



# STONE BEACH

INVESTMENT MANAGEMENT

## Form ADV Part 2 A Brochure

### **ITEM 1: Cover Page**

This Brochure provides information about the qualifications and business practices of Stone Beach Investment Management LLC. If you have any questions about the contents of this brochure, please contact us at 203-956-7620. The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission or by any state securities authority.

Additional information about Stone Beach Investment Management LLC also is available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). The searchable IARD/CRD number for Stone Beach Investment Management LLC is 163163.

Stone Beach Investment Management LLC is a registered investment adviser. Registration of an Investment Adviser does not imply any level of skill or training.

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**Brochure prepared on March 1, 2021**

## **ITEM 2: Material Changes**

This section of the Brochure will address only those “material changes” that have been incorporated since the last delivery or posting of this document on the SEC’s public disclosure website (IAPD). Pursuant to SEC Rules, we will ensure that you receive a summary of any material changes to this and subsequent Brochures within 120 days of the close of our business’ fiscal year. We may further provide other ongoing disclosure information about material changes as necessary.

Stone Beach Mortgage Opportunity Fund, LLC (“SBMOF”) has been liquidated. The SBMOF feeder fund shut down in 2014. The Stone Beach Fund, launched in 2014, is a private fund client of the Adviser.

Currently, the Stone Beach brochure may be requested by contacting David Lysenko, Chief Compliance Officer, at 203-956-7620 or [lysenko@sb-im.com](mailto:lysenko@sb-im.com).

Additional information about the Adviser is also available via the SEC’s web site [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). The SEC’s web site also provides information about any persons affiliated with the Adviser who are registered, or are required to be registered, as investment adviser representatives of the Adviser.

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#### **ITEM 4: Advisory Business**

Stone Beach Investment Management, LLC (“The Adviser” or “Adviser”), is a Delaware limited liability company that has filed for registration as an investment adviser with the U.S. Securities and Exchange Commission (“SEC”). The Adviser is an investment management company focused on mortgage-backed securities and related markets. The Adviser provides investment management services on a discretionary basis. For example, the Funds operate as pooled investment vehicles and attempt to provide diversification, management expertise and other advantages to their investors. The advisory services include, among other things, providing advice regarding asset allocation and the selection of investments. David Lysenko, one of the principals of Stone Beach Investment Management, founded Orchard Heritage Investments LLC to manage his personal and family assets upon leaving Renaissance Technologies in 2008. In order to extend the Adviser’s purview and manage external money, Ed Smith and Alan Swide joined David in 2011 to expand the management team and to reorganize Orchard Heritage Investments into Stone Beach Investment Management. The Adviser is also actively seeking subadvisory relationships with registered investment companies.

**The Adviser’s assets under management as of December 31, 2020 are 39,760,523 on a discretionary basis.**

#### **ITEM 5: Fees and Compensation**

Management fees are calculated based on a percentage of the value of the assets under management (referred to herein as “Management Fees”). In most cases, the fee will be 1.5% of net assets. In consideration for its services to The Stone Beach Fund (referred to herein as the “Fund” or “Client”), the Adviser shall receive a Management Fee, payable quarterly in advance equal to approximately 1.5% annually of each investor’s share the Fund’s net asset value.

In addition, the Adviser may collect incentive allocations and/or fees based on the performance of investments and number of investors in the Fund.

For a more complete description of the terms and conditions of the Adviser’s management of client accounts, please refer to the Investment Advisory Agreement which is provided (together with Form ADV Part 2A) to all prospective clients.

To the extent mutual funds are selected the annual advisory fee set forth above does not include the customary fees and expenses associated with investing in mutual funds or other costs of establishing and maintaining an account with mutual funds including Rule 12b-1 fees and expenses. In addition to the annual advisory fee each mutual fund in which your assets are invested will incur separate investment advisory fees and other expenses for which you will bear a proportionate share.

### ***Redemption***

A client may terminate his advisory relationship with the Adviser at any time upon 45 days' notice and upon payment to the Adviser of all unpaid fees then due for accounts that are billed in arrears.

With regards to investment companies that the Adviser sub-advises, in consideration for the services provided to such investment clients the Adviser receives a monthly fee equal to 1.00% (on an annualized basis) of the average net assets of the sub-advised account.

### ***Additional Fees and Expenses***

The Fund shall pay or reimburse the Adviser for all organizational and initial offering expenses of the Funds, including, but not limited to, legal and accounting fees, printing and mailing expenses and government filing fees (including blue sky filing fees). The Funds may amortize organizational and initial offering expenses over a period of 60 months from the date such Fund commenced operations because it believes such treatment is more equitable than expensing the entire amount of such expenses in such Fund's first year of operation, as required by U.S. generally accepted accounting principles ("GAAP").

The Fund will pay, from its own assets, all other expenses attributable to the activities of the Fund, including but not limited to: fees, costs, brokerage commissions, research services and products (including the research services and products), and other expenses (including travel costs) related to the purchase and sale of investments; expenses for custodians, outside counsel, administrators and accountants; printing; mailing; insurance for the Adviser; any litigation expenses; any taxes, fees or other governmental charges levied against the Fund; and any other expenses not expressly agreed to be paid by the Adviser. Such expenses may be significant and potentially exceed the Management Fee.

With regards to investment companies that the Adviser sub-advises, the Adviser is generally required to pay its own expenses incurred in connection with its obligations under the sub-advisory agreement.

## **ITEM 6: Performance Based Fees**

In addition to the Management Fee, the Adviser is compensated for its investment management services through an incentive allocation and/or fee, also known as a performance-based allocation and/or fee ("Performance Fee"). Under this arrangement, a Client will be charged a fee contingent upon the performance within the Client's account. The Performance Fee will be tied to the capital appreciation within the account as evaluated at the end of each calendar year. The Performance Fee will be payable annually, in arrears. The Adviser shall also receive the Performance Fee upon any withdrawal by an Investor, whether voluntary or involuntary, and upon dissolution of a Fund. The Performance Fee shall be in addition to the proportionate allocations of income and profits, or losses, to the Adviser and/or its affiliates based upon their capital accounts relative to the capital accounts of all Investors. The Performance Fee will be equal to 20% of net capital appreciation attained within the Client's account (net of all expenses, including any commissions, etc.). The Performance Fee shall not include any change in the value of a security position held in a side pocket account until such security is reallocated to the capital accounts of participating Clients. The Adviser, in its sole discretion, may waive or reduce the Performance Fee with respect to any Investor for any period of time, or agree to modify the Performance Fee for that Investor. The Adviser may, in its discretion, reallocate a portion of the Performance Fee to certain Investors.

In order for the Adviser to receive a Performance Fee, the Adviser must achieve capital appreciation within the account. The Adviser will charge Performance Fees in adherence to a "high water mark," which means that no Performance Fee will be earned unless the performance exceeds the previously achieved "high water mark" where Performance Fees were charged. The "high water mark" will be used in order to prevent a scenario whereby The Adviser could receive a Performance Fee merely for recouping prior losses. A full description of the entire fee arrangement will be disclosed to the Client in such Client's investment management agreement or other relevant documents. Fees generally are deducted directly from the Client's account, as specified in the relevant investment management agreement. The Adviser's receipt of Performance Fees is intended to align the Adviser's interests with those of the Adviser's Clients and to provide the Adviser with a greater incentive to manage assets well. The nature of the Performance Fee, however,

creates a potential conflict of interest among the Adviser, its associated persons, and Clients.

Such fees will be structured and charged in a manner consistent with the requirements of applicable law, including the Investment Advisers Act of 1940, as amended (“Advisers Act”), and the Employee Retirement Income Security Act of 1974, as amended. The Performance Fee creates an incentive for the Adviser to effect transactions in securities that are riskier or more speculative than would be the case in the absence of such an allocation. Since the Performance Fee is calculated on a basis which includes unrealized appreciation of Client assets, such allocation or fee may be greater than if it were based solely on realized gains. Where any part of the Adviser’s compensation is based in part on the unrealized appreciation of securities or instruments for which market quotations are not readily available, the Adviser shall disclose how such securities or instruments will be valued and the extent to which the valuation will be determined independently. To the extent the Adviser values any such securities or instruments, it has a conflict of interest as the Adviser will receive higher Performance Fees (and higher Management Fees) if it gives such securities and instruments higher valuations. The Adviser does not represent that the amount of the Performance Fees or the manner of calculating the Performance Fees is consistent with other performance-related fees charged by other investment advisers under the same or similar circumstances. The Performance Fees charged by the Adviser may be higher or lower than the Performance Fees charged by other investment advisers for the same or similar services.

In addition, in the event that the Adviser manages an account from which it collects Performance Fees and also at the same time manages an account from which it does not collect Performance Fees, the Adviser has an incentive to favor accounts from which it receives Performance Fees because it will receive a greater profit from the accounts that are charged Performance Fees. Therefore, the Adviser has an incentive to allocate investments that are expected to be more profitable to accounts from which it collects Performance Fees, on the one hand, and that are riskier, on the other hand, since in both scenarios, the Adviser may receive greater fees if the investment generates a positive return. Notwithstanding the foregoing, the Adviser does not favor accounts that pay performance fees.

## **ITEM 7: Types of Clients**

The Adviser's Client is a private investment fund whose investors are individuals, institutions, and other funds. The minimum investment in the Fund is \$500,000. The Adviser, however, has discretion to accept lesser amounts.

Additionally, the Adviser sub-advises a registered investment company.

## **ITEM 8: Methods of Analysis, Investment Strategies and Risk of Loss**

The Fund employs a relative value approach within the mortgage-backed securities market, purchasing securities we view as undervalued, while selling securities we view as overvalued. The investment team seeks to profit from the price convergence between undervalued and overvalued securities, as well as from carry or the net interest income generated by the portfolio.

The Fund uses a variety of instruments to hedge, including Treasuries, futures, options, and TBA pass-through contracts. While the portfolio may not always be strictly market neutral, the net duration exposure is generally small, as the crux of the strategy is to profit from asset selection and pricing aberrations within the MBS market rather than directionality of interest rates. Prepayments represent potentially the greatest risk to the portfolio; therefore, a core theme to the strategy is identifying the securities and market sectors that will prepay slowly.

The portfolio is close to duration neutral currently, containing slightly over 100 CMO derivative positions and hedges in pass-throughs and interest rate futures. Approximately 30% of the portfolio is in cash or highly liquid securities and derivatives, while the rest is in moderately liquid structured MBS.

### **Investment Philosophy**

A few key principles underlie the Stone Beach investment philosophy. One of these is identifying the "best use of equity." The Adviser is constantly evaluating and comparing different trades. Any potential investment is compared against a variety of benchmark trade ideas, to determine if a similar return profile can be realized more efficiently, either by risking less capital, or in a manner that maintains greater liquidity within the portfolio. This principle relies on the equivalence of many structured MBS to combinations of other securities. Another key principle is that the Adviser strives to find investment opportunities that it views as having asymmetric return profiles, i.e., investments which have greater potential upside than downside risk. While this isn't always achievable, the



upshot of this philosophy is that, by suitably combining such investments, a portfolio can be created that will generate positive returns under almost any scenario. Finally, the Adviser believes there is no substitute for judgment and experience in the MBS market. While it uses quantitative models in its investment process, and find them very useful, models are often tuned to past experience and don't capture all the dynamics that might be affecting markets. This is where human thought, judgment, and the qualitative aspect of the investment process experience come into play to recognize opportunities that the models may fail to capture.

### **Investment Process Described**

The strategic direction of the investment process begins with analysis of the dynamics of the housing market, mortgage finance, and government/Fed policy. This analysis aims to recognize broader trends in rates, demographics, and government policy initiatives that may influence mortgage refinancing and other drivers of prepayments. Using that backdrop, the investment team seeks to identify undervalued sectors and securities within the residential mortgage-backed securities market and profit from a combination of price convergence and portfolio carry. A relative value approach is followed in selecting structured MBS as well as liquid trades. Structured MBS positions include CMO derivatives such as Interest Only (IO) and Principal Only (PO) securities as well as Inverse Interest-Only securities (IIO) which contain inherent notional leverage. While the majority of the rate risk is hedged with Treasuries, derivatives, and pass-throughs, prepayments remain the most significant risk to the portfolio. Therefore, a core theme to the strategy is identifying the sectors and securities that will prepay most slowly.

Security collateral and structure are carefully analyzed in the asset selection process. More than ever, prepayment speeds are driven by factors such as origination date (and HARP program eligibility), loan-to-value ratio, loan size, credit quality, and seasoning. In addition to collateral characteristics, CMO structure drives the distribution of cash flows, which are carefully analyzed. Horizon returns under a variety of scenarios are analyzed for each potential investment to determine how it will perform, and fit within the portfolio.

### **Risks Associated with the Adviser's Investment Strategies**

Investing in securities involves risk of loss that Clients should be prepared to bear. An investment in the Fund is speculative and involves certain risk factors and other special considerations which prospective Investors should consider before subscribing for Interests. An investment in the Fund is suitable only for Investors who are willing to accept substantial risks of loss, including loss of entire principal.

## ***RMBS Risks***

Potential for Disruptions in Secondary Mortgage Markets; Risks of Extremely Limited Liquidity. The capital and credit markets, and particularly, the secondary mortgage markets, have experienced unprecedented disruptions in the past, including during and around the time of the 2008 financial crisis, and there is no guarantee such markets will not experience unprecedented disruptions again, now or in the future, resulting from, among other things, reduced investor demand for residential mortgage loans and RMBS, increased investor yield requirements for those loans and securities, downgrades of the ratings of mortgage-backed securities and underlying insurers by the rating agencies and liquidations of investment portfolios, CDOs and structured investment vehicles that contain RMBS. As a result, the secondary market for RMBS may experience extremely limited liquidity in times of market volatility or otherwise.

The Mortgage Loan Market Recently has Experienced Increasing Levels of Delinquencies and Defaults. The mortgage loan market recently has experienced increasing levels of delinquencies, defaults and losses, and the Adviser cannot assure that this will not continue. In addition, in recent months housing prices and appraisal values in many states have declined or stopped appreciating, after extended periods of significant appreciation. A continued decline or an extended flattening of those values may result in additional increases in rates of delinquencies, defaults and losses on residential mortgage loans generally, particularly with respect to second homes and investor properties and with respect to any residential mortgage loans whose aggregate loan amounts (including any subordinate liens) are close to or greater than the related property values.

In response to increased delinquencies and losses with respect to mortgage loans, many mortgage loan originators have implemented more conservative underwriting criteria for loans, which may result in reduced availability of financing alternatives for borrowers seeking to refinance their mortgage loans. The reduced availability of refinancing options for borrowers may result in higher rates of delinquencies, defaults and losses on mortgage loans, particularly with respect to adjustable rate mortgage loans that experience significant increases in their monthly payments following the adjustment date and interest only mortgage loans that experience significant increases in their monthly payments following the end of the interest only period.

The increased levels of delinquencies and defaults, as well as a deterioration in general real estate market conditions, have also resulted in loan originators being required to repurchase an increasingly greater number of mortgage loans pursuant to early payment

default and breaches of representation and warranty provisions in loan sale agreements, which has led to a deterioration in the financial performance of many loan originators, and has caused certain loan originators to cease operations. Even in cases where an original loan seller has the economic ability to repurchase loans, the increasing volume of repurchase claims has resulted in longer periods between when a repurchase claim is presented and when it is resolved, and a greater proportion of claims being refused or contested by original loan sellers. In response to the deterioration in the performance of mortgage loans, the rating agencies have lowered ratings on a large number of mortgage securitizations. There can be no assurance that the rating agencies will not continue to do so.

Difficulties in the Mortgage Loan Market and Related Regulatory Developments. In addition, numerous residential mortgage loan originators have experienced serious financial difficulties and, in some cases, bankruptcy. These difficulties may adversely affect the market value of the RMBS in which the Fund intends to invest, and the resulting performance of the Fund. Numerous laws, regulations and rules related to the servicing of mortgage loans, including foreclosure actions, have been proposed by federal, state and local governmental authorities. If enacted, these laws, regulations and rules may result in delays in the foreclosure process, reduced payments by borrowers or increased reimbursable servicing expenses, which are likely to result in delays and reductions in the distributions to be made to holders of the RMBS in which the Fund may invest. The Fund and investors in the Fund will bear the risk that these future regulatory developments will lead to delayed or reduced distributions or reduced market value, thereby resulting in losses on the RMBS in which the Fund may invest and adversely affecting the performance of the Fund.

