

Form ADV Part 2A: Firm Brochure

Item 1 - Cover Page



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This brochure provides information about the qualifications and business practices of Shelter Growth Capital Partners LLC. If you have any questions about the contents of this brochure, please contact Jay Strauss at (203) 355-6113. 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.

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

Any reference to Shelter Growth Capital Partners LLC as a "registered investment adviser" or as being "registered" does not imply a certain level of skill or training.

**Item 2 - Material Changes**

The most recent annual amendment to this Form ADV Part 2A was last filed on March 30, 2023. The only notable changes contained in this annual amendment are found in Item 4 reflecting updated Regulatory Assets Under Management and Item 8 reflecting updated applicable risk disclosures.

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**Item 4 - Advisory Business**

- A. Shelter Growth Capital Partners LLC (“Advisor,” “SGCP,” “we” or “us”) is a Delaware limited liability company that was formed in November 2014 to provide investment advisory services. SGCP is owned by SGCP Holdco LLC, which is 49% owned by One Dock Partners, LP (“One Dock”). Dan Sparks, Kevin Gasvoda and Justin Mahoney control One Dock and control a majority of the Board of Managers of SGCP and SGCP Holdco LLC.
- B. SGCP pursues investment strategies on behalf of clients by seeking to provide attractive risk-adjusted returns through fundamental analysis and relative value investing primarily in the structured credit and fixed income markets. SGCP participates across markets that provide opportunities for clients to achieve their objectives including fixed income securities, loans, derivatives, equities, mortgage-related assets and other asset classes. SGCP may provide these services as advisor to private funds or separately managed accounts.
- C. SGCP manages investments for clients in accordance with the investment objectives outlined in each fund’s applicable governing documents. Fund investors may not impose restrictions on investing in certain securities or types of securities. Separately managed account clients may, however, negotiate certain restrictions regarding the types of investment instruments and the level of leverage permitted.

All discussions regarding separately managed accounts, fund clients or other clients within this brochure, including but not limited to their investments, the strategies used in managing such clients, the fees and other costs associated with an investment related to each client, and conflicts of interest faced by SGCP in connection with management of the clients, are qualified in their entirety by reference to each client’s respective offering memorandum, term sheet, or advisory agreement as applicable.

- D. SGCP does not participate in wrap fee programs.
- E. SGCP anticipates providing advisory services to various types of clients, including, but not limited to, hedge funds, private equity funds, foundations, financial institutions, pension plans, insurance companies, ERISA-compliant vehicles, high net worth persons (including their family offices), and charitable organizations.

As of December 31, 2023, SGCP managed \$2,818,259,607 in regulatory assets on a discretionary basis. SGCP does not manage assets on a non-discretionary basis.

**Item 5 - Fees and Compensation**

- A. Fees charged to fund clients of SGCP are detailed in the fund documents. In the case of separately managed account clients, fees are separately negotiated and described in the investment management agreement for each client, as applicable. In general, SGCP typically charges both management fees and incentive fees to clients.
- B. SGCP deducts management fees periodically in advance from the accounts of its fund clients. This process is more fully described in the fund documents for each fund client. Separately managed account fees are separately negotiated and are billed to, and payable by, each separately managed account client in arrears pursuant to the investment management agreement for each separately managed account. This process may vary from client to client.
- C. Certain specific operating expenses incurred by clients of SGCP may be paid by SGCP and reimbursed by clients or paid directly from the accounts of fund clients by a fund administrator. These fees and expenses are detailed in the fund documents for each fund client or investment management agreement for each separately managed account.

- D. Management fees that are paid in advance are generally not refundable, and management fees that are paid in arrears are paid through the date of termination.
- E. Neither SGCP nor any of its supervised persons accepts compensation for the sale of securities or other investment products.

Funds and accounts managed by SGCP periodically enter into transactions with its affiliates, SG Capital Partners LLC, ClearEdge Lending LLC, or another affiliate. SGCP-managed funds and accounts purchase residential mortgage and commercial real estate loans or other structured credit assets from SG Capital Partners LLC, ClearEdge Lending LLC or another affiliate from time to time for investment purposes. Each such transaction is a “principal transaction” for purposes of Section 206(3) of the Investment Advisers Act of 1940 (the “Advisers Act”). SGCP has adopted a policy to address these transactions that consists of a third-party valuation company valuing any assets transferred and a committee of individuals unaffiliated with SGCP and acting on behalf of SGCP clients reviewing and approving in writing in advance based on the valuation all transactions between funds or accounts managed by SGCP and its affiliates.

SGCP receives loan transaction servicing fees per loan in connection with funds and separately managed accounts that purchase residential mortgage loans.

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

SGCP charges performance-based fees to its clients. These performance-based fees are more fully described in the fund documents for each fund client or investment management agreement for each separately managed account. Separately managed account clients are not charged performance-based fees except on a case-by-case basis as negotiated between parties.

The performance-based fee arrangements vary from client to client. SGCP advises clients to whom SGCP or its affiliates charge performance-based fees at the same time that SGCP advises clients to whom SGCP does not charge performance-based fees. This creates the potential for conflict of interest with respect to trade allocation as SGCP may have an incentive to favor accounts that are charged higher performance fees. SGCP is committed to providing fair and equitable allocation of trades and investment opportunities among clients regardless of any fee disparity among clients. SGCP has adopted a trade allocation policy pursuant to which trade allocations are tested periodically by the CCO or his designee to ensure fair allocation of investment opportunities among clients.

#### **Item 7 - Types of Clients**

SGCP provides advice to funds in the form of pooled investment vehicles for institutional and high net worth investors. Private funds managed by SGCP have various minimum investment amounts as more fully described in the fund documents for each such private fund client.

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

- A. **Methods of Analysis, Investment Strategies:** SGCP seeks attractive risk-adjusted returns through fundamental analysis and relative value investing primarily in the structured credit and fixed income markets. SGCP participates across markets including fixed income securities, loans, mortgage-related assets, derivatives, equities and other asset classes. SGCP’s analysis of the structured credit and fixed income markets, the macro-economic environment and the general interest rate environment is conducted through a variety of means. SGCP subscribes to various publications and data services and has compiled its own detailed research database. SGCP’s analysis reflects the extensive experience of the investment team in conducting fundamental analysis and managing risk in the securities and loan markets, and the debt and equity markets generally, over a series of decades.

**Risks:** The following is a general summary of the potential risks related to the investments made by SGCP on behalf of clients. With respect to funds managed by SGCP, the information below is intended to be a general summary of risks that is supplemented and superseded in all respects by each fund's applicable governing documents. SGCP may offer advisory services, engage in an investment strategy, and make any investment, including any not described in this brochure, that SGCP deems appropriate, subject to each client's investment objectives and guidelines. Potential investors should review the governing documents in their entirety and consult their own legal, tax, and/or financial advisers before investing with SGCP. This information may be both supplemented and superseded by information in each client's governing documents.

- B. Due to the risks inherent in the investment strategy pursued by SGCP on behalf of clients, investments managed by SGCP are not suitable for all investors and can result in losses including the risk of loss of principal. No assurance can be made that profits will be achieved or that substantial or complete losses will not be incurred. Past investment results generated by SGCP or its affiliates are not necessarily indicative of future performance.

#### **Credit Risk**

Credit risks include the risk that an investment is not paid in full and or the risk that payments are not made on time. Defaults by borrowers can impair the ability of a particular loan or security to make its payments as scheduled. SGCP attempts to manage credit risk through credit analysis, loan and security selection and, in some circumstances, the use of credit risk hedging techniques including the purchase of derivatives, indices and options on indices and securities. There can be no guarantee that these techniques will successfully mitigate the credit risks associated with investing in credit instruments. In addition, derivatives dependent upon credit events are priced incorporating many variables including the pricing and volatility of the underlying instruments, potential loss upon default and many factors which may not be easily quantified by market participants.

#### **Non-Investment Grade Securities**

SGCP may invest in non-investment grade instruments on behalf of clients. These instruments may represent opportunities for SGCP to increase investment returns on behalf of clients. However, the lack of an investment grade rating presents different and additional risks to investors, including reduced liquidity. SGCP will manage the risk of these investments through credit analysis, loan and security selection and hedging techniques. There can be no guarantee that these techniques will be successful.

#### **Concentration Risk**

SGCP may invest in markets or regions in a concentrated way that results in additional risk for investors. SGCP may look to mitigate certain concentrations if it is consistent with the relevant objectives of the fund and if such diversification of risk can be achieved economically.

