

ACR Opportunity Fund Investment Policy

Investment Policy

Objectives, Performance, and Benchmark

ACR Opportunity Fund strategy objectives are to preserve capital from permanent loss during periods of economic decline, and provide above-average absolute and relative returns in the long run. Return objectives are subordinate to the objective of preserving capital from permanent loss. “Above-average absolute returns” means higher than a “fair” return in the long run, where “fair” is defined as an equity-like return commensurate with the risk of investing in equities. “Absolute” refers to a minimum equity-like return expectation that could be higher than typically implied by general equity market values. The objective is to generate satisfactory absolute returns in the long run regardless of general equity market returns.

“Above average relative returns” means higher than the equity market benchmark in the long run. The ACROX strategy benchmark is the MSCI All-Country World Index (ACWI). The MSCI ACWI Index was chosen because it is a broad proxy for the world equity market.

“Long run” is a period that includes a full economic cycle of expansion and contraction in output and equity market prices. Even though most investments often have a shorter fruition period, general market conditions and less liquid holdings may require a longer horizon. Returns may vary widely, either positively or negatively, from the absolute return objective and ACWI in the short term.

The evaluation of returns presents only half the picture. Risk must also be evaluated. While return data can be generated easily, the quantification of risk is difficult. The fund manager attempts to provide sufficient information about the fund’s investments – at least as much information as the manager would like to have as an outside investor – to help investors properly assess the strategy’s risks.

“To preserve capital from permanent loss during periods of economic decline” references selecting securities that can withstand difficult economic conditions. Permanent loss occurs when a large portion of the earning power, or intrinsic value of an enterprise or security, becomes permanently impaired. The economics of the enterprise and security are carefully evaluated to determine their ability to weather adverse economic conditions.

Security Types, Selection Universe, and the Use of Cash and Leverage

ACROX is not limited by security type, selection universe, or geographic location. Fund investments are only limited by the investment quality and *diversification requirements described below*. A full list of permitted security types is included in the Prospectus. General investment classes are as follows:

Marketable Equity

Marketable common stocks or securities with equity claims that fluctuate in price like common stocks.

Arbitrage or Event Related

Securities with offsetting return characteristics or event contingent capital flows, in which market price volatility is either significantly reduced or uncorrelated compared to marketable equities.

Discounted Bonds, Private Loans, and Other Financing

Bonds selling at a discount to our estimate of intrinsic value, private loans and other types of financing, such as convertible bonds.

Control Equity

Marketable common stocks in which there is limited liquidity and management influence or effective control.

Private Equity

Privately held business ownership.

Real Estate Equity

Direct equity ownership of real estate.

The preference of the strategy is to remain fully invested; however, this will not always be the case. Cash is held for three general reasons: (1) “frictional cash” after one position is sold and before another is acquired; (2) “tactical cash” is held until a satisfactory opportunity is identified; (3) “hedged cash” is held to mitigate a potential negative outcome or fund a potential or known future liability.

Leverage may be employed conservatively and in a manner consistent with a very high standard of quality. Quality characteristics are discussed in detail under “investment quality”.

Investment Quality

Portfolio quality requirements consist of a durable intrinsic principal value and reliable investment return at the portfolio level. Intrinsic principal value refers to the underlying net asset or cash generating value of the enterprise and security, regardless of its short-term market price fluctuations.

To achieve these requirements, high standards of quality are maintained when establishing the underlying soundness and values of the enterprises, securities, guarantees, and hedges that comprise the portfolio. Standards will vary by enterprise, security and position strategy. The overarching requirement is an investment quality portfolio capable of withstanding severe economic and market conditions.

Investment-level quality is contingent on the probability, magnitude, and event frequency of an investment’s payoff. Higher investment quality is a function of a higher probability of success, a higher magnitude payoff, a lower risk of extreme negative outcomes, and a higher frequency of positive outcomes. Analytical rigor is essential in this regard. The quality of an investment is only as good as the quality of the investment analysis that supports it.

