

## FORM ADV PART 2A: FIRM BROCHURE



**Stellus Capital Management, LLC**  
**4400 Post Oak Parkway**  
**Suite 2200**  
**Houston, Texas 77027 USA**  
**Phone (713) 292-5400**  
**Fax (713) 292-5450**  
**[www.stelluscapital.com](http://www.stelluscapital.com)**  
**March 25, 2014**

This brochure provides information about the qualifications and business practices of Stellus Capital Management, LLC. If you have any questions regarding the contents of this brochure, please contact us at (713) 292-5414 or via email at [thuskinson@stelluscapital.com](mailto:thuskinson@stelluscapital.com). The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission (the "SEC") or by any state securities authority. Registration with the SEC or any state securities authority does not imply a certain level of skill or training. Additional information about Stellus Capital Management, LLC can also be found on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

## **Item 2   Material Changes**

This Brochure dated March 25, 2014 amends our Brochure that was filed on September 4, 2013. While there are no are no material changes to our business or the investment strategies we offer, we did launch three additional private funds on November 27, 2013. These new private funds have a master feeder structure and the investment strategy is similar to Stellus Capital Investment Corporation, the business development company, to which we are the investment adviser.

### Item 3 Table of Contents

Item 2	Material Changes .....	2
Item 3	Table of Contents.....	3
Item 4	Advisory Business.....	4
Item 5	Fees and Compensation.....	6
Item 6	Performance-Based Fees and Side- by-Side Management .....	7
Item 7	Types of Clients .....	7
Item 8	Methods of Analysis, investment Strategies, and Risk of Loss .....	8
Item 9	Disciplinary Information.....	23
Item 10	Other Financial Industry Activities and Affiliations.....	23
Item 11	Code of Ethics, Participation or Interest in Clients Transactions, and Personal Trading.....	23
Item 12	Brokerage Practices .....	26
Item 13	Review of Accounts.....	28
Item 14	Client Referrals and Other Compensation .....	28
Item 15	Custody .....	28
Item 16	Investment Discretion.....	29
Item 17	Voting Client Securities .....	29
Item 18	Financial Information .....	29

#### Item 4 Advisory Business

Stellus Capital Management, LLC (“Stellus”), a Delaware limited liability company, is an investment advisory firm which began operation on January 3, 2012. Stellus’ team consists of 21 people, including the management team. It is headquartered in Houston, Texas, with people located in Rye, New York and Bethesda, Maryland. There is one principal owner, Robert Ladd. Stellus’ non-discretionary regulatory assets under management as of December 31, 2013 were \$408,261,833. Stellus’ discretionary regulatory assets under management as of December 31, 2013 were \$719,482,704.

Stellus’ strategy is focused on providing debt and equity capital to small and midsize businesses in all industry sectors throughout North America. The team provides capital solutions at all levels of the capital structure, including:

- Senior Debt
- Second Lien Debt
- Mezzanine Debt
- Convertible Debt
- Preferred and common equity

Capital solutions can range from \$1 million to over \$100 million for public and private entities seeking capital for various purposes, including:

- Acquisitions
- Recapitalizations
- Growth opportunities
- Leveraged buyouts
- Rescue finance
- Distressed or turnaround situations
- Bridge loans

The management team of Stellus has worked together for a number of years across several different companies. In 2004, certain members of the team joined DESCO to start the direct capital business, a strategy within certain investment vehicles advised by DESCO.

Stellus has entered into an ongoing strategic relationship agreement with DESCO and certain of its affiliates whereby Stellus provides advisory assistance, on a non-discretionary basis, to DESCO and such affiliates regarding certain direct capital investment positions held by clients of DESCO and such

affiliates (“DC Positions”). Any transactions recommended by Stellus with respect to the DC Positions are subject to approval by DESCO or its affiliates, as applicable. DESCO or its affiliates are ultimately responsible for the valuation of all the DC Positions, and the preparation of any related financial statements and investor reporting.

The DC Positions are held in private investment vehicles that are not registered or required to be registered under the Investment Company Act of 1940, as amended (the “Investment Company Act”). The securities of these private investment vehicles are not registered or required to be registered under the Securities Act of 1933 (“the Securities Act”) and are privately placed to qualified investors.

In 2012, Stellus began providing discretionary investment advisory and management services to Stellus Capital Investment Corporation (“SCIC”), a non-diversified, closed-end management investment company that has elected to be regulated as a business development company (“BDC”) under the Investment Company Act.

In 2013, Stellus began providing discretionary investment advisory and management services to five private funds (individually, a “Private Fund” and together, the “Private Funds”). The Private Funds are investment vehicles that are not registered or required to be registered under the Investment Company Act. The securities of the Private Funds are not registered or required to be registered under the Securities Act and are privately placed to accredited and qualified investors. While the Private Funds pursue similar investment opportunities as Stellus’ other Clients, three of the Private Funds are focused in the energy sector (“Private Energy Funds”) and the other two Private Funds have the same broader credit focus as the BDC (“Private Credit Funds”).

Two of Private Energy Funds have the same initial investors. One of these two Private Energy Fund will be comprised of only the initial investors and their permitted transferees, while the second Private Fund will be open to additional investors subject to satisfying certain eligibility requirements. The strategies of all 3 of the Private Energy Funds are similar although the terms including the fees are different. Stellus or an affiliate may enter into side letters or other similar agreements with certain prospective or existing investors in the Private Energy Funds, whereby such investors may be subject to terms and conditions that are more favorable than other investors in the respective Private Energy Fund. For a detailed discussion of side letters and other terms, investors should refer to each Private Energy Fund’s official offering documents.

One of Private Credit Fund has a master-feeder structure where investors generally invest in the feeder fund, which in turn invest in the master fund, which conducts the actual investment activities. The other Private Credit Fund is a Venture Capital Operating Company (“VCOC”) and invests pre rata with the

master fund. Stellus or an affiliate may enter into side letters or other similar agreements with certain prospective or existing investors in the Private Credit Funds, whereby such investors may be subject to terms and conditions that are more favorable than other investors in the Private Credit Funds. For a detailed discussion of side letters and other terms, investors should refer to each Credit Private Fund's official offering documents.

DESCO and its affiliates (solely in their capacity as sponsors or managers of the investment vehicles containing the DC Positions), SCIC and the Private Funds, will each be referred to herein as, a "Client" and, collectively, the "Clients".

