

Fortress Investment Group LLC
Form 10-Q
November 13, 2008

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

- þ** **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2008
- or**
- o** **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission File Number: 001-33294

Fortress Investment Group LLC
(Exact name of registrant as specified in its charter)

Delaware
*(State or other jurisdiction of
incorporation or organization)*

20-5837959
*(I.R.S. Employer
Identification No.)*

**1345 Avenue of the Americas,
New York, NY**
(Address of principal executive offices)

10105
(Zip Code)

(212) 798-6100
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes **þ** No **o**

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒ Smaller reporting company ☐
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the last practicable date.

Class A Shares: 94,609,525 outstanding as of November 12, 2008.

Class B Shares: 312,071,550 outstanding as of November 12, 2008.

FORTRESS INVESTMENT GROUP LLC

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DEFINED TERMS

As used in this Quarterly Report on Form 10-Q, unless the context otherwise requires:

Management Fee Paying Assets Under Management, or AUM, refers to the management fee paying assets we manage, including, as applicable, capital we have the right to call from our investors pursuant to their capital commitments to various funds. Our AUM equals the sum of:

- (i) the capital commitments or invested capital (or NAV, if lower) of our private equity funds, depending on which measure management fees are being calculated upon at a given point in time, which in connection with funds raised after March 2006 includes the mark-to-market value of public securities held within the funds;
- (ii) the contributed capital of our publicly traded alternative investment vehicles, which we refer to as our Castles ;
- (iii) the net asset value, or NAV, of our hedge funds; and
- (iv) the NAV of our managed accounts, to the extent management fees are charged.

For each of the above, the amounts exclude assets under management for which we charge either no or nominal fees, generally related to our principal investments in funds as well as investments in funds by our principals, directors and employees.

Our calculation of AUM may differ from the calculations of other asset managers and, as a result, this measure may not be comparable to similar measures presented by other asset managers. Our definition of AUM is not based on any definition of assets under management contained in our operating agreement or in any of our Fortress Fund management agreements.

Fortress, we, us, our, and the company refer, (i) following the consummation of the reorganization and the Nomura transaction on January 17, 2007, collectively, to Fortress Investment Group LLC and its subsidiaries, including the Fortress Operating Group and all of its subsidiaries, and, (ii) prior to the consummation of the reorganization and the Nomura transaction on January 17, 2007, to the Fortress Operating Group and all of its subsidiaries, in each case not including funds that, prior to March 31, 2007, were consolidated funds, except with respect to our historical financial statements and discussion thereof unless otherwise specified. Effective March 31, 2007, all of our previously consolidated funds were deconsolidated. The financial statements contained herein represent consolidated financial statements of Fortress Investment Group LLC subsequent to the reorganization and combined financial statements of Fortress Operating Group, considered the predecessor, prior to the reorganization. See Part I, Item 1, Financial Statements.

Fortress Funds and our funds refers to the private investment funds and alternative asset companies that are managed by the Fortress Operating Group.

Fortress Operating Group refers to the combined entities, which were wholly-owned by the principals prior to the Nomura transaction and in each of which Fortress Investment Group LLC acquired an indirect controlling interest upon completion of the Nomura transaction.

principals or Principals refers to Peter Briger, Wesley Edens, Robert Kauffman, Randal Nardone and Michael Novogratz, collectively, who prior to the completion of our initial public offering and the Nomura transaction directly owned 100% of the Fortress Operating Group units and following completion of our initial public offering and the Nomura transaction own a majority of the Fortress Operating Group units and all of the Class B shares, representing a

majority of the total combined voting power of all of our outstanding Class A and Class B shares. The principals ownership percentage is subject to change based on, among other things, equity offerings by Fortress and dispositions by the principals.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some of the statements under Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations, Part I, Item 3, Quantitative and Qualitative Disclosures About Market Risk, Part II, Item 1A, Risk Factors, and elsewhere in this Quarterly Report on Form 10-Q may contain forward-looking statements which reflect our current views with respect to, among other things, future events and financial

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performance. Readers can identify these forward-looking statements by the use of forward-looking words such as outlook, believes, expects, potential, continues, may, will, should, seeks, approximately, predicts, estimates, anticipates or the negative version of those words or other comparable words. Any forward-looking statements contained in this report are based upon the historical performance of us and our subsidiaries and on our current plans, estimates and expectations. The inclusion of this forward-looking information should not be regarded as a representation by us or any other person that the future plans, estimates or expectations contemplated by us will be achieved. Such forward-looking statements are subject to various risks and uncertainties and assumptions relating to our operations, financial results, financial condition, business prospects, growth strategy and liquidity. If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, our actual results may vary materially from those indicated in these statements. These factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included in this report. We do not undertake any obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

CONSOLIDATED BALANCE SHEETS (Unaudited)
(Dollars in thousands, except share data)

	September 30, 2008	December 31, 2007
ASSETS		
Cash and cash equivalents	\$ 259,252	\$ 100,409
Due from affiliates	49,429	198,669
Investments		
Equity method investees	949,709	1,091,918
Options in affiliates	137	16,001
Deferred tax asset	517,578	511,204
Other assets	78,772	71,580
	\$ 1,854,877	\$ 1,989,781
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities		
Accrued compensation and benefits	\$ 146,702	\$ 269,324
Due to affiliates	395,508	455,734
Dividends payable		21,285
Deferred incentive income	163,635	173,561
Debt obligations payable	750,000	535,000
Other liabilities	57,726	36,729
	1,513,571	1,491,633
Commitments and Contingencies		
Principals and Others Interests in Equity of Consolidated Subsidiaries	174,854	308,023
Shareholders Equity		
Class A shares, no par value, 1,000,000,000 shares authorized, 94,609,525 and 94,597,646 shares issued and outstanding at September 30, 2008 and December 31, 2007, respectively		
Class B shares, no par value, 750,000,000 shares authorized, 312,071,550 shares issued and outstanding		
Paid-in capital	538,619	384,700
Retained earnings (accumulated deficit)	(373,004)	(193,200)

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Accumulated other comprehensive income (loss)	837	(1,375)
	166,452	190,125
	\$ 1,854,877	\$ 1,989,781

See notes to consolidated and combined financial statements

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

CONSOLIDATED AND COMBINED STATEMENTS OF OPERATIONS (Unaudited)
(Dollars in thousands, except share data)

	Three Months Ended		Nine Months Ended September 30,	
	September 30,	September 30,	September 30,	September 30,
	2008	2007	2008	2007
Revenues				
Management fees				
from affiliates	\$ 154,266	\$ 124,991	\$ 447,928	\$ 286,956
Incentive income				
from affiliates	718	106,690	56,162	283,879
Other revenues				
(affiliate portion				
disclosed in Note 6)	30,152	15,601	70,022	51,866
Interest and dividend				
income investment				
company holdings				
Interest income				243,713
Interest income from				
controlled affiliate				
investments				4,707
Dividend income				7,436
Dividend income				
from controlled				
affiliate investments				53,174
	185,136	247,282	574,112	931,731
Expenses				
Interest expense				
Investment company				
holdings				132,620
Other	9,481	7,285	29,705	26,016
Compensation and				
benefits	134,774	101,703	399,253	507,003
Principals agreement				
compensation	239,976	232,048	714,710	612,981
General,				
administrative and				
other	23,536	17,412	59,852	80,320
Depreciation and				
amortization	2,437	2,230	7,309	6,423
	410,204	360,678	1,210,829	1,365,363

**Other Income
(Loss)**Gains (losses) from
investmentsInvestment company
holdings

Net realized gains (losses)				86,264
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Net realized gains (losses) from controlled affiliate investments				715,024
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Net unrealized gains (losses)				(19,928)
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Net unrealized gains (losses) from controlled affiliate investments				(1,428,837)
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Other investments Net realized gains (losses)	(2,477)	777	(803)	831
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Net realized gains (losses) from affiliate investments	(671)	(2,475)	(516)	143,017
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Net unrealized gains (losses)		(1,921)		(2,597)
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Net unrealized gains (losses) from affiliate investments	(6,951)	(54,579)	(43,352)	(221,745)
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Earnings (losses) from equity method investees	(37,921)	(30,716)	(113,550)	(23,289)
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	(48,020)	(88,914)	(158,221)	(751,260)
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**Income (Loss)
Before Deferred
Incentive Income,
Principals and
Others Interests in
Income of
Consolidated**

Subsidiaries and Income Taxes	(273,088)	(202,310)	(794,938)	(1,184,892)
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Deferred incentive income				307,034
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Principals and others interests in (income) loss of consolidated subsidiaries	210,012	152,534	612,692	854,550
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Income (Loss)				
Before Income Taxes				
	(63,076)	(49,776)	(182,246)	(23,308)
Income tax benefit (expense)	5,636	12,219	333	(7,237)
Net Income (Loss)	\$ (57,440)	\$ (37,557)	\$ (181,913)	\$ (30,545)
Dividends declared per Class A share				
	\$	\$ 0.2250	\$ 0.4500	\$ 0.6174
Earnings Per Unit Fortress Operating Group				
January 1 through January 16				
Net income per Fortress Operating Group unit			\$	0.36
Weighted average number of Fortress Operating Group units outstanding				
367,143,000				
Earnings Per Class A share Fortress Investment Group				
January 17 through September 30				
Net income (loss) per Class A share, basic	\$ (0.61)	\$ (0.41)	\$ (1.96)	\$ (1.83)
Net income (loss) per Class A share, diluted	\$ (0.66)	\$ (0.52)	\$ (1.97)	\$ (1.83)
Weighted average number of Class A shares outstanding, basic				
	94,938,434	94,894,636	94,915,666	91,255,519
Weighted average number of Class A shares outstanding, diluted				
	407,009,984	406,966,186	406,987,216	91,255,519

See notes to consolidated and combined financial statements

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

CONSOLIDATED AND COMBINED STATEMENT OF SHAREHOLDERS EQUITY (Unaudited)
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2008
(Dollars in thousands)

	Class A	Class B	Paid-In	Retained Earnings	Accumulated Other	Total
	Shares	Shares	Capital	(Accumulated Deficit)	Comprehensive Income (Loss)	Shareholders Equity
Shareholders Equity December 31, 2007	94,597,646	312,071,550	\$ 384,700	\$ (193,200)	\$ (1,375)	\$ 190,125
Director restricted share grant	11,879		244			244
Dividends declared			(42,572)			(42,572)
Capital increase related to equity-based compensation			198,503			198,503
Dividend and distribution equivalents accrued in connection with equity-based compensation (net of tax)			(2,256)			(2,256)
Cumulative effect adjustment adoption of SFAS 159 (Note 3)				2,109	1,212	3,321
Comprehensive income (loss) (net of tax)						
Net income (loss)				(181,913)		(181,913)
Foreign currency translation					(787)	(787)
Comprehensive income (loss) from equity method investees					333	333
Allocation to Principals and others interests in equity of consolidated subsidiaries					1,454	1,454
Total comprehensive income (loss)						(180,913)
Shareholders Equity September 30, 2008	94,609,525	312,071,550	\$ 538,619	\$ (373,004)	\$ 837	\$ 166,452

See notes to consolidated and combined financial statements

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

CONSOLIDATED AND COMBINED STATEMENT OF CASH FLOWS (Unaudited)
(Dollars in thousands)

	Nine Months Ended September 30,	
	2008	2007
Cash Flows From Operating Activities		
Net income (loss)	\$ (181,913)	(30,545)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities		
Depreciation and amortization	7,309	6,423
Other amortization and accretion	3,401	1,876
(Earnings) losses from equity method investees	113,550	23,289
Distributions of earnings from equity method investees	9,386	9,765
(Gains) losses from investments	44,671	727,971
Deferred incentive income	(36,003)	(355,381)
Principals and others interests in income (loss) of consolidated subsidiaries	(612,692)	(854,550)
Deferred tax (benefit) expense	(8,297)	(16,775)
Options received from affiliates		(2,006)
Assignments of options to employees		4,627
Equity-based compensation	853,861	713,850
Cash flows due to changes in		
Cash held at consolidated subsidiaries and restricted cash		(166,199)
Due from affiliates	90,724	214,558
Receivables from brokers and counterparties and other assets	(13,052)	(23,024)
Accrued compensation and benefits	(93,466)	92,475
Due to affiliates	(50)	(6,392)
Deferred incentive income	26,077	
Due to brokers and counterparties and other liabilities	30,076	118,098
Investment company holdings		
Purchases of investments		(5,105,865)
Proceeds from sale of investments		3,398,739
Net cash provided by (used in) operating activities	233,582	(1,249,066)
Cash Flows From Investing Activities		
Purchase of other loan and security investments		(10,578)
Proceeds from sale of other loan and security investments		317
Contributions to equity method investees	(135,036)	(410,447)
Distributions of capital from equity method investees	211,162	115,190
Proceeds from sale of equity method investments		29,071
Cash received on settlement of derivatives		132
Purchase of fixed assets	(9,120)	(8,907)
Proceeds from disposal of fixed assets	53	2,532

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Net cash provided by (used in) investing activities	67,059	(282,690)
Cash Flows From Financing Activities		
Borrowings under debt obligations	450,000	1,999,070
Repayments of debt obligations	(235,000)	(2,010,025)
Payment of deferred financing costs	(5,020)	(6,813)
Issuance of Class A shares to Nomura		888,000
Issuance of Class A shares in initial public offering		729,435
Costs related to initial public offering		(76,766)
Dividends and dividend equivalents paid	(81,026)	(43,237)
Fortress Operating Group capital distributions to Principals		(219,112)
Purchase of Fortress Operating Group units from Principals		(888,000)
Principals and others interests in equity of consolidated subsidiaries contributions	145	3,183,792
Principals and others interests in equity of consolidated subsidiaries distributions	(270,897)	(1,916,216)
Net cash provided by (used in) financing activities	(141,798)	1,640,128
Net Increase (Decrease) in Cash and Cash Equivalents	158,843	108,372
Cash and Cash Equivalents, Beginning of Period	100,409	61,120
Cash and Cash Equivalents, End of Period	\$ 259,252	\$ 169,492
Supplemental Disclosure of Cash Flow Information		
Cash paid during the period for interest (excluding interest paid by master funds while such funds were consolidated of \$85.1 million in 2007)	\$ 26,084	70,003
Cash paid during the period for income taxes	\$ 7,184	30,158
Supplemental Schedule of Non-cash Investing and Financing Activities		
Employee compensation invested directly in subsidiaries	\$ 22,861	59,403
Investments of receivable amounts into Fortress Funds	\$ 59,133	149,825
Dividends, dividend equivalents and Fortress Operating Group unit distributions declared but not yet paid	\$	43,009
Fortress Operating Group pre-IPO distributions of investments to Principals	\$	196,764
Fortress Operating Group pre-IPO distributions of investments to employees	\$	23,338
See Note 1 regarding the non-cash deconsolidation transaction in 2007		

See notes to consolidated and combined financial statements

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**FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)**

**NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)**

1. ORGANIZATION AND BASIS OF PRESENTATION

Fortress Investment Group LLC (the Registrant, or, together with its subsidiaries, Fortress) is a global alternative asset management firm whose predecessor was founded in 1998. Its primary business is to sponsor the formation of, and provide investment management services for, various investment funds and companies (the Fortress Funds). Fortress generally makes principal investments in these funds.

Fortress has three primary sources of income from the Fortress Funds: management fees, incentive income, and investment income on its principal investments in the funds. The Fortress Funds fall into the following business segments in which Fortress operates:

1) Private equity funds:

a) Funds which make significant, control-oriented investments in debt and equity securities of public or privately held entities; and

b) Publicly traded alternative investment vehicles that Fortress refers to as the Castles, which are companies that invest primarily in real estate and real estate related debt investments.

2) Hedge funds:

a) Liquid hedge funds, which invest globally in fixed income, currency, equity and commodity markets, and their related derivatives; and

b) Hybrid hedge funds, which invest globally in diversified assets, opportunistic lending situations and securities through the capital structure, as well as investment funds managed by external managers.

3) Principal investments in the above described funds.

2007 Reorganization of Fortress Operating Group

Fortress Investment Group LLC was formed on November 6, 2006 for the purpose of becoming the general partner of Fortress Operating Group, completing the Nomura Transaction (described below), and effecting a public offering of shares and related transactions (the Transactions) in order to carry on the business of its predecessor, Fortress Operating Group, as a publicly traded entity. The Registrant is a limited liability company and its members are not responsible for any of its liabilities beyond the equity they have invested. Fortress's formation documents allow for an indefinite life.

In December 2006, the Principals entered into a securities purchase agreement with Nomura Investment Managers U.S.A., Inc., or Nomura (whose ultimate parent is Nomura Holdings, Inc., a Japanese corporation). On January 17, 2007, Nomura completed the transaction (the Nomura Transaction) by purchasing 55,071,450 Class A shares of the Registrant for \$888 million and the Registrant, in turn, purchased 55,071,450 Fortress Operating Group units, which

then represented 15% of Fortress Operating Group's economic interests, from the Principals for \$888 million.

On February 8, 2007, the Registrant completed an initial public offering (IPO) of 39,428,900 of its Class A shares for net proceeds of approximately \$652.7 million.

The accompanying consolidated and combined financial statements include the following:

subsequent to Fortress's reorganization and the inception of operations of Fortress Investment Group LLC on January 17, 2007, the accounts of Fortress Investment Group LLC and its consolidated subsidiaries, and

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**FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)**

**NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)**

prior to such reorganization and the inception of operations of Fortress Investment Group LLC, the accounts of eight affiliated entities under common control and management (Fortress Operating Group or the predecessor) and their respective consolidated subsidiaries. Each of the eight entities was owned either directly or indirectly by its members, Peter Briger, Wesley Edens, Robert Kauffman, Randal Nardone, and Michael Novogratz (the Principals).

2007 Consolidation and Deconsolidation of Fortress Funds

Certain of the Fortress Funds were consolidated into Fortress prior to the Transactions, notwithstanding the fact that Fortress has only a minority economic interest in these funds. Consequently, Fortress' s financial statements reflected the assets, liabilities, revenues, expenses and cash flows of the consolidated Fortress Funds on a gross basis through the date of their deconsolidation. The majority ownership interests in these funds, which are not owned by Fortress, were reflected as Principals' and others' interests in equity of consolidated subsidiaries in the accompanying financial statements during periods in which such funds were consolidated. The management fees and incentive income earned by Fortress from the consolidated Fortress Funds were eliminated in consolidation; however, Fortress' s allocated share of the net income from these funds was increased by the amount of these eliminated fees. Accordingly, the consolidation of these Fortress Funds had no net effect on Fortress' s earnings from the Fortress Funds.

Following the IPO, each Fortress subsidiary that acts as a general partner of a consolidated Fortress Fund granted rights, effective March 31, 2007, to the investors in the fund to provide that a simple majority of the fund' s unrelated investors are able to liquidate the fund, without cause, in accordance with certain procedures, or to otherwise have the ability to exert control over the fund. The granting of these rights has led to the deconsolidation of the Fortress Funds from Fortress' s financial statements as of March 31, 2007. The deconsolidation of the Fortress Funds has had significant effects on many of the items within these financial statements but has had no net effect on net income or equity. Since the deconsolidation did not occur until March 31, 2007, the statement of operations and the statement of cash flows for the nine months ended September 30, 2007 are presented with these funds on a consolidated basis for the period prior to the deconsolidation. The unaudited pro forma effects of the deconsolidation on these financial statements are described in Note 12 in order to provide more comparable information to 2008.

