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

**WARLANDER ASSET MANAGEMENT, LP**

**March 2018**

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*This brochure (this "Brochure") provides information about the qualifications and business practices of Warlander Asset Management, LP (the "Investment Adviser", "we", "us" and similar terms). If you have any questions about the contents of this Brochure, please contact us at 646-779-6200 or [rposner@warlander.com](mailto:rposner@warlander.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.*

*This Brochure also relates to Warlander Partners GP, LLC (the "Fund General Partner"); however, to the extent the qualifications and business practices of the General Partner are substantially similar to those of the Investment Adviser, no specific mention of the General Partner is made herein.*

*The Investment Adviser is registered as an investment adviser with the SEC. Registration with the SEC or with any state securities authority does not imply a certain level of skill or training.*

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

**ITEM 2**  
**MATERIAL CHANGES**

The Investment Adviser does not consider any of the information contained in this version of the Brochure to represent a material change from the information contained in the most recent version dated March 2017.

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## **ITEM 4**

### **ADVISORY BUSINESS**

#### **A. General Description of Advisory Firm.**

##### *1. Warlander Asset Management, LP*

Warlander Asset Management, LP (the "Investment Adviser", "we", "us" and similar terms), is a Delaware limited partnership that was formed in 2015.

We have only one office, which is located in New York.

We are controlled by our principal owners, Messrs. Eric Cole and Alex Ginzburg (the "Principal Owners") and Marc Pfeffer, our President and Chief Operating Officer (together with the Principal Owners, the "Principals"). The President and Principals are limited partners of the Investment Adviser and members of Warlander Management GP, LLC, a Delaware limited liability company and our general partner (the "Investment Adviser General Partner"). Mr. Cole controls the Investment Adviser as the managing member of the Investment Adviser General Partner. The Investment Adviser General Partner has ultimate responsibility for our management, operations and investment decisions.

##### *2. Warlander Partners GP, LLC*

Our registration on Form ADV also covers Warlander Partners GP, LLC (the "Fund General Partner"), a limited liability company organized under the laws of the state of Delaware. The Fund General Partner is an affiliate of the Investment Adviser and it serves or may serve as the general partner of pooled investment vehicles that are U.S. or offshore partnerships. The Fund General Partner's facilities and personnel are provided by the Investment Adviser.

The Principals are members of the Fund General Partner. Eric Cole controls the Fund General Partner as its managing member.

#### **B. Description of Advisory Services.**

This Brochure generally includes information about us and our relationships with our clients. While much of this Brochure applies to all such clients, certain information included herein applies to specific clients only.

##### *1. Advisory Services*

We serve as the investment adviser, with discretionary trading authority, to private pooled investment vehicles, the securities of which are offered to investors on a private placement basis (each, a "Fund" and collectively, the "Funds"). The Funds include:

- (1) Warlander Partners, LP, a Delaware limited liability partnership (the "Domestic Fund");
- (2) Warlander Offshore Fund, Ltd., a Cayman Islands exempted company (the "Offshore Fund", and together with the Domestic Fund, the "Feeder Funds"); and

- (3) Warlander Offshore Mini-Master Fund, LP, a Cayman Islands exempted limited partnership (the "Offshore Mini-Master Fund", which serves as a mini-master fund into which the Offshore Fund invests substantially all of its assets through a "master feeder" structure.

The Fund General Partner serves as the general partner of the Domestic Fund and the Offshore Mini-Master Fund. The Offshore Mini-Master Fund invests on a "side-by-side" basis with the Domestic Fund.

## 2. *Managed Accounts*

In addition, the Investment Adviser may in the future serve as an investment adviser with discretionary trading authority over, and may also provide discretionary advisory services to, separately managed accounts (the "Managed Accounts").

As used herein, the term "Client" generally refers to each Fund and each beneficial owner of a Managed Account.

*This Brochure does not constitute an offer to sell or solicitation of an offer to buy any securities. The securities of the Funds are offered and sold on a private placement basis under exemptions promulgated under the Securities Act of 1933 and other applicable state, federal or non-U.S. laws. Significant suitability requirements apply to prospective investors in the Funds, including requirements that they be "accredited investors" as defined in Regulation D, "qualified purchasers" as defined in the Investment Company Act, or non-"U.S. Persons" as defined in Regulation S. Persons reviewing this Brochure should not construe this as an offer to sell or a solicitation of an offer to buy the securities of any of the Funds described herein. Any such offer or solicitation will be made only by means of a confidential private placement memorandum.*

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

The Investment Adviser's investment objective is to maximize absolute returns on its Clients' capital through opportunistic investments, long and short, in securities and other financial instruments (including senior, secured and unsecured bank debt and public debt, private debt, junior debt, trade claims, equities, convertible securities, debt and equity indices, asset-backed and structured credit securities, futures, options, swaps (including credit default swaps) and other derivatives) identified across the full spectrum of global fixed income and equities (including all types of performing, distressed and non-performing corporate debt and credit-sensitive equity in developed and emerging markets, and sovereign, quasi-sovereign and municipal debt).

The Investment Adviser aims to capture market opportunities by identifying and capitalizing on dislocations at the market, asset class, sector and security levels that result from over-bought or over-sold market conditions or other factors that the Investment Adviser identifies from time to time. The Investment Adviser also rigorously develops various investment themes based on its analysis of global macro-economic conditions (including, but not limited to, currency, interest rate, commodity and other market conditions, and the fiscal and central bank policies of governments) and seeks to utilize the perspective gained from these investment themes to inform top-down portfolio capital allocations as well as integrate these views into its research process for individual positions. Idiosyncratic ideas may also represent significant exposure in the portfolio.

We seek to utilize the expertise of Eric Cole who has over 20 years of research, trading and investing experience across global capital markets, along with the experience of the other Principals, for the benefit of Clients. Mr. Cole has experience investing across many sectors and markets, and combines deep fundamental bottom-up security analysis, macro-economic analysis and trading experience across the sectors and securities in which the Fund seeks to invest. Mr. Cole will collaborate with and be supported by an experienced team of research and trading professionals, each of whom has significant expertise in security research and investing. Clients also benefit from the extensive network of professional relationships developed and maintained by the Principals. These relationships enhance our ability to identify, source, research and execute on investment opportunities.

Individual investment opportunities will generally be subjected to rigorous, fundamental, bottom-up analysis. This analysis will typically incorporate our emphasis on integrating our macro-economic perspective into an assessment of the drivers of the opportunity's investment thesis. The analysis also assesses, where appropriate, legal, financial, regulatory, litigation and timing issues. Additionally, our analysis of the capital structure assists in identifying the security or instrument that is perceived to present the most efficient execution and favorable risk/reward profile for our Clients. Making and monitoring investments is a complex process, and this overview should not be seen as predictive or as a set of required steps or elements for each investment. In actual investment and monitoring, different or substitute criteria or instruments may be utilized.

The descriptions set forth in this Brochure of specific advisory services that we offer to our Clients and investment strategies pursued and investments made by us on behalf of our clients, should not be understood to limit in any way our investment activities. We may offer any advisory services, engage in any investment strategy and make any investment, including any not described in this Brochure, that we consider appropriate, subject to each Client's investment objectives and guidelines. The investment strategies we pursue 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 objectives of any Client will be achieved.

C. Availability of Customized Services for Individual Clients.

Our investment decisions and advice with respect to each Client will be subject to each Client's investment objectives and guidelines, as set forth in its respective offering documents or investment management agreements as applicable.

If, in the future, we determine to offer Managed Accounts, the investment objectives and guidelines of the Managed Accounts would be determined in conjunction with the applicable Client.

D. Wrap Fee Programs.

We do not currently participate in any Wrap Fee Programs.

E. Assets Under Management.

As of December 31, 2017, the Investment Adviser had \$1,667,454,082 of regulatory assets under management.

## ITEM 5 FEES AND COMPENSATION

### A. Advisory Fees and Compensation.

The fees applicable to each Fund are set forth in detail in each Fund's offering documents. A brief summary of such fees is provided below.

#### 1. *Domestic Fund*

Management Fee. Generally, the Domestic Fund pays the Investment Adviser a fee for investment management services (the "Management Fee") for each fiscal quarter of between 0.375% and 0.5% (1.5-2% per annum) of the beginning net asset value of each investor's capital account for such fiscal quarter. The Management Fee is calculated and paid in advance but is amortized monthly by the Domestic Fund over the quarter for which such Management Fee is paid.

The Management Fee will be prorated for any capital contribution or withdrawal by an investor that is effective other than as of the first day of a quarter. In the event of a withdrawal by an investor other than as of the last day of a quarter, the Investment Adviser will pay to the Domestic Fund an amount equal to the *pro rata* portion of the Management Fee, based on the actual number of days remaining in such quarter, and the Domestic Fund will distribute such amount to the withdrawing investor. The Investment Adviser, in its sole discretion, may elect to reduce, waive or calculate differently the Management Fee with respect to any employee or affiliate of the Investment Adviser, or any family member or estate planning vehicle of such person. The Fund General Partner will not be charged the Management Fee.

Incentive Allocation. Generally, at the end of each fiscal year of the Domestic Fund, the Fund General Partner is entitled to an incentive allocation (the "Incentive Allocation") in an amount equal to 20% of the net capital appreciation (which includes both realized gains and losses and unrealized appreciation and depreciation of securities held in the Domestic Fund's portfolio) allocated to an investor's capital account for such fiscal year after deducting the Management Fee debited to such investor's capital account for such fiscal year, subject to a loss carryforward mechanism.

In the event that the Domestic Fund is terminated, or an investor withdraws other than at the end of a fiscal year, then for purposes of determining the Incentive Allocation allocable at such time to the Fund General Partner, net capital appreciation will be determined as if such dates were the end of the fiscal year, subject to certain adjustments. The Fund General Partner, in its sole discretion, may elect to reduce, waive or calculate differently the Incentive Allocation with respect to any employee or affiliate of the Investment Adviser, or any family member or estate planning vehicle of such person.

#### 2. *Offshore Fund*

Management Fee. Generally, the Offshore Fund pays the Investment Adviser a Management Fee for each fiscal quarter of between 0.375% and 0.5% (1.5-2% per annum) of the net asset value of each series of shares as of the beginning of such fiscal quarter. The Management Fee is calculated and paid in advance but is amortized monthly by the Offshore Fund over the quarter for which such Management Fee is paid.



The Management Fee will be prorated for any subscription or redemption by an investor that is effective other than as of the first day of a quarter. In the event of a redemption by an investor other than as of the last day of a quarter, the Investment Adviser will pay to the Offshore Fund an amount equal to the *pro rata* portion of the Management Fee, based on the actual number of days remaining in such quarter, and the Offshore Fund will distribute such amount to the redeeming investor. The Investment Adviser, in its sole discretion, may elect to reduce, waive or calculate differently the Management Fee with respect to any employee or affiliate of the Investment Adviser, or any family member or estate planning vehicle of such person. The Fund General Partner will not be charged the Management Fee.

Incentive Allocation. Because all of the Offshore Fund's investible assets will be invested in the Offshore Mini-Master Fund, any appreciation and depreciation of the Offshore Fund's net asset value will be based on the net capital appreciation or net capital depreciation of the Offshore Mini-Master Fund's assets.

Generally, at the end of each fiscal year, the Fund General Partner is entitled to receive an Incentive Allocation (together with the Incentive Allocation from the Domestic Fund, the "Performance Compensation") in an amount equal to 20% of the net realized and unrealized appreciation in the net asset value of the Offshore Mini-Master Fund corresponding to a series of shares in the Offshore Fund, adjusted for any redemption of shares in the series made during the year and any accruals of the Incentive Allocation and subject to a loss carryforward mechanism.

In the event that shares are redeemed other than at the end of a fiscal year, the Incentive Allocation will be determined solely with respect to the shares so redeemed as of the redemption date. The Fund General Partner, in its sole discretion, may elect to reduce, waive or calculate differently the Incentive Allocation with respect to any employee or affiliate of the Investment Adviser, or any family member or estate planning vehicle of such person.

#### B. Payment of Fees.

Fees and compensation paid to the Investment Adviser or its affiliates by the Funds are generally deducted from the assets of such clients. As discussed above, Management Fees are generally deducted on a quarterly basis and Performance Compensation is generally deducted on an annual basis.