#### Item 5 Fees and Compensation

All Clients may incur expenses in connection with custodial or brokerage services discussed in Item 12. In addition, Clients bear their own operating costs and expenses relating to their organization and operations, which may include, but are not limited to expenses incurred in identifying, assessing, acquiring, negotiating, structuring, and disposing of investment opportunities, including any financing, legal, accounting, management and consulting fees whether or not a Client actually invests in the specific investment opportunity or not; administrative expenses associated with an annual audit, financial and tax returns and tax reporting to a Client's investors; registration and other investment costs; interest and fees associated with any permitted borrowings; costs of any litigation, D&O insurance and other types of insurance, indemnification or extraordinary expense or liability; meetings of Client investors; fees and disbursements to attorneys, consultants, accountants, fund administrators, service providers and any other professionals relating to Client matters.

To the extent any Clients are pooled investment vehicles, investors and eligible potential investors should consult each Client's official governing documents for a detailed discussion of the specific fees and expense associated with that Client.

Neither Stellus nor its supervised persons receive compensation for the sale of securities or other investment products to investors.

#### DC Positions

Pursuant to the strategic relationship with DESCO and certain of its affiliates, Stellus is paid management fees and performance fees by DESCO and/or its affiliates with respect to the DC Positions.

## SCIC

The fee for investment advisory and management services provided to SCIC consists of two components; a base management fee and an incentive payment. The SCIC prospectus contains the calculation and payment method for the investment advisory and management services provided to SCIC. For additional information about the incentive payment, please refer to the section entitled “Performance-Based Fees”.

## Private Funds

Pursuant to the governing documents of each Private Fund, Stellus or an affiliate is paid an annual asset-based management fee which ranges between 1.5% and 2% and performance based fees which ranges between 15% and 20% of realized net profits calculated after non-Stellus affiliated Private Fund investors have first received the return of their capital and a specific annual cumulative compounded rate of return. The management fees may be reduced by any net fees paid to Stellus or its affiliates due to certain deal fees and breakup fees received from companies in which the Private Funds have or may invest.

## **Item 6 Performance-Based Fees and Side- by-Side Management**

Stellus' base management fee for advising SCIC is calculated based on the gross assets of SCIC excluding cash and cash equivalents. Therefore, Stellus benefits when SCIC incurs debt or uses leverage, and Stellus controls the amount of debt or leverage used by SCIC. Stellus will only incur debt and/or leverage if it is in the best interest of investors and not for its own financial benefit.

If Stellus is paid a higher performance-based fee from one Client, it may have an incentive to devote more research and development or other activities, and/or to recommend the allocation of investment opportunities, to such higher fee-paying Client.

Stellus will always endeavor to recommend the allocation of investment opportunities in a fair and equitable manner.

## **Item 7 Types of Clients**

Stellus currently only provides advice to SCIC, the Private Funds and to DESCO and certain of its affiliates regarding the DC Positions. SCIC and the Private Funds are Stellus sponsored pooled investment

vehicles and the DC Positions are held in various DESCO or affiliate sponsored pooled investment vehicles.

SCIC is a non-diversified, closed-end management investment company that has elected to be regulated as a BDC under the Investment Company Act.

The DESCO affiliated sponsored pooled investment vehicles and the Private Funds are not registered or required to be registered under the investment Company Act and their securities are not registered or required to be registered under the Securities Act and are privately placed to qualified investors; and generally have a minimum investment requirement that may be waived by the investment manager at its sole discretion.

## **Item 8   Methods of Analysis, investment Strategies, and Risk of Loss**

### **Methods of Analysis and investment Strategies**

Stellus will provide investment recommendations related to Clients' specific investment strategies which are primarily with respect to corporate loans, and also with respect to securities, commodities, other financial instruments, and other interests. Stellus' focus will be on providing debt and equity capital to small and mid-sized businesses in all industry sectors throughout North America. The Private Funds, while employing similar investments are focused in the energy sector.

Stellus is seeking to accomplish its investment objective through the origination of debt and/or equity financing and, purchase and sale of investments. Investment recommendations provided to the Funds may include for example, loans, bonds, notes, debentures, bills, trade claims, and other forms of indebtedness or liability issued or incurred by corporations or other entities; common and preferred stock of corporations (including investment companies); options, rights, warrants, convertible securities, exchangeable securities, synthetic and/or structured convertible or exchangeable products, participation instruments, and investment contracts; bank notes, term loans, debtor-in-possession ("DIP") loans, revolving loans, bank guarantees, letters of credit, and other forms of lender assets or obligations; currencies; swaps and other derivative instruments; futures, options on futures, and forward contracts; mortgages, mortgage- and other asset-backed securities, real estate, easements, other forms of real property-related instruments, and interests in the foregoing and in real estate investment trusts ("REITs"); commodities; money market instruments; receivables; financial interests in settlements of legal disputes; assets with specified tax attributes; limited partnership and other limited liability interests; general partnership and other unlimited liability interests; royalty rights and real



property interests; and/or contracts or derivatives relating to the foregoing; in each case whether now existing or created in the future. Stellus may also engage in activities in furtherance of or incidental to the origination, purchase and sale, and/or holding of the above investments, including entering into repurchase agreements, reverse repurchase agreements, buy-sellbacks, sell-buybacks, and other trading or financing transactions.

#### Potential Risk Factors

The following analysis of risk factors refers to Stellus and discusses certain risks that may exist for investors in Funds advised by Stellus.

Any investment involves substantial risks that should be carefully considered. Certain risk factors that may be considered applicable to an investment recommended by Stellus are outlined below. Additional risk factors are outlined in the offering documents for the applicable Client. It should be noted, however, that there may be other risk factors applicable to such an investment that are not identified but that might still result in material losses to investors. Prospective investors should also consult their own legal, investment, tax, and other advisers, and the applicable offering documents, as to whether an investment recommended by Stellus is appropriate for them. All investments in securities involve a risk of loss that investors should be prepared to bear.

It should be noted that many of the risks outlined under one caption or heading are applicable to one or more other captions and headings.

#### No Assurance of investment Return

An investment advised by Stellus is not intended as a complete investment program. Such an investment should be regarded as speculative in nature and appropriate only for a sophisticated investor that can afford a loss of all of such investment and that is able to invest for an indefinite period. It should not be assumed that an investment in a Fund will be profitable. In addition to the risk of loss on its investments, Fund investments are subject to the direct and indirect fees and expenses or applicable offering documents, which will reduce returns and require that Stellus make a certain level of profit from its investing activities in order for an investment simply to break even.

