

**KDC Investment Management, LP**  
**September 30, 2011**

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**This brochure provides information about the qualifications and business practices of KDC Investment Management, LP (“KDCIM”), an investment advisor registered with the United States Securities and Exchange Commission (the “SEC”). If you have any questions about the content of this brochure, please contact us at 212-350-0262 or [glen@kellnerdileo.com](mailto:glen@kellnerdileo.com). This information has not been approved or verified by the United States Securities and Exchange Commission or by any state securities authority.**

**Additional information about KDCIM is also available on the SEC’s website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).**

**Registration with the SEC or with any state securities authority does not imply a certain level of skill or training.**

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**Item 2. MATERIAL CHANGES**

This brochure represents the first time we have use the SEC's new Form ADV Part 2. Much of the information called for by the firm is new and many of the responses, therefore, may differ from those in previous versions of our Form ADV. The last version of Form ADV Part II was released in March 2011. This brochure, because it is based on the new form, should be reviewed in its entirety.

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#### **Item 4. ADVISORY BUSINESS**

KDC Investment Management, LP (“KDCIM”) is an SEC registered investment advisor that was founded in 2002. KDCIM is owned by its general partner, Kellner DiLeo & Co., LLC and its limited partner, George A. Kellner.

KDCIM provides investment management services on a discretionary basis to its clients who include affiliated pooled investment vehicles intended for sophisticated investors and institutional investors and an institution with a separately managed account. Each client may impose restrictions on investing in certain securities or types of securities. KDCIM does not tailor advisory services to the individual needs of investors in the pooled investment vehicles. Investment management services are provided across four broad investment strategies; distressed/high income investing, merger arbitrage, securities lending, and event investing

As of September 30, 2011, KDCIM had approximately \$180 million of client assets under management, all on a discretionary basis.

#### **Item 5. FEES AND COMPENSATION**

KDCIM charges its affiliated pooled investment vehicles an investment management fee of 1-2% per annum of their net asset or net capital value. Investment management fees are deducted from client account on a monthly basis in arrears. Additionally, an affiliate of KDCIM, receives a performance allocation equal to 20% of the profits allocable to investors in the affiliated pooled investment vehicles (subject to a high-water mark provision). The method of calculating the performance allocation complies with Rule 205-3 under the Investment Advisors Act of 1940 (the “Advisers Act”), to the extent possible.

KDCIM or its affiliate may waive or reduce the investment management fee or performance allocation with respect to certain investors in its affiliated pooled investment vehicles

KDCIM charges its separately managed account client 45% of the profits allocable to its limited partners.

In addition to investment management fees and performance based compensation, client accounts also incur brokerage and other transaction costs. Please refer to Item 12 of the Brochure for a discussion of KDCIM’s brokerage practices. Additionally, clients may also be subject to other expenses such as administrator expenses, custodian fees, filing fees, research expenses, legal fees, compliance fees, taxes, tax preparation and audit fees. In instances where client assets are invested in ETFs and other pooled investment vehicles, the clients bear their pro rata share of the investment management and performance fees of the underlying funds.

**Item 6. PERFORMANCE –BASED FEES AND SIDE-BY-SIDE MANAGEMENT**

KDCIM provides investment management services to affiliated pooled investment vehicles and a separately managed account. KDCIM, or an affiliated entity, is entitled to be paid or allocated performance-based compensation by each of these vehicles and by the managed account. In addition, KDCIM's investment personnel are typically compensated on a basis that includes a performance-based component. Because one of the pooled investment vehicles and a separately managed account managed by KDCIM have a similar investment strategy, KDCIM and certain of its investment personnel have an incentive to favor the account that pays higher performance-based fees.

KDCIM has adopted and implemented policies and procedures intended to address conflicts of interest relating to multiple accounts that share a similar investment strategy and the allocation of investment opportunities. KDCIM reviews investment decisions for the purpose of ensuring that accounts with a similar investment strategy are treated equitably. The performance of similarly managed accounts is compared at least monthly to determine whether there are any unexplained significant discrepancies. In addition, KDCIM's procedures relating to the allocation of investment opportunities require that similarly managed accounts participate in investment opportunities pro rata based upon assets size and require to the extent that orders are aggregated, that they be done so on an average price basis. Finally, KDCIM's procedures also require that objective allocation for limited opportunities to ensure fair and equitable allocation amount accounts.