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**FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)**

**NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)**

Financial Statement Guide

Selected Financial Statement Captions	Note Reference	Explanation
<u>Balance Sheet</u>		
Due from Affiliates	6	Generally, management fees and incentive income earned from Fortress Funds which are expected to be received in the short term.
Investments in Equity Method Investees	3	The carrying value of Fortress's principal investments in the Fortress Funds.
Options in Affiliates	3	The fair value of common stock options received from the Castles.
Deferred Tax Asset	5	Relates to tax benefits expected to be realized in the future.
Due to Affiliates	6	Generally, amounts due to the Principals related to their interests in Fortress Operating Group and the tax receivable agreement.
Deferred Incentive Income	2	Incentive income already received from certain Fortress Funds based on past performance, which is subject to contingent repayment based on future performance.
Debt Obligations Payable	4	The balance outstanding on the credit agreement.
Principals and Others Interests in Equity of Consolidated Subsidiaries	6	The GAAP basis of the Principals' ownership interests in Fortress Operating Group as well as employees' ownership interests in certain subsidiaries.

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)

Selected Financial Statement Captions	Note Reference	Explanation
<u>Income Statement</u>		
Management Fees from Affiliates	2	Fees earned for managing Fortress Funds, generally determined based on the size of such funds.
Incentive Income from Affiliates	2	Income earned from Fortress Funds, based on the performance of such funds.
Compensation and Benefits	7	Includes equity-based, profit-sharing and other compensation to employees.
Principals Agreement Compensation	N/A	As a result of the principals agreement, the value of a significant portion of the Principals equity in Fortress prior to the Nomura Transaction is being recorded as an expense over a five year period. Fortress is not a party to this agreement. It is an agreement between the Principals to further incentivize them to remain with Fortress. This GAAP expense has no economic effect on Fortress or its shareholders.
Gains (Losses) from Other Investments	N/A	Subsequent to the IPO, the result of asset dispositions or changes in the fair value of assets which are marked to market (primarily the Castles).
Earnings (Losses) from Equity Method Investees	3	Fortress's share of the net earnings (losses) of Fortress Funds resulting from its principal investments.
Principals and Others Interests in (Income) Loss of Consolidated Subsidiaries	6	Primarily the Principals and employees share of Fortress's earnings based on their ownership interests in subsidiaries, including Fortress Operating Group. This amount is recorded in order to provide a net income (loss) which relates only to Fortress's Class A shareholders.
Income Tax Benefit (Expense)	5	The net tax result related to the current period. Certain of Fortress's revenues are not subject to taxes because they do not flow through taxable entities. Furthermore, Fortress has significant permanent differences between its GAAP and

Earnings Per Share	8	tax basis earnings. GAAP earnings per share based on Fortress's capital structure, which is comprised of outstanding and unvested equity interests, including interests which participate in Fortress's earnings, at both the Fortress and subsidiary levels.
	8	

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Selected Financial Statement Captions	Note Reference	Explanation
<u>Other</u>		
Distributions	8	A summary of dividends and distributions, and the related outstanding shares and units, is provided.
Distributable Earnings	10	A presentation of our financial performance by segment (fund type) is provided, on the basis of the operating performance measure used by Fortress's management committee.

The accompanying consolidated and combined financial statements and related notes of Fortress have been prepared in accordance with accounting principles generally accepted in the United States for interim financial reporting and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared under U.S. generally accepted accounting principles have been condensed or omitted. In the opinion of management, all adjustments considered necessary for a fair presentation of Fortress's financial position, results of operations and cash flows have been included and are of a normal and recurring nature. The operating results presented for interim periods are not necessarily indicative of the results that may be expected for any other interim period or for the entire year. These financial statements should be read in conjunction with Fortress's consolidated and combined financial statements for the year ended December 31, 2007 and notes thereto included in Fortress's annual report on Form 10-K filed with the Securities and Exchange Commission. Capitalized terms used herein, and not otherwise defined, are defined in Fortress's consolidated and combined financial statements for the year ended December 31, 2007.

Certain prior period amounts have been reclassified to conform to the current period's presentation.

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2. MANAGEMENT AGREEMENTS AND FORTRESS FUNDS***Management Fees and Incentive Income***

Fortress recognized management fees and incentive income as follows:

		Three Months Ended September 30,		Nine Months Ended September 30,	
		2008	2007	2008	2007(A)
Private Equity Funds					
Management fees	affil.	\$ 44,221	\$ 35,064	\$ 128,626	\$ 97,358
Incentive income	affil.	509	105,632	38,684	317,574
Castles					
Management fees	affil.	12,755	12,256	38,828	35,251
Management fees, options	affil.				2,006
Incentive income	affil.		691	12	18,596
Hedge Funds					
Liquid Hedge Funds					
Management fees	affil.	59,530	44,319	169,721	112,381
Incentive income	affil.	47	(640)	16,885	157,559
Management fees	non-affil.(B)	110	32	246	311
Incentive income	non-affil.(B)	36	431	240	431
Hybrid Hedge Funds					
Management fees	affil.	37,760	33,352	110,753	93,032
Incentive income	affil.	162	1,007	581	1,832
Management fees	non-affil.(B)	270	24	730	83
Incentive income	non-affil.(B)	13,094		13,094	
Total					
Management fees	affil.	\$ 154,266	\$ 124,991	\$ 447,928	\$ 340,028
Incentive income	affil.(C)	\$ 718	\$ 106,690	\$ 56,162	\$ 495,561
Management fees	non-affil.(B)	\$ 380	\$ 56	\$ 976	\$ 394
Incentive income	non-affil.(B)	\$ 13,130	\$ 431	\$ 13,334	\$ 431

(A) Presented on a pro forma basis (Note 12), as adjusted for the deconsolidation of the Fortress Funds as if it had occurred on January 1, 2007.

(B) Included in Other Revenues on the statement of operations.

(C) See Deferred Incentive Income below.

Deferred Incentive Income

Incentive income from certain Fortress Funds, primarily private equity funds, is received when such funds realize profits, based on the related agreements. However, this incentive income is subject to contingent repayment by Fortress to the funds until certain overall fund performance criteria are met. Accordingly, Fortress does not

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recognize this incentive income as revenue until the related contingencies are resolved. Until such time, this incentive income is recorded on the balance sheet as deferred incentive income and is included as distributed-unrecognized deferred incentive income in the table below. Incentive income from such funds, based on their net asset value, which has not yet been received is not recorded on the balance sheet and is included as undistributed deferred incentive income in the table below.

Incentive income from certain Fortress Funds, primarily hybrid hedge funds, is earned based on achieving annual performance criteria. Accordingly, this incentive income is recorded as revenue at year end (in the fourth quarter of each year), is generally received subsequent to year end, and has not been recognized for these funds during the nine months ended September 30, 2008 and 2007. If the amount of incentive income contingent on achieving annual performance criteria was not contingent on the results of the subsequent quarters, \$0.0 million and \$92.0 million of additional incentive income from affiliates would have been recognized during the nine months ended September 30, 2008 and 2007, respectively. Incentive income based on achieving annual performance criteria that has not yet been recognized is not recorded on the balance sheet and is included as undistributed deferred incentive income in the table below.

Deferred incentive income from the Fortress Funds, subject to contingent repayment, was comprised of the following, on an inception to date basis:

	Distributed- Gross	Distributed- Recognized(A)	Distributed- Unrecognized(B)	Undistributed, net (C)(D)
Deferred incentive income as of December 31, 2007	\$ 444,721	\$ (271,160)	\$ 173,561	\$ 384,520
Share of income (loss) of Fortress Funds	26,077		26,077	(313,058)
Recognition of previously deferred incentive income		(36,003)	(36,003)	
Deferred incentive income as of September 30, 2008	\$ 470,798	\$ (307,163)	\$ 163,635	\$ 71,462

(A) All related contingencies have been resolved.

(B) Reflected on the balance sheet.

(C)

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On a deconsolidated basis, subsequent to March 31, 2007, undistributed incentive income is no longer recorded and is not reflected on the balance sheet. At September 30, 2008, the undistributed incentive income is comprised of \$155.0 million of gross undistributed incentive income, net of \$83.5 million of previously distributed incentive income that would be returned by Fortress to the related funds if such funds were liquidated on September 30, 2008 at their net asset values.

- (D) From inception to September 30, 2008, Fortress has recognized and paid compensation expense under its employee profit sharing arrangements (Note 7) in connection with the \$470.8 million of distributed incentive income. If the \$71.5 million of undistributed incentive income were realized, Fortress would recognize and pay an additional \$30.4 million of compensation expense.

Private Equity Funds

In 2008, Fortress made an additional \$100 million commitment to Fund V. Fortress's affiliates, including employees and the Principals, made additional commitments to this fund of \$67.3 million at the same time.

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During the nine months ended September 30, 2008, Fortress formed new private equity funds which had capital commitments as follows:

Fortress's commitments	\$ 48,328
Fortress's affiliates' commitments	87,963
Third party investors' commitments	3,966,006
 Total capital commitments	 \$ 4,102,297

Unrealized losses in a significant portion of Fortress's private equity funds have resulted in higher future returns being required before Fortress earns incentive income from such funds.

Liquid Hedge Funds and Hybrid Hedge Funds

During the nine months ended September 30, 2008, Fortress formed new hedge funds with net asset values as follows:

	September 30, 2008	
	NAV	
	Liquid	Hybrid
Fortress(A)	\$ 1,265	\$
Fortress's affiliates	497,654	
Third party investors	1,369,993	
 Total NAV	 \$ 1,868,912	 \$

(A) Includes a third quarter incentive income allocation of \$159,000.

As of September 30, 2008, the liquid hedge funds had received redemption notices totaling \$0.9 billion which were paid in October 2008 (subject to certain holdbacks).

As a result of not meeting the incentive income thresholds with respect to current investors, the incentive income from a significant portion of the capital invested in Fortress's hybrid and liquid hedge funds has been discontinued for an indeterminate period of time. Returns earned on capital from new investors continue to be incentive income eligible.

3. INVESTMENTS IN EQUITY METHOD INVESTEEs AND OTHER EQUITY INVESTMENTS

Fortress elected to record its investments in and options from Newcastle and Eurocastle at fair value pursuant to SFAS 159 (The Fair Value Option For Financial Assets and Financial Liabilities) beginning January 1, 2008. Fortress made this election to simplify its accounting for these publicly traded equity securities (and related options), which were previously recorded based on the equity method of accounting. As a result, Fortress recorded an aggregate increase to the carrying amounts of these assets of \$22.9 million, which was recorded as a cumulative effect adjustment to retained earnings (\$2.1 million) and also impacted the Principals' interests in the equity of consolidated subsidiaries (Fortress Operating Group) (\$17.6 million), deferred tax assets (\$1.9 million), and accumulated other comprehensive income (\$1.2 million). Fortress accounts for dividends received from these investments as dividend income, a component of Other Revenues.

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Investments in Equity Method Investees

Fortress holds investments in certain unconsolidated Fortress Funds which are recorded based on the equity method of accounting. Upon the deconsolidation of the consolidated Fortress Funds on March 31, 2007 (Note 1), these funds also became equity method investees. Fortress's maximum exposure to loss with respect to these entities is generally equal to its investment plus its basis in any options received from such entities as described below, plus any receivables from such entities as described in Note 6. In addition, unconsolidated affiliates also hold ownership interests in certain of these entities. Summary financial information related to these investments is as follows:

	Fortress's Investment September 30, December 31,		Fortress's Equity in Net Income (Loss)			
			Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007	2008	2007
Private equity funds, excluding NIH(A)	\$ 667,180	\$ 623,830	\$ (6,309)	\$ (33,658)	\$ (74,606)	\$ (41,682)
NIH	4,523	5,770	(9)	4,019	872	2,995
Newcastle(B)	6,513	3,184	N/A	(412)	N/A	777
Eurocastle(B)	4,150	11,799	N/A	1,487	N/A	1,398
Total private equity	682,366	644,583	(6,318)	(28,564)	(73,734)	(36,512)
Liquid hedge funds(A)	32,535	73,748	(3,668)	(3,801)	(3,117)	192
Hybrid hedge funds(A)	232,166	371,310	(27,940)	1,649	(36,715)	12,984
Other	2,642	2,277	5		16	47
	\$ 949,709	\$ 1,091,918	\$ (37,921)	\$ (30,716)	\$ (113,550)	\$ (23,289)

(A) These entities were consolidated prior to March 31, 2007.

(B) Fortress elected to record these investments at fair value pursuant to SFAS 159 beginning on January 1, 2008.

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A summary of the changes in Fortress's investments in equity method investees is as follows:

	Nine Months Ended September 30, 2008							
	Private Equity Funds		Castles(A)		Liquid Hedge Funds	Hybrid Hedge Funds	Other	Total
	NIH	Other	Newcastle	Eurocastle				
Investment, beginning	\$ 5,770	\$ 623,830	\$ 3,184	\$ 11,799	\$ 73,748	\$ 371,310	\$ 2,277	\$ 1,091,918
Earnings from equity method investees	872	(74,606)	N/A	N/A	(3,117)	(36,715)	16	(113,550)
Other comprehensive income from equity method investees	(17)	3,309	N/A	N/A				3,292
Contributions to equity method investees		134,511	N/A	N/A	59,037	262	359	194,169
Distributions of earnings from equity method investees	(2,102)	(7,021)	N/A	N/A	(253)		(10)	(9,386)
Distributions of capital from equity method investees		(11,706)	N/A	N/A	(96,880)	(102,691)		(211,277)
Total distributions from equity method investees	(2,102)	(18,727)	N/A	N/A	(97,133)	(102,691)	(10)	(220,663)
Sale of investments		(1,137)						(1,137)
Mark to fair value January 1, 2008(B)	N/A	N/A	10,110	12,762	N/A	N/A	N/A	22,872
Mark to fair value during period(C)	N/A	N/A	(6,781)	(21,524)	N/A	N/A	N/A	(28,305)
Translation adjustment				1,113				1,113
Investment, ending	\$ 4,523	\$ 667,180	\$ 6,513	\$ 4,150	\$ 32,535	\$ 232,166	\$ 2,642	\$ 949,709
Ending balance of undistributed earnings	\$	\$	N/A	N/A	\$ 75	\$ 1,066	\$ 6	\$ 1,147

- (A) Fortress elected to record these investments at fair value pursuant to SFAS 159 beginning on January 1, 2008.
- (B) Recorded as a cumulative effect adjustment as described above.
- (C) Recorded to Other Investments Net Unrealized Gains (Losses) from Affiliate Investments.

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The ownership percentages presented in the following tables are reflective of the ownership interests held as of the end of the respective periods. For tables which include more than one Fortress Fund, the ownership percentages are based on a weighted average by total equity of the funds as of period end.

	Private Equity Funds Excluding NIH(C)		Newcastle Investment Holdings LLC (NIH)	
	September 30, 2008	December 31, 2007	September 30, 2008	December 31, 2007
Assets	\$ 17,091,841	\$ 16,982,495	\$ 299,219	\$ 336,176
Liabilities	(2,711,408)	(3,445,658)	(218,648)	(230,457)
Equity	\$ 14,380,433	\$ 13,536,837	\$ 80,571	\$ 105,719
Fortress's Investment	\$ 667,180	\$ 623,830	\$ 4,523	\$ 5,770
Ownership(A)	4.6%	4.6%	4.8%	4.8%

	Nine Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Revenues and gains (losses) on investments	\$ (3,325,753)	\$ (3,329,819)	\$ 35,773	\$ 93,918
Expenses	(345,364)	(194,551)	(16,808)	(22,962)
Net Income (Loss)	\$ (3,671,117)	\$ (3,524,370)	\$ 18,965	\$ 70,956
Fortress's equity in net income (loss)	\$ (74,606)	\$ (41,682)	\$ 872	\$ 2,995

(B)

(A) Excludes ownership interests held by other Fortress Funds, the Principals, employees and other affiliates.

(B) The revenues and expenses of these entities were consolidated through March 31, 2007, the effective date of the deconsolidation (Note 1). As a result, the amounts shown for Fortress's equity in net income of these entities relate to the period subsequent to March 31, 2007.

- (C) Includes one entity which is recorded on a one quarter lag (i.e. the balances reflected for this entity are for June 30, 2008 and the period then ended). It is recorded on a lag because it is a German entity and does not provide financial reports under U.S. GAAP within the reporting timeframe necessary for U.S. public entities. During the quarter ended September 30, 2008, this entity had a significant revenue realization event. Fortress's share of this revenue was \$11.9 million, which will be recorded by Fortress in the fourth quarter of 2008.

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	Newcastle Investment Corp.		Eurocastle Investment Ltd.	
	September 30, 2008	December 31, 2007	September 30, 2008	December 31, 2007
Assets	\$ 5,785,226	\$ 8,037,770	\$ 9,302,638	\$ 10,713,687
Liabilities	(6,125,327)	(7,590,145)	(8,036,326)	(8,865,921)
Minority interest			(8)	(8)
Equity	\$ (340,101)	\$ 447,625	\$ 1,266,304	\$ 1,847,758
Ownership, basic(A)	1.9%	1.9%	1.7%	1.6%
Ownership, diluted(A)(B)	4.8%	4.7%	10.3%	9.8%
Ownership by Fortress and affiliates, diluted(B)	15.1%	15.5%	31.3%	29.3%
Market value of shares owned(A)(C)	\$ 6,513	\$ 13,293	\$ 4,150	\$ 24,561
	Nine Months Ended September 30, 2008		Nine Months Ended September 30, 2008	
	2008	2007	2008	2007
Revenues and gains (losses) on investments	\$ 361,461	\$ 543,369	\$ 589,854	\$ 552,586
Expenses	(268,053)	(505,690)	(656,097)	(542,100)
Other income (loss)	(355,968)		47,911	65,846
Discontinued operations	(8,724)	(2)		
Preferred dividends	(10,126)	(9,265)		
Net Income (Loss)	\$ (281,410)	\$ 28,412	\$ (18,332)	\$ 76,332
Fortress's equity in net income (loss)		N/A		N/A
		\$ 777		\$ 1,398

(A) Excludes ownership interests held by other Fortress Funds, the Principals, employees and other affiliates.

(B)

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Fully diluted ownership represents the percentage of outstanding common shares assuming that all options are exercised. Currently, all of the options are out of the money (that is, their strike price is below the current market price per share).

- (C) Based on the closing price of the related shares and, if applicable, the foreign currency exchange rate on the last day of trading in the applicable period.

	Liquid Hedge Funds		Hybrid Hedge Funds	
	September 30, 2008	December 31, 2007	September 30, 2008	December 31, 2007
Assets	\$ 9,761,791	\$ 8,358,378	\$ 12,674,623	\$ 12,098,175
Liabilities	(1,012,898)	(67,483)	(4,606,119)	(4,493,901)
Minority Interest			(30,299)	(26,834)
Equity	\$ 8,748,893	\$ 8,290,895	\$ 8,038,205	\$ 7,577,440
Fortress's Investment	\$ 32,535	\$ 73,748	\$ 232,165	\$ 371,310
Ownership(A)	0.4%	0.9%	2.9%	4.9%

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	Nine Months Ended September 30, 2008		Nine Months Ended September 30, 2007	
Revenues and gains (losses) on investments	\$	(716,901)	\$	1,092,573
Expenses		(490,442)		(710,854)
				(312,522)
				(255,716)
Net Income	\$	(1,207,343)	\$	381,719
				(798,079)
				\$ 464,739
Fortress's equity in net income (loss)	\$	(3,117)	\$	192
				(36,715)
				\$ 12,984
			(B)	(B)

(A) Excludes ownership interests held by other Fortress Funds, the Principals, employees and other affiliates.

