

This brochure, dated March 30, 2012,  
provides information about the qualifications and business practices of

**MacKay Shields LLC**  
9 West 57<sup>th</sup> Street  
New York, NY 10019  
<http://www.mackayshields.com>

If you have any questions about the contents of this brochure, please contact:

Ellen Metzger  
Senior Managing Director and General Counsel  
Telephone: 212-230-3959  
Email: [ellen.metzger@mackayshields.com](mailto:ellen.metzger@mackayshields.com)

**The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission (“SEC”) or by any state securities authority. In addition, registration with the SEC does not imply a certain level of skill or training.**

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

## **MATERIAL CHANGES**

This brochure dated March 30, 2012, makes the following material changes since our last annual update to our brochure, dated March 29, 2011:

- In June 2011, we announced that we were no longer accepting new clients in our International Equity investment strategy. We discontinued managing assets in that investment strategy in December 2011.
- We included information on additional investment strategies: Crossover Investment Grade with Municipal Securities; Defensive Bond Arbitrage; Low Volatility High Yield; Municipal Total Return; Short Duration High Yield; and Global Convertible. See “Advisory Business – Clients and Investment Services”, “Fees and Compensation – Fee Schedule” and “Methods of Analysis, Investment Strategies and Risk of Loss”.
- In June 2011, we also included new fee schedules for certain fixed income investment strategies. See “Fees and Compensation – Fee Schedule”.
- In December 2011, Jeffrey S. Phlegar became our Chairman and Chief Executive Officer. At the same time, Lucille Protas, a 37-year veteran of our firm who had been serving as Acting Chief Executive Officer, became our President.

## **TABLE OF CONTENTS**

	<b>Page</b>
MATERIAL CHANGES .....	2
TABLE OF CONTENTS.....	3
ADVISORY BUSINESS .....	5
History .....	5
Clients and Investment Services .....	5
Wrap Fee Programs .....	6
Portfolio Management Practices .....	6
FEES AND COMPENSATION .....	7
Fee Schedule .....	7
Affiliated Accounts .....	11
Performance-Based Fees .....	12
Payment of Fees .....	12
Other Expenses .....	13
Termination .....	13
Sale of Investment Products and Referral of Clients .....	13
PERFORMANCE-BASED FEES AND SIDE-BY-SIDE MANAGEMENT.....	14
TYPES OF CLIENTS .....	15
METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS .....	15
Introduction .....	15
Fixed Income Investment Strategies .....	17
Other Investment Strategies .....	47
Additional Material Risks .....	50
DISCIPLINARY INFORMATION .....	56
OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS.....	56
Affiliated Broker-Dealers .....	56
Ownership, Management and Compensation .....	57
Affiliated Client Relationships .....	58
Other Arrangements with Affiliates .....	59
Additional Information About Our Activities and Affiliates.....	60
Information Barrier with Affiliates.....	61

CODE OF ETHICS, PARTICIPATION OR INTEREST IN CLIENT TRANSACTIONS AND PERSONAL TRADING .....	61
Code of Ethics.....	61
Interests of Affiliates .....	63
BROKERAGE PRACTICES.....	64
Selection and Compensation of Broker-Dealers.....	64
Soft Dollar Benefits .....	65
Brokerage for Client Referrals.....	66
Directed Brokerage .....	67
Wrap Fee Programs .....	67
Aggregating and Allocating Trades .....	68
REVIEW OF ACCOUNTS .....	69
CLIENT REFERRALS AND OTHER COMPENSATION .....	70
CUSTODY .....	71
INVESTMENT DISCRETION .....	71
VOTING CLIENT SECURITIES .....	72
FINANCIAL INFORMATION .....	73

## **ADVISORY BUSINESS**

### **History.**

MacKay Shields LLC (“MacKay Shields”) was founded in 1938 as an economic consulting firm and became a registered investment adviser in April 1969. In 1984, New York Life Insurance Company (“NYLIC”) purchased MacKay Shields. Today, our firm is a wholly-owned subsidiary of New York Life Investment Management Holdings LLC (“NYL Investments Holdings”), which in turn is wholly owned by NYLIC.

### **Clients and Investment Services.**

MacKay Shields managed approximately \$53.7 billion in assets on a discretionary basis and approximately \$4.4 billion on a non-discretionary basis, as of December 31, 2011. These figures differ from our “regulatory assets under management” reported in Part 1A of our Form ADV, which are calculated differently.

We provide discretionary and non-discretionary investment advisory services primarily to institutions such as U.S. registered investment companies, corporate pension funds, endowments and foundations, Taft-Hartley and public funds, private investment funds and other pooled investment vehicles, wrap fee programs, non-U.S. investment companies and other non-U.S. clients. In addition, we provide discretionary investment advisory services to high net worth clients.

We offer a variety of investment strategies that clients can select depending on their investment objectives. These are:

### **Fixed Income**

- Bank Debt
- Core Investment Grade
- Core Plus
- Core Plus Opportunities
- Credit Fixed Income
- Crossover Investment Grade with Municipal Securities
- Defensive Bond Arbitrage
- Emerging Market Debt
- Global High Yield
- Government/Credit
- High Yield
- High Yield Active Core
- High Yield Opportunities
- Intermediate
- Long Duration
- Low Volatility High Yield

- Municipal High Yield
- Municipal Intermediate
- Municipal Investment Grade
- Municipal Long-Term
- Municipal Short-Term
- Municipal Taxable
- Municipal Total Return
- Municipal Ultra Short
- Short Duration High Yield
- Short-Term

### **Other**

- Convertible
- Global Convertible

Our clients can impose restrictions or limitations on how we manage their accounts according to these strategies. These restrictions or limitations generally appear either in the client's investment management agreement or in the investment guidelines adopted for the account. Additional information about this process can be found under "Investment Discretion".

More detailed information about these strategies is found under "Methods of Analysis, Investment Strategies and Risk of Loss".

### **Wrap Fee Programs.**

We participate in wrap fee programs by providing portfolio management or portfolio modeling services. In some of these arrangements, we are retained as the adviser directly by the sponsor of the wrap fee program. In other wrap fee arrangements, we act as a sub-adviser when our affiliate New York Life Investment Management LLC ("NYL Investments") is the adviser. In wrap fee programs, clients typically pay a single wrap fee to the sponsor firm that covers advisory fees as well as trade and execution services, including commission costs. Our sub-advisory or advisory fee is paid out of that single wrap fee. We receive our fee either from the wrap fee sponsor or from NYL Investments. Please see "Brokerage Practices", below, for more detailed information about our brokerage practices. In the arrangements where we are providing portfolio modeling services, we do not execute any trades; instead, we designate to the sponsor (or NYL Investments) the trades that we recommend, and the sponsor (or NYL Investments) executes the trade. We do not provide portfolio modeling services for other non-wrap accounts.

### **Portfolio Management Practices.**

We may take a position for an advisory client (including a private investment fund) in a security contrary to the position held in the same security (for example, a short versus a long position) by our other clients. From time to time, short sales may be executed following long transactions for other clients in the same security, even though the short sale may have been communicated to the trading desk before the long transaction. We may also purchase a security for one client and sell the same security for another client.

We or our affiliates may purchase on behalf of clients securities that represent different classes of a security of the same issuer, or securities or other instruments that have different rights with respect to the same issuer. These securities include long-term and short-term debt and equity and private securities and assets, including bank debt or loan participation interests.

Sometimes our portfolio managers or our affiliates' portfolio managers may serve on the board of directors, a creditors' committee or a bondholders' committee of an issuer whose securities are held in client accounts. This is typically the result of the issuer filing bankruptcy or entering into a reorganization proceeding. MacKay Shields, individually as investment adviser or with other investment advisers or bondholders, may also correspond and enter into discussions and negotiations with issuers, trustees and other parties relating to defaults and alleged defaults by issuers and other parties under the indentures or other documents governing securities held by our clients. As a member of such committee or engaging in such discussions or negotiations, or as a result of investing in certain securities or assets, these portfolio managers may acquire material non-public information, which may result in restrictions on trading securities. We are not permitted to communicate any such information to or for the benefit of our clients, or otherwise to act on the basis of any such information in providing services to clients. We may also refrain from receiving material non-public information or from serving on a board of directors, creditors' committee or bondholders' committee or engaging in such discussions or negotiations in order to avoid restrictions on trading in other securities of the same issuer, even if such material non-public information might otherwise be relevant to our investment decisions.

We have separate groups of portfolio managers that may compete with each other for the same or similar investment opportunities. In most instances, the broker-dealer will determine the allocation to each group. In those instances where we are making allocation decisions among competing groups, we seek to manage client assets in a manner that is consistent with each client's investment objectives and strategies, while not favoring any one client over another client. Investment opportunities in certain securities and asset classes may be limited. As a result, a client may not receive an allocation in the first instance or as large an allocation in respect of limited investment opportunities as it might otherwise receive in the absence of such competition. This can be particularly acute if the market for the securities is illiquid and the supply limited.

## **FEES AND COMPENSATION**

We receive fees for our services based on a percentage of the value of the assets in the client's account. These are referred to as "asset-based fees". Certain clients also have performance-based fees, as more fully described under "Performance-Based Fees and Side-by-Side Management", below.

### **Fee Schedule.**

Below is our current schedule of asset-based fees, including the minimum amount for opening an account. While there is no minimum size for maintaining an account, we may impose a minimum fee.

## **FIXED INCOME**

### **Bank Debt**

*(Minimum \$75,000,000)*

0.50% annually on all assets

### **Core Investment Grade**

*(Minimum \$75,000,000)*

0.30% annually on assets up to \$75,000,000

0.25% annually on assets in excess of \$75,000,000 and less than \$150,000,000

0.20% annually on assets in excess of \$150,000,000

### **Core Plus**

*(Minimum \$75,000,000)*

0.35% annually on assets up to \$75,000,000

0.30% annually on assets in excess of \$75,000,000 and less than \$150,000,000

0.25% annually on assets in excess of \$150,000,000

### **Core Plus Opportunities**

*(Minimum \$75,000,000)*

0.40% annually on assets up to \$75,000,000

0.35% annually on assets in excess of \$75,000,000 and less than \$150,000,000

0.30% annually on assets in excess of \$150,000,000

### **Credit Fixed Income**

*(Minimum \$75,000,000)*

0.35% annually on assets up to \$75,000,000

0.30% annually on assets in excess of \$75,000,000 and less than \$150,000,000

0.25% annually on assets in excess of \$150,000,000

### **Crossover Investment Grade with Municipal Securities**

*(Minimum \$75,000,000)*

0.35% annually on assets up to \$75,000,000

0.25% annually on assets in excess of \$75,000,000 and less than \$150,000,000

0.20% annually on assets in excess of \$150,000,000

### **Defensive Bond Arbitrage**

*Minimum investment and fee schedule to be determined on a case-by-case basis*

### **Emerging Market Debt**

*(Minimum \$75,000,000)*

0.45% annually on all assets

### **Global High Yield**

*(Minimum \$75,000,000)*

0.50% on annually on all assets



**Government/Credit**

*(Minimum \$75,000,000)*

0.30% annually on assets up to \$75,000,000

0.25% annually on assets in excess of \$75,000,000 and less than \$150,000,000

0.20% annually on assets in excess of \$150,000,000

**High Yield**

*(Minimum \$50,000,000)*

0.50% annually on all assets

**High Yield Active Core**

*(Minimum \$75,000,000)*

0.50% annually on all assets

**High Yield Opportunities**

*(Minimum \$75,000,000)*

0.65% annually on all assets

(Client must be able to establish a prime brokerage arrangement)

**Intermediate**

*(Minimum \$75,000,000)*

0.25% annually on assets up to \$75,000,000

0.20% annually on assets in excess of \$75,000,000 and less than \$150,000,000

0.15% annually on assets in excess of \$150,000,000

**Long Duration**

*(Minimum \$75,000,000)*

0.30% annually on assets up to \$75,000,000

0.25% annually on assets in excess of \$75,000,000 and less than \$150,000,000

0.20% annually on assets in excess of \$150,000,000

**Low Volatility High Yield**

*(Minimum \$50,000,000)*

0.40% annually on all assets

**Municipal High Yield**

*(Minimum \$50,000,000)*

0.50% annually on assets up to \$100 million

0.40% annually on all assets thereafter

Minimum annual fee: \$250,000

**Municipal Intermediate**

*(Minimum \$20,000,000)*

0.25% annually on assets up to \$100 million  
0.20% annually on assets on the next \$400 million  
0.15% annually on assets on the next \$500 million  
0.125% annually on assets over \$1 billion

**Municipal Investment Grade**

*(Minimum \$20,000,000)*

0.25% annually on assets up to \$100 million  
0.20% annually on assets on the next \$400 million  
0.15% annually on assets on the next \$500 million  
0.125% annually on assets over \$1 billion

**Municipal Long-Term**

*(Minimum \$20,000,000)*

0.25% annually on assets up to \$100 million  
0.20% annually on assets on the next \$400 million  
0.15% annually on assets on the next \$500 million  
0.125% annually on assets over \$1 billion

**Municipal Short-Term**

*(Minimum \$20,000,000)*

0.25% annually on assets up to \$100 million  
0.20% annually on assets on the next \$400 million  
0.15% annually on assets on the next \$500 million  
0.125% annually on assets over \$1 billion

**Municipal Taxable**

*(Minimum \$20,000,000)*

0.25% annually on assets up to \$100 million  
0.20% annually on assets on the next \$400 million  
0.15% annually on assets on the next \$500 million  
0.125% annually on assets over \$1 billion

**Municipal Total Return**

*Minimum investment and fee schedule to be determined on a case-by-case basis*

**Municipal Ultra Short**

*(Minimum \$20,000,000)*

0.25% annually on assets up to \$100 million  
0.20% annually on assets on the next \$400 million  
0.15% annually on assets on the next \$500 million  
0.125% annually on assets over \$1 billion

**Short Duration High Yield**

*(Minimum \$75,000,000)*

0.45% annually on all assets

**Short-Term**

*(Minimum \$75,000,000)*

0.25% annually on assets up to \$150,000,000

0.20% annually on assets in excess of \$150,000,000

**OTHER****Convertible**

*(Minimum \$10,000,000)*

0.50% annually on assets up to \$100,000,000

0.40% annually on assets thereafter

**Global Convertible**

*(Minimum \$10,000,000)*

0.60% annually on all assets

In our sole discretion, we may change our fee schedule at any time, negotiate a performance-based fee or a different asset-based fee for any client, and/or adjust the minimum for opening any account. We may waive, rebate, reallocate or reduce asset-based and/or performance-based fees for certain clients, in our sole discretion.

**Affiliated Accounts.**

We may charge lower fees for advisory services to the accounts we manage for NYLIC and its affiliated insurance companies. These include general accounts of NYLIC and its affiliated insurance companies. In addition, such affiliated accounts may pay us a performance fee.

We may also charge lower fees for accounts we manage for NYL Investments Holdings and for NYL Investments, which, like MacKay Shields, is a wholly-owned subsidiary of NYL Investments Holdings.

We also act as investment adviser to private investment funds that we sponsor. The asset-based fees and performance fees (if applicable) payable by investors in those funds is described in each fund's offering memorandum, which is provided to investors. From time to time, we and a private investment fund may separately enter into certain arrangements with certain investors or prospective investors without applying terms negotiated with such investors, including but not limited to, terms relating to fees, to all investors in the fund. Although we may provide substantial input, the modifications are solely at the discretion of the private investment fund. To the extent we are a party to such arrangements, modifications are also subject to our discretion. Private investment funds may only enter into such arrangements as permitted by the applicable fund's operating documents, which arrangements may include terms that are more favorable than those given to other investors in such fund.

We also act as sub-adviser to certain U.S. registered open- and closed-end funds for which our affiliates or unaffiliated third parties serve as investment adviser or manager. For these sub-advisory services, we receive an asset-based fee from the investment advisers or managers to those U.S. registered funds, which is paid out of the investment advisory or management fee of the investment advisers or managers.

We also serve as sub-adviser to separate accounts managed by our affiliate McMorgan & Company LLC (“McMorgan”), a registered investment adviser which, like MacKay Shields, is a wholly-owned subsidiary of NYL Investments Holdings. For these sub-advisory services, we receive an asset-based fee from McMorgan that is paid out of the investment advisory or investment management fee received by McMorgan.

