

**ITEM 1  
COVER PAGE**

---

---

**PART 2A OF FORM ADV: FIRM BROCHURE**  
**MERCHANTS' GATE ASSET MANAGEMENT LP**

January 30, 2018

---

---

Merchants' Gate Asset Management LP  
135 East 57<sup>th</sup> Street, 15<sup>th</sup> Floor  
New York, New York 10022  
Tel: (212) 993-7040  
Fax: (212) 993-7050

*This brochure (this "Brochure") provides information about the qualifications and business practices of Merchants' Gate Asset Management LP ("Merchants' Gate", the "Firm", or the "Advisor"). If you have any questions about the contents of this Brochure, please contact us at (212) 993-7040 or [jmarra@mgatecap.com](mailto:jmarra@mgatecap.com). The information in this Brochure has not been approved or verified by the United States Securities and Exchange Commission (the "SEC") or by any state securities authority.*

*A copy of this Brochure and additional information about Merchants' Gate are also available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).*

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

## **ITEM 2**

### **MATERIAL CHANGES**

This is Merchants' Gate's Annual Updating Amendment to its Form ADV, for the fiscal year ending December 31, 2017. Merchants' Gate made no material changes since the last update of this Brochure on March 24, 2017.

# **ITEM 3** **TABLE OF CONTENTS**

## **ITEM 1 COVER PAGE**

## **ITEM 2 MATERIAL CHANGES ..... i**

## **ITEM 3 TABLE OF CONTENTS ..... ii**

## **ITEM 4 ADVISORY BUSINESS ..... 1**

- A. General Description of Advisory Firm..... 1
- B. Description of Advisory Services ..... 1
- C. Availability of Customized Services for Individual Clients..... 2
- D. Wrap Fee Programs..... 2
- E. Assets Under Management ..... 2

## **ITEM 5 FEES AND COMPENSATION ..... 3**

- A. Advisory Fees and Compensation..... 3
- B. Payment of Fees ..... 3
- C. Additional Fees and Expenses ..... 3
- D. Prepayment of Fees ..... 4
- E. Additional Compensation and Conflicts of Interest ..... 4

## **ITEM 6 PERFORMANCE-BASED FEES AND SIDE-BY-SIDE MANAGEMENT ..... 5**

## **ITEM 7 TYPES OF CLIENTS ..... 6**

## **ITEM 8 METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS ..... 7**

- A. Methods of Analysis and Investment Strategies ..... 7
- B. Material, Significant or Unusual Risks Relating to Investment Strategies and Risks  
Associated with Particular Types of Securities ..... 7

## **ITEM 9 DISCIPLINARY INFORMATION ..... 22**

## **ITEM 10 OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS ..... 23**

- A. Broker-Dealer Registration Status..... 23
- B. Futures Commission Merchant, Commodity Pool Operator or Commodity Trading  
Adviser Registration Status ..... 23
- C. Material Relationships or Arrangements with Industry Participants..... 23
- D. Material Conflicts of Interest Relating to Other Investment Advisers ..... 23

|  |    |
|--|----|
| <b>ITEM 11 CODE OF ETHICS, PARTICIPATION OR INTEREST IN<br/>CLIENT TRANSACTIONS AND PERSONAL TRADING</b> | 24 |
| A. <u>Code of Ethics</u>   | 24 |
| B. <u>Securities in which Merchants' Gate or a Related Person has a Material Financial<br/>Interest</u>  | 24 |
| C. <u>Investing in Securities that Merchants' Gate or a Related Person Recommends to<br/>Clients</u>     | 25 |
| <b>ITEM 12 BROKERAGE PRACTICES</b>   | 26 |
| A. <u>Factors Considered in Selecting or Recommending Broker-Dealers for Client<br/>Transactions</u>     | 26 |
| B. <u>Trade Allocation and Aggregation Policies and Procedures</u>                                       | 28 |
| <b>ITEM 13 REVIEW OF ACCOUNTS</b>  | 29 |
| A. <u>Frequency and Nature of Review of Client Accounts or Financial Plans</u>                           | 29 |
| B. <u>Factors Prompting Review of Client Accounts Other than on a Periodic Review</u>                    | 29 |
| C. <u>Content and Frequency of Account Reports to Clients</u>  | 29 |
| <b>ITEM 14 CLIENT REFERRALS AND OTHER COMPENSATION</b>   | 30 |
| A. <u>Economic Benefits for Providing Services to Clients</u>  | 30 |
| B. <u>Compensation to Non-Supervised Persons for Client Referrals</u>                                    | 30 |
| <b>ITEM 15 CUSTODY</b>   | 31 |
| <b>ITEM 16 INVESTMENT DISCRETION</b>   | 32 |
| <b>ITEM 17 VOTING CLIENT SECURITIES</b>  | 33 |
| <b>ITEM 18 FINANCIAL INFORMATION</b>   | 34 |

## ITEM 4 ADVISORY BUSINESS

### A. General Description of Advisory Firm.

Merchants' Gate, a Delaware limited partnership, was formed on September 28, 2015 and is located in New York City. The principal owner of Merchants' Gate is Jason Capello. Mr. Capello owns interests in Merchants' Gate directly (as a limited partner) and indirectly (as a member of Merchants' Gate Asset Management GP LLC, a Delaware limited liability company that is the general partner of Merchants' Gate (the "General Partner")).

### B. Description of Advisory Services.

#### 1. *Advisory Services.*

Merchants' Gate serves as the investment adviser with discretionary trading authority to Merchants' Gate Asset Management Fund LP (the "Fund"), a Delaware limited partnership. Subject to the terms described below, the Fund offers and sells its interests in private transactions solely to accredited investors, qualified clients, qualified purchasers and certain knowledgeable employees of Merchants' Gate and its affiliates.

As used herein, the term "client" generally refers to the Fund. As of the date of this Brochure, Merchants' Gate does not have any clients other than the Fund.

#### 2. *Investment Strategies and Types of Investments.*

The Advisor plans to own or invest in businesses that will compound value over time. The Advisor believes that there are a limited number of extraordinary investment opportunities available at any time. The Advisor further believes that many investors seek diversification to the point of diluting returns. In addition, controlling the quality of research becomes more difficult in an analyst-intensive model. As a result, rather than spread the Advisor's capital and human resources across a large number of investments, Merchants' Gate generally concentrates a substantial portion of its portfolio in a small number of investments, typically 15 to 30 long equity positions. While this concentration may result in more volatility in the short-term as compared to a larger or hedged portfolio, the quality of the research and the businesses Merchants' Gate anticipates owning should compensate for it over the longer term and deliver returns consistent with the success of its investments, not simply the returns of the related global indices. (See "The Investment Program.")

The Advisor invests globally. While Merchants' Gate may invest in companies of all market capitalizations, position size typically limits Merchants' Gate's ability to invest in the smallest capitalization companies.

The Advisor's investment program is speculative and entails substantial risks. There can be no assurance that the Advisor's investment objective of each client will be achieved or that investment results might not vary substantially on a monthly, quarterly or annual basis. A more

detailed description of the investment strategies pursued and types of investments made by Merchants' Gate is provided in Item 8 (Methods of Analysis, Investment Strategies and Risk of Loss).

C. Availability of Customized Services for Individual Clients.

As of the date of this Brochure, Merchants' Gate has a single client, the Fund. Merchants' Gate's investment decisions and advice are subject to the Fund's investment objectives and guidelines, as set forth in the Fund's confidential offering document and/or constituent documents, which may impose restrictions on investing in certain securities or types of securities.

D. Wrap Fee Programs.

Merchants' Gate does not participate in wrap fee programs.

E. Assets Under Management.

As of December 31, 2017, Merchants' Gate's total regulatory assets under management were approximately \$128,868,466. All such assets were managed on a discretionary basis.

## **ITEM 5**

### **FEES AND COMPENSATION**

#### **A.     Advisory Fees and Compensation.**

As of the date of this Brochure Merchants' Gate has a single client, the Fund. The advisory fees applicable to the Fund are set forth in detail the Fund's confidential offering memorandum and/or constituent documents. A brief summary of such fees is provided below.

The Fund pays the Advisor a fee for management services, payable in advance at the beginning of each quarter (the "Management Fee"), equal to 0.375% (1.5% annualized) of the value of each Capital Account balance as of the beginning of such quarter. The Management Fee is pro-rated for partial periods.

Merchants' Gate may elect to reduce, waive or calculate differently the Management Fee with respect to any Limited Partner, including, without limitation, Limited Partners that are members, affiliates or personnel of the Advisor, members of their immediate family and trusts and other entities for their benefit or for charitable purposes and for strategic investors.

In consideration for the Management Fee, Merchants' Gate renders, directly or indirectly, certain administrative and managerial services to the Fund. The Management Fee generally exceeds the expenses borne by the Advisor on behalf of the Fund.

