

HENNESSY ADVISORS INC

Form 10-K

December 03, 2010

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-K**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Fiscal Year Ended September 30, 2010

or

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Transition Period From \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 000-49872

**HENNESSY ADVISORS, INC.**

(Exact name of registrant as specified in its charter)

**California**  
(State or other jurisdiction of  
incorporation or organization)

**68-0176227**  
(IRS Employer  
Identification No.)

**7250 Redwood Blvd., Suite 200**

**Novato, California**  
(Address of principal executive office)

**94945**  
(Zip Code)

**(415) 899-1555**

(Registrant's telephone number, including area code)

**Securities registered pursuant to Section 12(b) of the Act:**

**None.**

**Securities registered pursuant to Section 12(g) of the Act:**

**Common Stock, no par value**

(Title of class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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 (or for such shorter period that the registrant was required to file such reports), 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer

Accelerated filer

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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 aggregate market value of Common Stock held by non-affiliates (as affiliates are defined in Rule 12b-2 of the Exchange Act) of the Registrant, based on the closing price of \$2.50 on March 31, 2010, was \$8,800,295.

### APPLICABLE ONLY TO CORPORATE REGISTRANTS

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date:

As of October 25, 2010 there were 5,709,839 shares of Common Stock (no par value) issued and outstanding.

### DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the registrant's definitive proxy statement for its 2011 annual meeting of stockholders will be, when filed, incorporated by reference in Part III, Items 10, 11, 12, 13 and 14.

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HENNESSY ADVISORS, INC.

FORM 10-K

For the Fiscal Year Ended September 30, 2010

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PART I

ITEM 1. DESCRIPTION OF BUSINESS  
GENERAL

Overview

We are a publicly traded investment management firm. Our principal business activity is managing, servicing and marketing our ten open-end mutual funds. All of our mutual funds are no-load, meaning investors do not pay any upfront or deferred sales charges. We have two series of mutual funds. Our Cornerstone Series of mutual funds use quantitative stock selection strategies to manage their portfolios. It includes: the Hennessy Cornerstone Growth Fund, the Hennessy Cornerstone Growth Fund, Series II, the Hennessy Focus 30 Fund, the Hennessy Cornerstone Large Growth Fund, the Hennessy Cornerstone Value Fund, the Hennessy Total Return Fund and the Hennessy Balanced Fund (the Hennessy Cornerstone Series of Funds). Our Select Series of mutual funds are actively managed and each employs a seasoned sub-advisor. It includes: the Hennessy Select Large Value Fund, the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund (the Hennessy Select Series of Funds). In total, the net assets of the mutual funds we manage have increased by 360% from \$194 million on September 30, 2001 to \$892 million as of September 30, 2010. Collectively, we refer to the Hennessy Cornerstone Series of Funds and the Hennessy Select Series of Funds as the Hennessy Funds.

Each of the Hennessy Funds pays fees to us for our management services. Management services include investment research, supervision of investments, conducting investment programs (including the evaluation, sale and reinvestment of assets), the placement of orders for purchase and sale of securities, solicitation of brokers to execute transactions, sub-advisor oversight and the preparation and distribution of reports and statistical information. The original class shares of our mutual funds also pay fees to us for shareholder services. Shareholder services consist primarily of providing a call center to respond to shareholder inquiries, including inquiries regarding specific mutual fund account and investment information. The fees that we receive for management and shareholder services are based on a percentage of the average daily net asset values of our mutual funds.

Company History

We were founded in 1989 as a California corporation under the name Edward J. Hennessy Incorporated. We initially registered with the appropriate federal, state and self-regulatory organizations as a broker-dealer with a retail business. In addition, we were a member of the National Association of Securities Dealers, serving mainly individual investors, but we terminated this registration in July 2000 and are no longer engaged in the broker-dealer business. In 1990, we registered as an investment advisor. From 1990 to 1996, we provided management services to private clients and limited partnerships utilizing strategies similar to those we use in advising our mutual funds today. In 1996, we launched our first mutual fund, the Hennessy Balanced Fund. We initially managed the Hennessy Balanced Fund through The Hennessy Management Co., L.P., a California limited partnership for which we served as the general partner. As general partner, we performed all of the management functions on behalf of The Hennessy Management Co., L.P. for the Hennessy Balanced Fund.

In 1998, we launched our second mutual fund, the Hennessy Total Return Fund. We initially managed the Hennessy Total Return Fund through The Hennessy Management Co. 2, L.P., another California limited partnership for which we served as the general partner and as such, performed all of the management functions on behalf of The Hennessy Management Co. 2, L.P. for the Hennessy Total Return Fund.

In 2000, we began acquiring the rights to manage the assets of additional mutual funds by entering into agreements with the funds' investment advisors to acquire management contracts related to such funds. When we acquire the rights to manage the assets of a mutual fund, we generally either enter into a management agreement covering the mutual fund or reorganize the assets of the mutual fund into one of our existing mutual funds.

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In June 2000, we completed our first acquisition by entering into a management agreement covering the O Shaughnessy Cornerstone Growth Fund and the O Shaughnessy Cornerstone Value Fund and changed the names of these funds to the Hennessy Cornerstone Growth Fund and the Hennessy Cornerstone Value Fund. In connection with this acquisition, we obtained an exclusive, perpetual license to use the names and investment strategies of the Cornerstone Growth Fund and the Cornerstone Value Fund from Netfolio, Inc. These two mutual funds had approximately \$197 million in combined net assets at the time we began managing them.

In May 2002, we completed our initial public offering, raising \$5.7 million in a non-underwritten offering at a split-adjusted price of \$2.97 and became a public reporting company as a small-business issuer. At the time of our initial public offering, assets under management were approximately \$348 million. In connection with our initial public offering, the limited partners of The Hennessy Management Co., L.P. and The Hennessy Management Co. 2, L.P. agreed to merge their partnerships into our new public company, thereby allowing the consolidation of all our management activities directly into Hennessy Advisors, Inc.

In September 2003, we acquired the management agreement for the SYM Select Growth Fund. In connection with that acquisition, we launched our fifth mutual fund, the Hennessy Focus 30 Fund, into which we reorganized the assets of the SYM Select Growth Fund. At the time of this acquisition, the SYM Fund had approximately \$35 million in net assets.

In March 2004, we acquired the management agreements for five funds managed by Lindner Asset Management, Inc., which we refer to as the Lindner Funds. In connection with this acquisition, the assets of the Lindner Funds were reorganized into four of our existing mutual funds. At the time of this acquisition, the Lindner Funds had approximately \$301 million in combined net assets.

In July 2005, we acquired the management agreement for The Henlopen Fund and changed the name to the Hennessy Cornerstone Growth Fund, Series II. At the time of this acquisition, The Henlopen Fund had approximately \$299 million in net assets.

In November 2007, we opened the Hennessy Micro Cap Growth Fund, LLC, a non-registered private pooled investment fund. Hennessy Advisors, Inc. is the managing member and invested approximately \$0.5 million in the Micro Cap Growth Fund at inception.

In March 2008, we established an institutional share class for four of our mutual funds: the Hennessy Cornerstone Growth Fund, the Hennessy Cornerstone Growth Fund, Series II, the Hennessy Focus 30 Fund and the Hennessy Cornerstone Value Fund. The institutional shares require a minimum investment of \$0.25 million per fund, and net expenses do not exceed 0.98% of the average daily net assets of the Funds.

In March 2009, we acquired the management agreements for two funds managed by RBC Global Asset Management (U.S.) Inc.: the Tamarack Large Cap Growth Fund and the Tamarack Value Fund (which we refer to as the Tamarack Funds). In connection with this acquisition, shares of the Tamarack Large Cap Growth Fund were exchanged for shares of the Hennessy Cornerstone Large Growth Fund (original class shares), and shares of the Tamarack Value Fund were exchanged for shares of the Hennessy Select Large Value Fund (original class shares). Both funds also offer institutional class shares. Additionally, we retained RBC Global Asset Management (U.S.) Inc. as sub-advisor to manage the portfolio of the Hennessy Select Large Value Fund. This Fund was the first of the new Hennessy Select Series of Funds launched for the purpose of employing seasoned, yet undiscovered asset managers.

In September 2009, we acquired the management agreements for two funds managed by SPARX Investment & Research, USA, Inc., and sub-advised by SPARX Asset Management Co., Ltd.: the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund (which we refer to as the SPARX Funds) as additions to our Hennessy Select Series of Funds. Once the acquisition was approved, we changed the names to the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund, respectively. However, we retained SPARX Asset Management Co., Ltd. as sub-advisor to continue to handle the day to day portfolio management of the SPARX Funds and the investment objectives and strategies remain the same. The Hennessy Select SPARX Japan Fund also offers institutional class shares.

**Table of Contents****BUSINESS OPERATIONS, PRODUCTS and STRATEGIES****Management Agreements and Fees**

We have entered into management agreements covering all of our mutual funds with the registered investment companies or trusts under which our mutual funds are organized. Our registered investment companies or trusts are currently Hennessy Funds, Inc., Hennessy Mutual Funds, Inc., Hennessy Funds Trust, and Hennessy SPARX Funds Trust. Our management agreement with (1) Hennessy Funds, Inc. covers the Hennessy Total Return Fund and the Hennessy Balanced Fund; (2) Hennessy Mutual Funds, Inc. covers the Hennessy Cornerstone Growth Fund, the Hennessy Cornerstone Value Fund and the Hennessy Focus 30 Fund; (3) Hennessy Funds Trust covers the Hennessy Cornerstone Growth Fund, Series II, the Hennessy Cornerstone Large Growth Fund and the Hennessy Select Large Value Fund; and (4) Hennessy SPARX Funds Trust covers the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund. Under these agreements, we are responsible for overall investment and management services, subject to the oversight of the applicable board of directors or trustees and according to each mutual fund's particular fundamental investment objectives and policies. The boards of each of Hennessy Funds, Inc., Hennessy Mutual Funds, Inc., Hennessy Funds Trust, and Hennessy SPARX Funds Trust consist of four individuals, including our chairman of the board and chief executive officer, Neil J. Hennessy, and three directors or trustees who are not interested persons of the funds (disinterested directors or trustees). Under the Investment Company Act of 1940, a majority of the disinterested directors or trustees must approve the entry into and continuation of our management agreements. The disinterested directors also have sole responsibility for selecting and nominating other disinterested directors or trustees.