#### C. Additional Fees and Expenses.

Each Client bears its own expenses, including, without limitation, the Management Fee, the Performance Compensation, investment-related expenses (*e.g.*, brokerage commissions and transaction costs, clearing and settlement charges, custodial fees, interest expense, commitment fees payable to lenders, borrowing charges on securities sold short, research-related expenses (including, without limitation, consulting, legal and other professional fees and expenses), third-party research, news and quotation equipment and services (including fees for data, pricing and software providers), third-party trading-, risk-management- and portfolio-management-related systems and software, including trade order management software (*i.e.*, software used to transmit and receive trades and orders), investment-related travel (including meals, lodging and transportation), legal and compliance

expenses (which include, without limitation, responding to formal and informal inquiries, indemnification expenses and expenses associated with regulatory filings relating to clients and for their respective portfolios), insurance costs incurred in connection with clients' business (including, without limitation, acquiring and maintaining D&O and/or E&O insurance for the members of the Advisory Board and for the Investment Adviser, the Fund General Partner and their respective affiliates), valuation expenses (including, without limitation, costs of third-party valuation agents), accounting fees and expenses (including, without limitation, auditor fees), tax preparation expenses, expenses relating to the offer and sale of interests in the Funds, investor reporting costs, entity-level taxes, fees and expenses of the Funds' administrator (as defined below) and the members of the Advisory Board, entity-level taxes, fees and expenses of the Funds' Administrator(s) and the members of the Advisory Board, corporate licensing, extraordinary expenses and other similar expenses.

D. Prepayment of Fees.

Generally, each Client pays the Investment Adviser a fee for investment management services quarterly in advance based on the net asset value of each Client. In the event that a Client's net asset value is reduced in connection with a withdrawal or redemption by an investor of such Client other than as of the last day of a quarter, the Investment Adviser will pay such Client an amount equal to the *pro rata* portion of the Management Fee, based on the actual number of days remaining in such quarter, and such Client will distribute such amount to the investor.

E. Additional Compensation and Conflicts of Interest.

Neither the Investment Adviser nor any of its “Supervised Persons”<sup>1</sup> accepts compensation (*e.g.*, brokerage commissions) for the sale of securities or other investment products.

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<sup>1</sup> An investment adviser's Supervised Persons are its partners, officers, directors (or other persons occupying a similar status or performing similar functions) and employees, as well as any other persons who provide advice on behalf of the adviser and are subject to the adviser's supervision and control.

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

We and our affiliates accept performance-based compensation from every Client (other than Clients that are not assessed performance-based compensation because it is assessed through another entity in a single master-feeder or similar structure). As a result, we and our affiliates do not face certain conflicts of interest that may arise when an investment adviser accepts performance-based fees from some clients, but not from other clients.

**ITEM 7**  
**TYPES OF CLIENTS**

We provide investment advice to the Funds, as described above.

As discussed above, we may in the future provide investment advice to Managed Accounts for institutional and other investors.

## **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 we offer to Clients, and investment strategies pursued and investments made by us on behalf of our Clients, should not be understood to limit in any way our investment activities. We may offer any advisory services, engage in any investment strategy and make any investment, including any not described in this Brochure, that we consider appropriate, subject to each Client's investment objectives and guidelines. The investment strategies we pursue 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 objectives of any Client will be achieved.

The Investment Adviser aims to capture market opportunities by identifying and capitalizing on dislocations at the market, asset class, sector and security levels that result from over-bought or over-sold market conditions or other factors that the Investment Adviser identifies from time to time. The Investment Adviser also rigorously develops various investment themes based on its analysis of global macro-economic conditions (including, but not limited to, currency, interest rate, commodity and other market conditions, and the fiscal and central bank policies of governments) and seeks to utilize the perspective gained from these investment themes to inform top-down portfolio capital allocations as well as integrate these views into its research process for individual positions. Idiosyncratic ideas may also represent significant exposure in the portfolio.

Individual investment opportunities will generally be subjected to rigorous, fundamental, bottom-up analysis. This analysis will typically incorporate the Investment Adviser's emphasis on integrating its macro-economic perspective into an assessment of the drivers of the opportunity's investment thesis. The analysis also assesses, where appropriate, legal, financial, regulatory, litigation and timing issues. Additionally, the analysis of the capital structure assists in identifying the security or instrument that is perceived to present the most efficient execution and favorable risk/reward profile for the Client. Making and monitoring investments is a complex process, and this overview should not be seen as predictive or as a set of required steps or elements for each investment. In actual investment and monitoring, different or substitute criteria or instruments may be utilized.

The portfolio will be predominantly invested in issuers based in North America, Europe and Latin America, although investments may also be made in other regions including, but not limited to, Asian and Australian issuers. The Investment Adviser has not established any specific limits with respect to diversification of its portfolio, but the General Partner does not anticipate that the Clients' long exposure to the securities of any single issuer will exceed 5% of net asset value of the Client's portfolio at inception of the investment. The Investment Adviser anticipates larger positions for credit shorts, which could be more than 3-4 times as large as long positions in the Clients' portfolios, given the lower risk entailed with shorting bonds. The Investment Adviser also expects to be more concentrated across multiple investments within in a single investment theme, and does not specify a percentage limit for such concentrations. In aggregate, the overall portfolio is expected to range from 100% net long to 100% net short, but such a range may be exceeded. In addition, in the discretion of the Investment Adviser on a case-by-case basis, the Investment Adviser may cause Clients to invest in market opportunities that deviate from the investment program set forth herein.

The Investment Adviser may cause Clients to invest in residential mortgage-backed securities, commercial mortgage-backed securities, collateralized debt obligations, collateralized loan obligations and other securitized assets where the underlying collateral may or may not be considered to be distressed or otherwise non-performing.

While it is expected that a significant percentage of Clients' positions will consist of debt instruments (including investment grade, cross-over, high yield and distressed bonds, bank debt, private debt, junior debt, trade claims, sovereign debt, quasi-sovereign debt and municipal debt, indices, and asset-backed and structured credit securities), investments and hedges may also be established in equities (including preferred stocks), convertible securities, options, warrants and rights, credit and other derivatives, such as swaps, forward contracts and futures, and credit default swaps, foreign exchange contracts, commodity futures, real estate, and physical assets, as well as in other instruments (both publicly traded and privately offered) that the Investment Adviser deems appropriate. The Investment Adviser may cause its Clients to also invest in both public and private non-investment grade and non-rated securities, including, without limitation, loans, high-yield bonds, distressed securities, second lien loans, mezzanine securities, credit derivatives, trade claims and asset-backed and structured credit securities. Clients may also participate in the origination of loans, as further described below.

The Investment Adviser may have a portion of its Clients' assets invested in highly liquid, lower risk corporate securities and bank loans which will be used as cash substitutes. The Investment Adviser may cause its Clients to enter into repurchase agreements and reverse repurchase agreements. Excess Client funds of may be invested in U.S. or non-U.S. money market instruments, overnight repurchase agreements or other cash equivalents deemed appropriate by the Investment Adviser.

The Investment Adviser may seek to minimize the impact of interest rate, foreign exchange or commodity fluctuations by hedging such exposures through interest rate, foreign exchange or commodity swaps, futures, or options or other instruments as available. The Investment Adviser is, however, not obligated to hedge its Clients' portfolios in this or any other manner, and there is no guarantee that any hedges will be successful.

In connection with its Clients' distressed and non-performing security investments, the Investment Adviser may, in its sole discretion, determine to become involved on formal or ad-hoc creditor committees, and potentially take active roles in respect of such committees or otherwise seek to influence an issuer's management. In certain circumstances, these activities may restrict the Investment Adviser's ability to cause certain Clients to trade in associated securities for some period of time. In addition, the Investment Adviser may become involved in negotiating pre-packaged or traditional plans of reorganization.

The Investment Adviser has the ability to cause its Clients to borrow and may do so when it deems appropriate, including opportunistically to enhance the Client's returns. In addition to direct borrowing, a Client's portfolio may be leveraged by other means, including, without limitation, by investing in instruments that have embedded leverage such as futures, options and other derivatives. The Investment Adviser will generally not cause Clients to employ leverage to amplify returns on investments that the Investment Adviser perceives do not offer compelling standalone returns. There is, however, no limit, cap or restriction on the amount of borrowing that the Investment Adviser may cause its Clients to use or the exposure that Clients may have. Leverage will likely vary and could be significant at times.

While leverage presents opportunities for increasing the total return on investments, it has the effect of potentially increasing losses as well. Accordingly, any event which adversely affects the value of an investment could be magnified to the extent leverage is utilized and may result in a substantial loss to Clients.

The Investment Adviser may cause its Clients to participate in the origination of loans. From time to time, the Investment Adviser may offer to its affiliates, the Domestic Fund, the Offshore Mini-Master Fund or other funds or accounts managed by the Investment Adviser or other investment managers, participations in and/or assignments or sales of loans (or interests therein) that a Client has originated or purchased. Such offer and sale will typically be reviewed by the Advisory Board. In determining the target amount to allocate to a particular loan origination, the Investment Adviser will take into consideration the fact that it anticipates causing a Client to sell, assign or offer participations in such investment to other parties as described above. If the Investment Adviser is not successful in offering such participations, assignments or sales to third parties, the applicable Client will be forced to hold such excess until such time as it can be disposed. This may result in such Client being "overweighted" with respect to a particular borrower.

From time to time, the Investment Adviser may determine that circumstances exist such that certain assets or securities previously acquired by a Client (including assets or securities in connection with a bankruptcy proceeding or reorganization) may no longer have a readily assessable market value or should be held until the resolution of a special event or circumstance (each, a "Special Investment"). A Special Investment may include (in addition to the assets or securities being so designated by the Investment Adviser) any corresponding hedging positions.

**B. Material, Significant or Unusual Risks Relating to Investment Strategies.**

The following risk factors do not purport to be a complete list or explanation of the risks involved in an investment in the clients advised by us. These risk factors include only those risks we believe to be material, significant or unusual and relate to particular significant investment strategies or methods of analysis employed by us.

**Risks of Investments Generally.** The Investment Adviser causes its Clients to invest in and actively trade securities and other financial instruments using investment techniques with certain risk characteristics, including, without limitation, risks arising from the volatility of the global fixed income and equity markets and the potential illiquidity of securities and other financial instruments and the risk of loss from counterparty defaults. No guarantee or representation is made that a Client's investment objective will be achieved.

**General Economic and Market Conditions.** The Investment Adviser expects to cause its Clients to trade globally in and across different markets. Clients' activities will therefore be affected by general economic and market conditions in various markets, such as the relevant interest rates, availability of credit, credit defaults, inflation rates, commodity prices, economic uncertainty, changes in laws (including laws relating to taxation of such Clients' investments), trade barriers, currency exchange controls, and national and international political circumstances (including wars, terrorist acts or security operations). These factors may affect the level and volatility of the prices and the liquidity of the Clients' investments. Volatility or illiquidity could impair a Client's profitability or result in losses. The Investment Adviser may cause a Client to maintain substantial trading positions that can

be adversely affected by the level of volatility in the financial markets. Economic slowdowns or downturns could lead to financial losses in a Client's portfolio securities and a Client's net assets. In addition, many of a Client's investments may be similarly subject to the same economic conditions, which could adversely impact the Client's investment return. Debt and equity securities are susceptible to general stock market fluctuations and to volatile increases and decreases in value as market confidence and investor perceptions of issuers change. These investor perceptions are based on various and unpredictable factors, including expectations regarding government, economic, monetary and fiscal policies, inflation and interest rates, economic expansion or contraction, and global or regional political, economic or banking crises. Decreases in the market value of the investments that the Investment Adviser causes a Client to make will adversely affect the investment returns of such Client.

**Investment and Due Diligence Process.** Before making investments, the Investment Adviser will conduct due diligence that it deems reasonable and appropriate based on the facts and circumstances applicable to each investment. When conducting due diligence, the Investment Adviser may be required to evaluate important and complex business, financial, tax, accounting, environmental and legal issues. When conducting due diligence and making an assessment regarding an investment, the Investment Adviser will rely on the resources reasonably available to it, which in some circumstances, whether or not known to the Investment Adviser at the time, may not be sufficient, accurate, complete or reliable. Due diligence may not reveal or highlight matters that could have a material adverse effect on the value of an investment.

**Undervalued Securities.** The identification of investment opportunities in undervalued securities is a difficult task, and there are no assurances that such opportunities will be successfully recognized or acquired. While investments in undervalued securities offer the opportunity 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 that the Investment Adviser causes a Client to make may not adequately compensate for the business and financial risks assumed.

