Cowen Group, Inc.
Form 10-Q
May 09, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2008

or

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

For the transition period from to

Commission File Number: 000-52048

Cowen Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**84-1702964** (I.R.S. Employer Identification No.)
1221 Avenue of the Americas **New York, New York** (Address of principal executive offices)	**10020** (Zip Code)

(646) 562-1000
(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. ý Yes o 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 definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

As of May 8, 2008, there were 14,384,214 shares of the registrant's common stock outstanding.

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Special Note Regarding Forward-Looking Statements

We have made statements in this Quarterly Report on Form 10-Q in "Management's Discussion and Analysis of Financial Condition and Results of Operations" that are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. In some cases, you can identify these statements by forward-looking terms such as "may," "might," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "potential," "intend" or "continue," the negative of these terms and other comparable terminology. These forward-looking statements, which are subject to risks, uncertainties and assumptions about us, may include projections of our future financial performance, which in some cases may be based on our growth strategies and anticipated trends in our business. These statements are only predictions based on our current expectations and projections about future events. There are important factors that could cause our actual results, level of activity, performance or achievements to differ materially from those expressed or implied by the forward-looking statements. In particular, you should consider the risks contained in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2007.

Although we believe the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, level of activity, performance or achievements. Moreover, neither we nor any other person assumes responsibility for the accuracy or completeness of any of these forward-looking statements. You should not rely upon forward-looking statements as predictions of future events. We are under no duty to update any of these forward-looking statements after the date of this filing to conform our prior statements to actual results or revised expectations.

Unaudited Condensed Consolidated Financial Statements are presented for the three months ended March 31, 2008 and 2007. The Consolidated Financial Statements as of December 31, 2007 were audited.

PART I. FINANCIAL INFORMATION

Item 1. Unaudited Condensed Consolidated Financial Statements

Cowen Group, Inc.

Condensed Consolidated Statements of Financial Condition

(in thousands, except share and per share data)

(unaudited)

	March 31, 2008	December 31, 2007
Assets		
Cash and cash equivalents	$ 91,903	$ 139,879
Restricted cash pursuant to escrow agreement	23,401	23,515
Securities owned, at fair value	24,494	25,613
Receivable from brokers, dealers and clearing brokers	32,633	48,776
Corporate finance and syndicate receivables	7,556	12,956
Due from related parties	5,471	2,708
Exchange memberships, at cost (fair value of $808 and $961 at March 31, 2008 and December 31, 2007, respectively)	486	486
Furniture, fixtures, equipment and leasehold improvements (net of accumulated depreciation and amortization of $9,802 and $9,303 at March 31, 2008 and December 31, 2007, respectively)	11,169	11,414
Goodwill	50,000	50,000
Other assets	25,602	33,691
Total assets	$ 272,715	$ 349,038
Liabilities, Minority Interest and Stockholders' Equity		
Liabilities		
Bank overdrafts	$ 1,318	$ 1,719
Securities sold, not yet purchased, at fair value	12,744	25,639
Payable to brokers, dealers and clearing brokers	790	373
Employee compensation and benefits payable	12,784	73,077
Legal reserves and legal expenses payable (see Note 10, Commitments, Contingencies and Guarantees)	25,850	25,464
Accounts payable, accrued expenses and other liabilities	15,657	14,111
Total liabilities	69,143	140,383
Minority interest	121	
Stockholders' equity		
Preferred stock, par value $0.01 per share; 10,000,000 shares authorized, no shares issued and outstanding		
Common stock, par value $0.01 per share; 100,000,000 shares authorized, 14,429,232 and 14,641,776 shares issued, and 14,429,232 and 14,488,759 shares outstanding at March 31, 2008 and December 31, 2007, respectively (including 3,207,232 and 2,999,031 restricted shares, respectively)	110	115
Additional paid-in capital	211,201	217,102
Accumulated deficit	(7,908)	(8,562)
Accumulated other comprehensive income	48	
Less: common stock held in treasury, at cost: 153,017 shares at December 31, 2007		

	March 31, 2008	December 31, 2007
Total stockholders' equity	203,451	208,655
Total liabilities, minority interest and stockholders' equity	$ 272,715	$ 349,038

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Cowen Group, Inc.

Condensed Consolidated Statements of Operations

(in thousands, except per share data)

(unaudited)

	Three Months Ended March 31,	
	2008	**2007**
Revenues		
Investment banking	$ 13,862	$ 25,363
Brokerage	38,083	45,211
Interest and dividend income	1,223	2,137
Other	1,822	830
Total revenues	54,990	73,541
Expenses		
Employee compensation and benefits	28,809	45,167
Floor brokerage and trade execution	2,440	3,454
Service fees	4,209	3,503
Communications	3,649	4,197
Occupancy and equipment	4,189	4,277
Marketing and business development	3,626	3,215
Depreciation and amortization	638	766
Interest	43	141
Other	5,122	6,197
Total expenses	52,725	70,917
Operating income	2,265	2,624
Gain on exchange memberships		1,775
Income before income taxes	2,265	4,399
Provision for income taxes	1,611	1,928
Net income	$ 654	$ 2,471
Weighted average common shares outstanding:		
Basic	11,253	12,910
Diluted	11,895	13,417
Earnings per share:		
Basic	$ 0.06	$ 0.19
Diluted	$ 0.05	$ 0.18

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Cowen Group, Inc.

Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
Cash flows from operating activities		
Net income	$ 654	$ 2,471
Adjustments to reconcile net income to net cash used in operating activities:		
Share-based compensation	(1,726)	4,529
Depreciation and amortization	638	766
Deferred income taxes	1,279	(1,789)
(Increase) decrease in operating assets:		
Restricted cash pursuant to escrow agreement	114	762
Securities owned, at fair value	1,119	98,472
Receivable from brokers, dealers and clearing brokers	16,143	53,606
Corporate finance and syndicate receivables	5,400	6,704
Exchange memberships		325
Due from related parties	(2,763)	1,072
Other assets	6,991	(969)
Increase (decrease) in operating liabilities:		
Bank overdrafts	(401)	121
Securities sold, not yet purchased, at fair value	(12,895)	(122,980)
Payable to brokers, dealers and clearing brokers	417	(27,128)
Employee compensation and benefits payable	(60,293)	(91,673)
Legal reserves and legal expenses payable	386	(369)
Accounts payable, accrued expenses and other liabilities	1,415	281
Net cash used in operating activities	(43,522)	(75,799)
Cash flows from investing activities		
Purchase of fixed assets	(393)	(202)
Net cash used in investing activities	(393)	(202)
Cash flows from financing activities		
Share repurchases	(4,182)	
Contributions from minority interest holders	121	
Net cash used in financing activities	(4,061)	
Net decrease in cash and cash equivalents	(47,976)	(76,001)
Cash and Cash Equivalents		
Beginning of period	139,879	185,042
End of period	$ 91,903	$ 109,041
Supplemental disclosure of cash flow information		
Cash paid during the period for:		
Interest	$ 42	$ 286

	Three Months Ended March 31,	
Income taxes	$ 34	$ 3,020

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements

1. Organization and Basis of Presentation

Cowen Group, Inc. (together with its subsidiaries, the "Company") was incorporated in Delaware on February 15, 2006 with the issuance of 100 shares of common stock with a par value of $0.01 per share. The Company completed an initial public offering ("IPO") of its common stock on July 12, 2006. Prior to July 12, 2006, the Company was a wholly-owned subsidiary of SG Americas Securities Holdings, Inc. ("SGASH"). On that date, SGASH was a wholly-owned subsidiary of SG Americas, Inc. ("SGAI"), which in turn was a wholly-owned subsidiary of Société Générale ("SG"). The Company is operated and managed on an integrated basis as a single operating segment and primarily provides research, institutional brokerage and investment banking services to its clients. Certain material subsidiaries of the Company and other entities in which the Company has a controlling financial interest are discussed below.