#### **B.     Payment of Fees.**

Fees and compensation paid to Merchants' Gate or the General Partner by the Fund are generally deducted from the assets of such clients. As discussed above, Management Fees are generally deducted on a quarterly basis.

#### **C.     Additional Fees and Expenses.**

In addition to Management Fees, investors in the Fund bear other fees and expenses of the Fund as described in the confidential offering memoranda and/or constituent documents of the Fund. Expenses borne by the Fund typically include, but are not limited to, expenses related to risk management provided by third-parties, third-party valuation services, legal expenses (including with respect to litigation and threatened litigation, if any), any expenses associated with regulatory filings made in connection with the Fund's operations and portfolio holdings (*e.g.*, filings with the SEC, including Form PF (but excluding the preparation of the Advisor's Form ADV)), governmental filing fees (including blue sky filing fees) internal and external accounting (including portfolio accounting, decision support and reconciliations), audit and tax preparation expenses (including expenses of outsourced third-party service providers, such as middle-office support, bank-office support and trading services), costs associated with information technology (including business continuity and disaster recovery and costs associated with cybersecurity), organizational expenses, expenses relating to the offer and sale of the interests in the Fund (including with respect to all expenses relating to side letters), any and all taxes (including entity

level taxes) and governmental fees or other charges payable by or with respect to or levied against the Fund, its investments, or to federal, state or other governmental agencies, domestic or foreign, including real estate, stamp or other transfer taxes and expenses related to complying with Sections 1471 to 1474 of the U.S. Internal Revenue Code of 1986, as amended, fees of the Fund' administrator, expenses related to the maintenance of the Fund's registered office, corporate licensing, extraordinary expenses and other investment-related expenses. Other investment-related expenses may include, but are not limited to, brokerage commissions and transaction costs, clearing and settlement charges, custodial fees, interest expense, consulting, investment banking and any other professional fees, compensation relating to particular investments or contemplated investments and research-related expenses, including, without limitation and, quotation equipment and services.

The investors in the Fund also bear the brokerage and transaction costs incurred by the Fund in respect of their investment in the Fund. See Item 12 (Brokerage Practices).

D. Prepayment of Fees.

The Fund pays Merchants' Gate the Management Fee quarterly in advance based on the Fund's value. The Management Fee is pro-rated for any partial period.

E. Additional Compensation and Conflicts of Interest.

Neither Merchants' Gate nor its supervised persons (i.e., its officers, directors or employees) accept compensation for the sale of securities or other investment products to the Fund.



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

Merchants' Gate does not charge any performance-based fees (fees based on a share of capital gains on, or capital appreciation of, the assets of a client).

Merchants' Gate is committed to allocating investment opportunities on a fair and equitable basis and, although not applicable while the Advisor has only a single client, the Firm has established order aggregation and allocation policies and procedures to address the potential conflict of interest. Please see "Conflicts of Interest Created by Contemporaneous Trading" in Item 11 and "Trade Allocation and Aggregation Policies and Procedures" in Item 12.

## **ITEM 7**

### **TYPES OF CLIENTS**

As of the date of this Brochure, Merchants' Gate's only client is the Fund (i.e., there are presently no direct advisory clients other than the Fund). Investors in the Fund may include funds of hedge funds, family offices, endowments, charitable foundations, pension plans, investment companies, sovereign entities, other institutional investors, trusts and high net worth individuals. Investors in the Fund must meet certain suitability requirements as set forth in the Fund's confidential offering memorandum. Generally, the minimum initial capital contribution that an investor may make to the Fund is \$1,000,000, although that amount may be waived the Fund's General Partner.

## ITEM 8

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

#### A. Methods of Analysis and Investment Strategies.

*The descriptions set forth in this Brochure of specific advisory services that Merchants' Gate offers to clients, and investment strategies pursued and investments made by Merchants' Gate on behalf of its clients, should not be understood to limit in any way Merchants' Gate's investment activities. Merchants' Gate may offer any advisory services, engage in any investment strategy and make any investment, including any not described in this Brochure, that Merchants' Gate considers appropriate, subject to each client's investment objectives and guidelines. The investment strategies Merchants' Gate pursues are speculative and entail substantial risks. Clients should be prepared to bear a substantial loss of capital. There can be no assurance that the investment objective of any client will be achieved.*

The Advisor pursues a "bottom-up" strategy of analysis and portfolio construction, with long positions selected one stock at a time. At the same time, the Advisor considers industry-wide factors and certain broader market conditions in its assessment of the risk/reward profile with respect to determining position size.

The research process and investment framework the Advisor employs generally includes a detailed analysis of both the industry as well as the specific company. Industry analysis includes an understanding of peak, trough and mid-cycle economics; thorough analysis of past cycles; quantifying the economics of new supply to the industry as well as the competitiveness of alternative products or services; and understanding secular rates of growth for the industry as well as market share movements over time. Company analysis includes discussions with decision-makers at the company, competitors and suppliers, as well as modeling the business using a multivariable model and range of scenarios.

As a result of Merchants' Gate's concentration and long-term holding period, the Advisor needs to identify, research and execute a limited number of ideas. The Advisor's approach to independent investment research is not simply to find great investment ideas for the portfolio today, but also to uncover attractive businesses that may, due to changes in industry structure, management or valuation, become investments for Merchants' Gate in the future. Once such ideas are identified, they are included in the Advisor's "library," where they are monitored and updated over time, enabling the Advisor to act decisively and quickly when valuation becomes compelling.

#### B. Material, Significant or Unusual Risks Relating to Investment Strategies and Risks Associated with Particular Types of Securities.

*Merchants' Gate's investment program is speculative and may entail substantial risks. Since market risks are inherent in all securities investments to varying degrees, there can be no assurance that our investment objectives will be achieved. In fact, certain investment practices described above can, in some circumstances, increase the risk profile of the Fund's investment portfolios. The Fund's activities could result in substantial losses (including the complete loss of*

*all capital) under certain circumstances. The material risks presented by the strategies and financial assets pursued by Merchants' Gate are set forth below. Additional information is contained in the confidential offering memorandum of the Fund. This Brochure does not purport to contain a complete disclosure of all risks that may be relevant to prospective investors in the Fund. These risk factors include only those risks that Merchants' Gate believes to be material, significant or unusual and relate to particular significant investment strategies or methods of analysis employed by Merchants' Gate.*

#### Investment Strategy and Investment Risks.

*Concentration of Investments; Limited Diversification.* The Advisor intends to concentrate a substantial portion of its portfolio in a small number of investments, with typically 15 to 30 long equity positions. Subject to the Advisor's risk framework, in the normal course of making investments on behalf of Merchants' Gate, the Advisor may select investments for Merchants' Gate that potentially could be highly concentrated, for example, in a limited number or type of financial instruments or in any one issuer, industry, sector, strategy, emerging market or geographic region. At any given time, one or more of Merchants' Gate's investments may exceed 10% of Merchants' Gate's net asset value. Market conditions may create opportunities within certain investment strategies, which may cause the Advisor to increase the concentration of certain investment strategies. Such concentration of risk may expose Merchants' Gate to losses disproportionate to those incurred by the market in general if the areas in which Merchants' Gate's investments are concentrated are disproportionately adversely affected by price movements. Merchants' Gate could be subject to significant losses if it holds a large position in a particular investment that declines in value or is otherwise adversely affected, including as a result of the default of the issuer, and usually will not hedge Merchants' Gate's investments.

*Availability of Investment Strategies.* The success of the investment activities of Merchants' Gate will depend on the Advisor's ability to identify overvalued and undervalued investment opportunities and to exploit price discrepancies in the financial markets, as well as to assess the import of news and events that may affect the financial markets. Identification and exploitation of the investment strategies to be pursued by Merchants' Gate involves a high degree of uncertainty. No assurance can be given that the Advisor will be able to locate suitable investment opportunities in which to deploy all of Merchants' Gate's assets or to exploit discrepancies in the securities and derivatives markets. A reduction in money market liquidity or the pricing inefficiency of the markets in which Merchants' Gate seeks to invest, as well as other market factors, will reduce the scope for Merchants' Gate's investment strategies.

*Competition.* The markets for securities in Merchants' Gate's investment program are highly competitive. Merchants' Gate will be competing for investment opportunities with a significant number of financial institutions and other private funds as well as various institutional investors. Some of these competitors are larger and have greater financial, human and other resources than Merchants' Gate and may in certain circumstances have a competitive advantage over Merchants' Gate. As a result of this competition, there may be fewer attractively priced investment opportunities than in the past, which could have an adverse impact on the ability of Merchants' Gate to meet its investment goals or the length of time that is required for Merchants'

Gate to become fully invested. There can be no assurance that the returns on Merchants' Gate's investments will be commensurate with the risk of investment in Merchants' Gate.

