COHEN & STEERS INC
Form 10-Q
November 09, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2006**

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: 001-32236

COHEN & STEERS, INC.

(Exact name of Registrant as specified in its charter)

Delaware	**14-1904657**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
280 Park Avenue New York, NY	**10017**
(Address of principal executive offices)	**(Zip Code)**

(212) 832-3232

(Registrant s telephone number, including area code)

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 x No ¨

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

Large Accelerated Filer ¨ Accelerated Filer x Non-Accelerated Filer ¨

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

The number of shares of the Registrant s common stock, par value $0.01 per share, outstanding as of November 9, 2006 was 36,470,027.

COHEN & STEERS, INC. AND SUBSIDIARIES

Form 10-Q

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Forward-Looking Statements

This report and other documents filed by us contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which reflect our current views with respect to, among other things, our operations and financial performance. You can identify these forward-looking statements by the use of words such as outlook, believes, expects, potential, continues, may, should, seeks, approximately, predicts, intends, plans, estimates, anticipates or the negative versions of these comparable words. Such forward-looking statements are subject to various risks and uncertainties.

Accordingly, there are or will be important factors that could cause actual outcomes or results to differ materially from those indicated in these statements. We believe that these factors include, but are not limited to, those described in the Risk Factors section of our Annual Report on Form 10-K for the year ended December 31, 2005, which is accessible on the Securities and Exchange Commission s Web site at *http://www.sec.gov* and on our Web site at *www.cohenandsteers.com*. 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 undertake no obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.

Part I Financial Information

Item 1. Financial Statements

COHEN & STEERS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (Unaudited)

(in thousands, except share data)

	September 30, 2006	December 31, 2005
ASSETS		
Cash and cash equivalents	$ 56,303	$ 39,092
Marketable securities available-for-sale	31,675	87,276
Accounts receivable	24,509	19,044
Property and equipment net	10,229	8,936
Intangible asset net	5,921	9,252
Deferred commissions net	5,341	4,471
Equity investment	5,967	4,427
Deferred income tax asset net	19,145	21,604
Other assets	18,798	4,446
Total assets	$ 177,888	$ 198,548
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Accrued compensation	$ 15,706	$ 15,681
Dividends payable	5,164	4,385
Deferred rent	1,674	1,673
Other liabilities and accrued expenses	10,478	12,114
	33,022	33,853
Stockholders equity:		
Common stock, $0.01 par value; 500,000,000 shares authorized; 36,469,121 and 35,426,202 shares issued and outstanding at September 30, 2006 and December 31, 2005, respectively	362	354
Additional paid-in capital	202,062	183,860
Accumulated deficit	(33,265)	(6,377)
Accumulated other comprehensive income, net of tax	2,216	354
Less: Treasury stock, at cost, 309,270 and 1,043 shares at September 30, 2006 and December 31, 2005, respectively	(6,439)	(20)
Unearned compensation	(20,070)	(13,476)
Total stockholders equity	144,866	164,695
Total liabilities and stockholders equity	$ 177,888	$ 198,548

