

CLIFFWATER^{LLC}

INVESTMENT ADVISORY SERVICES

Los Angeles • New York

Hedge Fund Operations Due Diligence Report Wexford Spectrum Funds

June 2011

Investment Due Diligence Report provided under separate cover.

Hedge Fund Operations Due Diligence Report

Firm Name:	Wexford Capital LP		
Fund Name:	Wexford Spectrum Funds		
Style:	Multi-strategy	Location:	New York, NY
Review Date:	June 30, 2011	Reviewer:	[REDACTED]

Operations Score: [REDACTED]			
1. Business Management	[REDACTED]	4. Valuation	[REDACTED]
2. Trading and Investment Operations	[REDACTED]	5. Risk Management	[REDACTED]
3. Financing and Counterparty Risk	[REDACTED]	6. Investor Related Practices	[REDACTED]

Summary

Wexford's operational back office processes and procedures have remained very stable since Cliffwater's last review in May 2010 and there has been minimal personnel turnover among the operational team. However, the manager has implemented the below operational enhancements over the past year to further strengthen its overall non-investment infrastructure:

- Wexford has added [REDACTED] as another prime brokerage relationship. [REDACTED] will be utilized mainly as an f/x prime broker in the near term, although other prime services may be added over time.
- The manager has increased the transparency it provides to investors as it has started to include FAS 157 valuation levels on its monthly exposure and attribution report.
- [REDACTED], the order management system, will be upgraded to allow the automation of the fixed income positions into the portfolio. Currently, distressed bond positions cannot be viewed in the OMS.
- Wexford has started sending portfolio data to [REDACTED] and is currently reviewing the output of the risk reports. The manager is considering providing information to investors based upon the quality and completeness of the analysis.
- The firm's compliance manual has been updated to include an employee 'pay to play' policy.

The operational scores noted above remain unchanged since the May 2010 review.

Wexford's back office team of 47 non-investment professionals has developed an institutional-quality platform to handle the wide range of products it trades. The manager has developed processes for trading, reconciliation and valuation for each security type in the portfolio. In addition, the manager has been a Registered Investment Advisor for over 10 years and is also registered with the Commodity Futures Trading Commission and with the National Futures Association. Wexford has an affiliate office in Toronto, Canada and a wholly owned subsidiary office in Tel Aviv, Israel but all its operational professionals are located in their Greenwich, CT headquarters. No material departures from best practices were identified except that the risk management process is not completely independent from the portfolio management process.

Section 1: Business Management

Score:	[REDACTED]
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Wexford meets all business management best practices which assess firm organization, compliance, investor protections and disaster recovery.

This report reflects information only through the date hereof. Our reporting relies upon the accuracy and completeness of financial and other information publicly available or provided to us by the fund manager, its professional staff, and through other references we have contacted. We have not conducted an independent verification of the information provided other than as described in this report. Our conclusions do not reflect an audit of the investment nor should they be construed as providing legal advice. Past performance does not guarantee future performance. The information contained herein is confidential commercial or financial information, the disclosure of which would cause substantial competitive harm to you, Cliffwater LLC, or the person or entity from whom the information was obtained, and may be protected from disclosure by applicable law.

Mr. Arthur Amron is a partner and serves as the General Counsel and Chief Compliance Officer. He is responsible for ensuring the fund's policies are adhered to, monitoring personal trading, and filing regulatory reports as necessary. The compliance manual was developed with the assistance of [REDACTED] and can be provided to investors for review during onsite meetings. The personal trading policy limits personal trading by employees and is governed by the Code of Ethics. There is a restricted list which includes all of the positions the funds are currently holding or may consider trading in the future. The Compliance Officer receives brokerage statements from employees and confirms that all trades have received the requisite prior written approval. All employees must certify they are in compliance with the personal trading policy on a quarterly and annual basis. The manager is also registered with the Securities and Exchange Commission, Commodity Futures Trading Commission, and the National Futures Association. Its anti-money laundering procedures conform to the standards set out in Title III of the US PATRIOT Act of 2001.

