PIPER JAFFRAY COMPANIES
Form 10-Q
November 03, 2011
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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, 2011

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 No. 001-31720

PIPER JAFFRAY COMPANIES

(Exact Name of Registrant as specified in its Charter)

DELAWARE (State or Other Jurisdiction of Incorporation or Organization)	**30-0168701** (IRS Employer Identification No.)
800 Nicollet Mall, Suite 800 **Minneapolis, Minnesota** (Address of Principal Executive Offices)	**55402** (Zip Code)

(612) 303-6000

(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 þ 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 Regulation 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 þ 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: þ	Accelerated filer: ¨	Non-accelerated filer: ¨ (Do not check if a smaller reporting company)	Smaller reporting company: ¨

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

As of October 28, 2011, the registrant had 19,170,470 shares of Common Stock outstanding.

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Piper Jaffray Companies

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

Piper Jaffray Companies

Consolidated Statements of Financial Condition

(Amounts in thousands, except share data)	**September 30, 2011** (Unaudited)	**December 31, 2010**
Assets		
Cash and cash equivalents	**$ 42,808**	$ 50,602
Cash and cash equivalents segregated for regulatory purposes	**9,006**	27,006
Receivables:		
Customers	**47,812**	42,955
Brokers, dealers and clearing organizations	**144,786**	188,798
Securities purchased under agreements to resell	**195,659**	258,997
Financial instruments and other inventory positions owned	**418,715**	358,344
Financial instruments and other inventory positions owned and pledged as collateral	**704,862**	515,806
Total financial instruments and other inventory positions owned	**1,123,577**	874,150
Fixed assets (net of accumulated depreciation and amortization of $57,941 and $57,777, respectively)	**22,576**	21,477
Goodwill	**322,650**	322,594
Intangible assets (net of accumulated amortization of $19,639 and $18,232, respectively)	**53,373**	59,580
Other receivables	**47,257**	54,098
Other assets	**125,907**	133,530
Total assets	**$ 2,135,411**	$ 2,033,787
Liabilities and Shareholders Equity		
Short-term financing	**$ 195,827**	$ 193,589
Bank syndicated financing	**117,500**	125,000
Payables:		
Customers	**36,542**	51,814
Brokers, dealers and clearing organizations	**76,292**	18,519
Securities sold under agreements to repurchase	**362,536**	239,880
Financial instruments and other inventory positions sold, but not yet purchased	**347,561**	365,747
Accrued compensation	**91,158**	147,729
Other liabilities and accrued expenses	**37,223**	73,408
Total liabilities	**1,264,639**	1,215,686
Shareholders equity:		
Common stock, $0.01 par value:		
Shares authorized: 100,000,000 at September 30, 2011 and December 31, 2010;		
Shares issued: 19,524,512 at September 30, 2011 and 19,509,813 at December 31, 2010;		
Shares outstanding: 15,912,860 at September 30, 2011 and 14,652,665 at December 31, 2010	**195**	195
Additional paid-in capital	**794,988**	836,152
Retained earnings	**193,899**	179,555
Less common stock held in treasury, at cost: 3,611,652 shares at September 30, 2011 and 4,857,148 shares at December 31, 2010	**(150,614)**	(203,317)
Other comprehensive income	**671**	727
Total common shareholders equity	**839,139**	813,312

Noncontrolling interests	**31,633**	4,789
Total shareholders equity	**870,772**	818,101
Total liabilities and shareholders equity	**$ 2,135,411**	$ 2,033,787

See Notes to the Consolidated Financial Statements

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Piper Jaffray Companies

Consolidated Statements of Operations

(Unaudited)

(Amounts in thousands, except per share data)	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Revenues:				
Investment banking	**$ 44,729**	$ 56,243	**$ 158,832**	$ 171,736
Institutional brokerage	**31,533**	40,432	**116,934**	121,611
Asset management	**15,205**	16,812	**52,774**	41,839
Interest	**15,162**	11,497	**42,535**	39,259
Other income/(loss)	**441**	(368)	**12,578**	6,054
Total revenues	**107,070**	124,616	**383,653**	380,499
Interest expense	**8,894**	8,153	**24,748**	26,797
Net revenues	**98,176**	116,463	**358,905**	353,702
Non-interest expenses:				
Compensation and benefits	**65,307**	66,058	**224,228**	208,832
Occupancy and equipment	**7,477**	8,853	**24,917**	24,578
Communications	**5,978**	5,943	**18,792**	18,631
Floor brokerage and clearance	**2,233**	2,879	**6,918**	8,803
Marketing and business development	**5,708**	5,863	**18,643**	17,280
Outside services	**6,664**	7,945	**21,589**	23,684
Restructuring-related expenses		1,333		1,333
Intangible asset amortization expense	**2,069**	2,183	**6,207**	5,363
Other operating expenses	**2,440**	2,116	**8,643**	11,076
Total non-interest expenses	**97,876**	103,173	**329,937**	319,580
Income before income tax expense	**300**	13,290	**28,968**	34,122
Income tax expense	**3,676**	6,524	**13,778**	19,627
Net income/(loss)	**(3,376)**	6,766	**15,190**	14,495
Net income/(loss) applicable to noncontrolling interests	**207**	(288)	**846**	(447)
Net income/(loss) applicable to Piper Jaffray Companies	**$ (3,583)**	$ 7,054	**$ 14,344**	$ 14,942
Net income/(loss) applicable to Piper Jaffray Companies' common shareholders	**$ (3,583)**	$ 5,415	**$ 11,648**	$ 11,671
Earnings per common share				
Basic	**$ (0.23)**	$ 0.36	$ 0.74	$ 0.75
Diluted	**$ (0.23)**(1)	$ 0.36	$ 0.74	$ 0.75
Weighted average number of common shares outstanding				
Basic	**15,889**	15,035	15,638	15,588
Diluted	**15,889**(1)	15,038	15,655	15,626

(1) Earnings per diluted common share is calculated using the basic weighted average number of common shares outstanding for periods in which a loss is incurred.

See Notes to the Consolidated Financial Statements

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Piper Jaffray Companies

Consolidated Statements of Cash Flows

(Unaudited)

(Dollars in thousands)	**Nine Months Ended September 30, 2011**	**2010**
Operating Activities:		
Net income	**$ 15,190**	$ 14,495
Adjustments to reconcile net income to net cash provided by/(used in) operating activities:		
Depreciation and amortization of fixed assets	**5,439**	5,475
Deferred income taxes	**16,852**	13,385
Stock-based compensation	**21,114**	16,140
Amortization of intangible assets	**6,207**	5,363
Amortization of forgivable loans	**5,935**	5,411
Decrease/(increase) in operating assets:		
Cash and cash equivalents segregated for regulatory purposes	**18,000**	(11,000)
Receivables:		
Customers	**(4,891)**	(8,856)
Brokers, dealers and clearing organizations	**44,031**	116,098
Securities purchased under agreements to resell	**63,338**	(110,179)
Net financial instruments and other inventory positions owned	**(267,613)**	(74,363)
Other receivables	**958**	(15,489)
Other assets	**(9,087)**	1,912
Increase/(decrease) in operating liabilities:		
Payables:		
Customers	**(15,653)**	14,166
Brokers, dealers and clearing organizations	**57,754**	29,253
Securities sold under agreements to repurchase	**3,759**	33,988
Accrued compensation	**(45,861)**	(50,131)
Other liabilities and accrued expenses	**(35,870)**	20,466
Net cash provided by/(used in) operating activities	**(120,398)**	6,134
Investing Activities:		
Business acquisitions, net of cash acquired	**(56)**	(182,105)
Purchases of fixed assets, net	**6,534**	(8,961)
Net cash used in investing activities	**(6,590)**	(191,066)
Financing Activities:		
Increase in short-term financing	**2,238**	16,938
Decrease in bank syndicated financing	**(7,500)**	
Decrease in securities loaned		(25,988)
Increase in securities sold under agreements to repurchase	**118,897**	243,255
Increase in noncontrolling interests	**25,998**	208
Repurchase of common stock	**(20,280)**	(54,902)
Proceeds from stock option transactions	**40**	98
Net cash provided by financing activities	**119,393**	179,609
Currency adjustment:		
Effect of exchange rate changes on cash	**(199)**	(115)

		2011		2010
Net decrease in cash and cash equivalents		**(7,794)**		(5,438)
Cash and cash equivalents at beginning of period		**50,602**		43,942
Cash and cash equivalents at end of period	**$**	**42,808**	$	38,504
Supplemental disclosure of cash flow information -				
Cash paid during the period for:				
Interest	**$**	**26,642**	$	27,908
Income taxes	**$**	**20,618**	$	4,539
Non-cash investing activities -				
Issuance of restricted common stock for acquisition of Advisory Research, Inc.:				
893,105 shares for the nine months ended September 30, 2010	**$**		$	31,822
Non-cash financing activities -				
Issuance of common stock for retirement plan obligations:				
90,085 shares and 81,696 shares for the nine months ended September 30, 2011 and 2010, respectively	**$**	**3,814**	$	3,634
Issuance of restricted common stock for annual equity award:				
592,697 shares and 699,673 shares for the nine months ended September 30, 2011 and 2010, respectively	**$**	**25,095**	$	31,121

See Notes to the Consolidated Financial Statements

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Piper Jaffray Companies

Notes to the Consolidated Financial Statements

Note 1 *Background*

Piper Jaffray Companies is the parent company of Piper Jaffray & Co. (Piper Jaffray), a securities broker dealer and investment banking firm; Piper Jaffray Asia Holdings Limited, an entity providing investment banking services in China headquartered in Hong Kong; Piper Jaffray Ltd., a firm providing securities brokerage and mergers and acquisitions services in Europe headquartered in London, England; Advisory Research, Inc. (ARI), Fiduciary Asset Management, Inc. (FAMCO), and Piper Jaffray Investment Management LLC, entities providing asset management services to separately managed accounts, closed- and open-end funds and partnerships; Piper Jaffray Financial Products Inc., Piper Jaffray Financial Products II Inc. and Piper Jaffray Financial Products III Inc., entities that facilitate derivative transactions; and other immaterial subsidiaries. Piper Jaffray Companies and its subsidiaries (collectively, the Company) operate in two reporting segments: Capital Markets and Asset Management. A summary of the activities of each of the Company s business segments is as follows:

Capital Markets

The Capital Markets segment provides institutional sales, trading and research services and investment banking services. Institutional sales, trading and research services focus on the trading of equity and fixed income products with institutions, government and non-profit entities. Revenues are generated through commissions and sales credits earned on equity and fixed income institutional sales activities, net interest revenues on trading securities held in inventory, profits and losses from trading these securities and strategic trading opportunities. Investment banking services include management of and participation in underwritings, merger and acquisition services and public finance activities. Revenues are generated through the receipt of advisory and financing fees.