### **Performance-Based Fees.**

We have performance-based fee arrangements with certain clients. Performance-based fees may be calculated as a percentage of returns, or as a percentage of an increase in net asset value. They may be tied to a client-directed benchmark and may be subject to a loss carry forward. A performance-based fee for a client’s account may create an incentive to make riskier, more speculative investments than would be the case under a solely asset-based fee arrangement for that account. That is because we will receive a higher fee if the account’s performance exceeds the applicable benchmark. Higher fees benefit our company as well as our employees because the asset-based fees and performance-based fees we receive are included in the pool from which we pay incentive bonuses to our employees. In addition, the long-term incentive plan for our senior employees is based on our company’s financial results. However, regardless of their fee arrangements, when we manage accounts according to the same investment strategy, we anticipate that those accounts will generally have the same investment opportunities and be invested in the same or similar securities with the same or similar weighting. Please see “Performance-Based Fees and Side-by-Side Management”, below.

### **Payment of Fees.**

We generally bill clients for advisory services according to the fee schedule in their investment management agreement. Fees may be payable quarterly in advance based on the value of assets under management at the beginning of the quarter, or may be payable quarterly in arrears based on the value of assets under management at the end of the quarter. Fees also may be calculated using average assets during the billing period. We may make adjustments in the fee calculation in the event of significant withdrawals from, or deposits into, a client’s account during a calculation period. It is our policy to bill our clients for our advisory services.

### **Other Expenses.**

From time to time we engage outside counsel and financial advisors with regard to matters relating to particular issuers held in clients' portfolios. Through contractual arrangements with clients or pursuant to client policies, certain clients pay a pro rata portion of the fees of such counsel and financial advisors. We pay the balance of such fees not borne by such clients, which results in a benefit to the other clients.

Our separately managed account clients incur other fees associated with the management of client accounts in addition to the advisory fees described above. For example, your account's custodian charges a custodial fee and may also charge transaction fees or other administrative fees for services it provides. In addition, the broker-dealers that we select or recommend to execute transactions in your account charge a spread, commission or transaction fee, as the case may be, that your account pays. Registered funds and private investment funds incur expenses that are disclosed in a fund's prospectus or offering documents, which are in addition to our fees. In wrap fee programs, clients pay a single wrap fee to the sponsor firm. Our sub-advisory or advisory fee is paid out of that single wrap fee. We receive our fee either from the wrap fee sponsor or from NYL Investments. Typically, the single wrap fee also covers trade and execution services, including commission costs.

Under one of our investment strategies, if clients' guidelines permit, we invest a portion of their assets in up to two private investment funds that we manage. We do not receive a management fee from the funds with respect to those clients' investments. However, the clients utilizing that strategy pay an asset-based fee on all the assets being managed under that strategy, including the amounts invested in the funds. Clients in such investment strategies bear their proportionate share of fund expenses in connection with such investments.

More detailed information about our brokerage practices is found under "Brokerage Practices", below, including the factors that we consider when selecting or recommending broker-dealers for client transactions, including the use of client commissions to acquire research and brokerage services.

### **Termination.**

Unless otherwise specified in a client's investment agreement, our clients have the right to terminate their investment advisory contract at any time without penalty. In the event of termination, we will prorate any fees to the date of termination and we will refund any unearned fees for those clients who paid in advance.

### **Sale of Investment Products and Referral of Clients.**

Some of our employees who are registered representatives of our affiliated broker-dealer NYLIFE Distributors LLC ("NYLIFE Distributors") receive compensation for the sale of interests in private investment funds that we, our affiliates or unaffiliated third parties sponsor. See "Other Financial Industry Activities and Affiliations", below. The sales compensation paid to those employees comes out of the asset-based fee paid by such private investment funds to us or our affiliates, and is not an additional charge to such private investment funds or their investors. This practice presents a conflict of interest and gives the employee an incentive to

recommend these private investment funds based on the compensation received rather than a client's needs. There are policies and procedures in place that we believe are reasonably designed to address these conflicts of interest. For example, our employees who are registered representatives of NYLIFE Distributors may only recommend investments in these private investment funds if they believe they are suitable for the investor. In some instances, investors have the option to purchase these funds through unaffiliated brokers.

Some of our employees receive compensation from us for referring client accounts to us. See "Client Referrals and Other Compensation", below. The compensation paid to those employees comes out of the fee paid by such accounts and is not an additional charge to the account.

### **PERFORMANCE-BASED FEES AND SIDE-BY-SIDE MANAGEMENT**

Most of our clients pay us an investment advisory or management fee that is based on the amount of assets in the clients' accounts. These are commonly referred to as "asset-based fees".

Some of our clients pay us fees calculated as a percentage of returns, or as a percentage of the increase in net asset value. These fees may be tied to a client-directed benchmark and may be subject to a loss carry forward. They are commonly referred to as "performance-based fees".

Managing accounts that have a performance-based fee at the same time that we manage accounts that only have an asset-based fee is commonly referred to as "side-by-side management." Our portfolio managers may manage multiple accounts, including separate accounts, unregistered funds and registered funds, according to the same or similar investment strategies. This creates a conflict of interest by giving us an incentive to favor those accounts for which we receive a performance-based fee because we will receive a higher fee if their performance exceeds the applicable benchmark. Higher fees benefit our company as well as our employees because the asset-based fees and performance-based fees we receive are included in the pool from which we pay incentive bonuses to our employees. In addition, the long-term incentive plan for our senior employees is based on our company's financial results.

It is our policy not to favor the interest of one client over another. We address the conflicts of interest created by "side-by-side management" by having a trade allocation policy designed so that trades are allocated among client accounts in a fair and equitable manner over time. In addition, it is our policy that we will not permit cross trades between clients unless the portfolio manager instructing the trade deems it in the best interest of both clients at the time and obtains advance compliance approval of the transaction.

Regardless of their fee arrangements, when we manage accounts according to the same investment strategy, we anticipate that those accounts will generally have the same investment opportunities and be invested in the same or similar securities with the same or similar weighting. However, there are often differences in the nature or amount of securities that we buy or sell for client accounts, because of a variety of factors, including, among others:

- Specific client investment objectives
- Cash available in the account for investment
- Client-imposed investment restrictions

- Initial investment periods for new accounts
- Investment restrictions that laws or regulations impose
- Actual and anticipated cash inflows and outflows in client accounts
- Duration and/or average maturity of the client account
- Size of client account
- Deal size
- Current industry or issuer exposure in the client account
- Rounding to whole lots (for example, 100 shares or 10,000 bonds)
- Other practical limitations

We allocate securities among client accounts based on the above factors and usually do so before executing the trade. When it is impractical or not feasible to allocate prior to the execution of the trade, we will allocate the trade after the trade is executed but in no event later than the end of the day, in a fair and equitable manner among all the participating accounts, based on the above factors. In those situations in which there is a limited supply of a security, it is our general policy to make a *pro rata* allocation based on the original amounts targeted for the accounts. However, if in our portfolio managers' judgment the amount that would then be allocated to an account would be too small to properly manage, that account could be excluded from the *pro rata* allocation. More detailed information about our allocation and aggregation practice is found under "Brokerage Practices", below.

## **TYPES OF CLIENTS**

We provide discretionary and non-discretionary investment advisory services primarily to institutions such as U.S. registered investment companies, corporate pension funds, endowments and foundations, Taft-Hartley and public funds, private investment funds and other pooled investment vehicles, wrap fee programs, non-U.S. investment companies and other non-U.S. clients. In addition, we provide discretionary investment advisory services to high net worth clients. We also manage accounts for our affiliates. See "Fees and Compensation", above, and "Other Financial Industry Activities and Affiliations", below.

As shown on our schedule of fees (see "Fees and Compensation", above), there is a minimum account size for opening an account, depending on the investment strategy. We reserve the right, in our sole discretion, to adjust the account size minimum with respect to any client.

## **METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS**

### **Introduction.**

*Investment Strategies.* We offer a variety of investment strategies that clients can select depending on their investment objectives. These are:

## **Fixed Income**

- Bank Debt
- Core Investment Grade
- Core Plus
- Core Plus Opportunities
- Credit Fixed Income
- Crossover Investment Grade with Municipal Securities
- Defensive Bond Arbitrage
- Emerging Market Debt
- Global High Yield
- Government/Credit
- High Yield
- High Yield Active Core
- High Yield Opportunities
- Intermediate
- Long Duration
- Low Volatility High Yield
- Municipal High Yield
- Municipal Intermediate
- Municipal Investment Grade
- Municipal Long-Term
- Municipal Short-Term
- Municipal Taxable
- Municipal Total Return
- Municipal Ultra Short
- Short Duration High Yield
- Short-Term

## **Other**

- Convertible
- Global Convertible

We describe each of the above investment strategies, including our methods of analysis and related risks, below. Clients may adopt investment guidelines that combine elements of the above investment strategies and that contain limitations or refer to benchmarks that differ from those adopted by other clients.

Investors or potential investors in private investment funds that we sponsor should refer to the offering memoranda for those funds for a description of the investment strategies and risks associated with those funds. See “Additional Material Risks”.

*Risk of Loss.* Investing in securities involves risk of loss that clients should be prepared to bear. Please see the descriptions of risks that relate to each investment strategy. Material risks will



vary based on the types of investments purchased for the relevant strategy. Certain risks that relate to more than one investment strategy are referenced in the relevant strategy section and are fully set forth under “Additional Material Risks”.

*Methods of Analysis and Sources of Information.* We have an Investment Committee that reviews and provides objective feedback on investment results and the investment process of each investment product area. The members of our firm’s Investment Committee are senior professionals from the firm’s executive, investment and marketing areas. Some investment teams also have their own investment committees.

Our methods of security analysis include economic and industry analysis, fundamental research concerning specific companies, securities and issuers, quantitative analysis, technical analysis including computerized screening, evaluation and optimization techniques, and any other method that one or more of our investment personnel may deem appropriate from time to time. We may not utilize the described methods in connection with each investment strategy. Our investment professionals obtain information from a variety of sources, including:

- meetings and discussions with securities industry analysts
- discussion of publicly available information with issuers and company personnel, on-site inspections and corporate-sponsored meetings
- discussion with a company’s customers, competitors and suppliers
- computerized screening, evaluation, optimization studies and reports
- trade journals and services, governmental publications, statistical summaries and analysis
- with respect to private placements, the issuer and the intermediary
- rating agencies, analysts’ reports and various news and industry sources, on-line sources and periodicals
- such other sources as one or more of our investment personnel deem appropriate from time to time

### **Fixed Income Investment Strategies.**

#### **BANK DEBT**

##### *Investment Strategies*

The strategy focuses on high-yield investments in loan participation interests (bank debt).

This strategy may also invest in high-yield corporate debt securities, and may be composed of all types of high-yield domestic and foreign corporate debt securities that are rated below investment grade or, if unrated, that we determine to be of comparable quality.

The strategy may also invest in common stocks and other equity securities. In times of unusual or adverse market, economic or political conditions, the strategy may invest without limit in investment grade securities and may include a significant amount of U.S. government securities, or other high quality money market instruments.

This strategy imposes limits relating to credit, issuer and industry concentrations, as well as instrument type and duration.

This strategy rigorously follows a strict sell discipline. We will typically sell a loan or other instrument for one (or more) of the following reasons:

- credit deterioration
- repositioning caused by a change in our top-down outlook
- excessive downward price volatility
- recognition of a more attractive alternative relative value opportunity

### *Material Risks*

*Loan Participation Interest Risk.* There may not be a readily available market for loan participation interests, which in some cases could result in the strategy disposing of such interests at a substantial discount from face value or holding such interests until maturity. In addition, there is also the credit risk of the underlying corporate borrower as well as the lending institution or other participant from whom the strategy purchased the loan participation interests.

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as “junk bonds”) are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Convertible Securities Risk
- Currency Risk
- Debt Securities Risk
- Distressed Securities Risk
- Equity Securities Risk
- Floating Rate Loans Risk
- Foreign Securities Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Money Market/Short-Term Securities Risk
- Valuation Risk

## CORE INVESTMENT GRADE

### *Investment Strategies*

This strategy invests a substantial portion of its assets in all types of debt securities, such as: debt or debt-related securities issued or guaranteed by the U.S. or foreign governments, their agencies or instrumentalities; obligations of international or supranational entities; debt securities issued by U.S. or foreign corporate entities; zero coupon bonds; municipal bonds; and mortgage-related and other asset-backed securities. A majority of the strategy's total assets will be invested in debt securities that are rated investment grade or, if unrated, that we determine to be of comparable quality. The strategy may invest in mortgage dollar rolls, to-be-announced securities transactions (TBAs) and mortgage- and asset-backed securities. The strategy also invests in variable rate notes and floaters, as well as money market instruments and cash equivalents. The strategy's principal investments may have fixed or floating rates of interest.

The strategy may also include derivatives, such as financial futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

This strategy employs a top-down, macro-overlay incorporating the risk cycle; a relative value risk analysis incorporating what we believe to be the important fixed income risk factors; a bottom-up assessment of sector valuations; and a bottom-up analysis of security relative valuation.

### *Material Risks*

*Debt Securities Risk.* The risks of investing in debt securities include (without limitation): (i) credit risk -- the issuer may not repay the loan created by the issuance of that debt security; (ii) maturity risk -- a debt security with a longer maturity may fluctuate in value more than one with a shorter maturity; (iii) market risk -- low demand for debt securities may have a negative impact on their price; (iv) interest rate risk -- when interest rates go up, the value of a debt security goes down, and when interest rates go down, the value of a debt security goes up; (v) selection risk -- the securities that we select may underperform the market or other securities selected by other funds; and (vi) call risk -- during a period of falling interest rates, the issuer may redeem a security by repaying it early, which may reduce the strategy's income, if the proceeds are reinvested at lower interest rates.

Please see below under "Additional Material Risks" regarding the following risks:

- Derivatives Risk
- Floaters and Variable Rate Notes Risk
- Foreign Securities Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Mortgage Dollar Roll Transaction Risk

- Mortgage-Backed/Asset-Backed Securities Risk
- To-Be-Announced Securities Risk
- Valuation Risk

## **CORE PLUS**

### *Investment Strategies*

This strategy follows the Core Investment Grade strategy (see above), but also invests a portion of assets in high yield bonds and foreign bonds of developed countries and emerging countries. We refer to these as “plus” sectors, for their potential to add incremental returns. Some of the foreign securities may be denominated in foreign currency. The strategy invests in countries that are considered emerging markets, but may invest in countries with established economies that we believe present favorable conditions.

With respect to the “plus” sectors, we purchase high yield bonds that are generally rated below investment grade or, if unrated, that we determine to be of comparable quality.

The strategy may also include derivatives, such as futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings. In addition, the strategy may buy and sell currency on a spot basis and enter into foreign currency forward contracts for risk management.

### *Material Risks*

*Debt Securities Risk.* The risks of investing in debt securities include (without limitation): (i) credit risk -- the issuer may not repay the loan created by the issuance of that debt security; (ii) maturity risk -- a debt security with a longer maturity may fluctuate in value more than one with a shorter maturity; (iii) market risk -- low demand for debt securities may have a negative impact on their price; (iv) interest rate risk -- when interest rates go up, the value of a debt security goes down, and when interest rates go down, the value of a debt security goes up; (v) selection risk -- the securities that we select may underperform the market or other securities selected by other funds; and (vi) call risk -- during a period of falling interest rates, the issuer may redeem a security by repaying it early, which may reduce the strategy’s income, if the proceeds are reinvested at lower interest rates.

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as “junk bonds”) are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

*Foreign Securities Risk.* Investments in foreign securities are subject to risks that differ from those of U.S. issuers. These risks may include: fluctuating currency values; less liquid trading markets; greater price volatility; political and economic instability; less publicly available

information about issuers; changes in U.S. or foreign tax or currency laws; and changes in monetary policy. Foreign securities may be more difficult to sell than U.S. securities. These risks may be greater in emerging market countries than in more developed countries. Please see a more detailed description of Foreign Securities Risk under “Additional Material Risks”, below.