The firm maintains a comprehensive insurance package which includes a D&O and E&O policy for up to \$10 million which is primarily underwritten by [REDACTED]. The firm also has a comprehensive disaster recovery plan which includes a hot site in [REDACTED]. The plan is tested on a regular basis.

Best Practices Comparison

Organization and Governance		Yes	No
1	[REDACTED]		
2	[REDACTED]		
3	[REDACTED]		
4	[REDACTED]		
Compliance			
5	[REDACTED]		
6	[REDACTED]		
7	[REDACTED]		
8	[REDACTED]		
9	[REDACTED]		
10	[REDACTED]		
11	[REDACTED]		
12	[REDACTED]		
13	[REDACTED]		
14	[REDACTED]		
Investor Protections			
15	[REDACTED]		
16	[REDACTED]		
17	[REDACTED]		
18	[REDACTED]		
19	[REDACTED]		
20	[REDACTED]		
21	[REDACTED]		
22	[REDACTED]		
23	[REDACTED]		
24	[REDACTED]		

Disaster Recovery	
25	
26	
27	

Background

Criteria	Cliffwater Comments
Firm structure:	
Fund structure and domicile	
Compliance policies:	
Specific policies:	
Legal proceedings	

[Redacted]

[Redacted]

Regulatory authorities:

[Redacted]

[Redacted]

Systems and platforms:

[Redacted]

[Redacted]

IT staff size and turnover:

Backup procedures:

[Redacted]

[Redacted]

Business continuity and disaster recovery plan:

[Redacted]

[Redacted]

Insurance coverage:	

Section 2: Trading and Investment Operations

Score:

Wexford meets all trading and investment operations best practices which assess outside service providers, infrastructure, trading and accounting processes, counterparty monitoring, and cash management.

_____ serves as the fund’s administrator. _____ and _____ serve as the custodians and _____ serve as the prime brokers. The law firms of _____ and _____ are the domestic legal counsel and _____ serves as the offshore counsel.

The manager utilizes _____ as the order management system which interfaces with _____, the accounting system, intraday to capture trade activity. All equity, futures and fixed income trades are reconciled the day after the trade is executed. Most of the prime broker accounts are reconciled using the _____ program, an automated reconciliation tool. All over-the-counter trades are confirmed electronically via the Depository Trust & Clearing Corporation (“DTCC”).

All third party wire transfers must be approved by two designated authorized signatories, which include the partners and certain officers of the fund. The cash management team is responsible for entering the wire information into the transfer system of the custodian.

Best Practices Comparison

Outside Service Providers	Yes	No
28		
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30		
Infrastructure		
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33		
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36		
Trading Practices		
37		
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Core Accounting Processes	
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Cash, Margin, and Collateral Management	
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Entity and Contact	Onshore	Offshore
Prime Broker		
Administrator		
Audit		
Legal		
Tax		
Other (including custodian if not PB)		
Changes in providers (3 yrs)		
Any issues encountered in audit of firm or its products?		

Criteria	Cliffwater Comments
Organizational Structure:	

Control structure and oversight	
Trading team:	
Types of securities traded	
Trading practices:	
Trade flow process:	

[Redacted]

[Redacted]

Trade confirmation and reconciliation:

[Redacted]

[Redacted]

59	[Redacted]
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Background

Criteria	Cliffwater Comments
Sources of financing: [Redacted]	[Redacted]
Counterparties and terms of arrangements: [Redacted]	[Redacted]
Prime broker financing: [Redacted]	[Redacted]
Repo agreements [Redacted]	[Redacted]
ISDAs [Redacted]	[Redacted]

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Pricing Sources and FAS 157 Companies	
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Positions with No Readily Ascertainable Market Value	
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Valuation Committee	
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Background

