

## ITEM 1: COVER SHEET

# Prospect Capital Advisors, LLC

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This brochure provides information about the qualifications and business practices of Prospect Capital Advisors, LLC. If you have any questions about the contents of this brochure, please contact us at the telephone number and/or e-mail address above. The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission ("SEC") or any state securities authority.

Prospect Capital Advisors, LLC is a registered investment advisor. Registration of an investment advisor does not imply any level of skill or training.

Additional information about Prospect Capital Advisors, LLC is also available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

## **ITEM 2: MATERIAL CHANGES**

The previous annual ADV update for Prospect Capital Advisors, LLC (“Prospect,” or the “Firm”) was dated March 31, 2023. The following material change has been made to this brochure since that amendment.

- Item 4 has been amended to reflect that as of December 31, 2023, Prospect has \$439.7 million in discretionary regulatory assets under management.

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## **ITEM 4: ADVISORY BUSINESS**

### **Advisory Business**

Prospect Capital Advisors, LLC is currently registered as an investment adviser with the SEC. From January 2001 to June 2015, the Firm was registered with the State of California Department of Business Oversight. Daniel W. Mendoza is the principal owner and Managing Member of Prospect.

### **Advisory Services**

Prospect serves as the general partner and investment adviser to Prospect Advisors, L.P. and Prospect Advisors QP, L.P. (collectively, the “Funds”), which are privately-placed pooled investment vehicles. In addition, Prospect provides investment services to separately managed accounts (the “SMA(s)” or the “Client(s)”). Interests in the Funds are offered to certain qualified Investors as discussed herein.

The Funds are long/short funds investing primarily in equities. The Funds’ goal is to generate absolute returns, primarily through long and short investments in publicly traded domestic equities, seeking to protect and grow assets in all market environments.

Prospect’s investment philosophy is oriented towards a microeconomic approach to investment selection and risk minimization. Prospect makes investment decisions and attempts to reduce downside risk through in-depth analyses of portfolio companies.

The agreement of Limited Partnership, Confidential Offering Memorandum and Subscription Application (collectively, the “Fund Documents”) for the Funds impose no limits on the types of securities or other instruments in which the Funds may take positions, the type of positions it may take, the concentration of its investments, or the amount of “leverage” the Funds may employ. Prospect has broad discretion to employ a wide variety of investment techniques, even if they involve changes in the investment approach initially anticipated.

The Funds’ investments are tailored to comply with the investment guidelines disclosed in the Fund Documents. Each potential Investor receives a complete set of Fund Documents prior to investing in the Funds.

The investment strategy employed for SMAs may be similar to that of the Funds. By signing an Investment Advisory Agreement or Sub-Advisory Agreement (the “Agreement”), such Clients designate Prospect as an investment manager or sub-advisor over their account.

Certain SMA Agreements impose limits or restrictions on investing in certain securities or types of securities, which is specific to the corresponding Client’s tolerance and goals. Prospect is willing to accept certain restrictions in limited and specific instances through an SMA at the direction of such Clients.

Prospect does not provide portfolio management services to a wrap fee program.

## **Assets Under Management**

As of December 31, 2023, Prospect has \$439.7 million in discretionary regulatory assets under management. The Firm does not manage assets on a non-discretionary basis.

## **ITEM 5: FEES AND COMPENSATION**

### **Fees and Compensation**

For managing the Funds, the Firm receives both an asset-based fee and an incentive allocation. The asset-based fee is 1% per year, billed quarterly in advance, based on the value of the assets under management as of the beginning of the calendar quarter. The incentive allocation is calculated as of December 31 each year. When profits for the current period exceed the unrecouped net losses for prior periods, the Firm receives an incentive allocation of 20% of the profits generated. Solely for purposes of computing this incentive allocation, net profits and net losses include unrealized gains and losses.

For managing the SMAs, the Firm receives an incentive fee. For purposes of computing the incentive fee, net profits will include unrealized gains and losses when such calculation is set forth in the associated Agreement.

If you withdraw capital from the Funds or your SMA, the incentive fee or performance fee for the amount withdrawn will be calculated as of the withdrawal date. SMA incentive fees vary based on certain factors, including but not limited to the SMA type and underlying agreements.

Prospect has authority, at the sole discretion of the Firm, to admit Investors into the Funds who are not qualified to pay an incentive allocation. In this rare instance, Prospect will charge an asset-based fee of 1%, with no incentive allocation. This asset-based fee will be billed on the same schedule as described above.