**Item 7. TYPES OF CLIENTS**

KDCIM's clients consist of affiliated pooled investment vehicles and an institutional separately managed account. The underlying investors in the affiliated pooled investment vehicles consist primarily of high net worth individual, trusts, foundations, educational institutions, non profit institutions and other pooled investment vehicles.

KDCIM generally requires a minimum investment of \$10 million to open a separately managed account. KDCIM may change or waive this requirement.

Underlying investors in affiliated pooled investment vehicles are generally required to be Accredited Investors and Qualified Purchasers. Initial subscription minimums for investors in affiliated pooled investment vehicles are disclosed in the offering memorandum for each such vehicle.

**Item 8. METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS**

KDCIM provides investment management services to its client across four broad investment strategies; distressed/high income investing, merger arbitrage, securities lending and event investing.

***Distressed/high income investing***

Generally speaking, distressed/high income investing involves the purchase of securities in companies experiencing financial or operating difficulties. The principal objective is to invest in undervalued, under-followed, out-of-favor, or oversold securities in order to achieve a relatively high absolute return through the realization of increases in the trading prices of portfolio securities and interest income.

The investment process involves the continuous screening of the distressed and high income universe to optimize investment selection, maximize total returns, and manage risk. KDCIM utilizes a rigorous analytical process with investment decisions based on fundamental analysis, valuation, timing and risk/reward considerations.

The distressed/high income portfolio may be constructed of both long securities and securities sold short. Positions may be financed through the use of leverage. KDCIM may also purchase or sell options on the underlying equity securities in order to enhance returns or reduce risk. Investments and trades are made without regard to portfolio turnover considerations, and therefore annual portfolio turnover rate may be high. Such frequent trading affects investment performance through increased brokerage and transaction costs and the realization of taxable gains and losses.

Distressed and high income securities transactions are subject to a number of risks. Because of the inherently speculative nature of this activity, results may be expected to fluctuate from month to month and from period to period.

Debt securities generally are subject to credit risk. Credit risk relates to the ability of the issuer of a debt instrument to make interest and principal payments as they become due. If the issuer fails to pay interest, the portfolio's income might be reduced. If the issuer fails to repay principal, the value of the debt instrument and the portfolio might be reduced. Investments in debt securities that are below investment grade are particularly subject to risks of default. Debt securities below investment grade tend to offer higher yields than investment grade securities to compensate investors for the higher risk of default.

A portion of the distressed/high yield portfolio may be invested in securities of companies with small market capitalizations that may not be well known to the general public, have limited trading volumes and may have been in operation for only a short period of time. Such trading and investing may entail more risk because such securities are likely to be more volatile and have less trading liquidity than securities of more established companies.

KDCIM may, from time to time, employ various hedging techniques to reduce the risk of speculative investments in securities. There remains a substantial risk, however, that hedging techniques may not always be effective in limiting losses. If the portfolio manager analyzes market conditions incorrectly or employs a strategy that does not correlate well with the portfolio's investments, the hedging techniques could result in a loss, regardless of whether the intent was to reduce risk or increase return. These hedging techniques may also increase the volatility of results, involve a small investment of cash relative to the magnitude of risk assumed, or result in a loss if the other party to the transaction does not perform as promised.

The distressed/high yield portfolio is not subject to any significant limitations on the amount of capital which may be committed to any one investment. KDCIM's objective is to invest its capital in those situations which the portfolio manager believes will offer the greatest risk-adjusted returns. Although KDCIM will follow a general policy of seeking to spread risk among a number of investments, the distressed/high yield portfolio may, at certain times, hold a few relatively large (in relation to its capital) securities positions, with the result that a loss in any such position could have a material adverse impact on the portfolio's capital.

Since KDCIM will increase the number and/or size of its investment positions through the use of leverage (i.e., purchasing securities by putting up only a portion of the instrument's value and in effect borrowing the remainder), the possibilities for profit and the risk of loss will be increased. As the result of the use of leverage, fluctuations in the market value of the distressed/high yield portfolio may therefore have a disproportionately large effect on the value of its capital. Leveraged investments may result in losses in excess of the amounts invested. In addition, short-term fluctuations in the level of interest rates generally will affect the operating results of the portfolio, with respect to its own borrowing costs and rebates received on short sales.