*Equity Securities.* Merchants' Gate intends to invest in equity securities and equity-related security derivatives. The value of these financial instruments generally will vary with the performance of the issuer and movements in the equity markets. As a result, Merchants' Gate may suffer losses if it invests in equity instruments of issuers whose performance diverges from the Advisor's expectations or if equity markets generally move in a single direction and Merchants' Gate has not hedged against such a general move. Merchants' Gate also may be exposed to risks that issuers will not fulfill contractual obligations such as, in the case of convertible securities or private placements, delivering marketable common stock upon conversions of convertible securities and registering restricted securities for public resale.

*Equity Price Risk.* Merchants' Gate's investment portfolios will include long positions in equity securities of public and private, listed and unlisted companies. Equity securities fluctuate in value in response to many factors, including, among others, the activities and financial condition of individual companies, the business market in which individual companies compete, geographic markets, industry market conditions, interest rates and general economic environments. In addition, events such as the domestic and international political environments, terrorism and natural disasters, may be unforeseeable and contribute to market volatility in ways that may adversely affect investments made by Merchants' Gate.

*Debt Securities.* From time to time, Merchants' Gate may invest in bonds or other fixed income securities, including, without limitation, commercial paper and "higher yielding" (and, therefore, higher risk) debt securities. It is likely that a major economic recession could disrupt severely the market for such securities and may have an adverse impact on the value of such securities. It is likely that any such economic downturn could adversely affect the ability of the issuers of such securities to repay principal and pay interest thereon and increase the incidence of default for such securities.

*Derivatives.* Merchants' Gate may utilize both exchange-traded and "over-the-counter" ("**OTC**") derivatives, including, but not limited to, futures, forwards, swaps, options and contracts for differences, as part of its investment strategies and for hedging purposes. Regulatory restraints may restrict the instruments that Merchants' Gate may trade. Derivative instruments are highly volatile, involve certain special risks and expose investors to a high risk of loss. The low initial margin deposits normally required to establish a position in such instruments permit a high degree of leverage. As a result, depending on the type of instrument, a relatively small movement in the price of a contract may result in a profit or a loss which is high in proportion to the amount of funds actually placed as initial margin and may result in unquantifiable further losses exceeding any margin deposited. In addition, daily limits on price fluctuations and speculative position limits on exchanges may prevent prompt liquidation of positions resulting in potentially greater losses. Further, when used for hedging purposes, there may be an imperfect correlation between these instruments and the investments or market sectors being hedged. Transactions in over-the-counter contracts may involve additional risk as there is no exchange market on which to close out an open position. It may be impossible to liquidate an existing position, to assess the value of a position or to assess the exposure to risk. Contractual asymmetries and inefficiencies can also increase risk, such as break clauses, whereby a

counterparty can terminate a transaction on the basis of a certain reduction in net asset value of Merchants' Gate, incorrect collateral calls or delays in collateral recovery. Merchants' Gate may also sell covered and uncovered options on securities. To the extent that such options are uncovered, Merchants' Gate could incur an unlimited loss.

*OTC Derivatives.* The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**") includes provisions that comprehensively regulate the OTC derivatives markets for the first time. The European Market Infrastructure Regulation ("EMIR") has similar requirements applicable to derivatives traded in Europe.

The Dodd-Frank Act and regulations implementing the Act mandate that certain OTC derivatives must be submitted for clearing to regulated clearinghouses. OTC trades submitted for clearing will be subject to minimum initial and variation margin requirements set by the relevant clearing member and clearinghouse, as well as possible SEC- or CFTC-mandated margin requirements. The regulators also have broad discretion to impose minimum margin requirements on non-cleared OTC derivatives and new requirements on holding of customer collateral by OTC derivatives dealers. These requirements may increase the amount of collateral Merchants' Gate is required to provide and the costs associated with providing it. Although the Dodd-Frank Act includes limited exemptions from the clearing and margin requirements for certain "end-users," Merchants' Gate does not expect to be able to rely on such exemptions. In addition, the OTC derivative dealers with which Merchants' Gate executes the majority of its OTC derivatives will be subject to clearing and margin requirements irrespective of whether Merchants' Gate is subject to such requirements. OTC derivative dealers also will be required to post margin to the clearinghouses through which they clear their customers' trades instead of using such margin in their operations, as is currently permitted. This will increase the OTC derivative dealers' costs, and these increased costs are expected to be passed through to other market participants in the form of higher upfront and mark-to-market margin, less favorable trade pricing, and the possible imposition of new or increased fees.

The CFTC requires certain derivative transactions that were historically executed on a bi-lateral basis in the OTC markets to be executed through a regulated securities, futures, or swap exchange or execution facility. The SEC may impose similar execution requirements in the future. Such requirements may make it more difficult and costly for investment funds, including Merchants' Gate, to enter into tailored or customized transactions. They may also render certain strategies in which Merchants' Gate might otherwise engage impossible or so costly that they will no longer be economical to implement.

OTC derivative dealers and major OTC derivatives market participants will be required to register with the SEC and/or CFTC. Although neither Merchants' Gate nor the Advisor is required to register as dealers or major participants in the OTC derivatives markets, it is possible that going forward, Merchants' Gate and/or the Advisor may be required to be registered as dealers or major participants. Registered OTC derivatives dealers and major participants are subject to a number of regulatory requirements, including minimum capital and margin requirements. These requirements may apply irrespective of whether the OTC derivatives in question are OTC derivatives, exchange-traded or cleared. OTC derivatives dealers are also subject to new business conduct standards, disclosure requirements, reporting and recordkeeping requirements, transparency requirements, position limits, limitations on conflicts of interest, and

other regulatory burdens. These requirements may further increase the overall costs for OTC derivative dealers, which costs are also likely to be passed along to market participants. The overall impact of the Dodd-Frank Act on Merchants' Gate is highly uncertain and it is unclear how the OTC derivatives markets will adapt to this new regulatory regime.

Although the Dodd-Frank Act and EMIR will require many OTC derivative transactions previously entered into on a principal-to-principal basis to be submitted for clearing by a regulated clearinghouse, certain of the derivatives that may be traded by Merchants' Gate may remain over-the-counter or principal-to-principal contracts between Merchants' Gate and third parties entered into privately. The risk of counterparty nonperformance can be significant in the case of these over-the-counter instruments, and "bid-ask" spreads may be unusually wide in these heretofore substantially unregulated markets. While the Dodd-Frank Act, EMIR and other global regulations are intended in part to reduce these risks, its success in this respect may not be evident for some time after the regulations are fully implemented, a process that may take several years or more.

*Short Selling.* While Merchants' Gate does not intend for short selling to be a focus of its investment strategy, Merchants' Gate may engage in short selling of securities, to a limited extent, for hedging purposes. Short selling involves selling securities which may or may not be owned by the seller and borrowing the same securities for delivery to the purchaser, with an obligation to return the borrowed securities to the lender at a later date. Short selling allows the seller to profit from declines in market prices to the extent such decline exceeds the transaction costs and the costs of borrowing the securities and may be an important aspect of certain of the investment strategies of Merchants' Gate. A short sale creates the risk of a theoretically unlimited loss, in that the price of the underlying security could theoretically increase without limit, thus increasing the cost to Merchants' Gate of buying those securities to cover the short position. There can be no assurance that the securities necessary to cover a short position will be available for purchase at the time Merchants' Gate desires to close out such short position. Purchasing securities to close out the short position can itself cause the price of the securities to rise further, thereby exacerbating the loss. In addition, the securities borrowed by Merchants' Gate to effect the short sale may be recalled by the lender of those securities at any time, thus forcing Merchants' Gate to purchase the securities to close out the short position at a loss.

In response to dislocations in the financial services industry during the financial crisis of 2008 and other market events, the SEC and foreign regulators have imposed, and may continue to impose, restrictions on and reporting obligations with respect to short selling. Uncertainty surrounding the confidential nature of the required disclosures of Merchants' Gate's short sales could discourage short selling by Merchants' Gate in circumstances where the Advisor believes that the public disclosure of such short sales may be adverse to its interests. In addition, limitations on the short selling of securities could interfere with the ability of Merchants' Gate to execute certain aspects of its investment program, including its ability to hedge certain exposures and execute transactions to implement its risk management guidelines, and any such limitations may adversely affect the performance of Merchants' Gate.

