KKR & Co. L.P.
Form 10-Q
November 02, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-Q

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

For the quarterly period ended September 30, 2012

Or

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

For the Transition period from to .

Commission File Number 001-34820

KKR & CO. L.P.

(Exact name of Registrant as specified in its charter)

Delaware (State or other Jurisdiction of Incorporation or Organization)	**26-0426107** (I.R.S. Employer Identification Number)

9 West 57 th Street, Suite 4200

New York, New York 10019

Telephone: (212) 750-8300

(Address, zip code, and telephone number, including

area code, of registrant s principal executive office.)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

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

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

As of October 31, 2012, there were 243,654,461 Common Units of the registrant outstanding.

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FORM 10-Q

For the Quarter Ended September 30, 2012

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which reflect our current views with respect to, among other things, our operations and financial performance. You can identify these forward-looking statements by the use of words such as outlook, believe, expect, potential, continue, may, shoul approximately, predict, intend, will, plan, estimate, anticipate or the negative version of these words or other comparable words. With limiting the foregoing, statements regarding the expected synergies from the acquisition of Prisma Capital Partners LP and its affiliates may constitute forward-looking statements that are subject to the risk that the terms of these transactions may be modified, the transactions may not be completed at all or the benefits and anticipated synergies from such transactions are not realized. Forward-looking statements are subject to various risks and uncertainties. Accordingly, there are or will be important factors that could cause actual outcomes or results to differ materially from those indicated in these statements. We believe these factors include but are not limited to those described under the section entitled Risk Factors in this report. These factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included in this report and in our other periodic filings. We do not undertake any obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise, except as required by applicable law.

In this report, references to KKR, we, us, our and our partnership refer to KKR & Co. L.P. and its consolidated subsidiaries. Prior to KKR & L.P. becoming listed on the New York Stock Exchange (NYSE) on July 15, 2010, KKR Group Holdings L.P. consolidated the financial results of KKR Management Holdings L.P. and KKR Fund Holdings L.P. (together, the KKR Group Partnerships) and their consolidated subsidiaries.

References to our Managing Partner are to KKR Management LLC, which acts as our general partner and unless otherwise indicated, references to equity interests in KKR s business, or to percentage interests in KKR s business, reflect the aggregate equity of the KKR Group Partnerships and are net of amounts that have been allocated to our principals in respect of the carried interest from KKR s business as part of our carry pool and certain minority interests. References to our principals are to our senior employees and non-employee operating consultants who hold interests in KKR s business through KKR Holdings L.P., which we refer to as KKR Holdings , and references to our senior principals are to principals who also hold interests in our Managing Partner entitling them to vote for the election of its directors.

In this report, the term assets under management, or AUM , represents the assets from which KKR is entitled to receive fees or a carried interest and general partner capital. We believe this measure is useful to investors as it provides additional insight into KKR s capital raising activities and the overall activity in its investment funds and vehicles. KKR calculates the amount of AUM as of any date as the sum of: (i) the fair value of the investments of KKR s investment funds plus uncalled capital commitments from these funds; (ii) the fair value of investments in KKR s co-investment vehicles; (iii) the net asset value of certain of KKR s fixed income products; (iv) the value of outstanding structured finance vehicles and (v) the fair value of other assets managed by KKR. KKR s definition of AUM is not based on the definitions of AUM that may be set forth in agreements governing the investment funds, vehicles or accounts that it manages and is not calculated pursuant to any regulatory definitions.

In this report, the term fee paying assets under management, or FPAUM , represents only those assets under management from which KKR receives fees. We believe this measure is useful to investors as it provides additional insight into the capital base upon which KKR earns management fees. This relates to KKR s capital raising activities and the overall activity in its investment funds and vehicles, for only those funds and vehicles where KKR receives fees (i.e., excluding vehicles that receive only carried interest or general partner capital). FPAUM is the sum of all of the individual fee bases that are used to calculate KKR s fees and differs from AUM in the following respects: (i) assets from which KKR does not receive a fee are excluded (i.e., assets with respect to which it receives only carried interest); and (ii) certain assets, primarily in its private equity funds, are reflected based on capital commitments and invested capital as opposed to fair value because fees are not impacted by changes in the fair value of underlying investments.

In this report, the term fee related earnings, or FRE , is comprised of segment operating revenues less segment operating expenses and is used by management as an alternative measurement of the operating earnings of KKR and its business segments before investment income. We believe this measure is useful to investors as it provides additional insight into the operating profitability of our fee generating management companies and capital markets businesses. The components of FRE on a segment basis differ from the equivalent GAAP amounts on a consolidated basis as a result of: (i) the inclusion of management fees earned from consolidated funds that were eliminated in consolidation; (ii) the exclusion of fees and expenses of certain consolidated entities; (iii) the exclusion of charges relating to the amortization of intangible assets; (iv) the exclusion of charges relating to carry pool

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allocations; (v) the exclusion of non-cash equity charges and other non-cash compensation charges borne by KKR Holdings or incurred under the KKR & Co. L.P. 2010 Equity Incentive Plan; (vi) the exclusion of certain reimbursable expenses; and (vii) the exclusion of certain non-recurring items.

In this report, the term economic net income (loss), or ENI , is a measure of profitability for KKR s reportable segments and is used by management as an alternative measurement of the operating and investment earnings of KKR and its business segments. We believe this measure is useful to investors as it provides additional insight into the overall profitability of KKR s businesses inclusive of investment income and carried interest. ENI is comprised of: (i) FRE; plus (ii) segment investment income (loss), which is reduced for carry pool allocations and management fee refunds; less (iii) certain economic interests in KKR s segments held by third parties. ENI differs from net income (loss) on a GAAP basis as a result of: (i) the exclusion of the items referred to in FRE above; (ii) the exclusion of investment income (loss) relating to noncontrolling interests; and (iii) the exclusion of income taxes.

In this report, syndicated capital is the aggregate amount of debt or equity capital in transactions originated by KKR investment funds and vehicles, which has been distributed to third parties in exchange for a fee. It does not include capital committed to such transactions by carry-yielding co-investment vehicles, which is instead reported in committed dollars invested. Syndicated capital is used as a measure of investment activity for KKR and its business segments during a given period, and we believe that this measure is useful to investors as it provides additional insight into levels of syndication activity in KKR s Capital Markets and Principal Activities segment and across its investment platform.

You should note that our calculations of AUM, FPAUM, FRE, ENI, syndicated capital and other financial measures may differ from the calculations of other investment managers and, as a result, our measurements of AUM, FPAUM, FRE, ENI, syndicated capital and other financial measures may not be comparable to similar measures presented by other investment managers.

References to our funds or our vehicles refer to investment funds, vehicles and/or accounts advised, sponsored or managed by one or more subsidiaries of KKR, unless context requires otherwise.

In this report, the term GAAP refers to generally accepted accounting principles in the United States.

Unless otherwise indicated, references in this report to our fully diluted common units outstanding, or to our common units outstanding on a fully diluted basis, reflect (i) actual common units outstanding, (ii) common units into which KKR Group Partnership Units not held by us are exchangeable pursuant to the terms of the exchange agreement described in this report and (iii) common units issuable pursuant to any equity awards actually issued under the KKR & Co. L.P. 2010 Equity Incentive Plan, which we refer to as our Equity Incentive Plan, but do not reflect common units available for issuance pursuant to our Equity Incentive Plan for which grants have not yet been made.

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KKR & CO. L.P.

CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (Unaudited)

(Amounts in Thousands, Except Unit Data)

	September 30, 2012	December 31, 2011
Assets		
Cash and Cash Equivalents	$ 1,278,354	$ 843,261
Cash and Cash Equivalents Held at Consolidated Entities	325,084	930,886
Restricted Cash and Cash Equivalents	69,582	89,828
Investments	40,940,868	37,495,360
Due from Affiliates	124,932	149,605
Other Assets	909,800	868,705
Total Assets	$ 43,648,620	$ 40,377,645
Liabilities and Equity		
Debt Obligations	$ 1,314,845	$ 1,564,716
Due to Affiliates	58,191	43,062
Accounts Payable, Accrued Expenses and Other Liabilities	1,634,884	1,085,217
Total Liabilities	3,007,920	2,692,995
Commitments and Contingencies		
Redeemable Noncontrolling Interests	472,837	275,507
Equity		
KKR & Co. L.P. Partners Capital (241,407,805 and 227,150,182 common units issued and outstanding as of September 30, 2012 and December 31, 2011, respectively)	1,844,057	1,330,887
Accumulated Other Comprehensive Income (Loss)	(1,526)	(2,189)
Total KKR & Co. L.P. Partners Capital	1,842,531	1,328,698
Noncontrolling Interests	38,325,332	36,080,445
Total Equity	40,167,863	37,409,143
Total Liabilities and Equity	$ 43,648,620	$ 40,377,645

See notes to condensed consolidated financial statements.

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KKR & CO. L.P.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

(Amounts in Thousands, Except Unit Data)

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Revenues				
Fees	$ 162,154	$ 164,808	$ 390,821	$ 514,263
Expenses				
Compensation and Benefits	366,350	48,948	1,019,400	677,917
Occupancy and Related Charges	14,344	13,702	43,636	39,085
General, Administrative and Other	65,825	66,180	177,480	166,866
Total Expenses	446,519	128,830	1,240,516	883,868
Investment Income (Loss)				
Net Gains (Losses) from Investment Activities	2,308,613	(3,339,020)	6,997,166	467,278
Dividend Income	10,440	71,106	263,298	107,129
Interest Income	95,578	64,858	259,669	218,975
Interest Expense	(17,868)	(17,742)	(52,757)	(52,365)
Total Investment Income (Loss)	2,396,763	(3,220,798)	7,467,376	741,017
Income (Loss) Before Taxes	2,112,398	(3,184,820)	6,617,681	371,412
Income Taxes	9,612	11,535	37,777	67,923
Net Income (Loss)	2,102,786	(3,196,355)	6,579,904	303,489
Net Income (Loss) Attributable to Redeemable Noncontrolling Interests	9,994		18,551	
Net Income (Loss) Attributable to Noncontrolling Interests	1,965,381	(2,952,953)	6,097,245	347,705
Net Income (Loss) Attributable to KKR & Co. L.P.	$ 127,411	$ (243,402)	$ 464,108	$ (44,216)
Distributions Declared per KKR & Co. L.P. Common Unit	$ 0.24	$ 0.10	$ 0.52	$ 0.42
Net Income (Loss) Attributable to KKR & Co. L.P. Per Common Unit				
Basic	$ 0.53	$ (1.09)	$ 1.98	$ (0.20)
Diluted	$ 0.49	$ (1.09)	$ 1.86	$ (0.20)
Weighted Average Common Units Outstanding				
Basic	239,696,358	222,733,648	234,876,879	218,501,107
Diluted	257,646,622	222,733,648	249,359,200	218,501,107

See notes to condensed consolidated financial statements.

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KKR & CO. L.P.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(Amounts in Thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	**2011**	**2012**	**2011**
Net Income (Loss)	$ 2,102,786	$ (3,196,355)	$ 6,579,904	$ 303,489
Other Comprehensive Income (Loss), Net of Tax:				
Foreign Currency Translation Adjustments	5,768	(6,689)	362	(4,968)
Comprehensive Income (Loss)	2,108,554	(3,203,044)	6,580,266	298,521
Less: Comprehensive Income (Loss) Attributable to Redeemable Noncontrolling Interests	(9,994)		(18,551)	
Less: Comprehensive Income (Loss) Attributable to Noncontrolling Interests	(1,968,908)	2,957,592	(6,096,686)	(344,202)
Comprehensive Income (Loss) Attributable to KKR & Co. L.P.	$ 129,652	$ (245,452)	$ 465,029	$ (45,681)

See notes to condensed consolidated financial statements.

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KKR & CO. L.P.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (Unaudited)

(Amounts in Thousands, Except Unit Data)

	KKR & Co. L.P.					
	Common Units	**Partners Capital**	**Accumulated Other Comprehensive Income (Loss)**	**Noncontrolling Interests**	**Total Equity**	**Redeemable Noncontrolling Interests**
Balance at January 1, 2011	212,770,091	$ 1,324,530	$ 1,963	$ 34,673,549	$ 36,000,042	$
Net Income (Loss)		(44,216)		347,705	303,489	
Other Comprehensive Income (Loss)-Foreign Currency Translation Adjustments			(1,465)	(3,503)	(4,968)	
Contribution of Net Assets of previously Unconsolidated Entities				69,600	69,600	
Exchange of KKR Holdings L.P. Units to KKR & Co. L.P. Common Units	10,157,372	103,695	85	(103,780)		
Deferred Tax Effects Resulting from Exchange of KKR Holdings L.P. Units to KKR & Co. L.P. Common Units		1,530	20		1,550	
Delivery of Common Units - Equity Incentive Plan	17,205					
Equity Based Compensation		11,165		375,368	386,533	
Capital Contributions				3,812,856	3,812,856	
Capital Distributions		(132,068)		(4,522,612)	(4,654,680)	
Balance at September 30, 2011	222,944,668	$ 1,264,636	$ 603	$ 34,649,183	$ 35,914,422	$

	KKR & Co. L.P.					
	Common Units	**Partners Capital**	**Accumulated Other Comprehensive Income (Loss)**	**Noncontrolling Interests**	**Total Equity**	**Redeemable Noncontrolling Interests**
Balance at January 1, 2012	227,150,182	$ 1,330,887	$ (2,189)	$ 36,080,445	$ 37,409,143	$ 275,507
Net Income (Loss)		464,108		6,097,245	6,561,353	18,551
Other Comprehensive Income (Loss)-Foreign Currency Translation Adjustments			921	(559)	362	
	13,151,729	138,280	(161)	(138,119)		

Exchange of KKR Holdings L.P. Units to KKR & Co. L.P. Common Units						
Deferred Tax Effects Resulting from Exchange of KKR Holdings L.P. Units to KKR & Co. L.P. Common Units		1,320	(97)		1,223	
Delivery of Common Units - Equity Incentive Plan	1,105,894					
Equity Based Compensation		47,679		282,358	330,037	
Capital Contributions				2,276,163	2,276,163	179,767
Capital Distributions		(138,217)		(6,272,201)	(6,410,418)	(988)
Balance at September 30, 2012	241,407,805	$ 1,844,057	$ (1,526)	$ 38,325,332	$ 40,167,863	$ 472,837

See notes to condensed consolidated financial statements.

