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**March 30, 2023**

**This Brochure provides information about the qualifications and business practices of 400 Capital Management LLC (“400CM” or the “Adviser”). If you have any questions about the contents of this Brochure, please contact the Investor Relations team at (212) 612-3101 or by e-mail at [IR@400Capital.com](mailto:IR@400Capital.com). The information in this Brochure has not been approved or verified by the U.S. Securities and Exchange Commission (“SEC”) or by any state securities authority.**

**Additional information about 400 Capital Management LLC also is available on the SEC’s website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov). 400 Capital Management LLC is an SEC-registered investment adviser. Registration with the SEC does not imply a certain level of skill or training.**

**Item 2: Material Changes**

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400CM's investment adviser registration with the SEC became effective on March 27, 2012. 400CM is required to identify and discuss any material changes made to its Brochure since the last annual update. There are no material changes to report. However, clients and prospective clients should review the entire Brochure carefully. Set forth below is a summary of certain key amendments included in this Brochure since the last annual amendment dated March 30, 2022. Any defined terms used in this summary are defined within the Brochure.

400CM amended Item 8 to update and add certain risk factors.

**Item 3: Table of contents**

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Item 1: Cover Page .....	1
Item 2: Material Changes .....	2
Item 4: Advisory Business.....	4
Item 5: Fees and Compensation .....	4
Item 6: Performance-Based Fees and Side-By-Side Management.....	8
Item 7: Types of Clients .....	8
Item 8: Methods of Analysis, Investment Strategies and Risk of Loss .....	8
Item 9: Disciplinary Information.....	53
Item 10: Other Financial Industry Activities and Affiliations.....	53
Item 11: Code of Ethics, Participation or Interest in Client Transactions and Personal Trading .....	54
Item 12: Brokerage Practices.....	56
Item 13: Review of Accounts .....	58
Item 14: Client Referrals and Other Compensation .....	58
Item 15: Custody .....	58
Item 16: Investment Discretion .....	58
Item 17: Voting Client Securities .....	59
Item 18: Financial Information.....	59

**Item 4: Advisory Business**

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400CM was founded in October of 2008 and is organized as a Delaware limited liability company. 400CM has its principal place of business in New York, New York. Chris Hentemann is the managing member and principal owner of 400CM. Please see Form ADV Part 1, Schedule A for additional information on 400CM's current ownership.

400CM provides discretionary investment advisory services to privately offered pooled investment vehicles (each, a "**Fund**" and collectively, the "**Funds**"), both directly as the adviser and as a sub-adviser (such Funds for which 400CM acts as sub-adviser, the "**Sub-Advised Funds**"). References herein to Funds include Sub-Advised Funds unless Sub-Advised Funds are referred to separately or the context indicates otherwise. The Adviser also manages separate accounts for select institutional clients ("**Managed Account Clients**"). Collectively, the Funds and Managed Account Clients are referred to as the "**Client Accounts**."

Investment advisory services are provided directly to the Funds and not to investors in the Funds. Accordingly, such services are tailored to each Fund's investment objectives, strategies and guidelines as described in the respective Fund's offering documents. 400CM provides investment advisory services to its Managed Account Clients in accordance with each client's respective investment management agreement and the investment objectives, strategies and guidelines set forth in the respective investment management agreement. 400CM does not participate in wrap fee programs.

400CM generally invests across residential and commercial mortgage loans and securities (RMBS and CMBS), consumer loans and asset-backed securities (ABS), other structured credit products and corporate assets, related performing and distressed portfolios and derivatives. A more detailed description of the services and strategies is available in "Item 8: Methods of Analysis, Investment Strategies and Risk of Loss."

As of December 31, 2022, 400CM had approximately \$5.6 billion net assets under management, all of which are managed on a discretionary basis.

**Item 5: Fees and Compensation**

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

*Management Fee*

400CM generally charges each Client Account a management fee at an annual rate ranging from 0 to 1.5% of the net assets of the Client Account on a quarterly basis (either as of the first day of the period or as of the last day of the period) and are based on (i) the net asset value of the assets in the Client Account (including net unrealized appreciation or depreciation of investments and cash, cash equivalents and accrued interest) on such date and/or (ii) the amount of capital contributed to the Client Account (including, for the avoidance of doubt, capital reinvested) as of such date. The management fee will be prorated for additions to and withdrawals or distributions from a Client Account during a quarter and the applicable portion of the management fee will be refunded if paid in advance.

*Performance-Based Compensation*

With respect to certain Funds that are structured as hedge or open-end funds as well as certain Managed Account Clients, 400CM or one of its affiliates, as applicable, generally receives on an annual basis performance-based compensation equal to 10% to 20% of the net realized and unrealized capital appreciation, if any, of the capital accounts or the net asset value of the shares (as applicable) of the respective Client Account. Performance-based compensation will also be paid or allocated to 400CM or one of its affiliates, as applicable, upon an interim-year redemption or withdrawal as if such date were the end of the fiscal year, subject to certain adjustments. The receipt of performance-based compensation is subject to certain limitations including the application of a “high water mark” and, with respect to certain Client Accounts, 400CM or one of its affiliates, as applicable, will only receive performance-based compensation after the investors in the respective Client Account have earned a certain rate of return (i.e. a hurdle rate).

With respect to Client Accounts that are structured as private equity or closed-end funds, 400CM or one of its affiliates, as applicable, generally receives performance-based compensation equal to 10% to 20% of proceeds realized from the disposition of investments and/or distributions from investments, subject to the return of capital contributions to the investor and, often, subject to the receipt of a preferred return by the investors and catch-up distributions to 400CM or one of its affiliates, as applicable, and/or other performance hurdles.

With respect to certain hybrid Client Accounts that are structured with a portion of the Client Account as open-end and a portion of the Client Account as closed-end, 400CM or one of its affiliates, as applicable, generally receives the foregoing applicable performance-based compensation for the open-end and closed-end portion of the Client Accounts, respectively.

Performance-based compensation is charged to qualified clients in compliance with Rule 205-3 of the Investment Advisers Act of 1940, as amended (the “**Advisers Act**”).

Generally, with respect to Client Accounts that are Funds, the Adviser withdraws fees and expenses from the relevant Fund. With respect to a Sub-Advised Fund, the Adviser sends an invoice for fees and expenses which is paid directly by the Sub-Advised Fund. With respect to Client Accounts that are Managed Account Clients, payment of fees and expenses are authorized by the Managed Account Clients.

Although the performance-based compensation and management fees charged to investors in the Funds are generally not negotiable, 400CM reserves the right to waive or impose different performance-based compensation or management fees or otherwise modify the fee or compensation arrangements of certain large and/or strategic investors. Employees of 400CM, relatives of such persons and affiliates of 400CM may invest in the Funds on a fee free basis.

400CM may negotiate other compensation structures with clients, including fixed rate fees.

*Side Letters*

The Adviser or a Fund has entered into and may in the future enter into agreements (“**side letters**”) with certain prospective or existing investors in a Fund whereby such investors are subject to terms and conditions that are more advantageous than those set forth in the Fund’s offering documents, including, but not limited to, rights to make future investments in the Fund or other co-investment opportunities, special redemption rights, a reduction or rebate in management fee and performance compensation, or redemption charges to be paid by the investor, notification rights in connection with certain events occurring in the Fund or

Adviser's business, heightened portfolio transparency and such other rights as may be negotiated by the Adviser and such investor. The modifications are solely at the discretion of the Adviser/Fund and may, among other things, be based on the size of the investor's investment in the Fund or affiliated investment entity, an agreement by an investor to maintain such investment in the Fund for a significant period of time, or other similar commitment by an investor to the Fund or the Adviser.

### *Expenses*

The expenses borne by investors in a Fund are set forth in full in the respective Fund's offering documents. Please refer to the documents for each Fund for a complete description of the types of expenses an investor in a Fund may bear.

Generally, a Fund (and indirectly the investors in such Fund) shall be responsible, as applicable, for its organizational as well as for its operating expenses, including but not limited to all accounting (including third party accounting services) expenses; taxes, tax preparation and audit expenses (including custody audit); legal expenses; administrator fees and expenses; fund compliance expenses (including expenses related to compliance software); expenses associated with compliance with the U.S. Foreign Account Tax Compliance Act (together with any regulations, rules and other guidance implementing such sections of the Internal Revenue Code of 1986, as amended, and any applicable intergovernmental agreement or information exchange agreement and related statutes, regulations, rules and other guidance thereunder) expenses associated with compliance with the Tax Information Authority (International Tax Compliance) (Common Reporting Standard) Regulations, 2015, as amended ("**CRS Regulations**"); expenses associated with compliance with any regulations, rules and other guidance implementing regulations or laws (other than expenses of ensuring 400CM's compliance with the Advisers Act); expenses incurred in the initial and ongoing offering and sale of interests/shares, including compliance with U.S. and non-U.S. regulatory requirements and negotiation with prospective investors; expenses related to credit facilities and other borrowings; shareholder proxy voting services; investment expenses such as expenses and liabilities in connection with the investments in special purpose vehicles pursuing direct lending strategies and the associated expenses relating to sourcing and holding investments and taxes (including any entity-level taxes); commissions, research fees and expenses (including investment-related and research-related travel); risk management expenses; system expenses related to trading, research (including Bloomberg and similar subscription services), a Fund's accounting, data services, valuation services, risk management, order management systems and other analytical systems (collectively, "**System Expenses**"); investment, research or surveillance services provided by consultants; interest on margin accounts and other indebtedness; borrowing charges on securities sold short; custodial fees; bank service fees; fund-related insurance costs (including directors' and officers' (D&O and E&O) liability insurance costs even though the policy may potentially benefit 400CM); fees and expenses of the independent directors and advisory committee members of a Fund; with respect to feeder funds, their pro rata share of the master fund's expenses; and any other expenses related to the purchase, sale or transmittal of assets, and indemnification and other extraordinary expenses; and reasonable out of pocket investment expenses incurred by 400CM. Expenses related to software (as outlined above) may include software used by 400CM with respect to its management of a Fund and do not qualify for the Section 28(e) safe harbor ("**Section 28(e)**") of the U.S. Securities Exchange Act of 1934, as amended (the "**Exchange Act**").

To the extent that a group of Funds are structured as a master-feeder structure, the Fund expenses are generally paid at the master fund level and are allocated to the respective feeder funds on a pro rata basis based on each feeder fund's respective interest in the master fund. Allocating expenses in this manner may result in one feeder fund bearing a portion of an expense that is attributable solely to another feeder fund. Alternatively, 400CM may, at its

discretion, cause the master fund to specially allocate certain expenses to the feeder fund to which such expense solely relates.

With respect to certain Funds, 400CM has adopted a cap for organizational expenses or an annual limit for each fiscal year on the amount of certain ordinarily recurring expenses payable by such Funds (each, an “**Expense Cap**”). To the extent that an Expenses Cap is exceeded, 400CM or one of its affiliates, as applicable, would bear the portion of such expenses that exceed such Expense Cap or would reimburse the respective Fund for those expenses borne by the Fund that exceeded the relevant Expense Cap.

The expenses allocated to Managed Account Clients will be negotiated between each client and 400CM, but generally include all investment related expenses such as brokerage commissions and other trading related costs and fees, custodial fees, interest incurred on borrowings, legal, administrator fees and expenses, tax, accounting and other costs associated with operating the managed account. (See “**Item 12: Brokerage Practices**” for more information regarding brokerage expenses.)

Generally, expenses incurred between two or more Client Accounts shall be allocated between such Client Accounts pro rata based on the net asset value of the Client Account. For example, with respect to System Expenses (defined above), during each fiscal year 400CM will bear System Expenses on behalf of the Client Accounts and allocate such expenses across all Client Accounts for which such System Expenses are attributable on a pro rata basis according to the average monthly net asset value (which may be based on estimated figures) of the respective Client Account during the fiscal year. Additionally, with respect to investment related expenses, two or more Client Accounts participating in such investment shall generally be allocated such expenses pro rata based on the size of each Client Account’s participation in the respective investment opportunity. Sourcing and diligence expenses for un consummated or “broken” transactions are generally charged pro rata to Client Accounts based on such Client Accounts’ expected participation in the particular transaction. Generally, with regard to any broken deal expenses associated with a proposed co-investment, Client Accounts that would have participated in such investment will bear such broken deal expenses and not the co-investment entity.

In accordance with its Expense Management Policy and Procedures, 400CM retains the authority to determine the methodology to allocate expenses. If 400CM allocates expenses across Client Accounts by a methodology other than a pro rata allocation, then the methodology shall be approved and documented by 400CM’s Chief Compliance Officer (the “**CCO**”) (or designee).

In addition, at times, it may be appropriate for an expense to be allocated between 400CM and one or more Client Accounts. The allocation of such expenses presents a conflict of interest for 400CM. 400CM seeks to manage this conflict by adhering to its Expense Management Policy and Procedures. The policy requires any such allocations to be approved and documented by 400CM’s CCO (or designee).

There could be discrepancies in the pricing of the same asset held by the Funds and certain Managed Account Clients and/or Sub-Advised Funds as 400CM maintains responsibility for the valuation of assets held by the Funds and not of those held by such Managed Account Clients and/or Sub-Advised Funds. As a result, any such valuation discrepancies may impact the allocation of certain expenses, such as research, when the pro-rata allocation of such expenses is based on net asset value of the respective Funds, Managed Account Clients and/or Sub-Advised Funds. 400CM has established procedures to monitor pricing differences between accounts and to address any conflicts that may arise therefrom.



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

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400CM or one of its affiliates is entitled to be paid performance-based compensation by its Client Accounts. In addition, certain Client Accounts may have more favorable performance-based compensation arrangements than other accounts. Performance-based fee arrangements may create an incentive for 400CM to recommend investments which may be riskier or more speculative than those which would be recommended under a different fee arrangement. Such fee arrangements may also create an incentive to favor higher fee-paying accounts over other accounts in the allocation of investment opportunities. Furthermore, certain Client Accounts may have investment objectives, programs, strategies and/or positions that are similar to or may conflict with other Client Accounts and the Adviser may give advice or take action with respect to the investments held by, and transactions of, certain Client Accounts that may differ from the advice given or the timing or nature of any action taken with respect to the investments held by, and transactions of, other Client Accounts due to a variety of reasons, including, without limitation, differences between the investment strategy, liquidity needs, financing terms, regulatory treatment and tax treatment of the other Client Accounts. 400CM has adopted and implemented policies and procedures that are designed to address conflicts of interest relating to the management of multiple Client Accounts, including a trade allocation policy discussed in more detail below in Item 11.

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**Item 7: Types of Clients**

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As described above, 400CM serves as the investment manager or sub-advisor to the Funds and the Managed Account Clients. The Funds advised by 400CM are exempt from registration under the Investment Company Act of 1940, as amended (the “**Investment Company Act**”), pursuant to Section 3(c)(1) or Section 3(c)(7) of such act. Investors in the Funds are required to represent that they meet the requirements of an “**accredited investor**” as such term is defined in Rule 501 of Regulation D of the Securities Act of 1933, as amended (the “**Securities Act**”) and, if applicable, that they meet the requirements of a “**qualified purchaser**” as such term is defined in Section 2(a)(51) of the Investment Company Act. The Managed Account Clients consist of institutional investors.

Minimum investment requirements vary by Fund and can be as high as \$5,000,000; although 400CM reserves the discretion to accept less. There is no fixed minimum account size required for managed accounts, although the size of such account is, in general, significantly in excess of the minimum investment required for the Funds.

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

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***Methods of Analysis and Investment Strategies***

The methods of analysis and investment strategies utilized by the Adviser are set forth in detail in the offering documents provided to each investor in the Funds. A summary is provided below.

***General***

To the extent consistent with the Client Account’s investment mandate, 400CM provides investment advice across credit sectors and throughout an issuer’s capital structure with a primary focus on structured credit, which includes secured and structured commercial, consumer and corporate assets. 400CM invests across various investment sectors, including, but not limited to, risk sharing/risk transfer participations, agency and non-agency residential and commercial mortgage backed securities, residential and commercial mortgage loans, consumer and commercial asset backed securities and consumer loans (including credit



cards, automobile loans, student loans, or potentially other secured or unsecured consumer assets), municipal bonds, credit-linked notes, sovereign bonds, collateralized loan obligations, collateralized debt obligations (“CDO”), indices, private investments in public equity where the underlying asset class is structured credit and/or mortgages, special purpose vehicles (including trust certificates) where the underlying asset class is structured credit and/or mortgages and related corporate credit originated primarily in the U.S. and European markets. Corporate credit investments include, but are not limited to, high yield securities, distressed debt investments, bank debt, credit default swaps, trade claims, private debt, total return swaps, preferred shares, litigation certificates, enhanced equipment trust certificates and other hybrid capital instruments and related equities and options. 400CM may also opportunistically invest in the residential and commercial real estate sectors, including through direct holdings of real estate properties, where such holdings are consistent with a Client Account’s investment mandate.

Where applicable, and to the extent consistent with a Client Account’s investment mandate, to achieve a Client Account’s investment objective, 400CM, on behalf of a Client Account, invests in existing or emerging structured credit opportunities focused on consumer, residential and commercial real estate and commercial asset-backed investments by pursuing direct lending opportunities, including joint ventures with third parties and debt and/or equity investments in newly formed lending companies. In pursuing direct lending opportunities, the applicable Client Account may invest directly or indirectly through special purpose vehicles owned by the Client Account that directly or indirectly originate loan opportunities and engage in activities typically associated with direct lending, including (i) originating and warehousing loans with the intent to securitize and distribute liabilities while retaining targeted credit exposure and (ii) providing secured warehouse lending, mezzanine capital or bridge financing on a collateralized basis to new and emerging businesses and asset classes. All such investments may provide equity-type exposure and returns. 400CM also invests in newly issued or secondary securities, loans or risk-transfer transactions focused on consumer, real estate and commercial asset-backed investments with the intent to restructure or re-securitize to monetize or term finance. 400CM, to the extent consistent with a Client Account’s investment mandate, will seek to capture outsized liquidity premiums in secondary market transactions where market liquidity has been constrained and price volatility exacerbated by reduced bank balance sheet positioning or technical trading flow imbalances the form of which may be previously securitized notes or bonds. 400CM, to the extent consistent with a Client Account’s investment mandate, also initiates long and short positions and may access exposure to assets through derivative instruments.

### *Investment Strategies*

400CM bases its investment decisions on a combination of systematic and non-systematic risk and valuation considerations. The Adviser seeks to identify high conviction themes that reflect the Adviser’s outlook on the performance of macroeconomic factors, including the domestic and global economies, employment, monetary policy, cash flow, interest rates, commercial and consumer credit quality, volatility, liquidity and asset valuation and underlying credit trends. Such themes will influence portfolio allocations across credit asset classes within the Client Account’s investment mandate. Capital allocations to sectors are based on the direction and momentum of fundamental trends and related market technical dynamics that may drive asymmetric returns with positive convexity. 400CM utilizes bottom-up fundamental analysis combined with a top-down macroeconomic view.

With respect to investments in structured credit, 400CM uses a combination of loan and asset performance databases along with sophisticated proprietary and third-party analytic models to evaluate loan portfolios and underlying investment collateral, to forecast cash flows and to define and anticipate downside risk parameters. 400CM integrates economic and market research with loan-level prepayment, delinquency, and default analysis to identify attractive

investment opportunities. Individual security selection is done through an asset-level analysis of credit quality and performance, investment structure and cash flow priority with an emphasis on identifying idiosyncratic features that may enhance returns beyond favorable underlying fundamentals.

With respect to investments in corporate credit, the Adviser seeks to identify undervalued credit investments as well as credit investments most likely to default. This analysis focuses on an issuer's ability and willingness to pay down debt through free cash flow or assets sales, as well as the value of the underlying business relative to its debt. In addition, the Adviser also analyzes the quality of the issuer's business, its management team and standing within the industry. The Adviser looks to invest in opportunities where catalysts are present to unlock value (in the case of longs) or to cause the investment to trade lower (in the case of shorts). Such catalysts may include ratings upgrades/downgrades, bond exchanges, restructurings and refinancings, bankruptcy, mergers and acquisitions, liquidations, litigation and regulatory changes.