*Enhanced Regulation of Short Sales and Credit Default Swaps.* Since November 2012, short sales and credit default swaps are subject to the provisions of the EU Regulation on Short Selling and certain aspects of Credit Default Swaps (the "**Short Selling Regulation**"), which was

published in the Official Journal of the European Union on March 24, 2012. The Short Selling Regulation introduces restrictions and disclosure requirements for persons taking short positions in E.U. shares and sovereign bonds, and prohibits entering into uncovered credit default swaps in relation to E.U. sovereign debt (*i.e.*, where the investor does not have an exposure that it is seeking to hedge either to the sovereign debt itself or to assets or liabilities whose value is correlated to the sovereign debt). In addition, the Short Selling Regulation permits the competent authorities of E.U. Member States to prohibit or restrict short sales, limit sovereign credit default swaps and impose emergency disclosure requirements, among other things, during times of stressed markets. Competent authorities may also restrict short sales of individual financial instruments which have suffered a significant fall in price in a single day.

The provisions of the SEC rules and the Short Selling Regulation may hinder Merchants' Gate's investment program by preventing it from taking positions that the Advisor considers favorable. They may also result in overvaluations of certain financial instruments due to restrictions on market efficiency. In addition, the SEC's "Circuit Breaker Uptick Rule" and the emergency powers granted under the Short Selling Regulation to competent authorities during times of stressed markets and with respect to individual financial instruments, may adversely affect Merchants' Gate by preventing it from taking hedging positions or other positions that the Advisor considers to be in Merchants' Gate's best interests. The imposition of emergency measures under the Short Selling Regulation could, therefore, result in substantial losses to Merchants' Gate.

*Futures Contracts.* The value of futures depends upon the price of the financial instruments, such as commodities, underlying them. The prices of futures are highly volatile, and price movements of futures contracts can be influenced by, among other things, interest rates, changing supply and demand relationships, trade, fiscal, monetary and exchange control programs and policies of governments, and national and international political and economic events and policies. In addition, investments in futures are also subject to the risk of the failure of any of the exchanges on which Merchants' Gate's positions trade or of its clearing houses or counterparties.

Futures positions may be illiquid because certain commodity exchanges limit fluctuations in certain futures contract prices during a single day by regulations referred to as "daily price fluctuation limits" or "daily limits." Under such daily limits, during a single trading day, no trades may be executed at prices beyond the daily limits. Once the price of a particular futures contract has increased or decreased by an amount equal to the daily limit, positions in that contract can neither be taken nor liquidated unless traders are willing to effect trades at or within the limit. This could prevent Merchants' Gate from promptly liquidating unfavorable positions and subject Merchants' Gate to substantial losses or prevent it from entering into desired trades. In extraordinary circumstances, a futures exchange or the CFTC could suspend trading in a particular futures contract, or order liquidation or settlement of all open positions in such contract.

*Illiquid Securities.* From time to time, Merchants' Gate may invest in structured products, derivatives and other types of unregistered securities, which are generally not publicly traded. Merchants' Gate may not be able to readily dispose of such non-publicly traded financial instruments and, in some cases, may be contractually prohibited from disposing of such financial



instruments for a specified period of time. Accordingly, Merchants' Gate may be forced to sell its more liquid positions at a disadvantageous time, resulting in a greater percentage of the portfolio consisting of illiquid securities. In addition, the market prices, if any, for such illiquid financial instruments tend to be volatile, and Merchants' Gate may not be able to sell them when it desires to do so or to realize what it perceives to be their fair value in the event of a sale. The sale of illiquid securities also often requires more time and results in higher brokerage charges or dealer discounts and other selling expenses than does the sale of securities eligible for trading on national securities exchanges or in the over-the-counter markets. Furthermore, valuing such financial instruments may be difficult and lead to uncertain marks. It also should be noted that, even those markets which the Advisor expects to be liquid can experience periods, possibly extended periods, of illiquidity.

*Use of Options.* Merchants' Gate may buy or sell (write) both call options and put options (either exchange-traded, over-the-counter or issued in private transactions), and when it writes options it may do so on a "covered"<sup>1</sup> or an "uncovered" basis. Merchants' Gate's options transactions may be part of a hedging tactic (*i.e.*, offsetting the risk involved in another securities position) or a form of leverage, in which Merchants' Gate has the right to benefit from price movements in a large number of securities with a small commitment of capital. These activities involve risks that can be large, depending on the circumstances. In general, the principal risks involved in options trading can be described as follows, without taking into account other positions or transactions Merchants' Gate may enter into.

When Merchants' Gate buys an option, a decrease (or inadequate increase) in the price of the underlying security in the case of a call, or an increase (or inadequate decrease) in the security in the case of a put, could result in a total loss of Merchants' Gate's investment in the option (including commissions). Merchants' Gate could mitigate those losses by selling short the securities as to which it holds call options or taking a long position (*i.e.*, by buying the securities or buying options on them) on securities underlying put options.

When Merchants' Gate sells (writes) an option, the risk can be substantially greater than when it buys an option. The seller of an uncovered call option bears the risk of an increase in the market price of the underlying security above the exercise price. The risk is theoretically unlimited unless the option is "covered." If it is covered, an increase in the market price of the security above the exercise price would cause Merchants' Gate to lose the opportunity for gain on the underlying security — assuming it bought the security for less than the exercise price. If the price of the underlying security were to drop below the exercise price, the premium received on the option (after transaction costs) would provide profit that would reduce or offset any loss Merchants' Gate might suffer as a result of owning the security.

The seller of an uncovered put option theoretically could lose an amount equal to the entire aggregate exercise price of the option, if the underlying security were to become valueless. If the option were covered with a short position in the underlying security, this risk would be limited, but a drop in the security's price below the exercise price would cause Merchants' Gate to lose

---

<sup>1</sup> A call option is "covered" when the writer owns securities of the class and amount of those as to which the call option applies. A put option is covered when the writer has an open short position in securities of the relevant class and amount.

some or all of the opportunity for profit on the “covering” short position—assuming Merchants’ Gate is short for more than the exercise price. If the price of the underlying security were to increase above the exercise price, the premium on the option (after transaction costs) would provide profit that would reduce or offset any loss Merchants’ Gate might suffer in closing out its short position.

*Swap Agreements.* Merchants’ Gate may enter into swap agreements. Swap agreements can be individually negotiated and structured to include exposure to a variety of different types of investments or market factors. Depending on their structure, swap agreements may increase or decrease the exposure of Merchants’ Gate to long-term or short-term interest rates (in the United States or abroad), non-U.S. currency values, mortgage securities, corporate borrowing rates, asset-backed securities, collateralized debt obligations, indices, or other factors such as security prices, baskets of equity securities, or inflation rates. Swap agreements can take many different forms and are known by a variety of names. Merchants’ Gate is not precluded from any particular form of swap agreement if the Advisor determines it is consistent with the investment objective and policies of Merchants’ Gate.

Swap agreements tend to shift investment exposure from one type of investment to another. For example, if Merchants’ Gate agrees to exchange payments in dollars for payments in non-U.S. currency, the swap agreement would tend to decrease Merchants’ Gate’s exposure to U.S. interest rates and increase its exposure to non-U.S. currency and interest rates. Depending on how they are used, swap agreements may increase or decrease the overall volatility of the portfolio of Merchants’ Gate. The most significant factor in the performance of swap agreements is the change in the specific interest rate, currency, individual equity values or other factors that determine the amounts of payments due to and from Merchants’ Gate. If a swap agreement calls for payments by Merchants’ Gate, Merchants’ Gate must be prepared to make such payments when due. In addition, if a counterparty’s creditworthiness declines, the value of swap agreements with such counterparty can be expected to decline, potentially resulting in losses by Merchants’ Gate.

*Stock Index and Market Options.* Merchants’ Gate may also purchase and sell call and put options on stock indices and exchange-traded funds (“**ETFs**”) listed on national securities exchanges or traded in the over the counter market for the purpose of realizing its investment objective or for the purpose of hedging its portfolio. A stock index or ETF fluctuates with changes in the market values of the stocks included in the index or ETF. The changes in the value of an index or ETF may not accurately reflect the changes in the market values of the stocks included in the index or ETF. The effectiveness of purchasing or writing stock index or ETF options for hedging purposes will depend upon the extent to which price movements in Merchants’ Gate’s portfolio correlate with price movements of the stock indices or ETFs selected. Because the value of an index or ETF option depends upon movements in the level of the index or ETF rather than the price of a particular stock, whether Merchants’ Gate will realize gains or losses from the purchase or writing of options on indices or ETFs depends upon movements in the level of stock prices in the stock market generally or, in the case of certain indices or ETFs, in an industry or market segment, rather than movements in the price of particular stocks. Accordingly, successful use by Merchants’ Gate of options on stock indices or ETFs will be subject to the ability of the Advisor to correctly predict movements in the direction

of the stock market generally or of particular industries or market segments. This requires different skills and techniques than predicting changes in the price of individual stocks.