Past performance of Stellus' strategies or the investment vehicles that it has advised and/or managed, or of any investment strategies operated within any such investment vehicle, is not indicative of the results that will be achieved by Stellus in the future and provides no assurance of the success of Stellus in achieving its investment objective.

### General Factors

The prospects of an investment in a Fund could be materially adversely affected by changes or instability in market, economic, political, technological, regulatory, and social conditions, and by numerous other factors outside the control of Stellus.

Disruptions in the global financial markets may have materially adverse, and in certain cases catastrophic, consequences for the values, liquidity, and stability of certain investments. Such disruptions may occur in the future, and the duration, severity, and ultimate effect of such disruptions are difficult to forecast.

In addition, some of Stellus' investment strategies and/or investments are likely to be exposed to risks relating to weaknesses in various global economies and risks relating to the economic cycle. Numerous factors affecting the performance of Stellus' investment strategies, such as interest rates, commodity prices, equity prices, availability, and terms of financing, demand from market participants, and deflationary and inflationary pressures, may be affected by the economic cycle and long-term economic trends. Predictions about financial market conditions and economic factors are highly uncertain, and the presence, duration, and impact of any market or economic conditions could have a material adverse effect on Stellus' investment strategies.

### Special Risks of Certain Markets

Certain markets may pose special risks due to, among other factors, the limited availability of useful information, the reliance on self-interested persons for price and other information, and more or less regulation. For example, price information might be available only from dealers and might not be verifiable. Further, less regulation in certain markets might enable market intermediaries or other investors to engage in "frontrunning" (whether directly or through their customers or agents) of Stellus' trades, to misuse information about positions managed by Stellus to reduce the value or liquidity of those positions, and to take other actions that materially adversely affect Stellus' investment strategies. The limited availability of price information or actions of market intermediaries or investors could exacerbate other risk factors outlined in this brochure, including short squeezes, and could have a material adverse effect on Stellus' investment strategies. In addition, dealers may withdraw or substantially reduce the scope of their activity with regard to certain markets or investments without notice, resulting in disruptions to strategies, pricing, and/or the ability to liquidate or close out positions. Any of the foregoing could have a material adverse effect on Stellus' investment strategies.

### Availability of Investment Opportunities

Identification and exploitation of investment opportunities and investment strategies by Stellus involve a high degree of uncertainty. Stellus makes decisions based on its assumptions, assessments, and estimates, all of which are subject to error. There can be no assurance that Stellus will be able to identify and/or successfully take advantage of suitable investment opportunities. Even if Stellus takes advantage of an investment opportunity, there is a risk that such investment opportunity will result in losses. If Stellus is not able to identify and/or take advantage of suitable investment opportunities, it may change its risk parameters in order to deploy capital, which may have a material adverse effect on Stellus' investment strategies. In addition, Stellus may rely on market participants to inform it of particular trading and/or other investment opportunities. Returns may be reduced if market participants fail to provide such information or if Stellus is otherwise unable to source opportunities it considers appropriate for its investment strategies.

### Origination Activities

Stellus engages in the origination of debt and/or equity financing. The Funds are subject to applicable laws in each jurisdiction in which such activities take place.

The market for originating debt and equity financing is highly competitive, and Stellus may be unable to compete effectively with other market participants for origination opportunities. Price pressure from competitors (including market participants that are not directly originating loans) may cause Stellus to recommend a Client lower the interest rates that it charges borrowers, which consequently may lower the value of the loans. Further, if competitors adopt less stringent loan origination standards in order to maintain their loan origination volume, Stellus may cause Clients to do so as well. If Stellus adopts less stringent loan origination standards, a Client will bear increased risk for each loan originated under such less stringent standards, which may not be compensated by an increase in price.

Alternatively, Stellus may determine not to adopt less stringent origination standards in this competitive environment, which decision may result in a loss of market share. Increased pressure on pricing and origination opportunities likely would reduce the volume and quality of Stellus' origination activity and materially adversely affect Clients. Some competitors may have higher risk tolerances or different risk assessments than Stellus, thereby allowing such competitors to achieve a broad diversification of investments and to establish more relationships than Stellus. These competitive pressures could have a material adverse effect on Clients.

### Limited Diversification; Concentration; Correlation

Investments recommended by Stellus may not be broadly diversified among particular issuers, issuances, companies, countries, industries, exchanges, counterparties, strategies, types of investments, or other shared characteristics. In general, less diversification may lead to greater volatility and/or risk than would be the case with a more broadly diversified portfolio. Even if investments in respect of which Stellus has provided advice are diversified, however, there can be no assurance that such diversification will reduce volatility and/or risk. In addition, a portfolio may be concentrated in particular issuers, issuances, companies, countries, industries, exchanges, counterparties, strategies, types of investments, and/or other shared characteristics, without any limitation other than applicable law or regulation (if any). Such concentration would magnify the risks associated with such investments, including the risk of significant losses.

There can be no assurance that Stellus will achieve returns that are not closely correlated with various market indices or the returns of other investment vehicles. There can be no assurance that Stellus will value less-correlated returns more highly than any other factor in selecting the investments and strategies. In addition, certain of the strategies deployed by Stellus may maintain (possibly extensive) unhedged exposure for an indefinite period to various sources of equity, credit, interest-rate, and/or other risk, whether known or unknown, while other strategies deployed may have such unhedged exposures from time to time. There can be no assurance that an investment with Stellus would improve the risk/return profile of any investor's portfolio or otherwise improve the performance of the investor's overall portfolio.

### Low Creditworthiness Investments

There is no minimum credit standard for any of Stellus' investment strategies, and a (possibly substantial) portion may, whether at the time of investment or at a later time, involve investments that are unrated; rated below "investment grade" by recognized rating services; and/or defaulted. Unrated, sub-investment-grade, and defaulted investments generally involve greater risk of loss in either a short or a long position than do investment-grade investments. For example, the market values and yields of unrated, sub-investment-grade, and defaulted investments generally react more dramatically to changes in general economic conditions, in the levels of interest rates, and in the financial condition and prospects of their issuers than do those of more highly rated investments. During periods of economic downturn or rising interest rates, issuers of unrated, sub-investment-grade, and defaulted investments may experience, to a greater degree than issuers of more highly rated investments, certain forms of financial stress that could materially adversely affect such investments. Such issuers may be in early stages of development; may not have proven operating histories; may be operating at a loss or have

significant variations in operating results; may be engaged in rapidly changing businesses with products subject to a substantial risk of obsolescence; may require substantial additional capital to support their operations, to finance expansion, or to maintain their competitive position; or may otherwise have a weak financial condition. Additionally, such issuers may be highly leveraged, which may present greater risks to these companies.

