

**CARITAS ROYALTIES FUND (BERMUDA) LTD.  
AND SUBSIDIARY**

CONSOLIDATED FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT

DECEMBER 31, 2011

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

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### INDEPENDENT AUDITORS' REPORT

To the Shareholders and Board of Directors of  
Caritas Royalties Fund (Bermuda) Ltd.

We have audited the accompanying consolidated statement of assets and liabilities of Caritas Royalties Fund (Bermuda) Ltd. and Subsidiary (collectively the "Fund"), including the consolidated schedule of investments, as of December 31, 2011, and the related consolidated statements of operations, changes in net assets and cash flows for the year then ended. These consolidated financial statements are the responsibility of the management of the Fund. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Caritas Royalties Fund (Bermuda) Ltd. and Subsidiary as of December 31, 2011, and the consolidated results of its operations, changes in its net assets and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.



Beverly Hills, California  
April 12, 2012

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## CONSOLIDATED STATEMENT OF ASSETS AND LIABILITIES

*(Expressed in United States Dollars)*

**December 31, 2011**

### Assets

Note receivable from American Assurance 2000, L.P., at fair value	\$ 48,781,186
Cash	218,791
Other	<u>12,000</u>
Total assets	<u>49,011,977</u>

### Liabilities

Redemptions payable	9,750,000
Accrued expenses	94,663
Management and performance fee payable	<u>594,201</u>
Total liabilities	<u>10,438,864</u>

<b>Net assets</b>	<u>38,573,113</u>
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Less: Attributable to Founder Shares	<u>12,000</u>
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<b>Net assets attributable to investor shares</b>	<u><b>\$ 38,561,113</b></u>
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# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## CONSOLIDATED STATEMENT OF OPERATIONS

*(Expressed in United States Dollars)*

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**Year Ended December 31, 2011**

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### **Investment income**

Unrealized gain on note receivable from American Assurance 2000, L.P.	\$ 3,789,942
Interest on note receivable from American Assurance 2000, L.P.	<u>2,752,472</u>
Total investment income	<u>6,542,414</u>

### **Expenses**

Performance fee	896,007
Professional fees	79,176
Management fee	348,497
Administrative fees and other expenses	<u>419,817</u>
Total expenses	<u>1,743,497</u>

<b>Net change in net assets resulting from operations</b>	<b>\$ <u>4,798,917</u></b>
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# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS

*(Expressed in United States Dollars)*

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### Year Ended December 31, 2011

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#### Operations

Net change in net assets resulting from operations	\$ 4,798,917
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#### Capital share transactions

Issuance of shares	2,290,000
Redemption of shares	<u>(11,660,256)</u>
Net change in net assets resulting from capital share transactions	<u>(9,370,256)</u>

<b>Net change in net assets</b>	<b>(4,571,339)</b>
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<b>Net assets, beginning of year</b>	<b><u>43,144,452</u></b>
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<b>Net assets, end of year</b>	<b><u>\$ 38,573,113</u></b>
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# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## CONSOLIDATED STATEMENT OF CASH FLOWS

(Expressed in United States Dollars)

**Year Ended December 31, 2011**

### Cash flows from operating activities

Net change in net assets resulting from operations	\$ 4,798,917
Adjustments to reconcile net change in net assets resulting from operations to net cash provided by operating activities:	
Interest on note receivable from American Assurance 2000, L.P.	(2,752,472)
Unrealized gain on note receivable from American Assurance 2000, L.P.	(3,789,942)
Changes in operating assets and liabilities:	
Proceeds on repayment of note receivable from American Assurance 2000, L.P.	2,102,058
Other assets	30,402
Accrued expenses	(34,677)
Management and performance fee payable	(126,750)

<b>Net cash provided by operating activities</b>	<b><u>227,536</u></b>
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### Cash flows from financing activities

Proceeds from issuance of shares	2,290,000
Payments for redemption of shares, net of change in redemptions payable	(2,326,641)

<b>Net cash used in financing activities</b>	<b><u>(36,641)</u></b>
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<b>Net change in cash</b>	<b>190,895</b>
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<b>Cash, beginning of year</b>	<b><u>27,896</u></b>
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<b>Cash, end of year</b>	<b><u>\$ 218,791</u></b>
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### Supplemental disclosure of noncash activities

