



# KALEIDOSCOPE CAPITAL

## **PART 2A OF FORM ADV FIRM BROCHURE**

**March 22, 2018**

**This brochure provides information about the qualifications and business practices of Kaleidoscope Capital, LP ("Kaleidoscope Capital"). If you have any questions about the contents of this brochure, please contact us at (617) 765–2064. The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission or by any state securities authority.**

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

## ITEM 2 MATERIAL CHANGES

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This brochure was updated on March 22, 2018 in order to provide information that is supplemental to the previous version dated March 29, 2017. Material updates include the following:

- Discussion of performance allocations were updated to include an additional sub-class of interest applicable to the Kaleidoscope Spectrum Fund (Item 5). Sub-class A-3 was added with an applicable performance incentive of 15%.
- Discussion of performance allocations were updated to include an additional benchmark applicable to the Kaleidoscope Prism Fund (Item 5). Sub-class A-5 was added with an Emerging Market Equity benchmark.
- Data costs were added to the discussion of additional expenses (Item 5).
- The discussion of withdrawal fees was updated to clarify preferential terms (Item 5).
- The minimum investment applicable to the Kaleidoscope Spectrum Fund was increased from \$15 million to \$25 million (Item 7).
- The description of the Kaleidoscope Prism Fund strategy was expanded (Item 8).
- Kaleidoscope's Trade Error Policy was added to the description of Brokerage Practices (item 12).

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## ITEM 4 ADVISORY BUSINESS

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Kaleidoscope Capital, LP (“Kaleidoscope Capital” or the “Investment Manager”), was established in 2015. Kaleidoscope Capital is headquartered in Boston, Massachusetts and provides investment management services on a discretionary basis to privately offered pooled investment vehicles (the “Kaleidoscope Funds” or the “Funds”). Kaleidoscope Capital’s principal owners are its founding partners Nick Nanda and Kai Wu.

The Kaleidoscope Funds are organized into two master-feeder structures. The first structure was established in 2015 and consists of (i) Kaleidoscope Prism Fund, LP (the “Prism Onshore Feeder”), a Delaware limited partnership, (ii) Kaleidoscope Prism Offshore Fund, Ltd (the “Prism Offshore Feeder”), a Cayman Islands exempted company, (iii) Kaleidoscope Prism Master Fund, LP (the “Prism Master Fund”), a Cayman Islands exempted limited partnership (collectively, “Prism” or the “Prism Funds”).

The second structure was established in 2016 and consists of (i) Kaleidoscope Spectrum Fund, LP (the “Spectrum Onshore Feeder”), a Delaware limited partnership, (ii) Kaleidoscope Spectrum Offshore Fund, Ltd (the “Spectrum Offshore Feeder”), a Cayman Islands exempted company, (iii) Kaleidoscope Spectrum Master Fund, LP (the “Spectrum Master Fund”), a Cayman Islands exempted limited partnership (collectively, “Spectrum” or the “Spectrum Funds”).

Kaleidoscope Capital provides investment management and advisory services to the Kaleidoscope Funds in accordance with the terms set forth in investment management agreements with the Funds and pursuant to the investment objectives, strategies and restrictions as set forth in each of the relevant Funds’ offering documents. Kaleidoscope Capital does not tailor its advisory service to the individual needs of investors in the Funds and investors in the Funds may not impose restrictions on investing in any particular security or type of security.

As of December 31, 2017, Kaleidoscope Capital manages client assets totaling \$326.9 million, all of which are managed on a discretionary basis.

## ITEM 5 FEES AND COMPENSATION

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Kaleidoscope Capital and Kaleidoscope GP LP receive fees and compensation from the Kaleidoscope Funds as set forth in each Fund's offering memorandum. Kaleidoscope Capital charges the Funds an asset-based investment management fee. In addition, each of the Funds' offering documents describe the circumstances in which a performance based incentive allocation (a "Performance Allocation") is charged. Performance allocations are based on capital appreciation net of management fees and subject to (i) a benchmark (or "Hurdle Rate") as discussed below, and (ii) a loss carryforward mechanism commonly referred to as a "High Water Mark".

Kaleidoscope Capital does not accept any other compensation in connection with its advisory business. Management fees are charged each quarter in advance based on the value of the assets of each of the Funds as of the first business day of each calendar quarter. A pro rata portion of the management fee is paid in advance for investments made between calendar quarters, based on the number of remaining months in the quarter. Kaleidoscope Capital receives the management fee each quarter by instructing the administrator of the Funds to deduct the applicable management fee from the Fund accounts.

The management fees and performance allocations described below may be waived for investors that are members, employees or affiliates of Kaleidoscope Capital and relatives of such persons. The management fees and performance allocations have been waived for current investors who are Kaleidoscope Capital employees.

In addition to the management fee and performance allocations described below, Fund investments are also subject to additional fees, expenses and transaction costs relating to the Fund investments (including, without limitation, expenses related to the investment of the Fund assets such as brokerage commissions and other transaction costs, data costs (including without limitation, costs and fees of Bloomberg related execution and data products and services, subscription fees and other costs of third party databases and other data sources, and costs and fees of other web based services), clearing and settlement charges, custodial fees, margin and interest expenses on debit balances); expenses of professionals providing services to the Funds, including legal, audit and tax preparation expenses; accounting and administration fees and expenses; insurance expenses, including costs of any liability insurance obtained on behalf of the Funds (including, without limitation, directors and officers insurance), organizational expenses, regulatory costs and expenses (including filing and license fees), and other fees described in each Fund's offering memorandum.

### **Management Fee and Performance Allocation – Prism Funds**

Kaleidoscope Capital receives compensation for managing the Prism Fund investments. Investors in the Prism Funds are charged a management fee based on the capital account balance as of the beginning of each calendar quarter, in an amount equal to 0.1875% (0.75% annualized).

Kaleidoscope GP LP will also receive an annual performance-based incentive allocation from the Prism Funds in an amount equal to 20% of net capital appreciation in excess of an investor's benchmark.

