

CLIFFWATER^{LIC}

INVESTMENT ADVISORY SERVICES

Los Angeles • New York

**Hedge Fund Operations Due Diligence Report
Ascend Partners Fund II**

September 2010

Investment Due Diligence Report provided under separate cover.

Hedge Fund Operations Due Diligence Report

Firm Name:	Ascend Capital, LLC		
Fund Name:	Ascend Partners Fund II		
Style:	Equity Long/Short	Location:	New York, NY
Review Date:	September 8, 2010	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

Ascend has remained a very stable fund since Cliffwater's last onsite review in August 2009. Cliffwater also visited the fund's external administrator [REDACTED] on March 2010. Firmwide assets under management have increased from slightly over a billion to \$3 billion in the past year. Much of the new monies has flowed into separately managed accounts. The manager now has 11 managed accounts which have \$700 million in capital in total. The manager has made the following improvements in its operational practices over the past year:

- The manager changed the domicile of the offshore funds from the British Virgin Islands to the Cayman because the manager believes the Cayman now has a better tax and regulatory environment than the British Virgin Islands.
- The average daily trade volume has increased from 100 trades a day as of a year ago to 150 to 175 trades a day. The manager has adjusted to the new trade volume by automating some of their reconciliation reports.
- The manager has started to provide data to [REDACTED] to satisfy an investor reporting requirement. However, the manager does not receive any risk reporting from [REDACTED] nor use it to make any trading decisions.
- In November 2009, the manager switched from using [REDACTED] information technology group to back up all data to a new vender called [REDACTED]. [REDACTED] was founded by the former head of [REDACTED] primary facility is in Oakland and there is a secondary facility in Philadelphia.
- The manager upgraded its remote login procedures to allow employees to login via a [REDACTED] connection.

In addition, the manager received a no deficiency letter from the SEC relating to the custody audit which began in April 2009. This was an SEC sweep audit focusing on verifying the existence of assets and included sending out letters to clients and custodians. The letter was reviewed by Cliffwater [REDACTED] during the onsite due diligence visit.

Ascend's team of seven non-investment professionals effectively manages all trading and business operations and meets most all industry operational best practices. Ascend could bring its procedures fully in line with best practices by carrying professional management liability insurance including errors and omissions, performing a full reconciliation with their administrator on a daily basis rather than only at month end, and updating their valuation process to include a valuation committee and a process to note exceptions to pricing policies. In addition, the manager could separate its risk management process from its portfolio investment process. Despite these improvement areas, the middle and back office team led by Mr. Ben Slavet, CPA, is highly experienced and has an in-depth knowledge of the firm's trading strategy.

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.

Section 1: Business Management

Score:

Ascend meets all best practices which assess firm organization, compliance, investor protections and disaster recovery. One exception is that it does not carry professional liability insurance including an errors and omissions policy. The CFO has looked into purchasing insurance and has determined that given the cost of insurance and the level of protection, the fund is better off self-insuring.

Mr. Slavet is the manager's Chief Compliance Officer. The fund is registered with the SEC and, thus, has document retention policies, soft dollar procedure, and anti-money laundering screenings as required. There are no past or pending regulatory investigations or sanctions involving Ascend. Personal trading is heavily monitored. Employee must pre-clear trades by submitting the Securities Trading Pre-Approval Form from the Code of Ethics. The CCO receives all statements and checks them against clearance forms at least quarterly.

All hardware and software essential to the fund's daily operations are replicated at a co-location facility maintained by [REDACTED]. The firm's disaster recovery plan is comprehensive and includes a hot site in Texas on a separate power grid. Most employees have VPN access to all applications and servers essential to their business so that they can operate at a remote location. VPN access is backed up by extensive use of cell phones and PDA handhelds.