Fixed Income Risks; Generally. The total return of a debt instrument is composed of two elements: the percentage change in the security's price and interest income earned. The yield to maturity of a debt security estimates its total return only if the price of the debt security remains unchanged during the holding period and coupon interest is reinvested at the same yield to maturity. The total return of a debt instrument, therefore, will be determined not only by how much interest is earned, but also by how much the price of the security and interest rates change.

Interest Rates; Price. The price of a debt security generally moves in the opposite direction from interest rates (i.e., if interest rates go up, the value of the bond will go down, and vice versa). In general, securities with longer maturities are more sensitive to these price changes. Additionally, the prices of high yield, fixed-income securities fluctuate more than high quality debt securities. Prices are especially sensitive to

developments affecting the company's business and to changes in the ratings assigned by rating agencies (see "Credit Ratings" below).

Prices of RMBS and Related Derivatives are Highly Volatile. Prices of RMBS and RMBS derivatives are highly volatile. Price movements for such instruments are influenced by, among other things, changes in economic conditions, including changing supply and demand relationships, government, trade, fiscal, and economic events and changes in tax laws, as well as innumerable other factors which potentially could adversely affect the business and prospects of the Fund. None of these conditions are within the control of the Adviser. Moreover, the Fund may have only a limited ability to vary its investment portfolio in response to changing conditions.

The yield characteristics of RMBS differ from traditional debt securities. As further described (under "Risk Management"), the major differences include more frequent interest and principal payments, usually monthly, and the possibility that prepayments of principal may generally be made at any time. Prepayment rates are influenced by changes in current interest rates and a variety of other factors. In addition, the assets of each trust fund underlying an RMBS may generally be purchased when the principal balance of such assets declines to a specified percentage (in many cases 10%) of the original principal balance of those assets, which has the same effect as if such mortgage loans had all been prepaid in full.

In general, changes in the rate of prepayments will change a security's yield to maturity. These differences can result in significantly greater price and yield volatility than with respect to traditional debt securities. In addition, wide bid/asked spreads may often make it difficult to sell securities on short notice at a reasonable price. Accordingly, investors are advised to have a medium-to-long term investment horizon, so as to avoid sales by the Fund of securities in weak or illiquid markets.

Prepayment Risk. An RMBS, unlike most other debt securities, can decrease in value when interest rates fall because homeowners then tend to prepay principal. Receiving increasing prepayments in a falling interest rate environment causes the average maturity of the portfolio to shorten, reducing the potential for price gains. It also requires the Fund to reinvest proceeds at lower interest rates, which could reduce the portfolio's total return, reduce its yield, and/or result in capital losses. Particular investments may experience outright losses, as in the case of an IO in an environment of faster actual or anticipated prepayments, and may underperform relative to the hedges (if any) constructed with respect to such investment. In particular, prepayments (at par) may

limit the potential upside of many RMBS to their principal or par amounts, whereas their corresponding hedges often have the potential for unlimited loss.

The frequency at which prepayments (including voluntary prepayments by the obligors and liquidations due to default and foreclosures) occur on loans underlying RMBS will be affected by a variety of factors, including the prevailing level of interest rates, as well as economic, demographic, tax, social, legal and other factors. Generally, mortgage obligors tend to prepay their mortgages when prevailing mortgage rates fall below the interest rates on their mortgage loans. 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 RMBS will be discount securities when interest rates are high and premium securities when interest rates are low, these RMBS may be adversely affected by changes in prepayment rates in any interest rate environment.

Index Risk. The Fund may invest in structured notes and variable rate RMBS, including adjustable-rate mortgage securities, which are backed by mortgages with variable rates, and certain classes of collateralized mortgage obligation (CMO) derivatives, the rate of interest payable under which varies with a designated rate 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. This introduces additional risk factors related to the movements in specific indices or interest rates which may be difficult or impossible to hedge, and which also interact in a complex fashion with prepayment risks.

RMBS Derivatives. The RMBS markets were developed specifically to reallocate the various risks inherent in RMBS across various bond classes (known as “tranches”). For example, RMBS “companion” classes typically experience much greater average life variability than other RMBS classes or RMBS pass-throughs. IOs experience greater yield variability relative to changes in prepayments. Inverse floaters experience greater variability of returns relative to changes in interest rates. To the extent that the Fund concentrates its investments in these or other derivative securities, the prepayment risks, interest rate risks, and hedging risks associated with such securities will be severely magnified. See “Leverage and Derivatives” below.

Credit Support Limitations. The amount, type and nature of insurance policies, subordination, letters of credit and other credit support, if any, with respect to certain RMBS are based upon actuarial analysis. There can be no assurance that the historical

data supporting such actuarial analysis will not accurately reflect future experience, nor any assurance that the data derived from a large pool of mortgage loans will accurately predict the delinquency, foreclosure or loss experience of any particular pool of loans.

Credit Ratings. Credit ratings of debt securities are not a guarantee of quality. A credit rating represents only the applicable rating agency's opinion regarding credit quality based on the rating agency's evaluation of the safety of the principal and interest payments. In determining a credit rating, rating agencies do not evaluate the risks of fluctuations in market value. As a result, a credit rating may not fully reflect the risks inherent in the relevant security. Rating agencies may fail to make timely changes to credit ratings in response to subsequent events. In addition, to the extent that a rating agency rates a security at the request of an issuer, the rating agency has a conflict of interest in providing such rating.

Lower Credit Quality Securities. The Fund currently intends, but is not required, to focus its investments on RMBS rated, at the time of purchase, "AA+", "AAA" or the equivalent from one or more nationally recognized statistical rating organizations; however, it should be noted that the Fund may from time to time invest opportunistically in securities which may be deemed by rating companies to have substantial vulnerability to default in payment of interest and/or principal, or which have the lowest quality ratings or are unrated.

Lower rated and unrated securities have large uncertainties or major risk exposures to adverse conditions, and are considered to be predominantly speculative. Generally, such securities offer a higher potential return than higher rated securities, but involve greater volatility and greater risk of loss of income and principal. The market values of certain of these RMBS (such as subordinated RMBS) also tend to be more sensitive to changes in economic conditions than higher rated RMBS. Declining real estate values, in particular, will increase the risk of loss upon default, and may lead to a downgrading of the securities by rating agencies. The value of such RMBS may also be affected by changes in the market's perception of the entity issuing or guaranteeing them, or by changes in government regulations and tax policies.

Although as indicated above the Fund intends to focus its investments on RMBS rated, at the time of purchase, "AA+", "AAA" or the equivalent from one or more nationally recognized statistical rating organizations, RMBS held by the Fund may be backed by subprime mortgage loans secured by residential real estate wherein the borrowers may not meet conforming underwriting guidelines because of unusual loan-to-value ratios, the nature or absence of income documentation, limited credit histories, high

levels of consumer debt, and/or past credit difficulties. These types of subprime mortgage loans generally have higher delinquency and default rates than prime or ordinary course loans. Delinquency interrupts the flow of projected interest income from a loan and default can ultimately lead to a loss if the net realizable value of the property securing the loan is insufficient to cover the principal and interest due on the loan. Also, the cost of financing and servicing a delinquent or defaulted loan is generally higher than for a performing loan. In addition, because subprime mortgage loans frequently have a higher loan- to-value ratio than ordinary course loans, a decrease in the underlying property values increases the probability that a holder of a loan will receive less than the full amount due in the event of a default.

The residential mortgage market in the United States experienced a variety of difficulties and changed economic conditions that may adversely affect the performance and market value of RMBS and issuers backed by RMBS. Delinquencies, defaults and losses with respect to residential mortgage loans generally increased, particularly in the subprime sector. In addition, housing prices and appraisal values in many U.S. states have declined or stopped appreciating. A continued decline or an extended flattening of those values may result in additional increases in delinquencies and losses on RMBS generally, particularly with respect to second homes and investor properties and with respect to any residential mortgage loans whose aggregate loan amounts (including any subordinate liens) are close to or greater than the related property values.

Downgrade of U.S. Credit Rating and the Sovereign Debt Crisis in Europe. On August 5, 2011, Standard and Poor's Ratings Services ("S&P") lowered its long term sovereign credit rating on the U.S. from AAA to AA+. On August 8, 2011 S&P also lowered the credit rating of several related government agencies and institutions, including FHLMC, FNMA, the Federal Farm Credit Bank and the FHLB from AAA to AA+. While U.S. lawmakers reached an agreement to raise the federal debt ceiling, the downgrade reflects S&P's view that the plan fell short of what is required to stabilize the U.S. economy. The credit downgrade could have unforeseen and material adverse impacts on financial markets and general economic conditions which may adversely affect the Fund. Amongst other effects, the debt downgrade could increase interest rates and disrupt payment systems, money markets, commodities markets, foreign exchange markets, equity markets and fixed income markets, adversely affecting the cost and availability of funding, all of which could adversely affect the Fund. It could also affect the value and liquidity of government securities that the Fund may hold and could result in the Fund being required to post additional or alternative collateral for our borrowings and/or deposits.

These actions by S&P initially had an adverse effect on financial markets and, although the Fund cannot predict the longer-term impact of such actions, it may be material and adverse to the Fund. These events (and future events, such as a further downgrade or default) could adversely impact many of the securities and investments that the Fund may hold, including, but not limited to, its investments in RMBS, U.S. Treasury securities, and other U.S. government agency obligations and municipal obligations. The Fund cannot predict the impact of the downgrade and its potential adverse effect on many of the securities and investments that the Fund may hold.

In addition, global markets and economic conditions have been negatively impacted by the ability of certain European Union (EU) member states to service their sovereign debt obligations. The continued uncertainty over the outcome of the EU governments' financial support programs and the possibility that other E.U. member states may experience similar financial troubles could further disrupt global markets. In particular, it has and could in the future disrupt equity markets and result in volatile bond yields on the sovereign debt of EU members. Additionally, European counterparties, swap payments slated to be made in Euros, and Euro based companies, currencies or share classes may be particularly vulnerable to disruptions, risks, and volatility. Furthermore, there is a risk that certain E.U. members may exercise their sovereignty to control their own monetary systems and declare that they are replacing their currency and force a redenomination into a new currency based upon an exchange rate stipulated by such state. Where contractual monetary obligations exist, the parties or a court will have to determine in what currency they must be paid and therefore, how much they are really worth. While contractual obligations will generally not vanish as a result of a state's change in currency, their relative value to the parties could be greatly affected. These factors could have an adverse effect on the Fund.

Subordinated Securities. The Fund may invest in RMBS and other securities that are subordinate to one or more senior classes, whereby proceeds from realizations on the underlying mortgage collateral are first be allocated to the senior classes of securities in accordance with the priority of payments prior to any allocation to the subordinated securities. Investments in subordinated securities involve significantly greater credit risk of default than the senior classes of the issue or series. Default risks may be further pronounced in the case of RMBS secured by, or evidencing an interest in, a relatively small or less diverse pool of underlying mortgage loans.

Certain subordinated securities ("first loss 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. As a result, changes in the value of the performance of subordinated securities are expected to be greater than the change in the value or payment performance of the underlying mortgages or other collateral.

Risks Associated with TBAs. The TBA market effectively allows mortgage lenders to sell the loans they intend to fund even before the loans are closed. This also allows the lender to lock in an interest rate for the borrower. Changes in interest rates and/or mortgage refinancing activity will affect the value of TBAs; *e.g.*, an increase in interest rates will generally cause their values to decline. In addition, because TBAs can be acquired with small amounts of margin, the effect of such leveraging could exacerbate Fund losses. There is also the risk that TBAs may not enjoy the same rights or priorities as customers of brokerage houses or securities under the Securities Investor Protection Act, including, but not limited to, in a bankruptcy proceeding.

Risk of Governmental Actions Related to RMBS and GSEs. Future governmental actions concerning the status of the GSEs (FNMA and FHLMC) and housing finance, in general, may affect liquidity and availability of RMBS securities, and yield/spread relationships in products the Fund invests in. The Dodd- Frank Wall Street Reform and Consumer Protection Act (the “Dodd Frank Act”) was enacted in July 2010 and required the U.S. Department of the Treasury to report its recommendations regarding options for ending the conservatorship of the GSEs. This report was released on February 11, 2011 and includes proposals to reduce the role of Fannie Mae and Freddie Mac in the mortgage market and, ultimately, wind down both institutions. Accordingly, it is uncertain what role the GSEs may play in the housing finance system in the future. The report also proposed: positioning private markets as the primary source of mortgage credit; requiring banks and other financial institutions to hold more capital and adhere to more conservative underwriting standards; reforming aspects of securitization; and implementing the reforms in Dodd-Frank Act and mobilizing all tools available to address the system of mortgage servicing and foreclosure processing. In addition, the Federal Housing Finance Agency, which is the conservator of both FHLMC and FNMA, released an updated strategic plan on February 21, 2012. The updated strategic plan set forth three strategic goals for its conservatorship: 1) building new infrastructure for the secondary mortgage market; 2) reducing the GSEs' dominant position in housing finance as well as simplifying and shrinking the GSEs' operations; and 3) maintaining foreclosure prevention activities and credit availability for new and refinanced mortgages. On August 17, 2012, the U.S. Department of the Treasury announced a Third Amendment to the Amended and Restated Senior Preferred Stock Purchase Agreements (“PSPAs”) with the Federal Housing Finance Agency (“FHFA”), as conservator of the GSEs. The modified

PSPAs require an accelerated reduction of the GSEs' investment portfolios. The modified PSPAs further require that on an annual basis, each GSE will, under the direction of FHFA, submit a risk management plan to the U.S. Department of the Treasury on each GSE's actions to reduce its enterprise-wide risk profile and taxpayer exposure to mortgage credit risk for both its guarantee book of business and its retained investment portfolio. The modified PSPAs will replace the 10% dividend payment previously required with a quarterly sweep of every dollar of profit that each the Adviser earns going forward that exceeds a specified capital reserve amount that each GSE is authorized and required to maintain by the amended PSPAs. The capital reserve amount shall be \$3 billion for 2013 and shall be reduced subsequently by \$600 million each year so that the capital reserve amount shall be zero for all years on or after January 1, 2018. This variable dividend based on net profits will eliminate the need for the GSEs to borrow from the U.S. Department of the Treasury in order to pay the previous fixed 10% dividend. For dividend payments, the Third Amendment is effective no later than September 30, 2012 for each quarter commencing January 1, 2013. It is uncertain what role the GSEs may play in the housing finance system in the future as the conservatorship progresses. It is difficult to estimate when Congressional action would be final and how long any associated phase-in period may last. Such reforms could materially impact the Fund and its RMBS or other investments (if any). It is difficult to estimate when Congressional action would be final and how long any associated phase-in period may last.

Additional Risk Factors Related to RMBS. There are RMBS risks involving unpredictability of prepayments and the effect of prepayments on yields. There are restrictions on transfers of RMBS in which the Fund may invest, which may adversely affect the market value and liquidity of such RMBS. The assets of trust funds underlying RMBS are limited. The credit enhancement for RMBS is limited in amount and coverage. A borrower may be unable to make a balloon payment related to the RMBS. Governmental action may affect foreclosures related to the RMBS. A servicers' ability to modify the terms of defaulted mortgage loans is uncertain; the effect of modifications to or of failure to modify, such loans may be adverse. Mortgage loans underwritten as nonconforming credits may experience relatively higher losses. High loan-to-value ratios increase risk of loss. High balance mortgage loans increase the risk of loss. Interest only loans have a greater risk upon default. Assets underlying an RMBS in which the Fund invests may include delinquent and sub-performing residential loans, which would adversely impact the Fund. Geographic concentration could increase losses on any loans underlying RMBS in which the Fund invests. The rate of default on loans that are secured by investor properties may be higher than on other loans. Changes to the weighted average net mortgage rate on any loans underlying an RMBS in which the Fund invests may reduce the yield with respect to such RMBS. The nature of mortgage loans

could adversely affect value of mortgaged properties. The inadequacy of value of properties could affect severity of losses. The bankruptcy of borrowers may adversely affect distributions on any RMBS in which the Fund invests. Violations of environmental laws may reduce recoveries on properties. A transfer of servicing may result in increased losses and delinquencies on any loans underlying RMBS in which the Fund invests. The method of book keeping and recording of the mortgages may affect the liquidity, payments, and/or yield on the related RMBS in which the Fund invests. Violations of federal laws may adversely affect ability to collect on loans. The party required to repurchase or replace defective assets may not be able to effect such repurchases or replacements. The Rating of RMBS in which the Fund invests is limited and may be withdrawn or lowered. Creditworthiness of credit enhancement providers may impact the ratings on RMBS in which the Fund invests. Adverse conditions in the residential real estate markets may result in a decline in property values. The RMBS in which the Fund invests are obligations of the related trust fund only. Unsecured home improvement contracts may experience relatively higher losses. Changes in the market value of properties may adversely affect payments on the RMBS in which the Fund invests. The return on RMBS in which the Fund invests could be reduced due to the application of the Service Members Civil Relief Act. Failure of master servicer or servicers to perform their obligations may adversely affect distributions on RMBS in which the Fund invests. Bankruptcy or insolvency of a servicer or master servicer may affect the timing and amount of distributions on RMBS in which the Fund invests. The nature of reverse mortgage loans may increase risk of loss.

