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Fortress Investment Group LLC
Form 10-Q
October 29, 2015
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2015

or

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

20-5837959

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

1345 Avenue of the Americas, New York, NY

10105

(Address of principal executive offices)

(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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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):

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: 215,714,060 outstanding as of October 23, 2015.

Class B Shares: 226,331,513 outstanding as of October 23, 2015.

FORTRESS INVESTMENT GROUP LLC
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Set forth below is information about certain terms used in this Quarterly Report on Form 10-Q:

“Management Fee Paying Assets Under Management,” or “AUM,” refers to the management fee paying assets we manage or co-manage, including, as applicable, capital we have the right to call from our investors pursuant to their capital commitments to various funds. In addition, AUM includes management fee paying assets managed by autonomous businesses in which we retain a minority interest under our affiliated manager platform. Our AUM equals the sum of:

- (i) the capital commitments or invested capital (or net asset value, "NAV," if lower) of our private equity funds, private permanent capital vehicle through May 2015 and credit PE funds, depending on which measure management fees are being calculated upon at a given point in time, which in connection with private equity funds raised after March 2006 includes the mark-to-market value of public securities held within the funds,
- (ii) the contributed capital or book equity of our publicly traded permanent capital vehicles,
- (iii) the NAV of our hedge funds, including the Value Recovery Funds which pay fees based on realizations;
- (iv) the NAV or fair value of our managed accounts, to the extent management fees are charged; and
- (v) AUM related to affiliated managers and co-managed funds.

For each of the above, the amounts exclude assets under management for which we charge either no or nominal fees, generally related to our investments in our funds as well as investments in our 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. Finally, our calculation of AUM differs from the manner in which our affiliates registered with the United States Securities and Exchange Commission report “Regulatory Assets Under Management” on Form ADV and Form PF in various ways. Significantly, Regulatory Assets Under Management, unlike Management Fee Paying Assets Under Management, is not reduced by liabilities or indebtedness associated with assets under management and it includes assets under management and uncalled capital for which Fortress receives no compensation.

“Fortress,” “we,” “us,” “our,” the “company” and the “public company” refer, collectively, to Fortress Investment Group LLC its subsidiaries, including the Fortress Operating Group (as defined below) and all of its subsidiaries.

“Fortress Funds” and “our funds” refers to the private investment funds, permanent capital vehicles and related managed accounts that we manage or co-manage. The Fortress Macro Fund is our flagship liquid hedge fund and the Drawbridge Special Opportunities Fund is our flagship credit hedge fund.

“Fortress Operating Group” or “FOG” refers to the limited partnerships and their subsidiaries through which we conduct our business and hold our investments. The public company controls the Fortress Operating Group through wholly owned subsidiaries that serve as the general partner of each FOG entity.

Economic interests in each FOG entity are represented by Class A common units and Class B common units. Class A common units are (indirectly) owned by the public company, and Class B common units are owned by the principals (defined below) and, from time to time, a former senior employee who owned securities convertible into Class B common units.

The number of outstanding Class A common units equals the number of outstanding Class A shares of the public company. The number of outstanding Class B common units equals the number of outstanding Class B shares of the public company.

“Fortress Operating Group units” or “FOGUs” is the term we use to refer to the aggregate of one limited partner interest (either a Class A common unit or a Class B common unit, as applicable) in each FOG entity. One FOGU together with one Class B share is convertible into one Class A share. A surrendered Class B common unit automatically converts into a Class A common unit.

“principals” or “Principals” refers to Peter Briger, Wesley Edens, Randal Nardone and Michael Novogratz, collectively, as well as Robert Kauffman until his retirement in December 2012. The principals control the public company through their ownership of the public company’s Class B shares (together with, from time to time, a former senior employee who owned securities convertible into Class B shares). The Class B shares and the Class A shares are each entitled to one vote per share, and the number of Class B shares outstanding represents a majority of the aggregate number of Class B shares and Class A shares outstanding. The Class B shares do not represent an economic interest in the public company and therefore are not entitled to any dividends. The principals own their economic interest in the public company primarily through their direct ownership of FOGUs.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

FORTRESS INVESTMENT GROUP LLC

CONSOLIDATED BALANCE SHEETS

(dollars in thousands)