Prospect will not manage money on an SMA basis for clients who are not qualified to pay an incentive fee.

In order to pay an incentive allocation/fee, each Client and Investor must meet the requirements of SEC Rule 205-3. Effective August 16, 2021, typically, the following criteria must be met:

- Net worth of at least \$2.2 million individually (or jointly with a spouse).
- At least \$1,100,000 invested with Prospect.

Investors and Clients with initial contributions prior to August 16, 2021, may continue to rely on the exemption available at the time of initial investment.

The applicable Agreement and Fund Documents provide additional qualification standards. All incentive fees will be calculated and charged in a manner that complies with applicable rules and regulations, including SEC Rule 205-3.

SMA clients can generally terminate Prospect's management of the respective SMA by providing 60 days written notice. The Firm will calculate the incentive allocation due and send an invoice showing the amount due to us. In addition, the Firm will observe all appropriate refund provisions in the applicable SMA.

Investors in the Funds may make withdrawals as of the last day of any calendar month by providing 60 days written notice as outlined in the Fund Documents.

It should be noted that the terms described above are current account termination and withdrawal terms. Clients and investors should review terms applicable at the time of SMA account opening or original Fund investment as they could vary.

### **Other Costs Involved**

In addition to the advisory fees discussed above, expenses associated with making investments on behalf of SMAs and Funds will also be incurred. These fees include:

- Management fees for ETFs and mutual funds. These are fees charged by the managers of the ETF or mutual fund and are a portion of the expenses of the ETF or mutual fund.
- Brokerage costs and transaction fees for any securities or fixed income trades. These are generally charged by the custodian and/or executing broker.
- Audit costs and third-party administration costs for the Funds and SMAs.

Additional information about brokerage costs and services is provided in "Item 12: Brokerage Practices." Investors should also refer to the Fund Documents for details on the expenses associated with investing in the particular Fund. SMA clients should refer to the Agreement for details on the associated expenses.

## **ITEM 6: PERFORMANCE-BASED FEES AND SIDE-BY-SIDE MANAGEMENT**

Prospect receives an incentive allocation/fee for the Funds and all SMAs as described in "Item 5: Fees and Compensation."

Incentive allocation arrangements could create an incentive for Prospect to make investments that are riskier or more speculative than would be the case in the absence of the arrangement, or favor Funds or SMAs paying higher incentive allocations versus other Funds or SMAs who pay lower incentive allocations. In some circumstances, the Firm may receive increased compensation as a result of unrealized appreciation as well as realized gains.

Prospect has implemented procedures designed to ensure that all Funds and SMAs are treated fairly and equally, and to prevent this conflict from influencing the allocation of investment opportunities among Funds and SMAs.

## **ITEM 7: TYPES OF CLIENTS**

Prospect provides investment advice to Funds, which are pooled investment vehicles. In addition, the Firm provides advice to SMA clients, whose underlying investors may include high net worth individuals, trusts, businesses, and pension or profit-sharing plans.

Generally, Investors in the Funds are required to maintain a minimum \$500,000 investment with the Funds. This minimum may be waived at the sole discretion of Prospect as set forth in the associated Fund Documents.

## **ITEM 8: METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS**

Prospect seeks capital appreciation in the Funds and SMAs that it manages and will invest primarily in publicly traded securities, including common stocks, preferred stocks, stock warrants and rights, bonds, debentures, convertible securities, and other debt obligations, as well as options to purchase and/or sell securities and options on stock market indexes. The Firm is also permitted to engage in short sales of securities. The methods of analysis and investment strategies for SMAs will be identical to the methods applied to the Funds and will be consistent with Prospect's typical investment strategy unless otherwise directed by the SMA client.

Portfolios managed by Prospect will not necessarily represent a broad diversification of investments among issuers, industries, geography, or types of securities. Prospect may invest in restricted securities and other securities for which there is no public market but will not invest more than 10% of the Funds' assets (computed at the time the investment is made) in such securities.

Prospect can buy securities on margin and arrange with banks, brokers and others to borrow money in order to employ leverage when the Firm deems such action appropriate. Prospect generally does not employ these leverage techniques.

Prospect's investment philosophy is oriented towards a microeconomic approach to investment selection and risk minimization. Investment decisions are made in a manner to reduce downside risk by conducting in-depth analysis of the companies in which Prospect invests. These analyses typically involve evaluating a company's management by meeting with the company's managers, assessing management's strategy for the company and analyzing the company's finances in order to test its ability to meet its goals. Prospect believes market risk can be reduced through the use of short positions, with the relative magnitude of the Funds' or SMAs long and short positions being weighted to reflect Prospect's perception of investment opportunities, both long and short. Prospect generally focuses on small and mid-capitalization growth companies.