The securities markets are speculative; prices are volatile; and market movements are difficult to predict. Supply and demand for securities change rapidly and are affected by a variety of factors, including interest rates and general trends in the overall economy or particular industrial or other economic sectors. Government actions, especially those of the Federal Reserve Board, have a profound effect on interest rates, which, in turn, affect the price of securities. In addition, a variety of other factors which are inherently difficult to predict, such as domestic and international political developments, governmental trade and fiscal policies, patterns of trade and war or other military conflict can also have significant effects on such markets. The portfolio manager may have only limited ability to vary its investment portfolio in response to changing economic, financial and investment conditions. No assurance can be given as to when or whether adverse events might occur which could cause significant and immediate loss in the value of the portfolio. Even in the absence of such events, investing and trading securities can quickly lead to large losses.

KDCIM may from time to time engage in short selling. Selling securities short runs the risk of losing an amount greater than the amount invested. Short selling is subject to unlimited risk of loss because there is no limit on how much the price of the stock might

appreciate before the short position is closed. A short sale may result in a sudden and substantial loss if, for example, an acquisition proposal is made for the subject company at a substantial premium over market price.

At various times, the markets for securities purchased or sold by KDCIM, although organized and active, may nevertheless be “thin” or illiquid, making the purchase or sale of securities at desired prices or in desired quantities difficult or impossible. For example, many securities exchanges have authority to suspend trading in a particular security without notice.

If KDCIM buys an option (either to sell or purchase a security), it may pay a premium representing the market value of the option. If the option is not exercised and the security underlying the option at expiration is less than the exercise price, the portfolio may lose the entire amount of the premium. Conversely, if KDCIM sells an option (either to sell or purchase a security), it will be credited with the premium but will have to deposit margin or collateral due to its contingent liability to take or deliver the securities underlying the option in the event the option is exercised. Traders who sell options are subject to the entire loss occurring with respect to the underlying security (less any premium received). The writing or purchasing of an option runs the risk of losing the entire investment or substantially more than the entire investment, thereby causing significant losses in a relatively short period of time. The ability to trade in or exercise options also may be restricted in the event that trading in the underlying security becomes restricted. Options trading may also be illiquid in the event the portfolio manager invests in contracts with extended expirations.

### ***Merger Arbitrage***

Merger arbitrage involves the purchase and selling of public securities which are the subject of an acquisition attempt, exchange offer, tender offer, recapitalization or other corporate reorganization or liquidation. The strategy seeks profits thru the trading of securities (primarily public equities) and leverages its portfolio with borrowed funds. Investments and trades are made without regard to portfolio turnover considerations, and therefore annual portfolio turnover rate may be high. Such frequent trading affects investment performance through increased brokerage and transaction costs and the realization of taxable gains and losses.

When a proposal for a merger or an exchange offer is publicly announced, KDCIM will evaluate the proposed transaction and form a judgment as to the probability of its consummation. KDCIM utilizes a rigorous analytical process with investment decisions based on fundamental analysis, valuation, timing and risk/reward considerations.

If KDCIM determines that it is probable that the transaction will be consummated, it may purchase shares of the target company. In order to hedge against the risk of market fluctuation in the securities to be received, KDCIM may sell securities of the acquiring company short (transactions in listed stock options are also used to hedge long and short positions).



Because of the inherently speculative nature of the merger arbitrage strategy, the results of the merger arbitrage portfolios may be expected to fluctuate from month to month and from period to period.

In this activity, when KDCIM determines that it is probable that a transaction will be consummated, KDCIM will purchase securities at prices often only slightly below the anticipated value to be paid or exchanged for such securities in the merger, exchange offer or cash tender offer (and substantially above the prices at which such securities traded immediately prior to the announcement of the merger, exchange offer or cash tender offer). If the proposed merger, exchange offer or cash tender offer appears likely not to be consummated or in fact is not consummated or is delayed, the market price of the security to be tendered or exchanged will usually decline sharply by more than the difference between the purchase price and the anticipated consideration to be paid (the anticipated profit). In addition, where a security to be issued in a merger or exchange offer has been sold short in the expectation that the short position will be covered by delivery of such security when issued, failure of the merger or exchange offer to be consummated may force KDCIM to cover its short position in the market at a higher price than its short sale, with a resulting loss.

In addition, KDCIM may determine that the offer price for a security which is the subject of a tender offer is likely to be increased, either by the original bidder or by another party. In those circumstances, KDCIM may purchase securities above the offer price, thereby exposing the merger portfolio to an even greater degree of risk.

