaudited)	12/31/2008
<b>ASSETS</b>		
Cash and cash equivalents	\$ 10,523,583	\$ 15,788,560
Investment portfolio	18,025,958	17,185,611
Accounts receivable	4,656,082	5,339,558
Prepaid expenses	682,753	1,067,388
Fixed assets, net of depreciation, and other assets	972,816	835,314
Income tax receivable	1,051,811	2,334,836
Deferred taxes	3,210,921	1,989,016
Total assets	\$ 39,123,924	\$ 44,540,283
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Liabilities		
Accounts payable and accrued expenses	\$ 1,034,472	\$ 1,294,396
Accrued incentive compensation	1,760,000	13,000,000
Total liabilities	2,794,472	14,294,396
Commitments and contingencies		
Shareholders' Equity		
Common stock, no par value		
7,000,000 shares authorized;		
2,593,762 issued and outstanding at March 31, 2009;		
2,447,299 issued and outstanding at December 31, 2008	21,939,138	16,233,501
Preferred stock, undesignated, 1,000,000 shares authorized and unissued		
Deferred compensation	(4,881,658)	(4,908,215)
Retained earnings	19,271,972	18,920,601
Total shareholders' equity	36,329,452	30,245,887
Total liabilities and shareholders' equity	\$ 39,123,924	\$ 44,540,283

See notes to consolidated financial statements.



**Table of Contents****Diamond Hill Investment Group, Inc.  
Consolidated Statements of Income (unaudited)**

	Three Months Ended March 31,	
	2009	2008
<b>REVENUES:</b>		
Investment advisory	\$ 7,788,943	\$ 9,512,895
Mutual fund administration, net	1,094,531	1,390,329
Total revenue	8,883,474	10,903,224
<b>OPERATING EXPENSES:</b>		
Compensation and related costs	5,138,095	5,841,754
General and administrative	646,180	557,148
Sales and marketing	145,588	114,030
Third party distribution	248,670	396,105
Mutual fund administration	577,185	468,615
Total operating expenses	6,755,718	7,377,652
<b>NET OPERATING INCOME</b>	2,127,756	3,525,572
Investment return	(1,578,852)	(374,664)
<b>INCOME BEFORE TAXES</b>	548,904	3,150,908
Income tax provision	(197,533)	(1,165,219)
<b>NET INCOME</b>	\$ 351,371	\$ 1,985,689
Earnings per share		
Basic	\$ 0.14	\$ 0.85
Diluted	\$ 0.14	\$ 0.82
Weighted average shares outstanding		
Basic	2,508,451	2,337,706
Diluted	2,515,633	2,426,400

See notes to consolidated financial statements.

**Table of Contents****Diamond Hill Investment Group, Inc.  
Consolidated Statements of Cash Flow (unaudited)**

	Three Months Ended March 31,	
	2009	2008
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net Income	\$ 351,371	\$ 1,985,689
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation on furniture and equipment	51,258	38,465
Amortization of deferred compensation	452,499	559,538
(Increase) decrease in accounts receivable	683,476	(688,653)
Change in deferred taxes	(1,232,325)	1,091,993
Stock option expense		1,340
Noncash director fee expense	150,062	
Investment gain/loss, net	4,580,382	834,487
(Decrease) in accrued liabilities	(6,647,708)	(2,993,296)
Other changes in assets and liabilities	1,792,594	55,699
Net cash provided by operating activities	181,609	885,262
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchase of property and equipment	(188,761)	(194,502)
Cost of investments purchased and other portfolio activity	(10,881,666)	(333,610)
Proceeds from sale of investments	5,460,937	
Net cash (used in) investing activities	(5,609,490)	(528,112)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Payment for repurchase of common shares		(116,896)
Payment of taxes withheld on employee stock transactions	(23,471)	(131,800)
Proceeds from common stock issuance	186,375	404,341
Net cash provided by financing activities	162,904	155,645
<b>CASH AND CASH EQUIVALENTS</b>		
Net change during the period	(5,264,977)	512,795
At beginning of period	15,788,560	11,783,278
At end of period	\$ 10,523,583	\$ 12,296,073
Cash paid during the period for:		
Interest		
Income taxes		



Noncash Transactions during the period for:

Common Stock Issued as Incentive Compensation

4,852,216

5,754,140

See notes to consolidated financial statements.

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**Diamond Hill Investment Group, Inc.**

**Notes to Consolidated Financial Statements (unaudited)**

Note 1 Organization

Diamond Hill Investment Group, Inc. (the Company) was incorporated as a Florida corporation in April 1990 and in May 2002 reincorporated in Ohio, the Company's principal place of business. The Company has four operating subsidiaries.

Diamond Hill Capital Management, Inc. (DHCM), an Ohio corporation, is a wholly owned subsidiary of the Company and a registered investment advisor. DHCM is the investment adviser to the Diamond Hill Funds (the Funds), a series of open-end mutual funds, private investment funds (Private Funds), and also offers advisory services to institutional and individual investors.

