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Fortress Investment Group LLC
Form 10-K
February 25, 2016
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

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

For the fiscal year ended December 31, 2015

or

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

For the transition period from _____ to _____

Commission File Number: 001-33294

Fortress Investment Group LLC

(Exact name of registrant as specified in its charter)

Delaware

20-5837959

(State or other jurisdiction of incorporation or organization)

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

1345 Avenue of the Americas, New York, NY

10105

(Address of principal executive offices)

(Zip Code)

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

Securities registered pursuant to Section 12 (b) of the Act:

Title of each class:

Name of exchange on which registered:

Class A shares

New York Stock Exchange (NYSE)

Securities registered pursuant to Section 12 (g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this form 10-K.

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

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

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

The aggregate market value of the Class A shares held by non-affiliates as of June 30, 2015 (computed based on the closing price on such date as reported on the NYSE) was \$1.5 billion.

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

Class A shares: 221,183,518 outstanding as of February 19, 2016.

Class B shares: 169,514,478 outstanding as of February 19, 2016.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant’s definitive proxy statement for the registrant’s 2016 annual meeting, to be filed within 120 days after the close of the registrant’s fiscal year, are incorporated by reference into Part III of this Annual Report on Form 10-K.

FORTRESS INVESTMENT GROUP LLC
FORM 10-K
INDEX

	PAGE
	<u>PART I</u>
<u>Item 1.</u>	<u>Business</u> <u>1</u>
<u>Item 1A.</u>	<u>Risk Factors</u> <u>13</u>
<u>Item 1B.</u>	<u>Unresolved Staff Comments</u> <u>45</u>
<u>Item 2.</u>	<u>Properties</u> <u>45</u>
<u>Item 3.</u>	<u>Legal Proceedings</u> <u>45</u>
<u>Item 4.</u>	<u>Mine Safety Disclosures</u> <u>45</u>
	<u>PART II</u>
<u>Item 5.</u>	<u>Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u> <u>46</u>
<u>Item 6.</u>	<u>Selected Financial Data</u> <u>47</u>
<u>Item 7.</u>	<u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> <u>49</u>
	<u>Overview and Understanding the Asset Management Business</u> <u>49</u>
	<u>Market Considerations</u> <u>55</u>
	<u>Assets Under Management</u> <u>58</u>
	<u>Performance of Our Funds</u> <u>61</u>
	<u>Results of Operations</u> <u>65</u>
	<u>Liquidity and Capital Resources</u> <u>85</u>
	<u>Critical Accounting Policies</u> <u>94</u>
	<u>Contractual Obligations</u> <u>101</u>
<u>Item 7A.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u> <u>102</u>
<u>Item 8.</u>	<u>Financial Statements and Supplementary Data</u> <u>106</u>
	<u>Report of Independent Registered Public Accounting Firm</u> <u>107</u>
	<u>Report of Independent Registered Public Accounting Firm or Internal Control over Financial Reporting</u> <u>108</u>
	<u>Consolidated Balance Sheets</u> as of December 31, 2015 and December 31, 2014 <u>109</u>
	<u>Consolidated Statements of Operations</u> for the years ended December 31, 2015, 2014 and 2013 <u>110</u>
	<u>Consolidated Statements of Comprehensive Income</u> for the years ended December 31, 2015, 2014 and 2013 <u>111</u>
	<u>Consolidated Statements of Changes in Equity</u> for the years ended December 31, 2015, 2014 and 2013 <u>112</u>
	<u>Consolidated Statements of Cash Flows</u> for the years ended December 31, 2015, 2014 and 2013 <u>115</u>
	<u>Notes to Consolidated Financial Statements</u> <u>117</u>
	<u>Note 1</u> <u>Organization and Basis of Presentation</u> <u>117</u>
	<u>Note 2</u> <u>Summary of Significant Accounting Policies</u> <u>122</u>
	<u>Note 3</u> <u>Management Agreements and Fortress Funds</u> <u>126</u>
	<u>Note 4</u> <u>Investments and Fair Value</u> <u>138</u>
	<u>Note 5</u> <u>Debt Obligations</u> <u>150</u>
	<u>Note 6</u> <u>Income Taxes and Tax Related Payments</u> <u>152</u>
	<u>Note 7</u> <u>Related Party Transactions and Interests in Consolidated Subsidiaries</u> <u>157</u>
	<u>Note 8</u> <u>Equity-Based and Other Compensation</u> <u>161</u>
	<u>Note 9</u> <u>Earnings Per Share and Distributions</u> <u>165</u>
	<u>Note 10</u> <u>Commitments and Contingencies</u> <u>170</u>
	<u>Note 11</u> <u>Segment Reporting</u> <u>172</u>