	September 30, 2015 (Unaudited)	December 31, 2014
Assets		
Cash and cash equivalents	\$ 337,109	\$ 391,089
Due from affiliates	195,619	326,575
Investments	1,125,443	1,121,545
Investments in options	33,849	71,844
Deferred tax asset, net	426,274	417,623
Other assets	158,420	173,708
Total Assets	\$2,276,714	\$2,502,384
Liabilities and Equity		
Accrued compensation and benefits	\$ 242,492	\$ 374,709
Due to affiliates	383,685	375,424
Deferred incentive income	348,267	304,526
Debt obligations payable	75,000	75,000
Other liabilities	124,303	88,053
Total Liabilities	1,173,747	1,217,712
Commitments and Contingencies		
Redeemable Non-controlling Interests	—	1,717
Equity		
Class A shares, no par value, 1,000,000,000 shares authorized, 215,714,060 and 208,535,157 shares issued and outstanding at September 30, 2015 and December 31, 2014, respectively	—	—
Class B shares, no par value, 750,000,000 shares authorized, 226,331,513 shares issued and outstanding at September 30, 2015 and December 31, 2014, respectively	—	—
Paid-in capital	1,909,349	1,996,137
Retained earnings (accumulated deficit)	(1,326,338)	(1,350,122)
Accumulated other comprehensive income (loss)	(1,900)	(2,416)
Total Fortress shareholders' equity	581,111	643,599
Principals' and others' interests in equity of consolidated subsidiaries	521,856	639,356
Total Equity	1,102,967	1,282,955
Total Liabilities, Redeemable Non-controlling Interests and Equity	\$2,276,714	\$2,502,384

See notes to consolidated financial statements.

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FORTRESS INVESTMENT GROUP LLC

CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

(dollars in thousands, except per share data)

	Three Months Ended September		Nine Months Ended September	
	30,		30,	
	2015	2014	2015	2014
Revenues				
Management fees: affiliates	\$ 134,414	\$ 138,135	\$ 413,057	\$ 403,890
Management fees: non-affiliates	15,400	16,774	45,657	52,112
Incentive income: affiliates	48,773	30,941	155,154	125,634
Incentive income: non-affiliates	439	343	735	1,030
Expense reimbursements: affiliates	59,988	50,600	168,544	153,448
Expense reimbursements: non-affiliates	2,757	4,869	9,573	9,931
Other revenues (affiliate portion disclosed in Note 6)	2,248	1,518	6,476	4,589
	264,019	243,180	799,196	750,634
Expenses				
Compensation and benefits	169,027	187,249	547,023	543,882
General, administrative and other	37,887	41,313	126,053	121,322
Depreciation and amortization (see Note 1)	16,102	4,997	34,201	14,335
Interest expense	918	916	2,796	2,554
Transfer of interest in Graticule (see Note 1)	—	—	101,000	—
	223,934	234,475	811,073	682,093
Other Income (Loss)				
Gains (losses) (affiliate portion disclosed in Note 3)	(39,888	) (23,917	) (15,114	) (30,108
Tax receivable agreement liability adjustment	(390	) (4,036	) (7,890	) (4,036
Earnings (losses) from equity method investees	(22,195	) 38,928	(16,808	) 81,750
Gain on transfer of Graticule (see Note 1)	—	—	134,400	—
	(62,473	) 10,975	94,588	47,606
Income (Loss) Before Income Taxes	(22,388	) 19,680	82,711	116,147
Income tax benefit (expense)	(3,584	) (3,024	) (16,784	) (16,934
Net Income (Loss)	\$(25,972	) \$ 16,656	\$ 65,927	\$ 99,213
Allocation of Net Income (Loss):				
Principals' and Others' Interests in Income (Loss) of Consolidated Subsidiaries	\$(11,727	) \$ 12,623	\$ 42,149	\$ 60,800
Redeemable Non-controlling Interests in Income (Loss) of Consolidated Subsidiaries	—	(2,042	) (6	) (1,885
Net Income (Loss) Attributable to Class A Shareholders	(14,245	) 6,075	23,784	40,298
	\$(25,972	) \$ 16,656	\$ 65,927	\$ 99,213
Dividends declared per Class A share	\$0.08	\$0.26	\$0.54	\$0.42
Earnings (Loss) Per Class A share				

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Net income (loss) per Class A share, basic	\$ (0.07) \$ 0.03	\$ 0.10	\$ 0.19
Net income (loss) per Class A share, diluted	\$ (0.07) \$ 0.02	\$ 0.09	\$ 0.17
Weighted average number of Class A shares outstanding, basic	216,439,077	208,014,692	216,138,405	210,874,640
Weighted average number of Class A shares outstanding, diluted	216,439,077	220,792,711	222,213,743	457,019,507

See notes to consolidated financial statements.