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KKR & CO. L.P.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(Amounts in Thousands)

	Nine Months Ended September 30, 2012	2011
Operating Activities		
Net Income (Loss)	$ 6,579,904	$ 303,489
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided (Used) by Operating Activities:		
Equity Based Compensation	330,037	386,533
Net Realized (Gains) Losses on Investments	(3,240,874)	(2,906,193)
Change in Unrealized (Gains) Losses on Investments	(3,756,292)	2,438,915
Other Non-Cash Amounts	(35,113)	(55,782)
Cash Flows Due to Changes in Operating Assets and Liabilities:		
Change in Cash and Cash Equivalents Held at Consolidated Entities	605,227	268,555
Change in Due from / to Affiliates	(31,536)	(16,091)
Change in Other Assets	48,239	(29,892)
Change in Accounts Payable, Accrued Expenses and Other Liabilities	372,000	212,613
Investments Purchased	(8,006,391)	(6,958,884)
Cash Proceeds from Sale of Investments	11,754,084	7,248,851
Net Cash Provided (Used) by Operating Activities	4,619,285	892,114
Investing Activities		
Change in Restricted Cash and Cash Equivalents	20,246	(30,998)
Purchase of Furniture, Computer Hardware and Leasehold Improvements	(28,627)	(4,801)
Net Cash Provided (Used) by Investing Activities	(8,381)	(35,799)
Financing Activities		
Distributions to Partners	(138,217)	(132,068)
Distributions to Redeemable Noncontrolling Interests	(988)	
Contributions from Redeemable Noncontrolling Interests	179,767	
Distributions to Noncontrolling Interests	(6,233,832)	(4,522,612)
Contributions from Noncontrolling Interests	2,276,163	3,812,856
Proceeds from Debt Obligations	519,996	79,476
Repayment of Debt Obligations	(770,924)	(1,356)
Financing Costs Paid	(7,776)	(9,535)
Net Cash Provided (Used) by Financing Activities	(4,175,811)	(773,239)
Net Increase/(Decrease) in Cash and Cash Equivalents	435,093	83,076
Cash and Cash Equivalents, Beginning of Period	843,261	738,693
Cash and Cash Equivalents, End of Period	$ 1,278,354	$ 821,769

See notes to condensed consolidated financial statements.

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KKR & CO. L.P.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited) (Continued)

(Amounts in Thousands)

	Nine Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
Supplemental Disclosures of Cash Flow Information				
Payments for Interest	$	124,522	$	42,195
Payments for Income Taxes	$	59,041	$	59,680
Supplemental Disclosures of Non-Cash Investing and Financing Activities				
Non-Cash Contributions of Equity Based Compensation	$	330,037	$	386,533
Non-Cash Distributions to Noncontrolling Interests	$	38,369	$	
Exchange of KKR Holdings L.P. Units to KKR & Co. L.P. Common Units	$	138,119	$	103,780
Net Deferred Tax Effects Resulting from Exchange of KKR Holdings L.P. Units to KKR & Co. L.P. Common Units Including the Effect of the Tax Receivable Agreement	$	1,223	$	1,550
Foreign Exchange Gains (Losses) on Debt Obligations	$	(901)	$	
Contribution of Net Assets of Previously Unconsolidated Entities				
Investments	$		$	57,722
Cash and Cash Equivalents Held at Consolidated Entities	$		$	11,504
Due from Affiliates	$		$	4,244
Other Assets	$		$	4,164
Accounts Payable, Accrued Expenses and Other Liabilities	$		$	8,034

See notes to condensed consolidated financial statements.

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KKR & CO. L.P.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(All Dollars are in Thousands, Except Unit, Per Unit Data, and Except Where Noted)

1. ORGANIZATION

KKR & Co. L.P. (NYSE:KKR), together with its consolidated subsidiaries (KKR), is a leading global investment firm that offers a broad range of investment management services to investors and provides capital markets services for the firm, its portfolio companies and third parties. Led by Henry Kravis and George Roberts, KKR conducts business with offices around the world, which provides a global platform for sourcing transactions, raising capital and carrying out capital markets activities. KKR operates as a single professional services firm and carries out its investment activities under the KKR brand name.

KKR & Co. L.P. was formed as a Delaware limited partnership on June 25, 2007 and its general partner is KKR Management LLC (the Managing Partner). KKR & Co. L.P. is the parent company of KKR Group Limited, which is the non-economic general partner of KKR Group Holdings L.P. (Group Holdings), and KKR & Co. L.P. is the sole limited partner of Group Holdings. Group Holdings holds a controlling economic interest in each of (i) KKR Management Holdings L.P. (Management Holdings) through KKR Management Holdings Corp., a Delaware corporation which is a domestic corporation for U.S. federal income tax purposes, and (ii) KKR Fund Holdings L.P. (Fund Holdings and together with Management Holdings, the KKR Group Partnerships) directly and through KKR Fund Holdings GP Limited, a Cayman Island limited company which is a disregarded entity for U.S federal income tax purposes. Group Holdings also owns certain economic interests in Management Holdings through a wholly owned Delaware corporate subsidiary of KKR Management Holdings Corp. and certain economic interests in Fund Holdings through a Delaware partnership of which Group Holdings is the general partner with a 99% economic interest and KKR Management Holdings Corp. is a limited partner with a 1% economic interest. KKR & Co. L.P., through its indirect controlling economic interests in the KKR Group Partnerships, is the holding partnership for the KKR business.

KKR & Co. L.P. both indirectly controls the KKR Group Partnerships and indirectly holds equity units in each KKR Group Partnership (collectively, KKR Group Partnership Units) representing economic interests in KKR s business. The remaining KKR Group Partnership Units are held by KKR s principals through KKR Holdings L.P. (KKR Holdings), which is not a subsidiary of KKR. As of September 30, 2012, KKR & Co. L.P. held 35.27% of the KKR Group Partnership Units and KKR s principals held 64.73% of the KKR Group Partnership Units through KKR Holdings. The percentage ownership in the KKR Group Partnerships will continue to change as KKR Holdings and/or KKR s principals exchange units in the KKR Group Partnerships for KKR & Co. L.P. common units.

The following table presents the effects of changes in the ownership interest in the KKR Group Partnerships on KKR & Co. L.P. s equity:

	Three Months Ended September 30,	Nine Months Ended September 30,

	2012	2011	2012	2011
Net income (loss) attributable to KKR & Co. L.P.	$ 127,411	$ (243,402)	$ 464,108	$ (44,216)
Transfers from noncontrolling interests:				
Increase in KKR & Co. L.P. partners capital for exchange of 2,784,209 and 413,061 for the three months ended September 30, 2012 and 2011, respectively and 13,151,729 and 10,157,372 for the nine months ended September 30, 2012 and 2011, respectively KKR Group Partnership units held by KKR Holdings, net of deferred taxes	31,308	4,224	139,342	105,330
Change from net income (loss) attributable to KKR & Co. L.P. and transfers from noncontrolling interests held by KKR Holdings	$ 158,719	$ (239,178)	$ 603,450	$ 61,114

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of KKR & Co. L.P. have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and the instructions to Form 10-Q. The condensed consolidated financial statements, including these notes, are unaudited and exclude some of the disclosures required in annual financial statements. Management believes it has made all necessary adjustments (consisting of only normal recurring items) such that the condensed consolidated financial statements are presented fairly and that estimates made in preparing the condensed consolidated financial statements are reasonable and prudent. The operating results presented for interim periods are not necessarily indicative of the results that may be expected for any other interim period or for the entire year. These condensed consolidated financial statements should be read in conjunction with the audited consolidated and combined financial statements included in KKR & Co. L.P. s Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC).

The condensed consolidated financial statements (referred to hereafter as the financial statements) include the accounts of KKR s management and capital markets companies, the general partners of certain unconsolidated funds, general partners of consolidated funds and their respective consolidated funds (the KKR Funds) and certain other entities.

KKR & Co. L.P. consolidates the financial results of the KKR Group Partnerships and their consolidated subsidiaries. KKR Holdings ownership interest in the KKR Group Partnerships is reflected as noncontrolling interests in the accompanying financial statements.

References in the accompanying financial statements to KKR s principals are to KKR s senior employees and non-employee operating consultants who hold interests in KKR s business through KKR Holdings, including those principals who also hold interests in the Managing Partner entitling those principals to vote for the election of the managing partners directors (the Senior Principals).

Use of Estimates

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of fees, expenses and investment income (loss) during the reporting periods. Such estimates include but are not limited to the valuation of investments and financial instruments. Actual results could differ from those estimates and such differences could be material to the financial statements.

Consolidation

General

KKR consolidates (i) those entities in which it holds a majority voting interest or has majority ownership and control over significant operating, financial and investing decisions of the entity, including the KKR Funds in which KKR, as general partner, is presumed to have control, or (ii) entities determined to be variable interest entities (VIEs) for which KKR is considered the primary beneficiary.

With respect to the consolidated KKR Funds, KKR generally has operational discretion and control, and limited partners have no substantive rights to impact ongoing governance and operating activities of the fund. The KKR Funds are consolidated by KKR notwithstanding the fact that KKR has only a minority economic interest in those funds. KKR s financial statements reflect the assets, liabilities, fees, expenses, investment income (loss) and cash flows of the consolidated KKR Funds on a gross basis, and the majority of the economic interests in those funds, which are held by third party investors, are attributed to noncontrolling interests in the accompanying financial statements. All of the management fees and certain other amounts earned by KKR from those funds are eliminated in consolidation. However, because the eliminated amounts are earned from, and funded by, noncontrolling interests, KKR s attributable share of the net income (loss) from those funds is increased by the amounts eliminated. Accordingly, the elimination in consolidation of such amounts has no effect on net income (loss) attributable to KKR or KKR partners capital.

The KKR Funds are, for GAAP purposes, investment companies and therefore are not required to consolidate their investments, including majority-owned and controlled investments in portfolio companies (Portfolio Companies). Rather, KKR reflects their investments at fair value as described below.

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All intercompany transactions and balances have been eliminated.

Variable Interest Entities

KKR consolidates all VIEs in which it is considered the primary beneficiary. An enterprise is determined to be the primary beneficiary if it has a controlling financial interest under GAAP. A controlling financial interest is defined as (a) the power to direct the activities of a variable interest entity that most significantly impact the entity s business and (b) the obligation to absorb losses of the entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity. The consolidation rules which were revised effective January 1, 2010 require an analysis to (a) determine whether an entity in which KKR has a variable interest is a VIE and (b) whether KKR s involvement, through the holding of equity interests directly or indirectly in the entity or contractually through other variable interests unrelated to the holding of equity interests, would give it a controlling financial interest under GAAP. Performance of that analysis requires the exercise of judgment. Where KKR has an interest in an entity that has qualified for the deferral of the consolidation rules, the analysis is based on consolidation rules prior to January 1, 2010. These rules require an analysis to (a) determine whether an entity in which KKR has a variable interest is a VIE and (b) whether KKR s involvement, through the holding of equity interests directly or indirectly in the entity or contractually through other variable interests would be expected to absorb a majority of the variability of the entity. Under both guidelines, KKR determines whether it is the primary beneficiary of a VIE at the time it becomes involved with a VIE and reconsiders that conclusion at each reporting date. In evaluating whether KKR is the primary beneficiary, KKR evaluates its economic interests in the entity held either directly by KKR or indirectly through related parties. The consolidation analysis can generally be performed qualitatively; however, if it is not readily apparent that KKR is not the primary beneficiary, a quantitative analysis may also be performed. Investments and redemptions (either by KKR, affiliates of KKR or third parties) or amendments to the governing documents of the respective entities could affect an entity s status as a VIE or the determination of the primary beneficiary. At each reporting date, KKR assesses whether it is the primary beneficiary and will consolidate or deconsolidate accordingly. KKR s accounting conclusion under the existing consolidation rules determined that effective January 1, 2011, KKR became the primary beneficiary of certain entities and consolidated such entities that were unconsolidated prior to that date.

As of September 30, 2012 and December 31, 2011, the maximum exposure to loss for those VIEs in which KKR is determined not to be the primary beneficiary but in which it has a variable interest is as follows:

	September 30, 2012	December 31, 2011
Investments	$ 193,524	$ 61,053
Due from Affiliates, net	6,120	2,095
Maximum Exposure to Loss	$ 199,644	$ 63,148

For those unconsolidated VIEs in which KKR is the sponsor, KKR may have an obligation as general partner to provide commitments to such funds. For the three and nine months ended September 30, 2012 and 2011, KKR did not provide any support other than its obligated amount.

KKR s investment strategies differ by investment fund; however, the fundamental risks have similar characteristics, including loss of invested capital and loss of management fees and carried interests. Accordingly, disaggregation of KKR s involvement with VIEs would not provide more useful information.