Cowen and Company, LLC ("Cowen"), a Delaware single member limited liability company, is the United States ("U.S.") broker-dealer subsidiary of the Company. Cowen is a full-service investment banking and securities brokerage firm focused on the emerging growth sectors of healthcare, technology, media and telecommunications, consumer, aerospace & defense, and alternative energy, operating primarily in the United States. Cowen's predecessor was SG Cowen Securities Corporation ("SGCSC"). Effective January 26, 2007, Cowen clears its securities transactions on a fully disclosed basis through National Financial Services, LLC and does not carry customer funds or securities.

Cowen International Limited ("CIL"), a corporation formed under the laws of England and Wales, is the United Kingdom ("U.K.") broker-dealer subsidiary of the Company. CIL is an investment banking and brokerage firm also focused on the emerging growth sectors of healthcare, technology, media and telecommunications, aerospace & defense, alternative energy and consumer, primarily in Europe. CIL's predecessors were SG London Securities Limited and SG London Branch.

Cowen Asset Management, LLC ("CAM US"), a Delaware single member limited liability company, is a wholly-owned subsidiary of the Company. CAM US focuses on a growth-oriented investment style centered on small and mid-sized companies based in North America whose stocks are listed on the major exchanges. CAM US also serves as the investment manager for an equity long-short hedge fund.

Cowen Asset Management Limited ("CAM UK"), a corporation formed under the laws of England and Wales, is a wholly-owned subsidiary of the Company. CAM UK provides traditional asset management services for investors outside the United States, focusing on a global equity strategy.

Cowen Funds, p.l.c. ("Cowen Funds"), an open-ended investment company ("OEIC") with variable capital, is incorporated with limited liability in Ireland, regulated by the Irish Financial Services Regulatory Authority, and established as an undertaking for collective investment in transferable securities ("UCITS"). A UCITS is a public limited company that manages investment funds in the European Union. As such, Cowen Funds is structured as an umbrella fund with segregated liability between sub-funds which are listed on the Irish Stock Exchange. Cowen Funds is an entity in which the Company, through Cowen, has a controlling financial interest.

Cowen Healthcare Royalty Management, LLC ("CHRP Management"), a Delaware single member limited liability company, is an indirect wholly-owned subsidiary of the Company. CHRP Management manages an investment program that invests principally in commercial-stage biopharmaceutical products and companies.

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

1. Organization and Basis of Presentation (Continued)

Cowen Capital Partners, LLC ("Cowen Capital"), a Delaware single member limited liability company, is an indirect wholly-owned subsidiary of the Company. Cowen Capital focuses on providing investment management services to management teams who acquire significant equity positions in growing businesses engaged in business services, healthcare services and specialty manufacturing.

Concurrent with the Company's IPO, the Board of Directors of the Company approved a return of capital distribution to SGASH which left the Company with initial stockholders' equity of $207.0 million at July 12, 2006. In connection with the IPO, the Company distributed cash of $180.3 million to SGASH pursuant to this authorization. Under the terms of the Separation Agreement, the amount of this distribution is subject to adjustment based on a final review of the Company's separation from SG (See Note 11, "Separation from Société Générale and Other Related Matters" for further discussion of the Separation Agreement). At March 31, 2008 and December 31, 2007, the Company had accrued approximately $2.1 million as a capital distribution to SG related to this final review, which is included in accounts payable, accrued expenses and other liabilities on the accompanying Condensed Consolidated Statements of Financial Condition. SGASH received all the proceeds from the sale of 11,517,392 shares as a result of the IPO. In addition, 2,100,000 restricted shares were granted to employees of the Company. SGASH retained 1,382,608 shares of the Company out of the total 12,900,000 shares available for sale. On December 5, 2007, the Company filed a Registration Statement on Form S-3 on behalf of SG. As a result, SG may sell their shares at any time.

Basis of Presentation

Management believes that these Condensed Consolidated Financial Statements include normally recurring adjustments and accruals necessary for a fair presentation of the Condensed Consolidated Statements of Financial Condition, Operations and Cash Flows for the periods presented. These Condensed Consolidated Financial Statements and related notes are unaudited and exclude some of the disclosures required in annual financial statements.

The Condensed Consolidated Statements of Operations do not include litigation expenses incurred by the Company in connection with certain litigation and other legal matters that are indemnified by SG through an indemnification agreement (the "Indemnification Agreement"). The legal reserves related to these indemnified matters are included in legal reserves and legal expenses payable in the Condensed Consolidated Statements of Financial Condition. Before becoming a public company, payments related to these matters were included in the Condensed Consolidated Statements of Cash Flows as financing activities because the Company was a wholly-owned subsidiary of SG. Since the Company became a public company, these payments have been included as operating activities. The effect of this indemnification on the Company's consolidated results of operations is that when a future increase to a loss contingency reserve that is related to litigation covered by the Indemnification Agreement is recorded, the litigation cost and the indemnification recovery will be reflected as an increase in litigation and related expense and the indemnification recovery will be recorded as a reduction to the Company's litigation and related expense. See Note 10, "Commitments, Contingencies and Guarantees" and Note 11, "Separation from Société Générale and Other Related Matters" for further discussion.

The Condensed Consolidated Financial Statements include the accounts of the Company, its subsidiaries and entities in which the Company has a controlling financial interest. All intercompany accounts and transactions have been eliminated upon consolidation. Certain reclassifications have been

1. Organization and Basis of Presentation (Continued)

made to conform prior-period amounts to the current-period presentation, including (i) commissions of $24.0 million and principal transactions of $20.7 million for the three months ended March 31, 2007, have been combined for that period into a new revenue line entitled brokerage in the Condensed Consolidated Statements of Operations and (ii) the reclassification of $0.6 million related to fees paid to the Company for equity research from other revenue to the new revenue line entitled brokerage in the Condensed Consolidated Statements of Operations for the three months ended March 31, 2007.