#### **Market Price Volatility**

Investment values will fluctuate in price due to a number of factors including movements in interest rates and credit spreads. The market price of assets held on behalf of clients may vary significantly during volatile market conditions. SGCP may employ hedging strategies in an attempt to mitigate this risk; however, there can be no guarantee that any hedging strategy employed by SGCP will be successful.

#### **Liquidity Risk**

Many of the investments that SGCP plans to hold on behalf of clients trade in the over the counter markets. These over-the-counter instruments may be difficult to sell at favorable prices during certain market conditions due to lack of liquidity. SGCP will attempt to manage liquidity risk through loan and security selection, maintaining a large number of counterparty relationships, pursuing hedging activities, and attempting to secure financing terms and maturities that are consistent with the liquidity of assets, however, there is no guarantee that these strategies will be successful. Furthermore, due to the potentially limited

number of counterparties in the marketplace for certain over-the-counter instruments, there is no guarantee that SGCP will be able to find a suitable counterparty when necessary in order to obtain liquidity. Furthermore, SGCP may be required to sell certain instruments on unfavorable terms due to unanticipated market conditions. Occasions may arise whereby previously liquid investments have rapidly become illiquid.

**Investor Withdrawal Limitations**

Investors may be subject to certain withdrawal limits detailed in the fund documents, which may limit the amount of funds that an investor can withdraw at any given redemption date. Although investors in open-end funds managed by SGCP may request redemption of their interests on specified redemption dates, withdrawals of greater than 25% of invested capital are satisfied over successive withdrawal dates as set forth in the fund documents. The withdrawal limitations imposed by SGCP have the effect of limiting liquidity for investors.

**Leverage**

SGCP may use leverage in funds and client accounts for any one of a number of reasons, including enhancement of returns, and meeting withdrawals that might otherwise result in premature liquidation of investments at a loss. The use of leverage can magnify the effect of any increase or decrease in the market price of assets and thereby increase volatility.

**Financing**

Investments made by SGCP may be financed. Risks in relation to financing include that financing for these instruments will not be available when it is needed to fund existing levered assets or new purchases and that the term of financing may be such that SGCP will be unable to refinance at financing roll dates or have to refinance at unknown rates in the future. SGCP may attempt to mitigate this risk by diversifying financing across multiple counterparties, staggering financing maturities and, when possible, terming out financing to match the anticipated length of the investment, but there is no guarantee that these strategies will be successful.

**Counterparty Risk**

Trading strategies employed by SGCP may involve certain financial exposures to counterparties including but not limited to margin deposits, unsettled trades and mark to market exposure. SGCP will attempt to mitigate counterparty risk by rigorous counterparty selection, counterparty exposure analysis and diversity by number and type of counterparty. There can be no assurance that this process will reduce counterparty risk.

**Geopolitical Risk**

An unstable geopolitical climate and continued threats of terrorism could have a material adverse effect on general economic conditions, market conditions and market liquidity. For example, the United States and governments globally have seen a rise in populist and nationalist tendencies, with political parties espousing such themes gaining strength in local and national elections. In addition, geopolitical tensions, including the conflict between Russia and Ukraine, the attack on Israel by Hamas, the effects of which have destabilized the region, and rising tensions between the United States and China, and the impact of long term financial and economic sanctions, could lead to uncertainty, disruption, and volatility in global markets and industries that could negatively impact SGCP. Moreover, certain current events and resulting movements (including protests) have caused social unrest in the United States and in other parts of the world. At times, such movements have been accompanied by violence and looting which has seen certain businesses suffer physical damage and economic loss. In addition, such movements have seen certain businesses become subject to adverse publicity and heightened scrutiny as a result of historical action or inaction. To the extent that SGCP invests in companies that are impacted by such social unrest, physical damage and economic loss or the threat thereof (e.g., in the retail sector), there could be a material adverse impact on SGCP and its investments.

As of the date of this brochure, Russian forces continue to attack Ukraine, and it is uncertain how or when the war in Ukraine will end, or if it will broaden to areas beyond the Ukrainian border. As a result of the war, the United States and Western European countries, among others, have imposed economic sanctions on Russia, which are having an impact on the rate of inflation here and abroad. It is possible additional economic sanctions will be imposed, or that the nature of the war will change or expand to additional territories; as a result, it is impossible to predict their impact on the U.S. and the global economies, or their markets, and whether they could have a deleterious effect on investments chosen by SGCP for its clients.

SGCP could also be materially affected by Hamas' attack on Israel and Israel's counterattack into Gaza. The conflict has created tensions throughout the region which could expand creating a global crisis which has already increased U.S. military involvement. There have been over one hundred attacks on U.S. bases in the region, which has resulted in the death of three U.S. service members. Subsequently, there have been over one hundred air strikes by the U.S. against various terrorist organizations. Since the conflict began, various terrorist organizations have started attacking international shipping in the Red Sea, especially at the Bab el-Mandeb Strait which connects the Red Sea to the Gulf of Aden. Twelve percent of the oil and eight percent of the liquefied natural gas seaborne trade passes through the strait. The attacks on shipping are already causing some major oil and natural gas carriers to forgo the strait and take the longer trip around Africa which adds expense and delays. Such geopolitical tensions could create disruptions in the global supply chain and the global and U.S. economies which could negatively impact SGCP.

### **General Economic and Market Conditions**

General economic and capital market conditions may affect the investments made by SGCP. Interest rates, availability of credit, credit defaults, inflation rates, economic uncertainty, changes in laws (including laws relating to taxation of investments), trade barriers, currency exchange controls, national and international political circumstances (including wars, terrorist acts or security operations), the price of investments and participation by other investors in the financial markets may also affect the value of investments. Clients should realize that distributions may not be made by funds or accounts managed by SGCP due to general economic conditions, conditions in the credit markets, the illiquidity of investments, constraints imposed by financing arrangements, contractual prohibitions, inability to dispose of investments at attractive prices due to buyers' inability to secure financing or other reasons mentioned below. General fluctuations in the market prices of securities may adversely affect the value of investments and/or the ability to dispose of investments at attractive valuations. SGCP may be unsuccessful in structuring its investments to minimize any detrimental impact that a recession may have on its investments and as a result the funds or accounts managed by SGCP may suffer losses.

Market uncertainty may have a significant impact on SGCP's business. Among other things, the overall availability of investment opportunities may decline from SGCP's current expectations. One possible consequence is that SGCP may take a longer than anticipated period to invest capital. In addition, the slowdown in the global economy and changes in the prices of oil and gas, raw materials, and agricultural commodities may affect inflation rates and currency exchange rates, which may in turn have a negative impact on SGCP's investments.

### **Governmental Interventions**

Extreme volatility and illiquidity in markets has in the past led to, and may in the future lead to, extensive governmental interventions in equity, credit and currency markets. Generally, such interventions are intended to reduce volatility and precipitous drops in value. In certain cases, governments have intervened on an "emergency" basis, suddenly and substantially eliminating market participants' ability to continue to implement certain strategies or manage the risk of their outstanding positions. In addition, these interventions have typically been unclear in scope and application, resulting in uncertainty. It is impossible to predict when



these restrictions will be imposed, what the interim or permanent restrictions will be and/or the effect of such restrictions on the SGCP's strategies.

**Credit Ratings**

In general, the credit rating assigned by a nationally recognized rating agency to a security represents such rating agency's opinion of the safety of the principal and interest payments of the rated instrument based on available information. Such ratings are relative and subjective; they are not absolute standards of quality and do not evaluate the market value risk of such securities. Such ratings also do not reflect macroeconomic or systemic risk, including the risk of increased illiquidity in the credit markets. Rating agencies rate debt securities based upon their assessment of the likelihood of receipt of principal and interest payments. Rating agencies do not consider the risks of fluctuations in market value or other factors that may influence the value of debt securities and, therefore, the assigned credit rating may not fully reflect the true risks of an investment in the securities. Further, credit ratings may change over time due to various factors, including changes in the creditworthiness of the issuer and/or changes in the rating agency's analytics and processes. These changes may occur quickly and often. The rating agencies rating the securities may change their ratings criteria after issuance and any changes in ratings criteria may adversely affect the ratings assigned to the securities. There can be no assurance that the assigning rating agencies will not downgrade the securities or that any other rating agency will not assign ratings to the securities that are lower than those assigned by any rating agency requested to assign ratings to the securities. It is also possible that a rating agency might not change its rating of a particular issue on a timely basis to reflect subsequent events and, as a result, outstanding ratings may not reflect the issuer's current credit standing. SGCP clients may incur losses if it makes investments based on credit ratings that subsequently change in a way not favorable to client investment objectives.