Diamond Hill GP (Cayman) Ltd. (DHGP) was incorporated in the Cayman Islands as an exempted company on May 18, 2006 for the purpose of acting as the general partner of a Cayman Islands exempted limited partnership. This partnership acts as a master fund for Diamond Hill Offshore Ltd., a Cayman Islands exempted company; and Diamond Hill Investment Partners II, L.P., an Ohio limited partnership. Diamond Hill GP (Cayman) Ltd. has no operating activity.

Beacon Hill Fund Services, Inc. (BHFS), an Ohio corporation, is a wholly owned subsidiary of the Company incorporated on January 29, 2008. BHFS provides certain compliance, treasury, and fund administration services to small to mid size mutual funds.

BHIL Distributors, Inc. (BHIL), an Ohio corporation, is a wholly owned subsidiary of BHFS incorporated on February 19, 2008. BHIL will provide underwriting and distribution services to small to mid size mutual funds.

Note 2 Significant Accounting Policies

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenues and expenses for the periods. Actual results could differ from those estimates. The following is a summary of the Company's significant accounting policies:

Principles of Consolidation

The accompanying consolidated financial statements include the operations of the Company and its subsidiaries. All material inter-company transactions and balances have been eliminated in consolidation.

Segment Information

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, establishes disclosure requirements relating to operating segments in annual and interim financial statements. Management has determined that the Company operates principally in one business segment, namely as an investment adviser and administrator to mutual funds, separate accounts, and private investment funds.

Cash and Cash Equivalents

Cash and cash equivalents include demand deposits and money market funds.

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Note 2 **Significant Accounting Policies (Continued)**

**Accounts Receivable**

Accounts receivable are recorded when they are due and are presented in the balance sheet, net of any allowance for doubtful accounts. Accounts receivable are written off when they are determined to be uncollectible. Any allowance for doubtful accounts is estimated based on the Company's historical losses, existing conditions in the industry, and the financial stability of those individuals or entities that owe the receivable. No allowance for doubtful accounts was deemed necessary at March 31, 2009 or December 31, 2008.

**Valuation of Investment Portfolio**

Under Statement of Financial Accounting Standards No. 157 – Fair Value Measurements ( SFAS 157 ), investments held by the Company are valued based upon the definition of Level 1 inputs and Level 2 inputs. In general, SFAS 157 defines Level 1 inputs, as fair values which use quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 inputs are defined as quoted prices in markets that are not considered to be active for identical assets or liabilities, quoted prices in active markets for similar assets or liabilities and inputs other than quoted prices that are directly observable or indirectly through corroboration with observable market data. \$2,824,710 and \$15,201,248 in Company investments are valued based upon Level 1 and Level 2 inputs, respectively. The changes in market values on the investments are recorded in the Consolidated Statement of Income as investment returns.

**Limited Partnership Interests**

DHCM is the managing member of Diamond Hill General Partner, LLC, the General Partner of Diamond Hill Investment Partners, LP ( DHIP ), Diamond Hill Investment Partners II, LP ( DHIP II ), and Diamond Hill Research Partners, LP ( DHRP ), collectively (the Partnerships ), each a limited partnership whose underlying assets consist of marketable securities. DHCM in its role as the managing member of the General Partner exerts significant influence over the financial and operating policies of the Partnerships but does not exercise control. Therefore, DHCM's investment in the Partnerships is accounted for using the equity method, under which DHCM's share of the net earnings or losses from the partnership is reflected in income as earned, and distributions received are reflected as reductions from the investment. Several board members, officers and employees of the Company invest in the Partnerships through Diamond Hill General Partner, LLC. These individuals receive no remuneration as a result of their personal investment in the Partnerships. The capital of Diamond Hill General Partner, LLC is not subject to a management fee or an incentive fee.

**Furniture and Equipment**

Furniture and equipment, consisting of computer equipment, furniture, and fixtures, are carried at cost less accumulated depreciation. Depreciation is calculated using the straight-line method over estimated lives of three to seven years.

**Revenue Recognition – General**

The Company earns substantially all of its revenue from investment advisory and fund administration services. Mutual fund investment advisory and administration fees, calculated as a percentage of assets under management, are recorded as revenue as services are performed. Managed account and private investment fund clients provide for monthly or quarterly management fees, in addition to quarterly or annual performance fees.