### ***Other Business Risks***

Liquidity. Certain sectors of the fixed income markets (such as the RMBS markets) have in the past, including in the recent past, experienced significant falloffs in liquidity. During such periods of market illiquidity, the Fund may not be able to sell assets in its portfolio or may only be able to do so at unfavorable prices. In addition, mortgage-related securities and derivatives are generally traded among broker-dealers and other institutional investors in over-the-counter markets. There is no assurance that a liquid secondary market will exist for mortgage-related securities and related derivatives held by the Fund, or that the Fund will be able to dispose of such instruments. The Fund's portfolio may include securities which are not actively or widely traded or which are not registered under U.S. federal and state securities laws, and are therefore subject to restrictions on resale, and the Fund may invest in financial instruments for which no liquid market exists. In addition, wide bid/asked spreads often may make it difficult to sell securities on short notice at a reasonable price. The sale of illiquid

securities often requires more time and results in higher dealer discounts and other selling expenses than does the sale of financial instruments eligible for trading on national securities exchanges or in more conventional the over-the- counter markets. As a result of the foregoing, a Member should view its investment in the Fund as a longer-term investment than most hedge funds.

Inconsequential Risk Reduction Strategies. The Adviser may employ various risk reduction strategies designed to minimize the risk of the Fund's trading positions. A substantial risk nonetheless remains that such strategies will not always be possible to implement and, when possible to implement, will not be effective in limiting losses. If the Adviser analyzes market conditions incorrectly, or employs a risk reduction strategy that does not correlate well with the Fund's investments, such risk reduction strategy could result in losses regardless of whether the intent was to reduce risk or increase return. Any such risk reduction techniques may also increase the volatility of the Fund and/or result in a loss if the counterparty to a particular transaction does not perform as promised.

No Assurance of Investment Return. The Fund cannot provide assurance that it will be able to choose, make, and realize investments in any particular company or portfolio of companies or securities or instruments thereof. There can be no assurance that the Fund will be able to generate returns or that the returns will be commensurate with the risks of investing in the type of companies and transactions described herein. Accordingly, an investment in the Fund should only be considered by persons who can afford a loss of their entire investment. Past activities of investment entities associated with the Adviser provide no assurance of future success.

Securities Risks in General; Equity Risks. The Fund may invest in equity securities, which generally involves a high degree of risk. Prices are volatile and market movements are difficult to predict. These price movements may result from factors affecting individual companies or industries. Furthermore, the Fund is not subject to a specific percentage limit on any particular industry or issuer. Price changes may be temporary or last for extended periods. In addition to, or in spite of, the impact of movements in the overall stock market, the value of the Fund's investments may decline if the particular companies in which the Fund invests do not perform well in the market. Furthermore, the prices of growth stocks may be more sensitive to changes in current or expected earnings than the prices of other stocks. The prices of growth stocks also may fall or fail to appreciate as anticipated by the Adviser, regardless of movements in the securities markets.

General Economic and Market Conditions. The success of the Fund's activities will be affected by general economic and market conditions, such as interest rates, availability of credit, inflation rates, oil prices, economic uncertainty, changes in laws, trade barriers, currency exchange controls, and national and international political circumstances. These factors may affect the level and volatility of securities prices and the liquidity of the Fund's investments. Such volatility or illiquidity could impair the Fund's profitability or result in losses.

Risk of Governmental Action: Generally. The instability experienced in the financial markets in 2008 resulted in the U.S. Government and various other governmental and regulatory entities taking actions to seek to address issues related to the financial crisis. These actions included, but were not limited to, the enactment of the Dodd-Frank Act, which dramatically changed the way in which the U.S. financial system is supervised and regulated. More specifically, the Dodd-Frank Act provided for widespread regulation of financial institutions, consumer financial products and services, broker-dealers, over-the-counter derivatives, investment advisers, credit rating agencies, and mortgage lending, which expanded federal oversight in the financial sector and affected the investment management industry as a whole (see "Business and Regulatory Risks of Hedge Funds"). Given the broad scope and sweeping nature of the Dodd-Frank Act, and its relative recency, the ultimate impact of the Dodd-Frank Act, and its resulting regulations, is not yet certain. As a result, there can be no assurance that these measures will not have an adverse effect on the value or marketability of securities held by the Fund, including potentially limiting or completely restricting the ability of the Fund to use a particular investment instrument as part of its investment strategy, increasing the costs of using these instruments, or possibly making them less effective in general.

Furthermore, no assurance can be made that the U.S. Government or any U.S. regulatory entity (or other authority or regulatory entity) will not continue to take further legislative or regulatory action, and the effect of such actions, if taken, cannot be known.

Extraordinary Events. Terrorist activity and United States involvement in armed conflict may negatively affect general economic fortunes, including sales, profits and production, and may lead to depressed securities prices and problems with trading facilities and infrastructure.

Concentration of Investments. The Adviser is not limited in the amount of Fund capital which it may commit to any one investment. Although the Adviser currently intends to follow a general policy of seeking to spread the Fund's capital among a number of investments, the Adviser may depart from such policy from time to time and may hold a

few, relatively large securities positions in relation to the Fund's capital. The result of such concentration of investments is that a loss in any such position could materially reduce the Fund's capital.

Volatility. Volatility produces various adverse effects. In general, volatility has a tendency to discourage the participation of small investors and reduce the participation of some professionals in the financial market. This lack of participation, in turn, may tend to reduce liquidity, the ability to enter into transactions at a price close to that of the previous transaction. A consequence of illiquidity is that market-makers and specialists tend to increase the spread between the price they are willing to pay for a security (the bid) and the price at which they are willing to sell a security (the offer). For these reasons illiquid markets and/or securities may be more difficult to trade and may possess greater risk. Although volatility provides the opportunity for significant profits it also can result in equally significant losses. Such volatility theoretically could result in losses greater than the amount which would cause the Fund to terminate. This could occur if prices in the financial markets "gap" (open much higher or lower than the previous days' close).

Smaller Companies. While smaller companies may offer substantial opportunities for capital growth, they also involve substantial risks and should be considered speculative. Historically, smaller company securities have been more volatile in price than larger company securities, especially over the short term. Among the reasons for the greater price volatility are the less certain growth prospects of smaller companies, the lower degree of liquidity in the markets for such securities, and the greater sensitivity of smaller companies to changing economic conditions. In addition, smaller companies may lack depth of management and resources, be unable to generate funds necessary for growth or development, be unable to borrow funds at low cost, or be dependent on narrower product lines or business than larger companies, and therefore may be more susceptible to particular economic events or competitive factors than are larger, more broadly diversified companies. The risk that a smaller company will not have enough cash flow to meet financial obligations is a serious risk. Smaller companies typically have limited operating histories and limited following from Wall Street. Smaller companies are also more prone to market manipulation by private investment funds and market makers. Some of the smaller companies that the Fund may buy are quoted on the pink sheet over-the-counter system; such smaller companies do not need to meet minimum requirements or file with the SEC and entail significant risks.

Venture Capital Risks. Although venture capital investments offer the opportunity for significant gains, each investment involves a high degree of business and financial risk that can result in substantial losses. Among these are the risks associated with investing

in companies in an early stage of development or with little or no operating history, companies operating at a loss or with substantial variations in operating results from period to period, and companies with the need for substantial additional capital to support expansion or to achieve or maintain a competitive position. Such companies may face intense competition, including competition from companies with greater financial resources, more extensive development, manufacturing, marketing, and service capabilities, and a larger number of qualified managerial and technical personnel.

Fund's Limited Rights as Investor. The Fund will generally not be able to direct or administer the day-to-day operations of any company or any underlying activities related to any security in which the Fund invests, including, but not limited to, the RMBS. The Fund, however, may exercise its rights as a shareholder or lender and may, although it is not required to, communicate its views on important matters of policy to management, the Board of Directors, shareholders of a company, and holders of other securities of the company when the Adviser determines that such matters could have a significant effect on the value of the Fund's investment in the company. The activities in which the Fund may engage, either individually or in conjunction with others, may include, among others, supporting or opposing proposed changes in a company's corporate structure or business activities; seeking changes in a company's directors or management; seeking changes in a company's direction or policies; seeking the sale or reorganization of the company or a portion of its assets; supporting or opposing third-party takeover efforts; supporting the filing of a bankruptcy petition; or foreclosing on collateral securing a security. This area of corporate activity is increasingly prone to litigation and it is possible that the Fund could be involved in lawsuits related to such activities. The Adviser will generally seek to monitor such activities with a view to mitigating, to the extent possible, the risk of litigation against the Fund and the risk of actual liability if the Fund is involved in litigation. No guarantee can be made, however, that litigation against the Fund will not be undertaken or liabilities incurred.

Convertible Securities. Convertible securities are subject to credit and interest rate risk. When the interest rate rises, the value of such securities may decline. The interest rate or dividend performance on a convertible security may be less than that of a common stock equivalent if the yield on the convertible security is at a level which causes it to sell at a discount. In addition, companies may require the convertible securities holders to convert the securities to common stock by "calling the bonds," a technique known as forced conversion. Thus, an investment may be subject to additional risk depending on the price at which the convertible security is callable. Furthermore, the credit risk may be affected by the credit quality of the issuer. Convertible securities may or may not be rated within the four highest categories by S&P and Moody's and if not so rated, would

not be investment grade. To the extent that convertible securities are rated lower than investment grade or not rated, there would be greater risk as to timely repayment of the principal of, and timely payment of interest or dividends on, those securities.

Also, in the absence of adequate anti-dilution provisions in a convertible security, dilution in the value of the Fund's holding may occur in the event the underlying stock is subdivided, additional securities are issued, a stock dividend is declared or the issuer enters into another type of corporate transaction which increases its outstanding securities.

As a result of the conversion feature, convertible securities typically offer lower interest rates than if the securities were not convertible. It is possible that the potential for appreciation on convertible securities may be less than that of a common stock equivalent.

Preferred Stock. The Fund may invest in preferred stock. Preferred stock has a preference over common stock in liquidation (and generally dividends as well) but is subordinated to the liabilities of the issuers in all respects. As a general rule, the market value of preferred stock with a fixed dividend rate and no conversion element varies inversely with interest rates and perceived credit risk, while the market price of convertible preferred generally also reflects some element of conversion value. Because preferred stock is junior to debt securities and other obligations of the issuer, deterioration in the credit quality of the issuer will cause greater changes in the value of a preferred stock than in a more senior debt security with similar stated yield characteristics. Unlike interest payments on debt securities, preferred stock dividends are payable only if declared by the issuer's board of directors. Preferred stock also may be subject to optional or mandatory redemption provisions.

Non U.S. Investment Risks. The Fund may invest in assets located outside the U.S. Such non U.S. investments involve additional risks not involved in domestic investments. The value of non U.S. investments could be materially adversely affected by inflation, currency devaluation, interest rate changes, exchange rate fluctuations, changes in government policies, more volatile and less liquid capital markets, different infrastructure and business environments, natural disasters, armed conflicts, political or social instability and other developments affecting such countries. In general, less information is publicly available with respect to foreign-based companies than is available with respect to U.S. companies. Most foreign based companies are also not subject to the uniform accounting and financial reporting requirements applicable to companies based in the United States.



Certain Risks of Other Funds and Managers and Separately Managed Accounts. An investment in Other Funds and Managers may cause the Fund indirectly to hold opposite positions in an investment, thereby decreasing or eliminating the possibility of positive returns from such investment. Certain Other Funds and Managers that the Fund may invest in will not be registered, as applicable, under the Company Act or the Advisers Act, each as amended (or any other similar state or federal laws). Some of the Other Funds and Managers may also be recently organized and have no operating histories upon which the Fund may evaluate their possible performance. Regardless of whether the Fund utilizes leverage, the Members may indirectly be exposed to the use of leverage through the Fund's investments, if any, in Other Funds and Managers. The Managing Member and Fund generally will have no power to control the management of certain Other Funds and Managers including investments, valuation, brokerage policies, conflicts of interest, etc. Certain Other Funds and Managers may use proprietary investment strategies that are based on considerations and factors that are not fully disclosed to the Adviser. These strategies may involve risks under some market conditions that are not anticipated by the Adviser or the Other Funds and Managers. The strategies employed by Other Funds and Managers may involve significantly more risk and higher transaction costs than more traditional investment methods. If invested in any Other Funds and Managers, the Fund will receive periodic reports at the same time as, and containing the same information provided to, any other investor in such Other Funds and Managers. The Adviser may make requests for additional, more detailed information from such Other Funds and Managers, but there can be no assurance that any such additional information will be provided. Such lack of access may also impact the Adviser's ability to value the Fund's assets. The ability of the Fund to withdraw all or part of its investment from its Other Funds and Managers is generally limited to a quarterly, semiannual or annual basis depending upon the investment, and may be subject to lockups and additional restrictions (including possible redemption fees) imposed by the managers or general partners of such Other Funds and Managers. The Fund may be unable to make withdrawal payments to the Members to the extent it has invested in such Other Funds and Managers that do not permit withdrawals, will not honor the Fund's withdrawal requests or that have invested in or distributed to the Fund a side pocket or illiquid investment. To the extent that the Fund invests in Other Funds and Managers, the Fund will bear additional costs and expenses in addition to the Fund's own expenses, Management Fee, and Incentive Allocation. Such Other Funds and Managers will charge their own advisory fees (which may include both management fees and performance fees) and expenses. To the extent any of the Other Funds and Managers are, or invest in stock of non-U.S. corporations that are, classified as passive foreign

investment companies ("PFICs"), U.S. Investors will be subject to special rules with respect to the Fund's or its Other Funds and Managers' interest in such PFICs.

Events in the world financial markets, such as those that occurred in September and October 2008, may materially adversely affect Other Funds and Managers, potentially limiting the Fund's ability to fully exercise its redemption rights with regard to Other Funds and Managers due to "gates," suspensions and distributions in kind. Additionally, in some cases Other Funds and Managers may also suspend the determination of the net asset value of all or a portion of their portfolios. The absence of such valuations will make it more difficult for the Adviser to accurately value the Fund's portfolio.

Certain Other Funds and Managers (if any) may require the Fund to be a qualified purchaser as defined under Section 2(a)(51)(A) of the Company Act at the time of investment. In order to qualify as a qualified purchaser, the Fund must at all times have net investments of at least U.S. \$25 million. Thus, the Fund's qualification to purchase such certain Other Funds and Managers will be dependent upon it maintaining qualified purchaser status under relevant regulations. A failure to maintain qualified purchaser status may severely impede the Fund's ability to make new or additional investments in such Other Funds and Managers.

The Fund may invest in Other Funds and Managers, and other investors may invest with the Adviser, via separately managed accounts. Managed accounts offer greater visibility and flexibility for larger investors in general by giving them direct ownership of underlying assets and the option to sell such assets if they want to get out quickly. However, investors in private investment funds (e.g. the Fund or certain of the Other Funds and Managers) could be disadvantaged if managed account holders with the Adviser or the adviser of certain Other Funds and Managers pull out of an asset before such private investment fund investors are able to redeem from such private investment fund or the Adviser or such adviser are able to sell such assets of the Fund or Other Funds and Managers, respectively. Accordingly, a risk to investors of private investment funds is that managed account investors of the advisers to such private investment funds get an edge on private fund investors by having the ability to sell their positions whenever they want, independent of the fund manager. If this occurs before the fund manager sells a private investment fund's positions, then, among other things: (1) less liquid assets could see prices depressed; and (2) selling the Fund's positions could be harder.

