AQUACELL TECHNOLOGIES INC
Form S-3
October 22, 2003

As filed with the Securities and Exchange Commission on October 22, 2003
Registration No. 333- ______________

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM S-3
REGISTRATION STATEMENT
Under
THE SECURITIES ACT OF 1933

AQUACELL TECHNOLOGIES, INC.
(Exact name of registrant as specified in charter)

Delaware	3590	33-0750453
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

10410 Trademark Street
Rancho Cucamonga, CA 91730
(909) 987-0456
(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

James C. Witham
Chief Executive Officer
10410 Trademark Street
Rancho Cucamonga, CA 91730
(909) 987-0456
(Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies to:

Harold W. Paul, Esq.
Harold W. Paul, LLC
1465 Post Road East
Westport, CT 06880
(203) 256-8005

Approximate date of commencement of proposed sale to public: As soon as practicable after this Registration Statement becomes effective and from time to time thereafter as determined by market conditions.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. [X]

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ]

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ]

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ]

If delivery of the prospectus is expected to be made pursuant to Rule 434 under the Securities Act, please check the following box. [ ]

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to Be Registered	Amount to Be Registered	Proposed Maximum Offering Price Per Share(2)	Proposed Maximum Aggregate Offering Price(2)	Amount of Registration Fee
Common Stock, par value $.001 per share (1)....	8,867,006 shares	$8.25	$22,634,040	$1,831.09

(1) Includes 5,833,638 shares of common stock issuable upon exercise of warrants and 1,185,000 shares of common stock issuable upon conversion of Series A preferred stock.

(2) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(c) under the Securities Act and based upon the average of the high and low trading price for the common stock on American Stock Exchange on October 15, 2003 with respect to common stock and pursuant to Rule 457(i) with respect to common stock underlying warrants.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to such Section 8(a), may determine.

PROSPECTUS

Subject to Completion
Preliminary Prospectus dated October ___, 2003.

8,837,006 Shares

[AquaCell Technologies, Inc.]
[Company Logo]

Common Stock

The selling stockholders identified in this prospectus may offer from time to time an aggregate of up to 8,867,006 shares of AquaCell Technologies, Inc.'s common stock, including 5,833,638 shares underlying common stock purchase warrants. We will not receive any of the proceeds from the sale of shares. We may receive funds of up to $14,898,952 upon the exercise of up to 5,833,638 common stock purchase warrants exercisable at various prices.

The selling stockholders may offer their shares through public or private transactions, on or off the American Stock Exchange, at prevailing market prices or at privately negotiated prices.

Our common stock trades on the American Stock Exchange under the symbol "AQA". On October 15, 2003, the last reported sale price of our common stock on the American Stock Exchange was $2.55 per share.

Investing in our common stock involves risks which are described in the "Risk Factors" section beginning on page 6 of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is _________ ___, 2003.

The information in this prospectus is not complete and may be changed. We have filed a registration statement relating to these shares with the Securities and Exchange Commission. We cannot sell these shares until the registration statement becomes effective. This prospectus is not an offer to sell these receipts and we are not soliciting offers to buy these shares in any state where such offer or sale is not permitted.

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"Purific" and "Never Change Another Bottle" are our trademarks. All other trademarks or service marks appearing in this prospectus are trademarks and service marks of the respective companies that use them.

You should rely only on the information contained or incorporated by reference in this prospectus. We have not, and the selling stockholders have not, authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the selling stockholders are not, making an offer to sell our common stock in any jurisdiction except where the offer or sale is permitted. You should not assume that the information contained or incorporated by reference in this prospectus is accurate as of any date other than the date on the front cover of this prospectus or the date of such other documents.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

When used in this prospectus and in future filings by the Company with the Commission, statements identified by the words "believe", "positioned", "estimate", "project", "target", "continue", "will", "intend", "expect", "future", "anticipates", and similar expressions express management's present belief, expectations or intentions regarding the Company's future performance within the meaning of the Private Securities Litigation Reform Act of 1995. Readers are cautioned not to place undue reliance on any such forward-looking statements, each of which speaks only as of the date made. Such statements are subject to certain risks and uncertainties that could cause actual results to differ materially from historical earnings and those presently anticipated or projected. The Company has no obligations to publicly release the result of any revisions which may be made to any forward-looking statements to reflect anticipated or unanticipated events or circumstances occurring after the date of such statements.

WHERE YOU CAN FIND MORE INFORMATION

We are a public company and file annual, quarterly and special reports, proxy statements and other information with the Securities and Exchange Commission. You may read and copy any document we file at the SEC's public reference room at 450 Fifth Street, N.W., Washington, D.C. 20549. You can request copies of these documents by writing to the SEC and paying a fee for the copying cost. Please call the SEC at 1-800-SEC-0330 for more information about the operation of the public reference room. Our SEC filings are also available to the public at the SEC's web site at http://www.sec.gov. In addition, you can read and copy our SEC filings at the office of the National Association of Securities Dealers, Inc. at 1735 K Street, Washington, D.C. 20006.

We have filed a registration statement on Form S-3 with the SEC covering the common stock offered by this prospectus. We refer you to this registration statement and its exhibits for additional information about us and our common stock. Copies of the registration statement may be obtained at the above referenced SEC offices or on the SEC's web site at www.sec.gov. Our internet address is www.aquacell.com.

INCORPORATION OF INFORMATION WE FILE WITH THE SEC

The SEC allows us to incorporate by reference the information we file with them, which means:

- Incorporated documents are considered part of the prospectus,
- We can disclose important information to you by referring you to those documents, and
- Information that we file with the SEC will automatically update and supersede this prospectus.

We incorporate by reference the documents listed below which were filed with the SEC under the Securities Exchange Act of 1934 (the "Exchange Act"):

- Annual Report on Form 10-KSB for the fiscal year ended June 30, 2003.

We also incorporate by reference each of the following documents that we will file with the SEC after the date of this prospectus but before all the common stock offered by this prospectus has been sold:

- Reports filed under Sections 13(a) and (c) of the Exchange Act,
- Definitive proxy or information statements filed under Section 14 of the Exchange Act in connection with any subsequent stockholders' meeting, and
- Any reports filed under the Section 15(d) of the Exchange Act.

You may request a copy of any filings referred to above (excluding exhibits), at no cost, by contacting us at the following address:

AquaCell Technologies, Inc.
Attention: Karen B. Laustsen
10410 Trademark Street
Rancho Cucamonga, CA 91730
(909) 987-0456

THE COMPANY

AquaCell Technologies, Inc. (the "Company") is engaged in the manufacture and sale of products for water filtration and purification through our operating subsidiaries, Global Water-Aquacell, Inc. and Water Science Technologies, Inc. (WST). Our products address various water treatment applications for industrial, commercial, institutional and residential purposes. These applications range from providing purified drinking water- through our point-of-use patented self-filling Purific(R) Water Cooler and production of water bottling plant equipment- to equipment for processing water for ultra-pure purposes, such as micro-chip and pharmaceutical manufacturing. The Company was incorporated in Delaware on March 19, 1997.

Our flagship product is our patented five-gallon self-refilling bottle Purific water cooler, manufactured by our Global Water-Aquacell subsidiary. We manufacture five different models of Purific water coolers with varying complexity of filtration systems, designed to meet the needs of the customers to which they are sold. The various filtration systems available on our cooler contain different combinations of systems, which utilize sediment filters, reverse osmosis, carbon block, multi-media filters and ultra-violet light. We replace traditional five-gallon bottle water coolers with a permanently installed convenient alternative where the bottle never needs changing and water bottles no longer need to be delivered, stored or replaced. In addition, we replace water fountains where users tend to have greater concerns as to sanitation and water quality.

We recently announced a successful product test that was funded by a Fortune 100 company on our Purific water cooler. The results of this test confirmed the competitive advantages of the Purific system, particularly for the residential market, the fastest growing segment of the bottled water industry.

We sell our Purific coolers directly to corporations with an emphasis on Fortune 500 headquarter locations and to the US Government under a General Services Administration contract, and indirectly through marketing partners. Additionally, we have an arrangement with Roto-Rooter Plumbers for the installation and sales of our Purific coolers. We intend to maintain a small in-house sales force and rely on our marketing partners for most of our sales.

Corporate Information

Our principal executive offices are located at 10410 Trademark Street, Rancho Cucamonga, CA 91730 and our telephone number is (909) 987-0456. Our website can be accessed at www.aquacell.com. The reference to our website address does not constitute incorporation by reference of the information contained at the website.

RISK FACTORS

Before you invest in our common stock, you should be aware that there are risks, including those described below which may affect our business, financial condition or results of operations. You should consider carefully these risk factors together with all of the other information included in this memorandum before you decide to purchase shares of our common stock.

Risks Relating to Our Business

We have incurred substantial operating losses and an accumulated deficit. We expect to continue to have operating losses and a growing accumulated deficit in the future.