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	[Redacted]
26	[Redacted]
27	[Redacted]

Background

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

[Redacted]	
Regulatory authorities: [Redacted]	[Redacted]
Systems and platforms: [Redacted]	[Redacted]
[Redacted]	[Redacted]
Backup procedures: [Redacted]	[Redacted]
Business continuity and disaster recovery plan: [Redacted]	[Redacted]
Insurance coverage: [Redacted]	[Redacted]

Section 2: Trading and Investment Operations

Score: [Progress Bar]

Ascend meets all trading and investment operations best practices which assess outside service providers, infrastructure, trading and accounting processes, counterparty monitoring, and cash management except that it does not fully reconcile with its administrator on a daily basis. Even though it

departs from this best practice by reconciling only at month end, the increase to operational risk is greatly mitigated because all trading activity is reconciled between the fund and the administrator on a daily basis (only positions, cash, and accruals are reconciled on a weekly or monthly basis.)

Portland, Maine-based [REDACTED] serves as the funds' administrator. [REDACTED] are the prime brokers. Ascend retains the law firm of [REDACTED] to advise them as needed.

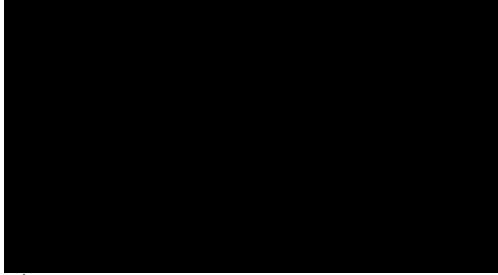
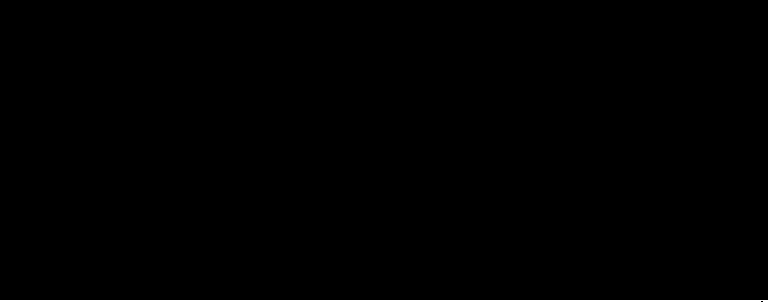


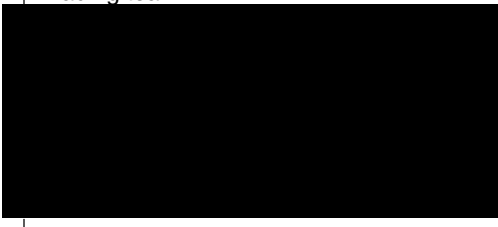

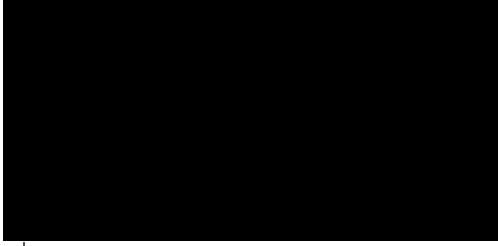

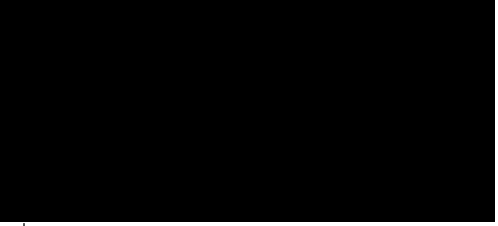

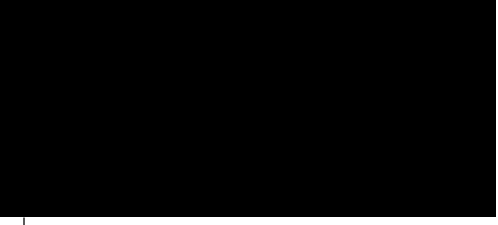

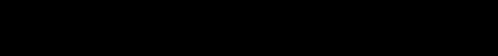



There are three execution only traders and they enter all trades into [REDACTED] a widely used trade entry tool, immediately after a trade is executed. Trade information is transmitted to executing brokers through direct real-time feeds using [REDACTED] order management system and [REDACTED] connections. The manager trades mainly listed equities, but also have some convertible bonds, total return swaps, and options. These products have standardized terms so there are rarely any trade breaks, and the accounting group is able to reconcile all trading activity with the prime brokers and the administrator the morning after every trade is executed.