2. Summary of Significant Accounting Policies

Principles of Consolidation

The Condensed Consolidated Financial Statements include the accounts of Cowen Group, Inc., its subsidiaries, and all other entities which the Company has a controlling financial interest. All intercompany accounts and transactions have been eliminated in consolidation. The Company determines whether it has a controlling financial interest by first evaluating whether the entity is a voting interest entity or a variable interest entity ("VIE").

Voting interest entities are those in which the total equity investment at risk is sufficient to enable the entity to finance its activities independently. Voting interest entities provide equity holders with the obligation to absorb losses, the right to receive residual returns and the right to make decisions about the entity's activities. Voting interest entities are consolidated in accordance with Accounting Research Bulletin No. 51, *Consolidated Financial Statements* ("ARB 51"). ARB 51 provides that ownership of a majority voting interest is a condition for a controlling financial interest in an entity.

According to Financial Accounting Standards Board ("FASB") Interpretation No. 46R, *Consolidation of Variable Interest Entities* ("FIN 46R"), VIEs lack one or more of the characteristics of a voting interest entity as described above. FIN 46R provides that a controlling financial interest in an entity is present when an entity has one or more variable interests that are expected to absorb a majority of the entity's expected losses, receive a majority of the entity's residual returns, or both. The entity that is determined to be the primary beneficiary holds the controlling financial interest and is required to consolidate the VIE. Accordingly, the Company consolidates VIEs in which the Company is deemed to be the primary beneficiary.

When the Company does not have a controlling financial interest in an entity but exerts significant influence over the entity's operating and financial policies, the Company accounts for its investment in accordance with the equity method of accounting prescribed by Accounting Principles Board Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*. This generally applies to cases in which the Company owns a voting or economic interest of between 20 and 50 percent.

In addition to the situations described above, the Company evaluates partnerships, limited liability companies and similar entities that are not VIEs under FIN 46R according to the provisions of EITF 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights* ("EITF 04-5"). The Company consolidates any such entities over which the Company, as general partner or managing member, has the presumption of control according to EITF 04-5.

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

2. Summary of Significant Accounting Policies (Continued)

Minority Interest

The Company reports the proportionate share of equity interests held by minority interest holders in Cowen Healthcare Royalty GP, LLC, as minority interest on the Condensed Consolidated Financial Statements.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Management believes that the estimates utilized in preparing its Condensed Consolidated Financial Statements are reasonable and prudent; however, actual results could differ from those estimates.

Cash and Cash Equivalents

The Company considers all highly liquid investments with original maturities of three months or less at the date of purchase to be cash equivalents.

Valuation of Financial Instruments

Substantially all of the Company's financial instruments are recorded at fair value or contract amounts that approximate fair value. Securities owned and securities sold, not yet purchased and derivative financial instruments including options and warrant positions are stated at fair value, with related changes in unrealized appreciation or depreciation reflected in brokerage revenue in the Condensed Consolidated Statements of Operations. Financial instruments carried at contract amounts include amounts receivable from and payable to brokers, dealers and clearing brokers, and corporate finance and syndicate receivables.

On January 1, 2008, the Company adopted SFAS No. 157, *Fair Value Measurements* ("SFAS 157") as it relates to financial assets and financial liabilities. SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This statement establishes a fair value hierarchy that distinguishes between valuations obtained from sources independent of the entity and those from the entity's own unobservable inputs that are not corroborated by observable market data.

Fair value is generally based on independent sources such as quoted market prices or dealer price quotations. To the extent certain financial instruments trade infrequently or are non-marketable securities, they may not have readily determinable fair values. In these instances, primarily for warrants, the Company estimates the fair value of these instruments using various pricing models and available information that management deems most relevant. Among the factors considered by the Company in determining the fair value of financial instruments are discounted anticipated cash flows, the cost, terms and liquidity of the instrument, the financial condition, operating results and credit ratings of the issuer or underlying company, the quoted market price of publicly traded securities with similar quality and yield, and other factors generally pertinent to the valuation of financial instruments. See Note 9, "Fair Value Measurements" for further discussion.

Prior to January 1, 2008, the Company followed the American Institute of Certified Public Accountants ("AICPA") Audit and Accounting Guide, *Brokers and Dealers in Securities*, when determining fair value for financial instruments, which permitted the recognition of a discount to the quoted price when determining the fair value for a substantial block of a particular security, when the quoted price was not considered to be readily realizable (*i.e.*, a block discount).

Receivable from and Payable to Brokers, Dealers and Clearing Brokers

Amounts receivable from and payable to brokers, dealers and clearing brokers primarily include proceeds from securities sold short including commissions and fees related to securities transactions, net receivables and payables for unsettled transactions, and deposits with the clearing brokers. Proceeds related to securities sold, not yet purchased, may be restricted until the securities are purchased.

Corporate Finance and Syndicate Receivables

Corporate finance and syndicate receivables include receivables relating to the Company's investment banking and advisory engagements. The Company records an allowance for doubtful accounts on these receivables on a specific identification basis. No valuation allowance has been recorded as of March 31, 2008 and December 31, 2007.

Furniture, Fixtures, Equipment, and Leasehold Improvements

Furniture, fixtures, equipment, computer software and leasehold improvements are stated at cost, less accumulated depreciation and amortization. Depreciation of furniture, fixtures, equipment and computer software is provided on the straight-line method over the estimated useful lives of the assets, which range from three to five years. Leasehold improvements are amortized over the lesser of the useful life of the improvement or the term of the lease.

Goodwill

Goodwill represents the excess of the purchase price of a business acquisition over the fair value of the net assets acquired. In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets* ("SFAS 142"), goodwill is not amortized. The Company monitors goodwill annually or more frequently if events or circumstances indicate a possible impairment.

A two-step test is used to determine whether goodwill is impaired. The first step is to compare the carrying value of the Company with the fair value of the Company. If the carrying value of the Company exceeds the fair value of the Company, the second step is applied. The second step is to compare the carrying amount of the goodwill with the implied fair value of the goodwill as determined in accordance with SFAS 142. Goodwill impairment is recognized if its carrying value exceeds its implied fair value. The determination of fair value includes considerations of projected cash flows, relevant trading multiples of comparable exchange listed corporations, and the trading price of the Company's common shares.

Goodwill impairment tests are subject to significant judgment in determining the estimation of future cash flows, discount rates and other assumptions. Changes in these estimates and assumptions could have a significant impact on the fair value and any resulting impairment of goodwill.

2. Summary of Significant Accounting Policies (Continued)

Exchange Memberships

Exchange memberships representing both ownership interest and the right to conduct business on the exchange are carried at cost. The Company evaluates exchange memberships for other-than-temporary impairment annually or more frequently if events or circumstances indicate a possible impairment.

Share-Based Compensation

Share-based awards related to the Company's equity and incentive compensation plans are accounted for according to the provisions of SFAS No. 123(R), *Share-Based Payment* ("SFAS 123R"). See Note 13, "Share-Based Compensation" for a description of these awards.