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FORTRESS INVESTMENT GROUP LLC

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(dollars in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Comprehensive income (loss) (net of tax)				
Net income (loss)	\$ (25,972	) \$ 16,656	\$ 65,927	\$ 99,213
Foreign currency translation	621	351	249	(1,251
Total comprehensive income (loss)	\$ (25,351	) \$ 17,007	\$ 66,176	\$ 97,962
Allocation of Comprehensive Income (Loss):				
Comprehensive income (loss) attributable to principals' and others' interests	\$ (11,473	) \$ 12,778	\$ 42,095	\$ 59,935
Comprehensive income (loss) attributable to redeemable non-controlling interests	—	(2,042	) (6	) (1,885
Comprehensive income (loss) attributable to Class A shareholders	(13,878	) 6,271	24,087	39,912
	\$ (25,351) \$ 17,007	\$ 66,176	\$ 97,962

See notes to consolidated financial statements.

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FORTRESS INVESTMENT GROUP LLC

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (Unaudited)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2015

(dollars in thousands)

	Class A Shares	Class B Shares	Paid-In Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income (Loss)	Total Fortress Shareholders' Equity	Principals' and Others' Interests in Equity of Consolidated Subsidiaries	Total Equity
Equity - December 31, 2014	208,535,157	226,331,513	\$1,996,137	\$(1,350,122)	\$(2,416)	\$643,599	\$639,356	\$1,282,955
Contributions from principals' and others' interests in equity	—	—	—	—	—	—	70,602	70,602
Distributions to principals' and others' interests in equity (net of tax)	—	—	—	—	—	—	(234,946)	(234,946)
Dividends declared	—	—	(113,758)	—	—	(113,758)	—	(113,758)
Dividend equivalents accrued in connection with equity-based compensation (net of tax)	—	—	(2,660)	—	—	(2,660)	(4,643)	(7,303)
Net deferred tax effects resulting from acquisition and exchange of Fortress Operating Group units	—	—	4,922	—	—	4,922	147	5,069
Director restricted share grant	111,969	—	271	—	—	271	289	560
Capital increase related to equity-based compensation, net	7,066,934	—	16,232	—	—	16,232	17,374	33,606

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Dilution impact of equity transactions (Note 6)	—	—	8,205	—	213	8,418	(8,418) —
Comprehensive income (loss) (net of tax)								
Net income (loss) (excludes loss allocated to redeemable non-controlling interests)	—	—	—	23,784	—	23,784	42,149	65,933
Foreign currency translation	—	—	—	—	303	303	(54	) 249
Total comprehensive income (loss)						24,087	42,095	66,182
Equity - September 30, 2015	215,714,060	226,331,513	\$1,909,349	\$(1,326,338)	\$(1,900)	\$581,111	\$521,856	\$1,102,967

See notes to consolidated financial statements.

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FORTRESS INVESTMENT GROUP LLC

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(dollars in thousands)

