HIGH-WIRE ACT AT FORTRESS

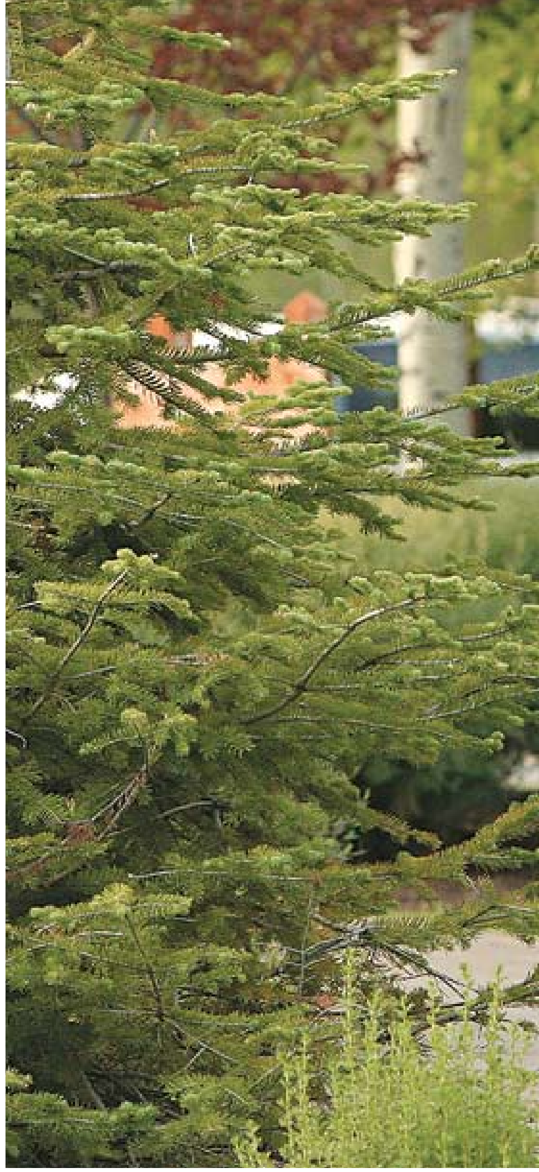
The secretive hedge fund and private equity firm, whose stock has sunk 95 percent since its 2007 IPO, is accused by a Vancouver official of setting 'onerous' terms for a housing loan it made for the 2010 Winter Olympics.

By ANTHONY EFFINGER **Photograph by ROBBIE McCLARAN**

ONE OF THE THINGS Wesley Edens did soon after his company bought Canadian ski-resort conglomerate Intrawest Corp. in October 2006 was to finance construction of a $43 million gondola at Whistler, British Columbia.

The new lift, completed in December 2008, is the longest unsupported span for any gondola in the world, stretching 2.73 miles (4.4 kilometers). It's also the highest, dangling 1,427 feet (435 meters) over Fitzsimmons Creek between Whistler mountain and its sister peak, Blackcomb. Visitors to the 2010 Winter Olympics, for which Intrawest's Whistler Blackcomb resort is a venue, are likely to ride it just for thrills: Two

Edens began work on his **sky-high gondola** before the meltdown.



Fortress shares have lost 95 percent of their value since their first trading day. **'THERE'S BEEN A LOT OF HARDSHIP IN THE WORLD SINCE THEN,' EDENS SAYS.**

of the 28 cars have glass bottoms.

Two years after commissioning the ski lift, Edens, 47, finds himself staring into an abyss of a different sort. He's the chief executive officer of publicly listed money manager Fortress Investment Group LLC. Edens and his partners became instant billionaires when the company, which manages $34.3 billion in private equity and hedge fund holdings, went public in 2007. The Montana-born Edens, who ski-raced in high school, could have paid for the gondola himself.

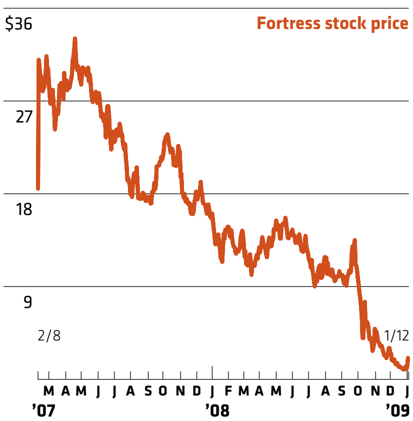
Since then, shares of Fortress have lost most of their value, falling 95 percent to $1.56 as of Jan. 12 from $31 on Feb. 9, 2007, their first trading day. The stock prices of a half dozen other publicly traded companies controlled by Fortress have also plunged.