See notes to condensed consolidated financial statements

COHEN & STEERS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

(in thousands, except per share data)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Revenue				
Investment advisory and administration fees	$ 38,480	$ 31,402	$ 106,784	$ 87,732
Distribution and service fees	4,015	3,122	10,746	8,941
Portfolio consulting and other	1,080	720	3,179	2,515
Investment banking fees	10,375	1,187	13,208	9,618
Total revenue	53,950	36,431	133,917	108,806
Expenses				
Employee compensation and benefits	16,066	10,154	38,655	27,963
Distribution and service fees	5,642	7,838	94,436	21,861
General and administrative	8,159	5,195	20,557	16,400
Depreciation and amortization	1,597	1,380	4,771	4,144
Amortization, deferred commissions	1,139	826	2,879	2,625
Total expenses	32,603	25,393	161,298	72,993
Operating income (loss)	21,347	11,038	(27,381)	35,813
Non-operating income (expense)				
Interest and dividend income	686	877	2,388	2,232
Gain from sale of marketable securities	834	827	2,023	1,976
Gain from sale of property and equipment		289	1,056	289
Foreign currency transaction loss	(8)	(33)	(53)	(64)
Interest expense		(54)		(102)
Net non-operating income	1,512	1,906	5,414	4,331
Income (loss) before provision for income taxes and equity in earnings of affiliate	22,859	12,944	(21,967)	40,144
Provision for income taxes	7,648	5,226	(7,368)	17,250
Equity in earnings of affiliate	513	285	1,221	683
Net income (loss)	$ 15,724	$ 8,003	$ (13,378)	$ 23,577
Earnings (loss) per share				
Basic	$ 0.39	$ 0.20	$ (0.34)	$ 0.59
Diluted	$ 0.39	$ 0.20	$ (0.34)	$ 0.58
Weighted average shares outstanding				
Basic	39,927	39,980	39,865	39,999
Diluted	40,647	40,371	39,865	40,303

See notes to condensed consolidated financial statements

COHEN & STEERS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS EQUITY

(Unaudited)

Nine Months Ended September 30, 2006

(in thousands)

	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income, Net	Treasury Stock	Unearned Compensation	Total
Beginning balance, January 1, 2006	$ 354	$ 183,860	$ (6,377)	$ 354	$ (20)	$ (13,476)	$ 164,695
Dividends			(13,510)				(13,510)
Issuance of common stock	8	1,004					1,012
Acquisition of treasury stock					(6,419)		(6,419)
Tax benefits associated with restricted stock units		2,884					2,884
Issuance of restricted stock units		14,455				(12,118)	2,337
Amortization of unearned compensation						5,403	5,403
Forfeitures of restricted stock awards		(141)				121	(20)
Net loss			(13,378)				(13,378)
Other comprehensive income, net				1,862			1,862
Ending balance, September 30, 2006	$ 362	$ 202,062	$ (33,265)	$ 2,216	$ (6,439)	$ (20,070)	$ 144,866

See notes to condensed consolidated financial statements

COHEN & STEERS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(in thousands)

	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Cash flows from operating activities:		
Net income (loss)	$ (13,378)	$ 23,577
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Stock compensation expense	5,535	4,020
Amortization, deferred commissions	2,879	2,625
Depreciation and amortization	4,771	4,144
Amortization, bond discount	(30)	(131)
Deferred rent	1	1,164
Gain from sale of marketable securities	(2,023)	(1,976)
Gain from sale of property and equipment	(1,056)	(289)
Equity in earnings of affiliate	(1,221)	683
Deferred income taxes	3,132	(2,958)
Foreign currency transaction loss	53	64
Tax benefits associated with stock compensation	3,464	941
Changes in operating assets and liabilities:		
Accounts receivable	(5,465)	(3,683)
Deferred commissions	(3,749)	(1,649)
Other assets	(15,271)	(4,814)
Accrued compensation	1,938	6,336
Other liabilities and accrued expenses	(1,149)	5,486
Net cash (used in) provided by operating activities	(21,569)	33,540
Cash flows from investing activities:		
Purchases of marketable securities available-for-sale	(34,006)	(52,450)
Proceeds from maturities of marketable securities available-for-sale	64,057	24,747
Proceeds from sale of marketable securities available-for-sale	29,551	8,199
Purchases of property and equipment	(3,266)	(2,981)
Proceeds from sale of property and equipment	1,152	
Net cash (used in) provided by investing activities	57,488	(22,485)
Cash flows from financing activities:		
Dividends to stockholders	(13,114)	(11,954)
Acquisition of treasury stock	(6,419)	
Payment of capital lease obligations	(55)	(76)
Principal payments on long-term debt		(1,673)
Issuance of common stock	880	215
Net cash used in financing activities	(18,708)	(13,488)
Net increase (decrease) in cash and cash equivalents	17,211	(2,433)
Cash and cash equivalents, beginning of the period	39,092	30,164
Cash and cash equivalents, end of the period	$ 56,303	$ 27,731

See notes to condensed consolidated financial statements

COHEN & STEERS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited) (Continued)

Supplemental disclosures of cash flow information:

For the nine months ended September 30, 2006, there was no cash paid for interest. For the nine months ended September 30, 2005, cash paid for interest totaled $107,000.