Investors in the Prism Funds select from one of five benchmarks: (i) the S&P 500® Total Return Index (Bloomberg Ticker: SPXT) less 2.3 basis points (0.023%) per month (the "Domestic Equity Benchmark"), (ii) the MSCI EAFE Net Total Return Index (Bloomberg Ticker: NDDUEAFE) less 2.3 basis points (0.023%) per month (the "International Equity Benchmark"), (iii) the Citigroup 3-Month Treasury Bill Index (Bloomberg Ticker: SBMMTB3 (the "Cash Benchmark"), (iv) a composite benchmark consisting of 25% Domestic Equity, 25% International Equity, and 50% Cash (the "Blend Benchmark"), and (v) the MSCI Emerging Net Total Return Index (Bloomberg Ticker: NDUEEGF) less 3.3 basis points (0.033%) per month (the "Emerging Equity Benchmark").

The performance allocation is effectively determined based on the relative performance of an investor's capital account as compared to the performance of the relevant benchmark. Kaleidoscope GP LP will receive the performance allocation in an amount equal to 20% of the positive relative performance at the end of each fiscal

year; provided, however, that no performance allocation for a particular investment is made unless the cumulative relative performance is positive (the “High Water Mark”). For the avoidance of doubt, an investment may incur a performance allocation even when the performance of such investment is negative.

#### **Management Fee and Performance Allocation – Spectrum Funds**

Kaleidoscope Capital receives compensation for managing the Spectrum Fund investments. Investors in the Spectrum Funds are charged a management fee based on the capital account balance as of the beginning of each calendar quarter, in an amount equal to 0.25% (1.00% annualized).

Kaleidoscope GP LP will also receive annual performance-based incentive allocations from the Spectrum Funds, calculated as a percentage of net capital appreciation in excess of the performance of the Citigroup 3-Month Treasury Bill Index (the “Hurdle Rate”).

There are three sub-classes of investment in the Spectrum Funds: A-1, A2 and A-3. Investments in the A-1 sub-class were made on or before January 1, 2017 and do not incur a performance allocation. Investments in sub-class A-2 and A-3 incur performance fees if in any fiscal year the net return of such investment exceeds the Hurdle Rate. Kaleidoscope GP LP will receive a performance allocation at the end of such fiscal year in an amount equal to 10% of such excess for A-2 interests, or 15% of such excess for A-3 interests. No performance allocation for a particular investment is made unless the cumulative relative performance is positive (the “High Water Mark”).

#### **Terms of Withdrawal Fees Applicable to Investors in the Kaleidoscope Funds**

Investments in the Kaleidoscope Funds may incur a withdrawal charge, commonly referred to as a “soft lock”. Investors in the Kaleidoscope Funds may generally withdraw capital as of the last day of each calendar quarter, subject to the withdrawal gate and other withdrawal restrictions; provided, however, if such withdrawal date occurs prior to the end of the last business day of the twelfth (12th) calendar month following the date on which such capital account was established, the proceeds in respect of any such withdrawal will be subject to a withdrawal charge equal to four percent (4%) of the amount permitted to be withdrawn. Withdrawals by an investor that has made more than one capital contribution are made on a “first in-first out” basis. Any withdrawal charge applied with respect to a withdrawal is credited pro rata to the investors in the master fund for which the withdrawal is requested.

Requests for withdrawals must be provided in writing at least sixty (60) days prior to the requested withdrawal date, stating the investor’s intention to withdraw and the amount of such withdrawal, if less than the entire balance in such investor’s capital account. The maximum withdrawal percentage per calendar quarter is 25%; provided, however, that on each of the next three successive withdrawal dates for such capital account, the maximum withdrawal percentage will be 33-1/3%, and then 50% and then 100%;

The following preferential terms apply to investments in the Prism Fund and the Spectrum Fund A-1 sub-class. These terms do not apply to Spectrum Fund A-2 and A-3 sub-classes. For each applicable capital account that has been maintained for:

- (i) at least thirty six (36) calendar months but less than sixty (60) calendar months, the maximum withdrawal percentage is 33-1/3%, provided, however, that on each of the next two successive withdrawal dates for such capital account, the maximum withdrawal percentage will be 50% and then 100%; or

at least sixty (60) calendar months, the maximum withdrawal percentage is 50%, provided, however, that on the next withdrawal date for such capital account, the maximum withdrawal percentage will be 100%.

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

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Kaleidoscope Capital and its investment personnel provide investment management and advisory services to the Funds, each of which is charged performance-based fees in addition to asset-based fees. Each Fund incurs varying levels of performance-based and asset-based fees. A potential exists for Kaleidoscope Capital to favor the Fund from which its affiliates receive a larger performance based fee. The Investment Manager may, for example, be incentivized to allocate profitable trades to the higher fee-paying Fund.

Kaleidoscope Capital has adopted and implemented policies and procedures intended to address the conflicts of interest inherent in managing multiple accounts and to allocate investment opportunities in a fair and equitable manner. Kaleidoscope Capital's investment process is systematic and maintains a pre-trade allocation policy. Kaleidoscope's execution system employs a fair and equitable turn-based approach to the order of executions in instances where transactions in the same security and buy/sell direction are suitable for multiple Funds. The allocation policy is tested quarterly and the trade population is analyzed to confirm fair and equitable allocations. The Investment Manager maintains documentation of the testing procedure.

Kaleidoscope Capital does not aggregate multiple trade orders to transact in the same security on behalf of multiple Funds. Kaleidoscope Capital's allocation policy is further discussed in Item 12.

## **ITEM 7 TYPES OF CLIENTS**

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Kaleidoscope Capital's clients consist of the Funds. Investors in the Funds consist primarily of endowments, foundations, family offices, high net worth individuals and employees or affiliates of Kaleidoscope Capital. The minimum amount for an initial investment in the Prism Funds is USD \$15 million. The minimum amount for an initial investment in the Spectrum Funds is USD \$25 million. The minimum investment amounts may be waived for investors that are members, employees, strategic partners or affiliates of Kaleidoscope Capital. Such waivers have been made for current investors who are members and strategic partners.