Legal Reserves

The Company estimates potential losses that may arise out of legal and regulatory proceedings and records a reserve and takes a charge to income when losses with respect to such matters are deemed probable and can be reasonably estimated, in accordance with SFAS No. 5, *Accounting for Contingencies* ("SFAS 5"). These amounts are reported in other expenses, net of recoveries, in the Condensed Consolidated Statements of Operations. The Condensed Consolidated Statements of Operations do not include litigation expenses incurred by the Company in connection with certain litigation matters. See Note 10, "Commitments, Contingencies, and Guarantees" and Note 11, "Separation from Société Générale and Other Related Matters" for additional information. As the successor of the named party in these litigation matters, the Company recognizes the related legal reserve in the Condensed Consolidated Statements of Financial Condition.

Revenue Recognition

Investment Banking

Investment banking revenue includes underwriting fees earned through the Company's participation in public offerings of equity securities. The Company acts as an underwriter and earns revenue including management fees, selling concessions and underwriting fees. Fee revenue relating to underwriting commitments is recorded when all significant items relating to the underwriting cycle have been completed and the amount of the underwriting revenue has been determined. This generally is the point at which all of the following have occurred: (i) the issuer's registration statement has become effective with the Securities and Exchange Commission ("SEC"), or the other offering documents are finalized, (ii) the Company has made a firm commitment for the purchase of shares from the issuer, and (iii) the Company has been informed of the number of shares that it has been allotted.

As co-manager for registered equity underwriting transactions, management must estimate the Company's share of transaction related expenses incurred by the lead manager in order to recognize revenue. Transaction related expenses are deducted from the underwriting fee and therefore reduce the revenue the Company recognizes as co-manager. Such amounts are adjusted to reflect actual expenses in the period in which the Company receives the final settlement, typically within 90 days following the closing of the transaction.

Private placement fees which include warrants received in certain transactions, strategic advisory fees and financial advisory fees, are recorded when the services for the transactions are completed

2. Summary of Significant Accounting Policies (Continued)

under the terms of each assignment or engagement and collection is reasonably assured. Expenses associated with such transactions are deferred until the related revenue is recognized or the engagement is otherwise concluded.

Brokerage

Brokerage revenue consists of commissions, principal transactions and equity research fees.

Commissions. Commission revenue includes fees from executing client transactions in listed securities. These fees are recognized on a trade date basis. The Company permits institutional customers to allocate a portion of their gross commissions to pay for research products and other services provided by third parties. The amounts allocated for those purposes are commonly referred to as soft dollar arrangements. Commissions on soft dollar brokerage are recorded net of the related expenditures on an accrual basis.

Principal Transactions. Principal transaction revenue includes net trading gains and losses from the Company's market-making activities in over-the-counter equity securities, listed options trading, trading of convertible securities, and from trading gains and losses on firm inventory positions, which include warrants previously received as part of investment banking transactions. In certain cases, the Company provides liquidity to clients buying or selling blocks of shares of listed stocks without previously identifying the other side of the trade at execution, which subjects the Company to market risk. These positions are typically held for a very short duration.

Equity Research Fees. Equity research fees are paid to the Company for providing equity research. These fees are recognized as revenue when they are earned.

Other

Other revenue includes fees for managing assets and investments for private equity, asset management and alternative asset management funds, fees for managing a portfolio of merchant banking investments on behalf of SG and other third party investors, and miscellaneous income such as fees for managing venture capital investments. Management fees are recognized in the periods during which the related services are performed and the amounts have been contractually earned.

Revenue Recognition on Incentive Income

Incentive income is calculated as a percentage of the profits earned by CHRP Management, subject to clawback and waterfall provisions. The Company has elected to account for incentive income that is subject to contingencies in accordance with Method 1 of Emerging Issues Task Force Topic D-96, *Accounting for Management Fees Based on a Formula* ("D-96"). Under Method 1 of D-96, incentive income is recognized at the end of the contract period when all of the contingencies have been resolved. As of March 31, 2008, the Company has not yet recorded any incentive income related to this arrangement.

Derivative Financial Instruments

The Company used futures contracts for proprietary trading activities, and utilized credit default swaps to buy credit protection during 2007. The Company uses listed options for trading activities and to economically hedge trading positions. The Company also holds warrant positions. Warrants provide

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

2. Summary of Significant Accounting Policies (Continued)

the holder the right to purchase securities from the issuer, and may be received in connection with certain private placement transactions.

The fair values of the credit default swaps and options are based on current market quotes. The fair value of warrants is based on a valuation model that considers contractual term, market price and volatility. Initially, the fair value of warrants received in connection with private placement transactions is included in investment banking revenues in the Condensed Consolidated Statement of Operations. Subsequent realized and unrealized gains and losses related to changes in the fair value of warrants are included in brokerage revenue in the Condensed Consolidated Statement of Operations. The fair value of listed options, warrants, and credit default swaps is included in securities owned and securities sold, not yet purchased in the Condensed Consolidated Statements of Financial Condition. The fair value of futures contracts and required margin deposits are included in receivable from brokers, dealers and clearing brokers in the Condensed Consolidated Statements of Financial Condition, and were de minimis at March 31, 2008 and December 31, 2007.

Realized and unrealized gains and losses from changes in the fair value of derivatives are included in brokerage revenue in the Condensed Consolidated Statements of Operations. The Company does not use hedge accounting as described in SFAS 133, *Accounting for Derivatives and Hedging Activities.*

Earnings Per Share

The Company computes earnings per share in accordance with SFAS No. 128, *Earnings per Share.* Basic earnings per common share is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted earnings per common share is calculated by adjusting the weighted average outstanding shares to assume conversion of all potentially dilutive nonvested restricted stock and stock options, in accordance with the treasury stock method.

Leases

Leases are accounted for under SFAS No. 13, *Accounting for Leases*. All of the Company's leases are classified as operating leases.

Foreign Currency Translation

The Company consolidates certain foreign subsidiaries which have designated a foreign currency as the functional currency. For entities which have designated a foreign currency as the functional currency, assets and liabilities are translated into US dollars based on current rates, which are the rates prevailing at each statement of financial condition date, and revenues and expenses are translated at historical rates, which are the average rates for the relevant periods. The resulting translation gains and losses, and the tax effects of such gains and losses, are recorded in other comprehensive income, a separate component of stockholders' equity. Gains or losses resulting from foreign currency transactions are included in net income.

Income Taxes

The income tax provision reflected in the Condensed Consolidated Statements of Operations is consistent with the liability method prescribed by SFAS No. 109, *Accounting for Income Taxes*. Under the liability method, deferred income taxes reflect the net tax effects of temporary differences between

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

2. Summary of Significant Accounting Policies (Continued)

the carrying amount of assets and liabilities for financial statement and income tax purposes, as determined under applicable tax laws and rates. A valuation allowance is provided for deferred tax assets when it is more likely than not that the benefits of net deductible temporary differences and net operating loss carryforwards will not be realized.