Where KDCIM determines that it is probable that a transaction will not be consummated, KDCIM may sell the securities of the target company short, at times significantly below the announced price for the securities in the transaction. If the transaction (or another transaction, such as a “defensive” merger or a “friendly” tender offer) is consummated at the announced price or a higher price, KDCIM may be forced to cover the short position in the market at a higher price than the short sale price, with a resulting loss.

The consummation of mergers, exchange offers and cash tender offers can be prevented or delayed by a variety of factors. An exchange offer or a cash tender offer by one company for the securities of another will often be opposed by the management or shareholders of the target company on the grounds that the consideration offered is inadequate or for a variety of other reasons. This opposition will often result in litigation in which it may be alleged, among other things, that the offering material supplied by the offeror contains inadequate, false or misleading disclosures, that the offeror has, by its activities in connection with the offer, violated federal and/or state securities or takeover laws, or that the proposed acquisition would violate federal antitrust laws, margin regulations or other statutes or regulations. The same allegations may be made in litigation brought by federal or state regulatory agencies or authorities to prevent or delay the proposed acquisition, including litigation brought by the SEC, the Antitrust Division of the Department of Justice or the Federal Trade Commission. Depending on the industry involved in a particular transaction, the consummation of the transaction may require the approval or non-action of other regulatory bodies, such as the Federal Reserve Board, the Department of Transportation, the Interstate Commerce Commission, the

Office of Thrift Supervision or the Federal Communications Commission. In addition, management of a target company may seek a “defensive” merger with, or a “friendly” tender offer by, a company other than the offeror, or propose its own recapitalization plan, although such action would not usually result in a loss to the Partnership.

Offerors in tender or exchange offers customarily reserve the right to cancel such offers in the above and a variety of other circumstances, including an insufficient response from shareholders of the target company. Even if the defensive activities of a target company or the actions of regulatory authorities fail to defeat an acquisition, they may result in significant delays, during which the merger portfolio’s capital will be committed to the transaction and interest charges on funds borrowed to finance its arbitrage activities in connection with the transaction may be incurred.

Where a merger, an exchange offer or a cash tender offer has been agreed upon by the management of the two companies involved, its consummation may be prevented by intervention of a government regulatory agency (as described above), a shareholder’s suit to enjoin the proposed transaction or, in the case of a merger, the failure of the shareholders of the company to be acquired, and, where necessary, the acquiring company, to approve the merger, market conditions resulting in material changes in securities prices, and a variety of other circumstances, including, but not limited to, the failure to meet certain conditions customarily specified in acquisition agreements.

The consummation of a transaction may be delayed for various reasons, including compliance with the Hart-Scott-Rodino Antitrust Improvements Act of 1976 which requires certain waiting periods before the transaction may be completed, waiting periods required under state takeover laws, and, with respect to mergers, exchange offers and recapitalization plans in which securities are to be offered, the need to register the offered securities under the Securities Act.

Cash tender offers by corporations, or their controlling shareholders, management or other affiliates, for the shares of such corporations, made with the intent of “going private”, are often opposed by minority shareholders alleging that the proposed transaction is financially inadequate or inherently unlawful, and such transactions have on occasion been enjoined. Certain rules of the SEC require especially complicated disclosures relating to such transactions concerning, among other things, the fairness of such transactions to public shareholders. Such rules can be expected to generate grounds for additional litigation by shareholders or the SEC.

An exchange offer or a cash tender offer will often be made for less than all of the outstanding securities of an issuer, with the provision that, if a greater number is tendered, securities will be accepted pro rata. Thus, after the completion of a tender offer, and at a time when the market price of the securities has declined below its cost, KDCIM may have returned to it, and be forced to sell at a loss, a portion of the securities it tendered.

KDCIM will attempt to assess all of the foregoing risk factors, and others, in determining the extent of the position it will take in the relevant securities and the price it is willing to

pay for such securities. However, many risks, such as the outcome of pending or threatened litigation, cannot be quantified.

KDCIM will not be subject to any significant limitations on the amount of the merger arbitrage portfolios' capital which may be committed to any one investment. Its objective will be to invest its capital in those situations which the KDCIM believes will offer the greatest risk-adjusted returns. Accordingly, KDCIM from time to time may hold a few, relatively large (in relation to its capital) securities positions, with the result that a loss in any such position could have a material adverse impact on the merger arbitrage portfolios' capital.