**Prepayment Risk**

SGCP invests in certain mortgage loans, mortgage-backed securities, and asset-backed securities that generally provide for the payment of interest or principal (or both) on the instruments on a frequent basis. There exists the possibility, particularly with respect to residential mortgage-backed instruments, that principal may be prepaid at any time. As a result of prepayments, SGCP may be forced to reinvest assets at an inopportune time, which may expose the funds to a lower rate of return than anticipated. The rate of prepayments on underlying assets affects the price and volatility of an asset-backed security and may have the effect of shortening or extending the effective maturity beyond what was anticipated. Various types of asset-backed securities are subject to varying degrees of prepayment risk.

**Risks Relating to the Operations of Funds**

SGCP implements and develops appropriate systems for the fund's activities that rely heavily on a daily basis on financial, accounting and other data processing systems to execute, clear and settle transactions across numerous and diverse markets and to evaluate certain securities, to monitor portfolios and capital, and to generate risk management and other reports that are critical to oversight of client activities. This may require reliance on third-party systems, and SGCP may not be in a position to verify the risks or reliability of such third-party systems. Failures in the systems employed by SGCP including prime brokers (if any), administrators, counterparties, exchanges and similar clearance and settlement facilities and other parties could result in mistakes made in the confirmation or settlement of transactions or in transactions not being properly booked, evaluated or accounted for. Failures to such systems or disruptions could have material adverse effects on clients and any underlying investments.

**Cybersecurity Risks**

As part of its business, the Advisor processes, stores and transmits large amounts of electronic information, including information relating to the transactions of funds or accounts managed by the Advisor and personally identifiable information of investors. Similarly, service providers of the Advisor or funds or accounts managed by the Advisor, especially the Administrator, may process, store and transmit such information. The Advisor

has procedures and systems in place to protect such information and prevent data loss and security breaches. However, such measures cannot provide absolute security. The loss or improper access to, use or disclosure of the proprietary information maintained by SGCP may cause SGCP or its clients to suffer, among other things, financial loss, the disruption of its business, liability to third parties, regulatory intervention or reputational damage. Any of the foregoing events could have a material adverse effect on SGCP and client investments.

**Valuation Risk**

Client assets and liabilities are valued in accordance with SGCP's Valuation Policy. The valuation of any asset or liability involves inherent uncertainty. The value of a security determined in accordance with the Valuation Policy may differ materially from the value that could have been realized in an actual sale or transfer for a variety of reasons, including the timing of the transaction and liquidity in the market. Uncertainties as to the valuation of portfolio positions could have an impact on the net asset value of client assets if the judgment of SGCP, or our affiliates, as general partner or investment advisers to a client, regarding the appropriate valuation should prove to be incorrect.

**Epidemics; Pandemics**

There was an outbreak of a novel and highly contagious form of coronavirus ("COVID-19"), which spread throughout the world beginning in 2020. In the future, there are likely to be other epidemics and possibly pandemics. The outbreak of COVID-19 led to significant uncertainty, breakdowns, delays and other disruptions in the global financial markets and the economies of nations worldwide. COVID-19 also led to certain governmental interventions that were implemented suddenly and on an emergency basis. This outbreak of COVID-19, or any future epidemic or pandemic, could adversely affect the ability of funds or accounts managed by SGCP to fulfill their investment objectives, and could materially result in significant losses to such funds or accounts.

**Force Majeure**

SGCP may be affected by force majeure events (i.e., events beyond the control of the party claiming that the event has occurred, including, without limitation, acts of God, fire, flood, earthquakes, outbreaks of an infectious disease, pandemic or any other serious public health concern, war, terrorism, labor strikes, major plant breakdowns, pipeline or electricity line ruptures, failure of technology, defective design and construction, accidents, demographic changes, government macroeconomic policies, social instability, etc.). Some force majeure events may adversely affect the ability of a party to perform its obligations until it is able to remedy the force majeure event. These risks could, among other effects, adversely impact the cash flows for an investment, cause personal injury or loss of life, damage property, or instigate disruptions of service. In addition, the cost to SGCP or a client of repairing or replacing damaged assets resulting from such force majeure event could be considerable. Force majeure events that are incapable of or are too costly to cure may have a permanent adverse effect on an investment. Certain force majeure events (such as war or an outbreak of an infectious disease) could have a broader negative impact on the world economy and international business activity generally, or in any of the countries in which SGCP may invest specifically. Additionally, a major governmental intervention into industry, including the nationalization of an industry or the assertion of control over one or more investments, could result in a loss to clients, including if the investment is canceled or unwound. Any of the foregoing may therefore adversely affect the performance of a client.

**Institutional Risk and Custodial Risks**

SGCP may be subject to the risk of bank failure and the inability of, or refusal by, a bank to perform. The institutions, including brokerage firms and banks, with which a fund or client (directly or indirectly) does business, or to which securities have been entrusted for custodial and prime brokerage purposes, may encounter financial difficulties that impair the operational capabilities or the capital position of the client. Banking institutions are subject to liquidity, solvency, and similar required capital requirements that if not met

pose a risk to financial markets. Where such institutions experience systematic failure, such as rapid deposit reductions (a "Run on the Bank") institutions such as the Federal Deposit Insurance Corp ("FDIC") may not be able to insure assets held in excess of the FDIC insured limits (\$250,000), if at all. Any such default would deprive the clients of profit potential, hedging opportunity, or force the portfolio to cover their commitments for resale, if any, at the current market price, and could result in a loss.

Events involving limited liquidity, defaults, non-performance or other adverse developments that affect financial institutions or the financial services industry generally, or concerns or rumors about any events of these kinds, have in the past and may in the future lead to market-wide liquidity problems. For example, on March 10, 2023, Silicon Valley Bank ("SVB") was closed by the California Department of Financial Protection and Innovation, which appointed the FDIC as receiver. Despite subsequent actions taken by the U.S. Department of the Treasury, the U.S. Federal Reserve and the FDIC to ensure that all depositors of SVB had access to all of their cash deposits following the closure of SVB, uncertainty and liquidity concerns in the broader financial services industry remain.

SGCP regularly maintains cash balances at banks or other custodians in excess of the FDIC insurance limit. Each of these parties' access to cash in amounts adequate to pay expenses, purchase new investments and otherwise operate its business could be significantly impaired by the financial institutions with which it maintains cash balances to the extent such financial institutions face liquidity constraints or failures. In addition, investor concerns regarding the U.S. or international financial systems may increase the risk of default of particular investments, negatively impact market value, increase market volatility and cause credit spreads to widen and reduce liquidity, all of which could have a material adverse effect on the performance of the SGCP's investments, returns and the ability of SGCP to make and/or dispose of investments. No assurance can be given as to the effect of these events on the value of, or markets for, investments, or SGCP's ability to recover therefrom. In addition, while it is not always possible to predict the extent of the impact that the failure of any financial institution or the high market volatility and instability of the banking sector could have on economic activity and SGCP in particular, the failure of other banks and financial institutions and the measures taken by governments, businesses and other organizations in response to these events could adversely impact SGCP and its investments.

- C. The following risks are associated with the types of securities recommended by SGCP:

**Residential Mortgage-Backed Securities and Residential Mortgage Loans**

Holders of Residential Mortgage-Backed Securities ("RMBS") and residential mortgage loans bear various risks, including credit, market, interest rate, structural, regulatory and legal risks. RMBS represent interests in pools of one to four family residential mortgage loans. Such loans may be prepaid at any time. Residential mortgage loans are obligations of the borrowers thereunder only and are not typically insured or guaranteed by any other person or entity, although such loans may be securitized by government agencies in which case the securities issued are guaranteed or partially guaranteed. The rate of defaults and losses on residential mortgage loans will be affected by a number of factors, including general economic conditions and those in the geographic area where the mortgaged property is located, the terms of the mortgage loan, the borrower's "equity" in the mortgaged property and the financial circumstances of the borrower. If a residential mortgage loan is in default, foreclosure of such residential mortgage loan may be a lengthy and difficult process and may involve significant expenses. Furthermore, the market for defaulted residential mortgage loans or foreclosed properties may be very limited.