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

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### Methods of Analysis

Kaleidoscope Capital utilizes systematic and quantitative processes to make investment decisions and recommendations. Kaleidoscope makes investment decisions in the context of both security selection and portfolio construction. Each of the strategies makes use of Exchange Traded Funds (“ETFs”) and US Treasury Securities, as well as Futures, Options on Futures, and Equity Index Options across a variety of geographies and asset classes, including: Equity, Fixed Income, Currencies and Commodities.

The strategies used and the percentage of the Fund’s capital invested in each asset class may vary greatly over time, as determined by the Investment Manager. In time, the Investment Manager expects to broaden the scope of investment activity to include other securities, including, but not limited to stocks, swaps, currency forwards as well as options on these assets.

### Investment Strategies of the Prism Fund

The Prism Fund seeks to provide both (i) an investment return equal to the return of an investor’s benchmark (the “Benchmark Program”) and (ii) an additional excess investment return (the “Excess Return Program”). The Benchmark Program attempts to minimize costs and tracking error while gaining exposure to the relevant benchmark of each sub-class. The Excess Return Program employs a systematic long-short investment program and attempts to achieve its investment objective by constructing a portfolio of uncorrelated risk exposures. The strategy analyzes every asset in its investable universe as a bundle of systemic and idiosyncratic risks. By trading in long and short pairs, the strategy attempts to isolate idiosyncratic risks and construct a portfolio of uncorrelated risk exposures.

### Investment Strategies of the Spectrum Fund

The Spectrum Fund employs a systematic long-short investment program and attempts to achieve its investment objective by constructing a portfolio of systemic risk factors inherent in options markets. The strategy employs quantitative methods to evaluate the value of options contracts. The strategy will seek to buy options it finds to be undervalued and to sell options it finds to be overvalued.

### Material Risks

Investing in securities involves risk of loss. An investment in the Funds may be deemed speculative and is not intended as a complete investment program. The investment strategies are designed only for experienced and sophisticated persons who are able to bear the risk of the substantial impairment or loss of their investment. The following does not intend to describe all possible risks of such investments.

**Investment and Trading Risks.** An investment in the Funds involves a high degree of risk, including the risk that the entire amount invested may be lost. No guarantee or representation is made that the Fund investment programs will be successful. The Investment Manager will be investing substantially all of the Funds’ assets in securities and instruments, which may be particularly sensitive to economic, market, industry, regulatory and other variable conditions. The markets in which the Investment Manager expects to invest have recently experienced and continue to experience significant volatility and losses. No assurance can be given as to when or whether adverse events might occur that could cause immediate and significant losses to the Funds.

**Overpriced and Undervalued Options.** The Funds intend to achieve their investment objectives by selling options that the Investment Manager believes are overpriced across all major asset classes (including, but not limited to, equities, bonds, currencies and commodities). The Funds may also purchase underpriced options as a hedge,

depending on the opportunity set and market environment. Opportunities in overpriced or underpriced options may arise for various reasons, which may include market inefficiencies or a lack of wide recognition of the potential impact (positive or negative) that specific events or trends may have on the value of an option. The identification of investment opportunities in overpriced and/or underpriced options is a difficult task, and there is no assurance that such opportunities will be successfully recognized or acquired. While such investments offer the opportunities for above-average capital appreciation, these investments involve a high degree of financial risk and can result in substantial losses.

**Risks of Investments in Options.** Investing in options can provide greater potential for profit or loss than an equivalent investment in the underlying asset. The value of an option may decline because of a change in the value of the underlying asset relative to the strike price, the passage of time, changes in the market's perception as to the future price behavior of the underlying asset, or any combination thereof. In the case of the purchase of an option, the risk of loss of an investor's entire investment (i.e., the premium paid plus transaction charges) reflects the nature of an option as a wasting asset that may become worthless when the option expires. Where an option is written or granted (i.e., sold) uncovered, the seller may be liable to pay substantial additional margin, and the risk of loss is unlimited, as the seller will be obligated to deliver, or take delivery of, an asset at a predetermined price which may, upon exercise of the option, be significantly different from the market value. Currently, the Funds focus on listed instruments but in due course it may trade OTC instruments. Over-the-counter options ("OTC") generally are not assignable except by agreement between the parties concerned, and no party or purchaser has any obligation to permit such assignments. The over-the-counter market for options is relatively illiquid, particularly for relatively small transactions.

**Put and Call Options.** The Funds write and sell covered or uncovered call and put option contracts. It is anticipated that the Funds will include long/short positions in options on equity indices and options on futures. The Funds may also purchase exchange-listed and OTC put and call options. Investing in options can provide greater potential for profit or loss than an equivalent investment in the underlying asset. The value of an option may decline because of a change in the value of the underlying asset relative to the strike price, the passage of time, changes in the market's perception as to the future price behavior of the underlying asset, or any combination thereof. In the case of the purchase of an option, the risk of loss of an investor's entire investment (i.e., the premium paid plus transaction charges) reflects the nature of an option as a wasting asset that may become worthless when the option expires.

A call option gives the purchaser of the option the right to buy, and obligates the writer to sell, the underlying investments at a stated exercise price at any time prior to the expiration of the option. Similarly, a put option gives the purchaser of the option the right to sell, and obligates the writer to buy, the underlying investments at a stated exercise price at any time prior to the expiration of the option. Options written by the Funds may be wholly or partially covered (meaning that the portfolio holds an offsetting position) or uncovered. Options on specific investments may be used by the Funds to seek enhanced profits with respect to a particular investment. Alternatively, they may be used for various defensive or hedging purposes. For example, they may be used to protect against a future adverse change in the market price of particular portfolio investments held by the Funds without requiring a sale of the investments.

Use of put and call options may result in losses to the Funds, force the sale or purchase of portfolio investments at inopportune times or for prices higher than (in the case of put options) or lower than (in the case of call options) current market values, limit the amount of appreciation the Funds can realize on their investments or cause the Fund to hold an investment it might otherwise sell. For example, a decline in the market price of a particular investment could result in a complete loss of the amount expended by the Fund to purchase a call option (equal to the premium paid for the option and any associated transaction charges). An adverse price movement may result in unanticipated losses with respect to covered options sold by the Funds. The use of uncovered option writing techniques may entail greater risks of potential loss to the Funds than other forms of options transactions. For example, a rise in the market

price of the underlying investment will result in the Funds realizing a loss on the calls written, which would not be offset by the increase in the value of the underlying investments to the extent the call option position was uncovered.