**Short-Selling.** The Investment Adviser causes its Clients to engage in short-selling. Short-selling involves selling securities which are not owned and borrowing them for delivery to the purchaser, with an obligation to replace the borrowed securities at a later date. Short-selling allows the investor to profit from declines in market prices to the extent such decline exceeds the transaction costs and the costs of borrowing the securities. The extent to which the Investment Adviser may cause a Client to engage in short sales will depend upon the Investment Adviser's ability to identify and sell short securities that are overvalued. 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 the Client of buying those securities to cover the short position. There can be no assurance that the Investment Adviser will be able to maintain the Client's ability to borrow securities sold short. In such cases, the Client can be "bought in" (*i.e.*, forced to repurchase securities in the open market to return to the lender). There also can be no assurance that the securities necessary to cover a short position will be available for purchase at or near prices quoted in the market. Purchasing securities to close out a short position can itself cause the price of the securities to rise further, thereby exacerbating the loss. Short strategies can also be implemented synthetically through various instruments and be used with respect to indices or in the over-the-counter market and with respect to futures and other instruments. In some cases of synthetic short sales, there is no floating supply of an underlying instrument with



which to cover or close out a short position and the Client may be entirely dependent on the willingness of over-the-counter market makers to quote prices at which the synthetic short position may be unwound. There can be no assurance that such market makers will be willing to make such quotes. Short strategies can also be implemented on a leveraged basis. Lastly, even though the Investment Adviser secures for its Client a "good borrow" of the securities sold short at the time of execution, the lending institution may recall the lent security at any time, thereby forcing the Investment Adviser to cause its Client to purchase the security at the then-prevailing market price, which may be higher than the price at which such security was originally sold short by the Client.

**Leverage; Interest Rates; Margin.** The use of leverage has attendant risks and can substantially increase the adverse impact to which the Client's investment portfolio may be subject. The use of leverage will allow the Investment Adviser to make additional investments on behalf of its Clients, thereby increasing its Clients' exposure to assets, such that its total assets may be greater than its capital. However, leverage will also magnify the volatility of changes in the value of the Client's portfolio. The effect of the use of leverage by a Client in a market that moves adversely to its investments could result in substantial losses to such Client, which would be greater than if the Client's portfolio were not leveraged. In addition, any leverage used by the Investment Adviser on behalf of its Clients is subject to the risk that changes in the general level of interest rates may adversely affect expenses and operating results.

In general, any use of short-term margin borrowings by the Investment Adviser on behalf of its Clients results in certain additional risks. For example, should the securities pledged to brokers to secure the portfolio's margin accounts decline in value, the portfolio could be subject to a "margin call," pursuant to which the portfolio must either deposit additional funds with the broker, or suffer mandatory liquidation of the pledged securities to compensate for the decline in value. In the event of a sudden precipitous drop in the value of the portfolio's assets, the portfolio might not be able to liquidate assets quickly enough to pay off its margin debt.

In the futures and forward markets, margin deposits are typically low relative to the value of the futures contracts purchased or sold. Such low margin deposits are indicative of the fact that any futures or forward contract trading is typically accompanied by a high degree of leverage. Low margin deposits mean that a relatively small price movement in a contract may result in immediate and substantial losses to the investor.

To the extent that the Investment Adviser causes its Clients to purchase an option in the U.S., there is no margin requirement because the option premium is paid for in full. The premiums for certain options traded on non-U.S. exchanges may be paid for on margin. Whether any margin deposit will be required for over-the-counter options and other over-the-counter instruments will depend on the credit determinations and specific agreements of the parties to the transaction, which are individually negotiated.

**Lending of Portfolio Securities.** The Investment Adviser may cause its Clients to lend securities on a collateralized and an uncollateralized basis from its portfolio to creditworthy securities firms and financial institutions. While a securities loan is outstanding, such Clients will continue to receive the equivalent of the interest or dividends paid by the issuer on the securities, as well as interest on the investment of the collateral or a fee from the borrower. The risks in lending securities, as with other extensions of secured credit, if any,

consist of possible delay in receiving additional collateral, if any, or in recovery of the securities or possible loss of rights in the collateral, if any, should the borrower fail financially.

**Loan Origination.** The Investment Adviser may cause its Clients to participate in certain loan origination activities. If the Investment Adviser is unable to sell, assign or successfully close transactions for participations in the loans that it causes its Clients to originate, such Clients will be forced to hold its excess interest in such loans for an indeterminate period of time.

**Diversification and Concentration.** The Investment Adviser may select investments that are concentrated in a limited number or types of securities. In addition, a Client's portfolio may become significantly concentrated in securities related to a single or a limited number of issuers, industries, sectors, markets, strategies, countries or geographic regions. This limited diversification may result in the concentration of risk, which, in turn, could expose the Fund to losses disproportionate to market movements in general if there are disproportionately greater adverse price movements in such securities.

**Hedging Transactions.** The Investment Adviser is not required to, and may not attempt to, hedge market risks or other risks inherent in its Clients' positions. In addition, the Investment Adviser may not anticipate a particular risk so as to hedge against it.

The Investment Adviser, however, may cause its Clients to utilize a variety of financial instruments (including options and derivatives), both for investment purposes and (to the extent desired) for risk management purposes in order to: (i) protect against possible changes in the market value of a Client's investment portfolio resulting from fluctuations in the securities or commodities markets and changes in interest rates; (ii) protect the unrealized gains in the value of a Client's investment portfolio; (iii) facilitate the sale of any such investments; (iv) enhance or preserve returns, spreads or gains on any investment in a Client's portfolio; (v) hedge the interest rate or currency exchange rate on any of a Client's liabilities or assets; (vi) protect against any increase in the price of any securities or commodities the Investment Adviser anticipates purchasing on behalf of a Client at a later date; or (vii) for any other reason that the Investment Adviser deems appropriate.

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

**Fundamental Analysis.** The Investment Adviser's investment process is based on fundamental analysis. Data on which fundamental analysis relies may be inaccurate or may be generally available to other market participants. To the extent that any such data are inaccurate or that other market participants have developed, based on such data, trading strategies similar to the Investment Adviser's trading strategies, Clients may not be able to realize their investment goals. In addition, fundamental market information is subject to interpretation. To the extent that the Investment Adviser misinterprets the meaning of certain data, its Clients may incur losses.

**Analytical Model Risks.** The Investment Adviser employs certain strategies which depend upon the reliability, accuracy and analysis of the Investment Adviser's analytical models. To the extent such models (or the assumptions underlying them) do not prove to be correct, Client portfolios may not perform as anticipated, which could result in substantial losses. All models ultimately depend upon the judgment of the Investment Adviser and the assumptions embedded in them. To the extent that with respect to any investment, the judgment or assumptions are incorrect, Clients can suffer losses.

**Counterparty Risk.** The Investment Adviser expects to cause its Clients to establish relationships to obtain financing, derivative execution, derivative intermediation and prime brokerage services that permit the Investment Adviser to trade on behalf of its Clients in any variety of markets or asset classes over time. However, there can be no assurance that Clients will be able to establish or maintain such relationships. An inability to establish or maintain such relationships could limit the Investment Adviser's trading activities, create losses, preclude its Clients from engaging in certain transactions or prevent its Clients from trading at optimal rates and terms. Moreover, a disruption in the financing, derivative intermediation and prime brokerage services provided by any such relationships could have a significant impact on a Client's business due to the Client's reliance on such counterparties.

The Investment Adviser may cause its Clients to effect transactions in the "over-the-counter" or "OTC" derivatives markets. The stability and liquidity of OTC derivatives transactions depends in large part on the creditworthiness of the parties to the transactions. In the OTC markets, the Investment Adviser causes its Clients to enter into contracts directly with dealer counterparties, which may expose such Clients to the risk that a counterparty will not settle a transaction in accordance with its terms because of a solvency or liquidity problem with the counterparty. Delays in settlement may also result from disputes over the terms of the contract (whether or not bona fide). In addition, Clients may have a concentrated risk in a particular counterparty, which may mean that if such counterparty were to become insolvent or have a liquidity problem, losses would be greater than if the Investment Adviser had caused such Clients to enter into contracts with multiple counterparties. Certain OTC derivative contracts require that Clients post collateral.

If there is a default by a counterparty, under most normal circumstances Clients will have contractual remedies pursuant to the agreements related to the transaction. However, exercising such contractual rights may involve delays or costs which could result in the net asset value of the Client's portfolio being less than if the Investment Adviser had not caused such Client to enter into the transaction. Furthermore, there is a risk that any of such counterparties could become insolvent and/or the subject of insolvency proceedings. In such case, the recovery of a Client's securities from such counterparty or the payment of claims therefore may be significantly delayed and the Investment Adviser may recover substantially less on behalf of the Client than the full value of the securities entrusted to such counterparty.

In addition, there are a number of proposed rules that, if they were to go into effect, may impact the laws that apply to insolvency proceeding and may impact whether a Client may terminate its agreement with an insolvent counterparty.

Collateral that the Investment Adviser causes a Client to post to its counterparties that is not segregated with a third-party custodian may not have the benefit of customer-protected "segregation" of such funds. In the event that a counterparty were to become insolvent, such a Client may become subject to the risk that it may not receive the return of its collateral or that the collateral may take some time to return.

In addition, the Investment Adviser may cause a Client to use counterparties located in jurisdictions outside the United States. Such local counterparties usually are subject to laws and regulations in non-U.S. jurisdictions that are designed to protect customers in the event of their insolvency. However, the practical effect of these laws and their application to a Client's assets are subject to substantial limitations and uncertainties. Because of the range of possible factual scenarios involving the insolvency of a counterparty and the potentially large number of entities and jurisdictions that may be involved, it is impossible to generalize about the effect of such an insolvency on a Client and its assets. Investors in a Fund should assume that the insolvency of any such counterparty would result in significant delays in recovering the Fund's securities from or the payment of claims therefore by such counterparty and a loss to the Fund, which could be material.

**Central Clearing.** In order to mitigate counterparty risk and systemic risk in general, various U.S. and international regulatory initiatives are underway to require certain derivatives to be cleared through a clearinghouse. In the United States, clearing requirements were part of the Dodd-Frank Act. The Commodity Futures Trading Commission ("CFTC") imposed its first clearing mandate on December 13, 2012 affecting certain interest rate and credit default swaps. It is expected that the CFTC and the SEC will introduce clearing requirements for other derivatives in the future. Trades submitted for clearing will be subject to minimum initial and variation margin requirements set by the relevant clearinghouse, the futures commission merchant ("FCM"), as well as possible SEC- or CFTC-mandated margin requirements. The Investment Adviser's Clients are not in direct privity with the clearinghouse, but instead act through a member of the clearinghouse, an FCM, which acts as a quasi-agent, guaranteeing the obligations of the Client to the clearinghouse. This regime is modeled in large part after the U.S. futures clearing regime. Clearing through FCMs has in certain cases led to losses caused by operational failure or fraud.

As products become more standardized in order to be cleared, standardized derivatives may mean that the Investment Adviser may not be able to hedge its Clients' risks or express an investment view as well as it would using customizable derivatives available in the over-the-counter markets. Compared to the OTC derivatives market, Clients may be subject to more onerous and more frequent (daily or even intraday) margin calls from both the clearinghouse and the FCM. Virtually all of the margin models that are utilized by the clearinghouses are dynamic, meaning that, unlike many of a Client's bilateral swap contracts where the amount of initial margin posted on the contract is typically static throughout the life of the contract, the amount of the initial margin that is required to be posted in respect of a cleared contract will fluctuate, sometimes significantly, throughout the life of the contract. The dynamic nature of the margin models utilized by the clearinghouses and the fact that the margin models might be changed at any time may subject the Client to an unexpected increase in collateral obligations by clearinghouses during a volatile market environment

which could have a detrimental effect on the Client. Clearinghouses also limit collateral that they will accept to cash, U.S. treasuries and, in some cases, other highly rated sovereign and private debt instruments, which may require a Client to borrow eligible securities from a dealer to meet margin calls and raise the costs of cleared trades to the Client. In addition, clearinghouses may not allow the Investment Adviser to portfolio margin (or cross margin) its Clients' positions, which may increase the amount of overall margin that the Client needs to post. While clearinghouse margin models are dynamic and may change daily, they are also different from the margin models applied by OTC derivative dealers. The OTC derivative dealers generally have a model that is supported by a team of individuals that analyze the credit risk of each fund and fund manager by reviewing, among other variables, strategy, performance, key portfolio managers, sophistication of technology and operations, traditional volatility, types of products, and lock-up periods. The model used by the dealers to apply margin is tailored for the risk of each fund and fund manager. In contrast, the clearinghouse margin model is applied across all types of counterparties and there is no analysis of individual counterparty risks. This may mean that the clearinghouse margin model may be less fluid. It may mean that it is also more expensive overall for the Client than if specific factors of the Client were considered.

Also, each clearinghouse only covers a limited range of products and the Investment Adviser may have to spread its Clients' derivative portfolios across multiple clearinghouses, which in turn reduces the benefits of netting that derivatives users rely on to mitigate counterparty risk.

