

Cowen Group, Inc.
Form 10-K/A
July 17, 2007

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

Form 10-K/A

**Amendment No. 1
Annual Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934**

For the fiscal year ended: **December 31,**
2006

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 10020
(646) 562-1000**

(Address, including zip code, and telephone number, including area code, of registrant's principal executive office)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Exchange on Which Registered
Common Stock, par value \$0.01 per share	The Nasdaq Global Market

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes No

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

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

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

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Large accelerated filer Accelerated filer Non-accelerated filer

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

The aggregate market value of the common stock of the registrant held by non-affiliates of the registrant on December 29, 2006, the last business day of the registrant's fiscal year was: \$272,835,000.

As of March 23, 2007 there were 15,980,077 shares of the registrant's common stock outstanding.

Documents incorporated by reference:

Part III of this Annual Report on Form 10-K incorporates by reference information (to the extent specific sections are referred to herein) from the Registrant's Proxy Statement for its 2007 Annual Meeting of Stockholders.

EXPLANATORY NOTE

Cowen Group, Inc. is filing this Amendment No. 1 on Form 10-K/A to its Annual Report on Form 10-K for the fiscal year ended December 31, 2006 (the Original Form 10-K), to correct a typographical error in the content of Note 2 to the Consolidated Financial Statements contained in Item 8. Financial Statements and Supplementary Data. The following language intended to be included immediately following the paragraph captioned Legal Reserves on page F-11 of the Original Form 10-K in Note 2 Summary of Significant Accounting Policies was inadvertently omitted:

Revenue recognition

Investment Banking

Investment banking revenues include underwriting fees, private placement fees, strategic advisory fees and financial advisory fees. Underwriting revenues are earned in securities offerings in which the Company acts as an underwriter and include management fees, sales concessions and underwriting fees. Management fees are recorded on the offering date, sales concessions on settlement date and underwriting fees are recognized net of related syndicate expenses, at the time the underwriting is complete and the income is reasonably determinable. 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 reduces 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 90 days following the closing of the transaction.

Private placement fees, including warrants received in certain private placement transactions, are recorded on the closing date of the placement. Strategic advisory and financial advisory fees are recorded when the services to be performed and/or the transactions are substantially completed, and fees are determinable and collection is reasonably assured. Expenses associated with these transactions are recognized, net of client reimbursements, when the related revenue is recognized or the engagement is otherwise concluded.

No other changes are being made to the Financial Statements or other information in Item 8. In addition, no changes are being made pursuant to this amendment to any other item of our Form 10-K other than the updating of the Exhibits to include updated Certifications of the Chief Executive and Chief Financial Officers. In accordance with the SEC's rules applicable to the filing of amendments to Form 10-K, we are including in this amendment the complete text of Item 8.

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of
Cowen Group, Inc.

We have audited the accompanying consolidated statements of financial condition of Cowen Group, Inc. and subsidiaries (the Company) as of December 31, 2006 and 2005, and the related consolidated statements of operations, stockholders' group equity, and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Cowen Group, Inc. and subsidiaries at December 31, 2006 and 2005, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2006, in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young LLP

New York, New York
March 28, 2007

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Cowen Group, Inc.**Consolidated Statements of Financial Condition**

As of December 31, 2006 and 2005

	2006 (in thousands)	2005
Assets		
Cash and cash equivalents	\$ 185,042	\$ 2,150
Restricted cash pursuant to escrow agreement	52,099	
Cash segregated under Federal or other regulations		1,107
Securities owned, at fair value	259,921	220,086
Securities purchased under agreements to resell with related party		410,981
Receivable from brokers , dealers and clearing brokers (see Note 12, Related Party Disclosures)	83,564	25,849
Corporate finance and syndicate receivables	27,022	16,120
Insurance claims receivable		5,316
Due from affiliates	1,367	568
Exchange memberships , cost (fair value of \$2,561 and \$27,019 at December 31, 2006 and 2005, respectively)	812	8,167
Furniture, fixtures , equipment and leasehold improvements (net of accumulated depreciation and amortization of \$6,001 and \$3,632 at December 31, 2006 and 2005, respectively)	12,629	3,223
Goodwill	50,000	50,000
Other assets	11,982	41,772
Total assets	\$ 684,438	\$ 785,339
Liabilities and Stockholders / Group Equity		
Liabilities		
Bank overdrafts	\$ 1,858	\$ 1,581
Securities sold , not yet purchased, at fair value	251,580	143,223
Payable to brokers , dealers and clearing brokers (see Note 12, Related Party Transactions)	29,918	15,376
Employee compensation and benefits payable	116,021	156,924
Legal reserves and legal expenses payable (see Note 10, Commitments , Contingencies and Guarantees)	53,167	78,732
Accounts payable, accrued expenses and other liabilities (see Note 12, Related Party Transactions)	13,766	15,552
Total liabilities	466,310	411,388
Stockholders / Group 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, 15,000,000 shares issued and 14,988,472 shares outstanding (including 2,088,472 restricted shares)	129	
Additional paid-in capital	215,240	
Retained earnings	2,759	
Less common stock held in treasury, at cost: 11,528 shares at December 31, 2006 and -0- shares at December 31, 2005		
Group equity		373,951
Total stockholders equity (2006)/group equity (2005)	218,128	373,951
Total liabilities and stockholders /group equity	\$ 684,438	\$ 785,339

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

Cowen Group, Inc.**Consolidated Statements of Operations****For the Years Ended December 31, 2006, 2005 and 2004**

	2006 (in thousands)	2005	2004
Revenues			
Investment banking	\$ 164,342	\$ 126,253	\$ 113,795
Commissions	93,346	93,450	99,669
Principal transactions	64,376	52,250	64,519
Interest and dividend income (see Note 12, Related Party Transaction)	17,766	16,990	9,504
Other	5,137	5,348	5,574
Total revenues	344,967	294,291	293,061
Expenses			
Employee compensation and benefits	215,707	172,128	170,546
Floor brokerage and trade execution (see Note 12, Related Party Transactions)	11,838	10,025	16,136
Service fees, net (see Note 12, Related Party Transactions)	16,961	18,446	24,389
Communications	24,289	22,985	19,812
Occupancy and equipment (see Note 12, Related Party Transactions)	17,772	15,071	14,633
Marketing and business development	12,581	12,382	12,087
Litigation and related expense, net of recoveries	4,411	6,930	(44,835)
Depreciation and amortization	2,369	2,140	2,409
Interest	980	1,178	825
Other	21,443	20,691	18,077
Total expenses	328,351	281,976	234,079
Operating income	16,616	12,315	58,982
Gain (loss) on exchange memberships	25,843	918	(1,993)
Income before income taxes	42,459	13,233	56,989
Provision for income taxes	4,548	1,152	1,877
Net income	\$ 37,911	\$ 12,081	\$ 55,112
Weighted average common shares outstanding:			
Basic	12,903	12,900	12,900
Diluted	12,966	12,900	12,900
Earnings per share:			
Basic	\$ 2.94	\$ 0.94	\$ 4.27
Diluted	\$ 2.92	\$ 0.94	\$ 4.27

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

Cowen Group, Inc.

Consolidated Statements of Changes in Stockholders / Group Equity

For the Years Ended December 31, 2006, 2005 and 2004

	Common Shares Outstanding (amounts in thousands, except share amounts)	Common Stock	Additional Paid-in Capital	Retained Earnings	Group Equity	Stockholders / Group Equity
Balance, December 31, 2003		\$	\$	\$	\$ 262,943	\$ 262,943
Net income					55,112	55,112
Change in liability related to the retail brokerage business not conducted by the Company (see Note 1)					(46,829)	(46,829)
Capital contribution					82,252	82,252
Balance, December 31, 2004					353,478	353,478
Net income					12,081	12,081
Change in liability related to the retail brokerage business not conducted by the Company (see Note 1)					5,696	5,696
Capital contribution					2,696	2,696
Balance, December 31, 2005					373,951	373,951
Net income, pre IPO					35,152	35,152
Change in liability related to the retail brokerage business not conducted by the Company (see Note 1)					(1,817)	(1,817)
Capital contributions					6,843	6,843
Capital distributions (see Note 1)					(207,129)	(207,129)
Underwriting discount received in connection with the IPO (see Note 1)			3,020			3,020
Net income, post IPO				2,759		2,759
Stock issuance (see Note 1, includes 2,100,000 of restricted shares)	15,000,000	129	206,871		(207,000)	
Amortization of share based compensation			5,349			5,349
Forfeitures of restricted stock awards	(11,528)					
Balance, December 31, 2006	14,988,472	\$ 129	\$ 215,240	\$ 2,759	\$	\$ 218,128

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

Cowen Group, Inc.

Consolidated Statements of Cash Flows

For the Years Ended December 31, 2006, 2005 and 2004

	2006 (in thousands)	2005	2004
Cash flows from operating activities			
Net income	\$ 37,911	\$ 12,081	\$ 55,112
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Exchange membership impairment			1,980
Gain on sale of exchange membership	(24,827)	108	
Share-based compensation	5,440	105	383
Depreciation and amortization	2,369	2,140	2,409
Income taxes	(832)	1,152	1,877
(Increase) decrease in operating assets :			
Restricted cash pursuant to escrow agreement	(52,099)		
Cash segregated under federal and other regulations	1,107	(502)	(605)
Securities owned, at fair value	(39,835)	(29,768)	16,967
Securities purchased under agreement to resell	410,981	34,353	(158,604)
Receivable from brokers, dealers and clearing brokers	(57,715)	4,977	80,438
Corporate finance and syndicate receivables	(10,902)	(4,556)	1,347
Exchange memberships		(114)	
Insurance claims receivable	5,316	23,184	(28,500)
Due from affiliates	(799)	10,562	(11,008)
Other assets	30,811	(4,668)	(83)
Increase (decrease) in operating liabilities :			
Bank overdrafts	277	(1,474)	3,055
Securities sold, not yet purchased, at fair value	108,357	16,084	2,421
Payable to brokers , dealers and clearing brokers	14,542	612	(6,701)
Employee compensation and benefits payable	(40,903)	3,491	1,080
Legal reserves and legal expenses payable	2,206	(25,342)	(21,171)
Accounts payable, accrued expenses and other liabilities	(2,844)	2,511	8,385
Net cash provided by (used in) operating activities	388,561	44,936	(51,218)
Cash flows from investing activities			
Proceeds from sale of exchange memberships		148	
Proceeds from the sale of fixed assets		22	891
Purchase of fixed assets from Société Générale	(228)		
Purchase of fixed assets	(11,547)	(705)	(5,923)
Net cash used in investing activities	(11,775)	(535)	(5,032)
Cash flows from financing activities			
Payments related to the Retail brokerage business not conducted by the Company (see Note 1)			
Capital distributions	(180,332)	(45,670)	(22,064)
Capital contributions, net	14,209	1,439	79,991
Net cash (used in) provided by financing activities	(193,894)	(44,231)	57,927
Net increase in cash	182,892	170	1,677
Cash and Cash Equivalents			
Beginning of year	2,150	1,980	303
End of year	\$ 185,042	\$ 2,150	\$ 1,980
Supplemental disclosure of cash flow information			
Cash paid during the year for:			
Interest	\$ 801	\$ 1,157	\$ 829
Income taxes	3,351		
Supplemental disclosure of non-cash flow information			
Exchange membership demutualization	\$	\$ 774	\$
Transfer to SGASH of consideration of NYSE merger with Archipelago	32,182		
Accrued capital withdrawal payable to Société Générale	1,965		

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

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Cowen Group, Inc.
Notes to 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). SGASH is a wholly-owned subsidiary of SG Americas, Inc. (SGAI), which in turn is a wholly-owned subsidiary of Société Générale. The Company is operated and managed on an integrated basis as a single operating segment and primarily provides research, institutional sales and trading and investment banking services to its clients.