	Nine Months Ended September 30,	
	2015	2014
Cash Flows From Operating Activities		
Net income (loss)	\$65,927	\$99,213
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities		
Depreciation and amortization	34,201	14,335
Other amortization (included in interest expense)	585	585
(Earnings) losses from equity method investees	16,808	(81,750)
Distributions of earnings from equity method investees	32,345	78,337
(Gains) losses	15,114	30,108
Deferred incentive income	(115,892)	(66,778)
Deferred tax (benefit) expense	(5,786)	8,426
Options received from affiliates	(25,158)	(6,309)
Tax receivable agreement liability adjustment	7,890	4,036
Equity-based compensation	32,562	29,584
Options in affiliates granted to employees	1,912	759
Other	1,096	(654)
Transfer of interest in Graticule (see Note 1)	101,000	—
Gain on transfer of Graticule (see Note 1)	(134,400)	—
Cash flows due to changes in		
Due from affiliates	8,185	(13,183)
Other assets	(10,113)	22,945
Accrued compensation and benefits	(59,386)	(81,405)
Due to affiliates	(7,050)	(21,685)
Deferred incentive income	146,001	99,553
Other liabilities	37,525	38,884
Purchase of investments by consolidated funds	(134,474)	(400,640)
Proceeds from sale of investments by consolidated funds	85,313	386,242
Receivables from brokers and counterparties	(1,694)	(40,825)
Due to brokers and counterparties	3,421	12,577
Net cash provided by (used in) operating activities	95,932	112,355
Cash Flows From Investing Activities		
Contributions to equity method investees	(26,435)	(21,537)
Distributions of capital from equity method investees	181,874	368,373
Purchase of securities	(883)	(14,936)
Proceeds from sale of securities	18,101	83,039
Proceeds from exercise of options	51,543	—
Purchase of fixed assets	(19,848)	(7,631)
Purchase of software and technology-related assets	—	(25,976)
Net cash provided by (used in) investing activities	204,352	381,332

Continued on next page.

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FORTRESS INVESTMENT GROUP LLC

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(dollars in thousands)

	Nine Months Ended September 30,	
	2015	2014
Cash Flows From Financing Activities		
Repayments of debt obligations	—	(50,000)
Borrowings under debt obligations	—	125,000
Proceeds from public offering (Note 8)	—	186,551
Repurchase of Class B shares (Note 8)	—	(186,551)
Payments to repurchase Class A shares (Note 8)	(9,676)	(363,410)
Dividends and dividend equivalents paid	(122,663)	(88,617)
Principals' and others' interests in equity of consolidated subsidiaries - contributions	1,285	600
Principals' and others' interests in equity of consolidated subsidiaries - distributions	(225,994)	(152,686)
Excess tax benefits from delivery of RSUs	4,476	3,030
Redeemable non-controlling interests - (distributions) contributions	(1,692)	16,253
Net cash provided by (used in) financing activities	(354,264)	(509,830)
Net Increase (Decrease) in Cash and Cash Equivalents	(53,980)	(16,143)
Cash and Cash Equivalents, Beginning of Period	391,089	364,583
Cash and Cash Equivalents, End of Period	\$337,109	\$348,440
Supplemental Disclosure of Cash Flow Information		
Cash paid during the period for interest	\$1,552	\$1,500
Cash paid during the period for income taxes	\$10,376	\$4,207
Supplemental Schedule of Non-cash Investing and Financing Activities		
Employee compensation invested directly in subsidiaries	\$69,244	\$59,285
Investments of incentive receivable amounts into Fortress Funds	\$137,561	\$256,993
Dividends, dividend equivalents and Fortress Operating Group unit distributions declared but not yet paid	\$5,774	\$—
Retained equity interest related to Graticule transfer (Note 1)	\$33,400	\$—
Non-cash redeemable non-controlling interest - contributions	\$—	\$20,519

See notes to consolidated financial statements.

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FORTRESS INVESTMENT GROUP LLC
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
SEPTEMBER 30, 2015
(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 leading, highly diversified global investment 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, permanent capital vehicles and managed accounts (collectively, the "Fortress Funds"). Fortress generally makes investments in these funds.

Fortress has three primary sources of income from the Fortress Funds: management fees, incentive income, and investment income on its investments in the funds. In addition, Fortress receives expense reimbursements pursuant to management agreements. The Fortress Funds fall into the following business segments in which Fortress operates:

1) Private equity:

a) General buyout and sector-specific funds focused on control-oriented investments in cash flow generating assets and asset-based businesses in North America and Western Europe; and