For the nine months ended September 30, 2006 and 2005, cash paid for taxes, net of refunds totaled $1.3 million and $21.2 million, respectively.

Supplemental disclosures of non-cash investing and financing activities:

For the nine months ended September 30, 2006 and 2005, the Company acquired property and equipment under capital leases in the amount of $68,000 and $116,000, respectively.

In connection with its stock incentive plan, the Company issued for the nine months ended September 30, 2006 and 2005, fully vested restricted stock units in the amount of $2.0 million and $92,000, respectively. For the nine months ended September 30, 2006 and 2005, the Company issued unvested restricted stock units in the amount of $12.1 million and $5.0 million, respectively. For the nine months ended September 30, 2006 and 2005, forfeitures of restricted stock units totaled $141,000 and $1.4 million, respectively. In addition, for the nine months ended September 30, 2006, the Company recorded restricted stock unit dividend equivalents in the amount of $298,000.

COHEN & STEERS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. Organization and Description of Business

Cohen & Steers, Inc. (CNS) was organized as a Delaware corporation on March 17, 2004. CNS was formed to be the holding company for Cohen & Steers Capital Management, Inc. (CSCM), a New York corporation, and to allow for the issuance of common stock to the public.

The condensed consolidated financial statements set forth herein include the accounts of CNS and its direct and indirect subsidiaries. CNS s significant wholly-owned subsidiaries are CSCM, Cohen & Steers Securities, LLC (Securities) and Cohen & Steers Capital Advisors, LLC (Advisors and collectively, the Company). All material intercompany balances and transactions have been eliminated in consolidation.

The Company provides investment management services to individual and institutional investors through a wide range of open-end mutual funds, closed-end mutual funds and institutional separate accounts. The Company manages high-income equity portfolios, specializing in U.S. REITs, international real estate securities, preferred securities, utilities and large cap value stocks. Its clients include Company-sponsored open-end and closed-end mutual funds and domestic corporate and public pension plans, foreign pension plans, endowment funds and individuals. Through its registered broker/dealers, Securities and Advisors, the Company provides distribution services for certain of its funds as well as investment banking services to companies in real estate and real estate intensive businesses, including healthcare.

2. Basis of Presentation and Significant Accounting Policies

The condensed consolidated financial statements of the Company included herein are unaudited and have been prepared in accordance with the instructions to Form 10-Q pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the interim results have been made. The preparation of the condensed consolidated financial statements requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the condensed consolidated financial statements and the reported amounts of revenue and expenses during the reporting periods. Management believes the estimates used in preparing the condensed consolidated financial statements are reasonable and prudent. Actual results could differ from those estimates.

The Company s condensed consolidated financial statements and the related notes should be read together with the consolidated financial statements and the related notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005 and the condensed consolidated financial statements and the related notes included in the Company s Form 10-Q for the periods ended March 31, 2006 and June 30, 2006. Certain prior period amounts have been reclassified to conform to the September 30, 2006 unclassified balance sheet presentation.

Cash and Cash Equivalents Cash equivalents consist of short-term, highly liquid investments, which are readily convertible into cash and have original maturities of three months or less.