**Non-QM Loans**

For a significant portion of consumer residential mortgage loans, rulemaking pursuant to the Dodd-Frank Act, which amended the federal Truth-in-Lending Act ("TILA") and specified the "ability to repay" ATR Rules ("ATR Rules"), requires that lenders make a reasonable, good-faith determination that a mortgagor has an ability to

repay the loan as determined by the following eight (8) underwriting factors: (i) current or reasonably expected income or assets (other than the value of the property that secures the loan) that the mortgagor will rely on to repay the loan, (ii) current employment status (if the originator relies on employment income when assessing the mortgagor's ability to repay), (iii) monthly mortgage payment for the loan, (iv) monthly payment on any simultaneous loans secured by the same property, (v) monthly payments for property taxes and required insurance, and certain other costs related to the property such as homeowners association fees or ground rent, (vi) debts, alimony, and child-support obligations, (vii) monthly debt-to-income ratio or residual income, calculated using the total of all of the mortgage and non-mortgage obligations listed above, as a ratio of gross monthly income and (viii) credit history. The ATR Rules were implemented by a final rulemaking issued by the US Consumer Financial Protection Bureau (the "CFPB") that created new sections of Regulation Z, TILA's implementing regulation, and which became effective for mortgage loans for which the application was taken on or after January 10, 2014.

The ATR Rules are enforceable by the CFPB through its administrative enforcement authority and by mortgagors through a private right of action against lenders or as a defense to foreclosure. Recoverable damages can include: (i) special statutory damages equal to the sum of all finance charges, points and fees paid by the mortgagor (capped at three (3) years of finance charges, points and fees) unless the lender demonstrates that the failure to comply was immaterial; (ii) actual damages; (iii) statutory damages in an individual action or class action, up to a certain threshold; and (iv) court costs and attorneys' fees. A mortgagor must, however, bring such an action within three (3) years of such alleged violation or such private right of action is extinguished. A mortgagor may also assert a violation of the ATR Rules in a foreclosure proceeding at any time following origination of the mortgage loan "as a matter of defense by recoupment or setoff," but this right cannot bar foreclosure. The special statutory damages available for a violation of the ATR Rules can be up to three years of the sum of all finance charges, points and fees paid by the consumer. The likelihood of actual damages, which are uncapped, being awarded in an ATR claim is still unclear. While actual damages have been historically difficult to prove under TILA given that TILA is primarily a disclosure statute, the ATR Rules are more substantive in nature and may give rise to more frequent awards of actual damages. If a mortgagor of a mortgage loan asserts a defense to foreclosure due to a violation of the ATR Rules, fund owning the mortgage loan may incur liability if the mortgage loan does not satisfy the requirements for a Qualified Mortgage (as defined below). If a court of competent jurisdiction found a violation of ATR Rules, the foreclosure would proceed but the amount of the debt could be reduced by the recoverable damages set forth above. These claims may result in delays in foreclosure and additional costs may be incurred in connection with such claims, even if any such claims by the related mortgagor were not successful, which may increase the severity of losses on any such mortgage loan. Such claims may be more likely in judicial foreclosure jurisdictions than in non-judicial foreclosure jurisdictions where there may be higher costs associated with a mortgagor making such claims, and it may be more likely that such claims are made in such jurisdictions since any such mortgagor would already be exposed to the judicial system to process the foreclosure.

In connection with the establishment of the ATR Rules, the CFPB created enhanced legal protection for originators if they originate a loan to a more restrictive credit standard than just determining a mortgagor's ability to repay. These regulations (as amended from time to time, the "Qualified Mortgage Rule"), which became effective in January 2014, specified the characteristics of a Qualified Mortgage and two levels of presumption of compliance with the ATR Rules, a safe harbor (applicable to "Safe Harbor Qualified Mortgages") and a rebuttable presumption of compliance for higher priced loans (applicable to "Rebuttable Presumption Qualified Mortgages"). Under the initial version of the Qualified Mortgage Rule, a "Qualified Mortgage" was required to meet each of the following criteria: (1) terms of the mortgage loan must not include any negative amortization, interest only payments or balloon payments other than certain limited circumstances, (2) the loan term cannot exceed thirty (30) years, (3) the lender must verify mortgagor income, (4) points and fees paid by the mortgagor cannot exceed certain ceilings based on the applicable loan amount

(3% of the total loan amount in most cases), (5) the lender must calculate monthly payments based on the highest monthly payments required any time during the first five years of the loan and the total "back end" debt-to-income ratio cannot exceed 43% and (6) the verification of income and assets and determination of the debt-to-income-ratio must be in accordance with the "Standards for Determining Monthly Debt and Income" of the ATR Rules ("Appendix Q") (although both Appendix Q and the 43% debt-to-income ratio threshold were replaced with loan pricing thresholds by the General QM Final Rule as described below). In addition, mortgage loans eligible for purchase, guarantee or insurance by certain governmental agencies or government-sponsored enterprises ("GSEs"), including Fannie Mae and Freddie Mac, as applicable, constituted qualified mortgages under the Qualified Mortgage Rule, although such mortgage loans are not required to meet certain requirements that are otherwise applicable under the Qualified Mortgage Rule (the "QM Patch"). As further described below, the QM Patch ceased to apply for mortgage loans acquired by a GSE after August 31, 2021 with application dates on or after July 1, 2021.

In connection with the establishment of the ATR Rules, the CFPB included a "safe harbor" for a covered transaction that meets the definition of Qualified Mortgage and that is not a "higher-priced covered transaction." For any covered transaction that meets the definition of a Qualified Mortgage and is not a "higher-priced covered transaction," the creditor or assignee will be deemed to have complied with the ability-to-repay requirement (i.e., will be conclusively presumed to have made a good faith and reasonable determination of the consumer's ability to repay), although the mortgagor could still subsequently contend that the covered transaction did not actually meet the criteria for a Qualified Mortgage.

The rebuttable presumption means that a lender who has complied with the requirements for a Qualified Mortgage, but whose loan is higher-priced in excess of certain thresholds, is presumed to have complied with the ATR Rules. A mortgagor can rebut that presumption by raising specific facts that demonstrate that, based on information that the lender was aware of at the time of origination, the mortgagor's income, debt obligations, alimony, child support, and monthly mortgage payment and mortgage-related obligations left insufficient residual income or assets (other than the value of the secured real property) to meet living expenses, including any recurring and material non-debt obligations that the creditor was aware of at the time of origination. With respect to the presumption of compliance for higher-priced loans, the CFPB noted in the final rule that the longer a mortgagor has made timely payments on its fixed rate mortgage loan following consummation (or for an adjustable rate loan, the longer the timely payments after recast), the less likely the mortgagor will be able to rebut the presumption of compliance. Claims by mortgagors of violations of the ATR Rules may result in issues and delays in foreclosure, and additional costs may be incurred in connection with challenging such claims, even if a mortgagor's claim is not successful, which may increase the severity of losses on any such mortgage loan.

On December 10, 2020, the CFPB published two final rules, each effective as of March 1, 2021, that amended the Qualified Mortgage Rule. The first rule, which had a mandatory compliance date of October 1, 2022, amended the Qualified Mortgage Rule by removing the 43% debt-to-income ratio threshold and replacing it with a price-based test which limits the amount by which the annual percentage rate of a mortgage loan may exceed the average prime offer rate (the "General QM Final Rule"). Under the General QM Final Rule, the CFPB adopted a set of "bright-line" loan pricing thresholds to replace the previous 43% debt-to-income threshold calculated in accordance with Appendix Q. For most first-lien residential mortgages, a loan will not constitute a Qualified Mortgage if its annual percentage rate exceeds the average prime offer rate by 2.25 percentage points or more (higher thresholds would apply for loans with smaller loan amounts and for subordinate-lien transactions). The General QM Final Rule preserved the threshold separating Safe Harbor Qualified Mortgages from Rebuttable Presumption Qualified Mortgages. Accordingly, a mortgage loan that otherwise meets the general Qualified Mortgage definition would be a Safe Harbor Qualified Mortgage if its annual percentage rate exceeds the average prime offer rate for a comparable transaction by less than 1.5 percentage points (for first-lien transactions); all other Qualified Mortgage loans (those with a rate spread at

or above 1.5 but less than 2.25 percentage points) would be considered Rebuttable Presumption Qualified Mortgages. In addition to replacing the 43% debt-to-income threshold, the General QM Final Rule removes Appendix Q. However, lenders are still required to consider and verify a consumer's income or assets, debt obligations, alimony, child support and consider debt-to-income ratio or residual income when making a Qualified Mortgage, subject to less prescriptive standards than those set forth in Appendix Q. To address the potential uncertainty that may result from the removal of Appendix Q, the General QM Final Rule also provides for a safe harbor for the verification requirement if creditors comply with the standards identified in certain third-party manuals, such as the GSE guidelines.