Although standardized clearing for derivatives is intended to reduce risk (for instance, they may reduce the counterparty risk to the dealers to which a Client would be exposed under OTC derivatives), it does not eliminate risk. Rather, standardized clearing transfers risk of default from the over-the-counter derivatives dealer to the central clearinghouse, which may increase systemic risk, potentially more so than a failure by an OTC derivatives counterparty. The failure of a clearinghouse could have a significant impact on the financial system. Even if a clearinghouse does not fail, large losses could force significant capital calls on member firms during a financial crisis, which could lead member firms to default, worsening the crisis. Because these clearinghouses are still developing and the related bankruptcy process is untested, it is difficult to speculate what the actual risks would be to a Client related to the default of a clearinghouse. While the futures model worked well during the Lehman crisis in 2008, there has been no testing whether the model is scalable so that it would apply to derivatives more generally. In addition, there is no one international standard for clearinghouses; existing clearinghouses have different waterfalls that apply upon the insolvency of a clearinghouse or a clearinghouse member and it is possible that a Client could be in a worse position if a clearinghouse were to fail than had the Investment Adviser executed a trade on such Client's behalf with a traditional derivatives counterparty. Also, a clearinghouse will likely require that a Client relinquish control of its transactions if the clearinghouse were to become insolvent, and, therefore, the Investment Adviser would not be able to cause a Client to terminate and close out of a defaulting clearinghouse's positions, but would become subject to regulators' control over those positions. In such a circumstance, the Investment Adviser may not be able to take actions that it deems appropriate to lessen the impact of such clearinghouse default. Clearinghouses tend to trade in particular products in order to achieve economy of scale. This heightens the concentration risk for Clients, which might not be easily hedged. In such case, the Investment Adviser may only be able to protect its Clients from clearinghouse risk by exiting the market entirely, potentially foregoing an entire segment of beneficial transactions.

Applicable regulations may also require the Investment Adviser to make public a Client's information regarding its swaps volume, position size and/or trades, which could detrimentally impact the Investment Adviser's ability to achieve its Clients' investment objectives.

**Credit Ratings.** In general, the credit rating assigned by a nationally recognized rating agency to a security represents such rating agency's opinion of the safety of the principal and interest payments of the rated instrument based on available information. Such ratings are relative and subjective; they are not absolute standards of quality and do not evaluate the market value risk of such securities. Such ratings also do not reflect macroeconomic or systemic risk, including the risk of increased illiquidity in the credit markets. Further, credit ratings may change over time due to various factors, including changes in the creditworthiness of the issuer and/or changes in the rating agency's analytics and processes. It is possible that a rating agency might not change its rating of a particular issue on a timely basis to reflect subsequent events and, as a result, outstanding ratings may not reflect the issuer's current credit standing. Clients may incur losses if the Investment Adviser makes investments based on credit ratings that subsequently change in a way not favorable to such Clients' investment objectives.

**Counterparty Fraud.** Of paramount concern in investments is the possibility of material misrepresentation or omission on the part of a counterparty. Such inaccuracy or incompleteness may adversely affect the valuation of the collateral underlying an investment. The Investment Adviser relies upon the accuracy and completeness of representations made by counterparties to the extent reasonable, but cannot guarantee such accuracy or completeness. Under certain circumstances, payments to a Client may be reclaimed if any such payment or distribution is later determined to have been a fraudulent conveyance or a preferential payment.

**Counterparty Insolvency.** A Client's assets may be held in one or more accounts maintained for such Client by counterparties, including its prime brokers. There is a risk that any of such counterparties could become insolvent. The insolvency of a Client's counterparties is likely to impair the operational capabilities or the assets of such Client. Although the Investment Adviser regularly monitors the financial condition of the counterparties it uses, if one or more of a Client's counterparties were to become insolvent or the subject of liquidation proceedings in the U.S. (either under the Securities Investor Protection Act or the U.S. Bankruptcy Code), there exists the risk that the recovery of the Client's securities and other assets from such prime broker or broker-dealer will be delayed or be of a value less than the value of the securities or assets originally entrusted to such prime broker or broker-dealer.

In addition, the Investment Adviser may cause its Clients to use counterparties located in various jurisdictions outside the U.S. 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 a Client'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 a Client and its assets. Investors in a Fund should assume that the insolvency of any Fund counterparty would result in a loss to the Fund, which could be material.

**Competition; Availability of Investments.** Certain markets in which the Investment Adviser may cause its Clients to invest are extremely competitive for attractive investment opportunities. As a result, there can be no assurance that the Investment Adviser will be able to identify or successfully pursue attractive investment opportunities in such environments.

**Exposure to Material Non-Public Information.** From time to time, the Investment Adviser may receive material non-public information with respect to an issuer of publicly traded securities. In such circumstances, the Investment Adviser may be prohibited, by law, policy or contract, for a period of time from causing a Client to (i) unwind a position in such issuer, (ii) establish an initial position or take any greater position in such issuer, (iii) pursue other investment opportunities related to such issuer, and (iv) invest in securities of other issuers for which the Investment Adviser deems itself and its Clients restricted by virtue of the Investment Adviser's involvement in such issuer of publicly traded securities.

**Currency Exchange Exposure.** The Investment Adviser may cause its Clients to invest in securities denominated in non-U.S. currencies, the prices of which are determined with reference to currencies other than the U.S. dollar. The Investment Adviser, however, values its Clients' securities in U.S. dollars. The Investment Adviser may or may not seek to hedge its Clients' non-U.S. currency exposure by entering into currency hedging transactions, such as treasury locks, forward contracts, futures contracts and cross-currency swaps. There can be no guarantee that securities suitable for hedging currency or market shifts will be available at the time when the Investment Adviser wishes to use them, or that hedging techniques employed by the Investment Adviser will be effective. Furthermore, certain currency market risks may not be fully hedged or hedged at all. To the extent unhedged, the value of a Client'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. Such fluctuations may result in a loss to any affected Clients.

Furthermore, Clients may incur costs in connection with conversions between various currencies. Non-U.S. currency exchange dealers realize a profit based on the difference between the prices at which they are buying and selling various currencies. Thus, a dealer normally will offer to sell currency to a Client at one rate, while offering a lesser rate of exchange should the Investment Adviser desire immediately to cause its Client to resell that currency to the dealer. The Investment Adviser will cause its Clients to conduct currency exchange transactions either on a spot (*i.e.*, cash) basis at the spot rate prevailing in the currency exchange market, or through entering into forward or options contracts to purchase or sell non-U.S. currencies. It is anticipated that most of a Client's currency exchange transactions will occur at the time non-U.S. dollar denominated investments are purchased and sold and will be executed through a Client's prime brokers or a local broker or custodian acting for the Client.

The Investment Adviser may seek to protect the value of some portion or all of its Clients' portfolio holdings against currency fluctuations by engaging in hedging transactions, but there can be no assurance that such hedging transactions will be effective. The Investment Adviser may cause its Clients to enter into forward contracts on currencies, as well as purchase put or call options on currencies, in U.S. or non-U.S. markets. There can be no guarantee that instruments suitable for hedging currency risk will be available at the time when the Investment Adviser wishes to cause its Clients to use them or will be able to be liquidated when the Investment Adviser wishes to do so.

**Restricted Investments.** The Investment Adviser may cause its Clients to invest in securities which are subject to legal or other restrictions on transfer. The market prices, if any, for such securities tend to be volatile and may not be readily ascertainable, and the Client 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. Restricted securities may sell at a price lower than similar securities that are not subject to restrictions on resale.

**Non-U.S. Investments.** The Investment Adviser expects to cause its Clients to make investments in companies outside the United States. Investing in the securities of companies in non-U.S. countries involves certain considerations not usually associated with investing in securities of U.S. companies or U.S. markets, 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, gross sale or disposition proceeds 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 the investment opportunities that the Investment Adviser may be able to pursue on behalf of its Clients. In addition, accounting and financial reporting standards that prevail in such countries generally are not equivalent to U.S. standards and, consequently, less information is available to investors in companies located in such countries than is available to investors in companies located in the U.S. There is also less regulation, generally, of the securities markets in such countries than there is in the U.S. As a result, the Investment Adviser may be unable to structure its Clients' transactions to achieve the intended results or to mitigate all risks associated with such markets. It may also be difficult to enforce a Client's rights in such markets. For example, securities traded on non-U.S. exchanges and the non-U.S. persons that trade these instruments are not subject to the jurisdiction of the SEC or the CFTC, the securities and commodities laws and regulations of the U.S. Accordingly, the protections accorded to a Client under such laws and regulations are unavailable for transactions on non-U.S. exchanges and with non-U.S. counterparties.

**Emerging Markets Generally.** In addition to the risks associated with investments outside of the United States, investments in emerging markets (*i.e.*, developing countries, such as certain Asian, European or Latin American countries) may involve additional risks. Emerging markets generally are not as efficient as those in developed countries. In some cases, a market for the financial instrument may not exist locally, and transactions will need to be made on a neighboring exchange or OTC. Volume and liquidity levels in emerging markets are lower than in developed countries. When seeking to sell emerging market financial instruments, little or no market may exist for such instruments. In addition, imposition of exchange regulations, limitations on removal of funds, political instability, corruption and confiscatory taxation are more likely to occur in emerging markets.

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 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.

Many of the laws that govern private and foreign investment, securities transactions and contractual relationships in non-U.S. countries, particularly in developing countries, are new and largely untested. As a result, Clients may be subject to a number of unusual risks, including inadequate investor protection, contradictory legislation, incomplete, unclear and changing laws, ignorance or breaches of regulations on the part of other market participants, lack of established or effective avenues for legal redress, lack of standard practices and confidentiality customs characteristic of developed markets, and lack of enforcement of existing regulations.

### C. Risks Associated With Particular Types of Securities.

We do not recommend a particular type of investment instrument to our Clients, but rather, we recommend and invest in multiple investment instruments. Given the broad discretion we have in managing our Clients' portfolios, any one or more of the risks listed in the previous section may be incurred by our clients.

However, because it may be useful in understanding our investment program, set forth below is a non-exclusive list of certain risks related to securities and other instruments that may be utilized within our Clients' portfolios:

**Debt Investments.** Private and public debt investments of all types may have speculative characteristics, regardless of whether they are rated. The issuers of such instruments (including sovereign issuers) may face significant ongoing uncertainties and exposure to adverse conditions that may undermine the issuer's ability to make timely payment of interest and principal in accordance with the terms of the obligations.

*Dealer Market Making.* The value of a Client's fixed-income investments will be affected by general fixed-income market conditions, such as the volatility and liquidity of the fixed-income market, which are affected by the ability of dealers to "make a market" in fixed-income investments. In recent years, the market for bonds has significantly increased while dealer inventories have significantly decreased, relative to market size. This reduction in dealer inventories may be attributable to regulatory changes, such as capital requirements, and is expected to continue. As dealers' inventories decrease, so does their ability to make a market (and, therefore, create liquidity) in the fixed-income market. Especially during periods of rising interest rates, this could result in greater volatility and illiquidity in the fixed-income market, which could impair a Client's profitability or result in losses.

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

*Prepayment Risk.* The frequency at which prepayments (including voluntary prepayments by the obligors and accelerations due to defaults) occur on debt instruments will be affected by a variety of factors including the prevailing level of interest rates and spreads as well as economic, demographic, tax, social, legal and other factors. Generally, obligors tend to prepay their fixed rate obligations when prevailing interest rates fall below the coupon rates on their obligations. Similarly, floating rate issuers and borrowers tend to prepay their obligations when spreads narrow.

In general, "premium" securities (securities whose market values exceed their principal or par amounts) are adversely affected by faster than anticipated prepayments, and "discount" securities (securities whose principal or par amounts exceed their market values) are adversely affected by slower than anticipated prepayments. Since many fixed rate obligations will be discount instruments when interest rates and/or spreads are high, and will be premium instruments when interest rates and/or spreads are low, such debt instruments may be adversely affected by changes in prepayments in any interest rate environment.

The adverse effects of prepayments may impact a Client's portfolio in two ways. First, particular investments may experience outright losses, as in the case of an interest-only instrument in an environment of faster actual or anticipated prepayments. Second, particular investments may underperform relative to hedges that the Investment Adviser may have constructed for these investments, resulting in a loss to the Client's overall portfolio. In particular, prepayments (at par) may limit the potential upside of many instruments to their principal or par amounts, whereas their corresponding hedges often have the potential for unlimited loss.

*Zero-Coupon and Deferred Interest Bonds.* Zero-coupon bonds and deferred interest bonds are debt obligations issued at a significant discount from face value. The original discount approximates the total amount of interest the bonds will accrue and compound over the period until maturity or the first interest accrual date at a rate of interest reflecting the market rate of the security at the time of issuance. While zero-coupon bonds do not require the periodic payment of interest, deferred interest bonds generally provide for a period of delay before the regular payment of interest begins. Such investments experience greater volatility in market value due to changes in interest rates than debt obligations that provide for regular payments of interest.