Accrued interest on note receivable from American Assurance 2000, L.P. converted into principal balance on note receivable from American Assurance 2000, L.P.	<b><u>\$ 1,828,090</u></b>
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# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## CONSOLIDATED SCHEDULE OF INVESTMENTS

*(Expressed in United States Dollars)*

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**December 31, 2011**

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	<b>Principal Amount</b>	<b>Percentage of Net Assets</b>	<b>Fair Value</b>
<b>Note receivable from American Assurance 2000, L.P., at fair value</b>			
<b>United States</b>			
<b>Oil and Energy</b>			
American Assurance 2000, L.P. (See Note 3)	\$ 45,634,243	126.5 %	\$ 48,781,186



# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

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### 1. Nature of operations and summary of significant accounting policies

#### *Nature of Operations*

Caritas Royalties Fund (Bermuda) Ltd. and Subsidiary (collectively the “Fund”) was incorporated in Bermuda as an open-ended mutual fund company on July 22, 2004. Refer to the Fund’s prospectus for more information.

The Fund’s investment objective is to receive profits derived from royalty income from a diversified portfolio of United States oil and natural gas royalty interests (“Royalty Interests”) owned by American Assurance 2000, L.P. (“American Assurance”). Royalty Interests are contractual rights to receive a fixed percentage of production revenues from crude oil and natural gas properties which are owned and operated by third parties. The Fund derives profits from American Assurance’s investments in Royalty Interests through fixed interest it receives from its note receivable from American Assurance, as well as a fair value adjustment on that note receivable, and previously through fixed and contingent interest it received from a note receivable from American Assurance.

Centaur Performance Group (Bermuda) Ltd. is the manager of the Fund (“Manager”). Cornerstone Acquisition and Management Company, LLC (“Cornerstone”) is the investment consultant to the Manager (“Investment Consultant”). Cornerstone is also the manager of American Assurance.

#### *Principles of Consolidation*

The accompanying consolidated financial statements include the accounts of Caritas Royalties Fund (Bermuda) Ltd. and the accounts of Cornerstone Olaj, its wholly owned subsidiary. Intercompany transactions and balances have been eliminated in consolidation. Cornerstone Olaj was dissolved effective April 2011.

#### *Basis of Presentation*

The consolidated financial statements are expressed in United States dollars and have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”).

These consolidated financial statements were approved by management and available for issuance on April 12, 2012. Subsequent events have been evaluated through this date.

#### *Valuation of Note Receivable at Fair Value - Definition and Hierarchy*

In accordance with GAAP, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the “exit price”) in an orderly transaction between market participants at the measurement date.

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

### 1. Nature of operations and summary of significant accounting policies (continued)

#### *Valuation of Note Receivable at Fair Value - Definition and Hierarchy (continued)*

In determining fair value, the Fund uses various valuation approaches. A fair value hierarchy for inputs is used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs are to be used when available. Observable inputs are those that market participants would use in pricing the asset or liability based on market data obtained from sources independent of the Fund. Unobservable inputs reflect the Fund's assumptions about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The fair value hierarchy is categorized into three levels based on the inputs as follows:

*Level 1* - Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the Fund has the ability to access. Valuation adjustments are not applied to Level 1 investments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these investments does not entail a significant degree of judgment.

*Level 2* - Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

*Level 3* - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The availability of valuation techniques and observable inputs can vary from investment to investment and are affected by a wide variety of factors, including the type of investment, whether the investment is new and not yet established in the marketplace, and other characteristics particular to the transaction. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Those estimated values do not necessarily represent the amounts that may be ultimately realized due to the occurrence of future circumstances that cannot be reasonably determined. Because of the inherent uncertainty of valuation, those estimated values may be materially higher or lower than the values that would have been used had a ready market for the investments existed. Accordingly, the degree of judgment exercised by the Fund in determining fair value is greatest for investments categorized in Level 3. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes, the level in the fair value hierarchy within which the fair value measurement falls in its entirety, is determined based on the lowest level input that is significant to the fair value measurement.