Indemnification Obligations to Other Funds and Managers; Clawbacks. Subsequent to its withdrawal from Other Funds and Managers, the Fund may have indemnification or reimbursement obligations to Other Funds and Managers that survive beyond its

withdrawal and exceed any unpaid holdback, with respect to liabilities, expenses, or other adjustments to the withdrawal value which relate to the period during which the Fund was invested in the Other Funds and Managers (or, with respect to a partial withdrawal, that portion which has been withdrawn). A reimbursement obligation could arise or be asserted, or an agreement or compromise could be reached, for example, based on the terms of the governing documents of the Other Funds and Managers, applicable law, litigation, or other less formal dispute resolution processes (a "Reimbursement Claim"). The Fund also may be subject to a Reimbursement Claim if the governing documents of the Other Funds and Managers require that the Fund be subject to a "clawback" in the event of an overpayment of withdrawal proceeds or as a result of bankruptcy proceedings involving any Other Funds and Managers. It is likely that the legal, contractual, and other authority relevant to any Reimbursement Claim will be uncertain and require the Fund, together with legal counsel, to evaluate any Reimbursement Claim and determine a course of action in a manner it considers in the best interests of the Fund and, if relevant and to the extent permitted under applicable law, other clients for whom the Adviser or any of its affiliates provide investment management services and other investment funds or accounts managed by any of them. Such an evaluation may be time consuming and expensive for the Fund, its Members, and such other clients or investment funds or accounts.

A determination to pay all or a portion of a Reimbursement Claim might have different impacts on existing Members or former Members of the Fund. For example, the law, contractual agreements, or other considerations between the Fund and Members may be different from those relevant to the underlying Reimbursement Claim, and a separate determination might be necessary with respect to whether the Fund (and its remaining Members) or former Members would be responsible for a portion of any Reimbursement Claim attributable to the former Members' previous investment in the Fund. The Fund's ability to require any former Members (with respect to all or a portion of its investment) to contribute to a Reimbursement Claim may be limited, and such Reimbursement Claims may be difficult to collect. As a result, the remaining Members in the Fund may bear the full cost of any Reimbursement Claim.

As a result of the difference between redemption policies of the Fund and the withdrawal policies' of the respective Other Funds and Managers, the Adviser may be required to select Other Funds and Managers for liquidation on the basis of the redemption policies of Other Funds and Managers rather than other investment considerations, which may result in the remaining portfolio of Other Funds and Managers being less diverse in terms of investment strategies, number of Other Funds and Managers, or liquidity or other investment considerations than would otherwise be the case. Furthermore,

redemptions from the Fund may result in an increased portion of the Fund's portfolio being invested in Other Funds and Managers which are relatively less liquid. In addition, the withdrawal of the Fund from an Other Fund and Manager could also involve expense to the Fund under the terms of the Fund's investment. In paying redemptions from the Fund, the Fund will consider the timing of notice and the size of the withdrawal amount in order to pay withdrawal proceeds to withdrawing Members in a manner which it deems equitable.

Misconduct, Bad Judgment, or Fraud of Other Funds and Managers and Their Service Providers. Misconduct by employees of Other Funds and Managers or by their third-party service providers could cause losses to the Fund. Employee misconduct may include binding a fund to transactions that exceed authorized limits or present unacceptable risks and unauthorized trading activities or concealing unsuccessful trading activities (which, in either case, may result in unknown and unmanaged risks or losses) or other fraud. Losses could also result from actions by third-party service providers, including, without limitation, failing to recognize trades and misappropriating assets. Although the Adviser will seek to monitor Other Funds and Managers, such measures may not be effective in all cases in detecting fraud or misconduct. In addition, the Fund will still face the risk of Other Funds' and Managers' misrepresentation, material strategy alteration (see "Style Drift" below) or poor judgment.

When the Fund invests in Other Funds and Managers, it does not have custody of the Other Funds and Managers' assets. Therefore, there is the risk that the custodian for the Other Funds and Managers could abscond with those assets. The Other Funds and Managers are generally private and have not registered their securities under U.S. federal or state securities laws. Moreover, there can be no assurances that the Other Funds and Managers will be operated in accordance with all applicable laws and that assets entrusted to Other Funds and Managers will be protected. Instances of fraud and other deceptive practices committed by Other Funds and Managers may undermine the Adviser's due diligence efforts with respect to such parties, and if such fraud is discovered, negatively affect the valuation of the Fund's investments. In addition, when discovered, investment fraud may contribute to overall market volatility that can negatively impact the Fund's investment program.

Misuse of Confidential Information. In the past there have been a number of widely reported instances of participants involved in corporate takeovers and in risk arbitrage having violated the securities laws through the misuse of confidential information. Such violations may result in substantial liabilities for damages caused to others, for the

disgorgement of profits realized and for penalties. If another Fund and Manager commit any such violation, the Fund could be exposed to significant losses.

Financial Fraud. Instances of fraud and other deceptive practices committed by senior management of certain companies in which the Fund invests may undermine our due diligence efforts with respect to such companies, and if such fraud is discovered, negatively affect the valuation of the Fund's investments. In addition, when discovered, financial fraud may contribute to overall market volatility that can negatively impact the Fund's investment program.

Style Drift. The Adviser cannot control the investments made by Other Funds and Managers and relies primarily on information provided by Other Funds and Managers in assessing Other Funds' and Managers' defined investment strategies, the underlying risks of such strategies and, ultimately, determining whether, and to what extent, it will allocate the Fund's assets to such Other Funds and Managers. "Style drift" is the risk that another Fund or Manager may deviate from the stated or expected investment strategy. Style drift can occur abruptly if a manager believes it has identified an investment opportunity for higher returns from a different approach (and the manager disposes of an interest quickly to pursue this approach) or it can occur gradually, such as if, for instance, a "value" oriented manager gradually increases investments in "growth" stocks. Style drift can also occur if a manager focuses on factors it had deemed immaterial in its offering documents - such as particular statistical information or returns relative to certain benchmarks. Additionally, style drift may result in a manager pursuing investment opportunities in an area in which it has a competitive disadvantage or is outside the manager's area of expertise (e.g., a large-cap manager focusing on small-cap investment opportunities). Moreover, style drift poses a particular risk for multiplemanager structures since, as a consequence, the Fund may be exposed to particular markets or strategies to a greater extent than was anticipated by the Adviser when it assessed the portfolio's risk-return characteristics and allocated assets to Other Funds and Managers (and which may, in turn, result in overlapping investment strategies among various Other Funds and Managers). The Adviser's sole remedy in the event of a deviation by another Fund or Manager from its offering or other governing documents may only be to cause the Fund to withdraw capital, subject to any applicable withdrawal restrictions.

Exchange Traded Funds ("ETFs"). An ETF's NAV changes daily based on changes in market conditions and interest rates and in response to other economic, political, or financial developments. Factors that may cause an ETF's NAV to react to such developments include, but are not limited to, (1) the types of securities in which an ETF

invests, (2) the financial condition, industry and economic sector, and geographic location of an issuer, and (3) an ETF's level of investment in the Securities of an issuer. An ETF's performance could depend heavily on the performance of an industry or group of industries and could be more volatile than the performance of less concentrated funds. In addition, because certain ETF's may invest a significant percentage of their assets in a single issuer, such an ETF's performance could be closely tied to one such issuer and could be more volatile than the performance of other, more diversified, funds.

An ETF's NAV will generally fluctuate with changes in the market value of an ETF's holdings. ETFs are listed and can be bought and sold in the secondary market at market prices. Although an ETF's market price is expected to approximate its NAV, it is possible that the market price and NAV will vary significantly. As a result, the Fund may pay more than the ETF's NAV when buying such ETF in the secondary market and receive less than the ETF's NAV when selling such ETF.

The market price of ETFs during the trading day, like the price of any exchange-traded security, includes a "bid/ask" spread charged by the exchange specialist, market makers, or other participants that trade the particular security. In times of severe market disruption, the bid/ask spread can increase significantly. At those times, ETFs are most likely to be traded at a discount to NAV, and the discount is likely to be greatest when the price of ETFs are falling fastest, which may be the time that the Fund most wants to sell its interest in an ETF.

A lack of liquidity can lead to wide bid/ask spreads. Wider spreads may have a negative impact on the Fund's returns when it buys or sells ETFs. Lack of liquidity may also cause an ETF to trade at a large premium or discount to NAV, meaning that the Fund may overpay for a portfolio when buying or obtain less than the basket of securities is worth when selling.

Funds with lower levels of assets may also experience wide spreads in bid/ask prices. ETF market makers often receive rebates from exchanges that are calculated on a pershare basis. Thus, market makers may not have much incentive to maintain narrow gaps between bid and ask prices in funds with low trading volume. There are also risks when an issuer suspends issuing shares because wide gaps can develop between the ETF share price and the value of its underlying holdings.

Authorized participants may swap a basket of the ETF's underlying holdings for ETF shares, or vice versa. This process may help arbitrage away significant gaps between the ETF's share price and its NAV. However, when underlying holdings are costly to trade

and/or difficult to obtain, authorized participants may be less willing to round up that basket of securities which may cause wide gaps to develop between the ETF's share price and NAV. Additionally, when underlying holdings are traded less frequently (or not at all), an ETF's returns may diverge from the benchmark which it is designed to track.

The performance of an index based ETF (an "Indexed ETF") and its corresponding index ("Index") may vary somewhat due to factors such as fees and expenses of an Indexed ETF, imperfect correlation between an Indexed ETF's securities and those in the Index, timing differences associated with additions to and deletions from the Index, and changes in the shares outstanding of the component securities. An Indexed ETF may not be fully invested at times. The use of sampling techniques or futures or other derivative positions may affect an Indexed ETF's ability to achieve close correlation with the Index.

Although shares of ETFs are listed, there can be no assurance that an active trading market will be maintained. Trading of ETFs in the secondary market may be halted, for example, due to activation of market-wide "circuit breakers."

Certain Risks of Exchange Traded Notes ("ETNs"). ETNs are riskier than ordinary unsecured debt securities and have no principal protection. ETN investors are taking on credit risk that the issuer will be solvent when they want to sell shares or when they reach maturity. Investing in ETNs is not equivalent to investing directly in index components or the relevant index itself. The price at which the Fund can sell its ETNs for prior to their maturity will depend on a number of factors, and may be substantially less than the amount the Fund paid for such ETNs. The market value of ETNs may be influenced by many unpredictable factors. Risks include limited portfolio diversification, uncertain principal repayment, and illiquidity. Even though ETNs are listed on exchanges, there is no guarantee a trading market will exist for ETNs at anytime. ETNs may be subject to foreign exchange risk since ETNs may be denominated in USD while the underlying components of the relevant index may be denominated in other currencies. Also, investors in ETNs will be subject to fees, which will reduce the amount of investors' returns at maturity or on redemption of the ETNs, and as a result they may receive less than the principal amount of their investment at maturity or upon redemption of the ETNs, even if the value of the relevant index has increased. Brokerage commissions will apply to purchases and sales of ETNs in the secondary market. The sale, redemption or maturity of ETNs will generate tax consequences. The indicative value calculation of ETNs is provided for reference purposes only and is not intended as a price or quotation, or as an offer or solicitation for the purchase, sale, redemption, or termination of ETNs, nor does it reflect hedging or transaction costs, credit considerations, market liquidity, or bid-offer spreads. Published index levels from the sponsors of the indexes underlying the

ETNs may occasionally be subject to delay or postponement. Any such delays or postponements will affect the current index level and therefore the indicative value of the ETNs. Index levels provided by the sponsors of the indexes underlying the ETNs do not necessarily reflect the depth and liquidity of the underlying relevant market. For this reason and others, the actual trading price of the ETNs may be different from their indicative value. The trading prices of ETNs will reflect changes in their intrinsic value as well as market supply-and-demand, among other factors. Regardless of their published indicative value, the trading prices of ETNs may also be influenced by changes in the credit rating of the issuers thereof. Significant valuation risks and tax consequences, many of which are uncertain, exist when investing in ETNs. Among other risks, ETNs may have limited following, if any, from Wall St.

Initial Public Offerings. Securities issued through an IPO can experience an immediate drop in value if the demand for the securities does not continue to support the offering price. Information about the issuers of IPO securities is also difficult to acquire since they are new to the market and may not have lengthy operating histories. The Fund may engage in short-term trading in connection with its IPO investments, which could produce higher trading costs and adverse tax consequences. The number of securities issued in an IPO is limited, so it is likely that IPO securities will represent a small component of the Fund's portfolio as the Fund's assets increase (and thus have a more limited effect on the Fund's performance). The foregoing IPO risks should also be deemed to apply to certain newly issued RMBS in which the Fund may invest.

Private Placements and Other Similar Investments. Investments in private placements and other similar investments all may involve a high degree of business and financial risk that can result in substantial losses. Furthermore, these assets will be illiquid and difficult to value and the Fund may not be able to readily sell such investments or may only be able to sell them at substantial discounts.

Risks Related to Collateralized Debt Obligations ("CDOs"). The risks of an investment in a CDO depend largely on the type of the collateral securities, the degree of diversification within the CDO and the tranche of the CDO in which the Fund invests. Normally, the CDO is privately offered and sold, and thus, are not registered under the securities laws. As a result, investments in CDOs may be characterized by the Fund as illiquid securities; however an active dealer market may exist for CDOs allowing a CDO to qualify for Rule 144A transactions. In addition to the normal risks associated with fixed income securities discussed elsewhere in this Memorandum (e.g., interest rate risk and default risk), CDOs carry additional risks including, but are not limited to: (i) the possibility that distributions from collateral securities will not be adequate to make interest or other payments; (ii) the



quality of the collateral may decline in value or default; (iii) the Funds may invest in CDOs that are subordinate to other classes; and (iv) the complex structure of the security may not be fully understood at the time of investment and may produce disputes with the issuer or unexpected investment results.

Illiquid and Long-Term Investments. The Fund may invest in illiquid investments (including, but not limited to, private placements and other similar investments) valued at cost or otherwise until disposition. The return of capital and the realization of gains, if any, from such illiquid investments generally will occur only upon the partial or complete disposition of such investment. In addition, the lack of an established, liquid secondary market for some of the Fund's investments may have an adverse effect on the market value of the Fund's investments and on the Fund's ability to dispose of them. Additionally, the Fund's investments may be subject to certain transfer restrictions that may also contribute to illiquidity. Finally, assets of the Fund that are typically traded in a liquid market may become illiquid if the applicable trading market tightens as a result of a significant macro-economic shock or for any other reason. Therefore, no assurance can be given that, if the Fund is determined to dispose of a particular investment, the Fund could dispose of such investment at the prevailing market price. The Fund may sometimes not be able to sell securities it holds publicly unless their sale is registered under applicable securities laws, or unless an exemption from such registration requirements is available. In addition, in some cases the Fund may be prohibited by contract or legal or regulatory reasons from selling certain securities for a period of time. Although it currently does not intend to, the Fund may, as described elsewhere herein, designate certain Securities as Designated Investments. As a result of the foregoing, a Member should view its investment in the Fund as a longer-term investment than most hedge funds.

Securities Lending Risks. If the borrower defaults on its obligation to return the securities loaned because of insolvency or other reasons, the Fund could experience delays and costs in recovering the securities loaned or in gaining access to the collateral. These delays and costs could be greater for foreign securities. If the Fund is not able to recover the securities loaned, the Fund may sell the collateral and purchase a replacement investment in the market. The value of the collateral could decrease below the value of the replacement investment by the time the replacement investment is purchased. Cash received as collateral through loan transactions may be invested in other Securities. Investing this cash subjects that investment, as well as the securities loaned, to market appreciation or depreciation.

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Cybersecurity Risks. Cybersecurity incidents and cyber attacks have been occurring globally at a more frequent and severe level and will likely continue to increase in frequency in the future. The Adviser will seek to prevent and mitigate any such incidents but there is no guarantee that it will be successful in such efforts. A cybersecurity incident could have numerous material adverse effects on the Fund. Such incidents could impair the operations, liquidity and financial condition of the Fund, amongst other potential threats and risks. Cyber threats and/or incidents could cause financial costs from the theft of Fund assets (including proprietary information and intellectual property) as well as numerous unforeseen costs including, but not limited to: litigation costs, preventative and protective costs, remediation costs and costs associated with reputational damage.

### ***Leverage and Derivatives***

Leverage; Interest Rates; Margin. The use of leverage will expose the Fund and its Partners to substantial risk of loss. The Fund may utilize substantial leverage and the amount of borrowings outstanding at any time may therefore be large in relation to its capital. Consequently, the level of interest rates generally, and the rates at which the Fund can borrow in particular, will affect the operating results of the Fund. The low margin deposits normally required in connection with certain of the Fund's activities permit a considerable degree of leverage and, as a result, relatively small price movements can result in immediate and substantial losses.