Redeemable Noncontrolling Interests

Redeemable Noncontrolling Interests represent noncontrolling interests of certain investment vehicles and funds that are subject to periodic redemption by investors following the expiration of a specified period of time (typically between one and three years), or may be withdrawn subject to a redemption fee during the period when capital may not be otherwise withdrawn. Limited partner interests subject to redemption as described above are presented as Redeemable Noncontrolling Interests within the condensed consolidated statements of financial condition and presented as Net Income (Loss) attributable to Redeemable Noncontrolling Interests within the condensed consolidated statements of operations. When redeemable amounts become legally payable to investors, they are classified as a liability and included in Accounts Payable, Accrued Expenses and Other Liabilities in the condensed consolidated statements of financial condition. For all consolidated investment vehicles and funds in which redemption rights have not been granted, noncontrolling interests are presented within Partners Capital in the condensed consolidated statements of financial condition as Noncontrolling Interests.

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Noncontrolling Interests

Noncontrolling interests represent (i) noncontrolling interests in consolidated entities and (ii) noncontrolling interests held by KKR Holdings.

Noncontrolling Interests in Consolidated Entities

Noncontrolling interests in consolidated entities represent the non-redeemable ownership interests in KKR that are held primarily by:

(i) third party investors in the KKR Funds;

(ii) a former principal and such person s designees representing an aggregate of 1% of the carried interest received by the general partners of KKR s funds and 1% of KKR s other profits (losses) until a future date;

(iii) certain of KKR s former principals and their designees representing a portion of the carried interest received by the general partners of KKR s private equity funds that was allocated to them with respect to private equity investments made during such former principals previous tenure with KKR;

(iv) certain of KKR s current and former principals representing all of the capital invested by or on behalf of the general partners of KKR s private equity funds prior to October 1, 2009 and any returns thereon; and

(v) a third party in KKR s capital markets business (representing an aggregate of 2% of the equity in the capital markets business).

Noncontrolling Interests held by KKR Holdings

Noncontrolling interests held by KKR Holdings include economic interests held by KKR s principals in the KKR Group Partnerships. KKR s principals receive financial benefits from KKR s business in the form of distributions received from KKR Holdings and through their direct and indirect participation in the value of KKR Group Partnership Units held by KKR Holdings. These financial benefits are not paid by KKR and are borne by KKR Holdings.

The following table presents the calculation of Noncontrolling interests held by KKR Holdings:

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Balance at the beginning of the period	$ 4,795,697	$ 4,727,983	$ 4,342,157	$ 4,346,388
Net income (loss) attributable to noncontrolling interests held by KKR Holdings (a)	249,460	(484,879)	946,484	52,051
Other comprehensive income (loss) (b)	3,396	(4,238)	(797)	(3,165)
Impact of Exchange of KKR Holdings units to KKR & Co. L.P. units (c)	(31,203)	(4,071)	(138,119)	(103,780)
Equity Based Compensation	104,792	117,044	282,358	375,368
Capital contributions	437	692	1,658	4,698
Capital distributions	(78,106)	(63,606)	(389,268)	(382,635)
Balance at the end of the period	$ 5,044,473	$ 4,288,925	$ 5,044,473	$ 4,288,925

(a) Refer to the table below for calculation of Net income (loss) attributable to noncontrolling interests held by KKR Holdings.

(b) Calculated on a pro rata basis based on the weighted average KKR Group Partnership Units held by KKR Holdings during the reporting period.

(c) Calculated based on the proportion of KKR Holdings units exchanged for KKR & Co. L.P. common units pursuant to the exchange agreement during the reporting period. The exchange agreement provides for the exchange of KKR Group Partnership Units held by KKR Holdings for KKR & Co. L.P. common units.

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Income (loss) attributable to KKR after allocation to noncontrolling interests held by KKR Holdings, with the exception of certain tax assets and liabilities that are directly allocable to KKR Management Holdings Corp., is attributed based on the percentage of the weighted average KKR Group Partnership Units held by KKR and KKR Holdings, each of which hold equity of the KKR Group Partnerships. However, primarily because of the contribution of certain expenses borne entirely by KKR Holdings as well as the periodic exchange of KKR Holdings units for KKR & Co. L.P. common units pursuant to the exchange agreement, the equity allocations shown in the condensed consolidated statement of changes in equity differ from their respective pro-rata ownership interests in KKR s net assets.

The following table presents the calculation of Net income (loss) attributable to noncontrolling interests held by KKR Holdings:

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Net income (loss)	$ 2,102,786	$ (3,196,355)	$ 6,579,904	$ 303,489
Less: Net income (loss) attributable to Redeemable Noncontrolling Interests	9,994		18,551	
Less: Net income (loss) attributable to Noncontrolling Interests in consolidated entities	1,715,921	(2,468,074)	5,150,761	295,654
Plus: Income taxes attributable to KKR Management Holdings Corp.	7,070	8,770	28,187	56,000
Net income (loss) attributable to KKR & Co. L.P. and KKR Holdings	$ 383,941	$ (719,511)	$ 1,438,779	$ 63,835
Net income (loss) attributable to noncontrolling interests held by KKR Holdings	$ 249,460	$ (484,879)	$ 946,484	$ 52,051

Investments

Investments consist primarily of private equity, fixed income, and other investments. Investments are carried at their estimated fair values, with unrealized gains or losses resulting from changes in fair value reflected as a component of Net Gains (Losses) from Investment Activities in the condensed consolidated statements of operations. Investments denominated in currencies other than the U.S. dollar are valued based on the spot rate of the respective currency at the end of the reporting period with changes related to exchange rate movements reflected as a component of Net Gains (Losses) from Investment Activities in the accompanying condensed consolidated statements of operations. Security and loan transactions are recorded on a trade date basis. Further disclosure on investments is presented in Note 4, Investments.

Private Equity **-** Consists primarily of investments in Portfolio Companies of KKR Funds and investments in infrastructure, natural resources and real estate.

Fixed Income - Consists primarily of investments in below investment grade corporate debt securities (primarily high yield bonds and syndicated bank loans), distressed and opportunistic debt and interests in collateralized loan obligations.

Other Consists primarily of investments in common stock, preferred stock, warrants and options of companies that are not private equity or fixed income investments.

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Securities Sold Short

Whether part of a hedging transaction or a transaction in its own right, securities sold short, represent obligations of KKR to deliver the specified security at the contracted price at a future point in time, and thereby create a liability to repurchase the security in the market at the prevailing prices. The liability for such securities sold short is marked to market based on the current fair value of the underlying security at the reporting date with changes in fair value recorded as unrealized gains or losses in Net Gains (Losses) from Investment Activities in the accompanying condensed consolidated statements of operations. These transactions may involve market risk in excess of the amount currently reflected in the accompanying statements of financial condition.

Derivatives

Derivative contracts include forward, swap and option contracts related to foreign currencies and credit standing of reference entities to manage foreign exchange risk and credit risk arising from certain assets and liabilities. All derivatives are recognized as either Other Assets or Accounts Payable, Accrued Expenses and Other Liabilities in the condensed consolidated statements of financial condition and measured at fair value with changes in fair value recorded in Net Gains (Losses) from Investment Activities in the accompanying condensed consolidated statements of operations. KKR s derivate financial instruments contain credit risk to the extent that its counterparties may be unable to meet the terms of the agreements. KKR attempts to minimize this risk by limiting its counterparties to major financial institutions with strong credit ratings.

Fair Value Measurements

Investments and other financial instruments are measured and carried at fair value. The majority of investments and other financial instruments are held by the consolidated KKR Funds. The KKR Funds are, for GAAP purposes, investment companies and reflect their investments and other financial instruments at fair value. KKR has retained the specialized accounting for the consolidated KKR Funds in consolidation. Accordingly, the unrealized gains and losses resulting from changes in fair value of the investments held by the KKR Funds are reflected as a component of Net Gains (Losses) from Investment Activities in the condensed consolidated statements of operations.

For investments and certain other financial instruments that are not held in a consolidated KKR Fund, KKR has elected the fair value option since these investments and other financial instruments are similar to those in the consolidated KKR Funds. Such election is irrevocable and is applied on an investment by investment basis at initial recognition. Unrealized gains and losses resulting from changes in fair value are reflected as a component of Net Gains (Losses) from Investment Activities in the condensed consolidated statements of operations. The methodology for measuring the fair value of such investments and other financial instruments is consistent with the methodologies applied to investments and other financial instruments that are held in consolidated KKR Funds.

The carrying amount of cash and cash equivalents, cash and cash equivalents held at consolidated entities, restricted cash and cash equivalents, due from / to affiliates, other assets, accounts payable, accrued expenses and other liabilities approximate fair value due to their short-term maturities. KKR s debt obligations, except for KKR s Senior Notes, bear interest at floating rates and therefore fair value approximates carrying value. Further information on KKR s Senior Notes is presented in Note 8, Debt Obligations. The fair value for KKR s Senior Notes was derived using Level II inputs similar to those utilized in valuing fixed income investments.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Where available, fair value is based on observable market prices or parameters or derived from such prices or parameters. Where observable prices or inputs are not available, valuation techniques are applied. These valuation techniques involve varying levels of management estimation and judgment, the degree of which is dependent on a variety of factors. See Note 5, Fair Value Measurements for further information on KKR s valuation techniques that involve unobservable inputs. Assets and liabilities recorded at fair value in the statements of financial condition are categorized based upon the level of judgment associated with the inputs used to measure their value. Hierarchical levels, as defined under GAAP, are directly related to the amount of subjectivity associated with the inputs to the valuation of these assets and liabilities. The hierarchical levels defined under GAAP are as follows:

Level I

Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date. The type of investments and other financial instruments included in this category are publicly-listed equities and debt, and securities sold short.

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Level II

Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. Level II inputs include quoted prices for similar instruments in active markets, and inputs other than quoted prices that are observable for the asset or liability. The type of investments and other financial instruments included in this category are fixed income investments, convertible debt securities indexed to publicly-listed securities, and certain over-the-counter derivatives.

Level III

Inputs are unobservable for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability. The types of assets and liabilities generally included in this category are private Portfolio Companies and fixed income investments for which a sufficiently liquid trading market does not exist.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. KKR s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and consideration of factors specific to the asset.

A significant decrease in the volume and level of activity for the asset or liability is an indication that transactions or quoted prices may not be representative of fair value because in such market conditions there may be increased instances of transactions that are not orderly. In those circumstances, further analysis of transactions or quoted prices is needed, and a significant adjustment to the transactions or quoted prices may be necessary to estimate fair value.

The availability of observable inputs can vary depending on the financial asset or liability and is affected by a wide variety of factors, including, for example, the type of instrument, whether the instrument has recently been issued, whether the instrument is traded on an active exchange or in the secondary market, and current market conditions. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised by KKR in determining fair value is greatest for instruments categorized in Level III. The variability and availability of the observable inputs affected by the factors described above may cause transfers between Levels I, II, and III, which KKR recognizes at the beginning of the reporting period.

Investments and other financial instruments that have readily observable market prices (such as those traded on a securities exchange) are stated at the last quoted sales price as of the reporting date. KKR does not adjust the quoted price for these investments, even in situations where KKR holds a large position and a sale could reasonably affect the quoted price.

Level II Valuation Methodologies

Financial assets and liabilities categorized as Level II consist primarily of debt securities indexed to publicly-listed securities and fixed income and other investments. Fixed income investments generally have bid and ask prices that can be observed in the marketplace. Bid prices reflect the highest price that KKR and others are willing to pay for an asset. Ask prices represent the lowest price that KKR and others are willing to accept for an asset. For financial assets and liabilities whose inputs are based on bid-ask prices obtained from third party pricing services, fair value may not always be a predetermined point in the bid-ask range. KKR s policy is to allow for mid-market pricing and adjusting to the point within the bid-ask range that meets KKR s best estimate of fair value. For debt securities indexed to publicly listed securities, such as convertible debt, the securities are typically valued using standard convertible security pricing models. The key inputs into these models that require some amount of judgment are the credit spreads utilized and the volatility assumed. To the extent the company being valued has other outstanding debt securities that are publicly-traded, the implied credit spread on the company s other outstanding debt securities would be utilized in the valuation. To the extent the company being valued does not have other outstanding debt securities that are publicly-traded, the credit spread will be estimated based on the implied credit spreads observed in comparable publicly-traded debt securities. In certain cases, an additional spread will be added to reflect an illiquidity discount due to the fact that the security being valued is not publicly-traded. The volatility assumption is based upon the historically observed volatility of the underlying equity security into which the convertible debt security is convertible and/or the volatility implied by the prices of options on the underlying equity security.

Level III Valuation Methodologies

The valuation methodologies used for the assets that are valued using Level III of the fair value hierarchy are described below.

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Private Equity Investments: KKR generally employs two valuation methodologies when determining the fair value of a private equity investment. The first methodology is typically a market comparables analysis that considers key financial inputs and recent public and private transactions and other available measures. The second methodology utilized is typically a discounted cash flow analysis, which incorporates significant assumptions and judgments. Estimates of key inputs used in this methodology include the weighted average cost of capital for the investment and assumed inputs used to calculate terminal values, such as exit EBITDA multiples. Other inputs are also used. Upon completion of the valuations conducted using these methodologies, a weighting is ascribed to each method, and an illiquidity discount is typically applied where appropriate. The ultimate fair value recorded for a particular investment will generally be within a range suggested by the two methodologies.

Fixed Income Investments: Fixed income investments are valued using values obtained from dealers or market makers, and where these values are not available, fixed income investments are valued by KKR using internally developed valuation models. Valuation models are based on discounted cash flow analyses, for which the key inputs are determined based on market comparables, which incorporate similar instruments from similar issuers.

Other Investments: Other investments primarily represent privately-held equity and equity-like securities (e.g. warrants) in companies that are not private equity or fixed income investments. KKR generally employs the same valuation methodologies as described above for private equity investments when valuing these other investments.