We also provide any ordinary clerical and bookkeeping services needed by our mutual funds that are not provided by the funds' custodian, administrator or transfer agent. We fulfill requests for information about our mutual funds or pay the fulfillment expenses that our mutual funds would otherwise incur.

In exchange for all of these services, we receive a management fee from each of our mutual funds, which is based on the amount of each fund's average daily net assets. The annual management fees payable to us by our mutual funds are as follows:

Fund	Management Fee (as a percentage of fund assets)
Hennessy Cornerstone Growth Fund (all classes)	0.74%
Hennessy Cornerstone Growth Fund, Series II (all classes)	0.74%
Hennessy Focus 30 Fund (all classes)	0.74%
Hennessy Cornerstone Value Fund (all classes)	0.74%
Hennessy Cornerstone Large Growth Fund (all classes)	0.74%
Hennessy Total Return Fund	0.60%
Hennessy Balanced Fund	0.60%
Hennessy Select Large Value Fund (all classes)	0.85%
Hennessy Select SPARX Japan Fund (all classes)	1.00%
Hennessy Select SPARX Japan Smaller Companies Fund	1.20%

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For the institutional share classes of the funds (all of the funds other than the Hennessy Total Return Fund, the Hennessy Balanced Fund and the Hennessy Select SPARX Japan Smaller Companies Fund have an institutional share class), we have a contractual obligation to waive the advisory fee or reimburse fund expenses to the extent necessary to ensure that net expenses do not exceed 0.98% of the average daily net assets of the funds, except for the institutional share class of the Hennessy Select SPARX Japan Fund, which has does not have an expense ratio cap.

After an initial two year term, our management agreements must be renewed annually by (1) the board of directors or trustees of the applicable investment company or by the vote of a majority of the outstanding shares of the applicable fund and (2) by the vote of a majority of the directors or trustees of the applicable investment company who are not parties to the management agreement and are disinterested directors or trustees. Two other circumstances might lead to termination of the management agreements: the assignment of a management agreement to another advisor automatically terminates the agreement (assignment includes indirect assignment, which is the transfer of our common stock in sufficient quantities deemed to constitute a controlling block), and the termination of the agreement, upon 60 days written notice by our firm or by one of the funds investment companies. The current management agreements were renewed by the Board of Directors of the Hennessy Funds, Inc. and Hennessy Mutual Funds, Inc. and by the trustees of the Hennessy Funds Trust on March 3, 2010 for a period of one year.

The management agreements for the Hennessy Cornerstone Large Growth Fund and the Hennessy Select Large Value Fund were approved by the Board of Trustees of Hennessy Funds Trust on March 3, 2009 for an initial period of two years (expiring on March 3, 2011), to be renewed annually thereafter; and the management agreements for the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund were approved by the Board of Trustees of Hennessy SPARX Funds Trust on July 13, 2009 and by the shareholders of the SPARX Funds on September 17, 2009 for an initial period of two years (expiring on September 17, 2011), to be renewed annually thereafter.

As of October 1, 2007, Hennessy Advisors, Inc. was also appointed the Managing Member of the Hennessy Micro Cap Growth Fund, LLC. Hennessy Advisors, Inc. will serve as the Managing Member until its resignation or removal. The Managing Member may voluntarily resign with 30 days prior written notice to the other members or 60 days prior written notice if there is not then a remaining Managing Member. At any time, the Managing Member may designate an additional Managing Member or designate a successor Managing Member with no further consent or approval required from the other members. The Managing Member may be removed at any time, with or without cause, by the vote of the other members owning a majority-in-interest of the capital accounts of the Disinterested Members, defined as members other than members who are the Managing Member or affiliates of the Managing Member.

In the Hennessy Micro Cap Growth Fund, LLC, the annual advisory fee is 2.0% of the aggregate capital accounts of the members, but no management fee is charged to the capital account of the Managing Member. Additionally, an incentive allocation can potentially be earned on any member's balance, other than the Managing Member. The allocation is determined at the end of each calendar quarter as 20% of the amount by which net profits (defined as the amount by which the net asset value on the last day of a period exceeds the net asset value on the commencement of the same period), if any, exceed the positive balance, if any, of a member's loss carryforward (defined as a memorandum account kept for each member having an initial balance of zero that is increased by the net loss, if any, allocated to each member for each calendar period).



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Shareholder Services

In addition to our management agreements, we also have shareholder servicing agreements covering the original share classes of the Hennessy Cornerstone Growth Fund, the Hennessy Cornerstone Growth Fund, Series II, the Hennessy Focus 30 Fund, the Hennessy Cornerstone Value Fund, the Hennessy Cornerstone Large Growth Fund, the Hennessy Select Large Value Fund, the Hennessy Select SPARX Japan Fund, the Hennessy Select SPARX Japan Smaller Companies Fund, the Hennessy Total Return Fund and the Hennessy Balanced Fund. We have provided shareholder services under a shareholder servicing agreement to the Hennessy Cornerstone Growth Fund and the Hennessy Cornerstone Value Fund since October 2003; to the Hennessy Focus 30 Fund since June 30, 2005; to the Hennessy Cornerstone Growth Fund, Series II since July 1, 2005; to the Hennessy Total Return Fund and the Hennessy Balanced Fund since July 1, 2007; to the Hennessy Cornerstone Large Growth Fund and the Hennessy Select Large Value Fund since March 23, 2009; and to the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund since June 1, 2010. Under these agreements, we provide administrative support services to these funds, including, among other things, the following:

maintaining an 800 number that current fund shareholders may call to ask questions about the funds or their accounts with the funds;

assisting shareholders in processing exchange and redemption requests;

assisting shareholders in changing dividend options, account designations and addresses;

responding generally to shareholder questions; and

providing other similar services that the funds may request.

In exchange for these services, we receive an annual shareholder servicing fee from each of the above-named funds of 0.10% of the fund's average daily net assets.

Sub-advisory agreements and Fees

We have entered into sub-advisory agreements covering our Hennessy Select Series of Funds with the same asset management companies that previously managed the Funds. The management companies are currently RBC Global Asset Management (U.S.) Inc. and SPARX Asset Management Co., Ltd. Our sub-advisory agreement with RBC Global Asset Management (U.S.) Inc. covers the Hennessy Select Large Value Fund and with SPARX Asset Management Co., Ltd. covers the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund. Under these agreements, the sub-advisor is responsible for the investment and reinvestment of the assets of the fund, in accordance with the terms of the sub-advisory agreement, the fund's Prospectus and the fund's Statement of Additional Information and subject to the direction, supervision and control of Hennessy Advisors, the manager of the Hennessy Select Series of Funds, and the Trustees of the Hennessy Funds Trust and Hennessy SPARX Funds Trust.

In exchange for the sub-advisory services, we (not the funds) pay a sub-advisor fee to the sub-advisors, which is based on the amount of each fund's average daily net assets. The annual sub-advisor fees payable by us to our sub-advisors are as follows:

Fund	Sub-Advisor Fee (as a percentage of fund assets)
Hennessy Select Large Value Fund (all classes)	0.35%
Hennessy Select SPARX Japan Fund (all classes)	0.35%
Hennessy Select SPARX Japan Smaller Companies Fund	0.20%



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The sub-advisory agreement for the Hennessy Select Large Value Fund was approved by the Board of Trustees of Hennessy Funds Trust on March 3, 2009 for an initial period of two years, to be renewed annually thereafter, and the sub-advisory agreement for the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund were approved by the Board of Trustees of Hennessy SPARX Funds Trust on July 13, 2009 and by the shareholders of the SPARX Funds on September 17, 2009 for an initial period of two years, to be renewed annually thereafter. After the initial period of two years, the agreements may be renewed from year to year, as long as continuance is specifically approved at least annually in accordance with the requirements of the Investment Company Act of 1940. Each sub-advisory agreement will terminate in the event of its assignment, or it may be terminated by Hennessy Funds Trust or Hennessy SPARX Funds Trust (either by the Board of Trustees or by vote of a majority of the outstanding voting securities of a Fund), respectively, or by Hennessy Advisors, upon 60 days' prior written notice.

### 12b-1 Plan

The Hennessy Total Return Fund and the Hennessy Balanced Fund have each adopted a 12b-1 plan. Under Rule 12b-1 of the Investment Company Act of 1940, mutual funds can adopt a plan that allows them to make payments to third parties in connection with the distribution of their fund shares. Such distribution activities might include: advertising; compensation paid to financial institutions, broker-dealers, and others for sales and marketing; shareholder accounting services; the printing and mailing of prospectuses to possible new shareholders; and the printing and mailing of sales literature. Mutual funds can also employ a distributor to distribute and market mutual fund shares. 12b-1 fees can be used to pay the distributor for expenses incurred for telephone costs, overhead costs, costs of employees who engage in or support the distribution of the fund shares, the printing of prospectuses and other reports for possible new shareholders, advertising and the preparation and distribution of sales literature. The 12b-1 plan adopted by the Hennessy Total Return Fund and the Hennessy Balanced Fund authorizes each fund to make payments at an annual rate not to exceed 0.15% of each Fund's average daily net assets. The Securities and Exchange Commission (SEC) has considered changes to Rule 12b-1 of the Investment Company Act of 1940 and has proposed changes to Rule 12b-1. At this time, it is not clear what final changes the SEC will adopt. Such final changes (depending on the form they take), or other future changes, could restrict our current practices.

### Custodial and Brokerage Arrangements

All shareholder funds are held by third party custodians. Independent brokerage firms execute all trades for our funds, at our direction.

Currently, we participate in soft dollar arrangements with four brokers. This means that we receive research reports and real-time electronic research to assist us in trading and managing our mutual funds. Under these soft dollar arrangements, we pay brokerage commissions for securities trades on behalf of a mutual fund, but in exchange we receive research or other services that benefit our mutual funds. Our soft dollar arrangements comply with SEC guidance regarding soft dollars.

### License Agreement

Our ability to use the names and formulaic investment strategies of the funds now known as the Hennessy Cornerstone Growth Fund and the Hennessy Cornerstone Value Fund are governed by the terms and conditions of a license agreement, dated as of April 10, 2000, with Netfolio, Inc. Under the license agreement, Netfolio, Inc. granted us a perpetual, paid-up, royalty-free, exclusive license to use certain trademarks, such as Strategy Indexing, Cornerstone Growth and Cornerstone Value, as well as the formula investment strategies used by the Hennessy Cornerstone Growth Fund and the Hennessy Cornerstone Value Fund. All of our advertising, marketing, promotional and other materials incorporating or referring to the trademarks are subject to the prior written approval of Netfolio, Inc., except that we do not need Netfolio Inc.'s prior written approval to use the trademarks in a manner that is not substantially unchanged from any prior use by Netfolio, Inc. in its own business or from any prior use by us previously approved by Netfolio, Inc. We can assign the license to another person or entity if the assignee agrees in writing to be bound by the terms of the license agreement. There are no ongoing licensing fees associated with this license agreement and Netfolio, Inc. does not have any contractual rights to terminate the license agreement.