In addition, after the mandatory compliance date of October 1, 2022, the General QM Final Rule phased out and removed the QM Patch. For loans for which the lender received an application on or after the March 1, 2021 effective date but prior to October 1, 2022, lenders had the option of complying with the terms of the General QM Final Rule or the Qualified Mortgage Rule as it existed prior to the March 1, 2021. However, on April 8, 2021 and May 26, 2021, each of the GSEs released a lender letter/bulletin requiring that any loan that has an application date on or after July 1, 2021 and is acquired by one of the GSEs after August 31, 2021 meet the Qualified Mortgage Rule (as amended by the General QM Final Rule), which meant that the QM Patch effectively ceased to apply for GSE-eligible loans, notwithstanding the later mandatory compliance date of the General QM Final Rule.

The second rule (the "Seasoned QM Rule") created a new category of Qualified Mortgages known as "Seasoned Qualified Mortgages." Under the Seasoned QM Rule, a residential mortgage loan constitutes a Seasoned Qualified Mortgage and is entitled to a safe harbor if the mortgage loan, among other things, satisfies certain underwriting requirements, is held in portfolio by the originating lender or first purchaser (so long as such purchase is not in connection with a securitization) until the end of the applicable seasoning period and has no more than two delinquencies of 30 or more days and no delinquencies of 60 or more days at the end of the applicable seasoning period (which will be at least 36 months from the date on which the first periodic payment is due). Seasoned Qualified Mortgages are also required to be secured by a first lien, have a fixed interest rate, not allow for negative amortization, not have a balloon payment and comply with the points and fees limits of the Qualified Mortgage Rule.

On February 23, 2021, the CFPB issued a statement indicating: (i) that the agency will consider at a later date whether to initiate another rulemaking in order to reconsider other aspects of the General QM Final Rule; and (ii) that the agency is considering whether to initiate a rulemaking to revisit the Seasoned QM Rule, and that any potential rulemaking that amends or revokes the Seasoned QM Rule could affect transactions for which an application was received during the period from March 1, 2021 until the effective date of such final rule.

On June 17, 2022, the CFPB stated that it is reviewing the Qualified Mortgage Rule to explore ways to encourage streamlined modification and refinancing in the mortgage market, as well as assessing aspects of the Seasoned QM Rule. On September 22, 2022, the CFPB indicated that it would reconsider certain aspects of the ATR Rules, in that the agency issued a Request for Information regarding mortgage refinances and forbearances. At this time, however, there can be no assurance whether or when there will be subsequent amendments to the Qualified Mortgage Rule and, if there are, what impact they will have on mortgage loans subject to the ATR Rules, given the ability of Congress to repeal certain regulations pursuant to the Congressional Review Act and the change in directorship at the CFPB.

Funds or accounts managed by SGCP will purchase certain types of mortgage loans and related RMBS, such as interest-only loans, negative-amortization loans certain types of balloon loans, loans not underwritten in compliance with Appendix Q, as well as loans with a debt-to-income ratio exceeding 43% (although both Appendix Q and the 43% debt-to-income ratio threshold were replaced with loan pricing thresholds under the General QM Final Rule described above) or points and fees exceeding 3% of the original loan amount, that do

not qualify for these enhanced protections from legal liability ("Non-QM Loans"). Non-QM Loans are not expected to have the benefit of either a safe harbor from liability under the ATR Rules or a rebuttable presumption of compliance with the ATR Rules. The CFPB's rules may result in a reduction in the availability of these types of loans and may adversely affect the ability of mortgagors to refinance certain of their loans.

Non-QM Loans are subject to the potential for increased challenges in the ATR analysis used in qualifying a mortgagor. Even if the mortgagor does not succeed in the challenge, additional costs may be incurred in connection with challenging and defending such claims. These mortgagor claims may be more likely and more costly in judicial foreclosure jurisdictions than in non-judicial foreclosure jurisdictions, and there may be more of a likelihood such claims are made since the mortgagor is already exposed to the judicial system to process the foreclosure.

The inclusion of these Non-QM Loans in RMBS purchased by the funds or accounts managed by SGCP may adversely affect the value of the RMBS relative to mortgage-backed securities that are backed only by Qualified Mortgages.

Importantly, there is little, if any, established case law as of yet with respect to both: (i) the substance of the ATR Rules, analyzing the consumer's ability to repay and the weight and mechanics given to the rebuttable presumption of compliance, as well as (ii) the damages provisions of the ATR Rules and how they will be determined and allocated by a court. The lack of judicial precedent regarding the ATR Rules and potential claims increases the risk with respect to Non-QM Loans.

Various state and local jurisdictions may adopt similar or more onerous provisions in the future. SGCP is unable to predict how these laws and regulations relating to assignee liability may affect the performance of the funds and accounts it manages.

#### **Investor Loans and Second Homes**

Funds or accounts managed by SGCP may purchase mortgage loans or related RMBS secured by residential properties that are not occupied by their owners ("Investor Loans") or secured by second homes. An investor property is a property which, at the time of origination, the mortgagor represented would not be owner-occupied or used as a second home. Second homes are typically used for vacation purposes and are not regularly occupied by the related mortgagors. Because the mortgagor is not living on the property, the mortgagor may be more likely to default on the mortgage loan than on a comparable mortgage loan secured by a primary residence.

Mortgage loans secured by investor properties may have a greater likelihood of delinquency and foreclosure, and a greater likelihood of loss in the event thereof, than mortgage loans secured by owner occupied single-family residential properties. The ability of a mortgagor to repay an owner-occupied single-family loan typically depends primarily on such mortgagor's household income rather than on the capacity of the mortgaged property to appreciate in value or produce income. Accordingly, a reduction in a related mortgagor's income may adversely affect the performance of the mortgage loan, but may not directly affect the liquidation value of such mortgaged property. In contrast, the ability of a mortgagor to repay a loan secured by an investor property typically depends primarily on (i) the successful operation and management of such mortgaged property, rather than on any independent income or assets of the mortgagor or (ii) the mortgagor's ability to realize the value of such mortgaged property (e.g. via refinancing or profitable disposition). In some cases, the mortgagor may have no material assets other than the mortgaged property. As a result, if the net operating income of the mortgaged property is reduced (for example, if rental or occupancy rates decline, competition increases, or real estate tax rates or other operating expenses increase), the mortgagor's ability to repay the mortgage loan may be impaired, and the liquidation value of the related mortgaged property also may be adversely affected.

While the originators take certain steps in the course of their origination process to confirm that each Investor Loan is primarily made for a business or commercial purpose, a regulatory authority could find that an Investor Loan was originated as a consumer loan (i.e., primarily for personal, family or household use, and therefore subject to various consumer protection laws). Violations of consumer protection laws may limit the ability to collect all or part of the principal or interest on the Investor Loans, may result in a defense to foreclosure or an "unwinding" or rescission of the Investor Loans, or may entitle the mortgagor to a refund of amounts previously paid, and could subject the related originator and/or an assignee to damages and/or administrative enforcement.

In addition, even though a mortgagor may make certain representations regarding such mortgagor's intent to utilize a property primarily for a business purpose, the mortgagor may have misrepresented the intended purpose of the loan or have changed circumstances such that the proceeds of the loan may ultimately be used for personal, family, or household purposes. Therefore, an Investor Loan may be originated in accordance with applicable law even if such Investor Loan proceeds and the property are used for a consumer purpose. In such a case, the mortgagor's ability to repay such Investor Loan may be impaired if such property is not a profitable investor property, and the liquidation value of the related property also may be adversely affected.

Investor Loans are not subject to TILA because, based on representations by the related mortgagors, each such Investor Loan is an extension of credit primarily for a business purpose and is not a "covered transaction" as defined in Section 1026.43(b)(1) of Regulation Z. However, to the extent an Investor Loan is found to be a covered transaction, failure to comply with the ATR Rules may result in, among other things, civil liability and a mortgagor's ability to bar or postpone foreclosure proceedings with respect to the related property by raising defenses.