Our business operations have generated operating losses since inception of the business in 1997. For the year ended June 30, 2003, our business operations generated operating losses of $3,434,000. We had an accumulated deficit of $12,909,000 at June 30, 2003. We expect to continue to generate net operating losses while we continue to expand our marketing efforts. We can give no assurance that we will obtain a customer base sufficient to support the costs of our operations.

We cannot assure you that we will become profitable or that our cash flow will become positive at any time in the foreseeable future, or at all, or that we will generate sufficient cash flow from product sales to liquidate liabilities as they become due. In the event that we are unable to liquidate our liabilities, we may delay or eliminate some expenditures and we may scale back our planned operations. Accordingly, we expect to need additional funds to meet our planned obligations, and we will seek to raise such amounts through a variety of options, including future cash from operations, borrowings and proceeds from equity financings. Additional funding may not be available when needed or on terms acceptable to us, which could have a material adverse effect on our business, financial condition and results of operations. In addition, if we raise additional funds through the issuance of equity, equity-linked or debt securities, those securities may have rights, preferences or privileges senior to those of the rights of our common stock and our stockholders may experience additional dilution.

Our Purific Water Cooler is new and may not be accepted by our target market.

Our primary product is based upon a permanently attached plastic bottle with a filtration system. Municipal water passes through the filter to keep the bottle filled. This is a different approach from the conventional replaceable five gallon bottle. Our target customers may not be willing to use our approach which would significantly hinder our growth potential and would negatively affect our business.

We are dependent on our marketing partners to distribute our products.

We maintain a small in-house sales force and rely primarily on our marketing partners to distribute our products, none of whom are required to meet specific performance goals or commit specific resources to the marketing of our products. The failure of these marketing partners to act effectively on our behalf will have a material adverse effect on the future performance of our business.

The market for bottled water is highly competitive and we compete with large, well established companies. If we are unable to compete effectively, the demand for, or prices of, our products may be reduced.

The bottled water market is intensely competitive. We may not be able to compete successfully against current or potential competitors and our failure to do so could seriously harm our business, operating results and financial condition.

We compete directly with large, well-established companies such as Nestle (Perrier), Danone (Evian) and Culligan. These and many of our current and potential competitors have significantly greater financial, selling and marketing, technical, manufacturing and other resources than we have. As a result, these competitors may be able to

devote greater resources toward the development, promotion, sale and support of their products than we can. These companies may introduce additional products that compete with ours or enter into strategic relationships to offer complete solutions which we do not currently offer.

In addition, we recently introduced our Purific Water Cooler to the market and we have not had enough experience selling the product to fully assess its competitiveness. If we find that our new products are not competitive, our business could be materially harmed.

We depend on key personnel and could be materially adversely affected if we do not retain those personnel.

Our operations will depend on the efforts of our executive officers, in particular James C. Witham, our Chairman and Chief Executive Officer, and Karen B. Laustsen, our President, Chief Operating Officer and Secretary. Should we be unable to retain any of our executive officers, our business and prospects could be materially adversely affected. We have entered into five year employment agreements with Mr. Witham and Ms. Laustsen that expire in February, 2006. Our business or prospects could be materially adversely affected if any of these senior management personnel do not continue in their management roles and if we are unable to attract and retain qualified replacements and additional members of management. We have secured a $1,000,000 key man life insurance policy on Mr. Witham that expires in February, 2004.

We could be adversely affected if we do not effectively manage growth.

If we successfully implement our business strategy, the resulting growth will place significant demands on our management and internal controls. There can be no assurance that management will effectively be able to direct us through a period of significant growth. In particular, the pursuit of our business strategy will place a significant strain on our managerial, operational and financial resources. We will need to improve our financial and management controls, reporting systems and procedures. We will also need to expand, train and manage our work force and manage multiple relationships with various suppliers, strategic partners and other third parties. We will need to continually expand and upgrade our systems and ensure continued high levels of service, speedy operation and reliability. If we do not effectively manage such growth, our business, results of operations and financial condition will be materially adversely affected.

Our quarterly results may fluctuate and could fall below the expectations of securities analysts and investors.

We may experience quarterly fluctuations in operating results. Accordingly, results for any one quarter will not necessarily be indicative of the results to be expected for any other quarter or for any year, and comparable sales for any particular future period may decrease. In the future, results of operations may fall below the expectations of public market analysts and investors. In that event, the price of our common stock would likely decrease. Quarterly sales and operating results will depend in part on the volume and timing of orders received and performed within the quarter, which are difficult to forecast. Any significant delay or cancellation of an order could have a material adverse effect on our operations in any particular period. As a result, our operating results could prove to be volatile and this could have a material adverse effect on our business, financial condition and results of operations.

Risks Relating to the Offering

Exercise of our outstanding warrants and options and the conversion of our preferred shares may affect the price of our common stock.

As of October 9, 2003, there were outstanding options to purchase 481,000 shares of common stock, outstanding warrants to purchase 5,833,638 shares of common stock and 1,185,000 outstanding convertible preferred shares. The exercise of the outstanding stock options and warrants and the conversion of preferred shares will dilute the percentage ownership of our stockholders. Any sales in the public

market of shares of our common stock underlying the stock options, warrants and preferred shares may adversely affect prevailing market prices for our common stock.

We do not intend to pay cash dividends on our common stock in the future.

We have never paid cash dividends on our common stock and do not anticipate that any cash dividends will be declared or paid on our common stock in the foreseeable future. We presently intend to retain future earnings, if any, to finance the expansion and growth of our business. Payment of future dividends on our common stock, if any, will be at the discretion of our board of directors after taking into account various factors, including our financial condition, operating results, current and anticipated cash needs and plans for expansion.

We may issue additional shares of stock without your approval, including shares of other series of preferred stock with superior liquidation and other rights that may adversely affect your rights.

Our certificate of incorporation authorizes our board of directors, without any action by our stockholders, to issue up to 10,000,000 shares of "blank check" preferred stock in one or more series on terms that our board of directors may determine at the time of issuance including 1,870,000 Series "A" preferred shares already designated. In certain instances, a series of preferred stock could include voting rights, preferences as to dividends and liquidation, conversion and redemption rights senior to the Series A preferred stock, and in all instances, senior to our common stock. The future issuance of preferred stock could effectively diminish or supersede the dividends and liquidation preferences of the Series A preferred stock and adversely affect our common stock.

We may not satisfy the Amex listing standard and if we fai l to do so, our common stock is subject to delisting.

The Company may not satisfy the Amex' maintenance requirements in the future and as a result may have its common stock de-listed from the Amex. If the Company fails to maintain its Amex listing, the ability of stockholders to trade their stock in an efficient market would be decreased.

USE OF PROCEEDS

All of the net proceeds from the sale of the common stock of

AquaCell covered by this prospectus will go to the stockholders who offer and sell their shares. Accordingly, we will not receive any of the proceeds from the sales of the common stock. AquaCell receives funds only upon sales from warrant conversions and not from the sale of the shares offered by the selling stockholders. The warrants held by the selling stockholders are exercisable at various prices. If all warrants are exercised, AquaCell will receive proceeds of $14,898,952 (including underwriters warrants issued by the Company in February, 2001) which would be used for general corporate purposes.

DIVIDEND POLICY

We have never declared or paid any cash dividends on our common stock and we currently expect to retain future earnings, if any, to support operations and to finance the growth and development of our business. Consequently, we do not anticipate paying cash dividends on our common stock in the foreseeable future. Payment of future dividends, if any, will be at the discretion of our board of directors after taking into account various factors, including our financial condition, operating results, current and anticipated cash needs and plans for expansion.

The outstanding Series A preferred stock pays an 8% annual dividend, payable in cash in quarterly installments until such time as the preferred shares are converted into common shares.

SELLING STOCKHOLDERS

Pursuant to subscription agreements in a series of private placements completed on or about and between April and September, 2003, we agreed to register the shares issuable upon conversion of series "A" preferred shares and upon exercise of warrants held by these stockholders. Additionally, we have agreed to register shares underlying other warrants issued from time to time by the Company and certain common shares issued in March, 2002 to creditors of our acquired subsidiary. We have agreed to keep the registration statement effective for two years, or until all of the registered shares are sold, whichever comes first. Our registration of the common stock held by the selling stockholders and the shares issuable upon exercise of warrants held by the selling stockholders does not necessarily mean that the selling stockholders will sell all or any of their shares.

The prospectus covers the offer and sale by each selling stockholder of common stock owned by the selling stockholder. Set forth below are (i) the names of each selling stockholder, (ii) the nature of any position, office or other material relationship that the selling stockholder has had within the past three years with us, (iii) the number of shares of common stock and (if one percent or more) the percentage of common stock beneficially owned as of October 9, 2003 by each selling stockholder to the Company's best knowledge, (iv) the number of shares that may be offered and sold by or on behalf of each selling stockholder hereunder, and (v) the amount and (if one percent or more) the percentage of common stock to be owned by each selling stockholder upon the completion of the offering if all shares offered by such selling stockholder are sold. Any or all of the shares listed below under the heading "Shares to be Sold" may be offered for sale by or on behalf of the selling stockholder.