Best Practices Comparison

Outside Service Providers		Yes	No
28	[REDACTED]		
29	[REDACTED]		
30	[REDACTED]		
Infrastructure			
31	[REDACTED]		
32	[REDACTED]		
33	[REDACTED]		
34	[REDACTED]		
35	[REDACTED]		
36	[REDACTED]		
Trading Practices			
37	[REDACTED]		
38	[REDACTED]		
39	[REDACTED]		
40	[REDACTED]		
41	[REDACTED]		
42	[REDACTED]		
43	[REDACTED]		
44	[REDACTED]		
45	[REDACTED]		
Core Accounting Processes			
46	[REDACTED]		
47	[REDACTED]		
48	[REDACTED]		
49	[REDACTED]		
50	[REDACTED]		

51	[REDACTED]
Cash, Margin, and Collateral Management	
52	[REDACTED]
53	[REDACTED]
54	[REDACTED]
55	[REDACTED]
56	[REDACTED]

Entity and Contact	Onshore	Offshore
Prime Broker	[REDACTED]	[REDACTED]
Administrator	[REDACTED]	[REDACTED]
Audit	[REDACTED]	[REDACTED]
Legal	[REDACTED]	[REDACTED]
Tax	[REDACTED]	[REDACTED]
Other (including custodian if not PB)	[REDACTED]	[REDACTED]
Changes in providers (3 yrs)	[REDACTED]	[REDACTED]
Any issues encountered in audit of firm or its products?	[REDACTED]	[REDACTED]

Criteria	Cliffwater Comments
Organizational Structure: 	
Control structure and oversight 	
Trading team: 	
	
Trading practices: 	
Trade flow process: 	
Trade confirmation and reconciliation: 	
Specialized groups 	
Reconciliation process with administrator: 	

Cash movements:	

Section 3: Financing and Counterparty Risk

Score:

Ascend meets all financing and counterparty monitoring best practices which assess how the manager finances its portfolio and manages its cash.

Ascend takes a very conservative approach to financing and the fund has maintained a defensive balance sheet which helped the firm avoid the funding and liquidity issues faced by other funds during the credit crisis. The funds major sources of financing are margin financing from prime brokers and use of derivative contracts governed by ISDA master agreements. The fund does not use repurchase agreements to finance assets nor does it manage any special purpose vehicles, CDOs, or other long-term financing structures. The firm has six ISDA master agreements in place and is in the process of negotiating more to further diversity its counterparty exposure.

Best Practices Comparison

Financing and Counterparty Risk		Yes	No
57			
58			
59			
60			
61			
62			
63			
64			
65			

Background

Criteria	Cliffwater Comments
Sources of financing:	
Counterparties and terms of arrangements:	
Prime broker financing:	

Repo agreements	
ISDAs	
Other (i.e. CDOs, debt offerings, etc.)	

Section 4: Valuation

Score:

Ascend meets all valuation best practices except that it does not have a valuation committee to review all month end valuations, and its valuation policy does not establishes appropriate procedures for recording any material pricing exceptions and the reason for the exception. Per the CFO, the fund has not established a valuation committee because over 99% of its portfolio is priced via third party pricing services such as [REDACTED] or by multiple broker dealer quotations. As of August 31, 2010, the fund anticipated to have 30 basis points of the funds' value categorized as level 3 assets under FAS 157. The fund does not allow side pockets and the portfolio manager and the chief financial officer review the valuation of any privately held security if needed. Ascend's Chief Financial Officer is knowledgeable about Ascend's trading strategy and works independently from the portfolio managers. He personally reviews the valuations of the 200 to 300 positions which are part of the portfolio at every month end.