In constructing a portfolio, the Adviser reviews investment opportunities and compares opportunities against each other with regards to expected price appreciation, cash flow yield, volatility and hedging strategies. If the Adviser believes that an investment is undervalued relative to its risk profile, a long position may be initiated. For other investments, a short position may be taken. When an investment reaches its target price or can be replaced with a more attractive investment, it is reassessed, and the position is sold or covered unless the target price is changed. Proprietary and third-party models are employed to eliminate model bias, develop risk and return profiles and perform ongoing surveillance across the portfolio.

***Material Risks (Including Significant, or Unusual Risks) Relating to Investment Strategies***

The risks associated with investments in a specific Fund are included within the respective Fund's offering documents. Investors or prospective investors in a Fund are strongly urged to review the risk factors set forth in the Fund's offering documents for a discussion of the specific risks involved in investing in such Fund.

Below is a general description of certain risks associated with investing in a structured credit strategy as well as risks associated with investing in the types of securities that are generally part of 400CM's investment strategy. The following summary does not intend to identify all risks associated with an investment in a Client Account portfolio or provide a full description of the identified risks.

These risk factors include only those risks that 400CM believes to be material, significant or unusual and relate to particular significant investment strategies or methods of analysis employed by 400CM.

Investing in securities, futures, swaps, loans and the other assets described above and below involves a risk of loss that clients should be prepared to bear.

**Nature of Investments**

There can be no assurance that the Adviser will correctly evaluate the nature and magnitude of the various factors that could affect the value of and return on investments. Prices of investments may be volatile, and a variety of factors that are inherently difficult to predict, such as domestic or international economic and political developments, may significantly affect the results of a Client Account's activities and the value of its investments. In addition, the value of Client Account portfolios may fluctuate as the general level of interest rates fluctuates. No guarantee or representation is made that investment objectives will be achieved.

**Illiquidity of Investments**

The Adviser, on behalf of certain Client Accounts will invest a significant amount of its capital in securities, loans or other assets for which no, or only a limited, market exists or that are subject to legal or other restrictions on transfer. The market prices, if any, for such assets tend to be volatile, and may fluctuate due to a variety of factors that are inherently difficult to predict, including, but not limited to, changes in interest rates, prevailing credit spreads, general economic conditions, financial market conditions, domestic or international economic or political events, developments or trends in any particular industry, and the financing condition of the obligors on a Client Account's assets. Accordingly, the Adviser may not be able to sell assets when the Adviser desires to do so or to realize what the Adviser perceives to be the fair value of their assets in the event of a sale. The sale of illiquid assets and restricted securities often requires more time and the incurrence of significant selling expenses. Restricted securities may sell at a price lower than similar securities that are not subject to restrictions on resale.

**Highly Competitive Markets**

The Adviser operates in competitive markets and faces competition for the investment opportunities that it pursues. The Adviser competes with broker/dealer companies, public and private funds, commercial and investment banks, commercial financing companies, insurance companies, high yield investors, hedge funds, and, to the extent they provide alternative forms of financing, private equity funds. Some of the Adviser's competitors are larger and have greater financial resources than the Adviser, which may cause those competitors to have lower funding costs than the Adviser and better access to funding sources. In addition, some of the Adviser's competitors may have higher risk tolerances or different risk assessment standards, which could allow them to consider a wider variety of investments or establish more referral relationships than the Adviser.

**Residential Mortgage-Backed Securities**

The Adviser, on behalf of certain Client Accounts, invests in RMBS. Holders of RMBS bear various risks, including credit, market, interest rate, structural and legal risks. RMBS represent interests in pools of residential mortgage loans secured by one to four family residential mortgage loans. Such loans may be prepaid at any time. Residential mortgage loans underlying RMBS securities are obligations of the borrowers thereunder only and are not typically insured or guaranteed by any other person or entity. Agency RMBS securities are guaranteed by one of Government National Mortgage Association, Federal National Mortgage ("Fannie Mae"), or Federal Home Loan Mortgage Corp. ("Freddie Mac"). Non-Agency RMBS securities are not guaranteed by any government agency. The rate of defaults and losses on residential mortgage loans will be affected by a number of factors, including general economic conditions and those in the geographic area where the related mortgaged property is located, the terms of the loan, the borrower's "equity" in the mortgaged property and the financial circumstances of the borrower. If a residential mortgage loan is in default, foreclosure of such residential mortgage loan may be a lengthy and difficult process and may involve significant expenses. Furthermore, the market for defaulted residential mortgage loans or foreclosed properties may be very limited.

At any one time, a portfolio of RMBS may be backed by residential mortgage loans with disproportionately large aggregate principal amounts secured by properties in only a few states or regions. As a result, the residential mortgage loans may be more susceptible to geographic risks relating to such areas, such as adverse economic conditions, adverse events affecting industries located in such areas and natural hazards affecting such areas, than would be the case for a pool of mortgage loans having more diverse property locations. In addition, the residential mortgage loans often may be "jumbo" mortgage loans, with an original

principal balance that is higher than the Fannie Mae and Freddie Mac loan balance limitations. As a result, such RMBS may experience increased losses.

Prepayments on the underlying residential mortgage loans in an issue of RMBS will be influenced by the prepayment provisions of the related mortgage notes and may also be affected by a variety of economic, geographic and other factors, including the difference between the interest rates on the underlying residential mortgage loans (giving consideration to the cost of refinancing) and prevailing mortgage rates and the availability of refinancing. In general, if prevailing interest rates fall significantly below the interest rates on the related residential mortgage loans, the rate of prepayment on the underlying residential mortgage loans would be expected to increase. Conversely, if prevailing interest rates rise to a level significantly above the interest rates on the related mortgages, the rate of prepayment would be expected to decrease. Prepayments could reduce the yield received on the related issue of RMBS. RMBS are particularly susceptible to prepayment risks as they generally do not contain prepayment penalties and a reduction in interest rates will increase the prepayments on the RMBS, resulting in a reduction in yield to maturity for holders of such securities.

The RMBS may be backed by non-conforming mortgage loans, which are mortgage loans that do not qualify for purchase by government-sponsored agencies such as Fannie Mae and Freddie Mac because of credit characteristics and size that do not satisfy Fannie Mae and Freddie Mac guidelines, including loans to borrowers whose creditworthiness and repayment ability do not satisfy Fannie Mae and Freddie Mac underwriting guidelines and loans to borrowers who may have a record of credit write-offs, outstanding judgments, prior bankruptcies and other negative credit items. Accordingly, non-conforming mortgage loans are likely to experience rates of delinquency, foreclosure and loss that are higher, and that may be substantially higher, than mortgage loans originated in accordance with Fannie Mae or Freddie Mac underwriting guidelines. The principal differences between conforming mortgage loans and non-conforming mortgage loans include the applicable loan-to-value ratios, the credit and income histories of the related borrowers, the documentation required for approval of the related mortgage loans, the types of properties securing the mortgage loans, the loan sizes and the borrowers' occupancy status with respect to the mortgaged properties. As a result of these and other factors, the interest rates charged on non-conforming mortgage loans are often higher than those charged for conforming mortgage loans. The combination of different underwriting criteria and higher rates of interest may also lead to higher delinquency, foreclosure and losses on non-conforming mortgage loans as compared to conforming mortgage loans.

RMBS may be backed by reverse mortgage loans or reverse home equity conversion loans ("HECMs"), whereby the underlying borrower is entitled to receive scheduled or unscheduled payments. HECM terms may include (1) a line of credit whereby the borrower receives unscheduled payments or installments, drawn down at times and in amounts of the borrower's choosing, up to the related net principal limit, (2) a tenure loan whereby the borrower is entitled to receive a monthly payment from the mortgagee for the remainder of the borrower's life, so long as the borrower continues to occupy the related mortgaged property and is in compliance with the terms of the mortgage, (3) a term loan whereby the borrower is entitled to receive a monthly payment from the mortgagee for a specified term, (4) a modified tenure loan, whereby a portion of the principal limit of the loan is made available to the borrower in a series of monthly payments for the remainder of the borrower's life, and the remainder of the principal limit is a line of credit whereby the borrower may borrow, repay and reborrow the portion of the principal thereof, up to the related net principal limit, (5) a modified term loan, whereby a portion of the principal limit of the loan is made available to the borrower in a series of monthly payments for a specified term, and the remainder of the principal limit is a line of credit whereby the borrower may borrow, repay and reborrow the portion of the principal thereof, up to the related net principal limit or (6) a fixed-rate loan whereby the borrower receives a single lump sum on the funding date for such

loan, in each case provided that borrower continues to occupy the related mortgaged property and is in compliance with the terms of the mortgage and the borrower is not in default. Payments on a HECM RMBS will depend in part upon receipt of payments with respect to the mortgage loans following the occurrence of a maturity event, including the occurrence of the following: (a) the sale or transfer of the related mortgaged property, (b) the death of the last remaining mortgagor, (c) the change in principal residence of the mortgagor, for reasons other than the death of such mortgagor, and the related mortgaged property is not the principal residence of at least one other mortgagor, (d) the failure by the mortgagor to occupy the related mortgaged property for a prescribed period due to certain factors, or (e) the related mortgagor is in default under the terms of such HECM. HECMs are non-recourse to the borrower so if the value of the mortgaged property is not sufficient to repay the principal balance, there is no additional recourse to the borrower.

RMBS may be backed by home equity lines of credit (“**HELOCs**”), whereby the underlying borrower is entitled to receive revolving credit disbursements during a designated draw period. HELOCs typically have a maturity date of 10 years and require the borrower to make monthly payments, although borrowers may be permitted to make interest-only payments meaning that a balloon payment may be required upon maturity. RMBS backed by HELOCs are more subject to interest rate risk than HECMs, as when interest rates increase monthly HELOC payments also increase. Further, HELOCs may be secured by junior lien mortgages which are subordinate to the rights of the mortgagee under each senior lien mortgage and there is an increased risk that the related property may not provide sufficient security for a junior lien mortgage.

RMBS may be backed by investor bridge mortgage loans, also known as “fix and flip loans” (“**Investor Bridge Loans**”). Investor Bridge Loans are a relatively new mortgage product and may consist of performing and non-performing, fixed and floating rate, amortizing and interest-only, non-owner occupied mortgage loans at various stages of seasoning, to real estate investors, secured by first and second liens on primarily one- to four-family residential properties, multifamily properties and mixed-use properties at various stages of completion, with original terms to maturity of 10 to 36 months excluding current extensions and future extension options. As such, these Mortgage Loans contain risks that are not present in typical residential mortgage loans made to consumers. These risks include: (a) they may be short term interest-only loans, with the full amount of principal due at maturity, and the mortgagors generally rely on the sale or refinancing of the related mortgaged properties to generate the funds necessary to repay the balloon payment due at maturity, (b) they are secured by non-owner occupied mortgaged properties, (c) they often require construction repairs or rehabilitation projects and the mortgaged properties are often in a general state of disrepair, (d) certain of the mortgage loans may be ground-up construction loans, which involve a greater scope of work compared to a repair or rehabilitation project, which, in turn, increases the likelihood of additional risks and issues, including, but not limited to, planning issues, labor shortages, supply and equipment interruptions, scheduling conflicts, construction delays, cost overruns, zoning, permitting and completion risks, (e) multiple mortgage loans may have been made to the same mortgagor, (f) the ability of a mortgagor to repay a mortgage loan may be based largely on the ability to sell the related mortgaged property or to convert the property to a rental property and the ability to refinance the mortgage loan into a longer term loan, (g) the mortgage loans may have had their maturity dates extended (h) the mortgage loans may have longer than expected liquidation timelines upon the occurrence of an event of default and (i) the mortgagors may be thinly capitalized.

RMBS may contain certain credit enhancement features intended to enhance the likelihood that holders of such securities will receive regular payments of interest and principal. If delinquencies or defaults occur on the mortgage loans underlying such RMBS, neither the related servicers nor any other entities will advance scheduled monthly payments of interest and principal on delinquent or defaulted mortgage loans if such advances are not likely to be



recovered within those transactions. There can be no assurance that the credit enhancement, if any, applicable to RMBS will adequately cover any shortfalls in cash available to make payments on such RMBS as a result of such delinquencies or defaults. If substantial losses occur as a result of defaults and delinquent payments on the mortgage loans, a Client Account invested in RMBS may suffer losses with respect to its ownership of such RMBS.

Another factor that may result in higher delinquency rates is the increase in monthly payments on adjustable rate mortgage loans. Borrowers with adjustable rate mortgage loans are being exposed to increased monthly payments when the related mortgage interest rate adjusts upward from the initial fixed rate or a low introductory rate. Borrowers seeking to avoid these increased monthly payments by refinancing their mortgage loans may no longer be able to find available replacement loans at comparably low interest rates. A decline in housing prices may also leave borrowers with insufficient equity in their homes to permit them to refinance. Furthermore, borrowers who intend to sell their homes on or before the expiration of the fixed rate periods on their mortgage loans may find that they cannot sell their properties for an amount equal to or greater than the unpaid principal balance of their loans. These events, alone or in combination, may contribute to higher delinquency rates and, as a result, adversely affect the performance and market value of RMBS.

The terms of mortgage loans underlying RMBS may be modified by the servicer, if the loans are in default or default is reasonably foreseeable. Changes in the terms of a mortgage loan may include the capitalization of past due payments, lowering of the interest rate, conversion of an adjustable interest rate to a fixed interest rate, extension of the maturity date, the forgiveness of past due principal and/or interest payments, or other modifications, any of which will reduce or delay payment of the amount owed to the trust fund by the related borrower or delay the receipt of payments from the borrower. Any of the various possible modifications of the terms of a mortgage loan that is in default or as to which default is reasonably foreseeable may, even if beneficial to the securitization trust in the aggregate, affect some holders of RMBS adversely. In determining whether a particular loan modification should be made, the servicer will not consider the interests of individual classes of RMBS. Conversely, failure by the servicer to timely modify the terms of a defaulted mortgage loan may reduce amounts available for distribution to holders of RMBS in respect of that mortgage loan.

RMBS may be subordinated to one or more other senior classes of securities of the same series for purposes of, among other things, offsetting losses and other shortfalls with respect to the related underlying mortgage loans. In addition, in the case of certain RMBS, no distributions of principal will generally be made with respect to any class until the aggregate principal balances of the corresponding senior classes of securities have been reduced to zero. As a result, subordinate classes of RMBS are more sensitive to risk of loss and write-downs than senior classes of RMBS.

Numerous federal and state statutory provisions, including the federal bankruptcy laws, the Mortgage Debt Relief Act of 2007 and state debtor relief laws, moratoriums on foreclosures and evictions related to COVID-19 and numerous proposals at the federal, state or local level, if enacted, also may adversely affect the ability of an issuer of a RMBS to collect the principal of or interest on the loans, or to foreclose upon defaulted mortgage loans and holders of the affected RMBS may suffer a loss if the applicable laws result in these loans becoming uncollectible.

Legislative or regulatory initiatives by federal, state or local legislative bodies or administrative agencies that have been or may be enacted or adopted, including for example, in New York, the "Foreclosure Abuse Prevention Act" (s5473), could delay foreclosure, provide new defenses to foreclosure or otherwise impair the ability of the servicer to foreclose on a defaulted mortgage loan. Various jurisdictions have considered or are

currently considering such actions, and the nature or extent of limitations on foreclosure that may be enacted cannot be predicted. Any such governmental actions that interfere with the foreclosure process could delay the timing or reduce the amount of recoveries on defaulted mortgage loans and could adversely affect the yields on RMBS.

### **Developments in the Residential Mortgage Market**

Delinquencies, defaults and losses on residential mortgage loans may affect the performance of RMBS, in particular RMBS that are backed by subprime and midprime mortgage loans, as well as “Alt-A” and “Alt-B” mortgage loans and second lien mortgage loans (collectively, “**Non-Prime Residential Mortgage Securities**”). Subprime and midprime mortgage loans are generally made to borrowers with lower credit scores and having higher loan-to-value ratios. Alt-A and Alt-B loans may also have some of the characteristics of subprime and midprime mortgage loans. Accordingly, mortgage loans backing Non-Prime Residential Mortgage Securities are more sensitive to economic factors that could affect the ability of borrowers to pay their obligations under the mortgage loans backing these securities. A decline of housing prices and appraisal values may result in additional increases in delinquencies and losses on RMBS generally.

General trends in consumer borrowing and mortgage lending may have increased the sensitivity of the subprime market to changes in economic conditions. As a general matter, mortgage lenders may, in certain cases, have loosened their credit criteria. Discoveries of fraudulent mortgage loan applications in connection with rising default rates with respect to subprime mortgage loans may indicate that the risks with respect to these mortgage loans are particularly acute. Equity contributions by borrowers required in order to obtain financing may also have decreased. In addition, certain borrowers may have financed their equity contributions with “piggy-back” loans, resulting in little to no equity with respect to their mortgage loan financing. An increase may also have occurred with respect to mortgage loans entered into to finance investment properties, which generally have a higher tendency to become delinquent and to default than mortgage loans made to finance primary residences. These trends in the mortgage loan industry and in consumer behavior may increase the likelihood of defaults, delinquencies and losses on mortgage loan portfolios.

With respect to adjustable rate mortgage loans and hybrid mortgage loans that have or will enter their adjustable-rate period, borrowers are likely to experience increases in their monthly payments and become increasingly likely to default on their payment obligations. Higher combined loan-to-value ratios may result in lower recoveries on foreclosure, and an increase in net losses above those that would have been realized had property values remained the same or increased. A decline in property values is particularly likely to impact recoveries on any second lien mortgage loans included in the mortgage pools backing RMBS.

Market conditions may impair borrowers’ ability to refinance or sell their properties, which may contribute to higher delinquency and default rates. Borrowers seeking to avoid increased monthly payments by refinancing may no longer be able to find available replacement loans at comparably low interest rates. A decline in housing prices may also leave borrowers with insufficient equity in their homes to permit them to refinance. Borrowers who intended to sell their homes on or before the expiration of the fixed rate periods on their mortgage loans may find that they cannot sell their property for an amount equal to or greater than the unpaid principal balance of their loans. In addition, some mortgage loans may include prepayment premiums that would further inhibit refinancing.

Structural features of RMBS may contribute to the impact of increased delinquencies and defaults and lower recoveries on the underlying mortgage pool. In particular, there may be a decline in the interest rate payable under those RMBS structured to limit interest payable to investors based on a weighted average coupon cap. Mortgage loans bearing interest at a



higher rate will have a greater tendency to default than those with lower mortgage rates. Such defaults will reduce the weighted average coupon of the underlying mortgage loans and accordingly the interest rate payable to investors in the related RMBS. In addition, delinquencies, defaults and lower recoveries on underlying mortgage loans will reduce interest and principal actually paid to investors to less than the amounts owed to investors in accordance with the terms of their RMBS. RMBS may not be structured with significant or any overcollateralization, so their performance will be sensitive to delays or reductions in payments, particularly in the case of subordinated tranches of RMBS. To the extent that RMBS provide for write-downs of principal, interest will cease to accrue on the portion of principal of an RMBS that has been written down.

RMBS may provide that the servicer is required to make advances in respect of delinquent mortgage loans. However, servicers experiencing financial difficulties may not be able to perform these obligations. Servicers who have sought bankruptcy protection may, due to application of the provisions of bankruptcy law, not be required to advance such amounts. Even if a servicer were able to advance amounts in respect of delinquent mortgage loans, its obligation to make such advances may be limited to the extent that it does not expect to recover such advances due to the deteriorating credit of the delinquent mortgage loans. In addition, a servicer's obligation to make such advances may be limited to the amount of its servicing fee.

A number of originators and servicers of mortgage loans have experienced serious financial difficulties and, in some cases, have entered bankruptcy proceedings. These difficulties have resulted in part from declining markets for their mortgage loans and claims for repurchases by them of mortgage loans previously sold under provisions that require repurchase in the event of early payment defaults or for material breaches of representations and warranties made on the mortgage loans, such as fraud claims. These difficulties have been compounded by a general decline in the willingness by banks and other financial institutions to extend credit to originators and servicers in the asset-backed securities industry and the resulting disappearance of available credit and liquidity lines to such originators and servicers. Higher delinquencies and defaults may also be contributing to these difficulties by reducing the value of mortgage loan portfolios, requiring originators to sell their portfolios at greater discounts to par. In addition, the costs of servicing an increasingly delinquent mortgage loan portfolio may be rising without a corresponding increase in servicing compensation. The value of any residual interests retained by sellers of mortgage loans in the securitization market may also be declining in these market conditions. Declining real estate values may decrease the number of borrowers seeking or able to refinance their mortgage loans, resulting in a decrease in overall originations. These factors, among others, may have the overall effect of increasing costs and expenses of originators and servicers while at the same time decreasing servicing cash flow and loan origination revenues. Such financial difficulties may have a negative effect on the ability of servicers to pursue collection on mortgage loans that are experiencing increased delinquencies and defaults and to maximize recoveries on sale of underlying properties following foreclosure. Many servicers have become overwhelmed by the number of defaulted loans in their servicing portfolios and are unable or unwilling to pursue collections or other remedies or commence foreclosure proceedings on many defaulted mortgage loans.