Investments The management of the Company determines the appropriate classification of its investments at the time of purchase and re-evaluates such determination at each statement of financial condition date. Marketable securities classified as available-for-sale are primarily comprised of Company-sponsored open-end and closed-end mutual funds as well as highly rated debt and preferred instruments. These investments are carried at fair value based on quoted market prices, with unrealized gains and losses, net of tax, reported in accumulated other comprehensive income. The Company reviews each individual security position that has an unrealized loss, or impairment, to determine if that impairment is other than temporary. If the Company believes an impairment on a security position is other than temporary, the loss will be recognized in operations. Impairments that arise from changes in interest rates and not credit quality are generally considered temporary.

Goodwill and Intangible Assets Intangible assets are amortized over their useful life. Goodwill represents the excess of the cost of the Company s investment in the net assets of an acquired company over the fair value of the underlying identifiable net assets at the date of acquisition. Goodwill is not amortized but is tested at least annually for impairment by comparing the fair value to the carrying amount, including goodwill. See Notes 3 and 4 for further discussion about the Company s goodwill and intangible asset.

Investment Advisory and Administration Fees The Company earns revenue by providing asset management services to Company-sponsored open-end and closed-end mutual funds and to institutional separate accounts. This revenue is earned pursuant to the terms of the underlying advisory contract, and is based on a contractual investment advisory fee applied to the assets in the client s portfolio. The Company also earns revenue from administration fees paid by certain Company-sponsored open-end and closed-end mutual funds, based on the average daily net assets of such funds. This revenue is recognized as the services are performed.

Distribution and Service Fees Distribution and service fee revenue is earned as the services are performed, generally based on contractually-predetermined percentages of the average daily net assets of the open-end load mutual funds. Distribution and service fee revenue is recorded gross of any third-party distribution and service arrangements. The expenses associated with these third-party distribution and service arrangements are recorded as incurred. During the second quarter of 2006, the Company made payments of $75.7 million to terminate compensation agreements entered into in connection with the common share offerings of certain of its closed-end mutual funds. These payments were reflected as expenses in distribution and service fees on the accompanying statements of operations for the nine months ended September 30, 2006.

Income Taxes The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards (SFAS) No. 109, Accounting For Income Taxes (SFAS 109). The Company recognizes the current and deferred tax consequences of all transactions that have been recognized in the condensed consolidated financial statements using the provisions of the enacted tax laws. Deferred tax assets are recognized for temporary differences that will result in deductible amounts in future years. Deferred tax liabilities are recognized for temporary differences that will result in taxable income in future years. The effective tax rate for interim periods represents the Company s best estimate of the effective tax rate expected to be applied to the full fiscal year.

Stock-based Compensation The Company accounts for stock-based compensation awards in accordance with SFAS No. 123(R), Share-Based Payment (SFAS 123(R)), which requires public companies to recognize expense for the grant-date fair value of awards of equity instruments granted to employees. This expense is recognized over the period during which employees are required to provide service. SFAS 123(R) also requires the Company to estimate forfeitures at the date of grant.

New Accounting Pronouncements In September 2006, the SEC issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108). SAB 108 provides guidance on the consideration of effects of the prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 is effective for the first annual period ending after November 15, 2006. The Company does not anticipate that the adoption of SAB No. 108 will have a material impact on the Company s condensed consolidated financial position or results of operations.

In June 2006, Financial Accounting Standards Board Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48) was issued prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company does not anticipate that the adoption of FIN 48 will have a material impact on its condensed consolidated financial position or results of operations.

3. Intangible Asset

The Company s intangible asset, which will be fully amortized at January 31, 2008, reflects the independently determined value of the non-competition agreements that the Company received from certain employees who were awarded fully vested restricted stock units (RSUs) at the time of its initial public offering. The intangible asset, with an original value of $15,400,000, is being amortized on a straight-line basis over the life of these agreements. The following table details the gross carrying amounts and accumulated amortization for the intangible asset at September 30, 2006 and December 31, 2005 (in thousands):

	September 30, 2006	December 31, 2005
Gross carrying amount	$ 15,400	$ 15,400
Accumulated amortization	(9,479)	(6,148)
Intangible asset, net	$ 5,921	$ 9,252