**Futures Contracts.** The value of futures depends upon the price of the securities, commodities, instruments, indices or other financial measures underlying them. The prices of futures are volatile, and price movements of futures contracts can be influenced by, among other things, interest rates, inflation, foreign exchange 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 the positions trade or of clearinghouses or futures commission merchants. Futures positions may be illiquid because certain 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 the Funds from promptly liquidating unfavorable positions and subject the Funds to substantial losses or could prevent the Funds from entering into desired trades. In extraordinary circumstances, a futures exchange, the CFTC or another similar non-U.S. regulatory body or agency could suspend trading in a particular futures contract, or order liquidation or settlement of all open positions in such contract.

**Forward Trading.** The Funds may enter into forward contracts with counterparties. Forward contracts and options thereon, unlike futures contracts, are not traded on exchanges and are not standardized; rather banks and dealers act as principals in these markets, negotiating each transaction on an individual basis. Forward and “cash” trading is substantially unregulated; there is no limitation on daily price movements and speculative position limits are not applicable. The principals who deal in the forward markets are not required to continue to make markets in the currencies and commodities they trade and these markets can experience periods of illiquidity, sometimes of significant duration. There have been periods during which certain participants in these markets have refused to quote prices for certain currencies or commodities or have quoted prices with an unusually wide spread between the price at which they were prepared to buy and that at which they were prepared to sell. Disruptions can occur in any market traded by the Investment Manager due to unusually high trading volume, political intervention or other factors. The imposition of controls by governmental authorities might also limit such forward (and futures) trading to less than that which the Investment Manager would otherwise recommend, to the possible detriment of the Funds. Market illiquidity or disruption could result in major losses to the Funds.

**Futures Commission Merchants.** The Funds enter into transactions to purchase, hold, sell, clear and settle investments, with or through futures commission merchants (“FCMs”). In connection with their role accepting and soliciting orders for futures contracts, options for futures contracts and swaps, FCMs are required to be registered with the CFTC and are subject to CFTC rules and regulations, including with respect to minimum capital requirements, segregation of customer accounts, margin lending rules, customer disclosure requirements and filing requirements. FCMs are also subject to the rules and regulations of the various clearinghouses and exchanges of which they are members. Investments may also be adversely affected if an FCM with which the Funds transact decides to terminate its relationship with the Funds or call in any margin loans extended to the Funds. As active participants in the financial markets, FCMs are also subject to systemic risk as well as significant counterparty risk. A political or economic event affecting other participants in U.S. or global financial and commodities markets could have an adverse effect on the FCM’s financial viability and/or ability to successfully complete and execute transactions.

**Foreign Exchange.** Spot and forward prices are highly volatile. Price movements for spot and forward contracts may be influenced by, among other things, changing supply and demand relationships, trade, fiscal, monetary, and exchange control programs and policies of governments, domestic and foreign political and economic events, changes in domestic and foreign interest rates and rates of inflation, currency devaluations and revaluations and

emotions of the marketplace. In addition, governments from time to time intervene directly and by regulation in certain markets. Such intervention is often intended to influence prices directly. None of these factors can be controlled by the Investment Manager, and no assurance can be given that the Investment Manager's advice will result in profitable trades for the Funds or that the Funds will not incur substantial losses. Spot and forward contracts are not traded on exchanges. Rather, banks and dealers act as principals in these markets, negotiating each transaction on an individual basis. Neither the CFTC nor banking authorities currently regulate trading in forward contracts on currencies, nor is there a limitation on the daily price movements of forward contracts. Speculative position limits are not applicable to forward trading. The Funds will be subject to the risk of the inability or refusal to perform on the part of the principals or agents or through whom such forward contracts are traded.

**Swap Transactions.** The Funds may enter into swap agreements with respect to securities, indexes of securities and other assets or other measures of risk or return. Swap agreements are typically two-party contracts entered into primarily by institutional investors for periods ranging from a few weeks to many years. In a standard "swap" transaction, two parties agree to exchange the returns (or the differential in rates of return) earned or realized on particular predetermined investments, instruments, or indices. The gross returns to be exchanged or "swapped" between the parties are generally calculated with respect to a "notional amount". Whether the use of swap agreements will be successful will depend on the Investment Manager's ability to select appropriate transactions for the Funds. Swap transactions may be highly illiquid. Moreover, the Funds bear the risk of loss of the amount expected to be received under a swap agreement in the event of the default or insolvency of its counterparty. Many swap markets are relatively new and still developing. It is possible that developments in the swap markets, including potential government regulation, could adversely affect the ability to terminate existing swap transactions or to realize amounts to be received under such transactions. Swaps and certain other custom instruments are subject to the risk of non-performance by the swap counterparty, including risks relating to the creditworthiness of the swap counterparty.

Total return swaps are another form of swap transaction that the Funds may utilize in their investment programs. A total return swap allows the total return receiver to receive the change in market value of an asset (whether a security, interest rate, form of debt, currency or other asset) from the total return payer in return for paying a floating or fixed interest-rate on a predetermined amount. The total return payer is synthetically short and the total return receiver is synthetically long. Thus, total return swap agreements may effectively add leverage to the portfolio because, in addition, to total net assets, the Funds would be subject to investment exposure on the notional amount of the swap agreement.

**Other Derivative Investments.** Derivative instruments or "derivatives" include futures, options, structured securities and other instruments and contracts that are derived from, or the value of which is related to, one or more underlying securities, financial benchmarks, currencies or indices. Derivatives allow an investor to hedge or speculate upon the price movements of a particular security, financial benchmark, currency or index at a fraction of the cost of investing in the underlying asset. The value of a derivative depends largely upon price movements in the underlying asset. Therefore, many of the risks applicable to trading the underlying asset are also applicable to derivatives of such asset. However, there are a number of other risks associated with derivatives trading. For example, because many derivatives are leveraged, and thus provide significantly more market exposure than the money paid or deposited when the transaction is entered into, a relatively small adverse market movement may expose the Funds to the possibility of a loss exceeding the original amount invested. Derivatives may also expose investors to liquidity risk, as there may not be a liquid market within which to close or dispose of outstanding derivatives contracts. Swaps and certain options and other custom instruments are subject to the risk of non-performance by the swap counterparty, including risks relating to the creditworthiness of the swap counterparty.