Asset Management

The Asset Management segment provides asset management services with product offerings in equity and fixed income securities and a municipal hedge fund, to institutions and high net worth individuals through proprietary distribution channels. Revenues are generated in the form of management fees and performance fees. The majority of the Company s performance fees, if earned, are recognized in the fourth quarter.

Basis of Presentation

The consolidated financial statements include the accounts of Piper Jaffray Companies, its wholly owned subsidiaries and other entities in which the Company has a controlling financial interest. Noncontrolling interests represent equity interests in consolidated entities that are not attributable, either directly or indirectly, to Piper Jaffray Companies. Noncontrolling interests include the minority equity holders proportionate share of the equity in a municipal hedge fund and private equity investment vehicles. All material intercompany balances have been eliminated. Certain financial information for prior periods has been reclassified to conform to the current period presentation.

The consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (SEC) with respect to Form 10-Q and reflect all adjustments that in the opinion of management are normal and recurring and that are necessary for a fair statement of the results for the interim periods presented. In accordance with these rules and regulations, certain disclosures that are normally included in annual financial statements have been omitted. The consolidated financial statements included in this Form 10-Q should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

The consolidated financial statements are prepared in conformity with U.S. generally accepted accounting principles (U.S. GAAP). These principles require management to make certain estimates and assumptions that may affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The nature of the Company s business is such that the results of any interim period may not be indicative of the results to be expected for a full year.

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Note 2 *Summary of Significant Accounting Policies*

Refer to the Company s Annual Report on Form 10-K for the year ended December 31, 2010, for a full description of the Company s significant accounting policies.

Note 3 *Recent Accounting Pronouncements*

Adoption of New Accounting Standards

Fair Value Measurements

In January 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-06, Improving Disclosures about Fair Value Measurements, (ASU 2010-06) amending FASB Accounting Standards Codification Topic 820, Fair Value Measurements and Disclosures (ASC 820). The amended guidance requires entities to disclose additional information regarding assets and liabilities that are transferred between levels of the fair value hierarchy and to disclose information in the Level III rollforward about purchases, sales, issuances and settlements on a gross basis. ASU 2010-06 also further clarifies existing guidance pertaining to the level of disaggregation at which fair value disclosures should be made and the requirements to disclose information about the valuation techniques and inputs used in estimating Level II and Level III fair value measurements. The guidance in ASU 2010-06 was effective for the Company January 1, 2010, except for the requirement to separately disclose purchases, sales, issuances and settlements on a gross basis in the Level III rollforward, which was effective January 1, 2011. While the adoption of ASU 2010-06 did not change accounting requirements, it did impact the Company s disclosures about fair value measurements.

Future Adoption of New Accounting Standards

Repurchase Agreements

In April 2011, the FASB issued ASU No. 2011-03, Reconsideration of Effective Control for Repurchase Agreements, (ASU 2011-03) amending FASB Accounting Standards Codification Topic 860, Transfers and Servicing (ASC 860). The amended guidance addresses the reporting of repurchase agreements (repos) and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. ASC 860 states that the accounting for repos depends in part on whether the transferor maintains effective control over the transferred financial assets. If the transferor maintains effective control, the transferor is required to account for its repo as a secured borrowing rather than a sale. ASU 2011-03 removes from the assessment of effective control the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets. ASU 2011-03 is applicable to new transactions and transactions that are modified on or after the first interim or annual period beginning on or after December 15, 2011. The adoption of ASU 2011-03 is not expected to have an impact on the consolidated financial statements of the Company because the Company accounts for all of its repurchase transactions as secured borrowings.

Fair Value Measurements and Disclosures

In May 2011, the FASB issued ASU No. 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs, (ASU 2011-04) amending ASC 820. The amended guidance improves the comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with U.S. GAAP and International Financial Reporting Standards. Although most of the amendments only clarify existing guidance in U.S. GAAP, ASU 2011-04 requires new disclosures, with a particular focus on Level III measurements, including quantitative information about the significant unobservable inputs used for all Level III measurements and a qualitative discussion about the sensitivity of recurring Level III measurements to changes in the unobservable inputs disclosed. ASU 2011-04 also requires the hierarchy classification for those items whose fair value is not recorded on the balance sheet but is disclosed in the footnotes. ASU 2011-04 is effective during interim and annual periods beginning after December 15, 2011. Disclosures are not required in earlier periods for comparative purposes. The adoption of ASU 2011-04 is not expected to have a material impact on the Company s results of operations or financial position, but it will impact the Company s disclosures about fair value measurements.

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Comprehensive Income

In June 2011, the FASB issued ASU No. 2011-05, Presentation of Comprehensive Income, (ASU 2011-05) amending FASB Accounting Standards Codification Topic 220, Comprehensive Income. The amended guidance improves the comparability, consistency, and transparency of financial reporting and increases the prominence of items reported in other comprehensive income. ASU 2011-05 eliminates the option to present components of other comprehensive income as part of the statement of changes in stockholders equity, and requires that all nonowner changes in stockholders equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 is effective for interim and annual periods beginning after December 15, 2011, and will be applied on a retrospective basis. The adoption of ASU 2011-05 will not impact the Company s results of operations or financial position. The Company will update its presentation of other comprehensive income, and the components of other comprehensive income in a single continuous statement of comprehensive income.

Goodwill

In September 2011, the FASB issued ASU No. 2011-08, Testing Goodwill for Impairment, (ASU 2011-08) amending FASB Accounting Standards Codification Topic 350, Intangibles Goodwill and Other (ASC 350). The amended guidance permits companies to first assess qualitative factors in determining whether the fair value of a reporting unit is less than its carrying amount. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. The adoption of ASU 2011-08 will not impact the Company s results of operations or financial position.

Note 4 *Acquisition of Advisory Research, Inc.*

On March 1, 2010, the Company completed the purchase of ARI, an asset management firm based in Chicago, Illinois. The purchase was completed pursuant to the securities purchase agreement dated December 20, 2009. The fair value as of the acquisition date was $212.1 million, consisting of $180.3 million in cash and 893,105 shares (881,846 of which vest in four equal annual installments) of the Company s common stock valued at $31.8 million. The fair value of the 881,846 shares of common stock with vesting restrictions was determined using the market price of the Company s common stock on the date of the acquisition discounted for the liquidity restrictions in accordance with the valuation principles of ASC 820. The vesting provisions of these 881,846 shares (of which 220,466 shares vested on March 1, 2011) are principally time-based, but also include certain post-termination restrictions. The remaining 11,259 shares had no vesting restrictions and the fair value was determined using the market price of the Company s common stock on the date of the acquisition. A portion of the purchase price payable in cash was funded by proceeds from the issuance of variable rate senior notes (Notes) in the amount of $120 million pursuant to the note purchase agreement (Note Purchase Agreement) dated December 31, 2009 with certain entities advised by Pacific Investment Management Company LLC (PIMCO) and discussed further in Note 14 to these consolidated financial statements.

The acquisition was accounted for under the acquisition method of accounting in accordance with FASB Accounting Standards Codification Topic 805, Business Combinations. Accordingly, goodwill was measured as the excess of the acquisition-date fair value of the consideration transferred over the amount of acquisition-date identifiable assets acquired net of assumed liabilities. The Company recorded $152.3 million of goodwill as an asset on the consolidated statements of financial condition, which is deductible for income tax purposes. In management s opinion, the goodwill represents the reputation and expertise of ARI in the asset management business.

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Identifiable intangible assets purchased by the Company consisted of customer relationships and the ARI trade name with acquisition-date fair values of $52.2 million and $2.9 million, respectively. Acquisition costs of $96,000 were incurred in the nine months ended September 30, 2010, and are included in outside services on the consolidated statements of operations.

The following table summarizes the fair value of assets acquired and liabilities assumed at the date of the acquisition:

(Dollars in thousands)	
Assets:	
Cash and cash equivalents	$ 2,008
Other receivables	8,861
Fixed assets	377
Goodwill	152,282
Intangible assets	55,059
Other assets	369
Total assets acquired	218,956
Liabilities:	
Accrued compensation	149
Other liabilities and accrued expenses	6,726
Total liabilities assumed	6,875
Net assets acquired	$ 212,081

ARI s results of operations have been included in the consolidated Company s financial statements prospectively beginning on the date of acquisition.

The following unaudited pro forma financial data assumes the acquisition had occurred on January 1, 2010, the beginning of the period in which the acquisition occurred. Pro forma results have been prepared by adjusting the consolidated Company s historical results to include ARI s results of operations adjusted for the following changes: depreciation and amortization expenses were adjusted as a result of acquisition-date fair value adjustments to fixed assets, intangible assets, deferred acquisition costs and lease obligations; interest expense was adjusted for revised debt structures; and the income tax effect of applying the Company s statutory tax rates to ARI s results. The consolidated Company s unaudited pro forma information presented does not necessarily reflect the results of operations that would have resulted had the acquisition been completed at the beginning of the applicable period presented, nor does it indicate the results of operations in future periods.