Entities which Fortress collectively refers to as "permanent capital vehicles" which includes (i) Newcastle Investment Corp. ("Newcastle"), New Residential Investment Corp. ("New Residential"), Eurocastle Investment Limited ("Eurocastle"), New Media Investment Group Inc. ("New Media"), New Senior Investment Group Inc. ("New Senior") and Fortress Transportation and Infrastructure Investors LLC ("FTAI"), which are publicly traded companies that are externally managed by Fortress pursuant to management agreements (collectively referred to as the "publicly traded permanent capital vehicles") and

b) (ii) FHC Property Management LLC, (together with its subsidiaries, referred to as "Blue Harbor"), a senior living property management business. The publicly traded permanent capital vehicles invest in a wide variety of real estate related assets, including securities, loans, real estate properties and mortgage servicing related assets, media assets and transportation and infrastructure assets. All of the capital of Worldwide Transportation and Infrastructure Investors ("WWTAI"), a private fund managed by Fortress, was contributed to FTAI which completed its initial public offering ("IPO") in May 2015 (see Note 2).

Liquid hedge funds that invest globally in fixed income, currency, equity and commodity markets, and related derivatives to capitalize on imbalances in the financial markets. In addition, this segment includes an endowment style fund, which invests in Fortress Funds, funds managed by external managers, and direct investments; a fund that primarily focuses on an international "event driven" investment strategy, particularly in Europe, Asia-Pacific and Latin America; and a fund that seeks to generate returns by executing a positively convex investment strategy.

On January 5, 2015, Fortress Asia Macro Funds and related managed accounts became the first group of funds to join Fortress's affiliated manager platform ("Affiliated Managers") as they transitioned to an autonomous asset management business named Graticule Asset Management Asia, L.P. ("Graticule"). Fortress retained a perpetual minority interest in Graticule amounting to 30% of earnings during 2015 and declining to approximately 27% of earnings over time. Fortress also receives additional fees for providing infrastructure services (technology, back office, and related services) to Graticule. Fortress will continue to earn fees for providing services to Graticule through the effective date of the termination. Fortress recorded the results of this transaction at fair value. During the nine months ended September 30, 2015, Fortress recorded a non-cash gain of \$134.4 million, non-cash expense of \$101.0 million related to the fair value of the controlling interest in Graticule transferred to a former senior employee for no

consideration, and \$33.4 million from its resulting retained interest as an equity method investment. Fortress utilized an income approach to value Graticule, its retained interest in Graticule and the controlling interest in Graticule which was transferred. This approach relies on a number of factors, including actual operating results, discount rates and economic projections. During the second quarter of 2015, Graticule notified Fortress of its intention to terminate the infrastructure services agreement effective at the end of May 2016.

During 2015, Fortress determined that certain software and technology-related assets which were used in its liquid hedge funds business had not met certain growth and performance targets which triggered an asset impairment test. As a result of this test, \$10.7 million and \$18.2 million of assets were written off and included in Depreciation and Amortization for the three months and nine months ended September 30, 2015, respectively.

On October 13, 2015, Fortress announced that it will close the Fortress Macro Funds and related managed accounts and Fortress expects to return most capital to investors by the end of 2015. (See Note 11).

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FORTRESS INVESTMENT GROUP LLC

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

SEPTEMBER 30, 2015

(dollars in tables in thousands, except share data)

3) Credit funds:

Credit hedge funds, which make highly diversified investments in direct lending, corporate debt and securities, portfolios and orphaned assets, real estate and structured finance, on a global basis and throughout the capital structure, with a value orientation, as well as non-Fortress originated funds for which Fortress has been retained as manager or co-manager as part of an advisory business; and

a) Credit private equity ("PE") funds which are comprised of a family of "credit opportunities" funds focused on investing in distressed and undervalued assets, a family of "long dated value" funds focused on investing in undervalued assets with limited current cash flows and long investment horizons, a family of "real assets" funds focused on investing in tangible and intangible assets in the following principal categories (real estate, capital assets, natural resources and intellectual property), a family of Asia funds, including Japan real estate funds and an Asian investor based global opportunities fund, and a family of real estate opportunities funds, as well as certain sector-specific funds with narrower investment mandates tailored for the applicable sector.

Logan Circle Partners, L.P. ("Logan Circle"), which represents Fortress's traditional asset management business providing institutional clients actively managed investment solutions across a broad spectrum of fixed income strategies. Logan Circle's core fixed income products cover the breadth of the maturity and risk spectrums, including short, intermediate and long duration, core/core plus, investment grade credit, high yield and emerging market debt.