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### Business Strategy

From 1996, when we started our first mutual fund, until September 30, 2010, we have grown our assets under management to \$892 million, with fluctuations during that time. Recent market conditions have created significant volatility in the equity markets, causing increased redemptions and negative performance. However, we strive to increase our profitability and assets under management by implementing the following key strategies:

-Utilizing our branding and marketing campaign for growth.

We believe that we can attract investors to our Hennessy Cornerstone Series of Funds by effectively marketing our unique quantitative investment style. We believe that our investment philosophy appeals to investors who want to understand exactly how their investments are managed and who favor statistical analysis and empirical evidence as the basis for investment decisions. Additionally, we believe the talents of the seasoned sub-advisors managing our Hennessy Select Series of Funds will attract investors who appreciate fundamental, hands-on investment management.

We will continue our efforts to make Hennessy a name readily recognizable by investors through frequent print media, radio and television appearances. We use our media appearances to convey to investors that we manage our Hennessy Cornerstone Series of Funds with the discipline and consistency of an index fund by never straying from our strategies. We believe that a straightforward, quantitative approach is easily understood by investors and makes them more likely to recommend us to others by word of mouth. As our brand recognition broadens, we believe that our investment philosophy will generate organic growth through new investments in our mutual funds. We will also team up with our sub-advisors for media coverage in order to promote our Hennessy Select Series of Funds when co-branding opportunities arise.

-Expanding our distribution network to additional mutual fund supermarkets.

One of the ways that investors can buy shares of our mutual funds is through mutual fund supermarkets, principally Schwab, Fidelity, TD Ameritrade and Pershing. Mutual fund supermarkets can offer funds of many different investment companies to investors, often without a transaction fee or sales charge to the investor. Instead of charging a fee to investors, mutual fund supermarkets are reimbursed for their services by the applicable fund or that fund's investment advisor. This ability to purchase various mutual funds at no cost in a single location is very attractive to investors. Mutual fund supermarkets have been a significant source of our asset growth. Of the \$892 million of assets under management in our mutual funds as of September 30, 2010, approximately 52% of those assets came from mutual fund supermarkets. We see continued opportunities to form new relationships with mutual fund supermarkets, thereby enhancing the accessibility of our no-load mutual funds to investors.

-Increasing our current base of investment professionals who utilize no-load mutual funds for their clients.

Investment professionals generally have a wide variety of investment products that they can recommend to their clients. A recommendation by an investment professional to a client to buy one of our mutual funds can be very influential to that client. Thus, we believe that expanding our current base of investment professionals who utilize no-load funds for their clients will help us increase the amount of assets that we manage, which will in turn increase our revenues.

-Securing participation in the platforms of national full-service firms that permit their investment professionals to utilize no-load funds for their clients.

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We will strive to continue developing relationships with national full-service firms that permit their investment professionals to offer no-load funds to their clients as a way to increase the amount of assets that we manage, which will in turn increase our revenues.

-Pursuing selective acquisitions.

We selectively consider strategic acquisitions of management agreements of additional mutual funds. Through our acquisition strategy, we have added over \$1.06 billion of net assets to our family of mutual funds over a period of approximately ten years. We believe there are a number of attractive acquisition opportunities from smaller mutual fund managers who are reaching retirement age or whose investment strategy does not lend itself to the economies of scale inherent in our strictly quantitative approach. We have been able to offer lower overall expense ratios to the shareholders of acquired funds. We have also been able to improve performance in some instances. The addition of our Hennessy Select Series of Funds has expanded the pool of possible acquisition candidates to now include actively managed funds wishing to retain their manager in a sub-advisory role.

-Delivering strong, high quality financial results.

We seek to manage our investment management business to the highest regulatory, ethical and business standards while strenuously controlling costs, maintaining a relatively small staff, and creating high margins for our shareholders.

### Marketing

We generate all of our operating revenues by providing management and shareholder services to our mutual funds. The revenues that we receive from the mutual funds are based on the amount of average daily net assets in the funds and thus, we can increase our revenues by growing the amount of net assets in the funds. One of the best ways we can grow the assets of the mutual funds is by delivering strong investment performance, which we believe should:

result in an increase in the value of existing assets in the funds;

encourage more investors to buy shares of our mutual funds and decrease the number of investors who redeem their shares and leave our mutual funds; and

motivate current investors to invest additional money in our mutual funds.

We have developed an aggressive public relations outreach program to target audiences we would otherwise be unable to address. Our public relations outreach program has resulted in the Hennessy Funds being mentioned in national print and broadcast media an average of once every two to three days in such vehicles as CNBC, Fox News, The Wall Street Journal, The New York Times, Smart Money, Barron's, and Investors Business Daily. To facilitate our presence in the media, we installed LiveStudio, an in-house studio providing a direct link to media broadcasts. Along with our primary spokesperson, Neil J. Hennessy, our CIO and Portfolio Manager, we now utilize Frank Ingarra, Jr., our Co-Portfolio Manager, in a spokesperson role. Mr. Ingarra has enabled us to further expand our public relations program.

We also send quarterly information mailings, fund performance updates, news articles pertaining to the funds and commentaries from Neil J. Hennessy to clients and prospective clients, and we exhibit at select investment advisor trade shows throughout the year. Additionally, we attend strategic industry-related conferences.

### Acquisition Strategy and Market Opportunity

We believe that we are well positioned to experience organic growth, and possibly growth by acquisition, in the future. Our scalable business model allows us to increase our profit margins as assets under management grow, since we do not necessarily need to add personnel proportional to the increase in assets under management.

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Together with organic growth, our growth strategy revolves around the acquisition of management agreements. We believe the regulatory burden imposed upon the mutual fund industry has compressed the margins of smaller mutual fund managers, making those managers more receptive to an acquisition. We believe that we are well positioned to benefit from these attractive acquisition trends and from the increasing supply of potential targets.

### Investment Strategy

#### Hennessy Cornerstone Series of Funds:

Each of the Hennessy Cornerstone Series of Funds employs a consistent and repeatable investment process, combining time-tested, purely quantitative stock selection formulas with a highly disciplined, team-managed approach. Our stock selection formulas have been tested over historical periods for hypothetical performance results, and we adhere to our proven formulas in all types of market conditions. A brief description of each of the Cornerstone Funds' objectives and investment formulas follows:

-Hennessy Cornerstone Growth Fund (original class symbol HFCGX and institutional class symbol HICGX). The Hennessy Cornerstone Growth Fund seeks long-term growth of capital. While it has historically selected small cap companies, the formula may select mid and large cap companies. This fund screens a universe of stocks with a market capitalization of more than \$175 million, a price-to-sales ratio of less than 1.5, higher annual earnings than in the previous year and stock price appreciation, or positive relative strength, over the prior three- and six-month periods. The fund then invests in the 50 stocks with the highest one-year price appreciation.

-Hennessy Cornerstone Growth Fund, Series II (original class symbol HENLX and institutional class symbol HINLX). The Hennessy Cornerstone Growth Fund, Series II seeks long-term capital appreciation. This fund utilizes the same investment formula as the Hennessy Cornerstone Growth Fund but rebalances its portfolio at a different time of the year, in an effort to create as different a portfolio of stocks as possible.

-Hennessy Focus 30 Fund (original class symbol HFTFX and institutional class symbol HIFTX). The Hennessy Focus 30 Fund seeks long-term growth of capital by investing in mid-cap, growth-oriented companies. This fund screens a universe of stocks with a market capitalization of between \$1 to \$10 billion, excluding American Depositary Receipts (ADRs), a price-to-sales ratio of less than 1.5, higher annual earnings than in the previous year and positive stock price appreciation over a three- and six-month periods. The fund then invests in the 30 stocks with the highest one-year price appreciation.

-Hennessy Cornerstone Large Growth Fund (original class symbol HFGLX and institutional class symbol HIGLX). The Hennessy Cornerstone Large Growth Fund invests in growth-oriented common stocks of larger companies by utilizing a highly disciplined, purely quantitative formula. This fund screens a universe of stocks, excluding ADRs, with a market capitalization that exceeds the average of the database, a price-to-cash flow ratio less than the median of the database (this value criterion helps to uncover relative bargains among large companies), and positive total capital. The fund then invests in the 50 stocks with the highest one-year return on total capital.

-Hennessy Cornerstone Value Fund (original class symbol HFCVX and institutional class symbol HICVX). The Hennessy Cornerstone Value Fund seeks total return, consisting of capital appreciation and current income, by investing in large, dividend-paying companies. This fund screens a universe of stocks with above average market capitalization, shares outstanding and cash flow, and 12-month sales that are at least 50% higher than average. The fund then invests in the 50 stocks with the highest dividend yield, which is calculated as the annual dividends paid by a company divided by the per share price of its stock.

-Hennessy Total Return Fund (original class symbol HDOGX). The Hennessy Total Return Fund seeks total return, consisting of capital appreciation and current income, by investing approximately 75% of its assets in the 10 highest dividend-yielding common stocks of the Dow Jones Industrial Average (commonly referred to as the "Dogs of the Dow") and the remaining 25% in U.S. Treasury securities with a maturity of less than one year.

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-Hennessy Balanced Fund (original class symbol HBF BX). The Hennessy Balanced Fund seeks a combination of capital appreciation and current income by investing approximately 50% of its assets in the Dogs of the Dow stocks and approximately 50% in U.S. Treasury securities with a maturity of less than one year.

Hennessy Select Series of Funds:

The Hennessy Select Series of Funds, launched with the acquisition of the Hennessy Select Large Value Fund in March 2009, are actively managed and each employs a seasoned sub-advisor. This newer series of funds allows us to expand our product offering and to showcase the talents of what we believe are excellent, yet undiscovered asset managers. We have sought out highly qualified category experts to oversee the day to day portfolio management of each of the Hennessy Select Series of Funds. A brief description of the objective and investment strategy of each Select Fund is set forth below:

-Hennessy Select Large Value Fund (original class symbol HSVFX and institutional class symbol HSVIX). The Hennessy Select Large Value Fund seeks long-term growth of capital and current income by purchasing larger capitalization companies that are out of favor and undervalued. The fund invests in stocks which its portfolio managers consider to be undervalued based on earnings, dividends and/or assets, or on other widely recognized stock value measurements. Further, the portfolio managers believe that these companies have sound businesses with good future potential based on their fundamental characteristics.