Fair value is a market-based measure considered from the perspective of a market participant rather than an entity-specific measure. Therefore, even when market assumptions are not readily available, the Fund's own assumptions are set to reflect those that market participants would use in pricing the asset or liability at the measurement date. The Fund uses prices and inputs that are current as of the measurement date, including periods of market dislocation. In periods of market dislocation, the observability of prices and inputs may be reduced for many investments. This condition could cause an investment to be reclassified to a lower level within the fair value hierarchy.

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

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### 1. Nature of operations and summary of significant accounting policies (continued)

#### *Valuation Techniques*

##### Note Receivable from American Assurance

Fair value of the note receivable approximates the sum of the principal balance, interest receivable on the note receivable and any principal and fair value adjustments on the note receivable (see Note 3). The note receivable is categorized in Level 3 of the fair value hierarchy.

#### *Investment Transactions and Related Investment Income*

Interest income and expense are recognized on the accrual basis as earned or incurred. Investment transactions are accounted for on a trade-date basis.

#### *Income Taxes*

Under current laws of Bermuda, the Fund is not required to pay any taxes in Bermuda on either income or capital gains. Accordingly, no provision for income taxes has been made in the accompanying consolidated financial statements. The Fund has received an undertaking from the Minister of Finance in Bermuda exempting it from any such taxes until the year 2016.

The Fund is required to determine whether its tax positions are more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The tax benefit recognized is measured as the largest amount of benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement with the relevant taxing authority. De-recognition of a tax benefit previously recognized results in the Fund recording a tax liability that reduces ending net assets. Based on its analysis, the Fund has determined that it has not incurred any liability for unrecognized tax benefits as of December 31, 2011. However, the Fund's conclusions may be subject to review and adjustment at a later date based on factors including, but not limited to, on-going analyses of and changes to tax laws, regulations and interpretations thereof.

The Fund recognizes interest and penalties related to unrecognized tax benefits in interest expense and other expenses, respectively. No interest expense or penalties have been recognized as of and for the year ended December 31, 2011.

The Fund is subject to income tax examinations by major taxing authorities for all years since inception.

The Fund may be subject to potential examination by U.S. federal or foreign jurisdiction authorities in the areas of income taxes. These potential examinations may include questioning the nexus of income among various tax jurisdictions and compliance with U.S. federal or foreign tax laws. The Fund's management does not expect that the total amount of unrecognized tax benefits will materially change over the next twelve months.

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

### 1. Nature of operations and summary of significant accounting policies (continued)

#### Use of Estimates

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions in determining the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Such estimates include the measurement of fair value of the note receivable from American Assurance. Actual results could differ from those estimates.

### 2. Fair value measurements

The Fund's assets recorded at fair value have been categorized based upon a fair value hierarchy as described in the Fund's significant accounting policies in Note 1.

The following table presents information about the Fund's assets measured at fair value as of December 31, 2011 (in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2011
<b>Assets</b>				
Note receivable from American Assurance, at fair value	\$ -	\$ -	\$ 48,781	\$ 48,781

The following table presents additional information about Level 3 assets measured at fair value. There were no Level 3 liabilities during the year ended December 31, 2011. Both observable and unobservable inputs may be used to determine the fair value of positions that the Fund has classified within the Level 3 category. As a result, the unrealized gains and losses for assets within the Level 3 category may include changes in fair value that were attributable to both observable and unobservable inputs.

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

### 2. Fair value measurements (continued)

Changes in Level 3 assets measured at fair value for the year ended December 31, 2011 (in thousands) were as follows:

LEVEL 3						
	Beginning Balance January 1, 2011	Realized & Unrealized Gains (Losses) (a)	Purchases	Sales and Settlements	Ending Balance December 31, 2011	Change in Unrealized Gains (Losses) for Investments still held at December 31, 2011 (b)
<b>Assets</b>						
Note receivable from American Assurance, at fair value	\$ 44,341	\$ 6,542	\$ 45,519	\$ (47,621)	\$ 48,781	\$ 3,147

(a) Realized and unrealized gains and losses are included in total investment income in the consolidated statement of operations.

(b) The change in unrealized gains (losses) for the year ended December 31, 2011 for investments still held at December 31, 2011 are reflected in unrealized gain on note receivable from American Assurance and interest income on note receivable from American Assurance in the consolidated statement of operations.