Adverse publicity and investor perceptions, whether based on fundamental analysis, market rumors, distress of related issuers, or other sources, may materially adversely affect such low creditworthiness investments. Adverse effects on long positions in these investments include the increased probability of default, the decreased value of any recovery in connection with a reorganization proceeding, decreased secondary market prices (if any) for these investments, and general decreases in the liquidity of these investments. The secondary market for these investments is concentrated among relatively few market-makers or investors and may be expected to be less liquid than the secondary market for investments that have higher ratings or are issued by non-distressed issuers. In addition, the lower liquidity of unrated, sub-investment-grade, and defaulted investments, as well as other factors outlined above, could exacerbate the risks of short positions in these investments.

Certain forms of low creditworthiness investments may be issued pursuant to note indentures, promissory notes, or other indicia of indebtedness that contain fewer debt covenants, rights, and remedies compared to those afforded to lenders under a credit agreement. As a result, such investments may be more sensitive to certain risk factors as compared to similar debt instruments with greater debt covenants, rights, and remedies. Moreover, the lack of certain financial covenants with respect to such investments may result in a higher risk of loss and may hinder the ability of Stellus to restructure a problematic loan in order to mitigate its exposure to loss.

### Derivative Instruments

Stellus may recommend all types of derivative instruments without limitation other than any applicable limitations imposed by regulations and/or by counterparties and clearing brokers. Derivative instruments are financial instruments that derive their performance, at least in part, from the performance of an underlying asset, index, interest rate, or other reference instrument. Examples of derivative instruments include swaps, futures, forwards, options, warrants, options on futures, and swaptions.

Investments and trading in derivative instruments are generally highly speculative and involve various risks that are different in certain respects from, and are possibly greater than, the risks associated with investing directly in the applicable underlying assets or reference instrument.

## Debt investments

Without limiting the scope of its possible activities, Stellus may recommend holding, structuring, and restructuring loans and other forms of indebtedness.

### Secured Loans; Second Lien Loans; Unsecured or Subordinated Loans

Measures taken by Stellus to protect investors' interests in loans in which they may invest, including the validity or enforceability of such loans and the creation and maintenance of the anticipated priority and perfection of applicable security interests, may prove to be inadequate. There can be no assurance that any collateral would be sufficient to cover the obligations being collateralized or the amount of an investor's investment. Any collateral may decline in value; may be subject to competing claims of creditors; may be difficult to recover or sell due to legal, regulatory, or other reasons; or otherwise may be inadequate to allow an investor to recoup its investment.

Stellus may recommend an investment in certain loans ("Second Lien Loans") that are secured by a second priority interest or lien on collateral but are subordinated to other secured obligations. Second Lien Loans are subject to a risk that the cash flow of the related borrower and the property securing the Second Lien Loan may be insufficient to make scheduled payments on the Second Lien Loans after giving effect to any obligations in respect of the senior secured loans of the borrower. Second Lien Loans are also expected to be less liquid than senior secured loans.

Finally, Stellus may recommend investments in various types of unsecured indebtedness (such as senior unsecured, subordinated, or general indebtedness) that would be junior in priority to the claims of secured creditors. The claims of secured or senior creditors may exhaust some or all of the assets of a borrower before unsecured, subordinated, or general creditors may participate in such assets.

### Lender Liability; Equitable Subordination; Fraudulent Conveyance

Investments structured as loans or other forms of indebtedness may subject investors to claims of lender liability and/or may be subject to claims of equitable subordination or recharacterization.

The risk of such claims may be exacerbated if an investor holds a significant equity position and/or certain management positions (including representation on the board of directors) with respect to the applicable borrower. Under the concept of "equitable subordination," a court may subordinate the claim of a lender or bondholder to the claims of other creditors in certain circumstances, such as if the court finds that such lender or bondholder engaged in inequitable conduct to the detriment of other creditors. In addition, under certain circumstances, a loan may be recharacterized as an equity

contribution if a court determines that the loan was in substance a disguised equity contribution to a company. If a court recharacterizes a loan as an equity contribution, such loan would be made subordinate to the claims of all creditors. Any successful claims of lender liability against an investor or any successful claims of equitable subordination or recharacterization could have a material adverse effect on such investment held by such investor (possibly resulting in losses that exceed the value of such investment).

Investments structured as loans or other forms of indebtedness may also be subject to claims of fraudulent conveyance. Any claims of fraudulent conveyance or preferential payment with respect to an investment could have a material adverse effect on an investor, which could be required to return related payments.

#### Certain Additional Risks

The terms of certain loans or other forms of indebtedness held by investors advised by Stellus may obligate such investors to extend to a borrower additional credit in the future, either at the request of the borrower or if certain other conditions are met. Any such additional extension of credit would increase such investor's exposure to the applicable borrower. In addition, if an investor does not have adequate available funds or chooses not to fund at the time additional credit is required, the borrower may seek to assert claims for damages against such investor.

Certain of the loans in which Stellus may recommend investing may require the investor to indemnify or reimburse the lead or agent bank for the loan for costs incurred by such bank. Such indemnification or reimbursement may cause substantial losses to the investor and may be required in addition to any costs incurred by such investor itself. In addition, lenders and other persons may seek to bring claims against the investor for the acts or omissions of a lead or agent bank.

#### Distressed Issuers

Stellus may recommend that an investor invest in long and short positions in investments issued by or otherwise related to companies that at the time of the applicable investment are experiencing, or subsequent to the applicable investment do experience, various forms of financial, business, operational, legal, and/or other distress or impairment, including companies involved in bankruptcy or other reorganization or liquidation proceedings (collectively, "Reorganization Proceedings"), as well as those emerging from Reorganization Proceedings and those seeking financial restructurings or reorganizations outside such proceedings. These investments involve a high degree of risk and the total value of the applicable investment may be lost.

Stellus also may recommend that an investor purchase from banks, other financial institutions, or other investors bank loans (whether through assignment or participation transactions) and other forms of direct or indirect indebtedness (including revolving loans and letters of credit) of distressed companies.

Investments in loan participations would expose an investor to risks related to the creditworthiness of the banks or other financial institutions issuing such participations.

Stellus also may recommend that an investor purchase bankruptcy claims (including trade claims), which are amounts owed to creditors of a distressed company. Investments in bankruptcy claims are difficult to value. Moreover, bankruptcy claims generally are illiquid and non-interest-bearing, and there can be no assurance that a company will be able to satisfy its obligations under a claim.