(B) The revenues and expenses of these entities were consolidated through March 31, 2007, the effective date of the deconsolidation (Note 1). As a result, the amounts shown for Fortress's equity in net income of these entities relate to the period subsequent to March 31, 2007.

Options in Affiliates

Fortress holds options to purchase additional shares of its equity method investees with carrying values as follows:

	September 30, 2008	December 31, 2007	Accounting Treatment
Newcastle options	\$ 33	\$ 5	Recorded at fair value
Eurocastle options	104	15,996	Recorded at fair value
	\$ 137	\$ 16,001	

Investments in Variable Interest Entities

As part of the deconsolidation of the consolidated Fortress Funds (Note 1), Fortress caused reconsideration events to occur in each of the variable interest entities in which it was deemed to be the primary beneficiary. As a result of these reconsideration events, Fortress is no longer considered the primary beneficiary of, and therefore does not consolidate, any of the variable interest entities in which it holds an interest. No reconsideration events occurred during the nine

months ended September 30, 2008 which caused a change in Fortress's accounting.

The following table presents information as of September 30, 2008 regarding entities formed during the nine months ended September 30, 2008 that were determined to be VIEs in which Fortress holds a variable interest. The amounts presented below are included in, and not in addition to, the equity method investment tables above.

Business Segment	Fortress is not Primary Beneficiary		Notes
	Gross Assets	Fortress Investment(A)	
Private Equity Funds	\$ 1,154,601	\$ 8,013	(B)
Liquid Hedge Funds	\$ 315,747	\$ 85	

(A) Represents Fortress's maximum exposure to loss with respect to these entities, which includes direct and indirect investments in the funds.

(B) Fortress investment includes \$0.1 million of management fees receivable from the Private Equity Funds.

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Fair Value of Financial Instruments

The following table presents information regarding Fortress's financial instruments which are recorded at fair value:

	September 30, 2008 Fair Value	Valuation Method
Assets Carried at Fair Value		
Newcastle and Eurocastle common shares	\$ 10,663	Level 1 Quoted prices in active markets for identical assets
Newcastle and Eurocastle options	\$ 137	Level 2 Lattice-based option valuation models using significant observable inputs

4. DEBT OBLIGATIONS

The following table presents information regarding Fortress's debt obligations:

Debt Obligation	Month Issued	Face Amount and Carrying Value		Contractual Interest Rate	Final Stated Maturity	September 30, 2008	
		September 30, 2008	December 31, 2007			Weighted Average Funding Cost(A)	Weighted Average Maturity (Years)
Credit agreement(B)							
Revolving debt(C)	May 2007	\$	\$ 185,000	LIBOR + 0.85%(D)	May 2012	0.00%	N/A
Term loan	May 2007	350,000	350,000	LIBOR + 0.85%	May 2012	4.52%	3.61
Delayed term loan	May 2007	400,000		LIBOR + 0.85%	May 2012	4.55%	1.47
Total		\$ 750,000	\$ 535,000			4.54%	2.47

(A) The weighted average funding cost is calculated based on the contractual interest rate (utilizing the most recently reset LIBOR rate) plus the amortization of deferred financing costs. The most recently reset LIBOR rate was 3.19%.

(B)

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Collateralized by substantially all of Fortress Operating Group's assets as well as Fortress Operating Group's rights to fees from the Fortress Funds and its equity interests therein.

- (C) Approximately \$189 million was undrawn under the revolving debt facility as of September 30, 2008, including a \$25 million letter of credit subfacility of which \$11 million was utilized. However, as a result of the amendments described in Note 11, the aggregate amount of revolving credit facility commitments has been reduced from \$200 million to \$125 million. In addition, Lehman Brothers Commercial Paper, Inc., which is committed to fund \$11.9 million of the \$125 million revolving credit facility, has filed for bankruptcy protection, and it is reasonably possible that it will not fund its portion of the commitments. As a result, approximately \$102 million of the undrawn amount is currently available.
- (D) Subject to unused commitment fees of 0.25% per annum.

In connection with the repayment of a portion of a prior term loan, \$2.0 million of deferred loan costs were written off to interest expense in February 2007. In May 2007, Fortress entered into a new credit agreement to refinance its existing credit agreement, reduce the amount of interest and other fees payable under its credit facilities, and increase the amount of funds available for investments.

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On April 17, 2008, Fortress entered into an amendment to its credit agreement. The amendment, among other things, (i) permits Fortress to issue an unlimited amount of subordinated indebtedness with specified terms so long as 40% of the net proceeds are used to repay amounts outstanding under the credit agreement, (ii) increased the applicable rate on Eurodollar loans and letters of credit by 20 basis points (making the current rate LIBOR plus 0.85%) and the undrawn commitment fee by 5 basis points (making the current fee 0.25%), (iii) added an amortization schedule requiring Fortress to repay \$100 million of amounts outstanding under the agreement each year during the next three years (with the first payment due on January 15, 2009), (iv) modified the financial covenants by (a) replacing the EBITDA-based financial covenant with a Consolidated Leverage Ratio covenant, (b) increasing the minimum amount of management fee earning assets by \$3 billion to \$21.5 billion (which minimum amount increases annually by \$500 million) and (c) eliminating the annual \$50 million increase in required minimum investment assets, and (v) revised various definitions and clarified terms with respect to swap providers who are lenders under the agreement. In connection with this amendment, Fortress incurred \$4.9 million of deferred loan costs which were recorded in Other Assets. In addition, on May 29, 2008, Fortress entered into an amendment to its credit agreement to change from a co-borrower structure to a single borrower structure.

On November 12, 2008, Fortress entered into an amendment to its credit agreement as described in Note 11.

Fortress was in compliance with all of its debt covenants as of September 30, 2008.

5. INCOME TAXES AND TAX RELATED PAYMENTS

For the nine months ended September 30, 2008, an estimated annual effective tax rate of 0.18% was used to compute the tax provision. Fortress incurred a loss before income taxes for financial reporting purposes, after deducting the compensation expense arising from the Principals' forfeiture agreement. However, this compensation expense is not deductible for income tax purposes. Also, a portion of Fortress's income is not subject to U.S. federal income tax, but is allocated directly to Fortress's shareholders.

The provision for income taxes consists of the following:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2008	2007	2008	2007
Current				
Federal income tax	\$ (3,310)	\$ 5,016	\$ (1,316)	\$ 10,071
Foreign income tax	891	620	2,090	1,686
State and local income tax	1,646	1,688	7,190	11,794
	(773)	7,324	7,964	23,551

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	Deferred				
Federal income tax expense (benefit)	(2,506)	(12,716)	(2,526)	(1,648)	
Foreign income tax expense (benefit)	(281)	(57)	(101)	(790)	
State and local income tax expense (benefit)	(2,076)	(6,770)	(5,670)	(13,876)	
	(4,863)	(19,543)	(8,297)	(16,314)	
Total expense (benefit)	\$ (5,636)	\$ (12,219)	\$ (333)	\$ 7,237	

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The tax effects of temporary differences have resulted in deferred income tax assets and liabilities as follows:

	September 30, 2008	December 31, 2007
Deferred tax assets	\$ 517,578	\$ 511,204
Deferred tax liabilities(A)	\$ 644	\$ 891

(A) Included in Other Liabilities

For the nine months ended September 30, 2008, a deferred income tax provision of \$0.2 million was credited to other comprehensive income, primarily related to the equity method investees. A current income tax benefit of \$2.1 million was credited to additional paid in capital, related to (i) dividend equivalent payments on RSU's (Note 7), and (ii) distributions to Fortress Operating Group restricted partnership unit holders (Note 7), which are currently deductible for income tax purposes.

Tax Receivable Agreement

Although the tax receivable agreement payments are calculated based on annual tax savings, for the nine months ended September 30, 2008, the payments which would have been made pursuant to the tax receivable agreement, if such period was calculated by itself, were estimated to be \$12.7 million.

6. RELATED PARTY TRANSACTIONS AND INTERESTS IN CONSOLIDATED SUBSIDIARIES

Due from affiliates was comprised of the following:

	Private Equity Funds	Castles	Liquid Hedge Funds	Hybrid Hedge Funds	Other	Total
September 30, 2008						
Management fees and incentive income	\$ 15,794	\$ 6,401	\$ 418	\$ 2,350	\$	\$ 24,963
Expense reimbursements	4,324	3,782	3,899	3,460		15,465
Dividends and distributions		257				257
Other	6,583			273	1,888	8,744

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Total	\$	26,701	\$	10,440	\$	4,317	\$	6,083	\$	1,888	\$	49,429
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		Private Equity Funds	Castles	Liquid Hedge Funds	Hybrid Hedge Funds	Other	Total
December 31, 2007							
Management fees and incentive income	\$	1,733	\$ 45,004	\$ 40,751	\$ 98,197	\$	\$ 185,685
Expense reimbursements		1,307	2,051	3,074	3,487		9,919
Dividends and distributions			739				739
Other					1	2,325	2,326
Total	\$	3,040	\$ 47,794	\$ 43,825	\$ 101,685	\$ 2,325	\$ 198,669

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Due to affiliates was comprised of the following:

	September 30, 2008	December 31, 2007
Principals		
Tax receivable agreement Note 5	\$ 393,595	\$ 393,265
Distributions payable on Fortress Operating Group units		60,176
Other	1,913	2,293
	\$ 395,508	\$ 455,734

For the nine months ended September 30, 2008 and 2007, Other Revenues included approximately \$44.6 million and \$32.3 million, respectively, of revenues from affiliates, primarily expense reimbursements. Dividend income from affiliates of approximately \$1.7 million was recorded during the nine months ended September 30, 2008.

Fortress has entered into cost sharing arrangements with the Fortress Funds, including market data services and subleases of certain of its office space. Expenses borne by the Fortress Funds under these agreements are generally paid directly by those entities (i.e. they are generally not paid by Fortress and reimbursed). For the nine months ended September 30, 2008 and 2007, these expenses, mainly related to subscriptions to market data services, approximated \$15.6 million and \$14.9 million, respectively.

In July 2008, three of the Principals invested an aggregate of \$14.4 million in preferred equity interests of a subsidiary of one of the private equity Fortress Funds. The preferred equity does not pay a dividend.

Principals and Others Interests in Consolidated Subsidiaries

These amounts relate to equity interests in Fortress's consolidated, but not wholly owned, subsidiaries, which are held by the Principals, employees and others.

This balance sheet caption was comprised of the following:

	September 30, 2008	December 31, 2007
Principals Fortress Operating Group units	\$ 139,489	\$ 232,826
Employee interests in majority owned and controlled fund advisor and general partner entities	35,189	75,062

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Other		176		135
Total		\$ 174,854	\$	308,023

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This statement of operations caption was comprised of shares of consolidated net income (loss) related to the following, on a pre-tax basis:

	Three Months Ended September 30, 2008		Nine Months Ended September 30, 2008	
	Actual	2007 Actual	Actual	2007 Actual
Principals Fortress Operating Group units	\$ (208,169)	\$ (154,893)	\$ (611,760)	\$ (402,294)
Employee interests in majority owned and controlled fund advisor and general partner entities	(1,843)	2,359	(1,401)	8,359
Third party investors in Fortress Funds(A)				(460,615)
Other			469	
Total	\$ (210,012)	\$ (152,534)	\$ (612,692)	\$ (854,550)

(A) Prior to the deconsolidation (Note 1) on March 31, 2007.

7. EQUITY-BASED AND OTHER COMPENSATION

Fortress's total compensation and benefits expense, excluding Principals Agreement compensation, is comprised of the following:

	Three Months Ended September 30, 2008		Nine Months Ended September 30, 2008	
	2008	2007	2008	2007
Equity-based compensation, per below	\$ 57,755	\$ 36,570	\$ 139,152	\$ 100,870
Profit-sharing expense, per below	8,158	9,857	49,866	234,868
Discretionary bonuses	35,737	29,838	109,793	82,897
Other payroll, taxes and benefits	33,124	25,438	100,442	88,368
	\$ 134,774	\$ 101,703	\$ 399,253	\$ 507,003

Equity-Based Compensation

The following tables present information regarding equity-based compensation during the nine months ended September 30, 2008.

	RSUs				Restricted Shares Issued to Directors		RPU's Employees	
	Employees Number	Value(A)	Non-Employees Number	Value(A)	Number	Value(A)	Number	Value(A)
Outstanding as of December 31, 2007	43,215,535	\$ 16.74	9,318,968	\$ 15.22	97,296	\$ 18.50		\$
Issued	2,175,184	10.57	394,404	9.38	11,878	11.72	31,000,000	13.75
Forfeited	(1,874,192)	17.47	(753,412)	14.54				
Outstanding as of September 30, 2008(B)	43,516,527	\$ 16.40	8,959,960	\$ 15.02	109,174	\$ 17.76	31,000,000	\$ 13.75

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	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2008	2007	2008	2007
Expense incurred(B)				
Employee RSUs	\$ 29,088	\$ 28,265	\$ 82,997	\$ 82,280
Non-Employee RSUs	3,970	5,300	9,381	13,778
Restricted Shares	151	152	450	385
LTIP	1,733	2,853	5,162	4,427
RPUs	22,813		41,162	
Total equity-based compensation expense	\$ 57,755	\$ 36,570	\$ 139,152	\$ 100,870

(A) Represents the weighted average grant date estimated fair value per share or unit. The weighted average estimated fair value per unit as of September 30, 2008 for RSU awards granted to non-employees was \$9.78.

(B) In future periods, Fortress will recognize compensation expense on its non-vested equity based awards of \$968.2 million, with a weighted average recognition period of 4.4 years. This does not include amounts related to the Principals Agreement.

In April 2008, Fortress granted 31 million Fortress Operating Group (FOG) restricted partnership units (RPUs) to a senior employee. In connection with the grant of these interests, the employee receives partnership distribution equivalent payments on such units with economic effect as from January 1, 2008. The interests will vest into full capital interests in FOG units in three equal portions on the first business day of 2011, 2012 and 2013, respectively, subject to continued employment with Fortress. In connection with this grant, Fortress has reduced the employee's profit sharing interests in various Fortress Funds.

When Fortress records equity-based compensation expense, including that related to the Principals Agreement, it records a corresponding increase in capital. Of the total increase in capital during the nine months ended September 30, 2008 from equity-based compensation arrangements of \$853.9 million, \$198.5 million increased Fortress's paid-in capital, as reflected in the Statement of Shareholders' Equity, and \$655.4 million increased Principals' interests in equity of consolidated subsidiaries, corresponding to the Principals' interest in the equity-based compensation expense.

Profit Sharing Expense

Recognized profit sharing compensation expense is summarized as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Private equity funds(A)	\$ (5,412)	\$ 1,556	\$ (2,868)	\$ 94,001
Castles	1,248	1,155	3,589	8,029
Liquid hedge funds	5,455	1,629	38,572	89,075
Hybrid hedge funds	6,867	5,517	10,573	43,763
Total	\$ 8,158	\$ 9,857	\$ 49,866	\$ 234,868

(A) Negative amounts reflect the reversal of previously accrued profit sharing expense resulting from the determination that this expense is no longer probable of being incurred.

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8. EARNINGS PER SHARE AND DISTRIBUTIONS

Our potentially dilutive equity instruments fall primarily into two general categories: (i) instruments that we have issued as part of our compensation plan, and (ii) ownership interests in our subsidiary, Fortress Operating Group, that are owned by the Principals and are convertible into Class A shares. Based on the rules for calculating earnings per share, there are two general ways to measure dilution for a given instrument: (a) calculate the net number of shares that would be issued assuming any related proceeds are used to buy back outstanding shares (the treasury stock method), or (b) assume the gross number of shares are issued and calculate any related effects on net income available for shareholders (the if-converted and two-class methods). Fortress has applied these methods as prescribed by the rules to each of its outstanding equity instruments as shown below.

As a result of Fortress's reorganization in January 2007 (Note 1), Fortress has calculated its earnings per share for two different periods within the nine months ended September 30, 2007. For the first period, prior to the reorganization on January 17, 2007, the calculation is based on the income and outstanding units of Fortress Operating Group, which were owned by the Principals, as if such units had been outstanding from the beginning of the period. For the second period, subsequent to the reorganization and commencement of operations of the Registrant, the calculation is based on the consolidated income of Fortress from January 17, 2007 through September 30, 2007 and the Class A shares outstanding for such period.

The computations of net income per Fortress Operating Group unit, prior to the reorganization, are set forth below:

	January 1 through January 16, 2007	
	Basic	Diluted
Weighted average units outstanding		
Fortress Operating Group units outstanding	367,143,000	367,143,000
Total weighted average units outstanding	367,143,000	367,143,000
Net income per unit is calculated as follows:		
Net income	\$ 133,397	\$ 133,397
Dilution in earnings of certain equity method investees		
Net income available to Fortress Operating Group unitholders	\$ 133,397	\$ 133,397
Weighted average units outstanding	367,143,000	367,143,000
Net income per unit	\$ 0.36	\$ 0.36

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The computations of basic and diluted net income (loss) per Class A share, subsequent to the reorganization, are set forth below:

	Three Months Ended September 30, 2007		January 17 through September 30, 2007	
	Basic	Diluted	Basic	Diluted
Weighted average shares outstanding				
Class A shares outstanding	94,500,350	94,500,350	90,971,694	90,971,694
Fully vested restricted Class A share units with dividend equivalent rights	394,286	394,286	283,825	283,825
Fortress Operating Group units exchangeable into Fortress Investment Group LLC Class A shares(1)		312,071,550		
Class A restricted shares and Class A restricted share units granted to employees and directors (eligible for dividend and dividend equivalent payments)(2)				
Class A restricted share units granted to employees (not eligible for dividend and dividend equivalent payments)(3)				
Total weighted average shares outstanding	94,894,636	406,966,186	91,255,519	91,255,519
Basic and diluted net income (loss) per Class A share				
Net income (loss)	\$ (37,557)	\$ (37,557)	\$ (163,942)	\$ (163,942)
Dividend equivalents declared on non-vested restricted Class A share units	(1,125)	(1,125)	(2,742)	(2,742)
Dilution in earnings of certain equity method investees				
Add back Principals and others interests in loss of Fortress Operating Group, net of assumed corporate income tax at enacted rates, attributable to Fortress Operating Group units exchangeable into Fortress Investment Group LLC Class A		(173,093)		

shares(1)

Net income (loss) available to Class A shareholders	\$	(38,682)	\$	(211,775)	\$	(166,684)	\$	(166,684)
Weighted average shares outstanding		94,894,636		406,966,186		91,255,519		91,255,519
Basic and diluted net income (loss) per Class A share	\$	(0.41)	\$	(0.52)	\$	(1.83)	\$	(1.83)

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	Three Months Ended September 30, 2008		Nine Months Ended September 30, 2008	
	Basic	Diluted	Basic	Diluted
Weighted average shares outstanding				
Class A shares outstanding	94,500,351	94,500,351	94,500,351	94,500,351
Fully vested restricted Class A share units with dividend equivalent rights	394,286	394,286	394,286	394,286
Fully vested restricted Class A shares	43,797	43,797	21,029	21,029
Fortress Operating Group units exchangeable into Fortress Investment Group LLC Class A shares(1)		312,071,550		312,071,550
Class A restricted shares and Class A restricted share units granted to employees and directors (eligible for dividend and dividend equivalent payments)(2)				
Class A restricted share units granted to employees (not eligible for dividend and dividend equivalent payments)(3)				
Total weighted average shares outstanding	94,938,434	407,009,984	94,915,666	406,987,216
Basic and diluted net income (loss) per Class A share				
Net income (loss)	\$ (57,440)	\$ (57,440)	\$ (181,913)	\$ (181,913)
Dilution in earnings due to RPU's treated as a participating security of Fortress Operating Group and fully vested restricted Class A share units with dividend equivalent rights treated as outstanding Fortress Operating Group units(4)	(298)	(298)	(2,071)	(2,071)
Dividend equivalents declared on non-vested restricted Class A shares and restricted Class A share units			(2,276)	(2,276)
Add back Principals' and others' interests in loss of Fortress Operating Group, net of assumed corporate income taxes at enacted rates, attributable to Fortress Operating Group units exchangeable into Fortress Investment Group LLC Class A shares(1)		(210,477)		(613,553)

Net income (loss) available to Class A shareholders	\$	(57,738)	\$	(268,215)	\$	(186,260)	\$	(799,813)
Weighted average shares outstanding		94,938,434		407,009,984		94,915,666		406,987,216
Basic and diluted net income (loss) per Class A share	\$	(0.61)	\$	(0.66)	\$	(1.96)	\$	(1.97)

- (1) The Fortress Operating Group units not held by Fortress (that is, those held by the Principals) are exchangeable into Class A shares on a one-to-one basis. These units are not included in the computation of basic earnings per share. These units enter into the computation of diluted net income (loss) per Class A share when the effect is dilutive using the if-converted method.
- (2) Restricted Class A shares granted to directors and certain restricted Class A share units granted to employees are eligible to receive dividend or dividend equivalent payments when dividends are declared and paid on our Class A shares and therefore participate fully in the results of our operations from the date they are granted. They are included in the computation of both basic and diluted earnings per Class A share using the two-class method for participating securities, except during periods of net losses.