**Table of Contents**Note 2 Significant Accounting Policies (Continued)Revenue Recognition Performance Incentive Revenue

The Company's private investment funds and certain managed accounts provide for performance incentive fees. EITF Abstract Topic No. D-96, Accounting for Management Fees Based on a Formula, identifies two methods by which incentive revenue may be recorded. Under Method 1, incentive fees are recorded at the end of the contract period; under Method 2, the incentive fees are recorded periodically and calculated as the amount that would be due under the formula at any point in time as if the contract was terminated at that date. Management has chosen Method 1, in which incentive fees are recorded at the end of the contract period for the specific client in which the incentive fee applies. The table below shows assets under management (AUM) subject to performance incentive fees and the performance incentive fees as calculated under each of the above methods:

	As Of March 31,	
	2009	2008
AUM Contractual Period Ends Quarterly	\$ 84,077,397	\$ 284,542,311
AUM Contractual Period Ends Annually	143,724,736	376,395,460
Total AUM Subject to Performance Incentive	\$ 227,802,133	\$ 660,937,771

	For The Three Months Ending March 31,	
	2009	2008
Performance Incentive Fees Method 1	\$ 4,645	\$ 280,900
Performance Incentive Fees Method 2	\$ 4,645	\$ 280,900

Amounts under Method 1 and Method 2 may differ throughout the year, but will generally be the same at fiscal year end because all client account contract periods end on December 31.

Revenue Recognition Mutual Fund Administration

DHCM has an administrative and transfer agency services agreement with the Diamond Hill Funds (Funds), under which DHCM performs certain services for each fund. These services include mutual fund administration, transfer agency and other related functions. For performing these services, each fund compensates DHCM a fee at an annual rate of 0.30% for Class A and Class C shares and 0.18% for Class I shares times each series' average daily net assets. Effective April 30, 2008, the fee for administrative services was reduced from 0.32% to 0.30% for Class A and Class C shares. The Funds have selected and contractually engaged certain vendors to fulfill various services to benefit the Funds' shareholders or to satisfy regulatory requirements of the Funds. These services include, among others, required fund shareholder mailings, registration fees, legal and audit fees. DHCM, in fulfilling a portion of its role under the administration agreement with the Funds, acts as agent to pay these obligations of the Funds. Each vendor is independently responsible for fulfillment of the services it has been engaged to provide and negotiates fees and terms with the management and board of trustees of the Funds. The fee that the Funds pay to DHCM is reviewed annually by the Funds' board of trustees and specifically takes into account the contractual expenses that DHCM pays on behalf of the Funds. As a result, DHCM is not involved in the delivery or pricing of these services and bears no risk related to these services. Consistent with EITF 99-19, revenue has been recorded net of these Fund expenses. In addition, DHCM finances the up-front commissions which are paid by the Fund's principal underwriter to brokers who sell C shares of the Funds. As financier, DHCM advances to the underwriter the commission amount to be paid to the selling broker at the time of sale. These advances are capitalized and amortized over 12 months to correspond with the re-payments DHCM receives from the principal underwriter to recoup this commission advancement. Mutual fund administration (admin) gross and net revenue are summarized below:



**Table of Contents**Note 2 Significant Accounting Policies (Continued)Revenue Recognition – Mutual Fund Administration (Continued)

	Three Months Ended March 31,	
	2009	2008
Mutual fund admin revenue, gross	\$ 1,846,223	\$ 2,044,549
Mutual fund admin, fund related expense	715,552	661,038
Mutual fund admin revenue, net of fund related expenses	1,130,671	1,383,511
C-Share broker commission advance repayments	347,453	398,947
C-Share broker commission amortization	383,593	392,129
C-Share financing activity, net	(36,140)	6,818
Mutual fund administration revenue, net	\$ 1,094,531	\$ 1,390,329

Third Party Distribution Expense

Third party distribution expenses are earned by various third party financial services firms based on sales and/or assets of the Company's investment products generated by the respective firm. Expenses recognized represent actual payments made to the third party firms and are recorded in the period earned based on the terms of the various contracts.

Income Taxes

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 109 Accounting for Income Taxes ( SFAS 109 ). A net deferred tax asset or liability is determined based on the tax effects of the various temporary differences between the book and tax bases of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws.

Effective January 1, 2007, the Company adopted the provisions of FASB Interpretation No. 48 Accounting for the Uncertainty in Income Taxes ( FIN 48 ), an interpretation of SFAS 109. As a result of the implementation of FIN 48, the Company has analyzed its tax positions taken on federal income tax returns for all open tax years (tax years ended December 31, 2005 through 2008) and has recognized no adjustment in the net liability.

Earnings Per Share

Basic earnings per share ( EPS ) excludes dilution and is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution of EPS that could occur if options, warrants, and restricted stock units to issue common stock were exercised.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current period financial presentation.