Sophisticated financial and legal analysis is often necessary for successful investment in distressed companies. There is no assurance that Stellus will correctly evaluate the value of the collateral (if any) supporting the investments held by an investor or the prospects for a successful reorganization or similar action. Such investments may be subject to additional risks, such as significant volatility in the value of the investment; the involuntary exchange of such investments for cash, financial instruments, or other property (including illiquid investments) having substantially less value than the original investment; and/or delayed or extended payment for such investments.

In addition, Reorganization Proceedings, as well as other financial restructurings or reorganizations, are subject to a number of risks. For example, such proceedings may be of uncertain duration; may be subject to unanticipated and possibly lengthy delays; may involve substantial legal, professional, and administrative costs to the reorganizing company and its investors; may involve other factors that are beyond the control of the reorganizing company and its investors; and/or may result in the liquidation of the reorganizing company. Further, Stellus, on behalf of an investor, may decide to become involved in the restructuring of a particular distressed company, including through representation on creditors' or equity holders' committees or other groups (whether formal or informal) and participation in litigation or direct negotiations with the company's management, each of which may involve special risks and/or conflicts of interest for an investor. The occurrence of any of these risks could have a material adverse effect on the value of the applicable investment or on Stellus' ability to dispose of or to act to protect the value of such investment.



### Illiquid Investments

Stellus may recommend that an investor make investments characterized by varying degrees of liquidity, such as investments for which there exists no actively traded secondary market and which are thus highly illiquid or for which there is an absence of readily ascertainable market values. Any illiquidity with respect to the investments recommended by Stellus may or may not be anticipated and/or may vary over time. Such investments may constitute a substantial portion of the investor's assets in respect of which Stellus provides investment recommendations and may involve significant transaction costs when they are purchased or disposed of, whether through adverse price movements (whether related to liquidity or otherwise), increased spreads between quotes and dealer mark-ups (which may already be material for such investments), and/or other transaction costs. Stellus may recommend to liquidate illiquid investments (quickly or otherwise) if it believes that such liquidations may be warranted by market conditions or other considerations.

In addition, Stellus may recommend that an investor make investments that are subject to resale restrictions due to regulatory, statutory, or contractual provisions that limit the ability of Stellus to liquidate such investments. Such regulatory, statutory, or contractual restrictions could cause liquidity-related losses, could result in exposure to unhedged positions, and could have other material adverse effects on investors.

### Leverage

Stellus may recommend that investors borrow or otherwise use leverage to increase profit potential while increasing risk of loss and volatility. Leverage may take the form of borrowed money, uncovered short positions, uncovered put options, derivative instruments that are inherently leveraged, and other forms of direct and indirect borrowings. If the interest expense on borrowings were to exceed the net return on the portfolio of securities purchased with borrowed funds, returns would be lower than if the investors were not leveraged. Additionally, the use of leverage, while providing the opportunity for higher returns, also increases volatility and the risk of loss.

### Private Investment Activities

Stellus may engage in certain private investment activities, certain risks of which are outlined below.

### Private Equity-Related Investments Generally

Stellus may recommend that an investor acquire controlling or non-controlling positions in privately held companies.

Private equity-related investments are generally characterized by an extremely high degree of illiquidity, frequently lasting several years and possibly indefinitely. The realization of a private equity return, if any, generally occurs only upon the partial or complete monetization of an investment by means of a dividend, distribution, recapitalization, initial public offering, asset liquidation, sale, other disposition, or similar financial event. Contractual or legal restrictions may delay realization of a private equity-related investment beyond the occurrence of any such financial event. In addition, an investor generally is expected to earn little or no current cash income on such investments prior to any realization event. Private equity-related investments may be extremely difficult to value, particularly in the absence of a specific liquidity event, readily available comparables, or a material change in the company associated with such investment or the industry in which such company operates. Even if a valuation change is ultimately made, the change may be, by necessity, highly subjective.

The long time horizons of investing in private equity-related investments may expose an investor to shifts in market, economic, political, technological, regulatory, and/or social conditions to an unusual degree. Developments occurring after a private equity-related investment is acquired may fundamentally alter the anticipated market for such investment, preventing Stellus from disposing of the investment profitably or at all, or subjecting investors to risk of a potentially complete loss on such investment.

Stellus may become involved in the exercise of control of a particular privately held company, including in the form of representation on the boards of directors, equity holders' committees, or other groups (whether formal or informal) and participation in litigation.

### Follow-on investments; Co-investments

Following an initial investment in a privately held company, Stellus may be presented with the opportunity to provide additional capital to such company. Even if such an investment is desired, it is possible that investors will have insufficient available capital to act. Any recommendation by Stellus not to make a follow-on investment or any inability by an investor to fund such an investment could have a material adverse effect on a privately held company in need of capital, potentially materially adversely affecting investors.

Stellus may recommend co-investing with third parties (including other investors advised by Stellus, or other Related Persons of Stellus) through consortiums of investors, partnerships, joint ventures, or other similar arrangements. Such investments may involve risks in connection with such third-party involvement, including the possibility that any such third party may have financial, legal, or regulatory difficulties that have a material adverse effect on such investment, may have economic or business interests or goals that are inconsistent with those of the relevant investor, may pursue interests inconsistent with those of the relevant investor, may default on their obligations, and/or may be in a position to take (or block) action in a manner contrary to the relevant investor's investment objective. In addition, an investor may in certain circumstances be liable for the actions of its co-investors. Such investments may involve performance charges, incentive compensation arrangements, and/or other fees payable to such third parties.

#### Hedging Transactions

Stellus may seek to limit an investor's exposure to various risk factors through the use of various hedging techniques. There can be no assurance that such hedging techniques will be effective or that they will result in higher or more stable returns than would have been the case had they not been employed. Moreover, such hedging techniques will tend to limit any potential gain that might result from an increase in the value of a hedged position.

It should be noted that any hedging techniques recommended by Stellus would be intended only to reduce exposure to certain risks and not to reduce all forms of investment risk. Further, Stellus is not obliged to hedge any particular form of risk in any particular situation, and Stellus will be free to recommend investors assume such risks and/or change their investment policies and practices in any manner as determined by Stellus. Moreover, certain of the investment strategies recommended by Stellus may from time to time have extensive unhedged exposure to various sources of equity, credit, interest rate, and/or other risk, whether known or unknown.