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<u>Note 12</u>	<u>Subsequent Events</u>	<u>179</u>
<u>Note 13</u>	<u>Quarterly Financial Information</u> (Unaudited)	<u>179</u>
<u>Item 9.</u>	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>180</u>
<u>Item 9A.</u>	<u>Controls and Procedures</u>	<u>180</u>
<u>Item 9B.</u>	<u>Other Information</u>	<u>181</u>

PART III

<u>Item 10.</u>	<u>Directors, Executive Officers and Corporate Governance</u>	<u>182</u>
<u>Item 11.</u>	<u>Executive Compensation</u>	<u>182</u>
<u>Item 12.</u>	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>182</u>
<u>Item 13.</u>	<u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>183</u>
<u>Item 14.</u>	<u>Principal Accounting Fees and Services</u>	<u>183</u>
<u>PART IV</u>		
<u>Item 15.</u>	<u>Exhibits, Financial Statement Schedules</u>	<u>184</u>
	<u>Signatures</u>	<u>187</u>

Set forth below is information about certain terms used in this Annual Report on Form 10-K:

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

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

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

Our calculation of AUM may differ from the calculations of other asset managers and, as a result, this measure may not be comparable to similar measures presented by other asset managers. Our definition of AUM is not based on any definition of assets under management contained in our operating agreement or in any of our Fortress Fund management agreements. Finally, our calculation of AUM differs from the manner in which our affiliates registered with the United States Securities and Exchange Commission report “Regulatory Assets Under Management” on Form ADV and Form PF in various ways. Significantly, Regulatory Assets Under Management, unlike Management Fee Paying Assets Under Management, is not reduced by liabilities or indebtedness associated with assets under management and it includes assets under management and uncalled capital for which Fortress receives no compensation.

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

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

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

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

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

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

“principals” or “Principals” refers to Peter Briger, Wesley Edens and Randal Nardone, collectively, as well as Michael Novogratz until his retirement in January 2016. The principals control the public company through their ownership of the public company’s Class B shares (together with, from time to time, a former senior employee who owned securities convertible into Class B shares). The Class B shares and the Class A shares are each entitled to one vote per share, and the number of Class B shares outstanding represents a majority of the aggregate number of Class B shares and Class A shares outstanding. The Class B shares do not represent an economic interest in the public company and therefore are not entitled to any dividends. The principals own their economic interest in the public company primarily through their direct ownership of FOGUs.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some of the statements under Part I, Item 1, “Business,” Part I, Item 1A, “Risk Factors,” Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” Part II, Item 7A, “Quantitative and Qualitative Disclosures About Market Risk” and elsewhere in this Annual Report on Form 10-K may contain forward-looking statements which reflect our current views with respect to, among other things, future events and financial performance. Readers can identify these forward-looking statements by the use of forward-looking words such as “outlook,” “believes,” “expects,” “potential,” “continues,” “may,” “will,” “should,” “seeks,” “approximately,” “predicts,” “plans,” “estimates,” “anticipates” or the negative version of those words or other comparable words. Any forward-looking statements contained in this report are based upon the historical performance of us and our subsidiaries and on our current plans, estimates and expectations. The inclusion of this forward-looking information should not be regarded as a representation by us or any other person that the future plans, estimates or expectations contemplated by us will be achieved. Such forward-looking statements are subject to various risks and uncertainties and assumptions relating to our operations, financial results, financial condition, business prospects, growth strategy and liquidity. If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, our actual results may vary materially from those indicated in these statements. Accordingly, you should not place undue reliance on any forward-looking statements. These factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included in this report. We do not undertake any obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.