(Dollars in thousands)	**Nine Months Ended September 30, 2010**
Net revenues	$ 361,748
Net income applicable to Piper Jaffray Companies	$ 16,689

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Note 5 *Financial Instruments and Other Inventory Positions Owned and Financial Instruments and Other Inventory Positions Sold, but Not Yet Purchased*

Financial instruments and other inventory positions owned and financial instruments and other inventory positions sold, but not yet purchased were as follows:

(Dollars in thousands)	**September 30, 2011**	**December 31, 2010**
Financial instruments and other inventory positions owned:		
Corporate securities:		
Equity securities	**$ 32,064**	$ 18,089
Convertible securities	**56,990**	37,290
Fixed income securities	**76,993**	58,591
Municipal securities:		
Taxable securities	**255,423**	295,439
Tax-exempt securities	**316,618**	137,340
Short-term securities	**87,705**	48,830
Asset-backed securities	**87,042**	88,922
U.S. government agency securities	**162,194**	153,739
U.S. government securities	**7,609**	6,569
Derivative contracts	**40,939**	29,341
	$ 1,123,577	$ 874,150
Financial instruments and other inventory positions sold, but not yet purchased:		
Corporate securities:		
Equity securities	**$ 49,278**	$ 23,651
Convertible securities	**4,423**	8,320
Fixed income securities	**25,629**	17,965
Asset-backed securities	**9,674**	12,425
U.S. government agency securities	**16,622**	52,934
U.S. government securities	**236,338**	250,452
Derivative contracts	**5,597**	-
	$ 347,561	$ 365,747

At September 30, 2011 and December 31, 2010, financial instruments and other inventory positions owned in the amount of $704.9 million and $515.8 million, respectively, had been pledged as collateral for the Company s repurchase agreements and short-term financings.

Inventory positions sold, but not yet purchased represent obligations of the Company to deliver the specified security at the contracted price, thereby creating a liability to purchase the security in the market at prevailing prices. The Company is obligated to acquire the securities sold short at prevailing market prices, which may exceed the amount reflected on the consolidated statements of financial condition. The Company economically hedges changes in market value of its financial instruments and other inventory positions owned utilizing inventory positions sold, but not yet purchased, interest rate derivatives, credit default swap index contracts, futures and exchange-traded options.

Derivative Contract Financial Instruments

The Company uses interest rate swaps, interest rate locks, credit default swap index contracts and foreign currency forward contracts to facilitate customer transactions and as a means to manage risk in certain inventory positions and firm investments. The following describes the Company s derivatives by the type of transaction or security the instruments are economically hedging.

Customer matched-book derivatives: The Company enters into interest rate derivative contracts in a principal capacity as a dealer to satisfy the financial needs of its customers. The Company simultaneously enters into an interest rate derivative contract with a third party for the same

notional amount to hedge the interest rate and credit risk of the initial client interest rate derivative contract. In certain limited instances, the Company has only hedged interest rate risk with a third party, and retains uncollateralized credit risk as described below. The instruments use interest rates based upon either the London Interbank Offer Rate (LIBOR) index or the Securities Industry and Financial Markets Association (SIFMA) index.

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Trading securities derivatives: The Company enters into interest rate derivative contracts to hedge interest rate and market value risks associated with its fixed income securities. The instruments use interest rates based upon either the Municipal Market Data (MMD) index, LIBOR or the SIFMA index. The Company also enters into credit default swap index contracts to hedge credit risk associated with its taxable fixed income securities.

Firm investments: The Company entered into foreign currency forward contracts to manage the currency exposure related to its non-U.S. dollar denominated firm investments.

The following table presents the total absolute notional contract amount associated with the Company s outstanding derivative instruments:

(Dollars in thousands) **Transaction Type or Hedged Security**	**Derivative Category**	**September 30, 2011**	**December 31, 2010**
Customer matched-book	Interest rate derivative contract	**$ 6,045,651**	$ 6,505,232
Trading securities	Interest rate derivative contract	**174,750**	192,250
Trading securities	Credit default swap index contract	**160,000**	200,000
Firm investments	Foreign currency forward contract	-	16,645
		$ 6,380,401	$ 6,914,127

The Company s interest rate derivative contracts, credit default swap index contracts and foreign currency forward contracts do not qualify for hedge accounting, therefore, unrealized gains and losses are recorded on the consolidated statements of operations. The following table presents the Company s unrealized gains/(losses) on derivative instruments:

(Dollars in thousands)		**Three Months Ended September 30,**		**Nine Months Ended September 30,**	
Derivative Category	**Operations Category**	**2011**	**2010**	**2011**	**2010**
Interest rate derivative contract	Investment banking	**$ 238**	$ 6,434	**$ (3,107)**	$ 3,566
Interest rate derivative contract	Institutional brokerage	**(10,090)**	(2,299)	**(17,315)**	(2,485)
Credit default swap index contract	Institutional brokerage	**1,416**	(3,492)	**1,356**	(419)
Foreign currency forward contract	Other operating expenses	**-**	(502)	**59**	12
		$ (8,436)	$ 141	**$ (19,007)**	$ 674

The gross fair market value of all derivative instruments and their location on the Company s consolidated statements of financial condition prior to counterparty netting are shown below by asset or liability position *(1)*:

(Dollars in thousands)		**Asset Value at**		**Liability Value at**
Derivative Category	**Financial Condition Location**	**September 30, 2011**	**Financial Condition Location**	**September 30, 2011**
Interest rate derivative contract	Financial intruments and other inventory positions owned	$ 641,702	Financial intruments and other inventory positions sold, but not yet purchased	$ 624,146
Credit default swap index contract	Financial intruments and other inventory positions owned	3,327	Financial intruments and other inventory positions sold, but not yet purchased	2,749
		$ 645,029		$ 626,895

(1) Amounts are disclosed at gross fair value in accordance with the requirement of FASB Accounting Standards Codification Topic 815, Derivatives and Hedging (ASC 815).

Derivatives are reported on a net basis by counterparty when legal right of offset exists and when applicable provisions are stated in master netting agreements. Cash collateral received or paid is netted on a counterparty basis, provided a legal right of offset exists.

Credit risk associated with the Company s derivatives is the risk that a derivative counterparty will not perform in accordance with the terms of the applicable derivative contract. Credit exposure associated with the Company s derivatives is driven by uncollateralized market movements in the fair value of the contracts with counterparties and is monitored regularly by the Company s financial risk committee. The Company considers counterparty credit risk in determining derivative contract fair value. The majority of the Company s derivative contracts are substantially collateralized by its counterparties, who are major financial institutions. The Company has a limited number of counterparties who are not required to post collateral. Based on market movements, the

uncollateralized amounts representing the fair value of the derivative contract can become material, exposing the Company to the credit risk of these counterparties. As of September 30, 2011, the Company had $35.0 million of uncollateralized credit exposure with these counterparties (notional contract amount of $206.0 million), including $17.7 million of uncollateralized credit exposure with one counterparty.

Note 6 *Fair Value of Financial Instruments*

The Company records financial instruments and other inventory positions owned and financial instruments and other inventory positions sold, but not yet purchased at fair value on the consolidated statements of financial condition with unrealized gains and losses reflected on the consolidated statements of operations.

The degree of judgment used in measuring the fair value of financial instruments generally correlates to the level of pricing observability. Pricing observability is impacted by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established and other characteristics specific to the instrument. Financial instruments with readily available active quoted prices for which fair value can be measured generally will have a higher degree of pricing observability and a lesser degree of judgment used in measuring fair value. Conversely, financial instruments rarely traded or not quoted will generally have less, or no, pricing observability and a higher degree of judgment used in measuring fair value.

The following is a description of the valuation techniques used to measure fair value.

Cash Equivalents

Cash equivalents include highly liquid investments with original maturities of 90 days or less. Actively traded money market funds are measured at their net asset value and classified as Level I.

Financial Instruments and Other Inventory Positions Owned

Equity securities Exchange traded equity securities are valued based on quoted prices from the exchange for identical assets or liabilities as of the period-end date. To the extent these securities are actively traded and valuation adjustments are not applied, they are categorized as Level I. Non-exchange traded equity securities (principally hybrid preferred securities) are measured primarily using broker quotations, pricing service data from external providers and prices observed for recently executed market transactions and are categorized within Level II of the fair value hierarchy. Where such information is not available, non-exchange traded equity securities are categorized as Level III financial instruments and measured using valuation techniques involving quoted prices of or market data for comparable companies. When using pricing data of comparable companies, judgment must be applied to adjust the pricing data to account for differences between the measured security and the comparable security (e.g., issuer market capitalization, yield, dividend rate and geographical concentration).

Convertible securities Convertible securities are valued based on observable trades, when available. Accordingly, these convertible securities are categorized as Level II. When observable price quotations are not available, fair value is determined based upon model-based valuation techniques with observable market inputs, such as specific company stock price and volatility and unobservable inputs such as option adjusted spreads. These instruments are categorized as Level III.

Corporate fixed income securities Fixed income securities include corporate bonds which are valued based on recently executed market transactions of comparable size, pricing service data from external providers when available, or broker quotations. Accordingly, these corporate bonds are categorized as Level II. When observable price quotations are not available, fair value is determined using model-based valuation techniques with observable inputs such as specific security contractual terms and yield curves and unobservable inputs such as credit spreads. Corporate bonds measured using model-based valuation techniques are categorized as Level III.