Moreover, it is likely that many of the merger arbitrage portfolios' positions will be in securities the then current market for which consists primarily of other merger arbitrage firms and partnerships. Consequently, it is likely that adverse developments of a kind which may trigger a determination to dispose of a position may require KDCIM to sell into a limited market which is crowded with other significant sellers.

Since KDCIM will maximize its investment positions by borrowing, the possibilities for profit and the risk of loss will be increased. As the amount of borrowings which the merger arbitrage portfolio may have outstanding at any time may be large in relation to its capital, fluctuations in the market value of the merger arbitrage portfolio may therefore have a disproportionately large effect on the value of its capital. In addition, short-term fluctuations in the level of interest rates generally will affect the operating results of the merger arbitrage portfolios, not only with respect to its own borrowing costs, but also with respect to their effect on the market value of target company securities and the cost of money to bidders therefore.

Changing market and economic conditions (including fluctuations in the credit markets), and other factors such as changes in U.S. federal or state tax laws, U.S. federal or state securities laws or accounting standards, may make corporate acquisitions less desirable or may make merger arbitrage less profitable or unprofitable. For example, an increase in the prices of equity securities generally might diminish the number of such transactions. In addition, legislation is proposed from time to time which would limit or prohibit certain transactions. Similarly, rule making, adjudicatory or other activities of the SEC, FINRA, or any securities exchange may make the merger arbitrage trading activities less feasible, less profitable or both.

### ***Securities Lending***

Securities lending involves the borrowing and relending of securities (U.S. equities, foreign equities, corporate bonds and government bonds) to capture the spread in interest rates between offsetting contracts. KDCIM's investment professionals use proprietary trading technology, quantitative analytics and industry relationships to locate opportunities within its counterparty network where such interest rate spread opportunities exist.

The objective of the securities lending strategy is to generate pure alpha returns with low risk principally through matched book trades. In a matched book trade, KDCIM borrows stock from one or more counterparties and then re-lends the stock to one or more other

counterparties. Both the borrow and loan are collateralized by cash and are on terms that are fixed at the time that the trade is entered, thus establishing the spread to be earned. The securities lending portfolio receives a portion of the interest earned by its lender on the cash collateral in the form of a rebate and pays a portion of that rebate to its borrower. At the conclusion of the securities loan, the borrower returns the borrowed security to the portfolio, and KDCIM in turn returns the borrowed security to its lender. Simultaneously, the lender returns the cash collateral to the portfolio, and KDCIM returns such collateral to its borrower.

In addition to matched book trades, KDCIM may engage in other related activities, including a variety of synthetic lending strategies which simulate the borrowing or lending of securities in a market neutral environment (swaps, contracts for differences, and exchange for physical/single stock futures). KDCIM may also enter into reverse repurchase agreements and non-purpose borrows with its counterparties to enhance the yield on the portfolio's capital. KDCIM may enter into term trades and use mismatch duration to add spread to the securities lending portfolio.

The principal risks of the securities lending strategy include counterparty risk, operational risk, trading risk and contractual risk.

Securities lending transactions involve risks related to the possibility of a borrower's default, insolvency or failure to return the borrowed stock. The security lending portfolio's exposure to counterparty risk is minimized through careful selection of counterparties that consist of major regulated financial institutions, well-capitalized broker dealers and global custodian banks and by close monitoring of the counterparties and aggregate exposure to each.

Exposure to potential loss resulting from counterparty risk is determined by the difference between the closing prices on all borrows and loans extended to a counterparty versus the collateral received and/or paid by such counterparty. This mark-to-market exposure is satisfied daily with each counterparty before the market opens and thus risk is limited with such counterparty. In addition, standard industry securities lending agreements provide for remedying potential shortfalls in collateral through buybacks or sales of securities to close out existing or open obligations.

Operational risk is related to the operational complexity of securities lending transactions (possibility of processing and administrative errors, as well as untimely counterparty correspondence related to corporate actions).

Securities lending activities present risks related to the potential execution of loans at a higher rate than borrowings, which would result in mismatched loans (in terms of duration and size), as well as mismatched dividend levels.

Usually, both parties negotiate terms before commitments in securities lending transactions are made, and the portfolio's domestic matched book is carried out on an open basis, which means that securities can be returned to the portfolio, or by KDCIM to

the counterparty, the next day. International trades usually have pre-determined end dates (usually after the record date), but are considered open and subject to recall.