### **Regulation of the Mortgage Industry**

In response to increased delinquencies and losses with respect to residential mortgage loans starting in late 2006, many mortgage loan originators implemented more restrictive underwriting criteria for mortgage loans, which resulted in reduced availability of refinancing alternatives for borrowers. In response to these and other circumstances, the Federal Reserve Bank began a quantitative easing program whereby the Federal Reserve Bank purchased a significant amount of RMBS and other securities in order to support the market. In addition, federal, state and local authorities have enacted and continue to propose new legislation, rules and regulations relating to the origination, servicing and treatment of mortgage loans in default or in bankruptcy. These initiatives could result in delayed or reduced collections from mortgagors, limitations on the foreclosure process and generally increased servicing costs. Further, the conservatorships of Fannie Mae and Freddie Mac in September 2008 have impacted both the real estate market and the value of real estate assets generally. While Fannie Mae and Freddie Mac currently act as the primary sources of liquidity in the residential mortgage markets, both by purchasing mortgage loans for their own portfolios and by guaranteeing mortgage-backed securities, their long-term role is uncertain as there are a number of legislative proposals to reduce and eventually eliminate their role in the residential mortgage markets. A reduction in the ability of mortgage loan originators to access Fannie Mae and Freddie Mac to sell their mortgage loans may adversely affect the financial condition of mortgage loan originators. In addition, any decline in the value of securities issued by Fannie Mae and Freddie Mac may affect the value of residential mortgage loans and RMBS in general. These adverse changes in market and credit conditions have had, and may continue to have, the effect of depressing the market values and reducing the liquidity of residential mortgage loans and RMBS generally.

Residential mortgage loans, including those backing RMBS, are subject to U.S. federal laws, including:



- TILA provides that subsequent purchasers of mortgage loans originated in violation of certain requirements specified in TILA may have liability for such violations, and includes a requirement codifying a provision of the Dodd-Frank Act prohibiting lenders from originating residential mortgage loans unless the lender determines that the borrower has a reasonable ability to repay the loan;
- the Real Estate Settlement Procedures Act, as amended ("RESPA") and its regulations, which (among other things) prohibit the payment of referral fees for real estate settlement services (including mortgage lending and brokerage services) and regulate escrow accounts for taxes and insurance and billing inquiries made by mortgagors;
- the CFPB's Know Before You Owe TILA – RESPA Integrated Disclosure rule, which became effective for mortgage loans whose applications were received on or after October 3, 2015, reconciles overlapping disclosure obligations under TILA and RESPA to provide for integrated closing disclosure and loan estimate forms that would satisfy those requirements under both TILA and RESPA.
- the Equal Credit Opportunity Act and Regulation B promulgated under the Equal Credit Opportunity Act, which prohibit discrimination on the basis of age, race, color, sex, religion, marital status, national origin, receipt of public assistance or the exercise of any right under the Consumer Credit Protection Act, in the extension of credit;
- the Americans with Disabilities Act, which, among other things, prohibits discrimination on the basis of disability in the full and equal enjoyment of the goods, services, facilities, privileges, advantages, or accommodations of any place of public accommodation;
- the Fair Credit Reporting Act, which regulates the use and reporting of information related to the borrower's credit experience;
- the Home Ownership and Equity Protection Act of 1994, which regulates the origination of high cost loans;
- the Depository Institutions Deregulation and Monetary Control Act of 1980, which preempts certain state usury laws;
- the Alternative Mortgage Transaction Parity Act of 1982, which preempts certain state lending laws which regulate alternative mortgage transactions; and
- the U.S. Servicemembers' Civil Relief Act of 2003, as amended which provides relief to mortgagors who enter into active military service or who were on reserve status but are called to active duty after the origination of their mortgage loans.

In addition, the Dodd-Frank Act made extensive changes to laws regulating financial services firms, including the creation of (1) the CFPB within the Federal Reserve to regulate providers of consumer financial services and products and (2) the Financial Stability Oversight Council to identify, monitor and address emerging systemic risks posed by the activities of financial services firms and make recommendations to the Federal Reserve to alleviate those risks. The CFPB has sole rulemaking and interpretive authority under existing and future consumer financial services laws and supervisory, examination and enforcement authority over institutions subject to its jurisdiction. The Dodd-Frank Act also provides for enhanced regulation of derivatives and securitization transactions (including the addition of risk retention requirements, third-party due diligence disclosure requirements, expanded asset-level data requirements and new standards relating to eligibility of securities as "mortgage-related securities" under the Exchange Act), restrictions on executive compensation and enhanced oversight of credit rating agencies. In addition, the law provides for the elimination of prepayment penalties for mortgage loans and expanded consumer protection in respect of high-cost mortgage loans.

On February 9, 2012, the Department of Justice, the Department of Housing and Urban Development, and attorneys general representing 49 states and the District of Columbia reached a settlement agreement ("2012 Servicing Settlement") with five large mortgage servicers in connection with servicing and foreclosure issues. The 2012 Servicing Settlement provides for financial relief for homeowners, including mortgage loan principal reduction, refinancing and increased benefits and protections for service members and veterans, and requires

a comprehensive reform of mortgage servicing practices for the five servicers. In addition, the CFPB, U.S. Treasury Department, several regulatory bodies and state attorneys general have recently increased scrutiny of mortgage servicers and have imposed, or are seeking to impose, requirements on servicers to substantially revise their servicing practices, including the establishment of national servicing standards that would be applicable to all residential mortgage servicers. Any changes to the servicers' servicing procedures could cause delays in payments on mortgage loans and RMBS.

Violations of provisions of these U.S. federal laws may limit the ability of the issuer of RMBS or holder of a residential mortgage loan to collect all or part of the principal of or interest on the loan(s) and in addition could subject such issuer to damages and administrative enforcement. In this event, the holder of such RMBS or the holder of the residential mortgage loan may suffer a loss.

In addition, there are applicable state laws which generally regulate interest rates and other charges, require licensing of lenders and require specific disclosures. Other state laws, public policy and general principles of equity relating to the protection of consumers, unfair and deceptive practices and debt collection practices may apply to the origination, servicing and collection of the loans backing RMBS. Depending on the provisions of the applicable law and the specific facts and circumstances involved, violations of these laws, policies and principles may limit the ability of the issuer of a RMBS or of a holder of a residential mortgage loan to collect all or part of the principal of or interest on the underlying loans, may entitle a borrower to a refund of amounts previously paid and, in addition, could subject the owner of a mortgage loan to damages and administrative enforcement.

#### **Homeowner's Insurance**

Insurers in some areas have become less willing to continue writing coverage on residential properties or charge significantly increased insurance premiums to address the rising risks. For example, insurers have ceased providing coverage in wildfire-prone areas in California or are exiting the state entirely. As coverage becomes less available or prohibitively expensive, home prices may decline. Ultimately, the desirability of homes in areas that frequently experience hurricanes, wildfires or other natural disasters may diminish over time, which can depress home prices and adversely affect both SGCP's ability to source loans for, and the performance of the loans in, funds and accounts managed by SGCP.

#### **Commercial Mortgage-Backed Securities and Commercial Real Estate Loans**

The commercial real estate loans owned by funds or accounts managed by SGCP ("CRE Loans") and the commercial real estate collateral underlying commercial mortgage-backed securities owned by funds or accounts managed by SGCP ("CMBS") generally are secured by income-producing property, such as office buildings, industrial or warehouse properties, hotels, rental apartments, student housing, senior living centers, regional malls, other retail space, nursing homes and self-storage properties. The market value of a commercial property depends on its income generating ability. As a result, income generation will affect both the likelihood of default and the severity of losses with respect to a CRE Loan or CMBS investment. Any decrease in income or value of the CRE Loans or the commercial real estate underlying an issue of CMBS could result in cash flow delays and losses. Successful management and operation of the related business (including property management decisions, such as pricing, maintenance and capital improvements) will have a significant impact on performance on a CRE Loan or CMBS investment. Issues such as tenant mix, success of tenant business, property location and condition, competition, increases in interest rates, real estate taxes and other operational expenses, general or local economic conditions and/or specific industry segments, declines in real estate values, declines in rental or occupancy rates and civil disturbances, changes in governmental rules, regulations and fiscal policies, the economic impact of the COVID-19 outbreak, acts of God, social unrest and insurance coverage are among the factors that may impact both performance and market value. The value of commercial real estate is also subject to limitations on remedies imposed by bankruptcy laws and state laws regarding foreclosures and rights of redemption. At any one time, a group of

CRE Loans owned by a fund or account managed by SGCP or a portfolio of CMBS may be backed by commercial real estate loans with disproportionately large aggregate principal amounts secured by properties in only a few states or regions. As a result, the commercial real estate loans may be more susceptible to geographic risks relating to such areas, such as adverse economic conditions, adverse events affecting industries located in such areas and natural hazards affecting such areas, than would be the case for a pool of commercial real estate loans having more diverse property locations. Commercial real estate loans often are structured so that a substantial portion of the loan principal is not amortized over the loan term but is payable at maturity, and repayment of the loan principal thus often depends upon the future availability of real estate financing from the existing or an alternative lender and/or upon the current value and salability of the real estate. Therefore, the unavailability of real estate financing may lead to default. Most commercial real estate loans are effectively nonrecourse obligations of the borrower, meaning that there is no recourse against the borrower's assets other than the collateral. If borrowers are not able or willing to refinance or dispose of encumbered property to pay the principal and interest owed on such mortgage loans, payments on the CRE Loans or CMBS are likely to be adversely affected. Foreclosure can be costly and delayed by litigation and/or bankruptcy.