Please see below under “Additional Material Risks” regarding the following risks:

- Currency Risk
- Derivatives Risk
- Distressed Securities Risk
- Floaters and Variable Rate Notes Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- To-Be-Announced Securities Risk
- Valuation Risk

## **CORE PLUS OPPORTUNITIES**

### *Investment Strategies*

This strategy invests primarily in investment grade debt securities and seeks to add incremental returns by taking opportunistic exposures to asset classes such as international fixed income, emerging market debt and high yield debt securities. Eligible investments generally include, but are not limited to, U.S. Treasuries, TIPS, agencies, corporates, mortgage- and asset-backed securities, preferred securities, convertible securities, bank loans, taxable municipals and money market instruments (including STIF) and the strategy may make both long and short investments. We evaluate long and short term investments across the fixed income spectrum combining both top-down and bottom-up processes.

Additionally, where client guidelines permit, this strategy typically makes allocations in up to two private funds that are also managed by the same investment team.

The strategy may also include derivatives, such as financial futures, to try to manage interest rate risk. In addition, the strategy may buy and sell currency on a spot basis and enter into foreign currency forward contracts for risk management.

### *Material Risks*

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as “junk bonds”) are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In

times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

*Foreign Securities Risk.* Investments in foreign securities are subject to risks that differ from those of U.S. issuers. These risks may include: fluctuating currency values; less liquid trading markets; greater price volatility; political and economic instability; less publicly available information about issuers; changes in U.S. or foreign tax or currency laws; and changes in monetary policy. Foreign securities may be more difficult to sell than U.S. securities. These risks may be greater in emerging market countries than in more developed countries. Please see a more detailed description of Foreign Securities Risk under “Additional Material Risks”, below.

*Private Investment Funds Risk.* The investment strategies and risks associated with the private funds that may be used in this strategy are set forth in the offering memoranda for those funds that are provided to investors.

Additional material risks associated with an investment in the portfolio include the following: (i) not all U.S. government securities are insured or guaranteed by the U.S. Government - some are backed only by the issuing agency, which must rely on its own resources to repay the debt; and (ii) the portfolio’s yield will fluctuate with changes in short-term interest rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Currency Risk
- Debt Securities Risk
- Derivatives Risk
- Distressed Securities Risk
- Equity Securities Risk
- Floaters and Variable Rate Notes Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- Short-Selling Risk
- Valuation Risk
- When-Issued Securities Risk

## **CREDIT FIXED INCOME**

### *Investment Strategies*

This strategy invests a substantial portion of its assets in credit-related instruments, which include all types of debt instruments, such as: debt or debt-related securities issued or guaranteed by the U.S. or foreign governments, their agencies or instrumentalities; obligations of international or supranational entities; debt securities issued by U.S. or foreign corporate entities; zero coupon bonds; municipal bonds; mortgage-related and other asset-backed securities; and

loan participation interests. This strategy combines a top-down assessment of the climate for risk and the outlook for the economy, while security selection represents the bottom-up element of the investment process. The strategy's bottom-up process for issuer selection involves an analysis of credit fundamentals, a review of company management and a competitive analysis. The strategy may also include derivatives, such as futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

### *Material Risks*

*Debt Securities Risk.* The risks of investing in debt securities include (without limitation): (i) credit risk -- the issuer may not repay the loan created by the issuance of that debt security; (ii) maturity risk -- a debt security with a longer maturity may fluctuate in value more than one with a shorter maturity; (iii) market risk -- low demand for debt securities may have a negative impact on their price; (iv) interest rate risk -- when interest rates go up, the value of a debt security goes down, and when interest rates go down, the value of a debt security goes up; (v) selection risk -- the securities that we select may underperform the market or other securities selected by other funds; and (vi) call risk -- during a period of falling interest rates, the issuer may redeem a security by repaying it early, which may reduce the strategy's income, if the proceeds are reinvested at lower interest rates.

Please see below under "Additional Material Risks" regarding the following risks:

- Currency Risk
- Derivatives Risk
- Floaters and Variable Rate Notes Risk
- Foreign Securities Risk
- High-Yield Securities Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- To-Be-Announced Securities Risk
- Valuation Risk

## **CROSSOVER INVESTMENT GRADE WITH MUNICIPAL SECURITIES**

### *Investment Strategies*

This strategy invests a substantial portion of its assets in all types of debt securities across the taxable and tax-exempt fixed income markets, such as: debt or debt-related securities issued or guaranteed by the U.S. or foreign governments, their agencies or instrumentalities; obligations of international or supranational entities; debt securities issued by U.S. or foreign corporate entities; zero coupon bonds; municipal bonds; and mortgage-related and other asset-backed securities.

Municipal bonds include debt obligations issued by or on behalf of a governmental entity or other qualifying entity/issuer that pays interest that is, in the opinion of bond counsel to the issuer, generally excludable from gross income for federal income tax purposes (except that the interest may be includable in taxable income for purposes of the federal alternative minimum tax). Municipal bonds may be obligations of a variety of issuers, such as governmental entities or other qualifying issuers. Issuers may be states, territories and possessions of the U.S. and the District of Columbia and their political subdivisions, agencies and instrumentalities. Municipal bonds also include short-term, tax-exempt obligations such as municipal notes and variable rate demand obligations.

A majority of the strategy's total assets will be invested in debt securities that are rated investment grade or, if unrated, that we determine to be of comparable quality. The strategy may invest in mortgage dollar rolls, to-be-announced securities transactions (TBAs) and mortgage- and asset-backed securities. The strategy also invests in variable rate notes and floaters, as well as money market instruments and cash equivalents. The strategy's principal investments may have fixed or floating rates of interest.

The strategy may also include derivatives, such as financial futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

The investment objective of the strategy is to optimize the asset allocation between the taxable and tax-exempt bond markets in order to maximize a portfolio's after-tax total return.

### *Material Risks*

*Debt Securities Risk.* The risks of investing in debt securities include (without limitation): (i) credit risk -- the issuer may not repay the loan created by the issuance of that debt security; (ii) maturity risk -- a debt security with a longer maturity may fluctuate in value more than one with a shorter maturity; (iii) market risk -- low demand for debt securities may have a negative impact on their price; (iv) interest rate risk -- when interest rates go up, the value of a debt security goes down, and when interest rates go down, the value of a debt security goes up; (v) selection risk -- the securities that we select may underperform the market or other securities selected by other funds; and (vi) call risk -- during a period of falling interest rates, the issuer may redeem a security by repaying it early, which may reduce the strategy's income, if the proceeds are reinvested at lower interest rates.

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under "Additional Material Risks", below.

Please see below under "Additional Material Risks" regarding the following risks:

- Build America Bonds Risk



- Derivatives Risk
- Floaters and Variable Rate Notes Risk
- Foreign Securities Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- To-Be-Announced Securities Risk
- Valuation Risk

## **DEFENSIVE BOND ARBITRAGE**

### *Investment Strategies*

The strategy seeks to take advantage of different sources of return available in U.S. securities to generate risk adjusted returns superior to those available from conventional high yield bonds. This strategy seeks to achieve this objective through the active management of U.S. dollar-denominated fixed-income corporate securities rated less than investment grade. This strategy may also invest in a range of other financial instruments including, but not limited to, common stock, preferred stock, convertible debt, bank debt, loan participations, trade claims, non-U.S. dollar-denominated securities, private placements, credit default swaps, futures, options and warrants. In addition, this strategy may take both long and short positions in the high yield bond market and other securities.

### *Material Risks*

*Debt Securities Risk.* The risks of investing in debt securities include (without limitation): (i) credit risk -- the issuer may not repay the loan created by the issuance of that debt security; (ii) maturity risk -- a debt security with a longer maturity may fluctuate in value more than one with a shorter maturity; (iii) market risk -- low demand for debt securities may have a negative impact on their price; (iv) interest rate risk -- when interest rates go up, the value of a debt security goes down, and when interest rates go down, the value of a debt security goes up; (v) selection risk -- the securities that we select may underperform the market or other securities selected by other funds; and (vi) call risk -- during a period of falling interest rates, the issuer may redeem a security by repaying it early, which may reduce the strategy's income, if the proceeds are reinvested at lower interest rates.

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as "junk bonds") are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

*Foreign Securities Risk.* Investments in foreign securities are subject to risks that differ from those of U.S. issuers. These risks may include: fluctuating currency values; less liquid trading markets; greater price volatility; political and economic instability; less publicly available information about issuers; changes in U.S. or foreign tax or currency laws; and changes in monetary policy. Foreign securities may be more difficult to sell than U.S. securities. These risks may be greater in emerging market countries than in more developed countries. Please see a more detailed description of Foreign Securities Risk under “Additional Material Risks”, below.

Additional material risks associated with an investment in the portfolio include the following: (i) not all U.S. government securities are insured or guaranteed by the U.S. Government - some are backed only by the issuing agency, which must rely on its own resources to repay the debt; and (ii) the portfolio’s yield will fluctuate with changes in short-term interest rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Currency Risk
- Derivatives Risk
- Distressed Securities Risk
- Equity Security Risk
- Floating Rate Loans Risk
- Floaters and Variable Rate Notes Risk
- Foreign Securities Risk
- High-Yield Securities Risk
- Leverage Risk
- Liquidity Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- Short Selling Risk
- To-Be-Announced Securities Risk
- Valuation Risk
- When-Issued Securities Risk

## **EMERGING MARKET DEBT**

### *Investment Strategies*

This strategy typically invests in debt securities issued by governments, their agencies and authorities, and corporations that are located in foreign countries. The strategy focuses on debt securities that are rated investment grade and below investment grade or, if unrated, that we determine to be of comparable quality. We employ a combination of top-down macro analysis for overall risk levels and asset allocation coupled with a bottom-up approach to security selection.

A significant portion of the strategy's assets typically include foreign securities, which are securities issued by companies and sovereign entities organized outside the U.S. and which may be denominated in foreign currency. The strategy principally invests in countries that are considered emerging markets, but may invest in countries with established economies that we believe present favorable conditions. The strategy may also include foreign currency options, swaps (including credit default swaps) and futures. These techniques may be used to try to increase the strategy's return, manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

We maintain quantitative models to guide country allocation decisions. We assess whether exposures should be held in U.S. dollar-denominated foreign sovereign bonds, U.S. dollar-denominated foreign corporate bonds or local currency bonds. Exposure to foreign currency may also be made by using the foreign currency forward market. The strategy may buy and sell currency on a spot basis and enter into foreign currency forward contracts for risk management.

The strategy may also include derivatives, such as futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

### *Material Risks*

*Foreign Securities Risk.* Investments in foreign securities are subject to risks that differ from those of U.S. issuers. These risks may include: fluctuating currency values; less liquid trading markets; greater price volatility; political and economic instability; less publicly available information about issuers; changes in U.S. or foreign tax or currency laws; and changes in monetary policy. Foreign securities may be more difficult to sell than U.S. securities. These risks may be greater in emerging market countries than in more developed countries. Please see a more detailed description of Foreign Securities Risk under "Additional Material Risks", below.

Please see below under "Additional Material Risks" regarding the following risks:

- Currency Risk
- Debt Securities Risk
- Derivatives Risk
- Floaters and Variable Rate Notes Risk
- High-Yield Securities Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Money Market/Short-Term Securities Risk
- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- Valuation Risk

## GLOBAL HIGH YIELD

### *Investment Strategies*

This strategy follows the same strategy as the High Yield Active Core strategy (see below), but generally invests a greater portion of assets in securities of foreign issuers. The strategy may buy and sell currency on a spot basis and enter into foreign currency forward contracts for risk management.

### *Material Risks*

*Foreign Securities Risk.* Investments in foreign securities are subject to risks that differ from those of U.S. issuers. These risks may include: fluctuating currency values; less liquid trading markets; greater price volatility; political and economic instability; less publicly available information about issuers; changes in U.S. or foreign tax or currency laws; and changes in monetary policy. Foreign securities may be more difficult to sell than U.S. securities. These risks may be greater in emerging market countries than in more developed countries. Please see a more detailed description of Foreign Securities Risk under “Additional Material Risks”, below.

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as “junk bonds”) are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Convertible Securities Risk
- Currency Risk
- Debt Securities Risk
- Derivatives Risk
- Distressed Securities Risk
- Equity Securities Risk
- Floating Rate Loans Risk
- Liquidity Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Money Market/Short-Term Securities Risk
- Valuation Risk

## GOVERNMENT/CREDIT

### *Investment Strategies*

This strategy invests a substantial portion of its assets in all types of debt securities, such as: debt or debt-related securities issued or guaranteed by the U.S. or foreign governments, their agencies or instrumentalities; obligations of international or supranational entities; debt securities issued by U.S. or foreign corporate entities; zero coupon bonds; municipal bonds; and mortgage-related and other asset-backed securities. A majority of the strategy's total assets will be invested in debt securities that are rated investment grade or, if unrated, that we determine to be of comparable quality. The strategy may invest in mortgage dollar rolls, to-be-announced securities transactions (TBAs) and mortgage- and asset-backed securities. The strategy also invests in variable rate notes and floaters, as well as money market instruments and cash equivalents. The strategy's principal investments may have fixed or floating rates of interest.

The strategy may also include derivatives such as financial futures to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

### *Material Risks*

Material risks associated with an investment in the strategy include the following: (i) not all U.S. government securities are insured or guaranteed by the U.S. Government -- some are backed only by the issuing agency, which must rely on its own resources to repay the debt; and (ii) the strategy's yield will fluctuate with changes in short-term interest rates.

Please see below under "Additional Material Risks" regarding the following risks:

- Debt Securities Risk
- Derivatives Risk
- Floaters and Variable Rate Notes Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Money Market/Short-Term Securities Risk
- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- To-Be-Announced Securities Risk
- Valuation Risk

## HIGH YIELD

### *Investment Strategies*

This strategy uses a bottom-up approach by investing in companies we believe have strategic importance in their industries, with characteristics such as low cost assets, large market shares and high barriers to entry. Focusing on securities that we believe have sufficient asset coverage, we search for companies with a near-term catalyst that we believe will drive capital appreciation. We categorize every security into one of four risk groups, which we define by asset coverage, cash flow volatility and default rates.

This strategy includes high yield corporate debt securities, consisting of all types of high yield domestic and foreign corporate debt securities that are rated below investment grade or, if unrated, that we determine to be of comparable quality.

The strategy's high yield investments may also include convertible corporate bonds, loan participation interests (bank debt), common stocks and other equity-related securities.

In times of unusual or adverse market, economic or political conditions, the strategy may invest without limit in investment grade securities and may include a significant amount of U.S. government securities, or other high quality money market instruments.

The strategy may enter into foreign currency forward contracts for risk management.

This strategy rigorously follows a strict sell discipline. We will typically sell an instrument for one of the three following reasons:

- the security has reached its target price or yield that makes its relative value unattractive
- the issuer's fundamentals have deteriorated, for example, asset coverage has been reduced to an unacceptable level
- to diversify the portfolio if a security exceeds the weightings described above

### *Material Risks*

*High-Yield Securities Risk.* Investments in high yield securities (commonly referred to as "junk bonds") are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

Please see below under "Additional Material Risks" regarding the following risks:

- Convertible Securities Risk
- Currency Risk
- Debt Securities Risk
- Derivatives Risk

- Distressed Securities Risk
- Equity Securities Risk
- Floating Rate Loans Risk
- Foreign Securities Risk
- Liquidity Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Money Market/Short-Term Securities Risk
- Valuation Risk

## **HIGH YIELD ACTIVE CORE**

### *Investment Strategies*

This strategy invests in high-yield corporate debt securities, and may be composed of all types of high-yield domestic and foreign corporate debt securities that are rated below investment grade or, if unrated, that we determine to be of comparable quality.

The strategy's high-yield investments may also include convertible corporate bonds and loan participation interests (bank debt). The strategy may also include common stocks and other equity securities.

In times of unusual or adverse market, economic or political conditions, the strategy may invest without limit in investment grade securities and may include a significant amount of U.S. government securities, or other high quality money market instruments.

This strategy imposes limits relating to credit, issuer and industry concentrations, as well as bond type and duration.