The Company follows the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 prescribes a recognition and measurement of a tax position taken or expected be taken in a tax return and provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

3. Accounting Developments

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements*, ("SFAS 160"). SFAS 160 will significantly change financial accounting and reporting for noncontrolling (or minority) interests in consolidated financial statements. SFAS 160 is effective for the first annual reporting period beginning on or after December 15, 2008. Earlier application is prohibited. The Company is currently assessing the impact of SFAS 160 on its consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* ("SFAS 141R"), which replaces SFAS 141. SFAS 141R establishes principles and requirements for how an acquirer in a business combination (i) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any controlling interest; (ii) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase; and (iii) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141R is effective for the first annual reporting period beginning on or after December 15, 2008. Earlier application is prohibited.

In February 2008, the FASB issued FASB Staff Position SFAS 157-2, *Effective Date of FASB Statement No. 157* ("FSP SFAS 157-2"). FSP SFAS 157-2 delays the effective date of SFAS 157 to fiscal years beginning after November 15, 2008 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The adoption of FSP SFAS 157-2 is not expected to have a material impact on the Company's consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133* ("SFAS 161"). SFAS 161 requires enhanced disclosures for derivative instruments and hedging activities that include how and why an entity uses derivatives, how these instruments and the related hedged items are accounted for under SFAS 133 and related interpretations, and how derivative instruments and related hedged items affect the entity's financial position, results of operations and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. Early adoption is permitted. The Company is currently evaluating the impact that SFAS 161 will have on its consolidated financial statements.

In June 2007, the AICPA issued Statement of Position ("SOP") No. 07-1, *Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and*

3. Accounting Developments (Continued)

Equity Method Investors for Investments in Investment Companies ("SOP 07-1"). SOP 07-1 addresses when the accounting principles of the AICPA Audit and Accounting Guide for Investment Companies must be applied by an entity and whether those accounting principles must be retained by a parent company in consolidation or by an investor in the application of the equity method of accounting. The effective date for SOP 07-1 was initially for fiscal years beginning on or after December 15, 2007; however, in February 2008, the FASB directed the FASB staff to issue SOP 07-1-1, *Effective Date of AICPA Statement of Position 07-1* ("SOP 07-1-1"), which indefinitely delays the effective dates for SOP 07-1 and FASB Staff Position ("FSP") FIN 46(R)-7, *Application of FASB Interpretation No. 46(R) to Investment Companies* which was effective upon adoption of SOP 07-1.

4. Restricted Cash Pursuant to Escrow Agreement and Related Indemnification Agreement with Société Générale

In connection with the IPO, the Company entered into an Indemnification Agreement with SG under which (1) SG will indemnify, and will defend and hold harmless the Company and each of the Company's subsidiaries from and against certain liabilities assumed or retained by SG, and (2) SG will indemnify the Company for known, pending and threatened litigation (including the costs of such litigation) and certain known regulatory matters, in each case, that existed prior to the date of the IPO to the extent the cost of such litigation results in payments in excess of the amount placed in escrow to fund such matters (See Note 11, "Separation from Société Générale and Other Related Matters", for further discussion of the Indemnification Agreement).

On July 12, 2006, the Company entered into an Escrow Agreement with SGASH and a third-party escrow agent (the "Escrow Agreement") and deposited with the escrow agent $72.3 million for the payment of liabilities arising out of the matters for which SG has agreed to indemnify the Company. Subsequent to making this deposit, certain matters covered by the Escrow Agreement have been settled and excess reserves related to these settled matters were returned to SGASH. The escrow agent will, when and as directed by SGASH, distribute funds from the escrow account to satisfy specified contingent liabilities for which SG has assumed responsibility should such liabilities become due. Any amounts remaining in the escrow account after final conclusion of the related litigation will be paid to SGASH. SGASH is also entitled to any interest earned on such deposits held in escrow. The balance in the escrow account was $23.4 million as of March 31, 2008 and $23.5 million as of December 31, 2007.

The effect of this indemnification on the Company's consolidated results of operations is that when a future increase to a loss contingency reserve that is related to litigation covered by the Indemnification Agreement is recorded, the litigation cost and the indemnification recovery will be reflected as an increase in legal expenses and the indemnification recovery will be recorded as a reduction to the Company's legal expenses. Legal expenses are included within other expenses in the Condensed Consolidated Statements of Operations.

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

5. Securities Owned and Securities Sold, Not Yet Purchased

Securities owned and securities sold, not yet purchased, both at fair value, consist of the following at March 31, 2008 and December 31, 2007:

	March 31, 2008		December 31, 2007	
	Owned	Sold, Not Yet Purchased	Owned	Sold, Not Yet Purchased
	(in thousands)			
Equity securities	$ 16,628	$ 10,902	$ 16,715	$ 23,705
Options	857	1,842	3,247	1,363
Mutual and other investment funds	5,245		2,660	
Warrants	1,764		2,420	
Corporate debt securities			571	571
Total	$ 24,494	$ 12,744	$ 25,613	$ 25,639

Securities sold, not yet purchased, represent obligations of the Company to deliver a specified security at a contracted price and, thereby, create a liability to purchase that security in the market at prevailing prices. The Company's liability for securities to be delivered is measured at their fair value as of the date of the financial statements. However, these transactions result in off-balance sheet risk, as the Company's ultimate cost to satisfy the delivery of securities sold, not yet purchased, may exceed the amount reflected in the Condensed Consolidated Statements of Financial Condition. Substantially all securities owned are pledged to the clearing broker under terms which permit the clearing broker to sell or re-pledge the securities to others subject to certain limitations.

6. Receivable from and Payable to Brokers, Dealers and Clearing Brokers

Amounts receivable from and payable to brokers, dealers and clearing brokers at March 31, 2008 and December 31, 2007 consist of the following:

	March 31, 2008		December 31, 2007	
	Receivable	Payable	Receivable	Payable
	(in thousands)			
Clearing brokers	$ 23,654	$ 674	$ 42,941	$ 34
Fees and commissions	8,979	116	5,835	339
Total	$ 32,633	$ 790	$ 48,776	$ 373

7. Exchange Memberships

Exchange memberships provide the Company with the right to do business on the exchanges of which it is a member. No impairment was recorded during the three months ended March 31, 2008 and 2007. The fair value of the exchange memberships was approximately $0.8 million and $1.0 million at March 31, 2008 and December 31, 2007, respectively.

8. Goodwill

All of the Company's goodwill resulted from the 1998 acquisition of the former Cowen private partnership by SG. The entire goodwill balance is recorded at the Cowen entity, the U.S. broker-dealer

8. Goodwill (Continued)

subsidiary of the Company. Goodwill is reviewed for possible impairment at least annually, consistent with valuation methodologies pursuant to SFAS 142. There were no additions to goodwill and no impairment losses during the three months ended March 31, 2008.

9. Fair Value Measurements

The Company adopted the provisions of SFAS 157 on January 1, 2008. SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS 157 also establishes a framework for measuring fair value and a valuation hierarchy based upon the transparency of inputs used in the valuation of an asset or liability. Classification within the hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The valuation hierarchy contains three levels:

Level 1 Valuation inputs are unadjusted quoted market prices for identical assets or liabilities in active markets.