Selling Stockholders	Shares Beneficially Owned Prior to the Offering		Shares Which May be Offered	Shares Beneficially Owned After the Offering	
	Number	Percent		Number	Percent
Albert Auer	5,000	*	5,000	5,000	*
BD Advisor Corp. (7)	400,000	2.3%	400,000	400,000	2.3%
Brighton Capital, Ltd	340,607	1.9%	340,607	340,607	1.9%
Corbett Water Technologies	389,557	2.2%	100,000	389,557	2.2%
Excelsior Group I (7)	400,000	2.3%	400,000	400,000	2.3%
Leonard Florence	300,000	1.7%	200,000	300,000	1.7%
Douglas Gass	10,000	*	10,000	10,000	*
Glenn Michael Financial	75,000	*	75,000	75,000	*
Anthony J. Kirincic	54,000	*	54,000	54,000	*
Kirlin Holding Corp.	72,000	*	72,000	72,000	*
Kirlin Securities	14,355	*	14,355	14,355	*
Donald Lefari	10,000	*	10,000	10,000	*
Limestone Capital Corp. (7)	200,000	1.1%	200,000	200,000	1.1%
David Lindner	54,000	*	54,000	54,000	*
Mastodon Ventures	100,000	*	100,000	100,000	*
Pat Paolini	5,000	*	5,000	5,000	*
Harold Paul (1)(6)	180,000	1.0%	130,000	180,000	1.0%
Gary Robinson	100,000	*	100,000	100,000	*
Sky Capital	150,000	*	150,000	150,000	*
Somerset Financial Group	105,645	*	105,645	105,645	*
Somerset Financial Partners	100,000	*	100,000	100,000	*
STG, Inc.	150,000	*	150,000	150,000	*
Nick Thompson	30,000	*	30,000	30,000	*
Douglas Toth	180,000	1.0%	180,000	180,000	1.0%
TNT	20,000	*	20,000	20,000	*
Richard Vitello	206,000	1.2%	100,000	206,000	1.2%
James & Joan Barton (1)	80,000	*	80,000	80,000	*
Glenn Bergenfield (1) (5)	374,500	2.1%	150,000	374,500	2.1%
Alan & Marie Brenner (1)	40,000	*	40,000	40,000	*
William & Cathe DiTuro (1)(5)	337,500	1.9%	160,000	337,500	1.9%
Ronald & Susan Farrell (1)	80,000	*	80,000	80,000	*
Raymond & Catherine Fernandez(1)	80,000	*	80,000	80,000	*
Tom Genco (1)	200,000	1.1%	200,000	200,000	1.1%
Steven Hitchcock (1)	80,000	*	80,000	80,000	*
Joseph & Nancy Jaffe (1)	40,000	*	40,000	40,000	*
Alton Jones (1)	300,000	1.7%	300,000	300,000	1.7%
Dennis Schneider (1)	80,000	*	80,000	80,000	*
Kathleen A. Ashcroft (2)	20,000	*	20,000	20,000	*
Thomas J. Fucili (2)	26,666	*	26,666	26,666	*
Dennis Josifovich (2)	26,666	*	26,666	26,666	*
Mountain Extremes (2)	33,334	*	33,334	33,334	*
Brendon Myers (2)	20,000	*	20,000	20,000	*
James Noonan (2)	20,000	*	20,000	20,000	*
Providence Investment Mgmt Grp (2)	800,000	4.6%	800,000	800,000	4.6%
James Solakian (2)	63,334	*	63,334	63,334	*
Alpha, AG (3)	566,666	3.2%	566,666	566,666	3.2%
Ellis International (3)	439,998	2.5%	439,998	439,998	2.5%
Everspring (3)	66,666	*	66,666	66,666	*
Gamma Opportunity Capital Partners, LP (3)	66,666	*	66,666	66,666	*

Joseph Giamanco, Sr. (3)	200,000	1.1%	200,000	200,000	1.1%
Michael Hamblet (3)	260,000	1.5%	260,000	260,000	1.5%
JAS Securities, LLC (3)	201,334	1.2%	201,334	201,334	1.2%
Michael Lauria (3)	20,000	*	20,000	20,000	*

Michael Maloney (3)	20,000	*	20,000	20,000	*
OTAPE Investments LLC (3)	536,000	3.1%	536,000	536,000	3.1%
Platinum Partners Value Arbitrage Fund LP (3)	666,666	3.8%	666,666	666,666	3.8%
Anthony J. Spatacco, Jr. (3)	34,000	*	34,000	34,000	*
TCMP3 Partners L.P. (3)	201,400	1.2%	201,400	201,400	1.2%
Truk Opportunity Fund, LLC(3)	60,000	*	60,000	60,000	*
WEC Partners (3)	66,666	*	66,666	66,666	*
A & M Composites Corporation (4)	714	*	714	714	*
Arizona Valve & Fitting Co. (4)	232	*	232	232	*
Case Sandblasting, Inc. (4)	110	*	110	110	*
Chemical Injection Technology, Inc. (4)	777	*	777	777	*
Don Craver (4)	9,974	*	9,974	9,974	*
Dale Foster Co. (4)	257	*	257	257	*
Electric Supply, Inc.(4)	1,383	*	1,383	1,383	*
Filtemp Sales, Inc. (4)	396	*	396	396	*
Grand Canyon Pump & Supply (4)	506	*	506	506	*
Ionics Pure Solutions, Inc.(4)	128	*	128	128	*
J. K. Williams Co. (4)	49	*	49	49	*
King Lee Chemical Co. (4)	387	*	387	387	*
Lambertson Industries, Inc.(4)	166	*	166	166	*
Monterry Pass Road Building(4)	13,849	*	13,849	13,849	*
Morrison & Hecker LLP (4)	719	*	719	719	*
Norgren (4)	209	*	209	209	*
Pacific RO Products (4)	2,063	*	2,063	2,063	*
Radio Engineering Industries, Inc. (4)	11,662	*	11,662	11,662	*
Reilly Harris Sales, Inc. (4)	2,770	*	2,770	2,770	*
Ryan Herco Products Corp. (4)	1,299	*	1,299	1,299	*
Shelco Filters (4)	470	*	470	470	*
Spaulding Composites Co. (4)	446	*	446	446	*
Sta-Rite Industries, Inc. (4)	2,156	*	2,156	2,156	*
Sunstate Equipment Co. (4)	182	*	182	182	*
Swift Systems, Inc. (4)	1,166	*	1,166	1,166	*
Time Master Trading, Inc. (4)	1,738	*	1,738	1,738	*
Tranter Phe, Inc. (4)	299	*	299	299	*
UltraViolet Systems (4)	186	*	186	186	*
Valley Commercial Landscape(4)	263	*	263	263	*
Watson Williams Freight Agency, Inc. (4)	423	*	423	423	*
Wendland Manufacturing Corp.(4)	358	*	358	358	*
	9,814,563		8,867,006	9,814,563	

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(1) In connection with a private placement in March 2003, each purchaser was issued a warrant to purchase shares of common stock equal to the number of preferred shares purchased in the private placement.

(2) In connection with a private placement in May 2003, each purchaser was issued a warrant to purchase shares of common stock equal to the number of preferred shares purchased in the private placement.
(3) In connection with a private placement in September 2003, each purchaser was issued a warrant to purchase shares of common stock equal to the number of common shares purchased in the private placement.
(4) In connection with the acquisition of Water Science Technologies, Inc. in March 2002, the selling stockholder agreed to accept shares of common stock of the Company as payment for the outstanding obligation.
(5) Director of the Company since inception.
(6) Owns 50,000 common shares, 50,000 common stock purchase warrants and as a purchaser in the March, 2003 private placement, owns 40,000 series A preferred shares and 40,000 common stock purchase warrants.
(7) The selling stockholder has agreed to lockup 50% of its shares until August 6, 2004 and the remaining 50% until August 6, 2005.

PLAN OF DISTRIBUTION

We are registering shares of our common stock on behalf of the selling stockholders. As used in this prospectus, "selling stockholders" includes donees and pledgees selling shares received from a named selling stockholder after the date of this prospectus. We will pay for all costs, expenses and fees in connection with the registration of the shares. The selling stockholders will pay for all selling discounts and commissions, if any. The selling stockholders may offer and sell their shares from time to time in one or more of the following types of transactions (including block transactions):

- on the American Stock Exchange,
- in privately negotiated transactions,
- through put or call options transactions relating to the shares,
- through short sales of shares, or
- a combination of such methods of sale.

The selling stockholders may sell their shares at prevailing market prices, or at privately negotiated prices. Such transactions may or may not involve brokers or dealers. To the Company's knowledge, the selling stockholders have not entered into any agreements, understanding or arrangements with any underwriters or broker-dealers regarding the sale of their shares, nor is there an underwriter or coordinating broker acting in connection with the proposed sale of shares by the selling stockholders.