Cowen and Company, LLC (Cowen), a Delaware single member limited liability company, is the United States (U.S.) broker-dealer subsidiary of Cowen Group, Inc. Cowen is a full-service investment banking and securities brokerage firm focused on the emerging growth sectors of healthcare, technology, media and telecommunications, and consumer, operating primarily in the United States. Cowen's predecessor was SG Cowen Securities Corporation (SGCSC). On April 23, 2004, Société Générale reorganized SGCSC into two separate affiliated single member limited liability broker-dealers: SG Cowen & Co., LLC (which subsequently was renamed as Cowen and Company, LLC) and SG Americas Securities, LLC (SGAS). Cowen clears its securities transactions on a fully disclosed basis through its clearing broker, SGAS, 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, and consumer, primarily in Europe. CIL's predecessors were SG London Securities Limited and SG London Branch.

Cowen Capital Partners, LLC (Cowen Capital), a Delaware single member limited liability company, is the wholly-owned direct investment private equity subsidiary of the Company. Cowen Capital focuses on partnering with management teams to 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 (See Note 11 for further discussion of the Separation Agreement), the amount of this distribution is subject to adjustment based on a final review of the Company's separation from Société Générale. The Company has accrued approximately \$2.0 million as a capital distribution to Société Générale related to this final review. SGASH received all the proceeds from the issuance of 11,517,392 shares. 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.

Basis of Presentation

Management believes that these consolidated financial statements include normally recurring adjustments and accruals necessary for a fair presentation of the Consolidated Statements of Financial Condition, Operations, Cash Flows, and Changes in Stockholders' / Group Equity for the periods presented.

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Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

1. Organization and Basis of Presentation (continued)

The consolidated financial statements for all periods prior to July 13, 2006 include the carve-out accounts of Cowen and the carve-out accounts of SG London Branch, the predecessor of CIL, in each case using the historical basis of accounting for the results of operations, assets and liabilities of the businesses that currently constitute Cowen and CIL. The consolidated financial information included herein may not necessarily be indicative of the Company's results of operations, financial condition and cash flows in the future or what its results of operations, financial condition and cash flows would have been had the Company been a stand-alone company during the entire periods presented.

The Consolidated Statements of Operations do not include litigation expenses incurred by Cowen in connection with the Gruttadauria litigation and other legal matters related to the retail brokerage business of SGCSC, which was sold in October 2000, and is not part of the businesses currently conducted by the Company. The legal reserves related to this matter are included in legal reserves and legal expenses payable in the Consolidated Statements of Financial Condition. Before becoming a public company, payments related to the Gruttadauria litigation were included in the Consolidated Statements of Cash Flows as financing activities because the Company was a wholly-owned subsidiary of Société Générale. After becoming a public company, these payments are 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.

The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany transactions have been eliminated upon consolidation.

2. Summary of Significant Accounting Policies

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. 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. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Securities owned and securities sold, not yet purchased and derivative financial instruments including futures, options and warrant positions are stated at fair value, with related changes in unrealized appreciation or depreciation reflected in principal transactions in the Consolidated Statements of Operations. Financial instruments carried at contract amounts include receivable from brokers, dealers and clearing brokers, payable to brokers, dealers and clearing brokers, securities purchased under agreements to resell and corporate finance and syndicate receivables.

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

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 and, therefore, do not have readily determinable fair values, 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.

Securities Purchased Under Agreements to Resell

Securities purchased under agreements to resell generally are collateralized by U.S. government and agency obligations, are treated as collateralized financing transactions and are carried at amounts at which the securities will be resold plus accrued interest. It is the Company's policy to take possession or control of securities purchased under agreements to resell. The Company requires the fair value of the collateral to be equal to or in excess of the principal amount loaned under the resale agreements. The Company minimizes credit risk associated with these activities by monitoring credit exposure and collateral values on a daily basis and requiring additional collateral or principle to be deposited or returned when deemed appropriate.

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 December 31, 2006 and 2005.

Furniture, Fixtures, Equipment, and Leasehold Improvements

Furniture, fixtures, equipment, and 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 which range from one to nine years.

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* (FAS 142), goodwill is not amortized. The Company monitors goodwill annually or more frequently if events or circumstances indicate a possible impairment.

Cowen Group, Inc.**Notes to Consolidated Financial Statements (continued)****2. Summary of Significant Accounting Policies (continued)**

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 FAS 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, revenue 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.

Exchange Memberships

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

Stock-Based Compensation***Stock-based awards issued by Société Générale***

On January 1, 2006, the Company adopted SFAS No. 123(R), *Share-Based Payment* (FAS 123R). Prior to January 1, 2006, the Company accounted for stock-based awards issued by Société Générale under the intrinsic value method, which followed the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25), and related Interpretations, which requires that compensation be measured by the quoted market price of stock at the measurement date less the amount that the employee is required to pay. The Company had recognized compensation expense for these awards of \$0.1 and \$0.4 million for the years ended December 31, 2005 and 2004, respectively.

The following table illustrates the effect on net income if the Company had applied the fair value recognition provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation*, to its stock incentive plans for the years ended December 31, 2005 and 2004. The compensation expense for stock options disclosed under the fair value method is not shown net of any tax effects as the Company has not taken any tax deductions for awards exercised by its employees.

	2005	2004
	(in thousands)	
Net income, as reported	\$ 12,081	\$ 55,112
Add: Stock-based employee compensation expense included in reported net income	105	383
Deduct: Total stock-based employee compensation expense determined under fair value method for all awards	(342)	(817)
Pro forma net income	\$ 11,844	\$ 54,678

When the Company adopted FAS 123R on January 1, 2006, the modified prospective transition method was used. This method requires measurement of compensation cost for all stock-based awards at fair value on the date of grant and recognition of compensation over the service period for awards expected to vest. The fair value of stock-based compensation is consistent with the valuation techniques previously utilized for options in footnote disclosures required under SFAS No. 123, *Accounting for Stock-*

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Based Compensation, as amended by SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*. Such value is recognized as an expense over the service period, net of estimated forfeitures, using the straight-line method. All unvested stock-based awards vested on April 22, 2006, and accordingly, estimated forfeitures with respect to these awards were deemed to be zero. Therefore, no adjustment to reflect the net cumulative impact of estimating forfeitures in the determination of period expense was deemed necessary in the preparation of these Consolidated Financial Statements, nor will any such future expense be deemed necessary. The Company recognized \$0.1 million in compensation expense for these awards for the year ended December 31, 2006.

Stock-based awards issued by Cowen Group, Inc.

Upon becoming a public company, the Company established a stock-based compensation plan. Awards related to this plan are accounted for under the recognition and measurement provisions of FAS 123R. See Note 14 for a description of these awards.

Legal Reserves

The Company estimates potential losses that may arise out of legal and regulatory proceedings and recognizes liabilities for such contingencies to the extent such losses are probable and the amount of loss can be reasonably estimated. These amounts are reported in litigation and related costs, net of recoveries, on the Consolidated Statements of Operations. The Consolidated Statements of Operations do not include litigation expenses incurred by the Company in connection with the Gruttadauria litigation matter (see Notes 10 and 11) as it relates to a business conducted by SGCSC that was sold in October 2000. As the successor of the named party in the litigation the Company recognizes the legal reserve related to this matter in the Consolidated Statements of Financial Condition.

Revenue recognition

Investment Banking

Investment banking revenues include underwriting fees, private placement fees, strategic advisory fees and financial advisory fees. Underwriting revenues are earned in securities offerings in which the Company acts as an underwriter and include management fees, sales concessions and underwriting fees. Management fees are recorded on the offering date, sales concessions on settlement date and underwriting fees are recognized net of related syndicate expenses, at the time the underwriting is complete and the income is reasonably determinable. 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 reduces 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 90 days following the closing of the transaction.

Private placement fees, including warrants received in certain private placement transactions, are recorded on the closing date of the placement. Strategic advisory and financial advisory fees are recorded when the services to be performed and/or the transactions are substantially completed, and fees are determinable and collection is reasonably assured. Expenses associated with these transactions are recognized, net of client reimbursements, when the related revenue is recognized or the engagement is otherwise concluded.

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

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

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 transactions revenue includes net trading gains and losses from the Company's market-making activities in over-the-counter common equity securities, convertible securities and options, from commitment of capital to facilitate customer trades for listed stocks and from proprietary trading activities. In certain cases, the Company provides liquidity to clients buying or selling blocks of shares 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.

The Company's securities and derivative financial instruments are recorded at fair value. Changes in net unrealized gains or losses are reflected in principal transactions in the Consolidated Statements of Operations.

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Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Derivative Financial Instruments

The Company uses U.S. Treasury futures and options to economically hedge proprietary trading positions. In addition, the Company uses options for proprietary trading activities. Futures contracts are executed on an exchange, and cash settlement is made on a daily basis for market movements. Options are stated at fair value which is based on current market prices. Realized and unrealized gains and losses associated with futures transactions and options are included in principal transactions on the Consolidated Statements of Operations. The fair value of futures contracts and required margin deposits are included in receivable from brokers, dealers and clearing brokers on the Consolidated Statements of Financial Condition and were de minimis at December 31, 2006 and 2005. The Company also holds warrants, which are reported at fair value.

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 year. 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.

Leases

Leases are accounted for under Statement of Financial Accounting Standards (SFAS) No. 13, *Accounting for Leases*. All of our leases are classified as operating leases.

Foreign Currency Translation

The Company's assets and liabilities denominated in foreign currencies are translated based on the rate of exchange prevailing at each statement of financial condition date. Revenues and expenses are translated at the average exchange rates prevailing during the periods. Gains of \$0.3 million on foreign currency transactions are included in other revenue in the Consolidated Statements of Operations.

Income Taxes

The taxable results of the Company's U.S. operations were historically included in the consolidated income tax returns of SGAI through the IPO date. The tax results of the Company's U.K. operations were historically included in the tax returns of SG London Branch through April 30, 2006. For the period May 1, 2006 through December 31, 2006, the U.K. operations are included in CIL's U.K. tax filing. The U.S. impact of CIL's operations is included in the SGAI consolidated tax returns for the period May 1, 2006 through the IPO date and in the Company's tax filings post-IPO.