The strategy may also include derivatives, such as futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings. In addition, the strategy may buy and sell currency on a spot basis and enter into foreign currency forward contracts for risk management.

This strategy rigorously follows a strict sell discipline. We will typically sell an instrument for one (or more) of the following reasons:

- credit deterioration
- repositioning caused by a change in our top-down outlook
- excessive downward price volatility
- recognition of a more attractive alternative relative value opportunity

### *Material Risks*

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as “junk bonds”) are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Convertible Securities Risk
- Currency Risk
- Debt Securities Risk
- Derivatives Risk
- Distressed Securities Risk
- Equity Securities Risk
- Floating Rate Loans Risk
- Foreign Securities Risk
- Liquidity Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Money Market/Short-Term Securities Risk
- Valuation Risk

## **HIGH YIELD OPPORTUNITIES**

### *Investment Strategies*

This strategy follows the same strategy as the High Yield Active Core strategy (see above), but it has the ability to take short positions and reinvest the proceeds to leverage the portfolio depending upon client guidelines.

The strategy will take long positions that we believe offer the potential for attractive returns and will take short positions in securities that we believe in the aggregate will underperform the relevant benchmark. The long and short positions held by the strategy may vary over time as market opportunities develop. The proceeds from the strategy’s short positions may be used to purchase all or a portion of the additional long positions. Regulatory limitations or bans on short selling activities may prevent full implementation of the strategy. The strategy may also include futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

In pursuing the investment strategy, we seek to identify investment opportunities based on the financial condition and competitiveness of individual companies and bond structure. The



strategy's principal investments include, but are not limited to, domestic corporate debt securities; Yankee debt securities, which are dollar-denominated securities of foreign issuers that are traded in the United States; non-U.S. dollar-denominated corporate debt securities; derivatives, such as forward currency exchange contracts and swaps (including credit default swaps); and sovereign debt.

The strategy's high-yield investments may also include convertible corporate bonds and loan participation interests (bank debt).

Generally, the strategy will include distressed securities when we believe that such an investment offers significant potential for higher returns or can be exchanged for other securities that offer this potential. However, the strategy cannot guarantee that it will achieve these returns or that an issuer will make an exchange offer or emerge from bankruptcy.

### *Material Risks*

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as "junk bonds") are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

*Short Selling Risk.* If a security sold short increases in price, the strategy may have to cover its short position at a higher price than the short sale price, resulting in a loss. The strategy may have substantial short positions and must borrow those securities to make delivery to the buyer. The strategy may not be able to borrow a security that it needs to deliver or it may not be able to close out a short position at an acceptable price and may have to sell related long positions before it had intended to do so. Thus, we may not be able to successfully implement the short sale strategy due to limited availability of desired securities or for other reasons. Please see a more detailed description of Short Selling Risk under "Additional Material Risks", below.

Please see below under "Additional Material Risks" regarding the following risks:

- Convertible Securities Risk
- Currency Risk
- Debt Securities Risk
- Derivatives Risk
- Distressed Securities Risk
- Equity Securities Risk
- Floating Rate Loans Risk
- Foreign Securities Risk
- Leverage Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk

- Valuation Risk

## INTERMEDIATE

### *Investment Strategies*

This strategy invests a substantial portion of its assets in all types of debt securities, such as: debt or debt-related securities issued or guaranteed by the U.S. or foreign governments, their agencies or instrumentalities; obligations of international or supranational entities; debt securities issued by U.S. or foreign corporate entities; zero coupon bonds; municipal bonds; and mortgage-related and other asset-backed securities. A majority of the strategy's total assets will be invested in debt securities that are investment grade or, if unrated, that we determine to be of comparable quality. The strategy may invest in mortgage dollar rolls, to-be-announced securities transactions (TBAs) and mortgage- and asset-backed securities. The strategy also invests in variable rate notes and floaters, as well as money market instruments and cash equivalents. The strategy's principal investments may have fixed or floating rates of interest.

The strategy may also include derivatives, such as financial futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

This strategy employs a top-down, macro-overlay incorporating the risk cycle; a relative value risk analysis incorporating what we believe to be the important fixed income risk factors; a bottom-up assessment of sector valuations; and a bottom-up analysis of security relative valuation.

The effective maturity of the strategy's investments will generally be in intermediate maturities (three to ten years), although it may vary depending on market conditions, as we may determine. Effective maturity is a measure of a debt security's maturity that takes into consideration the possibility that the issuer may call the debt security before its maturity date.

### *Material Risks*

*Debt Securities Risk.* The risks of investing in debt securities include (without limitation): (i) credit risk -- the issuer may not repay the loan created by the issuance of that debt security; (ii) maturity risk -- a debt security with a longer maturity may fluctuate in value more than one with a shorter maturity; (iii) market risk -- low demand for debt securities may have a negative impact on their price; (iv) interest rate risk -- when interest rates go up, the value of a debt security goes down, and when interest rates go down, the value of a debt security goes up; (v) selection risk -- the securities that we select may underperform the market or other securities selected by other funds; and (vi) call risk -- during a period of falling interest rates, the issuer may redeem a security by repaying it early, which may reduce the strategy's income, if the proceeds are reinvested at lower interest rates.

Please see below under "Additional Material Risks" regarding the following risks:

- Derivatives Risk
- Floaters and Variable Rate Notes Risk
- Foreign Securities Risk

- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- To-Be-Announced Securities Risk
- Valuation Risk

## LONG DURATION

### *Investment Strategies*

This strategy typically follows the Core Investment Grade strategy (see above), but the effective maturity of this portion of the strategy's investments will generally be in the longer range (10+ years), although it may vary depending on client guidelines or market conditions, as we may determine. Effective maturity is a measure of a debt security's maturity that takes into consideration the possibility that the issuer may call the debt security before its maturity date. The strategy may buy and sell currency on a spot basis and enter into foreign currency forward contracts for risk management. If client guidelines permit, investments in high yield and/or emerging market debt may be made.

### *Material Risks*

*Debt Securities Risk.* The risks of investing in debt securities include (without limitation): (i) credit risk -- the issuer may not repay the loan created by the issuance of that debt security; (ii) maturity risk -- a debt security with a longer maturity may fluctuate in value more than one with a shorter maturity; (iii) market risk -- low demand for debt securities may have a negative impact on their price; (iv) interest rate risk -- when interest rates go up, the value of a debt security goes down, and when interest rates go down, the value of a debt security goes up; (v) selection risk -- the securities that we select may underperform the market or other securities selected by other funds; and (vi) call risk -- during a period of falling interest rates, the issuer may redeem a security by repaying it early, which may reduce the strategy's income, if the proceeds are reinvested at lower interest rates.

Please see below under "Additional Material Risks" regarding the following risks:

- Currency Risk
- Derivatives Risk
- Floaters and Variable Rate Notes Risk
- Foreign Securities Risk
- High-Yield Securities Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk

- Mortgage Dollar Roll Transaction Risk
- Mortgage-Backed/Asset-Backed Securities Risk
- To-Be-Announced Securities Risk
- Valuation Risk

## **LOW VOLATILITY HIGH YIELD**

### *Investment Strategies*

This strategy uses a bottom-up approach by investing in companies we believe have strategic importance in their industries, with characteristics such as low cost assets, large market shares and high barriers to entry. We focus on higher quality investments with the strongest credit profiles that we believe have sufficient asset coverage.

This strategy includes higher quality, short duration high yield corporate debt securities that in our view are often undervalued.

The strategy's high yield investments may also include convertible corporate bonds and loan participation interests (bank debt).

In times of unusual or adverse market, economic or political conditions, the strategy may invest without limit in investment grade securities and may include a significant amount of U.S. government securities, or other high quality money market instruments.

The strategy may enter into foreign currency forward contracts for risk management.

This strategy rigorously follows a strict sell discipline. We will typically sell an instrument for one of the three following reasons:

- the security has reached its target price or yield that makes its relative value unattractive
- the issuer's fundamentals have deteriorated, for example, asset coverage has been reduced to an unacceptable level
- to diversify the portfolio if a security exceeds the weightings described above

### *Material Risks*

*High-Yield Securities Risk.* Investments in high yield securities (commonly referred to as "junk bonds") are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

Please see below under "Additional Material Risks" regarding the following risks:

- Convertible Securities Risk
- Currency Risk

- Debt Securities Risk
- Derivatives Risk
- Distressed Securities Risk
- Equity Securities Risk
- Floating Rate Loans Risk
- Foreign Securities Risk
- Liquidity Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Money Market/Short-Term Securities Risk
- Valuation Risk

## **MUNICIPAL HIGH YIELD**

### *Investment Strategies*

The strategy may invest in municipal bonds in any rating category, but focuses on medium- to low-quality, including municipal bonds that are the subject of bankruptcy proceedings, that are in default as to the payment of principal or interest, or that are rated in the lowest rating category or, if unrated, that we determine to be of comparable quality (“distressed securities”). It is possible that the strategy could invest up to 100% of its assets in these securities. However, the strategy reserves the right to invest less of its assets in medium- to low-quality bonds if we determine that there is insufficient supply of such obligations available for investment. The strategy will generally include investments in municipal bonds that have a maturity of five years or longer at the time of purchase.

Municipal bonds include debt obligations issued by or on behalf of a governmental entity or other qualifying entity/issuer that pays interest that is, in the opinion of bond counsel to the issuer, generally excludable from gross income for federal income tax purposes (except that the interest may be includable in taxable income for purposes of the federal alternative minimum tax). Municipal bonds may be obligations of a variety of issuers, such as governmental entities or other qualifying issuers. Issuers may be states, territories and possessions of the U.S. and the District of Columbia and their political subdivisions, agencies and instrumentalities. Municipal bonds also include short-term, tax-exempt obligations such as municipal notes and variable rate demand obligations.

We use active management in an effort to identify tax-exempt securities we believe to be mispriced and to build a consistent yield advantage. We focus on reducing volatility through a disciplined investment process that includes fundamental, bottom-up credit research and risk management.

The strategy may also invest in municipal bonds that are related in such a way that an economic, business or political development or change affecting one such security could also affect the other securities.

The strategy may also invest in industrial development bonds. Such bonds are usually revenue bonds issued to pay for facilities with a public purpose operated by private corporations. The credit quality of industrial development bonds is usually directly related to the credit standing of the owner or user of the facilities.

Generally, the strategy will incorporate distressed securities when we believe that such an investment offers significant potential for higher returns or can be exchanged for other securities that offer this potential. However, the strategy cannot guarantee that it will achieve these returns or that an issuer will make an exchange offer or emerge from bankruptcy.

The strategy may also invest in Build America Bonds, which are taxable municipal securities issued by state and local governments.

The strategy may include derivatives, such as futures, options and swap agreements to seek enhanced returns or to reduce the risk of loss of (that is, hedge) certain of its holdings.

### *Material Risks*

*High Yield Municipal Bonds Risk.* High yield municipal bonds may be subject to increased liquidity risk as compared to other high yield debt securities. There may be little or no active trading market for certain high yield municipal bonds, which may make it difficult for the strategy to sell such securities at or near their perceived value. In such cases, the value of a high yield municipal bond may decline dramatically, even during periods of declining interest rates. The high yield municipal bonds in which the strategy intends to invest may be more likely to pay interest that is includable in taxable income for purposes of the federal alternative minimum tax than other municipal bonds.

The strategy may invest more heavily in bonds from certain cities, states or regions than others, which may increase the strategy's exposure to losses resulting from economic, political, or regulatory occurrences impacting these particular cities, states or regions.

Investments in high-yield securities (commonly referred to as "junk bonds") are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under "Additional Material Risks", below.

*Distressed Securities Risk.* Investments in distressed securities are subject to substantial risks in addition to the risks of investing in other types of high-yield securities. Distressed securities are speculative and involve substantial risk that principal will not be repaid. Generally, the strategy will not receive interest payments on such securities and may incur costs to protect its investment. In addition, the strategy's ability to sell distressed securities and any securities received in exchange for such securities may be restricted.

Please see below under "Additional Material Risks" regarding the following risks:

- Build America Bonds Risk
- Debt Securities Risk
- Derivatives Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

## **MUNICIPAL INTERMEDIATE**

### *Investment Strategies*

This strategy follows the same strategy as Municipal Investment Grade (see below), but typically invests in municipal securities with an average modified duration between three and ten years.

### *Material Risks*

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under "Additional Material Risks", below.

Please see below under "Additional Material Risks" regarding the following risks:

- Build America Bonds Risk
- Debt Securities Risk
- Derivatives Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

## MUNICIPAL INVESTMENT GRADE

### *Investment Strategies*

The strategy focuses on municipal bonds that are rated investment grade or, if unrated, that we determine to be of comparable quality. The strategy will typically invest in municipal bonds that have a modified duration of 2.5 to 15 years.

Municipal bonds include debt obligations issued by or on behalf of a governmental entity or other qualifying entity/issuer that pays interest that is, in the opinion of bond counsel to the issuer, generally excludable from gross income for federal income tax purposes (except that the interest may be includable in taxable income for purposes of the federal alternative minimum tax). Municipal bonds may be obligations of a variety of issuers, such as governmental entities or other qualifying issuers. Issuers may be states, territories and possessions of the U.S. and the District of Columbia and their political subdivisions, agencies and instrumentalities. Municipal bonds also include short-term, tax-exempt obligations such as municipal notes and variable rate demand obligations.

The strategy includes duration management, sector allocation, yield curve positioning and buy/sell trade execution. We use active management in an effort to identify mispriced tax-exempt securities and build a consistent yield advantage. We attempt to reduce volatility through a disciplined investment process that includes fundamental, bottom-up credit research and risk management.

The strategy may also invest in municipal bonds that are related in such a way that an economic, business or political development or change affecting one such security could also affect the other securities (for example, securities whose issuers are located in the same state).

The strategy may also invest in Build America Bonds, which are taxable municipal securities issued by state and local governments.

The strategy may include derivatives, such as futures, options and swap agreements to try to enhance returns or reduce the risk of loss of (that is, hedge) certain of its holdings.

### *Material Risks*

***Municipal Securities Risk.*** Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under “Additional Material Risks”, below.

Please see below under “Additional Material Risks” regarding the following risks:

- Build America Bonds Risk
- Debt Securities Risk



- Derivatives Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

## **MUNICIPAL LONG-TERM**

### *Investment Strategies*

This strategy follows the same strategy as Municipal Investment Grade (see above), but typically invests in municipal securities with an average maturity of ten years or more.

### *Material Risks*

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under “Additional Material Risks”, below.

Please see below under “Additional Material Risks” regarding the following risks:

- Build America Bonds Risk
- Debt Securities Risk
- Derivatives Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

## **MUNICIPAL SHORT-TERM**

### *Investment Strategies*

This strategy follows the same strategy as Municipal Investment Grade (see above), but typically invests in municipal securities with a maximum maturity of two years.

### *Material Risks*

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To

be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under “Additional Material Risks”, below.

Please see below under “Additional Material Risks” regarding the following risks:

- Build America Bonds Risk
- Debt Securities Risk
- Derivatives Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

## **MUNICIPAL TAXABLE**

### *Investment Strategies*

This strategy follows the same strategy as Municipal Investment Grade (see above), but focuses the construction of the portfolio on taxable municipal securities including Build America Bonds (“BABs”) with an average modified duration between five and fifteen years. BABs are taxable municipal securities issued by state and local governments. Issuers of BABs are eligible to receive a subsidy of the U.S. Treasury of up to 35% of the interest paid on the bonds. Subsidy payments received by issuers of BABs may be subject to offset against amounts owed by them to the federal government and may be reduced or eliminated.

### *Material Risks*

*Build America Bonds.* The Build America Bond market is smaller and less diverse than the broader municipal securities market. In addition, BABs are a new form of municipal financing and bonds issued after December 31, 2010 do not qualify as BABs because the BAB enabling legislation expired on December 31, 2010. It is difficult to predict the extent to which a market for such bonds will develop, meaning that BABs may experience greater illiquidity than other types of municipal securities. There can be no assurance that BABs will be actively traded. In addition, illiquidity may have a negative effect on the value of the bonds.

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under “Additional Material Risks”, below.