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- (3) Certain restricted Class A share units granted to employees are not entitled to dividend or dividend equivalent payments until they are vested and are therefore non-participating securities. These units are not included in the computation of basic earnings per share. They are included in the computation of diluted earnings per share when the effect is dilutive using the treasury stock method. As a result of the net loss incurred for the period, the effect of the units on the calculation is anti-dilutive for the periods. The weighted average restricted Class A share units which are not entitled to receive dividend or dividend equivalent payments outstanding were:

Period	Share Units
Three months ended:	
September 30, 2008	28,063,543
September 30, 2007	26,087,366
Nine months ended September 30, 2008	27,841,459
Period from January 17, 2007 to September 30, 2007	23,462,014

- (4) Fortress Operating Group RPU's are eligible to receive partnership distribution equivalent payments when distributions are declared and paid on Fortress Operating Group units. The RPU's represent a participating security of Fortress Operating Group and the resulting dilution in Fortress Operating Group earnings available to Fortress is reflected in the computation of both basic and diluted earnings per Class A share using the method prescribed for securities issued by a subsidiary. For purposes of the computation of basic and diluted earnings per Class A share, the fully vested restricted Class A share units with dividend equivalent rights are treated as outstanding Class A shares of Fortress and as outstanding partnership units of Fortress Operating Group.

The Class B shares have no net income (loss) per share as they do not participate in Fortress's earnings (losses) or distributions. The Class B shares have no dividend or liquidation rights. Each Class B share, along with one Fortress Operating Group unit, can be exchanged for one Class A share, subject to certain limitations. The Class B shares have voting rights on a pari passu basis with the Class A shares. The number of Class B shares outstanding did not change subsequent to the IPO.

Fortress's dividend paying shares and units were as follows:

	Weighted Average			
	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2008	2007	2008	2007
Class A shares	94,500,351	94,500,350	94,500,351	85,640,019
Restricted Class A shares	108,661	97,296	103,411	83,396

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Restricted Class A share units(A)	394,286	394,286	394,286	267,190
Restricted Class A share units(B)	24,101,891	23,730,308	23,840,819	20,430,657
Fortress Operating Group units	312,071,550	312,071,550	312,071,550	315,299,181
Fortress Operating Group RPU's	31,000,000		18,781,022	
Total	462,176,739	430,793,790	449,691,439	421,720,443

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	As of September 30, 2008	As of December 31, 2007
Class A shares	94,500,351	94,500,350
Restricted Class A shares	109,174	97,296
Restricted Class A share units(A)	394,286	394,286
Restricted Class A share units(B)	24,040,462	23,906,779
Fortress Operating Group units	312,071,550	312,071,550
Fortress Operating Group RPU's	31,000,000	
Total	462,115,823	430,970,261

(A) Represents fully vested restricted Class A share units which are entitled to dividend equivalent payments.

(B) Represents nonvested restricted Class A share units which are entitled to dividend equivalent payments.

Dividends and distributions during the nine months ended September 30, 2008 are summarized as follows:

	Declared in Prior Year, Paid Current Year	Declared and Paid	Current Year Declared but Not Yet Paid	Total
Dividends on Class A Shares	\$ 21,285	\$ 42,572	\$	\$ 42,572
Dividend equivalents on restricted Class A share units(A)	5,428	10,914		10,914
Distributions to Fortress Operating Group unit holders (Principals)	60,176	143,462		143,462
Distributions to Fortress Operating Group RPU holders (Note 7)		6,975		6,975
Total distributions	\$ 86,889	\$ 203,923	\$	\$ 203,923

(A)

A portion of these dividend equivalents, related to RSUs expected to be forfeited, is included as compensation expense in the consolidated statement of operations and is therefore considered an operating cash flow.

9. COMMITMENTS AND CONTINGENCIES

Other than as described below, Fortress's commitments and contingencies remain materially unchanged from December 31, 2007.

Private Equity Fund Capital Commitments Fortress has remaining capital commitments to certain of the Fortress Funds which aggregated \$153.7 million as of September 30, 2008. These commitments can be drawn by the funds on demand.

Minimum Future Rentals Fortress is a lessee under operating leases for office space located in New York, Atlanta, Bethesda, Charlotte, Chicago, Dallas, Dubai, Frankfurt, Geneva, Hong Kong, London, Los Angeles, New Canaan, Rome, San Diego, San Francisco, Shanghai, Sydney, Tokyo, and Toronto.

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Minimum future rent payments under these leases is as follows:

October 1 to December 31, 2008	\$ 4,606
2009	19,223
2010	21,890
2011	12,369
2012	11,785
2013	11,587
Thereafter	34,164
Total	\$ 115,624

Rent expense recognized on a straight-line basis during the nine months ended September 30, 2008 and 2007 was \$14.7 million and \$11.0 million, respectively, and during the three months ended September 30, 2008 and 2007 was \$5.3 million and \$3.6 million, respectively, and was included in General, Administrative and Other Expense.

Litigation Fortress is, from time to time, a defendant in legal actions from transactions conducted in the ordinary course of business. Management, after consultation with legal counsel, believes the ultimate liability arising from such actions that existed as of September 30, 2008, if any, will not materially affect Fortress's results of operations, liquidity or financial position.

On September 15, 2005, a lawsuit captioned David T. Atkins et al. v. Apollo Real Estate Advisors, L.P. et al. was brought on behalf of current and former limited partners in certain investing partnerships related to the sale of certain facilities to Ventas Realty Limited Partnership (Ventas) against a number of defendants, including one of the Portfolio Companies and a subsidiary of Fortress (FIG). FIG was the investment manager of consolidated Fortress Funds that were controlling shareholders of the Portfolio Company during the relevant time periods. The suit alleges that the defendants improperly obtained certain rights with respect to such facilities from the investing partnerships. The plaintiffs have asked for damages in excess of \$100 million on each of nine counts, as to which FIG is a defendant on seven counts, including treble damages with respect to certain counts. On April 18, 2006, Fortress filed a motion to dismiss the claims with prejudice. On April 30, 2008, the court entered a memorandum and order granting the motion and dismissing the plaintiff's complaint in its entirety. The plaintiffs were granted a period of 30 days from April 30, 2008 in which to file an amended complaint, after which the parties entered into a settlement, which has been paid in its entirety by Brookdale.

In addition, in the ordinary course of business, the Fortress Funds are and can be both the defendant and the plaintiff in numerous actions with respect to bankruptcy, insolvency and other types of proceedings. Such lawsuits may involve claims that adversely affect the value of certain financial instruments owned by the Fortress Funds. Although the ultimate outcome of actions cannot be ascertained with certainty, Fortress believes that the resolution of any such actions will not have a material adverse effect on its financial condition, liquidity or results of operations.

10. SEGMENT REPORTING

Fortress conducts its management and investment business through the following five primary segments: (i) private equity funds, (ii) Castles, (iii) liquid hedge funds, (iv) hybrid hedge funds, and (v) principal investments in these funds as well as cash that is available to be invested. These segments are differentiated based on their varying investment strategies. Due to the increased significance of the principal investments segment, it has been disaggregated from the other segments in this period and for all periods presented.

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Distributable earnings is a measure of operating performance used by management in analyzing its segment and overall results. For the existing Fortress businesses it is equal to net income adjusted as follows:

Incentive Income

(i) a. for Fortress Funds which are private equity funds, adding (a) incentive income paid (or declared as a distribution) to Fortress, less an applicable reserve for potential future clawbacks if the likelihood of a clawback is deemed greater than remote by Fortress's chief operating decision maker as discussed below (net of the reversal of any prior such reserves that are no longer deemed necessary), minus (b) incentive income recorded in accordance with GAAP,

b. for other Fortress Funds, at interim periods, adding (a) incentive income on an accrual basis as if the incentive income from these funds were payable on a quarterly basis, minus (b) incentive income recorded in accordance with GAAP,

Other Income

(ii) with respect to income from certain principal investments and certain other interests that cannot be readily transferred or redeemed:

a. for equity method investments in the Castles (prior to 2008) and private equity funds as well as indirect equity method investments in hedge fund special investment accounts (which generally have investment profiles similar to private equity funds), treating these investments as cost basis investments by adding (a) realizations of income, primarily dividends, from these funds, minus (b) impairment with respect to these funds, if necessary, minus (c) equity method earnings (or losses) recorded in accordance with GAAP,

b. subtracting gains (or adding losses) on stock options held in the Castles,

c. subtracting unrealized gains (or adding unrealized losses) from consolidated private equity funds,

d. subtracting unrealized gains (or adding unrealized losses) from the Castles subsequent to the election of the fair value option under SFAS 159,

(iii) adding (a) proceeds from the sale of shares received pursuant to the exercise of stock options in certain of the Castles, in excess of their strike price, minus (b) management fee income recorded in accordance with GAAP in connection with the receipt of these options,

Expenses

(iv) adding or subtracting, as necessary, the employee profit sharing in incentive income described in (i) above to match the timing of the expense with the revenue,

(v) adding back equity-based compensation expense (including Castle options assigned to employees, RSUs and RPU's (including the portion of related dividend and distribution equivalents recorded as compensation expense), restricted shares and the LTIP),

(vi) adding back compensation expense recorded in connection with the forfeiture arrangements entered into among the principals,

(vii) adding the income (or subtracting the loss) allocable to the interests in consolidated subsidiaries attributable to Fortress Operating Group units, and

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(viii) adding back income tax expense and any expense recorded in connection with the tax receivable agreement (Note 5).

Total segment assets are equal to total GAAP assets adjusted for:

(i) the difference between the GAAP carrying amount of equity method investments and their carrying amount for segment reporting purposes, which is generally fair value for publicly traded investments and cost for nonpublic investments,

(ii) employee portions of investments, which are reported gross for GAAP purposes (as assets offset by Principals and others' interests in equity of consolidated subsidiaries) but net for segment reporting purposes, and

(iii) the difference between the GAAP carrying amount for options owned in certain of the Castles and their carrying amount for segment reporting purposes, which is intrinsic value.

Distributable Earnings Impairment

For purposes of this discussion, the term private equity funds includes hedge fund special investment accounts, which have investment profiles that are generally similar to private equity funds, and Castles.

Pursuant to the definition of Distributable Earnings (DE) above, impairment is taken into account in the calculation in two ways: first, in section (i)(a) regarding private equity incentive income, and, second, in section (ii)(a) regarding equity method investments in private equity funds.

DE is Fortress's segment measure of operating performance and is defined by Fortress's chief operating decision maker (CODM), which is its management committee, as specified under SFAS 131, Disclosures about Segments of an Enterprise and Related Information. The CODM receives performance reports on our segments on a DE basis pursuant to their requirements for managing Fortress's business.

Investments in Private Equity Funds

For DE purposes, investments in private equity funds are held at their cost basis, subject to potential impairment. An analysis for potential impairment is performed whenever the reported net asset value (NAV) of a fund attributable to our investment is less than our cost basis in such investment. The NAV of a fund is equal to the fair value of its assets less its liabilities. Fortress analyzes these investments for impairment using the other than temporary impairment criteria in a manner similar to the one specified by SFAS 115 Accounting for Certain Investments in Debt and Equity Securities. As a result, a fund investment is considered impaired for DE purposes whenever it is determined by the CODM that Fortress does not have the intent and ability to hold the investment to an anticipated recovery in value, if any, to or above Fortress's cost basis. Prior to September 30, 2008, Fortress had not recorded any impairment with respect to such investments other than \$9.5 million of impairment recorded with respect to Newcastle at June 30, 2008.

Private Equity Incentive Income

For DE purposes, incentive income is recognized from private equity funds as it is realized, subject to a reserve for potential clawback if the likelihood of clawback is determined to be greater than remote by the CODM. Incentive income from our private equity funds is paid to Fortress as particular investments are realized. However, it is subject to contingent repayment (or clawback) if the fund as a whole does not meet certain performance criteria. Fortress's CODM has defined "remote" in this context to mean that management does not believe there is reasonable likelihood of a clawback and therefore its base case expectations of a fund's performance do not include

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a promote clawback. This is an easier threshold to meet than the other than temporary threshold used for estimating investment impairment. Management's base case expectations are generally not greatly impacted by short-term volatility in the value of a fund's portfolio companies, including the market prices of the shares of publicly traded portfolio companies, unless either (a) the operating performance of the underlying company, or the value of its assets, are expected to be impacted on a long-term basis (long-term being defined in relation to the remaining life of a given fund), or (b) the value has been depressed below a breakeven point (as described below) for a period in excess of 6-9 months (as circumstances and other factors dictate). These criteria reflect the CODM's belief that short term changes in the values of portfolio companies do not have a material impact on the likelihood of a clawback, absent deterioration in such companies' operating performance or in the value of their underlying assets.

Fortress conducts an analysis at each quarter end to determine whether a clawback reserve is required. The factors that enter into this analysis include: the amount of intrinsic unrealized gains or losses within each fund, the period of time until expected final realization, the diversification of the fund's investments, the expected future performance of the fund, the period of time the fund has been in an intrinsic clawback position (i.e. liquidation at NAV would indicate a clawback, if any), and others as determined by management and the CODM. The point at which a liquidation at NAV would indicate no clawback and no additional promote payment is referred to as the breakeven point.

For instance, with respect to Fund III as described below, management believes that with the fund only being in an intrinsic clawback position for two quarters it is too soon to determine that a reserve for promote clawback is necessary. Furthermore, Fund III's life allows six years for potential recovery and its diversified nature allows for the recovery of a subset of the fund's investments to drive the entire fund above the breakeven point. Management has updated its base case expectations for this fund to take into account developments through September 30, 2008. This base case scenario contemplates management's expectations for each of the fund's underlying investments (the portfolio companies), including its expectations regarding the net asset values of the portfolio companies. This base case scenario does not reflect a promote clawback as it projects significant additional incentive income being earned from Fund III over its life. Management believes that the assumptions underlying the base case scenario are reasonable. However, the ultimate outcome of Fund III is subject to significant uncertainties and may be materially different than management's expectations at September 30, 2008.

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Investment Impairment for DE purposes

The following investments in private equity funds had reported NAVs below their cost basis as of September 30, 2008:

Fund	Fortress Share of NAV	Fortress Cost Basis	Deficit	% Below Cost Basis	Periods in Deficit	Sep 30, 2008 DE Impairment Recorded	Notes
<u>Main Funds</u>							
Fund III	\$ 6,929	\$ 9,150	\$ (2,221)	(24)%	2 Quarters	\$	(A)
Fund IV and Fund IV CO	104,092	113,566	(9,474)	(8)%	4 Quarters		(A)
Fund V and Fund V CO	49,119	101,363	(52,244)	(52)%	4 Quarters		(A)
<u>Single Investment Funds (combined)</u>							
GAGFAH (XETRA: GFJ)	45,289	66,315	(21,026)	(32)%	2 Quarters	(21,026)	(B)
Brookdale (NYSE: BKD)	31,067	46,603	(15,536)	(33)%	4 Quarters	(15,536)	(B)
Private investment #1	58,216	63,874	(5,658)	(9)%	2 Quarters		(C)
Private investment #2	4,223	8,455	(4,232)	(50)%	3 Quarters	(4,232)	(D)
Private investment #3	270,220	273,449	(3,229)	(1)%	4 Quarters		(C)
<u>Castles</u>							
Eurocastle (EURONEXT: ECT)	4,150	13,011	(8,861)	(68)%	2 Quarters	(8,861)	(B)
Newcastle (NYSE: NCT)	6,513	7,190	(677)	(9)%	1 Quarter		(C)
Total	\$ 579,818	\$ 702,976	\$ (123,158)			\$ (49,655)	

(A) These funds are diversified private equity main funds with multiple underlying investments and fund lives extending to between 2014 and 2017. The CODM anticipates a sufficient recovery in value of a number of the underlying investments to cause each of the funds as a whole to recover to at least Fortress's cost basis within the period of the funds' respective lives. Fortress has the intent and ability to hold these investments until such

recovery and therefore has not recorded DE impairment with respect to them.

- (B) These are single asset coinvestment funds which have investments in public equity securities (or, in the case of Eurocastle, a direct investment in a public equity security). These public equity securities have traded significantly below Fortress's cost basis for a substantial period and Fortress's CODM has determined that these declines in value meet the definition of other than temporary impairment for DE purposes at this time.
- (C) These investments have reported NAVs less than 10% below Fortress's cost basis. The CODM anticipates a recovery in value to at least Fortress's cost basis. Fortress has the intent and ability to hold these investments until such recovery and therefore has not recorded DE impairment with respect to them.
- (D) This is a single asset coinvestment fund which has an investment in a private operating company. This private operating company has experienced liquidity issues as a result of the recent credit crisis and the CODM has determined that the resulting decline in value meets the definition of other than temporary impairment for DE purposes at this time.

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Clawback Reserve on Incentive Income for DE Purposes

Fortress had recognized incentive income for DE purposes from the following private equity funds, which are subject to contingent clawback, as of September 30, 2008:

								Sep 30, 2008	
	Incentive	No		Intrinsic	Employee		Periods in	Gross	
	Income	Longer		Clawback	Portion	Net	Intrinsic	DE	
Fund	Received	Subject to	Subject to	(A)	(B)	Clawback	Clawback	Reserve	Notes
		Clawback	Clawback					Recorded	
Fund I	\$ 308,633	\$ 296,882	\$ 11,751	\$	\$	\$	N/A	\$	(C)
Fund II	254,688	178,286	76,402				N/A		(C)
Fund III	72,483		72,483	72,483	27,068	45,415	3 Quarters		(D)
Fortress Residential Inv.									
Deutschland	16,447		16,447	16,447	6,406	10,041	5 Quarters	(16,447)	(E)
Total	\$ 652,251	\$ 475,168	\$ 177,083	\$ 88,930	\$ 33,474	\$ 55,456		\$ (16,447)	

(A) Intrinsic clawback is the maximum amount of clawback that would be required to be repaid to the fund if the fund were liquidated at its NAV as of the reporting date.