SPECIAL NOTE REGARDING EXHIBITS

In reviewing the agreements included as exhibits to this Annual Report on Form 10 K, please remember they are included to provide you with information regarding their terms and are not intended to provide any other factual or disclosure information about the Company or the other parties to the agreements. The agreements contain representations and warranties by each of the parties to the applicable agreement. These representations and warranties have been made solely for the benefit of the other parties to the applicable agreement and:

- should not in all instances be treated as categorical statements of fact, but rather as a way of allocating the risk to one of the parties if those statements prove to be inaccurate;
- have been qualified by disclosures that were made to the other party in connection with the negotiation of the applicable agreement, which disclosures are not necessarily reflected in the agreement;
- may apply standards of materiality in a way that is different from what may be viewed as material to you or other investors; and
- were made only as of the date of the applicable agreement or such other date or dates as may be specified in the agreement and are subject to more recent developments.

Accordingly, these representations and warranties may not describe the actual state of affairs as of the date they were made or at any other time. Additional information about the Company may be found elsewhere in this Annual Report on Form 10-K and the Company’s other public filings, which are available without charge through the SEC’s website at <http://www.sec.gov>. See “Business — Where Readers Can Find Additional Information.”

The Company acknowledges that, notwithstanding the inclusion of the foregoing cautionary statements, it is responsible for considering whether additional specific disclosures of material information regarding material contractual provisions are required to make the statements in this report not misleading.

PART I

Item 1. Business.

Fortress Investment Group LLC (NYSE listed under the symbol "FIG") is a leading, highly diversified global investment management firm with approximately \$70.5 billion in AUM as of December 31, 2015. Fortress applies its deep experience and specialized expertise across a range of investment strategies - private equity, credit, liquid markets and traditional fixed income - on behalf of our over 1,700 institutional clients and private investors worldwide. We earn management fees based on the amount of capital we manage, incentive income based on the performance of our alternative investment funds, and investment income (loss) from our investments in our funds.

Fortress was founded in 1998 as an asset-based investment management firm with a fundamental philosophy premised on alignment of interests with the investors in our funds. Our managed funds primarily employ absolute return strategies — we strive to have positive returns regardless of the performance of the markets. Investment performance is our cornerstone — as an investment manager, we earn more if our investors earn more. In keeping with our fundamental philosophy, Fortress invests capital in each of its alternative investment businesses. As of December 31, 2015, Fortress's investments in and commitments to our funds were \$1.2 billion, consisting of the net asset value of Fortress's investments in the Fortress Funds of \$1.1 billion, and unfunded commitments to private equity funds and credit PE funds of \$0.1 billion.

As of December 31, 2015, we had 1,172 asset management employees, including approximately 285 investment professionals, at our headquarters in New York and our affiliate offices around the globe. Additionally, we had 1,868 employees at the senior living properties that we manage on behalf of New Senior Investment Group Inc. ("New Senior") and a third party (whose compensation expense is reimbursed to us by the owners of the facilities).

We plan to grow our fee paying assets under management and will continue to seek to generate superior risk-adjusted investment returns in our funds over the long term. We are guided by the following key objectives and values:

- introducing new investment products, while remaining focused on, and continuing to grow, our existing lines of business;
- maintaining our disciplined investment process and intensive asset management; and
- adhering to the highest standards of professionalism and integrity.

Recent Developments

In February 2016, we announced the commencement of a modified "Dutch auction" self-tender offer to repurchase up to \$100.0 million in cash of our Class A shares, at a price per share within the range of \$4.25 to \$4.75, less applicable withholding taxes and without interest.

Fortress's board of directors declared a base quarterly dividend of \$0.08 per share for the fourth quarter of 2015.

In the fourth quarter of 2015, we closed the Fortress Macro Funds and related managed accounts. Michael Novogratz, a principal, officer and director of Fortress retired effective January 2016. In November 2015, we purchased from Mr. Novogratz 56.8 million Fortress Operating Group units and corresponding Class B shares at \$4.50 per share, or an aggregate purchase price of \$255.7 million. In connection with this purchase, we paid \$100.0 million of cash in November 2015 and issued a \$155.7 million promissory note, of which one-half of the principal amount matures in November 2016 and the remainder in November 2017.

In January 2016, we entered into a new \$275.0 million senior unsecured revolving credit facility with a \$15.0 million letter of credit subfacility and repaid our existing \$150.0 million senior secured revolving credit facility. After giving effect to the initial extensions of credit thereunder of \$75.0 million, and a subsequent borrowing of \$100.0 million in February 2016, approximately \$97.3 million was available to be drawn. The new revolving credit facility matures in

January 2021.