### 3. Note receivable from American Assurance

From January 1, 2011 to March 31, 2011, the Fund through its wholly owned subsidiary, Cornerstone Olaj provided a subordinate note to American Assurance. The note receivable bears interest as follows: (i) at a rate of two percent (2%) per annum beginning as of the date of the note receivable ("Fixed Interest"); (ii) at a floating amount equal to that portion of the gross profits of American Assurance for each month calculated by the ratio of the principal value of this note receivable for such month to the aggregate of (a) the principal value of this note receivable for such month and (b) the dollar amount of capital balances of the partners in American Assurance for such month, net of the Fixed Interest component ("Contingent Interest"); and (iii) both Fixed Interest and Contingent Interest are calculated on the principal value of this note receivable and any unpaid interest.

As of April 1, 2011, this note receivable has been replaced by a subordinate note provided by the Fund to American Assurance. The note payable (the "Note") bears fixed interest at a rate of two percent (2%), calculated monthly on the last day of each month based on the fair value of the principal amount of this Note and any unpaid interest at such time. The fair value of the Note shall be adjusted monthly based on gains and losses of American Assurance for such month as reflected on its regularly prepared month-end net asset value statement. This adjustment is accounted for similar to an embedded derivative feature, and as a result, the note receivable from American Assurance is accounted for at fair value. Each adjustment shall be calculated by the ratio of the aggregate of (a) the fair value of this Note and (b) any unpaid interest for such month and (c) the dollar amount of capital balances of the Class A preferred members in American Assurance for such month, net of the Fixed Interest component ("Fair Value Adjustment").

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

### 3. Note receivable from American Assurance (continued)

As of December 31, 2011, the note receivable was valued at \$48,781,186 which consists of the original principal amount of \$45,634,243, fair value adjustment of \$2,904,990 and accrued fixed interest of \$241,953. The note receivable matured on January 1, 2012 and has been renewed through July 1, 2012.

American Assurance invests in oil and gas royalty interests and in Royalty Repository II, LLC, an investment company managed by Cornerstone, which invests in oil and gas royalty and working interests and is 79.11% owned by American Assurance at December 31, 2011. As part of its investment strategy to hedge against changes in crude oil and natural gas prices, American Assurance also invests in total return swap contracts with an institutional counterparty. American Assurance values its investments in royalty interests and swap contracts at fair value. The original cost of acquisition of oil and gas royalty interests is depleted using the units-of-production method.

The following is a summary of the audited statement of financial condition and the statement of operations of American Assurance on GAAP basis as of December 31, 2011 and for the year then ended:

American Assurance 2000, L.P.  
Statement of Financial Condition  
As of December 31, 2011

**Assets**

Investment in affiliated investment company, at fair value (cost \$14,005,699)	\$ 48,554,289
Investments in oil and gas royalty interests, at fair value (cost \$9,570,995, net of accumulated depletion of \$7,766,518)	29,884,544
Derivative contracts, at fair value	809,779
Cash and cash equivalents	2,564,902
Accrued royalty income	475,000
Deferred loan fees, net	97,345
Other assets	13,424
	<u>\$ 82,399,283</u>

**Liabilities and partners' capital**

Note payable to related party (the Fund)	\$ 48,781,186
Note payable	10,852,877
Capital withdrawals payable	470,000
Accrued expenses	84,304
Partners' capital	22,210,916
	<u>\$ 82,399,283</u>

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

### 3. Note receivable from American Assurance (continued)

American Assurance 2000, L.P.  
Statement of Operations  
For the year ended December 31, 2011

Royalties income	\$ 3,116,505
Interest income	5,344
Total investment income	<u>3,121,849</u>
<b>Expenses</b>	
Unrealized gain on note payable to related party (the Fund)	3,789,942
Interest on note payable to related party (the Fund)	2,752,472
Depletion expense	794,925
Interest and loan fees	422,471
Other expenses	405,445
Total expenses	<u>8,165,255</u>
<b>Net investment loss</b>	<u>(5,043,406)</u>
Net change in unrealized appreciation on investment in affiliated investment company	5,672,107
Net realized gain on investment in affiliated investment company	191,389
Net change in unrealized appreciation on investments in oil and gas royalty interests	1,655,982
Net realized gain from derivative contracts	1,223,783
Net change in unrealized depreciation on derivative contracts	<u>(1,018,415)</u>
Net gain on investments	<u>7,724,846</u>
<b>Net income</b>	<u>\$ 2,681,440</u>