"There's been a lot of hardship in the world since then," says Edens in a rare interview.

Analysts are bearish on Fortress, even at a rock-bottom price. "The more I've learned about Fortress, the less comfortable I've become," says Jackson Turner, who follows the company at New York–based Argus Research Co. "There's just this drip, drip, drip of bad news." He's been covering Fortress since August and recommends selling the shares. Only one of nine Fortress analysts tracked by Bloomberg rates the shares a buy.

DOWNHILL RACER

Fortress shares peaked two months after the IPO. They've slid since.



Source: Bloomberg

FORTRESS IS A prime example of what happens when the secretive world of hedge funds collides with the public disclosure required of listed companies. Two years after its initial public offering, Fortress remains a tangled web of subsidiaries and partnerships that analyst Turner says is anything but transparent. The New York–based firm buys stocks and bonds through its hedge funds and whole companies through private equity funds. Last year, it started a fund that trades commodities. Fortress owns assisted living facilities for seniors, short-line railroads, newspapers and an array of distressed debt.

Many of the company's hedge and private equity funds are based in the Cayman Islands. Fortress itself is structured as a partnership, which reduces its U.S. taxes and requires the company to use a diagram with five footnotes to lay out the corporate structure in disclosure documents.

Edens manages his sprawling company with a minimum of paperwork. He insists subordinates present plans for asset sales and other complex actions on a single sheet, according to a person who worked with him. "We all got creative with the font sizes we used," the person says.

The credit crunch has forced Fortress into the unwanted glare of publicity. Fortress bought its trove of companies and securities with money from wealthy individuals, endowments and pension funds, augmented with debt. Now, investors are asking for their money back and banks aren't making the loans that financial wizards like Edens used for a decade to double and triple returns on investors' cash. Blackstone Group LP, the $116 billion private equity and hedge fund firm that listed itself four months after Fortress, is facing the same dilemma. (See "Schwarzman Unbowed," page 56.)

In December, Edens cut off disbursements from the company's $8 billion flagship Drawbridge Global Macro hedge funds after investors asked for $3.5 billion back, Fortress said in a December regulatory filing. Since the financial system went

Edens takes a call at the 2007 Allen & Co. media conference in Sun Valley.

MATTHEW STAVER/BLOOMBERG NEWS

haywire in September, other hedge funds, including Chicago-based Citadel Investment Group LLC, run by Kenneth Griffin, and D.E. Shaw & Co., based in New York, have also told investors to wait.

Edens is bailing water in private equity too. In July, Fortress abandoned a $6.1 billion purchase of Penn National Gaming Inc., a racetrack-and-casino company, after borrowing costs jumped and the U.S. economy faltered. Fortress and three partners had to fork over $1.475 billion to terminate the purchase. They paid Penn $225 million in cash and agreed to buy $1.25 billion of preferred Penn stock. The shares pay no dividend, and Penn doesn't have to buy them back until 2015. In essence, it's a seven-year $1.25 billion no-interest loan.

Fortress made headlines again in October when it had difficulty refinancing $1.7 billion of two-year debt it took on in 2006 to buy Intrawest, which runs ski and golf resorts. The company didn't announce the refinancing until the Oct. 23 deadline, spurring concern that Intrawest would run out of cash. "Getting that thing done was challenging," Edens says.

Fortress's dealmaking roiled Canada in January when the mayor of Vancouver disclosed that Fortress had stopped disbursing a C$750 million ($616 million) loan to the builder of a C$1.1 billion village to house Olympic athletes. The developer, Millennium Development Corp., is erecting 16 glass buildings that are to become condominiums after the Games. The terms of the loan, negotiated by Fortress, are that if Millennium defaults, the city will complete the project at taxpayer expense, sell the condos and repay Edens's company.

"The Olympic village is a billion-dollar project, and the city's taxpayers are on the hook for all of it," Mayor Gregor Robertson, 44, said at a news conference. On the hook, that is, to Fortress.

Millennium declined to comment on the matter.