The income tax provision reflected in the Consolidated Statements of Operations is presented as if the Company operated on a stand-alone basis for all periods presented, 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 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.

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

3. Accounting Developments

In February 2007, the FASB issued Statement of Financial Accounting Standard No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (FAS 159). FAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. FAS 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact, if any, of implementing FAS 159.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurement. This statement shall be effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Earlier application is encouraged, provided that the reporting entity has not yet issued financial statements for that fiscal year, including any financial statements for an interim period within that fiscal year. The provisions of this statement should be applied prospectively as of the beginning of the fiscal year in which this statement is initially applied, except in some circumstances where the statement shall be applied retrospectively. The Company is currently evaluating the impact, if any, that the adoption of FAS 157 will have on the Company's Consolidated Financial Statements.

In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements* (SAB 108), which provides guidance on quantifying and evaluating the materiality of unrecorded prior year misstatements. The SEC staff indicates that an entity should quantify the impact of correcting all misstatements, including both the carryover and reversing effects of prior year misstatements, on the current year financial statements. Companies may choose to restate their financial statements for any material misstatements arising from the application of SAB 108 or recognize a cumulative effect adjustment within the current year opening balance in retained earnings, with disclosure of such items. SAB 108 is effective for fiscal years ending after November 15, 2006. The Company has determined that the adoption of SAB 108 did not have a material impact on the Consolidated Financial Statements.

In June 2006, the FASB issued Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact, if any, that the adoption of FIN 48 will have on the Company's Consolidated Financial Statements.

Emerging Issues Task Force Issue No. 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 04-05), has two effective dates. For general partners of all new limited partnerships formed and for existing limited partnerships for which the partnership agreements are modified, EITF 04-05 is effective after June 29, 2005. For general partners in all other limited partnerships, it is effective no later than the beginning of the first reporting period in fiscal years beginning after December 15, 2005. Two transition methods are available. EITF 04-05 provides guidance for assessing when a general partner controls, and therefore should consolidate, a limited partnership or similar entity when the limited partners

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

3. Accounting Developments (continued)

have certain rights. The Company has evaluated the impact of EITF 04-05 and determined that the adoption of EITF 04-05 did not result in the Company having to consolidate any limited partnerships that would otherwise not be consolidated absent EITF 04-05.

FASB Staff Position FAS 115-1/FAS 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (FSP 115-1/124-1) was finalized November 3, 2005 and is applicable to reporting periods beginning after December 15, 2005. FSP 115-1/124-1 nullifies certain requirements of EITF Issue 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*, and supersedes EITF Topic No. D-44, *Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value*. FSP 115-1/124-1 provides guidance on determining whether an investment is impaired, whether impairment is temporary or other than temporary, measurement of the impairment loss, accounting subsequent to an impairment write-down, and disclosures about unrecognized losses. The Company has determined that the adoption of FSP 115-1/124-1 did not have any impact on the Company's Consolidated Financial Statements.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3* (FAS 154). FAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. APB Opinion 20 previously required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. FAS 154 requires retrospective application to prior period financial statements of a voluntary change in accounting principle unless it is impracticable. FAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. FAS 154 did not have a material impact on the Company's Consolidated Financial Statements.

In December 2004, the FASB issued SFAS No. 123(R). FAS 123R amends FAS 123, *Accounting for Stock-Based Compensation*, and requires all share-based payments to employees to be recognized in the financial statements. FAS 123R was effective in fiscal years beginning after December 15, 2005. The Company adopted FAS 123R on January 1, 2006, and used the modified prospective transition method. This method requires measurement of compensation cost for all stock-based awards at fair value on the date of grant and recognition of compensation over the service period for awards expected to vest. The adoption of FAS 123R did not have a material effect on the Company's financial position, results of operations or cash flows, however, the level of future equity based compensation grants, if any, could have a material effect on amounts recorded in the Consolidated Statements of Operations.

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

In connection with the IPO, the Company has an Indemnification Agreement with Société Générale under which (1) Société Générale 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 Société Générale, and (2) Société Générale 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 Société Générale and SGASH and a third-party escrow agent. Also on July 12, 2006, the Company deposited with the escrow agent \$72.3 million for the payment of liabilities arising out of the matters for which Société Générale has

Cowen Group, Inc.**Notes to Consolidated Financial Statements (continued)****4. Restricted Cash Pursuant to Escrow Agreement and Related Indemnification Agreement with Société Générale (continued)**

agreed to indemnify Cowen. Subsequent to making this deposit, certain matters covered by the escrow arrangement 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 Société Générale 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 \$52.1 million as of December 31, 2006.

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.

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 December 31, 2006 and 2005:

	2006		2005	
	Owned	Sold Not Yet Purchased	Owned	Sold, Not Yet Purchased
Corporate debt securities	\$ 171,124	\$ 91,904	\$ 155,465	\$ 56,427
Equity securities	54,802	156,449	31,168	86,796
Mutual funds	3,266		12,160	
Money market funds			19,660	
Options	25,874	3,106		
Warrants	4,088		1,633	
Governments	767			
Other		121		
Total	\$ 259,921	\$ 251,580	\$ 220,086	\$ 143,223

Included in corporate debt securities owned are non-marketable securities totaling \$0.9 million and \$23.9 million at December 31, 2006 and 2005, respectively, which consist of securities that have not been registered under the Securities Act of 1933, and are being offered only to qualified institutional buyers under Rule 144A.

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 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.

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

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

Amounts receivable from and payable to brokers, dealers and clearing brokers at December 31, 2006 and 2005 consist of the following:

	2006 Receivable (in thousands)	Payable	2005 Receivable	Payable
Clearing brokers	\$ 70,032	\$ 22,215	\$ 25,635	\$ 8,860
Fees and commissions	13,532	7,703	214	6,516
Total	\$ 83,564	\$ 29,918	\$ 25,849	\$ 15,376

7. Exchange Memberships

Exchange memberships provide the Company with the right to do business on the exchanges of which it is a member. An impairment in value of the Company's exchange memberships occurred in 2004, at which time the Company recorded an impairment loss of approximately \$2.0 million. No impairment occurred in 2006 or 2005. The fair value of the exchange memberships was approximately \$2.6 million and \$27.0 million at December 31, 2006 and 2005, respectively.

On November 16, 2006, as a result of the demutualization of the New York Mercantile Exchange (NYMEX), the Company exchanged its seats at the Commodity Exchange (COMEX) for 16,800 shares of restricted NYMEX common stock and two trading rights in the restructured COMEX. The NYMEX shares and the trading rights were recognized at fair value on the date of exchange, and the Company recognized a gain of approximately \$1.0 million representing the difference between the previous carrying value of the seats and the fair value of the shares that were received from the exchange at the time of demutualization. The initial gain was recorded in gain on exchange memberships on the Consolidated Statements of Operations. The shares and the trading rights are included in securities owned and exchange memberships, respectively, in the Consolidated Statements of Financial Condition.

As of January 1, 2006, the Company owned seven New York Stock Exchange (NYSE) memberships with a carrying value on that date of \$7.3 million. On March 7, 2006 the NYSE merger with Archipelago Holdings, Inc. (the Merger) was consummated and each member received cash and shares of NYSE Group, Inc. common stock. The Company recorded a gain of \$24.8 million as a result of the merger, which is included in gain on exchange memberships in the Consolidated Statements of Operations. In connection with these events, the Company directed its interests from the Merger to SGASH. After the Merger, the right to trade on the Exchange ceased to be tied to membership. Trading privileges are now exercised through trading licenses obtained by Dutch auction. The Company purchased seven licenses.

On October 18, 2005, with the demutualization of the Chicago Board of Trade (CBOT) the Company exchanged its seats at the CBOT for Class A common shares and Class B membership interests of the restructured CBOT. The shares of the restructured CBOT were recognized at fair value at the date of exchange and the Company recognized a gain of approximately \$1.0 million representing the difference between the previous carrying value of the seats and the fair value of the shares and membership interests received from the exchange. The Class A shares and Class B membership interests of the restructured CBOT are included in securities owned, at fair value and exchange memberships, respectively, on the Consolidated Statements of Financial Condition.

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Cowen Group, Inc.**Notes to Consolidated Financial Statements (continued)****8. Furniture, Fixtures, Equipment, and Leasehold Improvements**

Furniture, fixtures, equipment, and leasehold improvements consisted of the following at December 31, 2006 and 2005:

	2006	2005
	(in thousands)	
Leasehold improvements	\$ 8,824	\$ 1,285
Equipment	2,034	510
Furniture and fixtures	2,506	885
Computer software	5,266	4,175
Total	18,630	6,855
Less accumulated depreciation and amortization	6,001	3,632
Total	\$ 12,629	\$ 3,223

Depreciation and amortization expense related to furniture, equipment and leasehold improvements totaled approximately \$1.4 million, \$0.7 million and \$0.6 million for the years ended December 31, 2006, 2005 and 2004, respectively. Amortization expense related to computer software costs totaled approximately \$1.0 million, \$1.4 million and \$1.8 million for the years ended December 31, 2006, 2005 and 2004, respectively. During the year ended December 31, 2005, the Company wrote-off furniture, fixtures and equipment with a net book value of approximately \$0.7 million. This write-off was included in depreciation and amortization expense on the Consolidated Statements of Operations.

Unamortized capitalized computer software costs as of December 31, 2006 and 2005, were \$0.7 million and \$1.7 million, respectively.

9. Goodwill

The Company has \$50.0 million of goodwill recorded on the Consolidated Statements of Financial Condition that relates to Société Générale's acquisition of the Company in 1998. Goodwill is reviewed for possible impairment at least annually, consistent with valuation methodologies pursuant to FAS 142.

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 FAS 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, revenue multiples of comparable exchange listed corporations, and the trading price of the Company's common shares. Based upon analysis performed during the years ended December 31, 2006, 2005, and 2004 no impairment charges were recognized.

The following table reflects the changes in the carrying value of goodwill for the years ended December 31, 2006 and 2005:

	2006	2005
	(in thousands)	
Beginning balance	\$ 50,000	\$ 50,000
Goodwill acquired		
Impairment losses		
Ending balance	\$ 50,000	\$ 50,000

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

10. Commitments, Contingencies and Guarantees

Litigation

The Company is subject to numerous litigation and regulatory matters, including securities class action lawsuits.

Although there can be no assurances as to the ultimate outcome, the Company has established reserves for litigation and regulatory matters that it believes are adequate as of December 31, 2006. The Company believes that the eventual outcome of the actions against it, including the matters described below, will not in the aggregate, have a material adverse effect on its financial position or cash flows, but may be material to its operating results for any particular period, depending on the level of the Company's operating results for such period.

Following are summaries of the Company's most significant pending legal and regulatory matters at December 31, 2006.