*High-Yield.* Bonds or other fixed-income securities that are "higher yielding" (including non-investment grade) debt securities are generally not exchange-traded and, as a result, these securities trade in the over-the-counter marketplace, which is less transparent and has wider bid/ask spreads than the exchange-traded marketplace. High-yield securities face ongoing uncertainties and exposure to adverse business, financial or economic conditions, which could lead to the issuer's inability to meet timely interest and principal payments. High-yield securities are generally more volatile and may or may not be subordinated to certain other outstanding securities and obligations of the issuer, which may be secured by substantially all of the issuer's assets. High-yield securities may also not be protected by financial covenants or limitations on additional indebtedness. The market values of certain lower-rated and unrated debt securities tend to reflect individual corporate developments to a greater extent than do higher-rated securities, which react primarily to fluctuations in the general level of interest rates, and tend to be more sensitive to economic conditions than are higher-

rated securities. Companies that issue such securities may be highly leveraged and may not have available to them more traditional methods of financing. In addition, the Investment Adviser may cause its Clients to invest in bonds of issuers that do not have publicly traded equity securities, making it more difficult to hedge the risks associated with such investments.

The Investment Adviser may cause its Clients to invest in obligations of issuers that are generally trading at significantly higher yields than had been historically typical of the applicable issuer's obligations. Such investments may include debt obligations that have a heightened probability of being in covenant or payment default in the future or that are currently in default and are generally considered speculative. The repayment of defaulted obligations is subject to significant uncertainties. Defaulted obligations might be repaid only after lengthy workout or bankruptcy proceedings, during which the issuer might not make any interest or other payments. Typically such workout or bankruptcy proceedings result only in partial recovery of cash payments or an exchange of the defaulted security for other debt or equity securities of the issuer or its affiliates, which may in turn be illiquid or speculative.

*Corporate Debt.* Bonds, notes and debentures issued by corporations may pay fixed, variable or floating rates of interest, and may include zero-coupon obligations. Corporate debt instruments may be subject to credit ratings downgrades. Other instruments may have the lowest quality ratings or may be unrated. In addition, the Investment Adviser may cause its Clients to pay interest in kind in connection with its investments in corporate debt and related financial instruments (*e.g.*, the principal owed to the Client in connection with a debt investment may be increased by the amount of interest due on such debt investment). Such investments may experience greater market value volatility than debt obligations that provide for regular payments of interest in cash and, in the event of a default, Clients may experience substantial losses.

*Mezzanine Debt.* Mezzanine debt is typically junior to the obligations of a company to senior creditors, trade creditors and employees. The ability of the Investment Adviser to influence a company's affairs, especially during periods of financial distress or following an insolvency, will be substantially less than that of senior creditors. Mezzanine debt instruments are often issued in connection with leveraged acquisitions or recapitalizations in which the issuers incur a substantially higher amount of indebtedness than the level at which they had previously operated. Default rates for mezzanine debt instruments have historically been higher than for more senior instruments. In the event of the insolvency of a portfolio company of a Client or similar event, the Client's debt investment therein will be subject to fraudulent conveyance, subordination and preference laws.

*Stressed Debt.* Stressed issuers are issuers that are not yet deemed distressed or bankrupt and whose debt securities are trading at a discount to par, but not yet at distressed levels. An example would be an issuer that is in technical default of its credit agreement, or undergoing strategic or operational changes, which results in market pricing uncertainty. The market prices of stressed and distressed instruments are highly volatile, and the spread between the bid and the ask prices of such instruments is often unusually wide.

*Non-Performing Nature of Debt.* Certain debt instruments may be non-performing or in default. Furthermore, the obligor or relevant guarantor may also be in bankruptcy or liquidation. There can be no assurance as to the amount and timing of payments, if any, with respect to such debt instruments.

*Troubled Origination.* When financial institutions or other entities that are insolvent or in serious financial difficulty originate debt, the standards by which such instruments were originated, the recourse to the selling institution, or the standards by which such instruments are being serviced or operated may be adversely affected.

*Sovereign Debt and Other Public Debt.* Several factors may affect (i) the ability of a government, its agencies, instrumentalities or its central bank to make payments on the debt it has issued ("Sovereign Debt"), including securities that the Investment Adviser believes are likely to be included in restructurings of the external debt obligations of the issuer in question, (ii) the market value of such debt and (iii) the inclusion of Sovereign Debt in future restructurings, including such issuer's (x) balance of trade and access to international financing, (y) cost of servicing such obligations, which may be affected by changes in international interest rates, and (z) level of international currency reserves, which may affect the amount of non-U.S. exchange available for external debt payments. Significant ongoing uncertainties and exposure to adverse conditions may undermine the issuer's ability to make timely payment of interest and principal, and issuers may default on their Sovereign Debt.

*Equitable Subordination.* Under common law principles that in some cases form the basis for lender liability claims, if a lender (i) intentionally takes an action that results in the undercapitalization of a borrower or issuer to the detriment of other creditors of such borrower or issuer, (ii) engages in other inequitable conduct to the detriment of such other creditors, (iii) engages in fraud with respect to, or makes misrepresentations to, such other creditors or (iv) uses its influence as a stockholder to dominate or control a borrower or issuer to the detriment of other creditors of such borrower or issuer, a court may elect to subordinate the claim of the offending lender or bondholder to the claims of the disadvantaged creditor or creditors (a remedy called "equitable subordination"). If the Investment Adviser causes a Client to engage in such conduct, the Client may be subject to claims from creditors of an obligor that debt held by the Client should be equitably subordinated.

**Loan Investments.** The Investment Adviser's success in the area of loan origination and loan investing will depend, in part, on its ability to originate or obtain loans on advantageous terms. In originating or purchasing loans, Clients will compete with a broad spectrum of investors and institutions. Increased competition for, or a diminution in the available supply of, qualifying loans could result in lower yields on such loans, which could reduce returns to investors.

*Leveraged Loans.* "Leveraged loans" are loans made to companies with a below investment-grade rating from any nationally recognized rating agency. Such loans may be performing poorly when the Client acquires them. There is no assurance that the Investment Adviser will correctly evaluate the value of the assets collateralizing such loans or the prospects for distribution on or repayment of such loans. A Client may lose its entire investment or may be required to accept cash, property or securities with a

value less than the Client's original investment and/or may be required to accept payment over an extended period of time.

*Hung Loans.* The term "hung loan" commonly refers to a loan that has been made (or has been committed to be made), and the lender is not able to syndicate the loan on the originally anticipated terms. Hung loans are illiquid and lack readily ascertainable market values; there is no assurance that the price to be paid for hung loans by a Client will reflect a discounted price that should allow the Investment Adviser to achieve a positive return for a Client on such loans or avoid losses. Since the price of the loans to be purchased is expected to continue to be significantly impacted by, in addition to the specific circumstances relating to each loan (*e.g.*, in the case of a loan relating to a leveraged buyout ("LBO"), the financial condition of the target), global and macro-economic conditions (*e.g.*, monetary policy, changes to currency exchange rates, governmental intervention or changes to existing laws, international geo-political events, etc.) as well as other systemic factors, it is possible that loans purchased by a Client will suffer significant impairments in value as a result of events not predicted by the Investment Adviser. The Investment Adviser may also face difficulties in disposing of or leveraging such loans, or in doing so without incurring losses for its Clients. The markets in which hung loans are purchased and sold have been volatile and are likely to continue to be volatile in the future.

*Bank Loans.* Bank loans are subject to unique risks, including: (i) the possible invalidation of an investment transaction as a fraudulent conveyance under relevant creditors' rights laws; (ii) so-called lender-liability claims by the issuer of the obligations; (iii) environmental liabilities that may arise with respect to collateral securing the obligations; and (iv) limitations on the ability of the Investment Adviser to directly enforce a Client's rights with respect to participations. Successful claims by third parties arising from these and other risks will be borne by the Client.

As secondary market trading volumes increase, new loans are frequently adopting standardized documentation to facilitate loan trading, which may improve market liquidity. There can be no assurance, however, that future levels of supply and demand in loan trading will provide an adequate degree of liquidity or that the current level of liquidity will continue. Because of the provision to holders of such loans of confidential information relating to the borrower, the unique and customized nature of the loan agreement, and the private syndication of the loan, loans are not as easily purchased or sold as a publicly traded security, and historically the trading volume in the loan market has been small relative to the high-yield debt market.

*Second Lien Loans.* The Investment Adviser may cause its Clients to originate or invest in loans that are secured by a second lien on assets. Second lien loans have been a developed market for a relatively short period of time, and there is limited historical data on the performance of second lien loans in adverse economic circumstances. In addition, second lien loan products are subject to intercreditor arrangements with the holders of first lien indebtedness, pursuant to which the second lien holders have waived many of the rights of a secured creditor, and some rights of unsecured creditors, including rights in bankruptcy that can materially affect recoveries. While there is broad market acceptance of some second lien intercreditor terms, no clear market standard has developed for certain other material intercreditor terms for second lien loan products. This variation in key intercreditor terms may result in dissimilar

recoveries across otherwise similarly situated second lien loans in insolvency or distressed situations. While uncertainty of recovery in an insolvency or distressed situation is inherent in all debt instruments, second lien loan products carry more risks than certain other debt products. Beginning in August 2007, the market for many loan products, including second lien loans, contracted significantly which made virtually all leveraged loan products, particularly second lien loan products, less liquid or illiquid. Many participants ceased underwriting and purchasing certain second lien loan products. There can be no assurance that the market for second lien loans will not contract further.

*Bridge Loans.* It is a common practice for financial institutions to commit to providing bridge loans to facilitate acquisitions, including LBOs, where they serve as advisers to the purchaser. Bridge loans are frequently made because, for timing or market reasons, longer-term financing is not available at the time the funds are needed, which is often at the time of the closing of an acquisition. In the past, these commitments were not frequently drawn upon due to the availability of other sources of financing; however, due to market conditions affecting the availability of these other sources of financing (principally high-yield bond transactions), bridge loan commitments have been and may be drawn upon more regularly. Since these commitments were not regularly drawn upon in the past, there is little history for investors to rely upon in evaluating investments in bridge loans. Bridge loans often have shorter maturities. Borrower and lenders typically agree to shorter maturities based on the anticipation that the bridge loans will be replaced with other forms of financing within such shorter time period. However, the source and timing of such replacement financing may be uncertain and can be affected by, among other things, market conditions and the financial condition of the borrower at the maturity date of the bridge. If the borrower is unable to obtain replacement financing and repay the bridge loan at maturity, the terms of the bridge loan may provide for the bridge loan to be converted to a longer term loan. If bridge loans are not repaid (or cannot be disposed of on favorable terms) on the dates projected by the Investment Adviser, there may be an adverse effect upon the ability of the Investment Adviser to manage the assets of its Clients in accordance with its models and projections or an adverse effect upon its Clients' performance and the ability of the Funds to make distributions.

*Debtor-in-Possession ("DIP") Loans.* Loans to companies that have filed for protection under Chapter 11 of the U.S. Bankruptcy Code, as amended, are most often asset-based, revolving working-capital facilities put into place at the outset of a Chapter 11 case to provide the debtor with both immediate cash and the ongoing working capital that will be required during the reorganization process. While such loans are generally less risky than many other types of loans as a result of their seniority in the debtor's capital structure and because their terms have been approved by a U.S. federal bankruptcy court order, it is possible that the debtor's reorganization efforts may fail and the proceeds of the ensuing liquidation of the DIP lender's collateral might be insufficient to repay in full the DIP loan.

*Fraud Associated with Loans.* Of paramount concern in loan investments is the possibility of material misrepresentation or omission on the part of the borrower or loan seller. Such inaccuracy or incompleteness may adversely affect the valuation of the collateral underlying the loans or may adversely affect the ability of the Investment Adviser to cause its Clients to perfect or effectuate a lien on the collateral securing the

loan. Clients will rely upon the accuracy and completeness of representations made by borrowers to the extent reasonable, but cannot guarantee such accuracy or completeness. Under certain circumstances, payments to a Client may be reclaimed if any such payment or distribution is later determined to have been a fraudulent conveyance or a preferential payment.

*Lender Liability Claims.* There may be circumstances where a loan or other debt investment of a Client could be subordinated to claims of other creditors or the Client could be subject to lender liability claims. If a company that a Client is invested in were to go bankrupt, even though the Investment Adviser may have structured the Client's investment as senior debt, depending on the facts and circumstances, a bankruptcy court might recharacterize such debt holding as an equity investment and subordinate or disallow all or a portion of the Client's senior debt claim to that of other creditors. In addition, lenders can be subject to lender liability claims for actions taken by them where they become too involved in the borrower's business or exercise control over the borrower as described above for debt instruments.

Additionally, should the Client need to collect on a defaulted loan, litigation could result. There is a high cost associated with any litigation and the results of litigation are always uncertain. Even before litigation is commenced, the Client could experience substantial costs in trying to collect on defaulted investments, such as legal fees, collection agency fees, or discounts related to the assignment of a defaulted loan to a third party.