Level 2 Valuation inputs are quoted prices for identical assets or liabilities in markets that are not active, quoted market prices for similar assets and liabilities in active markets and other observable inputs directly or indirectly related to the asset or liability being measured.

Level 3 Valuation inputs are unobservable and significant to the fair value measurement.

The following describes the valuation methodologies the Company uses to measure different financial instruments at fair value, including an indication of the level in the fair value hierarchy in which each instrument is generally classified.

Equity securities. Equity securities are valued based on quoted market prices. Equity securities that trade in active markets are classified within Level 1, and equity securities that trade in inactive markets are classified within Level 2.

Options. Listed options are valued based on quoted market prices. All options trade in active markets and are classified within Level 3.

Mutual and other investment funds. Mutual funds are valued based on quoted net asset values. All mutual funds trade in active markets and are classified within Level 1. Other investment funds include an investment in an affiliated alternative investment fund, and are classified within Level 3.

Warrants. Warrants in public companies are valued using a Black-Scholes valuation model, based on observable inputs directly related to the warrants. These warrants are classified within Level 2. Warrants in private companies are valued using inputs that are unobservable and significant to the fair value measurement, such as third party transactions in that security, and are classified within Level 3.

We maintain policies and procedures to value our financial instruments using the best and most relevant data available. In addition, management reviews valuations, including independent price validation for certain instruments. In some instances, we retain an independent pricing vendor to assist in valuing certain instruments.

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

9. Fair Value Measurements (Continued)

The following table summarizes the Company's financial assets and liabilities that are measured and recognized at fair value on a recurring basis classified under the appropriate level of the fair value hierarchy as of March 31, 2008:

	Level 1	Level 2	Level 3	Total
		(in thousands)		
Assets:				
Equity securities	$ 16,553	$ 75	$	$ 16,628
Options	857			857
Mutual and other investment funds	2,472		2,773	5,245
Warrants		1,330	434	1,764
Total	$ 19,882	$ 1,405	$ 3,207	$ 24,494
Liabilities:				
Equity securities	$ 10,902	$	$	$ 10,902
Options	1,842			1,842
Total	$ 12,744	$	$	$ 12,744

The Company made an investment of approximately $2.8 million in an affiliated alternative investment fund during the three months ended March 31, 2008, which has been classified within Level 3. For the three months ended March 31, 2008 there were no changes in the value of assets classified within Level 3.

The Company has not applied the provisions of SFAS 157 related to disclosures surrounding nonfinancial assets, including goodwill, and nonfinancial liabilities. In February 2008, the FASB issued FSP SFAS 157-2, which deferred the required implementation of these disclosures until 2009.

10. Commitments, Contingencies and Guarantees

Legal Proceedings

The Company is involved in a number of legal and regulatory matters that arise from time to time in connection with the conduct of its businesses. The Company estimates potential losses that may arise out of these matters and records a reserve and takes a charge to income when losses with respect to such matters are deemed probable and can be reasonably estimated, in accordance with SFAS 5. To the extent that the Company is indemnified by SG, indemnified legal expenses and liabilities will be paid out of escrow pursuant to the Escrow Agreement. See Note 4, "Restricted Cash Pursuant to Escrow Agreement and Related Indemnification Agreement with Société Générale" and Note 11, "Separation from Société Générale and Other Related Matters," for further discussion of the Escrow and Indemnification Agreements. Although there can be no assurances as to the ultimate outcome, Cowen has established reserves for litigation and regulatory matters that it believes are adequate as of March 31, 2008. Estimates, by their nature, are based on judgment and currently available information and involve a variety of factors, including, but not limited to, the type and nature of the litigation, claim or proceeding, the progress of the matter, the advice of legal counsel, the Company's defenses and its experience in similar cases or proceedings as well as its assessment of matters, including settlements, involving other defendants in similar or related cases or proceedings. The Company may increase or decrease its legal reserves in the future, on a matter-by-matter basis, to account for developments in such matters.

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

10. Commitments, Contingencies and Guarantees (Continued)

Based on information currently available, the Company believes that the amount, or range, of reasonably possible losses will not have a material adverse effect on the Company's consolidated financial condition or cash flows. However, losses may be material to the Company's operating results in a future period, depending in part, on the operating results for such period and the extent to which the Company is indemnified by SG.

Lease commitments

The Company's headquarters is located in New York City and other office locations include Boston, San Francisco, Cleveland, Dallas, London and Geneva. Certain office space is leased under operating leases that extend up to 2015. In addition, certain lease agreements are subject to escalation clauses. Under the terms of the Boston office lease, which expires on November 30, 2014, there is a five-year extension option which would allow the Company to extend the lease through November 30, 2019.

As of March 31, 2008, the Company had the following lease commitments related to these agreements:

	Minimum Lease Payments
	(in thousands)
Remainder of 2008	$ 7,074
2009	9,631
2010	9,741
2011	9,730
2012	9,232
Thereafter	11,477
Total	$ 56,885

Rent expense was approximately $2.8 million and $2.7 million for the three months ended March 31, 2008 and 2007, respectively. Rent expenses above include building operating expenses which are charged to the Company.

Guarantees

The Company has outsourced certain information technology services under agreements which are in place until 2010. As of March 31, 2008, the Company's annual minimum guaranteed payments under these agreements are as follows:

	Minimum Guaranteed Payments
	(in thousands)
Remainder of 2008	$ 9,061
2009	10,477
2010	4,388
Total	$ 23,926

10. Commitments, Contingencies and Guarantees (Continued)

The Company applies the provisions of the FASB's Interpretation No. 45, *Guarantor's Accounting and Disclosure Required for Guarantees, Including Indirect Indebtedness of Others*, which provides accounting and disclosure requirements for certain guarantees. In this regard, the Company has agreed to indemnify its clearing broker for losses that it may sustain from the customer accounts introduced by the Company. Pursuant to the clearing agreement, the Company is required to reimburse the clearing broker, without limit, for any losses incurred due to the counterparty's failure to satisfy its contractual obligations.

The Company is a member of various securities exchanges. Under the standard membership agreement, members are required to guarantee the performance of other members and, accordingly, if another member becomes unable to satisfy its obligations to the exchange, all other members would be required to meet the shortfall. The Company's liability under these arrangements is not quantifiable and could exceed the cash and securities it has posted as collateral. However, management believes that the potential for the Company to be required to make payments under these arrangements is remote. Accordingly, no contingent liability is recorded in the Condensed Consolidated Statements of Financial Condition for these arrangements.

11. Separation from Société Générale and Other Related Matters

In connection with the IPO, the Company entered into the Separation Agreement, the Indemnification Agreement and a number of other agreements for the purpose of accomplishing the separation from SG, the transfer of the Cowen and CIL businesses to the Company, the return of capital to SGASH, and various other matters regarding the separation and the IPO. These agreements provide, among other things, for the allocation of employee benefits, tax and other liabilities and obligations attributable or related to periods or events prior to, in connection with and after the IPO.