*Other Derivative Instruments.* Merchants' Gate may take advantage of opportunities with respect to certain other derivative instruments that are not presently contemplated for use or that are currently not available, but that may be developed, to the extent such opportunities are both consistent with the investment objective of Merchants' Gate and legally permissible. Special risks may apply to instruments that are invested in by Merchants' Gate in the future that cannot be determined at this time or until such instruments are developed or invested in by Merchants' Gate. Certain swaps, options and other derivative instruments may be subject to various types of risks, including market risk, liquidity risk, the risk of non-performance by the counterparty, including risks relating to the financial soundness and creditworthiness of the counterparty, legal risk and operations risk.

*Commodity-Related Instruments.* The production and marketing of commodities may be affected by actions and changes in governments. In addition, commodity-related instruments may be cyclical in nature. During periods of economic or financial instability, commodity-related instruments may be subject to broad price fluctuations, reflecting volatility of energy and basic material prices and possible instability of supply of various commodities. Commodity-related instruments may also experience greater price fluctuations than the relevant commodity. In periods of rising commodity prices, such instruments may rise at a faster rate; and conversely, in times of falling commodity prices, such instruments may suffer a greater price decline.

*Loans of Portfolio Securities.* Merchants' Gate may lend its portfolio securities. By doing so, Merchants' Gate attempts to increase its income through the receipt of interest on the loan. In the event of the bankruptcy of the other party to a securities loan, Merchants' Gate could experience delays in recovering the securities it lent. To the extent that the value of the securities Merchants' Gate lent has increased, Merchants' Gate could experience a loss if such securities are not recovered.

*Non-U.S. Investments and Emerging Markets.* Investing in the securities of companies located outside the U.S. (including, western countries, "emerging market" countries and underdeveloped countries) involves certain considerations not usually associated with investing in securities of U.S. companies, including political and economic considerations, such as greater risks of expropriation and nationalization, confiscatory taxation, the potential difficulty of repatriating funds, general social, political and economic instability and adverse diplomatic developments; the possibility of imposition of withholding or other taxes on dividends, interest, capital gain or other income; the small size of the securities markets in such countries and the low volume of trading, resulting in potential lack of liquidity and in price volatility; fluctuations in the rate of exchange between currencies and costs associated with currency conversion; and certain government policies that may restrict Merchants' Gate's investment opportunities.

In addition, accounting and financial reporting standards that prevail in non-U.S. countries generally are not equivalent to U.S. standards and, consequently, less information is available to shareholders of companies located in such countries than is available to shareholders of companies located in the U.S. Moreover, an issuer of securities may be domiciled in a country other than the country in whose currency the instrument is denominated. The values and relative

yields of investments in the securities markets of different countries, and their associated risks, are not expected to be highly correlated with each other and may behave in unpredictable ways. There is also less regulation, generally, of the securities markets in non-U.S. countries.

Merchants' Gate may be subject to additional risks which include possible adverse political and economic developments, possible seizure or nationalization of non-U.S. deposits and possible adoption of governmental restrictions which might adversely affect the payment of principal and interest to investors located outside the country of the issuer, whether from currency blockage or otherwise. Furthermore, some of the securities may be subject to brokerage, stamp or other taxes levied by governments, which have the effect of increasing the cost of such investment and reducing the realized gain or increasing the realized loss on such securities at the time of sale. Furthermore, a non-U.S. issuer of debt or the non-U.S. governmental authorities that control the repayment of the debt may be unable or unwilling to repay principal or interest when due, and Merchants' Gate may have limited recourse in the event of a default. Some of these risks do not apply equally to issuers in larger, more developed countries. These risks are more pronounced in investments in issuers in countries with emerging markets or if Merchants' Gate invests significantly in a particular country.

Investment in emerging market securities and underdeveloped markets involves a greater degree of risk than an investment in securities of issuers based in developed countries. Among other things, emerging market securities investments may carry the risks of less publicly available information, more volatile markets, less strict securities market regulation, less favorable tax provisions and a greater likelihood of severe inflation, unstable currency, war and expropriation of personal property than investments in securities of issuers based in developed countries. In addition, Merchants' Gate's investment opportunities in certain emerging markets may be restricted by legal limits on foreign investment in local securities.

Emerging markets generally are not as efficient as those in developed countries. In some cases, a market for the security may not exist locally, and transactions will need to be made on a neighboring exchange. Volume and liquidity levels in emerging markets are lower than in developed countries. When seeking to sell emerging market securities, little or no market may exist for the securities. In addition, issuers based in emerging markets are not generally subject to uniform accounting and financial reporting standards, practices and requirements comparable to those applicable to issuers based in developed countries, thereby potentially increasing the risk of fraud or other deceptive practices. Furthermore, the quality and reliability of official data published by the government or securities exchanges in emerging markets may not accurately reflect the actual circumstances being reported.

The issuers of some non-U.S. securities, such as banks and other financial institutions, may be subject to less stringent regulations in emerging markets than would be the case for issuers in developed countries and therefore potentially carry greater risk. Custodial expenses for a portfolio of emerging markets securities generally are higher than for a portfolio of securities of issuers based in developed countries.

While the Advisor will take these factors into consideration in making investment decisions for Merchants' Gate, no assurance can be given that they will be able to fully avoid these risks.

*Undervalued Securities.* One of the key objectives of Merchants' Gate is to identify and invest in misvalued securities ("**misvalued securities**"). The identification of investment opportunities in misvalued securities is a difficult task, and there can be no assurance that such opportunities will be successfully recognized. While investments in misvalued securities offer opportunities for above-average capital appreciation, these investments involve a high degree of financial risk and can result in substantial losses. Returns generated from the investments of Merchants' Gate may not adequately compensate for the business and financial risks assumed.

Merchants' Gate may make certain speculative investments in securities which the Advisor believes to be misvalued; however, there can be no assurance that the securities purchased and sold will in fact be misvalued. In addition, Merchants' Gate may be required to maintain positions in such securities for a substantial period of time before realizing their anticipated value. During this period, a portion of the capital of Merchants' Gate may be committed to the securities, thus possibly preventing Merchants' Gate from investing in other opportunities. In addition, Merchants' Gate may finance any such purchases with borrowed funds and thus will have to pay interest on such funds during such waiting period.

*"Widening" Risk.* For reasons not necessarily attributable to any of the risks enumerated above (for example, supply/demand imbalances or other market forces), the prices of the securities in which Merchants' Gate invests may decline substantially. In particular, purchasing assets at what may appear to be "undervalued" levels is no guarantee that these assets will not be trading at even more "undervalued" levels at a time of valuation or at the time of sale. It may not be possible to predict, or to hedge against, such "spread widening" risk.

*Small and Medium Capitalization Companies.* While the Advisor believes securities in companies with small and medium capitalizations often provide significant potential for appreciation, the securities of certain companies, particularly smaller-capitalization companies, involve higher risks in some respects than do investments in securities of larger companies. For example, prices of small-capitalization and even medium-capitalization securities are often more volatile than prices of large-capitalization securities and the risk of bankruptcy or insolvency of many smaller companies (with the attendant losses to investors) is higher than for larger, "blue-chip" companies. In addition, due to thin trading in the securities of some small-capitalization companies, an investment in those companies may be illiquid.

*Unforeseen Events.* Merchants' Gate may be adversely affected by unforeseen events involving such matters as changes in interest rates or the credit status of an issuer, forced withdrawals of securities or acquisition proposals, break-up of planned mergers, unexpected changes in relative value, short squeezes, inability to short stock or changes in tax treatment.

*Leverage and Borrowing.* While Merchants' Gate does not intend that leverage will be a component of Merchants' Gate's investment strategies, nor does Merchants' Gate expect to generally engage in substantial borrowing or margin financing, it may do so when deemed appropriate by the Advisor, including for cash management purposes. The use of leverage would, in many instances, enable Merchants' Gate to achieve a higher rate of return than would be otherwise possible. Generally, with respect to the overall portfolio of Merchants' Gate, the Advisor generally will seek to balance the amount of leverage, if any, to be employed by Merchants' Gate and the estimated long-term volatility of the portfolio. Merchants' Gate's

perception of any strategy's volatility is expected to change from time to time and the market for leverage is expected to be dynamic. Accordingly, the amount, kinds and pricing of leverage utilized with respect to such strategy, if any, will also change. If Leverage is employed, it may take the form of, without limitation, any of the financial instruments described herein, including derivative instruments which are inherently leveraged and trading in products with embedded leverage such as options, short sales, swaps and forwards.

The instruments and borrowings utilized by Merchants' Gate to leverage investments may be collateralized by Merchants' Gate's portfolio. Accordingly, Merchants' Gate may pledge its financial instruments in order to borrow additional funds or otherwise obtain leverage for investment or other purposes. The amount of borrowings which Merchants' Gate may have outstanding at any time may be substantial in relation to its capital.