4) For a reconciliation between the financial statements and the segment-based financial data that management uses for making operating decisions and assessing performance, see Note 10.

FINANCIAL STATEMENT GUIDE

Selected Financial Statement
Captions

Note Reference

Explanation

Balance Sheet

Due from Affiliates	6	Generally, management fees, expense reimbursements and incentive income due from Fortress Funds.
Investments and Investments in Options	3	Primarily the carrying value of Fortress's investments in the Fortress Funds.
Deferred Tax Asset, net	5	Relates to potential future net tax benefits.
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.

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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' and a former senior employee's ownership interests in Fortress Operating Group as well as employees' ownership interests in certain subsidiaries.
Statement of Operations		
Management Fees: Affiliates	2	Fees earned for managing Fortress Funds and other affiliates, generally determined based on the size of such funds.
Management Fees: Non-Affiliates	2	Fees earned from managed accounts and the traditional fixed income asset management business, generally determined based on the amount managed.

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FINANCIAL STATEMENT GUIDE

Selected Financial Statement Captions	Note Reference	Explanation
Incentive Income: Affiliates	2	Income earned from Fortress Funds, based on the performance of such funds.
Incentive Income: Non- Affiliates	2	Income earned from managed accounts, based on the performance of such accounts.
Compensation and Benefits	7	Includes equity-based, profit-sharing and other compensation to employees.
Gains (Losses)	3	The result of asset dispositions or changes in the fair value of investments or other financial instruments which are marked to market (including the publicly traded permanent capital vehicles and publicly traded portfolio companies).
Tax Receivable Agreement Liability Adjustment	5	Represents a change in the amount due to the Principals under the tax receivable agreement.
Earnings (Losses) from Equity Method Investees	3	Fortress's share of the net earnings (losses) of the Fortress Funds resulting from its investments in these funds.
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 tax basis earnings.
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.
Earnings Per Share	8	GAAP earnings per Class A 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.

Other

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Distributions	8	A summary of dividends and distributions, and the related outstanding shares and units, is provided.
Distributable Earnings	10	A presentation of Fortress's financial performance by segment (fund type) is provided, on the basis of the operating performance measure used by Fortress's management committee.

Recent Accounting Pronouncements

In May 2014, the FASB issued a comprehensive new revenue recognition standard for contracts with customers that will supersede most current revenue recognition guidance, including industry-specific guidance. This standard contains principles that an entity will apply to determine the measurement of revenue and timing of when it is recognized. The entity will recognize revenue to reflect the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. In July 2015, the FASB voted to approve a one year deferral of the effective date of the new revenue recognition standard. The new standard is effective for Fortress beginning January 1, 2018. Early adoption is permitted but not before the original public entity effective date (that is, annual periods beginning after December 15, 2016). The standard permits the use of either the retrospective or cumulative effect transition method. Fortress is currently evaluating the impact on its consolidated financial statements upon the adoption of this new standard.

The FASB has recently issued or discussed a number of proposed standards on such topics as, leases, financial instruments and hedging. Some of the proposed changes are significant and could have a material impact on Fortress's financial reporting. Fortress has not yet fully evaluated the potential impact of these proposals, but will make such an evaluation as the standards are finalized.

In February 2015, the FASB issued ASU No. 2015-02, Consolidation (Topic 810) - Amendments to the Consolidation Analysis ("ASU 2015-02"). ASU 2015-02 eliminates the deferral of Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46 (R) previously provided to investment companies and certain other entities pursuant to ASC

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810-10-65-2. ASU 2015-02 also amends the evaluation of whether (1) fees paid to a decision maker or service provider represent a variable interest, (2) a limited partnership or similar entity has the characteristics of a variable interest entity ("VIE") and (3) a reporting entity is the primary beneficiary of a VIE. ASU 2015-02 eliminates certain conditions for evaluating whether a fee paid to a decision maker or a service provider represents a variable interest. Fees received by a decision maker or service provider are no longer considered variable interests and are now excluded from the evaluation of whether the reporting entity is the primary beneficiary of a VIE if the fees are both customary and commensurate with the level of effort required for the services provided and the decision maker or service provider does not hold other interests in the entity being evaluated that would absorb more than an insignificant amount of the expected losses or returns of the entity. If the reporting entity determines that it does not have a variable interest in an entity, no further consolidation analysis is performed as the reporting entity would not be required to consolidate the entity.