In January 2002, the Company learned that Frank Gruttadauria (Gruttadauria), a former employee of SG Cowen Securities Corporation's (SGCSC's) retail brokerage business that was sold in October 2000, had defrauded numerous customers and misappropriated their assets at various firms that had employed him, including the Company. Following the discovery of Gruttadauria's fraud, numerous former customers commenced or threatened to commence lawsuits and arbitrations against the Company arising out of Gruttadauria's actions. In addition, government and regulatory authorities initiated investigations of the matter. The Company cooperated fully with all of the governmental and regulatory investigations and all known regulatory matters arising out of Gruttadauria's conduct were resolved in 2003. The Company has also reached settlements with the vast majority of former customers, and has arbitrated several other customers' claims. The Company is attempting to resolve the remaining disputes. Separately, the securities brokerage firm that purchased SGCSC's former retail brokerage business in October 2000 had threatened to file an arbitration against the Company in connection with the liabilities, costs and expenses that it has incurred as a result of Gruttadauria's actions. The parties have resolved this separate matter which was also subject to the Indemnification Agreement between Société Générale and the Company. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction in connection with Gruttadauria's actions, the Company will be indemnified by Société Générale.

The Company is one of several defendants named in lawsuits involving Lernout & Hauspie Speech Products, N.V. (L&H):

- In *Nisselson v. Lernout, et al.*, No. 05-1774, filed in the United States District Court for the District of Massachusetts on May 5, 2003, the Trustee of the Dictaphone Litigation Trust alleged that the Company made material misrepresentations to Dictaphone while the Company was a financial advisor to L&H on its acquisition of Dictaphone, and further alleged that the Company published materially misleading research on L&H, in violation of various federal and state laws. On August 9, 2004, the District Court granted the Company's motion to dismiss the amended complaint. The Trustee appealed the District Court's ruling to the United States Court of Appeal for the First Circuit and, on November 8, 2006, the First Circuit affirmed the dismissal of all claims against the Company. On February 23, 2007, the plaintiff filed a petition for writ of certiorari to the Supreme Court of the United States. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

10. Commitments, Contingencies and Guarantees (continued)

• In *Rocker Management, L.L.C., et al. v. Lernout & Hauspie Speech Products, N.V., et al.*, Civil Action No. 00-CV-5965 (D.N.J.) filed in the United States District Court for the District of New Jersey, on December 8, 2000, short-sellers of L&H stock allege that the Company violated federal securities laws and state common law by participating in a scheme to artificially inflate L&H's stock price through the Company's role as underwriter and adviser for L&H on several acquisitions and through the Company's published research on L&H. On April 3, 2001, the Company filed a motion to dismiss which was denied by the court and the Company subsequently filed an answer denying liability. On November 10, 2006, the Company filed a motion for summary judgment seeking dismissal of all claims. That same day the plaintiffs filed a motion for spoliation sanctions against the Company in which they sought, alternatively, the striking of the Company's answer or an adverse jury instruction. Although both motions have been fully briefed, no date has been set for oral argument. Discovery has not been stayed pending resolution of the motions. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

The Company is one of many financial institutions named as defendants in a number of putative securities class actions entitled *In re: Initial Public Offering Securities Litigation*, filed in the United States District Court for the Southern District of New York relating to numerous initial and other public offerings of common stock from approximately 1998 through 2000. The various complaints allege that the underwriters of certain initial public offerings, including the Company, made material misrepresentations and omissions to purchasers of the stock sold in the initial public offerings, thereby inflating the value of the stock. Specifically, the plaintiffs allege that the defendants failed to disclose, among other things, the purported existence of improper tie-in and compensation arrangements they had with certain purchasers of the stock and alleged conflicts of interest relating to research published by the underwriters, all in violation of federal securities laws. The district court granted plaintiffs' motion to certify six focus cases as class actions. The Company is a named defendant in four of these focus cases. The Company appealed the class certification decision to the Second Circuit Court of Appeals and on December 4, 2006, the Second Circuit reversed the district court's decision and remanded the matter for reconsideration in light of the Second Circuit's opinion. Plaintiffs petitioned for rehearing and rehearing en banc by the Second Circuit. On December 14, 2006, the district court stayed discovery in the consolidated banc. On January 24, 2007, the Second Circuit instructed defendants to submit a response to plaintiffs' petition. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

The Company and other underwriters are defendants in two separate, but related, antitrust actions alleging that the underwriter defendants conspired to fix initial public offering underwriting fees at 7%. On February 11, 1999, the United States District Court in the Southern District of New York (the Court) consolidated three actions brought by purchasers of securities in initial public offerings under the caption *In re Public Offering Fee Antitrust Litigation*, 98 Civ. 7890 (LMM). In that action, plaintiffs' damages claims were dismissed by the district court, but their claims for injunctive relief remain pending. In a related case, on April 10, 2001, the Court consolidated several actions filed by certain issuers of initial public offerings under the caption *In re Issuer Plaintiff Initial Public Offering Antitrust Litigation*, No. 00 Civ. 7804 (LMM). In this action, the damages are unspecified and the district court had denied the defendants' motion to dismiss. On April 18, 2006, the court denied the issuer plaintiffs' motion for class certification and ordered further briefing on the investor plaintiffs' motion for class certification. The plaintiffs have also filed a joint motion for summary judgment on liability and the issuers have filed a motion for leave to amend their Consolidated Class Action Complaint. The district court proceedings in both actions are

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

10. Commitments, Contingencies and Guarantees (continued)

stayed pending resolution of the issuers' motion for class certification, which is on appeal. The Second Circuit heard oral argument on the appeal on March 19, 2007. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

The Company is a named defendant in several litigations relating to Adelphia Communications, a cable company that filed for bankruptcy in June 2002. The complaints generally allege that the Rigas family who controlled Adelphia took advantage of Adelphia's assets, including through the use of certain loans, or co-borrowing facilities, that allowed the family to take more than \$3 billion for their private use. The Company has been named as a defendant in four actions arising out of certain offerings of Adelphia securities in which the Company participated as a member of the underwriting syndicate. All four actions are pending before the United States District Court for the Southern District of New York. The complaints in each of these actions raise a variety of claims arising out of the sale of Adelphia securities, including claims under the federal securities laws.

These actions are generally referred to as the Adelphia Securities Class Action, W.R. Huff Asset Management, Appaloosa, and Stocke. The district court granted the Company's motion to dismiss all federal securities claims brought against the Company in the Adelphia Class Action. Thereafter, the financial institution defendants reached a settlement with the plaintiffs. On June 15, 2006, the district court preliminarily approved the settlement. A fairness hearing before Judge McKenna was held on November 10, 2006, and he entered an order approving the settlement on November 20, 2006. The Company's share of the settlement is approximately \$1.7 million plus interest at 4.37% beginning December 1, 2006 (all of which is covered by the indemnification agreement between Société Générale and the Company). This amount has been placed in an escrow account bearing the required rate of interest. On December 8, 2006, a group of class members appealed the order approving the settlement agreement with the class plaintiffs to the United States Court of Appeals for the Second Circuit. If Judge McKenna's approval of the settlement is upheld on appeal or otherwise becomes final, claims made by all class members who did not opt out (including plaintiffs in Stocke) will be dismissed and released. The court also has granted in part and denied in part certain motions to dismiss filed by various defendants, including the Company, in Huff, Appaloosa and Stocke, but has not ruled on other potential bases for dismissal set forth in the Company's motions in these cases. In addition, in August 2005 the district court denied the Company's motion to dismiss based on Huff's lack of standing, and subsequently granted leave to file an interlocutory appeal to the Second Circuit Court of Appeals of that ruling. The Second Circuit granted the Company's petition to appeal under 28 U.S.C. § 1292, and that appeal is pending. In addition to the cases in which the Company has been named as a defendant, the Company may also face potential liability pursuant to the applicable master agreements among underwriters for any judgments or settlements in other cases involving the Adelphia securities offerings in which the Company participated. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

10. Commitments, Contingencies and Guarantees (continued)

The Company is also one of many defendants in two related adversary proceedings filed in the Adelphia Bankruptcy Proceeding, which is pending in the United States Bankruptcy Court for the Southern District of New York. These adversary proceedings were filed by the Official Committee of Unsecured Creditors and the Official Committee of Equity Security Holders (the Committees). Both of these cases raise a variety of common law and federal claims, which are generally similar to the claims asserted in the Adelphia Securities Class Action and other cases described above. With respect to the Company and other investment banks, the complaints taken together set forth claims for violation of the Bank Holding Company Act, equitable disallowance or equitable subordination, breach of fiduciary duty, aiding and abetting breach of fiduciary duty, aiding and abetting fraud, gross negligence and breach of contract, among others. On August 30, 2005, the bankruptcy court ruled that the two Committees have standing to prosecute the adversary proceedings, but has not ruled on the various motions to dismiss that are pending, including motions filed by the Company. On February 9, 2006, the district court withdrew the reference from the bankruptcy court so that after the bankruptcy court rules on the pending motions, the cases will proceed before the district court. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

The Company has been named as a defendant in a purported class action filed in the United States District Court for the Northern District of Alabama on January 8, 2004 as a result of the Company's predecessor's involvement as one of the initial purchasers in a March 1998 private placement of debt securities issued by HealthSouth Corporation, which were subsequently exchanged for materially identical registered securities. The complaint alleges that the offering materials for the private placement and the registration statement in the associated offering violated federal securities laws by failing to disclose HealthSouth's subsequently revealed accounting irregularities. On June 8, 2006, the district court, among other things, dismissed the claims arising out of the March 1998 private placement (the only claims against the Company). On August 21, 2006, following plaintiffs' subsequent submission of amendments to the complaint, the district court so-ordered a stipulation and order dismissing all amended counts against the Company. The dismissal is not yet a final judgment from which an appeal may be taken by plaintiffs. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

The Company was one of several named defendants in a putative securities class action filed in the United States District Court for the District of New Jersey on September 2, 2005. The plaintiffs in this matter sought to recover losses allegedly caused by misrepresentations and omissions in connection with the December 2004 initial public offering of Arbinet-theexchange, an electronic marketplace for trading, routing and settling telecommunications capacity. The complaint alleged that these misrepresentations and omissions artificially inflated the price of Arbinet's securities and that subsequent disclosures of the true state of Arbinet's market and its business in May and June 2005 caused Arbinet's securities to decline in value. The defendants, including the Company, filed a motion to dismiss the complaint and, on December 22, 2006, the court granted defendants' motion, dismissing the complaint in its entirety, but granting leave to re-plead. By stipulation and order dated January 22, 2007, plaintiffs agreed that the case should be dismissed with prejudice, each side to bear its own costs. Accordingly, the case now has been fully resolved in the Company's favor.

The Company is one of three underwriter defendants in a lawsuit filed in the District Court of Travis County, Texas, on May 24, 2006 by Crossroads Systems, Inc., a company that designs, develops, and manufactures computer storage devices. The lawsuit alleges that the underwriters of Crossroads' 1999 IPO, which were led by the Company, purposely underpriced the IPO for their own improper purposes.