-Hennessy Select SPARX Japan Fund (original class symbol SPXJX and institutional class symbol SPARX). The Hennessy Select SPARX Japan Fund seeks long-term capital appreciation by investing at least 80% of its net assets in equity securities of Japanese companies. The Fund invests in companies regardless of market capitalization, and portfolio construction is unconfined to benchmarks or tracking error. The fund invests in stocks which its portfolio managers believe to be good businesses with exceptional management and which are trading at an attractive price. Individual stock selection is based on rigorous, on-site research and focuses on factors such as market growth potential, management quality, earnings quality and balance sheet strength. The Fund seeks arbitrage opportunities between a company's fundamental value and its market price. The portfolio selects just the managers' best ideas and has a concentrated number of holdings.

- Hennessy Select SPARX Japan Smaller Companies Fund (original class symbol SPJSX). The Hennessy Select SPARX Japan Smaller Companies Fund seeks long-term capital appreciation. The Fund normally invests at least 80% of its net assets in equity securities of smaller Japanese companies, defined as those with market capitalization of approximately \$200 million to \$1.5 billion at time of purchase. The Fund's portfolio construction is unconfined to benchmarks or tracking error. The investment strategy mirrors the Hennessy Select SPARX Japan Fund, but it operates within the market capitalizations discussed above.

### Historical Fund Investment Performance

The following table presents the average annualized returns for each of our mutual funds and the relevant benchmark indices for the one-year, three-year, five-year, ten-year and since inception periods ended September 30, 2010.

Although we did not begin managing the Hennessy Cornerstone Growth Fund and the Hennessy Cornerstone Value Fund until June 2000, we have included historical performance information for these funds from their inception date of November 1, 1996 because the previous investment manager to these funds managed the funds using the same strategies that we still use today.

Although we did not begin managing the Hennessy Select Large Value Fund until March 2009, and we did not begin managing the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund until September 2009, we have included historical performance information for these funds from their inception dates because the previous investment managers have remained in a sub-advisory role and continue to adhere to the same investment strategies.

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The performance shown for the period 4/20/04 to 3/20/09 for the Hennessy Select Large Value Fund reflects performance for the Tamarack Value Fund, the predecessor to the Hennessy Select Large Value Fund, and the performance shown for the period 9/30/84 to 4/19/04 reflects performance for the Babson Value Fund, the predecessor to the Tamarack Value Fund.

Returns are presented net of all expenses borne by mutual fund shareholders, but are not net of fees waived or expenses borne by us. The past investment performance of our mutual funds is no guarantee of future performance and all of these mutual funds have experienced negative performance over various time periods in the past and may do so again in the future.

Hennessy Funds Performance as of September 30, 2010:

Hennessy Cornerstone Growth Fund	1 Year	3 Years	5 Years	10 Years	Since Inception (11/01/96)
Institutional Class Share - HICGX	10.03%	-15.54%	-7.26%	2.27%	7.83%
Original Class Share - HFCGX	9.52%	-15.83%	-7.53%	2.01%	7.55%
Russell 2000 Index (2)(3)	13.35%	-4.29%	1.60%	4.00%	6.45%
S&P 500 Index(1)(2)	10.16%	-7.16%	0.64%	-0.43%	5.37%
Hennessy Cornerstone Growth Fund, Series II	1 Year	3 Years	5 Years	10 Years	Since Inception (07/01/05)
Institutional Class Share - HINLX	13.35%	16.56%	-7.85%	N/A	-7.52%
Original Class Share - HENLX	12.64%	-17.06%	-8.28%	N/A	-7.94%
Russell 2000 Growth (2)(3)	14.79%	-3.75%	2.35%	N/A	3.35%
S&P 500 Index (1)(2)	10.16%	-7.16%	0.64%	N/A	1.23%
Hennessy Focus 30 Fund	1 Year	3 Years	5 Years	10 Years	Since Inception (09/17/03)
Institutional Class Share - HIFTX	19.27%	-3.77%	2.64%	N/A	9.07%
Original Class Share - HFTEFX	18.82%	-4.10%	2.32%	N/A	8.70%
S&P 400 Mid cap Index (2)(6)	17.78%	-1.67%	3.77%	N/A	7.66%
S&P 500 Index (1)(2)	10.16%	-7.16%	0.64%	N/A	3.59%
Hennessy Cornerstone Value Fund	1 Year	3 Years	5 Years	10 Years	Since Inception (11/01/96)
Institutional Class Share - HICVX	12.81%	-6.27%	1.62%	4.55%	5.45%
Original Class Share - HFCVX	12.50%	-6.51%	1.39%	4.21%	5.01%
Russell 1000 Value (2)(4)	8.90%	-9.39%	-0.48%	2.59%	6.40%
S&P 500 Index (1)(2)	10.16%	-7.16%	0.64%	-0.43%	5.37%
Hennessy Cornerstone Large Growth Fund	1 Year	3 Years	5 Years	10 Years	Since Inception (3/20/09)
Institutional Class Share - HILGX	18.89%	N/A	N/A	N/A	41.28%
Original Class Share - HFLGX	18.38%	N/A	N/A	N/A	40.79%
Russell 1000 Index (2)(4)	10.75%	N/A	N/A	N/A	33.48%
S&P 500 Index (1)(2)	10.16%	N/A	N/A	N/A	32.20%



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	1 Year	3 Years	5 Years	10 Years	Since Inception (9/30/84)
Hennessy Select Large Value Fund					
Institutional Class Share - HSVIX	4.29%	-9.45%	-1.52%	1.99%	9.37%
Original Class Share - HSVFX	3.86%	-9.64%	-1.67%	1.92%	9.34%
Russell 1000 Value (2)(4)	8.90%	-9.39%	-0.48%	2.59%	10.75%
S&P 500 Index (1)(2)	10.16%	-7.16%	0.64%	-0.43%	10.35%
	1 Year	3 Years	5 Years	10 Years	Since Inception (10/31/03)
Hennessy Select SPARX Japan Fund					
Institutional Class Share - SPARX	4.47%	-8.64%	-5.09%	N/A	4.75%
Original Class Share - SPXJX	4.41%	-8.65%	-5.17%	N/A	4.65%
MSCI Japan Index (2)(7)	0.25%	-9.95%	-2.38%	N/A	2.63%
TOPIX (2)(8)	-0.34%	-9.31%	-2.95%	N/A	2.05%
	1 Year	3 Years	5 Years	10 Years	Since Inception (8/31/07)
Hennessy Select SPARX Japan Smaller Companies Fund					
Original Class Share - SPJSX	-2.10%	-0.94%	N/A	N/A	-0.27%
MSCI Japan Small Cap Index (2)(9)	-1.64%	-5.76%	N/A	N/A	-5.79%
TOPIX (2)(8)	-0.34%	-9.31%	N/A	N/A	-8.52%
	1 Year	3 Years	5 Years	10 Years	Since Inception (07/29/98)
Hennessy Total Return Fund					
Original Class Share - HDOGX	15.31%	-6.33%	1.94%	3.34%	2.45%
Dow Jones Industrial Average (2)(5)	14.12%	-5.38%	3.13%	2.51%	3.87%
S&P 500 Index (1)(2)	10.16%	-7.16%	0.64%	-0.43%	1.90%
	1 Year	3 Years	5 Years	10 Years	Since Inception (03/08/96)
Hennessy Balanced Fund					
Original Class Share - HBFBX	8.23%	-2.89%	2.57%	2.52%	3.71%
Dow Jones Industrial Average (2)(5)	14.12%	-5.38%	3.13%	2.51%	7.06%
S&P 500 Index (1)(2)	10.16%	-7.16%	0.64%	-0.43%	5.99%

- (1) The S&P 500 is the Standard & Poor's Composite Index of 500 stocks, a widely recognized index of U.S. stocks.
- (2) Reflects no deduction for fees or expenses.
- (3) The Russell 2000 Index is a recognized small-cap index of the 2,000 smallest stocks of the Russell 3000 Index, which is comprised of the 3,000 largest U.S. stocks as determined by total market capitalization.
- (4) The Russell 1000 Value Index is a recognized large-cap index of U.S. stocks.
- (5) The Dow Jones Industrial Average is an index of common stocks comprised of major industrial companies and assumes reinvestment of dividends.
- (6) The S&P Mid-cap 400 Index is a recognized mid-cap index of U.S. stocks.
- (7) The MSCI Japan Index is a market capitalization-weighted index of Japanese equities.
- (8) The Tokyo Stock Price Index (TOPIX) is a market capitalization-weighted index of all companies listed on the First Section of the Tokyo Stock Exchange.
- (9) The MSCI Japan Small Cap Index represents the universe of small capitalization companies in the Japanese equity markets.

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Development of New Investment Strategies and Expanding Our Product Offerings

We begin developing new investment strategies or expanding our product offerings by identifying client needs and reviewing asset allocation tables to determine where we can augment our family of mutual funds. Once we identify an attractive market segment, we select one of the following methods to gain the new strategy: (a) by screening the appropriate universe of stocks with a set of parameters that we believe identify stocks that will produce higher long-term returns with lower associated risk than their relative indices and introducing the new investment strategies into the marketplace by opening and directly marketing a new mutual fund, (b) by acquiring the management agreement for an existing mutual fund and implementing our new strategy, or (c) by acquiring the management agreement for an existing fund and utilizing strategic sub-advisors to expand our product offering.

Competition

We face substantial competition in the investment management industry. The investment management industry is characterized by a relatively low cost of entry and by the formation of new investment management entities that may compete directly with us. We compete directly with a large number of global and U.S. investment advisors, commercial banks, brokerage firms, broker-dealers, insurance companies and other financial institutions. These institutions range from small boutique firms to large financial services complexes. We compete on a wide variety of factors, including:

investment performance of our mutual funds;

expense ratio of our mutual funds;

product offerings;

quality of service;

brand recognition; and

business reputation.