The Fund may use short-term margin borrowings in purchasing Securities (including, but not limited to, swaps, commodities, derivatives, or other instruments purchased for speculative, leveraging, hedging, and/or performance enhancing purposes). In general, the use of short-term margin borrowings, if any, results in certain additional risks. For example, should the securities pledged to brokers to secure margin accounts decline in value, the Fund could be subject to a "margin call", pursuant to which it must either deposit additional funds with the broker, or suffer mandatory liquidation of the pledged

securities to compensate for the decline in value, which could require the liquidation of Fund assets at inopportune times. Furthermore, in the event of a sudden precipitous drop in the value of its assets, the Fund might not be able to liquidate assets quickly enough to pay off its margin debt.

The Fund's margin provider will have a lien over the assets of the Fund which are deposited with the margin provider as collateral. In the event of the insolvency of the margin provider, those assets may become available to the creditors of the margin provider. The insolvency of the margin provider could seriously damage the operations of the Fund, as assets of the Fund which are deposited with the margin provider as margin will become available to the creditors of the margin provider.

When the Fund purchases an option in the United States, there is no margin requirement because the option premium is paid for in full. The premiums for certain options traded on foreign exchanges may be paid for on margin. The margin requirements imposed on the writing of options, although adjusted to reflect the probability that out-of-the money options will not be exercised can in fact be higher than those imposed in dealing in the securities markets directly. Whether any margin deposit will be required for over-the-counter ("OTC") options will depend on the credit determinations and agreement of the parties to the transaction.

Short Selling. The Fund's investment program may include short selling. Short positions may be taken if the Fund determines that certain securities are overvalued or an event is likely to have a downward impact on the market price of the securities. In addition, short positions may be taken if in the view of the Adviser, such positions will reduce the risk inherent in the Fund's portfolio long positions. The extent to which the Fund engages in short sales will depend upon its investment strategy. Such practices can, in certain circumstances, substantially increase the impact of adverse price movements on the Fund's portfolio. A short sale of a security involves the risk of a theoretically unlimited increase in the market price of the security, which could result in an inability to cover the short position or a theoretically unlimited loss. There can be no assurance that securities necessary to cover a short position will be available for purchase.

Options. The Fund may engage in options transactions against long or short positions in its portfolio. The seller ("writer") of a put option which is covered (*i.e.*, the writer has a short position in the underlying asset) assumes the risk of an increase in the market price of the underlying asset above the sales price (in establishing the short position) of the underlying asset plus the premium received, and gives up the opportunity for gain on the underlying asset below the exercise price of the option. If the seller of the put option

owns a put option covering an equivalent quantity of the asset, with an exercise price equal to or greater than the exercise price of the put written, the position is "fully hedged" if the option owned expires at the same time or later than the option written. The seller of an uncovered put option assumes the risk of a decline in the market price of the underlying asset below the exercise price of the option. The buyer of a put option assumes the risk of losing his, her or its entire investment in the put option. If the buyer of the put holds the underlying asset, the loss on the put will be offset in whole or in part by any gain on the asset.

The seller ("writer") of a call option which is covered (*i.e.*, the writer holds the underlying asset) assumes the risk of a decline in the market price of the underlying asset below the purchase price of the underlying asset less the premium received, and gives up the opportunity for gain on the underlying asset 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 asset above the exercise price of the option. The buyer of a call option assumes the risk of losing his, her or its entire investment in the call option. If the buyer of the call sells short the underlying asset, the loss on the call will be offset, in whole or in part, by any gain on the short sale of the underlying asset.

Hedging Transactions. The Fund may utilize financial instruments such as forward contracts, currency options, stock index futures and options, and interest rate swaps, caps and floors both for investment purposes and to seek to hedge against fluctuations in the relative values of its portfolio as a result of changes in currency exchange rates, market interest rates and equity prices. Hedging against a decline in the value of a portfolio position does not eliminate fluctuations in the values of portfolio positions or prevent losses if the values of such positions decline, but establishes other positions designed to gain from those same developments, thus moderating the decline in the portfolio positions' value. Such hedging transactions also limit the opportunity for gain if the value of the portfolio position should increase. Moreover, it may not be possible for the Fund to hedge against an exchange rate, interest rate or equity price fluctuation that is so generally anticipated that it is not able to enter into a hedging transaction at a price sufficient to protect it from the decline in value of the portfolio position anticipated as a result of such a fluctuation.

The success of hedging transactions will be subject to the Fund's ability to anticipate movements in the direction of currency exchange and interest rates and equity prices. Therefore, while the Fund may enter into such transactions to seek to reduce currency exchange rate, interest rate or equity value risks, unanticipated changes in currency exchange or interest rates may result in a poorer overall performance for the Fund than if

it had not engaged in any such hedging transaction. In addition, the degree of correlation between price movements of the instruments used in a hedging strategy and price movements in the portfolio position being hedged may vary. Moreover, for a variety of reasons, the Fund may not seek to establish a perfect correlation between such hedging instruments and the portfolio holdings being hedged. Such imperfect correlation may prevent the Fund from achieving the intended hedge or expose it to risk of loss. The successful utilization of hedging and risk management transactions requires skills complementary to those needed in the selection of portfolio holdings. The Fund is under no obligation to hedge any existing exposures.

Reverse Repurchase Agreements. The use of reverse repurchase agreements by the Fund involves certain risks. For example, if the seller of securities under a repurchase agreement defaults on its obligation to repurchase the underlying securities, as a result of its bankruptcy or otherwise, the Fund will seek to dispose of such securities, which action could involve costs or delays. If the seller becomes insolvent and subject to liquidation or reorganization under applicable bankruptcy or other laws, the Fund's ability to dispose of the underlying securities may be restricted. Finally, it is possible that the Fund may not be able to substantiate its interest in the underlying securities. If the seller fails to repurchase the securities, the Fund may suffer a loss to the extent proceeds from the sale of the underlying securities is less than the repurchase price.

Repurchase Agreements. The Fund also may obtain leverage through repurchase agreements whereby it effectively will “borrow” funds by selling its interests in investments to a financial institution for cash and agreeing to repurchase those interests at a specified future date for an amount equal to the sales price plus interest at a negotiated rate. Although similar in many respects to a secured loan, the repurchase transaction provides for the outright transfer of the securities that are subject to the repurchase agreement from the Fund to the buyer. As the seller of the securities, the Fund will be subject to the risk that its counterparty may default on its obligation to return those securities upon tender of the repurchase price. The repurchase agreement generally will apply the concept of set-off of exposure of the counterparties to each other in the event of insolvency or other default. The occurrence of an event of default will have the effect of accelerating outstanding transactions, converting delivery obligations in respect of the securities to cash sums based on the default market value of the securities, and then netting outstanding amounts to result in a single sum payable from one party to the other. The counterparty may not be able to discharge any such payment obligation to the Fund.

Forward Contracts on Securities or Currencies. The Fund may trade in forward purchases and sales of securities and purchase and sell forward contracts on currencies ("forwards"). The principal risks relating to the use of forwards are: (a) when used for hedging purposes, the possible imperfect correlation between the prices of the forwards and the market value of the securities or currencies in the Fund's portfolio intended to be hedged by the forwards; (b) possible lack of a liquid secondary market for closing out a forwards position; (c) losses on forwards resulting from interest rate or currency movements not anticipated by the Fund; and (d) the risk of counterparty default (see below).

Futures and Options on Futures Trading. In addition to the risks with trading in futures and options on futures that arise from the leverage and volatility associated with such investments, futures positions may be illiquid because certain commodity exchanges limit fluctuations in certain futures contract prices during a single day by regulations referred to as "daily price fluctuations limits" or "daily limits." Under such daily limits, during a single day trading no trades may be executed at prices beyond the daily limits. Once the price of a particular futures contract has increased or decreased by an amount equal to the daily limit, positions in that contract can neither be taken nor liquidated unless traders are willing to effect trades at or within the limit. This could prevent the Adviser from promptly liquidating unfavorable positions and subject the Portfolio to substantial losses. The placing of certain orders (e.g. "stop-loss orders", where permitted under local law, or "stop-limit" orders) which are intended to limit losses to certain amounts may not be effective because market conditions and/or limits may make it impossible to execute such orders. Strategies using combinations of positions, such as "spread" and "straddle" positions may be as risky as taking simple "long" or "short" positions.

The CFTC and the U.S. commodities exchanges have also established limits referred to as "speculative position limits" on the maximum net long or short speculative futures positions that any person may hold or control in derivatives traded on U.S. commodities exchanges. All accounts owned or managed by a commodity trading adviser, its principals and their affiliates will be combined for position limit purposes. Because futures position limits allow a commodity trading advisor, its principals and their affiliates to control only a limited number of contracts in any one commodity, the Adviser is potentially subject to a conflict among the interests of all accounts the Adviser and its principals and their affiliates control (if any) which are competing (if at all) for shares of that limited number of contracts. Although the Adviser may be able to achieve the same performance results with OTC substitutes for futures contracts, the OTC market may be subject to differing prices, lesser liquidity and greater counterparty credit risks than the regulated U.S. commodities exchanges. The Adviser may be required to reduce the size of

positions that would otherwise be taken for the Fund or not trade in certain markets on behalf of the Fund in order to avoid exceeding such limits. Modification of trades that would otherwise be made by the Fund, if required, could adversely affect the Fund's operations and profitability. A violation of speculative position limits by the Adviser could lead to regulatory action materially adverse to the Fund's prospects for profitability.

With respect to any Fund trading on non-U.S. commodity exchanges, the Fund would be subject to the risk of fluctuations in the exchange rate between the non-U.S. currency and U.S. dollars (i.e., a decline in the value of the dollar relative to the particular non-U.S. currency will reduce the profits or increase the losses on the position) and the possibility that exchange controls would be imposed in the future. Non-U.S. commodity exchanges are not regulated by any United States government agency.

Use of Swaps and Other Derivatives. The Fund may make use of swaps and other forms of derivative contracts. In general, a derivative contract typically involves leverage, i.e., it provides exposure to potential gain or loss from a change in the level of the market price of a security, currency or commodity (or a basket or index) in a notional amount that exceeds the amount of cash or assets required to establish or maintain the derivative contract. Consequently, an adverse change in the relevant price level can result in a loss of capital that is more exaggerated than would have resulted from an investment that did not involve the use of leverage inherent in the derivative contract. Some of the derivative contracts used by the Fund may be privately negotiated in the over-the-counter market. These contracts also involve exposure to credit risk, since contract performance depends in part on the financial condition of the counterparty. These transactions are also expected to involve significant transaction costs. New derivative techniques and instruments continue to be developed, and the Fund reserves the right to use any such techniques and instruments as may be developed to the extent it determines that they are consistent with applicable regulatory requirements.

Over-the Counter Derivatives Markets. The Dodd-Frank Act includes provisions that comprehensively regulate the over-the-counter ("OTC") derivatives markets for the first time. The Dodd-Frank Act will require that a substantial portion of OTC derivatives must be executed in regulated markets and submitted for clearing to regulated clearinghouses. OTC trades submitted for clearing will be subject to minimum initial and variation margin requirements set by the relevant clearinghouse, as well as possible SEC or CFTC mandated margin requirements. The regulators also have broad discretion to impose margin requirements on non-cleared OTC derivatives. Although the Dodd-Frank Act includes limited exemptions from the clearing and margin requirements for so-called

“end-users,” the Fund does not expect to be able to rely on such exemptions. In addition, the OTC derivative dealers with which the Fund executes the majority of their OTC derivatives will not be able to rely on the end-user exemptions under the Dodd-Frank Act and therefore such dealers will be subject to clearing and margin requirements irrespective of whether the Fund is subject to such requirements. OTC derivative dealers also will be required to post margin to the clearinghouses through which they clear their customers’ trades instead of using such margin in their operations, as is currently permitted. This will further increase the dealers’ costs, which costs are expected to be passed through to other market participants in the form of higher fees and less favorable dealer marks.

The SEC and CFTC may also require a substantial portion of derivative transactions that are currently executed on a bi-lateral basis in the OTC markets to be executed through a regulated securities, futures, or swap exchange or execution facility. Such requirements may make it more difficult and costly for the Fund to enter into highly tailored or customized transactions. They may also render certain strategies in which the Fund might otherwise engage impossible or so costly that they will no longer be economical to implement.

OTC derivative dealers and major OTC derivatives market participants will be required to register with the SEC and/or CFTC. Dealers and major participants will be subject to minimum capital and margin requirements. These requirements may apply irrespective of whether the OTC derivatives in question are exchange-traded or cleared. OTC derivatives dealers will also be subject to new business conduct standards, disclosure requirements, reporting and recordkeeping requirements, transparency requirements, position limits, limitations on conflicts of interest, and other regulatory burdens. These requirements may further increase the overall costs for OTC derivative dealers, which costs are also likely to be passed along to market participants. The overall impact of the Dodd-Frank Act on the Fund is highly uncertain and it is unclear how the OTC derivatives markets will adapt to this new regulatory regime.

Although the Dodd-Frank Act will require many OTC derivative transactions previously entered into on a principal-to-principal basis to be submitted for clearing by a regulated clearinghouse, certain of the derivatives that may be traded by the Fund may remain principal-to-principal or OTC contracts between the Fund and third parties entered into privately. The risk of counterparty nonperformance can be significant in the case of these over-the-counter instruments, and “bid-ask” spreads may be unusually wide in these heretofore substantially unregulated markets. See “Risk of Counterparty Default & Other Risks” below. While the Dodd-Frank Act is intended in part to reduce these risks, its



success in this respect may not be evident for some time after the Dodd-Frank Act is fully implemented a process that may take several years.

Imperfect Correlation of Price Changes. The Fund may invest in options and futures contracts based on securities with different issuers, maturities, or other characteristics from the securities in which the fund typically invests, which involves a risk that the options or futures position will not track the performance of the fund's other investments. Accordingly, the Fund may purchase such options and futures contracts for purely speculative and return enhancement, if any, purposes.

Options and futures prices can also diverge from the prices of their underlying instruments, even if the underlying instruments match the Fund's investments well. Options and futures prices are affected by such factors as current and anticipated shortterm interest rates, changes in volatility of the underlying instrument, and the time remaining until expiration of the contract, which may not affect security prices the same way. Imperfect correlation may also result from differing levels of demand in the options and futures markets and the securities markets, from structural differences in how options and futures and securities are traded, or from imposition of daily price fluctuation limits or trading halts.

Risk of Counterparty Default & Other Risks. The stability and liquidity of futures contracts, repurchase agreements, swap transactions, forwards and other over-the-counter derivative transactions depend in large part on the creditworthiness of the parties to the transactions. The creditworthiness of the Advisers with which the Fund will enter into futures contracts, repurchase agreements, interest rate swaps, caps, floors, collars or other over-the-counter derivatives will be monitored on an ongoing basis by the Fund. If there is a default by the counterparty to such a transaction, the Fund will have contractual remedies pursuant to the agreements related to the transaction; however, exercising such contractual rights may involve days or costs which could result in the net asset value of the Fund being less than if the Fund had not entered into the transaction. If one or more of the Fund's securities counterparties were to become insolvent or the subject of liquidation proceedings in the United States (either under the Securities Investor Protection Act or the United States Bankruptcy Code), there exists the risk that the recovery of the Fund'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.

Under CFTC regulations, the Fund's clearing brokers are required to maintain customers' assets in segregated accounts. If one fails to do so, the Fund may be subject to risk of loss

of the funds on deposit with the clearing broker in the event of its bankruptcy. In addition, under certain circumstances, such as the inability of other customers of the clearing broker or the clearing broker itself to satisfy substantial deficiencies in such other customers' accounts, the Fund may be subject to a risk of loss of the funds on deposit with the clearing broker. In the case of any such bankruptcy or customer loss, the Fund might recover, even in respect of property specifically traceable to the Fund, only a pro rata share of all property available for distribution to all of the Fund's clearing brokers' customers. The Fund's property may also be frozen for an extended period of time.

In addition, the Fund may use counterparties located in various jurisdictions outside the United States. Such local counterparties are subject to various laws and regulations in various jurisdictions that are designed to protect their customers in the event of their insolvency. However, the practical effect of these laws and their application to the Fund'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 the Fund and its assets. Investors should assume that the insolvency of any counterparty would result in a loss to the Fund, which could be material.

The Fund may trade on non-U.S. commodity exchanges. The non-U.S. commodity exchanges include "principals' markets" in which performance is the responsibility only of the individual member with whom the trader has entered into a contract and not of an exchange or clearing corporation. The Fund will be subject to the risk of failure of the member with which it is trading or its refusal to perform a contract. In addition, the rights and responsibilities of clients in the event of an exchange or clearing house default or bankruptcy are likely to differ from those existing on U.S. exchanges.

