

GLEACHER & COMPANY, INC.

Form 10-Q

August 08, 2011

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

**x Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**for the quarterly period ended June 30, 2011**

- 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 014140**

**GLEACHER & COMPANY, INC.**

(Exact name of registrant as specified in its charter)

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**Delaware**

(State or other jurisdiction of incorporation or organization)

**22-2655804**

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

**1290 Avenue of the Americas, New York, New York**

(Address of principal executive offices)

**10104**

(Zip Code)

Registrant's telephone number, including area code **(212) 273-7100**

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 Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large Accelerated Filer

Accelerated Filer

Non-accelerated Filer

Smaller Reporting Company

(Do not check if a smaller reporting company)

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

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

127,834,829 shares of Common Stock were outstanding as of the close of business on July 29, 2011

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**GLEACHER & COMPANY, INC. AND SUBSIDIARIES**

FORM 10-Q

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## GLEACHER &amp; COMPANY, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

**Part I Financial Information****Item 1. Financial Statements**

| (In thousands, except for per share amounts)                                  | Three Months Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|---|--------------------------------|------------|------------------------------|------------|
|   | 2011                           | 2010       | 2011                         | 2010       |
| <i>Revenues:</i>  |                                |            |                              |            |
| Principal transactions  | \$ 32,560                      | \$ 33,035  | \$ 95,970                    | \$ 79,341  |
| Commissions   | 4,109                          | 5,139      | 9,097                        | 9,304      |
| Investment banking  | 10,042                         | 5,777      | 20,364                       | 20,575     |
| Investment banking revenues from related party                                |                                | 1,050      |                              | 1,350      |
| Investment gains/(losses), net  | 368                            | (1,662)    | (318)                        | (1,512)    |
| Interest income   | 14,885                         | 12,379     | 29,958                       | 28,540     |
| Gain from bargain purchase ClearPoint Funding, Inc. acquisition (See Note 11) |                                |            | 2,330                        |            |
| Fees and other  | 2,401                          | 1,575      | 4,215                        | 2,485      |
| Total revenues  | 64,365                         | 57,293     | 161,616                      | 140,083    |
| Interest expense  | 3,057                          | 2,760      | 5,649                        | 6,247      |
| Net revenues  | 61,308                         | 54,533     | 155,967                      | 133,836    |
| <i>Expenses (excluding interest):</i>   |                                |            |                              |            |
| Compensation and benefits   | 40,298                         | 44,875     | 104,871                      | 113,076    |
| Impairment of goodwill and intangible assets (See Note 12)                    | 14,311                         |            | 14,311                       |            |
| Clearing, settlement and brokerage  | 5,871                          | 1,684      | 11,266                       | 3,164      |
| Communications and data processing  | 3,903                          | 3,533      | 7,916                        | 6,635      |
| Occupancy, depreciation and amortization                                      | 2,478                          | 5,671      | 4,693                        | 7,917      |
| Selling   | 2,281                          | 1,273      | 3,963                        | 2,468      |
| Other   | 4,494                          | 4,534      | 9,010                        | 9,667      |
| Total expenses (excluding interest)   | 73,636                         | 61,570     | 156,030                      | 142,927    |
| Loss before income taxes  | (12,328)                       | (7,037)    | (63)                         | (9,091)    |
| Income tax (benefit)/expense  | (1,322)                        | (1,800)    | 3,739                        | (3,643)    |
| Net loss  | \$ (11,006)                    | \$ (5,237) | \$ (3,802)                   | \$ (5,448) |
| Per share data:   |                                |            |                              |            |
| Basic loss per share  | \$ (0.09)                      | \$ (0.04)  | \$ (0.03)                    | \$ (0.05)  |
| Diluted loss per share  | (0.09)                         | (0.04)     | (0.03)                       | (0.05)     |
| Weighted average shares of common stock:                                      |                                |            |                              |            |
| Basic   | 124,061                        | 121,128    | 123,825                      | 120,546    |
| Diluted   | 124,061                        | 121,128    | 123,825                      | 120,546    |

The accompanying notes are an integral part  
of these consolidated financial statements.

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## GLEACHER &amp; COMPANY, INC.

## CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(Unaudited)

| <b>(In thousands of dollars, except for share and per share amounts)</b>  | <b>June 30,<br/>2011</b> | <b>December 31,<br/>2010</b> |
|---|--------------------------|------------------------------|
| <i>Assets</i>   |                          |                              |
| Cash and cash equivalents   | \$ 46,436                | \$ 40,009                    |
| Cash and securities segregated for regulatory purposes  | 4,000                    | 100                          |
| Securities purchased under agreements to resell   | 303,000                  | 86,484                       |
| Receivables from:   |                          |                              |
| Brokers, dealers and clearing organizations   | 21,787                   | 25,721                       |
| Related parties   | 1,307                    | 2,245                        |
| Others  | 18,460                   | 18,283                       |
| Financial instruments owned, at fair value (includes assets pledged of \$1,169,365 and \$1,280,443 at June 30, 2011 and December 31, 2010, respectively)  | 1,241,745                | 1,281,243                    |
| Investments   | 16,098                   | 18,084                       |
| Office equipment and leasehold improvements, net  | 7,505                    | 6,653                        |
| Goodwill  | 96,766                   | 105,694                      |
| Intangible assets   | 9,457                    | 15,565                       |
| Income taxes receivable   | 13,468                   | 14,782                       |
| Deferred tax assets, net  | 30,028                   | 34,154                       |
| Other assets  | 11,186                   | 8,915                        |
| <b>Total Assets</b>   | <b>\$ 1,821,243</b>      | <b>\$ 1,657,932</b>          |
| <i>Liabilities and Stockholders' Equity</i>   |                          |                              |
| <i>Liabilities</i>  |                          |                              |
| Payables to:  |                          |                              |
| Brokers, dealers and clearing organizations   | \$ 1,020,905             | \$ 1,101,440                 |
| Related parties   | 5,019                    | 4,986                        |
| Others  | 2,764                    | 2,347                        |
| Securities sold under agreements to repurchase  | 191,449                  |                              |
| Securities sold, but not yet purchased, at fair value   | 154,189                  | 112,275                      |
| Secured borrowings  | 60,084                   |                              |
| Accrued compensation  | 23,526                   | 74,202                       |
| Accounts payable  | 2,990                    | 1,161                        |
| Accrued expenses  | 9,331                    | 7,595                        |
| Income taxes payable  | 3,671                    | 3,468                        |
| Deferred tax liabilities  | 2,377                    | 3,390                        |
| Subordinated debt   | 801                      | 909                          |
| <b>Total Liabilities</b>  | <b>1,477,106</b>         | <b>1,311,773</b>             |
| <i>Commitments and Contingencies (See Note 16)</i>  |                          |                              |
| <i>Stockholders' Equity</i>   |                          |                              |
| Common stock; \$.01 par value; authorized 200,000,000 shares; issued 133,714,786 and 131,457,586 shares; and outstanding 127,831,586 and 130,809,868 shares; in each case, at June 30, 2011 and December 31, 2010, respectively | 1,337                    | 1,315                        |
| Additional paid-in capital  | 462,144                  | 449,754                      |
| Deferred compensation   | 161                      | 276                          |
| Accumulated deficit   | (107,565)                | (103,763)                    |
| Treasury stock, at cost (5,883,200 shares and 647,718 shares at June 30, 2011 and December 31, 2010, respectively)  | (11,940)                 | (1,423)                      |
| <b>Total Stockholders' Equity</b>   | <b>344,137</b>           | <b>346,159</b>               |