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We are considered a small investment management firm. Many competing firms are part of larger financial services companies and have greater marketing, financial, technical, research and other capabilities. Most larger firms offer a broader range of financial services than we do and compete with us for retail and institutional clients. Nonetheless, we have learned to compete successfully with these firms by creating unique investment strategies and by branding our investment style through public relations and outstanding customer service.

Our mutual funds also face competition, primarily from nationally and regionally distributed funds that offer equivalent financial products with returns equal to or greater than those we offer. The competition for new investors is intense, but we feel that by increasing our mutual funds distribution channels and continuing to brand our investment style and the competency of our sub-advisors, we can capture portions of the available investment business.

### Regulation

Virtually all aspects of our business are subject to federal and state laws and regulations. These laws and regulations are intended to protect shareholders of registered investment companies and clients of registered investment advisors. We believe that we are in compliance in all material respects with all laws and regulations.

We are registered as an investment advisor with the SEC. As a registered investment advisor, we must comply with the requirements of the Investment Advisors Act of 1940 and related SEC regulations. Such requirements relate to, among other things, fiduciary duties to clients, engaging in transactions with clients, maintaining an effective compliance program, solicitation arrangements, conflicts of interest, advertising, limitations on agency cross and principal transactions between an advisor and advisory clients, recordkeeping and reporting requirements, disclosure requirements and general anti-fraud provisions. Our mutual funds are registered with the SEC under the Investment Company Act of 1940. The Investment Company Act of 1940 imposes additional obligations on both the funds and the advisor, including detailed operational requirements. The SEC is authorized to institute proceedings and impose sanctions for violations of the Investment Advisors Act and Investment Company Act, ranging from fines and censures to termination of an investment advisor's registration. Our failure to comply with the SEC requirements could have a material adverse effect on us. We believe we are in compliance with SEC requirements.

In response to the 2001 to 2004 scandals in the financial services industry regarding late trading, market timing and the selective disclosure of portfolio information, the U.S. Congress and the various regulatory agencies that supervise our operations adopted various legislative and regulatory proposals. The SEC, other regulators and Congress continue to investigate certain practices in our industry. In addition, we are subject to periodic examination by the SEC under SEC rules and regulations. The most recent SEC examination occurred in August, 2007 for the period of January 1, 2005 to June 30, 2007. The findings of the examination were minor in nature and had no effect on our financial statements.

At the end of 2003, the SEC adopted rules requiring investment advisors and investment companies to adopt written compliance programs designed to prevent violations of the federal securities laws. These compliance programs must be reviewed annually for adequacy and effectiveness. Investment advisors and investment companies must also designate a chief compliance officer to implement the compliance policies and procedures and to report directly to the fund's board of directors or trustees.

Over the past several years, Congress has occasionally advanced the ideas of eliminating asset-based distribution fees or Rule 12b-1 fees for open-end mutual funds. The changes could prohibit revenue sharing, which allows a mutual fund company to pay for "shelf space" at brokerage firms or other intermediaries selling mutual fund shares. Although such reforms have been advanced, they have not been adopted. Should adoption occur, it may become more expensive for us to distribute and manage our mutual funds.

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Because many regulations are subject to varying interpretations, our firm's compliance with these regulations subjects it to a number of risks. Regulators make periodic examinations and review annual, monthly and other reports on our operations, track record and financial condition. In the event that we violate or fail to comply with an applicable law or regulation, governmental regulators may institute administrative or judicial proceedings against us that could result in censures, fines, compensation orders, civil penalties, criminal penalties, the issuance of cease-and-desist orders, the deregistration or suspension of our firm, the suspension or disqualification of our officers or employees and other adverse consequences. We have not experienced any such penalties to date. Such violations or non-compliance could also subject us and/or our employees to civil actions by private persons.

**EMPLOYEES**

As of September 30, 2010, Hennessy Advisors, Inc. employed eleven full-time employees.

The executive officers of the company are Neil J. Hennessy, President, Chairman of the Board, Chief Executive Officer, and Chief Investment Officer; Teresa M. Nilsen, Executive Vice President, Chief Operating Officer, Chief Financial Officer, Secretary and a Director of Hennessy Advisors; and Daniel B. Steadman, Executive Vice President in charge of expansion, Chief Compliance Officer and a Director of Hennessy Advisors. In addition to our executive officers' responsibilities at Hennessy Advisors, Inc., Mr. Hennessy serves as President, Portfolio Manager of the Hennessy Funds and a member of the board of directors and board of trustees of the Hennessy Funds, Ms. Nilsen is an Executive Vice President and Treasurer of the Hennessy Funds and Mr. Steadman is an Executive Vice President and Secretary of the Hennessy Funds.

Other employees of Hennessy Advisors include: Frank Ingarra, Jr., Co-Portfolio Manager; Tania Kelley, Marketing Director; Brian Peery, Director of Research; Kathryn Fahy, Controller; Ana Miner, Operations Specialist; Joseph Fahy, Chief Compliance Officer of Hennessy Funds; Michelle Hennessy, Sales Associate; and Lauren Puliafico, Receptionist.

**ITEM 1A. RISK FACTORS**  
Risks relating to our business

-Our revenues decline when the value of the securities held by the mutual funds we manage declines.

We derive all of our operating revenues from management fees and shareholder servicing fees paid to us by the mutual funds we manage. These fees are calculated as a percentage of the average daily net assets of our mutual funds and vary from fund to fund. The securities markets are inherently volatile and may be affected by factors beyond our control, including global economic conditions, interest rate fluctuations, inflation rate increases and other factors, such as the sub-prime lending crisis, that are difficult to predict. Volatility in the securities markets, and the equity markets in particular, has reduced the net assets of our mutual funds and consequently reduced our revenues, and could continue to do so in the future. In addition to declines in the equity markets, failure of these markets to sustain prior levels of growth or continued short-term volatility in these markets has resulted in investors withdrawing their investments from our mutual funds and decreasing their rate of investment, both of which have adversely affected our revenues. This risk is further discussed and quantified in Item 7A in this Annual Report on Form 10-K.

-Investors in our mutual funds can redeem their investments in our funds at any time and for any reason, including poor investment performance. This adversely affects our revenues.

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Fund investors may redeem their investments in any of our mutual funds at any time and for any reason without prior notice. Investors may also reduce the total amount of assets that they have invested with us for a number of reasons, including our investment performance, changes in prevailing interest rates and financial market performance. Success in the investment management and mutual fund business is dependent on investment performance, as well as distribution and client servicing. If our mutual funds perform poorly compared to the mutual funds of other investment management firms, we may experience a decrease in purchases of shares of our mutual funds and an increase in redemptions of shares of our mutual funds. A decrease in the net assets of our mutual funds adversely affects our revenues.

-Adverse opinions of our mutual funds by third party rating agencies or industry analysts could decrease new investments in or accelerate redemptions from our mutual funds, which adversely affects our revenues.

Many investors rely heavily on the opinions of third party rating agencies and industry analysts when making decisions to purchase or redeem shares of mutual funds. Adverse opinions regarding our mutual funds could erode investor confidence, potentially leading to a decrease in new investments and an increase in redemptions, thereby reducing the net assets of our mutual funds. A decrease in the net assets of our mutual funds adversely affects our revenues.

-Investor behavior is influenced by short-term investment performance of mutual funds.

Investor behavior may be based on many factors, including short-term investment performance. Poor short-term performance of our mutual funds, irrespective of longer-term success, could potentially lead to a decrease in new investments and an increase in redemptions, thereby reducing the net assets of our mutual funds. A decrease in the net assets of our mutual funds adversely affects our revenues.

-For our Hennessy Cornerstone Series of Funds, we utilize quantitative investment strategies that require us to invest in specific portfolios of securities and hold these positions for a specified period of time.

Our Hennessy Cornerstone Series of Funds adhere to the investment strategies for each of our mutual funds during the annual rebalancing period and throughout the course of the year. Adhering to our investment strategies during the annual rebalancing of our mutual funds may result in the elimination of better performing assets from our funds' portfolios and an increase in investments with relatively lower total return. Additionally, we will maintain a position in a relatively poorly performing security throughout the course of the portfolio holding period. Either of these actions could result in relatively lower performance of our mutual funds and adversely affect the net assets of our mutual funds. A decrease in the net assets of our mutual funds adversely affects our revenues.

-The Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund invest in the Japanese stock market in Yen. Since the assets are held in U.S. dollars, there is currency risk.

The Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund are invested in Japanese securities and are sub-advised by the Tokyo-based (but U.S. registered) SPARX Asset Management Co., Ltd. The value of these funds fluctuates with changes in the value of the Japanese Yen versus the U.S. dollar. Furthermore, any changes in the political climate of Japan may have an effect on the value of the stocks in these funds.

-We depend upon key personnel to manage our business. Their loss would adversely affect our business and financial condition.

Our success is largely dependent on the skills, experience and performance of key personnel, including Neil J. Hennessy, our Chairman of the Board, Chief Executive Officer, Portfolio Manager and President; Teresa M. Nilsen, our Executive Vice President, Chief Operating Officer, Chief Financial Officer and Secretary; and Daniel B. Steadman, our Executive Vice President in charge of expansion and Chief Compliance Officer. The loss of such individuals or other key personnel could have an adverse effect on our business, financial condition and results of operations. Moreover, in order to retain certain key personnel, we may be required to increase compensation to such individuals, resulting in additional expense.

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-Our business is extensively regulated and our failure to comply with regulatory requirements may harm our financial condition.

Our business is subject to extensive regulation in the United States, particularly by the SEC. Our failure to comply with applicable laws or regulations could result in fines, suspensions of personnel or other sanctions, including revocation of our registration as an investment advisor. The mutual fund industry has undergone increased scrutiny by the SEC and state regulators for the past several years, resulting in numerous enforcement actions, sweep examinations, and new rules and rule proposals. These actions have increased our costs in managing our mutual funds, and we could continue to experience higher costs if new rules and other regulatory actions or legislation require us to spend more time, hire additional personnel or buy new technology to comply with these rules and laws. Additional changes in laws or regulations, the interpretation or enforcement of existing laws and rules or governmental policies could also have a material adverse effect on us by limiting the sources of our revenues and increasing our costs. Our business may be materially affected not only by securities regulations, but also by regulations of general application. For example, the amount of net assets in our mutual funds in a given time period could be affected by, among other things, existing and proposed tax legislation and other governmental regulations and policies, including the interest rate policies of the Federal Reserve Board.