Edens, who cut his financial teeth buying bad debt during the savings and loan crisis of the 1980s, says he's optimistic his company will make it through the crisis. Bad times are good for his style of investing, he says. "From 2003 to '06, there was no distress," he says. "Now everything is distressed. This should be the golden age."

Founded in 1998 by Edens and two partners, Fortress has about 900 employees raising money and investing it. Fortress indirectly employs tens of thousands of additional people in its various private equity investments, 22,000 at Intrawest alone.

Edens is an eclectic investor. In 2005, for example, he refinanced $272.5 million of debt that pop singer Michael Jackson owed to Bank of America Corp., according to documents from a legal dispute over the deal. Jackson was a sketchy risk at the time. He was under indictment for allegedly plying a teenage boy with liquor and molesting him.

Still, Jackson had good collateral: his 2,700-acre (1,093-hectare) Neverland Ranch near Santa Barbara, California—complete with amusement park—and a 50 percent stake in the rights to a collection of Beatles songs.

Jackson was acquitted by a jury in June 2005, the same month that Fortress made the loan. Fortress offered to lend

Jackson a total of $537.5 million so he could buy the remaining 50 percent of the Beatles catalogue, according to court documents. That deal didn't happen.

Fortress filed a notice of default on Neverland on Oct. 16, 2007, after Jackson fell behind in payments. Colony Capital LLC, another private equity firm, bought $23.5 million of the debt in May 2008. Fortress spokeswoman Lilly Donohue declined to comment on what happened to the rest of the loan.

Fortress's other investments are humdrum compared with financing the King of Pop. It owns 60 percent of Brookdale Senior Living Inc., a network of 550 assisted living centers and retirement communities based in Tennessee, and RailAmerica Inc., an operator of short-line railroads. RailAmerica's Bauxite & Northern Railway Co., for one, hauls alumina, the raw material for aluminum, three miles from Bauxite Junction, Arkansas, to Bauxite, Arkansas, where it's refined.

FORTRESS'S INCENTIVE FEES FELL TO $718,000 IN THE THIRD QUARTER OF 2008 FROM $106.7 MILLION. The firm paid no dividend for the past two quarters.

Brookdale shares fell 80 percent in 2008. RailAmerica is closely held.

In addition to its funds and private equity investments, Fortress controls a batch of public companies that all carry the suffix *-castle*. Lately, the castles have been under siege. Aircastle Ltd. buys jetliners and leases them. Its shares fell 82 percent in 2008. Newcastle Investment Corp. buys real estate loans, financing the purchases by selling collateralized-debt obligations—bonds that are sliced into tranches, each of which carries a different credit rating and risk of default. The stock last year was down 94 percent.

Eurocastle Investment Ltd. is an owner of malls and office buildings in Germany. Its stock fell 99 percent in 2008. Seacastle Inc., which rents out shipping containers, remains private after postponing a public offering in January 2008.

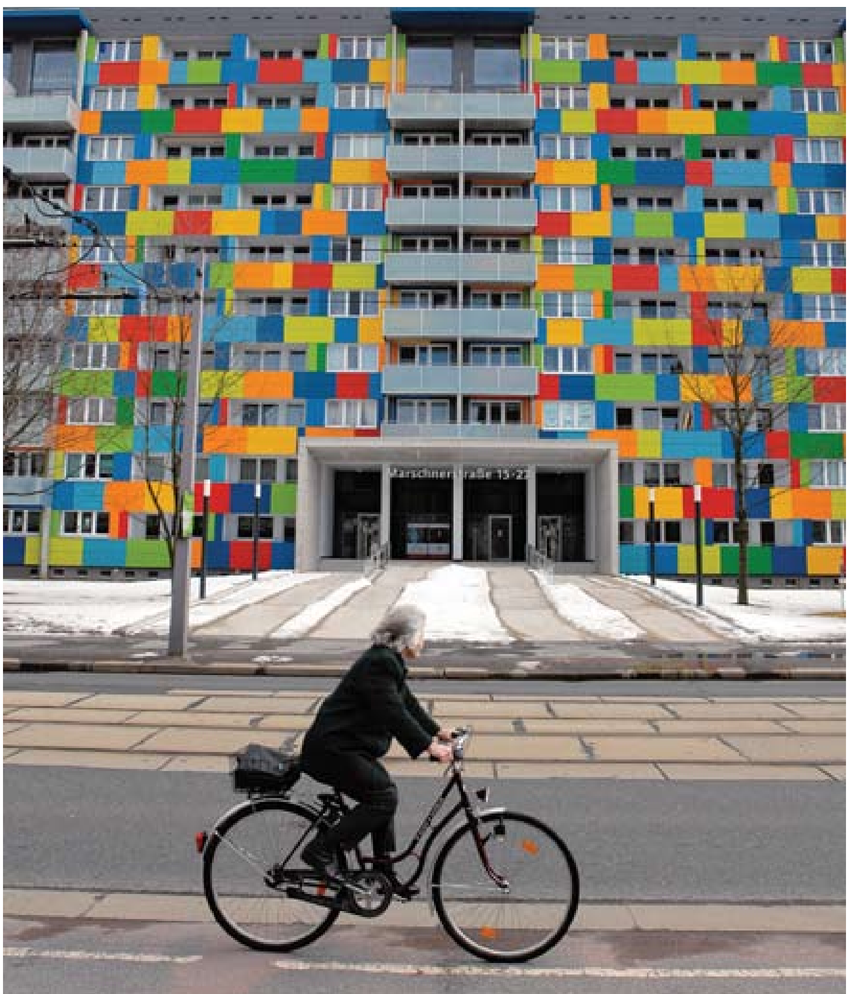
Fortress's revenue comes from fees it earns for managing investments. As with most hedge and private equity funds, it charges a management fee of 1–2 percent of assets, plus an incentive fee of 20 percent of any profits.