In addition to the risks generally associated with a borrower's ability to make payments due on its commercial real estate loan as described above, if any major repair or improvement is required at a property, there are no assurances that the related borrower (or tenant, if required under its lease) will be able to obtain funds to make such repair or improvement. As with all real estate, if reconstruction (for example, following fire or other casualty) or any major repair or improvement is required at a property, changes in governmental approvals may be applicable and may materially affect the cost to, or ability of, the related borrower to complete such reconstruction, major repair or improvement. Furthermore, certain of the reciprocal easement and operating agreements or anchor tenant leases may provide that the anchor tenant is permitted to terminate its lease or operating covenant in certain circumstances, including if a property is substantially damaged or taken by condemnation.

In the financial crisis of 2008, the real estate and securitization markets, including the markets for CRE Loans and CMBS, as well as the debt markets, global financial markets and the economy generally, experienced significant dislocations, illiquidity and volatility. Declining real estate values, coupled with diminished availability of leverage and/or refinancings for commercial real estate resulted in increased delinquencies and defaults on commercial real estate loans, which negatively impacted the value of CMBS. In addition, during the financial crisis of 2008 the general economy affected the financial strength of many commercial real estate tenants and resulted in increased rent delinquencies and increased vacancies, particularly in the retail sector.

Another economic downturn may lead to increased vacancies, decreased rents or other declines in income from, or the value of, commercial real estate, which would likely have an adverse effect on the value and/or liquidity of loans secured by such commercial real estate and any related CMBS. SGCP cannot assure investors that there will not be another dislocation in the CMBS and commercial real estate loan market. Even if such market does recover from such a dislocation, the properties and, therefore, the mortgage loans, related CMBS and commercial real estate loans generally, may decline in value. Another economic downturn may adversely affect the financial resources of the related borrower under the loans and may result in the inability of the related borrower to make principal and interest payments on, or refinance, the outstanding debt when due or to sell the properties for an aggregate amount sufficient to pay off the outstanding debt when due. In the event of default by a borrower under any of the loans, such loans may suffer a partial or total loss. In addition, significant changes in regional climate conditions could have effects that are difficult to foresee. Areas of the United States may from time to time be affected by flooding, severe storms, hurricanes, landslides, wildfires, earthquakes or other natural disasters, or the effects of global climate change (which may include flooding, drought or severe weather). To the extent that a locality becomes more susceptible to extreme temperatures or weather events or otherwise becomes less desirable as a place to live, property values could be adversely

affected, and rates of default could increase. Any delinquency or loss on the loans may have an adverse effect on the distributions of principal and interest received by investors in CMBS.

Even if CMBS are performing as anticipated, the value of such CMBS in the secondary market may nevertheless decline as a result of a deterioration in general market conditions for other asset-backed securities or structured products. Trading activity associated with CMBS indices may also drive spreads on those indices wider than spreads on CMBS, thereby resulting in a decrease in value of such CMBS.

**CMBS Subordinated Securities**

Funds or accounts managed by SGCP may invest in subordinated CMBS, which will expose the funds or accounts to greater credit risk of default than the senior classes of the same issue of CMBS. Default risks may be further pronounced in the case of CMBS secured by, or evidencing an interest in, a relatively small or less diverse pool of underlying loans. Subordinated securities absorb all losses from default before any other class of securities is at risk, particularly if such securities have been issued with little or no credit enhancement or equity. Such securities, therefore, possess some of the attributes typically associated with equity investments.

**Collateralized Loan Obligations**

Funds or accounts managed by SGCP may invest in collateralized loan obligations backed by loans secured by commercial real estate assets ("CRE CLOs"). CRE CLOs are instruments representing interests in, or secured by, pools of commercial real estate loans and related assets, such as CMBS. Similar to CMBS, the assets are limited-recourse obligations of the issuer thereof payable solely from the underlying assets in the portfolio of such issuer. CRE CLOs are subject to the risks relating to CMBS described herein, as well as to additional risks, including the following:

**Limited Diversification**

A CRE CLO may invest in a concentrated portfolio of assets. The concentration of an underlying portfolio of commercial mortgage loans in a specific state or geographic region may subject the holder of the related CRE CLOs to a greater degree of risk with respect to defaults by such obligor and the concentration of a portfolio in any one state or region may subject the holder of the related CRE CLOs to a greater degree of risk with respect to economic downturns relating to such region.

**Financial Condition of Obligors**

The value of the CRE CLOs owned by the funds or accounts managed by SGCP generally will fluctuate with, among other things, the financial condition of the obligors or issuers of the underlying portfolio of assets of the related CRE CLO ("CRE CLO Collateral"), general economic conditions, the condition of the financial markets, political events, developments or trends in the real estate market and changes in prevailing interest rates.

**Interest Rate Mismatch**

CRE CLOs could be subject to significant interest rate risk. Some of the CRE CLO Collateral may bear interest at a fixed rate, while the CRE CLO notes may bear interest at a floating rate. As a result, there could be a mismatch between such CRE CLO notes and the CRE CLO Collateral.

**Liquidity of Markets**

At times, the fixed income and bond markets have experienced significant falloffs in liquidity. While such events may sometimes be attributable to changes in interest rates or other factors, the cause is not always apparent. Such "liquidity risk" could adversely impact the value of the Fund's portfolio and may be difficult or impossible to hedge against. The bond securities purchased by the funds or accounts managed by SGCP may not have any market.

**Fees Paid to Collateral Manager**

Funds or accounts managed by SGCP may invest in a CRE CLO managed by a collateral manager (which is not affiliated with SGCP), and the CRE CLO may pay management fees to the third-party collateral manager. As an investor in the CRE CLO, funds or accounts managed by SGCP could have very limited (or no) rights to control the investment decisions or other actions taken by the third-party collateral manager of the CRE CLO, and the return on the fund's or account's investment in the CRE CLO may be dependent upon the skill and decisions of the third-party collateral manager.

**Credit Default Swaps**

Credit default swaps can be used to implement the view that a particular credit or index, or group of credits or indices, will experience credit improvement or deterioration. In the case of expected credit improvement, SGCP clients may sell credit default protection in which it receives a premium to take on the risk. In such an instance, the obligation of clients to make payments upon the occurrence of a credit event creates leveraged exposure to the credit risk of the referenced entity. Clients may also buy credit default protection with respect to a referenced entity if, in SGCP's judgment, there is a high likelihood of credit deterioration. In such instance, the clients will pay a premium regardless of whether there is a credit event.

**Debt Instruments**

Bonds, notes and debentures issued by corporations may pay fixed, variable or floating rates of interest, and may include zero-coupon obligations. Corporate debt instruments may be subject to credit ratings downgrades. Other instruments may have the lowest quality ratings or may be unrated.

**Interest Rate Risk**

Changes in interest rates can affect the value of SGCP client investments in fixed-income instruments. Increases in interest rates may cause the value of the client's debt investments to decline. Clients may experience increased interest rate risk to the extent it invests, if at all, in lower-rated instruments, debt instruments with longer maturities, debt instruments paying no interest (such as zero-coupon debt instruments) or debt instruments paying non-cash interest in the form of other debt instruments.

**Agency Securities**

Since the Advisor may invest in the debt of Fannie Mae and Freddie Mac as well as mortgage-backed securities guaranteed by Fannie Mae and Freddie Mac, it will be exposed to the credit risk of such agencies. Any action that affects the credit quality of the guarantees provided by Fannie Mae, Freddie Mac and Ginnie Mae could materially adversely affect the value of agency RMBS held by the fund. If Fannie Mae, Freddie Mac or Ginnie Mae were eliminated, or their structures were to change radically or the U.S. government significantly reduced its support for any or all of them, the fund may be unable or significantly limited in its ability to acquire agency RMBS and the debt of Fannie Mae, Freddie Mac and Ginnie Mae.