Taxable municipal securities Taxable municipal securities are valued using recently executed observable trades or market price quotations and therefore are generally categorized as Level II.

Tax-exempt municipal securities Tax-exempt municipal securities are valued using recently executed observable trades or market price quotations and therefore are generally categorized as Level II. Certain illiquid tax-exempt municipal securities are valued using market data for comparable securities (maturity and sector) and management judgment to infer an appropriate current yield and are categorized as Level III.

Short-term municipal securities Short-term municipal securities include auction rate securities, variable rate demand notes, and other short-term municipal securities. Variable rate demand notes and other short-term municipal securities are valued using recently executed observable trades or market price quotations and therefore are generally categorized as Level II. Auction rate securities are categorized as Level III.

Asset-backed securities Asset-backed securities are valued using observable trades, when available. Certain asset-backed securities are valued using models where inputs to the model are directly observable in the market, or can be derived principally from or corroborated by observable market data. These asset-backed securities are categorized as Level II. Other asset-backed securities, which are principally collateralized by residential mortgages or aircraft, have experienced low volumes of executed transactions that results in less observable transaction data. Asset-backed securities collateralized by residential mortgages are valued using cash flow models that utilize unobservable inputs including credit default rates ranging from 0.5-10%, prepayment rates ranging from 4-10% of CPR, severity ranging from 30-80% and valuation yields ranging from 4-10%. Asset-backed securities collateralized by aircraft are valued using cash flow models that utilize unobservable inputs including airplane lease rates, aircraft residual valuation, trust costs, and other factors impacting security cash flows. The Company s aircraft asset-backed securities had a weighted average yield of 8.9% at September 30, 2011. As judgment is used to determine the range of these inputs, these asset-backed securities are categorized as Level III.

U.S. government agency securities U.S. government agency securities include agency debt bonds and mortgage bonds. Agency debt bonds are valued by using either direct price quotes or price quotes for comparable bond securities and thus, are categorized as Level II. Mortgage bonds include mortgage bonds, mortgage pass-through securities and agency collateralized mortgage-obligations (CMO). Mortgage pass-through securities and CMO securities are valued using recently executed observable trades or other observable inputs, such as prepayment speeds and therefore, generally are categorized as Level II. Mortgage bonds are valued using observable market inputs, such as market yields ranging from 60-140 basis point spreads to treasury securities, or models based upon prepayment expectations ranging from 300-400 Public Securities Association (PSA) prepayment levels. These securities are categorized as Level II.

U.S. government securities U.S. government securities include highly liquid U.S. treasury securities which are generally valued using quoted market prices and therefore categorized as Level I.

Derivatives Derivative contracts include interest rate, forward purchase agreement and basis swaps, interest rate locks, futures, credit default swap index contracts and foreign currency forward contracts. These instruments derive their value from underlying assets, reference rates, indices or a combination of these factors. The majority of the Company s interest rate derivative contracts, including both interest rate swaps and interest rate locks, are valued using market standard pricing models based on the net present value of estimated future cash flows. The valuation models used do not involve material subjectivity as the methodologies do not entail significant judgment and the pricing inputs are market observable, including contractual terms, yield curves and measures of volatility. These instruments are classified as Level II within the fair value hierarchy. Certain interest rate locks transact in less active markets and were valued using valuation models that used the previously mentioned observable inputs and unobservable inputs that required significant judgment. These instruments are classified as Level III. The Company s credit default swap index contracts and foreign currency forward contracts are valued using market price quotations and classified as Level II.

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Investments

The Company s investments valued at fair value include investments in public companies, warrants of public or private companies and investments in certain illiquid municipal bonds. These investments are included in other assets on the consolidated statements of financial condition. Exchange traded direct equity investments in public companies and registered mutual funds are valued based on quoted prices on active markets and reported in Level I. Company-owned warrants, which have a cashless exercise option, are valued based upon the Black-Scholes option-pricing model that uses discount rates and stock volatility factors of comparable companies as inputs. These inputs are subject to management judgment to account for differences between the measured investment and comparable companies. Company-owned warrants are reported as Level III assets. Investments in certain illiquid municipal bonds that the Company is holding for investment are measured using valuation techniques involving significant management judgment and are reported as Level III assets.

Fair Value Option The fair value option permits the irrevocable fair value option election on an instrument-by-instrument basis at initial recognition of an asset or liability or upon an event that gives rise to a new basis of accounting for that instrument. The fair value option was elected for certain merchant banking investments at inception to reflect economic events in earnings on a timely basis. At September 30, 2011, $13.6 million in merchant banking investments, included within other assets on the consolidated statements of financial condition, are accounted for at fair value and are classified as Level III assets. The gains and losses from fair value changes included in earnings as a result of electing to apply the fair value option to certain financial assets, were not material for the nine months ended September 30, 2011.

The following table summarizes the valuation of our financial instruments by pricing observability levels defined in ASC 820 as of September 30, 2011:

(Dollars in thousands)	Level I	Level II	Level III	Counterparty Collateral Netting (1)	Total
Assets:					
Financial instruments and other inventory positions owned:					
Corporate securities:					
Equity securities	$ 24,386	$ 7,678	$ -	$ -	$ 32,064
Convertible securities	-	51,311	5,679	-	56,990
Fixed income securities	-	73,264	3,729	-	76,993
Municipal securities:					
Taxable securities	-	255,423	-	-	255,423
Tax-exempt securities	-	308,924	7,694	-	316,618
Short-term securities	-	87,530	175	-	87,705
Asset-backed securities	-	19,842	67,200	-	87,042
U.S. government agency securities	-	162,122	72	-	162,194
U.S. government securities	7,609	-	-	-	7,609
Derivative contracts	-	59,926	1,143	(20,130)	40,939
Total financial instruments and other inventory positions owned:	31,995	1,026,020	85,692	(20,130)	1,123,577
Cash equivalents	16,831	-	-	-	16,831
Investments	5,979	-	21,958	-	27,937
Total assets	$ 54,805	$ 1,026,020	$ 107,650	$ (20,130)	$ 1,168,345
Liabilities:					
Financial instruments and other inventory positions sold, but not yet purchased:					
Corporate securities:					
Equity securities	$ 45,349	$ 3,929	$ -	$ -	$ 49,278
Convertible securities	-	4,423	-	-	4,423
Fixed income securities	-	23,162	2,467	-	25,629
Asset-backed securities	-	8,067	1,607	-	9,674
U.S. government agency securities	-	16,622	-	-	16,622

U.S. government securities	236,338	-	-	-	236,338
Derivative contracts	-	28,253	14,682	(37,338)	5,597
Total financial instruments and other inventory positions sold, but not yet purchased:	$ 281,687	$ 84,456	$ 18,756	$ (37,338)	$ 347,561

(1) Represents cash collateral and the impact of netting on a counterparty basis. The Company had no securities posted as collateral to its counterparties.

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The following table summarizes the valuation of our financial instruments by pricing observability levels defined in ASC 820 as of December 31, 2010:

(Dollars in thousands)	Level I	Level II	Level III	Counterparty Collateral Netting (1)	Total
Assets:					
Financial instruments and other inventory positions owned:					
Corporate securities:					
Equity securities	$ 14,509	$ 2,240	$ 1,340	$ -	$ 18,089
Convertible securities	-	34,405	2,885	-	37,290
Fixed income securities	-	52,323	6,268	-	58,591
Municipal securities:					
Taxable securities	-	295,439	-	-	295,439
Tax-exempt securities	-	131,222	6,118	-	137,340
Short-term securities	-	48,705	125	-	48,830
Asset-backed securities	-	43,752	45,170	-	88,922
U.S. government agency securities	-	153,739	-	-	153,739
U.S. government securities	6,569	-	-	-	6,569
Derivative contracts	-	58,047	4,665	(33,371)	29,341
Total financial instruments and other inventory positions owned:	21,078	819,872	66,571	(33,371)	874,150
Cash equivalents	9,923	-	-	-	9,923
Investments	4,961	-	9,682	-	14,643
Total assets	$ 35,962	$ 819,872	$ 76,253	$ (33,371)	$ 898,716
Liabilities:					
Financial instruments and other inventory positions sold, but not yet purchased:					
Corporate securities:					
Equity securities	$ 23,651	$ -	$ -	$ -	$ 23,651
Convertible securities	-	6,543	1,777	-	8,320
Fixed income securities	-	15,642	2,323	-	17,965
Asset-backed securities	-	10,310	2,115	-	12,425
U.S. government agency securities	-	52,934	-	-	52,934
U.S. government securities	250,452	-	-	-	250,452
Derivative contracts	-	21,084	339	(21,423)	-
Total financial instruments and other inventory positions sold, but not yet purchased:	$ 274,103	$ 106,513	$ 6,554	$ (21,423)	$ 365,747

(1) Represents cash collateral and the impact of netting on a counterparty basis. The Company had no securities posted as collateral to its counterparties.

The Company s Level III assets were $107.7 million and $76.3 million, or 9.2 percent and 8.5 percent of financial instruments measured at fair value at September 30, 2011 and December 31, 2010, respectively. Transfers between levels are recognized at the beginning of the reporting period. There were $6.5 million of transfers of financial assets from Level II to Level III during the nine months ended September 30, 2011 related to tax-exempt securities, fixed income securities, and convertible securities for which no recent trade activity was observed and valuation inputs became unobservable. There were no transfers of financial liabilities from Level II to Level III during the nine months ended September 30, 2011. There were $2.9 million of transfers of financial assets and $3.6 million of transfers of financial liabilities from Level III to Level II during the nine months ended September 30, 2011 related to fixed income and convertible securities for which market trades were observed that provided transparency into the valuation of these assets. In addition, a transfer restriction on a principal investment expired in the third quarter of 2011, resulting in a $4.5 million transfer from Level III to Level I. Transfers between Level I and Level II were not material for the nine months ended September 30, 2011 and 2010, respectively.