Management fees rise with assets. Incentive fees rise with performance, and performance has been poor lately. Fortress collected just $718,000 in incentive payments in the third quarter of 2008, down from $106.7 million a year earlier. The firm canceled its dividend for the last two quarters of 2008.

The problem for Fortress and other hedge funds is that incentive fees could be zero for a long time. In order to collect them again, Fortress must first make up any losses in its funds, returning to the "high-water mark." It can collect its 20 percent only after losses are recouped.

At the end of October, Drawbridge Global Macro was 26 percent below its high-water mark, Fortress said in a regulatory filing. Drawbridge Special Opportunities, another hedge fund, was down 18 percent.

Edens says Fortress will survive because it doesn't have to give panicked investors their money back immediately. About 73 percent of the $34.3 billion that Fortress managed in September was locked up for at least 2.6 years, according to a table Fortress distributed to analysts in November. And even if returns are zero, the company makes $500 million annually from its management fees, it says.



Fortress bought 48,000 apartments from the city of Dresden, Germany, in 2006.

MATTHIAS RIETSCHEL/AP WIDEWORLD

Moreover, only 8 percent of the debt that Fortress borrowed to make private equity purchases—about $3.1 billion out of $36.8 billion—must be paid off in 2009, according to a Fortress chart.

Edens rules his empire from an office in midtown Manhattan. He lives in an apartment on exclusive Central Park West with his wife and children and owns a house tucked into the trees on the island of Martha's Vineyard, Massachusetts.

EDENS HAS AN interest in politics. He is friends with Montana Senator Max Baucus, a Democrat, and has given about $125,000 to Democratic candidates since 2000 compared with $4,600 to Republicans, according to the Washington-based Center for Responsive Politics.

Former North Carolina Senator John Edwards was on the payroll at Fortress for about a year starting in October 2005. He earned an annual salary of $479,512 and invested in Fortress funds. He left the firm in December 2006 to run for president. His former Fortress co-workers supported his bid, donating more than $150,000 to his campaign.

Clockwise from top: Fortress's diverse holdings include **industrial railroads** and the **Brookdale** chain of assisted living facilities. Edens refinanced a loan on **Michael Jackson's Neverland ranch**.

BOB PICKERING (TOP); LOIS BERNSTEIN/AP WIDEWORLD; JEFF ADKINS

Edens grew up near Helena, Montana. His father was a school psychologist who later started a stable where he raised Morgan horses. Wesley Edens still jumps horses with his daughter. "Nice kid, bright kid," says Randy Carlson, one of Edens's teachers at Capital High School in Helena and a friend of his father's. "He'd speak his mind and ask questions."