Best Practices Comparison

Valuation Personnel		Yes	No
66			
67			
Valuation Policy			
68			
69			
70			
71			
72			
73			
74			
75			
76			
77			

78	[REDACTED]
Pricing Sources and FAS 157 Companies	
79	[REDACTED]
80	[REDACTED]
81	[REDACTED]
82	[REDACTED]
83	[REDACTED]
84	[REDACTED]
85	[REDACTED]
86	[REDACTED]
87	[REDACTED]
88	[REDACTED]
Positions with No Readily Ascertainable Market Value	
89	[REDACTED]
90	[REDACTED]
91	[REDACTED]
92	[REDACTED]
93	[REDACTED]
94	[REDACTED]
Valuation Committee	
95	[REDACTED]
96	[REDACTED]
97	[REDACTED]
98	[REDACTED]
99	[REDACTED]
100	[REDACTED]
101	[REDACTED]
102	[REDACTED]
103	[REDACTED]
104	[REDACTED]
105	[REDACTED]
106	[REDACTED]
107	[REDACTED]
108	[REDACTED]
109	[REDACTED]

Background

Criteria	Cliffwater Comments
Month end closing process [REDACTED]	[REDACTED]
Valuation of exchange traded (level 1) assets: [REDACTED]	[REDACTED]

Valuation of OTC / illiquid instruments / private placement (level 2 and 3) assets	
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Section 5: Risk Management

Score:

Ascend meets all risk management best practices except that it does not have an independent risk manager and its risk management process is not separate from the portfolio management process.

CIO Malcolm Fairbairn is in charge of the risk management process. He uses an in-house proprietary system and [REDACTED] risk system. The fund also gives some risk data to [REDACTED] to satisfy an investor requirement but the fund does not receive any risk reporting from [REDACTED]. The fund does not have any hard risk limits or stop loss requirements, but it does have several soft limits. Specifically, position sizes are determined based on several factors, including level of conviction, the beta of stock, and the timing of events and liquidity. Long positions generally range from 0.50% to 7.00%. Short positions generally range from 0.25% to 4.00%. Generally, net exposure to any one sector will not exceed 10% in Ascend Partners Fund I and 15% in Ascend Partners Fund II.

Best Practices Comparison

Structure		Yes	No
110	[REDACTED]		
111	[REDACTED]		
112	[REDACTED]		
113	[REDACTED]		
114	[REDACTED]		
115	[REDACTED]		
116	[REDACTED]		
117	[REDACTED]		
118	[REDACTED]		
119	[REDACTED]		
Risk Manager			
120	[REDACTED]		
121	[REDACTED]		
122	[REDACTED]		
123	[REDACTED]		
124	[REDACTED]		
125	[REDACTED]		
Risk Limits and Testing			
126	[REDACTED]		
127	[REDACTED]		
128	[REDACTED]		

129	
130	
131	
Leverage and Liquidity Risk	
132	
133	
134	
135	
136	

Background

Criteria	Cliffwater Comments
Structure of risk management group: [Redacted]	[Redacted]
Liquidity risk and funding: [Redacted]	[Redacted]

Section 6: Investor Related Practices

Score: [Progress Bar]

Ascend 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 fund is very transparent and frequently communicates with investors. Weekly performance estimates are sent every Monday. On the first business day after each month end, a monthly estimate is sent to investors. Capital account statements, a summary risk report showing exposures and risks, and performance attribution is usually sent to investors by the fifteenth business day after every month end. The CIO also sends a quarterly commentary letter.

Ascend's financial statements are audited by [Redacted] and audited financial statements are sent to investors by the end of February, which is well ahead of the industry average. Schedule K-1 tax information is usually sent to investors on a very timely basis, usually in March.

Best Practices Comparison

Initial Disclosures		Yes	No
137			
138			
139			
140			
141			
142			
143			
144			
145			
Fees and Expenses			
146			
147			
148			
149			
150			
151			
Ongoing Information Provided to Investors			
152			
153			
154			
155			
156			
157			
158			
159			
160			
Financial Statement and Tax			
161			
162			
163			
164			
165			
166			
Investor Terms			
167			
168			
169			
170			

Background

Criteria	Cliffwater Comments
Fund financial and tax statements:	

Meeting History

Date	Location	Cliffwater Attendees	Manager Attendees
November 17, 2008	San Francisco		Benjamin Slavet, CPA (CFO)
August 18, 2009	San Francisco		Ben Slavet, CFA (CFO), Ramona Shenoy (Controller)
September 8, 2010	San Francisco		Ben Slavet, CFA (CFO), Ramona Shenoy (Controller)

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. Mortgage-backed securities are an example of this type of asset.
Leverage	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

	<p>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.