Under certain circumstances, hedging techniques intended to reduce certain forms of risk may actually increase risk, whether due to the unintended market impact of hedging transactions, leverage effects associated with hedging positions, unexpected adverse price movements of a hedging instrument relative to the hedged instrument (i.e., adverse changes in the "basis" between the hedging and hedged instrument), lower liquidity of the hedged and hedging positions relative to an unhedged position, the risks related to the use of derivative instruments, or other factors. In addition, even where Stellus seeks to hedge a particular risk, a suitable hedging transaction might not be identified by Stellus, not be available to an investor, and/or not be successfully executed.

### Unlimited Liability investments

Stellus may recommend that an investor invest directly or indirectly in unlimited liability entities, which investments would expose such investor to a risk of loss in excess of its initial investment in such entities. Such investments may be made in general partnerships and/or other unlimited liability entities.

### Price Volatility

The price of investments increases or decreases due to among other things credit risk, interest rate risk or changes in market factors (market risk). Generally, the longer the portfolio duration, the greater the degree of price fluctuation. Also, more concentrated portfolios have greater potential volatility. Below investment -grade securities are more susceptible to market risk and general economic factors than investment-grade securities, and, thus, typically bear increased price volatility risk.

### Bridge Investments

Investments may include bridge financing to portfolio companies. While a bridge financing is outstanding, the bridge lender bears the risk of changes in the capital markets. A portfolio company's inability to refinance a bridge loan may result in retaining a long-term investment in a junior security or having its bridge loan converted to equity.

### Control Position and Participation on Creditors' Committees and Boards of Directors.

As part of its strategy for certain Clients, Stellus often seeks investment opportunities that allow it to control or exercise significant influence over management and the strategic direction of the companies in which it invests. The exercise of control over a portfolio company imposes additional risks on Clients of liability for environmental damage, product defects, failure to supervise management, labor disputes and other types of liability associated with a portfolio company's operations. The exercise of control over a portfolio company could expose Clients' assets to claims by such portfolio company or by its security holders and its creditors.

In other situations, where Stellus is not in a position to exercise control or significant influence representatives of Stellus, on behalf of investors, may participate on committees formed by creditors to negotiate with the management of financially troubled companies that may or may not be in bankruptcy. Stellus may also seek to negotiate directly with debtors with respect to restructuring issues. In the situation where a representative of Stellus chooses to join a creditors' committee, the representative would likely be only one of many participants, each of whom would be interested in

obtaining an outcome that is in its individual best interest. There can be no assurance that the representative would be successful in obtaining results most favorable to the investors advised by Stellus in such proceedings, although the representative may incur significant legal fees and other expenses in attempting to do so. As a result of participation by the representative on such committees, the representative may be deemed to have duties to other creditors represented by the committees, which might thereby expose the investors advised by Stellus to liability to such other creditors who disagree with the representative's actions. It is possible that Stellus or its affiliates will be represented on the boards of some of the companies in which investors advised by Stellus make investments. Such representation may have the effect of impairing the ability of Stellus to sell such investors' related investments when, and upon the terms, they might otherwise desire, including as a result of applicable securities laws. If Stellus or any of Stellus' affiliates or employees earns compensation with regard to any such board representation, such compensation will generally be remitted to the applicable investors advised by Stellus.

#### Reliance on Key Personnel

The success of a Stellus Client depends upon the skill and expertise of key personnel of Stellus to identify, close and manage portfolio investments. The loss of their services could have material adverse effect on Stellus and its Clients.

### **Risks Specific to Energy Related Investments**

#### Nature of Investments in the Energy Sector

Investments in the energy sector may be subject to a variety of risks, not all of which can be foreseen or quantified. Such risks may include but are not limited to: (i) the risk that the technology employed in an energy project will not be effective or efficient, (ii) uncertainty about the availability or efficacy of energy sales agreements or fuel supply agreements that may be entered into in connection with a project, (iii) risks that regulations affecting the energy industry will change in a manner detrimental to the industry, (iv) environmental liability risks related to energy properties and projects, (v) risks of equipment failures, fuel interruptions, loss of sale and supply contracts or fuel contracts, decreases or escalations in power contract or fuel contract prices, bankruptcy of key customers or suppliers, tort liability in excess of insurance coverage, inability to obtain desirable amounts of insurance at economic rates, acts of God and other catastrophes, (vi) uncertainty about the extent, quality and availability of oil and gas reserves, (vii) the risk that interest rates may increase, making it difficult or impossible to obtain project financing, or impairing the cash flow of leveraged projects, and (viii) the risk of changes in values of companies in the energy sector whose operations are affected by changes in

prices and supplies of energy fuels (prices and supplies of energy fuels can fluctuate significantly over a short period of time due to changes in international politics, energy conservation, the success of exploration projects, the tax and other regulatory policies of various governments, and the economic growth of countries that are large consumers of energy, as well as other factors). The occurrence of events related to the foregoing may have a material adverse effect on Stellus and its investments.

#### Drilling, Exploration and Development Risks

Oil and gas exploration and development companies are subject to specific risks inherent in acquiring or developing recoverable oil and natural gas reserves. Substantial capital expenditures are required for the identification and acquisitions of projects, the drilling and completing of wells and the conduct of development and production operations which may not be profitable. Although an oil or gas well may be producing there may not be sufficient revenues to return a profit after drilling, operating and other costs are considered.

The risk of unanticipated events such as equipment failures, accidents in drilling and completing wells, adverse weather conditions, fires, the unintended release of hazardous materials can result in losses. In addition, successful investment in oil and natural gas properties and other related facilities and properties requires making estimates of oil and gas reserves and corresponding production rates. The process of making these estimations is complex and requires making important assumptions concerning the evaluation of available geological, geophysical, engineering and economic data. These estimates are inherently imprecise.

#### Volatility of Oil and Natural Gas Prices

The value of energy related investments is usually highly correlated to the current market price of oil and natural gas. Oil and natural gas prices can be volatile making it difficult to estimate future prices. An extended decline in prices could reduce the revenues, cash flow and market valuation of these investments. A number of external factors affect prices of oil and natural gas, including:

- Worldwide and domestic supplies of oil and natural gas,
- Political instability or armed conflict in oil and natural gas producing regions,
- Worldwide economic conditions,
- The price of foreign imports,
- The level of consumer demand,
- The price, availability and acceptance of alternative fuels,
- Weather conditions, and

- Actions of federal, state, local and foreign authorities, including changes in existing government regulation, taxation and price control.