Key unobservable inputs that have a significant impact on KKR s Level III investment valuations as described above are included in Note 5 Fair Value Measurements. KKR utilizes several unobservable pricing inputs and assumptions in determining the fair value of its Level III investments. These unobservable pricing inputs and assumptions may differ by investment and in the application of KKR s valuation methodologies. KKR s reported fair value estimates could vary materially if KKR had chosen to incorporate different unobservable pricing inputs and other assumptions or, for applicable investments, if KKR only used either the discounted cash flow methodology or the market comparables methodology instead of assigning a weighting to both methodologies.

Level III Valuation Process

The valuation process involved for Level III measurements for private equity, fixed income, and other investments is completed on a quarterly basis and is designed to subject the valuation of Level III investments to an appropriate level of consistency, oversight, and review. KKR has a valuation committee for private equity investments and a valuation committee for fixed income and other investments. The private equity valuation committee may be assisted by subcommittees for example in the valuation of real estate investments. Each of the private equity valuation committee and the fixed income valuation committee is assisted by a valuation team, which is comprised only of employees who are not investment professionals responsible for preparing preliminary valuations or for oversight of any of the investments being valued. However, the valuation teams for natural resources and real estate investments may contain investment professionals who participate in the preparation of preliminary valuations and oversight for those investments. The valuation committees and teams are responsible for coordinating and consistently implementing KKR s quarterly valuation policies, guidelines and processes. For investments classified as Level III, investment professionals prepare preliminary valuations based on their evaluation of financial and operating data, company specific developments, market valuations of comparable companies and other factors. These preliminary valuations are reviewed with the investment professionals by the applicable valuation team and are also reviewed by an independent valuation firm engaged by KKR to perform certain procedures in order to assess the reasonableness of KKR s valuations for all Level III investments, except for certain investments other than KKR private equity investments. All preliminary valuations are then reviewed by the applicable valuation committee, and after reflecting any input by their respective valuation committees, the preliminary valuations are presented to a single committee consisting of Senior Principals involved in various aspects of the KKR business. When these valuations are approved by this single committee after reflecting any input from it, the valuations of Level III investments, as well as the valuations of Level I and Level II investments, are presented to the audit committee of KKR s board of directors and are then reported on to the board of directors.

As of September 30, 2012, upon completion by the independent valuation firm of certain limited procedures requested to be performed by them, the independent valuation firm concluded that the fair values, as determined by KKR, of the investments reviewed by them were reasonable.

Fees

Fees consist primarily of (i) monitoring and consulting fees from providing advisory and other services, (ii) management and incentive fees from providing investment management services to unconsolidated funds, a specialty finance company, structured finance and other vehicles, and separately managed accounts, and (iii) transaction fees earned in connection with successful investment transactions and from capital markets activities. These fees are based on the contractual terms of the governing agreements and are recognized when earned, which coincides with the period during which the related services are performed.

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For the three and nine months ended September 30, 2012 and 2011, fees consisted of the following:

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Transaction Fees	$ 74,168	$ 96,624	$ 161,290	$ 217,451
Monitoring & Consulting Fees	49,148	47,926	136,195	210,156
Management Fees	21,070	20,258	61,841	58,497
Incentive Fees	17,768		31,495	28,159
Total Fee Income	$ 162,154	$ 164,808	$ 390,821	$ 514,263

Transaction Fees

Transaction fees are earned by KKR primarily in connection with successful investment transactions and capital markets activities. Transaction fees are recognized upon closing of the transaction. Fees are typically paid on or around the closing of a transaction.

In connection with pursuing successful Portfolio Company investments, KKR receives reimbursement for certain transaction-related expenses. Transaction-related expenses, which are reimbursed by third parties, are typically deferred until the transaction is consummated and are recorded in Other Assets on the condensed consolidated statements of financial condition on the date incurred. The costs of successfully completed transactions are borne by the KKR Funds and included as a component of the investment s cost basis. Subsequent to closing, investments are recorded at fair value each reporting period as described in the section above titled Investments . Upon reimbursement from a third party, the cash receipt is recorded and the deferred amounts are relieved. No fees or expenses are recorded for these reimbursements.

Monitoring and Consulting Fees

Monitoring fees are earned by KKR for services provided to Portfolio Companies and are recognized as services are rendered. These fees are generally paid based on a fixed periodic schedule by the Portfolio Companies either in advance or in arrears and are separately negotiated for each Portfolio Company.

In connection with the monitoring of Portfolio Companies and certain unconsolidated funds, KKR receives reimbursement for certain expenses incurred on behalf of these entities. Costs incurred in monitoring these entities are classified as general, administrative and other expenses and reimbursements of such costs are classified as monitoring fees. In addition, certain monitoring fee provisions may provide for a termination payment following an initial public offering or change of control. These termination payments are recognized in the period when the related transaction closes.

Consulting fees are earned by certain consolidated entities for consulting services provided to Portfolio Companies and other companies and are recognized as the services are rendered. These fees are separately negotiated with each company for which services are provided.

Management Fees

Management fees are earned by KKR for management services provided to private equity funds, other investment vehicles, structured finance vehicles, separately managed accounts and a specialty finance company which are recognized in the period during which the related services are performed in accordance with the contractual terms of the related agreement. Management fees earned from private equity funds and certain investment vehicles are based upon a percentage of capital committed during the investment period, and thereafter based on remaining invested capital. For certain other investment vehicles, structured finance vehicles, separately managed accounts and a specialty finance vehicle, management fees are recognized in the period during which the related services are performed and are based upon the net asset value, gross assets or as otherwise defined in the respective agreements.

Management fees received from consolidated KKR Funds are eliminated in consolidation. However, because these amounts are funded by, and earned from, noncontrolling interests, KKR s allocated share of the net income from consolidated KKR Funds is increased by the amount of fees that are eliminated. Accordingly, the elimination of these fees does not have an effect on the net income (loss) attributable to KKR or KKR partners capital.

Incentive Fees

KKR s management agreement with a specialty finance company entitles KKR to quarterly incentive fees. The incentive fees are calculated and paid quarterly in arrears and are not subject to any hurdle or clawback provisions. The management agreement with the specialty finance company was renewed on January 1, 2012 and will automatically be renewed for successive one-year terms following December 31, 2012 unless the agreement is terminated in accordance with its terms.

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Compensation and Benefits

Compensation and Benefits expense includes cash compensation consisting of salaries, bonuses, and benefits, as well as equity based compensation consisting of charges associated with the vesting of equity-based awards and carry pool allocations.

All KKR principals and other employees of certain consolidated entities receive a base salary that is paid by KKR or its consolidated entities, and is accounted for as Compensation and Benefits expense. These employees are also eligible to receive discretionary cash bonuses based on performance, overall profitability and other matters. While cash bonuses paid to most employees are funded by KKR and certain consolidated entities and result in customary Compensation and Benefits expense, cash bonuses that are paid to certain of KKR s most senior employees are funded by KKR Holdings with distributions that it receives on its KKR Group Partnership Units. To the extent that distributions received by these individuals exceed the amounts that they are otherwise entitled to through their vested units in KKR Holdings, this excess is funded by KKR Holdings and reflected in Compensation and Benefits in the condensed consolidated statements of operations.

Further disclosure regarding equity based compensation is presented in Note 10 Equity Based Compensation.

Carried Interest

Carried interest entitles the general partner of a fund to a greater allocable share of the fund s earnings from investments relative to the capital contributed by the general partner and correspondingly reduce noncontrolling interests attributable share of those earnings. Amounts earned pursuant to carried interest are included as investment income (loss) in Net Gains (Losses) from Investment Activities in the condensed consolidated statements of operations and are earned by the general partner of those funds to the extent that cumulative investment returns are positive and where applicable, preferred return thresholds have been met. If these investment returns decrease or turn negative in subsequent periods, recognized carried interest will be reversed and reflected as investment losses in Net Gains (Losses) from Investment Activities in the condensed consolidated statements of operations. Carried interest is recognized based on the contractual formula set forth in the agreements governing the fund as if the fund was terminated at the reporting date with the then estimated fair values of the investments realized. Due to the extended durations of KKR s private equity funds and other investment vehicles, KKR believes that this approach results in income recognition that best reflects the periodic performance of KKR in the management of those funds. See Note 12 Segment Reporting for the amount of carried interest income earned or reversed for the three and nine months ended September 30, 2012 and 2011.

The agreements governing KKR s private equity funds generally include a clawback or, in certain instances, a net loss sharing provision that, if triggered, may give rise to a contingent obligation that may require the general partner to return or contribute amounts to the fund for distribution to investors at the end of the life of the fund. See Note 13 Commitments and Contingencies .

Carry Pool Allocation

With respect to KKR s active and future funds and co-investment vehicles that provide for carried interest, KKR will allocate to its principals and other professionals a portion of the carried interest earned in relation to these funds as part of its carry pool. KKR currently allocates approximately 40% of the carry it earns from these funds and vehicles to its carry pool. These amounts are accounted for as compensatory profit-sharing arrangements in conjunction with the related carried interest income and recorded as compensation expense for KKR employees and general, administrative and other expense for certain non-employee consultants and service providers in the condensed consolidated statements of operations. See Note 12 Segment Reporting for the amount of carry pool allocation expense recognized or reversed for the three and nine months ended September 30, 2012 and 2011.

Tax Receivable Agreement

Certain exchanges of KKR Group Partnership Units from KKR Holdings or transferees of its KKR Group Partnership Units for KKR & Co. L.P. common units may occur pursuant to KKR s exchange agreement. These exchanges are expected to result in an increase in KKR Management Holdings Corp. s and its corporate subsidiary s share of the tax basis of the tangible and intangible assets of KKR Management Holdings, a portion of which is attributable to the goodwill inherent in our business, that would not otherwise have been available. This increase in tax basis may increase depreciation and amortization for U.S. federal income tax purposes and therefore reduce the amount of income tax that our intermediate holding companies would otherwise be required to pay in the future. KKR & Co. L.P. entered into a tax receivable agreement with KKR Holdings pursuant to which our intermediate holding companies will be required to pay to KKR Holdings or transferees of its KKR Group Partnership Units 85% of the amount of cash savings, if any, in U.S. federal, state and local income taxes that the intermediate holding companies actually realize as a result of this increase in tax basis, as well as 85% of the amount of any such savings the intermediate holding companies actually realize as a result

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of increases in tax basis that arise due to payments under the tax receivable agreement. Although KKR is not aware of any issue that would cause the IRS to challenge a tax basis increase, neither KKR Holdings nor its transferees will reimburse KKR for any payments previously made under the tax receivable agreement if such tax basis increase, or the benefits of such increases, were successfully challenged. Payments made under the tax receivable agreement are required to be made within 90 days of the filing of the tax return of KKR Management Holdings Corp. As of September 30, 2012, approximately $0.2 million of cumulative cash payments have been made under the tax receivable agreement. No amounts were paid for the three and nine months ended September 30, 2012.

KKR records any changes in basis as a deferred tax asset and the liability for any corresponding payments as amounts due to affiliates, with a corresponding net adjustment to equity at the time of exchange. KKR records any benefit of the reduced income tax the intermediate holding companies may recognize as such benefit is recognized.

Recently Adopted Accounting Pronouncements

On January 1, 2012, KKR adopted ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in GAAP and International Financial Reporting Standards. The ASU specifies that the concepts of highest and best use and valuation premise in a fair value measurement are relevant only when measuring the fair value of nonfinancial assets and are not relevant when measuring the fair value of financial assets or liabilities. The amendments include requirements specific to measuring the fair value of those instruments, such as equity interests used as consideration in a business combination. An entity should measure the fair value of its own equity instrument from the perspective of a market participant that holds the instrument as an asset. With respect to financial instruments that are managed as part of a portfolio, an exception to fair value requirements is provided. That exception permits a reporting entity to measure the fair value of such financial assets and financial liabilities at a price that would be received to sell a net asset position for a particular risk or to transfer a net liability position for a particular risk in an orderly transaction between market participants at the measurement date. The amendments also clarify that premiums and discounts should only be applied if market participants would do so when pricing the asset or liability. Premiums and discounts related to the size of an entity s holding (e.g., a blockage factor) rather than as a characteristic of the asset or liability (e.g., a control premium) is not permitted in a fair value measurement.

The guidance also requires enhanced disclosures about fair value measurements, including, among other things, (a) for fair value measurements categorized within Level III of the fair value hierarchy, (1) a quantitative disclosure of the unobservable inputs and assumptions used in the measurement, (2) the valuation process used by the reporting entity, and (3) a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs and the interrelationships between those unobservable inputs, if any, and (b) the categorization by level of the fair value hierarchy for items that are not measured at fair value in the statement of financial position but for which the fair value is required to be disclosed (for example, a financial instrument that is measured at amortized cost in the statement of financial position but for which fair value is disclosed). The guidance also amends disclosure requirements for significant transfers between Level I and Level II and requires disclosure of all transfers between Levels I and II in the fair value hierarchy. As a result of adopting ASU 2011-04, KKR expanded its fair value disclosures. See section Fair Value Measurements above and Note 5 Fair Value Measurements.

On January 1, 2012, KKR adopted ASU 2011-05, Comprehensive Income. The ASU provides an entity with an option to present the total of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The guidance is effective for fiscal years, and interim periods within those years beginning after December 15, 2011 and should be applied on a retrospective basis. KKR has adopted the presentation of total comprehensive income in two consecutive statements. See the condensed consolidated statements of operations and condensed consolidated statements of comprehensive income (loss).

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3. NET GAINS (LOSSES) FROM INVESTMENT ACTIVITIES

Net Gains (Losses) from Investment Activities in the condensed consolidated statements of operations consist primarily of the realized and unrealized gains and losses on investments (including foreign exchange gains and losses attributable to foreign denominated investments and related activities) and other financial instruments, including those for which the fair value option has been elected. Unrealized gains or losses result from changes in the fair value of these investments and other financial instruments during a period. Upon disposition of an investment or financial instrument, previously recognized unrealized gains or losses are reversed and an offsetting realized gain or loss is recognized in the current period.