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|   |    |           |    |           |
|---|----|-----------|----|-----------|
| Total Liabilities and Stockholders Equity | \$ | 1,821,243 | \$ | 1,657,932 |
|---|----|-----------|----|-----------|

The accompanying notes are an integral part  
of these consolidated financial statements.

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## GLEACHER &amp; COMPANY, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

| (In thousands of dollars)  | Six Months Ended |               |
|--|------------------|---------------|
|  | 2011             | June 30, 2010 |
| <i>Cash flows from operating activities:</i>   |                  |               |
| Net loss   | \$ (3,802)       | \$ (5,448)    |
| <i>Adjustments to reconcile net loss to net cash provided by operating activities:</i> |                  |               |
| Impairment of goodwill and intangible assets   | 14,311           |               |
| Amortization of stock-based compensation   | 9,326            | 23,547        |
| Deferred income taxes  | 2,887            | (9,478)       |
| Gain from bargain purchase ClearPoint Funding, Inc. acquisition                        | (2,330)          |               |
| Amortization of intangible assets  | 1,528            | 2,038         |
| Depreciation and amortization  | 961              | 742           |
| Investment losses/(gains), net   | 318              | 1,512         |
| Amortization of discount of mandatorily redeemable preferred stock                     |                  | 116           |
| Amortization of debt issuance costs  |                  | 84            |
| Loss from disposal of office equipment and leasehold improvements                      |                  | 312           |
| <i>Changes in operating assets and liabilities:</i>                                    |                  |               |
| Cash and securities segregated for regulatory purposes                                 | (3,900)          |               |
| Securities purchased under agreements to resell  | (216,516)        |               |
| Net receivable/payable from/to related parties   | 971              | (2,053)       |
| Net receivable from others   | 394              | 5,372         |
| Financial instruments owned, at fair value   | 86,341           | 24,478        |
| Income taxes receivable/payable, net   | (120)            | (12,512)      |
| Other assets   | 1,081            | (312)         |
| Net payable to brokers, dealers and clearing organizations                             | (76,601)         | 7,168         |
| Securities sold under agreements to repurchase   | 191,449          |               |
| Securities sold, but not yet purchased, at fair value                                  | 41,541           | 12,588        |
| Accounts payable and accrued expenses  | 16               | 1,348         |
| Accrued compensation   | (41,219)         | (42,823)      |
| Drafts payable   | (897)            | (423)         |
| Net cash provided by operating activities  | 5,739            | 6,256         |
| <i>Cash flows from investing activities:</i>   |                  |               |
| Return of capital investments  | 1,772            | 609           |
| Purchases of office equipment and leasehold improvements                               | (1,709)          | (3,776)       |
| ClearPoint acquisition net cash acquired (See Note 11)                                 | 626              |               |
| Capital contribution investments   | (103)            | (433)         |
| Loan receivable held for investment  |                  | (5,000)       |
| Payment to sellers of American Technology Holdings, Inc.                               |                  | (1,382)       |
| Net cash provided by (used in) investing activities                                    | 586              | (9,982)       |
| <i>Cash flows from financing activities:</i>   |                  |               |
| Proceeds from secured borrowings   | 373,039          |               |
| Repayments of secured borrowings   | (357,293)        |               |
| Purchases of treasury stock  | (10,333)         |               |
| Payment for employee tax withholdings on stock-based compensation                      | (5,441)          | (2,732)       |
| Repayment of subordinated debt   | (108)            | (288)         |
| Excess tax benefits related to stock-based compensation                                | 238              | 2,156         |
| Net cash provided by/(used in) by financing activities                                 | 102              | (864)         |
| Increase/(decrease) in cash and cash equivalents                                       | 6,427            | (4,590)       |



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|  |    |        |    |        |
|--|----|--------|----|--------|
| Cash and cash equivalents at beginning of the period |    | 40,009 |    | 24,997 |
| Cash and cash equivalents at the end of the period   | \$ | 46,436 | \$ | 20,407 |

### NON CASH INVESTING AND FINANCING ACTIVITIES

During the six months ended June 30, 2011 and 2010, the Company issued approximately 0.6 million and 0.9 million shares out of treasury stock, net of forfeitures, respectively, for stock-based compensation exercises and vesting and distributions of deferred compensation related to the employee stock trust.

During the six months ended June 30, 2011 and 2010, the Company issued approximately 2.3 million and 3.3 million, respectively, shares of common stock for settlement of stock-based compensation awards.

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The fair value of non-cash assets acquired and liabilities assumed in the ClearPoint Funding, Inc. acquisition on January 3, 2011 were \$51.6 million and \$49.9 million, respectively (See Note 11).

During the six months ended June 30, 2010, Goodwill increased by \$0.8 million in connection with a contingent consideration arrangement related to the acquisition of American Technology Research Holdings, Inc. ( AmTech ) (See Note 16). In addition, during the six months ended June 30, 2010, the Company issued approximately 345,000 shares of common stock to the former shareholders of AmTech in connection with this arrangement.