Edens attended Oregon State University in Corvallis, where he studied finance, graduating in 1984. He went to work for a California savings and loan after college, then did short stints at Merrill Lynch & Co. and Smith Barney. He joined Lehman Brothers Holdings Inc. in 1987 and made his name there buying distressed mortgages from the Resolution Trust Corp. during the savings and loans crisis. He joined New York–based investment firm BlackRock Inc. in 1993 and there started his first private equity fund, called BlackRock Asset Investors. In 1997, Edens and two BlackRock colleagues—Randal Nardone, now 53, and Robert Kauffman, 45—bolted to UBS AG, where they invested the Swiss bank's money in distressed assets. A year and a day later, the trio resigned to start Fortress. Two Goldman Sachs Group Inc. partners, Peter Briger, now 45, and Michael Novogratz, 44, joined as co-owners of Fortress in 2002.

Fortress grew rapidly, taking advantage of the big investor appetite for hedge funds and private equity. Assets under management rocketed to $30 billion in 2006 from $1.2 billion at the end of 2001. Net income at the company rose to $192.7 million in 2005 from $14.6 million in 2001, a 13-fold increase in four years. Management fees and incentive income rose 30-fold to $284.3 million in 2005 from $9.1 million in 2001.

The five owners prospered, earning a portion of management fees plus gains on investments Fortress made with its

A TANGLED WEB

Fortress's Edens manages a diverse group of funds and companies.

ASSETS UNDER MANAGEMENT, IN BILLIONS

PRIVATE EQUITY FUNDS	$13.7
Intrawest (resorts)	
RailAmerica (railroads)	
Mapeley (U.K. property management)	
GateHouse Media (newspapers)	
Brookdale Senior Living (assisted living centers)	
LIQUID HEDGE FUNDS	**$9.1**
Drawbridge Global Macro funds	
Fortress Commodities Fund	
HYBRID HEDGE FUNDS	**$8.2**
Drawbridge Special Opportunities funds	
Fortress Partners funds	
CASTLES*	**$3.3**
Aircastle (aircraft leasing)	
Newcastle Investment (U.S. real estate debt)	
Eurocastle Investment (European real estate)	
Seacastle (shipping containers)	

*Public companies, except Seacastle, which suspended its IPO in January 2008. All figures are as of Sept. 30, 2008. Source: Fortress Investment Group

own cash. They paid themselves $447 million in 2006, according to regulatory filings. Edens got the most at $109.2 million. Kauffman brought up the rear at $66.4 million. By comparison, Lloyd Blankfein, CEO of Goldman Sachs, made $53.4 million that year.

"They fancy themselves the other Goldman," says a person who's dealt with Fortress and declined to be named. "And they are at least as sharp."

Fortress said in regulatory filings that it decided to do an IPO because the sale would allow it to raise capital, reward employees with equity in the company and establish Fortress as an institution with staying power.

Edens rang the bell on the New York Stock Exchange on Feb. 9, 2007; that day, the shares rose 68 percent. Fortress's principals kept 78 percent of the stock, and by day's end Edens's 18.1 percent stake was worth $2.3 billion.

Today, almost all of Edens's pay comes from dividends on the stock. If Fortress doesn't restart its dividend, Edens and his co-owners will make only their salaries of $200,000 this year.

The only Fortress partner who cuts any kind of public figure is Novogratz. He runs the Fortress hedge funds that invest in stocks, bonds and currencies. Fellow Goldman alumnus Briger runs hedge funds that invest in more-esoteric real estate loans and the debt of distressed companies.

Novogratz was a wrestler at Princeton University and a helicopter pilot for the U.S. Army before his career in finance. He bought a duplex apartment in Manhattan's Tribeca neighborhood from actor Robert DeNiro for $12.3 million in 2005. A year later, he added the apartment below for $5.3 million. Novogratz throws parties that usually attract a celebrity or two, according to a person who's been to them.

Novo, as he's known, is more outspoken than his boss. In May, he appeared at a *New Yorker* magazine conference, where he said that financiers made big money because the world is short of talented investment managers. "Wall Street is getting paid these enormous sums—not because they are manipulating the system," Novogratz said. "It's because there is a supply-demand imbalance."

He expounded on globalization, too, saying he's a fan of China. People there work hard, which makes the country appealing to Americans, he said. "You go to the Middle East, and you say, broadly, this group of people is lucky they live on top of dead dinosaur bones," Novogratz said in reference to the region's oil wealth.

Fortress's highest-profile purchase to date has been Intrawest. Jackson at Argus says the Vancouver-based company is probably Fortress's biggest holding. Surprisingly for a former ski racer, Edens says he has never skied most of Intrawest's resorts. And he has yet to see the new gondola at Whistler.