The selling stockholders may offer and sell their shares directly to purchasers or to or through broker-dealers, which may act as agents or principals. Such broker-dealers may receive compensation in the form of discounts, concessions, or commissions from the selling stockholders and/or the purchasers of shares.

We have agreed to indemnify certain selling stockholders against certain liabilities, including liabilities arising under the Securities Act.

Selling stockholders also may resell all or a portion of the shares in open market transactions in reliance upon Rule 144 under the Securities Act of 1933, provided they meet the criteria and conform to the requirements of such rule.

DESCRIPTION OF CAPITAL STOCK

General

Our authorized capital stock consists of 50 million shares of capital stock, par value $0.001 per share. Currently 40 million of such shares of capital stock are classified as Common Stock and 10 million are classified as Preferred Stock. On October 3, 2003, 10,429,255 shares of our common stock were outstanding and held by 123 stockholders of record and the Company believes approximately 700 holders in the float. Our Restated Certificate of Incorporation authorizes the Board to classify any of the unissued shares of authorized Preferred Stock into one or more different classes or series of Preferred Stock which may be issued from time to time with such distinctive designations, rights and preferences as may be determined by the Board. We may issue Preferred Stock for possible future financings of acquisitions or for general corporate purposes without any legal requirement that further stockholder authorization for such issuance be obtained. The issuance of Preferred Stock could have the effect of making an attempt to gain control of us more difficult by means of a merger, tender offer, proxy contest or otherwise. Preferred Stock, if issued, could have a preference on dividend payments which could affect our ability to make dividend distributions to the holders of our Common Stock.

Common Stock

Dividends. Holders of our Common Stock will be entitled to dividends declared and payable at such times and in such amounts as the Board will from time to time determine out of funds legally available therefore. The rights of holders of our Common Stock to receive dividends will be subject and subordinate to the rights of any future holders of Preferred Stock as may be authorized by us.

Liquidation. Upon our liquidation, dissolution or winding up (either voluntary or involuntary), after payment of liabilities, any future holders of classes of our Preferred Stock or other senior stock, as may be authorized by us, will be entitled to receive the payment of all liquidation and other preference amounts; the holders of our Common Stock will be entitled to receive our remaining assets available for distribution to our stockholders pro rata according to the number of shares held. The following shall not constitute a liquidation, dissolution or winding up for the foregoing purposes:

- our consolidation or merger with or into another corporation;
- a merger of any other corporation with or into us or
- the sale of all or substantially all of our property or business (other than in connection with

a winding up of our business).

Voting. Each holder of our Common Stock is entitled to one vote for each share held of record on each matter submitted to vote of holders of our Common Stock.

Other Rights. There are no preemptive or other subscription conversion, redemption or sinking fund rights or provisions with respect to shares of our Common Stock. We hold annual stockholder meetings, and special meetings may be called by the President or Secretary or holders of at least 20% of the total voting power of all outstanding share of our capital stock then entitled to vote or a majority of the Board. Our Restated Certificate of Incorporation may be amended in accordance with the Delaware General Corporation Law, subject to certain limitations set forth therein.

Outstanding Options and Warrants

As of record date, up to 6,339,638 shares of Common Stock are issuable pursuant to outstanding options and warrants as follows:

- 481,000 shares of Common Stock are issuable, in connection with outstanding options, at a weighted average exercise price of $0.90; and

- 5,833,638 shares of Common Stock are issuable, in connection with outstanding warrants, at a weighted average exercise price of $2.55.

Series A Preferred Stock

Our Board has designated 1,870,000 shares of our preferred stock as Series A Preferred Stock, 1,185,000 shares of which were issued to private placement investors in April and May, 2003.

Dividends. The series A preferred stock will pay a cash dividend, payable quarterly, at the rate of 8% per annum. Dividends will cumulate if not paid.

Liquidation Preference. The series A preferred stock will have priority over common stock in the event of liquidation equal to its stated value, plus accrued and unpaid dividends.

Voluntary Conversion. Each share of the series A preferred stock will be convertible, at the option of the holder, into one share of common stock (subject to standard adjustments for stock splits and dividends).

Mandatory Conversion. Each share of the series A preferred stock automatically converts into common stock if (i) the closing price of the common stock is at least $1.89 per share (subject to standard adjustments for stocks, splits and dividends) for 20 consecutive trading days and (ii) either (a) at least one year has passed since the issuance of the preferred stock or (b) a registration statement registering the resale of the common stock issuable upon conversion has been declared effective by the SEC and the related prospectus remains current.

Voting. Holders of the series A preferred stock will not have voting rights until their shares are converted into common stock, except as required by Delaware Law.

Seniority. We may establish other series of preferred stock senior to or parri passu with the series A preferred stock.

Delaware Law and Certain Charter and By-Law Provisions and Antitakeover Effects

Delaware Law. We are subject to Section 203 of the Delaware General Corporation Law, which prevents an "interested stockholder" (defined in Section 203, generally, as a person owning 15% or more of a corporation's outstanding voting stock) from engaging in a "business combination" with a publicly held Delaware corporation for three years following the date such person became an interested stockholder, unless: (i) before such person became an interested stockholder, the board of directors of the corporation approved the transaction in which the interested stockholder became an interested stockholder or approved the business combination; (ii) upon consummation of the transaction that resulted in the interested stockholder becoming an interested stockholder, the interested stockholder owns at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced (subject to certain exceptions); or (iii) following the transaction in which that person became an interested stockholder, the business combination is approved by the board of directors of the corporation and authorized at a meeting of stockholders by affirmative vote of the holders of 66% of the outstanding voting stock of the corporation not owned by the interested stockholder. A "business combination" includes mergers, stock or asset sales and other transactions resulting in a financial benefit to the interested stockholder. The provisions of Section 203 could have the effect of delaying, deferring or preventing a change of control.

Certificate of Incorporation and Bylaws. Our restated certificate of incorporation provides for the division of the board of directors into three classes with staggered three-year terms. These provisions result in an increase in the time required for stockholders to change the composition of the board, and consequently may impede a change of control.

Transfer Agent, Warrant Agent and Registrar

The transfer agent and registrar for our common stock is U. S. Stock Transfer & Trust Corp., Glendale, California.

LEGAL MATTERS

The validity of the common stock offered with this prospectus has been passed upon for AquaCell Technologies, Inc. by Harold W. Paul, LLC, Westport, Connecticut.

EXPERTS

Our consolidated financial statements as of June 30, 2003 and for each of the two fiscal years in the period ended June 30, 2003, which are incorporated by reference herein from our Annual Report on Form 10-KSB for the year ended June 30, 2003 have been audited by Wolinetz, Lafazan & Company, PC, independent auditors, as stated in their report, which is also incorporated by reference herein, and have been so included in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

[AquaCell Technologies, Inc.]
Company Logo

Common Stock

P R O S P E C T U S

________________ , 2003

PART II

INFORMATION NOT REQUIRED IN PROSPECTUS

Item 14. Other Expenses of Issuance and Distribution.

The expenses expected to be incurred in connection with the issuance and distribution of the securities being registered, other than underwriting compensation, are as set forth below. Except for the registration fee payable to the Securities and Exchange Commission, all such expenses are estimated:

Securities and Exchange Commission registration fee	$ 1,831
Printing and engraving expenses	2,000
Legal fees and expenses	20,000
Miscellaneous (Est.)	1,169
Total	$ 25,000

Item 15. Indemnification of Directors and Officers.

Our Restated Certificate of Incorporation obligates us to indemnify our directors and officers and to pay or reimburse expenses for such individuals, in advance of the final disposition of a proceeding, to the maximum extent permitted from time to time by the Delaware General Corporation Law. With respect to our directors and officers, the Delaware General Corporation Law permits us to indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by us or in the right of us) by reason of the fact that the person is or was a director, officer, employee or agent of ours, or is or was serving at our request as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by the person in connection with such action, suit or proceeding if the person acted in good faith and in a manner the person reasonably believed to be in or not opposed to our best interests, and, with respect to any criminal action or proceeding, the person had no reasonable cause to believe the conduct was unlawful. The Delaware General Corporation Law also permits us to indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action or suit by us or in the right of us to procure a judgment in our favor by reason of the fact that the person is or was a director, officer, employee or agent of ours, or is or was serving at our request as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise against expenses (including attorneys' fees) actually and reasonably incurred by the person in connection with the defense or settlement of such action or suit if the person acted in good faith and in a manner the person reasonably believed to be in or not opposed to our best interests and except that no indemnification shall be made in respect of any claim, issue or matter as to which such person is adjudged to be liable to us unless and only to the extent that the Court of Chancery or the court in which such action or suit was brought determines upon application that, despite the adjudication of liability but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses that the Court of Chancery or such other court deems proper.