General Economic, Governmental and Market Conditions. Prospect's investments are affected by general economic and market conditions, such as interest rates, availability of credit, inflation rates, pandemics, economic uncertainty, changes in laws, developments in governmental regulation and national and international political circumstances. These factors affect the success of the businesses in which the Funds' or SMAs' portfolio companies are engaged as well as the market for the securities the Funds hold. Unexpected volatility or illiquidity could impair the Funds' profitability or result in losses.

Pandemics. The impact of epidemics and pandemics greatly affect the economies of many nations, including the United States, individual companies, and financial markets. Pandemics cause volatility and disruption in both the U.S. and global markets, causing uncertainty and risks to economic growth, among other risk. Health crises caused by the recent coronavirus outbreak intensified other pre-existing political, social, and economic risks in certain countries and globally. Also, pandemics may result, as the outbreak of coronavirus has resulted, in closing borders, enhanced health screenings, healthcare service preparation, and delivery, quarantines, cancellation of travel, disruptions to supply chains and customer activity, as well as general concern and uncertainty that present additional risks to financial markets.

Reliance on Key Personnel. Prospect's operations are substantially dependent upon the skill, judgment and expertise of Daniel Mendoza and the employees of the Firm. The death, disability, departure or other unavailability of any key personnel could have a material and adverse effect on the Funds, SMAs and the Firm.

Concentration of Investments. The Fund Documents and SMA agreements do not limit the amount of capital Prospect may commit to any single investment, industry or sector on behalf of the Funds or SMAs. While the Firm will attempt to spread capital among a number of investments, portfolios will not be as diversified as many other investment funds or accounts. Prospect generally will focus the Funds' and SMAs' investments on a relatively small number of positions, each representing a relatively large portion of the Funds' or SMAs' capital. Prospect will at times have a relatively large portion of the Funds' capital exposed to a particular industry or market sector. Losses in one or more large positions, or a downturn in an industry or market sector in which the Funds or SMAs are concentrated, could materially adversely affect the Funds' or SMAs' performance in a particular period and could have a materially adverse effect on the Funds' or SMAs' overall financial condition.

Timing of Gains and Losses; Volatility. Some of Prospect's investments on behalf of the Funds or SMAs may be positions the Funds or SMAs must hold for significant periods before the success or failure of the investment becomes apparent or any gains can be realized. It may take longer for successful investments to realize their potential than for unsuccessful ones to reveal their weaknesses. Market prices of portfolio positions may be expected to fluctuate significantly over the Funds' holding periods, causing the Funds' or SMAs' performance to be volatile over the short term.



Short Selling. Prospect can sell securities short as a regular part of investing activities and may do so to profit from declines in the prices of securities that are considered overvalued or to hedge long positions.

In a short sale, Prospect sells securities it does not own for the Funds' or SMAs' portfolio, in the expectation that the market price will decline, and the Funds or SMAs will be able to buy replacement securities later at a lower price. To accomplish this, Prospect would borrow the securities from a broker or other third party on behalf of the Funds or SMAs. Prospect would "close" the position by "returning" the security (buying a replacement security on the lender's behalf). This "return" obligation does not typically have a specified "maturity" date and the lender generally could require replacement of the securities whenever it chooses. A short sale theoretically involves the risk of unlimited loss: the price at which Prospect must buy "replacement" securities could increase without limit. The Funds or SMAs may experience losses on short positions that are not offset by gains on long positions. As collateral for its return obligation, Prospect must leave the proceeds of its short sales with the lender—generally, a Prime Broker or account custodian. Ordinarily, all the Funds' or SMAs' assets held by the Prime Broker or account custodian will serve as collateral not only for the Funds' or SMAs' short sale return obligation, but also for any other credit the Prime Broker or account custodian extends and any other obligations the Funds or SMAs owe the Prime Broker or account custodian. If the amount of the Funds' or SMAs' return obligation were to increase significantly due to increases in a short-sold security's price, or if the value of collateral were to decrease, the Funds or SMAs could be required to deliver additional cash or other collateral to the Prime Broker. But, if substantially all the Funds' or SMAs' assets were already serving as collateral, it is unlikely that the Funds would be able to meet such a demand, and the Prime Broker would likely cause the Funds or SMAs to "buy in" or "close" some or all of its short positions. Such a "buy-in" could well be at a time and on terms that are adverse to the Funds or SMAs. Less dramatically, market-driven increases in short-sale-related liabilities and reductions in collateral value could also reduce Prospect's ability to effect transactions or distribute cash to fund Limited Partner withdrawals in the Funds. Lenders such as the Prime Broker or account custodian have great discretion in their decisions regarding the adequacy of collateral, and the Funds' or SMAs' short selling activities and actions that depend on the availability of assets not being relied on for collateral (e.g., distributing cash) could be curtailed, potentially significantly and without notice.