**Counterparty Risk.** Currently, the Funds focus on trading listed instruments only. In the event that the Funds trade OTC instruments, such instruments will not be cleared through a central clearing agency, and thus will be bilateral contracts between the Funds and a dealer. It is anticipated that, over time, some and perhaps many of these OTC

instruments will be required to be centrally cleared pursuant to the Dodd-Frank Act, however, clearing is not presently required and the central clearing houses are not yet ready to clear most of these instruments.

In the OTC markets, the Funds will bear the credit risk that one or more counterparties will be unable to pay in full their obligations under such contracts, except to the extent that the Fund is collateralized. OTC counterparties are typically not subject to credit evaluation and regulatory oversight as are members of “exchange-based” markets – provided, however that, the Dodd-Frank Act is bringing increasing regulatory oversight to the OTC markets. Less regulation exposes the Funds to the risk that counterparties will not meet their obligations under transactions in accordance with their terms and conditions because of disputes over the terms of the contracts (whether or not bona fide) or because of credit or liquidity problems (including, without limitation, the insolvency, bankruptcy or liquidation of the counterparty), thus causing the Funds to suffer a loss. Any bankruptcy, insolvency, receivership or other similar creditors’ rights event of a material counterparty of the Funds would likely result in losses to the Funds and may impair the operational capabilities of the Funds. Such “counterparty risk” is accentuated for contracts with longer maturities where events may intervene to prevent settlement, or where the Funds might have concentrated transactions with a single or small group of counterparties.

The Funds are not restricted from dealing with any particular counterparty or limited in the number or amount of transactions they may enter into with any particular counterparty or restricted from concentrating any or all of their transactions with one counterparty, although they generally use, and anticipate that they will generally continue to use a number of different counterparties. The Investment Manager will monitor concentration risk. To the extent that the Funds trade OTC instruments (if at all), the Funds may trade actively with a number of different counterparties and, in placing trades, take into account their exposures to counterparties. In doing so, the Funds will take into account such exposures on a current basis and also measure potential future exposures to counterparties assuming extreme market conditions.

To reduce counterparty credit risk, derivative positions are marked to market daily and variation margin is exchanged on a bilateral basis as the parties agree from time to time. The variation margin may be held either by the Funds or their counterparty, depending on which party is, as of a given valuation day, “in-the-money”. The Funds will often be required to post initial margin or “independent amounts” as additional security for the benefit of their counterparties (generally, dealers). Variation and initial margin are generally comprised of U.S. Treasury securities, U.S. agency securities or U.S. dollars. If the variation margin is held by the counterparty, then any additional margin posted by the Funds to the counterparty as initial margin would increase the total amount of margin held by the counterparty. If the variation margin is held by the Funds, then any additional margin required as initial margin from the Funds would reduce the amount of variation margin held by the Funds. Thus, posting initial margin increases the counterparty credit risk of the posting party. In a number of cases, the Funds will not post initial margin directly with the derivatives counterparty, but instead will post the initial margin to a separate “tri-party collateral account” owned by the Funds in which the counterparty has been granted a security interest. This arrangement is intended to reduce counterparty credit risk associated with posting initial margin directly to a counterparty (or with allowing initial margin to reduce the amount of variation margin held by the Funds). The Funds may not have such arrangements in place with all counterparties, and there can be no assurance that these arrangements will be effective to eliminate or reduce counterparty credit risk.

The Investment Manager has no internal credit function that independently evaluates the creditworthiness of the Funds counterparties; however, the Investment Manager reviews published credit ratings regarding the counterparties that are prepared by independent third parties, which may or may not be accurate or entirely reliable. The ability of the Funds to transact business with any one or a number of counterparties, the lack of any meaningful and independent evaluation of such counterparties’ financial capabilities, and the absence of a regulated market to facilitate settlement may increase the potential for losses by the Funds. Although increased regulatory oversight of the OTC markets may decrease some of the risks associated with trading with OTC counterparties, it may increase other risks, including, without limitation, risks associated with clearing organizations, futures

commission merchants and with certain mandated reorganizations of OTC trading activities. In addition, in recent periods, the number of potential counterparties has been reduced due to merger and acquisition activity in the investment banking and banking industries and through the insolvency and winding up of certain major market participants. Further consolidation in the industry could lead to more highly concentrated positions and could limit trading opportunities and the beneficial effects of competition.

**Equity Options.** The Funds may invest in equity options in the U.S. and other countries. The value of these financial instruments generally will vary with the performance of the issuer and movements in the equity markets. As a result, the Funds may suffer losses if they invest in equity options of issuers whose performance diverges from the Investment Manager's expectations or if equity markets generally move in a single direction and the Funds have not hedged against such a general move. The Funds may also 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 or otherwise qualifying restricted securities for public resale.

**Fixed Income and Corporate Debt Securities.** The Funds intend to invest in; debt securities issued or guaranteed by the U.S. government or one of its agencies or instrumentalities, sovereign debt issued or guaranteed by foreign governments; commercial paper and "higher yielding" (and, therefore, higher risk) debt securities of the former categories. These securities may pay fixed, variable or floating rates of interest and may include zero coupon obligations. The value of fixed income securities in which the Fund invests will change in response to fluctuations in interest rates. In addition, the value of certain fixed-income securities can fluctuate in response to perceptions of creditworthiness, political stability or soundness of economic policies. Fixed income securities are subject to the risk of the issuer's inability to meet principal and interest payments on its obligations (i.e., credit risk) and are subject to price volatility due to such factors as interest rate sensitivity, market perception of the creditworthiness of the issuer and general market liquidity (i.e., market risk). A major economic recession could disrupt severely the market for such securities and may have an adverse impact on the value of such securities. In addition, 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.