In addition, the inability of the originator to repurchase such mortgage loans in the event of early payment defaults and loan representation breaches may also affect the performance of RMBS backed by those mortgage loans. These difficulties may adversely affect the performance and market value of RMBS originated, serviced or sub-serviced by these companies.

Under certain circumstances, including a failure to perform its servicing obligations or a bankruptcy of the servicer and in some cases, certain loss and/or delinquency triggers being

exceeded, investors may be entitled to remove and replace the existing servicer. There is no guarantee, however, that a suitable servicer could be found to assume the obligations of the existing servicer, and the transition of servicing responsibilities to a replacement servicer could have an adverse effect on performance of servicing functions during or following a transition period and result in an increase in delinquencies and losses and decreases in recoveries. The loss by a servicer of its right to service a mortgage loan portfolio would decrease servicing revenues and may result in reputational damage as a servicer.

Transfers of mortgage loans by the related originator or seller will be characterized in the applicable sale agreement as a sale transaction. Nevertheless, in the event of a bankruptcy of the originator or seller, the trustee in bankruptcy could attempt to recharacterize the sale of the mortgage loans as a borrowing secured by a pledge of the mortgage loans. If such attempt were successful, the trustee in bankruptcy could prevent the trustee for the RMBS from exercising any of the rights of the owner of the mortgage loans and also could elect to liquidate the mortgage loans. Investors may suffer a loss to the extent that the proceeds of the liquidation of the underlying mortgage loans would not be sufficient to pay amounts owed in respect of their investments. If this occurs, investors would lose the right to future payments of interest and may fail to recover their initial investment. Regardless of whether a trustee elects to foreclose on the underlying mortgage loan pool, delays in payments on the RMBS and possible reductions in the amount of these payments could occur as a result of the bankruptcy of the originator or seller.

The rise in the rate of foreclosures of properties backing subprime loans in certain states or localities has resulted in legislators, regulators and attorney generals in such states or localities seeking measures to prevent or restrict foreclosures and bringing lawsuits against participants in the financing of subprime loans in their states or localities, including issuers and underwriters of RMBS backed by such loans and investors in such RMBS. Such trends in forestalling or limiting foreclosures may continue to increase.

The rating agencies have placed on credit watch with negative implications or downgraded the ratings previously assigned to a large number of RMBS (as well as ABS CDO Securities backed by such RMBS). An “ABS CDO Security” is any CDO security (a “**CDO Security**”) with respect to which the related underlying portfolio of assets consists primarily of ABS, real estate investment trust debt securities and/or CDO Securities.

Non-prime mortgage loans that were originated by certain originators in the recent past have experienced higher and earlier-than-expected rates of delinquency and are likely to experience default and loss levels that are substantially higher than those suggested by historical default and loss data. Since the delinquency rates of non-prime loans are continuing to rise, it is unclear what the ultimate default and loss experience on these loans will be. Non-Prime Residential Mortgage Securities (as well as ABS CDO Securities backed by such RMBS) may have significant exposure to such subprime, midprime and other non-prime mortgage loans, and any such security will likely experience loss levels that may substantially exceed losses that were expected of such security based on historical default and loss data regarding the underlying subprime, midprime and other non-prime mortgage loans.

A portion of the RMBS may be RMBS which were originated or are serviced (or both) by mortgage companies which are currently in bankruptcy proceedings or regulatory enforcement actions which have restricted the ability of the lender or its affiliates to originate mortgage loans and may affect its ability to service or subservice mortgage loans. Servicers who have sought bankruptcy protection may, due to the application of applicable law in the proceeding, also no longer be required to make service advances.

The foregoing adverse changes in market conditions and regulatory climate may reduce the cashflow received from RMBS (or credit default swaps, embedded credit default swaps or other synthetic securities that reference RMBS or ABS CDO Securities backed by RMBS) and increase the incidence and severity of credit events and floating amount events under the credit default swaps, embedded credit default swaps or other synthetic securities. In addition, interest rate spreads for RMBS (and fixed rates on synthetic securities which reference them) have widened and are more volatile when compared to the recent past due to these adverse changes in market conditions. In the event that interest rate spreads for RMBS (and/or fixed rates on synthetic securities referencing RMBS), continue to widen following the purchase of such assets, the market value of such assets is likely to decline and, in the case of a substantial spread widening, could decline by a substantial amount. Furthermore, these adverse changes in market conditions have resulted in a severe liquidity crisis in the market for RMBS (as well as ABS CDO Securities backed by RMBS) and increasing unwillingness by banks, financial institutions and investors to extend credit to servicers, originators and other participants in the market for these securities and other asset-backed securities. As a result, the liquidity and/or the market value of RMBS, ABS CDO Securities backed by RMBS and other asset-backed securities may experience further declines after purchase and may face significant lack of liquidity.

### **Commercial Mortgage-Backed Securities**

Collateral underlying CMBS generally consists of mortgage loans secured by income producing property, such as regional malls, other retail space, office buildings, industrial or warehouse properties, hotels, rental apartments, nursing homes, senior living centers and self-storage properties. The Adviser, on behalf certain Client Accounts, invests in CMBS and in credit derivatives that reference CMBS and also invests in ABS CDO Securities that are backed in whole or in part by CMBS. Performance of a commercial mortgage loan depends primarily on the net income generated by the underlying mortgaged property. The market value of a commercial property similarly depends on its income-generating ability. As a result, income generation will affect both the likelihood of default and the severity of losses with respect to a commercial mortgage loan. Any decrease in income or value of the commercial real estate underlying an issue of CMBS could result in cash flow delays and losses on the related issue of CMBS.

Most commercial mortgage loans underlying CMBS are effectively non-recourse obligations of the borrower, meaning that there is no recourse against the borrower's assets other than the collateral. If borrowers are not able or willing to refinance or dispose of encumbered property to pay the principal and interest owed on such mortgage loans, payments on the subordinated classes of the related CMBS are likely to be adversely affected. The ultimate extent of the loss, if any, to the subordinated classes of CMBS may only be determined after a negotiated discounted settlement, restructuring or sale of the mortgage note, or the foreclosure (or deed in lieu of foreclosure) of the mortgage encumbering the property and subsequent liquidation of the property. Foreclosure can be costly and delayed by litigation and/or bankruptcy. Factors such as the property's location, the legal status of title to the property, its physical condition and financial performance, environmental risks and governmental disclosure requirements with respect to the condition of the property may make a third party unwilling to purchase the property at a foreclosure sale or to pay a price sufficient to satisfy the obligations with respect to the related CMBS. Revenues from the assets underlying such CMBS may be retained by the borrower and the return on investment may be used to make payments to others, maintain insurance coverage, pay taxes or pay maintenance costs. Such diverted revenue is generally not recoverable without a court appointed receiver to control collateral cash flow. The owner of CMBS does not have a contractual relationship with the borrowers of the underlying commercial mortgage loans. The CMBS holder typically has no right directly to enforce compliance by the borrowers with the terms of the loan agreement, nor any rights of set-off against the borrower, nor will

it have the right to object to certain changes to the underlying loan agreements, nor to move directly against the collateral supporting the related loans.

Successful management and operation of the related business (including property management decisions such as pricing, maintenance and capital improvements) will have a significant impact on performance of commercial mortgage loans. Issues such as tenant mix, success of tenant business, property location and condition, competition, increases in interest rates, real estate taxes and other operational expenses, general or local economic conditions and/or specific industry segments, declines in real estate values, declines in rental or occupancy rates and civil disturbances, changes in governmental rules, regulations and fiscal policies, acts of God, social unrest and insurance coverage are among the factors that may impact both performance and market value. The value of commercial real estate is also subject to a number of laws, and limitations on remedies imposed by bankruptcy laws and state laws regarding foreclosures and rights of redemption.

Property-specific issues with respect to the underlying mortgaged property, such as significant government regulation of a particular industry, reliance on franchise, management or operating agreements, transferability on purchase or foreclosure of related valuable assets such as liquor and other licenses and ease of conversion of a commercial property to an alternative use will impact both risk of loss and loss severity with respect to the underlying mortgage loan pool and the CMBS.

At any one time, a portfolio of CMBS may be backed by commercial mortgage loans with disproportionately large aggregate principal amounts secured by properties in only a few states or regions. As a result, the commercial mortgage loans may be more susceptible to geographic risks relating to such areas, such as adverse economic conditions, adverse events affecting industries located in such areas and natural hazards affecting such areas, than would be the case for a pool of mortgage loans having more diverse property locations.

Certain of the commercial mortgage loans underlying the collateral debt securities may bear interest at adjustable rates based on interest indices. Accordingly, debt service for any such commercial mortgage loan will increase as interest rates rise. In contrast, rental and other income on the related mortgaged properties is not expected to rise significantly as interest rates rise. Accordingly, debt service coverage ratios of the underlying floating rate commercial mortgage loans generally will be adversely affected by rising interest rates, and a borrower's ability to make all payments due on such floating rate commercial mortgage loans may be adversely affected. Additionally, it is expected that the London Interbank Offered Rate ("LIBOR") will be discontinued as a reference rate within various financial contracts (any such rate, a "**Reference Rate**"). Although the outcome of LIBOR's redaction is presently unclear, Reference Rates such as Sterling Overnight Interbank Average Rate and Secured Overnight Financing Rate may replace LIBOR as Reference Rates. As a general matter, the expected discontinuation of LIBOR may significantly impact financial markets; specifically, discontinuation may impact financial contracts to which Client Accounts are party. Generally, the transition to alternative Reference Rates may (i) cause the value of a Reference Rate to be uncertain or to be lower or more volatile than it would otherwise be; (ii) result in uncertainty as to the functioning, liquidity or value of certain financial contracts; (iii) involve actions of regulators or rate administrators that adversely affect certain markets or specific financial contracts; and (iv) impact the strategy, products, processes, legal positions and information systems of market participants, including Client Accounts and their respective counterparties. Considered in their entirety, the impacts of the discontinuation of LIBOR on financial markets generally and on the specific financial contracts to which Client Accounts are party may adversely affect the performance of various Client Accounts.

Mortgage loans underlying a CMBS issue may provide for no amortization of principal or may provide for amortization based on a schedule substantially longer than the maturity of

the mortgage loan, resulting in a “balloon” payment due at maturity. If the underlying mortgage borrower experiences business problems, or other factors limit refinancing alternatives, such balloon payment mortgages are likely to experience payment delays or even default. As a result, the related issue of CMBS could experience delays in cash flow and losses.

CMBS may also be backed by Investor Bridge Loans and therefore may be subject to similar risks relating to Investor Bridge Loans as RMBS backed by Investor Bridge Loans.

In connection with COVID-19, federal, state and local governmental authorities implemented measures designed to provide relief to borrowers and tenants, including moratoria on foreclosure or eviction proceedings and mandated forbearance programs. In addition, leases for certain of the tenants at the mortgaged properties may include provisions which allow the tenants to abate or delay rent payments or, in certain circumstances, to terminate the lease, if the tenant is required to suspend its business operations, or its business operations are otherwise disrupted, as a result of COVID-19. Any such measures relating to commercial real estate may lead to shortfalls and losses on CMBS securities.

### **Asset-Backed Securities**

The Adviser, on behalf of certain Client Accounts, invests in ABS and the loans or receivables underlying such ABS. The structure of an ABS, and the terms of the investors' interest in the underlying collateral, can vary widely depending on the type of collateral, the desires of investors and the use of credit enhancements. Consumer ABS is backed by cash flows from personal financial assets such as student loans, credit card receivables, and auto loans. Commercial ABS is backed by cash flows from receivables, such as trade receivables, loans, or leases on shipping containers, aircraft, and other commercial equipment. Individual transactions can differ markedly in both structure and execution. Important determinants of the risk associated with issuing or holding ABS include (i) the relative seniority or subordination of the class of ABS held by an investor, (ii) the relative allocation of principal and interest payments in the priorities by which such payments are made under the governing documents, (iii) the effect of credit losses on both the issuing vehicle and investors' returns, (iv) whether the underlying collateral represents a fixed set of specific assets or accounts, (v) whether the underlying collateral assets are revolving or closed-end, (vi) the terms (including maturity of the ABS) under which any remaining balance in the accounts may revert to the issuing vehicle and (vii) the extent to which the entity that sold the underlying collateral to the issuing vehicle is obligated to provide support to the issuing vehicle or to investors. .

In addition, certain ABS (particularly subordinated ABS) may provide that the non-payment of interest thereon in cash will not constitute an event of default in certain circumstances, and the holders of such ABS will not have available to them any associated default remedies. Interest not paid in cash will generally be capitalized and added to the outstanding principal balance of the related security. Deferral of interest through such capitalization will reduce the yield on such ABS.

Holders of ABS bear various risks, including credit risks, liquidity risks, interest rate risks, market risks, operations risks, structural risks and legal and regulatory risks. Credit risk arises from (i) losses due to defaults by obligors under the underlying collateral and (ii) the issuing vehicle's or servicer's failure to perform their respective obligations under the transaction documents governing the ABS. These two risks may be related, as, for example, in the case of a servicer that does not provide adequate credit-review scrutiny to the underlying collateral, leading to a higher incidence of defaults.

Market risk arises from the cash flow characteristics of the ABS, which for most ABS tend to be predictable. The greatest variability in cash flows comes from credit performance,



including the presence of wind-down or acceleration features designed to protect the investor in the event that credit losses in the portfolio rise well above expected levels.

Interest rate risk arises for the issuer from (i) the pricing terms on the underlying collateral, (ii) the terms of the interest rate paid to holders of the ABS and (iii) the need to mark to market the excess servicing or spread account proceeds carried on the issuing vehicle's balance sheet. For the holder of the security, interest rate risk depends on the expected life of the ABS, which may depend on prepayments on the underlying assets or the occurrence of wind-down or termination events. If the servicer becomes subject to financial difficulty or otherwise ceases to be able to carry out its functions, it may be difficult to find other acceptable substitute servicers and cash flow disruptions or losses may occur, particularly with underlying collateral comprised of non-standard receivables or receivables originated by private retailers who collect many of the payments at their stores.

Structural and legal risks include the possibility that, in a bankruptcy or similar proceeding involving the originator or the servicer (often the same entity or affiliates), a court having jurisdiction over the proceeding could determine that, because of the degree to which cash flows on the assets of the issuing vehicle may have been commingled with cash flows on the originator's other assets (or similar reasons), (i) the assets of the issuing vehicle could be treated as never having been truly sold by the originator to the issuing vehicle and could be substantively consolidated with those of the originator, or (ii) the transfer of such assets to the issuer could be voided as a fraudulent transfer. The time and expense related to a challenge of such a determination also could result in losses and/or delayed cash flows.

A Client Account may obtain exposure to ABS through its purchase of ABS CDO Securities. In addition to the risks related to ABS discussed above, an ABS CDO Security will also be subject to the general risks applicable to a CDO Security described below. A Client Account may purchase ABS CDO Securities that are CDO Equity Tranches or CDO Mezzanine Tranches of the CDO issuing such ABS CDO Security. The risks related to both ABS and CDO Securities (particularly CDO Equity Tranches or CDO Mezzanine Tranches) should be carefully considered when evaluating the impact of the risks of ABS CDO Securities on the performance of the Adviser's investments on behalf of certain Client Accounts.

A Client Account may also invest directly in pools of consumer and commercial loans. Such investments will not have the benefit of the credit enhancement features of ABS but will be subject to similar risks with respect to the underlying collateral.

### **Collateralized Loan Obligations**

The Adviser, on behalf of certain Client Accounts, invests, among other things, in cash and synthetic CLO debt and equity securities ("**CLO Securities**"), through purchases in the new issues or secondary market. The CLO securities into which the Adviser invests are principally collateralized by senior secured assets. CLO Securities are subject to various risks including the following credit, liquidity, interest rate and other risks:

(a) *Limited Diversification.* Certain CLOs may invest in concentrated portfolios of assets. The concentration of an underlying portfolio in any one obligor would subject the holder of the related CLO Securities (and the related CLO equity securities in particular) to a greater degree of risk with respect to defaults by such obligor and the concentration of a portfolio in any one industry or region would subject the holder of the related CLO Securities (and the related CLO equity securities in particular) to a greater degree of risk with respect to economic downturns relating to such industry or region.

(b) *Leverage Risk.* Investment in CLOs involves significant leverage. Leverage is embedded in all classes of a CLO other than the most senior tranche, with the highest

leverage applicable to an investment in CLO equity securities. While the leverage presents opportunities for increasing total return, it has the effect of potentially increasing losses as well. Accordingly, any event that adversely affects the value of an investment in a CLO would be magnified to the extent that a CLO security is leveraged. The cumulative effect of the use of leverage by a CLO in a market that moves adversely to the CLO's investments could result in a substantial loss to the investor in the CLO with the greatest loss applicable to the equity securities issued by the CLO. When entering into a credit derivative transaction, leverage often will be embedded in such transaction as well, which will expose the investor to a greater risk of loss.

(c) *Risks of Investment Focus.* The value of the CLO Securities generally will fluctuate with, among other things, the financial condition of the obligors or issuers of the underlying portfolio of assets of the related CLO ("**CLO Collateral**"), market conditions, general economic conditions, the condition of certain financial markets, political events, developments or trends in any particular industry and changes in prevailing interest rates. CLO Securities are issued on a non-recourse basis and holders of CLO Securities must rely solely on distributions on the CLO Collateral or proceeds thereof for payment in respect thereof. If distributions on the CLO Collateral are insufficient to make payments on the CLO Securities, no other assets will be available for payment of the deficiency and following liquidation of the CLO Collateral, the obligations of such issuer to pay such deficiency will be extinguished.

(d) *Lower Credit Quality Securities.* There are limited restrictions on the credit quality of the investments of the Adviser on behalf of certain Client Accounts. CLO Securities may be deemed by rating agencies to have substantial vulnerability to default in payment of interest and/or principal. Other securities may have the lowest quality ratings or may be unrated. The Adviser, on behalf of certain Client Accounts, may purchase CLO Securities which have ratings that have been downgraded or placed on "credit watch" for future downgrading. 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 return potential than higher rated securities but involve greater volatility of price and greater risk of loss of income and principal.

The market values of CLO Securities also tend to be more sensitive to changes in market or economic conditions than other securities. The value of the leveraged loans underlying a CLO 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.

(e) *Liquidity of Markets.* At times, the fixed income markets have in the past experienced significant falloffs in liquidity. While such events may sometimes be attributable to changes in interest rates or other factors, the cause is not always apparent. During such periods of market illiquidity, a CLO may not be able to sell assets in its portfolio or may only be able to do so at unfavorable prices. The market for CLO Securities has experienced a rapid decline in liquidity. Such "liquidity risk" could adversely impact the value of a Client Account's portfolio and may be difficult or impossible to hedge against. Further, a Client Account may not be able to readily dispose of portions of its portfolio under such and other circumstances and, in some cases, may be contractually prohibited from disposing of certain portions of its portfolio for a specified period of time. CLO Securities may have no, or only a limited, trading market, which may make it difficult to sell them quickly without incurring significant losses. Because CLO Securities may be illiquid, they can be difficult to value and the valuations are often based on models or an indicative price from a dealer, rather than on prices at which the security was actually sold; as a result, a CLO Security may experience large movements in price that may not reflect the actual sales prices of the security. If holders of CLO Securities attempt to liquidate large portfolios of such



securities over a short period of time, difficulties in the market for such securities may be exacerbated, resulting in further decreased liquidity and pricing.

(f) *Default and Recovery Rates of CLO Collateral.* There are varying sources of statistical default and recovery rate data for loans and high yield securities and numerous methods for measuring default and recovery rates. The historical performance of the high yield market or the leveraged loan market is not necessarily indicative of its future performance.