Any use of leverage will allow Merchants' Gate to borrow in order to make additional investments, thereby increasing its exposure to assets, such that its total assets are greater than its capital. The use of leverage will magnify the volatility of changes in the value of the investments of Merchants' Gate. Accordingly, any event which adversely affects the value of an investment would be magnified to the extent the investment is leveraged. The cumulative effect of the use of leverage by Merchants' Gate in a market that moves adversely to its investments could result in substantial losses to Merchants' Gate, which would be greater than if Merchants' Gate were not leveraged.

*Co-Investments with Third Parties.* Merchants' Gate may co-invest with third parties through joint ventures or other entities. Such investments may involve risks in connection with such third-party involvement, including the possibility that a third-party co-venturer may have financial difficulties resulting in a negative impact on such investment; may have economic or business interests or goals that are inconsistent with those of Merchants' Gate; or may be in a position to take (or block) action in a manner contrary to Merchants' Gate's investment objectives. In those circumstances where such third parties involve a management group, such third parties may enter into compensation arrangements relating to such investments, including incentive compensation arrangements. Such compensation arrangements will reduce the returns to participants in the investments and create potential conflicts of interest between such parties and Merchants' Gate.

*Systemic Risk.* Credit risk may also arise through a default by one of several large institutions that are dependent on one another to meet their liquidity or operational needs, so that a default by one institution causes a series of defaults by the other institutions. This is sometimes referred to as a "systemic risk" and may adversely affect financial intermediaries, such as clearing agencies, clearing houses, banks, securities firms and exchanges, with which Merchants' Gate interacts on a daily basis.

*Counterparty and Custodial Risk.* To the extent that Merchants' Gate invests in swaps, "synthetic" or derivatives instruments, repurchase agreements, certain types of option or other customized financial instruments, Merchants' Gate takes the risk of non-performance by the other party to the contract. This risk may include credit risk of the counterparty and the risk of settlement default. This risk may differ materially from those entailed in exchange-traded transactions which generally are supported by guarantees of clearing organizations, daily marking-to-market and settlement, and segregation and minimum capital requirements applicable to intermediaries. Transactions entered

directly between two counterparties generally do not benefit from such protections and expose the parties to the risk of counterparty default. Merchants' Gate's use of derivatives and other techniques (such as short sales) involves certain additional risks, including: (i) dependence on the ability to predict movements in the price of the derivative instrument and (ii) imperfect correlations between movements in the assets on which the derivative is based and movements in the reference asset.

Some of the markets in which Merchants' Gate may effect its transactions are "over-the-counter" or "interdealer" markets. The participants in such markets are typically not subject to credit evaluation and regulatory oversight as are members of "exchange-based" markets. This exposes Merchants' Gate to the risk that a counterparty will not settle a transaction in accordance with its terms and conditions because of a dispute over the terms of the contract (whether or not *bona fide*) or because of a credit or liquidity problem, thus causing Merchants' Gate to suffer a loss. In addition, in the case of a default, Merchants' Gate could become subject to adverse market movements while replacement transactions are executed. Such "counterparty risk" is accentuated for contracts with longer maturities where events may intervene to prevent settlement, or where Merchants' Gate has concentrated its transactions with a single counterparty or small group of counterparties.

In addition, there are risks involved in dealing with the custodians or brokers who settle Merchants' Gate trades. Securities and other assets deposited with custodians or brokers may not be identified as being assets of Merchants' Gate and hence Merchants' Gate may be exposed to a credit risk with respect to such parties. There is a risk that any of such parties could become insolvent. Although the Advisor regularly monitors the financial condition of the counterparties it uses, if one or more of Merchants' Gate's counterparties were to become insolvent or the subject of liquidation proceedings in the United States (either under the Securities Investor Protection Act or the Bankruptcy Code), there exists the risk that the recovery of Merchants' Gate's securities and other assets from broker-dealer will be delayed or be of a value less than the value of the securities or assets originally entrusted to broker-dealer.

In addition, Merchants' Gate may use counterparties located in various jurisdictions outside the United States. Such local counterparties are subject to various laws and regulations in various jurisdictions that are designed to protect their customers in the event of their insolvency. However, the practical effect of these laws and their application to Merchants' Gate's assets are subject to substantial limitations and uncertainties. Because of the large number of entities and jurisdictions involved and the range of possible factual scenarios involving the insolvency of a counterparty, it is impossible to generalize about the effect of their insolvency on Merchants' Gate and its assets. Investors should assume that the insolvency of any counterparty would result in a loss to Merchants' Gate, which could be material.

Merchants' Gate reserves the right, in its sole discretion, to change its counterparties (including, without limitation, its brokers and/or custodians) without notice to Limited Partners. Merchants' Gate is not subject to any formal requirements regarding the credit ratings of such counterparties and, as recent developments have shown, such credit ratings may not be accurate measures of a counterparty's creditworthiness.

*Risk of Litigation or Proceedings.* Merchants' Gate, as an independent legal entity, may be subject to lawsuits or proceedings by government entities and private persons in connection with its investment activities. These lawsuits or proceedings may have an adverse effect on Merchants' Gate and otherwise involve a substantial commitment of time and significant resources and expenses.

As a general matter, the banks and dealers that provide financing to Merchants' Gate can apply essentially discretionary margin, haircut financing as well as security and collateral valuation policies. Changes by banks and dealers in such policies, or the imposition of other credit limitations or restrictions, whether due to market circumstances or government, regulatory or judicial action, may result in large margin calls, loss of financing, forced liquidations of positions at disadvantageous prices, termination of swap and repurchase agreements and cross-defaults to agreements with other dealers. Any such adverse effects may be exacerbated in the event that such limitations or restrictions are imposed suddenly and/or by multiple market participants. The imposition of any such limitations or restrictions could compel Merchants' Gate to liquidate all or part of its portfolio at disadvantageous prices, perhaps leading to a complete loss of Merchants' Gate's equity.

*Hedging Transactions.* Merchants' Gate may (but is not required to) utilize financial instruments, including forward contracts, stock index futures, commodities-related instruments, derivative positions and options, and swaps, caps, and floors, both for investment purposes and for risk management purposes in order to (i) protect against possible changes in the market value of Merchants' Gate's investment portfolios resulting from fluctuations in the markets and changes in interest rates; (ii) protect Merchants' Gate's unrealized gains in the value of its investment portfolio; (iii) facilitate the sale of any such investments; (iv) enhance or preserve returns, spreads or gains on any investment in Merchants' Gate's portfolios; (v) hedge against a directional trade; (vi) hedge the interest rate, credit or currency exchange rate on any of Merchants' Gate's financial instruments; (vii) protect against any increase in the price of any financial instruments Merchants' Gate anticipates purchasing at a later date; or (viii) act for any other reason that the Advisor deems appropriate. Merchants' Gate may also engage in short selling for hedging purposes. Merchants' Gate will not be required to hedge any particular risk in connection with a particular transaction or its portfolios generally.

The success of Merchants' Gate's hedging strategy will be subject to the Advisor's ability to correctly assess the degree of correlation between the performance of the instruments used in the hedging strategy and the performance of the investments in the portfolio being hedged. Since the characteristics of many securities change as markets change or time passes, the success of Merchants' Gate's hedging strategy will also be subject to the Advisor's ability to continually recalculate, readjust, and execute hedges in an efficient and timely manner. While Merchants' Gate may enter into hedging transactions to seek to reduce risk, such transactions may result in a poorer overall performance for Merchants' Gate than if it had not engaged in any such hedging transactions. For a variety of reasons, the Advisor may not seek to establish a perfect correlation between such hedging instruments and the portfolio holdings being hedged. Such imperfect correlation may prevent Merchants' Gate from achieving the intended hedge or expose Merchants' Gate to risk of loss. The successful utilization of hedging and risk management transactions requires skills complementary to those needed in the selection of Merchants' Gate's portfolio



holdings. Moreover, it should be noted that the portfolio will always be exposed to certain risks that cannot be hedged.

*Currency Exposure.* The Interests will be issued and generally withdrawal proceeds will be paid in U.S. Dollars. The assets of Merchants' Gate may, however, be invested in securities and other investments which are denominated in currencies other than U.S. Dollars. Accordingly, the value of such assets may be affected favorably or unfavorably by fluctuations in currency rates. The Advisor may hedge the non-U.S. currency exposure of Merchants' Gate by entering into currency hedging transactions, such as treasury locks, forward contracts, futures contracts, cross-currency swaps or by shorting non-U.S. debt. However, the assets of Merchants' Gate will necessarily be subject to foreign exchange risks. In addition, prospective investors whose assets and liabilities are predominately in other currencies should take into account the potential risk of loss arising from fluctuations in value between the U.S. Dollar and other currencies.