The following table summarizes total Net Gains (Losses) from Investment Activities for the three and nine months ended September 30, 2012 and 2011, respectively.

	Three Months Ended September 30, 2012		Three Months Ended September 30, 2011		Nine Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
	Net Realized Gains (Losses)	**Net Unrealized Gains (Losses)**	**Net Realized Gains (Losses)**	**Net Unrealized Gains (Losses)**	**Net Realized Gains (Losses)**	**Net Unrealized Gains (Losses)**	**Net Realized Gains (Losses)**	**Net Unrealized Gains (Losses)**
Private Equity Investments (a)	$ 1,250,696	$ 1,109,999	$ 508,138	$ (3,888,713)	$ 3,200,945	$ 3,752,513	$ 2,839,163	$ (2,318,353)
Fixed Income and Other (a)	8,694	153,260	(30,445)	(190,040)	65,780	198,803	19,634	(165,854)
Foreign Exchange Forward Contracts (b)	5,736	(174,299)	9,445	176,053	21,891	(129,679)	17,332	27,220
Foreign Currency Options (b)		(2,597)		6,592	(10,740)	3,939		(6,400)
Securities Sold Short (b)	(21,083)	(3,226)	35,177	18,720	(26,527)	(6,836)	25,704	24,885
Other Derivative Liabilities	(11,577)	(2,756)	3,959	(413)	(10,538)	(4,972)	3,959	(413)
Contingent Carried Interest Repayment Guarantee (c)				13,885		(55,937)		
Foreign Exchange Gains (Losses) on Debt Obligations	307	(4,551)			540	(1,441)		
Foreign Exchange Gains (Losses) on Cash and Cash Equivalents held at Consolidated Entities	(59)	69	(1,378)		(477)	(98)	401	
Total Net Gains (Losses) from Investment Activities	**$ 1,232,714**	**$ 1,075,899**	**$ 524,896**	**$ (3,863,916)**	**$ 3,240,874**	**$ 3,756,292**	**$ 2,906,193**	**$ (2,438,915)**

(a) See Note 4 Investments.

(b) See Note 7 Other Assets and Accounts Payable, Accrued Expenses and Other Liabilities.

(c) See Note 13 Commitments and Contingencies.

4. INVESTMENTS

Investments consist of the following:

	Fair Value		Cost	
	September 30, 2012	December 31, 2011	September 30, 2012	December 31, 2011
Private Equity	$ 36,860,169	$ 34,637,901	$ 31,953,444	$ 33,545,298
Fixed Income	3,035,120	2,228,210	2,902,973	2,199,390
Other	1,045,579	629,249	981,042	650,802
	$ 40,940,868	$ 37,495,360	$ 35,837,459	$ 36,395,490

As of September 30, 2012 and December 31, 2011, Investments totaling $2.4 billion and $2.2 billion, respectively were pledged as direct collateral against various financing arrangements. See Note 8 Debt Obligations.

As of September 30, 2012 and December 31, 2011, private equity investments which represented greater than 5% of the total private equity investments included:

	Fair Value	
	September 30, 2012	December 31, 2011
Alliance Boots GmbH	$ 3,309,619	$ 2,459,263
HCA, Inc.	2,801,619	1,854,248
Dollar General Corporation	2,624,964	3,399,221
	$ 8,736,202	$ 7,712,732

The majority of the securities underlying private equity investments represent equity securities. As of September 30, 2012 and December 31, 2011, the fair value of investments that were other than equity securities amounted to $0.8 billion and $1.9 billion, respectively.

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5. FAIR VALUE MEASUREMENTS

The following tables summarize the valuation of KKR s investments and other financial instruments measured and reported at fair value by the fair value hierarchy levels described in Note 2 Summary of Significant Accounting Policies as of September 30, 2012 and December 31, 2011 including those investments and other financial instruments for which the fair value option has been elected.

Assets, at fair value:

	September 30, 2012			
	Quoted Prices in Active Markets for Identical Assets (Level I)	Significant Other Observable Inputs (Level II)	Significant Unobservable Inputs (Level III)	Total
Private Equity	$ 10,598,292	$ 795,012	$ 25,466,865	$ 36,860,169
Fixed Income		1,579,895	1,455,225	3,035,120
Other	654,682	204,553	186,344	1,045,579
Total Investments	11,252,974	2,579,460	27,108,434	40,940,868
Other Derivatives		3,147		3,147
Total Assets	$ 11,252,974	$ 2,582,607	$ 27,108,434	$ 40,944,015

	December 31, 2011			
	Quoted Prices in Active Markets for Identical Assets (Level I)	Significant Other Observable Inputs (Level II)	Significant Unobservable Inputs (Level III)	Total
Private Equity	$ 10,772,277	$ 1,897,363	$ 21,968,261	$ 34,637,901
Fixed Income	16,847	1,194,604	1,016,759	2,228,210
Other	284,997	248,073	96,179	629,249
Total Investments	11,074,121	3,340,040	23,081,199	37,495,360
Foreign Exchange Forward Contracts		114,224		114,224
Other Derivatives		490		490
Total Assets	$ 11,074,121	$ 3,454,754	$ 23,081,199	$ 37,610,074

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Liabilities, at fair value:

	September 30, 2012			
	Quoted Prices in Active Markets for Identical Assets (Level I)	Significant Other Observable Inputs (Level II)	Significant Unobservable Inputs (Level III)	Total
Securities Sold Short	$ 343,855	$ 36,841	$	$ 380,696
Foreign Currency Options		7,842		7,842
Foreign Exchange Forward Contracts		15,455		15,455
Unfunded Revolver Commitments		1,700		1,700
Total Liabilities	$ 343,855	$ 61,838	$	$ 405,693

	December 31, 2011			
	Quoted Prices in Active Markets for Identical Assets (Level I)	Significant Other Observable Inputs (Level II)	Significant Unobservable Inputs (Level III)	Total
Securities Sold Short	$ 202,908	$	$	$ 202,908
Foreign Currency Options		11,736		11,736
Total Liabilities	$ 202,908	$ 11,736	$	$ 214,644

The following tables summarize changes in private equity, fixed income, and other investments measured and reported at fair value for which Level III inputs have been used to determine fair value for the three and nine months ended September 30, 2012 and 2011, respectively.

	Three Months Ended September 30, 2012			
	Private Equity	Fixed Income	Other	Total Level III Investments
Balance, Beginning of Period	$ 25,378,631	$ 1,136,459	$ 140,019	$ 26,655,109
Transfers In (1)		32,076		32,076
Transfers Out (2)		(22,839)		(22,839)
Purchases	611,970	319,180	30,762	961,912
Sales	(2,429,813)	(63,797)	(191)	(2,493,801)
Settlements		12,031		12,031
Net Realized Gains (Losses)	1,250,696	2,075	(1,081)	1,251,690
Net Unrealized Gains (Losses)	655,381	40,040	16,835	712,256
Balance, End of Period	$ 25,466,865	$ 1,455,225	$ 186,344	$ 27,108,434
Changes in Net Unrealized Gains (Losses) Included in Net Gains (Losses) from Investment Activities (including foreign exchange gains and losses attributable to foreign-denominated investments) related to Investments still held at Reporting Date	$ 1,662,956	$ 42,141	$ 16,835	$ 1,721,932

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	Three Months Ended September 30, 2011			
	Private Equity	Fixed Income	Other	Total Level III Investments
Balance, Beginning of Period	$ 21,065,234	$ 938,944	$ 81,468	$ 22,085,646
Transfers In (1)		787		787
Transfers Out (2)		(35,630)	(19,230)	(54,860)
Purchases	1,511,546	50,531	8,589	1,570,666
Sales	(72,931)	(10,166)	(1,102)	(84,199)
Settlements		(218)		(218)
Net Realized Gains (Losses)	38,456	194		38,650
Net Unrealized Gains (Losses)	(920,061)	(31,783)	(5,063)	(956,907)
Balance, End of Period	$ 21,622,244	$ 912,659	$ 64,662	$ 22,599,565
Changes in Net Unrealized Gains (Losses) Included in Net Gains (Losses) from Investment Activities (including foreign exchange gains and losses attributable to foreign-denominated investments) related to Investments still held at Reporting Date	$ (893,749)	$ (26,917)	$ (3,244)	$ (923,910)

(1) The Transfers In noted in the tables above for fixed income investments are principally attributable to certain corporate credit investments that experienced an insignificant level of market activity during the period and thus were valued in the absence of observable inputs.

(2) The Transfers Out noted above for fixed income and other investments are principally attributable to certain investments that experienced a significant level of market activity during the period and thus were valued using observable inputs.

	Nine Months Ended September 30, 2012			
	Private Equity	Fixed Income	Other	Total Level III Investments
Balance, Beginning of Period	$ 21,968,261	$ 1,016,759	$ 96,179	$ 23,081,199
Transfers In (1)		32,387	1,061	33,448
Transfers Out (2)		(35,466)	(613)	(36,079)
Purchases	1,435,288	538,043	46,988	2,020,319
Sales	(2,757,806)	(146,288)	(2,852)	(2,906,946)
Settlements		13,439		13,439
Net Realized Gains (Losses)	1,419,440	10,326	98	1,429,864
Net Unrealized Gains (Losses)	3,401,682	26,025	45,483	3,473,190
Balance, End of Period	$ 25,466,865	$ 1,455,225	$ 186,344	$ 27,108,434
Changes in Net Unrealized Gains (Losses) Included in Net Gains (Losses) from Investment Activities (including foreign exchange gains and losses attributable to foreign-denominated investments) related to Investments still held at Reporting Date	$ 4,566,675	$ 32,058	$ 45,699	$ 4,644,432

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	Nine Months Ended September 30, 2011			
	Private Equity	Fixed Income	Other	Total Level III Investments
Balance, Beginning of Period	$ 23,172,797	$ 666,014	$ 45,188	$ 23,883,999
Transfers In (1)		129,428		129,428
Transfers Out (2)	(4,622,552)	(35,630)	(23,060)	(4,681,242)
Purchases	2,999,121	307,874	52,934	3,359,929
Sales	(1,791,690)	(72,279)	(5,969)	(1,869,938)
Settlements		(88,946)		(88,946)
Net Realized Gains (Losses)	1,025,699	465	210	1,026,374
Net Unrealized Gains (Losses)	838,869	5,733	(4,641)	839,961
Balance, End of Period	$ 21,622,244	$ 912,659	$ 64,662	$ 22,599,565
Changes in Net Unrealized Gains (Losses) Included in Net Gains (Losses) from Investment Activities (including foreign exchange gains and losses attributable to foreign-denominated investments) related to Investments still held at Reporting Date	$ 496,081	$ 13,984	$ 522	$ 510,587

(1) The Transfers In noted in the tables above for fixed income and other investments are principally attributable to certain corporate credit and other investments that experienced an insignificant level of market activity during the period and thus were valued in the absence of observable inputs.

(2) The Transfers Out noted in the tables above for private equity investments are attributable to certain Portfolio Companies that completed an initial public offering during the period. The Transfers Out noted above for fixed income and other investments are principally attributable to certain investments that experienced a significant level of market activity during the period and thus were valued using observable inputs.

Total realized and unrealized gains and losses recorded for Level III investments are reported in Net Gains (Losses) from Investment Activities in the accompanying condensed consolidated statements of operations. There were no transfers between Level I and Level II during the three and nine months ended September 30, 2012 and 2011, respectively.

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The following table presents additional information about valuation methodologies and inputs used for investments that are measured at fair value and categorized within Level III as of September 30, 2012:

	Fair Value September 30, 2012	Valuation Methodologies	Unobservable Input(s) (1)	Weighted Average (2)	Range	Impact to Valuation from an Increase in Input (3)
Private equity investments	**$ 25,466,865(9)**	Inputs to both market comparable and discounted cash flow	Illiquidity Discount	9%	0%-20% (6)	Decrease
			Weight Ascribed to Market Comparables	48%	0%-100%	(4)
			Weight Ascribed to Discounted Cash Flow	52%	0%-100%	(5)
		Market comparables	Enterprise Value/LTM EBITDA Multiple	9x	4x-19x (7)	Increase
			Enterprise Value/Forward EBITDA Multiple	9x	4x-15x (7)	Increase
			Control Premium	0%	0%-20% (8)	Increase
		Discounted cash flow	Weighted Average Cost of Capital	11%	6%-22%	Decrease
			Enterprise Value/LTM EBITDA Exit Multiple	9x	5x-13x	Increase
Fixed income investments	**$ 1,455,225(10)**	Yield Analysis	Discount Margin	1369 bps	426-6371 bps	Decrease
			Yield	14%	5%-65%	Decrease
			Net Leverage	5x	1x-10x	Decrease
			Illiquidity Discount	2%	0%-20%	Decrease

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(1) In determining certain of these inputs, management evaluates a variety of factors including economic conditions, industry and market developments, market valuations of comparable companies and company specific developments including exit strategies and realization opportunities. Management has determined that market participants would take these inputs into account when valuing the investments. LTM means Last Twelve Months and EBITDA means Earnings Before Interest Taxes Depreciation and Amortization.

(2) Inputs were weighted based on the fair value of the investments included in the range.

(3) Unless otherwise noted, this column represents the directional change in the fair value of the Level III investments that would result from an increase to the corresponding unobservable input. A decrease to the unobservable input would have the opposite effect. Significant increases and decreases in these inputs in isolation could result in significantly higher or lower fair value measurements.