Please see below under “Additional Material Risks” regarding the following risks:

- Debt Securities Risk
- Derivatives Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

## **MUNICIPAL TOTAL RETURN**

### *Investment Strategies*

The strategy may invest in municipal bonds in any rating category and will typically use between 0 and 3 times leverage to invest in municipal bonds that have a modified duration of approximately 0 to 20 years. The strategy includes duration management, sector allocation, yield curve positioning and buy/sell trade execution. We use active management in an effort to identify mispriced tax-exempt securities. The strategy may also invest in municipal bonds that are related in such a way that an economic business or political development or change affecting one such security could also affect the other securities (for example, securities whose issuers are located in the same state). The strategy may also invest in taxable bonds, including Build America Bonds. The strategy may also include derivatives, such as futures, options and swap agreements to try to enhance returns or reduce the risk of loss (that is, hedge) certain of its holdings.

Municipal bonds include debt obligations issued by or on behalf of a governmental entity or other qualifying entity/issuer that pays interest that is, in the opinion of bond counsel to the issuer, generally excludable from gross income for federal income tax purposes (except that the interest may be includable in taxable income for purposes of the federal alternative minimum tax). Municipal bonds may be obligations of a variety of issuers, such as governmental entities or other qualifying issuers. Issuers may be states, territories and possessions of the U.S. and the District of Columbia and their political subdivisions, agencies and instrumentalities. Municipal bonds also include short-term, tax-exempt obligations such as municipal notes and variable rate demand obligations.

### *Material Risks*

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To be tax-exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under “Additional Material Risks”, below.

Please see below under “Additional Material Risks” regarding the following risks:

- Build America Bonds Risk
- Debt Securities Risk
- Derivatives Risk
- Distressed Securities Risk
- High Yield Municipal Bonds Risk
- Leverage Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

## **MUNICIPAL ULTRA SHORT**

### *Investment Strategies*

The effective maturity of this portion of the strategy’s investments will generally be in short-term maturities (one month to five years), although it may vary depending on market conditions, as we may determine. Effective maturity is a measure of a debt security’s maturity that takes into consideration the possibility that the issuer may call the debt security before its maturity date.

This strategy follows the same strategy as Municipal Investment Grade (see above), but typically invests in municipal securities with maturities of 30 days or less (which may be due to put features).

### *Material Risks*

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes which could affect the market for and value of municipal securities. To be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. Please see a more detailed description of Municipal Securities Risk under “Additional Material Risks”, below.

Please see below under “Additional Material Risks” regarding the following risks:

- Build America Bonds Risk
- Debt Securities Risk
- Derivatives Risk
- Liquidity Risk
- Loss of Money Risk
- Management Risk

- Market Changes Risk
- Valuation Risk

## **SHORT DURATION HIGH YIELD**

### *Investment Strategies*

This strategy follows the same strategy as the High Yield Active Core strategy (see above), but the portfolio will focus on maintaining an overall duration that is below the average for the high yield market, typically around 2 years and below.

The strategy may be comprised of all types of high yield domestic and foreign corporate debt securities that are rated below investment grade, or if unrated, that we determine to be of comparable quality. To lower the duration of the overall portfolio we focus on securities that are shorter in duration, closer to maturity or closer to the expected call date than the average high yield bond. We may also use futures and cash in conjunction with longer duration securities to manage the duration of the overall portfolio.

The strategy's high-yield investments may also include convertible corporate bonds and loan participation interests (bank debt). The strategy may also include common stocks and other equity securities.

In times of unusual or adverse market, economic or political conditions, the strategy may invest without limit in investment grade securities and may include a significant amount of U.S. government securities, or other high quality money market instruments.

This strategy imposes limits relating to credit, issuer and industry concentrations, as well as bond type and duration.

The strategy may also include derivatives, such as futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings. In addition, the strategy may buy and sell currency on a spot basis and enter into foreign currency forward contracts for risk management.

This strategy rigorously follows a strict sell discipline. We will typically sell an instrument for one (or more) of the following reasons:

- credit deterioration
- repositioning caused by a change in our top-down outlook
- excessive downward price volatility
- recognition of a more attractive alternative relative value opportunity

### *Material Risks*

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as “junk bonds”) are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher

rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Convertible Securities Risk
- Currency Risk
- Debt Securities Risk
- Derivatives Risk
- Distressed Securities Risk
- Equity Securities Risk
- Floating Rate Loans Risk
- Foreign Securities Risk
- Liquidity Risk
- Loan Participation Interest Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Money Market/Short-Term Securities Risk
- Valuation Risk

## **SHORT-TERM**

### *Investment Strategies*

The effective maturity of this portion of the strategy’s investments will generally be in short-term maturities (one month to five years), although it may vary depending on market conditions, as we may determine. Effective maturity is a measure of a debt security’s maturity that takes into consideration the possibility that the issuer may call the debt security before its maturity date.

This strategy invests a substantial portion of its assets in all types of debt securities, such as: debt or debt-related securities issued or guaranteed by the U.S. or foreign governments, their agencies or instrumentalities; obligations of international or supranational entities; debt securities issued by U.S. or foreign corporate entities; zero coupon bonds; municipal bonds; and mortgage-related and other asset-backed securities. A majority of the strategy’s total assets will be invested in debt securities that are rated investment grade or, if unrated, that we determine to be of comparable quality. The strategy may include mortgage dollar rolls, to-be-announced securities transactions (TBAs) and mortgage- and asset-backed securities. The strategy also invests in variable rate notes and floaters, as well as money market instruments and cash equivalents. The strategy’s principal investments may have fixed or floating rates of interest.

The strategy may also include derivatives, such as futures, to try to manage interest rate risk or reduce the risk of loss of (that is, hedge) certain of its holdings.

This strategy employs a top-down, macro-overlay incorporating the risk cycle; a relative value risk analysis incorporating what we believe to be the important fixed income risk factors; a bottom-up assessment of sector valuations; and a bottom-up analysis of security relative valuation.

### *Material Risks*

*Money Market/Short-Term Securities Risk.* To the extent the strategy holds cash or invests in short-term securities, there is no assurance that the strategy will achieve its investment objective.

Additional material risks associated with an investment in the strategy include the following: (i) not all U.S. government securities are insured or guaranteed by the U.S. Government - some are backed only by the issuing agency, which must rely on its own resources to repay the debt; and (ii) the strategy's yield will fluctuate with changes in short-term interest rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Debt Securities Risk
- Derivatives Risk
- Floaters and Variable Rate Notes Risk
- Foreign Securities Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- To-Be-Announced Securities Risk
- Valuation Risk

### **Other Investment Strategies.**

#### **CONVERTIBLE**

##### *Investment Strategies*

This strategy takes a flexible approach by investing in a broad range of securities of a variety of companies and industries. This strategy seeks to identify securities that offer asymmetric return potential. Diversification is a key risk control mechanism.

This strategy primarily consists of “convertible securities” such as bonds, debentures, corporate notes, and preferred stocks or other securities that are convertible into common stock or the cash value of a stock or a basket or index of equity securities. The balance of the assets may be invested or held in non-convertible debt, equity securities that do not pay regular dividends, U.S. Government securities, and cash or cash equivalents. A convertible security is a security issued by a company that the investor can “convert” for shares at a pre-set price.

The strategy may invest in debt securities that are rated investment grade and below investment grade or, if unrated, that we determine to be of equivalent quality.

The strategy may also be comprised of “synthetic” convertible securities, which are derivative positions composed of two or more securities whose investment characteristics, taken together, resemble those of traditional convertible securities. Unlike traditional convertible securities whose conversion values are based on the common stock of the issuer of the convertible security, “synthetic” and “exchangeable” convertible securities are preferred stocks or debt obligations of an issuer which are structured with an embedded equity component whose conversion value is based on the value of the common stock of one or more different issuers or a particular benchmark (which may include indices, baskets of domestic stocks, commodities, a foreign issuer or basket of foreign stocks, or a company whose stock is not yet publicly traded). The value of a synthetic convertible is the sum of the values of its preferred stock or debt obligation component and its convertible component.

The strategy may include foreign securities, which are securities issued by companies organized outside the U.S. and traded primarily in markets outside the U.S.

### *Material Risks*

*Convertible Securities Risk.* Convertible securities may be subordinate to other securities. In part, the total return for a convertible security depends upon performance of the underlying stock into which it can be converted. Also, issuers of convertible securities are often not as strong financially as those issuing securities with higher credit ratings, are more likely to encounter financial difficulties and typically are more vulnerable to changes in the economy, such as a recession or a sustained period of rising interest rates, which could affect their ability to make interest and principal payments. If an issuer stops making interest and/or principal payments, the strategy could lose its entire investment.

*Synthetic Convertible Securities Risk.* The values of a synthetic convertible and a true convertible security may respond differently to market fluctuations. In addition, in purchasing a synthetic convertible security, the strategy may have counterparty (including counterparty credit) risk with respect to the financial institution or investment bank that offers the instrument. Purchasing a synthetic convertible security may provide greater flexibility than purchasing a traditional convertible security.

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as “junk bonds”) are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Debt Securities Risk
- Distressed Securities Risk
- Equity Securities Risk
- Foreign Securities Risk



- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

## **GLOBAL CONVERTIBLE**

### *Investment Strategies*

This strategy follows the same strategy as the Convertible strategy (see above), but generally invests a greater portion of assets in securities of foreign issuers. The strategy may buy and sell currency on a spot basis.

Unlike U.S. convertible securities, non-U.S. convertibles may not only be converted into shares at a pre-set price, but may also be converted to shares at a pre-set equation.

### *Material Risks*

*Convertible Securities Risk.* Convertible securities may be subordinate to other securities. In part, the total return for a convertible security depends upon performance of the underlying stock into which it can be converted. Also, issuers of convertible securities are often not as strong financially as those issuing securities with higher credit ratings, are more likely to encounter financial difficulties and typically are more vulnerable to changes in the economy, such as a recession or a sustained period of rising interest rates, which could affect their ability to make interest and principal payments. If an issuer stops making interest and/or principal payments, the strategy could lose its entire investment.

*Synthetic Convertible Securities Risk.* The values of a synthetic convertible and a true convertible security may respond differently to market fluctuations. In addition, in purchasing a synthetic convertible security, the strategy may have counterparty (including counterparty credit) risk with respect to the financial institution or investment bank that offers the instrument. Purchasing a synthetic convertible security may provide greater flexibility than purchasing a traditional convertible security.

*Foreign Securities Risk.* Investments in foreign securities are subject to risks that differ from those of U.S. issuers. These risks may include: fluctuating currency values; less liquid trading markets; greater price volatility; political and economic instability; less publicly available information about issuers; changes in U.S. or foreign tax or currency laws; and changes in monetary policy. Foreign securities may be more difficult to sell than U.S. securities. These risks may be greater in emerging market countries than in more developed countries. Please see a more detailed description of Foreign Securities Risk under “Additional Material Risks”, below.

*High-Yield Securities Risk.* Investments in high-yield securities (commonly referred to as “junk bonds”) are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In

times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

Please see below under “Additional Material Risks” regarding the following risks:

- Debt Securities Risk
- Distressed Securities Risk
- Equity Securities Risk
- Loss of Money Risk
- Management Risk
- Market Changes Risk
- Valuation Risk

### **Additional Material Risks.**

**The additional material risks set forth below in alphabetical order relate to all investment strategies.**

*Loss of Money Risk.* Before considering an investment in the strategy, you should understand that you could lose money.

*Management Risk.* The investment strategies, practices and risk analysis that we use may not produce the desired results.

*Market Changes Risk.* The value of the strategy’s investments may change because of broad changes in the markets in which the strategy invests, which could cause the strategy to underperform other funds with similar objectives.

**The additional material risks set forth below in alphabetical order relate to more than one investment strategy as set forth in the relevant strategy section.**

*Build America Bonds Risk.* The Build America Bond (“BAB”) market is smaller and less diverse than the broader municipal securities market. In addition, BABs are a new form of municipal financing and bonds issued after December 31, 2010 do not qualify as BABs because the BAB enabling legislation expired on December 31, 2010. It is difficult to predict the extent to which a market for such bonds will develop, meaning that BABs may experience greater illiquidity than other types of municipal securities. There can be no assurance that BABs will be actively traded. In addition, illiquidity may have a negative effect on the value of the bonds.

*Convertible Securities Risk.* Convertible securities may be subordinate to other securities. In part, the total return for a convertible security depends upon performance of the underlying stock into which it can be converted. Also, issuers of convertible securities are often not as strong financially as those issuing securities with higher credit ratings, are more likely to encounter financial difficulties and typically are more vulnerable to changes in the economy, such as a recession or a sustained period of rising interest rates, which could affect their ability to make

interest and principal payments. If an issuer stops making interest and/or principal payments, the strategy could lose its entire investment.

*Currency Risk.* The value of a client's assets may be affected favorably or unfavorably by the changes in currency rates and exchange control regulations. Some currency exchange costs may be incurred by clients when a strategy changes investments from one country to another. Currency exchange rates may fluctuate significantly over short periods of time. They generally are determined by the forces of supply and demand in the respective markets and the relative merits of investments in different countries, actual or perceived changes in interest rates and other complex factors, as seen from an international perspective. Currency exchange rates can also be affected unpredictably by intervention by governments or central banks (or the failure to intervene) or by currency controls or political developments.

*Debt Securities Risk.* The risks of investing in debt securities include (without limitation): (i) credit risk -- the issuer may not repay the loan created by the issuance of that debt security; (ii) maturity risk -- a debt security with a longer maturity may fluctuate in value more than one with a shorter maturity; (iii) market risk -- low demand for debt securities may have a negative impact on their price; (iv) interest rate risk -- when interest rates go up, the value of a debt security goes down, and when interest rates go down, the value of a debt security goes up; (v) selection risk -- the securities that we select may underperform the market or other securities selected by other funds; and (vi) call risk -- during a period of falling interest rates, the issuer may redeem a security by repaying it early, which may reduce the strategy's income, if the proceeds are reinvested at lower interest rates.

*Derivatives Risk.* The strategy may lose money using derivatives. The use of derivatives may increase the volatility of the value of the strategy's assets and may involve a small investment of cash relative to the magnitude of risk assumed. The principal risk of forward commitments is that the security may be worth less when it is issued or received than the price the strategy agreed to pay when it made the commitment. The principal risks of swap agreements are that they may be difficult to value and may be susceptible to liquidity and credit risk. The principal risk of futures contracts is that they may result in losses in excess of the amount invested in the futures contract, which may be unlimited. The principal risk of options transactions is that they may increase the volatility of the value of the strategy's assets and may involve a small investment of cash relative to the magnitude of the risk assumed. Derivatives may also be subject to counterparty risk, that is, the risk that the other party in the transaction will not fulfill its contractual obligations.

*Distressed Securities Risk.* Investments in distressed securities are subject to substantial risks in addition to the risks of investing in other types of high-yield securities. Distressed securities are speculative and involve substantial risk that principal will not be repaid. Generally, the strategy will not receive interest payments on such securities and may incur costs to protect its investment. In addition, the strategy's ability to sell distressed securities and any securities received in exchange for such securities may be restricted.

*Equity Securities Risk.* Investments in common stocks and other equity securities are particularly subject to the risk of changing economic, stock market, industry and company conditions and the risks inherent in our ability to anticipate changes that can adversely affect the value of the strategy's holdings. Opportunity for greater gain often comes with greater risk of loss.

*Floaters and Variable Rate Notes Risk.* Floaters and variable rate notes provide for a periodic adjustment in the interest rate paid on the securities. The rate adjustment intervals may be regular and range from daily up to annually, or may be based on an event, such as a change in the prime rate. Floating and variable rate notes may be subject to greater liquidity risk than other debt securities, meaning that there may be limitations on the strategy's ability to sell the securities at any given time. Securities with floating interest rates generally are less sensitive to interest rate changes, but may decline in value if their interest rates do not rise as much or as fast as interest rates in general. Such securities also may lose value.

*Floating Rate Loans Risk.* The floating rate loans in which the strategy invests are usually rated below investment grade (commonly referred to as "junk bonds") and are generally considered speculative because they present a greater risk of loss, including default, than higher quality debt securities. Moreover, such securities may, under certain circumstances, be less liquid than higher quality debt securities. Although certain floating rate loans are collateralized, there is no guarantee that the value of the collateral will be sufficient to repay the loan. In times of unusual or adverse market, economic or political conditions, floating rate loans may experience higher than normal default rates. In the event of a recession or serious credit event, among other eventualities, the value of the strategy's assets could decline.