**Risk Management.** Although the Investment Manager expects to use certain risk management parameters and methods to seek to reduce exposure to certain risks, there is no assurance that such risk management parameters and methods will be successful. The Funds do not seek to reduce or limit, and may retain exposure to, various risks to the extent that the Investment Manager believes they provide appropriate opportunities for returns. Judgments about the relationship between risks and returns and appropriate risk reduction strategies are subjective, and the desired risk levels may not be obtained or may prove to have been too high or too low. The Investment Manager's risk assessment methods, as in effect from time to time, may not accurately identify or quantify the risks to which the Funds are exposed, which could limit the Investment Manager's ability to manage the risks. The Investment Manager's risk assessment methods are based in part on historical data. Risks and attendant losses may be significantly greater than may reasonably be predicted from historical data. Additionally, the Investment Manager's models may not correctly interpret or apply the historical data and may be unable to assess correctly the interaction of various risks. Moreover, not all historical data is taken into account by any model, and the Investment Manager's models may fail to include the relevant historical data. The Investment Manager's risk management techniques and strategies, as in effect from time to time, may not fully achieve the targeted risk exposures in all economic or market environments, and may be ineffective to reduce certain types of risk, including but not limited to unidentified or unanticipated risks. Anticipated correlations among the returns of various investments may not materialize. Risk management techniques may be difficult to calibrate and expensive to implement and thus may have the effect of reducing returns by more than anticipated. There can be no guarantee that the Investment Manager's risk assessment methods and management techniques and strategies will be effective or that the volatility management strategies will generate positive returns.

**Foreign Securities.** The Funds may invest in securities of non-U.S. issuers. Investments in securities and instruments in foreign markets involve substantial risks not typically associated with investments in U.S. securities. Foreign securities investments may be affected by changes in currency rates or exchange control regulations, changes in governmental administration or economic or monetary policy (in the United States and abroad) or changed circumstances in dealings between nations. Changes in foreign currency exchange rates relative to the U.S. dollar will affect the U.S. dollar value of Fund assets denominated in that currency and thereby impact the total return on such assets. The Funds may utilize options and forward contracts to hedge against currency fluctuations, but there can be no assurance that such hedging transactions will be effective.

Investments in foreign securities will also occasion risks relating to political and economic developments abroad, including the possibility of expropriations or confiscatory taxation, limitations on the use or transfer of Fund assets and any effects of foreign social, economic or political instability. Foreign companies are not subject to the regulatory requirements of U.S. companies and, as such, there may be less publicly available information about such companies. Moreover, foreign companies are not subject to uniform accounting, auditing and financial reporting standards and requirements comparable to those applicable to U.S. companies. Finally, in the event of a default of any foreign debt obligations, it may be more difficult for the Funds to obtain or enforce a judgment against the issuers of such securities.

Securities of foreign issuers may be less liquid than comparable securities of U.S. issuers and, as such, their price changes may be more volatile. Furthermore, foreign exchanges and broker-dealers are generally subject to less government and exchange scrutiny and regulation than their American counterparts. Brokerage commissions, dealer concessions and other transaction costs may be higher in foreign markets than in the U.S. Differences in clearance and settlement procedures in foreign markets may occasion delays in settlements of the trades affected in such markets.

**Difficulty of Locating Suitable Investments.** There can be no assurance that there will be a sufficient number of suitable investment opportunities to enable the Funds to invest all of their capital in opportunities that satisfy the investment objectives or that such investment opportunities will lead to completed investments by the Funds. The availability of investment opportunities, particularly with small issues, generally will be subject to competition from other investment entities.

**Competition.** The securities industry and the varied strategies engaged in by the Investment Manager are extremely competitive and each involves a degree of risk. The Funds compete with firms, including many of the larger securities and investment banking firms, which have substantially greater financial resources and research staffs.

**Concentration.** The Fund portfolios may, from time to time, be concentrated in a particular type of security, industry, geographic location or market capitalization. This may be the result of opportunistic investing, external market forces or the lack of liquidity in one security as compared to other securities the Funds hold. Losses incurred in a position making up a significant percentage of Fund capital could have a material adverse effect on the overall financial condition of the Funds. This limited diversity could expose the Funds to significantly greater volatility than in a more diversified portfolio.

**Hedging Transactions.** The Funds may also hedge short options positions by taking offsetting positions in the underlying instruments on which the options are being traded or by investing in any instrument that could be expected to be a reasonable hedge to the overall portfolio. Such hedging may seek to: (i) protect against possible changes in the market value of the Fund investment portfolios resulting from fluctuations in the securities markets and/or changes in interest rates, (ii) protect unrealized gains in the value of the Fund investment portfolios, (iii) facilitate the sale of any such investments, (iv) enhance or preserve returns, spreads or gains on any investment in the Fund portfolios, (v) hedge the interest rate or currency exchange rate on any of the Fund liabilities or assets, (vi) protect against any increase in the price of any securities the Funds anticipate purchasing at a later date or (vii) for any other reason that the Investment Manager deems appropriate.

When the Investment Manager decides to hedge one or more positions, its success will be based on the Investment Manager's ability to correctly assess the degree of correlation between the performance of the hedging instrument and the performance of the investment being hedged. Since the characteristics of many securities change as markets change or time passes, the success of a hedge will also be subject to the Investment Manager's ability to periodically recalculate, readjust, and execute the hedge in an efficient and timely manner. While the Funds may enter into hedging transactions to seek to reduce risk, such transactions may result in a poorer overall performance for the Funds than if they had not engaged in any such hedging transactions. In certain transactions, the Funds may not be "hedged" against market fluctuations, or, in liquidation situations, may not accurately value the assets of the company being liquidated. This can result in losses, even if the proposed transaction is consummated. When the Investment Manager desires to hedge a position in the Fund portfolios, it might not be able to do so because a hedge may not be available; it may be too costly in light of the likelihood of the possible risk actually occurring or the risk simply could not be reasonably anticipated.