**Table of Contents**Note 3 Investment Portfolio

As of March 31, 2009, the Company held investments worth \$18 million and a cost basis of \$22.7 million. The following table summarizes the market value of these investments as of March 31, 2009 and December 31, 2008:

	March 31, 2009	December 31, 2008
Diamond Hill Small Cap Fund	\$ 472,812	\$
Diamond Hill Small-Mid Cap Fund	473,118	
Diamond Hill Large Cap Fund	463,892	
Diamond Hill Select Fund	464,789	
Diamond Hill Long-Short Fund	467,110	
Diamond Hill Strategic Income Fund	482,989	
Diamond Hill Investment Partners, L.P.	6,864,427	7,494,929
Diamond Hill Investment Partners II, L.P.	3,411,821	3,767,480
Diamond Hill Research Partners, L.P.	4,925,000	
Other marketable equity securities		5,923,202
<b>Total Investment Portfolio</b>	<b>\$ 18,025,958</b>	<b>\$ 17,185,611</b>

DHCM is the managing member of the Diamond Hill General Partner LLC, which is the General Partner of the Partnerships. The underlying assets of the Partnerships are cash and marketable equity securities. The Company, as the parent entity to DHCM, is not contingently liable for the Partnership's liabilities but rather is only liable for its proportionate share, based on its membership interest. DHCM, as the managing member of the General Partner, is also not contingently liable for the Partnership's liabilities. Summary financial information, including the Company's carrying value and income from the Partnerships is as follows:

	March 31, 2009	December 31, 2008
Total partnership assets	\$ 175,092,093	\$ 196,021,226
Total partnership liabilities	23,067,642	33,056,747
Net partnership assets	152,024,451	162,964,479
Net partnership loss	(14,365,968)	(75,625,562)
DHCM's portion of net assets	15,201,248	11,262,409
DHCM's portion of net loss	(956,160)	(3,866,314)

DHCM's income from the Partnerships includes its pro-rata capital allocation and its share of an incentive allocation, if any, from the limited partners.

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Note 4 Capital Stock

Common Shares

The Company has only one class of securities, Common Shares.

Authorization of Preferred Shares

The Company's Articles of Incorporation authorize the issuance of 1,000,000 shares of blank check preferred shares with such designations, rights and preferences, as may be determined from time to time by the Company's Board of Directors. The Board of Directors is empowered, without shareholder approval, to issue preferred stock with dividend, liquidation, conversion, voting, or other rights, which could adversely affect the voting or other rights of the holders of the Common Shares. There were no shares of preferred stock issued or outstanding at March 31, 2009 or December 31, 2008.

Note 5 Stock-Based Compensation

Equity Incentive Plans

*2005 Employee and Director Equity Incentive Plan*

At the Company's annual shareholder meeting on May 12, 2005, shareholders approved the 2005 Employee and Director Equity Incentive Plan ( 2005 Plan ). The 2005 Plan is intended to facilitate the Company's ability to attract and retain staff, provide additional incentive to employees, directors and consultants, and to promote the success of the Company's business. The Plan authorizes the issuance of Common Shares of the Company in various forms of stock or option grants. As of March 31, 2009 shares available for issuance under the Plan are 366,970. The Plan provides that the Board of Directors, or a committee appointed by the Board, may grant awards and otherwise administer the Plan. Restricted stock grants issued under the plan which vest over time, are recorded as deferred compensation on grant date and then recognized as compensation expense over the vesting period of the respective grant.

Equity Compensation Grants

On May 13, 2004 the Company's shareholders approved terms and conditions of certain equity compensation grants to three key employees. Under the approved terms, a total of 75,000 shares of restricted stock and restricted stock units were issued to the key employees on May 31, 2004. These shares vested on October 3, 2008.

*Accelerated Vesting of Certain Equity Incentive Plans and Compensation Grants*

The board of directors of the Company approved the accelerated vesting of 82,064 shares of restricted stock from various vesting dates during the first five months of 2009 to October 3, 2008. This acceleration resulted in additional compensation expense of \$1.0 million in the fourth quarter of 2008 that otherwise would have been recorded in the first and second quarters of 2009. In addition, as a result of this acceleration, the Company received a \$6.3 million tax deduction in 2008.



**Table of Contents****Note 5 Stock-Based Compensation (Continued)****401(k) Plan**

The Company sponsors a 401(k) plan whereby all employees participate in the plan. Employees may contribute a portion of their compensation subject to certain limits based on federal tax laws. The Company makes matching contributions of Common Shares of the Company with a value equal to 200 percent of the first six percent of an employee's compensation contributed to the plan. Employees become fully vested in the matching contributions after six plan years of employment. For the three months ended March 31, 2009 and 2008, expenses attributable to the plan were \$186,424 and \$138,342 respectively.

**Stock Options and Warrants**

Effective October 1, 2005, the Company adopted SFAS No. 123(R), Accounting for Stock-Based Compensation (SFAS 123R). SFAS 123R requires all share-based payments to employees and directors, including grants of stock options, to be recognized as expense in the income statement based on their fair values. The amount of compensation is measured at the fair value of the options when granted, and this cost is expensed over the required service period, which is normally the vesting period of the options. SFAS 123R applies to the Company for options granted or modified after October 1, 2005. SFAS 123R also requires compensation cost to be recorded for prior option grants that vest after the date of adoption.