*Foreign Securities Risk.* Investments in foreign securities are subject to risks that differ from those of U.S. issuers. These risks may include: fluctuating currency values; less liquid trading markets; greater price volatility; political and economic instability; less publicly available information about issuers; changes in U.S. or foreign tax or currency laws; and changes in monetary policy. Foreign securities may be more difficult to sell than U.S. securities. These risks may be greater in emerging market countries than in more developed countries.

Investments in foreign securities may involve difficulties in receiving or interpreting financial and economic information, imposition of taxes, higher brokerage and custodian fees, currency rate fluctuations or exchange controls or other government restrictions, including seizure or nationalization of foreign deposits or assets. There may also be difficulty in invoking legal protections across borders. Some of these risks may cause the strategy's value to be more volatile than that of a U.S. only strategy. The strategy may also incur higher expenses and costs when making foreign investments, which could affect the strategy's total return. The risks of foreign securities are likely to be greater in emerging market countries than in foreign countries with developed securities markets and more advanced regulatory regimes. Among other things, emerging market countries may have economic structures that are less mature and political systems that are less stable. Moreover, emerging market countries may have less developed securities markets, high inflation, and rapidly changing interest and currency exchange rates. Exchange rate movements can be large and can endure for extended periods of time, affecting either favorably or unfavorably the value of the strategy's assets.

*High Yield Municipal Bonds Risk.* High yield municipal bonds may be subject to increased liquidity risk as compared to other high yield debt securities. There may be little or no active trading market for certain high yield municipal bonds, which may make it difficult for the strategy to sell such securities at or near their perceived value. In such cases, the value of a high yield municipal bond may decline dramatically, even during periods of declining interest rates. The high yield municipal bonds in which the strategy intends to invest may be more likely to pay

interest that is includable in taxable income for purposes of the federal alternative minimum tax than other municipal bonds.

The strategy may invest more heavily in bonds from certain cities, states or regions than others, which may increase the strategy's exposure to losses resulting from economic, political, or regulatory occurrences impacting these particular cities, states or regions.

Investments in high-yield securities (commonly referred to as "junk bonds") are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

*High-Yield Securities Risk.* Investments in high yield securities (commonly referred to as "junk bonds") are sometimes considered speculative as they present a greater risk of loss than higher quality securities. Such securities may, under certain circumstances, be less liquid than higher rated securities. These securities pay investors a premium (a high interest rate or yield) because of the increased risk of loss. These securities can also be subject to greater price volatility. In times of unusual or adverse market, economic or political conditions, these securities may experience higher than normal default rates.

*Leverage Risk.* Leverage, including borrowing, will cause the value of an account to be more volatile than if the account did not use leverage. This is because leverage tends to exaggerate the effect of any increase or decrease in the value of the account's portfolio securities. We may engage in transactions or purchase instruments that give rise to forms of leverage. These transactions and instruments may include, among others, the use of short sales. The use of leverage may cause an account to liquidate portfolio positions when it would not be advantageous to do so in order to satisfy its obligations. Certain types of leveraging transactions, such as short sales that are not "against the box," could theoretically be subject to unlimited losses in cases where the account, for any reason, is unable to close out the transaction.

*Liquidity Risk.* Securities purchased by the strategy that are liquid at the time of purchase may subsequently become illiquid due to events relating to the issuer of the securities, market events, economic conditions or investor perceptions. The value of illiquid securities may reflect a discount from the market price of comparable securities for which a liquid market exists, and accordingly may have a negative effect on the value of the strategy's assets. To meet client requests to withdraw assets, the strategy may be forced to sell securities at an unfavorable time and/or under unfavorable conditions.

*Loan Participation Interest Risk.* There may not be a readily available market for loan participation interests, which in some cases could result in the strategy disposing of such interests at a substantial discount from face value or holding such interests until maturity. In addition, there is also the credit risk of the underlying corporate borrower as well as the lending institution or other participant from whom the strategy purchased the loan participation interests.

*Money Market/Short-Term Securities Risk.* To the extent the strategy holds cash or invests in short-term securities, there is no assurance that the strategy will achieve its investment objective.

*Mortgage-Backed/Asset-Backed Securities Risk.* Prepayment risk is associated with mortgage-backed and asset-backed securities. If interest rates fall, the underlying debt may be repaid ahead of schedule, reducing the value of the strategy's investments. If interest rates rise, there may be fewer prepayments, which would cause the average bond maturity to rise, increasing the potential for the strategy to lose money. The value of these securities may be significantly affected by changes in interest rates, the market's perception of issuers, and the creditworthiness of the parties involved. The ability of a strategy to successfully utilize these instruments may depend on our ability to forecast interest rates and other economic factors correctly. These securities may have a structure that makes their reaction to interest rate changes and other factors difficult to predict, making their value highly volatile.

*Mortgage Dollar Roll Transaction Risk.* Mortgage dollar roll transactions are subject to certain risks, including the risk that securities returned to the strategy at the end of the roll, while substantially similar, may be inferior to what was initially sold to the counterparty.

*Municipal Securities Risk.* Municipal securities risks include the ability of the issuer to repay the obligation, the relative lack of information about certain issuers, and the possibility of future tax and legislative changes that could affect the market for and value of municipal securities. These risks include: (i) General Obligation Bonds Risk -- timely payments depend on the issuer's credit quality, ability to raise tax revenues and ability to maintain an adequate tax base; (ii) Revenue Bonds (including Industrial Development Bonds) Risk -- these payments depend on the money earned by the particular facility or class of facilities, or the amount of revenues derived from another source, and may be negatively impacted by the general credit of the user of the facility; (iii) Private Activity Bonds Risk -- Municipalities and other public authorities issue private activity bonds to finance development of industrial facilities for use by a private enterprise; the private enterprise pays the principal and interest on the bond, and the issuer does not pledge its full faith, credit and taxing power for repayment; (iv) Moral Obligation Bonds Risk -- moral obligation bonds are generally issued by special purpose public authorities of a state or municipality; if the issuer is unable to meet its obligations, repayment of these bonds becomes a moral commitment, but not a legal obligation, of the state or municipality; (v) Municipal Notes Risk -- municipal notes are shorter-term municipal debt obligations that pay interest that is, in the opinion of bond counsel, generally excludable from gross income for federal income tax purposes (except that the interest may be includable in taxable income for purposes of the federal alternative minimum tax) and that have a maturity that is generally one year or less; if there is a shortfall in the anticipated proceeds, the notes may not be fully repaid and the strategy may lose money; and (vi) Municipal Lease Obligations Risk -- in a municipal lease obligation, the issuer agrees to make payments when due on the lease obligation; although the issuer does not pledge its unlimited taxing power for payment of the lease obligation, the lease obligation is secured by the leased property.

Municipalities continue to experience economic and financial difficulties in the current economic environment. The ability of a municipal issuer to make payments and the value of municipal securities can be affected by uncertainties in the municipal securities market. Such uncertainties

could cause increased volatility in the municipal securities market and could have a negative impact on the strategy's performance.

To be tax exempt, municipal bonds must meet certain regulatory requirements. If a municipal bond fails to meet such requirements, the interest received by the strategy from its investment in such bonds may be taxable. It is possible that interest on a municipal bond may be declared taxable after the issuance of the bond, and this determination may apply retroactively to the date of the issuance of the bond, which could cause a portion of prior distributions made by the strategy to be taxable in the year of receipt.

*Private Investment Funds Risk.* The investment strategies and risks associated with the private investment funds that we manage are described in the offering memoranda for those funds that are provided to investors.

*Short Selling Risk.* If a security sold short increases in price, the strategy may have to cover its short position at a higher price than the short sale price, resulting in a loss. The strategy may have substantial short positions and must borrow those securities to make delivery to the buyer. The strategy may not be able to borrow a security that it needs to deliver or it may not be able to close out a short position at an acceptable price and may have to sell related long positions before it had intended to do so. Thus, we may not be able to successfully implement the short sale strategy due to limited availability of desired securities or for other reasons.

The strategy also may be required to pay a premium and other transaction costs, which would increase the cost of the security sold short. The amount of any gain will be decreased, and the amount of any loss increased, by the amount of the premium, dividends, interest or expenses the strategy may be required to pay in connection with the short sale.

Until the strategy replaces a borrowed security, it is required to maintain a segregated account of cash or liquid assets with a broker or custodian to cover the strategy's short position. Generally, securities held in a segregated account cannot be sold unless they are replaced with other liquid assets. The strategy's ability to access the pledged collateral may also be impaired in the event the broker fails to comply with the terms of the contract. In such instances, the strategy may not be able to substitute or sell the pledged collateral. Additionally, the strategy must maintain sufficient liquid assets (less any additional collateral pledged to the broker), marked-to-market daily, to cover the short sale obligations. This may limit the strategy's investment flexibility, as well as its ability to meet withdrawal requests or other current obligations.

Because losses on short sales arise from increases in the value of the security sold short, such losses are theoretically unlimited. By contrast, a loss on a long position arises from decreases in the value of the security and is limited by the fact that a security's value cannot go below zero.

By investing the proceeds received from selling securities short, the strategy could be deemed to be employing a form of leverage, which creates special risks. The use of leverage may increase the strategy's exposure to long positions and make any change in the value of the strategy's assets greater than it would be without the use of leverage. This could result in increased volatility of returns. There is no guarantee that the strategy will use leverage, or if it does, that the leveraging strategy will be successful.

Regulatory authorities in the United States or other countries may prohibit or restrict our ability to fully implement the short-selling strategy, either generally, or with respect to certain industries or countries, which may impact the strategy's ability to fully implement its investment strategies.

*To-Be-Announced Securities (TBAs) Risk.* The principal risks are that the counterparty may not deliver the security as promised and/or that the value of the to-be-announced security may decline prior to when the strategy receives the security.

*Valuation Risk.* There is no central place or exchange for fixed-income securities trading. Fixed-income securities generally trade on an "over-the-counter" market, which may be anywhere in the world where the buyer and seller can settle on a price. Due to the lack of centralized information and trading, the valuation of fixed-income securities may carry more risk than that of common stock.

Uncertainties in the conditions of the financial market, unreliable reference data, lack of transparency and inconsistency of valuation models and processes may lead to inaccurate asset pricing. In addition, other market participants may value securities differently. As a result, when a security or other instrument is sold in the market, the amount that the account receives may be less than the amount at which it was valued.

Valuations of the assets, which will affect the amount of fees (including, to the extent applicable, performance compensation) payable to MacKay Shields may involve uncertainties and judgmental determinations, and if such valuations prove to be incorrect, client portfolio value could be adversely affected. For example, in the case of an overvaluation of a client's portfolio, MacKay Shields' compensation would be greater than if the correct lower valuation had been used.

*When-Issued Securities Risk.* The principal risk of transactions involving when-issued securities is that the security will be worth less when it is issued or received than the price the strategy agreed to pay when it made the commitment.

## **DISCIPLINARY INFORMATION**

There are no legal or disciplinary events involving MacKay Shields or any senior officer of our firm that are material to our advisory business.

## **OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS**

### **Affiliated Broker-Dealers.**

Some of our employees, including some of our senior officers, are registered with the Financial Industry Regulatory Authority ("FINRA") as representatives and principals of our affiliate NYLIFE Distributors, which, like MacKay Shields, is a wholly-owned subsidiary of NYL Investments Holdings. NYLIFE Distributors is registered as a broker-dealer with the SEC.

Our employees who are registered representatives of NYLIFE Distributors, and other registered representatives of NYLIFE Distributors, may sell interests in private investment funds to institutions and high net worth individuals. These private investment funds are not required to be



registered with the SEC as investment companies. We manage certain of these private investment funds, and others are managed by affiliated investment advisers. If a registered representative of NYLIFE Distributors is responsible for the sale of interests in a private investment fund that we or an affiliate sponsors, the registered representative may receive a percentage of the management fee that is attributable to the sale.

Our employees who are registered representatives of NYLIFE Distributors, and other registered representatives of NYLIFE Distributors may also:

- promote the sale of various SEC-registered investment companies, known as The MainStay Funds, to registered representatives of other broker-dealers, who may recommend that their clients purchase these products
- assist NYL Investments in making presentations to investment consultants with respect to our sub-advisory services for wrap fee programs for which NYL Investments provides advisory services

We have an agreement with NYLIFE Distributors under which we provide supporting and consulting services regarding the sale by NYLIFE Distributors of interests in private investment funds managed by affiliated and unaffiliated investment advisers. We receive fees for such services.

NYLife Securities LLC, another subsidiary of NYLIC, is registered as a broker-dealer with the SEC.

We do not use broker-dealers that are affiliated with us in executing securities transactions for our clients.

### **Ownership, Management and Compensation.**

We are a wholly-owned subsidiary of NYL Investments Holdings, which in turn is a wholly-owned subsidiary of NYLIC.

In addition to senior executives of our firm, our Board of Managers includes senior executives of NYLIC and NYL Investments.

We are a participant in the New York Life Employee Progress-Sharing Investment Plan, a profit sharing plan that permits voluntary employee contributions. We match employee contributions up to a maximum of 3% of basic gross salary.

We have an agreement with NYLIC under which we pay NYLIC for certain administrative services. Under an agreement with NYL Investments Holdings, NYL Investments provides administrative services to us (as a subsidiary of NYL Investments Holdings), for which we make payments to NYL Investments.

Some of our employees are also officers of NYLIC or other affiliated companies. In addition, some of our senior employees serve on various committees of NYL Investments.

Employees of NYLIC and NYL Investments regularly work with our firm on the development of investment products and strategies.

Historically, long-term incentive compensation for some of our senior employees is phantom stock and options of NYL Investments Holdings and is based on the overall performance of NYL Investments Holdings. Beginning January 1, 2010, MacKay Shields adopted the MacKay Shields Equity Plan, which provides phantom stock to senior employees, and which replaces the prior plan for our employees. Awards under the prior plan continue to vest and pay out according to the terms of that plan.

Notwithstanding the ownership interests, organizational duties and compensation arrangements described above, we exercise completely independent judgment in the management of our clients' investments.

### **Affiliated Client Relationships.**

We act as investment manager, investment adviser or sub-adviser for:

- A portion of the general accounts of NYLIC and its affiliated insurance companies
- Accounts for which NYLIC or New York Life Trust Company, a related person, serves as Trustee
- Accounts with respect to which NYL Investments is a retirement plan administrator
- Wrap fee programs with respect to which NYL Investments provides advisory services
- Certain series of The MainStay Funds, MainStay VP Series Fund, Inc., MainStay Funds Trust, Eclipse Funds Inc. and Eclipse Funds, registered investment companies for which NYL Investments is the investment adviser and administrator and NYLIFE Distributors LLC, acts as Principal Underwriter and Distributor
- Separate accounts managed by McMorgan
- Accounts that are investment vehicles for insurance products sponsored by NYLIC and for which NYL Investments is the adviser
- Accounts that have contractual insurance arrangements with NYLIC
- Assets of NYL Investments and NYL Investments Holdings
- Private investment funds for which our related persons may act as general partner, manager, managing member, trustee, director or in a similar capacity
- Private investment funds in which NYLIC, its affiliated insurance companies and/or NYL Investments Holdings have a substantial interest
- Private investment funds in which senior officers of NYLIC, NYL Investments or our firm have investment interests

Conflicts may arise as to the allocation of investment opportunities among those clients and our other clients. We have policies and procedures in place to make sure that all of our clients are treated fairly and that no client account receives preferential treatment in the allocation of investment opportunities. See "Performance-Based Fees and Side-by-Side Management", above and "Brokerage Practices", below.

### **Other Arrangements with Affiliates.**

Under a services agreement with McMorgan, we pay McMorgan a percentage or portion of compensation we receive, for soliciting certain Taft-Hartley investment advisory clients and for providing various related solicitation support and client relations services to such clients. We also have a services agreement under which we pay McMorgan for servicing Taft-Hartley investors in private investment funds that we manage. The compensation we pay to McMorgan does not increase the fees or costs payable by the client or investor. McMorgan does not exercise investment discretion or otherwise provide investment advice to the Taft-Hartley client or investor about retaining our firm or investing in the private investment fund.