Our management activities are also subject to contractual commitments and our mutual fund business involves compliance with numerous investment, asset valuation, distribution and tax requirements. Failure to adhere to these requirements could result in losses that a client could recover from us. We have installed procedures and utilize the services of experienced administrators, accountants and lawyers to assist in satisfying these requirements. However, there can be no assurance that these precautions will protect us from potential liabilities.

-The costs of full compliance with new securities regulations may increase expenses and reduce earnings.

In order to comply with securities regulations, we may have additional expenses beyond our control, which may have a substantial impact on earnings per share. In October 2004, we hired a chief compliance officer as required by Rule 206(4)-7 of the Investment Advisors Act of 1940.

In addition to requiring the hiring of a chief compliance officer, Rule 206(4)-7 of the Investment Advisors Act of 1940 required that we adopt written compliance policies and procedures. Under Rule 38a-1 of the Investment Company Act of 1940, our mutual funds were also required to adopt written compliance policies and procedures, including policies and procedures that provide for oversight of the funds' key service providers, including us. We may experience increases in audit, legal, internal technology and other expenses associated with the regulations of the Sarbanes-Oxley Act of 2002, especially as they relate to internal controls and compliance with financial reporting.

-Management contracts acquired by the Company are currently classified as an indefinite life asset subject to impairment analysis. The impairment analysis is based on subjective criteria, and an impairment loss could be recorded.

The management contracts acquired by the Company, currently a \$22.3 million asset on the balance sheet, are considered an intangible asset with an indefinite useful life. Management reviews the classification of the asset as indefinite life each reporting period. If the contracts become an asset with a definite life, the Company would begin amortizing the contracts over the remaining useful life of the contracts. If the contracts are determined to remain an indefinite life asset, the Company reviews the carrying value of management contracts acquired to determine if any impairment has occurred. The analysis is based on anticipated future cash flows, which are calculated based on assets under management. Although the contracts are not currently impaired, there is always a possibility of impairment in the future, which could require the Company to write-off all or a portion of the contracts. A write-off, depending on the amount, could have a significant impact on earnings per share.

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-Acquisitions involve inherent risks that could adversely affect our operating results and financial condition as well as dilute the holdings of current shareholders.

As part of our business strategy, we intend to pursue additional acquisitions of management agreements for other mutual funds. Future acquisitions of management agreements would be accompanied by risks including, among others:

inability to secure enough affirmative votes to gain approval from the target fund's shareholders of a proposed acquisition;

the loss of mutual fund assets through redemptions by shareholders of newly acquired mutual funds;

higher than anticipated acquisition expenses;

the potential diversion of our management's time and attention; and

dilution to our shareholders if the acquisition is made with our common stock.

If one or more of these risks occur, we may be unable to successfully complete an acquisition of a management agreement, we may experience an impairment of management agreement valuations and we may not achieve the expected return on investment. Any of these results could have an adverse effect on our business, financial condition and results of operations.

-Our management and shareholder servicing agreements can be terminated on short notice and are subject to annual renewals.

We generate all of our operating revenues from the management and shareholder servicing agreements covering our mutual funds. Management and shareholder servicing agreements covering our mutual funds are terminable without penalty on 60 days notice and must be approved at least annually by a majority of each fund's board of directors or trustees and a majority of the disinterested members of each fund's board of directors or trustees. If any of these management or shareholder servicing agreements are terminated or not renewed, our revenues would substantially decline.

-We face intense competition in attracting investors and retaining net assets in our mutual funds.

The investment management business is intensely competitive. We are considered a small investment management company, but must compete with a large number of global and U.S. investment advisors, commercial banks, brokerage firms, broker-dealers, insurance companies and other financial institutions for investors in our mutual funds. Many organizations are attempting to market to and service the same investors as we do, not only with mutual fund products and services, but also with a wide range of other financial products and services. Many of our competitors have greater marketing, financial, technical, research, distribution and other capabilities than we do and offer more product lines and services. These competitors would tend to have a substantial advantage over us during periods when our investment performance is not strong enough to counter these competitors' greater resources or due to a wide variety of other factors, such as the expense ratios of our mutual funds or our small number of mutual funds. If we are not able to attract investors and retain net assets in our mutual funds, our revenues could decline and our business, financial condition and results of operations would suffer.

-Assets invested through mutual fund supermarkets have a higher risk of redemption due to more accessibility to alternative investment options.

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The mutual fund assets held through mutual fund supermarkets, as opposed to assets directly invested in our mutual funds, can be more easily moved to investments in funds outside of our fund family. Mutual fund supermarkets are attractive to investors because of the ease of accessibility to a variety of funds, but this causes the investments to be more sensitive to fluctuations in performance, especially in the short-term. If we are not able to retain the investor assets held through mutual fund supermarkets, it will cause decreased net assets in our mutual funds; as a result, our revenues could decline and our business, financial condition and results of operations would suffer.

-Market pressure to lower our management fees could reduce our profit margin.

To the extent we are forced to compete on the basis of the management fees we charge our mutual funds, we may not be able to maintain our current fee structure. Historically, we have competed primarily on the performance of our mutual funds and not on the level of our management fees relative to those of our competitors. In recent years, however, there has been a trend toward lower fees in some segments of the investment management industry. In order for us to maintain our fee structure in a competitive environment, we must be able to provide our mutual fund shareholders with investment returns and service that will encourage them to invest in the mutual funds that pay our fees. We cannot be assured that we will succeed in providing investment returns that will allow us to maintain our current fee structure. Fee reductions on existing or future business could have a material adverse effect on our results of operations.

-We may be required to forego all or a portion of our fees under our management agreements covering our mutual funds.

The board of directors or trustees of each of our mutual funds must make certain findings regarding the reasonableness of our fees. We monitor ratios of expenses to average daily net assets and waive management fees that we would otherwise receive from, or reimburse expenses incurred by, our mutual funds if we believe that our expense ratios might lead fund investors to redeem their shares in our mutual funds in order to seek lower expense ratios with other fund managers.

We currently waive our advisor fees or reimburse fund expenses to the extent necessary to maintain expense ratio limitations on the institutional share class of our funds. In the past, fees have only been waived based on contractual obligations. However, the Company regularly analyzes the fees and has the right to waive fees at its discretion to compete with other mutual funds with lower expense ratios. Any decision to waive fees would not apply to previous periods, but would apply on a going forward basis.

-Changes in mutual fund supermarkets fee structures could reduce our revenues, increase our expenses and slow our growth.

We derive a significant portion of our sales through individual investors and investment advisors who utilize mutual fund supermarkets. Mutual fund supermarkets provide services to their customers, but instead of charging their customers for these services, they charge us and our mutual funds. Fees paid to mutual fund supermarkets may increase in the future. Higher payments to mutual fund supermarkets by us or our mutual funds could increase our expenses or reduce our revenues by decreasing our assets under management, either of which could slow our growth.

-We depend on third party investment professionals and the distribution channels they utilize to market our mutual funds.



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Our ability to distribute our mutual funds is highly dependent on access to the retail distribution systems and client bases of third party investment professionals that also offer competing investment products. These investment professionals who recommend our mutual funds may reduce or eliminate their involvement in marketing our funds at any time, or may elect to emphasize the investment products of competing sponsors or the proprietary products of their own firms. In addition, an investment professional may only distribute our mutual funds for so long as we continue to participate in the platforms of national full-service firms that permit their investment professionals to utilize no-load funds for their clients. These firms can terminate their relationships with us on short notice, limiting our participation in these platforms. Either of these events could cause the net assets of our mutual funds to decline, which would decrease our revenues and have a material adverse effect on our results of operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. DESCRIPTION OF PROPERTY.

Our principal executive offices are located at 7250 Redwood Boulevard, Suite 200, Novato, California 94945, where we occupy approximately 13,728 square feet and have the right to use all common areas. The term of our lease expires on March 31, 2012, with one three-year extension available.

Additionally, we have an office for our Co-Portfolio Manager located at One Landmark Square, Suite 424, Stamford, Connecticut 06901, where we occupy approximately 1,400 square feet. The term of our lease expires on September 30, 2011.

ITEM 3. LEGAL PROCEEDINGS.

None.

ITEM 4. [RESERVED]

PART II

ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY  
SECURITIES  
MARKET INFORMATION

Our common stock is traded on the OTC Bulletin Board under the trading symbol HNNA.OB. Our stock began trading on July 15, 2002.

The following table sets forth the high and low sales prices for our common stock on the OTC Bulletin Board for the periods indicated:

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Fiscal Year Ended September 30, 2010	Price Range		Dividends Paid per Share
	High	Low	
First Quarter	\$ 3.35	\$ 2.50	
Second Quarter	2.95	2.41	\$ 0.09(1)
Third Quarter	3.45	2.48	
Fourth Quarter	2.78	2.20	

  

Fiscal Year Ended September 30, 2009	Price Range		Dividends Paid per Share
	High	Low	
First Quarter	\$ 5.00	\$ 1.50	
Second Quarter	3.00	2.00	\$ 0.09(2)
Third Quarter	3.75	2.10	
Fourth Quarter	3.50	3.00	

(1) We paid a cash dividend on March 4, 2010 of \$0.09 per share.

(2) We paid a cash dividend on March 5, 2009 of \$0.09 per share.

On October 25, 2010, the last reported sale price of our common stock on the OTC Bulletin Board was \$2.50 per share.

**HOLDERS**

As of October 28, 2010, there were 164 holders of record of Common Stock of the Company. The 164 holders of record include several brokerage firm accounts which represent about 450 additional individual shareholders for approximately 614 total shareholders as of October 28, 2010.

**DIVIDENDS**

We paid a cash dividend of \$0.09 per share on March 4, 2010.

We announced an additional cash dividend of \$0.09 per share to be paid on November 18, 2010 to shareholders of record as of October 27, 2010.

The declaration and payment of dividends to holders of our common stock by us, if any, are subject to the discretion of our board of directors. Our board of directors will take into account such matters as general economic and business conditions, our strategic plans, our financial results and condition, contractual, legal and regulatory restrictions on the payment of dividends by us, and such other factors as our board of directors may consider relevant.