*Incurrence of Additional Debt by Borrowers.* Although the Investment Adviser expects to negotiate approval rights on behalf of its Clients limiting or preventing borrowers from incurring further debt in addition to the loans, any such increase of debt levels could impair the ability of borrowers to service their loans, which in turn could result in higher rates of delinquency and loss on the loans originated by the Clients or otherwise underlying the Client's investments.

*Insufficient Collateral.* To the extent a Client originates loans based upon the adequacy of the borrower's collateral, an incorrect valuation of such collateral may result in unforeseen losses. Despite performing due diligence on the collateral, including, where appropriate (in the Investment Adviser's determination), by engaging third party independent valuers to estimate the value of the collateral pledged by the borrower, the inherent uncertainty of valuation of collateral may result in values that differ significantly from the values that can ultimately be obtained for such collateral. In addition, even if collateral is initially valued correctly, changes in market conditions, regulations or other circumstances, or changes directly related to such collateral, may materially adversely affect the value thereof.

**Distressed Obligations.** The obligations of issuers in weak financial condition, experiencing poor operating results, having substantial capital needs or negative net worth, facing special competitive or product obsolescence problems (including companies involved in bankruptcy or other reorganization and liquidation proceedings) are likely to be particularly risky investments although they also may offer the potential for correspondingly high returns. Among the risks inherent in investments in troubled entities is the risk that it frequently may be difficult to obtain information as to the true condition of such issuers. Such investments may also be adversely affected by laws relating to, among other things,

fraudulent transfers and other voidable transfers or payments, lender liability and the bankruptcy court's power to disallow, reduce, subordinate, re-characterize debt as equity or disenfranchise particular claims. Such companies' obligations may be considered speculative, and the ability of such companies to pay their debts on schedule could be affected by adverse interest rate movements, changes in the general economic climate, economic factors affecting a particular industry or specific developments within such companies. In addition, there is no minimum credit standard that is a prerequisite to the Client's investments in any security. Obligations in which the Investment Adviser causes a Client to invest may be less than investment grade, considered high yield or lack any conventional third-party rating. The level of analytical sophistication, both financial and legal, necessary for successful investment in companies experiencing significant business and financial difficulties is unusually high. There is no assurance that value of the assets collateralizing a Client's investments will be sufficient or that prospects for a successful reorganization or similar action will become available. In any reorganization or liquidation proceeding relating to a company in which a Client invests, the Client may lose its entire investment, may be required to accept cash or securities with a value less than its original investment and/or may be required to accept payment over an extended period of time. Under such circumstances, the returns generated from the Client's investments may not compensate the Client adequately for the risks assumed. In addition, under certain circumstances, payments and distributions may be disgorged if any such payment is later determined to have been a fraudulent conveyance or a preferential payment.

**Bankruptcy Claims.** Bankruptcy claims, which are amounts owed to creditors of companies that are debtors in pending bankruptcy cases, typically are illiquid and generally do not pay interest. The markets in U.S. bankruptcy claims are generally not regulated by U.S. federal securities laws or the SEC. Because bankruptcy claims are frequently unsecured, holders of such claims may have a lower priority in terms of payment than certain other creditors in a bankruptcy proceeding. In addition, the debt of companies in financial reorganization may be adversely affected by an erosion of the issuer's fundamental values. Accordingly, there can be no guarantee that the debtor will ever be able to satisfy the obligation on a bankruptcy claim.

Many of the events within a bankruptcy case are adversarial and often beyond the control of the creditors. While creditors generally are afforded an opportunity to appear and be heard, there can be no assurance that a bankruptcy court would not approve actions that may be contrary to the interests of Clients. Furthermore, there are instances where creditors lose their priority or are recharacterized as equity if, for example, they have exercised excessive control over management or engaged in misconduct that harms other creditors. In those cases where a Client, by virtue of such action, is found to exercise "domination and control" of a debtor, the Client may lose its priority if the debtor can demonstrate that its business was adversely impacted or other creditors and equityholders were harmed by the Client.

Generally, the duration of a bankruptcy case can only be roughly estimated. The reorganization of a company usually involves the development and negotiation of a plan of reorganization, plan approval by creditors and confirmation by the bankruptcy court. This process can involve substantial legal, professional and administrative costs to the company and Clients; it is subject to unpredictable and lengthy delays; and during the process the company's competitive position may erode, key management may depart and the company



may not be able to invest adequately. In some cases, the company may not be able to reorganize and may be required to liquidate assets.

U.S. bankruptcy law permits the classification of "substantially similar" claims in determining the classification of claims in a reorganization for the purpose of voting on a plan of reorganization. Because the standard for classification is vague, there exists a significant risk that a Client's influence with respect to a class of securities can be lost by the inflation of the number and the amount of claims in, or other gerrymandering of, the class. In addition, certain administrative costs and claims that have priority by law over the claims of certain creditors (for example, claims for taxes) may be quite high.

The Investment Adviser intends to cause its Clients to invest their assets in securities of issuers domiciled, or assets located, globally. Investment in the debt of financially distressed companies domiciled outside the United States involves additional risks. Bankruptcy law and process may differ substantially from that in the United States, resulting in greater uncertainty as to the rights of creditors, the enforceability of such rights, reorganization timing and the classification, seniority and treatment of claims. In certain developing countries, although bankruptcy laws have been enacted, the process for reorganization remains highly uncertain.

The Investment Adviser, on behalf of its Clients, may elect to serve on creditors' committees, equityholders' committees or other groups to ensure preservation or enhancement of the Client's positions as a creditor or equityholder. A member of any such committee or group may owe certain obligations generally to all parties similarly situated that the committee represents. The Investment Adviser may resign from that committee or group for any reason, including, for example, if the Investment Adviser concludes that its obligations owed to the other parties as a committee or group member conflict with its duties owed to its Clients. In such case, Clients may not realize the benefits, if any, of participation on the committee or group. In addition, if a Client is represented on a committee or group, it may be restricted or prohibited under applicable law from disposing of or increasing its investments in such company while it continues to be represented on such committee or group.

The Investment Adviser may cause its Clients to purchase creditor claims subsequent to the commencement of a bankruptcy case. Under judicial decisions, it is possible that such purchase may be disallowed by the bankruptcy court if the court determines that the purchaser has taken unfair advantage of an unsophisticated seller, which may result in the rescission of the transaction (presumably at the original purchase price) or forfeiture by the purchaser. Additionally, the claim may be disallowed or subordinated if the bankruptcy court determines that the seller engaged in inequitable conduct that harmed other creditors.

Reorganizations can be contentious and adversarial, and it is by no means unusual for participants to use the threat of, as well as actual, litigation as a negotiating technique. The expense of defending against claims by third parties and paying any amounts pursuant to settlements or judgments would generally be borne by Clients.

**Municipal Securities.** Various factors may adversely affect the value and yield of municipal securities. These factors include political or legislative changes and uncertainties related to the tax status of municipal securities or the rights of investors in these securities. To the extent that the Investment Adviser causes a Client to invest heavily in a particular state's

municipal securities, the Client will be more vulnerable to factors affecting that state. The Client's investments in revenue securities, where principal and interest payments are made from the revenue of a specific project or facility, and not general tax revenues, may have increased risks. Factors affecting the project or facility, such as local business or economic conditions, could have a significant impact on the project's ability to make payments of principal and interest on these securities. Appropriation bonds have legislative risk. The market for municipal securities does not permit shorting and has low liquidity and intermediation. Distressed issuers of such bonds may not be able to avail themselves of bankruptcy courts or the Bankruptcy Code in general.

**Convertible Securities.** A convertible security may be subject to redemption at the option of the issuer at a price established in the convertible security's governing instrument. If a convertible security held by a Client is called for redemption, the Client will be required to permit the issuer to redeem the security, convert it into the underlying common stock or sell it to a third party. Any of these actions could have an adverse effect on the Investment Adviser's ability to achieve the Client's investment objective.

**Structured Notes.** Structured notes, variable rate mortgage-backed and asset-backed securities may each have rates of interest that vary based on a designated floating rate formula or index. The value of these investments is closely tied to the absolute levels of such rates or indices, or the market's perception of anticipated changes in those rates or indices. The movements in specific indices or interest rates may be difficult or impossible to hedge.

**Collateralized Debt Obligations.** There are a variety of different types of collateralized debt obligations ("CDOs"), including CDOs collateralized by trust preferred securities and asset-backed securities and CDOs collateralized by corporate loans and debt securities called collateralized loan obligations ("CLOs"). CDOs may issue several types of securities, including, without limitation, CDO and CLO equity, multi-sector CDO equity, trust preferred CDO equity and CLO debt. CDOs are subject to credit, liquidity and interest rate risks, which are each discussed in greater detail above. The CDO equity will usually be unrated or non-investment grade. As a holder of CDO equity, Clients will have limited remedies available upon the default of the CDO. CDOs often invest in concentrated portfolios of assets. The concentration of an underlying portfolio in any one obligor would subject the related CDOs to a greater degree of risk with respect to defaults by such obligor and the concentration of a portfolio in any one industry would subject the related CDOs to a greater degree of risk with respect to economic downturns relating to such industry.

**Derivative Instruments Generally.** 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. Derivatives traded over-the-counter may not have an authoritative source of valuation and the models used to value such derivatives is subject to change. Special risks may apply in the future that cannot be determined at this time with respect to certain other derivative instruments that are not presently contemplated for use or that are currently not available. The regulatory and tax environment for derivative instruments in which the Investment Adviser may cause its Clients to participate is evolving, and changes in the regulation or taxation of such securities may have a material adverse effect on Clients.

*Call Options.* There are risks associated with the sale and purchase of call options. The seller (writer) of a call option which is covered (*e.g.*, the writer holds the underlying security) assumes the risk of a decline in the market price of the underlying security below the purchase price of the underlying security offset by the gain by the premium received if the option expires out of the money, and gives up the opportunity for gain on the underlying security above the exercise price of the option. The seller of an uncovered call option assumes the risk of a theoretically unlimited increase in the market price of the underlying security above the exercise price of the option. The buyer of a call option assumes the risk of losing the premium if the option expires out of the money.

*Put Options.* There are risks associated with the sale and purchase of put options. The seller (writer) of a put option which is covered (*e.g.*, the writer has a short position in the underlying security) assumes the risk of an increase in the market price of the underlying security above the sale price of the short position of the underlying security offset by the premium if the option expires out of the money, and thus the gain in the premium, and the option seller gives up the opportunity for gain on the underlying security below the exercise price of the option. The seller of an uncovered put option assumes the risk of a decline in the market price of the underlying security to zero. The buyer of a put option assumes the risk of losing the premium if the option expires out of the money.

*Index or Index Options.* The value of an index or index option fluctuates with changes in the market values of the securities included in the index. Because the value of an index or index option depends upon movements in the level of the index rather than the price of a particular security, whether Clients will realize appreciation or depreciation from the purchase or writing of options on indices depends upon movements in the level of instrument prices in the security market generally or, in the case of certain indices, in an industry or market segment, rather than movements in the price of particular securities.

*Index Futures.* The price of index futures contracts may not correlate perfectly with the movement in the underlying index because of certain market distortions. First, all participants in the futures market are subject to margin deposit and maintenance requirements. Rather than meeting additional margin deposit requirements, shareholders may close futures contracts through offsetting transactions that would distort the normal relationship between the index and futures markets. Second, from the point of view of speculators, the deposit requirements in the futures market are less onerous than margin requirements in the securities market. Therefore, increased participation by speculators in the futures market also may cause price distortions. Successful use of index futures contracts by the Investment Adviser on behalf of its Client is also subject to the Investment Adviser's ability to correctly predict movements in the direction of the market.

*Futures Contracts.* The Investment Adviser may cause its Clients to invest in futures contracts or options thereon. Futures positions may be illiquid because, for example, many 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 contract for a particular

future has increased or decreased by an amount equal to the daily limit, positions in the future can neither be taken nor liquidated unless traders are willing to effect trades at or within the limit. Futures contract prices on various commodities or financial instruments occasionally have moved the daily limit for several consecutive days with little or no trading. Similar occurrences could prevent the Investment Adviser from promptly liquidating unfavorable positions held by its Clients and subject such Clients to substantial losses. In addition, the Investment Adviser may not be able to execute futures contract trades at favorable prices if trading volume in such contracts is low. It is also possible that an exchange or a regulator may suspend trading in a particular contract, order immediate liquidation and settlement of a particular contract or order that trading in a particular contract be conducted for liquidation only.