Contractual risk relates to issues of compliance with counterparty parameters and guidelines. Standard agreements provide that if there is a default by either party, the non-defaulting party has the right to cause a liquidation of the contract and set off mutual debts and claims.

### ***Event Investing***

The investment objective of event investing is to achieve the highest total return on invested capital, consistent with minimizing the risk of loss of that capital. KDCIM will pursue this objective by allocating the event portfolio's assets among (1) investment funds sponsored and managed by an affiliate of KDCIM and (2) funds of unaffiliated investment managers with whom KDCIM has established relationships which together comprise the underlying funds. Prior to establishing a relationship with a fund manager, KDCIM will evaluate the fund, its strategy and its method of operations to assure that the fund manager has demonstrated a consistency of past success, and that the fund's strategy is one to which the Partnership is not presently exposed. The Partnership expects to invest primarily with portfolio managers who have extensive investment management experience and who invest alongside their clients' capital. The underlying funds invest in distressed/high income, merger arbitrage and securities lending and accordingly have the risks associated with each strategy as previously described.

These methods, strategies and investments involve risk of loss to clients and clients and investors in the affiliated pooled investment vehicles must be prepared to bear the loss of their entire investment.

## **Item 9. DISCIPLINARY INFORMATION**

On December 12, 2010, the Financial Industry Regulatory Authority ("FINRA") issued a "Letter of Acceptance, Waiver and Consent ("AWC") regarding KDC Securities, LP ("KDC"), an entity which is controlled by the same entity that controls KDCIM. KDC consented to the AWC without admitting or denying the findings. The AWC related to the settlement of two trades made in 2006 and 2007 and found that KDC mismarked one short sale as a long sale, failed to timely deliver threshold securities on or before settlement date on two occasions, failed to resolve these fails within the prescribed time period required by Regulation SHO and failed to specifically address Regulation SHO and threshold securities in its written supervisory procedures. The AWC censured KDC and imposed a fine of \$82,500.

On July 21, 2010, FINRA issued an AWC regarding KDC. KDC consented to the AWC without admitting or denying the findings. The AWC related to the operations of KDC's securities lending department during a period that ended in late 2004. The AWC found that KDC failed to maintain written procedures and fully accurate documents relating to the use of stock loan finders and failed to retain all required emails. The AWC censured KDC and imposed a fine of \$350,000.

**Item 10. OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS**

KDCIM has entered into investment management and administrative services agreements with affiliated pooled investment vehicles which offer limited partnership investments to their clients. The General Partner of KDCIM, Kellner DiLeo & Co., LLC, is also the General Partner and sponsor of these pooled investment vehicles. Additionally, Kellner DiLeo & Co., LLC is the General Partner and sponsor of KDC Securities, LP, an investment company registered as a broker dealer with the Securities and Exchange Commission.

Several management persons of KDCIM are registered representatives of KDC Securities, LP.

**Item 11. CODE OF ETHICS, PARTICIPATION OR INTEREST IN CLIENT TRANSACTIONS AND PERSONAL TRADING**

KDCIM has adopted a Code of Ethics (the “Code”) that obligates it and its supervised persons to put the interest of KDCIM’s clients before their own interests and to act honestly and fairly in all respects in their dealings with clients. All of KDCIM’s personnel are also required to comply with applicable federal securities laws. Clients or prospective clients may obtain a copy of the Code by contacting Glen M. Friedman, Chief Financial and Compliance Officer by email at [glen@kellnerdileo.com](mailto:glen@kellnerdileo.com), or by telephone at 212-350-0262.

KDCIM requires all personnel to obtain permission of a principal prior to opening a personal trading account with a broker-dealer. Copies of all confirmations and statements of such account must be furnished to KDCIM directly from the broker-dealer. In addition, all personal trading activity is required to be approved by a principal of KDCIM before being placed with a broker. No trading in any principal, employee or related person’s account will be permitted if such transaction would adversely affect any of KDCIM’s client accounts.

To monitor this process, personal trades are logged on a Personal Trade Blotter which is reviewed and initialed by a principal of KDCIM. Transaction activity in each principal, employee or related person’s account is reviewed periodically for compliance with KDCIM’s policy.