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## PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS

We purchased shares as part of a stock buyback program (announced August 5, 2010) as well as shares underlying vested restricted stock units ( RSUs ) from employees to provide withholding and tax payments on behalf of our employees. The stock repurchases are presented in the following table for the quarter ended September 30, 2010:

Period	Total number of shares purchased (a)	Average price paid per share (3) (b)	Total number of shares purchased as part of publicly announced plans or programs (4) (c)	Maximum number of shares that may yet be purchased under the plans or programs (4) (d)
July 2010	0	\$ 0.00	0	0
August 2010	2,076(1)	\$ 2.59	1,950	998,050
September 2010	89,243(2)	\$ 2.40	89,243	908,807
Total (5)	91,319	\$ 2.40	91,193	908,807

- (1) Includes 125 shares owned and tendered by employees to pay for tax expense and withholding on the compensation recognized for vested RSU s; and 1,951 shares repurchased pursuant to the stock buyback program described below.
- (2) The 89,243 shares repurchased in September, 2010 were repurchased pursuant to the stock buyback program described below.
- (3) Average price paid per share is calculated on a settlement basis and excludes commission.
- (4) The share repurchases above (other than those related to vested RSU s) were completed pursuant to a plan announced August 5, 2010. The company is authorized to purchase a maximum of 1,000,000 shares. The plan has no expiration date.

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The following financial information is derived from the Company's audited consolidated financial statements, included in the Company's annual reports, and should be read in conjunction therewith.

Hennessy Advisors, Inc.

**Financial Highlights**

(In thousands, except per share amounts)

Years Ended September 30,

	2010	2009	2008	2007	2006
<b>Income Statement Data:</b>					
Revenue	\$ 7,723	\$ 5,813	\$ 10,275	\$ 16,072	\$ 16,934
Net income (loss)	\$ 913	\$ (195)	\$ 1,611	\$ 4,133	\$ 4,403
<b>Balance Sheet Data:</b>					
Total assets	\$ 31,899	\$ 30,099	\$ 34,335	\$ 35,704	\$ 33,107
Cash and cash equivalents	\$ 8,054	\$ 5,747	\$ 12,788	\$ 13,760	\$ 10,360
Long-term debt	\$ 2,552	\$	\$ 4,417	\$ 6,508	\$ 8,599
<b>Per Share Data:</b>					
<b>Earnings per share:</b>					
Basic	\$ 0.16	\$ (0.03)	\$ 0.29	\$ 0.73	\$ 0.79
Diluted	\$ 0.16	\$ (0.03)	\$ 0.28	\$ 0.70	\$ 0.73
Cash dividends declared	\$ 0.09	\$ 0.09	\$ 0.09	\$ 0.08	\$ 0.06

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Forward Looking Statements**

This report contains forward-looking statements within the meaning of the securities laws, for which we claim the protection of the safe harbors for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. These forward-looking statements include statements about, among other things, assets under management, our anticipated financial performance, business prospects, new developments and similar matters, and statements preceded by, followed by or including the words expect, anticipate, intend, may, plan, will, should, believe, estimate, predict, project, continue, seek or similar expressions. We have based these forward-looking statements on our current expectations and projections about future events, based on information currently available to us. Forward-looking statements should not be read as a guarantee of future performance or results, and will not necessarily be accurate indications of the times at, or means by, which such performance or results will be achieved. These forward-looking statements are subject to risks, uncertainties and assumptions, including those described in the section entitled **Risks Relating to Our Business** and elsewhere in this report that could cause actual performance or results to differ substantially from those expressed in or suggested by the forward-looking statements.

Factors that may affect the Company's actual results include those described in Item 1A under **Risks Relating to Our Business**. There is no regulation requiring an update of any of the forward-looking statements after the date of this report and prior to our next Form 10-Q to conform these statements to actual results or to changes in our expectations.

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## Overview

We derive our operating revenue from management fees and shareholder servicing fees paid to us by the Hennessy Funds. These fees are calculated as a percentage of the average daily net assets in our mutual funds and vary from fund to fund. The fees we receive fluctuate with changes in the total net asset value of the assets in our mutual funds, which are affected by our investment performance, redemptions, completed acquisitions of management agreements, market conditions and the success of our marketing efforts. Average assets under management were \$902.8 million for the fiscal year ended September 30, 2010 compared to \$713.4 million for the prior comparable period.

The assets we manage have decreased as a result of net fund outflows. The following table illustrates the change by year in assets under management since the beginning of fiscal year 2007:

	9/30/2007	Assets Under Management At Each Fiscal Year End 2007-2010		
		9/30/2008	9/30/2009	9/30/2010
		(In Thousands)		
Beginning assets under management	\$ 2,056,253	\$ 1,720,763	\$ 876,069	\$ 923,404
Acquisition inflows			232,549	
Organic inflows	320,090	264,998	80,409	132,560
Redemptions	(917,280)	(632,474)	(231,054)	(262,547)
Market appreciation (depreciation)	261,700	(477,218)	(34,569)	99,048
Ending assets under management	\$ 1,720,763	\$ 876,069	\$ 923,404	\$ 892,465

A significant portion of our expenses, including employee compensation, are fixed and have historically demonstrated minimal variation. However, our staffing has decreased throughout the current year, causing a decrease in our expenses. Additionally, we have had increasing revenues, causing our fixed costs to become a smaller percent of revenues and therefore further increasing our profitability.

The principal asset on our balance sheet, management contracts net of accumulated amortization, represents the capitalized costs incurred in connection with the acquisition of management agreements. This asset had a net balance of \$22.3 million as of September 30, 2010 compared to \$22.2 million at the end of the prior comparable period.

The principal liability on our balance sheet is the bank debt incurred in connection with the acquisition of management agreements for the Lindner Funds and the Henlopen Fund. As of September 30, 2010, this liability had a balance of \$3.13 million, compared to \$1.95 million at the end of the prior comparable period. The current period increase in funds is due to a loan amendment to borrow an additional \$2.0 million entered into September 27, 2010, net of principal payments of \$0.83 million.

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## RESULTS OF OPERATIONS

The following table sets forth information about components of our revenue and expense for the periods shown:

	Fiscal Year Ended September 30,			
	2010	2009		
	(In thousands, except percentages)			
	Amounts	Percent of Total Revenue	Amounts	Percent of Total Revenue
<b>Revenue:</b>				
Investment advisory fees	\$ 6,887	89.2%	\$ 5,114	88.0%
Shareholder service fees	816	10.6	680	11.7
Other	20	0.2	19	0.3
<b>Total revenue</b>	<b>7,723</b>	<b>100.0</b>	<b>5,813</b>	<b>100.0</b>
<b>Operating expenses:</b>				
Compensation and benefits	2,765	35.8	3,044	52.4
General and administrative	1,847	23.9	1,980	34.1
Mutual fund distribution	662	8.6	620	10.7
Sub-advisor fees	698	9.0	239	4.1
Amortization and depreciation	128	1.7	120	2.0
<b>Total operating expenses</b>	<b>6,100</b>	<b>79.0</b>	<b>6,003</b>	<b>103.3</b>
<b>Operating income (loss)</b>	<b>1,623</b>	<b>21.0</b>	<b>(190)</b>	<b>(3.3)</b>
Interest expense	35	0.5	87	1.5
Other income (expense)	4	(0.0)	(38)	(0.7)
<b>Income (loss) before income tax expense (benefit)</b>	<b>1,584</b>	<b>20.5</b>	<b>(239)</b>	<b>(4.1)</b>
<b>Income tax expense (benefit)</b>	<b>671</b>	<b>8.7</b>	<b>(44)</b>	<b>(0.7)</b>
<b>Net income (loss)</b>	<b>\$ 913</b>	<b>11.8%</b>	<b>\$ (195)</b>	<b>(3.4)%</b>

Revenues: Total revenue increased 32.9% to \$7.7 million in the year ended September 30, 2010, due to increased average assets under management. Investment advisory fees increased 34.7% to \$6.9 million in the year ended September 30, 2010, and shareholder service fees increased 20.0% to \$0.8 million in the year ended September 30, 2010. These increases resulted from increases in the average daily net assets of our mutual funds, which can differ considerably from total net assets of our mutual funds at the end of an accounting period.

Average daily net assets in our mutual funds for the year ended September 30, 2010 increased by \$189.4 million, or 26.6%, to \$902.8 million from \$713.4 million in the prior comparable period. The increase in average daily net assets is attributable to market appreciation in nearly all of the Hennessy Funds, coupled with net inflows into the Hennessy Cornerstone Value Fund (of \$11.8 million) and the Hennessy Total Return Fund (of \$5.9 million). The increase in average daily net assets is also attributable to the fact that fiscal 2010 results include a full year of the assets held in the Hennessy Select SPARX Japan Fund (\$53.8 million) and the Hennessy Select SPARX Japan Smaller Companies Fund (\$14.8 million), which were acquired in September, 2009. The largest net outflows were from the Hennessy Cornerstone Growth Fund (\$59.2 million) and the Hennessy Focus 30 Fund (\$51.7 million).

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Almost a quarter of the average daily net assets (\$220.3 million) for the year are concentrated in the Hennessy Cornerstone Growth Fund. All of the largest funds generate revenue at a rate of 0.84% of average daily net assets, except for the Hennessy Select Large Value Fund, which generates revenue at a rate of 0.95% of average daily net assets. However, the Company pays a sub-advisor fee of 0.35% of average daily net assets of the Hennessy Select Large Value Fund, which reduces the net impact to the Company's financial operations.

Total net assets of \$892.5 million in our mutual funds decreased by \$30.9 million, or 3.4%, as of September 30, 2010, from \$923.4 million as of the end of the prior comparable period. The \$30.9 million decrease in net mutual fund assets is attributable to net redemptions of \$130.0 million, offset by market appreciation of \$99.1 million. Redemptions as a percentage of assets under management decreased from an average of 2.5% per month to 2.4% per month during the same period due to increased assets under management.

The increase in average assets under management is mainly based on acquisitions and market appreciation due to growth in the stock market during the year. The acquisitions occurred in March and September of 2009, meaning the funds were only managed for a portion of the prior fiscal year, whereas these newly acquired funds were managed throughout the entire current fiscal year. Offsetting this increase, there are still net outflows from the Funds as investors remain apprehensive of the equity market, though net outflows have decreased from the prior year.

The market appreciation was due, among other factors, to the following:

During the most recent economic downturn, many public companies reduced their expenses, such as their number of employees, creating leaner, more profitable companies. The increased corporate profits have created an upturn in the stock market.

Even though the markets remain volatile, some investors are gradually returning to the equity market.

The economy has shown some signs of strengthening, which has encouraged appreciation in the stock market. Redemptions from the funds were due, among other factors, to the following:

The economic environment remains a difficult one, which is still requiring some investors to draw-down liquid investments, such as investments in mutual funds, to pay for daily living expenses.