Under the Separation Agreement, both the Company and SG have assumed and/or retained certain actual or contingent liabilities. Specifically, the Company retained or assumed, among others, certain liabilities reflected in the Company's Condensed Consolidated Statements of Financial Condition, all liabilities associated with the Company's stock ownership and incentive compensation plans, liabilities associated with certain contracts and accounts that the Company shares with SG, liabilities associated with the breach of or failure to perform any of the Company's obligations under certain agreements, certain specified liabilities and all other liabilities expressly allocated to the Company in connection with the separation, and all other known and unknown liabilities (to the extent not specifically assumed by SG) relating to, arising out of or resulting from the Company's business, assets, liabilities or any business or operations conducted by the Company at any time prior to, on or after the date of separation. Liabilities retained or assumed by SG include, among others, liabilities associated with the sale and transfer of its interests in the SG Merchant Banking Fund L.P. to a third party, its portion of liabilities associated with certain contracts and accounts that it shares with the Company, liabilities associated with the breach of or failure to perform any of its obligations under certain agreements, liabilities arising from the operation of its business, liabilities associated with certain businesses previously conducted by the Company, certain liabilities associated with any known or unknown employee-related claims made by any current or former employees of SG or any of its subsidiaries (other than the Company), certain specific contingent liabilities to the extent that such liabilities exceed the aggregate dollar amount held in escrow pursuant to the Escrow Agreement, certain specified liabilities and all other liabilities expressly allocated to it under the Separation Agreement and the other agreements entered into in connection with the separation, and all other

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

11. Separation from Société Générale and Other Related Matters (Continued)

known and unknown liabilities relating to, arising out of or resulting from its business, assets, liabilities or any business or operations conducted by SG.

Under the Indemnification Agreement, the Company will indemnify, and will defend and hold harmless SG and its subsidiaries from and against all liabilities specifically retained or assumed by the Company following the IPO. SG will indemnify, and will defend and hold harmless the Company and each of the Company's subsidiaries from and against certain liabilities assumed or retained by them, and SG will indemnify the Company for known, pending and threatened litigation (including the costs of such litigation) and certain known regulatory matters, in each case, that existed prior to the date of the IPO to the extent the cost of such litigation results in payments in excess of the amount placed in escrow to fund such matters.

During the third quarter of 2007, the Company concluded that a receivable recorded on its Condensed Consolidated Statement of Financial Condition in the amount of $1.9 million owed to it from SG is in dispute. The receivable had been previously established on the Consolidated Statement of Financial Condition of the Company prior to the time of the IPO as a "Receivable from brokers, dealers and clearing brokers" and reported as such, and has since been reclassified to "Other assets." The Company has been informed that SG currently disputes its obligation to pay the receivable. The Company believes, based on current facts and circumstances and in consultation with counsel, that it holds a valid legal claim to the receivable. Based upon the validity of its legal claim, the Company believes the receivable is realizable. Therefore, no reserves have been established. The Company and SG are continuing to review the matter in an effort to reach a mutually acceptable resolution.

12. Related Party Transactions

The Company has related party transactions with Cowen Investments Holdings, LLC, an unconsolidated investment fund holding company and, beginning in the third quarter of 2007, the unconsolidated investment funds managed by CHRP Management.

Amounts receivable from related parties were $5.5 million and $2.7 million as of March 31, 2008 and December 31, 2007, respectively. There were no amounts payable to related parties as of March 31, 2008 and December 31, 2007. For the three months ended March 31, 2008, revenues from related parties were $1.6 million and are included in other revenues in the Condensed Consolidated Statements of Operations. There were no related party revenues for the three months ended March 31, 2007. The related party revenues and receivable balances primarily relate to management fees earned by the Company, and amounts receivable from the unconsolidated investment funds managed by CHRP Management.

13. Share-Based Compensation

Upon becoming a public company, the Company established the 2006 Equity and Incentive Plan (the "2006 Plan"). The 2006 Plan permits the grant of options, restricted shares, restricted stock units and other equity based awards to its employees, consultants and directors for up to 4,725,000 shares of common stock. On June 7, 2007, the Company's shareholders approved the 2007 Equity and Incentive Plan (the "2007 Plan"), which permits the grant of options, restricted shares, restricted stock units and other equity and cash based awards to its employees, consultants and directors for up to an additional 1,500,000 shares of common stock. Stock options granted generally vest over two to five year periods and expire seven years from the date of grant. Restricted shares issued generally vest over three to five

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

13. Share-Based Compensation (Continued)

year periods. Restricted stock units may be immediately vested or may generally vest over a three to five year period. As of March 31, 2008, there were 11,131 restricted stock units outstanding for awards to non-employee directors, which were immediately vested and expensed upon issuance. There were no restricted stock units granted to non-employee directors during the three months ended March 31, 2008. As of March 31, 2008, there were 18,766 restricted stock units outstanding for awards to employees, which generally vest over a three to five year period. For the three months ended March 31, 2008, the Company awarded 4,117 restricted stock units to employees. As of March 31, 2008, there were approximately 1.9 million shares available for future issuance under the 2006 and 2007 Plans.

The Company measures compensation cost for these awards according to the fair value method prescribed by SFAS 123R. In accordance with the expense recognition provisions of SFAS 123R, unearned compensation associated with share-based awards with graded vesting periods is amortized using the accelerated method over the vesting period of the option or award.

In relation to these awards, the Company recognized a benefit of $1.7 million for the three months ended March 31, 2008 and recognized an expense of approximately $4.5 million for the three months ended March 31, 2007. The income tax effect recognized for these awards was a provision of $0.8 million for the three months ended March 31, 2008 and a benefit of $1.9 million the three months ended March 31, 2007.

Effective March 4, 2008, Kim S. Fennebresque, formerly Chairman, President and Chief Executive Officer of the Company, resigned as President and Chief Executive Officer. In connection with Mr. Fennebresque's resignation, he forfeited, in its entirety, the equity award of 975,000 restricted shares he received in connection with the Company's IPO (the "IPO Award"). As a result, compensation expense for the three months ended March 31, 2008 includes a reversal of $5.1 million of expense previously recognized for Mr. Fennebresque's IPO award.

In addition, as part of his resignation agreement with the Company, Mr. Fennebresque will continue to vest in the equity awards he received as part of his 2006 and 2007 annual compensation. The fair value of the related shares were remeasured as a result of this vesting modification, and any remaining expense associated with these awards was expensed in the first quarter of 2008, as there is no longer a service period requirement relating to these awards. The net result of the remeasurement and acceleration of these awards was an expense of $0.1 million in the three months ended March 31, 2008.