#### Extensive Regulation of the Oil and Natural Gas Industry

Federal, state and local authorities extensively regulate the oil and natural gas industry. Legislation and regulations affecting the industry are under constant review raising the possibility of changes that may affect, among other things, the pricing, taxation or marketing of oil and natural gas production. Noncompliance with regulations may lead to substantial penalties. The overall regulatory burden on the industry increases the cost of doing business and, in turn, decreases profitability.

#### Environmental Matters

Environmental laws, regulations and regulatory initiatives play a significant role in the energy industry and can have a substantial impact on investments in this industry. The energy industry will likely continue to face considerable oversight from environmental regulatory authorities and the costs associated with environmental compliance can significantly reduce investment returns.

Failure to comply with environmental requirements could have a material adverse effect on an investment and there can be no assurance that an underlying investment will at all times comply with all applicable environmental laws, regulations and permit requirements.

### **Item 9 Disciplinary Information**

Stellus believes there are no legal or disciplinary events that are material to a Client's evaluation of Stellus' advisory business or the integrity of its management.

### **Item 10 Other Financial Industry Activities and Affiliations**

DESCO will have the right to receive a share of Stellus' revenues for a limited number of future years, and a share of the proceeds of any future sale of Stellus.

### **Item 11 Code of Ethics, Participation or Interest in Clients Transactions, and Personal Trading**

Stellus has adopted a code of ethics (the "Code") that establishes the standard of business conduct that must be followed by, among others, all partners, officers, and employees of Stellus (collectively "Supervised Persons"). The Code incorporates the following general principles, which all Supervised Persons are expected to uphold: act in the best interests of Clients; conduct personal securities

transactions in a manner consistent with the Code, which seeks to address certain conflicts of interest in this regard; avoid taking any inappropriate advantage of one's position at Stellus; maintain confidentiality of information concerning Stellus' securities recommendations and portfolio holdings and transactions; and provide accurate disclosure in reports required by auditors, regulators, or government bodies.

Stellus believes that these general principles not only help Stellus fulfill its obligations undertaken as an investment adviser, but also protect Stellus' reputation and instill in employees Stellus' commitment to honesty, integrity, and professionalism.

The Code also provides guidelines for Supervised Persons regarding adherence to securities laws generally, transactions in personal accounts involving public and private securities and commodities, activities outside of the investment adviser's business, giving and receiving business-related gifts, and the maintenance and memorialization of certain family and/or close personal relationships. For example, the Code requires that all Supervised Persons obtain approval prior to affecting any securities or commodities transaction in a personal or related account for which the employee has not granted discretion to a third party adviser. In addition, the Code requires that all Supervised Persons report Code violations and outlines potential sanctions for such violations. Stellus' Chief Compliance Officer is responsible for various aspects of the Code's administration, including without limitation the monitoring and review of personal securities and commodities transactions of Supervised Persons, and is available for any questions Supervised Persons have regarding the Code. Stellus will provide a copy of the Code to any Client or prospective Client upon request and may elect to provide a copy of the Code to investors in investment vehicles advised or sub-advised by Stellus.

#### Certain Potential Conflicts of Interest

Certain activities of Stellus may present a potential conflict of interest. These activities may include for example, advising other Clients of Stellus, sponsoring other investment vehicles (including those with investment objectives similar to or overlapping with those of current Clients), making investments for their own accounts, or engaging in other lines of business.

Stellus and its related persons may have various advisory, transactional, financial, and other interests in securities and/or other financial instruments that may be purchased or sold by the Funds. These other activities could compete for the purchase, sale, trading, structuring, and restructuring or other investment vehicles in respect of which Stellus provides investment advice of investments. In addition, such activities could conflict with advice Stellus gives to Clients. For example, Stellus could advise that Clients buy or sell certain investments while simultaneously advising other Clients to undertake a



different (including potentially opposite) strategy with respect to those investments. Any common (or opposing) positions described above may limit the ability of Stellus to add to the position held on behalf of any Fund (or any other investment vehicle in respect of which Stellus provides investment advice), to readily liquidate such a position, or to obtain a favorable price in the course of such liquidation. In effecting transactions for any Fund, a related person, and/or any other persons or entities, it may not always be possible or consistent with the investment objective of the Fund or of such other persons or entities to take or liquidate the same investment positions at the same time or at the same prices. The “market impact” associated with liquidation by such other persons or entities may adversely affect the ability of a portfolio, other person, or entity to liquidate its position; or where the position is liquidated, the price at which such liquidation occurs; or where the position of a Fund or other person or entity does not liquidate its position, the mark-to-market value of such position.

In general, Stellus will act in the best interests of its Clients, subject to applicable law and to any agreement, organizational or other document, or disclosure applicable to a particular Fund or underlying investor. Stellus and/or its related persons may hold the same (or the opposite) position in a given security, commodity, or other financial instrument as that held by the Fund at the same time.

Certain Funds may also invest in other proprietary Funds.

Such activities could also expose Stellus to material risks. Stellus has established a variety of restrictions, procedures, and disclosures designed to address potential conflicts between the interests of its Clients and the interests of itself and/or its related persons in this regard, to ensure that its actions are consistent with the best interests of its advisory Clients in this context. When conflicts of interest in this regard arise, they are addressed in compliance with all legal requirements and such restrictions, procedures, and disclosures, as applicable. Restrictions and procedures generally are established by heads of the applicable strategies, senior management, and/or compliance personnel.

Although Stellus expects to devote a certain amount of time and effort to the business and affairs of each Client, it will also devote a substantial amount of its working time and effort to generating new business. These other activities may require substantial commitments of time and resources by Stellus.

Stellus has no obligation to recommend for purchase or sale by Clients any securities that Stellus, or any of its related persons may purchase for themselves or for any other Fund or Client. In addition, the ability of Stellus to effect and/or recommend transactions for certain or all Clients may be restricted due to actual or perceived regulatory requirements in the United States or elsewhere, to Stellus’ or a related person’s internal policies designed to comply with such requirements, to actual or perceived conflicts of interest, to operational issues, and/or to other issues. Regulatory or contractual limitations related to

effecting transactions for certain Clients may not apply to other Clients, resulting in differences in investments and returns.

Stellus generally does not itself trade securities on a principal basis with Clients. Certain Clients and related persons of Stellus, however, could be principals, based on SEC staff guidance, due to an investment in any such Fund or related person by Stellus and controlling persons exceeding 25% of that Fund's or related person's assets. To the extent that Stellus and/or its related persons engage (or are deemed to engage) in principal securities transactions, any such transactions will comply with applicable law. Stellus and/or its related persons may have interests in such transactions that are adverse to a particular Client.