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As discussed in Note 3, the Company began disclosing information in the Level III rollforward on a gross basis for purchases, sales, issuances and settlements effective January 1, 2011. The following tables summarize the changes in fair value associated with Level III financial instruments during the nine months ended September 30, 2011 and 2010:

(Dollars in thousands)	**Balance at December 31, 2010**	Purchases	Sales	Transfers in	Transfers out	Realized gains/ (losses) (1)	Unrealized gains/ (losses) (1)	**Balance at September 30, 2011**
Assets:								
Financial instruments and other inventory positions owned:								
Corporate securities:								
Equity securities	**$ 1,340**	$ -	$ (1,467)	$ -	$ -	$ 127	$ -	**$ -**
Convertible securities	**2,885**	101,985	(97,622)	2,550	(2,885)	729	(1,963)	**5,679**
Fixed income securities	**6,268**	24,435	(27,437)	198	-	113	152	**3,729**
Municipal securities:								
Tax-exempt securities	**6,118**	13,799	(15,934)	3,791	-	47	(127)	**7,694**
Short-term securities	**125**	50	-	-	-	-	-	**175**
Asset-backed securities	**45,170**	128,641	(106,609)	-	-	3	(5)	**67,200**
U.S. government agency securities	**-**	121	(48)	-	-	-	(1)	**72**
Derivative contracts	**4,665**	2,141	(2,363)	-	-	222	(3,522)	**1,143**
Total financial instruments and other inventory positions owned:	**66,571**	271,172	(251,480)	6,539	(2,885)	1,241	(5,466)	**85,692**
Investments	**9,682**	14,421	(688)	-	(4,536)	688	2,391	**21,958**
Total assets	**$ 76,253**	$ 285,593	$ (252,168)	$ 6,539	$ (7,421)	$ 1,929	$ (3,075)	**$ 107,650**
Liabilities:								
Financial instruments and other inventory positions sold, but not yet purchased:								
Corporate securities:								
Convertible securities	**$ 1,777**	$ -	$ -	$ -	$ (1,777)	$ -	$ -	**$ -**
Fixed income securities	**2,323**	(2,581)	4,613	-	(1,838)	(21)	(29)	**2,467**
Asset-backed securities	**2,115**	(4,925)	4,484	-	-	19	(86)	**1,607**
Derivative contracts	**339**	(1,482)	-	-	-	1,482	14,343	**14,682**
Total financial instruments and other inventory positions sold, but not yet purchased:	**$ 6,554**	$ (8,988)	$ 9,097	$ -	$ (3,615)	$ 1,480	$ 14,228	**$ 18,756**

(Dollars in thousands)	**Balance at December 31, 2009**	Purchases/ (sales), net	Net transfers in/(out)	Realized gains/ (losses) (1)	Unrealized gains/ (losses) (1)	**Balance at September 30, 2010**
Assets:						
Financial instruments and other inventory positions owned:						
Corporate securities:						
Equity securities	**$ -**	$ 2,411	$ -	$ 9	$ (140)	**$ 2,280**
Convertible securities	**-**	7,103	(86)	1,753	1,119	**9,889**

Fixed income securities	**-**	(2,326)	6,102	575	(176)	**4,175**
Municipal securities:						
Tax-exempt securities	**-**	3,352	-	-	1	**3,353**
Short-term securities	**17,825**	(15,389)	-	(2,291)	130	**275**
Asset-backed securities	**24,239**	(9,678)	7,232	4,621	(93)	**26,321**
Total financial instruments and other inventory positions owned:	**42,064**	(14,527)	13,248	4,667	841	**46,293**
Investments	**2,240**	(365)	-	219	1,053	**3,147**
Total assets	**$ 44,304**	$ (14,892)	$ 13,248	$ 4,886	$ 1,894	**$ 49,440**
Liabilities:						
Financial instruments and other inventory positions sold, but not yet purchased:						
Corporate securities:						
Fixed income securities	**$ 7,771**	$ (7,960)	$ 2,053	$ 7	$ 209	**$ 2,080**
Asset-backed securities	**2,154**	4,768	(3,872)	(95)	185	**3,140**
Total financial instruments and other inventory positions sold, but not yet purchased:	**$ 9,925**	$ (3,192)	$ (1,819)	$ (88)	$ 394	**$ 5,220**

(1) Realized and unrealized gains/(losses) related to financial instruments, with the exception of foreign currency forward contracts and customer matched-book derivatives, are reported in institutional brokerage on the consolidated statements of operations. Realized and unrealized gains/(losses) related to foreign currency forward contracts are recorded in other operating expenses. Realized and unrealized gains/(losses) related to customer matched-book derivatives are reported in investment banking. Realized and unrealized gains/(losses) related to investments are reported in investment banking revenues or other income/(loss) on the consolidated statements of operations.

The carrying values of some of the Company s financial instruments approximate fair value due to their liquid or short-term nature. Such financial assets and financial liabilities include cash, securities either purchased or sold under agreements to resell, receivables and payables either from or to customers and brokers, dealers and clearing organizations and short-term financings.

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Note 7 *Variable Interest Entities*

In the normal course of business, the Company periodically creates or transacts with entities that are investment vehicles organized as limited partnerships or limited liability companies. These entities were established for the purpose of investing in securities of public or private companies, or municipal debt obligations and were initially financed through the capital commitments of the members. The Company has investments in and/or acts as the managing partner of these entities. In certain instances, the Company provides management and investment advisory services for which it earns fees generally based upon the market value of assets under management and may include incentive fees based upon performance. At September 30, 2011, the Company s aggregate investment in these investment vehicles totaled $46.3 million and is recorded in other assets on the consolidated statements of financial condition. The Company s remaining capital commitments to these entities was $1.7 million at September 30, 2011.

Variable interest entities (VIEs) are entities in which equity investors lack the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities. The determination as to whether an entity is a VIE is based on the amount and nature of the members equity investment in the entity. The Company also considers other characteristics such as the power through voting rights or similar rights to direct the activities of an entity that most significantly impact the entity s economic performance. For those entities that meet the deferral provisions defined by FASB ASU No. 2010-10, Consolidation: Amendments for Certain Investment Funds, (ASU 2010-10), the Company considers characteristics such as the ability to influence the decision making about the entity s activities and how the entity is financed. The Company has identified certain of the entities described above as VIEs. These VIEs had net assets approximating $0.9 billion at September 30, 2011. The Company s exposure to loss from these VIEs is $7.3 million, which is the carrying value of its capital contributions recorded in other assets on the consolidated statements of financial condition at September 30, 2011. The Company had no liabilities related to these VIEs at September 30, 2011.

The Company is required to consolidate all VIEs for which it is considered to be the primary beneficiary. The determination as to whether the Company is considered to be the primary beneficiary is based on whether the Company has both the power to direct the activities of the VIE that most significantly impact the entity s economic performance and the obligation to absorb losses or the right to receive benefits of the VIE that could potentially be significant to the VIE. For those entities that meet the deferral provisions defined by ASU 2010-10, the determination as to whether the Company is considered to be the primary beneficiary is based on whether the Company will absorb a majority of the VIE s expected losses, receive a majority of the VIE s expected residual returns, or both. It was determined the Company is not the primary beneficiary of the VIEs and accordingly does not consolidate them.

The Company has not provided financial or other support to the VIEs that it was not previously contractually required to provide as of September 30, 2011.

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Note 8 *Receivables from and Payables to Brokers, Dealers and Clearing Organizations*

Amounts receivable from brokers, dealers and clearing organizations at September 30, 2011 and December 31, 2010 included:

(Dollars in thousands)	**September 30, 2011**	**December 31, 2010**
Receivable arising from unsettled securities transactions, net	**$ -**	$ 65,923
Deposits paid for securities borrowed	**79,945**	62,720
Receivable from clearing organizations	**19,322**	19,168
Deposits with clearing organizations	**33,313**	24,795
Securities failed to deliver	**9,137**	1,361
Other	**3,069**	14,831
	$ 144,786	$ 188,798

Amounts payable to brokers, dealers and clearing organizations at September 30, 2011 and December 31, 2010 included:

(Dollars in thousands)	**September 30, 2011**	**December 31, 2010**
Payable arising from unsettled securities transactions, net	**$ 45,974**	$ -
Payable to clearing organizations	**4,635**	2,320
Securities failed to receive	**17,389**	499
Other	**8,294**	15,700
	$ 76,292	$ 18,519

Deposits paid for securities borrowed approximate the market value of the securities. Securities failed to deliver and receive represent the contract value of securities that have not been delivered or received by the Company on settlement date.

Note 9 *Collateralized Securities Transactions*

The Company s financing and customer securities activities involve the Company using securities as collateral. In the event that the counterparty does not meet its contractual obligation to return securities used as collateral, or customers do not deposit additional securities or cash for margin when required, the Company may be exposed to the risk of reacquiring the securities or selling the securities at unfavorable market prices in order to satisfy its obligations to its customers or counterparties. The Company seeks to control this risk by monitoring the market value of securities pledged or used as collateral on a daily basis and requiring adjustments in the event of excess market exposure.

In the normal course of business, the Company obtains securities purchased under agreements to resell, securities borrowed and margin agreements on terms that permit it to repledge or resell the securities to others. The Company obtained securities with a fair value of approximately $289.9 million and $351.7 million at September 30, 2011 and December 31, 2010, respectively, of which $261.7 million and $309.9 million, respectively, had been either pledged or otherwise transferred to others in connection with the Company s financing activities or to satisfy its commitments under financial instruments and other inventory positions sold, but not yet purchased.