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

10. Commitments, Contingencies and Guarantees (continued)

Specifically, Crossroads alleges that the underwriter defendants allocated stock to favored clients who shared their profits with the underwriters either directly or indirectly through excessive trading commissions in connection with the IPO stock and/or unrelated securities trading. Crossroads sets forth causes of action for breach of fiduciary duty, fraud, and unjust enrichment. The damages are unspecified. In July 2006, the Company filed an answer denying the allegations of the complaint, and the case is now in the discovery phase. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

On June 28, 2006, a group of approximately 60 medical doctors filed a lawsuit against the Company in San Francisco Superior Court. Plaintiffs allege that the Company negligently rendered a fairness opinion in 1998 in connection with the acquisition of Orange Coast Managed Care Services and St. Joseph Medical Corporation by FPA Medical Management, Inc. According to the complaint, plaintiffs received restricted FPA stock as consideration in the sale and, shortly after the acquisition, FPA went bankrupt, rendering the stock worthless. On August 14, 2006, the Company removed the case to United States District Court for the Northern District of California. On August 17, 2006 the Company filed a motion to dismiss the complaint. Plaintiffs are seeking a remand to state court. On March 8, 2006, the court granted the Company's motion to dismiss, with leave to replead, and denied Plaintiffs' move to remand. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

On June 6, 2005, SGC Partners I LLC, SGC Partners II LLC, SG Merchant Banking Fund, SG Capital Partners LLC and former employees of SGCSC were served with a First Amended Complaint in a case entitled *Janice E. Stanton v. SGC Partners I, LLC*, Case No. 02-40208, Adv. No. 05-40145 (Stanton I). The action was brought in connection with the bankruptcy proceeding filed by House of Lloyd (HOL) pending in that court. The Trustee seeks damages based on claims of breach of fiduciary duty, corporate waste, fraudulent transfers, insider preferences and illegal distributions. On December 29, 2006, the Trustee filed a separate complaint against the Company, Cowen Capital Partners, LLC, and SG Americas Securities, LLC in a case entitled *Janice E. Stanton v. Cowen and Company, LLC* et al., Case No. 02-40208, Adv. No. 06-04283 (Stanton II) based on virtually identical facts alleged in Stanton I arising out of the HOL bankruptcy. The complaint further alleges that the Company owned and controlled the Defendants in Stanton I and/or that the Company is the successor of the defendants in Stanton I. The two cases have been consolidated. Discovery is proceeding with a trial date scheduled for January 22, 2008. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

The SEC has conducted an investigation arising out of the proprietary trading activities of Guillaume Pollet, a former Managing Director and proprietary trader in the former equity derivatives division of SGCSC (which is now part of SGAS), who was terminated by the Company in 2001 for violating firm policy and misleading the firm's management about certain of his trading activity. The trading activity at issue involved private placements in public equity, or so-called PIPE s. The Company received a Wells Notice in July 2004, and submitted a response in August 2004. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction, the Company will be indemnified by Société Générale.

Based on information voluntarily disclosed to regulators by the Company, the SEC and NYSE are conducting informal inquiries that appear to be focused principally on certain conduct of a research salesperson who was terminated by the Company in late 2004. The employee was discharged after the Company discovered that the employee had sought and obtained access to sensitive information about a company, shared such information with certain of his clients and others, and made investment recommendations to clients in part on the basis of that information. The Company has fully cooperated

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

10. Commitments, Contingencies and Guarantees (continued)

with this continuing investigation. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction related to this matter, the Company will not be indemnified by Société Générale.

The Company has provided various data and information to the NASD in response to its request for information as part of an industry-wide sweep relating to the Company's gifts, gratuities and entertainment policies, practices, and procedures. In addition, the Company has also received a subpoena for documents and information from the SEC, and additional requests for information from the NASD, seeking information concerning, among other things, gifts, gratuities and entertainment and the use of one of the Company's error accounts primarily involving an unaffiliated mutual fund company. The Company is cooperating fully with these continuing investigations. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction related to this matter, the Company will not be indemnified by Société Générale.

The Company received requests for documents and information from the SEC's Office of Compliance Inspections and Examinations seeking documents and certain financial and other information concerning, among other things, the Company's various trading desks, institutional sales team and internal accounts, including error accounts, and related compliance procedures. The Company is cooperating fully with this inquiry. To the extent that the Company incurs additional legal fees or pays any fine or monetary sanction related to this matter, the Company will not be indemnified by Société Générale.

In October 2004, the Company received a request from the NYSE, as part of an industry-wide sweep, for data and information relating to its compliance with provisions of the federal securities laws, and related rules and regulations, concerning delivery of prospectuses and/or product descriptions in connection with customer purchases of, inter alia, new issue securities, mutual funds and exchange-traded funds. The Company has provided periodic reports to the NYSE concerning its progress in responding to their request and will continue to cooperate fully with this continuing inquiry. The Company will be indemnified by Société Générale in part against any liabilities, including legal fees that arise out of any future litigation or the pending regulatory investigation relating to this matter.

Lease commitments

The Company's headquarters is located in New York and other offices are located in Boston, San Francisco, Cleveland, Denver, 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.

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

10. Commitments, Contingencies and Guarantees (continued)

As of December 31, 2006, the Company had the following lease commitments related to these agreements:

	Minimum Lease Payments (in thousands)
2007	\$ 8,866
2008	8,981
2009	9,284
2010	9,395
2011	9,351
Thereafter	20,429
	\$ 66,306

Rent expense for the years ended December 31, 2006, 2005 and 2004 was approximately \$10.7 million, \$9.4 million and \$8.8 million, respectively.

Guarantees

The Company has outsourced certain information technology services to Hewlett-Packard Company and Savvis Communications Corporation. The agreements are in place until 2010. As of December 31, 2006, the Company's annual minimum guaranteed payments under these agreements are as follows:

	Minimum Guaranteed Payments (in thousands)
2007	\$ 11,118
2008	11,578
2009	9,904
2010	4,189
	\$ 36,789

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* (FIN 45) 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. However, these transactions are collateralized by the underlying security, thereby reducing the associated risk to changes in the market value of the security through the settlement date.

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.

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

10. Commitments, Contingencies and Guarantees (continued)

Accordingly, no contingent liability is recorded in the Consolidated Statements of Financial Condition for these arrangements.

In connection with the IPO, the Company has an Indemnification Agreement with Société Générale under which the Company will indemnify, and will defend and hold harmless Société Générale and its subsidiaries from and against certain liabilities specifically retained or assumed by the Company after becoming a public company (See Note 11, Separation from Société Générale and Other Related Matters, for further discussion of the Indemnification Agreement). There were no contingent liabilities related to these matters recognized by the Company through the period ended December 31, 2006.

11. Separation from Société Générale and Other Related Matters

In connection with the IPO, the Company entered into a Separation Agreement, an Indemnification Agreement and a number of other agreements with Société Générale for the purpose of accomplishing the separation from Société Générale, 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. The Separation Agreement and Indemnification Agreement were executed on July 11, 2006. The other agreements described below were executed on July 12, 2006. 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.

The Separation Agreement provides that, as of July 18, 2006, both the Company and Société Générale will assume and/or retain certain actual or contingent liabilities. Specifically, the Company will retain or assume, among others, certain liabilities reflected on the Company's 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 Société Générale, 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 Société Générale) 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 Société Générale 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 Société Générale 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 known and unknown liabilities relating to, arising out of or resulting from its business, assets, liabilities or any business or operations conducted by Société Générale.

The Company entered into an Indemnification Agreement with Société Générale on July 11, 2006. Under the Indemnification Agreement, the Company will indemnify, and will defend and hold harmless Société Générale and its subsidiaries from and against all liabilities specifically retained or assumed by us

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

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

after becoming a public company. Société Générale 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 Société Générale 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.

The Company entered into an Employee Matters Agreement with Société Générale in connection with the IPO. The Employee Matters Agreement provides, among other things, for the allocation, between the Company and Société Générale, of responsibilities and liabilities for employees, employee compensation and benefit plans, programs, policies and arrangements following the transactions contemplated by the Separation Agreement. Such allocation includes the transfer to Société Générale of certain assets and liabilities associated with identified deferred compensation plans sponsored by Société Générale.

The Company entered into a Stockholders Agreement with SGASH in connection with the IPO. The Stockholders Agreement, among other agreements, governs SGASH's right to appoint members of the Board of Directors of the Company, SGASH's registration rights relating to shares of the Company's common stock, if any, held by SGASH after the IPO and restrictions on SGASH's ability to sell, transfer or otherwise convey shares of the common stock, if any, held by SGASH after the IPO. As of July 21, 2006 SGASH holds less than 10% of the Company's common stock. As such, SGASH can no longer appoint members of the Board of Directors of the Company pursuant to the Stockholders Agreement.

The Company entered into a Transition Services Agreement with Société Générale in connection with the IPO pursuant to which the companies agreed to provide each other certain administrative and support services and other assistance consistent with a limited number of the services provided before the separation. Services that the Company agreed to provide to Société Générale included merchant banking oversight services. Services that Société Générale agreed to provide to the Company included facilities management, business continuity management, certain legal services and litigation management services and access to Société Générale data rooms and e-mail archives.

The Company entered into a Tax Matters Agreement with Société Générale in connection with the IPO. The Tax Matters Agreement includes a description of the Company's continuing tax sharing arrangements with Société Générale relating to periods prior to the separation, and also allocates responsibility and benefits associated with the elections made in connection with the separation from Société Générale. The Tax Matters Agreement also allocates rights, obligations and responsibilities in connection with certain administrative matters relating to taxes. In connection with the Company's separation from Société Générale, SGAI retained the tax benefits of the Company's net operating loss carryforwards.

On July 11, 2006 the Board of Directors of the Company approved the Equity and Incentive Plan pursuant to which the Company can offer employees, independent contractors and non-employee Directors equity-based awards. 4,725,000 shares of common stock have been allocated for issuance under this plan. In connection with the IPO, the Company made equity awards of 2,100,000 shares of restricted stock and granted options to purchase 1,125,000 shares of common stock to certain of its senior employees.

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Cowen Group, Inc.**Notes to Consolidated Financial Statements (continued)****12. Related Party Transactions**

Effective July 21, 2006 (the date on which Société Générale's ownership level was reduced to below 10%), the Company's affiliation with Société Générale was ended. As such, the Consolidated Statements of Operations include related party items through July 21, 2006. Accordingly, any balances due to or from Société Générale as of December 31, 2006 are no longer separately reported as related party amounts in the Consolidated Statements of Financial Condition.

Balances with affiliated companies at December 31, 2006 and 2005 are included in the Consolidated Statements of Financial Condition under the following captions:

	2006 (in thousands)	2005
Assets		
Cash and cash equivalents	\$	\$ 303
Securities purchased under agreements to resell		410,981
Receivable from brokers, dealers and clearing brokers		25,635
Due from affiliates	1,367	568
Other assets		1,629
Total assets	1,367	439,116
Liabilities		
Payable to brokers, dealers and clearing brokers		9,010
Accounts payable, accrued expenses and other liabilities		5,615
Total liabilities		14,625
Total net assets	\$ 1,367	\$ 424,491

Until the date of the IPO, the Company's excess cash was invested in securities purchased under agreements to resell (reverse repos) with the New York branch of Société Générale (SGNY). These reverse repos were collateralized by U.S. government and agency obligations, were monitored daily for credit exposure and were payable on demand.