American Assurance's investments in affiliated investment company, oil and gas royalty interests, and derivative contracts, all of which are in United States, approximate 218.6%, 134.5% and 3.6%, respectively, of American Assurance's partners' capital as of December 31, 2011. American Assurance's derivative contracts consist of total return swaps in crude oil and natural gas which approximate 0.8% and 2.8%, respectively, of American Assurance's partners' capital as of December 31, 2011 with expiration dates ranging from January 2012 to December 2014.

Risks may arise from unanticipated movements in the fair value of the underlying investments in Royalty Interests by American Assurance and the lack of market liquidity to unwind the Royalty Interest positions at current fair values.

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

*(Expressed in United States Dollars)*

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### **4. Concentration of credit risk**

In the normal course of business, the Fund maintains cash balances in a U.S. based financial institution, which at times may exceed federally insured limits. U.S. cash accounts are guaranteed by the Federal Deposit Insurance Corporation up to \$250,000 per institution. The Fund is subject to credit risk to the extent any financial institution with which it conducts business is unable to fulfill contractual obligations on its behalf. Management monitors the financial condition of such financial institutions and does not anticipate any losses from these counterparties.

The Fund has a note receivable from American Assurance which is approximately 127% of the total net asset value of the Fund as of December 31, 2011.

### **5. Capital share transactions**

The authorized share capital of the Fund is 2,012,000 shares, consisting of 12,000 Founder Shares and 2,000,000 redeemable shares of \$1.00 par value each ("Investor shares"). There are 2 classes of shares: Regular Class and Restricted Class NL. Shareholders who are not subject to management and performance fees are issued Restricted Class NL shares. All other shareholders are issued Regular Class shares. All of the Founder Shares have been issued to the Manager.

Investor shares are available for subscription and redemption on the first business day of each January and July at a price equal to the net asset value per share on the last business day of the preceding month. In the event that the Fund records a loss, the Fund will issue a separate series of shares on the first business day following that month to facilitate the performance fee computation. Subsequent allocations of income to the series that have loss carryforwards are based on the loss recovery method whereby losses are recovered in reverse chronological order. The new series of shares will convert into the original series on the basis of their relative net asset values when all losses allocated to the original series have been recovered.



# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

### 5. Capital share transactions (continued)

Transactions in investor shares during the year ended December 31, 2011, and the investor shares outstanding and the net asset value ("NAV") per share as of December 31, 2011 are as follows:

	<u>Beginning Shares</u>	<u>Share Transfers/ Conversions</u>	<u>Shares Issued</u>	<u>Shares Redeemed</u>	<u>Ending Shares</u>
Regular Class	59,462.15	34,410.82	5,988.18	(28,907.48)	70,953.67
Restricted Class NL	51,800.36	(30,935.30)	-	-	20,865.06
	<u>111,262.51</u>	<u>3,475.52</u>	<u>5,988.18</u>	<u>(28,907.48)</u>	<u>91,818.73</u>
	<u>Amounts Issued</u>	<u>Amounts Transferred</u>	<u>Amounts Redeemed</u>	<u>Ending Net Assets</u>	<u>Ending NAV Per Share</u>
Regular Class	\$ 2,290,000	\$ 13,000,000	\$ (11,660,256)	\$ 28,850,473	\$ 406.61
Restricted Class NL		(13,000,000)	-	9,710,640	465.40
	<u>\$ 2,290,000</u>	<u>\$ -</u>	<u>\$ (11,660,256)</u>	<u>\$ 38,561,113</u>	

Shareholders have redemption rights which contain certain restrictions with respect to rights of redemption of shares as specified in the offering memorandum.

Redemptions payable represent amounts due to shareholders based on redemption requests effective through December 31, 2011.

### 6. Related party transactions

The Manager is entitled to a monthly management fee at the rate of 1/12 of 1% of the Fund's net assets as determined on the first day of each month. The Manager and the Investment Consultant share the management fee under the terms of a separate agreement.