As authorized by the Delaware General Corporation Law, our Restated Certificate of Incorporation provides that none of our directors will be personally liable to us or our stockholders for monetary damages for breach of fiduciary duty as a director except for liability (i) for any breach of the director's duty of loyalty to us or our stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law,

(iii) in respect of certain unlawful dividend payments or stock redemptions or repurchases and (iv) for any transaction from which the director derives an improper personal benefit. The effect of this provision is to eliminate our rights and our stockholders' rights (through stockholders' derivative suits on our behalf) to recover monetary damages against a director for breach of the fiduciary duty of care as a director (including breaches resulting from negligent or

grossly negligent behavior) except in the situations described in clauses (i) through (iv) above. This provision does not limit or eliminate our rights or the rights of any stockholder to seek nonmonetary relief such as an injunction or rescission in the event of a breach of a director's duty of care. In addition, our Restated Certificate of Incorporation provides that if the Delaware General Corporation Law is amended to authorize the further elimination or limitation of the liability of a director, then the liability of the directors shall be eliminated or limited to the fullest extent permitted by the Delaware General Corporation Law, as so amended.

Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted for directors, officers and controlling persons of AquaCell pursuant to the foregoing provisions, or otherwise, we have been advised that in the opinion of the Securities and Exchange Commission, such indemnification is against public policy as expressed in the Securities Act of 1933 and is, therefore, unenforceable.

Item 16. Exhibits.

See Exhibit Index.

Item 17. Undertakings.

The undersigned Registrant hereby undertakes:

(1) To file, during any period in which offers or sales are being made, a post-effective amendment to this Registration Statement:

(i) To include any prospectus required by Section 10(a)(3) of the Securities Act of 1933.

(ii) To reflect in the prospectus any facts or events arising after the effective date of the registration statement (or the most recent post-effective amendment thereof) which, individually or in the aggregate, represent a fundamental change in the information set forth in the registration statement. Notwithstanding the foregoing, any increase or decrease in volume of securities offered (if the total dollar value of securities offered would not exceed that which was registered) and any deviation from the low or high end of the estimated maximum offering range may be reflected in the form of the prospectus filed with the Commission pursuant to Rule 424(b) if, in the aggregate, the changes in volume and price represent no more than 20 percent change in the maximum aggregate offering price set forth in the "Calculation of Registration Fee" table in the effective registration statement.

(iii) To include any material information with respect to the plan of distribution not previously disclosed in the registration statement or any material change to such information in the registration statement.

Provided, however, that paragraphs 1(a) and 1(b) do not apply if the Registration Statement is on Form S-3 or S-8 and the information required to be included in a post-effective amendment by those paragraphs is contained in periodic reports filed with or furnished to the Commission by the Company pursuant to Section 13 or Section 15(d) of the Exchange Act that are incorporated by reference in the Registration Statement.

(2) That, for the purpose of determining any liability under the Securities Act of 1933, each such post-effective amendment shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(3) To remove from registration by means of a post-effective amendment any of the securities being registered which remain unsold at the termination of the offering.

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(4) That, for purposes of determining any liability under the Securities Act, each filing of the registrant's annual report pursuant to Section 13(a) or 15(d) of the Exchange Act that is incorporated by reference in the Registration Statement shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(5) Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers and controlling persons of the registrant pursuant to Item 15 of this registration statement, or otherwise, the registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Act and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the registrant of expenses incurred or paid by a director, officer or controlling person of the registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Act and will be governed by the final adjudication of such issue.

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SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, the registrant hereby certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form S-3 and has duly caused this Registration Statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Rancho Cucamonga, State of California on October 21, 2003.

AQUACELL TECHNOLOGIES, INC.

By: /s/ James C. Witham

Name: James C. Witham
Title: Chief Executive Officer

Pursuant to the requirements of the Securities Act of 1933, this Registration Statement has been signed by the following persons in the capacities indicated on October 21, 2003.

Signatures	Title	Date
/s/ James C. Witham James C. Witham	Chairman of the Board of Directors and Chief Executive Officer (Principal Executive Officer)	October 21, 2003
/s/ Karen B. Laustsen Karen B. Laustsen	Director and President	October 21, 2003
/s/ Gary S. Wolff Gary S. Wolff	Director and Chief Financial Officer (and Principal Accounting Officer)	October 21, 2003
/s/ Glenn Bergenfield Glenn Bergenfield	Director	October 21, 2003
/s/ Dr. William DiTuro Dr. William DiTuro	Director	October 21, 2003

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INDEX TO EXHIBITS

Exhibits

5.1 Opinion of Harold W. Paul, LLC on the validity of the common stock registered hereby

10.1 Form of Subscription Agreement I

10.2 Form of Warrant dated April 1, 2003

10.3 Form of Subscription Agreement II

10.4 Form of Warrant dated May 9, 2003

10.5 Form of Subscription Agreement III

10.6 Form of Warrant dated September 10, 2003

10.7 Stock Purchase Agreement*

23.1 Consent of Harold W. Paul, LLC (included in the opinion delivered under Exhibit 5.1)

23.2 Consent of Wolinetz, Lafazan & Company, PC

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* Incorporated by reference from Form 8-K filed on April 3, 2002.

td>$66,224 $3,661 $(61,050) $8,835

Deferred Tax Expense	(823)	158	-	(665)
Change in Valuation Allowance	-	-	1,069	1,069
Balance at March 31, 2012	$65,401	$3,819	$(59,981)	$9,239
Deferred Tax Expense	(835)	320	-	(515)
Change in Valuation Allowance	-	-	(446)	(446)
Balance at June 30, 2012	$64,566	$4,139	$(60,427)	$8,278
Deferred Tax Expense	(843)	203	-	(640)
Unit Exchange	2,213	-	(1,935)	278
Change in Valuation Allowance	-	-	2,075	2,075
Balance at September 30, 2012	$65,936	$4,342	$(60,287)	$9,991

Pzena Investment Management, Inc.
Unaudited Notes to Consolidated Financial Statements (Continued)

The change in the Company's deferred tax liabilities, which is included in other liabilities on the Company's consolidated statements of financial condition, for the three and nine months ended September 30, 2012, is summarized as follows:

	Total (in thousands)
Balance at December 31, 2011	$ (13)
Deferred Tax Expense	(59)
Balance at March 31, 2012	$ (72)
Deferred Tax Expense	5
Balance at June 30, 2012	$ (67)
Deferred Tax Expense	5
Balance at September 30, 2012	$ (62)

The change in the Company's deferred tax assets, net of valuation allowance, for the three and nine months ended September 30, 2011 is summarized as follows:

	Section 754	Other	Valuation Allowance	Total
		(in thousands)		
Balance at December 31, 2010	$ 65,468	$ 2,797	$ (59,431)	$ 8,834
Deferred Tax Expense	(777)	96	-	(681)
Unit Exchange	2,381	-	(2,075)	306
Change in Valuation Allowance	-	-	865	865
Balance at March 31, 2011	$ 67,072	$ 2,893	$ (60,641)	$ 9,324
Deferred Tax Expense	(816)	71	-	(745)
Change in Valuation Allowance	-	-	1,980	1,980
Balance at June 30, 2011	$ 66,256	$ 2,964	$ (58,661)	$ 10,559
Deferred Tax Expense	(789)	166	-	(623)
Unit Exchange	1,544	-	(1,339)	205
Change in Valuation Allowance	-	-	(282)	(282)
Balance at September 30, 2011	$ 67,011	$ 3,130	$ (60,282)	$ 9,859

The change in the Company's deferred tax liabilities for the three and nine months ended September 30, 2011 is summarized as follows:

Total
(in
thousands)

Balance at December 31, 2010	$	(51)
Deferred Tax Expense		1
Balance at March 31, 2011	$	(50)
Deferred Tax Expense		19
Balance at June 30, 2011	$	(31)
Deferred Tax Expense		-
Balance at September 30, 2011	$	(31)

As of September 30, 2012 and December 31, 2011, the net values of the liability to selling and converting shareholders were approximately $11.7 million and $11.2 million, respectively.

Pzena Investment Management, Inc.
Unaudited Notes to Consolidated Financial Statements (Continued)

Note 8—Investments, at Fair Value

Investments in equity securities consisted of the following at September 30, 2012:

	Cost	Unrealized Gain/(Loss) (in thousands)	Fair Value
Equity Securities	$ 2,109	$ 126	$ 2,235
Investments in Mutual Funds	2,531	340	2,871
Total	$ 4,640	$ 466	$ 5,106

Investments in equity securities consisted of the following at December 31, 2011:

	Cost	Unrealized Gain/(Loss) (in thousands)	Fair Value
Equity Securities	$ 2,382	$ (97)	$ 2,285
Investments in Mutual Funds	2,542	92	2,634
Total	$ 4,924	$ (5)	$ 4,919

Note 9—Non-Controlling Interests

Non-Controlling Interests in the operations of the Company's operating company and consolidated subsidiaries are comprised of the following:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
	(in thousands)			
Non-Controlling Interests of Pzena Investment Management, LLC	$ 7,523	$ 7,811	$ 22,240	$ 26,841
Non-Controlling Interests of Consolidated Subsidiaries	210	(714)	563	(663)
Non-Controlling Interests	$ 7,733	$ 7,097	$ 22,803	$ 26,178

Distributions to non-controlling interests represent tax allocations and dividend equivalents paid to the members of the operating company, as well as withdrawals made by the Company's consolidated subsidiaries.