The effective date of ASU 2015-02 is for fiscal years and interim periods within those fiscal years, beginning after December 15, 2015 for public companies and early adoption is permitted. Fortress has elected to early adopt ASU 2015-02 on a retrospective basis as permitted, for all periods presented. The consolidated financial statements and related footnote disclosures have been adjusted for the impact of the adoption. The adoption did not result in a cumulative effect adjustment to Fortress's retained earnings (accumulated deficit). Fortress's accounting policy, updated for the adoption of ASU 2015-02, is described below.

Basis of Accounting and Consolidation - The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). The accompanying consolidated financial statements include the accounts of Fortress and its consolidated subsidiaries, which are comprised of VIEs in which it is the primary beneficiary as described below and voting interest entities ("VOEs") in which it is determined to have a controlling financial interest under ASC 810, as amended by ASU 2015-02.

For legal entities evaluated for consolidation, Fortress must determine whether the interests that it holds and fees paid to it qualify as a variable interest in the entity. This includes an evaluation of fees paid to Fortress where Fortress acts as a decision maker or service provider to the entity being evaluated. Fees received by Fortress are not variable interests if (i) the fees are compensation for services provided and are commensurate with the level of effort required to provide those services, (ii) the service arrangement includes only terms, conditions, or amounts that are customarily present in arrangements for similar services negotiated at arm's length and (iii) Fortress's other economic interests in the VIE held directly and indirectly through its related parties, as well as economic interests held by related parties under common control, where applicable, would not absorb more than an insignificant amount of the entity's losses or receive more than an insignificant amount of the entity's benefits.

For those entities in which it has a variable interest, Fortress performs an analysis to first determine whether the entity is a VIE. This determination includes considering whether the entity's equity investment at risk is sufficient, whether the voting rights of an investor are not proportional to its obligation to absorb the income or loss of the entity and substantially all of the entity's activities either involve or are conducted on behalf of that investor and its related parties and whether the entity's at-risk equity holders have the characteristics of a controlling financial interest. A VIE must be consolidated by its primary beneficiary. Performance of such analysis requires the exercise of judgment.

The primary beneficiary of a VIE is generally defined as the party who has a controlling financial interest in the VIE. Fortress is generally deemed to have a controlling financial interest in a VIE if it has (i) the power to direct the

activities of the VIE that most significantly affect the VIE's economic performance and (ii) the obligation to absorb losses of the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. For purposes of evaluating (ii) above, fees paid to Fortress are excluded if the fees are compensation for services provided commensurate with the level of effort required to be performed and the arrangement includes only customary terms, conditions or amounts present in arrangements for similar services negotiated at arm's length. Fortress also evaluates its economic interests in the VIE held directly by it and indirectly through its related parties, as well as economic interests held by related parties under common control, where applicable. The primary beneficiary evaluation is generally performed qualitatively on the basis of all facts and circumstances. However, quantitative information may also be considered in the analysis, as appropriate. These analyses require judgment. Changes in the economic interests (either by Fortress, related parties of Fortress or third parties) or amendments to the governing documents of the VIE could affect an entity's status as a VIE or the determination of the primary beneficiary. The primary beneficiary evaluation is updated continuously.

For VOEs, Fortress shall consolidate the entity if it has a controlling financial interest. Fortress has a controlling financial interest in a VOE if (i) for legal entities other than limited partnerships, Fortress owns a majority voting interest in the VOE or, for limited partnerships and similar entities, Fortress owns a majority of the entity's kick-out rights through voting limited partnership interests

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and (ii) non-controlling shareholders or partners do not hold substantive participating rights and no other conditions exist that would indicate that Fortress does not control the entity.

For entities over which Fortress exercises significant influence but which do not meet the requirements for consolidation, Fortress uses the equity method of accounting whereby it records its share of the underlying income of these entities. These entities include the Fortress Funds. The evaluation of whether Fortress exerts control or significant influence over the financial and operational policies of an entity requires judgment based on the facts and circumstances surrounding each individual entity.