The fair value of each option award is estimated on the date of grant using a Black-Scholes option valuation model that uses the following assumptions:

> *Expected term* Expected term represents the period of time that options granted are expected to be outstanding. The Company elected to use the "simplified" calculation method according to the provisions of SEC Staff Accounting Bulletin No. 107 ("SAB 107"): industry, market capitalization, stage of life cycle and capital structure, as applicable to companies that lack extensive historical data. The mid-point between the vesting date and the contractual expiration date is used as the expected term under this method.
>
> *Expected volatility* Based on the lack of historical data for the Company's own shares, the Company based its expected volatility on a representative peer group that took into account the criteria outlined in SAB 107.

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

13. Share-Based Compensation (Continued)

Risk free rate The risk-free rate for periods within the expected term of the option is based on the interest rate of a traded zero-coupon U.S. Treasury bond with a term equal to the options' expected term on the date of grant.

Dividend yield The Company has not paid and does not expect to pay dividends in the foreseeable future. Accordingly, the assumed dividend yield is zero.

There were no stock option grants during the three months ended March 31, 2008 and 2007. The following table summarizes the Company's stock option activity for the three months ended March 31, 2008:

	Shares Subject to Option	Weighted Average Exercise Price/Share[1]	Weighted Average Remaining Term	Aggregate Intrinsic Value[2]
			(in years)	(in thousands)
Balance outstanding at December 31, 2007	977,861	$ 16.01		
Options granted				
Options exercised				
Options forfeited	(73,705)	16.00		
Options expired				
Balance outstanding at March 31, 2008	904,156	$ 16.01	5.34	$
Options exercisable at March 31, 2008		$		$

(1) No options were exercised through March 31, 2008.

(2) Based on the Company's closing stock price of $7.09 on March 31, 2008.

As of March 31, 2008, there was approximately $1.9 million of unrecognized compensation expense related to the Company's grant of stock options. Unrecognized compensation expense related to stock options is expected to be recognized over a weighted-average period of 1.9 years. No stock options vested during the period ended March 31, 2008.

The following table summarizes the Company's restricted shares activity for the three months ended March 31, 2008:

	Nonvested Restricted Shares	Weighted-Average Grant Date Fair Value
Balance outstanding at December 31, 2007	2,999,031	$ 17.39
Granted	1,586,314	9.57
Vested	(199,543)	19.47
Forfeited	(1,178,570)	15.60
Balance outstanding at March 31, 2008	3,207,232	$ 13.75

The fair value of restricted stock is determined based on the number of shares granted and the quoted price of the Company's common stock on the date of grant.

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

13. Share-Based Compensation (Continued)

As of March 31, 2008, there was approximately $21.0 million of unrecognized compensation expense related to the Company's grant of nonvested restricted shares. Unrecognized compensation expense related to nonvested restricted shares is expected to be recognized over a weighted-average period of 2.1 years. The total fair value of shares vested during the three months ended March 31, 2008 was $1.8 million. No shares vested during the three months ended March 31, 2007.

14. Income Taxes

The taxable results of the Company's U.S. operations are included in the consolidated income tax returns of Cowen Group, Inc. as well as stand alone state and local tax returns. For the period ended March 31, 2008, the tax results of the Company's U.K. operations are reported by CIL and CAM UK separately in their respective U.K. tax filings. If applicable, CIL and CAM UK share tax losses to the extent permitted by local law. For the period ended March 31, 2007, the tax results of the Company's U.K. operations are included in CIL's U.K. tax filing since CAM UK started business in October 2007.

The reconciliation of the Company's federal statutory tax rate to the effective income tax rate for the three months ended March 31, 2008 and 2007 is as follows:

	Three Months Ended March 31,	
	2008	**2007**
Statutory U.S. federal income tax rate	35.0%	35.0%
State and local taxes	9.6	5.6
Syndication costs	18.6	
Share-based compensation	10.1	
Meals and entertainment	7.0	2.4
Other, net	(0.4)	0.9
Change in valuation allowance	(8.8)	(0.1)
Effective tax rate	71.1%	43.8%

For the three months ended March 31, 2008, the tax expense of $1.6 million consisted of current tax expense of $0.4 million and a net deferred expense of $1.2 million. The net deferred expense is primarily attributable to the reversal of share-based compensation that occurred during the quarter as well as the amortization of tax deductible goodwill. The 2008 effective tax rate differs from the statutory tax rate of 35% primarily due to syndication costs and meals and entertainment as well as state and local taxes. The syndication costs relate to expected non-deductible placement agent fees associated with an alternative asset management product. For the period ended March 31, 2007 the effective tax rate differed from statutory tax rate of 35% primarily due to meals and entertainment and state and local taxes.

For 2008, share-based compensation increased the effective tax rate since the book expense is based on the grant date share price of $20.67 while the 2008 tax deduction is based on the vest date share price of $9.25. This book-tax difference is permanent because the Company does not have a windfall of tax benefits under SFAS 123R. At December 31, 2007, the Company had established a valuation allowance to account for the decrease in share price and tax deduction. As such, the share-

Cowen Group, Inc.

Notes to Condensed Consolidated Financial Statements (Continued)

14. Income Taxes (Continued)

based compensation permanent difference for the period is offset by the release of the federal and state local valuation allowance.

The Company's effective tax rate depends upon the results of its business. If the Company does not have sufficient income, it will not realize tax benefits, such as compensation and legal reserve deductions and foreign tax credits. Additionally, if the Company sustains losses, deferred tax assets will be subject to impairment through the establishment of a valuation allowance. Moreover, if the Company decides for business reasons to incur additional non-deductible syndication costs such expenses will increase the effective tax rate. Furthermore, a high concentration of the Company's deferred tax assets is attributable to share-based compensation. To the extent that share-based compensation vests at a share price less than the grant price, such shortfall will result in an unfavorable permanent book-tax difference.

15. Earnings Per Share

The Company calculates its basic and diluted earnings per share in accordance with SFAS No. 128, *Earnings Per Share*. Basic earnings per common share is calculated by dividing net income by the weighted average number of common shares outstanding for the period. As of March 31, 2008, there were 14,429,232 shares outstanding, of which 3,207,232 are restricted. To the extent that restricted shares are unvested, they are excluded from the calculation of basic earnings per share. The Company has included 17,659 fully vested restricted stock units in its calculation of basic earnings per share.

Diluted earnings per common share is calculated by adjusting the weighted average outstanding shares to assume conversion of all potentially dilutive nonvested restricted stock and stock options. The Company uses the treasury stock method to reflect the potential dilutive effect of the unvested restricted shares and unexercised stock options. In calculating the number of dilutive shares outstanding, the shares of common stock underlying unvested restricted shares are assumed to have been delivered, and options are assumed to have been exercised, on the grant date. The assumed proceeds from the assumed vesting, delivery and exercising were calculated as the sum of (a) the amount of compensation cost attributed to future services and not yet recognized as of the end of the period and (b) the amount of tax benefit that was credited to additional paid-in capital assuming vesting and delivery of the restricted shares. The tax benefit is the amount resulting from a tax deduction for compensation in excess of compensation expense recognized for financial statement reporting purposes. Stock options outstanding were not included in t