Note 10—Members' Equity Interests of Operating Company

Except as otherwise provided by law, the liability of a member of the operating company is limited to the amount of its capital account. A member may transfer or assign all or any part of its membership interest only with the prior written consent of the Company, which may be withheld in its sole discretion. Any transferee admitted as a member shall succeed to the capital account, or portion thereof, transferred or assigned, as if no such transfer or assignment had occurred.

Note 11—Equity

The Company functions as the sole managing member of the operating company. As a result, the Company: (i) consolidates the financial results of the operating company and reflects the membership interest in it that it does not own as a non-controlling interest in its consolidated financial statements; and (ii) recognizes income generated from its economic interest in the operating company's net income. Class A and Class B units of the operating company have the same economic rights per unit. As of September 30, 2012, the holders of Class A common stock (through the Company) and the holders of Class B units of the operating company held approximately 17.3% and 82.7%, respectively, of the economic interests in the operations of the business.

Each Class B unit of the operating company has a corresponding share of the Company's Class B common stock, par value $0.000001 per share. Each share of the Company's Class B common stock entitles its holder to five votes, until the first time that the number of shares of Class B common stock outstanding constitutes less than 20% of the number of all shares of the Company's common stock outstanding. From this time and thereafter, each share of the Company's Class B common stock entitles its holder to one vote. When a Class B unit is exchanged for a share of the Company's Class A common stock or forfeited, a corresponding share of the Company's Class B common stock will automatically be redeemed and cancelled. Conversely, to the extent that the Company causes the operating company to issue additional Class B units to employees pursuant to its equity incentive plan, these additional holders of Class B units would be entitled to receive a corresponding number of shares of the Company's Class B common stock (including if the Class B units awarded are subject to vesting).

All holders of the Company's Class B common stock have entered into a stockholders' agreement, pursuant to which they agreed to vote all shares of Class B common stock then held by them, and acquired in the future, together on all matters submitted to a vote of the common stockholders.

The outstanding shares of the Company's Class A common stock represent 100% of the rights of the holders of all classes of the Company's capital stock to receive distributions, except that holders of Class B common stock will have the right to receive the class's par value upon the Company's liquidation, dissolution or winding up.

Pursuant to the operating agreement of the operating company, each vested Class B unit is exchangeable for a share of the Company's Class A common stock, subject to certain exchange timing and volume limitations.

On August 31, 2012, September 15, 2011, and March 28, 2011, certain of the operating company's members exchanged an aggregate of 772,521, 670,902, and 536,528, respectively, of their Class B units for an equivalent number of shares of Company Class A common stock. The acquisition of additional operating company membership interest was treated as a reorganization of entities under common control as required by the Business Combinations Topic of the FASB ASC.

During the nine months ended September 30, 2012, a net amount of 74,271 options to purchase Class B units were exercised.

The Company's current share repurchase program was announced on April 24, 2012. The Board of Directors authorized the Company to repurchase an aggregate of $10 million of the Company's outstanding Class A common stock and the operating company's Class B units on the open market and in private transactions in accordance with applicable securities laws. The timing, number and value of common shares and units repurchased are subject to the Company's discretion. The Company's share repurchase program is not subject to an expiration date and may be suspended, discontinued, or modified at any time, for any reason.

During the three months ended September 30, 2012, the Company purchased and retired 24,666 shares of Class A common stock and 3,131 Class B units under the current repurchase authorization at an average price per share of $5.15 and $5.03, respectively. During the nine months ended September 30, 2012, the Company repurchased and retired 53,120 shares of Class A common stock and 3,131 Class B units under the repurchase authorization at an average price of $4.74 and $5.03, respectively. The Company records the repurchase of shares and units at cost based on the trade date of the transaction.

Note 12—Subsequent Events

The Company evaluated the need for disclosures and/or adjustments resulting from subsequent events through the date the financial statements were issued. This evaluation did not result in any subsequent events that necessitated disclosures and/or adjustments.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

We are a public-equity investment management firm that utilizes a classic value investment approach across all of our investment strategies. We currently manage assets in a variety of value-oriented investment strategies across a wide range of market capitalizations in both U.S. and non-U.S. capital markets. At September 30, 2012, our assets under management, or AUM, was $16.8 billion. We manage separate accounts on behalf of institutions and high net worth individuals, and act as sub-investment adviser for a variety of SEC-registered mutual funds and offshore funds.

We function as the sole managing member of our operating company, Pzena Investment Management, LLC (the "operating company"). As a result, we: (i) consolidate the financial results of our operating company with our own, and reflect the membership interest in it that we do not own as a non-controlling interest in our consolidated financial statements; and (ii) recognize income generated from our economic interest in our operating company's net income. As of September 30, 2012, the holders of Class A common stock (through the Company) and the holders of Class B units of our operating company held approximately 17.3% and 82.7%, respectively, of the economic interests in the operations of our business.

Non-GAAP Net Income

Our results for the three and nine months ended September 30, 2012, and 2011 include the recurring adjustments related to the Company's tax receivable agreement and the associated liability to its selling and converting shareholders. We believe that these accounting adjustments add a measure of non-operational complexity which partially obscures the underlying performance of our business. In evaluating our financial condition and results of operations, we also review certain non-GAAP measures of earnings, which exclude these items. Excluding these adjustments, non-GAAP diluted net income and non-GAAP diluted earnings per share were $5.2 million and $0.08, respectively, for the three months ended September 30, 2012, and $5.3 million and $0.08, respectively, for the three months ended September 30, 2011. Excluding these adjustments, non-GAAP diluted net income and non-GAAP diluted earnings per share were $15.2 million and $0.23, respectively for the nine months ended September 30, 2012, and $18.1 million and $0.28, respectively, for the nine months ended September 30, 2011. GAAP and non-GAAP net income for diluted earnings per share generally assumes all operating company membership units are converted into Company stock at the beginning of the reporting period, and the resulting change to our net income associated with our increased interest in the operating company is taxed at our historical effective tax rate, exclusive of one-time prior period adjustments and the adjustments related to our tax receivable agreement and the associated liability to selling and converting shareholders. Our effective tax rate, exclusive of these adjustments, was approximately 42.9% for the each of the three and nine months ended September 30, 2012 and 2011, as noted in the section "Operating Results - Income Tax Expense" below.

We use these non-GAAP measures to assess the strength of the underlying operations of the business. We believe that these adjustments, and the non-GAAP measures derived from them, provide information to better analyze our operations between periods, and over time. Investors should consider these non-GAAP measures in addition to, and not as a substitute for, financial measures prepared in accordance with GAAP.

A reconciliation of the non-GAAP measures to the most comparable GAAP measures is included below:

	For the Three Months Ended September 30, 2012	For the Three Months Ended September 30, 2011	For the Nine Months Ended September 30, 2012	For the Nine Months Ended September 30, 2011
	(in thousands, except share and per share amounts)			
GAAP Net Income	$ 1,263	$ 497	$ 2,884	$ 3,013
Net Effect of Tax Receivable Agreement	(391)	332	(356)	(256)
Non-GAAP Net Income	$ 872	$ 829	$ 2,528	$ 2,757
GAAP Income Attributable to Non-Controlling Interest of Pzena Investment Management, LLC	$ 7,523	$ 7,811	$ 22,240	$ 26,841
Less: Assumed Corporate Income Taxes	3,224	3,348	9,530	11,504
Assumed After-Tax Income of Pzena Investment Management, LLC	$ 4,299	$ 4,463	$ 12,710	$ 15,337
Non-GAAP Net Income of Pzena Investment Management, Inc.	872	829	2,528	2,757
Non-GAAP Diluted Net Income	$ 5,171	$ 5,292	$ 15,238	$ 18,094
Non-GAAP Diluted Earnings Per Share Attributable to Pzena Investment Management, Inc. Common Stockholders:				
Non-GAAP Net Income for Diluted Earnings per Share	$ 5,171	$ 5,292	$ 15,238	$ 18,094
Non-GAAP Diluted Earnings Per Share	$ 0.08	$ 0.08	$ 0.23	$ 0.28
Non-GAAP Diluted Weighted-Average Shares Outstanding	65,404,610	64,910,014	65,382,457	65,011,182

Revenue

We generate revenue primarily from management fees and performance fees, which we collectively refer to as our advisory fees, by managing assets on behalf of institutional accounts and for retail clients, which are generally open-end mutual funds catering primarily to retail investors. Our advisory fee income is recognized over the period in which investment management services are provided. Following the preferred method identified in the Revenue Recognition Topic of the Financial Accounting Standards Board Accounting Standards Codification (“FASB ASC”), income from performance fees is recorded at the conclusion of the contractual performance period, when all contingencies are resolved.