Revenues earned from and expenses incurred with affiliated companies for the years ended December 31, 2006 (through July 21, 2006, the date on which Société Générale's ownership level was reduced to below 10%), 2005 and 2004 are summarized as follows:

	2006 (in thousands)	2005	2004
Revenues			
Investment banking	\$	\$ 552	\$
Interest and dividend income	9,662	12,419	6,059
Other	1,141	5,425	5,565
Total revenues	10,803	18,396	11,624
Expenses			
Floor brokerage and trade execution	5,006	7,982	13,400
Service fees, net	3,675	13,392	22,285
Occupancy and equipment	7,297	12,502	12,493
Interest expense	159	142	140
Other	(69)	447	896
Total expenses	16,068	34,465	49,214
Total, net	\$ (5,265)	\$ (16,069)	\$ (37,590)

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

12. Related Party Transactions (continued)

Other than interest earned on reverse repos with SGNYS, revenues earned from and expenses incurred with affiliated companies primarily resulted from securities transactions and administrative services.

Investment banking revenues included fees earned by the Company for acting as Société Générale's agent broker in the U.S. market for the sale of certain assets.

Interest income for periods before the reorganization of SGCSC on April 23, 2004 (see Note 1) was based on the amount of reverse repos allocated to the Company's business. Interest income on the allocated reverse repos was based on current market rates for similar transactions.

Pursuant to service agreements with certain affiliates, the Company received fees related to portfolio, investment and administration services that were provided in connection with the management of certain assets. These fees are included in other revenue on the Consolidated Statements of Operations.

The Company clears its securities and futures transactions on a fully disclosed basis through clearing brokers that are affiliates of Société Générale. Clearing expenses are reported in floor brokerage and trade execution on the Consolidated Statements of Operations. The Company had entered into a commercial clearing agreement with SGAS as a result of the Company's separation from Société Générale, which had replaced the Company's pre-existing clearing agreement with SGAS. The initial terms of that clearing agreement terminated on December 31, 2006 and were extended until January 25, 2007, at which time the Company entered into a long term relationship with a new clearing firm.

Pursuant to a service agreement with SGAI and other affiliates through the date of the IPO, the Company incurred expenses for costs and services that included facilities administration and security, risk management, financial management and reporting, information systems management and support, insurance, legal and compliance. Total expenses pursuant to the service plan were approximately \$3.2 million, \$13.0 million and \$22.3 million during the years ended December 31, 2006, 2005 and 2004, respectively. In addition, the Company incurred expenses of approximately \$0.7 million, \$1.5 million and \$1.2 million with an affiliated company for certain presentation center services during the years ended December 31, 2006, 2005 and 2004, respectively. These expenses are included in service fees on the Consolidated Statements of Operations, net of approximately \$0.2 million, \$1.1 million and \$1.2 million of fees earned related to presentation center and library services provided by the Company to SGAI during the years ended December 31, 2006, 2005 and 2004, respectively. The Company entered into a Transition Services Agreement with Société Générale in connection with the IPO pursuant to which the companies agreed to provide each other certain administrative and support services and other assistance consistent with a limited number of the services provided before the separation. Pursuant to the Transition Services Agreement, the Company has also agreed to provide Société Générale various services that have previously been provided by the Company to Société Générale, including merchant banking oversight services. Société Générale will provide services to the Company, including, facilities management, business continuity management, certain legal services and litigation management services and access to Société Générale data rooms and e-mail archives.

Certain costs and services, which include real estate, project management and premises and securities maintenance through the date of the IPO were allocated to the Company by Société Générale. The total amount allocated was approximately \$7.3 million, \$12.5 million and \$12.5 million during the years ended December 31, 2006, 2005 and 2004, respectively, and are reported in occupancy and equipment on the Consolidated Statements of Operations. In connection with the IPO, the Company entered into a sub-lease agreement with Société Générale, related to the Company's New York office, which is in place until September 30, 2013.

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

12. Related Party Transactions (continued)

As a member of the NYSE, the Company incurs a monthly membership fee based on transaction volume. NYSE membership fees were \$1.1 million, \$1.7 million and \$1.1 million during the years ended December 31, 2006, 2005 and 2004, respectively. Pursuant to the Company's clearing agreement with SGAS, portions of these fees were recoverable. The recoverable portion of these fees totaled approximately \$0.4 million, \$0.8 million and \$0.2 million during the years ended December 31, 2006, 2005 and 2004, respectively. The Company reports these exchange membership fees in other expenses on the Consolidated Statements of Operations, net of recoveries.

Prior to the IPO, Société Générale provided letters of credit and performance guarantees on the Company's behalf and the Company provided performance guarantees to Société Générale for certain clients of the Company's underwriting business which were also clients of Société Générale's corporate banking business. Expenses under these performance guarantees amounted to approximately \$0.3 million, \$0.1 million, and \$0.1 million during the years ended December 31, 2006, 2005 and 2004, respectively, and are included in other expense in the Consolidated Statements of Operations.

13. Employee Benefits

Defined Contribution Plans

The Company sponsors a 401(k) Savings Plan (the "401(k) Plan"), which is a defined contribution plan. Employees are entitled to participate, based upon certain eligibility requirements as defined by the 401(k) Plan. The Company provides matching contributions for certain employees that are equal to a specified percentage of the eligible participant's contribution as defined by the 401(k) Plan. The expenses relating to this plan totaled approximately \$0.6 million, \$0.7 million, and \$0.9 million for the years ended December 31, 2006, 2005, and 2004, respectively, and are included in employee compensation and benefits on the Consolidated Statements of Operations.

The Company also sponsors a defined contribution plan for its Geneva and London employees. Contributions made for these plans were approximately \$0.4 million, \$0.5 million, and \$0.5 million for the years ended December 31, 2006, 2005, and 2004, respectively, and are included in employee compensation and benefits on the Consolidated Statements of Operations.

Deferred and Other Compensation Plans

Prior to the IPO, the Company required selected employees to defer a portion of their performance related compensation in the form of a Fidelity Bonus (the "Fidelity Bonus"). The Fidelity Bonus was announced at the time all other bonuses were announced and vested ratably over a three-year period. Participants were entitled to a rate of return on their Fidelity Bonus amount based on a hypothetical investment in various alternative investment vehicles. As a result of the IPO, all of the Company's employees under the plan became fully vested and certain employees were paid out in full. Participants who deferred the distribution of their vested amounts will be paid out in accordance with the plan's original distribution schedule. Expenses related to this plan are comprised of both the vesting of the deferred amounts and any change in value based on the performance of the investment alternatives selected by the participants. The Company recognized compensation expense of approximately \$10.3 million, \$8.2 million, and \$6.6 million for the years ended December 31, 2006, 2005, and 2004, respectively. All of these charges are included in employee compensation and benefits on the Consolidated Statements of Operations. The Company has recorded liabilities of approximately \$3.2 million and \$13.2 million as of December 31, 2006 and 2005, respectively, which are included in employee compensation and benefits payable on the Consolidated Statements of Financial Condition.

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

13. Employee Benefits (continued)

Prior to the IPO, Société Générale had sponsored a voluntary deferred compensation plan for certain of the Company's key executives (the Deferred Compensation Plan). The Company's employees ceased contributing to the Deferred Compensation Plan in 2003, and no further contributions were made thereafter. Participants were allowed to make hypothetical investments in various alternative investment funds and the corresponding liability fluctuated based on the performance of those hypothetical investments. The Company recognized compensation expense of approximately \$1.5 million, \$3.2 million and \$4.0 million for the years ended December 31 2006, 2005 and 2004, respectively. This expense is included in employee compensation and benefits on the Consolidated Statements of Operations. The Company recorded a liability of approximately \$44.8 million at December 31, 2005, which is included in employee compensation and benefits payable on the Consolidated Statement of Financial Condition. This liability was joint and several with Société Générale. As a result of the IPO and pursuant to the Separation Agreement, Société Générale assumed the remaining obligations under the plan and retains all liability for future payments thereunder. The Company invested in corporate owned life insurance to economically hedge certain aspects of the Deferred Compensation Plan. At December 31, 2005, the cash surrender value of the corporate owned life insurance was approximately \$35.2 million and is included in other assets on the Consolidated Statement of Financial Condition. Changes in the cash surrender value of corporate owned life insurance are included in employee compensation and benefits on the Consolidated Statements of Operations. For the years ended December 31, 2006, 2005 and 2004, the Company recognized increases in the cash surrender value of approximately \$1.2 million, \$2.3 million, and \$2.0 million, respectively. As a result of the IPO and pursuant to the Separation Agreement, the Company transferred the cash surrender value of corporate owned life insurance to Société Générale.

Prior to the IPO, Société Générale sponsored a plan enabling eligible employees of the Company to defer a portion of their annual performance related compensation to make a hypothetical investment in an alternative investment vehicle indexed to the performance of investments made in the SG Merchant Banking Fund L.P. The Company had not made an equity investment in the SG Merchant Banking Fund L.P., but its liability to its employees was based upon the performance of their hypothetical investments. Changes in the Company's liabilities to employees were approximately (\$0.9) million, (\$1.0) million, and \$0.3 million for the years ended December 31 2006, 2005 and 2004, respectively, and are included in employee compensation and benefits on the Consolidated Statements of Operations. The Company recorded a liability of approximately \$3.9 million for the year ended December 31, 2005, which is included in employee compensation and benefits payable on the Consolidated Statement of Financial Condition. Prior to the IPO, this liability was joint and several with Société Générale. As a result of the IPO and pursuant to the Separation Agreement, Société Générale assumed the remaining obligations under the plan and retains all liability for future payments thereunder.

Prior to the IPO, the Company sponsored a plan enabling eligible employees to invest a portion of their performance related compensation in SG Cowen Ventures I, L.P. Most plan participants met the U.S. Securities and Exchange Commission's definition of an accredited investor and qualified to become limited partners of the fund. Upon payment of the performance related compensation for the year in which the plan was offered, the Company had no further obligation to these accredited participants. Certain plan participants did not meet the requirements to be treated as an accredited investor, and accordingly were permitted to make a hypothetical investment with pre-tax dollars in the fund. The Company had not made an equity investment in SG Cowen Ventures I, L.P., but its liability to these non-accredited employees was based upon the performance of their hypothetical investment. Changes in the Company's liabilities to employees were approximately \$0.04 million, \$0.1 million, and (\$0.8) million for the years ended December 31, 2006, 2005 and 2004 respectively, and are included in employee compensation and benefits

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

13. Employee Benefits (continued)

on the Consolidated Statements of Operations. The Company recorded a liability of approximately \$0.4 million for the year ended December 31, 2005, which is included in employee compensation and benefits payable on the Consolidated Statement of Financial Condition. As a result of the IPO and pursuant to the Separation Agreement, Société Générale assumed the remaining obligations under the plan and retains all liability for future payments thereunder.