(B) Employees who have received profit sharing payments in connection with private equity incentive income are liable to repay Fortress for their share of any clawback. Fortress remains liable to the funds for these amounts even if it is unable to collect the amounts from employees (or former employees).

(C) These funds had significant unrealized gains at September 30, 2008. As a result, the CODM determined that no reserve for clawback was required.

(D) This fund is a diversified main fund with multiple underlying investments and a fund life extending to 2014. Management believes that the primary reason for its drop in unrealized gains and the incurrence of unrealized losses, which moved the fund into an intrinsic clawback position, is the current confidence and liquidity crisis. Based on the criteria determined by the CODM which are described above, the CODM expects that the

likelihood of a clawback with respect to Fund III is remote and has not recorded a reserve for such clawback. If this fund continues to be in an intrinsic clawback position, management will consider this factor (length of time in an intrinsic clawback position), as well as its updated base case scenario, in relation to the criteria described above and may come to a different conclusion at a future reporting date.

- (E) This is a single asset fund which is invested in a publicly traded equity security. As described above, Fortress's investment in this fund has been deemed to be other than temporarily impaired as of September 30, 2008. This fund has been in an intrinsic clawback position for a period in excess of 6-9 months. As a result, the CODM has determined that the likelihood of clawback based on the criteria described above is greater than remote and has recorded a reserve for this potential clawback.

Impairment Determination

Fortress has recorded a total of approximately \$69.2 million of impairment and reserves for DE purposes on certain private equity funds as described above for DE purposes as of September 30, 2008 (including approximately \$60 million during the third quarter of 2008). Additionally, values have generally deteriorated further since September 30, 2008. Fortress expects aggregate returns on its other private equity funds that are in an unrealized investment loss or intrinsic clawback position to ultimately exceed their carrying amount or breakdown point, as applicable. If such funds were liquidated at their September 30, 2008 NAV (although Fortress has no current intention of doing so), the result would be additional impairment losses and reserves for DE purposes of approximately \$118.9 million.

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Summary financial data on Fortress' segments is presented on the following pages, together with a reconciliation to revenues, assets and net income for Fortress as a whole. Fortress' investments in, and earnings from, its equity method investees by segment are presented in Note 3.

September 30, 2008 and the Nine Months Then Ended	Private Equity Funds	Castles	Liquid Hedge Funds	Hybrid Hedge Funds	Principal Investments	Unallocated
Revenues						
Fees	\$ 128,514	\$ 41,320	\$ 169,965	\$ 111,483	\$	\$
Income	12,294	12	17,125	14,128		
Revenues total	\$ 140,808	\$ 41,332	\$ 187,090	\$ 125,611	\$	\$
Distributable earnings	\$ 100,461	\$ 12,033	\$ 70,662	\$ 26,099	\$ (113,506)	\$ 21
Total assets	\$ 26,673	\$ 11,986	\$ 4,317	\$ 5,809	\$ 1,241,117	\$ 596,826

(A)

	Fortress Subtotal	Reconciliation to GAAP	Fortress Consolidated
Revenues	\$ 494,841	\$ 79,271	\$ 574,112
Pre-tax distributable earnings/net income	\$ 95,770	\$ (277,683)	\$ (181,913)
Total assets	\$ 1,886,728	\$ (31,851)	\$ 1,854,877

(A) Unallocated assets include deferred tax assets of \$517.6 million.

Three Months Ended September 30, 2008	Private Equity Funds	Castles	Liquid Hedge Funds	Hybrid Hedge Funds	Principal Investments	Fortress Unallocated Subtotal
Segment revenues						

Management fees	\$	44,184	\$	13,665	\$	59,640	\$	38,028	\$		\$	155,517			
Incentive income		(16,447)				85		13,256				(3,106)			
Segment revenues	total	\$	27,737	\$	13,665	\$	59,725	\$	51,284	\$		\$	152,411		
Pre-tax distributable earnings		\$	18,575	\$	3,829	\$	25,236	\$	14,820	\$	(82,850)	\$	14	\$	(20,376)

	Fortress Subtotal	Reconciliation to GAAP	Fortress Consolidated
Revenues	\$ 152,411	\$ 32,725	\$ 185,136
Pre-tax distributable earnings/net income	\$ (20,376)	\$ (37,064)	\$ (57,440)

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Reconciling items between segment measures and GAAP measures:

	September 30, 2008 and the Nine Months Then Ended	Three Months Ended September 30, 2008
<u>Adjustments from segment revenues to GAAP revenues</u>		
Adjust management fees*	\$ 488	\$ 163
Adjust incentive income	26,390	16,956
Adjust income from the receipt of options		
Other revenues*		
Adjust management fees from non-affiliates	(3,842)	(1,414)
Adjust incentive income from non-affiliates	(13,787)	(13,132)
Adjust other revenues	70,022	30,152
	52,393	15,606
Total adjustments	\$ 79,271	\$ 32,725

* Segment revenues do not include GAAP other revenues, except to the extent they represent management fees or incentive income; such revenues are included elsewhere in the calculation of distributable earnings.

Adjustments from pre-tax distributable earnings to GAAP net income

Adjust incentive income		
Incentive income received from private equity funds, subject to contingent repayment	\$ (26,077)	\$
Incentive income accrued from private equity funds, no longer subject to contingent repayment	36,003	509
Incentive income received from private equity funds, not subject to contingent repayment	17	
Incentive income received from hedge funds, subject to annual performance achievement		
Reserve for clawback, gross (see discussion above)	16,447	16,447

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	26,390	16,956
Adjust other income		
Distributions of earnings from equity method investees**	(367)	
Earnings (losses) from equity method investees**	(80,297)	(12,814)
Gains (losses) on options in equity method investees	(16,160)	(734)
Unrealized gains (losses) on Castles	(27,192)	(6,217)
Impairment of investments (see discussion above)	59,162	49,655
Adjust income from the receipt of options		
	(64,854)	29,890

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	September 30, 2008 and the Nine Months Then Ended	Three Months Ended September 30, 2008
Adjust employee compensation		
Adjust employee equity-based compensation expense (including Castle options assigned)	(146,246)	(57,739)
Adjust employee portion of incentive income from private equity funds, accrued prior to the realization of incentive income	9,648	
Adjust employee portion of incentive income from one private equity fund, not subject to contingent repayment	(4)	
	(136,602)	(57,739)
Adjust Principals equity-based compensation expense	(714,710)	(239,976)
Adjust Principals interests related to Fortress Operating Group units	611,760	208,169
Adjust income taxes	333	5,636
Total adjustments	\$ (277,683)	\$ (37,064)

** This adjustment relates to all of the Castles, private equity Fortress Funds and hedge fund special investment accounts in which Fortress has an investment.

Adjustments from total segment assets to GAAP assets	
Adjust equity investments from fair value	\$
Adjust equity investments from cost	(64,890)
Adjust investments gross of employee portion	32,902
Adjust option investments from intrinsic value	137
Total adjustments	\$ (31,851)

Nine Months Ended September 30, 2007	Private Equity Funds	Castles	Liquid Hedge Funds	Hybrid Hedge Funds	Principal Investments	Unallocated	Fortress Unconsolidated Subtotal
Segment revenues							

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management fees	\$ 97,749	\$ 34,877	\$ 113,692	\$ 94,096	\$	\$ 340,414
incentive income	273,890	18,596	157,989	93,832		544,307
management revenues total	\$ 371,639	\$ 53,473	\$ 271,681	\$ 187,928	\$	\$ 884,721
pre-tax distributable earnings	\$ 249,116	\$ 24,101	\$ 129,203	\$ 55,882	\$ 25,531	\$ (10,244) \$ 473,589

	Fortress Unconsolidated Subtotal	Consolidation of Fortress Funds	Eliminations	Reconciliation to GAAP	Fortress Consolidated
Revenues	\$ 884,721	\$ 317,114	\$ (269,607)	\$ (497)	\$ 931,731
Pre-tax distributable earnings/net income	\$ 473,589	\$ (326,375)	\$ 326,375	\$ (504,134)	\$ (30,545)

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Three Months Ended September 30, 2007	Private Equity Funds	Castles	Liquid Hedge Funds	Hybrid Hedge Funds	Principal Investments	Unallocated	Fortress Unconsolidated Subtotal
Segment revenues							
Management fees	\$ 35,133	\$ 12,131	\$ 44,351	\$ 33,376	\$	\$	\$ 124,991
Incentive income	83,592	691	(210)	9,463			93,536
Segment revenues total	\$ 118,725	\$ 12,822	\$ 44,141	\$ 42,839	\$	\$	\$ 218,527
Pre-tax distributable earnings	\$ 82,273	\$ 5,163	\$ 23,815	\$ 6,569	\$ (4,110)	\$ (2,958)	\$ 110,752

	Fortress Unconsolidated Subtotal	Reconciliation to GAAP	Fortress Consolidated
Revenues	\$ 218,527	\$ 28,755	\$ 247,282
Pre-tax distributable earnings/net income	\$ 110,752	\$ (148,309)	\$ (37,557)

Reconciling items between segment measures and GAAP measures:

	Nine Months Ended September 30, 2007	Three Months Ended September 30, 2007
<u>Adjustments from segment revenues to GAAP revenues</u>		
Adjust management fees*	\$ 488	\$ 163
Adjust incentive income	(48,316)	13,477
Adjust income from the receipt of options	2,006	
Other revenues*		
Adjust management fees from non-affiliates	(2,879)	(163)
Adjust incentive income from non-affiliates	(431)	(323)
Adjust other revenues	48,635	15,601

		45,325		15,115
Total adjustments	\$	(497)	\$	28,755

* Segment revenues do not include GAAP other revenues, except to the extent they represent management fees or incentive income; such revenues are included elsewhere in the calculation of distributable earnings.

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	Nine Months Ended September 30, 2007	Three Months Ended September 30, 2007
<u>Adjustments from pre-tax distributable earnings to GAAP net income</u>		
Adjust incentive income		
Incentive income received from private equity funds, subject to contingent repayment	\$ (191,948)	\$ (53,126)
Incentive income accrued from private equity funds, no longer subject to contingent repayment	309,275	97,333
Incentive income received from private equity funds, not subject to contingent repayment	(73,644)	(22,168)
Incentive income received from hedge funds, subject to annual performance achievement	(91,999)	(8,562)
Reserve for clawback	(48,316)	13,477
Adjust other income		
Distributions of earnings from equity method investees**	(13,741)	(1,415)
Earnings (losses) from equity method investees**	(49,762)	(30,514)
Gains (losses) on options in equity method investees, treated as derivatives	(82,810)	(58,354)
Adjust income from the receipt of options	2,006	
	(144,307)	(90,283)
Adjust employee compensation		
Adjust employee equity-based compensation expense (including Castle options assigned)	(99,014)	(31,651)
Adjust employee portion of incentive income from private equity funds, accrued prior to the realization of incentive income		19,657
Adjust employee portion of incentive income from one private equity fund, not subject to contingent repayment	5,427	5,427
	(93,587)	(6,567)
Adjust Principals equity-based compensation expense	(612,981)	(232,048)

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Adjust Principals interests related to Fortress Operating Group units	402,294	154,893
Adjust income taxes	(7,237)	12,219
Total adjustments	\$ (504,134)	\$ (148,309)

** This adjustment relates to all of the Castles, private equity Fortress Funds and hedge fund special investment accounts in which Fortress has an investment. On an unconsolidated basis, each of these funds is accounted for under the equity method.

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Fortress's depreciation expense by segment was as follows:

	Private Equity Funds	Castles	Liquid Hedge Funds	Hybrid Hedge Funds	Unallocated	Total
Nine Months Ended September 30,						
2008	\$ 841	\$ 538	\$ 2,302	\$ 2,195	\$ 1,433	\$ 7,309
2007	\$ 747	\$ 633	\$ 1,860	\$ 1,926	\$ 1,257	\$ 6,423
Three Months Ended September 30,						
2008	\$ 294	\$ 165	\$ 808	\$ 709	\$ 461	\$ 2,437
2007	\$ 265	\$ 207	\$ 649	\$ 697	\$ 412	\$ 2,230

11. SUBSEQUENT EVENTS

These financial statements include a discussion of material events which have occurred subsequent to September 30, 2008 (referred to as subsequent events) through November 12, 2008. Events subsequent to that date have not been considered in these financial statements.

In October 2008, one of the private equity Fortress Funds redeemed an aggregate of \$76.8 million in preferred equity investments previously made by three of the Principals in such fund. In October and November 2008, three of the Principals made new preferred equity investments in the net aggregate amount of \$72.2 million in another of the private equity Fortress Funds. As of November 12, 2008, the Principals had an aggregate of \$90.4 million invested in preferred equity interests of the private equity Fortress Funds and their subsidiaries.

In October and November 2008, the liquid hedge funds received redemption notices totaling \$1.7 billion, most of which are still subject to being rescinded, which would become payable on or before the end of January 2009 (and these funds may receive additional redemption requests). The hybrid funds received notices requesting the return of \$1.9 billion of capital to investors, most of which are still subject to being rescinded, which would be paid over time as the underlying investments are liquidated, in accordance with the governing documents of the applicable funds. During this period, such amounts would continue to be subject to management fees and, as applicable, incentive income.

On November 12, 2008, Fortress entered into an additional amendment to its credit agreement (Note 4). The amendment, among other things: (i) modified the definition of EBITDA, which is used to calculate the Consolidated Leverage Ratio, to exclude any realized or unrealized gains and losses on investments and to reflect private equity incentive income clawbacks on a cash basis; (ii) modified the financial covenants by (a) reducing the amount of required investment assets to \$975 million (less any future term loan repayments) and (b) changing the required

Consolidated Leverage Ratios for the quarters ending June 30 and September 30, 2009 from 2.5 to 1.0 to 2.75 to 1.0; (iii) increased the rate on LIBOR loans to LIBOR + 2.00% (and Base Rate loans to the prime rate + 1.00%) this rate is no longer subject to change pursuant to a ratings-based pricing grid; (iv) established the commitment fee for the unused portion of the revolving credit facility at 0.25% this rate is also no longer subject to change pursuant to a ratings-based pricing grid; (v) reduced the revolving credit facility commitments to \$125 million; (vi) established a requirement that outstanding term loans be prepaid with 25% of the amount by which EBITDA for any twelve-month period exceeds \$370 million (unless and until the amount of outstanding term loans equals or is less than \$250 million); (vii) required \$50 million of additional term loan repayments (\$25 million in July of 2009 and 2010); (viii) established a requirement that the borrower cash collateralize the letter of credit obligations of distressed lenders under certain circumstances, including lender non-funding or bankruptcy; and (ix) established an event of default under certain circumstances where the borrower, any guarantor or certain of their subsidiaries are required to make promote clawback payments in excess of \$20 million during any calendar year. In connection with

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)

the amendment, Fortress prepaid \$75 million of the outstanding term loans. Fortress is currently evaluating the impact that recording this amendment will have on its fourth quarter 2008 financial statements.

12. PRO FORMA FINANCIAL INFORMATION

The unaudited pro forma financial information is presented in order to provide data which is more comparable to the 2008 period as a result of the deconsolidation (Note 1).

The unaudited pro forma financial information presented below was derived from the application of pro forma adjustments to the combined and consolidated financial statements of Fortress, as applicable, to give effect to the deconsolidation of the consolidated Fortress Funds. The deconsolidation transaction occurred effective March 31, 2007 as described in Note 1. The unaudited pro forma statement of operations and statement of cash flows information for the nine months ended September 30, 2007 have been prepared as if this transaction had occurred on January 1, 2007.

The unaudited pro forma effects of the deconsolidation of the Fortress Funds on the statement of operations information are as follows:

	Nine Months Ended September 30, 2007		
	Consolidated	Deconsolidation Adjustments	Pro Forma Deconsolidated
Revenues			
Management fees from affiliates	\$ 286,956	\$ 53,072	\$ 340,028
Incentive income from affiliates	283,879	211,682	495,561
Other revenues	51,866	(3,232)	48,634
Interest and dividend income investment company holdings	309,030	(309,030)	
	931,731	(47,508)	884,223
Expenses			
Interest expense			
Investment company holdings	132,620	(132,620)	
Other	26,016		26,016
Compensation and benefits	507,003	(9,805)	497,198
Principals agreement compensation	612,981		612,981
General, administrative and other	80,320	(22,024)	58,296
Depreciation and amortization	6,423		6,423

1,365,363	(164,449)	1,200,914
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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)

	Nine Months Ended September 30, 2007		
	Consolidated	Deconsolidation Adjustments	Pro Forma Deconsolidated
Other income			
Gains (losses) from investments			
Investment company holdings	(647,477)	647,477	
Other investments			
Net realized gains	831		831
Net realized gains from affiliate investments	143,017		143,017
Net unrealized gains (losses)	(2,597)		(2,597)
Net unrealized gains (losses) from affiliate investments	(221,745)		(221,745)
Earnings (losses) from equity method investees	(23,289)	3,231	(20,058)
	(751,260)	650,708	(100,552)
Income (loss) before Deferred Incentive Income, Principals and Others Interests in Income of Consolidated Subsidiaries and Income Taxes	(1,184,892)	767,649	(417,243)
Deferred incentive income	307,034	(307,034)	
Principals and others interests in loss (income) of consolidated subsidiaries	854,550	(460,615)	393,935
Income (Loss) Before Income Taxes	(23,308)		(23,308)
Income tax expense	(7,237)		(7,237)
Net Income (Loss)	\$ (30,545)	\$	\$ (30,545)

Total comprehensive income for this period was calculated as follows:

Comprehensive income		
Net income (loss)		\$ (30,545)
Foreign currency translation		(24)
Net unrealized (loss) on derivatives designated as cash flow hedges		(8)
Net unrealized gain on securities available for sale		749
Comprehensive income (loss) from equity method investees		(9,299)
Allocation to Principals and others interests un equity of consolidated subsidiaries		5,082

Total comprehensive income	\$	(34,045)
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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)

The unaudited pro forma effects of the deconsolidation of the Fortress Funds on the statement of cash flows information are as follows:

	Nine Months Ended September 30, 2007		
	Consolidated	Deconsolidation Adjustments	Pro Forma Deconsolidation
Cash Flows From Operating Activities			
Net income (loss)	\$ (30,545)	\$	\$ (30,545)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities			
Depreciation and amortization	6,423		6,423
Other amortization and accretion	1,876	(483)	1,393
(Earnings) losses from equity method investees	23,289	(3,231)	20,058
Distributions of earnings from equity method investees	9,765	3,231	12,996
(Gains) losses from investments	727,971	(647,477)	80,494
Recognition of deferred incentive income		(156,326)	(156,326)
Deferred incentive income	(355,381)	307,034	(48,347)
Principals and others interests in income of consolidated subsidiaries	(854,550)	460,615	(393,935)
Deferred tax expense	(16,775)		(16,775)
Options received from affiliates	(2,006)		(2,006)
Assignments of options to employees	4,627		4,627
Equity-based compensation	713,850		713,850
Cash flows due to changes in			
Cash held at consolidated subsidiaries and restricted cash	(166,199)	166,199	
Due from affiliates	214,558	65,445	280,003
Receivables from brokers and counterparties and other assets	(23,024)	32,131	9,107
Accrued compensation and benefits	92,475	(144)	92,331
Due to affiliates	(6,392)	8,594	2,202
Deferred incentive income		142,041	142,041
Due to brokers and counterparties and other liabilities	118,098	(87,935)	30,163
Investment company holdings			
Purchases of investments	(5,105,865)	5,105,865	
Proceeds from sale of investments	3,398,739	(3,398,739)	
Net cash provided by (used in) operating activities	(1,249,066)	1,996,820	747,754

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)

	Nine Months Ended September 30, 2007		
	Consolidated	Deconsolidation Adjustments	Pro Forma Deconsolidation
Cash Flows From Investing Activities			
Purchase of other loan and security investments	(10,578)		(10,578)
Proceeds from sale of other loan and security investments	317		317
Contributions to equity method investees	(410,447)	(148,812)	(559,259)
Distributions of capital from equity method investees	115,190	22,685	137,875
Proceeds from sale of equity method investments	29,071		29,071
Cash received on settlement of derivatives	132		132
Purchase of fixed assets	(8,907)	125	(8,782)
Proceeds from disposal of fixed assets	2,532		2,532
Net cash used in investing activities	(282,690)	(126,002)	(408,692)
Cash Flows From Financing Activities			
Borrowings under debt obligations	1,999,070	(1,564,070)	435,000
Repayments of debt obligations	(2,010,025)	1,312,872	(697,153)
Payment of deferred financing costs	(6,813)	660	(6,153)
Issuance of Class A shares to Nomura	888,000		888,000
Issuance of Class A shares in initial public offering	729,435		729,435
Costs related to initial public offering	(76,766)		(76,766)
Dividends and dividend equivalents paid	(43,237)		(43,237)
Fortress Operating Group capital distributions to Principals	(219,112)		(219,112)
Purchase of Fortress Operating Group units from Principals	(888,000)		(888,000)
Principals and others interests in equity of consolidated subsidiaries contributions	3,183,792	(3,183,682)	110
Principals and others interests in equity of consolidated subsidiaries distributions	(1,916,216)	1,563,402	(352,814)
Net cash provided by (used in) financing activities	1,640,128	(1,870,818)	(230,690)
Net Increase in Cash and Cash Equivalents	108,372		108,372
Cash and Cash Equivalents, Beginning of Period	61,120		61,120
Cash and Cash Equivalents, End of Period	\$ 169,492	\$	\$ 169,492

NOTE 13 CONSOLIDATING FINANCIAL INFORMATION

The consolidating financial information presents the balance sheet, statement of operations and statement of cash flows for Fortress Operating Group (on a combined basis) and Fortress Investment Group LLC (including its consolidated subsidiaries other than those within Fortress Operating Group) on a deconsolidated basis, as well as the related eliminating entries for intercompany balances and transactions, which sum to Fortress Investment Group's consolidated financial statements as of, and for the nine months ended, September 30, 2008.