Suspension or Restriction of Trading and Pricing Relationships for Futures and Options. Market conditions (e.g. illiquidity) and/or the operation of the rules of certain markets (such as the suspension of trading in any contract or contract month because of price limits or "circuit breakers") may increase the risk of loss by making it difficult or impossible to effect transactions or liquidate/offset positions. If the Fund has sold options, this may increase the risk of loss.

### ***Certain General Fixed-Income Risks***

Generally. The total return of a debt instrument is composed of two elements: the percentage change in the security's price and interest income earned. The yield to maturity of a debt security estimates its total return only if the price of the debt security remains unchanged during the holding period and coupon interest is reinvested at the same yield to maturity. The total return of a debt instrument, therefore, will be determined not only by how much interest is earned, but also by how much the price of the security and interest rates change.

Interest Rates; Price. The price of a debt security generally moves in the opposite direction from interest rates (i.e., if interest rates go up, the value of the bond will go down, and vice versa). In general, securities with longer maturities are more sensitive to these price changes. Additionally, the prices of high yield, fixed-income securities fluctuate more than high quality debt securities. Prices are especially sensitive to developments affecting the company's business and to changes in the ratings assigned by rating agencies (see "Credit Ratings" below). Prices often are closely linked with the company's stock prices and typically rise and fall in response to factors that affect stock prices. In addition, the entire high yield securities market can experience sudden and sharp price swings due to changes in economic conditions, stock market activity, large sustained sales by major investors, a high profile default, or other factors.

Prepayment Risk. Lower rates motivate issuers to pay off fixed income securities if they're callable. The Fund may then have to reinvest the proceeds from such prepayments, if any, at lower interest rates, which can reduce its yield, if any. The unexpected timing of prepayments caused by the variations in interest rates may also shorten or lengthen the average maturity of the Fund's fixed income portfolio, if any. If left unattended, drifts in the average maturity of the Fund, if applicable, can have the unintended effect of increasing or reducing the effective duration of the Fund, if applicable, this may adversely affect the expected performance of the Fund.

Extension Risk. The other side of prepayment risk occurs when interest rates are rising. Rising interest rates can cause the average maturity of the Fund's fixed income portfolio, if any, to lengthen unexpectedly due to a drop in prepayments. This would increase the sensitivity of the Fund to rising rates and its potential for price declines.

Credit Ratings. Coupon interest is offered to shareholders of fixed income securities as compensation for assuming risk, although short-term Treasury securities, such as 3month treasury bills, are generally considered "risk free." Corporate fixed income securities offer higher yields than Treasury securities because their payment of interest and complete repayment of principal is less certain. The credit rating or financial

condition of an issuer may affect the value of a debt security. Generally, the lower the quality rating of a security, the greater the risks that the issuer will fail to pay interest and return principal. To compensate shareholders for taking on increased risk, issuers with lower credit ratings usually offer their shareholders a higher "risk premium" in the form of higher interest rates above comparable Treasury securities.

Changes in shareholder confidence regarding the certainty of interest and principal payments of a corporate debt security will result in an adjustment to this "risk premium." If an issuer's outstanding debt carries a fixed coupon, adjustments to the risk premium must occur in the price, which affects the yield to maturity of the bond. If an issuer defaults or becomes unable to honor its financial obligations, the bond may lose some or all of its value.

A security rated within the four highest rating categories by a rating agency is generally called "investment-grade" because its issuer is more likely to pay interest and repay principal than an issuer of a lower rated bond. Adverse economic conditions or changing circumstances, however, may weaken the capacity of the issuer to pay interest and repay principal.

Debt securities rated below investment-grade (junk bonds) are highly speculative securities that are usually issued by smaller, less credit worthy and/or highly leveraged (indebted) companies. A corporation may issue a junk bond because of a corporate restructuring or other similar event. Compared with investment-grade bonds, junk bonds carry a greater degree of risk and are less likely to make payments of interest and principal. Market developments and the financial and business condition of the corporation issuing these securities influence their price and liquidity more than changes in interest rates, when compared to investment-grade debt securities. Insufficient liquidity in the junk bond market may make it more difficult to dispose of junk bonds and may cause the Fund to experience sudden and substantial price declines. A lack of reliable, objective data or market quotations may make it more difficult to value junk bonds accurately.

Rating agencies are organizations that assign ratings to securities based primarily on the rating agency's assessment of the issuer's financial strength. The Fund may, but is not required to; use ratings compiled by Moody's Investor Services ("Moody's"), S&P, and Fitch. Credit ratings are only an agency's opinion, not an absolute standard of quality, and they do not reflect an evaluation of market risk. Furthermore, rating agencies often face conflicts of interest when rating securities (including, but not limited to, not maintaining appropriate independence from the issuers and underwriters), which may result in

inaccurate ratings of securities or the failure to adjust credit ratings in a timely manner; such inaccurate ratings could adversely impact the Fund's investments and portfolio decisions.

The Adviser may use ratings produced by ratings agencies as guidelines to determine the rating of a security at the time the Fund buys it. A rating agency may change its credit ratings at any time. The Fund is not obligated to dispose of securities whose issuers subsequently are in default or which are downgraded. The Fund may invest in securities of any rating.

Municipal Securities and Tax Reform Risk. As the Fund may purchase the debt securities of municipal issuers, changes or proposed changes in federal tax laws could impact the value of those securities. Of particular concern would be large changes in marginal income tax rates or the elimination of the tax preference for municipal interest income versus currently taxable interest income. Also, the failure or possible failure of such debt issuances to qualify for tax-exempt treatment may cause the prices of such municipal securities to decline, possibly adversely affecting the value of the Fund's portfolio. In addition, the municipal market is a fragmented market that is very technically driven. There can be regional variations in economic conditions or supplydemand fundamentals. Municipals essentially cannot be shorted or be the subject of standard repurchase agreements, and any interest or other expenses incurred for their purchase cannot be deducted. The municipal market is also still predominantly a retail buyer driven market. For these reasons, it is subject to very different supplydemand fundamentals. Public information in the municipal market is also less available than in other markets, increasing the difficulty of evaluating and valuing securities. Many bonds in the municipal market are insured by private companies. Changes in market conditions affecting the bonds insured, the availability of capacity to insure, or the downgrade of any or all of the insurers could have a negative impact on the municipal market and the Fund's performance.

There is no guarantee that municipal securities will remain free from taxation of the federal government and the state in which they were issued and that the Fund will be able to purchase municipal securities qualifying for tax-exempt treatment by any state. Unanticipated changes in state or federal tax law may materially impact the Fund. See also "Tax Risks" below.

Certain Credit Related, Mezzanine, and Subordinated Debt Investment Risks. When investing in credit related investments, including, but not limited to, subordinated debt instruments, the ability of the Fund to influence a portfolio company's affairs, especially

during periods of financial distress or following insolvency, is likely to be substantially less than that of senior creditors. For example, under terms of subordination agreements, senior creditors are typically able to block the acceleration of the mezzanine debt or other exercises by the Fund of its rights as a creditor. Accordingly, the Fund may not be able to take the steps necessary to protect its investments in a timely manner or at all. In addition, the debt securities in which the Fund may invest may not be protected by financial covenants or limitations upon additional indebtedness may have limited liquidity and may not be rated by a credit rating agency. Debt instruments are also subject to other creditor 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 and (iii) environmental liabilities that may arise with respect to collateral securing the obligations. The Fund's investments may be subject to early redemption features, refinancing options, prepayment options or similar provisions which, in each case, could result in the issuer repaying the principal on an obligation held by the Fund earlier than expected.

Fixed Income Liquidity Risks. Most of the Fund's fixed income securities are currently expected to be highly liquid. However, high yield securities, which the Fund may own without limitation, generally are less liquid than higher quality securities. Many of these securities do not trade frequently, and when they do their prices may be significantly higher or lower than expected. At times, it may be difficult to sell these securities promptly at an acceptable price, which may limit the Fund's ability to sell securities in response to specific economic events or to meet withdrawal requests.

Auction Rate Securities ("ARS"). If there are more ARS offered for sale than there are buyers for those ARS in any auction, the auction will fail and existing holders of such ARS will not be able to sell some or all of the ARS for which they have submitted sell orders through the auction. The relative buying and selling interest of market participants in the ARS and in the auction rate securities market as a whole vary over time, and may be adversely affected by, among other things, news relating to the issuer, the attractiveness of alternative investments, the perceived risk of owning the ARS (whether related to credit, liquidity or any other risk), the tax or accounting treatment accorded the ARS (as further described in part below), reactions of market participants to regulatory actions or press reports, financial reporting cycles and market conditions generally. Shifts of demand in response to any of the foregoing factors cannot be predicted and may be short lived or exist for longer periods.

Corporations are generally big buyers of ARS due to their attractive yields; however, there have been various interpretations from accounting the Advisers over the past couple of years as to whether corporations can classify ARS as cash and cash

equivalents on their balance sheets. If a strict interpretation of this ruling were to cause corporations to reduce and/or eliminate their exposure to ARS, this could lead to reduced demand that could possibly cause disruptions in the auction process.

Investment banks that issue ARS and run the auction process for the life of the bond are not legally bound to ensure an orderly market. A secondary market for ARS may not develop, continue, or be sufficiently liquid for re-sales. Any auction procedures and transfer requirements may limit the liquidity and marketability of ARS and may not yield a holder thereof the best possible price. Furthermore, issuers generally have the ability to convert an ARS into a long-term bond, thereby eliminating the auction process and the systematic yield resets.

Credit and Sub-Prime Risks. Developments in the credit market may have a substantial impact on the companies that the Fund invests in, and may in large part affect the success of such companies. Events in the sub-prime mortgage market have at times caused a decrease in global liquidity and significant dislocations and volatility in the structured credit, leveraged loan and high-yield bond markets, as well as in the wider global financial markets. Since 2007, the U.S. credit markets have been dealing with the effects of numerous defaults by homeowners on "sub-prime" mortgage loans. During 2007 and 2008, these defaults had also begun to increase with respect to mortgages considered to be of less credit risk than "sub-prime" mortgages. It is expected that mortgage default rates may continue to increase potentially beyond 2011. These defaults have not only had a materially adverse impact on the spending power of the borrowers of such defaulted mortgage loans, but have also reduced the value of investment portfolios containing securities affected by such mortgages. To the extent that such marketplace events are not temporary and continue, this may have an adverse impact on the availability of credit to businesses generally and could lead to an overall weakening of the U.S. and global economies. Such an economic downturn could adversely affect the financial resources of corporate borrowers and result in the inability of such borrowers to make principal and interest payments on outstanding debt when due. In the event of such defaults, the companies that the Fund invests in may suffer a partial or total loss of capital loaned to, or invested in, such companies, which could, in turn, have an adverse effect on the Fund's returns. The sub-prime and credit crisis could cause significant market disruption and may restrict the ability of the Fund, or the companies that the Fund invests in, to sell or liquidate investments at favorable times or for favorable prices.

LIBOR Scandal. Information has called into question the integrity of the process for determining LIBOR, and the full implications of such information may continue to develop. Negative consequences of the perceived inaccuracy of LIBOR could include

fewer loans utilizing LIBOR as an index for interest payments and/or erratic swings in LIBOR, both of which could result in interest rate mismatches between assets and its liabilities and expose parties to cash shortfalls. Actual inaccuracies could lead to losses on relevant instruments. Furthermore, questions surrounding the integrity in the process for determining LIBOR may have other unforeseen consequences, including potential litigation against banks and/or obligors on loans, which could result in a material and adverse effect on the Fund. There can be no assurance that LIBOR's prominence as a benchmark interest rate will not diminish, which may have unforeseen consequences on the Fund and the global economy.

### ***Management Risks***

Officers of the Adviser Not Full Time. The Adviser and its members, officers and employees, and their respective affiliates, will devote the time and effort that they deem adequate to develop and operate the Fund's business, but may not devote their full working time to the operations of the Fund. In addition, they are not prohibited from engaging in other investment related activities similar to or different from the investment activities engaged in by the Fund. The members, managers and employees of the Adviser and its respective affiliates who perform services for the Fund, may also perform similar or different services for others or for their own account and, accordingly, may have conflicts in allocating management time, services and functions among the Fund and other accounts for which they provide services, including other affiliates of the Adviser. In addition, the Adviser may manage accounts for other clients. There is no specific limit as to the number of accounts which may be managed or advised by the Adviser. In connection with its advisory activities on behalf of other accounts or entities, the Adviser may receive compensation which exceeds that which is received from the Fund. In such event, the Adviser may have an incentive to favor such other accounts and/or entities. The performance of the Fund could also be adversely affected by the manner in which particular orders are entered or trades are allocated for all such other accounts and entities; however, the Adviser will allocate trades fairly and reasonably with respect to the Fund.

Lack of Management Control by Members. Under the Limited Liability Company Agreement, the Members do not have the right to participate in the management, control or operation of the Fund or to remove the Adviser.

Reliance upon Adviser. The success of the Fund depends on the ability of the Adviser to identify, select and realize investments consistent with the Fund's objectives. See "The Fund and the Adviser."



Dependence of the Fund on Key Individuals. The Fund is dependent on the experience and expertise of the principal officers of the Adviser. In the event of death, disability or departure of such persons, the business of the Fund could be adversely affected. In the event of the dissolution of the Adviser, the Fund shall, pursuant to the terms of the Limited Liability Company Agreement, terminate and its assets shall be liquidated and appropriately distributed unless more than 50% of the Member Interests elect to continue the business and appoint one or more new Advisers within ninety (90) days.

Limited Assets for Investor Recourse. The Adviser may be thinly capitalized at any given time and may not be expected to have, or retain, any material amount of assets, which means there may be limited backstopping (if any) for Investor claims (if any), against the Adviser.

### ***Fund Risks***

Proprietary Investment Strategies. The Adviser may use proprietary investment strategies that are based on considerations and factors that are not fully disclosed to the Investors. These strategies may involve risks under some market conditions that are not anticipated by the Adviser. The Adviser generally uses investment strategies that are different than those typically employed by traditional managers of portfolios of stocks and bonds. Such strategies may not be, or may become less, profitable over time, if at all, as the Adviser and competing asset managers or investors manage a larger group of assets in the same or similar manner or market conditions change. The strategies employed by the Adviser may involve significantly more risk and higher transactions costs than more traditional investment methods.

Lack of Transferability of Interests. At present there is no public market for the Interests, and no public market for the Interests is contemplated. The Interests have not been registered under the 1933 Act or the Company Act and may not be transferred unless so registered or an exemption from registration is available. Consequently, the Interests are restricted securities and will not be liquid investments. Even if a purchaser for a Member's Interest is available, approval of the transfer by the Adviser (which may deny such approval in its absolute discretion) and satisfaction of certain requirements specified in the Limited Liability Company Agreement will be required before any transfer may occur. In addition, no interests in the Fund may be transferred if such transfer would result in Benefit Plan Investors holding 25% or more of any class of the Interests in the Fund (or such other amounts that may be deemed "significant" pursuant to 29 C.F.R. 2510.3-101 or other relevant ERISA guidelines).

Negotiation of the Limited Liability Company Agreement. The Adviser has generally determined the terms of the Limited Liability Company Agreement, which were not negotiated on an arm's-length basis. Legal counsel for the Adviser has not acted as counsel for or represented the interests of the Members. Potential Investors should consult with their own legal counsel with respect to the Fund.

Lack of Insurance. The assets of the Fund are not insured by any government or private insurer except to the extent portions may be deposited in bank accounts insured by the Federal Deposit Insurance Corporation or with brokers insured by the Securities Investor Protection Corporation and such deposits and securities are subject to such insurance coverage (which, in any event, is limited in amount). Therefore, in the event of the insolvency of a depository or custodian, the Fund may be unable to recover all of its funds or the value of its securities so deposited.

Lack of Operating History. The Fund is newly organized and has no operating history upon which Investors may evaluate its possible performance. However, the Adviser has experience managing one or more other investment funds.

Portfolio Turnover. The Fund intends to purchase or sell short a given security whenever it believes the transaction will contribute to its stated objective, even if the same security has only recently been traded. Similarly, a security position may be liquidated regardless of its holding period, whether the liquidation is at a gain or at a loss. It is generally not possible to estimate the rate of turnover and any portfolio turnover may be significant. Turnover may lead to realization of taxable gains for Members and increased brokerage and other transaction costs borne by Members and may exceed those of other investment entities of comparable size.