Prior to the IPO, certain of the Company's employees participated in and received awards from the SG Corporate and Investment Banking Partnership. The participants in the partnership were selected every year and entitled to receive an amount determined based on the net income of Société Générale's Corporate and Investment Banking division. Participants were eligible to receive the award only if certain return on equity goals were met in the partnership year. To the extent awards were earned, they were subject to a four year cliff vest. The Company's allocation of these compensation charges totaled approximately \$1.0 million, \$0.4 million and \$1.1 million for the years ended December 31, 2006, 2005 and 2004, respectively. All of these charges are included in employee compensation and benefits on the Consolidated Statements of Operations. As a result of the IPO, the Company's employee participants under the partnership became fully vested and were paid out in full.

14. Stock-Based Compensation

Stock-based awards issued by Cowen Group, Inc.

Upon becoming a public company, the Company established the 2006 Equity and Incentive Plan (The Plan). The Plan permits the grant of options, 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 July 12, 2006, the Company granted options to purchase 1,125,000 shares of the Company's stock and 2,100,000 restricted shares. The options were granted to employees of the Company with an exercise price equal to the IPO price of \$16.00. The options generally become exercisable upon the completion of a five-year vesting period and expire seven years from the date of grant. The restricted shares generally vest over five years.

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

The compensation cost that has been expensed for these awards was approximately \$5.3 million for the year ended December 31, 2006. An income tax benefit of \$2.3 million was recognized during the year ended December 31, 2006.

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 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 SEC Staff Accounting Bulletin No. 107 (SAB 107): industry, market capitalization, stage of life cycle and capital structure.

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 SAB 107 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.

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

14. Stock-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 future. Accordingly, the assumed dividend yield is zero.

Valuation assumptions :

	Grant Date	
Expected option term	5.25 years	
Expected volatility	31.8	%
Expected dividend yield		
Risk-free interest rate	4.97	%

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.

The following table summarizes the Company's stock option activity for the year ended December 31, 2006:

	Shares Subject to Option	Average Exercise Price/Share(1)	Average Remaining Term	Aggregate Intrinsic Value(2)
Balance outstanding at January 1, 2006		\$		\$
Options granted	1,125,000	16.00		
Options exercised				
Options forfeited	(11,573)			
Options expired				
Balance outstanding at December 31, 2006	1,113,427	\$ 16.00	6.53	\$

Options exercisable at December 31, 2006

- (1) No shares were exercised from July 12, 2006, the date of grant, through December 31, 2006.
- (2) No options were vested or exercisable through December 31, 2006. The weighted-average grant-date fair value of options granted on July 12, 2006 was \$6.11.

As of December 31, 2006, there was \$5.5 million of unrecognized compensation cost related to the Company's grant of stock options.

The following table summarizes the Company's nonvested restricted shares activity for the year ended December 31, 2006:

	Nonvested Restricted Shares	Weighted-Average Grant Date Fair Value
Balance outstanding at January 1, 2006		\$
Granted	2,100,000	16.00
Vested		
Forfeited	(11,528)	
Balance outstanding at December 31, 2006	2,088,472	\$ 16.00

Cowen Group, Inc.

Notes to Consolidated Financial Statements (continued)

14. Stock-Based Compensation (continued)

As of December 31, 2006, there was \$28.1 million of unrecognized compensation cost related to the Company's grants of nonvested restricted shares. Unrecognized compensation cost related to nonvested restricted shares is expected to be recognized over a weighted-average period of 2.35 years. None of the nonvested restricted shares vested during the period ended December 31, 2006.

There have been no modifications to any awards granted under the Plan during the year ended December 31, 2006.

During the year ended December 31, 2006 the Company issued 9,792 restricted stock units to non-employee directors which were immediately vested. The fair value at the date of grant of a restricted stock unit was \$15.32.

Stock-based awards issued by Société Générale

Prior to the IPO, certain of the Company's employees were granted awards under Société Générale's various stock incentive plans. Société Générale sponsors an Employee Stock Purchase Plan (ESPP), referred to as the SG International Group Savings Plan. This plan allowed employees to purchase Société Générale stock at a discount. The Company provided matching contributions to the ESPP, which were equal to a specified percentage of the employees' contribution, as defined by the ESPP. Beginning in 2005, the Company ceased providing matching contributions. Employee shares were non-forfeitable when issued and accordingly are not subject to any vesting provisions.

Also prior to the IPO, Société Générale granted certain employees of the Company options to purchase shares of Société Générale stock. Such options were granted to employees of the Company with exercise prices equal to the average of the opening trading price of Société Générale shares on the Euronext Paris SA exchange during the 20 trading days prior to the date of grant. Generally, the options become exercisable upon the completion of a three year vesting period and expire seven years from the date of grant.

All of the options under this plan became fully vested prior to the IPO. The Company recognized compensation expense for these awards of \$0.1 million, \$0.1 million and \$0.4 million for the years ended December 31, 2006, 2005 and 2004, respectively which are included in employee compensation and benefits on the Consolidated Statements of Operations.

15. Income Taxes

The taxable results of the Company's U.S. operations were historically included in the consolidated income tax returns of SGAI through the IPO date. The tax results of the Company's U.K. operations were historically included in the tax returns of SG London Branch through April 30, 2006. For the period May 1, 2006 through December 31, 2006, the U.K. operations are included in CIL's U.K. tax filing. The U.S. impact of CIL's operations is included in the SGAI consolidated tax returns for the period May 1, 2006 through the IPO date and in the Company's tax filings post-IPO.

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Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

15. Income Taxes (continued)

The components of the Company's income tax expense (benefit) for the years ended December 31, 2006, 2005 and 2004 are as follows:

	Federal (in thousands)	State and local	Foreign	Total
Current	\$ 3,469	\$ 2,351	\$ 656	\$ 6,476
Deferred	(1,374)	(671)	117	(1,928)
Total at December 31, 2006	\$ 2,095	\$ 1,680	\$ 773	\$ 4,548
Current		\$ 1,104	\$ 48	\$ 1,152
Deferred				
Total at December 31, 2005	\$	\$ 1,104	\$ 48	\$ 1,152
Current	\$ 1,423	\$ 1,003	\$ (549)	\$ 1,877
Deferred				
Total at December 31, 2004	\$ 1,423	\$ 1,003	\$ (549)	\$ 1,877

As of December 31, 2006, the Company has income taxes payable of approximately \$1.8 million which is included in accounts payable, accrued expenses and other liabilities on the Consolidated Statement of Financial Condition.

The reconciliation of the Company's federal statutory tax rate to the effective income tax rate for the years ended December 31, 2006, 2005 and 2004 is as follows:

	2006	2005	2004
Statutory U.S. federal income tax rate	35.0 %	35.0 %	35.0 %
State and local taxes	3.0	8.3	1.8
Change in valuation allowance	(30.2)	(41.9)	(34.7)
Other, net	2.9	7.3	1.2
Effective rate	10.7 %	8.7 %	3.3 %

Deferred income tax assets and liabilities reflect the tax effect of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for the same items for income tax reporting purposes.

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

15. Income Taxes (continued)

The components of the Company's deferred tax assets and liabilities as of December 31, 2006 and 2005 are as follows:

	2006 (in thousands)	2005
Deferred Tax Assets:		
Net operating loss carryforwards	\$	\$ 44,553
Deferred compensation and employee benefits	3,012	31,359
Legal reserves and other deferred deductions		11,940
Goodwill		36,225
Other	55	1,210
Gross deferred tax assets	3,067	125,287
Valuation allowance	(80)	(125,287)
Deferred tax assets, net of valuation allowance	\$ 2,987	\$
Deferred Tax Liabilities:		
Deferred compensation and employee benefits	\$ (49)	\$
Goodwill	(572)	
Depreciation	(140)	
Foreign income	(298)	
Deferred tax liabilities	(1,059)	
Net deferred tax assets	\$ 1,928	\$

Deferred tax assets and deferred tax liabilities are included in other assets and accounts payable, accrued expenses and other liabilities, respectively, on the Consolidated Statements of Financial Condition.

As discussed in Note 1, on April 23, 2004, Société Générale reorganized SGCSG into two separate single member limited liability broker-dealers: SG Cowen & Co., LLC and SGAS. As a result of the reorganization, the tax attributes, including net operating loss carryforwards (NOL) of Cowen & Co., LLC were transferred to SGAI. There is no financial statement impact for the Company as a result of the transfer since a full valuation allowance was reflected for the NOL attribute. The gross amount of the NOL transferred to SGAI as part of the reorganization totaled approximately \$192.0 million.

For the period January 1, 2004 through April 23, 2004 (the Period), the Company was taxable as a corporation. During the Period, the Company recognized alternative minimum federal tax expense of \$1.4 million and state and local tax expense of \$0.4 million based on federal taxable income of \$69.6 million. The state and local tax expense for the period April 24, 2004 through December 31, 2004 was \$0.6 million.

The NOL as of December 31, 2004 in the amount of \$94.2 million consists of the NOL generated for the tax period from April 24, 2004 through December 31, 2004. The NOL as of December 31, 2005 was \$98.5 million prior to the IPO; a full valuation allowance was established to offset the deferred tax assets primarily due to accumulated tax losses through the IPO date.

In connection with the Company's separation from Société Générale, SGAI has retained such tax benefits associated with the IPO, including the Company's net operating losses.

In 2006, a tax provision of \$4.5 million was recorded. The low effective tax rate is due to a net reversal in the valuation allowance primarily due to payments of deferred compensation arrangements related to the IPO and pre-IPO amortization of goodwill. The valuation allowance is attributable to the portion of organizational costs and director related restricted stock units that will be tax deductible after December 31, 2008.

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

16. Financial Instruments with Off-Balance Sheet Risk, Credit Risk, or Market Risk

The Company has an irrevocable Letter of Credit for \$5.0 million issued by the Bank of New York (BONY) at the prime commercial lending rate, expiring on July 12, 2008, supporting Cowen s Boston office lease. The Company has another irrevocable Letter of Credit for \$100 thousand issued by BONY at the prime commercial lending rate, expiring on July 26, 2008, supporting Cowen s worker compensation insurance with Safety National Casualty Corporation. As of December 31, 2006, there were no amounts due related to these letters of credit.

The Company is engaged in various securities underwriting, trading and brokerage activities servicing a diverse group of domestic and foreign corporations, and institutional investor clients. A substantial portion of the Company s transactions are collateralized and are executed with and on behalf of institutional investors including other brokers or dealers, commercial banks, and other financial institutions. The Company s exposure to credit risk associated with the nonperformance of these clients in fulfilling their contractual obligations pursuant to securities transactions can be directly impacted by volatile trading markets which may impair the client s ability to satisfy its obligations to the Company. The Company s principal activities are also subject to the risk of counterparty nonperformance.