Portfolio Leverage. Prospect can leverage the Funds' or SMAs' investment positions by borrowing funds from securities brokers or dealers, banks, or others. The Firm can also use derivatives to leverage the Funds' or SMAs' capital, as discussed below. Leverage increases both the possibilities for profit and the risk of loss. Borrowings are usually from securities brokers and dealers (primarily the Funds' Prime Broker or the SMAs' account custodian) and are typically secured by the Funds' or SMAs' securities and other assets. Under certain circumstances, such a broker or dealer can demand an increase in the collateral that secures the Funds' or SMAs' obligations, and if the Funds or SMAs' are unable to provide additional collateral, the broker or dealer could liquidate assets held in the Funds' or SMAs' account to satisfy the Funds' or SMAs' obligations. Liquidation in that manner could have extremely adverse consequences, including sales at disadvantageous times and prices and the acceleration of tax consequences.

Limited Liquidity of Some Investments. Some of Prospect's investments for the Funds or SMAs, while publicly traded, may be relatively illiquid. Illiquid positions are generally the result of a thinly traded security or because the Funds' or SMAs' position in a security is large in relation to the overall market for the security. Prospect may own securities in the Funds' or SMAs' accounts that are relatively liquid when acquired but become illiquid after we invest. Prospect may not be able to liquidate illiquid securities positions if the need were to arise; rapid sales of such securities could depress the market value of those securities, reducing the Funds' or SMAs' profits, or increasing its losses, in the positions. In limited circumstances, Prospect can cause the Funds or SMAs to acquire a security position that is not immediately saleable in the public markets. The Funds or SMAs generally would not do so unless Prospect believes the position would be so small that valuation or liquidity issues would not have a material impact on the Funds or SMAs and generally will not cause the Funds or SMAs to invest more than 10% of its net assets (measured at the time of investment) in such securities. The value assigned to illiquid securities (including thinly traded securities) and large blocks of securities for purposes of determining Partnership Percentages and determining Net Profit and Net Loss may differ from the value the Funds or SMAs are ultimately able to realize on those securities.

Leverage and Uncertainty in Portfolio Companies. Prospect's investments on the Funds' or SMAs' behalf may include portfolio companies whose structures include significant leverage. Leverage could increase the exposure of those companies to adverse economic factors, such as rising interest rates, downturns in the economy, or deteriorations in the companies' or their industries' condition. The investments can also include companies that are distressed or have experienced difficulties. Such investments present additional risks: the Funds or SMAs could lose its entire investment in a distressed company, could be required to accept cash or securities with a value less than the Funds' or SMAs' investment, and could be prohibited from exercising certain rights with respect to such investment. Such investments may not show any returns for a considerable period, and the markets for securities the Funds or SMAs own may be limited for extended periods or may disappear or fail to develop. Sales of securities held by the Funds may be dependent on the exercise of registration rights or the expiration of relevant securities law restrictions.

Hedging, Generally. Hedging strategies, in general, are usually intended to limit or reduce investment risk, but they can also be expected to involve transaction costs and may inherently limit or reduce the potential for profit. Hedges are often imperfectly inversely correlated with the underlying exposure that Prospect seeks to hedge and, to the extent that is the case, can subject the Funds or SMAs to additional risk if prices involved in the hedging position move against the Funds or SMAs. Prospect will not attempt to hedge all of the Funds' or SMAs investment positions.

Small Capitalization Stocks. Prospect expects to invest a significant portion of the Funds' or SMAs assets (either directly or through derivatives such as options) in stocks of companies with relatively small market capitalizations. While Prospect believes these stocks can provide significant potential for appreciation, they can involve higher risks than investments in stocks of larger companies. For example, prices of small-capitalization and even some medium-capitalization stocks are often more volatile than prices of large-

capitalization stocks, and the risk of bankruptcy or insolvency of many smaller companies (with the attendant losses to Investors) may be higher than for larger, “blue-chip” companies. In addition, thin trading in some small-capitalization stocks may make investments in those stocks less liquid.