Stock option and warrant transactions under the various plans are summarized below:

	Options		Warrants	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding December 31, 2007	92,500	\$ 10.40	25,400	\$ 47.00
Exercisable December 31, 2007	72,500	\$ 12.03	25,400	\$ 47.00
Granted				
Expired / Forfeited				
Exercised	17,500	11.81	1,000	22.50
Outstanding March 31, 2008	75,000	\$ 10.08	24,400	\$ 48.07
Exercisable March 31, 2008	55,000	\$ 12.10	24,400	\$ 48.07
Outstanding December 31, 2008		\$	10,000	\$ 13.00
Exercisable December 31, 2008		\$	10,000	\$ 13.00
Granted				
Expired / Forfeited				
Exercised				
Outstanding March 31, 2009		\$	10,000	\$ 13.00
Exercisable March 31, 2009		\$	10,000	\$ 13.00

The Company did not withhold any shares from issuing during the period ended, March 31, 2009, as no warrants or options were exercised. The Company withheld from issuing 352 of the 18,500 shares of warrants and options exercised during the period ended March 31, 2008. These shares were withheld to fulfill tax withholding requirements related to employee compensation earned on the exercises.



**Table of Contents**Note 5 Stock-Based Compensation (Continued)Stock Options and Warrants (Continued)

Options and warrants outstanding and exercisable at March 31, 2009 are as follows:

Number Outstanding	Remaining Life In Years	Warrants		Exercise Price
		Number Exercisable		
2,000	0.12	2,000		22.50
6,000	0.92	6,000		11.25
2,000	1.11	2,000		8.75
10,000	0.80	10,000		

The aggregate intrinsic value of options/warrants outstanding and exercisable as of March 31, 2009 is \$263,200.

Note 6 Operating Leases

The Company leases approximately 14,200 square feet of office space at its principal office under an operating lease agreement which terminates on July 31, 2013. In addition, the Company leases approximately 2,200 square feet of office space for a subsidiary company under an operating lease agreement which terminates on February 28, 2011. Total lease and operating expenses for the three months ended March 31, 2009 and 2008 were \$105,726 and \$93,961, respectively. The approximate future minimum lease payments under the operating lease are as follows:

2009	2010	2011	2012	2013
\$ 196,000	\$ 267,000	\$ 249,000	\$ 254,000	\$ 130,000

In addition to the above rent, the Company will also be responsible for normal operating expenses of the properties. Such operating expenses were approximately \$8.90 per square foot in 2008 and are expected to be approximately \$9.59 per square foot in 2009 on a combined basis.

Note 7 Income Taxes

The provision for income taxes for the three months ended March 31, 2009 and 2008 consists of federal, state and city income taxes. As of December 31, 2008, the Company and its subsidiaries had a capital loss carry forward for tax purposes of approximately \$3,476,000. The capital loss carryforward is available to offset capital gains in future years.

Tax Impact of Stock Option and Warrant Exercises

For the three months ended March 31, 2009, the Company received federal tax benefits of \$114,513 from the vesting of restricted stock grants and the disqualifying sale related to incentive stock options, which resulted in an increase to equity during the period. For the year ended December 31, 2008, the Company received federal tax benefits from the exercise of stock-based compensation of \$3,805,977, which resulted in an increase to equity.

**Table of Contents**Note 8 Earnings Per Share

The following table sets for the computation for basic and diluted earnings per share (EPS):

	Three Months Ended March 31,	
	2009	2008
Basic and Diluted net income	\$ 351,371	\$ 1,985,689
Weighted average number of outstanding shares		
Basic	2,508,451	2,337,706
Diluted	2,515,633	2,426,400
Earnings per share		
Basic	\$ 0.14	\$ 0.85
Diluted	\$ 0.14	\$ 0.82

Note 9 Commitments and Contingencies

The Company indemnifies its directors and certain of its officers and employees for certain liabilities that might arise from their performance of their duties to the Company. Additionally, in the normal course of business, the Company enters into agreements that contain a variety of representations and warranties and which provide general indemnifications. Certain agreements do not contain any limits on the Company's liability and would involve future claims that may be made against the Company that have not yet occurred. Therefore, it is not possible to estimate the Company's potential liability under these indemnities. Further, the Company maintains insurance policies that may provide coverage against certain claims under these indemnities.

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DIAMOND HILL INVESTMENT GROUP, INC.