The accompanying notes are an integral part  
of these consolidated financial statements.

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GLEACHER & COMPANY, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

**I. Basis of Presentation**

Organization and Nature of Business

Gleacher & Company, Inc. (together with its subsidiaries, the Company), is an independent, full service investment bank that provides corporate and institutional clients with strategic, research-based investment opportunities, capital raising, and financial advisory services, including merger and acquisition, restructuring, recapitalization, and strategic alternative analysis, as well as securities brokerage services, and, through the Company's acquisition of ClearPoint Funding, Inc. (ClearPoint), which closed on January 3, 2011, engages in residential mortgage lending. The Company offers a diverse range of products through its Investment Banking, Mortgage Backed/Asset Backed & Rates (MBS/ABS & Rates), Corporate Credit, Equities and ClearPoint divisions. The Company was incorporated under the laws of the State of New York in 1985 and reincorporated in Delaware in the second quarter of 2010. The Company's common stock is traded on the NASDAQ Global Market (NASDAQ) under the symbol GLCH.

The accounting and financial reporting policies of the Company conform to accounting principles generally accepted in the United States of America (GAAP). In preparing the consolidated financial statements in conformity with GAAP management is required to make estimates and assumptions that affect reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. Actual results could be different from these estimates. In the opinion of management, all normal, recurring adjustments necessary for a fair statement of this interim financial information are contained in the accompanying consolidated financial statements. The results for any interim period are not necessarily indicative of those for the full year.

The accompanying consolidated financial statements are presented in accordance with the U.S. Securities and Exchange Commission (SEC) requirements for Quarterly Reports on Form 10-Q and are unaudited. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been omitted. Reference should be made to the Company's audited consolidated financial statements and notes within the Company's Annual Report on Form 10-K for the year ended December 31, 2010 for additional information, including a summary of the Company's significant accounting policies.

Accounting Policy Updates

*Loans*

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The Company accounts for all of ClearPoint's originated residential mortgage loans under the fair value option ( FVO ) as prescribed by Accounting Standards Codification ( ASC ) 820 Fair Value Measurements and Disclosures ( ASC 820 ). Upfront costs and fees related to the loans are immediately recognized. Fees earned are recorded within Fees and other within the Consolidated Statements of Operations. All mortgage loans are sold on a servicing-released basis pursuant to various sale contracts. These contracts include recourse provisions related to loan repurchases if certain prescribed events occur.

Changes in the fair value of mortgage loans and any related hedging instruments are recorded within Principal transactions within the Consolidated Statements of Operations.

### Reclassification

Certain amounts in prior periods have been reclassified to conform to the current year presentation with no impact to previously reported net loss or stockholders' equity.

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GLEACHER & COMPANY, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) No. 2011-05, Presentation of Comprehensive Income ( ASU 2011-05 ), in order to improve the comparability, consistency, and transparency of financial reporting and to increase prominence of items reported in other comprehensive income. The amendments in this ASU include the requirement that all nonowner changes in stockholders' equity be presented in a single continuous statement of comprehensive income or in two separate but consecutive statements, and eliminates the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity. ASU 2011-05 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Since the amendments primarily impact presentation of financial information, the Company does not expect the adoption of ASU 2011-05 to have a material impact on the Company's consolidated financial statements.

In May 2011, the FASB issued ASU No. 2011-04 Fair Value Measurements: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS ( ASU 2011-04 ), in order to develop common requirements for measuring fair value and for disclosing information about fair value measurements in accordance with GAAP and International Financial Reporting Standards ( IFRS ). The amendments in this ASU include clarification of (i) the application of the highest and best use valuation premise concepts and specifies that such concepts are relevant only when measuring the fair value of nonfinancial assets, (ii) the requirement to measure certain instruments classified in stockholders' equity at fair value, such as equity interests issued as consideration in a business combination and (iii) disclosure requirements regarding quantitative information about the unobservable inputs used in a fair value measurement that is categorized within Level 3 of the fair value hierarchy. In addition, ASU 2011-04 changes particular principles or requirements for measuring fair value or for disclosing information about fair value measurements, including (a) measuring the fair value of financial instruments that are managed within a portfolio by permitting entities to measure such financial instruments on a net basis if such entities manage such financial instruments on the basis of their net exposure, (b) clarifying that premiums or discounts related to size as a characteristic of the reporting entity's holding (specifically, a blockage factor) rather than as a characteristic of the asset or liability (for example, a control premium) are not permitted in a fair value measurement and (c) the expansion of disclosures about fair value measurements, including the valuation processes of financial instruments categorized within Level 3 of the fair value hierarchy and sensitivity of the fair value measurement to changes in unobservable inputs and the interrelationships between those unobservable inputs, if any. ASU 2011-04 is effective during interim and annual periods beginning after December 15, 2011. The Company is currently evaluating the impact of ASU 2011-04 on the Company's consolidated financial statements.

In April 2011, the FASB issued ASU No. 2011-03 Transfers and Servicing: Reconsideration of Effective Control for Repurchase Agreements ( ASU 2011-03 ), in order to improve the accounting for repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. The amendments in this ASU remove from the assessment of effective control (i) the criterion requiring the transferor to have the ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee, and (ii) the collateral maintenance implementation guidance related to that criterion. ASU 2011-03 is effective for the first interim or annual period beginning on or after December 15, 2011. The Company does not expect the adoption of ASU 2011-03 to have a material impact on the Company's consolidated financial statements.

In December 2010, the FASB issued ASU No. 2010-29, Disclosure of Supplementary Pro Forma Information for Business Combinations ( ASU 2010-29 ), in order to address diversity in practice about the interpretation of the pro forma revenues and earnings disclosure requirements for

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business combinations. The amendments in this ASU specify that if a public entity presents comparative financial statements, the entity should disclose revenues and earnings of the combined entity as though the business combination(s) that occurred during the current period had occurred as of the beginning of the comparable prior annual period only. ASU 2010-29 is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 31, 2010. The adoption of ASU 2010-29 did not affect the Company's financial condition, results of operations or cash flows. Refer to Note 11 which includes the disclosures as required by this ASU.