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)

Fortress Operating Group includes all of Fortress's operating and investing entities. The upper tier Fortress Operating Group entities are the obligors on Fortress's credit agreement (Note 4). Segregating the financial results of this group of entities provides a more transparent view of the capital deployed in Fortress's businesses and the relevant ratios for borrowing entities.

The consolidating balance sheet information is as follows:

	As of September 30, 2008			
	Fortress Operating Group Combined	Fortress Investment Group LLC Consolidated(A)	Intercompany Eliminations	Fortress Investment Group LLC Consolidated
	(Dollars in tables in thousands, except share data)			
Assets				
Cash and cash equivalents	\$ 258,426	\$ 826	\$	\$ 259,252
Due from affiliates	49,429			49,429
Investments				
Equity method investees	949,709	48,306	(48,306)	949,709
Options in affiliates	137			137
Deferred tax asset	8,514	509,064		517,578
Other assets	72,193	6,579		78,772
	\$ 1,338,408	\$ 564,775	\$ (48,306)	\$ 1,854,877
Liabilities and Shareholders' Equity				
Liabilities				
Accrued compensation and benefits	\$ 146,702	\$	\$	\$ 146,702
Due to affiliates	1,913	393,595		395,508
Dividends payable				
Deferred incentive income	163,635			163,635
Debt obligations payable	750,000			750,000
Other liabilities	58,891	(1,165)		57,726
	1,121,141	392,430		1,513,571
Commitments and Contingencies				
Principals' and Others' Interests in				
Equity of Consolidated Subsidiaries	35,365	5,893	133,596	174,854
Shareholders' Equity				
Paid-in capital	1,381,565	538,619	(1,381,565)	538,619

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Retained earnings (accumulated deficit)	(1,202,007)	(373,004)	1,202,007	(373,004)
Accumulated other comprehensive income (loss)	2,344	837	(2,344)	837
	181,902	166,452	(181,902)	166,452
	\$ 1,338,408	\$ 564,775	\$ (48,306)	\$ 1,854,877

(A) Other than Fortress Operating Group.

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)

The consolidating statement of operations information is as follows:

	Nine Months Ended September 30, 2008			
	Fortress Operating Group Consolidated	Fortress Investment Group LLC Consolidated(A)	Intercompany Eliminations	Fortress Investment Group LLC Consolidated
	(Dollars in tables in thousands, except share data)			
Revenues				
Management fees from affiliates	\$ 447,928	\$	\$	\$ 447,928
Incentive income from affiliates	56,162			56,162
Other revenues	69,962	60		70,022
	574,052	60		574,112
Expenses				
Interest expense	29,375	330		29,705
Compensation and benefits	399,253			399,253
Principals agreement compensation	714,710			714,710
General, administrative and other	59,998	(146)		59,852
Depreciation and amortization	7,309			7,309
	1,210,645	184		1,210,829
Other Income (Loss)				
Gains (losses) from investments				
Net realized gains (losses)	(803)			(803)
Net realized gains (losses) from affiliate investments	(516)			(516)
Net unrealized gains (losses)				
Net unrealized gains (losses) from affiliate investees	(43,352)			(43,352)
Earnings (losses) from equity method investees	(113,550)	(185,425)	185,425	(113,550)
	(158,221)	(185,425)	185,425	(158,221)
Income (Loss) Before Principals and Others Interests in Income of	(794,814)	(185,549)	185,425	(794,938)

Consolidated Subsidiaries and Income

Taxes

Principals and others interests in (income)				
loss of consolidated subsidiaries	932		611,760	612,692
Income Before Income Taxes	(793,882)	(185,549)	797,185	(182,246)
Income tax benefit (expense)	(3,303)	3,636		333
Net Income (Loss)	\$ (797,185)	\$ (181,913)	\$ 797,185	\$ (181,913)

(A) Other than Fortress Operating Group.

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FORTRESS INVESTMENT GROUP LLC
(PRIOR TO JANUARY 17, 2007, FORTRESS OPERATING GROUP NOTE 1)

NOTES TO CONSOLIDATED AND COMBINED FINANCIAL STATEMENTS (Unaudited) (Continued)
SEPTEMBER 30, 2008
(dollars in tables in thousands, except share data)

The consolidating statement of cash flows information is as follows:

	Nine Months Ended September 30, 2008			
	Fortress Operating Group Consolidated	Fortress Investment Group LLC Consolidated(A)	Intercompany Eliminations	Fortress Investment Group LLC Consolidated
	(Dollars in tables in thousands, except share data)			
Cash Flows From Operating Activities				
Net income (loss)	\$ (797,185)	\$ (181,913)	\$ 797,185	\$ (181,913)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities				
Depreciation and amortization	7,309			7,309
Other amortization and accretion	3,401			3,401
(Earnings) losses from equity method investees	113,550	185,425	(185,425)	113,550
Distributions of earnings from equity method investees	9,386			9,386
(Gains) losses from investments	44,671			44,671
Deferred incentive income, net	(36,003)			(36,003)
Principals and others interests in income (loss) of consolidated subsidiaries	(932)		(611,760)	(612,692)
Deferred tax (benefit) expense	(3,842)	(4,455)		(8,297)
Equity-based compensation	853,861			853,861
Cash flows due to changes in				
Due from affiliates	90,724			90,724
Other assets	(9,396)	(3,656)		(13,052)
Accrued compensation and benefits	(94,665)	1,199		(93,466)
Due to affiliates	(379)	329		(50)
Deferred incentive income	26,077			26,077
Other liabilities	27,184	2,892		30,076
Net cash provided by (used in) operating activities	233,761	(179)		233,582
Cash Flows From Investing Activities				
Contributions to equity method investees	(135,036)			(135,036)
	211,162	61,730	(61,730)	211,162

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Distributions of capital from equity method investees				
Purchase of fixed assets	(9,120)			(9,120)
Proceeds from disposal of fixed assets	53			53
Net cash provided by (used in) investing activities	67,059	61,730	(61,730)	67,059
Cash Flows From Financing Activities				
Borrowings under debt obligations	450,000			450,000
Repayments of debt obligations	(235,000)			(235,000)
Payment of deferred financing costs	(5,020)			(5,020)
Dividends and dividend equivalents paid	(287,891)	(63,855)	270,720	(81,026)
Principals and others interests in consolidated subsidiaries distributions	145			145
Principals and others interests in consolidated subsidiaries contributions	(61,907)		(208,990)	(270,897)
Net cash provided by (used in) financing activities	(139,673)	(63,855)	61,730	(141,798)
Net Increase (Decrease) in Cash and Cash Equivalents	161,147	(2,304)		158,843
Cash and Cash Equivalents, Beginning of Period	97,279	3,130		100,409
Cash and Cash Equivalents, End of Period	\$ 258,426	\$ 826	\$	\$ 259,252

(A) Other than Fortress Operating Group.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(tables in thousands except as otherwise indicated and per share data)

The following discussion should be read in conjunction with Fortress Investment Group's consolidated and combined financial statements and the related notes (referred to as consolidated financial statements or historical consolidated financial statements) included within this Quarterly Report on Form 10-Q. This discussion contains forward-looking statements that are subject to known and unknown risks and uncertainties. Actual results and the timing of events may differ significantly from those expressed or implied in such forward-looking statements due to a number of factors, including those included in Part II, Item 1A, Risk Factors and elsewhere in this Quarterly Report on Form 10-Q.

During the first quarter of 2007, we consummated a number of significant transactions, including the Nomura transaction, the formation transactions, our initial public offering, and the deconsolidation of a number of Fortress Funds. The deconsolidation of the Fortress Funds has had significant effects on many of the items within our financial statements but had no net effect on net income or equity. Since the deconsolidation did not occur until March 31, 2007, the statement of operations and the statement of cash flows for the nine months ended September 30, 2007 are presented including these funds on a consolidated basis for the period prior to deconsolidation. The pro forma effects of the deconsolidation on these financial statements are described in Note 12 to Part I, Item 1, Financial Statements Pro Forma Financial Information.

General

Our Business

Fortress is a leading global alternative asset manager with approximately \$34.3 billion in AUM as of September 30, 2008. We raise, invest and manage private equity funds and hedge funds. We earn management fees based on the size of our funds, incentive income based on the performance of our funds, and investment income from our principal investments in those funds. We invest capital in each of our businesses.

As of September 30, 2008, we managed alternative assets in two core businesses:

Private Equity Funds – a business that manages approximately \$17.0 billion of AUM comprised of two business segments: (i) funds that primarily make significant, control-oriented investments in North America and Western Europe, with a focus on acquiring and building asset-based businesses with significant cash flows. We also manage a family of long dated value funds focused on investing in undervalued assets with limited current cash flows and long investment horizons; and (ii) publicly traded alternative investment vehicles, which we refer to as Castles, that invest primarily in real estate and real estate related debt investments.

Hedge Funds – a business that manages approximately \$17.3 billion of AUM comprised of two business segments; (i) hybrid hedge funds which make highly diversified investments globally in assets, opportunistic lending situations and securities through the capital structure with a value orientation, as well as investment funds managed by external managers; and (ii) liquid hedge funds which invest globally in fixed income, currency, equity and commodity markets and related derivatives to capitalize on imbalances in the financial markets.

In addition, we treat our principal investments in these funds as a distinct business segment.

Managing Business Performance

We conduct our management and investment business through the following five primary segments: (i) private equity funds, (ii) Castles (iii) liquid hedge funds, (iv) hybrid hedge funds, and (v) principal investments in those funds as well as cash that is available to be invested. These segments are differentiated based on the varying investment strategies of the funds we manage in each segment.

The amounts not allocated to a segment consist primarily of certain general and administrative expenses. Where applicable, portions of the general and administrative expenses have been allocated between the segments.

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Management makes operating decisions and assesses performance with regard to each of our primary segments based on financial data that is presented without the consolidation of any Fortress Funds. Accordingly, segment data for these segments is reflected on an unconsolidated basis, even for periods prior to the deconsolidation. Management also assesses our segments on a Fortress Operating Group and pre-tax basis, and therefore adds back the interests in consolidated subsidiaries related to Fortress Operating Group units (held by the principals) and income tax expense.

Management assesses the net performance of each segment based on its distributable earnings. Distributable earnings is not a measure of cash generated by operations which is available for distribution. Rather distributable earnings is a supplemental measure of the value created during any period which management uses in its determination of its periodic distributions to its dividend paying share and unit holders. Distributable earnings should not be considered as an alternative to cash flow in accordance with GAAP or as a measure of our liquidity, and is not necessarily indicative of cash available to fund cash needs (including dividends and distributions).

We believe that the presentation of distributable earnings enhances a reader's understanding of the economic operating performance of our segments. For a more detailed discussion of distributable earnings and how it reconciles to our GAAP net income (loss), see Results of Operations Segments Analysis below.

Market Considerations

Our revenues consist primarily of (i) management fees based generally on the size of our funds, (ii) incentive income based on the performance of our funds and (iii) investment income from our investments in those funds. Our ability to maintain and grow our revenues both at Fortress and within our funds depends on our ability to attract new capital and investors, secure investment opportunities, obtain financing for transactions, consummate investments and deliver attractive risk-adjusted returns. Our ability to execute this investment strategy depends upon a number of market conditions, including:

The strength and liquidity of U.S. and global financial institutions and the financial system.

Many market participants have become increasingly uncertain about the health of a number of financial institutions as well as the financial system in general. Continuing write-downs and capital related issues in the financial services industry have contributed to the recent wave of significant events affecting financial institutions, including the insolvency of Lehman Brothers, the government's placing Fannie Mae, Freddie Mac and AIG under its supervision and the announced distressed sales of all or portions of Bear Stearns, Merrill Lynch, Wachovia and Washington Mutual. These events have impacted the credit and equity markets and global economy in a number of ways (some of which are discussed in more detail below under The strength and liquidity of the U.S. and global equity and debt markets). In addition, certain of these institutions serve as key counterparties for a tremendous number of derivatives and other financial instruments held by Fortress and our funds. The consolidation and elimination of counterparties has increased our concentration of counterparty risk, decreased the universe of potential counterparties and reduced our ability to obtain competitive financing rates. Moreover, the insolvency of Lehman Brothers affected some of our funds in various ways. For example, some of our hedge funds had prime brokerage accounts with Lehman Brothers, and Lehman Brothers was the counterparty on a number of these funds' derivatives, repurchase agreements and other financial instruments. These funds are working to close out such arrangements, and we do not currently expect losses as a result of the Lehman insolvency to have a material effect on the net asset value of any Fortress Fund or on Fortress. However, due to the sudden nature of Lehman's insolvency, the complexity and ambiguity of both the contractual arrangements and applicable regulations, this process will take time, may be expensive and may result in one or more funds receiving only a portion of the amount they are owed (or potentially receiving nothing at all). Additional failures of financial institutions, particularly those who serve as counterparties to our financing arrangements, would have a meaningfully negative impact on the financial markets in which we operate and could have a meaningfully negative impact on Fortress and one of more of our funds.

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The strength and liquidity of the U.S. and global equity and debt markets.

Strong equity market conditions enable our private equity funds to increase the value, and effect realizations, of their portfolio company investments. In addition, strong equity markets make it generally easier for our funds that invest in equities to generate positive investment returns. The condition of debt markets also has a meaningful impact on our business. Several of our funds make investments in debt instruments, which are assisted by a strong and liquid debt market. In addition, our funds borrow money to make investments. Our funds utilize leverage in order to increase investment returns, which ultimately drive the performance of our funds. Furthermore, we utilize debt to finance our investments in our funds and for working capital purposes.

Although equity and debt market conditions had been favorable for a number of years, the debt market conditions began to deteriorate in mid-2007, as the United States experienced considerable turbulence in the housing and sub-prime mortgage markets, which negatively affected other fixed income markets. The difficult conditions in the fixed income markets prompted lenders to cease committing to new senior loans and other debt, which, in turn, made it extremely difficult to finance new and pending private equity acquisitions or to refinance existing debt. Recently announced private equity-led acquisitions have been smaller, less levered, and subject to more restrictive debt covenants than acquisitions done prior to the disruption.

As the turbulence continued and its intensity increased, equity market conditions also began to deteriorate in the latter part of 2007 as concerns of an economic slowdown began to affect equity valuations. The resulting reduction in liquidity and increase in volatility caused several commercial and investment banks, hedge funds and other financial institutions to reduce the carrying value of some of their fixed income holdings, which further reduced the liquidity of debt and, to a lesser extent, equity instruments. Although the United States and other governments took a number of significant steps to improve market conditions, such efforts to date have not brought stability or liquidity to the capital markets, and we cannot predict the future conditions of these markets or the impact of such conditions on our business.

The current market conditions have negatively impacted our business in several ways:

There currently is less debt and equity capital available in the market relative to the levels available in recent years, which, coupled with recent additional margin collateral requirements imposed by lenders on some types of investments, debt and derivatives, has increased the importance of maintaining sufficient liquidity without relying upon additional infusions of capital from the debt and equity markets. Based on cash balances, committed financing and short-term operating cash flows, in the judgment of management we and the funds we manage have sufficient liquidity in the current market environment. However, maintaining this liquidity rather than investing available capital, and the reduced availability of attractive financing, has reduced our returns. The dislocation of values and associated decreased liquidity in the global equity and debt markets have caused a material depreciation in equity and fixed income asset values, greater price volatility and weaker economic conditions around the globe.

There has been a reduction in market trading activity. This reduction and concern over market conditions have resulted in significant reductions in valuations by third party brokers and pricing agents.

The per share market prices of the investments held by our private equity funds in public companies have decreased substantially. This, in turn, has contributed to a significant decrease in our public company surplus. A decrease in this surplus hinders our ability to realize gains within these funds and therefore our ability to earn incentive income. Furthermore, the disruptions in the debt and equity markets have made exit strategies for private investments more difficult to execute as potential buyers have difficulty obtaining attractive financing and the demand for IPOs has been greatly reduced.

These conditions have made it more difficult to generate positive investment returns and have contributed to increased redemption requests from investors throughout the hedge fund industry, and a number of our funds have been affected by this trend.

As a result of the above factors:

Our year-to-date distributable earnings is lower than the amount of dividends we have paid in respect of such period, and we did not pay a dividend for the third quarter. The decision to pay a dividend, as well as

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the amount of any dividends paid, is subject to change at the discretion of our board of directors based upon a number of factors, including actual and projected distributable earnings.

Our share of the NAV of certain fund investments, including certain investments on which we have received incentive returns, has declined below their related carrying amounts for distributable earnings purposes. During the nine months ended September 30, 2008, we will have taken \$69.2 million of impairments related to such funds for distributable earnings purposes. While we expect aggregate returns on our other private equity fund investments to ultimately exceed their carrying amount, if such funds were liquidated at their current NAV (although we have no present intention of doing so), the result would be additional impairment and reserves of approximately \$118.9 million.