**Cash Balances.** The Funds may hold a portion of its assets in cash. The Funds will hold any cash balances it may accumulate for investment, reinvestment or distribution to the investors in securities subject to repurchase agreements, in money market mutual funds, in interest-bearing bank accounts or in other securities. The returns on the cash balances are expected to be low and the Funds could miss more significant returns if its cash balances are high.

**Loans of Portfolio Securities.** The Funds may lend their portfolio securities on terms customary in the securities industry, enter into reverse repurchase agreements or enter into other transactions constituting a loan of Fund assets. By doing so, the Funds attempt to increase its income through the receipt of interest on the loan. In the event of a default or the bankruptcy of the other party to a securities loan, the Funds could experience delays in recovering the securities it lent and there is no assurance that the securities will be recovered. To the extent that the value of the securities the Funds lent has increased, the Funds could experience a loss if such securities are not recovered.

**Money Market Instruments.** The Investment Manager may invest, for defensive purposes or otherwise, all or a portion of Fund assets in money-market instruments and foreign money-market mutual funds, or hold cash or cash equivalents in such amounts as the Investment Manager deems appropriate under the circumstances. Money market instruments are high quality, short term fixed-income obligations, which generally have remaining maturities of one year or less, and may include U.S. Government securities, commercial paper, certificates of deposit and bankers' acceptances issued by domestic branches of United States banks that are members of the Federal Deposit Insurance Corporation, and repurchase agreements. However, there can be no assurances that such investments will not be subject to significant risks.

**Exchange Traded Funds.** The Funds may invest in and sell short shares of exchange traded funds ("ETFs") and other similar instruments. These transactions may be used to adjust exposure to the general market or industry sectors and to manage the portfolios risk exposure. ETFs and other similar instruments involve risks generally associated with investments in a broadly based portfolio of common stocks, including the risk that the general level of stock prices, or that the prices of stocks within a particular sector, may increase or decrease, thereby affecting the value of the shares of the ETF or other instruments.

**General Economic and Market Conditions.** The success of investing activities will be affected by general economic and market conditions, such as interest rates, availability of credit, credit defaults, inflation rates, economic uncertainty, changes in laws (including laws relating to taxation of Fund investments), trade barriers, currency exchange controls, and national and international political circumstances (including wars, terrorist acts or security operations). These factors may affect, among other things, the level and volatility of securities' prices, the liquidity of Fund investments and the availability of certain securities and investments. Volatility or illiquidity could impair profitability or result in losses. The Funds may maintain substantial trading positions that can be materially adversely



affected by the level of volatility in the financial markets — the larger the positions, the greater the potential for loss.

**Suspension of Trading.** For all securities traded on public exchanges, each exchange typically has the right to suspend or limit trading in all securities that it lists. Such a suspension could render it impossible for the Funds to liquidate positions and thereby expose it to losses. In addition, there is no guarantee that non-exchange markets will remain liquid enough for the Funds to close out positions.

**Change in Investment Strategies.** The investment strategies, approaches and techniques discussed herein may evolve over time due to, among other things, market developments and trends, the emergence of new or enhanced investment products, changing industry practice and/or technological innovation. As a result, these investment strategies, approaches and techniques may not reflect the investment strategies, approaches and techniques actually employed by the Funds. Nevertheless, the investments made on behalf of the Funds will be consistent with the Fund investment objectives.

**Custody Risk.** Fund assets may be held in one or more accounts maintained for the Funds by custodian banks, prime brokers or at other brokers or banks, which may be located in various jurisdictions, including emerging market jurisdictions. The custodian banks, prime brokers, other brokers (including those acting as sub-custodians) and banks are subject to various laws and regulations in the relevant jurisdictions that are designed to protect their customers in the event of their insolvency. Accordingly, the practical effect of the laws protecting customers in the event of insolvency and their application to the Fund assets may be subject to substantial variations, limitations and uncertainties. For instance, in certain jurisdictions brokers could have title to Fund assets or not segregate customer assets. Because of the large number of entities and jurisdictions involved and the range of possible factual scenarios involving the insolvency of a custodian bank, prime broker, other broker or bank, or a clearing corporation, it is impossible further to generalize about the effect of the insolvency of any of them on the Funds and their assets. Investors should assume that the insolvency of any of the custodian banks, prime brokers, other brokers or banks or clearing corporations may result in the loss of all or a substantial portion of Fund assets or in a significant delay in the Funds having access to those assets.

## **ITEM 9 DISCIPLINARY INFORMATION**

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Investment advisors are required to disclose any legal or disciplinary events that are material to a client's or prospective client's evaluation of the advisory business or the integrity of management personnel. Kaleidoscope Capital and its management personal have not been involved in any such events.

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

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None of Kaleidoscope Capital, its affiliates and their partners, members or employees are registered, or have an application pending to register, as a broker-dealer or a registered representative of a broker-dealer.

In its capacity as a Commodity Trading Advisor (“CTA”), Kaleidoscope Capital, is registered with the Commodity Futures Trading Commission (“CFTC”) and is a member National Futures Association (“NFA”). In its capacity as a Commodity Pool Operator (“CPO”), Kaleidoscope GP LP is registered with the CFTC and is a member of the NFA. Nick Nanda and Kai Wu are Associated Persons of both Kaleidoscope Capital and Kaleidoscope GP LP.

Kaleidoscope Capital, its partners and employees may have conflicts in allocating their time to the management of the Funds. Kaleidoscope’s employees devote sufficiently all of their business time to fulfilling their fiduciary duties to the Funds. Employees may conduct outside business activities pursuant to Kaleidoscope’s compliance policies and procedures. Such activities are subject to disclosure and pre-approval.

Nick Nanda serves the Boston Ballet as Trustee, Chair of the Investment Committee and Member of the Finance Committee. There are no known relationships between Kaleidoscope and the Boston Ballet. Mr. Nanda does not receive compensation for his engagement.

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

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Kaleidoscope Capital is trusted to represent client interests in many matters, and must hold itself to the highest standard of fairness in all such matters. Kaleidoscope Capital has adopted a Code of Ethics (the “Code”) which detail the standards of business conduct for all employees. Clients and prospective clients may obtain a copy of the Code by contacting Mike Hegarty (Chief Compliance Officer) by email at [mike.hegarty@kldscap.com](mailto:mike.hegarty@kldscap.com), or by telephone at (617) 765-2064.