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GLEACHER & COMPANY, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

In December 2010, the FASB issued ASU No. 2010-28, *When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts* (ASU 2010-28), in order to address questions about entities with reporting units with zero or negative carrying amounts as some entities concluded that Step 1 of the test is passed in those circumstances because the fair value of their reporting unit will generally be greater than zero. For reporting units with zero or negative carrying amounts, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists, taking into consideration any adverse qualitative factors indicating that an impairment may exist. ASU 2010-28 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The Company does not expect the adoption of ASU 2010-28 to have a material impact on the Company's consolidated financial statements.

In July 2010, the FASB issued ASU No. 2010-20, *New Disclosure Requirements for Finance Receivables and Allowance for Credit Losses* (ASU 2010-20), in order to address concerns about the sufficiency, transparency, and robustness of credit disclosures for finance receivables and the related allowance for credit losses. ASU 2010-20 expands disclosure requirements regarding allowance, charge-off and impairment policies, information about management's credit assessment process, additional quantitative information on impaired loans and rollforward schedules of the allowance for credit losses and other disaggregated information. New disclosures are required for interim and annual periods ending after December 15, 2010, although the disclosures of reporting period activity (e.g., allowance rollforward) are required for interim and annual periods beginning after December 15, 2010. The Company's adoption of ASU 2010-20 did not materially change current disclosures, and since these amended principles require only additional disclosure, the adoption of ASU 2010-20 did not affect the Company's financial condition, results of operations or cash flows.

In March 2010, the FASB issued ASU 2010-11, *Scope Exception Related to Embedded Credit Derivatives* (ASU 2010-11). ASU 2010-11 clarifies and amends the accounting for credit derivatives embedded in beneficial interests in securitized financial assets and eliminates the scope exception for embedded credit derivatives (except for those that are created solely by subordination). Bifurcation and separate recognition may be required for certain beneficial interests that are not accounted for at fair value through earnings. The Company adopted ASU 2010-11 on July 1, 2010. The adoption did not have a material impact on the Company's consolidated financial statements as the majority of the Company's assets are recorded at fair value through earnings.

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## GLEACHER &amp; COMPANY, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

**2. (Loss)/Earnings Per Common Share**

The Company calculates its basic and diluted (loss)/earnings per share in accordance with ASC 260, Earnings Per Share. Basic (loss)/earnings per share is computed based upon weighted-average shares outstanding during the period. Dilutive (loss)/earnings per share is computed consistently with the basic computation while giving effect to all dilutive potential common shares and common share equivalents that were outstanding during the period. The Company uses the treasury stock method to reflect the potential dilutive effect of unvested stock awards, warrants, and unexercised options. The weighted-average shares outstanding were calculated as follows:

| (In thousands)   | Three Months Ended<br>June 30, |         | Six Months Ended<br>June 30, |         |
|--|--------------------------------|---------|------------------------------|---------|
|  | 2011                           | 2010    | 2011                         | 2010    |
| Weighted average shares for basic (loss)/earnings per share  | 124,061                        | 121,228 | 123,825                      | 120,546 |
| Effect of dilutive common share equivalents  |                                |         |                              |         |
| Weighted average shares and dilutive common share equivalents for dilutive (loss)/earnings per share | 124,061                        | 121,228 | 123,825                      | 120,546 |

The Company was in a net loss position for the three and six months ended June 30, 2011 and 2010 and therefore excluded approximately 9.1 million and 4.5 million, respectively, shares underlying stock options and warrants, 8.7 million and 13.5 million, respectively, shares of restricted stock, and 7.1 million and 6.9 million, respectively, shares underlying restricted stock units ( RSUs ) from its computation of dilutive loss per share because they were anti-dilutive.

**3. Cash and Cash Equivalents**

The Company has defined cash equivalents as highly liquid investments, with original maturities of less than 90 days that are not segregated for regulatory purposes or held for sale in the ordinary course of business. At June 30, 2011 and December 31, 2010, cash equivalents were approximately \$11.7 million and \$13.0 million, respectively. Cash and cash equivalents of approximately \$27.8 million and \$36.4 million at June 30, 2011 and December 31, 2010, respectively, were held at one financial institution.

**4. Cash and Securities Segregated for Regulatory Purposes**



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In November 2010, Gleacher & Company Securities, Inc. ( Gleacher Securities ) began self-clearing its trading activities in U.S. government securities (the Rates business ) and is therefore subject to the Customer Protection rules under Rule 15c3-3 promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act ). At June 30, 2011 and December 31, 2010, the Company segregated cash of \$4.0 million and \$0.1 million respectively, in a special reserve bank account for the exclusive benefit of customers pertaining to the results of the activities of the Company s Rates business and outstanding checks issued to customers and vendors when the Company was previously conducting self-clearing in prior years.

### 5. *Resale and Repurchase Agreements*

Transactions involving sales of securities under agreements to repurchase ( repurchase agreements ) or purchases of securities under agreements to resell ( resale agreements ) are presented on a net-by-counterparty basis when a legal right of offset exists. Refer to Note 1 within the footnotes to the consolidated financial statements in the Company s Annual Report on Form 10-K for the year ended December 31, 2010 for additional information related to the Company s accounting policies for these agreements.

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## GLEACHER &amp; COMPANY, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

At June 30, 2011 and December 31, 2010, the fair value of financial instruments received as collateral by the Company that it was permitted to deliver or repledge in connection with resale agreements was approximately \$302.2 million and \$86.8 million, respectively, of which \$189.3 million was repledged in the form of repurchase agreements at June 30, 2011. The Company had no outstanding repurchase agreements at December 31, 2010.