The U.S. government remains unclear on the future and their policies, which has created significant uncertainty in the economy and has contributed to the flows out of the equity markets.

The equity markets are still quite volatile, and the fear created by that volatility continues to send many mutual fund investors from equity mutual funds to fixed income investment products.

The Company has waived fees to comply with contractual expense ratio limitations, though the waiver contracts are now expired. The Company does not normally waive fees, nor does it anticipate waiving fees, on a voluntary basis. The Company waived fees of \$0.1 million for the year ended September 30, 2010, a decrease of \$0.1 million, or 49.9%, from the prior comparable period. The decrease is mainly due to the expiration of contractual waivers for the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund (on February 28, 2010) and the Hennessy Select Large Value Fund and the Hennessy Cornerstone Large Growth Fund (on March 31, 2010).

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Although the Company may earn incentive income on the Micro Cap Fund, the Company did not earn incentive income for the fiscal years ended September 30, 2010 and 2009.

**Operating Expenses:** Total operating expenses increased 1.6% to \$6.1 million in the fiscal year ended September 30, 2010, from \$6.0 million in the prior comparable period. The increase is due to: increased sub-advisor fees paid on the Hennessy Select Series of Funds (acquired in March and September, 2009), increased mutual fund distribution fees paid on increased assets held through financial platforms and increased depreciation expense on fixed asset acquisitions. As a percentage of total revenue, total operating expenses decreased by 24.3% to 79.0% in the fiscal year ended September 30, 2010, as compared to 103.3% in the prior comparable period.

**Compensation and Benefits Expense:** Compensation and benefits decreased 9.2% to \$2.8 million in the fiscal year ended September 30, 2010, from \$3.0 million in the prior comparable period. The decrease resulted primarily from the elimination of a position in January, 2010. As a percentage of total revenue, compensation and benefits decreased by 16.6% to 35.8% for the fiscal year ended September 30, 2010, compared to 52.4% in the prior comparable period.

**General and Administrative Expenses:** General and administrative expense decreased 6.7% to \$1.8 million in the fiscal year ended September 30, 2010, from \$2.0 million in the prior comparable period, primarily due to decreases in travel expense, business development expense, and office rent due to a lease re-negotiation for the Novato office. As a percentage of total revenue, general and administrative expense decreased by 10.2% to 23.9% in the fiscal year ended September 30, 2010, from 34.1% in the prior fiscal year.

**Mutual Fund Distribution Expense:** Distribution expenses increased 6.8% to \$0.7 million in the fiscal year ended September 30, 2010, from \$0.6 million in the prior fiscal year. As a percentage of total revenue, distribution expenses decreased by 2.1% to 8.6% in the fiscal year ended September 30, 2010, from 10.7% in the prior fiscal year.

The mutual fund distribution expense consists of fees paid for our mutual funds to be offered on various financial platforms. The platforms allow consumers to purchase from numerous mutual fund companies through a single location, which provides those customers with a single statement of investments and a single source for mutual fund information and customer service. When our funds are purchased through one of these platforms, such as Charles Schwab, Fidelity, TD Ameritrade or Morgan Stanley Smith Barney, the platform typically charges us an asset based fee which is recorded in mutual fund distribution expense in our statement of operations. The fees increase or decrease in line with the value of the funds held on the platforms, which can be affected by inflows, outflows and market impact.

The increased costs in the current year are due to an increase in the value of average assets held through mutual fund platforms such as Charles Schwab, Fidelity and TD Ameritrade due to acquisitions and market appreciation. For the year ended September 30, 2010, the value of the mutual funds held on Charles Schwab (the platform that makes up over half of our mutual fund fees) increased by over 17% from the prior year, mainly due to acquisitions and market appreciation.

The incremental assets purchased through the mutual fund platforms are not as profitable as those purchased in direct shareholder accounts due to the participation fees paid on assets held in the various mutual fund platforms. All of our funds are impacted by activity on the financial platforms as they are all available on several platforms.

**Sub-Advisor Fee Expense:** Sub-advisor fee expense increased 192.1% to \$0.7 million in the fiscal year ended September 30, 2010, from \$0.2 million in the prior fiscal year. As a percentage of total revenue, sub-advisor fee expense increased by 4.9% to 9.0% in the fiscal year ended September 30, 2010, from 4.1% in the prior fiscal year. Sub-advisor fee expenses are paid on assets in our new Hennessy Select Series of Funds. The Hennessy Select Series of Funds are actively managed by outside asset managers retained by Hennessy Advisors, Inc. The Hennessy Select Large Value Fund, the first in the Hennessy Select Series of Funds, was acquired in March 2009. The Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund, the other two Hennessy Select Series of Funds, were acquired in September 2009.



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**Amortization and Depreciation Expense:** Amortization and depreciation expense increased 6.7% to \$0.13 million in the fiscal year ended September 30, 2010, from \$0.12 million in the prior fiscal year, mainly due to more depreciation expense due to fixed asset purchases in the current year.

**Interest Expense:** Interest expense decreased 59.8% to \$0.004 million in the fiscal year ended September 30, 2010 from \$0.09 million in the prior fiscal year. The decrease is a result of the decreased interest rates (prime rate was reduced to 3.25% in December 2008) as well as principal payments of \$0.8 million during the current year. As a percentage of total revenue, interest expense decreased by 1.0% to 0.5% in the fiscal year ended September 30, 2010, from 1.5% in the prior fiscal year.

**Other Income:** Other income decreased 110.5% to an expense of \$0.04 million in the fiscal year ended September 30, 2010 from income of \$0.04 million in the prior fiscal year due to declining interest rates earned on our cash investments.

**Income Taxes:** The provision for income taxes increased by 1,625% to a tax expense of \$0.7 million in the year ended September 30, 2010, from a tax benefit of \$0.04 million in the prior fiscal year due to increased profitability in the current year creating net income before taxes versus a net loss before taxes.

The large change in the permanent differences in the tax rate is due to a large negative rate in the fiscal year ended September 30, 2009, which was due to the net loss before tax in that period. (The permanent differences consist of book expenses that are not tax deductible, specifically keyman insurance premiums, fifty percent of meals and entertainment expense and club membership fees.) The positive tax rate in the fiscal year ended September 30, 2010 is due to the net income before tax in the current period. The permanent tax differences in total value decreased by \$0.01 million, or 8.5%, from the prior comparable period.

**Net Income:** Net income increased 568.2% to \$0.9 million in the fiscal year ended September 30, 2010, from net loss of \$0.2 million in the prior fiscal year, as a result of the factors discussed above.

### **Off-Balance Sheet Arrangements**

We do not have and have not had any off-balance sheet arrangements.

### **Liquidity and Capital Resources**

We continually review our capital requirements to ensure that we have sufficient funding available to support our growth strategies. Management anticipates that cash and other liquid assets on hand as of September 30, 2010 will be sufficient to meet our short-term capital requirements. To the extent that liquid resources and cash provided by operations are not adequate to meet long-term capital requirements, management plans to raise additional capital through debt or equity markets. There can be no assurance that we will be able to borrow funds or raise additional equity.

Total assets under management as of September 30, 2010 were \$892.5 million, which was a decrease of \$30.9 million, or 3.3%, from September 30, 2009. The primary source of our revenue, liquidity and cash flow are our fees, which are based on and generated by our average assets under management. Property and equipment and management agreements acquired totaled \$22.5 million as of September 30, 2010. We also invested \$0.5 million in the Micro Cap Fund on October 30, 2007. We intend to keep this investment, decreasing our short-term liquidity. Our remaining assets are very liquid, consisting primarily of cash and receivables derived from mutual fund asset management activities. As of September 30, 2010, we had cash and cash equivalents of \$8.1 million.

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The following table summarizes key financial data relating to our liquidity and use of cash for the years ended September 30, 2010 and 2009:

	<b>For the Fiscal Year Ended September 30,</b>	
	<b>2010</b>	<b>2009</b>
<b>Cash flow data:</b>		
Operating cash flows	\$ 2,037	\$ 873
Investing cash flows	(133)	(2,839)
Financing cash flows	403	(5,075)
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>\$ 2,307</b>	<b>\$ (7,041)</b>

The increase in cash provided by operating activities of \$1.2 million is due to a \$1.1 million, or 568%, increase in net income from the prior period. The increase in net income is due to greater average assets under management during the current period.

The decrease in cash used for investing activities is due to \$2.8 million in payments to acquire the Tamarack Large Growth Fund (now the Hennessy Cornerstone Large Growth Fund), the Tamarack Value Fund (now the Hennessy Select Large Value Fund) and costs associated with the Hennessy Select SPARX Japan Fund and the Hennessy Select SPARX Japan Smaller Companies Fund transaction made in the prior period.

The decrease in cash used for financing activities is due to a large debt paydown of \$3.5 million in the prior period. The current period increase in funds is due to a loan amendment to borrow an additional \$2.0 million on September 27, 2010.

Dividend Payments. On March 4, 2010, we paid a cash dividend of \$0.09 per common share. The total payment from cash on hand was \$0.5 million.

Our Bank Loan. We have an outstanding bank loan with U.S. Bank National Association. We incurred \$7.9 million of indebtedness in connection with acquiring the management agreements for the Lindner Funds and an additional \$6.7 million of indebtedness in connection with acquiring the management agreement for The Henlopen Fund (now known as the Hennessy Cornerstone Growth Fund, Series II). The indebtedness we incurred to acquire the management agreement of The Henlopen Fund was rolled into a single loan with the indebtedness we incurred to acquire the management agreements of the Lindner Funds. On September 27, 2010, we amended the loan to borrow an additional \$2.0 million, which bears interest at U.S. Bank National Association's prime rate, as set by U.S. Bank National Association from time to time, less one percent (2.25% as of December 17, 2008) and is secured by the Company's assets. The loan was amended to require 60 monthly payments in the amount of \$52,083 plus interest, with the final installment of the then outstanding principal and interest due on September 30, 2015. The loan agreement includes certain reporting requirements and loan covenants requiring the maintenance of certain financial ratios. We are in compliance with our loan covenants as of September 30, 2010. As of September 30, 2010, we have \$3.13 million currently outstanding under our bank loan.

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Contractual Obligations

The following table sets forth our contractual obligations as of September 30, 2010, consisting of loan payments, including the related interest payments due, and operating leases:

	Total	Payments due by period (in thousands)			More Than 5 Years
		Less Than 1 Year	1 - 3 Years	3 - 5 Years	
Principal on bank loan	\$ 3,125	\$ 521			