Interests in affiliated pooled investment vehicles sponsored by the General Partner of KDCIM are solicited to investors of KDCIM’s clients pursuant to private placement transactions exempt from registration under the Securities Act of 1933. All such investors receive a copy of the appropriate private placement memorandum which discloses among other things certain conflicts of interest which may arise.

Pursuant to investment management agreements, KDCIM regularly effects securities transactions for client accounts. Trading portfolios of clients with similar investment strategies are generally managed on a pari-passu basis. As a result, conflicts of interest may arise between the trading accounts managed for its clients.

Investment decisions are made for the KDCIM's clients in a fair and equitable manner in light of the relevant investment considerations. KDCIM considers participation by clients with similar investment objectives in each transaction unless KDCIM makes specific determination that the transaction is not suitable for a particular client. In addition legal and structural differences between KDCIM's clients may result in different trade execution.

In certain instances, simultaneous transactions will occur for KDCIM clients. Purchases and sales are then allocated between the clients so that no party will be treated less favorably than the other. While in some cases this could have a detrimental effect upon the price or value of a security for one of the parties or upon its ability to complete an entire order, in other cases coordination and the ability to participate in volume transactions will be beneficial to parties. In general, purchases and sales that are deemed appropriate for the clients are allocated pro rata in accordance with relative assets under management (subject to rounding), after taking into account relative liquidity of each party and the security in question.

## **Item 12. BROKERAGE PRACTICES**

As a general matter in executing portfolio transactions, KDCIM may deal with such brokers or dealers as may, in KDCIM's best judgment, provide prompt and reliable execution of the transaction at favorable security prices and reasonable commission rates. In selecting brokers or dealers, KDCIM will consider all relevant factors, including the price (net of applicable brokerage commissions or dealer spread), size of the order, nature of the market for the security, timing of the transaction, the reputation, experience and financial stability of the broker or dealer, the quality of service, difficulty of execution and operation facilities of the firm involved.

KDCIM may allocate brokerage to broker-dealers which provide it with research even though such broker-dealers may charge commissions which exceed those other broker-dealers may have charged for the same transaction, if in KDCIM's view the commissions are reasonable in relation to the value of the brokerage and/or research services provided by the broker-dealer, viewed in terms of either the particular transaction or KDCIM's overall responsibilities with respect to the client as to which it exercises investment discretion. Thus, a client may be deemed to be paying for research, brokerage or other services provided by the broker-dealer which are included in the commission rate.

In allocation brokerage, KDCIM may take into consideration the receipt of research services as long as the objective of seeking best price and execution with the transaction is not jeopardized. When appropriate under its discretion, KDCIM may direct

transactions for clients to broker dealers who provide KDCIM with research and brokerage products and services. The brokerage commissions used to acquire research is the arrangements are know as “soft dollars”.

All commissions paid by KDCIM clients fall within the SEC’s “safe harbor” provisions (section 28(e) of the US Securities Act of 1934, as amended) which allows an investment adviser to pay for research and brokerage services with the “soft dollars” generated by client account transactions. In determining whether a service or product qualifies as research or brokerage, KDCIM evaluates whether the service or product provides lawful and appropriate assistance to KDCIM in carrying out its investment decision-making responsibilities. Research and other services provided by brokers may include economic and market information, technical data, recommendations and market data services.

KDCIM’s Chief Compliance Officer periodically reviews and evaluates KDCIM’s soft dollar practices to determine in good faith whether, with respect to any research or other products or services received from a broker-dealer, the commissions used to obtain those products and services were reasonable in relation to the value of the brokerage, research or other products or services provided by the broker-dealer. This determination will be viewed in terms of either the specific transactions or KDCIM’s overall responsibilities to the portfolios over which KDCIM exercises investment discretion.

The use of client commissions (or markups or markdowns) to obtain research and brokerage products and services raises conflicts of interest. For example, KCIM will not have to pay for the products and services itself. This creates an incentive to KDCIM to select or recommend a broker-dealer based on its interest in receiving those products and services.

KDCIM believes that its clients benefit from the services obtained with “soft dollars” generated by trades for the accounts of its clients. However, services received by KDCIM will not be used for the exclusive benefit of any one client, and may not be distributed on a pro rata basis.

During KDCIM’s last fiscal year, as a result of client brokerage commissions (or markups or markdowns), KDCIM and/or its related persons received research reports, attended conferences, and held discussions with research analysts, among other things.