(4) The directional change from an increase in the weight ascribed to the market comparables approach would increase the fair value of the Level III investments if the market comparables approach results in a higher valuation than the discounted cash flow approach. The opposite would be true if the market comparables approach results in a lower valuation than the discounted cash flow approach.

(5) The directional change from an increase in the weight ascribed to the discounted cash flow approach would increase the fair value of the Level III investments if the discounted cash flow approach results in a higher valuation than the market comparables approach. The opposite would be true if the discounted cash flow approach results in a lower valuation than the market comparables approach.

(6) All private equity investments are assigned a minimum 5% illiquidity discount, with the exception of investments in KKR s natural resources strategy.

(7) Ranges shown exclude inputs relating to a single portfolio company that was determined to lack comparability with other investments in KKR s private equity portfolio. This portfolio company had a fair value representing less than 0.5% of the total fair value of Private Equity Investments and had an Enterprise

Value/LTM EBITDA Multiple and Enterprise Value/Forward EBITDA Multiple of 27x and 18x, respectively. The exclusion of this investment does not impact the weighted average.

(8) Level III private equity investments whose valuations include a control premium represent less than 1% of total Level III private equity investments. The valuations for the remaining investments do not include a control premium.

(9) Amounts include $141.0 million of investments whose valuation inputs are not directly comparable to other private equity investments, and as such the inputs associated with these investments have been excluded from this table. These investments have a fair value representing less than 1% of the total fair value of private equity investments.

(10) Amounts include $177.0 million of investments that were valued using dealer quotes or third party valuation firms.

The table above excludes Other Investments in the amount of $186.3 million comprised primarily of privately-held equity and equity-like securities (e.g. warrants) in companies that are neither private equity nor fixed income investments. These investments were valued using Level III valuation methodologies that are generally the same as those shown for private equity investments.

The various unobservable inputs used to determine the Level III valuations may have similar or diverging impacts on valuation. Significant increases and decreases in these inputs in isolation and interrelationships between those inputs could result in significantly higher or lower fair value measurements as noted in the table above.

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6. EARNINGS PER COMMON UNIT

Basic earnings per common unit are calculated by dividing Net Income (Loss) Attributable to KKR & Co. L.P. by the total weighted average number of common units outstanding during the period.

Diluted earnings per common unit is calculated by dividing Net Income (Loss) Attributable to KKR & Co. L.P. by the weighted average number of common units outstanding during the period increased to include the weighted average number of additional common units that would have been outstanding if dilutive potential common units had been issued.

For the three and nine months ended September 30, 2012 and 2011, basic and diluted earnings per common unit were calculated as follows:

	Three Months Ended September 30, 2012		Three Months Ended September 30, 2011		Nine Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
	Basic	**Diluted**	**Basic**	**Diluted**	**Basic**	**Diluted**	**Basic**	**Diluted**
Net Income (Loss) Attributable to KKR & Co. L.P.	$ 127,411	$ 127,411	$ (243,402)	$ (243,402)	$ 464,108	$ 464,108	$ (44,216)	$ (44,216)
Net Income (Loss) Attributable to KKR & Co. L.P. Per Common Unit	$ 0.53	$ 0.49	$ (1.09)	$ (1.09)	$ 1.98	$ 1.86	$ (0.20)	$ (0.20)
Total Weighted-Average Common Units Outstanding	239,696,358	257,646,622	222,733,648	222,733,648	234,876,879	249,359,200	218,501,107	218,501,107

For the three and nine months ended September 30, 2012 and 2011, KKR Holdings units have been excluded from the calculation of diluted earnings per common unit given that the exchange of these units would proportionally increase KKR & Co. L.P. s interests in the KKR Group Partnerships and would have an anti-dilutive effect on earnings per common unit as a result of certain tax benefits KKR & Co. L.P. is assumed to receive upon the exchange.

For the three and nine months ended September 30, 2011, equity awards granted under the KKR & Co. L.P. 2010 Equity Incentive Plan (the Equity Incentive Plan) have been excluded from the calculation of diluted earnings per common unit given the equity awards would have an anti-dilutive effect on earnings per common unit as a result of the net loss incurred for the respective periods.

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7. OTHER ASSETS AND ACCOUNTS PAYABLE, ACCRUED EXPENSES AND OTHER LIABILITIES

Other assets consist of the following:

	September 30, 2012	December 31, 2011
Due from Broker (a)	$ 308,990	$
Interest and Note Receivable (b)	229,536	319,402
Unsettled Investment Sales (c)	93,326	230,970
Fixed Assets, net (d)	78,984	59,619
Deferred Tax Assets	57,788	34,125
Receivables	28,734	30,060
Deferred Financing Costs	22,479	17,691
Intangible Asset, net (e)	21,469	24,310
Deferred Transaction Costs	19,988	8,987
Prepaid Expenses	12,387	10,709
Refundable Security Deposits	7,717	8,242
Foreign Exchange Forward Contracts (f)		114,224
Other	28,402	10,366
	$ 909,800	$ 868,705

(a) Represents amounts held at clearing brokers resulting from securities transactions.

(b) Represents interest receivable and a promissory note received from a third party. The promissory note bears interest at a fixed rate of 3.0% per annum and matures on February 28, 2016.

(c) Represents amounts due from third parties for investments sold for which cash settlement has not occurred.

(d) Net of accumulated depreciation and amortization of $89,285 and $80,501 as of September 30, 2012 and December 31, 2011, respectively. Depreciation and amortization expense totaled $3,157 and $2,192 for the three months ended September 30, 2012 and 2011, respectively, and $8,987 and $7,501 for the nine months ended September 30, 2012 and 2011.

(e) Net of accumulated amortization of $16,417 and $13,576 as of September 30, 2012 and December 31, 2011, respectively. Amortization expense totaled $947 for the three months ended September 30, 2012 and 2011 and $2,841 for the nine months ended September 30, 2012 and 2011.

(f) Represents derivative financial instruments used to manage foreign exchange risk arising from certain foreign denominated investments. Such instruments are measured at fair value with changes in fair value recorded in Net Gains (Losses) from Investment Activities in the accompanying condensed consolidated statements of operations. The fair value of these instruments as of September 30, 2012 was an unrealized loss of $15,455. See Note 3 Net Gains (Losses) from Investment Activities for the net changes in fair value associated with these instruments.

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Accounts Payable, Accrued Expenses and Other Liabilities consist of the following:

	September 30, 2012	December 31, 2011
Amounts Payable to Carry Pool (a)	$ 765,318	$ 448,818
Securities Sold Short (b)	380,696	202,908
Unsettled Investment Purchases (c)	215,912	49,668
Accrued Compensation and Benefits	112,741	12,744
Accounts Payable and Accrued Expenses	75,444	105,453
Interest Payable	29,533	119,337
Deferred Rent and Income	18,894	6,141
Foreign Exchange Forward Contracts (d)	15,455	
Taxes Payable	11,242	27,259
Foreign Currency Options (e)	7,842	11,736
Due to Broker (f)		33,103
Fund Subscriptions Received in Advance		68,050
Other Liabilities	1,807	
	$ 1,634,884	$ 1,085,217

(a) Represents the amount of carried interest payable to KKR s principals, other professionals and other individuals with respect to KKR s active funds and co-investment vehicles that provide for carried interest. See Note 2 Summary of Significant Accounting Policies.

(b) Represents the obligations of KKR to deliver a specified security at a future point in time. Such securities are measured at fair value with changes in fair value recorded in Net Gains (Losses) from Investment Activities in the accompanying condensed consolidated statements of operations. See Note 3 Net Gains (Losses) from Investment Activities for the net changes in fair value associated with these instruments. The cost basis for these instruments at September 30, 2012 and December 31, 2011 were $371,925 and $200,973, respectively.

(c) Represents amounts owed to third parties for investment purchases for which cash settlement has not occurred.

(d) Represents derivative financial instruments used to manage foreign exchange risk arising from certain foreign denominated investments. Such instruments are measured at fair value with changes in fair value recorded in Net Gains (Losses) from Investment Activities in the accompanying condensed consolidated statements of operations. The fair value of these instruments as of December 31, 2011 was an unrealized gain of $114,224. See Note 3 Net Gains (Losses) from Investment Activities for the net changes in fair value associated with these instruments.

(e) Represents derivative financial instruments used to manage foreign exchange risk arising from certain foreign denominated investments. The instruments are measured at fair value with changes in fair value recorded in Net Gains (Losses) from Investment Activities in the accompanying condensed consolidated statements of operations. See Note 3 Net Gains (Losses) from Investment Activities for the net changes in fair value associated with these instruments. The cost basis for these instruments at September 30, 2012 and December 31, 2011 was $18,746 and $18,791, respectively.

(f) Represents amounts owed for securities transactions initiated at clearing brokers.

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8. DEBT OBLIGATIONS

Debt obligations consist of the following:

	September 30, 2012	December 31, 2011
Investment Financing Arrangements	$ 816,509	$ 1,066,536
Senior Notes	498,336	498,180
	$ 1,314,845	$ 1,564,716

Investment Financing Arrangements

Certain of KKR s investment vehicles have entered into financing arrangements with major financial institutions, generally in connection with specific investments with the objective of enhancing returns. These financing arrangements are generally not direct obligations of the general partners of KKR s investment vehicles or its management companies.

Approximately $796.4 million of financing was structured through the use of total return swaps which effectively convert third party capital contributions into borrowings of KKR. During May 2012, KKR entered into an agreement for an early redemption of one such financing arrangement. The terms of the agreement included a full repayment of the financing arrangement at par, which amounted to $625.0 million.

The remaining financing structured through the use of total return swaps of approximately $171.4 million had an expiration date in October 2012 in connection with the maturity of the underlying investment. As of September 30, 2012, the per annum rate of interest payable for the financing was 3.76%. During October 2012, KKR repaid the principal and accrued interest on the remaining outstanding financing in connection with the maturity of the underlying investment.

Approximately $182.2 million of financing was structured through the use of a syndicated term and a revolving credit facility (the Term Facility) that matures in August 2014. The per annum rate of interest for each borrowing under the Term Facility was equal to the Bloomberg United States Dollar Interest Rate Swap Ask Rate plus 1.75% at the time of each borrowing under the Term Facility through March 11, 2010. On March 11, 2010, the Term Facility was amended and the per annum rate of interest is the greater of the 5-Year interest rate swap rate plus 1.75% or 4.65% for periods from March 12, 2010 to June 7, 2012. For the period June 8, 2012 through maturity the interest rate is equal to one year LIBOR plus 1.75%. The per annum interest rate at September 30, 2012 on the borrowings outstanding was 2.82%. This financing arrangement is non-recourse to KKR beyond the specific assets pledged as collateral.

In April 2011, one of KKR s private equity investment vehicles entered into a revolving credit facility with a major financial institution (the Revolver Facility) with respect to a specific private equity investment. The Revolver Facility provides for up to $50.1 million of financing and matures on the first anniversary of the agreement. Upon the occurrence of certain events, including an event based on the value of the collateral and events of default, KKR may be required to provide additional collateral. KKR has the option to extend the agreement for an additional two years provided the value of the investment meets certain defined financial ratios. On April 5, 2012, an agreement was made to extend the maturity of the Revolver Facility to April 4, 2014. In addition, KKR may request to increase the commitment to the Revolver Facility up to

$75.1 million, subject to lender approval and provided the value of the investment meets certain defined financial ratios. The per annum rate of interest for each borrowing under the Revolver Facility is equal to the Hong Kong interbank market rate plus 3.75%. The interest rate at September 30, 2012 on the borrowings outstanding was 4.30%. As of September 30, 2012, $40.9 million of borrowings were outstanding under the Revolver Facility. This financing arrangement is non-recourse to KKR beyond the specific assets pledged as collateral.

During May 2011, a KKR investment vehicle entered into a $200.0 million non-recourse multi-currency three-year revolving credit agreement that bears interest at LIBOR plus 2.75% (the Mezzanine Investment Credit Agreement). The Mezzanine Investment Credit Agreement is expected to be used to manage timing differences between capital calls from limited partners in the investment vehicle and funding of investment opportunities and to borrow in foreign currencies for purposes of hedging the foreign currency risk of non-U.S. dollar investments. On June 18, 2012, an agreement was made to extend the maturity of the Mezzanine Investment Credit Agreement to May 15, 2015. During the nine months ended September 30, 2012, $173.1 million was drawn down and $99.2 million was repaid. As of September 30, 2012, $125.5 million of borrowings were outstanding under the Mezzanine Investment Credit Agreement. As of September 30, 2012, the interest rate on borrowings outstanding under the Mezzanine Investment Credit Agreement was 2.93%. This financing arrangement is non-recourse to KKR beyond the specific assets and capital commitments pledged as collateral.

In November 2011, a KKR investment vehicle entered into a $200.0 million five-year borrowing base revolving credit facility (the Lending Partners Credit Agreement). KKR has the option to extend the credit facility for up to two additional years. In

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addition, KKR may request to increase the commitment to the credit facility up to $400.0 million when the ratio of the loan commitments to committed equity capital is 1.50:1. On April 2, 2012, KKR increased the commitment to the credit facility to $400.0 million. The per annum rate of interest for each borrowing under the Lending Partners Credit Agreement ranges from LIBOR plus 1.75% for broadly syndicated loans and LIBOR plus 2.75% for all other loans until November 15, 2016 and thereafter, LIBOR plus 4.00% per annum for all loans. During the nine months ended September 30, 2012, $166.7 million was drawn down and $20.2 million was repaid. As of September 30, 2012, $146.5 million of borrowings were outstanding under the Lending Partners Credit Agreement. As of September 30, 2012, the interest rate on borrowings outstanding under the Lending Partners Credit Agreement was 2.97%. This financing arrangement is non-recourse to KKR beyond the specific assets pledged as collateral.