(g) *Subordination of CLO Securities.* Subordinate CLO Securities generally are fully subordinated to the related CLO senior tranches. Thus, investments by the Adviser on behalf of a Client Account in a CLO often will rank behind other creditors of the CLO and an investment by the Adviser on behalf of a Client Account in the equity tranche of a CLO will rank behind all creditors of the CLO. To the extent that any losses are incurred by a CLO in respect of its related CLO Collateral, such losses will be borne first by the holders of the related CLO equity, next by the holders of any related subordinated CLO debt and finally by the holders of the related CLO senior tranches. In addition, if an event of default occurs under the governing instrument or underlying investment, as long as any CLO senior tranches are outstanding, the holders thereof generally will be entitled to determine the remedies to be exercised under the instrument governing the CLO. Remedies pursued by such holders could be adverse to the interests of the holders of any related subordinated CLO debt or CLO equity. Investments by the Adviser on behalf of a Client Account may be the first to absorb any losses by the CLO on its underlying portfolio. This may result in losses on the invested proceeds and could result in the complete loss of invested proceeds.

(h) *Mandatory Redemption of CLO Senior Tranches.* Under certain circumstances, cash flows from CLO Collateral that otherwise would have been paid to the holders of its mezzanine CLO debt and the related CLO equity will be used to redeem the related CLO senior tranches. This could result in an elimination, deferral or reduction in the interest payments, principal repayments or other payments made to the holders of such CLO debt, which the CLO Securities in which the Adviser on behalf of a Client Account may invest, which could adversely impact the returns to such Client Account.

(i) *CLO Collateral.* CLO Collateral will generally consist of senior secured loans, including commercial loans. Such loans are typically negotiated by one or more commercial banks or other financial institutions and syndicated among a group of commercial banks and financial institutions and other investors. The loans will typically be to borrowers which have no ratings or below investment grade ratings and will generally be highly leveraged companies.

Corporate loans are typically at the most senior level of the capital structure, and may be secured by specific collateral, including, but not limited to, trademarks, patents, accounts receivable, inventory, equipment, buildings, real estate, franchises and common and preferred stock of the obligor and its subsidiaries. The corporate loans included (or referenced) in a CLO Security may be of a type generally incurred by the borrowers thereunder in connection with a highly leveraged transaction, often to finance internal growth, acquisitions, mergers, stock purchases, or for other reasons. As a result of the additional debt incurred by the borrower in the course of the transactions, the borrower's creditworthiness is often judged by rating agencies to be below investment grade. Certain of the loans included (or referenced in) a CLO Security may be "second lien" loans or loans that are subordinated to other obligations of the borrower. In order to induce the banks and institutional investors to invest in a borrower's loan facility, and to offer a favorable interest rate, the borrower often provides the banks and institutional investors with extensive information about its business, which is not generally available to the public. Because of the provision of confidential information, the unique and customized nature of a loan agreement,

and the private syndication of the loan, loans are not as easily purchased or sold as a publicly traded security and historically the trading volume in the loan market has been small relative to the high yield bond market.

Corporate loans often provide for restrictive covenants designed to limit the activities of the borrower in an effort to protect the right of lenders to receive timely payments of interest on, and repayment of principal of, the loans. Such covenants may include restrictions on dividend payments, specific mandatory minimum financial ratios, limits on total debt and other financial tests. Many loans have “covenant lite” loans under which covenants are only applicable if the borrower proposes to take a specified action. A breach of covenant (after giving effect to any cure period) in a loan that is not waived by the lending syndicate normally is an event of acceleration that allows the syndicate to demand immediate repayment in full of the outstanding loan. Loans usually have shorter terms than more junior obligations and may require mandatory prepayments from excess cash flow, asset dispositions and offerings of debt and/or equity securities. Generally, a borrower can prepay a loan at any time without paying a prepayment penalty.

The majority of corporate loans bear interest based on a floating rate index, the certificate of deposit rate, a prime or base rate (each as defined in the applicable loan agreement) or other index, which may reset daily (as most prime or base rate indices do) or offer the borrower a choice of one, two, three, six, nine or twelve month interest and rate reset periods. The purchaser of a loan may receive certain syndication or participation fees in connection with its acquisition. Other fees payable in respect of a loan, which are separate from interest payments on such loan, may include facility, commitment, amendment and prepayment fees.

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

In purchasing participations in loans, a CLO will usually have a contractual relationship only with the selling institution, and not the borrower. The CLO generally will have neither the right directly to enforce compliance by the borrower with the terms of the loan agreement, nor any rights of set-off against the borrower, nor have the right to object to certain changes to the loan agreement agreed to by the selling institution. The CLO may not directly benefit from the collateral supporting the related loan and may be subject to any rights of set-off the borrower has against the selling institution. In addition, in the event of the insolvency of the selling institution, under federal and state laws, the CLO may be treated as a general creditor of such selling institution, and may not have any exclusive or senior claim with respect to the selling institution’s interest in, or the collateral with respect to, the loan. Consequently, the CLO may be subject to the credit risk of the selling institution as well as of the borrower.

(j) *Synthetic Assets.* The Adviser, on behalf of certain Client Accounts, purchases or enters into CLO Securities synthetically with a synthetic asset counterparty through products such as credit default swaps (“CDS”), total return swaps, credit linked notes, structured notes, trust certificates and other derivative instruments (each, a “**Synthetic Asset**”). A Synthetic Asset could take many forms, including a credit derivative transaction which references a CLO debt or equity security or a credit derivative transaction which references a portfolio of corporate reference entities or a portfolio of reference obligations

consisting of loans, high yield bonds or other financial instruments (each, a “**Reference Obligation**”). Exposure to such Reference Obligations through Synthetic Assets presents risks in addition to those resulting from direct purchases of such CLO debt and CLO equity. Investors in Synthetic Assets will have a contractual relationship only with the synthetic asset counterparty, and not with the issuer(s) (the “**Reference Entity**”) of the Reference Obligations unless a credit event occurs with respect to any such Reference Obligation, physical settlement applies and the synthetic asset counterparty delivers the Reference Obligation to such investors in Synthetic Assets. Other than in the event of such delivery, the investor in Synthetic Assets generally will have no right directly to enforce compliance by the Reference Entity with the terms of any such Reference Obligation and will not have any rights of set-off against the Reference Entity. In addition, the investor generally will not have any voting or other consensual rights of ownership with respect to the Reference Obligation. Investors in Synthetic Assets also will not directly benefit from any collateral supporting the Reference Obligation and will not have the benefit of the remedies that would normally be available to a holder of such Reference Obligation.

In the event of the insolvency of the synthetic asset counterparty, the holder of the Synthetic Asset will be treated as a general creditor of such counterparty and will not have any claim of title with respect to the Reference Obligation. Consequently, the holder of the Synthetic Asset will be subject to the credit risk of the synthetic asset counterparty, as well as that of the Reference Entity. As a result, concentrations of Synthetic Assets entered into with any one synthetic asset counterparty will subject such Synthetic Assets to an additional degree of risk with respect to defaults by such synthetic asset counterparty as well as by the respective Reference Entities.

Synthetic Assets (together with synthetic CLO obligations) may comprise a significant portion of a Client Account portfolio. While returns on a Synthetic Asset may reflect those of each related Reference Obligation, as a result of the terms of the Synthetic Asset and the assumption of the credit risk of the synthetic asset counterparty, a Synthetic Asset may have a different expected return, a different (and potentially greater) probability of default and different expected loss and recovery characteristics following a default.

(k) *Optional Redemption of CLO Senior Tranches.* An optional redemption by a CLO of its notes could require the collateral or portfolio manager of the related CLO to liquidate positions more rapidly than would otherwise be desirable, which could adversely affect the realized value of the items of CLO Collateral sold (and which in turn could adversely impact the holders of any related CLO equity securities).

(l) *Insolvency Risks.* Various laws enacted for the protection of creditors may apply to the issuers of the CLO Collateral.

(m) *Price Volatility Risk.* The prices of the CLO Collateral are highly volatile. Price movements are influenced by, among other things: changing supply and demand relationships; trade, fiscal, monetary and exchange control programs and policies of governments; U.S. and foreign political events and policies; changes in national and/or international interest rates and rates of inflation; currency devaluations and revaluations, and market sentiments. None of these factors can be controlled by the Adviser and no assurance can be given that the advice of the Adviser will result in profitable investments.

### **Collateralized Debt Obligations**

The Adviser, on behalf of certain Client Accounts, invests in CDOs. CDOs may be fixed pools or may be “market value” or managed pools of collateral which entitle the holders thereof to receive payments that depend primarily on the cash flow from the pool of assets, which may include commercial loans, high yield and investment grade debt, structured

securities (for example, RMBS, CMBS and ABS) and derivative instruments relating to debt. Holders of CDOs bear various risks, including credit risk, liquidity risk, interest rate risk, market risk, operations risk, structural risk and legal risk. The pools of assets of CDOs are typically separated into tranches representing different degrees of credit quality, with lower rated tranches being subordinate to senior tranches. The senior tranches of CDOs, which represent the highest credit quality in the pool, have the greatest collateralization and pay the lowest spreads. Lower rated CDO tranches represent lower degrees of credit quality and pay higher spreads to compensate for the attendant risks. The bottom tranches specifically receive the residual interest payments (i.e., money that is left over after the higher tiers have been paid) rather than a fixed interest rate. The returns on the junior tranches of CDOs are especially sensitive to the rate of defaults in the collateral pool. In addition, the exercise of withdrawal rights, if any, by more senior CDO tranches and certain other events could result in an elimination or deferral of or reduction in the funds available to make interest or principal payments in respect of the junior tranches. The Adviser, on behalf of certain Client Accounts, may acquire mezzanine or equity tranches of CDOs which are particularly susceptible to these risks.

### **Corporate Commercial Loans**

The Adviser, on behalf of certain Client Accounts, invests in bank debt, which includes interests in loans to companies or their affiliates undertaken to finance a capital restructuring or in connection with recapitalizations, acquisitions, leveraged buyouts, refinancings or other financially leveraged transactions and may include loans which are designed to provide temporary or bridge financing to a borrower pending the sale of identified assets, the arrangement of longer-term loans or the issuance and sale of debt obligations. The Adviser, on behalf of certain Client Accounts, also invests in collateral on financial instruments, including interests on whole commercial, consumer and other loans and lease contracts. These loans, which may bear fixed or floating rates, have generally been arranged through private negotiations between a corporate borrower and one or more financial institutions (“**Lenders**”), including banks. Investment may be in the form of participations in loans (“**Participations**”) or of assignments of all or a portion of loans from third parties or special purpose vehicles that pursue direct lending opportunities (“**Assignments**”).

In certain cases, the rights and obligations acquired by a Client Account through the purchase of an Assignment may differ from, and be more limited than, those held by the assigning selling institution. Assignments are sold strictly without recourse to the selling institutions, and the selling institutions will generally make no representations or warranties about the underlying loan, the borrowers, the documentation of the loans or any collateral securing the loans.

An investing Client Account will have the right to receive payments of principal, interest and any fees to which it is entitled only from the Lender selling the Participation and only upon receipt by the Lender of the payments from the borrower. In connection with purchasing Participations, a Client Account generally will have no right to enforce compliance by the borrower with the terms of the loan agreement relating to the loan, nor any rights of set-off against the borrower, and such Client Account may not benefit directly from any collateral supporting the loan in which it has purchased the Participation. Thus, such Client Account assumes the credit risk of both the borrower and the Lender that is selling the Participation. In addition, in connection with purchasing Participations, such Client Account generally will have no role in terms of negotiating or effecting amendments, waivers and consents with respect to the loans underlying the Participations. In the event of the insolvency of the Lender, the Client Account may be treated as a general creditor of the Lender and may not benefit from any set-off between the Lender and the borrower.

Investments in Participations and Assignments involves additional risks, including the risk of nonpayment of principal and interest by the borrower, the risk that any loan collateral may become impaired and that the Client Account may obtain less than the full value for the loan interests sold because they may be illiquid. Purchasers of loans depend primarily upon the creditworthiness of the borrower for payment of interest and repayment of principal. If scheduled interest or principal payments are not made, the value of the instrument may be adversely affected.

Investments in loans through direct assignment of a financial institution's interests with respect to a loan may involve additional risks. For example, if a loan is foreclosed, the investing Client Account could become part owner of any collateral and would bear the costs and liabilities associated with owning and disposing of the collateral. In addition, it is conceivable that under emerging legal theories of lender liability, the Client Account could be held liable as a co-lender.

A loan is often administered by a bank or other financial institution that acts as agent for all holders. The agent administers the terms of the loan, as specified in the loan agreement. Unless, under the terms of the loan or other indebtedness, a Client Account has direct recourse against the borrower, such Client Account may have to rely on the agent to apply appropriate credit remedies against a borrower. If assets held by the agent for the benefit of the Client Account were determined to be subject to the claims of the agent's general creditors, such Client Account might incur certain costs and delays in realizing payment on the loan or loan participation and could suffer a loss of principal or interest.

Interests in loans are also subject to additional liquidity risks. Loans are generally subject to legal or contractual restrictions on resale. Loans are not currently listed on any securities exchange or automatic quotation system but are traded by banks and other institutional investors engaged in loan syndication. As a result, no active market may exist for some loans, and to the extent a secondary market exists for other loans, such market may be subject to irregular trading activity, wide bid/ask spreads and extended trade settlement periods. Consequently, a Client Account may have difficulty disposing of Assignments or Participations in response to a specific economic event such as deterioration in the creditworthiness of the borrower, which can result in a loss. In such market situations, it may be more difficult for a Client Account to assign a value to Assignments or Participations when valuing a Client Account's securities and calculating its assets.

### **Whole Loan Mortgages**

The Adviser, on behalf of certain Client Accounts, invests in whole loan mortgages, including subprime residential mortgage loans and non-performing and sub-performing residential mortgage loans, which are subject to increased risks. Unlike "credit enhanced" MBS, whole loan mortgages generally are not government guaranteed or privately insured, though in some cases they may benefit from private mortgage insurance. A whole loan mortgage is directly exposed to losses resulting from default and foreclosure. Therefore, the value of the underlying property, the creditworthiness and financial position of the borrower and the priority and enforceability of the lien will significantly impact the value of such mortgages. There can be no assurance as to the adequacy of the protection of the terms of the loan, including the validity or enforceability of the loan and the maintenance of the anticipated priority and perfection of the applicable security interests. Furthermore, claims may be asserted that might interfere with enforcement of a Client Account's rights. In the event of a foreclosure, a Client Account may assume direct ownership of the underlying real estate. The liquidation proceeds upon sale of such real estate may not be sufficient to recover a Client Account's cost basis in the loan, resulting in a loss to such Client Account. Any costs or delays involved in the effectuation of a foreclosure of the loan or a liquidation of the underlying property will further reduce the proceeds and thus increase the loss.



Whole loan mortgages are also subject to “special hazard” risk (property damage caused by hazards, such as earthquakes or environmental hazards, not covered by standard property insurance policies), and to bankruptcy risk (reduction in a borrower’s mortgage debt by a bankruptcy court). In addition, claims may be assessed against a Client Account on account of such Client Account’s position as mortgage holder or property owner, including responsibility for tax payments, environmental hazards and other liabilities.

Investing in performing, sub-performing and non-performing residential mortgage loans subjects a Client Account to the risks of residential real estate and residential real estate-related investments, including, among others: (i) continued declines in the value of residential real estate; (ii) risks related to general and local economic conditions; (iii) possible lack of availability of mortgage funds for borrowers to refinance or sell their homes; (iv) overbuilding; (v) the general deterioration of the borrower’s ability to keep a rehabilitated sub-performing or non-performing mortgage loan current; (vi) increases in property taxes and operating expenses; (vii) changes in zoning laws; (viii) costs resulting from the clean-up of, and liability to third parties for damages resulting from, environmental problems, such as indoor mold; (ix) casualty or condemnation losses; (x) uninsured damages from floods, earthquakes or other natural disasters; (xi) limitations on and variations in rents; (xii) fluctuations in interest rates; (xiii) fraud by borrowers, originators and/or sellers of mortgage loans; and (xiv) failure of the borrower to adequately maintain the property, particularly during times of financial difficulty. To the extent that assets underlying an investment are concentrated geographically, by property type or in certain other respects a Client Account may be subject to certain of the foregoing risks to a greater extent. Additionally, a Client Account may be required to foreclose on a mortgage loan and such actions would subject such Client Account to greater concentration of the risks of the residential real estate markets and risks related to the ownership and management of real property.

The mortgage loans and loan portfolios acquired by a Client Account will generally have been originated by third parties. While the Adviser will conduct due diligence on these loans and loan portfolios, there is a risk that the underlying mortgage loan documentation and calculations of outstanding principal, interest, late fees and other amounts will be deficient and/or inaccurate and that the Adviser will not detect such deficiencies and inaccuracies prior to acquisition. Accordingly, the mortgage loan portfolio may be compromised, reducing the value of an investing Client Account’s assets.

The borrowers under sub-performing or non-performing mortgage loans may have a variety of rights to contest the enforceability of the mortgage loans and prevent or significantly delay and increase the cost of any foreclosure action, including, without limitation, allegations regarding fraud in the inducement by the original lender or broker, failure of the lender to produce the original documentation, improper recordation of the mortgage, various theories of lender liability, and relief through the U.S. Bankruptcy Code and similar state laws providing debtor relief.

A significant concern in the purchase of loans secured by real estate is the possibility of material misrepresentation or omission on the part of the borrower or seller. The actual homeowner may not be responsible for such fraudulent residential mortgage loans. Such fraudulent mortgage loans may not be identified as such due to internal control weaknesses of a loan originator and failure of the loan originator or intermediary to be advised of such claims. Such mortgage loans could be acquired by a Client Account despite the exercise of prudent due diligence. Any inaccuracy or incompleteness on the part of the borrower or seller may adversely affect the valuation of the real estate underlying the loans or may adversely affect the ability of the Adviser to perfect or effectuate a lien on the real estate or other collateral securing the loan. Under certain circumstances, payments to a Client Account may be reclaimed if such payment or distribution is later determined to have been a fraudulent conveyance or a preferential payment.

**Consumer Receivable**

The Adviser, on behalf of certain Client Accounts, may invest in consumer receivable portfolio. The availability of consumer receivable portfolios at favourable prices and on terms acceptable to the Adviser, on behalf of certain Client Accounts, depends on a number of factors, including: the continued volume of consumer receivable portfolios available for sale, competitive factors affecting potential purchasers and sellers of consumer receivable portfolios, fluctuations in interest rates and growth in consumer spending. If a Client Account, invests in consumer receivable portfolios, the Adviser will compete with other purchasers, with third-party collection agencies and with financial services companies that manage their own portfolios. The consolidation of issuers of credit cards, which have been a principal source of consumer debt receivables, has limited the number of sellers in the market and has correspondingly given the remaining sellers increasing market strength in the price and terms of the sale of credit card accounts. The Adviser, on behalf of certain Client Accounts, may acquire receivables that fail to conform to certain terms of the purchase agreements and the Adviser, on behalf of certain Client Accounts, may seek to return these receivables to the seller for payment or replacement receivables. However, such sellers may not be able to meet their payment obligations to the Adviser, on behalf of certain Client Accounts.

**Securitization Risk**

The ability to securitize loans which a Client Account originates or invests in and/or the attractiveness thereof may lessen with changes in the capital markets, including any disruption in the proper functioning of the securitization market. A Client Account, where applicable, may have to retain a larger portion of the underlying loans and/or hold the loans to maturity.

**Equity Securities**

The Adviser, on behalf of certain Client Accounts, may invest in common and preferred stock and other equity securities, including both public and private equity securities. Equity securities generally involve a high degree of risk and will be subordinate to the debt securities and other indebtedness of the issuers of such equity securities. Prices of equity securities generally fluctuate more than prices of debt securities and are more likely to be affected by poor economic or market conditions. In some cases, the issuers of such equity securities may be highly leveraged or subject to other risks such as limited product lines, markets or financial resources. In addition, actual and perceived accounting irregularities may cause dramatic price declines in the equity securities of companies reporting such irregularities or that are rumored to be subject to accounting regularities. A Client Account may experience a substantial or complete loss on individual equity securities.