Prior to the IPO, the Company obtained securities under resale agreements on terms which permit it to repledge or resell the securities to others. At December 31, 2005, the Company s securities purchased under agreements to resell totaling \$411.0 million were collateralized by securities pledged with a fair value of approximately \$411.0 million.

Securities sold, not yet purchased are recorded as liabilities in the Consolidated Statements of Financial Condition and have market risk to the extent that the Company, in satisfying its obligations, may have to purchase securities at a higher value than what is recorded in securities sold, not yet purchased as of December 31, 2006.

Derivative contracts are financial instruments such as forwards, futures, swaps, warrants, or option contracts that derive their value from underlying assets, reference rates, indices, or a combination thereof. A derivative instrument generally represents future commitments to purchase or sell financial instruments at specified terms on a specified date, or to exchange currency or interest payment flows based on contractual or notional amounts. Derivatives often are referred to as off-balance-sheet instruments because neither their notional amounts nor the underlying instruments are reported in the Consolidated Statements of Financial Condition. Instead, fair values related to the derivative transactions are reported in the Consolidated Statements of Financial Condition. Changes in the fair value of derivatives are reported in principal transactions on the Consolidated Statements of Operations.

Derivatives are subject to various risks similar to other financial instruments, including market, credit and operational risk. In addition, the Company may be exposed to legal risks related to derivative activities, including the possibility a transaction may be unenforceable under applicable law. The risks of derivatives should not be viewed in isolation, but rather should be considered on an aggregate basis along with the Company s other trading-related activities. The Company manages the risks associated with derivatives on an aggregate basis along with the risks associated with market-making activities in cash instruments, as part of the Company s firm-wide risk management policies.

The Company uses U.S. Treasury futures and listed options to economically hedge proprietary trading positions. In addition, the Company uses listed options for proprietary trading activities. Futures contracts are executed on an exchange, and cash settlement is made on a daily basis for market movements. As a

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Cowen Group, Inc.**Notes to Consolidated Financial Statements (continued)****16. Financial Instruments with Off-Balance Sheet Risk, Credit Risk, or Market Risk (continued)**

writer of options, the Company receives a premium in exchange for giving the counterparty the right to buy or sell the security at a future date at a contracted price. Warrants provide an option to the holder to purchase securities from the issuer. Credit default swaps represent agreements in which one party pays a fixed fee in return for a payment by the other party contingent upon a specified default event relating to an underlying reference asset or pool of assets.

Realized and unrealized gains and losses associated with derivative transactions are included in principal transactions on the Consolidated Statements of Operations. The fair value of futures contracts and required margin deposits are included in receivable from brokers, dealers and clearing brokers on the Consolidated Statements of Financial Condition, and were de minimis at December 31, 2006 and 2005. The fair value of the listed options, warrants, and the credit default swap is included in securities owned and securities sold, not yet purchased on the Consolidated Statements of Financial Condition.

As of December 31, 2006 and 2005, the fair value of the Company's derivative financial instruments was as follows:

	2006 Assets	Liabilities (in thousands)	2005 Assets	Liabilities
Options	\$ 25,874	\$ 3,106	\$	\$
Warrants	4,088		1,633	
Credit default swap		121		
Total	\$ 29,962	\$ 3,227	\$ 1,633	\$

17. Stockholders' Equity

The certificate of incorporation of the Company provides for the issuance of up to 100,000,000 shares of common stock with a par value of \$0.01 per share and up to 10,000,000 shares of preferred stock with a par value of \$0.01 per share.

Common stock

The holders of the Company's common stock are entitled to one vote per share on all matters to be voted upon by the stockholders and do not have cumulative voting rights. Subject to preferences that may be applicable to any outstanding preferred stock of the Company, the holders of its common stock are entitled to receive ratably such dividends, if any, as may be declared from time to time by the Company's board of directors out of funds legally available for that purpose. In the event that the Company is liquidated or dissolved, the holders of its common stock are entitled to share ratably in all assets remaining after payment of liabilities, subject to any prior distribution rights of the Company's preferred stock, if any, then outstanding. The holders of the common stock have no preemptive rights, conversion rights or other subscription rights. There are no redemption or sinking fund provisions applicable to the Company's common stock. All outstanding shares of common stock are fully paid and non-assessable.

During the year ended December 31, 2006, the Company received 11,528 shares into treasury as a result of forfeitures related to the 2006 Equity and Incentive Plan.

Preferred stock

The Company's board of directors has the authority, without action by its stockholders, to designate and issue preferred stock in one or more series and to designate the rights, preferences, and privileges of

Cowen Group, Inc.
Notes to Consolidated Financial Statements (continued)

17. Stockholders Equity (continued)

each series, which may be greater than the rights associated with the common stock. It is not possible to state the actual effect of the issuance of any shares of preferred stock upon the rights of holders of common stock until the Company's board of directors determines the specific rights of the holders of preferred stock. However, the effects may include the following: restricting dividends on its common stock, diluting the voting power of its common stock, impairing the liquidation rights of its common stock and delaying or preventing a change in control of the Company without further action by its stockholders.

18. 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 December 31, 2006 there were 14,988,472 shares outstanding, of which 2,088,472 are restricted. The Company has included the weighted average of 9,792 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 December 31, 2006 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. In applying the treasury stock method to assume conversion of potentially dilutive stock options, there was no incremental dilutive effect of options through December 31, 2006.

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Cowen Group, Inc.**Notes to Consolidated Financial Statements (continued)****18. Earnings Per Share (continued)**

The computation of earnings per share is as follows:

	2006 (in thousands)	2005	2004
Net income	\$ 37,911	\$ 12,081	\$ 55,112
Shares for basic and diluted calculations			
Average shares used in basic computation	12,903	12,900	12,900
Stock options			
Restricted shares	63		
Average shares used in diluted computation	12,966	12,900	12,900
Earnings per share			
Basic	\$ 2.94	\$ 0.94	\$ 4.27
Diluted	\$ 2.92	\$ 0.94	\$ 4.27

19. Regulatory Requirements

As a registered broker-dealer, Cowen is subject to the Uniform Net Capital Rule 15c3-1 of the Securities Exchange Act of 1934. Under the alternative method permitted by this Rule, Cowen's net capital, as defined, is \$1.0 million. Cowen is not permitted to withdraw equity if certain minimum net capital requirements are not met. As of December 31, 2006, Cowen had net capital of approximately \$54.4 million, which was approximately \$53.4 million in excess of its net capital requirement of \$1.0 million.

Pursuant to an exemption under Rule 15c3-3(k)(2)(ii), Cowen is not required to calculate a reserve requirement and segregate funds for the benefit of customers since it clears its securities transactions on a fully disclosed basis and promptly transmits all customer funds and securities to the clearing broker-dealer which carries the accounts, maintains and preserves such books and records pertaining to them pursuant to Rules 17a-3 and 17a-4.

The Company rebates a portion of its commissions back to its customers. Under Rule 15c3-1(a)(2)(iv), it is required to maintain a segregated bank account where it issues payments to reimburse its customers. At December 31, 2005, approximately \$1.1 million has been segregated in a special account for the exclusive benefit of customers. There was no amount required to be segregated in a special account for the exclusive benefit of customers at December 31, 2006.

Proprietary balances of introducing brokers (PAIB) held at the clearing broker are considered allowable assets for net capital purposes, pursuant to agreements between Cowen and the clearing broker, which require, among other things, that the clearing broker performs computations for PAIB and segregates certain balances on behalf of Cowen, if applicable.

CIL is subject to the capital requirements of the Financial Services Authority (FSA) of the United Kingdom. Financial resources, as defined, must exceed the total financial resources requirement of the FSA. At December 31, 2006, CIL's financial resources of approximately \$4.4 million exceeded the minimum requirement of \$3.3 million by approximately \$1.1 million.

20. Subsequent Events

On January 26, 2007 the Company entered into a new clearing agreement with National Financial Services, LLC. The services provided under the new clearing agreement are substantially the same as the previous clearing agreement.

Supplemental Financial Information

The following table presents unaudited quarterly results of operations for 2006 and 2005. These quarterly results reflect all normal recurring adjustments that are, in the opinion of management, necessary for a fair presentation of the results. Revenues and net income can vary significantly from quarter to quarter due to the nature of our business activities.

Cowen Group, Inc.
Quarterly Financial Information (Unaudited)

	Three Months Ended			
	March 31, 2006	June 30, 2006 (in thousands)	Sept. 30, 2006	Dec. 31, 2006
Total revenues	\$ 103,793	\$ 83,617	\$ 60,200	\$ 97,357
Expenses:				
Compensation and benefits	62,738	48,838	44,999	59,132
Other expenses	27,571	28,859	27,270	28,944
Total expenses	90,309	77,697	72,269	88,076
Operating income (loss)	13,484	5,920	(12,069)	9,281
Gain on exchange memberships	24,832			1,011
Income (loss) before income taxes	38,316	5,920	(12,069)	10,292
Provision (benefit) for taxes	1,776	345	(655)	3,082
Net income (loss)	\$ 36,540	\$ 5,575	\$ (11,414)	\$ 7,210
Earnings per share:				
Basic	2.83	0.43	(0.88)	0.56
Diluted	2.83	0.43	(0.88)	0.55
Weighted average number of common shares :				
Basic	12,900	12,900	12,902	12,910
Diluted	12,900	12,900	12,902	13,162
	March 31, 2005	June 30, 2005	Sept. 30, 2005	Dec. 31, 2005
Total revenues	\$ 82,272	\$ 53,480	\$ 77,915	\$ 80,624
Expenses:				
Compensation and benefits	45,509	29,673	42,434	54,512
Other expenses	26,420	25,845	29,876	27,707
Total expenses	71,929	55,518	72,310	82,219
Operating income (loss)	10,343	(2,038)	5,605	(1,595)
Gain on exchange memberships				918
Income (loss) before income taxes	10,343	(2,038)	5,605	(677)
Provision (benefit) for taxes	782	(59)	488	(59)
Net income (loss)	\$ 9,561	\$ (1,979)	\$ 5,117	\$ (618)
Earnings per share:				
Basic	0.74	(0.15)	0.40	(0.05)
Diluted	0.74	(0.15)	0.40	(0.05)
Weighted average number of common shares :				
Basic	12,900	12,900	12,900	12,900
Diluted	12,900	12,900	12,900	12,900

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Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COWEN GROUP, INC.

By: /s/ Kim S. Fennebresque
Name: Kim S. Fennebresque
Title: Chairman, Chief Executive Officer
and President

Dated: July 17, 2007

EXHIBIT INDEX

Exhibit Number	Description
23.1	Consent of Ernst & Young LLP
31.1	Certification of CEO Pursuant to Section 302 of Sarbanes-Oxley Act of 2002
31.2	Certification of CFO Pursuant to Section 302 of Sarbanes-Oxley Act of 2002
32	Certification of CEO and CFO Pursuant to Section 906 of Sarbanes-Oxley Act of 2002