Our flagship liquid hedge fund, which generally has quarterly liquidity terms, received a total of \$0.9 billion in redemption requests for the notification period ended September 30, 2008 which were paid in October 2008, and in addition has received redemption requests for notification periods subsequent to September 30, 2008, most of which are still subject to being rescinded, for an additional \$1.7 billion, which would become payable on or before the end of January 2009 (and these funds may receive additional redemption requests). In comparison, the same liquid hedge fund received and paid redemption requests for a total of \$0.3 billion related to the third and fourth quarters of 2007. Investors in our flagship hybrid hedge funds are permitted to request that their capital be returned on an annual basis (the notice date for which is 90 days before each year end), and such returns of capital are paid over time as the underlying investments are liquidated, in accordance with the governing documents of the applicable funds. During this period, such amounts continue to be subject to management fees and, as applicable, incentive income. Return of capital requests for those hybrid hedge funds, most of which are still subject to being rescinded, totaled approximately \$1.9 billion for the 2008 notice date. In comparison, the same hybrid hedge funds received return of capital requests for a total of \$0.6 billion for the 2007 notice date.

As a result of not meeting the incentive income thresholds with respect to current investors, the incentive income from a significant portion of our hybrid and liquid hedge funds has been discontinued for an indefinite period of time. Returns earned on capital from new investors continue to be incentive income eligible. Unrealized losses in a significant portion of our private equity funds have resulted in substantially higher future returns being required before we earn incentive income from such funds.

The current ratio of our distributable earnings to our AUM is lower than it has been historically, and it is reasonably likely that the future ratios may also be below historic levels for an indeterminate period of time.

The strength of, and competitive dynamics within, the alternative asset management industry, including the amount of capital invested in, and withdrawn from, alternative investments.

The strength of the alternative asset management industry, and our competitive strength relative to our peers, are dependent upon several factors, including, among other things, (1) the investment returns alternative asset managers can provide relative to other investment options, (2) the amount of funds investors allocate to alternative asset managers and (3) our performance relative to our competitors and the related impact on our ability to attract new capital.

First, the strength of the alternative asset management industry is dependent upon the investment returns alternative asset managers can provide relative to other investment options. This factor depends, in part, on the interest rate and credit spreads (which represent the yield demanded on financial instruments by the market in comparison to a benchmark rate, such as the relevant U.S. treasury rate or LIBOR) available on other investment products because as interest rates rise and/or spreads widen, returns available on such investments would tend to increase and, therefore,

become more attractive relative to the returns offered by investment products offered by alternative asset managers. We have benefited in recent years from relatively tight interest rate spreads, which have allowed us and the funds we manage to obtain financing for investments at attractive rates and made our investment products attractive relative to many other products. Over the past year, interest rate spreads have widened significantly. In addition to potentially reducing the relative attractiveness of our investment products, this widening will typically increase our costs when financing our investments using debt, which, in turn, reduces

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the net return we can earn on those investments. Furthermore, wider spreads reduce the value of investments currently owned by our funds, including investments in our hedge funds. A reduction in the value of our hedge funds investments directly impacts our management fees and incentive income from such funds. As a result, this dynamic could slow capital flow to the alternative investment sector.

A second and related factor is the amount of capital invested with such managers. Over the past several years, institutions, high net worth individuals and other investors (including sovereign wealth funds) have increased their allocations of capital to the alternative investment sector. However, investors have recently begun reducing the amount of capital they are allocating to certain alternative asset investment products, particularly hedge funds, for two reasons. First, as discussed above, challenging market conditions have reduced the returns generated by hedge funds, with many funds posting negative returns this year. Second, the lack of available credit has prompted many investors to maximize their cash holdings. Because the terms of many hedge funds allow investors to redeem their capital periodically (as opposed to most private equity funds, which do not allow redemptions), investors have begun redeeming their investments at rates that are generally higher than redemptions rates in previous years. This wave of redemptions may affect the investment decisions, and impair the viability, of many hedge funds who may not have sufficient cash on hand to satisfy redemption requests and may thus be forced either to sell assets at distressed prices in order to generate cash or take other measures. As discussed above, certain of our hedge funds have recently received higher levels of redemption requests than those received in previous years.

The third factor, which most directly impacts our results, is our investment performance relative to other investment alternatives, including products offered by other alternative asset managers. As a leader in the alternative asset management sector based on the size, diversity and historical performance of our funds, we have been able to attract a significant amount of new capital. However, as noted above, current market conditions have reduced the flow of new capital into the alternative asset management sector, and we have recently experienced stronger headwinds in our capital raising efforts. As a result of market conditions, our net capital raised to date during 2008 has been lower than our expectations at the beginning of the year.

Summary

While short-term disruptions in the markets, with respect to equity prices, interest rates, credit spreads or other market factors, including market liquidity, may adversely affect our existing positions, we believe such disruptions generally present significant new opportunities for investment, particularly in distressed asset classes. Our ability to take advantage of these opportunities will depend on our ability to access debt and equity capital, both at Fortress and within the funds. No assurance can be given that future trends will not be disadvantageous to us, particularly if current challenging conditions persist or intensify.

We do not currently know the full extent to which this disruption will affect us or the markets in which we operate. If the disruption continues, or results in a permanent, fundamental change in the credit markets, we and the funds we manage may experience further tightening of liquidity, reduced earnings and cash flow, impairment charges, increased margin requirements, as well as challenges in maintaining our reputation, raising additional capital, obtaining investment financing and making investments on attractive terms, and may need to make corresponding fundamental changes in our investment practices. However, to date we have been able to continue raising capital for our funds, on a net basis, both through new and existing funds, which serves both to increase our AUM and our management fee income and to give us a significant amount of capital available to be invested at a time when we believe attractive returns in distressed and other asset classes are available.

Table of Contents**Results of Operations**

The following is a discussion of our results of operations as reported under GAAP. For a detailed discussion of distributable earnings and revenues from each of our segments, see **Segment Analysis** below.

Effective March 31, 2007, we deconsolidated our Fortress Funds and, subsequent to this transaction, our results of operations are presented on a deconsolidated basis. To provide better insight and understanding of our results of operations based on our current structure, and a better comparative basis, the following table compares results of operations for the nine months ended September 30, 2008 to our pro forma results of operations for the nine months ended September 30, 2007 on a deconsolidated basis. On a GAAP basis, excluding pro forma adjustments, we had broad decreases across all of our financial statement line items for the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007 as a result of the deconsolidation.

	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007 Deconsolidation Consolidated	Pro Forma Deconsolidated	Variance
Revenues				
Management fees from affiliates	\$ 447,928	\$ 286,956	\$ 53,072	\$ 340,028
Incentive income from affiliates	56,162	283,879	211,682	495,561
Other revenues	70,022	51,866	(3,232)	48,634
Interest and dividend income investment company holdings		309,030	(309,030)	
	574,112	931,731	(47,508)	884,223
				(310,111)
Expenses				
Interest expense	29,705	158,636	(132,620)	26,016
Compensation and benefits	399,253	507,003	(9,805)	497,198
Principals agreement compensation	714,710	612,981		612,981
General, administrative and other expense (including depreciation and amortization)	67,161	86,743	(22,024)	64,719
	1,210,829	1,365,363	(164,449)	1,200,914
				9,915
Other Income (Loss)				
Net gains (losses) investment company holdings		(647,477)	647,477	
Net gains (losses) other investments	(44,671)	(80,494)		(80,494)
Earnings (losses) from equity method investees	(113,550)	(23,289)	3,231	(20,058)
	(158,221)	(751,260)	650,708	(100,552)
				(57,669)

Income (Loss) Before Deferred Incentive Income, Principals and Others Interests in Income of Consolidated Subsidiaries and Income Taxes	(794,938)	(1,184,892)	767,649	(417,243)	(377,695)
Deferred incentive income		307,034	(307,034)		
Principals and others interests in loss (income) of consolidated subsidiaries	612,692	854,550	(460,615)	393,935	218,757
Income (Loss) Before Income Taxes	(182,246)	(23,308)		(23,308)	(158,938)
Income tax benefit (expense)	333	(7,237)		(7,237)	7,570
Net Income (Loss)	\$ (181,913)	\$ (30,545)	\$	\$ (30,545)	\$ (151,368)

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	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Variance
Revenues			
Management fees from affiliates	\$ 154,266	\$ 124,991	\$ 29,275
Incentive income from affiliates	718	106,690	(105,972)
Other revenues	30,152	15,601	14,551
	185,136	247,282	(62,146)
Expenses			
Interest expense	9,481	7,285	2,196
Compensation and benefits	134,774	101,703	33,071
Principals agreement compensation	239,976	232,048	7,928
General, administrative and other expense (including depreciation and amortization)	25,973	19,642	6,331
	410,204	360,678	49,526
Other Income (Loss)			
Net gains (losses) other investments	(10,099)	(58,198)	48,099
Earnings (losses) from equity method investees	(37,921)	(30,716)	(7,205)
	(48,020)	(88,914)	40,894
Income (Loss) Before Deferred Incentive Income, Principals and Others Interests in Income of Consolidated Subsidiaries and Income Taxes	(273,088)	(202,310)	(70,778)
Principals and others interests in loss (income) of consolidated subsidiaries	210,012	152,534	57,478
Income (Loss) Before Income Taxes	(63,076)	(49,776)	(13,300)
Income tax benefit (expense)	5,636	12,219	(6,583)
Net Income (Loss)	\$ (57,440)	\$ (37,557)	\$ (19,883)

Factors Affecting Our Business

During the periods discussed herein, the following are significant factors which have affected our business and materially impacted our results of operations:

changes in our AUM;

level of performance of our funds;

growth of our fund management and investment platform and our compensation structure to sustain that growth; and

the income tax expense as a result of our reorganization which occurred in 2007.

Fee Paying Assets Under Management

We measure AUM by reference to the fee paying assets we manage, including the capital we have the right to call from our investors due to their capital commitments. As a result of raising new funds with sizeable capital commitments for our private equity funds, raising capital for our Castles, and increases in the NAVs of our hedge funds from new investor capital and their retained profits, our AUM has increased significantly over the periods discussed.

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Average Fee Paying AUM

Average fee paying AUM represents the reference amounts upon which our management fees are based. The reference amounts for management fee purposes are: (i) capital commitments or invested capital (or NAV, if lower) for the private equity funds, which in connection with funds raised after March 2006 includes the mark-to-market value on public securities held within the fund, (ii) contributed capital for the Castles, or (iii) the NAV for hedge funds.

Management Fees

Significant growth of our average AUM has had a positive effect on our management fee revenues. As the AUM in our funds grew, so did the management fees we earned. Depending on the timing of capital contributions in a given period, the full economic benefits of an increase in AUM may not be recognized until the following period.

Performance of Our Funds

Incentive Income

Incentive income is calculated as a percentage of profits earned by the Fortress Funds. Incentive income that is not subject to contingent repayment is recorded as earned, as incentive income from affiliates. Incentive income received from funds that continues to be subject to contingent repayment is deferred and recorded as a deferred incentive income liability until the related contingency is resolved. The contingencies related to a portion of the incentive income we have received from certain private equity Fortress Funds have been resolved.

Fund Management and Investment Platform

In order to accommodate the increasing demands of our funds' rapidly growing investment portfolios, we have expanded our investment platforms, which are comprised primarily of our people, financial and operating systems and supporting infrastructure. Expansion of our investment platform required increases in headcount, consisting of newly hired investment professionals and support staff, as well as leases and associated improvements to corporate offices to house the increasing number of employees, and related augmentation of systems and infrastructure. Our headcount increased from 774 employees as of September 30, 2007 to 900 employees as of September 30, 2008. This resulted in increases in our compensation, office related and other personnel related expenses. In addition, in conjunction with and subsequent to our initial public offering, we have implemented an equity-based compensation plan described in Note 7 to Part I, Item 1, Financial Statements Equity-Based and Other Compensation as a means to provide an additional financial incentive to retain our existing and future employees.

Income Tax Expense

Prior to January 17, 2007, we, as a partnership, generally had not been subject to U.S. federal income tax but certain of our subsidiaries had been subject to the New York City unincorporated business tax (UBT) on their U.S. earnings based on a statutory rate of 4%. One of our subsidiaries was subject to U.S. federal corporate income taxes. Certain of our subsidiaries are subject to income tax of the foreign countries in which they conduct business.

In connection with the Nomura transaction and the initial public offering (see Note 1 to Part I, Item 1, Financial Statements Organization and Basis of Presentation), our operating entities were reorganized and a portion of our income is now subject to U.S. federal and state corporate income tax.

The amount of income taxes that we may be required to pay could increase significantly if legislation introduced in Congress is passed in its proposed form. During June 2007, legislation was introduced in the U.S. Senate, which would tax us and other publicly traded partnerships as corporations, and similar legislation was introduced in the House. The proposed Senate legislation would not apply to us for five years, but the House legislation does not include any corresponding exemption period. As of today, no action has been taken on either bill. In addition, legislation has also been introduced in the House, and passed by the House Ways and Means Committee, that would have the effect of taxing income recognized from carried interests as ordinary income thereby effectively causing such income to be treated as nonqualifying income under the publicly traded partnership rules, which would preclude us qualifying for treatment as a partnership for U.S. federal income tax purposes. If any

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of this legislation is enacted in its current or similar form, we would incur a material increase in our tax liability. For more information on the proposed legislation, see Part II, Item 1A, Risk Factors Risks Related to Taxation Legislation has been introduced that would, if enacted, preclude us from qualifying for treatment as a partnership for U.S. federal income tax purposes under the publicly traded partnership rules. Our structure also is subject to potential judicial or administrative change and differing interpretations, possibly on a retroactive basis.

Revenues

	Nine Months Ended September 30, 2008			Three Months Ended September 30, 2008		
	2007(A)	Variance		2007	Variance	
Management fees from affiliates	\$ 447,928	\$ 340,028	\$ 107,900	\$ 154,266	\$ 124,991	\$ 29,275
Incentive income from affiliates	56,162	495,561	(439,399)	718	106,690	(105,972)
Other revenues	70,022	48,634	21,388	30,152	15,601	14,551
Total Revenues	\$ 574,112	\$ 884,223	\$ (310,111)	\$ 185,136	\$ 247,282	\$ (62,146)

(A) Pro Forma results of our operations on a deconsolidated basis.

Nine months ended September 30

For the nine months ended September 30, 2008 compared with the nine months ended September 30, 2007, total revenues decreased as a result of the following:

Management fees from affiliates increased by \$107.9 million primarily due to the net effect of increases in average AUM of \$3.1 billion, \$0.3 billion, \$2.7 billion and \$1.7 billion in our private equity funds, our Castles, our liquid hedge funds and our hybrid hedge funds, respectively. The combined increase to average AUM generated \$99.4 million of additional management fees. In addition, management fees from affiliates increased by \$2.8 million as a result of changes in foreign currency exchange rates.

Incentive income from affiliates decreased by \$439.4 million as a result of \$38.7 million of incentive income recognized from our private equity funds for the nine months ended September 30, 2008, as contingencies for repayment had been resolved in certain funds allowing income recognition, compared to \$317.6 million of incentive income recognized from our private equity funds for the nine months ended September 30, 2007, which was no longer subject to contingencies. Furthermore, our liquid hedge funds, our Castles and our hybrid hedge funds contributed additional decreases of \$140.7 million, \$18.6 million and \$1.3 million, respectively, in incentive income primarily due to lower returns.

Other revenues increased by \$21.4 million primarily due to a \$10.4 million increase in expense reimbursements from our funds, which are recorded gross on our statement of operations, a \$12.9 million increase in incentive income from non-affiliates, dividend income of \$1.7 million from our Castles (prior to the adoption of SFAS 159, dividend income was recorded as return of capital on investments), and a \$1.0 million increase in fees from non-affiliates, which were offset by a decrease in interest income of \$5.4 million. Expense reimbursements increased primarily due to an increase

in expenses related to an increase in headcount needed to support the growth of the hybrid hedge funds and liquid hedge funds of \$5.1 million and \$1.4 million, respectively, and new private equity funds and liquid hedge funds of \$1.0 million and \$0.9 million, respectively. Incentive income from non-affiliates increased primarily due to a realization event in 2008 from a third party account we manage.

Three months ended September 30

For the three months ended September 30, 2008 compared with the three months ended September 30, 2007, total revenues decreased as a result of the following:

Management fees from affiliates increased by \$29.3 million primarily due to the net effect of increases in average AUM of \$2.8 billion, \$0.1 billion, \$2.2 billion and \$1.3 billion in our private equity funds, our Castles, our liquid hedge funds and our hybrid hedge funds, respectively. The combined increase to average AUM generated \$26.2 million of additional management fees.

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Incentive income from affiliates decreased by \$106.0 million as a result of \$0.5 million of incentive income recognized from our private equity funds for the three months ended September 30, 2008, as contingencies for repayment had been resolved in certain funds allowing income recognition, compared to \$105.6 million of incentive income recognized from our private equity funds for the three months ended September 30, 2007, which was no longer subject to contingencies.

Other revenues increased by \$14.6 million primarily due to a \$0.6 million increase in expense reimbursements from our funds, which are recorded gross on our statement of operations, a \$12.8 million increase in incentive income from non-affiliates, dividend income of \$0.7 million from our Castles (prior to the adoption of SFAS 159, dividend income was recorded as return of capital on investments), and a \$1.1 million increase in fees from non-affiliates, which were offset by a decrease in interest income of \$0.9 million.

Expenses

	Nine Months Ended September 30, 2008			Three Months Ended September 30, 2008		
	2008	2007(A)	Variance	2008	2007	Variance
Interest expense	\$ 29,705	\$ 26,016	\$ 3,689	\$ 9,481	\$ 7,285	\$ 2,196
Compensation and benefits	399,253	497,198	(97,945)	134,774	101,703	33,071
Principals agreement compensation	714,710	612,981	101,729	239,976	232,048	7,928
General, administrative and other (including depreciation and amortization)	67,161	64,719	2,442	25,973	19,642	6,331
Total Expenses	\$ 1,210,829	\$ 1,200,914	\$ 9,915	\$ 410,204	\$ 360,678	\$ 49,526

(A) Pro Forma results of our operations on a deconsolidated basis.

Nine months ended September 30

For the nine months ended September 30, 2008 compared with the nine months ended September 30, 2007, total expenses increased as a result of the following:

Interest expense increased by \$3.7 million primarily due to a net increase of \$3.5 million due to higher average borrowings in 2008, offset by a decrease in average interest rates.

Compensation and benefits decreased by \$97.9 million primarily due to a decrease in profit sharing compensation of \$185.0 million, offset by an increase due to growth in our employee population of \$39.7 million, a \$7.0 million discretionary bonus declared during the first quarter of 2008 to one senior employee, and an increase in equity based compensation of \$40.4 million primarily due to the 31 million FOG RPU's granted in April 2008 (see discussion below). Profit-sharing compensation decreased due largely to greater private equity realization events in the first nine months of 2007 than in the first nine months of 2008, and decreased profit from our liquid and hybrid hedge funds.

Our average headcount for the nine months ended September 30, 2008 grew 24% compared to the nine months ended September 30, 2007.

Principals agreement compensation increased by \$101.7 million because there was not a full nine months of amortization in 2007. In connection with the initial public offering in February 2007, the principals entered into an agreement among themselves, which provides that in the event a principal voluntarily terminates his employment with Fortress Operating Group for any reason prior to the fifth anniversary of the initial public offering, a portion of the equity interests held by that principal as of the completion of the initial public offering will be forfeited to the principals who remain employed by Fortress Operating Group. As a result of this service requirement, the fair value of Fortress Operating Group units subject to the risk of forfeiture of \$4,763.0 million is being charged to compensation expense on a straight-line basis over the five-year vesting period. When Fortress records this non-cash expense, it records a corresponding increase in capital.