In December 2011, a KKR investment vehicle entered into a $66.5 million (50.0 million) one-year borrowing base revolving credit facility that bears interest at LIBOR plus 1.75% (the Investment Credit Agreement). The Investment Credit Agreement is expected to be used to manage timing differences between capital calls and the funding of investment opportunities. During the nine months ended September 30, 2012, $30.2 million was drawn down and $26.6 million was repaid. As of September 30, 2012, no borrowings were outstanding under the Investment Credit Agreement. This financing arrangement is non-recourse to KKR beyond the specific assets and capital commitments pledged as collateral.

In January 2012, a KKR investment vehicle entered into a $200.0 million three-year borrowing base revolving credit facility (the KKR Debt Investors II Investment Credit Agreement). As of September 30, 2012, $150.0 million of borrowings were outstanding under the KKR Debt Investors II Investment Credit Agreement. During the nine months ended September 30, 2012, $150.0 million was drawn down. As of September 30, 2012, the interest rate on borrowings outstanding under the KKR Debt Investors II Investment Credit Agreement was 3.5%. This financing arrangement is non-recourse to KKR beyond the specific assets pledged as collateral.

Senior Notes

On September 29, 2010, KKR Group Finance Co. LLC (the Issuer), a subsidiary of KKR Management Holdings Corp., issued $500 million aggregate principal amount of 6.375% Senior Notes (the Senior Notes), which were issued at a price of 99.584%. The Senior Notes are unsecured and unsubordinated obligations of the Issuer and will mature on September 29, 2020, unless earlier redeemed or repurchased. The Senior Notes are fully and unconditionally guaranteed, jointly and severally, by KKR & Co. L.P. and the KKR Group Partnerships. The guarantees are unsecured and unsubordinated obligations of the guarantors.

The Senior Notes bear interest at a rate of 6.375% per annum, accruing from September 29, 2010. Interest is payable semi-annually in arrears on March 29 and September 29 of each year, commencing on March 29, 2011. Interest expense on the Senior Notes totaled $8.0 million for the three months ended September 30, 2012 and 2011 and $24.0 million for the nine months ended September 30, 2012 and 2011. As of September 30, 2012, the fair value of the Senior Notes was $577.7 million.

The indenture, as supplemented by a first supplemental indenture, relating to the Senior Notes includes covenants, including limitations on the Issuer s and the guarantors ability to, subject to exceptions, incur indebtedness secured by liens on voting stock or profit participating equity interests of their subsidiaries or merge, consolidate or sell, transfer or lease assets. The indenture, as supplemented, also provides for events of default and further provides that the trustee or the holders of not less than 25% in aggregate principal amount of the outstanding Senior Notes may declare the Senior Notes immediately due and payable upon the occurrence and during the continuance of any event of default after expiration of any applicable grace period. In the case of specified events of bankruptcy, insolvency, receivership or reorganization, the principal amount of the Senior Notes and any accrued and unpaid interest on the Senior Notes automatically becomes due and payable. All or a portion of the Senior Notes may be redeemed at the Issuer s option in whole or in part, at any time, and from time to time, prior to their stated maturity, at the make-whole redemption price set forth in the Senior Notes. If a change of control repurchase event occurs, the Senior Notes are subject to repurchase by the Issuer at a repurchase price in cash equal to 101% of the aggregate principal amount of the Senior Notes repurchased plus any accrued and unpaid interest on the Senior Notes repurchased to, but not including, the date of repurchase.

KKR Revolving Credit Agreements

Corporate Credit Agreement

On February 26, 2008, Kohlberg Kravis Roberts & Co. L.P. entered into a credit agreement with a major financial institution (the Corporate Credit Agreement). The Corporate Credit Agreement originally provided for revolving borrowings of up to $1.0 billion, with a $50.0 million sublimit for swing-line notes and a $25.0 million sublimit for letters of credit.

On February 22, 2011, the parties amended the terms of the Corporate Credit Agreement such that effective March 1, 2011, availability for borrowings under the credit facility was reduced from $1.0 billion to $700.0 million and the maturity was extended to March 1, 2016. In addition, the KKR Group Partnerships became co-borrowers of the facility, and KKR & Co. L.P. and the Issuer of the Senior Notes became guarantors of the amended and restated Corporate Credit Agreement, together with certain general partners of our private equity funds.

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On June 3, 2011, the Corporate Credit Agreement was amended to admit a new lender, subject to the same terms and conditions, to provide a commitment of $50.0 million. This commitment has increased the availability for borrowings under the credit facility to $750.0 million. As of September 30, 2012, no borrowings were outstanding under the Corporate Credit Agreement. For the three and nine months ended September 30, 2012, no amounts were drawn under the credit facility.

On June 22, 2012, KKR requested the issuance of a letter of credit in the amount of $14.5 million under the Corporate Credit Agreement in connection with a fee-generating transaction. The beneficiary of this letter of credit is an unaffiliated third party. The letter of credit was issued on July 2, 2012 and expires on July 3, 2013. Subsequent to this letter of credit issuance, a $10.5 million sublimit for letters of credit remains available under the Corporate Credit Agreement.

KCM Credit Agreement

On February 27, 2008, KKR Capital Markets entered into a revolving credit agreement with a major financial institution (the KCM Credit Agreement) for use in KKR s capital markets business. The KCM Credit Agreement, as amended, provides for revolving borrowings of up to $500 million with a $500 million sublimit for letters of credit. On March 30, 2012, an agreement was made to extend the maturity of the KCM Credit Agreement from February 27, 2013 to March 30, 2017. In addition to extending the term, certain other terms of the KCM Credit Agreement were renegotiated including a reduction of the cost of funding on amounts drawn and a reduced commitment fee. Borrowings under this facility may only be used for our capital markets business. As of September 30, 2012, no borrowings were outstanding under the KCM Credit Agreement. For the three and nine months ended September 30, 2012, no amounts were drawn under the credit facility.

9. INCOME TAXES

The consolidated entities of KKR are generally treated as partnerships or disregarded entities for U.S. and non-U.S. tax purposes. However, certain consolidated subsidiaries are treated as corporations for U.S. and non-U.S tax purposes and are therefore subject to U.S. federal, state and/or local income taxes and/or non-U.S. taxes at the entity-level. In addition, certain consolidated entities which are treated as partnerships for U.S. tax purposes are subject to the New York City Unincorporated Business Tax or other local taxes. KKR s tax provision therefore reflects taxes from each of these sources and amounted to $9.6 million and $11.5 million for the three months ended September 30, 2012 and 2011, respectively and $37.8 million and $67.9 million for the nine months ended September 30, 2012 and 2011, respectively.

The effective tax rate was 0.46% and (0.36)% for the three months ended September 30, 2012 and 2011, respectively and 0.57% and 18.29% for the nine months ended September 30, 2012 and 2011, respectively. The negative effective tax rate for the three months ended September 30, 2011 was due to a net loss before taxes on a consolidated basis. The effective tax rate differs from the statutory rate for the three and nine months ended September 30, 2012 and 2011, respectively, primarily due to the following: (a) a substantial portion of the reported net income (loss) before taxes is attributable to noncontrolling interests held in consolidated entities or through KKR Holdings, (b) a significant portion of the amount of the reported net income (loss) before taxes attributable to KKR is from certain subsidiaries that are not subject to U.S. federal, state or local income taxes and/or non-U.S. taxes, and (c) certain compensation charges attributable to KKR are not deductible for tax purposes.

During the three and nine month period ending September 30, 2012, there were no material changes to KKR s uncertain tax positions. KKR believes that there will not be a significant increase or decrease to the uncertain tax positions within 12 months of the reporting date.

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10. EQUITY BASED COMPENSATION

The following table summarizes the expense associated with equity based compensation for the three and nine months ended September 30, 2012 and 2011, respectively.

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
KKR Holdings Principal Awards	$ 68,309	$ 91,647	$ 202,977	$ 269,530
KKR Holdings Restricted Equity Units	4,346	672	8,650	13,452
Equity Incentive Plan Units	17,366	6,813	47,678	11,164
Discretionary Compensation	32,136	24,726	70,732	92,387
Total	**$ 122,157**	**$ 123,858**	**$ 330,037**	**$ 386,533**

KKR Holdings Equity Awards Principal Awards

KKR principals and certain non-employee consultants and service providers received grants of KKR Holdings units which are exchangeable for KKR Group Partnership Units. These units are subject to minimum retained ownership requirements and in certain cases, transfer restrictions, and allow for their exchange into common units of KKR & Co. L.P. on a one-for-one basis. As of September 30, 2012, KKR Holdings owns approximately 64.7%, or 443,062,506 of the outstanding KKR Group Partnership Units.

Except for any units that vested on the date of grant, units are subject to service based vesting up to a five-year period from the date of grant. The transfer restriction period will generally last for a minimum of (i) one year with respect to one-half of the interests vesting on any vesting date and (ii) two years with respect to the other one-half of the interests vesting on such vesting date. While providing services to KKR, these individuals will also be subject to minimum retained ownership rules requiring them to continuously hold at least 25% of their vested interests. Upon separation from KKR, certain individuals will be subject to the terms of a non-compete agreement that may require the forfeiture of certain vested and unvested units should the terms of the non-compete agreement be violated. Holders of KKR Group Partnership Units held through KKR Holdings are not entitled to participate in distributions made on KKR Group Partnership Units until such units are vested.

Because KKR Holdings is a partnership, all of the 443,062,506 KKR Holdings units have been legally allocated, but the allocation of 26,576,878 of these units has not been communicated to each respective principal. The units that have not been communicated are subject to performance based vesting conditions, which include profitability and other similar criteria. These criteria are not sufficiently specific to constitute performance conditions for accounting purposes, and the achievement, or lack thereof, will be determined based upon the exercise of judgment by the general partner of KKR Holdings. Each principal will ultimately receive between zero and 100% of the units initially allocated. The allocation of these units has not yet been communicated to the award recipients as this was management s decision on how to best incentivize its principals. It is anticipated that additional service-based vesting conditions will be imposed at the time the allocation is initially communicated to the respective principals. KKR applied the guidance of Accounting Standards Code (ASC) 718 and concluded that these KKR Holdings units do not yet meet the criteria for recognition of compensation cost because neither the grant date nor the service inception date has occurred. In reaching a conclusion that the service inception date has not occurred, KKR considered (a) the fact that the vesting conditions are not sufficiently specific to constitute performance conditions for accounting purposes, (b) the significant judgment that can be exercised by the general partner of KKR Holdings in determining whether the vesting conditions are ultimately achieved, and (c) the absence of communication to the principals of any information related to the number of units they were initially allocated. The allocation of these units will be communicated to the award recipients when the performance-based vesting conditions have been met, and currently there is no plan as to when the communication will occur. The determination as to whether the award recipients have satisfied the performance-based vesting conditions is made by the general partner of KKR Holdings, and is based on multiple factors primarily related to the award recipients individual performance.

The fair value of KKR Holdings unit grants is based on the closing price of KKR & Co. L.P. common units on the date of grant. KKR determined this to be the best evidence of fair value as a KKR & Co. L.P. common unit is traded in an active market and has an observable market price. Additionally, a KKR Holdings unit is an instrument with terms and conditions similar to those of a KKR & Co. L.P. common unit. Specifically, units in both KKR Holdings and KKR & Co. L.P. represent ownership interests in KKR Group Partnership Units and, subject to any vesting, minimum retained ownership requirements and transfer restrictions referenced above, each KKR Holdings unit is exchangeable into a KKR Group Partnership Unit and then into a KKR & Co. L.P. common unit on a one-for-one basis.

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Units granted to principals give rise to equity-based payment charges in the condensed consolidated statements of operations based on the grant-date fair value of the award. For units vesting on the grant date, expense is recognized on the date of grant based on the fair value of a KKR & Co. L.P. common unit on the grant date multiplied by the number of vested units. Equity-based payment expense on unvested units is calculated based on the fair value of a KKR & Co. L.P. common unit at the time of grant, discounted for the lack of participation rights in the expected distributions on unvested units, which ranges from 7% to 52%, multiplied by the number of unvested units on the grant date.

Units granted to certain non-employee consultants and service providers give rise to general, administrative and other charges in the condensed consolidated statements of operations. For units vesting on the grant date, expense is recognized on the date of grant based on the fair value of a KKR & Co. L.P. common unit on the grant date multiplied by the number of vested units. General, administrative and other expense recognized on unvested units is calculated based on the fair value of a KKR & Co. L.P. common unit on each reporting date and subsequently adjusted for the actual fair value of the award at each vesting date. Accordingly, the measured value of these units will not be finalized until each vesting date.

The calculation of equity-based payment expense and general administrative and other expense on unvested units assumes a forfeiture rate of up to 10% annually based upon expected turnover by class of principal, consultant, or service provider.

As of September 30, 2012, there was approximately $179.5 million of estimated unrecognized equity-based payment and general administrative and other expense related to unvested awards. That cost is expected to be recognized over a weighted-average period of 0.9 years, using the graded attribution method, which treats each vesting portion as a separate award.

A summary of the status of KKR Holdings unvested equity based awards granted to KKR principals from January 1, 2012 through September 30, 2012 are presented below:

	Units	Weighted Average Grant Date Fair Value
Balance, January 1, 2012	91,741,793	$ 7.66
Granted	7,895,091	9.67
Vested	(2,058,907)	11.37
Forfeited	(559,167)	8.14
Balance, September 30, 2012	97,018,810	$ 7.74

The weighted average remaining vesting period over which unvested units are expected to vest is 1.1 years.