**Repurchase and Reverse Repurchase Agreements**

In a repurchase transaction, a client "sells" and in a reverse repurchase transaction, a client "buys" a security issued from a broker-dealer or financial institution, subject to the obligation of the client, broker-dealer, or financial institution to repurchase or sell such securities at the price paid by the client, plus interest at a negotiated rate. The use of repurchase and reverse repurchase agreements by clients involves certain risks. For example, if the seller of securities to the client under a reverse repurchase agreement defaults on its obligation to repurchase the underlying securities, as a result of its bankruptcy or otherwise, the client will seek to dispose of such securities, which action could involve costs or delays. If the seller becomes insolvent and subject to liquidation or reorganization under applicable bankruptcy or other laws, the client's ability to dispose of the underlying securities may be restricted. It is possible, in a bankruptcy or liquidation scenario, that the client may not be able to substantiate its interest in the underlying securities. Finally, if a seller defaults on its obligation to repurchase securities under a reverse repurchase agreement, the client may suffer

a loss to the extent that it is forced to liquidate its position in the market and proceeds from the sale of the underlying securities are less than the repurchase price agreed to by the defaulting seller. Similar elements of risk arise in the event of bankruptcy or insolvency of the buyer.

### **Derivative Instruments**

Certain swaps, options and other derivative instruments may be subject to various types of risks, including market risk, liquidity risk, credit risk, legal risk and operations risk. The regulatory and tax environment for derivative instruments in which SGCP clients may participate is evolving, and changes in the regulation or taxation of such securities may have a material adverse effect on the clients. There are many rules related to derivatives that may negatively impact clients, such as requirements related to recordkeeping, reporting, portfolio reconciliation, central clearing, minimum margin for uncleared over-the-counter instruments and mandatory trading on electronic facilities, and other transaction-level obligations. Requirements such as these also raise the costs of entering into derivative transactions, and these increased costs will likely be passed on to clients. Regulations in the derivatives industry create reporting, clearing and margin related regulatory requirements to which SGCP is required to adhere.

### **Equity Instruments**

SGCP may invest its assets in equity securities, including preferred and common stock. Equity strategies are based on attempting to predict the future price level of different equity or equity-related securities. Numerous interrelated and difficult-to-quantify economic factors, as well as market sentiment, political, climate-related and geopolitical factors influence the prices of equities. There can be no assurance that SGCP will be able to predict future price levels. While diversification among issuers may mitigate these risks, a fund is not required to diversify its investments in equity securities, and investors should expect fluctuations based on market conditions in the value of equity securities held by the fund.

### **Investments in Equity of Private Companies**

SGCP may purchase equity in private companies. Such an investment involves a high degree of risk and is suitable only for investors with the financial sophistication and expertise to properly evaluate the merits and risks. Risks relating to this type of investment include, but are not limited to, lack of liquidity of the investment, limited or no control over the activities of the company, no assurance that the company will be able to generate returns for its investors, and diversification risk given that SGCP may only invest in a limited number of private companies.

## **Item 9 - Disciplinary Information**

In the past ten years, there have been no legal or disciplinary events involving either SGCP or any of its management persons that are material to SGCP's advisory business.

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

SGCP is registered with the Commodities Futures Trading Commission (the "CFTC") as a commodity pool operator and is a member of the National Futures Association. SGCP's Scott Barringer is registered with the CFTC as an Associated Person of SGCP.

Affiliates of SGCP invest in our fund clients. This may create an incentive to favor the funds and accounts in which our affiliates have invested over other funds and accounts managed by SGCP in which our affiliates have not invested. As disclosed in Item 6 and Item 12, SGCP maintains an allocation policy to ensure fair and equitable allocation of client transactions across client accounts.

**Item 11 - Code of Ethics, Participation or Interest in Client Transactions and Personal Trading**

- A. SGCP maintains a Code of Ethics (the “Code”) that is applicable to all of its employees. Copies of the Code are available for review by clients and prospective clients upon request. Requests for the Code should be made to Jay Strauss at [jstrauss@sgcp.com](mailto:jstrauss@sgcp.com) or (203) 355-6113. Key provisions of the Code include restrictions on personal trading, a requirement to report outside business activities, restrictions on political contributions, requirements to disclose key disciplinary events to the CCO, restrictions on the use of social media, restrictions on the receipt and delivery of gifts and recordkeeping.

The Code includes several restrictions on personal trading conducted by or on behalf of employees. Employees are restricted from trading key instruments that are also tradable by clients due to the potential for a conflict of interest.

Personal trading activity conducted by covered persons is reviewed by the CCO or his designee.

- B. Funds and accounts managed by SGCP periodically enter into transactions with SG Capital Partners LLC, ClearEdge Lending LLC or another affiliate. SGCP-managed funds and accounts purchase residential mortgage and commercial real estate loans or other structured credit assets from SG Capital Partners LLC, ClearEdge Lending LLC or another affiliate from time to time for investment purposes. Each such transaction is a “principal transaction” for purposes of Section 206(3) of the Advisers Act. SGCP has adopted a policy to address these transactions that consists of a third-party valuation company valuing any assets transferred and a committee of individuals unaffiliated with SGCP and acting on behalf of SGCP clients reviewing and approving in writing in advance based on the valuation all transactions between funds or accounts managed by SGCP and its affiliates.
- C. SGCP’s employees and related persons are prohibited from transacting in the same securities that are recommended to clients.

**Item 12 - Brokerage Practices**

- A. SGCP considers the following factors in selecting broker-dealers for client transactions: best execution (price), brokerage expenses, execution capabilities, financing arrangements, product mix, reporting capabilities, responsiveness, financial condition and quality of research.

SGCP does not participate in soft dollar programs. The investment activity conducted by SGCP will generally take place in the over-the-counter securities markets. In these markets, commissions are not typically distinguishable from transaction prices and soft dollar credits are not typically accrued.

SGCP does not consider client referrals when selecting or recommending a broker-dealer.

Certain managed account clients may provide a list of approved broker-dealers from which SGCP may select a broker-dealer to effect its trades, subject to SGCP’s approval.

- B. SGCP aggregates the purchase and sale of securities for client accounts if it is operationally efficient to do so and in the best interests of clients. SGCP maintains an allocation policy to ensure fair and equitable allocation of client transactions across client accounts.

**Item 13 - Review of Accounts**

SGCP employs a full-time investment and trading staff. This investment and trading team reviews client accounts daily as part of an ongoing monitoring process. These reviews and the supervision related thereto are the responsibility of Dan Sparks and Justin Mahoney.

Clients receive written statements from SGCP no less frequently than quarterly.

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

- A. No one other than clients provide to SGCP an economic benefit for providing investment advice or other advisory services to clients.
- B. SGCP has entered into agreements with third party marketers ("Solicitors") who solicit investors in the funds. SGCP pays these Solicitors a portion of the fees collected from investors introduced by the Solicitors and or a fixed fee as individually negotiated between each Solicitor and SGCP. SGCP also reserves the right to pay compensation to Solicitors in the future in accordance with applicable law.

**Item 15 - Custody**

SGCP will not physically maintain custody of any client funds or securities. All client funds and securities will be held by qualified custodians. However, private funds that are managed by SGCP may be structured in such a manner that SGCP or an affiliate serves as the general partner to certain limited partnerships and/or the manager of certain limited liability companies, in which case SGCP may be deemed to have custody of the funds and securities held by those entities. SGCP adheres to the applicable requirements of Rule 206(4)-2 of the Advisers Act with respect to these arrangements. SGCP does not have custody over assets held in managed accounts, as described in the applicable investment management agreement. SGCP may hold uncertificated interests in certain securities that are exempt from the requirement to be held by a qualified custodian.

Fund clients of SGCP will receive a copy of the audit for each fund within 120 days of each calendar year end. In addition, fund clients will receive account statements from the fund administrator and clients should carefully review those statements.

**Item 16 - Investment Discretion**

SGCP has investment discretion over all client accounts. Clients will delegate investment discretion to SGCP through an investment management agreement.

**Item 17 - Voting Client Securities**

SGCP may maintain discretion to vote client securities and has adopted a policy governing such arrangement that includes a screen for conflicts of interest prior to casting a vote. A complete copy of SGCP's proxy voting policy and proxy voting record is available to clients by contacting Jay Strauss at [jstrauss@sgcp.com](mailto:jstrauss@sgcp.com) or (203) 355-6113.

**Item 18 - Financial Information**

SGCP does not require or solicit pre-payment of more than \$1,200 in fees per client six months or more in advance, is not aware of any financial condition that is reasonably likely to impair its ability to meet its contractual obligations to its clients and has not been the subject of a bankruptcy petition. As such, Item 18 is not applicable.



**Item 19 - Requirements for State-Registered Advisers**

Not applicable.