To the extent unhedged, the value of Merchants' Gate's positions in non-U.S. investments will fluctuate with U.S. Dollar exchange rates as well as with the price changes of the investments in the various local markets and currencies. In such cases, an increase in the value of the U.S. dollar compared to the other currencies in which Merchants' Gate makes investments will reduce the effect of any increases and magnify the effect of any decreases in the prices of Merchants' Gate's financial instruments in their local markets and may result in a loss to Merchants' Gate. Conversely, a decrease in the value of the U.S. dollar will have the opposite effect on Merchants' Gate's non-U.S. Dollar investments.

*Liquidity and Market Characteristics.* In some circumstances, investments may be relatively illiquid making it difficult to acquire or dispose of them at the prices quoted on the various exchanges or by various dealers. At times it may be difficult to obtain price quotes at all. Accordingly, Merchants' Gate's ability to respond to market movements may be impaired and Merchants' Gate may experience adverse price movements upon liquidation of its investments. Settlement of transactions may be subject to delay and administrative uncertainties.

**ITEM 9**  
**DISCIPLINARY INFORMATION**

There are no legal or disciplinary events that are material to a client's or prospective client's evaluation of Merchants' Gate's advisory business or the integrity of Merchants' Gate's management.

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

A. Broker-Dealer Registration Status.

Merchants' Gate is not registered nor does it have an application pending to register with the SEC as a broker-dealer. Merchants' Gate's CCO is a registered representative of a broker-dealer unaffiliated with Merchants' Gate, and Merchants' Gate does not retain such broker-dealer for services on behalf of the Fund.

B. Futures Commission Merchant, Commodity Pool Operator or Commodity Trading Adviser Registration Status.

Merchants' Gate and its management persons are not registered as, and do not have any application to register as, futures commission merchants, commodity pool operators, commodity trading advisors or associated persons of the foregoing entities.

C. Material Relationships or Arrangements with Industry Participants.

Merchants' Gate serves as the investment manager of the Fund. Merchants' Gate has material business relationships with the General Partner of the Fund.

D. Material Conflicts of Interest Relating to Other Investment Advisers.

Merchants' Gate does not recommend or select other investment advisers for its clients.

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

A. Code of Ethics.

Merchants' Gate's has implemented and maintains a formal Code of Ethics (the "Code") that incorporates principles that all employees are obligated to uphold. These principles are designed not only to help Merchants' Gate fulfill its fiduciary obligations, but also to instill in employees Merchants' Gate's commitment to honesty, integrity and professionalism. The Code incorporates the following general principles, among others, that all employees are expected to uphold:

- employees must at all times place the interests of clients first;
- employees must conduct all personal securities transactions in a manner consistent with the Code and seek to avoid both conflicts of interest and the appearance of any conflicts of interest; and
- employees may not take inappropriate advantage of their positions.

The Code includes, among other things, provisions relating to personal securities trading, outside business activities, the acceptance of significant gifts, reporting of certain gifts and business entertainment items, and political and charitable contributions. All Merchants' Gate employees must acknowledge annually that they understand and agree to the terms of the Code.

The Code is distributed to each employee at the time of hire. The Code is supplemented with training materials upon hire of a new employee and periodically thereafter. Affiliated persons must provide Merchants' Gate with securities holdings reports upon commencement of employment and thereafter provide quarterly transactions reports and certifications of compliance with the Code on an annual basis.

Affiliated persons may not serve on the boards of for-profit enterprises without Merchants' Gate prior approval.

Clients and prospective clients may obtain a copy of the Code by addressing a request for such Code to Merchants' Gate Chief Compliance Officer, 135 East 57<sup>th</sup> Street, 15th Floor, New York, New York 10022.

B. Securities in which Merchants' Gate or a Related Person has a Material Financial Interest.

Neither Merchants' Gate nor any of its related persons recommends to clients, or buys or sells for client accounts, securities in which Merchants' Gate or any of its related persons has a material financial interest.

C. Investing in Securities that Merchants' Gate or a Related Person Recommends to Clients.

The Code generally prohibits employees from investing in single-name publicly traded stocks and bonds ("Covered Securities"). Merchants' Gate believes that this prohibition effectively addresses the material potential conflict of interest with our clients that may arise because of personal trading activities. In addition, employees must generally pre-clear sales of Covered Securities including ETFs from their personal accounts. Merchants' Gate also limits the ability of employees to participate in private placements.

Merchants' Gate, its affiliates and its employees may give advice or take action for their own accounts that may differ from, conflict with or be adverse to advice given or action taken for clients. These activities may adversely affect the prices and availability of other securities or instruments held by or potentially considered for one or more clients. Potential conflicts also may arise because Merchants' Gate and its personnel may have investments in the Fund.

Merchants' Gate has established policies and procedures to monitor and resolve conflicts with respect to investment opportunities in a manner it deems fair and equitable, including the restrictions placed on personal trading in the Code, as described above, and regular monitoring of employee transactions and trading patterns for actual or perceived conflicts of interest, including those conflicts that may arise as a result of personal trades in the same or similar securities made at or about the same time as client trades.

## ITEM 12 BROKERAGE PRACTICES

### A. Factors Considered in Selecting or Recommending Broker-Dealers for Client Transactions.

The securities transactions of the Fund can be expected to generate a substantial amount of brokerage commissions and other compensation, including clearing fees and charges, all of which will be paid by the Fund. Merchants' Gate has complete discretion in deciding what brokers and dealers the Fund will use and in negotiating the rates of compensation the Fund will pay. Merchants' Gate selects brokers and dealers on the basis of best execution and in consideration of relevant factors, including, but not limited to, price quotes; the size of the transaction and ability to find liquidity; the broker-dealer's promptness of execution; confidentiality considerations; the nature of the market for the financial instrument; the timing of the transaction; difficulty of execution; the broker-dealer's expertise in the specific financial instrument or sector in which the Fund seeks to trade; the extent to which the broker-dealer makes a market in the financial instrument involved or has access to such markets; the broker-dealer's skill in positioning the financial instruments involved; the broker-dealer's financial stability; reputation for diligence, fairness and integrity; quality of service rendered by the broker-dealer in other transactions for Merchants' Gate; the quality and usefulness of research services and investment ideas presented by the broker-dealer or third parties; the broker-dealer's willingness to correct errors; the broker-dealer's ability to accommodate any special execution or order handling requirements that may surround the particular transaction; and other factors deemed appropriate by Merchants' Gate. The Advisor need not solicit competitive bids and does not have an obligation to seek the lowest available commission cost or spread.

Accordingly, if Merchants' Gate concludes that the commissions charged by a broker, or the spreads applied by a dealer, are reasonable in relation to the quality of services rendered by such broker or dealer (including, without limitation, the value of the brokerage and research products or services provided by such broker or dealer), the Fund, may pay commissions to, or be subject to spreads applied by, such broker-dealer that are greater than those another broker-dealer might charge or apply.

Merchants' Gate maintains policies and procedures to review the quality of executions.

#### 1. *Research and Other Soft Dollar Benefits.*

Brokerage and research-related goods and services provided by brokers and dealers through which portfolio transactions for the Fund are executed, settled and cleared may include, but are not limited to, research reports on particular industries and companies, economic surveys and analyses, recommendations as to specific securities, certain research services, and other goods and services providing lawful and appropriate assistance to us in regards to our investment decision-making responsibilities on behalf of the Fund and related accounts (collectively "soft dollar items"). Soft dollar items may be provided directly by brokers and dealers, by third parties at the direction of brokers and dealers or purchased on behalf of the Fund with credits or

rebates provided by brokers and dealers. Soft dollar items may arise from over-the-counter principal transactions, as well as exchange-traded agency transactions.

From time to time, Merchants' Gate may pay a broker-dealer commissions (or markups or markdowns with respect to certain types of riskless principal transaction) for effecting transactions in excess of that which another broker-dealer might have charged for effecting the transaction in recognition of the value of the brokerage and research services provided by the broker-dealer. The use of commissions or "soft dollars" if any, generated by the Fund through agency and certain riskless principal transactions to pay for brokerage and research-related products or services, if any, will fall within the safe harbor created by Section 28(e) of the Securities Exchange Act of 1934, as amended. Under Section 28(e), brokerage and research-related products or services obtained with soft dollars generated by one client may be used by Merchants' Gate to service other clients. Soft dollars generated in respect of futures, currency and derivatives transactions and principal transactions (that are not riskless principal transactions) do not generally fall within the safe harbor created by Section 28(e) and will be utilized only with respect to brokerage- and research-related products and services for the benefit of the account generating such soft dollars.

When Merchants' Gate uses client brokerage commissions (or markups or markdowns) to obtain research or other products or services, Merchants' Gate may receive a benefit because it does not have to produce or pay for such products or services (unless the cost of such products or services is to be otherwise paid for by the Fund). Merchants' Gate may have an incentive to select or recommend a broker or dealer based on our interest in receiving research or other soft dollar items, rather than on our clients' interest in receiving most favorable execution.