Effect of Fund Size and Growth. As the Fund grows, it may experience greater difficulty in finding acceptable investments without adversely affecting the prices at which it buys and sells the securities. Also, new securities purchases will cause transaction costs that will be shared by all Investors.

Withdrawals. There are a number of restrictions on withdrawals. As a result, Investors should be aware that they may be required to bear the financial risks of this investment for an indefinite period of time. There is no guarantee that such limited withdrawal rights will allow an Investor to withdraw all, or any portion of, its investment at the most opportune time. Valuation estimates may cause uncertainty in the withdrawal amount the Investor will receive.

Effect of Withdrawals. Withdrawals by Members could require the Fund to liquidate or close out positions more rapidly than would otherwise be desirable, which could reduce the value of Fund assets and cause a resulting reduction in the value of the Interests, and can lead to increased trading costs and negative tax effects. Reduction in the size of the Fund could make it more difficult to generate a positive return or to recapture losses due, among other things, to reductions in the Fund's ability to take advantage of particular investment opportunities. Substantial withdrawals could also force the Fund to sell its more liquid holdings, leaving it with a higher proportion of relative illiquid securities in its portfolio and further reducing the Fund's ability to distribute in the event of further withdrawals. Withdrawals could also cause increased transaction costs and realization of taxable gains if the Fund needs to sell securities in order to raise cash for withdrawals.

Involuntary Liquidation of a Member's Interest. The Adviser may, in its sole discretion, upon written notice to any Member, terminate and redeem the interest of any Member in the Fund.

Trade Error Risks. On occasion, errors may occur with respect to trades executed on behalf of the Fund. Trade errors can result from a variety of situations, including, for example, when the wrong security is purchased or sold, when the correct security is purchased or sold but for the wrong account, and when the wrong quantity is purchased or sold (e.g. 1,000 shares instead of 10,000 shares are traded). Trade errors frequently result in losses but may, occasionally, result in gains. The Adviser will endeavor to detect trade errors prior to settlement and correct and/or mitigate them in an expeditious manner. To the extent an error is caused by a third party, such as a broker, the Adviser will strive to recover any losses associated with such error from such third party. The Adviser will determine whether any trade error has resulted from gross negligence on its part, and, unless it finds that to be the case, any losses will be borne by (and any gains will benefit) the Fund. The Adviser will establish internal policies regarding the manner in which such determinations are to be made, but investors should be aware that, in making such determinations, the Adviser will have a conflict of interest.

Valuation Risks. Generally, ASC 820, which sets forth certain GAAP related valuation requirements, and other accounting rules applicable to investment funds and various assets they invest in, are evolving. Such changes may adversely affect the Fund. For example, the evolution of rules governing the determination of the fair market value of assets to the extent such rules become more stringent would tend to increase the cost and/or reduce the availability of third-party determinations (if any) of fair market value. This may in turn increase the costs associated with selling assets or affect their liquidity

due to inability to obtain a third-party determination (if any) of fair market value. Furthermore, mistakes may be made in valuations, which may cause them to be inaccurate. There is no guarantee that valuations will represent the value that will be realized by the Fund on the eventual disposition of any Security. Furthermore, the value of any Security may decrease due to subsequent events. Therefore, valuations may not reflect a decrease in the value of any Security due to events subsequent to the date of the valuations. As a result of any of the foregoing, Members withdrawing from the Fund, prior to realization of any Security not designated as a side pocket at the time of purchase by the Fund, may not necessarily participate in gains or losses therefrom. Inaccurate valuations may impact the Management Fee, Performance Allocation, and the Capital Accounts of Investors whether or not they invest or redeem based on such valuations. Furthermore, once a Member withdraws, notwithstanding any inaccurate valuations at the time of such withdrawal, such Member no longer has any claims with respect to its past Interest if it turns out such Interest was really worth more; however, notwithstanding any other statement herein, the Fund may seek, and Members agree to allow the Fund, to recover amounts distributed to Members to the extent required by law or if such amounts are later found to have been distributed in excess or subject to an existing or subsequent applicable liability or expense. See "Clawback" below. Absent bad faith or manifest error, the Adviser's asset value determinations are conclusive and binding on all Members.

For future Investors in the Fund, the Adviser may, in effect, "sell" a piece of each current Investor's indirect interest in each specific investment to such future Investors. Implicit in any such "sale" is that the Fund carries each such investment at an estimated fair value, which may be cost. If the Adviser's estimate of fair value is wrong under such circumstances, say too low, then the Adviser may have "sold" it to the future Investor at a discount, which may be viewed as an adverse consequence to current Investors. Conversely, if the estimated fair value is too high a value for such investment, any future Investor will be "paying" too much for such investment, which may be viewed as an adverse consequence to future Investors.

Clawback. Notwithstanding any other statement herein, the Fund may seek, and Members agree to allow the Fund, to recover amounts distributed to Members to the extent required by law or if such amounts are later found to have been distributed in excess or subject to an existing or subsequent applicable liability or expense, including based on: (1) later, more accurate, valuations; (2) the discovery or recognition after any period of a liability or expense (including, but not limited to, indemnification rights of, or related to, the Fund and/or Adviser) that relates to the period in which such distribution was based upon; (3) bankruptcy proceedings; or (4) one of the Other Funds and Managers (if any)

requires the Fund to return distributions the Fund received from such Other Funds and Managers (including, but not limited to, as required by law or in connection with any indemnification obligation pursuant to the terms of such Other Funds and Managers).

Material Non-Public Information. By reason of their responsibilities in connection with the Fund and other investment activities, and notwithstanding procedural safeguards including, but not limited to, information barriers and restricted securities lists, personnel of the Adviser may acquire confidential or material, non-public information that would limit the ability of the Fund to buy and sell certain of its investments. The Fund's investment flexibility may be constrained due to the inability of the Adviser to use such information for investment purposes. Moreover, the Adviser may be restricted from initiating transactions in certain securities or selling certain investments, due to its acquisition of confidential or material, non-public information, at a time when the Adviser would otherwise take such action.

Increased Regulations. Legal, tax and regulatory changes could occur during the term of the Fund that may adversely affect the Fund. Securities and futures markets are subject to comprehensive statutes, regulations and margin requirements enforced by the SEC, other regulators and self-regulatory organizations and exchanges authorized to take extraordinary actions in the event of market emergencies. The regulation of derivatives transactions and funds that engage in such transactions is an evolving area of law and is subject to modification by government and judicial actions. The regulatory environment for private investment funds is evolving, and changes in the regulation of private investment funds may adversely affect the value of investments held by the Fund and the ability of the Fund to obtain leverage it might otherwise obtain or to pursue its trading strategy. Government measures to regulate the financial industry and in particular private investment funds, including, but not limited to, Dodd-Frank, in combination or in the aggregate have increased and will likely continue to increase compliance costs, force change of business practices, impose significant unforeseen costs, limit the products that private investment funds can offer, limit the ability to pursue opportunities in an efficient manner, require an increase in regulatory capital, affect the value of the assets that private investment funds hold, reduce revenues and generally adversely affect the business, financial condition and results of private investment funds, their managers, their counterparties and the companies in which they invest. There has been an increase in governmental, as well as self-regulatory, scrutiny of the alternative investment industry in general. It is impossible to predict what, if any, changes in regulations may occur, but any regulations which restrict the ability to trade in securities or employ, or brokers and other counterparties to extend; credit in their trading (as well as other regulatory changes that result) could have a material adverse impact on the

Fund's portfolio. Investors should understand that the Fund's regulatory framework is dynamic and expected to change over time. Therefore, the Fund may be subject to new or additional regulatory constraints in the future. This Memorandum cannot address or anticipate every possible current or future regulation that may affect the Fund or its affiliates or their respective businesses. Such regulations may have a significant impact on the shareholders, the operations of the Fund, including, without limitation, restricting the types of investments the Fund may make, preventing them from exercising voting rights with regard to certain financial instruments, requiring them to disclose the identity of their investors or otherwise. Prospective investors are encouraged to consult their own advisors regarding an investment in the Fund.

Performance Allocation and Other Risks. The Performance Allocation as described below may create an incentive for the Fund to make investments that are riskier than it would otherwise make. In addition, because the Performance Allocation is calculated on a basis that includes unrealized appreciation of the Fund's assets, it may be greater than if such allocation was based solely on realized gains. In addition, the Adviser's capital contribution to the Fund may be relatively small, so that the Fund may make riskier investments than would otherwise be the case.

The Fund's "high water mark" provision means that if there is a loss carry-forward in a prior calendar year, no Performance Allocation will be paid with respect to any subsequent calendar year until the aggregate Profit in such subsequent calendar year is greater than the sum of such net Loss, for that and such preceding calendar years, and then, only to the extent that the Profit exceeds the loss carry forward (the "High Water Mark"). While generally the High Water Mark seeks to achieve, but does not guarantee, that you will only incur a Performance Allocation on cumulative Profits, the Performance Allocation may be made even if the Fund doesn't generate a Profit over the life of your investment.

There is a potential conflict of interest between the responsibility of the Adviser to maximize profits from investment and trading and the possible desire of the Adviser to avoid taking risks which might reduce the net asset value of the Fund and, consequently, reduce the Management Fee paid to the Adviser. Conversely, there is also a potential conflict of interest between the responsibility of the Adviser to minimize risk from investment and trading and the possible desire of the Adviser to take excessive risks in order to increase the net asset value of the Fund and, consequently, increase the Management Fee paid to the Adviser.

Use of Side Letters. The Fund may from time to time seek to induce investment by offering investment terms which are not available to other investors in the Fund. In such cases the parties may enter into a written side arrangement varying the terms of the offer. Such variations may include, without limitation, variations to fees, minimum investment or redemption terms, with the effect that not all investors in the Fund will invest on the same terms and some investors may enjoy more favorable terms and information than other investors. There is no limit with respect to the percentage of Investors who may receive side letters in the Adviser's discretion. Accordingly, a significant percentage of Investors may have special rights. Direct or indirect minority seed investors, if any, of the Adviser may also get preferred terms on their investment, if any, in the Fund.

In some cases you may be at a disadvantage and suffer losses if we grant other Investors preferred access to information, especially if coupled with preferred rights to redeem. We believe such practice to be reasonable however, because it is fully disclosed, and we expect that in many cases preferential terms will be given only to large Investors or early Investors who provide benefits of scale to the Fund that benefit all Investors.

No Separate Counsel. Holland & Knight LLP acts as U.S. counsel to the Fund and the Adviser in connection with its offering of Interests. In connection with the Fund's offering of Interests and subsequent advice to the Adviser, Holland & Knight LLP does not represent Investors of the Fund. No independent counsel has been retained to represent Investors of the Fund.

### ***Tax Risks***

Generally. The Fund will not seek rulings from the Internal Revenue Service ("IRS") or any legal opinion with respect to any of the federal income tax considerations discussed in this Memorandum. Moreover, the Fund may take positions as to which the tax consequences are unclear. All statements contained in this Memorandum concerning the federal income tax consequences of an investment in the Fund are based upon existing law as contained in the Internal Revenue Code and administrative and judicial interpretations thereof. No assurance can be given that the currently anticipated income tax treatment of an investment in the Fund will not be modified by legislative, judicial or administrative changes, possibly with retroactive effect, to the detriment of the Members. A brief summary of some but not all of the tax consequences and attendant risks of an investment in the Fund is included in this Memorandum.

Unrelated Business Taxable Income and Tax-Exempt Investors. Tax-exempt investors, such as Individual Retirement Accounts (IRAs), Keogh Plans, charitable remainder trusts, employee benefit plans and other tax-exempt entities or accounts, are advised that the Fund anticipates that it will acquire debt- financed property and securities using margin accounts. This will probably cause the tax-exempt partners to recognize “unrelated business taxable income” within the meaning of Section 512 of the Code. Accordingly, such investors and, in particular, charitable remainder trusts, are strongly urged to consult with their own tax advisors concerning the income tax consequences and risks of making an investment in the Fund.

Partner’s Tax Liability May Exceed Distribution. Members may be liable for taxes on amounts of income allocated to them even though no distributions are made and even though the transaction that results in the gain does not generate any cash. Also, the Fund might sustain losses offsetting such profits after the end of the year, and the Members may never receive the profits on which they were taxed.

Disallowance of Certain Items. The right of Members to take deductions for certain expenses or losses may be challenged by the IRS, whose position may be sustained in the courts. No assurance can be given that any losses or deductions or other potential federal income tax advantages described in this Memorandum or in the tax opinion, or which prospective investors may otherwise contemplate, will be available for federal income tax purposes.

Characterization of Items. The IRS may take the position that gains treated by the Fund as capital gains are ordinary income, or that capital gains treated by the Fund as longterm are short-term, or that losses treated by the Fund as ordinary losses are capital losses. No assurance can be given that the treatment by the Fund of these or similar characterization issues will be ultimately sustained.

Audit Risks. The Fund must file annual federal information returns and will also be required to file state and local information returns. Any return filed by the Fund may be audited and any such audit may result in adjustments and in an audit of a Member’s own tax return. Such an audit could result in adjustments to non-Fund as well as Fund items and could involve additional expenses for the Member being audited.

Accounting for Uncertainty in Income Taxes. ASC 740, “Income Taxes” (in part formerly known as “FIN 48”), provides guidance on the recognition of uncertain tax positions. ASC 740 prescribes the minimum recognition threshold that a tax position is required to meet before being recognized in an entity’s financial statements. It also provides guidance on



recognition, measurement, classification and interest and penalties with respect to tax positions. A prospective investor should be aware that, among other things, ASC 740 could have a material adverse effect on the periodic calculations of the net asset value of the Fund, including reducing the net asset value of the Fund to reflect reserves for income taxes, such as foreign withholding taxes, that may be payable in respect of prior periods by the Fund. This could cause benefits or detriments to certain Investors, depending upon the timing of their entry and exit from the Fund.

Withholding Risks Related to FATCA. The Foreign Account Tax Compliance Act ("FATCA"), along with recently issued IRS guidance and regulations, imposes, as described more fully in the paragraphs below, a 30% withholding tax on certain payments (made on or after January 1, 2014) of U.S. source income and certain payments (made on or after January 1, 2015) of proceeds from the sale of certain assets that give rise to U.S. source payments, as well as a portion of certain payments by certain entities, to persons that fail to meet requirements under FATCA.

FATCA could give rise to such withholding for certain of the Other Funds and Managers (if any), unless such Other Funds and Managers enter into an agreement with the IRS to disclose the name, address and taxpayer identification number of certain U.S. persons that own, directly or indirectly, an interest in such Other Funds and Managers, as well as certain other information relating to such interest. Although we believe such Other Funds and Managers will attempt to satisfy any obligations imposed on them to avoid the imposition of this withholding tax, no assurance can be given that such Other Funds and Managers will be able to satisfy their obligations under FATCA. If Other Funds and Managers become subject to a withholding tax as a result of FATCA, the return of all Investors (to the extent the Fund invests in any Other Funds and Managers subject to FATCA) may be materially affected. Prospective Investors are encouraged to consult with their own tax advisors regarding the possible implications of FATCA on their investment in the Fund.

While the Fund may permit non-U.S. Investors, such Investors are currently not anticipated; accordingly, FATCA is generally not expected to impact the Fund significantly. However, to the extent non-U.S. Investors are permitted and payments are made to Investors that are not otherwise excluded from the FATCA regime, a non-U.S. holder that is not a financial institution may be required to provide the information described below or be subject to U.S. withholding tax on a portion of payments from the Fund and the proceeds from the sale or redemption of Interests. Non-U.S. Investors that are, or receive payments through, financial institutions that have not entered an IRS agreement re: FATCA (or otherwise established an exemption from FATCA) would also be subject to this U.S. withholding tax.

Each non-U.S. Investor or beneficial owner of Interests may be required to provide satisfactory documentation to establish that it is not a U.S. person and that it does not have any "substantial United States owners" (as defined in the Code). Each non-U.S. Investor or beneficial owner of Interests that is required to provide this information and fails to do so will generally be subject to a U.S. withholding tax on any payments made to

that person. A non-U.S. Investor or beneficial owner of Interests who fails to provide the necessary information (if any) due to a non-U.S. law prohibiting the provision of this information must execute a valid waiver of the relevant non-U.S. law or dispose of the Interests within a reasonable time.

FATCA is particularly complex and its future application to non-U.S. Investors (if any) is uncertain and it is not clear at this time what actions, if any, will be required to minimize any adverse impact of FATCA on Investors.