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At September 30, 2011, the Company s securities sold under agreements to repurchase (Repurchase Liabilities) exceeded 10 percent of total assets. The following is a summary of Repurchase Liabilities, the fair market value of collateral pledged and the interest rate charged by the Company s counterparty, which is based on LIBOR plus an applicable margin as of September 30, 2011:

(Dollars in thousands)	Repurchase Liabilities	Fair Market Value	Interest Rates
Overnight maturities:			
Corporate securities:			
Fixed income securities	$ 14,042	$ 16,646	1.05%
Municipal securities:			
Taxable securities	113,717	140,056	1.05%
Tax-exempt securities	123,224	148,109	1.05%
Short-term securities	29,349	35,812	1.05%
Term up to 30 day maturities:			
U.S. government agency securities	9,975	9,999	0.22%
On demand maturities:			
Corporate securities:			
Fixed income securities	12,340	12,919	0.65%
U.S. government agency securities	53,223	58,866	0.40 - 0.45%
U.S. government securities	6,666	6,629	0.12%
	$ 362,536	$ 429,036	

Note 10 *Other Assets*

Other assets include net deferred tax assets, prepaid expenses and proprietary investments. The Company s investments include direct equity investments in public companies, investments in private companies and partnerships, warrants of public or private companies, private company debt and investments to fund deferred compensation liabilities.

Other assets at September 30, 2011 and December 31, 2010 included:

(Dollars in thousands)	September 30, 2011	December 31, 2010
Net deferred income tax assets	**$ 45,328**	$ 62,180
Investments at fair value	**27,937**	14,643
Investments at cost	**25,088**	28,794
Investments accounted for under the equity method	**18,199**	16,653
Prepaid expenses	**6,433**	8,897
Other	**2,922**	2,363
Total other assets	**$ 125,907**	$ 133,530

Management regularly reviews the Company s investments in private company debt and has concluded that no valuation allowance is needed as it is probable that all contractual principal and interest will be collected.

At September 30, 2011, the estimated fair market value of investments carried at cost totaled $29.9 million. The estimated fair value of investments carried at cost was measured using valuation techniques involving market data for comparable companies (e.g., multiples of revenue and earnings before interest, taxes, depreciation and amortization (EBITDA)). Valuation adjustments, based upon management s judgment, were made to account for differences between the measured security and comparable securities.

Investments accounted for under the equity method include general and limited partnership interests. The carrying value of these investments is based on the investment vehicles net asset value. The net assets of investment partnerships consist of investments in both marketable and non-marketable securities. The underlying investments held by such partnerships are valued based on the estimated fair value ultimately

determined by management in our capacity as general partner or investor and, in the case of an investment in an unaffiliated investment partnership, are based on financial statements prepared by an unaffiliated general partner.

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Note 11 *Goodwill and Intangible Assets*

The following table presents the changes in the carrying value of goodwill and intangible assets for the nine months ended September 30, 2011:

(Dollars in thousands)			
Goodwill	**Capital Markets**	**Asset Management**	**Total**
Balance at December 31, 2010	**$ 120,298**	**$ 202,296**	**$ 322,594**
FAMCO earn-out payment	-	56	56
Balance at September 30, 2011	**$ 120,298**	**$ 202,352**	**$ 322,650**
Intangible assets			
Balance at December 31, 2010	**$ -**	**$ 59,580**	**$ 59,580**
Amortization of intangible assets	-	(6,207)	(6,207)
Balance at September 30, 2011	**$ -**	**$ 53,373**	**$ 53,373**

Note 12 *Short-Term Financing*

The following is a summary of short-term financing and the weighted average interest rate on borrowings as of September 30, 2011 and December 31, 2010:

	Outstanding Balance		**Weighted Average Interest Rate**	
(Dollars in thousands)	**September 30, 2011**	**December 31, 2010**	**September 30, 2011**	**December 31, 2010**
Bank lines (secured)	**$ 68,000**	$ 70,000	**1.25%**	1.31%
Commercial paper (secured)	**127,827**	123,589	**1.31%**	1.28%
Total short-term financing	**$ 195,827**	$ 193,589		

The Company has committed short-term bank line financing available on a secured basis and uncommitted short-term bank line financing available on both a secured and unsecured basis. The Company uses these credit facilities in the ordinary course of business to fund a portion of its daily operations and the amount borrowed under these credit facilities varies daily based on the Company s funding needs.

The Company s committed short-term bank line financing at September 30, 2011 consisted of a $250 million committed revolving credit facility with U.S. Bank, N.A., which was renewed in December 2010. Advances under this facility are secured by certain marketable securities. The facility includes a covenant that requires the Company s U.S. broker dealer subsidiary to maintain a minimum net capital of $150 million, and the unpaid principal amount of all advances under this facility will be due on December 30, 2011. The Company pays a nonrefundable commitment fee on the unused portion of the facility on a quarterly basis.

The Company s uncommitted secured lines at September 30, 2011 totaled $275 million with three banks and are dependent on having appropriate collateral, as determined by the bank agreement, to secure an advance under the line. The availability of the Company s uncommitted lines are subject to approval by the individual banks each time an advance is requested and may be denied. In addition, the Company has established arrangements to obtain financing by another broker dealer at the end of each business day related specifically to its convertible inventory.

The Company issues secured commercial paper to fund a portion of its securities inventory. The senior secured commercial paper notes (Series A CP Notes) are secured by the Company s securities inventory with maturities on the Series A CP Notes ranging from 28 days to 270 days from the date of issuance. The Series A CP Notes are interest bearing or sold at a discount to par with an interest rate based on LIBOR plus an applicable margin.

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Note 13 *Bank Syndicated Financing*

The following is a summary of bank syndicated financing and the weighted average interest rate on borrowings as of September 30, 2011 and December 31, 2010:

	Outstanding Balance		Weighted Average Interest Rate	
(Dollars in thousands)	**September 30, 2011**	**December 31, 2010**	**September 30, 2011**	**December 31, 2010**
Term loan	**$ 92,500**	$ 100,000	**3.05%**	5.00%
Revolving credit facility	**25,000**	25,000	**3.05%**	5.00%
Total bank syndicated financing	**$ 117,500**	$ 125,000		

On December 29, 2010, the Company entered into a three-year bank syndicated credit agreement (the Credit Agreement) comprised of a $100 million amortizing term loan and a $50 million revolving credit facility. SunTrust Bank is the administrative agent (Agent) for the lenders. Pursuant to the Credit Agreement, the term loan and revolving credit facility mature on December 29, 2013. The term loan is payable in equal quarterly installments in annual amounts as set forth below:

(Dollars in thousands)	
Remainder of 2011	$ 2,500
Due in 2012	25,000
Due in 2013	65,000
	$ 92,500

The interest rate for borrowing under the Credit Agreement is, at the option of the Company, equal to LIBOR or a base rate, plus an applicable margin, adjustable and payable quarterly. The base rate is defined as the highest of the Agent s prime lending rate, the Federal Funds Rate plus 0.50 percent or one-month LIBOR plus 1.00 percent. The applicable margin varies from 1.50 percent to 3.00 percent and is based on the Company s leverage ratio. The Company also pays a nonrefundable commitment fee of 0.50 percent on the unused portion of the revolving credit facility on a quarterly basis. In addition, the aggregate debt issuance costs will be recognized as additional interest expense over the three-year life under the effective yield interest expense method.

The Company s Credit Agreement is recorded at amortized cost. As of September 30, 2011, the carrying value of the Credit Agreement approximates fair value.

The Credit Agreement includes customary events of default, including failure to pay principal when due or failure to pay interest within three business days of when due, failure to comply with the covenants in the Credit Agreement and related documents, failure to pay or another event of default under other material indebtedness in an amount exceeding $5 million, bankruptcy or insolvency of the Company or any of its subsidiaries, a change in control of the Company or a failure of Piper Jaffray to extend, renew or refinance its existing $250 million committed revolving secured credit facility on substantially the same terms as the existing committed facility. If there is any event of default under the Credit Agreement, the Agent may declare the entire principal and any accrued interest on the loans under the Credit Agreement to be due and payable and exercise other customary remedies.

The Credit Agreement includes covenants that, among other things, limit the Company s leverage ratio, require maintenance of certain levels of cash and regulatory net capital, require the Company s asset management segment to achieve minimum earnings before interest, taxes, depreciation and amortization, and impose certain limitations on the Company s ability to make acquisitions and make payments on its capital stock. With respect to the net capital covenant, the Company s U.S. broker dealer subsidiary is required to maintain minimum net capital of $160 million. At September 30, 2011, the Company was in compliance with all covenants.

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Note 14 *Variable Rate Senior Notes*

On December 31, 2009, the Company issued unsecured variable rate senior notes (Notes) in the amount of $120 million. The initial holders of the Notes were certain entities advised by PIMCO. Interest was based on an annual rate equal to LIBOR plus 4.10 percent, adjustable and payable quarterly. The proceeds from the Notes were used to fund a portion of the ARI acquisition discussed further in Note 4 to these consolidated financial statements. The unpaid principal and interest on the Notes were repaid on December 30, 2010, from the proceeds of the Credit Agreement discussed above in Note 13 to these consolidated financial statements.

Note 15 *Legal Contingencies*

The Company has been named as a defendant in various legal actions, including complaints and litigation and arbitration claims, arising from its business activities. Such actions include claims related to securities brokerage and investment banking activities, and certain class actions that primarily allege violations of securities laws and seek unspecified damages, which could be substantial. Also, the Company is involved from time to time in investigations and proceedings by governmental agencies and self-regulatory organizations which could result in adverse judgments, settlement, penalties, fines or other relief.