Under a client and investor services agreement with NYL Investments, we pay NYL Investments a percentage of compensation we receive, for providing client relations services to certain international investment advisory clients and for servicing certain international investors in private investment funds that we manage. We also have a solicitation services agreement under which we pay NYL Investments for soliciting certain international investment advisory clients. The compensation we pay to NYL Investments does not increase the fees or costs payable by the client or investor. NYL Investments does not exercise investment discretion or otherwise provide investment advice to the international client or investor about retaining our firm or investing in the private investment fund.

New York Life Investments International Limited (“NYL Investments International”), a wholly-owned subsidiary of NYL Investments Holdings, has recently received authority from the Central Bank of Ireland to provide investment advisory services under European Communities (Markets in Financial Instruments) Regulations 2007, as amended. We expect to enter into arrangements to pay NYL Investments International a percentage of compensation we receive, for providing investment advice, investment services and/or investor relations services to certain of our international investment advisory clients and for servicing certain international investors in private investment funds that we manage. The compensation we will pay to NYL Investments International will not increase the fees or costs payable by the client or investor.

From time to time, we enter into agreements with our affiliated investment advisers or related persons by which the affiliated investment adviser or related person utilizes the services of one or more of our employees and may pay a fee to us, or we utilize the services of one or more employees of an affiliated investment adviser or related person and may pay a fee to the affiliated investment adviser or related person. In these arrangements, the employee is subject to our supervision and supervision by the affiliated investment adviser or related person.

Our affiliates NYLCAP Manager LLC and Private Advisors, LLC, both of which, like MacKay Shields, are wholly-owned subsidiaries of NYL Investments Holdings, are registered investment advisers that serve as investment manager or sponsor of various limited partnerships and other private investment funds. Our employees who are registered representatives of NYLIFE Distributors may solicit our clients to invest in such limited partnerships or other funds. These limited partnerships and other private investment funds generally pay a fee to our affiliated advisers. Those employees may receive a portion of that fee, and our firm may receive a fee from NYLIFE Distributors. These fees are not an additional charge to such limited partnerships or other funds or their investors. This practice presents a conflict of interest and gives the

employee an incentive to recommend that clients invest in these limited partnerships and other funds in order to increase the compensation paid to our affiliated advisers, to themselves and to our firm. There are policies and procedures in place that we believe are reasonably designed to address these conflicts of interest. For example, our employees who are registered representatives of NYLIFE Distributors may only recommend investments in these limited partnerships and other funds if they believe they are suitable for the client.

From time to time, we may enter into arrangements with our affiliated investment advisers to recommend advisory clients to each other. Please see “Client Referrals and Other Compensation”, below.

### **Additional Information About Our Activities and Affiliates.**

We may recommend securities or other investments to clients, or engage in transactions on behalf of clients, where a related person has a financial interest and buy and sell the same security or investment between or among clients’ accounts. See “Code of Ethics, Participation or Interest in Client Transactions and Personal Trading”, below.

Our employees, members of their families, and our affiliates may own and transact in securities that we purchase or sell for our clients, or various classes of the same security. The investors in such issuers could have different rights, for example in the event of a default or restructuring on the part of the issuer, or as a result of a bankruptcy proceeding. These securities include long-term and short-term debt and equity and private securities, and instruments such as bank loans. The investment strategy for certain clients includes transacting in different securities of the same issuer, different tranches of the same issue or the same issue denominated in different currencies, in the client account. We may purchase a security for one client and sell the same security for another client. Potential conflicts between client accounts are addressed through our procedures for allocating portfolio transactions and investment opportunities, as described under “Brokerage Practices”, below.

We have a Personal Investment Policy intended to regulate personal transactions in such a manner to satisfy our primary obligation of loyalty to our clients. See “Code of Ethics, Participation or Interest in Client Transactions and Personal Trading”, below.

We prohibit the use of material, non-public information (“inside information”) and maintain a restricted list of securities that may not be purchased by our employees for their own accounts or for client accounts because of the actual or possible possession of inside information. Our personnel or those of our affiliates may come into possession of inside information concerning various companies. We and our advisory affiliates have established information barrier policies that serve to limit the dissemination of such information and provide with flexibility in managing its clients’ portfolios. Nevertheless, if we or our affiliates possess such information, our ability to buy or sell securities of such issuers for our clients may be restricted, although any such restrictions are expected to be infrequent. We may also impose such restrictions in isolated instances to prevent even an appearance that such information has been used in a manner contrary to law. We are not obligated and may not be permitted to communicate any such information to or for the benefit of our clients, disclose that we are restricted from trading in a particular security or otherwise to act on the basis of any such information in providing services

to clients. We may also from time to time be subject to limitations on trading in the securities of certain issuers as a result of our clients' holdings or those of our affiliates and their clients.

### **Information Barrier with Affiliates.**

The investment management and operations functions at McKay Shields and our affiliates are autonomous and operate separately from each other. These functions include all decision-making on what, how and when to buy, sell or hold securities in client portfolios, the trading related to implementation of these decisions and operations. This policy is intended to limit the dissemination of inside information and to permit the investment management, trading and operations functions of each firm to operate without regard to or interference from the other. We believe this separation is in the best interest of clients of the firms as operating independently permits each firm to pursue the investment objectives of clients without reference to limitations resulting from investment activities of the other. To support this policy, we have adopted certain procedures, including a portfolio information barrier between us and these other affiliated investment firms. In the event such information is shared, appropriate controls are placed around the information in order to limit any potential conflicts of interest.

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

### **Code of Ethics.**

We have adopted a Code of Ethics ("Code"), which is designed to set forth the general fiduciary principles governing employees, require compliance with the federal securities laws, and to detect and prevent conflicts of interest.

In addition to the Code's policies regarding personal securities trading, the Code requires our employees to follow related policies. For example, all employees are required to complete an annual Conflict of Interest Questionnaire and to follow additional policies related to the conduct standards of our Code, including:

- Insider Trading Policy and Procedures
- Information Barrier Policy and Procedures
- Restricted List
- Watch List
- Gifts and Entertainment
- Policy on Anti-Corruption in International Business Transactions
- Personal Political Contributions Policy
- Information Security and Privacy Policy

- Policy on Selective Disclosure of Mutual Fund Portfolio Holdings, and
- CFA Code of Ethics and Standards of Professional Conduct (with respect to our employees who are Chartered Financial Analysts)

See “Other Financial Industry Activities and Affiliations”, above. We permit our personnel to engage in personal securities transactions, including buying or selling securities that we have recommended to, or purchased or sold on behalf of, clients. These transactions raise potential conflicts of interests, including when they involve securities owned or considered for purchase or sale by or on behalf of a client account. Potential conflicts of interest may arise in connection with an employee’s knowledge and timing of transactions, investment opportunities, broker selection, portfolio holdings and investments, including potential conflicts described in “Other Financial Industry Activities and Affiliations”, above. We manage these potential conflicts with client transactions by requiring that any transaction be made in compliance with our Code.

The Code imposes specific requirements concerning employees’ personal security investments:

- Employees are required to report personal securities transactions in all Covered Securities, which excludes the following:
  - direct obligations of the U.S. Government
  - shares of mutual funds for which we are not the investment adviser or sub-adviser and none of our affiliates is investment adviser or sub-adviser
  - commercial paper, certificates of deposit, and high quality short-term investments
  - shares issued by money market funds
  - shares issued by unit investment trusts that are invested exclusively in one or more mutual funds, unless those funds are affiliated funds or exchange-traded funds.
- Employees may not trade for their personal accounts while in possession of material, non-public information
- Employees may not trade for their personal accounts in securities of issuers that appear on our Restricted or Watch List
- Employees must receive prior written approval before trading in a Covered Security, which is provided through an automated system that provides feedback to an employee as to whether a request is approved or denied; authorization is effective only for the calendar day that the request was submitted and approved, except in limited situations related to foreign markets, where authorization is effective for 24 hours
- Employees may not engage in short-term trading (the purchase and sale or sale and purchase within 60 days) of any Covered Security or shares of a mutual fund for which we or our affiliates serve as investment adviser or sub-advisor
- Employees may not purchase securities in initial public offerings or in connection with private placements without the prior written approval of our General Counsel or Chief Compliance Officer
- All employees must file quarterly reports and certifications of covered trading activity
- Subject to certain exceptions, we prohibit employees from personal securities transactions in securities within seven days before or after we make a trade in such securities for a client

- Employees must report all brokerage related accounts that they or certain family members have a beneficial interest
- Employees must report any interest that they or certain family members have in shares of investment companies that we or any affiliate advises or sub-advises

In addition, our employees:

- must disclose any interest in any unaffiliated entity that does, or is seeking to do, business with us, or that otherwise presents a potential conflict of interest
- may not serve on the Board of Directors of any unaffiliated company without the approval of our General Counsel or Chief Compliance Officer

In addition, some of our employees are subject to the Code of Ethics and trading restrictions of the registered open- and closed-end funds that we advise or subadvise.

Our General Counsel or Chief Compliance Officer may grant exceptions to provisions of the Code in circumstances that present special hardship or special situations determined not to present potential harm to clients or conflicts with the spirit and intent of the Code.

Employees who violate our Code can have their personal securities trading privileges suspended, and we can impose severe sanctions for violations of the Code and the related policies listed above, including termination of employment.

We will provide a copy of our Code to any client or prospective client upon request. To request a copy, contact:

MacKay Shields LLC  
 9 West 57th Street  
 New York, NY 10019  
 Attn: Chief Compliance Officer

### **Interests of Affiliates.**

In the course of performing investment advisory services, we may also purchase or sell for our clients securities or other interests in which our affiliates have a material financial interest. See “Other Financial Industry Activities and Affiliations”, above. We may also purchase or sell for our clients securities or interests that clients of our affiliates also own. These practices create conflicts of interest relating to the allocation of limited investment opportunities between affiliated and unaffiliated accounts, allocation of investment opportunities to affiliated accounts that pay a performance fee, using information regarding transactions in affiliated accounts to benefit other accounts and placing trades for affiliated accounts before or after trades for unaffiliated accounts to take advantage of (or avoid) market impact.

It is our policy not to favor the interest of one client over another. We address the conflicts of interest created by management of affiliated and unaffiliated accounts by having a trade allocation policy designed so that trades are allocated among client accounts in a fair and equitable manner over time. In addition, it is our policy that we will not permit cross trades between clients unless the portfolio manager instructing the trade deems it in the best interest of

both clients at the time and obtains advance compliance approval of the transaction. See “Performance-Based Fees and Side-By-Side Management”, above and “Brokerage Practices”, below.

Regardless of whether they are affiliated or unaffiliated accounts, when we manage accounts according to the same investment strategy, we anticipate that those accounts will generally have the same investment opportunities and be invested in the same or similar securities with the same or similar weighting. However, there are often differences in the nature or amount of securities that we buy or sell for client accounts. See “Brokerage Practices”, below.

In addition, the investment management and operations functions at MacKay Shields and our affiliates are autonomous and operate separately from each other, including all decision-making on what, how and when to buy, sell or hold securities in client portfolios, the trading related to implementation of these decisions and operations. To support this policy, we have adopted certain procedures, including a portfolio information barrier between us and our affiliated investment firms. In the event such information is shared, appropriate controls are placed around the information in order to limit any potential conflicts of interest.

The information barrier also limits the dissemination of inside information. See “Other Financial Industry Activities and Affiliations”, above.

## **BROKERAGE PRACTICES**

### **Selection and Compensation of Broker-Dealers.**

When we select or recommend a broker-dealer for transactions in our clients’ accounts, we weigh a combination of criteria regarding the broker-dealer and the reasonableness of its compensation. The factors we may consider in selecting a broker-dealer and determining the reasonableness of its compensation include:

- The broker-dealer’s quality of executions, which includes the accuracy and timeliness of executions, clearance of transactions and error/dispute resolution
- The broker-dealer’s ongoing reliability and speed with which transactions are executed
- The broker-dealer’s integrity to handle transactions and ability to maintain the confidentiality of trading activity and information
- The broker-dealer’s reputation, financial condition, disciplinary history and stability
- The broker-dealer’s compensation, which includes net prices paid or received, negotiated commission rates available and other current transaction costs (for example, its brokerage commission or a mark-up or mark-down). When we evaluate the broker-dealer’s compensation, we consider its ability to execute a security transaction in the desired volume, the security price or the spread between the bid and asked prices of the security, and the size of a particular security order
- The broker-dealer’s ability to provide us with access to securities in underwritten offerings and in the secondary market, its willingness to commit its own capital, its trading expertise and market knowledge, and the nature and frequency of its coverage in terms of providing market outlook, quotes on specific securities and sector research



- The broker-dealer's block trading and block positioning capabilities and ability to execute difficult transactions
- The broker-dealer's responsiveness to our portfolio managers, traders and investment operations personnel
- The nature of the research created or developed by the broker-dealer, which is called "proprietary research"
- The broker-dealer's access to research that the broker-dealer itself has not created or developed, which is called "third party research"
- The value and quality of the research and other products and services other than brokerage services that we receive from the broker-dealer or that the broker-dealer pays for (either by cash payments or commission), as more fully described under "Soft Dollar Benefits", below
- Regulatory, legal and macro-economic matters that may affect the broker-dealer

When selecting broker-dealers to execute transactions, we are not required to solicit competitive bids and do not have an obligation to seek the lowest available commission cost, but rather best overall execution. In our experience, neither the lowest commission rate nor the most expeditious execution necessarily correlates to the best trade for the client.

In foreign markets, including those where we regularly purchase and sell securities for clients, commissions and other transaction costs are often higher than those charged in the United States. In addition, we may not have the ability to negotiate commissions in some of these markets. You should also note that services associated with foreign investing, including custody and administration, generally are more expensive than in the United States.

### **Soft Dollar Benefits.**

We may receive proprietary research from a broker-dealer in connection with client securities transactions. When we use client brokerage commissions to obtain proprietary research from a broker-dealer, we receive a benefit because we do not have to produce or pay for the research ourselves. As a result, we may have an incentive to select or recommend a broker-dealer based on our interest in receiving the research, rather than on our clients' interest in receiving most favorable execution of trades. The services benefit us by allowing us, at no additional cost to us to:

- supplement our own research, analysis and execution activities
- receive the views and information of individuals and research staffs of other securities firms
- gain access to persons having special expertise on certain companies, industries, areas of the economy and market factors

We describe below our policies concerning the use of soft dollars, what we receive with soft dollars, and how we manage these conflicts. We may cause clients to pay brokerage commissions higher than those charged by other broker-dealers in return for soft dollar benefits. For fixed income trades, we do not cause clients to pay mark-ups or mark-downs higher than

those charged by other broker-dealers in return for soft dollar benefits. Under no circumstances do we receive research or other benefits that is not produced or prepared by such broker-dealer (*i.e.*, third-party research).

In general, soft dollar services furnished by broker-dealers through which we trade are used for the benefit of our clients as a group and not solely or necessarily in all cases for the benefit of the particular client whose trades are handled by the broker-dealer who provides such services.

If we determine in good faith that the amount of client brokerage commissions is reasonable in relation to the value of the brokerage and research services provided, such commissions may be equal to or greater than the amount another broker-dealer might charge. We review the reasonableness of commission and other transaction costs incurred by our clients in light of the facts and circumstances we deem relevant from time to time, including information furnished by our traders.

We intend to use client brokerage commissions to pay only for brokerage and research services that are eligible under Section 28(e) of the Securities Exchange Act of 1934, as amended (the “1934 Act”), and related SEC interpretive releases.

The nature of the research services we receive from brokerage firms varies from time to time but generally includes among other information: current and historical financial data concerning particular companies and their securities; information and analysis concerning portfolio strategy, securities markets and economic and industry matters; technical and statistical models and studies and data dealing with various investment opportunities, values, risks and trends; analysis and reports concerning the performance of accounts; and advice as to the value of securities, the advisability of investing in or selling securities and the availability of securities or purchasers or sellers of securities.