*Non-U.S. Futures Transactions.* Foreign futures transactions involve executing and clearing trades on a foreign exchange. This is the case even if the foreign exchange is formally "linked" to a domestic exchange, whereby a trade executed on one exchange liquidates or establishes a position on the other exchange. No domestic organization regulates the activities of a foreign exchange, including the execution, delivery and clearing of transactions on such an exchange, and no domestic regulator has the power to compel enforcement of the rules of the foreign exchange or the laws of the foreign country. Moreover, such laws or regulations will vary depending on the foreign country in which the transaction occurs. For these reasons, Clients may not be afforded certain of the protections which apply to domestic transactions, including the right to use domestic alternative dispute resolution procedures. In particular, funds received from customers to margin foreign futures transactions may not be provided the same protections as funds received to margin futures transactions on domestic exchanges. In addition, the price of any foreign futures or option contract and, therefore, the potential profit and loss resulting therefrom, may be affected by any fluctuation in the foreign exchange rate between the time the order is placed and the time the foreign futures contract is liquidated or the time the foreign option contract is liquidated or exercised.

*Forward Trading.* Forward contracts and options thereon, unlike futures contracts, are generally 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 or 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 Adviser on behalf of its Clients 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 Adviser would otherwise recommend, to the possible detriment of its Clients. Market illiquidity or disruption could result in major losses to Clients.

*Swap Agreements.* The Investment Adviser may cause its Clients to enter into swap agreements. These agreements are individually negotiated and can be structured

to include exposure to a variety of different types of investments, asset classes or market factors. Depending on their structure, swap agreements may increase or decrease a Client's exposure to, for example, equity securities. Swap agreements can take many different forms and are known by a variety of names. The Investment Adviser is not limited to any particular form of swap agreement if consistent with the applicable Client's investment objective. Whether the Investment Adviser's use of swap agreements will be successful depends on the Investment Adviser's ability to select appropriate transactions for its Clients. Swap transactions may be highly illiquid and may increase or decrease the volatility of the Client's portfolio. Moreover, Clients 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. Clients also bear the risk of loss related to swap agreements, for example, for breaches of such agreements or the failure of the Investment Adviser to post or maintain required collateral on behalf of the applicable Clients. 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 Investment Adviser's ability to terminate a Client's existing swap transactions or to realize amounts to be received under such transactions.

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

*High Volatility.* The prices of derivative instruments, including currencies, futures and option prices, can be highly volatile. Price movements of derivative contracts in which a Client's portfolio's assets may be invested are 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, governments from time to time intervene, directly and by regulation, in certain markets, particularly those in currencies, financial instruments, futures and options. Such intervention often is intended directly to influence prices and may, together with other factors, cause all of such markets to move rapidly in the same direction because of, among other things, interest rate fluctuations. The Client's portfolio is also subject to the risk of the failure of any exchanges on which its positions trade or of their clearinghouses.

**Currencies.** The Investment Adviser may cause its Clients to enter into spot and forward currency contracts or invest in currency futures contracts and options on currencies and futures to hedge currency risk by shifting exposure to foreign currency fluctuations from one currency to another with respect to the Client. Currency transactions made on a spot (*i.e.*, cash) basis are at the spot rate prevailing in the currency exchange market. A forward currency contract, which involves an obligation to purchase or sell a specific currency at a future date at a price set at the time of the contract, reduces the Client's exposure with respect

to its investment to changes in the value of the currency it will deliver and increases the Client's exposure to changes in the value of the currency it will receive for the duration of the contract.

Currency trading is subject to risks different from those of other securities transactions. Because exchange rate control is of great importance to the issuing governments and influences economic planning and policy, purchases and sales of currency and related instruments can be negatively affected by government exchange controls, blockages, and manipulations or exchange restrictions imposed by governments. These government actions can result in losses to the Client if the Investment Adviser is unable to deliver or receive currency or funds on behalf of the Client in settlement of obligations. Buyers and sellers of currency futures are subject to the same risks that apply to the use of futures generally. Furthermore, settlement of a currency forward contract for the purchase of most currencies must occur at a bank based in the issuing nation. The ability to establish and close out options on currency futures is subject to the maintenance of a liquid market, which may not always be available. Currency exchange rates may fluctuate based on factors extrinsic to that country's economy.

At or before the maturity of a forward currency contract, the Investment Adviser may either cause the Client to make delivery of the currency, or terminate the Client's contractual obligation to deliver the currency by buying an "offsetting" contract obligating it to buy, on the same maturity date, the same amount of the currency.

If the Investment Adviser causes a Client to engage in an offsetting transaction, it may later enter into a new forward currency contract to sell the currency. If the Client engages in an offsetting transaction, it will incur a gain or loss to the extent that there has been movement in forward currency contract prices. If forward prices go down during the period between the date the Client enters into a forward currency contract for the sale of a currency and the date it enters into an offsetting contract for the purchase of the currency, the Client will realize a gain to the extent that the price of the currency it has agreed to sell exceeds the price of the currency it has agreed to buy. If forward prices go up, the Client will suffer a loss to the extent the price of the currency it has agreed to buy exceeds the price of the currency it has agreed to sell.

**Equity Securities.** The Investment Adviser will cause its Clients' investment portfolios to include equity and equity-related securities of U.S. and non-U.S. companies, especially (but not limited to) credit-sensitive equity and equity-related securities. The value of equity securities of public companies and equity derivatives generally varies with the performance of the issuer and movements in the equity markets. As a result, a Client may suffer losses if it will invest in equity instruments of issuers whose performance diverges from the Investment Adviser's expectations or if equity markets generally move in a single direction and the Investment Adviser has not caused the Client to hedge against such a general move.

**ABS and MBS Generally.** The investment characteristics of asset-backed securities ("ABS") and mortgage-backed securities ("MBS"), whether issued by U.S. or non-U.S. issuers, differ from traditional debt securities. Among the major differences are that interest and principal payments are made more frequently, usually monthly, and that the principal may be prepaid at any time because the underlying loans or other assets generally may be prepaid at any time.

*ABS and MBS Subordinated Securities.* Investments in subordinated MBS and ABS involve greater credit risk of default than the senior classes of the issue or series. Default risks may be further pronounced in the case of MBS and ABS secured by, or evidencing an interest in, a relatively small or less diverse pool of underlying loans. Certain subordinated securities absorb all losses from default before any other class of securities is at risk, particularly if such securities have been issued with little or no credit enhancement or equity. Such securities, therefore, possess some of the attributes typically associated with equity investments.

*Commercial MBS.* Mortgage loans on commercial properties often are structured so that a substantial portion of the loan principal is not amortized over the loan term but is payable at maturity and repayment of the loan principal thus often depends upon the future availability of real estate financing from the existing or an alternative lender and/or upon the current value and salability of the real estate. Therefore, the unavailability of real estate financing may lead to default.

Most commercial mortgage loans underlying MBS are effectively nonrecourse obligations of the borrower, meaning that there is no recourse against the borrower's assets other than the collateral. If borrowers are not able or willing to refinance or dispose of encumbered property to pay the principal and interest owed on such mortgage loans, payments on the subordinated classes of the related MBS are likely to be adversely affected. The ultimate extent of the loss, if any, to the subordinated classes of MBS may only be determined after a negotiated discounted settlement, restructuring or sale of the mortgage note, or the foreclosure (or deed in lieu of foreclosure) of the mortgage encumbering the property and subsequent liquidation of the property. Foreclosure can be costly and delayed by litigation and/or bankruptcy. Factors such as the property's location, the applicable U.S. or non-U.S. laws and regulations, the legal status of title to the property, its physical condition and financial performance, environmental risks and governmental disclosure requirements with respect to the condition of the property may make a third party unwilling to purchase the property at a foreclosure sale or to pay a price sufficient to satisfy the obligations with respect to the related MBS. Revenues from the assets underlying such MBS may be retained by the borrower and the return on investment may be used to make payments to others, maintain insurance coverage, pay taxes or pay maintenance costs. Such diverted revenue is generally not recoverable without a court appointed receiver to control collateral cash flow.

*ABS.* ABS are not secured by an interest in the related collateral. Credit card receivables, for example, are generally unsecured and the debtors are entitled to the protection of a number of U.S. federal and state or non-U.S. consumer loan laws, many of which give such debtors the right to set off certain amounts owed on the credit cards, thereby reducing the balance due. Most issuers of ABS backed by automobile receivables permit the servicers to retain possession of the underlying obligations. If the servicer were to sell these obligations to another party, there is a risk that the purchaser would acquire an interest superior to that of the holders of the related ABS. In addition, because of the large number of vehicles involved in a typical issuance and technical requirements under state laws, the trustee for the holders of the ABS may not have a proper security interest in all of the obligations backing such ABS. Therefore, there is a possibility that recoveries on repossessed collateral may not, in some cases,

be available to support payments on these securities. The risk of investing in ABS is ultimately dependent upon payment of consumer loans by the debtor.

The collateral supporting ABS is of shorter maturity than certain other types of loans and is less likely to experience substantial prepayments. ABS are often backed by pools of any variety of assets, including, for example, leases, mobile home loans and aircraft leases, which represent the obligations of a number of different parties and use credit enhancement techniques such as letters of credit, guarantees or preference rights. The value of an ABS is affected by changes in the market's perception of the asset backing the security and the creditworthiness of the servicing agent for the loan pool, the originator of the loans or the financial institution providing any credit enhancement, as well as by the expiration or removal of any credit enhancement.

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

Investments in RMBS may experience losses or reduced yield if, for example, (i) the borrower of an underlying residential mortgage loan defaults or is unable to make payments, (ii) the underlying residential mortgage loans are prepaid, (iii) there is a general decline in the housing market, or (iv) violations of particular provisions of certain U.S. federal laws by an issuer of RMBS limit the ability of the issuer to collect all or part of the principal of or interest on the related underlying loans.



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

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

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

**A. Broker-Dealer Registration Status.**

The Investment Adviser and its management persons are not registered as broker-dealers and do not have any application pending to register with the SEC as a broker-dealer or registered representative of a broker-dealer.

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

The Investment Adviser meets the definition of a commodity pool operator ("CPO") and, depending on the amount of commodity interests that we trade, we may be required to register with the CFTC and become a member of the National Futures Association ("NFA"). However, the Investment Adviser will claim an exemption from the obligations of a CFTC-registered CPO with respect to the Funds pursuant to CFTC Rule 4.13(a)(3) based on its trading a *de minimis* level of commodity interests and, accordingly, will not be subject to the CFTC's and NFA's regulatory requirements with respect to the Fund that would otherwise be applicable absent such an exemption. The Investment Adviser may in the future fully register as a CPO with the CFTC and instead claim an exemption from certain of the CFTC's disclosure, reporting and record-keeping requirements applicable to registered CPOs pursuant to CFTC Rule 4.7.

The Investment Adviser is exempt from registration with the CFTC as a commodity trading advisor.

**C. Material Relationships or Arrangements with Industry Participants.**

We do not have any material relationships or arrangements with industry participants.

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

We do not recommend or select other investment advisers for our clients.

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

A. Code of Ethics.

We strive to adhere to the highest industry standards of conduct based on principles of professionalism, integrity, honesty and trust. In seeking to meet these standards, we have adopted a Code of Ethics (the "Code"). The Code incorporates the following general principles that all employees are expected to uphold:

- employees must at all times place the interests of Clients first;
- all personal securities transactions must be conducted in a manner consistent with the Code and any actual or potential conflicts of interest or any abuse of an employee's position of trust and responsibility must be avoided;
- employees must not take any inappropriate advantage of their positions;
- information concerning the identity of securities and financial circumstances of Clients, including the Funds' investors, must be kept confidential; and
- independence in the investment decision-making process must be maintained at all times.

Clients or prospective clients may request a copy of the Code by contacting us at the address or telephone number listed on the first page of this document.

B. Securities in which the Investment Adviser or a Related Person Has a Material Financial Interest.

1. *Cross Trades*

The Investment Adviser may determine that it would be in the best interests of certain Clients to transfer a security from one Client to another (each such transfer, a "Cross Trade") for a variety of reasons, including, without limitation, tax purposes, liquidity purposes, to rebalance the portfolios of the Clients, or to reduce transaction costs that may arise in an open market transaction. If the Investment Adviser decides to engage in a Cross Trade, the Investment Adviser will determine that the trade is in the best interests of each Client involved in such trade and take steps to ensure that the transaction is consistent with the duty to obtain best execution for each of those Clients.

The Investment Adviser will generally execute Cross Trades with the assistance of a broker-dealer who executes and books the transaction at the close of the market on the day of the transaction. Alternatively, a Cross Trade between two Clients may occur as an "internal cross," where the Investment Adviser instructs the custodian for the Clients to book the transaction at the price determined in accordance with the Investment Adviser's valuation policy. If the Investment Adviser effects an internal cross, the Investment Adviser will not receive any fee in connection with the completion of the transaction.