**ITEM 2: Management's Discussion and Analysis of Financial Condition and Results of Operations**

**Forward-looking Statements**

Throughout this Form 10-Q, the Company may make forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 relating to such matters as anticipated operating results, prospects for achieving the critical threshold of assets under management, technological developments, economic trends (including interest rates and market volatility), expected transactions and acquisitions and similar matters. The words believe, expect, anticipate, estimate, should, seek, plan, intend and similar identify forward-looking statements that speak only as of the date thereof. While the Company believes that the assumptions underlying its forward-looking statements are reasonable, investors are cautioned that any of the assumptions could prove to be inaccurate and accordingly, the actual results and experiences of the Company could differ materially from the anticipated results or other expectations expressed by the Company in its forward-looking statements. Factors that could cause such actual results or experiences to differ from results discussed in the forward-looking statements include, but are not limited to: the adverse effect from a decline in the securities markets; a decline in the performance of the Company's products; changes in interest rates; a general or prolonged downturn in the economy; changes in government policy and regulation, including monetary policy; changes in the Company's ability to attract or retain key employees; unforeseen costs and other effects related to legal proceedings or investigations of governmental and self-regulatory organizations; and other risks identified from time-to-time in the Company's other public documents on file with the SEC.

**General**

Diamond Hill Investment Group, Inc. (the Company), an Ohio corporation organized in 1990, derives its consolidated revenue and net income from investment advisory and fund administration services provided by its subsidiary Diamond Hill Capital Management, Inc. (DHCM). DHCM is a registered investment adviser under the Investment Advisers Act of 1940 providing investment advisory services to individuals and institutional investors through the Diamond Hill sponsored mutual funds, separate accounts, and private investment funds (generally known as hedge funds). The Company was first incorporated in April 1990. During the first quarter of 2008, the Company incorporated two new subsidiaries, Beacon Hill Fund Services, Inc. (BHFS) and BHIL Distributors, Inc. (BHIL) to collectively operate as Beacon Hill. Beacon Hill will provide certain fund administration services and distribution services to small to mid size mutual funds, including Diamond Hill Funds.

In this section, the company discusses and analyzes the consolidated results of operations for the three month periods ending March, 2009 and 2008 and other factors that may affect future financial performance. This discussion should be read in conjunction with the Consolidated Financial Statements, Notes to the Consolidated Financial Statements, and Selected Financial Data.

The Company's revenue is derived primarily from investment advisory and administration fees received from Diamond Hill Funds and investment advisory fees received from separate accounts and private investment funds. Investment advisory and administration fees paid to the Company are based primarily on the value of the investment portfolios managed by the Company and fluctuate with changes in the total value of the assets under management. Such fees are recognized in the period that the Company manages these assets. The Company can also earn performance incentive fees which are generally 20% annually on the amount of client investment performance in excess of a certain annual return hurdle. Because performance incentive fees are based primarily on the performance of client accounts, they will be volatile from period to period. The Company's major expense is employee compensation and benefits.

**Table of Contents****Assets Under Management**

As of March 31, 2009, assets under management ( AUM ) totaled \$3.9 billion, a 16% decrease in comparison to March 31, 2008. Revenues are highly dependent on both the value and composition of AUM. The following is a summary of the firm's AUM by product and objective as of March 31, 2009 and 2008 and a roll-forward of AUM activity for the three months ended March, 31 2009 and 2008:

<b>Assets Under Management by Product</b>			
<b>As of March 31,</b>			
(in millions)	<b>2009</b>	<b>2008</b>	<b>% Change</b>
Mutual funds	\$ 2,643	\$ 3,152	-16%
Separate accounts	1,063	1,032	3%
Private investment funds	203	481	-58%
<b>Total</b>	<b>\$ 3,909</b>	<b>\$ 4,665</b>	<b>-16%</b>

<b>Assets Under Management by Objective</b>			
<b>As of March 31,</b>			
(in millions)	<b>2009</b>	<b>2008</b>	<b>% Change</b>
Small and Small-Mid Cap	\$ 445	\$ 566	-21%
Large Cap and Select	1,418	1,036	37%
Long-Short	1,930	2,799	-31%
Strategic and fixed income	116	264	-56%
<b>Total</b>	<b>\$ 3,909</b>	<b>\$ 4,665</b>	<b>-16%</b>

<b>Change in Assets Under Management</b>			
<b>For the Three Months Ended March 31,</b>			
(in millions)	<b>2009</b>	<b>2008</b>	
AUM at beginning of the period	\$ 4,510	\$ 4,403	
Net cash inflows (outflows)			
mutual funds	(138)	309	
separate accounts	39	74	
private investment funds	3	(13)	
	(96)	370	
Net market appreciation (depreciation) and income	(505)	(108)	
Increase (decrease) during the period	(601)	262	
AUM at end of the period	\$ 3,909	\$ 4,665	

**Consolidated Results of Operations**

The following is a discussion of the consolidated results of operations of the Company and its revenues and expenses.