Amortization expense related to the intangible asset was approximately $1,110,000 for each of the three months ended September 30, 2006 and 2005, and approximately $3,331,000 for each of the nine months ended September 30, 2006 and 2005, respectively. Estimated amortization expense from October 1, 2006 through January 31, 2008, the date the intangible asset is fully amortized, is as follows (in thousands):

Periods Ending December 31,	Estimated Amortization Expense
2006	$ 1,110
2007	4,441
2008	370

4. Investments

Marketable Securities

The following is a summary of the cost and fair value of investments in marketable securities at September 30, 2006 and December 31, 2005 (in thousands):

	September 30, 2006				December 31, 2005			
		Gross Unrealized				Gross Unrealized		
	Cost	Gains	Losses	Market Value	Cost	Gains	Losses	Market Value
Debt securities (1):								
Maturity Less than 1 year	$	$	$	$	$ 36,938	$	$ (243)	$ 36,695
Maturity Between 1 yr - 5 yrs					14,940		(119)	14,821
Preferred securities	5,018	60		5,078	18,710	223		18,933
Equities	2,938	478		3,416	3,852	123		3,975
Company sponsored mutual funds	20,125	3,056		23,181	11,180	1,672		12,852
Total marketable securities	$ 28,081	$ 3,594	$	$ 31,675	$ 85,620	$ 2,018	$ (362)	$ 87,276

(1) Debt securities consist of U.S. Treasury and U.S. Government agency securities.

For the three months ended September 30, 2006 and 2005, sales proceeds from Company-sponsored mutual funds were approximately $1,837,000 and $1,797,000, respectively, and gross realized gains were approximately $442,000 and $775,000 respectively. For the nine months ended September 30, 2006 and 2005, sales proceeds from Company-sponsored mutual funds were approximately $5,193,000 and $4,970,000, respectively, and gross realized gains were approximately $1,113,000 and $1,924,000, respectively. Dividend income from Company-sponsored mutual funds was approximately $51,000 and $85,000, for the three months ended September 30, 2006 and 2005, respectively, and approximately $189,000 and $288,000 for the nine months ended September 30, 2006 and 2005, respectively.

Equity Investment

At September 30, 2006 and December 31, 2005, the Company had a non-controlling 50% investment of approximately $5,967,000 and $4,427,000, respectively, which included approximately $2,866,000 and $2,676,000 of goodwill, respectively, in Houlihan Rovers S.A. (Houlihan Rovers), the Company s Brussels-based investment advisor affiliate. The Company accounts for its investment in Houlihan Rovers using the equity method of accounting. Under such accounting method, the investor recognizes its respective share of the investee s net income for the period. For the three months ended September 30, 2006 and 2005, the Company recognized income of approximately $513,000 and $285,000, respectively. For the nine months ended September 30, 2006 and 2005, the Company recognized income of approximately $1,221,000 and $683,000, respectively.

On October 5, 2006, the Company entered into an agreement to purchase the remaining 50% ownership interest in Houlihan Rovers. The purchase price will be paid using a combination of cash, which will be paid upon the completion of the transaction, and Cohen & Steers restricted stock that will be delivered over three years. The purchase is subject to Belgian regulatory approval and other customary closing conditions and is expected to close in the fourth quarter of 2006.

5. Comprehensive Income

Total comprehensive income includes net income and other comprehensive income, net of tax. The components of comprehensive income for the three and nine months ended September 30, 2006 and 2005 are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Net income (loss)	$ 15,724	$ 8,003	$ (13,378)	$ 23,577
Foreign currency translation gain (loss) adjustment	11	(330)	267	(369)
Net unrealized gain (loss) on available-for-sale securities, net of tax	348	(509)	250	(1,744)
Reclassification of realized gain on available-for-sale securities, net of tax	554	488	1,345	1,166
Total comprehensive income (loss)	$ 16,637	$ 7,652	$ (11,516)	$ 22,630

6. Property and Equipment

On June 1, 2006, the Company sold its fractional ownership interest in an aircraft for approximately $1,152,000. The aircraft had a net book value of approximately $96,000 at June 1, 2006. Pursuant to this transaction, the Company recognized a gain on the sale of approximately $1,056,000 for the nine months ended September 30, 2006.