Virtually all of the Fortress Funds are, for GAAP purposes, investment companies. Investment companies record realized and unrealized gains (losses) resulting from changes in the fair value of their investments as a component of current income. Additionally, investment companies generally do not consolidate their majority-owned and controlled investments (the "Portfolio Companies").

Distributions by Fortress and its subsidiaries are recognized when declared.

Redeemable Non-controlling Interests represent ownership interests in consolidated subsidiaries which are redeemable and not owned by Fortress.

Principals' and others' interests in consolidated subsidiaries represent the ownership interests in certain consolidated subsidiaries held by entities or persons other than Fortress. This is primarily related to the Principals' interests in Fortress Operating Group (Note 6). Non-Fortress interests also include employee interests in majority owned and controlled fund advisor and general partner entities.

Adoption of ASU No. 2015-02, Consolidation

Prior to the adoption of ASU 2015-02, Fortress consolidated certain VIEs. The financial results of the consolidated VIEs were included in Fortress's consolidated financial statements in previous filings with the Securities and Exchange Commission, based on the then existing consolidation guidance. The adoption of ASU 2015-02 resulted in the deconsolidation of certain of the consolidated VIEs as Fortress determined that under ASU 2015-02 it was not the primary beneficiary of these VIEs. The fee arrangements with the now deconsolidated VIEs are both commensurate with the level of effort required for the services provided, include only customary terms and Fortress does not hold other interests in the VIEs that would absorb more than an insignificant amount of the VIEs' losses or benefits. Therefore, Fortress no longer considers the fee arrangement with these VIEs to be a variable interest. Under ASU 2015-02, Fortress and its related parties under common control as a group, where applicable, do not have the obligation to absorb losses or the right to receive benefits from the VIEs that could potentially be significant to the VIEs. Also see Note 3 for the disclosures related to all of Fortress's VIEs.

The accompanying consolidated financial statements and related footnotes 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 GAAP 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

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interim period or for the entire year. These financial statements should be read in conjunction with Fortress's consolidated financial statements for the year ended December 31, 2014 and footnotes thereto included in Fortress's Annual Report on Form 10-K filed with the Securities and Exchange Commission on February 26, 2015, as revised in Fortress's Current Report on Form 8-K filed with the Securities and Exchange Commission on May 7, 2015. Capitalized terms used herein, and not otherwise defined, are defined in Fortress's consolidated financial statements for the year ended December 31, 2014.

All significant intercompany accounts and transactions have been eliminated.

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

Fortress has two principal sources of fee income from its agreements with the Fortress Funds: contractual management fees, which are generally based on a percentage of fee paying assets under management, and related incentive income, which is generally based on a percentage of returns, or profits, subject to the achievement of performance criteria. Substantially all of Fortress's net assets, after deducting the portion attributable to non-controlling interests, are a result of Fortress's investments in, or receivables from, these funds. The terms of agreements between Fortress and the Fortress Funds are generally determined in connection with third party fund investors.

Management Fees and Incentive Income

Fortress recognized management fees and incentive income as follows:

	Three Months Ended September		Nine Months Ended September	
	30,	2014	30,	2014
	2015		2015	
Private Equity				
Private Equity Funds				
Management fees: affil.	\$28,515	\$33,585	\$86,877	\$104,228
Management fees: non-affil.	—	53	—	364
Incentive income: affil.	—	—	—	22,094
Permanent Capital Vehicles				
Management fees: affil.	26,932	17,519	68,210	49,015
Management fees, options: affil.	—	4,705	25,158	6,309
Management fees: non-affil.	436	667	1,368	2,358
Incentive income: affil.	(2,625	) 8,887	23,119	32,142
Liquid Hedge Funds				
Management fees: affil.	14,004	29,263	49,137	86,328
Management fees: non-affil.	1,700	4,470	6,248	17,045
Incentive income: affil.	142	700	195	1,686
Incentive income: non-affil.	—	—	39	44
Credit Funds				
Credit Hedge Funds				
Management fees: affil.	35,395	28,755	94,883	84,044
Management fees: non-affil.	15	41	38	85
Incentive income: affil.	1,512	8,282	23,681	26,015
Incentive income: non-affil.	—	—	—	—

Credit PE Funds