The following table summarizes the remaining vesting tranches for KKR principals:

Vesting Date	Units
October 1, 2012	30,077,698

April 1, 2013	1,326,446
October 1, 2013	29,966,330
April 1, 2014	1,291,702
October 1, 2014	29,966,373
April 1, 2015	1,291,757
October 1, 2015	1,818,961
April 1, 2016	30,000
October 1, 2016	1,234,543
April 1, 2017	15,000
	97,018,810

KKR Holdings Equity Awards Restricted Equity Units

Grants of restricted equity units based on KKR Group Partnership Units held by KKR Holdings were made to professionals, support staff, and other personnel. These grants will be funded by KKR Holdings and will not dilute KKR s interests in the KKR Group Partnerships. The vesting of these restricted equity units occur in installments up to five years from the date of grant. Units granted to professionals, support staff and other personnel are measured and recognized on a basis similar to KKR Holdings equity

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awards granted to principals and certain non-employee consultants and service providers except that the fair value of a KKR & Co. L.P. common unit at the time of grant is not discounted for the lack of participation rights in expected distributions since certain unvested units are entitled to distributions.

As of September 30, 2012, there was approximately $4.8 million of estimated unrecognized expense related to unvested awards. That cost is expected to be recognized over a weighted average period of 0.9 years, using the graded attribution method, which treats each vesting portion as a separate award.

A summary of the status of KKR Holdings unvested restricted equity units granted to KKR professionals, support staff, and other personnel from January 1, 2012 through September 30, 2012 is presented below:

	Units	Weighted Average Grant Date Fair Value
Balance, January 1, 2012	2,812,497	$ 10.90
Granted		
Vested	(228,412)	13.71
Forfeited	(90,779)	10.67
Balance, September 30, 2012	2,493,306	$ 10.65

The weighted average remaining vesting period over which unvested units are expected to vest is 0.6 years.

A summary of the remaining vesting tranches of KKR Holdings restricted equity awards granted to KKR professionals, support staff, and other personnel is presented below:

Vesting Date	Units
October 1, 2012	1,408,256
April 1, 2013	207,309
October 1, 2013	262,208
April 1, 2014	178,847
October 1, 2014	255,549
April 1, 2015	152,808
October 1, 2015	28,329
	2,493,306

KKR & Co. L.P. 2010 Equity Incentive Plan

Under the KKR & Co. L.P. 2010 Equity Incentive Plan, KKR is permitted to grant equity awards representing ownership interests in KKR & Co. L.P. common units. Vested awards under the Equity Incentive Plan dilute KKR & Co. L.P. common unit holders and KKR Holdings pro rata in accordance with their respective percentage interests in the KKR Group Partnerships.

The total number of common units that may be issued under the Equity Incentive Plan is equivalent to 15% of the number of fully diluted common units outstanding, subject to annual adjustment. As of September 30, 2012, equity awards relating to 19,072,189 KKR & Co. L.P. common units have been granted under the Equity Incentive Plan, which generally vest over a period of up to five years from the date of grant. In certain cases, these awards are subject to transfer restrictions and minimum retained ownership requirements. The transfer restriction period, if applicable, lasts for (i) one year with respect to one-half of the interests vesting on any vesting date and (ii) two years with respect to the other one-half of the interests vesting on such vesting date. While providing services to KKR, if applicable, certain of these individuals are also subject to minimum retained ownership rules requiring them to continuously hold common unit equivalents equal to at least 15% of their cumulatively vested interests.

Expense associated with the vesting of these awards is based on the closing price of the KKR & Co. L.P. common units on the date of grant, discounted for the lack of participation rights in the expected distributions on unvested units, which ranges from 7% to 52% multiplied by the number of unvested units on the grant date. Expense is recognized on a straight line basis over the life of the award and assumes a forfeiture rate of up to 10% annually based upon expected turnover by class of recipient.

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As of September 30, 2012, there was approximately $119.5 million of estimated unrecognized expense related to unvested awards. That cost is expected to be recognized over a weighted average period of 1.5 years, using the straight line method.

A summary of the status of awards granted under the Equity Incentive Plan from January 1, 2012 through September 30, 2012 is presented below:

	Units	Weighted Average Grant Date Fair Value
Balance, January 1, 2012	5,850,184	$ 9.69
Granted	12,998,587	9.56
Vested	(869,324)	12.52
Forfeited	(135,195)	12.02
Balance, September 30, 2012	17,844,252	$ 9.44

The weighted average remaining vesting period over which unvested awards are expected to vest is 1.7 years.

A summary of the remaining vesting tranches of awards granted under the Equity Incentive Plan is presented below:

Vesting Date	Units
October 1, 2012	2,246,762
April 1, 2013	2,796,931
October 1, 2013	2,156,522
April 1, 2014	2,727,656
October 1, 2014	2,062,622
April 1, 2015	2,653,258
October 1, 2015	1,541,034
April 1, 2016	513,208
October 1, 2016	1,108,727
April 1, 2017	37,532
	17,844,252

Discretionary Compensation

Certain KKR principals who hold KKR Group Partnership Units through KKR Holdings are expected to be allocated, on a discretionary basis, distributions on KKR Group Partnership Units received by KKR Holdings. These discretionary allocations allow the principal to receive amounts in excess of their vested equity interests. Because unvested units do not have distribution participation rights, any amounts allocated in excess of a principal s vested equity interests are reflected as employee compensation and benefits expense. These compensation charges have been recorded based on the unvested portion of quarterly earnings distributions received by KKR Holdings.

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11. RELATED PARTY TRANSACTIONS

Due from and to Affiliates consists of:

		September 30, 2012		December 31, 2011
Due from Principals (a)	$		$	55,937
Due from Related Entities		84,505		53,764
Due from Portfolio Companies		40,427		39,904
Due from Affiliates	$	124,932	$	149,605

		September 30, 2012		December 31, 2011
Due to KKR Holdings in Connection with the Tax Receivable Agreement (b)	$	55,721	$	40,320
Due to Related Entities		2,470		2,742
Due to Affiliates	$	58,191	$	43,062

(a) Represents an amount due from KKR principals for the amount of the clawback obligation that would be required to be funded by KKR principals who do not hold direct controlling and economic interests in the KKR Group Partnerships. See Note 13 Commitments and Contingencies .

(b) Represents amounts owed to KKR Holdings and/or its principals under the Tax Receivable Agreement. See Note 2, Summary of Significant Accounting Policies Tax Receivable Agreement.

KKR Financial Holdings LLC (KFN)

KFN is a publicly traded specialty finance company whose limited liability company interests are listed on the NYSE under the symbol KFN. KFN is managed by KKR but is not under the common control of the Senior Principals or otherwise consolidated by KKR as control is maintained by third-party investors. KFN was organized in August 2004 and completed its initial public offering on June 24, 2005. As of September 30, 2012 and December 31, 2011, KFN had consolidated assets of $8.3 billion and $8.6 billion, respectively, and shareholders equity of $1.8 billion and $1.7 billion as of September 30, 2012 and December 31, 2011, respectively. Shares of KFN held by KKR represented less than 1% of KFN s outstanding shares as of September 30, 2012. There were no outstanding shares of KFN held by KKR as of December 31, 2011. If KKR were to exercise all of its outstanding vested options, KKR s ownership interest in KFN would be less than 1% of KFN s outstanding shares as of September 30, 2012 and December 31, 2011.

Discretionary Investments

Certain of KKR s investment professionals, including its principals and other qualifying employees, are permitted to invest, and have invested, their own capital in side-by-side investments with its private equity funds and other investment vehicles. Side-by-side investments are made on the same terms and conditions as those acquired by the applicable fund or investment vehicle, except that the side-by-side investments are not subject to management fees or a carried interest. The cash invested by these individuals aggregated $16.5 million and $51.9 million for the three months ended September 30, 2012 and 2011, respectively and $71.1 million and $82.0 million for the nine months ended September 30, 2012 and 2011, respectively. These investments are not included in the accompanying financial statements.

Aircraft and Other Services

Certain of the Senior Principals own aircraft that KKR uses for business purposes in the ordinary course of its operations. These Senior Principals paid for the purchase of these aircraft with personal funds and bear all operating, personnel and maintenance costs associated with their operation. The hourly rates that KKR pays for the use of these aircraft are based on current market rates for chartering private aircraft of the same type. KKR incurred $0.7 million and $1.4 million for the use of these aircraft for the three months ended September 30, 2012 and 2011, respectively and $3.2 million and $3.8 million for the nine months ended September 30, 2012 and 2011, respectively.

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Facilities

Certain of the Senior Principals are partners in a real-estate based partnership that maintains an ownership interest in KKR s Menlo Park location. Payments made to this partnership were $1.7 million and $1.6 million for the three months ended September 30, 2012 and 2011, respectively and $5.1 million and $4.8 million for the nine months ended September 30, 2012 and 2011, respectively.

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12. SEGMENT REPORTING

KKR operates through three reportable business segments. These segments, which are differentiated primarily by their investment objectives and strategies, consist of the following:

Private Markets

Through the Private Markets segment, KKR manages and sponsors a group of private equity funds and co-investment vehicles that invest capital for long-term appreciation, either through controlling ownership of a company or strategic minority positions. KKR also manages and sources investments in infrastructure, natural resources and real estate. These investment funds, vehicles and accounts are managed by Kohlberg Kravis Roberts & Co. L.P., an SEC registered investment adviser.

Public Markets

Through the Public Markets segment, KKR manages KFN, a specialty finance company, as well as a number of investment funds, structured finance vehicles and separately managed accounts that invest capital in (i) leveraged credit strategies, such as leveraged loans and high yield bonds, (ii) liquid long/short equity strategies and (iii) alternative credit strategies such as mezzanine investments, special situations investments and direct senior lending. These funds, vehicles and accounts are managed by KKR Asset Management LLC, an SEC registered investment adviser.

Capital Markets and Principal Activities

KKR s Capital Markets and Principal Activities segment combines KKR s principal assets with its global capital markets business. KKR s capital markets business supports the firm, its portfolio companies and select third parties by providing tailored capital markets advice and by developing and implementing both traditional and non-traditional capital solutions for investments and companies seeking financing. KKR s capital markets services include arranging debt and equity financing for transactions, placing and underwriting securities offerings, structuring new investment products and providing capital markets services. KKR s principal asset base primarily includes investments in its private equity funds, co-investments in certain portfolio companies of such private equity funds, general partner interests in various KKR-sponsored investment funds, and other assets owned by the firm s balance sheet.

Key Performance Measures

Fee Related Earnings (FRE), Economic Net Income (Loss) (ENI) and Book Value are key performance measures used by management. These measures are used by management in making resource deployment and operating decisions as well as assessing the overall performance of each of KKR s business segments.

FRE

FRE is comprised of segment operating revenues less segment operating expenses and is used by management as an alternative measurement of the operating earnings of KKR and its business segments before investment income. The components of FRE on a segment basis differ from the equivalent GAAP amounts on a consolidated basis as a result of: (i) the inclusion of management fees earned from consolidated funds that were eliminated in consolidation; (ii) the exclusion of fees and expenses of certain consolidated entities; (iii) the exclusion of charges relating to the amortization of intangible assets; (iv) the exclusion of charges relating to carry pool allocations; (v) the exclusion of non-cash equity charges and other non-cash compensation charges borne by KKR Holdings or incurred under the Equity Incentive Plan; (vi) the exclusion of certain reimbursable expenses; and (vii) the exclusion of certain non-recurring items.

ENI

ENI is a measure of profitability for KKR s reportable segments and is used by management as an alternative measurement of the operating and investment earnings of KKR and its business segments. ENI is comprised of: (i) FRE; plus (ii) segment investment income (loss), which is reduced for carry pool allocations and management fee refunds; less (iii) certain economic interests in KKR s segments held by third parties. ENI differs from net income (loss) on a GAAP basis as a result of: (i) the exclusion of the items referred to in FRE above; (ii) the exclusion of investment income (loss) relating to noncontrolling interests; and (iii) the exclusion of income taxes.

Book Value

Book Value is a measure of the net assets of KKR s reportable segments and is used by management primarily in assessing the unrealized value of our investment portfolio, including carried interest, as well as KKR s overall liquidity position. Book value

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differs from the equivalent GAAP amounts on a consolidated basis primarily as a result of the exclusion of ownership interests attributable to KKR Holdings.

KKR s reportable segments are presented prior to giving effect to the allocation of income (loss) between KKR and KKR Holdings and as such represents KKR s business in total.

The following table presents the financial data for KKR s reportable segments as of and for the three months ended September 30, 2012:

	As of and for the Three Months Ended September 30, 2012			
	Private Markets	**Public Markets**	**Capital Markets and Principal Activities**	**Total Reportable Segments**
Fees				
Management and incentive fees:				
Management fees	$ 105,035	$ 21,448	$	$ 126,483
Incentive fees		17,768		17,768
Management and incentive fees	105,035	39,216		144,251
Monitoring and transaction fees:				
Monitoring fees	29,969			29,969
Transaction fees	32,788	8,780	33,696	75,264
Fee credits (1)	(26,293)	(5,414)		(31,707)
Net monitoring and transaction fees	36,464	3,366	33,696	73,526
Total fees	141,499	42,582	33,696	217,777
Expenses				
Compensation and benefits	48,905	13,997	8,438	71,340
Occupancy and related charges	12,049	1,343	213	13,605
Other operating expenses	35,885	3,897	2,346	42,128
Total expenses	96,839	19,237	10,997	127,073
Fee related earnings	44,660	23,345	22,699	90,704
Investment income (loss)				
Gross carried interest	391,168	19,568		410,736
Less: Allocation to KKR carry pool (2)	(161,805)	(7,828)		(169,633)
Less: Management fee refunds (3)	(61,499)			(61,499)
Net carried interest	167,864	11,740		179,604
Other investment income (loss)	1,779	25	239,072	240,876
Total investment income (loss)	169,643	11,765	239,072	420,480
Income (loss) before noncontrolling interests in income of consolidated entities	214,303			