To the extent permitted by applicable law and the applicable governing documents, Stellus may effect "cross transactions" between the Client Accounts. Stellus would only recommend Clients enter into such transactions only if the transactions were consistent with the best interests of both Clients and at a price that Stellus and/or its related persons believe constitutes a fair valuation for both Clients. Neither Stellus nor any related party receives any commission or commission equivalent in connection with these transactions.

Disclosures regarding conflicts of interest and their resolution generally will be contained in the applicable offering documents, this brochure, and/or another document. Other documents, such as financial or periodic reports, furnished to investors may contain disclosure regarding conflicts of interest.

## **Item 12 Brokerage Practices**

Stellus generally negotiates directly with the underlying companies with which it invests. While Stellus may pay a finders' fee associated with identifying investment opportunities, Stellus does not normally pay a brokerage commission or select financial institutions or counterparties for transactions. If Stellus were involved in selecting financial institutions or counterparties for transactions, it would seek to obtain the best execution of transactions under the circumstances (consistent with what it believes to be the best overall interests of Clients), but need not solicit competitive bids, and would not have an obligation to seek the lowest available commission cost. The price offered by a financial institution or counterparty, including commissions and commission equivalents, if any, and other transaction costs, is normally an important factor in this decision, but financial institution and counterparty selection also takes into account the overall quality of the execution services offered, including without limitation such factors as: execution capability; willingness and ability to commit capital; creditworthiness and financial stability; clearance and settlement capability; ability to maintain confidentiality; the provision of

research and other services; and potential or perceived conflicts between and/or among Clients and Stellus related persons and/or other Stellus Clients. Accordingly, transactions may not always be executed at the best price or the lowest available commission. Clients advised by Stellus may need to maintain and use a number of brokerage accounts to facilitate the various trading strategies deployed by Stellus. Nevertheless, the clearing, settlement, and custody of Client positions may be carried out by a limited number of counterparties and, depending on the investment, may require negotiation on a transaction-by-transaction basis. This may create a concentration of exposure to the creditworthiness of the counterparties carrying out such clearing, settlement, and custody. Any failure of any such counterparty could have a material adverse effect on Funds.

If investment recommendations were to be made contemporaneously for multiple Clients in the same instrument, Stellus may, if consistent with market conditions, portfolio characteristics, and applicable law, bunch or aggregate orders (including orders for Clients in which Stellus, its related persons, and/or its personnel have beneficial interests) for execution. Such bunched or aggregated orders might facilitate execution and may reduce brokerage and other costs. Stellus, however, is not required to bunch or aggregate orders. If Stellus is unable to or does not fully execute a bunched transaction or if Stellus determines that it would be impractical to allocate a small number of positions among all of the accounts initially intended to participate in the transaction, Stellus may allocate such positions in a manner determined in good faith to be an appropriate allocation.

Subject to applicable legal restrictions, Stellus or its related persons may execute transactions in which it or its related persons act as principal as applicable, and may also execute transactions in which Stellus has an interest, as described in Item 10.

Stellus attempts to correct any identified potential trade errors. As with all financial gains and losses attributable to its investments, any financial gains or losses resulting from trade errors are generally borne by the applicable Client and underlying investors (as more fully described in the applicable offering documents).

When trading on behalf of multiple Clients with differing performance-based fees, Stellus endeavors to allocate investment opportunities among Clients in a fair and equitable manner. Stellus' trade allocation for any given Client may vary based on differences in investment objectives among Clients, different capital constraints of each Client, varying leverage preferences of each Client, and any scheduled increase or decrease of any particular Client's assets under management. Stellus does not alter its allocation policy with respect to a Client, or allocate trades among multiple advisory Clients, without the approvals of relevant senior management and compliance personnel.

Stellus does not currently participate in directed brokerage.

### **Item 13 Review of Accounts**

For the purposes of providing services to Clients, Robert Ladd, Managing Partner and Chief Investment Officer of Stellus and other members of Stellus' investment committees provides continuous review of Client investments. Stellus' investment committees generally meet at least weekly to discuss existing Client investments as well as to review prospective investment opportunities. As part of its ongoing review process, Stellus regularly reviews certain documents prepared in the investment process, trade data, and other reports for overseeing the investment activity, trading activity, and loan origination performed on behalf of Clients.

Stellus is expected to assist DESCO and its affiliates with written reports on a periodic basis that generally include, among other things, the net asset value or the capital balance of the account and a measure of performance based on the change in valuation of the account during the report period. The DC Positions' respective investment managers provide investors with annual reports including audited financials.

### **Item 14 Client Referrals and Other Compensation**

Stellus may enter into capital introduction agreements with certain financial institutions under which the financial institution does not receive compensation for this service. Stellus does not currently use solicitors for Client referrals. Stellus engaged external placement agents for placement of new fund interests into the private funds. Additionally, Stellus does not currently select or recommend broker-dealers based on whether Stellus or its related persons receive Client referrals.

### **Item 15 Custody**

Stellus does not have custody of any Client assets except in the case of the Private Funds. Stellus and its affiliates are deemed to have custody of the assets of the Private Funds pursuant to Rule 206(4)-2 under the Investment Advisers Act of 1940. Private Fund investors do not receive account statements from the custodian. Stellus arranges for each Private Fund's financial statements to be prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and audited at least annually by an independent public accountant that is registered with, and subject to regular inspection as of the commencement of the professional engagement period, and as of each calendar year-end, by, the

Public Company Accounting Oversight Board in accordance with its rules. Stellus makes those audited financial statements available to all limited partners in each Private Fund within 120 days of the end of the Private Fund's fiscal year. Investors should carefully review those financial statements. Upon liquidation of a Private Fund, Stellus will distribute its audited financial statements prepared in accordance with GAAP to all Investors in the Private Fund promptly after the completion of such audit.

#### **Item 16 Investment Discretion**

Stellus provides its advice to SCIC and the Private Funds on a discretionary basis and to DESCO and certain of its affiliates on a non-discretionary basis.

#### **Item 17 Voting Client Securities**

Stellus does not vote proxies unless applicable and only in cases where Stellus has discretion to vote.

#### **Item 18 Financial Information**

Stellus does not require or solicit prepayment of fees more than 6 months in advance. Stellus has not been the subject of a bankruptcy petition at any time during the past ten years.