Criteria	Cliffwater Comments
Month end closing process	

[Redacted]	[Redacted]
Valuation of exchange traded (level 1) assets: [Redacted]	[Redacted]
[Redacted]	[Redacted]
Valuation of OTC / illiquid instruments / private placement (level 2 and 3) assets [Redacted]	[Redacted]
[Redacted]	[Redacted]

Section 5: Risk Management

Score: [Progress bar showing approximately 25% completion]

Wexford meets all risk management best practices except that the risk management process is not completely independent from the portfolio management process. Robert Holtz, portfolio manager, is responsible for risk management and Charles Davidson, Chairman and CIO, has the ultimate decision making authority over the portfolio. The manager mitigates portfolio risk by maintaining a high degree of liquidity and utilizing minimal or no leverage. The portfolio is also extremely diversified and individual equity positions are generally less than 50 basis points of total assets. Exposure across names, themes and sectors are also reviewed on a regular basis. The manager is considering providing data to

Liquidity risk and funding: <div style="background-color: black; width: 100%; height: 20px;"></div>	

Section 6: Investor Related Practices

Score:

Wexford meets all disclosure and investor terms best practices. The PPM details the investment terms, fees, and conditions. The fees are calculated based on the audited financial statements and based on the dollar of value added. The lock-up and gate provisions protect the fund from having to liquidate the portfolio at a discount to meet investors redemptions.

The manager sends investors annual audited financials and monthly newsletters. Official NAVs are calculated monthly and are typically distributed to investors by [REDACTED] on or about the 20th day of each month. As noted, FAS 157 levels are now disclosed on the monthly investor report. 2010 fund expenses are approximately 39 basis points and 43 basis points for the onshore and offshore funds, respectively.

Wexford's financial statements are audited by [REDACTED]. The audited financial statements and Schedule K-1's are typically provided to investors within 90 calendar days of year end, which is slightly timelier than the industry standard.

Best Practices Comparison

Initial Disclosures	Yes	No
137		
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Fees and Expenses	
146	
147	
148	
149	
150	
151	
Ongoing Information Provided to Investors	
152	
153	
154	
155	
156	
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Financial Statement and Tax	
161	
162	
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Investor Terms	
167	
168	
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Background

Criteria	Cliffwater Comments

Criteria	Cliffwater Comments
Fund financial and tax statements:	

Meeting History

Date	Location	Cliffwater Attendees	Manager Attendees
January 6, 2010	New York, NY		Marc Leferman (IR), Celeste Jacobson (IR)
May 25, 2010	Conference Call		Celeste Jacobson (IR)
June 30, 2011	Greenwich, CT		Marc Leferman (IR), Saree Olkes (IR)

Appendix: Glossary

Administrator	A service provider such as Citco or International Fund Services that handles administrative responsibilities such as calculating the fund's NAV on a monthly basis, sending the investors performance reports, and maintaining the official books and records of the fund.
Fair Value (FAS 157)	FASB Statement No. 157, Fair Value Measurements ("FAS 157"), defines fair value as <i>"the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."</i> Cliffwater reviews valuations according to the Fair Value hierarchy established by FAS 157, the three levels of which are described below.
Level 1 assets	Liquid assets with readily observable prices, and therefore a reliable market value. Level 1 assets typically include stocks, bonds, mutual funds, and any other assets that have a regular "mark to market" pricing mechanism.