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General, administrative and other expenses increased by \$2.4 million, primarily as a result of a net increase of \$5.1 million in office and administrative costs to support a significantly larger workforce and increased infrastructure demands, and an increase of \$0.8 million in other general expenses related to being a public company, offset by a decrease in professional fees and consulting fees of \$3.5 million relating to our transition to being a public company during 2007.

Three months ended September 30

For the three months ended September 30, 2008 compared with the three months ended September 30, 2007, total expenses increased as a result of the following:

Interest expense increased by \$2.2 million primarily due to a net increase of \$0.8 million related to higher average borrowings in 2008, offset by a decrease in average interest rates, and an increase of \$1.1 million due to an increase in the amortization of financing costs associated with the amendments to our credit facility in May 2007 and April 2008.

Compensation and benefits increased by \$33.1 million primarily due to an increase in equity based compensation of \$26.1 million, primarily due to 31 million FOG RPU's granted in April 2008 (see discussion below), and an increase due to growth in our employee population of \$8.7 million, offset by a decrease in profit sharing compensation of \$1.7 million. Profit-sharing compensation decreased largely due to greater private equity realization events in the third quarter of 2007 than in the third quarter of 2008, and decreased profit from our liquid and hybrid hedge funds. Our average headcount for the three months ended September 30, 2008 grew 17% compared to the three months ended September 30, 2007.

Principals agreement compensation is being amortized over the term of the agreement.

General, administrative and other expenses increased by \$6.3 million primarily as a result of an increase in professional fees and consulting fees of \$4.8 million and an increase of \$1.7 million in office and administrative costs to support a significantly larger workforce and increased infrastructure demands.

Future Compensation Expense

In future periods, we will further recognize non-cash compensation expense on our non-vested equity-based awards of \$968.2 million with a weighted average recognition period of 4.4 years. This does not include amounts related to the Principals Agreement, which is discussed above.

In April 2008, we granted 31 million Fortress Operating Group (FOG) restricted partnership units (RPU's) to a senior employee. In connection with the grant of these interests, the employee receives partnership distribution equivalent payments on such units with economic effect as from January 1, 2008. The interests will vest into full capital interests in FOG units in three equal portions on the first business day of 2011, 2012 and 2013, respectively, subject to continued employment with Fortress. In connection with this grant, we have reduced the employee's profit sharing interests in various Fortress Funds.

Other Income (Loss)

Nine Months Ended September 30,			Three Months Ended September 30,		
2008	2007(A)	Variance	2008	2007	Variance

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Net gains (losses) other investments	\$ (44,671)	\$ (80,494)	\$ 35,823	\$ (10,099)	\$ (58,198)	\$ 48,099
Earnings (losses) from equity method investees	(113,550)	(20,058)	(93,492)	(37,921)	(30,716)	(7,205)
Total Other Income (Loss)	\$ (158,221)	\$ (100,552)	\$ (57,669)	\$ (48,020)	\$ (88,914)	\$ 40,894

(A) Pro Forma results of our operations on a deconsolidated basis.

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Nine months ended September 30

For the nine months ended September 30, 2008 compared with the nine months ended September 30, 2007, total other income (loss) decreased as a result of the following:

Gains (losses) other investments increased by \$35.8 million primarily due to the net effect of:

recognition of an unrealized loss of \$16.2 million for the nine months ended September 30, 2008 on our options in our Castles as a result of a decline in the relative performance of the underlying stock price, as compared to the recognition of an unrealized loss of \$79.2 million for the nine months ended September 30, 2007; and

recognition of an unrealized loss of \$27.2 million for the nine months ended September 30, 2008 attributable to a decline in the market value of our investments in the Castles. Our investments in the Castles are held at fair value as of January 1, 2008 pursuant to the provisions of SFAS 159.

Earnings (losses) from equity method investees decreased by \$93.5 million primarily due to the net effect of (i) the recognition of a \$113.6 million net loss from equity method investees in 2008 as a result of a loss attributable to investments in our private equity funds, liquid hedge funds and hybrid hedge funds, compared to (ii) the recognition of a \$20.1 million loss on our equity method investments for the nine months ended September 30, 2007. The overall decrease was primarily a result of diminished returns within the funds.

Three months ended September 30

For the three months ended September 30, 2008 compared with the three months ended September 30, 2007, total other income (loss) increased as a result of the following:

Gains (losses) other investments increased by \$48.1 million primarily due to the net effect of:

recognition of an unrealized loss of \$0.7 million for the three months ended September 30, 2008 on our options in our Castles as a result of a decline in the relative performance of the underlying stock price, as compared to the recognition of an unrealized loss of \$54.6 million for the three months ended September 30, 2007; and

recognition of an unrealized loss of \$6.2 million for the three months ended September 30, 2008 attributable to a decline in the market value of our investments in the Castles. Our investments in the Castles are held at fair value as of January 1, 2008 pursuant to the provisions of SFAS 159.

Earnings (losses) from equity method investees decreased by \$7.2 million primarily due to the net effect of (i) the recognition of a \$37.9 million net loss from equity method investees in 2008 as a result of a loss attributable to investments in our private equity funds, liquid hedge funds and hybrid hedge funds compared to (ii) the recognition of a \$30.7 million loss on our equity method investments for the three months ended September 30, 2007. The overall decrease was primarily a result of diminished returns within the funds.

Income Tax Benefit (Expense)

For the nine and three months ended September 30, 2008, Fortress recognized income tax expense (benefit) of (\$0.3 million) and (\$5.6 million), respectively. For the nine and three months ended September 30, 2007, Fortress

recognized income tax expense (benefit) of \$7.2 million and (\$12.2 million), respectively. The primary reason for the decrease in income tax expense for the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007 is a decrease in pre-tax book income. The primary reasons for the decrease in income tax benefit for the three months ended September 30, 2008 compared to the three months ended September 30, 2007 are (i) changes in the mix of business segments producing income, which may be subject to tax at different rates, and (ii) changes in the forecasts of annual taxable income which are used to calculate the tax provision.

Fortress has recorded a significant deferred tax asset, primarily in connection with the Nomura Transaction and IPO. A substantial portion of this asset is offset by a liability associated with the tax receivable agreement with our Principals. As of September 30, 2008, we believe that it is more likely than not that this tax benefit will be realized based on our expectations of future taxable income. Such expectations are dependant on achieving anticipated

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levels of AUM and fund performance among other factors, and actual results may differ materially. We analyze this asset on a quarterly basis to determine if a valuation allowance is necessary. If we were to determine that it is more likely than not that some portion, or all, of the deferred tax asset will not be realized, we would be required to record a valuation allowance for that portion. However, this would be substantially offset by a corresponding write off of a pro rata portion of the tax receivable agreement liability

Segment Analysis

Fortress conducts its management and investment business through the following five primary segments: (i) private equity funds, (ii) Castles, (iii) liquid hedge funds, (iv) hybrid hedge funds, and (v) principal investments in these funds as well as cash that is available to be invested. These segments are differentiated based on their varying investment strategies. Due to the increased significance of the principal investments segment, it has been disaggregated from the other segments in this period and for all periods presented.

Discussed below are our results of operations for each of our reportable segments. They represent the separate segment information available and utilized by our management committee, which consists of our principals and certain key officers, and which functions as our chief operating decision maker to assess performance and to allocate resources. Management evaluates the performance of each segment based on its distributable earnings.

As segment revenues reflected in our distributable earnings are presented on an unconsolidated basis, management fee and incentive income are reflected on a gross basis prior to elimination as required in consolidation. As a result of this presentation, management fees and incentive income are greater than those reflected on a consolidated GAAP basis for periods prior to the deconsolidation on March 31, 2007. Other items within distributable earnings are less than the related amounts on a GAAP basis for these periods, as they do not include the effects of consolidating the Fortress Funds.

As mentioned above, results of operations for each of our segments are reflected on an unconsolidated basis, even for periods prior to the deconsolidation. Management also assesses our segments on a Fortress Operating Group and pre-tax basis, and therefore adds back the non-controlling interests in consolidated subsidiaries related to Fortress Operating Group units (held by the principals) and income tax expense.

Distributable earnings is defined in Note 10 to Part I, Item 1, Financial Statements Segment Reporting. Furthermore, a complete discussion of DE basis impairment and reserves, including the methodology used in estimating the amounts as well as the amounts incurred in the relevant periods, is disclosed therein.

Private Equity Funds

	Nine Months Ended			Three Months Ended		
	September 30, 2008	September 30, 2007	Variance	September 30, 2008	September 30, 2007	Variance
Management Fees	\$ 128,514	\$ 97,749	\$ 30,765	\$ 44,184	\$ 35,133	\$ 9,051
Incentive Income	12,294	273,890	(261,596)	(16,447)	83,592	(100,039)
Segment revenues total	\$ 140,808	\$ 371,639	\$ (230,831)	\$ 27,737	\$ 118,725	\$ (90,988)
Pre-tax distributable earnings	\$ 100,461	\$ 249,116	\$ (148,655)	\$ 18,575	\$ 82,273	\$ (63,698)

Nine months ended September 30

Pre-tax distributable earnings decreased by \$148.7 million primarily due to:

a \$30.8 million increase in management fees. Management fees increased primarily due to (i) \$31.5 million of management fees generated by the creation of new private equity funds, most notably Fund V, Fund V Coinvestment, Florida Coinvestment Fund, Mortgage Opportunities Fund and Credit Opportunities Fund, and (ii) an increase in average AUM of \$9.5 million from Fund IV, Fund IV Coinvestment, Real Assets Fund and Holiday Investment Fund (FHIF). These increases to management fees were partially offset by a decrease of \$1.7 million in management fees collected from Fortress Residential Investment Deutschland (FRID) as a result of distributions to investors (which reduces AUM) during 2007, a decrease of

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\$2.6 million from Fund III as a result of the NAV of certain portfolio companies declining below their invested capital, a decrease of \$3.1 million from Fund IV, as a consequence of the creation of Fund V in May 2007 (which caused the management fees from Fund IV to be based on invested capital rather than capital commitments), and a decrease of \$2.1 million as a result of a decrease in the average management fee percentage earned;

a \$167.2 million net decrease in incentive income. Incentive income decreased by \$261.6 million partially offset by a corresponding decrease in the employees' share of incentive income of \$94.4 million reflected as profit sharing compensation expense. The decrease of \$261.6 million in incentive income was primarily attributable to a decline in the results of realization events of our private equity funds of \$247.8 million, and an impairment of incentive income from FRID of \$16.4 million, offset by an increase of \$2.7 million in incentive income due to higher FFO in excess of certain performance hurdles generated by NIH; and

an \$11.5 million increase in operating expenses primarily related to an increase in headcount.

Three months ended September 30

Pre-tax distributable earnings decreased by \$63.7 million primarily due to:

a \$9.1 million increase in management fees. Management fees increased primarily due to (i) \$5.2 million of management fees generated by the creation of new private equity funds, most notably Mortgage Opportunities Fund, Fund V Coinvestment and Credit Opportunities Fund, (ii) a \$4.5 million increase due to an increase in average AUM mainly from Fund IV and Real Assets Fund, offset by (iii) a decrease of \$0.4 million as a result of a decrease in the average management fee percentage earned;

a \$66.5 million net decrease in incentive income. Incentive income decreased by \$100.0 million partially offset by a corresponding decrease in the employees' share of incentive income of \$33.5 million reflected as profit sharing compensation expense. The decrease of \$100.0 million in incentive income was primarily attributable to a decline in the results of realization events of our private equity funds of \$83.5 million and an impairment of incentive income from FRID of \$16.4 million.

a \$6.2 million increase in operating expenses primarily related to an increase in headcount.

Publicly Traded Alternative Investment Vehicles ("Castles")

	Nine Months Ended September 30,			Three Months Ended September 30,		
	2008	2007	Variance	2008	2007	Variance
Management Fees	\$ 41,320	\$ 34,877	\$ 6,443	\$ 13,665	\$ 12,131	\$ 1,534
Incentive Income	12	18,596	(18,584)		691	(691)
Segment revenues total	\$ 41,332	\$ 53,473	\$ (12,141)	\$ 13,665	\$ 12,822	\$ 843
Pre-tax distributable earnings	\$ 12,033	\$ 24,101	\$ (12,068)	\$ 3,829	\$ 5,163	\$ (1,334)

Nine months ended September 30

Pre-tax distributable earnings decreased by \$12.1 million primarily due to:

a \$5.8 million net increase in management fees. Management fees increased primarily due to (i) \$3.7 million as a result of the growth of average AUM, and (ii) \$2.8 million as a result of changes in foreign currency exchange rates. These increases to management fees were partially offset by an increase in the employees' share of management fees of \$0.7 million;

a \$13.5 million net decrease in incentive income. Incentive income decreased by \$18.6 million which was offset by a decrease in the employees' share of incentive income of \$5.1 million reflected as profit sharing compensation expense. The decrease of \$18.6 million was primarily due to the recognition of incentive income generated by Newcastle and Eurocastle as a result of FFO exceeding certain performance hurdles for

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the nine months ended September 30, 2007. For the nine months ended September 30, 2008, Newcastle's and Eurocastle's FFO did not exceed these performance hurdles so no incentive income was generated; and

a \$4.4 million net increase in operating expenses primarily due to increases in general and administrative and other expenses.

Three months ended September 30

Pre-tax distributable earnings decreased by \$1.3 million primarily due to:

a \$1.3 million net increase in management fees. Management fees increased primarily due to (i) \$1.0 million as a result of the growth of average AUM, and (ii) \$0.5 million as a result of changes in foreign currency exchange rates. These increases to management fees were partially offset by an increase in the employees' share of management fees of \$0.2 million;

a \$0.5 million net decrease in incentive income. Incentive income decreased by \$0.7 million which was offset a decrease in the employees' share of incentive income of \$0.2 million reflected as profit sharing compensation expense. The decrease of \$0.7 million was primarily due to the recognition of incentive income generated by Newcastle and Eurocastle as a result of FFO exceeding certain performance hurdles for the three months ended September 30, 2007. For the three months ended September 30, 2008, Newcastle's and Eurocastle's FFO did not exceed these performance hurdles so no incentive income was generated; and

a \$2.1 million net increase in operating expenses primarily due increases in general and administrative and other expenses.

Liquid Hedge Funds

	Nine Months Ended September 30, 2008 2007			Three Months Ended September 30, 2008 2007		
			Variance			Variance
Management Fees	\$ 169,965	\$ 113,692	\$ 56,273	\$ 59,640	\$ 44,351	\$ 15,289
Incentive Income	17,125	157,989	(140,864)	85	(210)	295
Segment revenues total	\$ 187,090	\$ 271,681	\$ (84,591)	\$ 59,725	\$ 44,141	\$ 15,584
Pre-tax distributable earnings	\$ 70,662	\$ 129,203	\$ (58,541)	\$ 25,236	\$ 23,815	\$ 1,421

Nine months ended September 30

Pre-tax distributable earnings decreased by \$58.5 million primarily due to:

a \$59.1 million net increase in management fees. Management fees increased by \$56.3 million and the employees' share of management fees decreased by \$2.8 million (due to a reduction in the employees' percentage share of such fees). The \$56.3 million increase was primarily a result of the growth in average AUM, an increase in the average management fee percentage earned, and management fees generated by the formation of the new Commodities Fund, which generated \$36.5 million, \$9.7 million and \$11.2 million of

additional management fees, respectively, partially offset by a decrease in non-affiliate management fees of \$1.1 million;

a \$93.1 million net decrease in incentive income. Incentive income decreased by \$140.9 million partially offset by a corresponding decrease in the employees' share of incentive income of \$47.8 million, reflected as profit sharing compensation expense. The \$140.9 million decrease in incentive income is primarily attributable to a decrease of \$158.2 million due to lower returns in our liquid hedge funds, offset by an increase in incentive income generated by realization events from special investments and the new Commodities Fund of \$2.1 million and \$15.2 million, respectively; and

a \$24.5 million increase in operating expenses primarily due to an increase in headcount.

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Pre-tax distributable earnings increased by \$1.4 million primarily due to:

a \$17.1 million net increase in management fees. Management fees increased by \$15.3 million and the employees' share of management fees decreased by \$1.8 million (due to a reduction in the employees' percentage share of such fees). The \$15.3 million increase was primarily a result of the growth in average AUM, an increase in the average management fee percentage earned, and management fees generated by the formation of the new Commodities Fund, which generated \$7.2 million, \$2.9 million and \$5.2 million of additional management fees, respectively;

a \$5.4 million net decrease in incentive income. Incentive income increased by \$0.3 million and the return by the employees of their share of incentive income decreased by \$5.7 million. We accrue the employees' share of incentive income at the end of each interim period based on the year to date performance of the funds. For the three months ended September 30, 2008 and 2007, the liquid hedge funds recognized a negative return for each period. As a result, we adjusted the employees' share of incentive income for the three months ended September 30, 2008 and 2007 to reflect the respective cumulative amount of the employees' share of incentive income for the nine months ended September 30, 2008 and 2007. These adjustments for the three months ended September 30, 2008 and 2007 effectively represented a partial return by the employees of their incentive income earned for periods prior to the three months ended September 30, 2008 and 2007. There was a \$5.7 million net decrease in the amount of incentive income returned by employees for the three months ended September 30, 2008 compared to the three months ended September 30, 2007; and

a \$10.3 million increase in operating expenses primarily due to an increase in headcount.

Hybrid Hedge Funds

	Nine Months Ended September 30, 2008 2007			Three Months Ended September 30, 2008 2007		
			Variance			Variance
Management Fees	\$ 111,483	\$ 94,096	\$ 17,387	\$ 38,028	\$ 33,376	\$ 4,652
Incentive Income	14,128	93,832	(79,704)	13,256	9,463	3,793
Segment revenues total	\$ 125,611	\$ 187,928	\$ (62,317)	\$ 51,284	\$ 42,839	\$ 8,445
Pre-tax distributable earnings	\$ 26,099	\$ 55,882	\$ (29,783)	\$ 14,820	\$ 6,569	\$ 8,251

Nine months ended September 30

Pre-tax distributable earnings decreased by \$29.8 million primarily due to:

a \$14.9 million net increase in management fees. Management fees increased by \$17.4 million partially offset by a corresponding increase in the employees' share of management fees of \$2.5 million. The \$17.4 million increase in management fees was primarily a result of growth in AUM, which resulted in an \$18.9 million increase, offset by a decrease of \$1.2 million due to a decrease in the average management fee percentage

earned, and a \$0.3 million decrease in management fees from third party accounts we manage;

a \$44.0 million net decrease in incentive income. Incentive income decreased by \$79.7 million and the employees' share of incentive income, reflected as profit sharing compensation expense, decreased by \$35.7 million. The \$79.7 million decrease in incentive income was primarily attributable to a decline in the returns of our hybrid hedge funds which generated a decrease of \$104.3 million, partially offset by an increase of \$11.5 million due to the change in the average capital eligible for incentive income and a \$13.1 million realization event in 2008 from a third party account we manage; and

a \$0.7 million increase in operating expenses primarily related to an increase in headcount.

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Three months ended September 30

Pre-tax distributable earnings increased by \$8.3 million primarily due to:

a \$3.7 million net increase in management fees. Management fees increased by \$4.7 million partially offset by a corresponding increase in the employees