All employees must certify in writing initially upon commencement of employment and thereafter on an annual basis, and upon any material change to the Code, that they have read, understood and agreed to comply with the policies and procedures described in the Code, and that they will conduct themselves professionally in complete accordance with the requirements and standards described in the Code.

Kaleidoscope Capital maintains a strict personal trading and investment policy. This policy limits any and all personal trading and investing by any employee to Publicly Traded Mutual Funds, Exchange Traded Funds (ETFs), Private Investments in Hedge Funds, and U.S. Government Issued Securities.

Each employee must submit an initial holding report within 10 days of commencement of employment and annually by February 14th of each year thereon. Employees are required to instruct each broker, bank, or other financial institution in which the employee maintains a personal account (i.e., a securities trading account in which the employee has any direct or indirect beneficial ownership interest) to provide Kaleidoscope Capital with duplicates of all trade confirmations and all monthly or other periodic statements. In addition, each employee is required to provide a quarterly transaction report within 30 days after the end of each calendar quarter.

## ITEM 12 BROKERAGE PRACTICES

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As part of its fiduciary duty, Kaleidoscope Capital has an obligation to seek the best price and execution when directing trading for the Funds. Kaleidoscope Capital considers several qualitative and quantitative factors that influence execution quality, including the financial strength, integrity and stability of the futures commission merchant and/or broker-dealer and the commissions to be paid.

Kaleidoscope Capital may receive research or other products or services other than execution from a broker-dealer or a third party in connection with securities transactions (“soft dollar benefits”). However, Kaleidoscope’s policies prohibit the use of client brokerage to receive such benefits. Kaleidoscope Capital does not direct brokerage in exchange for client referrals and does not permit clients to direct transactions through any particular broker-dealer.

Kaleidoscope Capital does not aggregate orders on behalf of the Funds. The Funds primarily transact in listed securities with direct market access to the exchanges on which the securities trade. Execution and clearing commissions are incurred on a per contract or per share basis. The Investment Manager has not determined that aggregation of trade orders would result in a cost benefit to its clients.

Kaleidoscope Capital has adopted policies and procedures related to trade errors. Any trading errors must be reported immediately to the Chief Compliance Officer. The Chief Compliance Officer will determine whether it is possible and appropriate for the trade to be unwound. If the trade cannot be unwound, the Chief Compliance Officer will review the error and determine whether any clients have been harmed. Kaleidoscope shall not be liable to any investor or Fund for any losses, damages or expenses arising out of or relating to (i) any trade errors, acts or omissions, or alleged acts or omissions arising out of, related to or in connection with the Fund or any entity in which the Fund has an interest, any transaction or activity relating to the Fund or any entity in which it has an interest, any investment or proposed investment made or held, or to be made or held by the Fund, or arising out of the advisory contract or any similar matter, unless such trade error, action or inaction constitutes fraud, willful misconduct or gross negligence by Kaleidoscope or its employees or (ii) any trade errors, acts or omissions, or alleged acts or omissions of any broker, agent or other third party providing services to the Fund or Kaleidoscope, provided that the selection, engagement or retention of such broker, agent or other third party providing services to the Fund or Kaleidoscope was made with reasonable care. If a client benefits from a trading error, that client will generally be entitled to keep such benefit.

## ITEM 13 REVIEW OF ACCOUNTS

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The Kaleidoscope Fund portfolios are continuously monitored by the members of the investment and operations teams. The investment team is comprised of the Chief Investment Officer, Nick Nanda, and the Head of Portfolio Management and Research, Kai Wu. In addition, the operations team monitors the portfolios daily to ensure all transactions are recorded. The Chief Compliance Officer, Mike Hegarty, performs periodic reviews to determine if the portfolios are consistent with the investment objectives, risks and strategies set forth in the Fund offering documents. Certain events that may trigger a more detailed review of the portfolio include, but are not limited to: significant deviations or trends in portfolio performance, significant changes in trading volumes, and the addition or removal of a security type or market.

Investors in the Funds receive monthly capital statements and a quarterly investor letter. The quarterly letter contains commentary relevant to the performance and construction of the Fund portfolios. In addition, each of the Funds financial statements are audited on an annual basis and distributed to investors in the Funds no later than 90 following the end of the fiscal year.

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

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Kaleidoscope Capital does not directly nor indirectly compensate any third party for client referrals.

## ITEM 15 CUSTODY

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Kaleidoscope Capital does not maintain physical possession of client cash or securities. However, Kaleidoscope Capital is deemed to have custody of the Kaleidoscope Funds because an affiliate serves as general partner to the Funds. Kaleidoscope Capital has implemented procedures to safeguard Fund assets that are consistent with the requirements under the Investment Advisers Act of 1940. The Kaleidoscope Funds financial statements are prepared in accordance with generally accepted accounting principles. The statements are audited annually and distributed to each Fund investor within 90 days of the fiscal year end. Investors should carefully review the Funds audited financial statements and compare these statements to any financial information that may be distributed by the Investment Manager.



## **ITEM 16 INVESTMENT DISCRETION**

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Kaleidoscope Capital has full discretionary authority to manage the assets of the Kaleidoscope Funds. The authority is granted pursuant to investment management agreements with the Kaleidoscope Funds. The investment management agreements are intended to give the Investment Manager the flexibility to opportunistically invest Fund assets and otherwise conduct Fund business in a manner that is consistent with the objectives and strategies described in the fund confidential offering memorandums.

## **ITEM 17 VOTING CLIENT SECURITIES**

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The Kaleidoscope Funds pursue investment strategies that generally do not utilize securities for which voting rights are attached, and primarily for this reason, the Investment Manager does not accept proxy voting responsibility and will abstain from any proxies received.

## **ITEM 18 FINANCIAL INFORMATION**

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Investment advisors are required to disclose any financial condition that is reasonably likely to impair their ability to meet contractual commitments to clients. Kaleidoscope Capital does not have any such financial condition.