## 2. *Principal Transactions*

To the extent that Cross Trades may be viewed as “Adviser Principal Transactions”<sup>2</sup> due to the ownership interest in a Client by the Investment Adviser or its personnel, the Investment Adviser will comply with the requirements of Section 206(3) of the Advisers Act, including that any such Adviser Principal Transactions will be considered on behalf of investors in such a Client and approved or disapproved by (i) an advisory board comprised of representatives of such investors or (ii) a committee consisting of one or more persons selected by the Investment Adviser (or its affiliate), and any valuation approved by such a committee will be determined by an independent third party that has appropriate experience in providing such valuations.

### C. Investing in Securities that the Investment Adviser or a Related Person Recommends to Clients.

The Code places restrictions on personal trades by employees, including that they disclose their personal securities holdings and transactions to the Investment Adviser on a periodic basis, and requires that employees pre-clear certain types of personal securities transactions.

Generally, and subject to certain exceptions, the Investment Adviser's employees may engage in personal securities trading. Any purchases and sales of covered securities require pre-clearance and are subject to certain holding requirements and limitations with respect to the number of trades a related person may engage in over a given month. However, related persons may purchase and sell mutual funds and broad-based exchange-traded funds (“ETFs”) without pre-clearance, subject to certain minimum holding periods. Related persons are prohibited from making purchases and sales of securities that the Investment Adviser causes its Clients to invest in, unless a related person owned such securities prior to working for the Investment Adviser or before Clients invested in such securities, in which case such a related person may sell the applicable securities subject to pre-approval.

The Investment Adviser, 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 the Investment Adviser and its personnel may have investments in some Funds but not in others or may have different levels of investments in the various Funds.

The Investment Adviser 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.

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<sup>2</sup> In a Principal Transaction, an adviser, acting for its own account, buys a security from, or sells a security to, the account of a client.

D. Conflicts of Interest Created by Contemporaneous Trading.

The Investment Adviser manages investments on behalf of a number of Clients. Certain Clients have investment programs that are similar to or overlap and may, therefore, participate with each other in investments. It is the policy of the Investment Adviser to allocate investment opportunities among all Clients fairly, to the extent practical and in accordance with each Client's applicable investment strategies over a period of time. The Investment Adviser will have no obligation to purchase or sell a security for, enter into a transaction on behalf of, or provide an investment opportunity to any Client solely because the Investment Adviser purchases or sells the same security for, enters into a transaction on behalf of, or provides an opportunity to any Client if, in its reasonable opinion, such security, transaction or investment opportunity does not appear to be suitable, practical or desirable for the Client.

## **ITEM 12**

### **BROKERAGE PRACTICES**

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

As noted previously, we have full discretionary authority to manage our Clients' portfolios, including authority to make decisions with respect to which securities are bought and sold, the amount and price of those securities, the brokers or dealers to be used for a particular transaction, and commissions or markups and markdowns paid. The Investment Adviser's authority is limited by its own internal policies and procedures and each Client's investment guidelines.

The Investment Adviser causes its Clients to buy and sell securities directly from or to dealers acting as principal at prices that include markups or markdowns, and may buy securities from underwriters or dealers in public offerings at prices that include compensation to the underwriters and dealers. The Investment Adviser is under no obligation to seek the lowest price of a trade, but rather to seek “Best Execution,” considering a variety of factors relating to its Clients in determining the best price of a trade by a dealer (“principal transactions”) or a broker (“agency transactions”). A Client's investment transactions may also generate brokerage commissions and other compensation (in case of equity investments), including clearing fees and charges, all of which the Client, not the Investment Adviser, will be obligated to pay. The Investment Adviser has complete discretion in deciding what dealers (in case of principal transactions) or brokers (in case of agency transactions) the Client uses and in negotiating the prices, rates of brokerage commissions and other compensation the Client pays.

Portfolio transactions for each Client will be allocated to brokers and dealers on the basis of numerous factors and not necessarily lowest pricing. Brokers and dealers may provide other services that are beneficial to us and/or certain Clients, but not beneficial to all Clients. Subject to Best Execution, in selecting brokers and dealers (including prime brokers) to execute transactions, provide financing and securities on loan, hold cash and short balances and provide other services, we may consider, among other things, the following:

- the ability of the dealers or brokers to effect the transaction,
- the dealers' or brokers' facilities, creditworthiness, reliability and financial responsibility and
- the provision of, or payment for (or the rebate to Clients for payment of), the costs of research-related products or services that are of benefit to Clients, the Investment Adviser and related Funds and Client accounts.

The Investment Adviser need not solicit competitive bids and does not have an obligation to seek the lowest available net price of a trade, commissions and other costs. Accordingly, if the Investment Adviser determines in good faith that the commissions charged by a broker are reasonable in relation to the value of the services, including prime broker services, provided by such broker or dealer, Clients may pay commissions to such broker greater than those another might charge. Generally, neither the Investment Adviser nor its Clients separately compensate any broker or dealer for any of these other services.

If the Investment Adviser decides, based on the factors set forth above, to execute over-the-counter transactions on an agency basis through Electronic Communications Networks ("ECNs"), it will also consider the following factors when choosing to use one ECN over another:

- the ease of use;
- the flexibility of the ECN compared to other ECNs; and
- the level of care and attention that will be given to smaller orders.

We maintain policies and procedures to review the quality of executions, including periodic reviews by our investment professionals.

1. *Research and Other Soft Dollar Benefits.*

Research-related goods and services provided by brokers and dealers through which portfolio transactions for Clients are executed, settled and cleared may include research reports on particular industries and companies, economic surveys and analyses, recommendations as to specific securities, research services, and other goods and services providing lawful and appropriate assistance to the Investment Adviser in the performance of its investment decision-making responsibilities on behalf of the Fund and Other 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. In addition, such payments or rebates may be made by futures commission merchants ("FCMs") in connection with futures transactions. Brokers and dealers sometimes suggest a level of business they would like to receive in return for the various services they provide. Actual business received by any broker or dealer may be less than the suggested allocations, but can (and often does) exceed the suggestions, because total transaction volume is allocated on the basis of all the considerations described above. A broker or dealer will not be excluded from executing transactions for Clients because it has not been identified as providing Soft Dollar Items.

"Soft Dollars" will generally be used only for brokerage and research within the safe harbor provided by "Section 28(e)" of the U.S. Securities Exchange Act of 1934, as amended, even though Soft Dollars may be generated in transactions not falling within the requirements of Section 28(e). Soft Dollars generated in respect of principal transactions (other than riskless principal transactions), futures, currency and derivatives transactions do not 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 and other authorized Client expenses specified herein.

The Investment Adviser does not currently have any formal Soft Dollar arrangements in place at this time, but reserves the right to enter into such arrangements in the future. Any Soft Dollars generated under a formal Soft Dollar arrangement with respect to equity transactions and utilized by the Fund would fall within the safe harbor provided by Section 28(e). From time to time, brokers (including prime brokers) may assist the Fund in raising additional funds from investors, and representatives of the Investment Adviser may speak at conferences and programs sponsored by such brokers for investors interested in investing in

hedge funds. Through such "capital introduction" events, prospective shareholders would have the opportunity to meet with the Investment Adviser. Currently, none of the Investment Adviser or its Clients compensates any broker for organizing such events or for any investments ultimately made by prospective shareholders attending such events, nor do they anticipate doing so in the future. While such events and other services provided by a broker may influence the Investment Adviser in deciding whether to use such broker in connection with brokerage, financing and other activities of its Clients, the Investment Adviser will not commit to allocate a particular amount of brokerage to a broker in any such situation. In addition, the Investment Adviser may accept gifts or entertainment from entities or their affiliates who also provide services to its Clients, including counterparties. Relationships such as these could be viewed as creating a conflict of interest that potentially could affect the Investment Adviser's ability to seek Best Execution. The Investment Adviser maintains policies and procedures that require reporting of gifts and entertainment and monitors relevant counterparty relationships for potential conflicts of interest.

## *2. Brokerage for Client Referrals.*

Neither the Investment Adviser nor any related person receives client referrals from any broker-dealer or third party. However, as discussed above, subject to Best Execution, the Investment Adviser may consider, among other things, capital introduction and marketing assistance with respect to investors in the Funds in selecting or recommending broker-dealers for the Funds.

## *3. Directed Brokerage.*

The Investment Adviser does not recommend, request or require that a Client direct the Investment Adviser to execute transactions through a specified broker-dealer.

## *B. Allocations of Investments.*

The Investment Adviser is committed to allocating investment opportunities on a fair and equitable basis. As a general matter, we allocate securities among the Funds in each strategy on a pro rata basis. When an investment is appropriate for both sets of Funds, the investment typically is allocated among all of the Funds pursuant to a predetermined formula that generally results in a pro rata allocation. This general approach, however, may be subject to change based on a number of factors.

Regarding allocations of limited investment opportunities, such as privately placed securities and initial public offerings of securities, we will determine which Funds are eligible to participate in those opportunities. Limited investment opportunities generally will be allocated among all eligible Funds in proportion to their relative capital balances in accordance with the procedures set forth above. Funds without sufficient available capital will not participate. In certain circumstances, we may give added weight to those Funds whose investment programs are responsible for obtaining the investment opportunity when allocating limited investment opportunities.

## *C. Order Aggregation.*

If the Investment Adviser determines that the purchase or sale of a security is appropriate with regard to multiple Clients, the Investment Adviser may, but is not obligated



to, purchase or sell such a security on behalf of such Clients with an aggregated order for the purpose of reducing transaction costs (to the extent permitted by applicable law). When an aggregated order is filled through multiple trades at different prices on the same day, each participating Client will receive the average price, with transaction costs generally allocated *pro rata* based on the size of each Client's participation in the order (or allocation in the event of a partial fill) as determined by the Investment Adviser. In the event of a partial fill, allocations may be modified on a basis that the Investment Adviser deems to be appropriate, including, for example, in order to avoid odd lots or *de minimis* allocations. When orders are not aggregated, trades generally will be processed in the order that they are placed with the broker or counterparty selected by the Investment Adviser. As a result, certain trades in the same security for one Client (including a Client in which the Investment Adviser and its personnel may have a direct or indirect interest) may receive more or less favorable prices or terms than another Client, and orders placed later may not be filled entirely or at all, based upon the prevailing market prices at the time of the order or trade. In addition, some opportunities for reduced transaction costs and economies of scale may not be achieved.

**ITEM 13**  
**REVIEW OF ACCOUNTS**

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

We perform various daily, weekly, monthly, quarterly and periodic reviews of each Client's portfolio. Such reviews are conducted by the Principals, portfolio managers and research associates.

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

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

C. Content and Frequency of Account Reports to Clients.

We generally provide annual audited financial statements to the Funds within 120 days of the applicable Fund's fiscal year end (see Item 15., Custody, below).

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

A. Economic Benefits for Providing Services to Clients.

We do 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 we nor any of our related persons directly or indirectly compensates any person who is not a Supervised Person, including placement agents, for client referrals.

## **ITEM 15**

### **CUSTODY**

The Investment Adviser 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 each Fund because it complies with the provisions of the so-called "audit approach" which, among other things, requires that each 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**

The Investment Adviser serves as the management company with discretionary trading authority to each Client. The Investment Adviser or an affiliate of the Investment Adviser entered into an investment management agreement, or similar agreement, with each Client, pursuant to which the Investment Adviser or an affiliate of the Investment Adviser was granted discretionary trading authority.

Our investment decisions and advice with respect to each Client are subject to each Client's investment objectives and guidelines, as set forth in the Client's offering documents and/or investment management agreement (as applicable).

## **ITEM 17**

### **VOTING CLIENT SECURITIES**

#### **A. Policies and Procedures Relating to Voting Client Securities.**

In compliance with Advisers Act Rule 206(4)-6, the Investment Adviser has adopted proxy voting policies and procedures. The general policy is to vote proxy proposals, amendments, consents or resolutions (collectively, "Proxies") in a prudent and diligent manner that will serve the applicable Client's best interests and is in line with each Client's investment objectives.

We may take into account all relevant factors, as determined by us in our discretion, including, without limitation:

- the impact on the value of the securities or instruments owned by the relevant Client and the returns on those securities;
- the anticipated associated costs and benefits;
- the continued or increased availability of portfolio information; and
- industry and business practices.

In certain circumstances, the Investment Adviser may refrain from voting Proxies. Generally, Clients may not direct our vote in a particular solicitation.

Conflicts of interest may arise between the interests of the Clients on the one hand and us or our affiliates on the other hand. If we determine that we may have, or be perceived to have, a conflict of interest when voting Proxies, we will vote in accordance with our Proxy voting policies and procedures. Clients may obtain a copy of our Proxy voting policies and our Proxy voting record by contacting us at the address or telephone number listed on the first page of this document.

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

The Investment Adviser 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.