7. Earnings Per Share

Basic earnings per share are calculated by dividing net income by the weighted average shares outstanding. Diluted earnings per share for the three months ended September 30, 2006 and for the 2005 periods presented are calculated by dividing net income by the total weighted average shares of common stock outstanding and common stock equivalents. Common stock equivalents are comprised of dilutive potential shares from restricted stock unit awards. Common stock equivalents are excluded from the computation if their effect is anti-dilutive. Diluted earnings per share are computed using the treasury stock method. For the nine months ended September 30, 2006, due to the Company s loss, all common stock equivalents were excluded from the diluted loss per share calculation because their inclusion would have been anti-dilutive. Had the Company earned a profit for the nine months ended September 30, 2006, the Company would have added 628,000 common stock equivalent shares to the Company s basic weighted average shares outstanding to compute diluted weighted average shares outstanding. There were no anti-dilutive common stock equivalents excluded from the computation for the three and nine months ended September 30, 2005.

The following is a reconciliation of the income and share data used in the basic and diluted earnings per share computations for the three and nine months ended September 30, 2006 and 2005 (in thousands, except per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Net income (loss)	$ 15,724	$ 8,003	$ (13,378)	$ 23,577
Basic weighted average shares outstanding	39,927	39,980	39,865	39,999
Dilutive potential shares from restricted stock awards	720	391		304
Diluted weighted average shares outstanding	40,647	40,371	39,865	40,303
Basic earnings (loss) per share	$ 0.39	$ 0.20	$ (0.34)	$ 0.59
Diluted earnings (loss) per share	$ 0.39	$ 0.20	$ (0.34)	$ 0.58

8. Income Taxes

In accordance with SFAS 109, recognition of tax benefits or expenses is required for temporary differences between book and tax bases of assets and liabilities.

Deferred income taxes represent the tax effects of the temporary differences between book and tax bases and are measured using enacted tax rates that will be in effect when such items are expected to reverse. The provision for income taxes in the nine months ended September 30, 2006 includes U.S. federal, state and local taxes at a 33.5% effective tax rate, which represents management s estimate of the rate expected to be applied to the full fiscal year of 2006. The $75.7 million of payments made in the second quarter of 2006 to terminate certain compensation agreements entered into in connection with the common share offerings of certain of the Company s closed-end mutual funds is expected to create a tax loss for the full fiscal year 2006 and will be applied to periods in which the Company has lower tax rates. Management s estimate of the full year s effective tax rate includes an adjustment to the net deferred tax asset resulting from lower state and local taxes.

The Company s deferred tax asset is primarily attributable to future income tax deductions derived from vested restricted stock units granted at the time of the Company s initial public offering. The Company records a valuation allowance, when necessary, to reduce deferred tax assets to an amount that more likely than not will be realized. The Company has determined that no valuation allowance is required for the periods presented.

9. Regulatory Requirements

Securities and Advisors, as registered broker/dealers and member firms of the National Association of Securities Dealers, are subject to the SEC s Uniform Net Capital Rule 15c3-1 (the Rule), which requires that broker/dealers maintain a minimum level of net capital, as defined therein. As of September 30, 2006, Securities and Advisors had net capital of approximately $3,158,000 and $9,315,000, respectively, which exceeded their requirements by approximately $2,868,000 and $8,674,000, respectively. The Rule also provides that equity capital may not be withdrawn or cash dividends paid if the resulting net capital of a broker/dealer is less than the amount required under the Rule.