Fundamental quality and valuation analysis of businesses, governments and consumers is integral in the evaluation of investment quality. Practically all securities and investment commitments depend on the performance of these economic variables either directly or indirectly. Investment quality analysis also necessitates the evaluation of secondary and ancillary risk exposures, especially factors that may be taken for granted, such as security exchange risk.

Financing operations have different economic characteristics than traditional equity investment operations. Regardless of the type of investment, highly prudent levels of leverage and liquidity are essential elements of quality.

Portfolio Diversification

Policy regarding diversification is to strike a balance between appropriate diversification and proper concentration as described in the investment adviser's published investment principles. The optimal balance depends on market conditions. In over-valued markets with limited opportunities, a sufficient number of holdings must be balanced with a reduced number of holdings with an acceptable margin-of-safety in each holding. In under-valued markets with numerous opportunities, an adequate number of holdings must be balanced with a limited number of the best opportunities.

Position size limitations are contingent on the nature of the position and any offsetting related holding. Maximum net position exposure is 15% at cost and 25% at market. Maximum net industry exposure is 20% at cost and 30% at market. Requirements at maximum purchase levels are exceptional quality and under-valuation. Typical position sizes at cost and market are expected to be lower.

Holding Period and Sell Discipline

Holding periods are subject to the characteristics of each investment. The fund generally takes a long-term view of equity investments based on the projected future profits of the underlying business. Arbitrage, event related, and fixed-income investments by definition have more finite investment holding periods.

Investments are liquidated for four general reasons: (1) an unanticipated change in the characteristics of the investment (2) an error in the analysis of the investment, (3) a price increase that exceeds intrinsic value, (4) the purchase of a security with a significantly lower price-to-value.

Enterprise and market conditions change and analytical errors may occur in the first two situations. Quick action is taken if necessary to remedy the situation if this conclusion is reached in these cases. In the third instance, even though the fund maintains a long-term investment horizon, the opportunity to profit from significant price increases will be acted upon.

The margin-of-safety principle applies on all sales. Price must be higher than value to seek to assure that selling is more profitable than holding. The expense of selling is certain, but the outcome is not.

Fund Liquidity, Income and Appreciation

The alignment of investor objectives and investment characteristics is critical to a successful relationship between a fund manager and fund investors. ACROX is for investors with limited liquidity needs and a long-term investment horizon. ACROX policy is to invest for total return from both investment income and capital appreciation. In our opinion, the highest return portfolio for the risk taken will have some investments that pay a higher income and others that pay no income.

The alignment of objectives is extremely important in times of market stress. The nature of market volatility is at odds with rational economic behavior. Rapidly deteriorating market conditions induce fear. In turn, fear often produces selling that generates price declines, and price declines induce more over-reaction. The inevitable result is a downward spiral that can create excellent opportunities for the rational, valuation-oriented investor.

However, if investors panic and sell rather than allowing the fund to buy, we cannot take advantage of the opportunities at hand. Far worse, if the fund has to sell during a market panic, not only are we likely to be selling low, but our selling may drive the prices of less liquid fund investments even lower for our remaining investors. Therefore, it is imperative that ACROX is comprised of patient investors with long-term investment horizons who understand the fund's investment philosophy and strategy. It is equally imperative that we communicate with our investors every step of the way.

Specific liquidity requirements are discussed in further detail in the Prospectus. Investors are advised to carefully read all respective offering documents of the fund they are considering.

Tax Sensitivity

ACROX includes taxable and tax-exempt investors. Investors are advised to pay special attention to the tax implications of fund investments in the Prospectus. The fund manager views the tax implications of fund investments as if the fund were a person with the tax characteristics of the average fund investor, understanding that the fund manager may have limited information about the tax characteristics of certain fund investors, and that the fund manager's primary concern is to meet its return on investment objectives regardless of tax implications.