Counterparty and Custody Risk. Financial institutions with which Prospect does business, including the Prime Brokers, account custodians or counterparties that hold the Funds’ or SMAs’ assets as collateral, could become insolvent. In particular, if a Prime Broker or account custodian were to declare bankruptcy or become insolvent, the Firm may not be able to recover all or a portion of assets held either permanently or for years.

Trade Error Risk. Trade errors include, for example, keystroke errors that occur when entering trades into an electronic trading system or typographical or drafting errors related to derivatives contracts or similar agreements. Given the possibility of human error, trade errors can occur, notwithstanding the execution of due care and special procedures designed to prevent such errors. If trading errors do occur, Prospect will not be responsible for gains or losses resulting from trade errors, except where such trade error is the result of the Prospect’s gross negligence, willful misconduct or fraud.

Cybersecurity Risks. Prospect and its service providers are subject to risks associated with a breach in cybersecurity. Cybersecurity is a generic term used to describe the technology, processes and practices designed to protect networks, systems, computers, programs and data from cyber-attacks and hacking by other computer users, and to avoid the resulting damage and disruption of hardware and software systems, loss or corruption of data, and/or misappropriation of confidential information. In general, cyber-attacks are deliberate, but unintentional events may have similar effects. Cyber-attacks may cause losses to Funds and SMAs by interfering with the processing of transactions, affecting Prospect’s ability to calculate net asset value or impeding or sabotaging trading. Funds and SMAs may also incur substantial costs as the result of a cybersecurity breach, including those associated with forensic analysis of the origin and scope of the breach, increased and upgraded cybersecurity, identity theft, unauthorized use of proprietary information, litigation, and the dissemination of confidential and proprietary information. Any such breach could expose Prospect to civil liability as well as regulatory inquiry and/or action. In addition, the Funds and SMAs could be exposed to additional losses as a result of unauthorized use of their personal information. While the Firm has established business continuity plans and systems designed to prevent cyber-attacks, there are inherent limitations in such plans and systems, including the possibility that certain risks have not been identified. Similar types of cybersecurity risks also are present for issuers of securities in which we invest, which could result in material adverse consequences for such issuers and may cause an investment in such securities to lose value.

Effect of Substantial Withdrawals. Substantial Limited Partner withdrawals from a Fund over a short period could require the Firm to liquidate securities positions more rapidly than would otherwise be desirable, possibly reducing the value of the Funds’ assets and/or disrupting Prospect’s investment strategy. Among other things, such a reduction could impair Prospect’s ability to take advantage of particular investment opportunities, and it

would decrease the ratio of the Funds' income to its expenses. In addition, withdrawals or redemptions by investors in other investment vehicles or accounts Prospect or an affiliate manages, some of which may have more advantageous information and/or liquidity rights than those provided to Fund investors, could adversely affect the value of the Funds' portfolio positions.

All investments involve different degrees of risk, including the risk that the entire investment may be lost. Investors should be aware of their risk tolerance level and financial situation at all times. Prospect cannot guarantee the successful performance of an investment and it is expressly prohibited from guaranteeing accounts against losses arising from market conditions.

The risks described above are not a complete list of risks involved with investing with Prospect – specific risks and conflicts of interest associated with an investment are described in full detail in the Fund Documents and other materials accompanying the Agreement. Investors, clients, and prospective clients and investors should carefully review the applicable documents for further information.

## **ITEM 9: DISCIPLINARY INFORMATION**

Registered investment advisers are required to disclose any material facts regarding certain legal or disciplinary actions that would be material to a Client or Investor's evaluation of the investment adviser and each investment adviser representative providing investment advice to you. Prospect has no disciplinary information of this type to report.

## **ITEM 10: OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS**

Prospect serves as the general partner and investment adviser to the Funds and certain SMAs. Prospect is not engaged to advise investors as to the appropriateness of investing in the Funds, and the Firm does not receive any compensation for doing so and the Firm does not receive any compensation for advising investors of the Funds or for selling interests in the Funds.

## **ITEM 11: CODE OF ETHICS, PARTICIPATION OR INTEREST IN CLIENT TRANSACTIONS AND PERSONAL TRADING**

### **Code of Ethics**

Prospect has adopted a set of enforceable guidelines ("Code of Ethics"), which describes unacceptable conduct by Prospect and our employees ("Supervised Persons"). Summarized, this Code of Ethics prohibits The Firm and its Supervised Persons from:

- Placing personal or Firm interests before client interests,
- Using nonpublic information for personal gain,
- Engaging in any act, practice, or course of business that is, or might be considered fraudulent, deceptive, manipulative, or in violation of any applicable law, rule, or regulation of a governmental agency.