**6. Receivables from and Payables to Brokers, Dealers, and Clearing Organizations**

Amounts receivable from and payable to brokers, dealers and clearing organizations consists of the following:

| <b>(In thousands of dollars)</b>                       | <b>June 30,<br/>2011</b> | <b>December 31,<br/>2010</b> |
|--|--------------------------|------------------------------|
| Deposits with clearing organizations                   | \$ 11,506                | \$ 11,511                    |
| Receivable for unsettled trading activities            | 6,370                    | 8                            |
| Receivable from clearing organizations                 | 2,386                    | 13,218                       |
| Underwriting and syndicate fees receivable             | 333                      | 590                          |
| Commissions receivable                                 | 464                      | 394                          |
| Other  | 728                      |                              |
| <b>Total receivables</b>                               | <b>\$ 21,787</b>         | <b>\$ 25,721</b>             |
| Payable to brokers, dealers and clearing organizations | 1,020,905                | 1,101,440                    |
| <b>Total payables</b>                                  | <b>\$ 1,020,905</b>      | <b>\$ 1,101,440</b>          |

Included within deposits with clearing organizations at June 30, 2011 and December 31, 2010 is a deposit with the Fixed Income Clearing Corporation ( FICC ) of approximately \$10.3 million related to the Company's self clearing activities associated with the Rates business.

Securities transactions are recorded on their trade date as if they had settled. The related amounts receivable and payable for unsettled securities transactions are recorded net, by clearing organization, in Receivables from or Payables to brokers, dealers and clearing organizations in the Consolidated Statements of Financial Condition.

The clearing organizations may re-hypothecate all securities held on behalf of the Company.

**7. Receivables from and Payables to Others**

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Amounts Receivable from and Payable to others consist of the following:

| <b>(In thousands of dollars)</b>                                     | <b>June 30,<br/>2011</b> | <b>December 31,<br/>2010</b> |
|--|--------------------------|------------------------------|
| Interest receivable  | \$ 6,332                 | \$ 7,131                     |
| Principal paydowns Agency mortgage-backed securities                 | 5,404                    | 1,052                        |
| Loan receivable  | 2,958                    |                              |
| Investment banking and advisory fees receivable                      | 1,612                    | 7,755                        |
| Loans and advances   | 703                      | 1,007                        |
| Former stockholder of ClearPoint                                     | 401                      |                              |
| Management fees receivable   | 137                      | 119                          |
| Others   | 913                      | 1,219                        |
| Total receivables from others  | \$ 18,460                | \$ 18,283                    |
| Payable to employees for the Employee Investment Funds (see Note 10) | \$ 981                   | \$ 1,007                     |
| Reserve for loan repurchases - ClearPoint                            | 472                      |                              |
| Customer deposits held in escrow - ClearPoint                        | 400                      |                              |
| Draft payables   | 80                       | 978                          |
| Others   | 831                      | 362                          |
| Total payables to others   | \$ 2,764                 | \$ 2,347                     |

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GLEACHER & COMPANY, INC.

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(Unaudited)

The loan receivable represents the purchase of a floating rate mezzanine loan during the six months ended June 30, 2011, which is collateralized by commercial real estate and matures on October 1, 2011.

In connection with the Company's acquisition of ClearPoint on January 3, 2011 the Company is indemnified for certain matters, including losses resulting from any loan losses with respect to any loans presented to ClearPoint or originated on or prior to January 3, 2011. The Company's receivable for this indemnification claim at June 30, 2011 was approximately \$0.4 million.

The Company maintains a group of zero balance bank accounts which are included in Payable to others in the Consolidated Statements of Financial Condition. Drafts payable represent the balance in these accounts related to outstanding checks that have not yet been presented for payment at the bank. The Company has sufficient funds on deposit to clear these checks, and these funds will be transferred to the zero-balance accounts upon presentment.

**8. Financial Instruments**

Refer to Note 1 within the footnotes to the consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2010 for a detailed discussion of accounting policies related to the Company's securities transactions and derivative financial instruments. In addition, the Company has elected to apply the FVO to all residential mortgage loans originated by ClearPoint.

The Company's financial instruments are recorded within the Consolidated Statements of Financial Condition at fair value. ASC 820 defines fair value as the price that would be received upon the sale of an asset or paid upon the transfer of a liability (*i.e.*, the exit price) in an orderly transaction between market participants at the measurement date and establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect the Company's assumptions about the assumptions market participants would use in pricing the asset or liability based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

Level 1: Quoted prices in active markets that the Company has the ability to access at the reporting date, for identical assets or liabilities. Prices are not adjusted for the effects, if any, of the Company holding a large block relative to the overall trading volume (referred to as a blockage factor).

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Level 2: Directly or indirectly observable prices in active markets for similar assets or liabilities; quoted prices for identical or similar items in markets that are not active; inputs other than quoted prices (e.g., interest rates, yield curves, credit risks, volatilities); or market corroborated inputs.

Level 3: Unobservable inputs that reflect management's own assumptions about the assumptions market participants would make.

The availability of observable inputs can vary from product to product and is affected by a wide variety of factors, including, for example, the type of product, whether the product is new and not yet established in the marketplace, and other characteristics particular to the transaction. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised by management in determining fair value is greatest for instruments categorized in Level 3. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes, the level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

ASC 820 also provides (i) general guidance on determining fair value when markets are inactive including the use of judgment in determining whether a transaction in a dislocated market represents fair value, the inclusion of market participant risk adjustments when an entity significantly adjusts observable market data based on

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(Unaudited)

unobservable inputs, and the degree of reliance to be placed on broker quotes or pricing services as well as (ii) additional guidance for estimating fair value when the volume and level of activity for the asset or liability have significantly declined and guidance on identifying circumstances that indicate a transaction is not orderly.

Fair Valuation Methodology

**Cash Equivalents** These financial assets represent cash in banks or cash invested in highly liquid investments with original maturities less than 90 days that are not segregated for regulatory purposes or held for sale in the ordinary course of business. These investments are valued at par, which represent fair value, and are considered Level 1. Refer to Note 3 herein for additional information.

**Loans** These financial instruments primarily consist of residential mortgage loans originated by ClearPoint, for which the FVO has been elected, and are classified as Level 2 as there is no quoted market for these loans. Fair value is determined utilizing observable market factors and is principally based upon the fair value of the to-be-announced ( TBA ) forward securities market (See Derivatives below).

**Securities Owned/Securities Sold But Not Yet Purchased** These financial instruments primarily consist of investments in fixed income securities, as well as holdings in equity securities.