Before discontinuing our International Equity investment strategy, MacKay also used client brokerage commissions to pay for other products and services eligible under Section 28(e) of the 1934 Act and related SEC interpretive releases. As a result, we received the following types of products and services with client brokerage commissions within our last fiscal year:

- Traditional research reports analyzing the performance of a particular stock or company
- Market data and economic data, including stock quotes, last sale prices and trading volumes
- Quantitative analytical software and software that provides analyses of securities portfolios
- Seminars or conferences (excluding the cost of travel, entertainment and meals)
- Advice from broker-dealers on order execution including advice on execution strategies

### **Brokerage for Client Referrals.**

In selecting or recommending broker-dealers, we do not consider a broker-dealer’s referral of clients to us. We also do not consider a broker-dealer’s referral of investors to private investment funds that we, our related persons or third parties sponsor or sales of shares of registered investment companies that we or our affiliates advise or sub-advise. While we may

direct brokerage to broker-dealers that have consulting divisions that might refer clients or investors to us, we have no agreements to do so.

### **Directed Brokerage.**

At a client's request, we direct trades to broker-dealers that provide specific services for the benefit of that client, to certain broker-dealers in order for that client to participate in that broker-dealer's commission rebate or other programs or to specific types of broker-dealers. The client's request may relate to all of the transactions in its account, a specific portion of transactions in its account or may require that we use our best efforts to satisfy its request.

Directing brokerage may cost clients more money. When we satisfy a client's request to direct brokerage, we may not be able to achieve most favorable execution of transactions for that client. Clients who direct us to execute their trades with certain broker-dealers or types of broker-dealers may lose the benefit of more favorable commission rates or more favorable executions that may be obtained, for example, when we bunch or aggregate client orders. In addition, there may be times when trading with a directed broker-dealer occurs before or after we have completed the execution of other transactions in that security for other clients.

A directed trade may be executed directly with the broker-dealer or may be "stepped out" to that broker-dealer. In a step-out transaction, we bunch client-directed broker accounts with non-directed broker accounts and request that the executing broker allocate a portion of the transaction to the directed broker. In that event, the broker providing execution services would differ from a particular client's directed broker.

We may receive soft dollar benefits from a broker-dealer that a client directs us to use. To avoid any conflict of interest in that event, we will not execute any soft dollar trades on behalf of the client with the broker-dealer designated by the client, until the client's directed request has been satisfied.

Certain clients may execute trades independently through their broker-dealers. Although cost is only one component of best execution analysis, many directed brokerage accounts pay effective rates of commissions that are higher than client accounts that do not have directed brokerage arrangements. In these instances, a client may have an arrangement with the broker-dealer to receive a benefit that the client believes justifies the higher commission rate.

### **Wrap Fee Programs.**

For clients that invest through wrap fee programs, the wrap fee charged by the sponsor firm typically covers trade and execution services. As a result, the sponsor and client typically request that transactions for clients' accounts be executed by the sponsor of the wrap fee program (or its affiliate) or a broker-dealer designated by the sponsor firm. In the event that the sponsor or designated broker-dealer cannot provide "best execution" for a given transaction, we, as investment manager for the wrap fee program, have the option to trade away (that is, trade with a different broker-dealer), and the client may incur a commission cost. We may execute trades for other clients with similar strategies prior to placing trades with wrap sponsors.

### **Aggregating and Allocating Trades.**

If we believe that the purchase or sale of the same security is in the best interest of more than one client, we may aggregate the securities to be sold or purchased. We will not aggregate trades (also known as “bunching” trades) unless we believe that doing so is consistent with our duty to seek best execution for our clients. We are not obligated to aggregate trades, but if we desire to do so, we will only aggregate trades for clients whose investment advisory agreements authorize us to do so. Clients may pay more when we do not aggregate trades, as seeking to place separate, non-simultaneous transactions in the same security for multiple clients may have a negative effect on market price, transaction commissions and/or trade execution.

These bunched orders may be averaged as to price and allocated to accounts in amounts according to each account's daily purchase or sale orders or on some other equitable basis.

When we allocate bunched trades to client accounts, we do not favor the interest of one client over another. However, there may be differences in the amount purchased or sold for accounts. These differences may occur for a number of reasons, including, among others:

- Specific client investment objectives
- Cash available in the account for investment
- Client-imposed investment restrictions
- Initial investment periods for new accounts
- Investment restrictions that laws or regulations impose
- Actual and anticipated cash inflows and outflows in client accounts
- Duration and/or average maturity of the client account
- Size of client account
- Deal size
- Current industry or issuer exposure in the client account
- Rounding to whole lots (for example, 100 shares or 10,000 bonds)
- Other practical limitations

We usually determine the allocation of the security among client accounts before we execute the aggregated order. When it is impractical or not feasible for us to determine the allocation methodology for participating accounts before we execute the trade, we will allocate after the trade is executed, but in no event later than the end of the day, in a fair and equitable manner among all participating accounts based on the factors listed above.

There may be instances when there is a limited supply for a particular security or investment opportunity. In such cases, it is our general policy to make a *pro rata* allocation to accounts based on the original amounts targeted for each account. We may exclude certain accounts from such *pro rata* allocations if such allocations would result in such accounts receiving amounts that the portfolio manager believes are too small to properly manage. We cannot assure that in every instance an investment will be allocated on a *pro rata* basis, and differences may occur due to the factors mentioned above.

Our investment teams may also consider the factors listed above when determining the amount of securities to purchase or sell for each account they manage. When we cannot obtain a

sufficient amount of an instrument for all accounts managed by the teams, we may allocate the original minimum target amount first to those accounts that have the most available cash. As a result, the accounts to receive an allocation of the minimum target amount generally will be the accounts with higher available cash than other accounts. The order in which the remaining accounts will receive allocations will follow that same process until there are no more available securities or instruments to be allocated. Under this allocation system, some accounts may not receive any allocations of certain securities or instruments.

We monitor the allocation policy by periodically comparing the performance of accounts that have the same investment strategies to satisfy ourselves that variations in performance are due to investment factors such as those listed above, and not attributable to allocation decisions.

We have independently managed investment teams investing in the same general market that may maintain procedures applied independently of the other. In most instances, the broker-dealer selling securities to these investment teams will determine the allocation to each team.

## **REVIEW OF ACCOUNTS**

We maintain independently managed portfolio management teams, each of which conducts its own research and operates autonomously, with its own portfolio managers and traders. Our portfolio managers and client services groups review client portfolios on a regular basis in light of client objectives and guidelines and in response to market events and the portfolio management team's general policies and strategies. In addition, each investment team meets regularly to consider economic, market and general investment matters not related to specific client accounts. We assign each account a primary portfolio manager and primary service contact. The number of clients assigned to a primary portfolio manager and primary client service contact varies from time to time, depending upon a variety of circumstances. No single account is the sole responsibility of any one portfolio manager or client service contact. Portfolio managers review portfolios at least weekly to ensure consistency among clients with similar objectives and a member of the portfolio management team reviews client portfolio transactions daily.

We have several tools at our disposal to assess and monitor overall compliance of managed portfolios with their stated investment objectives. There are both manual and automated supervisory and compliance review procedures in place to monitor accounts. We have front-end and back-end compliance systems that have automated controls to help review investment transactions to confirm they are made in accordance with client investment mandates. We have also developed exception reports from our portfolio accounting system to assist in performing next day reviews.

Each quarter, all clients receive a comprehensive package that includes performance results and comparative benchmark returns, a detailed summary of quarterly purchases and sales, an asset listing, brokerage commission statement (if applicable) and a portfolio manager commentary on current investment strategy and outlook for the market and the client's portfolio.

We also report to the boards of the registered funds we subadvise. The boards of the registered funds receive a variety of written materials concerning the portfolios, including the materials made available to fund shareholders.

We also conduct telephonic or in-person meetings with clients to discuss their portfolios with them. In general, at least one portfolio manager and a client service representative participate in these meetings. The frequency of these meetings is usually included in a client's investment management agreement or guidelines with us, and we will schedule additional meetings at a client's request.

Clients who request monthly reporting receive an asset list providing a market valuation of each security (produced on a trade-date basis and including accrued interest), a transaction journal and performance compared to the clients' respective benchmarks.

We also review client portfolios monthly for the purpose of reconciling our records of our clients' account holdings with those of their custodian banks. In addition, on a daily or weekly basis, we review client accounts for purposes of reconciling cash balances.

We also provide separate specialized reports as requested by individual clients.

We have a policy regarding the correction of trade errors. In the event of an error, we attempt to identify, research and correct the error as soon as practicable. We will make a client whole for any losses resulting from a trade error that we have caused, while any gains realized as a result of a trade error remain in the client's account. On a case-by-case basis, where appropriate, we may net gains and losses within a client's account.

## **CLIENT REFERRALS AND OTHER COMPENSATION**

We enter into solicitation, referral and servicing agreements with affiliates and third parties under which we pay affiliates or third parties a percentage or portion of the compensation we receive on the accounts they solicit, refer or service. Please see "Other Financial Industry Activities and Affiliations", above, for a description of soliciting, referral and service arrangements we have with our affiliates.

If we pay a cash fee to anyone for soliciting clients on our behalf or if we receive a cash fee from another investment adviser for recommending clients to it, we comply with the requirements of the SEC's cash solicitation rule. This rule requires a written agreement between the investment adviser and the person soliciting clients on its behalf. The rule also requires that an unaffiliated solicitor provide a disclosure document to the potential client at the time they make the solicitation. As required by the rule, we will not engage another person to solicit clients on our behalf if that person has been subject to securities regulatory or criminal action within the preceding ten years. The fact that we may share a portion or percentage of the compensation we receive for investment advisory services will not result in charging any client fees at a rate in excess of, or less than, the rate or level of advisory fees we customarily charge to our investment advisory clients for similar services to comparable accounts. In addition, we will not charge any client any other amount for the purpose of offsetting our cost of obtaining an account through a third party referral.

Some of our employees receive compensation from us for referring client accounts to us. The compensation paid to those employees comes out of the fee paid by such accounts and is not an additional charge to the account.

We have also entered into placement agent agreements with NYLIFE Distributors and unaffiliated third parties who solicit investors for private investment funds for which we act as investment adviser. We pay such placement agents a percentage or portion of the compensation we receive from the investment in the private investment fund by the investor referred by the placement agent. Please see “Other Financial Industry Activities and Affiliations”, above for a description of placement agent arrangements we have with our affiliates.

### **CUSTODY**

We or an affiliate may, among other things, act as general partner to private investment funds for which we serve as investment adviser. Such powers may cause us to be deemed to have custody of the private investment fund’s assets for purposes of the SEC’s custody rule. Accordingly, to meet the requirements of the custody rule, private investment funds for which we serve as investment adviser are subject to an annual audit in accordance with generally accepted accounting principles conducted by an independent public accountant registered with the Public Company Accounting Oversight Board and the audited financial statements are distributed to investors in the private investment funds within 120 days of the end of the funds’ fiscal year.

With respect to separate accounts, we do not have custody of funds or securities. Clients select their own qualified custodians, such as banks or broker-dealers, to maintain client funds or securities. Clients receive account statements directly from their custodians and/or from their custodian banks’ accounting departments. Clients should carefully review those statements. In addition, clients receive account statements from us. When you receive account statements from us, we encourage you to compare them to the account statements you received from your custodian and/or custodian bank accounting department. There may be differences in market values between our account statements and the custodian’s account statement for various reasons. For example, we and your custodian may use different pricing sources to value securities held in your portfolio. Other differences can be because we and the custodian may generate account statements on different dates (such as on a trade date versus settlement date basis) or may be due to the custodian’s policies for handling certain assets or changes in the values of certain assets. To the extent you find such discrepancies and would like to obtain an explanation, we encourage you to call us to obtain such information.

### **INVESTMENT DISCRETION**

We have investment discretion to manage securities on behalf of client accounts. Clients customarily impose restrictions on this discretion, which limitations are included in the investment management agreement and guidelines for their account. The investment management agreement and guidelines specify the types of investments permitted for the account and often place limits on the amount of investments in issuers or industries that we can purchase for the account. Clients who have separately managed accounts with us can change these restrictions by amending their investment management agreements or guidelines or by other written instructions.

Our portfolio managers, client service and operations representatives and legal and compliance personnel participate in the review of the client's guidelines before we begin managing the account.

For funds or other pooled investment vehicles, guidelines and limitations are described in the respective fund's offering materials. For private investment funds, we have discretionary authority through investment management agreements, trust agreements or limited partnership agreements. For registered funds, we have discretionary authority through the sub-advisory agreement between us and the fund's adviser or manager.

## **VOTING CLIENT SECURITIES**

Typically, your investment management agreement will state whether or not you have authorized us to vote the securities in your account. We have adopted policies and procedures for when we have this voting authority.

We currently use Institutional Shareholder Services, Inc. ("ISS") to assist us in voting client securities. Clients who have given us authority to vote their securities also instruct us whether to vote in accordance with their own voting guidelines or in accordance with our standard guidelines for non-union clients or union clients. Clients must furnish any custom voting guidelines to us in writing. Our standard non-union or union guidelines follow ISS voting recommendations. For those clients who have given us voting authority, we instruct the client's custodian to send all ballots to ISS and we instruct ISS which guidelines to follow.

After the appropriate voting guidelines have been established for a client's account, ISS votes the client's securities in accordance with those guidelines unless a client makes a specific request with respect to a particular security held in the client's account or unless the portfolio manager believes in the case of a particular vote that it is in the best interest of the client to vote otherwise.

A client may make a specific request that we vote a proxy with respect to a particular security even if it is in a manner inconsistent with the applicable guidelines for the client's account. Clients who wish to make such a request must send a written request to MacKay sufficiently in advance of the meeting so that there is enough time for us to instruct ISS how to vote.

In the event that a portfolio manager believes, in the case of a particular vote, that it is in the best interest of the client(s) to vote otherwise, the portfolio manager must complete a form describing the reasons for departing from the guidelines and disclosing any facts that might suggest there is a conflict. Conflicts may exist in situations where our firm is called to vote on a proxy involving an issuer or proponent of a proxy proposal regarding the issuer where our firm or our affiliate also: (1) manages the issuer's or the proponent's pension plan; (2) administers the issuer's or proponents' employee benefit plan; (3) provides brokerage, underwriting, insurance or banking services to the issuer or proponent; or (4) manages money for an employee group. Additional conflicts may arise if an executive of our firm or our affiliate has a personal or business relationship with a director or executive officer of the issuer or the proponent, a person who is a candidate to be a director of the issuer, a participant in the proxy contest or a proponent of a proxy proposal. The portfolio manager must submit the form to our Legal/Compliance



Department for review. If the Legal/Compliance Department determines that no conflict exists, then we will approve the portfolio manager's voting recommendation and we will inform ISS how to vote. If our General Counsel or Chief Compliance Officer determines that a conflict exists, we will refer the matter to our Compliance Committee for consideration. Then the committee members will consider the matter and resolve the conflict as deemed appropriate under the circumstances.

In addition, for clients participating in securities lending programs, security recall provisions may interfere with, or prohibit, our ability to vote on shareholder matters. In these and similar circumstances, we may not, or may be unable to, act on specific proxy matters.

Voting on shareholder matters in foreign countries, particularly in emerging markets, may be subject to restrictions (including registration procedures that result in a holding being illiquid for a period of time and limitations that impede or make the exercise of shareholder rights impractical).

In the event the standard guidelines or any client's custom guidelines do not address how a security should be voted or state that the vote is to be determined on a "case-by-case" basis, the security is voted in accordance with ISS recommendations. If ISS does not make a recommendation, we ask the appropriate portfolio manager to make a decision and complete the same form, with a similar review process as described above.

Clients who wish to obtain either a copy of our voting policies and procedures or information as to how ISS voted securities in their account should send a written request to:

MacKay Shields LLC  
9 West 57<sup>th</sup> Street  
New York, NY 10019  
Attention: Client Services

## **FINANCIAL INFORMATION**

This item requires disclosure of any financial condition that is reasonably likely to impair our ability to meet contractual commitments to clients. Currently, there is no financial condition that is reasonably likely to impair our ability to meet contractual commitments to clients.