During 2015, we raised \$9.0 billion of new third-party capital and launched three new funds. As of December 31, 2015, we had \$7.5 billion of capital commitments from investors to our funds that will be included in AUM if called, of which \$4.6 billion is in newer vintage funds and is available for general investment purposes.

Subsequent to December 31, 2015, we paid \$66.9 million to Fund III representing prior net incentive income distributions received (\$45.1 million net of employee amounts). Following such payment, no remaining clawback exists for Fund III.

Key Performance Indicators

As mentioned above, we earn management fees, incentive income, and investment income (loss). From these earnings we pay compensation and other expenses, as well as taxes, to arrive at our net operating performance.

1

Net Income and Distributable Earnings

Our net income reflects our operating performance pursuant to generally accepted accounting principles (“GAAP”). We also use pre-tax distributable earnings, which is a non-GAAP measure, as a measure of our operating performance and to report segment results. For more information on these performance measures, please refer to Part II, Item 8 “Financial Statements and Supplementary Data.” Pre-tax distributable earnings is specifically addressed in “Note 11 — Segment Reporting” within those financial statements.

Assets Under Management

Our management fees are typically earned as a percentage of the amount of capital we manage, which is referred to as management fee paying assets under management, or AUM. For more information on our AUM, please refer to Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Assets Under Management.” For more information on our management fee rates, please refer to Part II, Item 8 “Financial Statements and Supplementary Data — Note 3 — Management Agreements and Fortress Funds.”

Fund Performance

Our incentive income is typically earned as a percentage of the profits of our alternative investment funds. In certain cases, we earn incentive income only if a fund’s investments meet specified performance thresholds. We therefore monitor our funds’ proximity to such performance thresholds. For more information on our funds’ performance, please refer to Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Performance of our Funds.” For more information on our funds’ incentive income terms and their proximity to their various performance thresholds, please refer to Part II, Item 8 “Financial Statements and Supplementary Data — Note 3 — Management Agreements and Fortress Funds.” For more information on embedded incentive income, which has not yet been distributed to us by our funds, and the portion thereof that has not yet been recognized in distributable earnings, please refer to Part II, Item 8 “Financial Statements and Supplementary Data — Note 11 — Segment Reporting — Embedded Incentive Income.”

Investment Performance

The investment income (loss) from our investments in the Fortress Funds is recorded currently (i.e., whether or not realized) in net income (loss), generally based on the net asset values of the funds in which we have invested. For segment reporting purposes, investment income (loss) is included in the segment that the investment relates to and is recorded only when income (loss) from a fund investment becomes realized or realizable, as applicable. Therefore, for segment reporting purposes, investment income (loss) does not reflect unrealized gains or losses embedded in certain of our investments. For more information on the investment income (loss) included in net income (loss), please refer to Part II, Item 8 “Financial Statements and Supplementary Data — Note 4 — Investments and Fair Value.” For more information on the unrealized gains (losses) currently embedded in our investments in the Fortress Funds for segment reporting purposes, please refer to Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Segment Analysis — Embedded Gains/Losses.”

Our Current Businesses

Our current offering of alternative investment products includes private equity funds and permanent capital vehicles, credit funds and liquid hedge funds. In addition, we offer traditional investment products. Private equity funds generally require fund investors to commit capital over a period of time, do not allow redemptions of capital and make long term, relatively illiquid investments. Hedge funds allow periodic contributions and redemptions of capital by investors and make relatively shorter-term, more liquid investments. Our credit funds share certain of the characteristics of both private equity and hedge funds. The permanent capital vehicles business consists of publicly

traded companies and a senior living property management business. See Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations — Understanding the Asset Management Business." We refer to these investment products, collectively, as the Fortress Funds. As of December 31, 2015, we managed the following businesses:

Private Equity — a business that manages approximately \$15.8 billion of AUM comprised of two business segments: (i) general buyout and sector-specific funds focused on control-oriented investments in cash flow generating assets and asset-based businesses in North America and Western Europe; and (ii) permanent capital vehicles, which includes publicly traded companies that are externally managed by Fortress pursuant to management agreements and a senior living property management business. The publicly traded companies invest in a wide variety of real estate related assets, including securities, loans, real estate properties and mortgage servicing related assets, media assets, senior living properties and transportation and infrastructure assets. All of the capital of Worldwide Transportation and Infrastructure Investors ("WWTAI"), formerly a private fund managed