Fixed income securities include securities traded in active markets, such as U.S. government and federal agency obligations, agency mortgage-backed securities, corporate debt, preferred stock and certain asset and mortgage-backed securities. The on-the-run treasuries are generally traded in active, quoted and highly liquid markets and therefore are generally classified as Level 1. As there is no quoted market for agency mortgage-backed securities, corporate debt, asset and mortgage-backed securities, and certain preferred stock, the Company utilizes observable market factors in determining fair value. These financial instruments are reported as Level 2. In certain circumstances, the Company may utilize unobservable inputs that reflect management's own assumptions about the assumptions market participants would make. These financial assets are reported as Level 3.

In determining fair value for Level 2 financial instruments, management utilizes benchmark yields, reported trades for comparable trade sizes, recent purchases or sales of the financial assets, issuer spreads, benchmark securities, bids and offers. These inputs relate either directly to the financial assets being evaluated or indirectly to a similar security (for example, another bond of the same issuer or a bond of a different issuer in the same industry with similar maturity, terms and conditions). Additionally, for certain mortgage-backed securities, management also considers various characteristics such as the issuer, underlying collateral, prepayment speeds, cash flows and credit ratings.

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In determining fair value for Level 3 financial instruments, management maximizes the use of market observable inputs when available. Management utilizes factors such as bids that were received, recent purchases or sales of the financial assets, spreads to the yield curve on similar offered financial assets, or comparing spreads to similar financial assets that traded and had been priced through an independent pricing source. Management considers these pricing methodologies consistent with assumptions in how other market participants value certain financial assets. These pricing methodologies involve management judgment and lead to a Level 3 classification.

Unrestricted equity securities traded in active markets are valued at quoted market prices and are reported as Level 1. Equity securities that are subject to legal restrictions on transfer are classified as Level 2. When quoted prices are not available, valuation models are applied to these financial assets. These valuation techniques involve some level of management estimation and judgment, the degree of which is dependent on the price transparency for the instruments or market and the instruments' complexity. Accordingly, these financial assets are reported as Level 3.

**Derivatives** These financial instruments primarily consist of TBAs, exchange treasury futures contracts and interest rate lock commitments ( IRLCs ).

TBA and exchange traded treasury futures contracts: In connection with mortgage-backed and U.S. government securities trading, and the mortgage lending activities of ClearPoint, the Company economically hedges certain exposures through the use of TBAs and exchange treasury futures contracts. A TBA is a forward mortgage-backed security whose collateral remains to-be-announced until just prior to the trade settlement. TBAs and exchange traded treasury futures contracts are traded in an active quoted market and therefore generally classified as Level 1.

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## GLEACHER &amp; COMPANY, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

IRLCs: The Company enters into mortgage loan IRLCs in connection with its mortgage lending activities. The fair value of the IRLCs are determined on an individual loan basis and are based on investor pricing tables stratified by product, note rate and term and considers the servicing release premium, expected loan origination fees and costs and loan pricing adjustments specific to each loan. The Company also applies an estimated rate of closure based on historical experience in determining the notional amount of the loans expected to be funded. All of these factors combined results in the classification of the IRLCs as Level 3.

**Investments** These financial assets primarily represent the Company's investment in FA Technology Ventures, L.P. ( FATV or the Partnership ), a venture capital limited partnership which provides early stage growth capital to companies in the information and new energy technology sectors. Valuation techniques applied by FATV GP LLC (the General Partner ) to the underlying portfolio companies predominantly include consideration of comparable market transactions and the use of valuation models to determine the discounted value of estimated future cash flows, adjusted as appropriate for market and/or other risk factors. In addition, certain portfolio companies are valued based upon quoted market prices. This investment is classified as Level 3 as the majority of the valuation techniques involve some level of management estimation and judgment, the degree of which is dependent on the price transparency for the instruments or market and the instruments' complexity.

The following tables summarize the categorization of the financial instruments within the fair value hierarchy including those for which the Company accounts for under the FVO, at June 30, 2011:

| (In thousands of dollars)                      | Assets at Fair Value |              |            | Total        |
|--|----------------------|--------------|------------|--------------|
|  | Level 1              | Level 2      | Level 3    |              |
| Financial instruments owned                    |                      |              |            |              |
| Agency mortgage-backed securities              | \$                   | \$ 992,103   | \$ 8,013   | \$ 1,000,116 |
| U.S. Government and federal agency obligations | 18,123               | 31,416       |            | 49,539       |
| Commercial mortgage-backed securities          |                      | 3,650        | 56,359     | 60,009       |
| Loans  |                      | 63,993       |            | 63,993       |
| Residential mortgage-backed securities         |                      | 3,304        | 27,193     | 30,497       |
| Corporate debt securities                      |                      | 14,225       |            | 14,225       |
| Preferred stock                                |                      | 201          |            | 201          |
| Other debt obligations                         |                      |              | 15,998     | 15,998       |
| Collateralized debt obligations                |                      | 3,568        | 1,424      | 4,992        |
| Equity securities                              | 1,043                |              | 60         | 1,103        |
| Derivatives (1)                                | 498                  |              | 574        | 1,072        |
| Investments                                    |                      |              | 16,098     | 16,098       |
| Total financial assets at fair value           | \$ 19,664            | \$ 1,112,460 | \$ 125,719 | \$ 1,257,843 |

| (In thousands of dollars)                      | Liabilities at Fair Value |           |         | Total      |
|--|---------------------------|-----------|---------|------------|
|  | Level 1                   | Level 2   | Level 3 |            |
| Securities sold but not yet purchased          |                           |           |         |            |
| U.S. Government and federal agency obligations | \$ 133,409                | \$ 11,834 | \$      | \$ 145,243 |



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|   |            |           |    |            |
|---|------------|-----------|----|------------|
| Equity securities                         | 101        |           |    | 101        |
| Corporate debt securities                 |            | 5,498     |    | 5,498      |
| Preferred stock                           |            | 3,158     |    | 3,158      |
| Derivatives (1)                           | 189        |           |    | 189        |
| Total financial liabilities at fair value | \$ 133,699 | \$ 20,490 | \$ | \$ 154,189 |

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(1) Unrealized gains/(losses) relating to derivatives are reported in Securities owned and Securities sold, but not yet purchased, at fair value in the Consolidated Statements of Financial Condition.

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GLEACHER & COMPANY, INC.