Securities and Advisors do not carry customer accounts and are exempt from the SEC s Rule 15c3-3 pursuant to provisions (k)(1) and (k)(2)(i) of such rule, respectively.

10. Related Party Transactions

The Company is an investment advisor to, and has administrative agreements with, affiliated open-end and closed-end mutual funds for which certain employees are officers and/or directors. The following table sets forth the amount of revenue the Company earned from these affiliated funds for the three and nine months ended September 30, 2006 and 2005 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Investment advisory and administration fees	$ 31,980	$ 27,269	$ 89,337	$ 76,248
Distribution and service fees	4,015	3,122	10,746	8,941
	$ 35,995	$ 30,391	$ 100,083	$ 85,189

For the three months ended September 30, 2006 and 2005, the Company had investment advisory agreements with certain affiliated closed-end mutual funds, pursuant to which the Company contractually waived approximately $5,153,000 and $5,493,000, respectively, of advisory fees it was otherwise entitled to receive. For the nine months ended September 30, 2006 and 2005, the Company waived approximately $14,839,000 and $13,934,000 of advisory fees, respectively. These investment advisory agreements contractually require the Company to waive a portion of the advisory fees the Company otherwise would charge for up to ten years from the respective fund s inception date. The board of directors of these mutual funds must approve the renewal of the advisory agreements each year, including any reduction in advisory fee waivers scheduled to take effect during that year. As of January 1, 2006, the first such scheduled reduction in advisory fee waivers commenced for one fund.

The Company has agreements with eight affiliated open-end mutual funds to reimburse certain fund expenses. For the three months ended September 30, 2006 and 2005, expenses of approximately $695,000 and $437,000, respectively, were incurred by the Company pursuant to these agreements and are included in general and administrative expenses. For the nine months ended September 30, 2006 and 2005, expenses of approximately $1,761,000 and $1,337,000, respectively, were incurred.

The Company incurs expenses associated with the launch of its open and closed-end mutual funds. These organizational costs, which are included in general and administrative expenses, totaled approximately $161,000 and $242,000 for the three months ended September 30, 2006 and 2005 and $437,000 and $2,411,000 for the nine months ended September 30, 2006 and 2005, respectively.

General and administrative expenses include $1,547,000 and $227,000 of sub-advisory fees paid to Houlihan Rovers for the three months ended September 30, 2006 and 2005, and $3,332,000 and $344,000 for the nine months ended September 30, 2006 and 2005, respectively.

Included in accounts receivable at September 30, 2006 and December 31, 2005 are receivables due from Company-sponsored mutual funds of approximately $12,928,000 and $10,344,000, respectively. Included in other assets at September 30, 2006 and December 31, 2005 are amounts due from Company-sponsored mutual funds of approximately $94,000 and $77,000, respectively.

See Note 4 relating to investments in Company-sponsored mutual funds.

11. Segment Reporting

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, establishes disclosure requirements relating to operating segments in the condensed consolidated financial statements. The Company operates in two business segments: Asset Management and Investment Banking. The Company s reporting segments are strategic divisions that offer different services and are managed separately, as each division requires different resources and marketing strategies.

The Company does not record revenue between segments (referred to as inter-segment revenue).

The Company evaluates performance of its segments based on profit or loss from operations before taxes. Information on the condensed consolidated statement of financial condition data by segment is not disclosed because it is not used in evaluating segment performance and deciding how to allocate resources to segments.

Summarized financial information for the Company s reportable segments is presented in the following tables (in thousands):

	Three Months Ended	
	September 30, 2006	September 30, 2005
Asset Management		
Total revenue, including equity in earnings of affiliate	$ 44,088	$ 35,529
Total expenses	(28,241)	(23,693)
Net non-operating income	1,308	1,838
Income before provision for income taxes	$ 17,155	$ 13,674
Investment Banking		
Total revenue	$ 10,375	$ 1,187
Total expenses	(4,362)	(1,700)
Net non-operating income	204	68