Please contact Prospect if you would like to receive a full copy of this Code of Ethics.

### **Personal Trading for Supervised Persons**

Although Prospect's policies and procedures generally prohibit Supervised Persons from trading in single-name stocks, exceptions may be made by the Chief Compliance Officer in certain circumstances. Further, there may be circumstances in which a Supervised Person owns the same securities as those owned by a Fund or SMA. However, Prospect does not generally permit Supervised Persons to trade in the same securities owned by a Fund or SMA. Prospect's Supervised Persons can invest directly in the Funds if appropriate qualification standards are met.

Prospect addresses the potential for conflicts of interest in personal trading matters by requiring Supervised Persons to sign and adhere to the Code of Ethics and report personal securities holdings and transactions to the Firm.

## **ITEM 12: BROKERAGE PRACTICES**

### **Selection of Brokers**

In selecting brokers to execute portfolio transactions, Prospect makes a good faith judgment about which broker would be appropriate. Prospect takes into consideration not only the available prices and rates of brokerage commissions but also other relevant factors that may include (without limitation):

- Execution capabilities of the broker/dealer,
- research (including economic forecasts, investment strategy advice, fundamental and technical advice on individual securities, valuation advice, and market analysis),
- custodial and other services provided by the broker/dealer that are expected to enhance our general portfolio management capabilities,
- Size of the transaction,
- The difficulty of execution,
- Operational facilities of the broker/dealers involved,
- Risk in positioning a block of securities, and
- Quality of the overall brokerage and research services provided by the broker/dealer.
- Solvency of the broker/dealer

When a broker/dealer is selected for a transaction, Prospect may cause the Funds or SMAs to pay a higher commission for effecting a transaction than another broker/dealer would have charged for effecting that transaction. Prospect does this if it is determined in good faith that the amount of the commission is reasonable in relation to the value of the brokerage and research services provided by the broker/dealer. The determination is viewed in terms of either the particular transaction or Prospect's overall responsibilities with respect to the Funds and SMAs.

### **Aggregation of Orders**

There are occasions on which portfolio transactions will be executed as part of concurrent authorizations to purchase or sell the same security for the Funds or an SMA.

Prospect may choose to block (aggregate) trades for a Fund with those of another Fund and/or SMA. When a block trade is placed, all participants included in the block receive the same price per share on the trade. The price is calculated by averaging the price of all of the shares traded. Due to the averaging of price over all of the participating accounts, aggregated trades could be either advantageous or disadvantageous. Commission costs are not averaged. You will pay the same commission whether your trade is placed as part of a block or on an individual basis. The objective of the aggregated orders is to allocate the executions in a manner that is deemed equitable to the accounts involved.

Trades are typically allocated in a pari passu manner for all accounts in which Prospect acts as a general partner. If the trade is being allocated to an SMA, it is declared at the time the position is opened, when a broker is given an order to execute the trade.

It is possible that different brokers would be handling the same trade for the Funds and an SMA. In this case, it is possible that the SMA and the Funds could get different prices. These price differences are likely to be minor and balance out over time. Prospect has a fiduciary duty to all clients to exercise good faith and fairness in all dealings.

### **Soft Dollars**

#### General Information

Prospect has a fiduciary duty to the Funds and SMA clients managed by the Firm to obtain best execution, on an overall basis, for any securities transactions. When determining whether best execution has been achieved, Prospect relies on Section 28(e) of the Securities Exchange Act of 1934, as amended (the "Safe Harbor"). A safe harbor is a provision of a statute or a regulation that reduces or eliminates a party's liability on the grounds that the party performed its actions in good faith. Legislators include safe-harbor provisions to protect legitimate or excusable violations.

This Safe Harbor is provided to an investment adviser like Prospect that has "investment discretion" over Fund and SMAs. It provides protection against certain state and federal breach of fiduciary obligation claims (including ERISA claims) because the adviser caused a fund or client to pay more than the lowest available commission when executing a

securities trade in exchange for receiving investment research services and products which helped make investment decisions of benefit to the funds or clients. To rely on the Safe Harbor provision, Prospect must determine in good faith that the amount of the commissions paid is reasonable in relation to the value of the research services received. Prospect takes into account not only the costs for a specific transaction but also the Firm's overall responsibility to Funds and SMAs. When Prospect causes an account to pay more than the lowest available commission to a broker/dealer in return for research products and services, these payments are commonly referred to as "soft dollar" benefits. The broker/dealer tracks the soft dollar benefits generated to be used on the Firm's behalf. Not all trades generate soft dollar benefits, and Prospect tries to limit "soft dollar" trades whenever preferable.