<b>Three Months Ended March 31,</b>		
<b>2009</b>	<b>2008</b>	<b>% Change</b>

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Net income (in thousands)	\$	351	\$	1,986	-82%
Net income per share					
Basic	\$	0.14	\$	0.85	-84%
Diluted	\$	0.14	\$	0.82	-83%
Weighted average shares outstanding (in thousands)					
Basic		2,508		2,338	
Diluted		2,516		2,426	

**Table of Contents****Three Months Ended March 31, 2009 compared with Three Months Ended March 31, 2008**

The Company generated net income of \$351,371, \$0.14 per diluted share, for the three months ended March 31, 2009, compared with net income of \$1,985,689, \$0.82 per diluted share, for the three months ended March 31, 2008. Net income decreased 82% despite a 16% decrease in AUM due to a negative return on the Company's corporate investment portfolio and the loss from Beacon Hill of approximately \$381 thousand.

**Revenue**

(in Thousands)	Three Months Ended March 31,		% Change
	2009	2008	
Investment advisory	\$ 7,789	\$ 9,513	-18%
Mutual fund administration, net	1,094	1,390	-21%
Total	\$ 8,883	\$ 10,903	-19%

As a percent of total first quarter 2009 revenues, investment advisory fees accounted for 88% and mutual fund administration fees accounted for the remaining 12% compared to the first quarter of 2008 where investment advisory fees accounted for 87% and mutual fund administration fees accounted for the remaining 13% of revenues.

**Investment Advisory Fees.** The overall decrease in investment advisory fees was primarily due to a decrease in AUM of just over \$756 million period over period. Investment advisory fees are calculated as a percent of average net assets under management at various levels depending on the investment product. The Company's average advisory fee rate for the three months ended March 31, 2009 was 0.76% compared to 0.82% for the three months ended March 31, 2008. During 2008, the Diamond Hill Long-Short Fund, which has a 0.90% advisory fee, was closed to new investors and effective December 31, 2008, it was reopened to new investors. As a result, there was a decrease in the cash flows into that Fund during the second half of 2008. In addition, there were cash outflows from the Long-Short Fund during the first quarter of 2009 resulting in a decrease in assets for that Fund of 18%. These factors contributed to the decrease in the average advisory fee rate for first quarter 2009 compared to first quarter 2008.

**Mutual Fund Administration Fees.** Mutual fund administration fees are calculated as a percent of average net assets under administration in the Diamond Hill Funds. The Company earns 0.30% on Class A and Class C shares and 0.18% on Class I shares. As assets in the Funds have grown the Company has realized certain economies of scale; and as a result, the Company has lowered its administration fees each of the last four years to pass on those economies of scale to fund shareholders. Given the decrease in mutual fund AUM from March 31, 2008 to March 31, 2009, effective April 30, 2009, the Company has increased its fees to 0.34% for Class A and Class C shares and to 0.20% for Class I shares. Due to a combination of fee changes and a reduction in mutual fund AUM, fund administration revenues decreased by \$296 thousand for the quarter ended March 31, 2009 compared to the quarter ended March 31, 2008.

**Expenses**

(in Thousands)	Three Months Ended March 31,		% Change
	2009	2008	
Compensation and related costs	\$ 5,138	\$ 5,842	-12%
General and administrative	646	557	16%
Sales and marketing	146	114	28%
Third party distribution	249	396	-37%
Mutual fund administration	577	469	23%



Total	\$	6,756	\$	7,378	-8%
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**Compensation and Related Costs.** Compensation expense decreased by \$704 thousand, or 12%, during the three months ended March 31, 2009 over the same period a year ago, reflecting increase in employee headcount, base salaries and related benefits offset by a lower incentive compensation accrual. Base salaries and related benefits increased by \$525,695, or 20% reflecting an increase in staffing from 47 to 57 employees. Incentive compensation decreased by \$1,384,400, or 44% reflecting a decrease in both revenue and operating income in the current fiscal year.

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**General and Administrative.** General and administrative expenses increased by \$89,000 or 16%, period over period. Despite a decrease in overall AUM, the Company has grown its separate account business and the general and administrative expense increase is primarily in support of that growth.

**Sales and Marketing.** Sales and marketing expenses increased by \$32,000 or 28%. This increase was primarily due to an increase in travel and other marketing expenses related to new business growth.

**Third Party Distribution.** Third party distribution expense represents payments made to intermediaries related to sales of the Company's investment products. The expense is directly correlated with investments in the Company's private investment funds. The period over period increase or decrease directly corresponds to the increase or decrease in investment advisory fees earned by the Company.

**Mutual Fund Administration.** Mutual fund administration expense increased by \$108 thousand or 23% period over period. The majority of mutual fund administration fees are variable based on the amount of mutual fund AUM. Despite the decrease in mutual fund AUM by \$509 million, or 16%, during first quarter 2009, mutual fund administration expenses increased related to a fee increase by the sub-administrator and timing difference of certain other administration expenses.

**Beacon Hill Fund Services**

Through the first three months of 2009, Beacon Hill generated a pre-tax loss of \$381 thousand on \$103 thousand in revenue. This compares to a loss of \$191 thousand on zero revenue during the first three months of 2008. Beacon Hill is currently staffed with eight experienced professionals, recently received approval for membership in FINRA as a limited purpose broker/dealer. Beacon Hill has been actively marketing its services and has commitments from several clients to commence services at various starting dates throughout 2009. These commitments are annually recurring engagements; however, there is no guarantee that the associated revenue will be realized. The company continues to believe that Beacon Hill will achieve a run rate breakeven by the end of 2009.