Our advisory fees are primarily driven by the level of our AUM. Our AUM increases or decreases with the net inflows or outflows of funds into our various investment strategies and with the investment performance thereof. In order to increase our AUM and expand our business, we must develop and market investment strategies that suit the investment needs of our target clients, and provide attractive returns over the long term. The value and composition of our AUM, and our ability to continue to attract clients, will depend on a variety of factors including, among other things:

- our ability to educate our target clients about our classic value investment strategies and provide them with exceptional client service;
- the relative investment performance of our investment strategies, as compared to competing products and market indices;
- competitive conditions in the investment management and broader financial services sectors;
- general economic conditions;
- investor sentiment and confidence; and
- our decision to close strategies when we deem it to be in the best interests of our clients.

For our institutional accounts, we are paid fees according to a schedule, which varies by investment strategy. The substantial majority of these accounts pay us management fees pursuant to a schedule in which the rate we earn on the AUM declines as the amount of AUM increases.

Pursuant to our sub-investment advisory agreements with our retail clients, we are generally paid a management fee according to a schedule in which the rate we earn on the AUM declines as the amount of AUM increases. Certain of these funds pay us fixed-rate management fees. Due to the substantially larger account size of certain of these accounts, the average advisory fees we earn on them, as a percentage of AUM, are lower than the advisory fees we earn on our institutional accounts.

Certain of our clients pay us fees according to the performance of their accounts relative to certain agreed-upon benchmarks, which results in a lower base fee, but allows us to earn higher fees if the relevant investment strategy outperforms the agreed-upon benchmark.

The majority of advisory fees we earn on institutional accounts is based on the value of our AUM at a specific date on a quarterly basis, either in arrears or advance. Advisory fees on certain of our institutional accounts, and with respect to all of our retail accounts, are calculated based on the average of the monthly or daily market value. Advisory fees are also generally adjusted for any cash flows into or out of a portfolio, where the cash flow represents greater than 10% of the value of the portfolio. While a specific group of accounts may use the same fee rate, the method used to calculate the fee according to the fee rate schedule may differ as described above.

Our advisory fees may fluctuate based on a number of factors, including the following:

- changes in AUM due to appreciation or depreciation of our investment portfolios, and the levels of the contribution and withdrawal of assets by new and existing clients;
- distribution of AUM among our investment strategies, which have differing fee schedules;
- distribution of AUM between institutional accounts and retail accounts, for which we generally earn lower overall advisory fees; and
- the level of our performance with respect to accounts on which we are paid performance fees.

Expenses

Our expenses consist primarily of compensation and benefits expense, as well as general and administrative expense. These expenses may fluctuate due to a number of factors, including the following:

- variations in the level of total compensation expense due to, among other things, bonuses, awards of equity to our employees and employee members of our operating company, changes in our employee count and mix, and competitive factors; and
- expenses, such as rent, professional service fees and data-related costs, incurred, as necessary, to run our business.

Compensation and Benefits Expense

Our largest expense is compensation and benefits, which includes the salaries, bonuses, equity-based compensation, and related benefits and payroll costs attributable to our employee members and employees. Compensation and benefits packages are benchmarked against relevant industry and geographic peer groups in order to attract and retain qualified personnel.

Pursuant to the Pzena Investment Management, LLC Amended and Restated 2006 Equity Incentive Plan (the “2006 Equity Incentive Plan”), we have issued restricted units and options to purchase units in our operating company. Under the Pzena Investment Management, Inc. 2007 Equity Incentive Plan ("the 2007 Equity Incentive Plan"), we have issued shares of nonparticipating restricted Class A common stock and options to acquire shares of our Class A common stock.

We use a fair-value method in recording the compensation expense associated with the granting of restricted units, restricted common stock, and options to purchase units and common stock, to new and existing employee members and employees of our operating company under the 2006 and 2007 Equity Incentive Plans. Under this method, compensation expense is measured at the grant-date based on the estimated fair value of the award and is recognized over the award's vesting period.

The fair value of awarded restricted Class B units is determined by reference to the market price of our Class A common stock on the date of grant, since these units are exchangeable for shares of our Class A common stock on a one-for-one basis. For each of the three months ended September 30, 2012 and 2011, there were no restricted operating company Class B units granted. For the nine months ended September 30, 2012 and 2011, we granted 53,116 and 6,000, respectively, restricted operating company Class B units, and the related shares of Class B common stock, under the 2006 Equity Incentive Plan.

The fair value of awarded restricted shares of Class A common stock is determined based on the closing market price of our Class A common stock on the date of grant, net of the present value of the dividends using the applicable risk-free interest rate, as these nonparticipating restricted shares of Class A common stock are not entitled to dividends or dividend equivalents while unvested. For the three and nine months ended September 30, 2012, we granted 44,484 shares of nonparticipating restricted Class A common stock pursuant to the 2007 Equity Incentive Plan. No such shares were granted for the three or nine months ended September 30, 2011.

For each of the three months ended September 30, 2012 and 2011, we recognized approximately $0.2 million in compensation and benefits expense associated with the amortization of all unvested restricted operating company Class B units and unvested shares of Class A common stock. For the nine months ended September 30, 2012 and 2011, we recognized approximately $0.7 million and $0.5 million, respectively, in such compensation and benefits expense.

The fair value of the options to purchase Class B units and Class A common stock is determined by using an appropriate option pricing model on the grant-date. For the three and nine months ended September 30, 2012 and 2011, there were no options granted to purchase units or shares of common stock under the 2006 and 2007 Equity Incentive Plans. For the three months ended September 30, 2012 and 2011, we recognized approximately $0.1 million and $0.5 million, respectively, in compensation and benefits expense associated with the amortization of all unvested options to acquire operating company Class B units and unvested options to acquire Class A common stock issued under the 2006 and 2007 Equity Incentive Plans. For the nine months ended September 30, 2012 and 2011, we recognized approximately $0.2 million and $1.6 million, respectively, in such expense.

Pursuant to the Pzena Investment Management, LLC Amended and Restated Bonus Plan (the “Bonus Plan”), eligible employees whose cash compensation is in excess of certain thresholds have a portion of that excess mandatorily deferred. These deferred amounts may be invested, at the employee’s discretion, in certain third-party mutual funds, restricted phantom units of our operating company, or money market funds. Amounts deferred in any calendar year reduce that year’s cash compensation expense and are amortized ratably over a four-year period commencing the following year. At September 30, 2012 and December 31, 2011, the liability associated with deferred compensation investment accounts was approximately $1.0 million and $1.2 million, respectively, and is recorded as deferred compensation liability on the consolidated statements of financial condition. For the three months ended September 30, 2012 and 2011, we recognized approximately $0.4 million and $0.3 million, respectively, in compensation and benefits expense associated with the amortization of all deferred compensation awards. For the nine months ended September 30, 2012 and 2011, we recognized approximately $1.2 million and $1.3 million, respectively, in such expense.

As of September 30, 2012, we had approximately $1.9 million in total unrecorded compensation expense related to unvested operating company phantom units issued pursuant to our Bonus Plan, shares of Class A common stock, and operating company unit and option grants issued under the 2006 and 2007 Equity Incentive Plan. We expect that the amortization of these amounts will be approximately $1.5 million in 2012, $0.9 million in 2013, $0.4 million in 2014 and $0.1 million in 2015.

We have historically granted delayed-vesting cash awards to certain of our employee members. These delayed-vesting cash awards have varying vesting schedules, with $0.8 million to be paid in 2012 and the remaining $0.4 million to be paid in 2013.

General and Administrative Expense

General and administrative expense includes office rent and other expenses, professional and outside services fees, depreciation, and the costs associated with operating and maintaining our research, trading, and portfolio accounting systems. Our occupancy-related costs and professional services expenses, in particular, generally increase or decrease in relative proportion to the overall size and scale of our business operations.

We incur additional expenses associated with being a public company for, among other things, director and officer insurance, director fees, SEC reporting and compliance (including Sarbanes-Oxley and Dodd-Frank compliance), professional fees, transfer agent fees, and other similar expenses. These additional expenses have and will continue to reduce our net income.

Other (Expense)

Other (expense) is derived primarily from investment income or loss arising from our consolidated subsidiaries, our investments in various private investment vehicles that we employ to incubate new strategies, income or loss generated by our investments in third-party mutual funds, and interest income generated on our cash balances. Other (expense) is also affected by changes in our estimates of the liability due to our selling and converting shareholders associated with payments owed to them under the tax receivable agreement which was executed in connection with our reorganization and offering on October 30, 2007. As discussed further below under “Tax Receivable Agreement,” this liability represents 85% of the amount of cash savings, if any, in U.S. federal, state, and local income tax that we realize as a result of the amortization of the increases in tax basis generated from our acquisitions of our operating company’s units from our selling and converting shareholders. Amounts waived by our selling and converting shareholders, if any, reduce this liability. We expect the interest and investment components of other (expense), in the aggregate, to fluctuate based on market conditions and the performance of our consolidated investment partnerships and other investments.