Intrawest was born in 1976 when Joe Houssian, a former Xerox Corp. salesman, started buying residential real estate in Vancouver. Ten years later, he bought Blackcomb Mountain and became a ski-area operator. He snapped up more resorts after that, including Quebec's Mont Tremblant in 1991 and both Whistler and Copper Mountain, Colorado, in 1996.

HOUSSIAN HELPED CHANGE the ski industry into what it is today—a real estate business with ski areas attached. Intrawest listed its shares on the New York Stock Exchange in 1997, and in 2006 Intrawest had revenue of $1.6 billion. That fiscal year, ended in June, operating profit from selling real estate totaled $147.6 million compared with $88.7 million for resort operations.

Early in 2006, Intrawest's biggest investor, Pirate Capital LLC, a $1.8 billion activist hedge fund in Norwalk, Connecticut, grumbled that the company was worth far more than what its share price reflected. Pirate founder Tom Hudson demanded that Houssian sell. "We urge you to fulfill your fiduciary duties to

Robert Kauffman, left, is one of the founders of Fortress. **Michael Novogratz**, center, runs hedge funds that invest in securities, while **Peter Briger** deals in real estate loans.

all shareholders by immediately initiating a sale of the entire company," Pirate wrote to Intrawest in March 2006.

Fortress rival Blackstone considered a bid, according to a person familiar with the situation. In the end, Fortress snatched Intrawest for $1.8 billion. Resorts were hot investments at the time. Condos in ski villages were selling as fast as developers could build them. Two months after the purchase closed, Intrawest announced a deal to buy the Steamboat ski resort in Colorado for $265 million.

Edens continued buying up resort real estate. In April 2007, just after announcing the gondola project at Whistler, Fortress's Drawbridge Special Opportunities fund and two other investors paid $54 million for a cluster of 1970s buildings at the base of Steamboat mountain, according to a solicitation to other investors. The plan was to tear them down and build condominiums to sell.

The old buildings are gone, yet new ones haven't begun. Fortress and its partners—Colorado developer Atira Group and Cafritz Interests LLC of Washington—would not comment on the status of the project.

Fortress shares closed at a record high of $33.07 on April 19, 2007. In May, Edens was honored as a Distinguished Business Professional by Oregon State and gave the keynote speech at a conference sponsored by the school's entrepreneurship program. "If you want to be expert in something, don't pick something small," Edens told the group. "Pick something big."

Edens picked something big two months later, when Fortress got involved in the construction of Vancouver's Olympic village. It has since become big and ugly. In June 2007, the Vancouver City Council held a secret meeting; it's allowed by law to meet in private. The council agreed to terms set by Fortress in exchange for lending C$750 million to Millennium, the developer of the village. Councillor Geoff Meggs described parts of the secret meeting at a public one on Jan. 12.

Eager to keep construction going so

Skiers wait to board the **Whistler gondola** for an early season ride down the mountain.

the athletes' housing would be finished by the time the Games began in the winter of 2010, the city agreed to pay C$190 million of the Fortress loan in cash if Millennium defaulted and to finish the development at taxpayers' expense if Millennium couldn't. City officials didn't disclose those guarantees until early 2008, when a description of them appeared on page 21 of the city of Vancouver's financial report for 2007.

"The city may face—and I hope does not—the largest financial loss in its history," Meggs said at the Jan. 12 meeting. He called Fortress's terms "onerous."

OLYMPIC FINANCIAL FIASCOES are a sore subject in Canada. When Montreal hosted the Summer Games in 1976, corruption, mismanagement and architectural snafus left taxpayers with about C$1.50 billion in debt that wasn't paid off until November 2006.

The Olympic village deal looked safe at first. In October 2007, people slept outside Millennium's showroom to put deposits on condominiums that weren't yet built and that they wouldn't be able to occupy for almost two years.

Fortress disbursed C$317 million of the loan in installments as Millennium worked and incurred expenses. In the meantime, the credit contagion crossed the Canadian border, and sales of the 733-unit project stalled. Millennium had sold about 250 of the 489 units that had hit the market as of mid-January. The rest are to be offered later in the year.

Fortress stopped funding construction in September, when Millennium went C$125 million over budget and could present no plan for raising money to close the gap, new City Manager Penny Ballem said at the Jan. 12 meeting. Fortress had the right to cut off credit under the loan agreement, she said.