For purposes of the Safe Harbor, "research services" means "advice," "analyses," and "reports" which meet the following criteria:

- The research is related to the market for securities, such as trade analytics (including analytics available through order management systems) and advice on market color and execution strategies; or
- The research constitutes market, financial, economic, or similar data.

For the purposes of the Safe Harbor, "brokerage services" are those products and services that relate to the execution of a trade from the point at which the investment manager communicates with the broker/dealer for the purpose of transmitting an order for execution, through the point at which funds or securities are delivered or credited to an account under our management.

See the section entitled "How We Use Soft Dollars" for additional details.

#### Prime Brokerage

Prospect obtains certain services for the Funds and SMAs, including custodial, recordkeeping, clearing, and related services, through what is known as a "prime brokerage" relationship. Under this relationship, a single brokerage firm that Prospect generally selects provides the following services:

- maintains custody of the Funds' or SMA's assets (either directly or through clearing firms),
- provides margin credit,
- locates securities to borrow to facilitate short sales, and
- provides related services but allows the Funds to use other brokers to execute transactions.

This relationship allows Prospect to seek valuable research and to compare execution quality and commission rates while maintaining only one custodial relationship. By using a brokerage firm, Prospect also may avoid paying custodial fees that banks charge other institutional investors. The prime broker receives interest on credit balances, margin borrowings, stock loans, and brokerage commissions as compensation.

Under this arrangement, the prime broker, among other things:

- Arranges for the delivery of securities bought, sold, borrowed, and lent,
- Makes and receives payments for securities,
- Maintains custody of cash and securities, and
- Provides detailed trading portfolio and related reports.

The Funds' and SMA's obligations to the prime broker (and its affiliates) may be secured by way of a first priority perfected security interest over all of the portfolio assets held in custody. The prime broker (and its affiliates) may transfer to themselves all rights, title, and interest in and to those assets as collateral and may deal with, lend, dispose of, pledge, or otherwise use all such collateral for their own purposes.

#### How We Use Soft Dollars

Prospect mainly uses soft dollars to purchase Alpha Sense, Bloomberg, services of certain expert networks, and research from sell-side brokerage firms. Each of these services are research services and fall within the Safe Harbor definitions described above.

#### Soft Dollar Procedures

A soft dollar account has been established at BTIG, and the soft dollar rate was established based on the projected cost of research services. BTIG maintains an account of accumulated soft dollars and uses that account to pay soft dollar invoices following their approval by Prospect.

A broker/dealer with whom Prospect has a soft dollar arrangement can establish "credits" relating to brokerage commissions paid in the past that may be used to pay or reimburse the broker/dealer for research or other specified expenses. In other cases, a broker/dealer can provide or pay for a service or product and suggest a higher "commission" level for future business to fully compensate the broker/dealer.

Prospect's actual transactional business with such a broker/dealer may be less than the suggested commission level but can-and likely will-exceed that level. This may be in part because the Firm's investment activities generate aggregate commissions in excess of the aggregate suggestions from all broker/dealers providing services and products. It may also be in part because those broker/dealers may also provide superior execution and may therefore be the most appropriate for particular transactions. Prospect will not exclude broker/dealers from transaction business simply because they have not provided research or other services.

Prospect believes the above procedures are consistent with the requirements of Safe Harbor to the extent the services we acquire otherwise qualify as research or brokerage services. Transactions effected on a principal basis, as most transactions with market-makers in over-the-counter securities are, with a markup or mark-down paid to the dealer, do not fall within the Safe Harbor.



## **Directed Brokerage**

Prospect selects brokers for the Funds in its sole discretion.

SMA clients can instruct the Firm to execute any or all securities transactions for the account with or through one or more broker/dealers as set forth in the associated Agreement. In these cases, the SMA client is responsible for negotiating the terms and conditions (including, but not limited to, commission rates) relating to all services to be provided by the broker/dealers, and the SMA client is satisfied with the terms and conditions. Prospect has no responsibility for obtaining the best prices or any particular commission rates for transactions with or through the broker/dealer in these situations. The SMA client recognizes that it may not obtain rates as low as it might otherwise obtain if Prospect had the discretion to select broker/dealers other than those set forth in the associated Agreement. If the SMA would like Prospect to cease executing transactions with or through the designated broker/dealer, the SME client must notify the Firm in writing.