**Common Stocks**

The Adviser, on behalf of certain Client Accounts, may invest in long and short positions in common stock. Common stock prices are directly affected by issuer-specific events, as well as general market conditions. In addition, in many countries investing in common stocks is subject to greater regulatory and self-regulatory scrutiny than investing in debt or other financial instruments.

**Preferred Stock**

The Adviser, on behalf of certain Client Accounts, invests in preferred stock. Preferred stock typically 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.

### **Convertible Securities**

Convertible securities are bonds, debentures, notes, preferred stocks or other securities that may be converted into or exchanged for a specified amount of common stock of the same or a different Issuer within a particular period of time at a specified price or formula. A convertible security generally entitles its holder to receive interest or a dividend until the convertible security matures or is redeemed or converted. Convertible securities generally: (i) have higher yields than the dividends on the underlying common stocks, but lower yields than non-convertible securities of a comparable duration; (ii) are less volatile in price than the underlying common stock due to their fixed-income characteristics; (iii) have a significant option component to their value which is directly impacted by the prevailing market volatility and interest rates; and (iv) provide the potential for capital appreciation if the market price of the underlying common stock increases.

The value of a convertible security is a function of its "investment value" (determined by its yield in comparison with the yields of other securities of comparable maturity and quality that do not have a conversion feature) and its "conversion value" (the security's worth, at market value, if converted into the underlying common stock). The investment value of a convertible security is influenced by changes in interest rates (with investment value declining as interest rates increase) as well as market volatility (with the conversion value increasing as market volatility increases). The credit standing of the Issuer and other factors may also have an effect on investment value. The conversion value of a convertible security is determined by the market price of the underlying common stock. If the conversion value is low relative to the investment value, the price of the convertible security is governed principally by its investment value. To the extent that the market price of the underlying common stock approaches or exceeds the conversion price, the price of the convertible security will be increasingly influenced by its conversion value. A convertible security generally will sell at a premium over its conversion value by the extent to which investors place value on the right to acquire the underlying common stock while holding a fixed-income security. Generally, the amount of the premium decreases (as with an option) as the convertible security approaches maturity.

A convertible security may be subject to redemption at the option of the Issuer. If a convertible security held by a Client Account is called for redemption, such Client Account will be required either to permit the Issuer to redeem the security or convert it into the underlying common stock. Either of these actions could have an adverse effect on the value of the position.

### **High Yield Securities**

The Adviser, on behalf of certain Client Accounts, invests in high-yield securities. Such securities are generally not exchange-traded and, as a result, these instruments trade in the over-the-counter marketplace, which is less transparent than the exchange-traded marketplace. In addition, while typically very limited, a Client Account may invest in bonds of issuers that do not have publicly traded equity securities, making it more difficult to hedge the risks associated with such investments. High-yield securities face ongoing uncertainties

and exposure to adverse business, financial or economic conditions which could lead to the issuer's inability to meet timely interest and principal payments. The market values of certain of these lower-rated and unrated debt securities tend to reflect individual corporate developments to a greater extent than do higher-rated securities which react primarily to fluctuations in the general level of interest rates and tend to be more sensitive to economic conditions than are higher-rated securities. Companies that issue such securities are often highly leveraged and may not have available to them more traditional methods of financing. It is possible that a major economic recession could disrupt severely the market for such securities and may have an adverse impact on the value of such securities. In addition, it is possible that any such economic downturn could adversely affect the ability of the issuers of such securities to repay principal and pay interest thereon and increase the incidence of default of such securities.

### **Commercial Paper**

The Adviser, on behalf of certain Client Accounts, may invest in money market instruments, which includes commercial paper. Commercial paper is a short-term obligation with a maturity generally ranging from one to 270 days and is issued by U.S. or foreign companies or other entities in order to finance their current operations. Such investments are unsecured and usually discounted from their value at maturity. The value of commercial paper may be affected by changes in the credit rating or financial condition of the issuing entities and will tend to fall when interest rates rise and rise when interest rates fall. Asset-backed commercial paper may be issued by structured investment vehicles or other conduits that are organized to issue the commercial paper and to purchase trade receivables or other financial assets. The repayment of asset-backed commercial paper depends primarily on the cash collections received from such an issuer's underlying asset portfolio and the issuer's ability to issue new asset-backed commercial paper.

### **Distressed Securities**

The Adviser, on behalf of certain Client Accounts, invests in "distressed" securities, claims and obligations of domestic and foreign entities which are experiencing significant financial or business difficulties. Investments may include consumer and commercial loans, structured products, commercial paper, loan participations, trade claims held by trade or other creditors, stocks, partnership interests and similar financial instruments, executory contracts and options or participations therein not publicly traded. Distressed securities may result in significant returns, but also involve a substantial degree of risk. A Client Account may lose a substantial portion or all of its investment in a distressed environment or may be required to accept cash or securities with a value less than such Client Account's investment. Among the risks inherent in investments in entities experiencing significant financial or business difficulties is the fact that it frequently may be difficult to obtain information as to the true condition of such issuers. Such investments also may be adversely affected by state and federal laws relating to, among other things, fraudulent conveyances, voidable preferences, lender liability and the bankruptcy court's discretionary power to disallow, subordinate or disenfranchise particular claims. The market prices of such instruments are also subject to abrupt and erratic market movements and above average price volatility, and the spread between the bid and asked prices of such instruments may be greater than normally expected. In trading distressed securities, litigation is sometimes required. Such litigation can be time-consuming and expensive and can frequently lead to unpredicted delays or losses. Moreover, to the extent that a Client Account invests in distressed sovereign debt obligations, it will be subject to additional risks and considerations not present in private distressed securities, including the uncertainties involved in enforcing and collecting debt obligations against sovereign nations, which may be affected by world events, changes in U.S. foreign policy and other factors outside of the control of the Adviser. The market for distressed securities

and instruments is generally thinner and less active than other markets, which can adversely affect the prices at which distressed securities can be sold.

There is no assurance that third parties will correctly evaluate the value of the collateral (if any) in the loans and securities purchased by a Client Account or the prospects for a successful reorganization or similar action. In any reorganization or liquidation proceeding relating to a company in which a Client Account invests, it may lose its entire investment, may be required to accept cash or securities with a value less than its original investment and/or may be required to accept payment over an extended period of time. Under such circumstances, the returns generated from the investments of a Client Account may not compensate a Client Account adequately for the risks assumed. Troubled company and other asset-based investments require active monitoring and may, at times, require participation in business strategy or reorganization proceedings by the Adviser. To the extent that the Adviser becomes involved in such proceedings, Client Account may have a more active participation in the affairs of the issuer than that assumed generally by an investor. In addition, involvement by the Adviser in an issuer's reorganization proceedings could result in the imposition of restrictions limiting a Client Account's ability to liquidate its position in the issuer.

The Adviser, on behalf of certain Client Accounts, invests in bonds or other fixed income instruments, including, without limitation, "higher yielding" (and, therefore, higher risk) debt securities, when the Adviser believes that such investments offer opportunities for capital growth. Such investments may be below "investment grade" and face ongoing uncertainties and exposure to adverse business, financial or economic conditions which could lead to the issuer's inability to meet timely interest and principal payments. The market values of certain of these lower rated debt instruments tend to reflect individual corporate developments to a greater extent than do higher rated debt instruments, which react primarily to fluctuations in the general level of interest rates. It is likely that a major economic recession could have a materially adverse impact on the value of such investments. In addition, adverse publicity and investor perceptions, whether or not based on fundamental analysis, may also decrease the value and liquidity of investments rated below investment grade.

### **Municipal Securities**

The Adviser, on behalf of certain Client Accounts, invests in securities issued by states, municipalities, agencies of states or municipalities or similar issuers (collectively, "**Municipal Securities**"). Various factors may adversely affect the value and yield of Municipal Securities. These factors include political or legislative changes and uncertainties related to the tax status of Municipal Securities or the rights of investors in such Municipal Securities. To the extent that a Client Account invests heavily in a particular issuer's Municipal Securities, such Client Account will be more vulnerable to factors affecting that issuer. Investments in Municipal Securities, where principal and interest payments are made from the revenue of a specific project or facility, and not general tax revenues, may have increased risks. Factors affecting the project or facility, such as local business or economic conditions, could have a significant impact on the project's ability to make payments of principal and interest on Municipal Securities.

### **Municipal Revenue Bonds**

The Adviser, on behalf of certain Client Accounts, invests in taxable and tax-exempt municipal revenue bonds. Such bonds are typically issued by or on behalf of states, territories and possessions of the United States, the District of Columbia and their political subdivisions, agencies or instrumentalities to obtain funds for a wide range of public facilities including housing projects, industrial projects, hospitals, schools, mass transportation, stadiums, waterworks and sewer systems and highways. In addition, certain types of industrial

development bonds are issued by or on behalf of public authorities to obtain funds for many types of local, privately operated facilities (such debt instruments are considered municipal obligations if the interest paid on them is exempt from U.S. federal income tax). Revenue bonds are municipal bonds that finance income-producing projects and are payable only from the revenue derived from a particular project, facility or specific revenue source. Unlike general obligation bonds, revenue bonds are not payable from the general taxing power of the municipality and holders of revenue bonds typically have no claims on the issuer's other resources. The primary source of repayment and collateral for revenue bonds generally consists of the following items:

- (a) revenue from the underlying project (fees, rent, tolls, concessions, etc.);
- (b) generally, a senior lien on the underlying asset; and
- (c) an obligation for repayment by the sponsor.

Municipal revenue bonds carry a higher default risk than general obligation bonds. Not only are they not backed by the full faith and credit of a municipality, but the income from the projects funded by revenue bonds cannot be predicted with certainty. If the projects do not produce enough revenue, the bonds may default. The success of revenue bonds ultimately depends on the projects' ability to produce revenue. The bonds in which the Adviser invests on behalf of certain Client Accounts will typically already be experiencing financial or operational difficulties, which heightens the risk that sufficient revenue will not be generated. If the Adviser is unable to manage and rehabilitate the assets underlying such bonds and improve the prospect for revenue generation, the value of the investment in such bonds will likely decline.

The value of a Client Account's investments in municipal revenue bonds will be affected by local, state, regional and national factors. These may include economic or policy changes, erosion of the tax base, legislative changes (especially those regarding taxes) and the possibility of credit problems. Any such changes or events may adversely affect the value of the investments.

### **Investment in Troubled Assets**

A Client Account may originate loans secured by non-performing or other troubled real estate assets which involve a degree of financial risk and are experiencing or are expected to experience severe financial difficulties, which may never be overcome. Investments in properties operating under the close supervision of a mortgage lender are, in certain circumstances, subject to certain additional potential liabilities that may exceed the value of a Client Account's original investment therein. For example, under certain circumstances, lenders who have inappropriately exercised control of the management and policies of a debtor may have their claims subordinated or disallowed or may be found liable for damages suffered by parties as a result of such actions. In addition, under certain circumstances, payments to a Client Account and distributions to its investors may be reclaimed if any such payment or distribution is later determined to have been a fraudulent conveyance or a preferential payment or the equivalent thereof. Bankruptcy laws may delay the ability of a Client Account to realize on collateral for loan positions held by it or may adversely affect the priority of such loans through doctrines, such as equitable subordination or may result in a restructuring of the debt through principles such as "cramdown" provisions of applicable bankruptcy laws.

**Private Equity Investments**

The Adviser, on behalf of certain Client Accounts, may acquire minority equity stakes in privately held companies. The success of a Client Account's investments in minority equity stakes of privately held companies will depend in part on the performance and abilities of such companies' controlling shareholders. Because a Client Account will not control such companies, the Adviser's ability to exit from such investments may be limited. Additionally, the Adviser is likely to have a reduced ability to influence management of such companies. The Adviser may also have disagreements with controlling shareholders over the strategy and operations of such companies. As a result of the foregoing, a Client Account's equity investments in such companies may perform poorly.

**Insufficient Collateral**

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

**Secured Loans**

A Client Account may be exposed to losses resulting from default and enforcement of security. Therefore, the value of the underlying collateral, the creditworthiness of the borrower and the priority of the lien may each be of great importance. The Adviser cannot guarantee the adequacy of the protection of a Client Account's interests, including the validity or enforceability of the loan and the maintenance of the anticipated priority and perfection of the applicable security interests. Furthermore, the Adviser cannot be certain that claims may not be asserted that might interfere with enforcement of a Client Account's rights. In the event of enforcement of the security for a loan in certain jurisdictions, a Client Account may assume direct ownership of the underlying asset. The liquidation proceeds upon sale of such asset may not satisfy the entire outstanding balance of principal and interest on the relevant loan, resulting in a loss to the Client Account. Any costs or delays involved in the enforcement of the security for a loan or a liquidation of the underlying property will further reduce the proceeds and thus increase the loss.

**Global Investments**

The Adviser, on behalf of certain Client Accounts, may invest a portion of its assets outside of the United States. Investments in non-U.S. securities and other investments involve risks relating to currency exchange matters, including fluctuations in the rate of exchange between the U.S. dollar (the currency in which the books of the Client Accounts are maintained) and the various foreign currencies in which Client Accounts' investments will be denominated and costs associated with conversion of investment principal and income from one currency into another.

A Client Account may be subject to additional risks which include possible adverse political and economic developments, possible seizure or nationalization of deposits and possible adoption of governmental restrictions which might adversely affect payments to investors located outside the country of the issuer, whether from currency blockage or otherwise. Furthermore, the acquisition and sale of certain investments may be subject to brokerage



taxes and duties levied by governments, which has the effect of increasing the cost of such investment and reducing the realized gain or increasing the realized loss on such investments at the time of sale. Income received by a Client Account from sources within some countries may be reduced by withholding and other taxes imposed by such countries. Any such taxes paid by a Client Account will reduce its net income or return from such investments. While the Adviser will take these factors into consideration in making investment decisions for a Client Account, no assurance can be given that such Client Account will be able to fully avoid these risks.

### **Lower Credit Quality Loans**

There are no restrictions on the credit quality of the loans that may be held in a Client Account's portfolio. Loans arranged or purchased by the Adviser, on behalf of a Client Account may be deemed to have substantial vulnerability to default in payment of interest and/or principal. Certain of the loans which the Adviser, on behalf of a Client Account may acquire have large uncertainties or major risk exposures to adverse conditions and may be considered to be predominantly speculative. Generally, such loans offer a higher return potential than higher quality loans but involve greater volatility of price and greater risk of loss of income and principal. The market values of certain of these loans also tend to be more sensitive to changes in economic conditions than better quality loans.

### **Senior Loans Risk**

The Adviser, on behalf of certain Client Accounts, may opportunistically invest in senior secured loans. Senior secured loans are usually rated below investment grade or may also be unrated. As a result, the risks associated with senior secured loans may be considered by credit rating agencies to be similar to the risks of below investment grade fixed income instruments, although senior secured loans are senior and secured in contrast to other below investment grade fixed income instruments, which are often subordinated or unsecured. Investment in senior secured loans rated below investment grade is considered speculative because of the credit risk of their issuers. Such companies are more likely than investment grade issuers to default on their payments of interest and principal owed to a Client Account, and such defaults could have a material adverse effect on such Client Account's performance. An economic downturn would generally lead to a higher non-payment rate, and a senior secured loan may lose significant market value before a default occurs. Moreover, any specific collateral used to secure a senior secured loan may decline in value or become illiquid, which would adversely affect the senior secured loan's value. Senior secured loans are subject to a number of risks including liquidity risk and the risk of investing in below investment grade fixed income instruments.

There may be less readily available and reliable information about most senior secured loans than is the case for many other types of securities, including securities issued in transactions registered under the Securities Act or registered under the Exchange Act. As a result, the Adviser will rely primarily on its own evaluation of a borrower's credit quality rather than on any available independent sources. Therefore, the Client Accounts will be particularly dependent on the analytical abilities of the Adviser.

In general, the secondary trading market for senior secured loans is not well developed. No active trading market may exist for certain senior secured loans, which may make it difficult to value them. Illiquidity and adverse market conditions may mean that the Adviser, on behalf of a Client Account, may not be able to sell senior secured loans quickly or at a fair price. To the extent that a secondary market does exist for certain senior secured loans, the market for them may be subject to irregular trading activity, wide bid/ask spreads and extended trade settlement periods.

**Subordinated Loans or Securities**

The Adviser, on behalf of certain Client Accounts, may opportunistically invest in subordinated loans or securities or interests in pools of securities that are subordinated or may be subordinated in right of payment and ranked junior to other securities issued by, or loans made to obligors. If an obligor experiences financial difficulty, holders of its more senior securities will be entitled to payments in priority to Client Accounts.

In addition, many of the obligors are highly leveraged and many of the investments will be in securities that are unrated or rated below investment grade. Such investments are subject to additional risks, including an increased risk of default during periods of economic downturn, the possibility that the obligor may not be able to meet its debt payments and limited secondary market trading, among other risks.

**Bank Loans**

The Adviser, on behalf of certain Client Accounts, may, directly or through affiliated entities, opportunistically invest in loans and participations. These obligations are subject to unique risks, including: (i) the possible invalidation of an investment transaction as a fraudulent conveyance under relevant creditors' rights laws; (ii) so-called lender-liability claims by the issuer of the obligations; (iii) environmental liabilities that may arise with respect to collateral securing the obligations; and (iv) limitations on the ability of the Adviser, on behalf of a Client Account, to directly enforce its rights with respect to participations. In analyzing each bank loan or participation, the Adviser compares the relative significance of the risks against the expected benefits of the investment. Successful claims by third parties arising from these and other risks will be borne by Client Accounts.

**DIP Loans**

The Adviser, on behalf of certain Client Accounts, may, directly or through affiliated entities, opportunistically invest in debtor-in-possession ("**DIP**") loans. DIP loans involve a fundamental credit risk based on the borrower's ability to make principal and interest payments and the inherent risks of the bankruptcy process. DIP loans are subject to a court approval process in which parties-in-interest may be heard but there can be no assurance that Adviser would be successful in obtaining favorable results. If the calculations of the Adviser as to the outcome or timing of reorganization are inaccurate, a company that has filed for bankruptcy may not be able to make payments on a DIP loan on time or at all. In addition, DIP loans may be privately negotiated transactions, each of which has individualized terms. These positions may be illiquid and difficult to value. DIP loans may be subject to price volatility due to various factors including, but not limited to, changes in interest rates, market perception of the creditworthiness of the borrower and general market liquidity.

**Liquidity in the Market for Bank Loans**

Purchasers of bank loans are predominantly commercial banks, investment funds and investment banks. As secondary market trading volumes increase, arrangers and obligors of new bank loans are frequently adopting standardized documentation to facilitate trading that should improve market liquidity. There can be no assurance, however, that future levels of supply and demand in loan trading will provide an adequate degree of liquidity or that the current level of liquidity will continue. No assurance can be given that a Client Account will be able to sell a loan whose obligor has deteriorated in credit quality.



**Borrower Fraud**

Of paramount concern in investing in loans and other debt instruments is the possibility of fraud, material misrepresentation or omission on the part of the borrower or the lack of adequate documentation or any documentation regarding such loans and debt obligations. Such occurrences may adversely affect the valuation of the collateral underlying the loans or may adversely affect the ability of the Adviser, on behalf of certain Client Accounts, to perfect or effectuate a lien on the collateral securing the loan. The Adviser will rely upon the accuracy and completeness of representations made by borrowers and lenders to the extent reasonable but cannot guarantee such accuracy or completeness or the adequacy or existence of required documentation. Under certain circumstances, payments to Client Accounts may be reclaimed if any such payment or distribution is later determined to have been a fraudulent conveyance or a preferential payment.

**Sovereign Risk**

Government interference with international transactions in its currency or the debt obligations of itself or its nationals through various means, including, without limitation, regulation of the local exchange market, restrictions on foreign investment by residents, limits on flows of investment funds from abroad and debt moratoria, may expose Client Accounts, to unanticipated losses.

There are increasing concerns regarding the ability of multiple sovereign entities to continue to meet their debt obligations. Many economies are facing acute fiscal pressures as they struggle to balance budgetary austerity with stagnant growth. Many observers predict that a depressed economic environment will cause budget deficits in these economies to expand in the short term and further increase the perceived risk of a default, thereby rendering access to capital markets even more expensive and compounding the debt problem.