In addition, the Manager is entitled to a semi-annual performance fee equal to 20% of the Fund's semi-annual net income before management fees are deducted. No performance fee shall be earned or paid with respect to any shareholder of the Fund that has a net loss (exclusive of management fees) which has not been fully recouped. Losses carried forward are adjusted for redemptions. The Manager and the Investment Consultant share the performance fee under the terms of a separate agreement.

The Manager charges the Fund for accounting, operating, and legal support. For the year ended December 31, 2011, the amount charged to the Fund was approximately \$285,000, which is included in the administrative fees and other expenses in the consolidated statement of operations. Fees payable to the Investment Manager as of December 31, 2011 of approximately \$21,000 is included in accrued expenses on the consolidated statement of assets and liabilities.

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

### 7. Regulatory matters

The Manager of American Assurance is currently undergoing a regulatory examination. In the opinion of management, the completion of this examination is not expected to have a material adverse effect on the financial condition and results of operations of the Fund.

### 8. Administrator

GlobeOp Financial Services (Cayman) Limited (the "Administrator") serves as the Fund's Administrator and performs certain administrative and clerical services on behalf of the Fund. For the year ended December 31, 2011, the administration fee charged by the Administrator amounted to approximately \$100,000.

### 9. Financial highlights

Financial highlights for the year ended December 31, 2011 are as follows:

	<b>Regular Class Shares</b>	<b>Restricted Class NL Shares</b>
Per share operating performance		
Net asset value, beginning of year	\$ 369.74	\$ 408.24
Income (loss) from investment operations:		
Net change in net assets resulting from operations	36.87	57.16
Net asset value, end of year	<u>\$ 406.61</u>	<u>\$ 465.40</u>
Total return		
Total return before performance fee	12.7 %	14.0 %
Performance fee	<u>(2.8)</u>	<u>-</u>
Total return after performance fee	<u>9.9 %</u>	<u>14.0 %</u>
Ratio of expenses to average net assets		
Operating expenses, excluding performance fee	2.0 %	1.2 %
Performance fee	<u>2.6</u>	<u>-</u>
Total expenses	<u>4.6 %</u>	<u>1.2 %</u>
Net investment income	<u>9.2 %</u>	<u>14.1 %</u>

Financial highlights are calculated for each investor class as a whole. An individual shareholder's financial highlights may vary based on the timing of capital share transactions.

# CARITAS ROYALTIES FUND (BERMUDA) LTD. AND SUBSIDIARY

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

*(Expressed in United States Dollars)*

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### 10. Subsequent events

Effective January 1, 2012, the Fund, American Assurance 2000, L.P., as well as other related entities underwent a restructuring. Pursuant to this restructuring, on January 1, 2012, the note payable by Royalty Repository II, LLC ("RRII") to Caritas Royalties Fund II (Bermuda) Ltd. ("C2BM") matured and all amounts due, including accrued interest were paid in full. Effective January 1, 2012, C2BM used these proceeds to purchase shares of the Fund, which were then distributed in-kind to shareholders of C2BM. The Fund used the proceeds from the issuance of shares to renew and increase the promissory note with American Assurance to approximately \$67,474,000 effective January 1, 2012.

Also, effective January 1, 2012, Caritas Royalty Fund II LLC ("C2US") exchanged its interest in RRII for interests in American Assurance. Subsequently, effective January 1, 2012, C2US exchanged its interest in American Assurance for interests in Caritas Royalty Fund LLC, the General Partner of American Assurance, which were then distributed in-kind to the investors in C2US.

As of January 1, 2012, RRII is wholly owned by American Assurance and RRII's open total return swap contracts and revolving credit facility with BNP Paribas have been assigned to American Assurance. Additional interests in RRII have also been obtained by American Assurance through the utilization of the increase in their revolving credit facility with BNP Paribas and promissory note with the Fund.

The net effect of the above transactions and subsequent contributions was that the Fund received capital contributions of approximately \$18,935,000 and \$10,668,000, respectively. The Fund increased the note receivable from American Assurance by approximately \$18,693,000 as of January 1, 2012 after satisfying the funding for the redemptions payable of \$9,750,000.