## **ITEM 13: REVIEW OF ACCOUNTS**

Holdings are reviewed daily to ensure that the investment thesis is intact and that the position size is appropriate based on the Firm's view of the future reward/risk based on the current price. All reviews are performed by Daniel Mendoza, Managing Member.

Investors in the Funds receive monthly letters and monthly unaudited capital account statements. SMA clients will receive monthly letters.

## **ITEM 14: CLIENT REFERRALS AND OTHER COMPENSATION**

### **Economic Benefits Provided by Third Parties**

Prospect does not receive any economic benefit, directly or indirectly, from any third party for advice rendered to the Funds or SMAs.

### **Compensation to Non-Advisory Personnel for Client Referrals**

Currently, Prospect does not directly or indirectly compensate any person who is not advisory personnel for client referrals. If in the future Prospect enters into such arrangements, this brochure will be appropriately amended.

## **ITEM 15: CUSTODY**

As the general partner for the Funds, Prospect is deemed to have custody of the Funds' assets. Prospect has implemented the following procedures for the Funds:

- Any disbursements or allocations from the Funds require two signatures and are subject to a callback procedure; and
- The Funds are subject to an annual audit with the audited financial statements distributed to the Fund's investors within 120 days of their fiscal year-end.

If an SMA client provides Prospect authority to deduct fees directly from the SMA, Prospect is deemed to have custody of those assets. In order to avoid additional regulatory requirements in these cases, Prospect follows the procedures outlined in "Item 5: Fees and Compensation." SMA clients will also receive quarterly statements directly from the custodian of the account that details all transactions in the account.

In no case do we accept physical custody of client assets.

## **ITEM 16: INVESTMENT DISCRETION**

Prospect manages the Funds on a discretionary basis and does not allow for any limitations to be placed on our investment authority. Prospect's investment philosophy is summarized above and more completely described in the Fund Documents. In order to invest in the Funds, an investor must:

- Review the Fund Documents we provide. This Part 2A and the Part 2B for Daniel Mendoza are included with the Fund Documents.
- Sign a copy of the Limited Partnership Agreement for the Fund.
- Complete subscription documents and sign the Subscription Agreement for the Funds. These provide information about each investor's qualifications to invest in the Funds.

As one of the conditions of SMAs, a client is required to provide discretionary authority for Prospect to manage the SMA assets. Discretionary authority means that the SMA is giving Prospect a limited power of attorney to place trades on behalf of the SMA. This limited power of attorney does not allow Prospect to withdraw money from the SMA account other than advisory fees if such authority is set forth in the associated Agreement.

Discretionary authority is provided by completing the following items:

- Sign the Agreement, which provides a limited power of attorney for Prospect to place trades on behalf of the SMA. Any limitations to the trading authorization will be added to this Agreement.
- Provide Prospect with discretionary authority on the new account forms that are submitted to the broker/dealer acting as custodian for the SMA account(s).

All SMAs are managed using the investment strategy described in the "Methods of Analysis, Investment Strategies, and Risk of Loss" section above. Prospect generally does not allow Clients to limit investments it makes that fall within the parameters of the investment strategy described.

## **ITEM 17: VOTING CLIENT SECURITIES**

Prospect votes all proxies for the Funds that, in its reasonable judgment alone, determines to affect the value of the Funds. In so doing, Prospect generally casts proxy votes in favor of proposals that increase shareholder value and generally cast against proposals having the opposite effect. Mr. Mendoza is responsible for the Firm's decisions on proxy voting and verifies that the proxies are voted in a prudent and diligent fashion and only after a careful evaluation of the issue presented on the ballot. Fund investors may not provide direction regarding any particular proxy solicitation.

SMA clients can provide authorization for Prospect to vote proxies as described above for the SMA(s). SMA clients may elect to retain the authority to vote the proxies itself. If the SMA retains this authority, Prospect will provide guidance related to a specific proxy solicitation upon request.

Fund investors can request a copy of our Proxy Policies and Procedures and/or information about how a proxy was voted at any time.

## **ITEM 18: FINANCIAL INFORMATION**

Prospect does not charge or solicit pre-payment of more than \$1,200 in fees per Fund investors six months or more in advance. In addition, Prospect has not previously filed for bankruptcy and is not aware of any financial conditions that are reasonably likely to impair the Firm's ability to meet its contractual obligations to Funds and SMA clients.