**Sovereign Debt**

The Adviser, on behalf of certain Client Accounts, may invest in financial instruments issued by a government, its agencies, instrumentalities or its central bank ("**Sovereign Debt**"). Sovereign Debt may include securities that the Adviser believes are likely to be included in restructurings of the external debt obligations of the issuer in question. The ability of an issuer to make payments on Sovereign Debt, the market value of such debt and the inclusion of Sovereign Debt in future restructurings may be affected by a number of other factors, including such issuer's (i) balance of trade and access to international financing, (ii) cost of servicing such obligations, which may be affected by changes in international interest rates, and (iii) level of international currency reserves, which may affect the amount of foreign exchange available for external debt payments. Significant ongoing uncertainties and exposure to adverse conditions may undermine the issuer's ability to make timely payment of interest and principal, and issuers may default on their Sovereign Debt.

**Debt Securities**

The Adviser, on behalf of certain Client Accounts, may invest in unrated or low-grade debt securities which are subject to greater risk of loss of principal and interest than higher-rated debt securities. The Adviser, on behalf of certain Client Accounts, invests in debt securities which rank junior to other outstanding securities and obligations of the issuer, all or a significant portion of which may be secured on substantially all of that issuer's assets. The Adviser, on behalf of certain Client Accounts, invests in debt securities which are not protected by financial covenants or limitations on additional indebtedness. In addition, evaluating credit risk for foreign debt securities involves greater uncertainty because credit

rating agencies throughout the world have different standards, making comparison across countries difficult.

The risks of debt investments include, but are not limited to: (i) limited liquidity and secondary market support, (ii) the possibility that earnings of the obligor may be insufficient to meet its debt service, (iii) the declining creditworthiness and potential for insolvency of the borrower during periods of economic downturn, (iv) spread compression over the reference interest rate available for reinvestment during any period in which prepayments are received and (v) if the investment is subordinated, subordination to the prior claims of other loans or senior lenders. Debt investments are generally subject to market value volatility that may not be apparent from historical volatility studies and that could be significant at times. An economic downturn could severely disrupt the market for corporate debt and adversely affect the value of outstanding fixed income holdings and the ability of the borrowers thereunder to repay principal and interest. Moreover, defaults may prove to be greater than indicated by historical data and the timing of defaults may vary significantly from historical observations.

Debt instruments may become non-performing for a variety of reasons. Non-performing instruments may require substantial workout negotiations or restructuring that may entail, among other things, a substantial reduction in the interest rate and/or a substantial write-down of the principal. A Client Account may incur additional expenses to the extent it is required to seek recovery upon a default or to participate in the restructuring of a debt instrument. Although a Client Account may have voting rights with respect to an individual holding, there can be no certainty that such Client Account will be able to exercise votes in respect of a sufficient percentage of voting rights with respect to such holding to determine the outcome of such vote. The Adviser, on behalf of certain Client Accounts, may attempt to enhance returns on debt securities by making hybrid debt and equity investments, which may include “equity kickers” such as warrants.

### **Directly Negotiated Investments**

This strategy contemplates the purchasing and selling, through private placements or public offerings, of securities offered by companies that are publicly traded. Directly negotiated investments generally include PIPEs as well as the following investments issued or offered by public companies: (i) convertible debt securities (senior notes and subordinated notes) and preferred stock, with and without embedded put (conversion price reset(s) and/or cash put) and call (discount and premium) features; (ii) common stock issued at a discount or implied discount; (iii) warrants, purchased alone or issued in connection with any of the above, which warrants may or may not be publicly traded and in which the underlying security may be restricted or unrestricted; (iv) registered direct offerings (which may be a negotiated sale by an issuer to an investor pursuant to an effective shelf registration statement); (v) confidentially marketed public offerings (or “**CMPOs**”) and (vi) other structured investments in public companies. While a Client Account may own interests in PIPEs and other directly negotiated investments, the Adviser expects such Client Account to do so where the underlying asset class is structured credit.

### **Risks Associated with the Lending SPVs**

The Adviser, on behalf of certain Client Accounts, invests, directly and indirectly, in special purpose vehicles (the “**Lending SPVs**”) that pursue direct lending opportunities. Such Lending SPVs operate independently and are not expected to make distributions on a regular basis. Proceeds realized from such lending activities may not be readily deployed into new lending opportunities and, accordingly, such investment proceeds may have a “drag” on the ultimate investment returns.

In connection with direct lending and loan origination activities, the Lending SPVs may be exposed to losses resulting from default and enforcement of security. Therefore, the value of the underlying collateral, the creditworthiness of the borrower and the priority of the lien may each be of great importance. The Lending SPVs cannot guarantee the adequacy of the protection of its interests, including the validity or enforceability of the loan and the maintenance of the anticipated priority and perfection of the applicable security interests. Furthermore, the Lending SPVs cannot be certain that claims may not be asserted that might interfere with enforcement of its rights. In the event of enforcement of the security for a loan in certain jurisdictions, a Lending SPV may assume direct ownership of the underlying asset. The liquidation proceeds upon sale of such asset may not satisfy the entire outstanding balance of principal and interest on the relevant loan, resulting in a loss to such Lending SPVs. Any costs or delays involved in the enforcement of the security for a loan or a liquidation of the underlying property will further reduce the proceeds and thus increase the loss.

### **Lender Liability Considerations and Equitable Subordination**

A number of judicial decisions in the United States have upheld the right of borrowers to sue lending institutions on the basis of various evolving legal theories (collectively termed “**lender liability**”). Generally, lender liability is founded upon the premise that an institutional lender has violated a duty (whether implied or contractual) of good faith and fair dealing owed to the borrower or has assumed a degree of control over the borrower resulting in a creation of a fiduciary duty owed to the borrower or its other creditors or shareholders. While believed to be unlikely, because of the nature of certain of investments, a Client Account could be subject to allegations of lender liability.

In addition, under common law principles that in some cases form the basis for lender liability claims, if a lending institution (a) intentionally takes an action that results in the undercapitalization of a borrower to the detriment of other creditors of such borrower, (b) engages in other inequitable conduct to the detriment of such other creditors, (c) engages in fraud with respect to, or makes misrepresentations to, such other creditors or (d) uses its influence as a stockholder to dominate or control a borrower to the detriment of other creditors of such borrower, a court may elect to subordinate the claim of the offending lending institution to the claims of the disadvantaged creditor or creditors, a remedy called “equitable subordination.” Because of the nature of certain investments, a Client Account could be subject to claims from creditors or shareholders of an obligor that the Client Account’s investments issued by such obligor that are held by the Client Account should be equitably subordinated. A significant number of a Client Account’s investments may involve investments in which the Client Account would not be the lead creditor. Accordingly, it is possible that lender liability or equitable subordination claims affecting a Client Account’s investments could arise without the direct involvement of such Client Account.

### **Risks Associated with Investments in De Novo Companies**

The Adviser, on behalf of certain Client Accounts, makes debt or equity investments (or hybrid debt and equity investments that may include “equity kickers” such as warrants) in newly formed companies pursuing lending opportunities. Such companies may be challenged by factors including rapidly changing market conditions and/or participants and competing borrowers. Moreover, the management of these businesses may be inexperienced, and newly formed companies may face legal, regulatory and/or industry-specific impediments to growth. For these reasons, the risks associated with the Adviser’s investment strategies are heightened with respect to an investment in a new venture.

**Risks Associated with Joint Venture Investments**

The Adviser, on behalf of certain Client Accounts, pursues direct lending opportunities, including joint ventures with third parties. Such investments may involve additional risks, including the possibility that a third-party co-venturer may have financial difficulties, resulting in a negative impact on such investment, may have economic or business interests or goals which are inconsistent with those of a Client Account, or may be in a position to take (or block) action in a manner contrary to a Client Account's investment objectives. In addition, a Client Account may, in certain circumstances, be liable for the actions of its third-party co-venturers. In those circumstances where such third parties involve a management group, such third parties may receive compensation arrangements relating to such investments, including incentive compensation arrangements.

**Risks Associated with Bankruptcy Cases**

Many of the events within a bankruptcy case are adversarial and often beyond the control of the creditors. While creditors generally are afforded an opportunity to object to significant actions, there can be no assurance that a bankruptcy court would not approve actions which may be contrary to the interests of a Client Account. Furthermore, there are instances where creditors and equity holders lose their ranking and priority as such when they take over management and functional operating control of a debtor. In those cases where a Client Account, by virtue of such action, is found to exercise "domination and control" of a debtor, the Client Account may lose its priority if the debtor can demonstrate that its business was adversely impacted or other creditors and equity holders were harmed by the Client Account.

Generally, the duration of a bankruptcy case can only be roughly estimated. Unless a Client Account's claim in such case is secured by assets having a value in excess of such claim, no interest will be permitted to accrue and, therefore, the Client Account's return on investment can be adversely affected by the passage of time during which the plan of reorganization of the debtor is being negotiated, approved by the creditors, and confirmed by the bankruptcy court. The risk of delay is particularly acute when a creditor holds unsecured debt or when the collateral value underlying secured debt does not equal the amount of the secured claim. Under most circumstances, unless the debtor is proved to be solvent, no interest or fees are permitted to accrue after the commencement of the debtor's case, as a matter of U.S. bankruptcy law. Such investments can result in a total loss of principal. It should also be noted that reorganizations outside of bankruptcy are also subject to unpredictable and potentially lengthy delays.

Investment in the debt of financially distressed companies domiciled outside the U.S. involves additional risks. Bankruptcy law and process may differ substantially from that in the U.S., resulting in greater uncertainty as to the rights of creditors, the enforceability of such rights, reorganization timing and the classification, seniority and treatment of claims. In certain developing countries, although bankruptcy laws have been enacted, the process for reorganization remains highly uncertain.

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

The administrative costs in connection with a bankruptcy proceeding are frequently high and will be paid out of the debtor's estate prior to any return to creditors (other than out of assets

or proceeds that are subject to valid and enforceable liens and other security interests) and equity holders. In addition, certain claims that have priority by law over the claims of certain creditors (for example, claims for taxes) may be quite high.

The Adviser, or its affiliates, on behalf of a Client Account, may elect to serve on creditors' committees or other groups to ensure preservation or enhancement of the Client Account's position as a creditor. A member of any such committee or group may owe certain obligations generally to all parties similarly situated that the committee represents. If the Adviser (or its affiliate, as applicable) concludes that its obligations owed to the other parties as a committee or group member conflict with its duties owed to the Client Account, it will resign from that committee or group or take other appropriate steps to adequately address the conflict, and the Client Account may not realize the benefits, if any, of participation on the committee or group. In addition, and also as discussed above, if the Client Account is represented on a committee or group, it may be restricted or prohibited under applicable law from disposing of its investments in such company while it continues to be represented on such committee or group.

A Client Account may purchase creditor claims subsequent to the commencement of a bankruptcy case. Under judicial decisions, it is possible that such purchases could be disallowed by a bankruptcy court if such court were to determine that the Client Account has taken unfair advantage of an unsophisticated seller, which may result in the rescission of the transaction (presumably at the original purchase price) or forfeiture by the Client Account.

### **Potential Involvement in Litigation**

As a result of the Adviser's activities generally, including investments in distressed investments and the possibility that the Adviser may participate in restructuring activities, it is possible that a Client Account may become involved in litigation, including litigation respecting creditor disputes and similar issues among classes of claimants. Litigation entails expense and the possibility of counterclaims against the Client Account including the Adviser and its affiliates and ultimately judgments may be rendered against a Client Account for which such Client Account does not carry insurance.

### **Trade and Other General Unsecured Claims**

The Adviser, on behalf of certain Client Accounts, acquires interests in claims of trade creditors and other general unsecured claim holders of a debtor ("**trade claims**"). Trade claims generally include, but are not limited to, claims of suppliers for goods delivered and not paid, claims for unpaid services rendered, claims for contract rejections and claims related to litigation. Trade claims are typically unsecured and may, in unusual circumstances, be subordinated to other unsecured obligations of the debtor. The repayment of trade claims is subject to significant uncertainties, including potential set-off by the debtor as well as the other uncertainties with respect to other distressed securities. A trade claim may be transferred or assigned before or after a petition in bankruptcy is filed, including after a proof of claim has been filed. Investments in trade claims and high risk receivables may also entail special risks including, but not limited to, fraud on the part of the assignor of the trade claim as well as logistical and mechanical issues which may affect the ability of a Client Account or its agent to collect the claim in whole or in part.

### **Non-U.S. Securities**

Investing in securities of non-U.S. governments and companies that are generally denominated in non-U.S. currencies and utilization of options on non-U.S. securities involves certain considerations comprising both risks and opportunities not typically associated with investing in securities of the United States Government or United States companies. These



considerations include (i) controls on foreign investment; (ii) limitations on repatriation of invested capital, the ability to exchange local currencies for U.S. dollars, and possible adoption of governmental restrictions which may adversely affect the payment of principal and interest to investors located outside the country of the issuer; (iii) a higher degree of governmental involvement in and control over the national or local economy; (iv) differences in auditing and financial reporting standards, which may result in the unavailability of material information about economies, assets and issuers; (v) less extensive regulatory oversight of securities and other markets; (vi) less liquidity in securities and other markets; (vii) longer settlement periods for transactions; (viii) less stringent laws regarding the fiduciary duties of officers and directors and protection of investors; (ix) difficulty in enforcing contractual obligations and legal rights, which may be costly and slow; (x) the risk of nationalization or expropriation of assets or confiscatory taxation; (xi) social, economic and political commodities prices; and (xii) potentially higher rates of inflations or deflation. International conventions and treaties may also impact certain assets of the Adviser, on behalf of certain Client Accounts. Certain non-U.S assets and/or income received a Client Account from sources within some countries may be reduced by withholding and other taxes imposed by such countries.

### **Hedging Transactions**

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

The success of the Adviser's hedging strategy will depend, in part, upon the Adviser's ability to correctly assess the degree of correlation between the performance of the instruments used in the hedging strategy and the performance of the portfolio investments being hedged. Since the characteristics of many assets change as markets change or time passes, the success of the Adviser's hedging strategy will also be subject to the Adviser's ability to continually recalculate, readjust and execute hedges in an efficient and timely manner. While the Adviser, on behalf of certain Client Accounts, may enter into hedging transactions to seek to reduce risk, such transactions may result in a poorer overall performance for a Client Account than if it had not engaged in such hedging transactions. For a variety of reasons, the Adviser may not seek to establish a perfect correlation between the hedging instruments utilized and the portfolio holdings being hedged. Such an imperfect correlation may prevent a Client Account from achieving the intended hedge or expose a Client Account to risk of loss. The Adviser may not hedge against a particular risk because it does not regard the probability of the risk occurring to be sufficiently high as to justify the cost of the hedge, or because it does not foresee the occurrence of the risk. The successful utilization of hedging and risk management transactions requires skills complementary to those needed in the selection of a Client Account's portfolio holdings.

### **Currency Exposure Risk**

Investments in foreign currency forwards, futures and options, as well as securities are subject to the risk that the value of a particular currency will change in relation to one or more other currencies. Among the factors that may affect currency values are trade balances, the level of short-term interest rates, differences in relative values of similar assets in different

currencies, long-term opportunities for investment, capital appreciation and political developments. The Adviser may try to hedge these risks, but there can be no assurance that it will implement a hedging strategy, or if it implements one, that it will be effective.

### **Index Risk**

The Adviser, on behalf of certain Client Accounts, invests in securities the value of which may be affected by 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.

To the extent that a Client Account's portfolios is invested in derivatives of various mortgage-backed securities, the prepayment risks, credit risks, interest rate risks and hedging risks associated with such securities may be substantially magnified.

### **Foreign Exchange Markets**

By trading in foreign exchange and investing in derivative instruments relating to international securities and such securities themselves, a Client Account will have exposure to fluctuations in currency exchange rates. It may, in part, seek to offset the risks associated with such exposure or to increase returns through foreign exchange transactions. Such transactions involve a significant degree of risk and the markets in which foreign exchange transactions are effected are volatile, specialized and technical. Significant changes, including changes in liquidity and prices, can occur in such markets within very short periods of time, often within minutes. Foreign exchange trading risks include, but are not limited to, exchange rate risk, maturity gaps, interest rate risk and potential interference by foreign governments through regulation of local exchange markets, foreign investment or particular transactions in foreign currency. The foreign exchange transactions can result in a Client Account's returns being substantially better or worse than what returns would have been had the transactions not been entered into.

### **Systemic Risk – OTC and Derivative Counterparty Risk**

World events and/or the activities of one or more large participants in the financial markets and/or other events or activities of others could result in a temporary systemic breakdown in the normal operation of financial markets. Such events could result in a Client Account losing substantial value caused predominantly by liquidity and counterparty issues, which could result in a Client Account incurring substantial losses.

There is the possibility that the institutions, including prime brokers, other brokerage firms and banks, with whom the Adviser does business, or with whom securities may be entrusted for custodial purposes, will encounter financial difficulties that may impair the operational capabilities or the capital position of such brokerage firms or banks and that could adversely affect a Client Account. Brokers may trade with an exchange as a principal on behalf of a Client Account, in a "debtor-creditor" relationship, unlike other clearing broker relationships where the broker is merely a facilitator of the transaction. Such broker could, therefore, have title to all of the assets of a Client Account or certain assets of a Client Account (for example, the transactions which the broker has entered into on behalf of a Client Account as principal as well as the margin payments which a Client Account provides). In the event of such broker's insolvency, the transactions which the broker has entered into as principal could default and certain of the Client Account's assets could become part of the insolvent broker's estate, to the detriment of the Client Account. In this regard, a Client Account's assets may

be held in “street name” such that a default by the broker may cause the Client Account’s rights to be limited to those of an unsecured creditor.

### **Derivative and Option Investments**

The Adviser, on behalf of certain Client Accounts, buys or sells (writes) both call options and put options, and when it writes options, it may do so on a “covered” or an “uncovered” basis. A call option is “covered” when the writer owns securities of the same class and amount as those to which the call option applies. A put option is covered when the writer has an open short position in securities of the relevant class and amount. A Client Account’s option transactions may be part of a hedging strategy (i.e., offsetting the risk involved in another securities position) or a form of leverage, in which the Client Account has the right to benefit from price movements in a large number of securities with a small commitment of capital. These activities involve risks that can be substantial, depending on the circumstances.

In general, without taking into account other positions or transactions a Client Account may enter into, the principal risks involved in options trading can be described as follows: when a Client Account buys an option, a decrease (or inadequate increase) in the price of the underlying security in the case of a call, or an increase (or inadequate decrease) in the price of the underlying security in the case of a put, could result in a total loss of the investment in the option (including commissions). A Client Account could mitigate those losses by selling short, or buying puts on, the securities for which it holds call options, or by taking a long position (e.g., by buying the securities or buying calls on them) in securities for which it holds put options.

When the Adviser, on behalf of a Client Account, sells (writes) an option, the risk can be substantially greater than when it buys an option. The seller of an uncovered call option bears the risk of an increase in the market price of the underlying security above the exercise price. The risk is theoretically unlimited unless the option is “covered.” If it is covered, the Client Account would forego the opportunity for profit on the underlying security should the market price of the security rise above the exercise price. If the price of the underlying security were to drop below the exercise price, the premium received on the option (after transaction costs) would provide profit that would reduce or offset any loss suffered as a result of owning the security.

Swaps and certain options and other customized instruments are subject to the risk of non-performance by the swap counterparty, including risks relating to the creditworthiness of the swap counterparty, market risk, liquidity risk and operations risk.

### **Futures Contracts**

The Adviser, on behalf of certain Client Accounts, trades in futures contracts (and options on futures). Futures positions may become illiquid. For example, most commodity exchanges limit fluctuations in certain futures contract prices during a single day by regulations referred to as “daily price fluctuation limits” or “daily limits.” Under such daily limits, during a single trading day no trades may be executed at prices beyond the daily limits. Once the price of a contract for a particular future has increased or decreased by an amount equal to the daily limit, positions in the future can neither be taken nor liquidated unless traders are willing to effect trades at or within the limit. Futures contract prices on various commodities or financial instruments occasionally have moved the daily limit for several consecutive days with little or no trading. Similar occurrences could prevent a Client Account from promptly liquidating unfavorable positions and subject such Client Account to substantial losses. In addition, the Adviser, on behalf of a Client Account, may not be able to execute futures contract trades at favorable prices if trading volume in such contracts is low. It is also

possible that an exchange or a regulator (such as the SEC or the U.S. Commodity Futures Trading Commission (“CFTC”)) may suspend trading in a particular contract, order immediate liquidation and settlement of a particular contract or order that trading in a particular contract be conducted for liquidation only. In addition, the CFTC and various exchanges impose speculative position limits on the number of positions that may be held in particular commodities. Trading in futures contracts and options are highly specialized activities that may entail greater than ordinary investment or trading risks.