The city council stepped up soon after Fortress stepped out. In another secret meeting in October, the council agreed to lend Millennium C$100 million to keep the project going. The city doled out the money as Millennium incurred costs, just as Fortress had, Ballem says. The last C$21 million was paid on Jan. 15.

PAGE LEFT: MATTHIAS HIEKEL/LANDOV; COURTESY WRESTLING HALL OF FAME; NAJLAH FEANNY/CORBIS;
TOP RIGHT: ROBBIE MCCLARAN

The Fortress-backed **Olympic village** under construction in Vancouver

Robertson says the city is talking with Fortress to get the money flowing again. "We are negotiating in good faith with Fortress," he said at a Jan. 9 press conference.

Standard & Poor's on Jan. 13 said it may cut Vancouver's AA+ credit rating because of its obligations to Fortress.

Fortress spokeswoman Donohue declined to comment on the Olympic village project.

Fortress's deal with Vancouver guarantees it will get most of its loan money back. And Edens insists that his other investments will also survive the carnage wrought by the credit collapse. Even with markets frozen, Fortress raised $8.7 billion in new capital in the first 10 months of 2008, more than offsetting redemptions by nervous investors.

Edens declined to say whether Fortress's owners are considering taking the company private again—even though its shares sell for less than the price of a New York City subway ride. "There are fewer reasons to be public now than there were two years ago," Edens says.

AT INTRAWEST, THE weather has been going Edens's way. Copper Mountain in Colorado got more than 3 feet (0.91 meters) of snow in early January. Steamboat got 4 feet in the first week of the new year alone. Fresh powder could lure cash-strapped skiers up to the mountains.

And there's that new gondola at Whistler. A notice to Fortress investors who've had enough excitement: The two cars with the glass floors are silver. The 26 without the dizzying view straight down are red. **B**

Anthony Effinger is a senior writer at Bloomberg News in Portland, Oregon. aeffinger@bloomberg.net With reporting by **Christopher Donville** in Vancouver and **Katherine Burton** in New York.

To write a letter to the editor, send an e-mail to bloombergmag@bloomberg.net or **type MAG <Go>**.

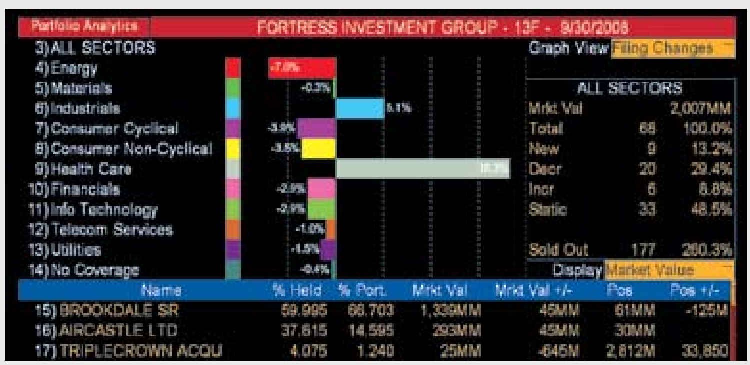
Tracking Fortress's Holdings

You can use the 13F Filing Summaries (FLNG) function to view Fortress Investment Group LLC's stock holdings as disclosed in the company's most recent quarterly filing with the U.S. Securities and Exchange Commission. Type FLNG <Go>. Tab in to the field under Company Name, enter *FORTRESS* and press <Go>. Click on the company's name to view stock holdings by industry and individual company name.

Click on the arrow to the right of Graph View and select Filing Changes and on the arrow to the right of Display and select Market Value if they aren't already selected. The top part of the screen breaks out Fortress's stock holdings by industry and shows any changes from the prior quarter, as shown at right. The bottom part lists Fortress's individual equity investments by market value.

For further analysis, click on the Portfolio Analytics button on the red tool bar to view a menu of analytical functions on another Bloomberg Professional screen. Click on PSD. The screen shows Fortress's top holdings and displays a snapshot of their value based on measures such as price-earnings ratio. To analyze the portfolio using gauges you select, click on the arrow to the right of Templates on the red tool bar at the top of the screen and select New Template. Click on the plus signs under Available Fields to select the measures you want to display. Enter a name in the field next to Name and click on Update to see the results.

BETH WILLIAMS



ROBBIE McCLARAN