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(Unaudited)

Included below is a discussion of the characteristics of the Company's Level 2 and Level 3 holdings at June 30, 2011. Unless otherwise stated, fair value of Level 2 assets are determined based upon observable third party information including recent trading activity, broker quotes and other relevant market data as noted above. Fair value for Level 3 assets are based predominantly on management's own assumptions about the assumptions market participants would make. The Company generally does not utilize internally developed valuation models to determine fair value during the relevant reporting periods for any holdings other than certain underlying portfolio companies comprising the Company's investment in FATV.

The Company's agency mortgage-backed securities positions classified as Level 2, of approximately \$992.1 million, have a weighted average loan size of approximately \$0.2 million paying interest of 5.8%, with a weighted average FICO score of 722. This portfolio has a weighted average coupon remitting payment of 5.3% and has a weighted average annualized constant prepayment rate of approximately 17.1%. Fair value is determined through a combination of matrix pricing as well as the information noted in the preceding paragraph.

The Company's net Level 2 U.S. Government and federal agency obligations of approximately \$19.6 million have a weighted average coupon of 3.6% and a weighted average maturity of 2019.

The Company's Level 2 commercial mortgage backed securities of approximately \$3.7 million are primarily subordinated tranches, have a weighted average credit rating of B and a weighted average issuance year of 2007.

The Company's Level 2 loans of approximately \$64.0 million (unpaid principal of approximately \$61.8 million), which are related to the mortgage lending activities of ClearPoint and for which the FVO has been elected, have a weighted average loan size of approximately \$0.3 million and have a weighted average coupon remitting payment of 4.6%. Unrealized losses arising from fair value changes of approximately (\$0.3) million have been recorded within Principal transactions within the Consolidated Statements of Operations as of June 30, 2011. There are no loans 90 days or more past due and no loans are in non-accrual status. The loans are underwritten using standards prescribed by conventional mortgage lenders and loan buyers such as the Federal National Mortgage Association and Federal Home Loan Mortgage Corporation.

The Company's Level 2 non-agency residential mortgage backed securities of approximately \$3.3 million are primarily senior tranches and have a weighted average credit rating of BB.

The Company's net holdings of corporate debt securities classified as Level 2 of approximately \$8.7 million have a weighted average credit rating of B, have a weighted average issuance year of 2006 and a weighted average maturity of 2024.

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The Company's net preferred stock holdings classified as Level 2 of approximately (\$3.0) million have a weighted average coupon of 7.65% and a weighted average credit rating of BBB.

The Company's Level 2 collateralized debt obligations of \$3.6 million is comprised of commercial real estate, with a weighted average vintage of 2007, has a weighted average credit rating of B.

The Company's Level 3 agency mortgage-backed securities positions of approximately \$8.0 million have a weighted average loan size of \$0.1 million paying interest of 6.6%, with a weighted average coupon of 14.8% and a weighted average vintage of 2006.

The Company's portfolio of Level 3 commercial mortgage backed securities of approximately \$56.4 million are primarily mezzanine, have a weighted average credit rating of B and a weighted average issuance year of 2006.

The Company's portfolio of Level 3 non-agency residential mortgage backed securities of approximately \$27.2 million are primarily senior tranches, have a weighted average credit rating of A, and have experienced on average, a weighted average default rate of 4.5% and 58.3% severity.

The Company's other debt obligations reported as Level 3 include holdings of approximately \$16.0 million of asset backed securities, paying interest of 4.0%, with a weighted average credit rating of A and a weighted average vintage of 2007.

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GLEACHER & COMPANY, INC.

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(Unaudited)

The Company's Level 3 collateralized debt obligations of \$1.4 million is comprised of commercial real estate, with a weighted average vintage of 2005, has a weighted average credit rating of CCC and have on average 12.3% subordination.

IRLCs are reported as derivatives and are classified as Level 3. Refer to Note 9 herein for additional information.

The Company's Investments of approximately \$16.1 million classified as Level 3, include the Company's investment in FATV of approximately \$14.8 million. FATV invests primarily in equity securities of closely held private companies and also invests in equity securities in public companies which are generally subject to legal restrictions on transfer. FATV is comprised of 24 holdings and fair value is determined based upon the nature of the underlying holdings. The Company has classified its entire investment as Level 3, as FATV is predominantly comprised of private companies.

- Investments in privately held companies: Valuation techniques include consideration of comparable market transactions (market approach) and utilizing the discounted value of estimated future cash flows, as adjusted for market and/or other risk factors. Relevant inputs include the current financial position and current and projected operating results of the issuer, sales prices of recent public or private transactions in the same or similar securities, significant recent events affecting the issuer, the price paid by FATV to acquire the asset, subsequent rounds of financing, completed or pending third-party transactions in the underlying investment or comparable issuers, recapitalizations and other transactions across the capital structure.

- Investments in public companies: Valuation is based on quoted market prices in active markets and adjusted as a result of legal restrictions on transfer, where applicable.

The Company's Level 3 Investments also include approximately \$1.3 million as a result of the consolidation of the Employee Investment Funds ( EIF ). For additional information regarding the Company's Investments, refer to Note 10 herein.

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## GLEACHER &amp; COMPANY, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

The following tables summarize the categorization of the financial instruments within the fair value hierarchy at December 31, 2010:

| (In thousands of dollars)                      | Assets at Fair Value |              |            | Total        |
|--|----------------------|--------------|------------|--------------|
|  | Level 1              | Level 2      | Level 3    |              |
| Financial instruments owned                    |                      |              |            |              |
| Agency mortgage-backed securities              | \$                   | \$ 1,084,576 | \$ 806     | \$ 1,085,382 |
| Commercial mortgage-backed securities          |                      |              | 46,571     | 46,571       |
| U.S. Government and federal agency obligations | 35                   | 47,546       |            | 47,581       |
| Other debt obligations                         |                      | 8,200        | 5,843      | 14,043       |
| Preferred stock                                |                      | 12,381       |            | 12,381       |
| Corporate debt securities                      |                      | 4,037        |            | 4,037        |
| Residential mortgage-backed securities         |                      |              | 33,604     | 33,604       |
| Collateralized debt obligations                |                      |              | 23,235     | 23,235       |
| Equity securities                              | 14,212               |              | 60         | 14,272       |
| Derivatives (1)                                | 137                  |              |            | 137          |
| Investments                                    |                      |              | 18,084     | 18,084       |
| Total financial assets at fair value           | \$ 14,384            | \$ 1,156,740 | \$ 128,203 | \$ 1,299,327 |