**Liquidity and Capital Resources**

The Company's entire investment portfolio is in liquid readily marketable securities, which provide for cash liquidity, if needed, within three business days. Investments in mutual funds are valued at their current net asset value. Investments in private investment funds and other equity securities are valued based on readily available market quotations. Inflation is expected to have no material impact on the Company's performance.

As of March 31, 2009, the Company had working capital of approximately \$30.4 million compared to \$24.1 million at December 31, 2008. Working capital includes cash, securities owned and accounts receivable, net of all liabilities. The Company has no debt and its available working capital is expected to be sufficient to cover current expenses. The Company does not expect any material capital expenditures during 2009.

During the third quarter of 2007 the board of directors authorized management to repurchase up to 350,000 shares of the Company's common stock. Management and the board believe that the most appropriate use for excess cash is to invest in Diamond Hill investment strategies or repurchase the Company's common stock. The deciding factor will be which alternative offers the most favorable risk-adjusted rate of return in the opinion of management and the board.

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**Off-Balance Sheet Arrangements**

The Company has no off-balance sheet arrangements with any obligation under a guarantee contract, or a retained or contingent interest in assets or similar arrangement that serves as credit, liquidity or market risk support for such assets, or any other obligation, including a contingent obligation, under a contract that would be accounted for as a derivative instrument or arising out of a variable interest.

**Critical Accounting Policies and Estimates**

There have been no material changes to the Critical Accounting Policies and Estimates provided in Item 7 of the Form 10-K Annual Report for 2008.

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DIAMOND HILL INVESTMENT GROUP, INC.

**ITEM 3: Quantitative and Qualitative Disclosures About Market Risk**

There has been no material change in the information provided in Item 7A of the Form 10-K Annual Report for 2008.

**ITEM 4: Controls and Procedures**

Management, including the Chief Executive Officer and the Chief Financial Officer, has conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) of the Securities Exchange Act of 1934) as of the end of the period covered by this quarterly report (the Evaluation Date). Based on such evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that as of the Evaluation Date, the Company's disclosure controls and procedures are effective to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and to ensure that the information required to be disclosed by the Company in the reports it files or submits under the Securities Exchange Act of 1934 is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. There have not been any changes in the Company's internal control over financial reporting that have materially affected or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II: OTHER INFORMATION**

**ITEM 1: Legal Proceedings**

From time to time, the Company is party to various claims that are incidental to its business. The Company believes these claims will not have a material adverse effect on its consolidated financial condition, liquidity or results of operations.

**ITEM 1A: Risk Factors**

There has been no material change to the information provided in Item 1A of the Form 10-K Annual Report for 2008.

**ITEM 2: Unregistered Sales of Equity Securities and Use of Proceeds**

The Company did not purchase any shares of its common stock during the first quarter of 2009. There remain 333,895 shares available to be purchased under a repurchase program approved by the board of directors and announced on August 9, 2007. This stock repurchase program is not subject to an expiration date.

**ITEM 3: Defaults Upon Senior Securities** None

**ITEM 4: Submission of Matters to a Vote of Security Holders** None

**ITEM 5: Other Information** None

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DIAMOND HILL INVESTMENT GROUP, INC.

**ITEM 6: Exhibits**

- 3.1 Amended and Restated Articles of Incorporation of the Company. (Incorporated by reference from Form 8-K Current Report for the event on May 2, 2002 filed with the SEC on May 7, 2002; File No. 000-24498.)
- 3.2 Code of Regulations of the Company. (Incorporated by reference from Form 8-K Current Report for the event on May 2, 2002 filed with the SEC on May 7, 2002; File No. 000-24498.)
- 31.1 Certification of Chief Executive Officer required by Rule 13a-14(a) or Rule 15d-14(a).
- 31.2 Certification of Chief Financial Officer required by Rule 13a-14(a) or Rule 15d-14(a).
- 32.1 Section 1350 Certifications.

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DIAMOND HILL INVESTMENT GROUP, INC.

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

DIAMOND HILL INVESTMENT GROUP, INC.

Date	Title	Signature
May 8, 2009	President, Chief Executive Officer, and a Director	/s/ R. H. Dillon  R. H. Dillon
May 8, 2009	Chief Financial Officer, Treasurer, and Secretary	/s/ James F. Laird  James F. Laird

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**EXHIBIT INDEX**

- 31.1 Certification of Chief Executive Officer required by Rule 13a-14(a) or Rule 15d-14(a).
- 31.2 Certification of Chief Financial Officer required by Rule 13a-14(a) or Rule 15d-14(a).
- 32.1 Section 1350 Certifications.