When appropriate, KDCIM aggregates client orders for the purchase or sale of the same security submitted contemporaneously for execution using the same executing broker to achieve more efficient execution or to provide for equitable treatment among client accounts. Clients participating in aggregated trades are allocated securities based on the average price achieved for such trades. Such aggregation may enable KDCIM to obtain for clients a more favorable price or better commission rate based upon the volume of a particular transaction. However, brokerage commission rates are not necessarily reduced as a result of such aggregation. In some instances, average pricing may result in higher or lower prices than otherwise obtainable by a single client. KDCIM allocates the



securities purchased or proceeds of a sale pro rate among the participant accounts, based on the purchase or sale order.

**Item 13. REVIEW OF THE ACCOUNTS**

Analysis of market conditions and positions within an account occur continuously by KDCIM's principals, portfolio managers and investment professionals. Trading strategies and portfolio positions for each account are discussed and reviewed at "morning meetings" which are held before the opening of the U.S. markets and are regularly attended by KDCIM's principals, portfolio managers and investment professionals.

In addition, KDCIM's principals, portfolio managers, investment professionals and other relevant personnel attend regularly scheduled weekly and monthly meetings to review account performance, market conditions, specific securities held, account portfolios and the risks inherent in such portfolios.

Investors in affiliated pooled investment vehicles receive monthly summaries, statements and quarterly reports describing account performance and prevailing market conditions. Annually, they receive tax return information and audited financials. They may also receive supplemental reports, data or other information upon request. The separately managed account holder regularly receives information on trade activity, positions and valuation which enables them to produce performance information.

**Item 14. CLIENT REFERRALS AND OTHER COMPENSATION**

KDCIM may allocate brokerage to broker-dealers which provide it with research even though such broker-dealers may charge commissions which exceed those other broker dealers may have charged for the same transaction, if in KDCIM's view the commissions are reasonable in relation to the value of the brokerage and/or research services provided by the broker-dealer, viewed in terms of either the particular transaction or KDCIM's overall responsibilities with respect to the account as to which it exercises investment discretion. Please see Item 12 for further information on KDCIM's brokerage practices.

KDCIM has arrangements where it may pay fees to internal and third party solicitors who introduce investors to KDCIM's affiliated pooled investment vehicles. Such fees may be based upon a flat percentage of invested capital and or profits earned on such capital.

**Item 15. CUSTODY**

This item is not applicable

**Item 16. INVESTMENT DISCRETION**

KDCIM provides investment management services on a discretionary basis to affiliated pooled investment vehicles pursuant to a grant of authority in the investment

management agreement and to a separately managed account pursuant to a sub-advisory agreement. Subject to certain limitations, restrictions and objectives set forth in the governing documents of the affiliated pooled investment vehicles and separately managed account, KDCIM has been granted complete discretion in the investment and reinvestment of client assets, is authorized to purchase and/or sell securities and other financial instruments and to determine the broker to be used for each securities transaction, subject to the requirements of best price and execution.

The sub-advisory agreement of the separately managed account restricts KDCIM from investing in certain securities such as new issues, low priced and restricted securities. In addition it provides limits with regard to exposure, concentration, liquidity, leverage

#### **Item 17. VOTING CLIENT SECURITIES**

KDCIM has adopted a written statement of Proxy Voting Policies, Procedures and Guidelines to assure that client securities over which KDCIM has voting discretion are voted in the best interests of the client and to resolve any material conflicts that may arise between the clients' interest and the interest of KDCIM. In general, the applicable portfolio manager will exercise discretion to vote securities held for client accounts in a manner consistent with achieving the investment objectives that have been established for the client's account. Any material conflicts of interest that may arise will be disclosed to, and direction will be sought from, the client and, in the absence of direction, KDCIM will abstain from voting the clients securities.

KDCIM's authority to vote proxies or act with respect to other shareholder actions is established through the delegation of discretionary authority under the investment management or sub advisory agreement with clients. Therefore, unless a client specifically reserves the right, in writing, to vote its own proxies or to take shareholder action with respect to other corporate actions requiring shareholder actions, KDCIM will vote all proxies and act on all other actions in a timely manner as part of its full discretionary authority over client assets.

Clients may obtain information on how their securities were voted or a copy of KDCIM's Proxy Voting Policies, Procedures and Guidelines by written request addressed to KDCIM.

#### **Item 18. FINANCIAL INFORMATION**

This item is not applicable.