| (In thousands of dollars)                      | Liabilities at Fair Value |          |         | Total      |
|--|---------------------------|----------|---------|------------|
|  | Level 1                   | Level 2  | Level 3 |            |
| Securities sold but not yet purchased          |                           |          |         |            |
| U.S. Government and federal agency obligations | \$ 92,971                 | \$       | \$      | \$ 92,971  |
| Preferred stock                                |                           | 2,469    |         | 2,469      |
| Corporate debt securities                      |                           | 1,004    |         | 1,004      |
| Equity securities                              | 13,148                    |          |         | 13,148     |
| Derivatives (1)                                | 2,683                     |          |         | 2,683      |
| Total financial liabilities at fair value      | \$ 108,802                | \$ 3,473 | \$      | \$ 112,275 |

(1) Fair value of derivatives are reported in Securities owned and Securities sold, but not yet purchased, at fair value in the Consolidated Statements of Financial Condition.

The Company reviews its financial instrument classification on a quarterly basis. As the observability and strength of valuation attributes change, reclassifications of certain financial assets or liabilities may occur between levels. The Company's policy is to utilize an end-of-period convention for determining transfers in or out of Levels 1, 2 and 3. During the three and six months ended June 30, 2011, there were no transfers between Levels 1 and 2.



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## GLEACHER &amp; COMPANY, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

The following table summarizes the changes in the Company's Level 3 financial instruments for the three months ended June 30, 2011:

| (In thousands)                         | Balance at March 31, 2011 | Total gains or (losses) (realized and unrealized) (1) | Purchases  | Sales        | Settlements | Transfers in and/or out of Level 3 (2) | Balance at June 30, 2011 | Changes in unrealized gains/(losses) on Level 3 assets still held at the reporting date (1) |
|--|---------------------------|---|------------|--------------|-------------|--|--------------------------|---|
| Commercial mortgage-backed securities  | \$ 68,247                 | \$ (3,726)  | \$ 62,245  | \$ (66,737)  | \$ (20)     | \$ (3,650)                             | \$ 56,359                | \$ (4,923)  |
| Residential mortgage-backed securities | 32,385                    | (575)   | 10,831     | (13,731)     | (1,717)     |  | 27,193                   | 101   |
| Other debt obligations                 | 9,555                     | 52  | 22,857     | (16,186)     | (280)       |  | 15,998                   | 13  |
| Agency mortgage-backed securities      | 2,430                     | (168)   | 8,043      | (2,292)      |             |  | 8,013                    | (146)   |
| Collateralized debt obligations        | 7,135                     | 6,566   | 3,766      | (12,463)     | (12)        | (3,568)                                | 1,424                    | (63)  |
| Equities                               | 60                        |   |            |              |             |  | 60                       |   |
| Investments                            | 16,883                    | (785)   |            |              |             |  | 16,098                   | (149)   |
| Derivatives                            | 685                       | 574   |            |              | (685)       |  | 574                      | 574   |
| Total                                  | \$ 137,380                | \$ 1,938  | \$ 107,742 | \$ (111,409) | \$ (2,714)  | \$ (7,218)                             | \$ 125,719               | \$ (4,593)  |

(1) Realized and unrealized gains/(losses) are reported in Principal transactions in the Consolidated Statements of Operations.

(2) During the three months ended June 30, 2011, the Company transferred approximately \$3.7 million of commercial mortgage backed securities and approximately \$3.6 million of collateralized debt obligations from Level 3 to Level 2 due to price discovery resulting from Company trading activity occurring in close proximity to June 30, 2011.

The following table summarizes the changes in the Company's Level 3 financial instruments for the three months ended June 30, 2010:

| (In thousands) | Balance at March 31, 2010 | Total gains or (losses) (realized and unrealized) (1) | Purchases | Sales | Settlements | Transfers in and/or out of Level 3 (2) | Balance at June 30, 2010 | Changes in unrealized gains/(losses) on Level 3 assets still held at the |
|----------------|---------------------------|---|-----------|-------|-------------|--|--------------------------|--|
|----------------|---------------------------|---|-----------|-------|-------------|--|--------------------------|--|

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|  | reporting date (1) |        |    |         |    |         |    |          |    |         |    |         |    |         |
|--|--------------------|--------|----|---------|----|---------|----|----------|----|---------|----|---------|----|---------|
| Commercial mortgage-backed securities  | \$                 | 48,859 | \$ | 5,078   | \$ | 74,331  | \$ | (72,391) | \$ | (14)    | \$ | 55,863  | \$ | (942)   |
| Other debt obligations                 |                    | 5,612  |    | 7       |    | 13,742  |    | (3,813)  |    | (1,715) |    | 13,833  |    | 3       |
| Residential mortgage-backed securities |                    | 9,081  |    | 248     |    | 8,241   |    | (7,418)  |    | (268)   |    | 9,884   |    | (295)   |
| Agency mortgage-backed securities      |                    | 4,759  |    | 1,350   |    | 3,377   |    | (5,805)  |    | (24)    |    | 3,657   |    | (154)   |
| Collateralized debt obligations        |                    | 1,604  |    | 14      |    | 4,971   |    | (4,607)  |    |         |    | 1,982   |    | 14      |
| Corporate debt securities              |                    | 1      |    |         |    |         |    |          |    |         |    | 1       |    |         |
| Equities                               |                    | 60     |    |         |    |         |    |          |    |         |    | 60      |    |         |
| Investments                            |                    | 19,756 |    | (1,664) |    | 155     |    | (609)    |    |         |    | 17,638  |    | (2,118) |
| Total                                  | \$                 | 89,732 | \$ | 5,033   | \$ | 104,817 | \$ | (94,643) | \$ | (2,021) | \$ | 102,918 | \$ | (3,492) |

(1) Realized and unrealized gains/(losses) are reported in Principal transactions in the Consolidated Statements of Operations.

(2)