### **Margin on Futures and Leverage**

In futures markets, margin deposits are typically low relative to the nominal value of the futures contracts purchased or sold. In the forward, currency and certain other derivative markets, margin deposits may be even lower or may not be required at all. Such low margin deposits are indicative of the fact that any futures contract trading typically is accompanied by a high degree of leverage. Low margin deposits mean that a relatively small price movement in a futures contract may result in immediate and substantial losses to the investor. For example, if at the time of purchase 5% of the price of a futures contract is deposited as margin, a 5% decrease in the price of the futures contract would, if the contract is then closed out, result in a total loss of the margin deposit before any deduction for the brokerage commission. Thus, like other leveraged investments, any purchase or sale of a futures contract may result in losses in excess of the amount invested.

### **Swap Transactions**

Depending on their structure, swap agreements may increase or decrease a Client Account’s exposure to equity securities, long-term or short-term interest rates, non-U.S. currency values, corporate borrowing rates or other reference assets. Depending on how they are used, swap agreements may increase or decrease the overall volatility of a Client Account’s portfolio. The most significant factors in the performance of swap agreements is the change in the individual equity values, the specific interest rate, the currency value and other reference assets that determine the amounts of payments due. If a swap agreement calls for payments by a Client Account, such Client Account must be prepared to make such payments when due. In addition, if a counterparty’s creditworthiness declines, the value of swap agreements with such counterparty can be expected to decline, potentially resulting in losses by the Client Account.

Swap transactions are not traded on exchanges and are not subject to the same type of government regulation as exchange markets. As a result, many of the protections afforded to participants on organized exchanges and in a regulated environment are not available in connection with these transactions. The swap markets are “principals’ markets,” in which performance with respect to a swap contract is the responsibility only of the counterparty to the contract, and not of any exchange or clearinghouse. As a result, a Client Account is subject to the risk of the inability or refusal to perform with respect to swap contracts on the part of the counterparties with which the Client Account trades. There are no limitations on daily price movements in swap transactions. Speculative position limits are not applicable to swap transactions, although a Client Account’s swap counterparties may limit the size or duration of positions available to the Client Account as a consequence of credit considerations. Participants in the swap markets are not required to make continuous markets in the swap contracts they trade. Participants could refuse to quote prices for swap contracts or quote prices with an unusually widespread between the price at which they are prepared to buy and the price at which they are prepared to sell. If an event of default or an additional termination event were to occur with respect to a Client Account under an ISDA master agreement governing the Client Account’s swap transactions, the relevant swap counterparty, other swap counterparties and/or prime brokers may terminate all transactions with the Client Account at significant losses to the Client Account.

Trading in swaps and other derivative instruments can permit a high degree of synthetic leverage. Accordingly, the leverage offered by trading in derivative instruments may magnify the gains and losses experienced by a Client Account and could cause the Client Account's net asset value to be subject to wider fluctuations than would be the case if derivative instruments that provide leverage were not used. Thus, like other leveraged investments, a derivatives trade may result in losses in excess of the amount invested. Any increase in the amount of leverage applied in trading will increase the risk of loss by the amount of additional leverage applied.

### **Enhanced Regulation of Swaps**

Subject to exceptions for certain commercial end-users engaged in hedging activity, the U.S. Wall Street Transparency and Accountability Act of 2010 (the "WSTAA"), as implemented through regulations adopted by the CFTC, (i) requires certain liquid, standardized swaps to be cleared through a derivatives clearing organization (a "DCO") and, if made available for trading through a designated contract market or swap execution facility to be so traded, (ii) requires margin to be exchanged for all uncleared, over-the-counter swap transactions, (iii) subjects traders with substantial positions in swaps over certain thresholds to registration and regulation requirements as a "major swap participant" or "swap dealer" (depending on the type and amount of trading activity at issue) and (iv) imposes position limits on swaps that are "economically equivalent" to any of the 25 physical commodity futures contracts that are subject to federal speculative position limits (i.e., that have identical material contractual specifications, terms and conditions as any of those futures contracts). Due to the requirements imposed by the WSTAA, Client Accounts may experience increased transaction costs to pay for the clearing, execution and segregation obligations. In addition, margin requirements may increase due to new margin requirements imposed by DCOs with input from the CFTC, which may limit Client Accounts' ability to engage in leverage and limit their returns. The application of position limits to swap contracts may also limit Client Accounts' ability to concentrate in any particular contract or exposure to an underlying commodity and may negatively impact their ability to take advantage of current market trends or conditions. Any tightening in the market for swaps may significantly impact the investment returns of Client Accounts.

### **Credit Default Swaps**

The Adviser, on behalf of certain Client Accounts, invests in CDSs. A CDS is a contract between two parties which transfers the credit risk associated with a particular debt instrument as it relates to the issuer's failure to pay principal or interest on time in respect of such referenced debt instrument or files for bankruptcy. Upon an event of default, the swap may be terminated in one of two ways: (i) by the purchaser of credit protection delivering the referenced instrument to the swap counterparty and receiving a payment of par value, or (ii) by the parties pairing off payments, with the purchaser of the protection receiving a payment equal to the par value of the reference security less the price at which the reference security trades subsequent to default. The first way is the more common form of CDS termination.

In the manner described above, CDSs can be used to hedge a portion of the default risk on a single bond or a portfolio of bonds and loans. CDSs can be used to implement the Adviser's view that a particular credit, or group of credits, will experience credit improvement. In the case of expected credit improvement, a Client Account may sell credit default protection in which it receives a premium to take on the risk. In such an instance, the obligation of the Client Account to make payments upon the occurrence of a credit event creates leveraged exposure to the credit risk of the referenced entity. The Client Account may also "purchase" credit default protection irrespective of whether the Client Account owns the referenced instrument if, in the judgment of the Adviser, there is a high likelihood of credit deterioration.



Swap transactions dependent upon credit events are priced incorporating many variables including the pricing and volatility of the common stock, potential loss upon default and the shape of the U.S. Treasury Yield curve, among other factors. As such, there are many factors upon which market participants may have divergent views. The Adviser may also enter into CDS transactions, even if the credit outlook is positive, if it believes that participants in the marketplace have incorrectly valued the components which determine the value of a swap.

If a Client Account and its affiliates enter into too large of credit default swaps, it may be required to register as a swaps dealer or securities-based swaps dealer and become subject to significant compliance costs.

### **Enhanced Regulation of Short Sales and Credit Default Swaps**

Short sales and credit default swaps are subject to the provisions of the EU Regulation on Short Selling and certain aspects of Credit Default Swaps (the “**Short Selling Regulation**”). The Short Selling Regulation imposes restrictions and disclosure requirements for persons taking short positions in EU shares and sovereign bonds, and prohibits entering into uncovered credit default swaps in relation to EU sovereign debt (i.e., where the investor does not have an exposure that it is seeking to hedge either to the sovereign debt itself or to assets or liabilities whose value is correlated to the sovereign debt). In addition, the Short Selling Regulation permits the competent authorities of EU member states to prohibit or restrict short sales, limit sovereign credit default swaps and impose emergency disclosure requirements, among other things, during times of stressed markets. Competent authorities may also restrict short sales of individual financial instruments which have suffered a significant fall in price in a single day.

The provisions of the Short Selling Regulation may hinder a Client Account’s investment program by preventing it from taking positions that the Adviser considers favorable. They may also result in overvaluations of certain financial instruments due to restrictions on market efficiency. In addition, the emergency powers granted to competent authorities during times of stressed markets and with respect to individual financial instruments may adversely affect a Client Account by preventing it from taking hedging positions or other positions that the Adviser considers to be in its best interests. The imposition of emergency measures under the Short Selling Regulation could, therefore, result in substantial losses to a Client Account.

### **Illiquid Investments**

The Adviser, on behalf of certain Client Accounts, invests in restricted, as well as thinly-traded, instruments and securities (including privately placed securities and instruments). The Adviser, on behalf of certain Client Accounts, also makes investments in privately held companies or special purpose entities, provided that it is allowed under the applicable regulation. There may be no trading market for these securities and instruments, and the Adviser might only be able to liquidate these positions, if at all, at disadvantageous prices. As a result, a Client Account may be required to hold such securities despite adverse price movements. In addition, if the Adviser makes a short sale of an illiquid security or instrument, it may have difficulty in covering the short sale, resulting in a potentially unlimited loss on that position.

### **Equity-Related Instruments in General**

The Adviser uses equity-related instruments in its investment program. Certain options and other equity-related instruments may be subject to various types of risks, including market risk, liquidity risk, counterparty credit risk, legal risk and operations risk. In addition, equity-related instruments can involve significant economic leverage and may, in some cases, involve significant risks of loss.



**PACE Financing**

The Adviser, on behalf of certain Client Accounts, invests in securities issued by a private company with a business model that depends upon legislative approval of a developing form of municipal financing (i.e., Property Assessed Clean Energy (“**PACE**”) financing). PACE financing may be unable to expand into other markets unless such a form of municipal financing is adopted in such markets, and there can be no guarantee that any market will continue to support the program. Even if other states adopt this form of municipal financing, there can be no guarantee that the program will have success. PACE financing primes the first-lien mortgage. The Federal Housing Finance Agency (“**FHFA**”) as conservator of Fannie Mae and Freddie Mac owns or insures many first-lien mortgages. To date, the FHFA has issued a directive stating that they will not purchase mortgages that have a PACE assessment on the underlying property. If FHFA took a more aggressive stance against PACE programs and its supporting legislation, it could negatively impact the private company’s business model.

PACE bonds are originated on the private company’s balance sheet using leverage, with the intention of selling risk through securitization. If there is a disruption in the securitization market or on its leverage, the private company will be exposed to the asset risk and could have cash flow constraints on its balance sheet. PACE financing is dependent upon a contract with participating Joint Power Authorities and Cities. It is possible that the municipalities will not renew the existing contracts or enter into new contracts. The Adviser, on behalf of certain Client Accounts, may also invest directly in securitizations of PACE financing. Each PACE assessment is serviced by the appropriate county. Generally, the collected assessments are comingled with the county’s general fund and it is unclear what would occur to such collections in the event of a bankruptcy. There are both PACE and non-PACE products that compete in the municipal financing market.

**Litigation Finance**

Client Account investments may require an evaluation of the outcome and timing of a dispute resolution process. Regardless of the amount of research and other due diligence that may be performed, predicting the outcome of litigation or other dispute resolution processes is inherently uncertain and depends on a variety of circumstances that may be unrelated to the legal merits of the substantive claims of the parties, including uncertainty regarding the application of law to particular facts, disputed factual records and testimony, unforeseen procedural issues, uneven quality of advocacy, misapplication of settled law by a judge or jury, or settlement dynamics in which the motivations of the parties may be unrelated, in whole or in part, to the merits of the dispute. Since the expenditures in this type of investment generally do not involve the acquisition of any assets having any residual value, an unfavorable outcome typically will result in a complete loss of a Client Account’s investment.

**Other Litigation Situations**

The Adviser, on behalf of certain Client Accounts, invests in companies involved in litigation or restructuring on the basis of the Adviser’s assessment of the likely outcome of such litigation and/or the impact of the bankruptcy process on the company. The Adviser, on behalf of certain Client Accounts, also invests in companies that are likely to be subject to reorganization, including as a result of a major litigation involving such company. Predicting the outcome of litigation or restructuring is speculative by nature and could involve lengthy delays following an appeal or an indirect attack on the outcome. The Adviser may invest in issuers which were — as entities, at the senior management level or both — the subject of criminal and administrative proceedings. These investments involve a particularly high degree of risk and uncertainty due to the unpredictability (and often politically motivated and

discretionary) outcome of such proceedings and the risk of government cancellation of franchises and licenses necessary for continued operations.

### **Use of Leverage**

To the extent consistent with the Client Account's investment mandate, leverage may be used selectively by the Adviser as a result of the structure and terms of certain investments and typically on an investment-by-investment basis as opposed to a Client Account's portfolio as a whole. Leverage results in a Client Account controlling substantially more assets than the Client Account has equity. Leverage increases a Client Account's returns if the Client Account earns a greater return on investments purchased with borrowed funds than the Client Account's cost of borrowing such funds. However, the use of leverage exposes the Client Account to additional levels of risk, including (i) greater losses from investments than would otherwise have been the case had the Client Account not borrowed to make the investments, (ii) margin calls or interim margin requirements which may force premature liquidations of investment positions and (iii) losses on investments where the investment fails to earn a return that equals or exceeds the Client Account's cost of borrowing such funds. In the event of a sudden, precipitous drop in value of the Client Account's assets, the Client Account might not be able to liquidate assets quickly enough to repay its borrowings, further magnifying its losses.

In an unsettled credit environment, the Adviser may find it difficult or impossible to obtain leverage for a Client Account. Since leveraging its assets is part of the investment strategy of certain Client Accounts, in such event the applicable Client Account could find it difficult to implement its entire strategy. In addition, any leverage obtained, if terminated on short notice by the lender, could result in the Adviser being forced to unwind positions quickly and at prices below what the Adviser deems to be fair value for the positions.

### **Special Situations**

The Adviser, on behalf of certain Client Accounts, invests in companies involved in (or the target of) acquisition attempts or tender offers or in companies involved in or undergoing work-outs, liquidations, spin-offs, reorganizations, bankruptcies or other catalytic changes or similar transactions. In any investment opportunity involving any such type of special situation, there exists the risk that the contemplated transaction either will be unsuccessful, will take considerable time or will result in a distribution of cash or a new security the value of which will be less than the purchase price of the security or other financial instrument in respect of which such distribution is received. Similarly, if an anticipated transaction does not in fact occur, a Client Account may be required to sell its investment at a loss. Because there is substantial uncertainty concerning the outcome of transactions involving financially troubled companies, there is a potential risk of loss by a Client Account of its entire investment in such companies.

### **Short Sales**

Short selling involves selling securities which are not owned and borrowing them for delivery to the purchaser, with an obligation to replace the borrowed securities at a later date. Short selling allows the investor to profit from declines in market prices to the extent such decline exceeds the transaction costs and the costs of borrowing the securities. The extent to which a Client Account engages in short sales will depend upon the Adviser's investment strategy and opportunities. A short sale creates the risk of a theoretically unlimited loss, in that the price of the underlying security could theoretically increase without limit, thus increasing the cost to a Client Account of buying those securities to cover the short position. There can be no assurance that a Client Account will be able to maintain the ability to borrow securities sold short. In such cases, the Client Account can be "bought in" (i.e., forced to repurchase

securities in the open market to return to the lender). There also can be no assurance that the securities necessary to cover a short position will be available for purchase at or near prices quoted in the market. Purchasing securities to close out the short position can itself cause the price of the securities to rise further, thereby exacerbating the loss. Furthermore, current and prospective restrictions on short selling may limit a Client Account's ability to take short positions, which could adversely affect performance and the Adviser's ability to implement a Client Account's investment strategy as desired.

### **Counterparty Risk**

Transactions entered into by the Adviser on behalf of certain Client Accounts involve credit risk to the extent that its market counterparties are unable or unwilling to fulfill their contractual obligations. These obligations may occur from investments in swaps, "synthetic" or derivative instruments, repurchase agreements, certain types of options or other customized financial instruments, or, in certain circumstances, non-U.S. securities. This risk also includes the risk of settlement default. The Adviser will use its best efforts to enter into such transactions with established, rated and reputable counterparties.

### **Convergence Risk**

The Adviser, on behalf of certain Client Accounts, pursues relative value strategies by taking long positions in securities believed to be undervalued and short positions in securities believed to be overvalued. In the event that the perceived mis-pricings underlying the Adviser's trading positions were to fail to converge toward, or were to diverge further from, the Adviser's expectations, a Client Account may incur a loss.

### **Interest Rate Risk**

Generally, the value of fixed income securities will change inversely with changes in interest rates. As interest rates rise, the market value of fixed income securities tends to decrease. Conversely, as interest rates fall, the market value of fixed income securities tends to increase. This risk will be greater for long-term securities than for short-term securities. The Adviser may attempt to minimize the exposure of the portfolios to interest rate changes through the use of interest rate swaps, interest rate futures and/or interest rate options. However, there can be no guarantee that the Adviser will be successful in fully mitigating the impact of interest rate changes.

### **Real Estate Risks**

The Adviser, on behalf of certain Client Accounts, may opportunistically make investments in direct holding of real estate properties. Such investments will be subject to the risks inherent in the ownership and operation of real estate and real estate related businesses and assets. These risks include, but are not limited to, those associated with the burdens of ownership of real property, general and local economic climate, local real estate conditions, changes in supply of or demand for competing properties in an area (as a result, for instance, of overbuilding), fluctuations in the average occupancy and room rates for hotel properties, the financial resources of tenants, changes in building, environmental and other laws, energy and supply shortages, various uninsured or uninsurable risks, natural disasters, changes in government regulations (such as rent control), changes in real property taxes, changes in interest rates and the availability of mortgage funds which may render the sale or refinancing of properties difficult or impracticable, negative developments in the economy that depress travel activity, environmental liabilities, contingent liabilities on disposition of assets, terrorist attacks and war and other factors which are beyond the control of the Adviser. There is no assurance that there will be a ready market for resale of real estate investments because real estate investments will generally not be liquid. Lack of liquidity may result from the

absence of an established market for such investments, as well as legal or contractual restrictions on their resale.

### **Real Estate Development Risks**

The Adviser, on behalf of certain Client Accounts, may acquire interests in real estate developments and/or in businesses that engage in real estate development. To the extent that a Client Account invests in such development activities, it will be subject to the risks normally associated with such activities. Such risks include, without limitation, risks relating to the availability and timely receipt of zoning and other regulatory approvals, the cost and timely completion of construction (including risks beyond the control of the Adviser, such as weather or labor conditions or material shortages) and the availability of both construction and permanent financing on favorable terms. These risks could result in substantial unanticipated delays or expenses and, under certain circumstances, could prevent completion of development activities once undertaken, any of which could have an adverse effect on the investment. Properties under development or properties acquired to be developed may generate little or no cash flow from the date of acquisition through the date of completion of development, if completed, and may experience operating deficits after the date of completion. In addition, market conditions may change during the course of development that make such development less attractive than at the time it was commenced.

### **Cyber Security Breaches and Identity Theft**

The Adviser's information and technology systems may be vulnerable to damage or interruption from computer viruses, network failures, computer and telecommunication failures, infiltration by unauthorized persons and security breaches, usage errors by their respective professionals, power outages and catastrophic events such as fires, tornadoes, floods, hurricanes and earthquakes.

The Adviser, its affiliates and Client Accounts and their third-party services providers are susceptible to operational and information security risks. While third-party service providers have procedures in place with respect to information security, their technologies may become the target of cyber-attacks or information security breaches that could result in the unauthorized gathering, monitoring, release, misuse, loss or destruction of the Adviser's confidential and other information, or otherwise disrupt a Client Account's operations or those of any third-party service providers. Disruptions or failures in the physical infrastructure or operating systems that third-party service providers, or cyber-attacks or security breaches of the networks, systems, or devices that third-party service providers use to service the Adviser, its affiliates or Client Account's operations, could disrupt and impact the service providers' and the Adviser's, its affiliates' or Client Account's operations, potentially resulting in financial losses, the inability to process transactions, inability to calculate valuations, violations of applicable privacy and other laws, regulatory fines, penalties, reputational damage, reimbursement or other compensation costs, and/or additional compliance costs. Although the Adviser has implemented various measures to manage risks relating to these types of events, if these systems are compromised, become inoperable for extended periods of time or cease to function properly, the Adviser, or its affiliates may have to make a significant investment to fix or replace them. The failure of these systems and/or of disaster recovery plans for any reason could cause significant interruptions in the Adviser, its affiliates or Client Account's operations and result in a failure to maintain the security, confidentiality or privacy of sensitive data, including personal information relating to investors (and the beneficial owners of investors). Such a failure could harm the Adviser, its affiliates or Client Account's reputation, subject any such entity and their respective affiliates to legal claims and otherwise affect their business and financial performance. There can be no assurance that the Adviser, its affiliates or Client Accounts or

third-party service providers will not suffer losses relating to cyber-attacks or other information security breaches in the future.