The Company has established reserves for potential losses that are probable and reasonably estimable that may result from pending and potential legal actions, investigations and regulatory proceedings. In many cases, however, it is inherently difficult to determine whether any loss is probable or even possible or to estimate the amount or range of any potential loss, particularly where proceedings may be in relatively early stages or where plaintiffs are seeking substantial or indeterminate damages. Matters frequently need to be more developed before a loss or range of loss can reasonably be estimated. With respect to certain matters, the Company may be able to estimate probable losses or ranges of losses but does not believe, based on currently available information, that such losses will have a material effect on the Company s consolidated financial condition.

Given uncertainties regarding the timing, scope, volume and outcome of pending and potential legal actions, investigations and regulatory proceedings and other factors, the amounts of reserves and ranges of reasonably possible losses are difficult to determine and of necessity subject to future revision. Subject to the foregoing and except for the legal proceeding described below, management of the Company believes, based on currently available information, after consultation with outside legal counsel and taking into account its established reserves, that pending legal actions, investigations and regulatory proceedings will be resolved with no material adverse effect on the consolidated financial condition of the Company. However, if during any period a potential adverse contingency should become probable or resolved for an amount in excess of the established reserves, the results of operations in that period could be materially adversely affected. In addition, there can be no assurance that material losses will not be incurred from claims that have not yet been brought to the Company s attention or are not yet determined to be reasonably possible.

The Company is a defendant in one legal proceeding where management of the Company believes that a material loss is reasonably possible. The U.S. Department of Justice (DOJ), Antitrust Division, the SEC and various state attorneys general are conducting broad investigations of numerous firms, including the Company, for possible antitrust and securities violations in connection with the bidding or sale of guaranteed investment contracts and derivatives to municipal issuers from the early 1990s to date. These investigations commenced in November 2006. In addition, several class action complaints have been brought on behalf of a proposed class of government entities that purchased municipal derivatives. The complaints allege antitrust violations and civil fraud and are pending in a U.S. District Court under the multi-district litigation rules. No loss contingency has been reflected in the Company s consolidated financial statements as this contingency is neither probable nor reasonably estimable at this time. Further, an estimate of the loss, or range of loss that is reasonably possible, cannot be made at this time.

Note 16 *Restructuring*

During 2010, the Company restructured its European operations to focus European resources on two areas: the distribution of U.S. and Asia securities to European institutional investors and merger and acquisition advisory services. As a result of the restructuring, the Company exited the origination and distribution of European securities and incurred pre-tax restructuring-related expenses of $9.3 million in 2010. As of September 30, 2011, the majority of these expenses had been paid and the remaining restructuring-related liability associated with the Company s European operations was not material.

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Note 17 *Shareholders Equity*

Share Repurchase Program

In the third quarter of 2010, the Company s board of directors authorized the repurchase of up to $75.0 million in common shares through September 30, 2012. During the nine months ended September 30, 2011, the Company did not repurchase any shares of the Company s common stock related to this authorization. The Company has $57.4 million remaining under this authorization.

Issuance of Shares

During the nine months ended September 30, 2011, the Company issued 90,085 common shares out of treasury stock in fulfillment of $3.8 million in obligations under the Piper Jaffray Companies Retirement Plan and issued 1,155,411 common shares out of treasury stock as a result of vesting and exercise transactions under the Piper Jaffray Companies Amended and Restated 2003 Annual and Long-Term Incentive Plan.

Note 18 *Noncontrolling Interests*

The consolidated financial statements include the accounts of Piper Jaffray Companies, its wholly owned subsidiaries and other entities in which the Company has a controlling financial interest. Noncontrolling interests represent equity interests in consolidated entities that are not attributable, either directly or indirectly, to Piper Jaffray Companies. Noncontrolling interests include the minority equity holders proportionate share of the equity in a municipal hedge fund and private equity investment vehicles.

Ownership interests in entities held by parties other than the Company s common shareholders are presented as noncontrolling interests within shareholders equity, separate from the Company s own equity. Revenues, expenses and net income or loss are reported on the consolidated statements of operations on a consolidated basis, which includes amounts attributable to both the Company s common shareholders and noncontrolling interests. Net income or loss is then allocated between the Company and noncontrolling interests based upon their relative ownership interests. Net income applicable to noncontrolling interests is deducted from consolidated net income to determine net income applicable to the Company s common shareholders. There has been no other comprehensive income or loss attributed to noncontrolling interests for the nine months ended September 30, 2011.

The following table summarizes the changes in common shareholders equity attributable to the Company and equity attributable to noncontrolling interests for the nine months ended September 30, 2011:

(Dollars in thousands)	**Common Shareholders Equity**	**Noncontrolling Interests**	**Total Shareholders Equity**
Balance at December 31, 2010	**$ 813,312**	**$ 4,789**	**$ 818,101**
Net income	14,344	846	15,190
Amortization/issuance of restricted stock	27,528	-	27,528
Foreign currency translation adjustment	(56)	-	(56)
Reissuance of treasury shares	(16,426)	-	(16,426)
Shares reserved to meet deferred compensation obligations	437	-	437
Contributions	-	28,038	28,038
Distributions	-	(2,040)	(2,040)
Balance at September 30, 2011	**$ 839,139**	**$ 31,633**	**$ 870,772**

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Note 19 *Earnings Per Share*

The Company calculates earnings per share using the two-class method. Basic earnings per common share is computed by dividing net income/(loss) applicable to Piper Jaffray Companies common shareholders by the weighted average number of common shares outstanding for the period. Net income/(loss) applicable to Piper Jaffray Companies common shareholders represents net income/(loss) applicable to Piper Jaffray Companies reduced by the allocation of earnings to participating securities. Losses are not allocated to participating securities. All of the Company s unvested restricted shares are deemed to be participating securities as they are eligible to share in the profits (e.g., receive dividends) of the Company. Diluted earnings per common share is calculated by adjusting the weighted average outstanding shares to assume conversion of all potentially dilutive stock options. The computation of earnings per share is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	**2010**	**2011**	**2010**
(Amounts in thousands, except per share data)				
Net income/(loss) applicable to Piper Jaffray Companies	**$ (3,583)**	$ 7,054	**$ 14,344**	$ 14,942
Earnings allocated to participating securities	**-**	(1,639) (1)	**(2,696)** (1)	(3,271) (1)
Net income/(loss) applicable to Piper Jaffray Companies common shareholders (2)	**$ (3,583)**	$ 5,415	**$ 11,648**	$ 11,671
Shares for basic and diluted calculations:				
Average shares used in basic computation	**15,889**	15,035	**15,638**	15,588
Stock options	**-**	3	**17**	38
Restricted stock	**2,730**	- (1)	**-** (1)	- (1)
Average shares used in diluted computation	**18,619** (3)	15,038	**15,655**	15,626
Earnings per share:				
Basic	**$ (0.23)**	$ 0.36	**$ 0.74**	$ 0.75
Diluted	**$ (0.23)** (3)	$ 0.36	**$ 0.74**	$ 0.75

(1) *Participating securities were included in the calculation of diluted EPS using the two-class method, as this computation was more dilutive than the calculation using the treasury-stock method.*

(2) *Net income/(loss) applicable to Piper Jaffray Companies common shareholders for diluted and basic EPS may differ under the two-class method as a result of adding the effect of the assumed exercise of stock options to dilutive shares outstanding, which alters the ratio used to allocate earnings to Piper Jaffray Companies common shareholders and participating securities for purposes of calculating diluted and basic EPS.*

(3) *Earnings per diluted common share is calculated using the basic weighted average number of common shares outstanding for periods in which a loss is incurred.*

The anti-dilutive effects from stock options were immaterial for the periods ended September 30, 2011 and 2010.

Note 20 *Employee Benefit Plans*

The Company has various employee benefit plans including a tax-qualified retirement plan (the Retirement Plan), a post-retirement medical plan, and health and welfare plans. The Company terminated its non-qualified unfunded cash balance pension plan (the Non-Qualified Plan) in 2010 through lump-sum cash distributions to all participants. These lump-sum cash payments, totaling $10.4 million, were based on the December 31, 2009 actuarial valuation of the Non-Qualified Plan and were distributed on March 15, 2010. For the nine month period ended September 30, 2010, the Company recognized a settlement expense of $0.2 million in compensation and benefits expense on the consolidated statements of operations related to the settlement of all Non-Qualified Plan liabilities.

Note 21 *Stock-Based Compensation*

The Company maintains two stock-based compensation plans, the Piper Jaffray Companies Amended and Restated 2003 Annual and Long-Term Incentive Plan (the Incentive Plan) and the 2010 Employment Inducement Award Plan (the Inducement Plan). The Company s equity awards are recognized on the consolidated statements of operations at grant date fair value over the service period of the award, net of estimated forfeitures.

The following table provides a summary of the Company s outstanding equity awards as of September 30, 2011:

Incentive Plan	
Restricted Stock	
Annual grants	1,623,437
Sign-on grants	503,445
Retention grants	90,060
Performance grants	307,820
	2,524,762
Inducement Plan	
Restricted Stock	116,610
Total restricted stock related to compensation	2,641,372
ARI deal consideration (1)	661,380
Total restricted stock outstanding	3,302,752
Incentive Plan	
Stock options outstanding	512,322

(1) The Company issued restricted stock as part of deal consideration for ARI. See Note 4 for further discussion.

Incentive Plan

The Incentive Plan permits the grant of equity awards, including restricted stock and non-qualified stock options, to the Company s employees and directors for up to 7.0 million shares of common stock. The Company believes that such awards help align the interests of employees and directors with those of shareholders and serve as an employee retention tool. The plan provides for accelerated vesting of awards if there is a severance event, a change in control of the Company (as defined in the plan), in the event of a participant s death, and at the discretion of the compensation committee of the Company s board of directors.