Level 2 assets	Assets with a value based on market inputs that are not directly observable on a central exchange. These assets are often priced via quotations from dealers. An example of a level 2 asset is a credit default swap which is typically priced via indicative quotations from broker dealers.
Level 3 assets	Illiquid assets with a value that cannot be determined by observable measures. The fair value of a level 3 asset can only be estimated by using significant assumptions as inputs to the valuation model. Illiquid private equity investments are an example of this type of asset.
Leverage	<p>The use of explicit debt (i.e. borrowing) or implicit debt (i.e. derivatives) to achieve investment positions that exceed invested capital (NAV), thereby amplifying return but also increasing risk. A common leverage calculation is the ratio of gross notional exposure to invested capital. For example, a \$100 investment in BP stock coupled with a \$100 short sale of Exxon stock yields gross notional exposure of \$200. Leverage in this example can be described in at least two ways:</p> <ol style="list-style-type: none"> The portfolio has 200% gross exposure (equal to \$200 gross notional exposure divided by \$100 NAV) The portfolio is one time (1x) levered (equal to \$100 in debt divided by \$100 NAV) <p>As illustrated in the example, the \$200 gross notional exposure equals the absolute value total of both \$100 long (“gross long”) and \$100 short (“gross short”) asset exposures. The measurement of gross notional exposure varies by asset class:</p> <ul style="list-style-type: none"> <i>Equities</i> – the market value of long and short positions <i>Corporate Debt and Municipal Bonds</i> – the market value of long and short positions <i>US Treasuries (and other highly rated government debt)</i> – the market value of long and short positions, adjusted to a 10 year bond equivalent maturity (approximate 9 year duration), so that a \$100 exposure to a 2 year duration bond is recognized as a lower risk compared to a \$100 20 year duration bond. The \$100 3 year duration bond is said to have a \$33 10 year bond equivalent exposure (\$100 times 3, divided by 9) while the \$100 20 year duration bond is said to have a \$222 10 year bond equivalent exposure (\$100 times 20, divided by 9) <i>Options</i> – the delta adjusted exposure rather than the total notional value of the underlying reference asset. Delta adjusted exposure represents the implied shares/holdings necessary to hedge the options position <i>Credit Default Swaps</i> – total notional exposure of the underlying reference credit <i>Interest Rate Swaps</i> – total notional exposure (expressed as 10-year bond equivalent, per the duration adjustment process described above) to reference security or index <i>Futures/Forwards</i> – total notional exposure to reference security or index
Net Asset Value (NAV)	A fund’s total assets less total liabilities.
Notional Exposure	The total dollar exposure represented by a position. Due to leverage, this amount may be greater than the equity in the position. For example, a CDS contract offering \$1 million of protection has a notional value of \$1 million even though the cost of the contract itself is likely to be a small fraction of that amount.
Gross Long	The total notional exposure of all long positions in a portfolio. Long positions benefit from increases in securities prices.
Gross Short	The total notional exposure of all short positions in a portfolio. Short positions benefit from decreases in securities prices.
Net	The difference between a portfolio’s gross long and gross short exposures. A net long position indicates a higher portion of long positions in the portfolio, and that the portfolio should generally benefit from an increase in asset prices. A net short position indicates the opposite.
Total Gross	The sum of a portfolio’s gross long and gross short exposures.
Operations Score	A measure of how well the firm meets best practice standards on a scale of A (meets all best practice standards) to F (does not meet several best practice standards). A rating of “C” or lower indicates Cliffwater believes the firm’s departure from best practices could hurt returns or lead to the misappropriation of firm assets.
Prime Broker	A prime broker custodies assets, provides settlement services, facilitates the borrowing of securities for short positions, and may provide performance reporting for hedge funds. JPMorgan, Goldman Sachs, Morgan Stanley and UBS are large prime brokers.
Side Pocket	A segregated portion of a portfolio that may be used to hold illiquid, less frequently priced securities. Once a holding is placed in a side pocket, only current investors participate in its performance. Subsequent investors do not share in the gains/losses associated with

	assets previously placed in side pockets. Performance fees are paid when side pocket investments are realized. Assets placed into side pockets are not available for withdrawal until the investments are realized.
Soft Dollars	Commission credits from trading securities that can be used to pay for research or other services that brokers provide to hedge funds and that are intended for the benefit of investors. Most funds operate under the SEC 28e safe harbor rules that restrict soft dollar use to research only.
Unencumbered Cash	Unencumbered cash is equal to cash holdings less margin requirements.