### **Capital Structure Investment Conflicts and Other Accounts**

Certain Client Accounts invest in a broad range of asset classes throughout the capital structure. These investments may include investments in loans and debt securities, preferred equity securities and common equity securities. As a result, a Client Account may invest in securities or other instruments of an issuer (or affiliated group of issuers) in which other Client Accounts invest in or have an interest in different parts of the capital structure. If the issuer becomes insolvent, restructures, or suffers financial distress, there may be a conflict between the interests of a Client Account and those other Client Accounts insofar as the issuer may be unable (or in the case of a restructuring prior to bankruptcy may be expected to be unable) to satisfy the claims of all of its creditors and security holders (which may include certain other Client Accounts that enter into loan agreements with certain entities in the capital structure). Certain Client Accounts and other Client Accounts may have competing claims for the assets of such issuers. Moreover, such investments or other interests in the capital structure may impact the investment made or interest in a different part of the structure.

Under these circumstances, it may not be feasible for 400CM to reconcile the conflicting interests of each Client Account in a way that protects each Client Account's interests. Additionally, 400CM or its nominees may hold board or creditor committee memberships which may require them to vote or take other actions in such capacities that might be conflicting with respect to certain funds managed by 400CM in that such votes or actions may favor the interests of one account over another account. Furthermore, 400CM's fiduciary responsibilities in these capacities might conflict with the best interests of the investors. 400CM has developed processes to address such conflicts of interest.

### **Epidemics, Pandemics and COVID-19**

Many countries have been susceptible to epidemics, such as severe acute respiratory syndrome, avian flu, H1N1/09 flu and, beginning in January 2020, the highly transmissible and pathogenic novel coronavirus (COVID-19), which the World Health Organization declared to be a pandemic at such time. Additional outbreaks of COVID-19 as new variants emerge could lead to a continual decline in global economic growth resulting in prolonged unemployment and recession and interruptions to the supply chain. It is currently unknown when the world economy will "re-open" to its status pre-pandemic as uncertainty remains around the global distribution and long-term efficacy of vaccines in fighting new variants of the disease. The spread of COVID-19 may have an adverse impact on the Client Accounts. In consumer goods, for example, a delay in discretionary spending and travel plans because of concerns about the pandemic could result in decreased tenant occupancy rates with respect to certain real estate holdings of Client Accounts. With respect to the banking industry, and in particular, the consumer finance sector, any credit losses resulting from financial difficulties of borrowers impacted by COVID-19 may also translate into an increased risk of default under any holdings of a Client Account. The impact of government intervention in the areas of tenant eviction and foreclosure remains fluid and it is uncertain how long such intervention will last. Any similar future outbreak or pandemic could have similar potential adverse effects on the global economy, 400CM and/or its Client Accounts.

### **European Instability**

Recent events, including the invasion of Ukraine by Russia, have interjected uncertainty into global financial markets, especially European markets. It is possible that any fallout from the Ukrainian conflict will have effects on other European countries as such countries address



cross-border refugee movements and other potential threats. A number of countries including the United States and certain European nations have imposed sanctions on Russia and businesses affiliated with that country. The long-term impact of these sanctions remains unclear, although they may prove to limit potential investment opportunities and may impair cash flow that is material to an investment if third parties doing business with a company underlying an investment are sanctioned parties. The regulatory framework of sanctions is often complex and at times counter-intuitive, and transactions involving sanctioned parties can result in increased compliance expenses.

### **Inflation**

In response to recent economic events, including the global financial crisis and the ongoing COVID-19 global pandemic, countries around the world have significantly loosened monetary policy and injected trillions of dollars into the global economy in an effort to prevent more severe economic turbulence. This level of support has given rise to significant increases in government spending globally and in many instances significant increases to the amount of debt issued by governments in the international bond markets. The United States and other countries have experienced, and in the future may experience, disruptions throughout the supply chain. Current and future disruption in supply of goods, combined with loose monetary policy and unprecedented levels of government spending, may materially increase inflation of the U.S. dollar and other currencies in the coming years. Inflation and rapid fluctuations in inflation rates have had in the past, and in the future may have, negative effects on economies and financial markets.

### **Item 9: Disciplinary Information**

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There are no legal or disciplinary events that 400CM believes are material to a client's or prospective client's evaluation of 400CM's advisory business or the integrity of 400CM's management.

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

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Neither 400CM nor any of its management persons is registered, or has an application pending to register, as a broker-dealer or a registered representative of a broker-dealer, a futures commission merchant, commodity pool operator, a commodity trading advisor, or is an associated person of any of the above.

The Adviser has entered into a sub-advisory relationship with 400 Capital Management Europe Limited, a limited company registered in England ("**400 Capital Management Europe**"). 400 Capital Management Europe is wholly owned by the Adviser. 400 Capital Management Europe was formed in November 2015 and commenced operations as of January 1, 2016. Currently, the Adviser is the sole advisory client of 400 Capital Management Europe. 400 Capital Management Europe provides certain research related services to the Adviser. 400CM does not believe that this sub-advisory relationship causes any conflicts of interest, as no additional management fees are charged by 400 Capital Management Europe.

Except as otherwise disclosed in this Brochure, neither 400CM nor any of its management persons has a relationship or arrangement that is material to its advisory business or to its clients with any related person. In addition, the Adviser does not recommend or select other investment advisers for its clients.



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

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***Code of Ethics***

400CM has adopted a Code of Ethics (“**Code**”) that is designed to meet the requirements of Rule 204A-1 of the Advisers Act and emphasize 400CM’s role as a fiduciary to its Client Accounts. The foundation of the Code consists of three underlying principles:

- access persons must at all times place the interests of Client Accounts first;
- access persons have an obligation to conduct all personal securities transactions consistent with the pre-clearance, reporting, restrictions and limitations contained in the Code; and
- access persons are prohibited from taking inappropriate advantage of their positions at 400CM.

The Code requires all access persons to comply with all provisions of the Code and all applicable federal securities laws and to report any known or suspected violations of the policies and procedures contained in the Code or other activities of any access person that could be construed as a violation of any law, rule or regulation applicable to 400CM’s business to the CCO, or in the CCO’s absence, 400CM’s General Counsel. The Code is distributed to each access person at the time of hire. All access persons are required to certify their adherence to the Code following their initial hire date, and on an annual basis thereafter, and when any material amendments are made to the Code. 400CM provides (or arranges for a qualified third party to provide) initial and ongoing training, on at least an annual basis, on the policies and procedures set forth in the Code to its access persons.

400CM is aware that certain conflicts of interest may arise relating to an access person’s personal trading. For example, persons related to 400CM, including its affiliates, officers, directors and employees, may buy, sell, or have a financial interest in securities owned or acquired by Client Accounts either by investing directly in the Funds managed by 400CM or through independent transactions in personal accounts. Within the Code, the Adviser has adopted policies and procedures designed to monitor such potential conflicts of interest relating to an access person’s personal trading activity, including (i) the reporting of transactions and holdings in certain securities and (ii) the pre-clearance of certain types of personal securities transactions. In addition, 400CM maintains a restricted list and watch list of issuers (or certain parts of the capital structure of an issuer). As a general rule, trades will not be allowed for Client Accounts, or for personal accounts of an access person, in the securities of an issuer appearing on the restricted list and with respect to trades in the securities listed on the watch list, such trades shall not be permitted unless pre-approved by the CCO (or designee). An issuer may be placed on the restricted list for a variety of reasons, including but not limited to: (i) 400CM or an access person has or may be exposed to material non-public information about an issuer; (ii) the occurrence of trading in the issuer’s securities or financial instruments presents the appearance of a conflict of interest; (iii) one of 400CM’s employees has accepted a position at the issuer, such as a director or a member of a credit committee, which may lead to 400CM or such employee receiving material non-public information; (iv) 400CM has executed an agreement (e.g., a confidentiality agreement) whereby it may be in a position to receive material non-public information about an issuer or otherwise restricts trading in an issuer’s securities (such as having “private side” information with respect to an issuer in connection with a loan); and (v) as otherwise determined by the CCO. An issuer may be placed on the watch list when trading in such issuer could present certain conflicts of interest to 400CM or a Client Account, respectively.

Prospective or existing investors in the Funds and Managed Account Clients may request a copy of the Code by contacting the Adviser at the address or telephone number listed on the cover page of this document.

### *Allocation and Aggregation of Trades*

400CM will perform investment management services for various Client Accounts, some of which follow similar investment strategies and invest in the same types of securities or instruments. 400CM recognizes that the side-by-side management of these client accounts may present or create the appearance of certain conflicts of interest. For example, employees of 400CM may maintain personal investments in certain Funds, but not others. Additionally, the fees payable to 400CM or one of its affiliates from certain Client Accounts may be higher than the fees payable by other Client Accounts. To manage these conflicts of interest, 400CM has adopted trade allocation policies and procedures to promote allocations to Client Accounts that are fair and equitable over time.

If more than one Client Account is considered to be eligible to participate in an investment or trading opportunity, it is the general policy of 400CM to allocate such investment opportunities to Client Accounts on a pro rata basis adjusted for (i) a Client Account's particular portfolio construction based on position/sector/sub-sector targets established by 400CM's Investment Committee, (ii) the liquidity requirements of a Client Account, and/or (iii) investment restrictions particular to a Client Account's investment mandate ((i)-(iii) shall collectively be referred to as the "**Target Allocations**").

When appropriate, allocations to more than one Client Account will be made in accordance with the Target Allocations. Allocations that are outside of the range will be deemed to be an exception to the policy. All exceptions will be documented and reasons that influenced the departure from the Target Allocations will also be documented.

In addition, when appropriate, the Adviser may, but is not required to, aggregate client orders to achieve more efficient execution or to provide for equitable treatment among accounts. With respect to equity investments and hedging transactions, to the extent orders are aggregated, each participating account generally will receive the average price. When orders are not aggregated, trades generally will be processed in the order that they are placed with the broker or counterparty selected by the Adviser. As a result, certain trades in the same security for one Client Account (including a Client Account in which the Adviser and its personnel may have a direct or indirect interest) may receive more or less favorable prices or terms than another Client Account, and orders placed later may not be filled entirely or at all, based upon the prevailing market prices at the time of the order or trade. In addition, some opportunities for reduced transaction costs and economies of scale may not be achieved.

In addition, Client Accounts from time to time invest in securities of issuers in which other Client Accounts have an interest in other parts of the capital structure. For further information, see "Capital Structure Investment Conflicts and Other Accounts" in "**Item 8: Methods of Analysis, Investment Strategies and Risk of Loss.**"

### *Cross Trades*

The Adviser may determine that it would be in the best interests of two or more Client Accounts to transfer a security from one Client Account to another Client Account (each such transfer, a "**Cross Trade**") for a variety of reasons, including, without limitation, tax purposes, liquidity purposes, to rebalance the portfolios of the Client Accounts, or to reduce transaction costs that may arise in an open market transaction. A Cross Trade can occur directly between Client Accounts or through a broker if the broker is instructed to cross the security at identical purchase and sale prices between Client Accounts. The contemporaneous

placing of buy and sell trades with a broker in a liquid market for that security without instructing the broker to cross the security does not constitute a Cross Trade. If the Adviser decides to engage in a Cross Trade, the Adviser will determine that the trade is in the best interests of both of the Client Accounts involved in it and take steps to verify that the transaction is consistent with the duty to obtain best execution for each of those Client Accounts. Cross Trades (including swaps) may be effected subject to the following guidelines: (i) such transactions shall be effected for cash consideration at the current fair market value of the particular securities, and (ii) no extraordinary brokerage commissions or fees (i.e., except for customary transfer fees or commissions) or other remuneration shall be paid in connection with any such transaction.

### ***Principal Transactions***

To the extent that a cross trade may be viewed as a “**Principal Transaction**” (as such term is used under the Advisers Act) due to the ownership interest in a Client Account by the Adviser, its affiliates or personnel, the Adviser will comply with the requirements of Section 206(3) of the Advisers Act, including the obtaining of specific consent from the Client Account or a representative of the Client Account for each Principal Transaction.

## **Item 12: Brokerage Practices**

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### ***Broker Selection and Best Execution***

Generally, with respect to Client Accounts, 400CM is authorized to select the broker or dealer to be used and negotiate the fees to be paid to the broker-dealer in connection with such transactions. When selecting a broker dealer, the Adviser considers relevant factors such as: the broker’s level of activity and experience in the securitized and structured credit market, the financial stability and reputation of brokerage firms, the responsiveness of the broker to 400CM, and the research, brokerage or other services provided by such brokers.

400CM recognizes its duty to obtain best execution. Best execution is determined on a trade-by-trade basis and should result in best qualitative execution and not necessarily the lowest possible commission cost. 400CM need not solicit competitive bids and does not have an obligation to seek the lowest available commission. It is not 400CM’s practice to negotiate “execution only” commission rates, thus Client Accounts may be deemed to be paying for research, brokerage or other services provided by the broker which are included in the commission (or spread) rate. In pursuing the “most favorable transaction” (i.e. best execution) for an investment, many factors will be taken into consideration, such as the price of the security, execution speed, confidentiality, market depth, capital commitments, recent order flow, size and liquidity of the traded position, knowledge of the other side of the trade, and trade settlement history.

Depending upon the portfolio transaction to be executed for a Client Account, the Adviser may not have a range of broker-dealers to select from. Specifically, when investing in securities that are traded in the over-the-counter market, the Adviser will engage primarily in transactions with dealers who make markets in such securities. In such cases, the dealer offering the security to the Adviser may be the only execution available for such investment.

### ***Other Brokerage Considerations***

From time to time, brokers (including prime brokers) may assist the Funds in raising additional funds from investors, and representatives of the Adviser may speak at conferences and programs sponsored by such brokers for investors interested in hedge funds. In attending such conferences, the Adviser will be afforded the opportunity to meet with prospective investors. While such events or services may influence the Adviser when deciding whether

to use such broker in connection with brokerage, financing and other activities of the Funds and other Client Accounts, the Adviser does not commit to allocate a certain volume of business to a broker and the Adviser will continue to seek best execution when placing transactions with such broker.

400CM and/or its personnel maintain relationships with service providers, including broker-dealers, who have employees that invest (or are affiliated with an investor) in a Client Account. As such, 400CM may be faced with a conflict of interest in recommending the retention or continuation of the relationship with such third-party service provider, in that 400CM has an incentive to maintain goodwill between it and the investing employee of the service provider. 400CM has developed policies and procedures to mitigate such conflicts of interest.

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

400CM does not have any formal soft dollar arrangements but reserves the right to enter into such arrangements in the future. Additionally, 400CM receives research (which includes but is not limited to proprietary and third-party research, economic and market information, industry/sector/company commentary, etc.) from certain broker-dealers that it executes transactions with or from broker-dealers that are seeking the Adviser's business. Research services may be in written or oral form or on-line. Receipt of research is a "soft dollar" benefit and is within the meaning of Section 28(e).

Except for services that would be a Client Account expense or as otherwise described below, the Adviser will limit the use of "soft dollars" to obtain research and brokerage services to services which constitute research and brokerage within the meaning of Section 28(e). Research is often made available to the Adviser and its personnel on an unsolicited basis and without regard to transaction costs charged or the volume of business the Adviser directs to the respective counterparty.

400CM is benefitted by trading with brokers that provide research because 400CM is not required to develop that research. Otherwise, 400CM would be required to develop it, which may potentially be expensed to the Client Accounts.

Any soft dollars or research benefits received will benefit the Adviser and many, but not necessarily all of the Adviser's Client Accounts and will not be allocated proportionally. The Adviser will have a conflict and incentive to select brokers that are providing such soft dollar benefits based on its desire to receive such product or service.

### ***Trade Errors***

The Adviser generally defines trade errors as an error in the placement, execution or settlement of a trade. The Adviser will seek to detect errors prior to settlement and correct and/or mitigate them in an expeditious manner. Errors that are detected and corrected prior to settlement and that did not have a profit or loss impact on the respective Client Accounts will not be deemed to be trade errors.

The Adviser will determine an appropriate method to correct a trade error in light of the facts and circumstances and on a case-by-case basis. Trade errors may result in losses or gains. To the extent an error is caused by a counterparty, such as a broker-dealer, the Adviser will seek to recover any losses associated with such error from the counterparty. The Client Account (and not the Adviser) will benefit from any gains resulting from trade errors and will be responsible for any losses (including additional trading costs) resulting from trade errors and similar human errors, absent the Adviser's negligence, wilful misfeasance or bad faith; provided that the Adviser shall not be responsible for trade errors caused by other

persons, including third-party brokers and custodians. See “**Item 11: Code of Ethics, Participation or Interest in Client Transactions and Personal Trading**” for a description of our trade aggregation practices.

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**Item 13: Review of Accounts**

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***Review of Accounts***

Most Client Accounts require active management by the Adviser, and, accordingly, reviews of transactions, positions and cash balances occur on a daily basis. Additionally, to the extent applicable, the Adviser reviews Client Account portfolios on a regular basis to assure compliance with an account’s specific investment guidelines.

***Reporting***

Unless otherwise disclosed in a Fund’s offering documents, the Adviser will distribute an audited financial report for each Fund with respect to the previous fiscal year to all investors within 120 days of year-end. In addition, the administrator to each Fund will generally distribute net asset value updates on a monthly or quarterly basis. Generally, Managed Account Clients receive reports and/or statements as set forth in the client’s investment management agreement.

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

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400CM has entered into relationships whereby certain third-party entities may introduce (each, an “**Introducer**”) prospective investors to 400CM for potential investment in interests/shares of the Funds. 400CM maintains an agreement with each Introducer and pays fees to the Introducer as compensation for its services. The fees paid to the Introducers do not result in an increase in fees or expenses paid by the investors in the Funds. 400CM does not currently maintain any agreements with an Introducer to solicit Managed Account Clients.

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**Item 15: Custody**

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Under Rule 206(4)-2 of the Advisers Act (the “**Custody Rule**”), 400CM and certain affiliated entities are deemed to have custody of the cash and/or securities of certain Funds. 400CM and its affiliates are exempt from many of the requirements of the Custody Rule because (i) such Funds are audited in accordance with U.S. generally accepted accounting principles on an annual basis by an independent public accountant that is registered with, and subject to regular inspection by the Public Company Accounting Oversight Board, and (ii) 400CM distributes such Funds’ audited financial statements to investors in such Funds within 120 days of such Funds’ fiscal year end. 400CM does not have custody with respect to its Managed Account Clients or Sub-Advised Funds.

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**Item 16: Investment Discretion**

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Subject to each Fund’s governing documents and any applicable side letter agreements, the Adviser has full investment discretion to manage the Fund, including authority to make decisions with respect to which securities are bought and sold, the amount and price of those securities, the brokers or dealers to be used for a particular transaction, and the commissions paid. With respect to the Managed Account Clients and Sub-Advised Funds, the Adviser has investment discretion, subject to any investment guidelines set forth in the respective investment management agreement for such Managed Account Clients and Sub-Advised Funds. Various securities and/or tax laws as well as internal compliance policies may impose

additional restrictions on the investments that the Adviser may make on behalf of any Client Account.

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**Item 17: Voting Client Securities**

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To the extent 400CM has been delegated proxy voting authority on behalf of its Client Accounts, 400CM complies with its proxy voting policies and procedures. Such policies and procedures are designed to verify that such proxies are voted in the best interest of the client. The investors in a Fund may not direct voting of proxies.

In furtherance of 400CM's goal of voting proxies in the best interests of Client Accounts, 400CM will follow its policies and procedures designed to identify and address material conflicts that may arise. If 400CM determines that it may have, or be perceived to have, a conflict of interest when voting proxies, 400CM will vote in accordance with its proxy voting policies and procedures and accordingly may refrain from voting certain proxies.

Upon request, the Adviser will provide Client Accounts with a copy of its proxy voting policies and procedures and/or a record of all proxy votes cast by 400CM on behalf of the respective Client Account.

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**Item 18: Financial Information**

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Registered investment advisers are required in this Item to provide you with certain financial information or disclosures about their financial condition. 400CM has no financial commitment that impairs its ability to meet contractual and fiduciary commitments to its Client Accounts and has not been the subject of a bankruptcy proceeding.