Restricted Stock Awards

Restricted stock grants are valued at the market price of the Company s common stock on the date of grant and are amortized over the related requisite service period. The Company grants shares of restricted stock to current employees as part of year-end compensation (Annual Grants) and as a retention tool. Employees may receive restricted stock upon initial hiring or as a retention award (Sign-on Grants). The Company has also granted incremental restricted stock awards with service conditions to key employees (Retention Grants) and restricted stock with performance conditions to members of senior management (Performance Grants).

The Company s Annual Grants are made each year in February. Prior to 2011, Annual Grants had three-year cliff vesting periods. Beginning in 2011, Annual Grants vest ratably over three years in equal installments. The Annual Grants provide for continued vesting after termination of employment, so long as the employee does not violate certain post-termination restrictions set forth in the award agreement or any agreements entered into upon termination. The vesting period refers to the period in which post-termination restrictions apply. The Company determined the service inception date precedes the grant date for the Annual Grants, and that the post-termination restrictions do not meet the criteria for an in-substance service condition, as defined by FASB Accounting Standards Codification Topic 718, Compensation Stock Compensation (ASC

718). Accordingly, restricted stock granted as part of the Annual Grants is expensed in the one-year period in which those awards are deemed to be earned, which is generally the calendar year preceding the February grant date. For example, the Company recognized compensation expense during fiscal 2010 for our

February 2011 Annual Grants. If an equity award related to the Annual Grants is forfeited as a result of violating the post-termination restrictions, the lower of the fair value of the award at grant date or the fair value of the award at the date of forfeiture is recorded within the consolidated statements of operations as other income. The Company recorded $0.2 million and $0.7 million of forfeitures through other income for the three months ended September 30, 2011 and 2010, respectively, and $3.4 million and $4.5 million for the nine months ended September 30, 2011 and 2010, respectively.

Sign-on Grants are used as a recruiting tool for new employees and are issued to current employees as a retention tool. The majority of these awards have three-year cliff vesting terms and employees must fulfill service requirements in exchange for rights to the awards. Compensation expense is amortized on a straight-line basis from the date of grant over the requisite service period. Employees forfeit unvested shares upon termination of employment and a reversal of compensation expense is recorded.

Retention Grants are subject to ratable vesting based upon a five-year service requirement and are amortized as compensation expense on a straight-line basis from the grant date over the requisite service period. Employees forfeit unvested retention shares upon termination of employment and a reversal of compensation expense is recorded.

Performance-based restricted stock awards granted in 2008 and 2009 cliff vest upon meeting a specific performance-based metric prior to May 2013. Performance Grants are amortized on a straight-line basis over the period the Company expects the performance target to be met. The performance condition must be met for the awards to vest and total compensation cost will be recognized only if the performance condition is satisfied. The probability that the performance conditions will be achieved and that the awards will vest is reevaluated each reporting period with changes in actual or estimated outcomes accounted for using a cumulative effect adjustment to compensation expense. In the third quarter of 2010, the Company deemed it improbable that the performance condition related to the Performance Grants would be met. As a result, the Company recorded a $6.6 million cumulative effect compensation expense reversal in the third quarter of 2010.

Annually, the Company grants stock to its non-employee directors. The stock-based compensation paid to non-employee directors is fully expensed on the grant date and included within outside services expense on the consolidated statements of operations.

Stock Options

The Company previously granted options to purchase Piper Jaffray Companies common stock to employees and non-employee directors in fiscal years 2004 through 2008. Employee and director options were expensed by the Company on a straight-line basis over the required service period, based on the estimated fair value of the award on the date of grant using a Black-Scholes option-pricing model. As described above pertaining to the Company s Annual Grants of restricted shares, stock options granted to employees were expensed in the calendar year preceding the annual February grant date. For example, the Company recognized compensation expense during fiscal 2007 for our annual February 2008 option grant. The maximum term of the stock options granted to employees and directors is ten years.

The Company did not grant stock options during the nine months ended September 30, 2011 and 2010, respectively.

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Inducement Plan

In 2010, the Company established the Inducement Plan in conjunction with the acquisition of ARI. The Company granted $7.0 million in restricted stock (158,801 shares) under the Inducement Plan to ARI employees upon closing of the transaction. These shares vest ratably over five years in equal annual installments ending on March 1, 2015. Inducement Plan awards are amortized as compensation expense on a straight-line basis over the vesting period. Employees forfeit unvested Inducement Plan shares upon termination of employment and a reversal of compensation expense is recorded.

Stock-Based Compensation

The Company recorded total compensation expense of $5.5 million and $0.8 million for the three months ended September 30, 2011 and 2010, respectively, and $23.9 million and $20.0 million for the nine months ended September 30, 2011 and 2010, respectively, related to employee restricted stock awards. The tax benefit related to stock-based compensation costs totaled $2.1 million and $0.3 million for the three months ended September 30, 2011 and 2010, respectively, and $9.3 million and $7.9 million for the nine months ended September 30, 2011 and 2010, respectively.

The following table summarizes the changes in the Company s unvested restricted stock (including the unvested restricted stock issued as part of the deal consideration for ARI) under the Incentive Plan and Inducement Plan for the nine months ended September 30, 2011:

	Unvested Restricted Stock	Weighted Average Grant Date Fair Value
December 31, 2010	**4,523,184**	**$ 39.84**
Granted	663,866	40.87
Vested	(1,648,140)	39.81
Cancelled	(236,158)	39.08
September 30, 2011	**3,302,752**	**$ 37.72**

As of September 30, 2011, there was $12.7 million of total unrecognized compensation cost related to restricted stock expected to be recognized over a weighted average period of 2.27 years.

The following table summarizes the changes in the Company s outstanding stock options for the nine months ended September 30, 2011:

	Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
December 31, 2010	**515,492**	**$ 44.64**	**4.9**	**$ 166,406**
Granted	-	-		
Exercised	(1,023)	39.62		
Cancelled	(2,147)	40.49		
September 30, 2011	**512,322**	**$ 44.67**	**4.1**	**$ -**
Options exercisable at September 30, 2011	**512,322**	**$ 44.67**	**4.1**	**$ -**

As of September 30, 2011, there was no unrecognized compensation cost related to stock options expected to be recognized over future years.

Cash received from option exercises for the nine months ended September 30, 2011 and 2010 was $0.1 million. The tax benefit realized for the tax deductions from option exercises was immaterial for the nine months ended September 30, 2011 and 2010, respectively.

Note 22 *Segment Reporting*

On March 1, 2010, the Company completed the purchase of ARI, which expanded the Company s asset management business and resulted in a change to its reportable business segments in the second quarter of 2010. In connection with this change, the Company has reclassified prior period segment results to conform to the current period presentation.

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Basis for Presentation

The Company structures its segments primarily based upon the nature of the financial products and services provided to customers and the Company s management organization. It evaluates performance and allocates resources based on segment pre-tax operating income or loss and segment pre-tax operating margin. Revenues and expenses directly associated with each respective segment are included in determining their operating results. Other revenues and expenses that are not directly attributable to a particular segment are allocated based upon the Company s allocation methodologies, including each segment s respective net revenues, use of shared resources, headcount or other relevant measures. The financial management of assets is performed on an enterprise-wide basis. As such, assets are not assigned to the business segments.

Reportable segment financial results are as follows:

	0000000000000	0000000000000	0000000000000	0000000000000
	Three Months Ended September 30,		**Nine Months Ended September 30,**	
(Dollars in thousands)	**2011**	**2010**	**2011**	**2010**
Capital Markets				
Investment banking				
Financing				
Equities	**$ 6,923**	$ 19,839	**$ 62,590**	$ 71,603
Debt	**11,106**	16,486	**39,355**	46,022
Advisory services	**27,294**	20,595	**58,852**	55,767
Total investment banking	**45,323**	56,920	**160,797**	173,392
Institutional sales and trading				
Equities	**23,482**	24,292	**70,562**	78,720
Fixed income	**14,496**	20,159	**66,079**	57,268
Total institutional sales and trading	**37,978**	44,451	**136,641**	135,988
Other income/(loss)	**1,157**	(1,956)	**9,125**	2,452
Net revenues	**84,458**	99,415	**306,563**	311,832
Operating expenses (1)	**84,828**	90,424	**287,487**	286,723
Segment pre-tax operating income/(loss)	**$ (370)**	$ 8,991	**$ 19,076**	$ 25,109
Segment pre-tax operating margin	**(0.4)%**	9.0%	**6.2%**	8.1%
Asset Management				
Management and performance fees				
Management fees	**$ 15,205**	$ 16,117	**$ 51,028**	$ 40,662
Performance fees	**-**	695	**1,746**	1,177
Total management and performance fees	**15,205**	16,812	**52,774**	41,839
Other income/(loss)	**(1,487)**	236	**(432)**	31
Net revenues	**13,718**	17,048	**52,342**	41,870
Operating expenses (1)	**13,048**	12,749	**42,450**	32,857
Segment pre-tax operating income	**$ 670**	$ 4,299	**$ 9,892**	$ 9,013

Segment pre-tax operating margin		**4.9%**		25.2%		**18.9%**		21.5%
Total								
Net revenues	**$**	**98,176**	$	116,463	**$**	**358,905**	$	353,702
Operating expenses (1)		**97,876**		103,173		**329,937**		319,580
Total segment pre-tax operating income	**$**	**300**	$	13,290	**$**	**28,968**	$	34,122
Pre-tax operating margin		**0.3%**		11.4%		**8.1%**		9.6%

(1) Operating expenses include intangible asset amortization as set forth in the table below:

		0000000000000		**0000000000000**		**0000000000000**		**0000000000000**
		Three Months Ended September 30,				**Nine Months Ended September 30,**		
(Dollars in thousands)		**2011**		**2010**		**2011**		**2010**
Capital Markets	**$**	**-**	$	-	**$**	**-**	$	-
Asset Management		**2,069**		2,183		**6,207**		5,363