No assurance can be given that the Fund will be able to satisfy its obligations (if any) under FATCA. If the Fund becomes subject to a withholding tax as a result of FATCA, the return of all Investors may be materially affected. Each Investor should consult its own tax advisor to obtain a more detailed explanation of FATCA and to learn how it might affect such Investor in its particular circumstance.

#### **ITEM 9: Disciplinary Information**

Registered investment advisers are required to disclose all material facts regarding any legal or disciplinary events that would be material to your evaluation of the adviser or the integrity of adviser's management.

There are no legal or disciplinary events that are material to an evaluation of the Adviser's advisory services or the integrity of management.

#### **ITEM 10: Disciplinary Information**

The Adviser is not registered, and does not have an application pending to register, as a broker-dealer or registered representative of a broker-dealer. Currently, no employees of the Adviser are registered representatives of a broker-dealer.

Neither the Adviser nor any of its management persons are registered, or have an application pending to register, as a futures commission merchant, commodity pool operator, commodity trading advisor, or an associated person of the foregoing entities.

The Adviser has no relationships or arrangements with any related person listed in the instructions to Item 10.C. that are material to its advisory business or to the Fund. The Adviser does not receive any compensation from third-party advisers that it or any

affiliate recommends or selects for the Fund. The Adviser has no business relationship that creates a material conflict of interest with any third-party advisers that it or any affiliate recommends or selects for the Fund.

## **ITEM 11: Code of Ethics, Participation or Interest in Client Transactions, and Client Privacy Policy**

### ***Code of Ethics***

The Adviser has adopted a written Code of Ethics designed to address and avoid potential conflicts of interest as required under Rule 204A-1 of the Advisers Act (the “Code”). The Code sets forth a standard of business conduct and compliance with federal securities laws by all of the Adviser's employees. The Code contains policies and procedures that ensure that all personal securities trading by employees of the Adviser is conducted in such a manner as to avoid actual or potential conflicts of interest or any abuse of an individual's position of trust and responsibility. The Adviser prohibits personal trading of certain securities or instruments; requires pre-clearance of personal trades in certain circumstances, including purchases of an IPO or a new private placement; requires periodic reporting of employees' personal securities transactions and holdings; and requires prompt internal reporting of Code violations.

While the Adviser very rarely has access to non-public information relating to public companies, as part of its Code, the Adviser has established procedures to prevent the abuse of material, non-public information, which includes procedures for, among other things, the use and maintenance of restricted trading lists. Because the structure of the Adviser would make information barriers impractical, the Adviser has not imposed information barriers to restrict the internal flow of possible material, non-public information. Thus, all professionals are deemed to be in receipt of material, non-public information in all instances where any professional of the Adviser has received material, non- public information and therefore may not trade on the basis of that information.

The Adviser will provide a copy of the Code to any investor or prospective investor upon request.

### ***Participation or Interest in Client Transactions***

Participation or Interest in Client Transactions: The Adviser recognizes that the personal securities transactions of its employees demand the application of a high code of ethics, and The Adviser requires that all such transactions be carried out in a way that does not endanger the interest of any Client. The Adviser recognizes that the personal securities transactions of its employees demand the application of a high code of ethics, and The Adviser requires that all such transactions be carried out in a way that does not endanger

the interest of any Client. At the same time, The Adviser believes that if investment goals are similar for Clients and for employees of The Adviser, it is logical and even desirable that there be common ownership of some securities. The Adviser and its related persons may invest their personal funds in Client transactions. Therefore, in order to address conflicts of interest, The Adviser has adopted a set of procedures, included in its Code of Ethics, with respect to transactions effected by its officers, directors and employees (hereafter in this Item 11, "Employees") for their personal accounts. In order to monitor compliance with its personal trading policy, The Adviser has adopted a quarterly securities transaction reporting system for all of its Employees. For purposes of the policy, an Employee's "personal account" generally includes any account (a) in the name of the Employee, his/her spouse, his/her minor children or other dependents residing in the same household, (b) for which the Employee is a trustee or executor, or (c) which the Employee controls, including The Adviser's Client accounts which the Employee controls and in which the Employee or a member of his/her household has a direct or indirect beneficial interest.

### ***Client Privacy Policy***

The Adviser has adopted a privacy policy that explains the manner in which The Adviser collects, utilizes and maintains nonpublic personal information about Clients, as required under federal legislation.

## **ITEM 12: Brokerage Practices**

The considerations described below apply to the Funds, as well as to any other clients of The Adviser (as applicable and as the context may require).

### ***Selection of Broker-Dealers***

Securities transactions for the Clients are executed through brokers selected by the Adviser in its sole discretion and without the consent of the Clients. In placing portfolio transactions, The Adviser will seek to obtain the best execution for the Clients, taking into account the following factors: the ability to effect prompt and reliable executions at favorable prices (including the applicable dealer spread or commission, if any); the operational efficiency with which transactions are effected and the efficiency of error resolution, taking into account the size of order and difficulty of execution; the financial strength, integrity and stability of the broker; special execution capabilities; clearance;

settlement; reputation; on-line pricing; block trading and block positioning capabilities; willingness to execute related or unrelated difficult transactions in the future; order of call; on-line access to computerized data regarding clients' accounts; performance measurement data; the quality, comprehensiveness and frequency of available research and related services considered to be of value; the availability of stocks to borrow for short trades; and the competitiveness of commission rates in comparison with other brokers satisfying The Adviser's other selection criteria.

### ***"Soft Dollar" Policy***

In addition to research services, The Adviser may be offered other non-monetary benefits by broker-dealers that it may engage to execute securities transactions on behalf of clients. These benefits may take the form of special execution capabilities, clearance, settlement, online pricing, block trading and block positioning capabilities, willingness to execute related or unrelated difficult transactions in the future, order of call, online access to computerized data regarding clients' accounts, performance measurement data, consultations, economic and market information, portfolio strategy advice, industry and company comments, technical data, recommendations, general reports, efficiency of execution and error resolution, quotation equipment and services, the availability of stocks to borrow for short trades, custody, travel, record keeping and similar services. These other services may also include payment of all or a portion of the clients' or The Adviser's or its affiliates' administrative costs and expenses of operation, such as office rent; office equipment and supplies; utilities (e.g., electricity, gas, oil, water); taxes; storage; employee salaries, including, but not limited to, bonuses, contingent salaries, and any other form of compensation determined by The Adviser, and benefits (including medical, dental and worker's compensation insurance); temporary help; recruiting services; newswire and quotation equipment and services (e.g., Reuters, Bloomberg, Bridge, First Call); data processing charges; periodical subscription fees (e.g., The Financial Times, The Wall Street Journal, The New York Times, Investors Business Daily); computer equipment used for brokerage or research purposes (e.g., computers, computer hardware, software, hard drives, monitors, PDAs, LANs) and related technical support, repair and maintenance; television and cable services used for research purposes; telephone and facsimile charges, equipment and installation and maintenance costs (e.g., telephones, telephone lease, telephone and facsimile lines, cellular phones used for business purposes, telephone call recording equipment, headsets, cordless phones, speaker phones, telephone switchboards and monthly and long distance telephone charges); facsimile machines and facsimile rental and repair costs; account record-keeping and related clerical services; printing services; messenger services; postal

and courier expenses; car service; expenses incurred in connection with investigating and researching issuers of securities and attending research conferences (e.g., airfare, car rentals, taxi fares, conference fees and related expenses, hotel accommodations and meals); economic consulting services; placement fees and other marketing costs; legal and accounting fees; and other reasonable expenses as determined by The Adviser.

The foregoing benefits may be available for use by The Adviser in connection with transactions in which clients will not participate. The availability of these benefits may influence The Adviser to select one broker rather than another to perform services for clients. Nevertheless, The Adviser will attempt to assure either that the fees and costs for services provided to clients by brokers offering these benefits are not materially greater than they would be if the services were performed by equally capable brokers not offering such services or that clients also will benefit from the services. The Adviser has the option to use “soft dollars” generated by clients to pay for the research and non-research related services described above. The term “soft dollars” refers to the receipt by an investment adviser of products and services provided by brokers, without any cash payment by the investment adviser, based on the volume of brokerage commission revenues generated from securities transactions executed through those brokers on behalf of the investment adviser’s clients. The products and services available from brokers include both internally generated items (such as research reports prepared by employees of the broker) as well as items acquired by the broker from third parties (such as quotation equipment). Section 28(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), provides a “safe harbor” to investment managers who use soft dollars generated by their advised accounts to obtain investment research and brokerage services that provide lawful and appropriate assistance to the investment adviser in the performance of investment decision-making responsibilities. In the event The Adviser elects to use its soft dollars for payment of all or a portion of The Adviser’s or its affiliates’ administrative costs and expenses of operation such as office rent, office equipment and supplies, utilities, employee benefits and salaries, newswire and quotation equipment, data processing charges, periodical subscription fees, computer equipment, telephone and facsimile charges and equipment costs, record-keeping services, consulting fees, issuer due diligence expenses, placement fees and other marketing costs, and legal and accounting fees, as more fully described above, such uses of soft dollars are not within the safe harbor afforded by Section 28(e) of the Exchange Act.

The use of brokerage commissions to obtain investment research services and to pay for the administrative costs and expenses of the Adviser or its affiliates creates a conflict of interest between the Adviser and clients because the clients pay for such products and



services that are not exclusively for the benefit of clients and that may be primarily or exclusively for the benefit of the Adviser. To the extent that the Adviser is able to acquire these products and services without expending its own resources (including management fees paid by clients), the Adviser's use of soft-dollars would tend to increase the Adviser's profitability. In addition, the availability of these nonmonetary benefits may influence the Adviser to select one broker rather than another to perform services for clients. The Adviser has an incentive to select or recommend a broker-dealer based on its interest in receiving the research or other products or services, rather than on a client's interest in receiving the most favorable execution. Moreover, the Adviser may cause clients to pay commissions (or markups or markdowns) higher than those charged by other broker-dealers in return for soft dollar benefits. In the event that the Adviser uses soft dollar benefits, the Adviser will use such benefits to service all client accounts rather than only those accounts that paid for the benefits.

When the Adviser uses Client brokerage commissions (or markups or markdowns) to obtain research or other products or services, the Adviser receives a benefit because The Adviser does not have to produce or pay for the research, products or services. The Adviser may have an incentive to select or recommend a broker-dealer based on the Adviser's interest in receiving the research or other products or services, rather than on Clients' interest in receiving most favorable execution.

The Adviser may cause Clients to pay commissions (or markups or markdowns) higher than those charged by other broker-dealers in return for soft dollar benefits (known as paying-up). The Adviser may use soft dollar benefits to service all Clients or only those Clients that paid for the benefits. The Adviser may or may not seek to allocate soft dollar benefits to Clients proportionately to the soft dollar credits the accounts generate.

### ***Directed Brokerage***

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

### ***Aggregation of Orders***

The Adviser may aggregate purchase and sale orders of securities held by a Client with similar orders being made simultaneously for other Clients or accounts if, in The Adviser's

reasonable judgment, such aggregation is reasonably likely to result in an overall economic benefit to the Clients based on an evaluation that the Clients will be benefited by relatively better purchase or sale prices, lower commission expenses or beneficial timing of transactions, or a combination of these and other factors. In many instances, the purchase or sale of securities for a Client will be affected simultaneously with the purchase or sale of like securities for other accounts or entities. Such transactions may be made at slightly different prices, due to the volume of securities purchased or sold. In such instances, the Adviser will average the price of all units of such security bought or sold by any Client and/or other accounts in any single trading day (the "Average Price"). The price that such Client and/or other accounts pay or receive for such securities bought or sold in the same trading day will be the Average Price multiplied by the number of units of such security bought or sold by such Client and/or other accounts, respectively. In rare circumstances, the Adviser may elect to use the actual purchase or sale price instead of the Average Price if it determines, in its sole discretion that using the Average Price would be unfairly prejudicial to such Client and/or other accounts. An individual trade may be affected at a price that is higher than would have been the case without the aggregation of orders. The Adviser, however, believes that the relationship as a whole will result in a net benefit to the Clients.

### ***Allocation of Trades***

The Adviser may, at times, determine that certain securities will be suitable for acquisition by the Clients and by other accounts managed by the Adviser, possibly including the Adviser's own accounts or accounts of an affiliate. If that occurs, and the Adviser is not able to acquire the desired aggregate amount of such securities on terms and conditions which the Adviser deems advisable, the Adviser will endeavor in good faith to allocate the limited amount of such securities acquired among the various accounts for which the Adviser considers them suitable. The Adviser may make such allocations among the accounts in any manner that it considers fair under the circumstances, including, but not limited to, allocations based on relative account sizes, the degree of risk involved in the securities acquired, and the extent to which a position in such securities is consistent with the investment policies and strategies of the various accounts involved.

### **ITEM 13: Review of Accounts**

All Clients managed by the Adviser are reviewed, at least on a monthly basis, by any one or more of David Lysenko or Edward Smith for conformity with Client objectives and guidelines. The calendar is the main triggering factor of a review of an account. More

frequent reviews may be also be triggered by, among other things, Client capital injections and/or withdrawals. From an investment management perspective, triggers for review include emerging trends and developments, market volatility, economic factors, financial results of a portfolio company, analyst commentary, and news.

In general, reports showing transactions and positions are sent to the Clients by qualified custodians. Monthly account statements showing performance (unaudited) are sent to Investors by the administrator. In addition, the Clients' realized gains/losses; interest and dividends earned are reported to Clients annually. Each Investor in a Fund also will receive the following: (i) annual financial statements of a Fund, audited by an independent certified public accounting firm; (ii) in the discretion of the Adviser or an affiliate of the Adviser, a periodic letter and/or report discussing the results of the accounts; (iii) copies of such Investor's Schedule K-1 to a Fund's tax returns (this applies to Investors in onshore Funds only); and (iv) other reports, as determined by the Adviser or an affiliate of the Adviser in its sole discretion. Additionally, within 120 days of year-end, Investors receive GAAP-compliant audited financial statements.

#### **ITEM 14: Client Referrals and Other Compensation**

The Adviser does not receive, from any non-Client, any economic benefit associated with advising Clients. The Adviser may use independent third-party solicitors to refer Clients to the Adviser and pay a portion of its advisory fees to such solicitors, in accordance with the Advisers Act. The Adviser may engage underwriters, brokers, dealers or finders to assist in the offering of Interests in a Fund, or in finding other Clients. Except for commissions on brokerage transactions (which will be paid by Clients), the advisor will pay (and will not charge Clients) fees and commissions that may be payable to any such brokers or finders for assisting in the offering or sale of Interests in a Fund, or in finding other Clients.

#### **ITEM 15: Custody**

The Adviser maintains Client funds and securities at qualified custodians. As indicated above at Item 13, the qualified custodians send monthly account statements directly to the Clients. The administrator sends monthly account statements to Investors. Clients should carefully review the account statements. The Funds send a GAAP-compliant audited financial statement to their Investors within 120 days of their fiscal year-end.

**ITEM 16: Investment Discretion**

The Adviser has discretionary investment authority over Client assets that are managed by the Adviser. Please also refer to Items 4 and 8.

**ITEM 17: Voting Client Securities**

The Adviser uses reasonable judgment to vote proxies in a manner it determines is in the best interest of its Clients. The Adviser monitors corporate actions of those securities it has purchased on behalf of its Investors. Receipt of proxy materials is logged into a proxy control sheet. Proxy votes will generally be submitted electronically or by mail. A record of the proxy votes cast will be made and retained by the Adviser. Investors can obtain information on how the proxies were voted and a detailed description of the Adviser's policies and procedures regarding proxy voting by requesting such information from the Chief Compliance Officer.

In some foreign markets, where proxy voting demands fee payment for agent services, the Adviser will balance the cost and benefit of proxy voting and may give up the proxy voting if the cost associated with it is greater than the benefits from voting.

The Adviser has authority to vote Client securities.

**ITEM 18: Financial Information:**

The Adviser solicits prepayment of Management Fees on a quarterly basis from the Clients. The Adviser does not solicit prepayment of more than \$1,200 in fees per Client six months or more in advance, and thus has not provided a balance sheet according to the specifications of 17 CFR Parts 275 and 279.

Because the Adviser has discretionary authority over and/or custody of Client funds or securities, the Adviser has disclosed, that there is no financial condition that is reasonably likely to impair its ability to meet contractual commitments to Clients.

The Adviser has not been the subject of a bankruptcy petition during the past ten years.