Merchants' Gate considers the amount and nature of research and research services, if any, provided by brokers and dealers, as well as the extent to which such services are relied upon, and attempts to allocate a portion of the brokerage business of the Fund on the basis of that consideration. Brokers and dealers sometimes suggest a level of business they would like to receive in return for the various products and services they provide. Actual brokerage business received by any broker or dealer may be less than the suggested allocation, but can (and often does) exceed the suggested level, because total brokerage is allocated on the basis of all of the considerations described above. In no case will Merchants' Gate make binding commitments as to the level of brokerage commissions it will allocate to a broker or dealer, nor will it commit to pay cash if any informal targets are not met. A broker or dealer will not be excluded from executing transactions for the Fund because it has not been identified as providing soft dollar items.

## *2. Brokerage for Client Referrals.*

Neither Merchants' Gate nor any related person receives client referrals from any broker or dealer or third party. However, from time to time, prime brokers may assist the Fund in raising additional funds from investors, and representatives of Merchants' Gate may speak at conferences and programs sponsored by such brokers for investors interested in investing in hedge funds. Through such "capital introduction" events, prospective investors in the Fund would have the opportunity to meet with Merchants' Gate. Currently, Merchants' Gate does not compensate any broker for organizing such events or for any investments ultimately made by

prospective investors attending such events, nor does Merchants' Gate anticipate doing so in the future. As discussed above, subject to best execution, Merchants' Gate may consider, among other things, capital introduction and marketing assistance with respect to investors in the Fund in selecting or recommending brokers or dealers for the Fund. While such events and other services provided by a prime broker may influence us in deciding whether to use such broker in connection with brokerage, financing and other activities of the Fund, Merchants' Gate will not commit to allocate a particular amount of brokerage to a broker in any such situation.

### 3. *Directed Brokerage.*

Merchants' Gate does not recommend, request, require or permit a client to direct Merchants' Gate to execute transactions through a specified broker or dealer.

### B. Trade Allocation and Aggregation Policies and Procedures.

Certain other investment funds sponsored by Merchants' Gate in which the Fund will have no interest (such other clients and funds, "Other Accounts") that may be formed in the future, may have investment objectives, programs, strategies and positions that are similar to, or may conflict with, those of the Fund, or may compete with, or have interests adverse to, the Fund. The portfolio strategies employed by Merchants' Gate for Other Accounts could conflict with the transactions and strategies employed by Merchants' Gate in managing the Fund and may affect the prices and availability of the securities and instruments in which the Fund invests. Conversely, participation in specific investment opportunities may be appropriate, at times, for both the Fund and Other Accounts.

It is the policy of Merchants' Gate to allocate investment opportunities fairly and equitably over time. When it is determined by Merchants' Gate that it would be appropriate for the Fund and one or more Other Accounts which may be formed in the future to participate in an investment opportunity, Merchants' Gate will ordinarily seek to execute orders for all such investment vehicles on an equitable basis, to be allocated fairly among those accounts. The Advisor determines for which of its accounts participation in a respective investment is considered appropriate and the allocation of such investment among such accounts, taking into account, among other things, such factors as (a) the relative amounts of capital available for new investments; (b) relative exposure to market trends; (c) the investment programs and portfolio positions of all such investment vehicles; (d) whether the risk-return profile of the proposed investment is consistent with the account's objectives; (e) the potential for the proposed investment to create an imbalance in the account's portfolio; (f) liquidity requirements; (g) potentially adverse tax consequences; (h) regulatory restrictions that would or could limit an account's ability to participate in a proposed investment; and (i) the need to adjust the risk in the account's portfolio. Such considerations may result in allocations among the Fund and one or more Other Accounts on an other than a *pari passu* basis. Orders may be combined for the Fund and the Other Accounts, and if any order is not filled at the same price, they may be allocated on an average price basis or on any other basis deemed fair and equitable by Merchants' Gate. Similarly, if such an order cannot be fully executed under prevailing market conditions, securities may be allocated on a basis that the General Partner or its affiliates consider equitable.



## **ITEM 13**

### **REVIEW OF ACCOUNTS**

A. Frequency and Nature of Review of Client Accounts or Financial Plans.

Prior to being made, all investments are carefully reviewed and approved by investment professionals of Merchants' Gate, including Merchants' Gate's Portfolio Manager. Merchants' Gate does not conduct formal periodic reviews of client accounts. The Advisor believes that such formal reviews are not necessary in light of the direct regular management of the account of the Fund, by Merchants' Gate's Portfolio Manager and other investment professionals.

B. Factors Prompting Review of Client Accounts Other than on a Periodic Review.

A review of a client account may be triggered by unusual activity or special circumstances.

C. Content and Frequency of Account Reports to Clients.

It is anticipated that investors in the Fund will periodically receive the following written and/or electronic reports: (1) monthly performance estimates and exposure reports; (2) monthly statements of net asset value; and (3) an annual report including audited financial statements with a report thereon by the independent auditors. Investors in the Fund will receive annual Schedules K-1 and, upon request, a tax estimate on an annual basis. Merchants' Gate may also provide certain investors with more detailed information upon request.

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

A. Economic Benefits for Providing Services to Clients.

Merchants' Gate does not receive economic benefits from non-clients for providing investment advice and other advisory services.

B. Compensation to Non-Supervised Persons for Client Referrals.

Neither Merchants' Gate nor any related person directly or indirectly compensates any person who is not a supervised person, including third-party solicitors, for client referrals. Any such arrangements in the future will be entered into consistent with applicable regulatory requirements, including the disclosure to the prospective client of the arrangement at the time of the solicitation. However, Merchants' Gate may receive client referrals from brokers providing services to the Fund. See Item 12 (Brokerage Practices) above.

## **ITEM 15**

### **CUSTODY**

All client assets are held in custody by unaffiliated broker-dealers or banks that serve as qualified custodians; however, Merchants' Gate may be deemed to have custody of client funds and securities because it or its affiliate has the authority to obtain client funds or securities, for example by deducting advisory fees from a client's account or otherwise withdrawing funds from a client's account. Account statements related to the Fund are sent by qualified custodians to Merchants' Gate. However, the investors of the Fund will not receive statements from the qualified custodians.

Merchants' Gate is subject to Rule 206(4)-2 under the Advisers Act (the "Custody Rule"). However, it is not required to comply (or is deemed to have complied) with certain requirements of the Custody Rule with respect to the Fund because it complies with the provisions of the so-called "Pooled Vehicle Annual Audit Exception," which, among other things, requires that such Fund be subject to audit at least annually by an independent public accountant that is registered with, and subject to regular inspection by, the Public Company Accounting Oversight Board, and requires that each Fund distribute its audited financial statements to all investors within 120 days of the end of its fiscal year.

**ITEM 16**  
**INVESTMENT DISCRETION**

Merchants' Gate has been granted discretionary authority to manage the securities accounts of the Fund pursuant to an investment management agreement and the Fund pursuant to the Fund's limited partnership agreement. Merchants' Gate's investment decisions and advice with respect to the Fund are subject to the Fund's constituent documents. Any limitations on Merchants' Gate's discretionary authority are described in the Fund's confidential offering memorandum.

**ITEM 17**  
**VOTING CLIENT SECURITIES**

Merchants' Gate has the authority to cast all proxy votes. Merchants' Gate has adopted a written proxy voting policy, as required by the Advisers Act. The policy provides that the Advisor will act in the best interests of our client funds, as determined by Merchants' Gate in good faith, in determining whether and how to vote on any proxy voting matter. As a general practice, Merchants' Gate will vote proxies on a case-by-case basis. Prior to voting a proxy, the relevant employees of Merchants' Gate will make a determination, in their opinion, as to what vote if any, is in the best interest of its clients. Merchants' Gate maintains written records of the proxy vote on each occasion a proxy is voted. Merchants' Gate's Portfolio Manager and Chief Compliance Officer will consult with each other concerning the best method to resolve any actual or apparent conflict between the interests of Merchants' Gate and its clients in a manner that affords priority to the interests of Merchants' Gate's clients taken as a whole. In order to facilitate the proxy voting process, Merchants' Gate may from time to time retain a third party proxy voting service to vote proxies in a timely manner for our client funds.

Investors may obtain a copy of the policy and information on how Merchants' Gate voted client securities by addressing a request for such policy or information to Merchants' Gate's Chief Compliance Officer, 135 East 57<sup>th</sup> Street, 15th Floor, New York, New York 10022.

**ITEM 18**  
**FINANCIAL INFORMATION**

Merchants' Gate is not required to include a balance sheet for its most recent fiscal year, is not aware of any financial condition reasonably likely to impair its ability to meet contractual commitments to clients, and has not been the subject of a bankruptcy petition at any time during the past ten years.