Non-Controlling Interests

Our operating company has historically consolidated the results of operations of the private investment partnerships over which we exercise a controlling influence. We are the sole managing member of our operating company and control its business and affairs and, therefore, consolidate its financial results with ours. In light of our employees’ and outside investors’ interest in our operating company, we have reflected their membership interests as a non-controlling interest in our consolidated financial statements. As a result, our income is generated by our economic interest in our operating company’s net income. As of September 30, 2012, the holders of Class A common stock (through the Company) and the holders of Class B units of the operating company held approximately 17.3% and 82.7%, respectively, of the economic interests in the operations of the business.

Income Tax Expense/(Benefit)

As a “C” corporation under the Internal Revenue Code, we are liable for federal, state and local taxes on the income derived from our economic interest in the operating company, which is net of its provision for New York City Unincorporated Business Taxes, or UBT. Correspondingly, in our consolidated financial statements, we report both the operating company’s provision for UBT, as well as our provision for federal, state and local corporate taxes.

Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount more likely than not to be realized. As of September 30, 2012 and December 31, 2011, our valuation allowance against the deferred tax asset associated with our acquisition of operating company units in conjunction with the offering and subsequent exchanges was $60.3 million and $61.1 million, respectively.

Operating Results

Assets Under Management and Flows

As of September 30, 2012, approximately $16.8 billion of AUM was invested in a variety of value-oriented investment strategies, representing distinct capitalization segments of U.S. and non-U.S. equity markets. The performance of our largest investment strategies as of September 30, 2012 is further described below. As of July 1, 2012, we launched a Large Cap Diversified Value strategy which, by asset size, is now one of our largest investment strategies. We follow the same investment process for each of these strategies. Our investment strategies are distinguished by the market capitalization ranges from which we select securities for their portfolios, which we refer to as each strategy’s investment universe, as well as the regions in which we invest. While our investment process includes ongoing review of companies in the investment universes described below, our actual investments may include companies outside of the relevant market capitalization range at the time of our investment. In addition, the number of holdings typically found in the portfolios of each of our investment strategies may vary, as described below.

The following table indicates the annualized returns, gross and net (which represents annualized returns prior to, and after, payment of advisory fees, respectively), of our largest investment strategies from their inception to September 30, 2012, and in the five-year, three-year, and one-year periods ended September 30, 2012, relative to the performance of: (i) the market index which is most commonly used by our clients to compare the performance of the relevant investment strategy, and (ii) the S&P 500® Index, which is provided for the limited purpose of providing a comparison to the broader equity market.

Investment Strategy (Inception Date)	Period Ended September 30, 2012(1) Since Inception		5 Years		3 Years		1 Year	
Large Cap Value (October 2000)								
Annualized Gross Returns	4.5	%	(3.5	)%	7.9	%	26.5	%
Annualized Net Returns	4.0	%	(4.0	)%	7.4	%	25.9	%
Russell 1000® Value Index	4.3	%	(0.9	)%	11.8	%	30.9	%
S&P 500® Index	2.0	%	1.0	%	13.2	%	30.2	%
Global Value (January 2004)								
Annualized Gross Returns	2.4	%	(6.2	)%	3.3	%	23.3	%
Annualized Net Returns	1.6	%	(6.8	)%	2.6	%	22.6	%
MSCI World(SM) Index(2)	4.8	%	(2.1	)%	7.5	%	21.6	%
S&P 500® Index	5.1	%	1.0	%	13.2	%	30.2	%
Large Cap Diversified Value (July 2012)								
Annualized Gross Returns(4)	6.4	%	—		—		—	
Annualized Net Returns(4)	6.4	%	—		—		—	
Russell 2000® Value Index	6.5	%	—		—		—	
S&P 500® Index	6.3	%	—		—		—	
International Diversified Value (November 2008)(3)								
Annualized Gross Returns	13.2	%	—		2.6	%	19.0	%
Annualized Net Returns	12.9	%	—		2.4	%	18.7	%
MSCI EAFE® Index(2)	8.5	%	—		2.1	%	13.7	%
S&P 500® Index	13.2	%	—		13.2	%	30.2	%
Value Service (January 1996)								
Annualized Gross Returns	9.7	%	(2.6	)%	9.6	%	29.0	%
Annualized Net Returns	8.9	%	(3.3	)%	8.8	%	28.2	%
Russell 1000® Value Index	7.8	%	(0.9	)%	11.8	%	30.9	%
S&P 500® Index	7.1	%	1.0	%	13.2	%	30.2	%
Small Cap Value (January 1996)								
Annualized Gross Returns	13.3	%	5.1	%	13.2	%	37.4	%
Annualized Net Returns	12.1	%	4.1	%	12.1	%	36.0	%
Russell 2000® Value Index	9.2	%	1.3	%	11.7	%	32.6	%
S&P 500® Index	7.1	%	1.0	%	13.2	%	30.2	%

(1) The historical returns of these investment strategies are not necessarily indicative of their future performance, or the future performance of any of our other current or future investment strategies.

(2) Net of applicable withholding taxes and presented in U.S.$.

(3) Formerly known as EAFE Diversified Value

(4) The Large Cap Diversified Value strategy, launched in July 2012, Annualized Gross and Net returns are the same due to timing of advisory fee payments.

Large Cap Value. We screen a universe of the 500 largest U.S.-listed companies, based on market capitalization, to build a portfolio generally consisting of 30 to 40 stocks. We launched this strategy in October 2000. At September 30, 2012, the Large Cap Value strategy generated a one-year annualized gross return of 26.5%, underperforming both its benchmark and the broader equity market in general. This underperformance relative to the benchmark was due primarily to our stock selection within the consumer discretionary and energy sectors and our overweight investment exposure to the technology sector, partially offset by our investment exposure to the materials sector and stock selection within the financial services sector.

Global Value. We screen a universe of the 1,500 largest non U.S.-listed companies, based on market capitalization, and the 500 largest U.S.-listed companies, based on market capitalization, to build a portfolio generally consisting of 40 to 60 stocks. We launched this strategy in January 2004. At September 30, 2012, the Global Value strategy generated a one-year annualized gross return of 23.3%, outperforming its benchmark and underperforming the broader equity market in general. This outperformance relative to the benchmark was due primarily to our stock selection within the industrials, materials and consumer discretionary sectors, partially offset by our stock selection within the information technology sector.

Large Cap Diversified Value. We screen a universe of the 500 largest U.S.-listed companies, based on market capitalization, to build a portfolio generally consisting of 50 to 80 stocks. We launched this strategy in July 2012. At September 30, 2012, the Large Cap Value strategy generated a gross return of 6.4% since inception, relatively even with both its benchmark and the broader equity market in general.

International Diversified Value (formerly known as EAFE Diversified Value). We screen a universe of the 1,500 largest non-U.S.-listed companies, based on market capitalization, to build a portfolio generally consisting of 60 to 100 stocks. We launched this strategy in November 2008. At September 30, 2012, the International Diversified Value strategy generated a one-year annualized gross return of 19.0%, outperforming its benchmark and underperforming the broader equity market in general. This outperformance relative to the benchmark was due primarily to our stock selection within the consumer discretionary, industrials, and materials sectors, partially offset by our stock selection within the financial services sector.

Value Service. We screen a universe of the 1,000 largest U.S.-listed companies, based on market capitalization, to build a portfolio generally consisting of 30 to 40 stocks. We launched this strategy in January 1996. At September 30, 2012, the Value strategy generated a one-year annualized gross return of 29.0%, underperforming both its benchmark and the broader equity market in general. This underperformance relative to the benchmark was due primarily to our overweight investment exposure to the technology sector and stock selection within the producer durables sector, partially offset by our investment exposure to the materials sector.

Small Cap Value. We screen a universe of U.S.-listed companies ranked from the 1,001st to 3,000th largest, based on market capitalization, to build a portfolio generally consisting of 40 to 50 stocks. We launched this strategy in January 1996. At September 30, 2012, the Small Cap Value strategy generated a one-year annualized gross return of 37.4%, outperforming both its benchmark and the broader equity market in general. This outperformance relative to the benchmark was due primarily to our stock selection within the financial services and materials sectors, and our underweight investment exposure to the utilities sector, partially offset by our investment exposure to the consumer discretionary sector.

Our earnings and cash flows are heavily dependent upon prevailing financial market conditions. Significant increases or decreases in the various securities markets, particularly the equities markets, can have a material impact on our results of operations, financial condition, and cash flows.

The change in AUM in our institutional accounts and our retail accounts for the three and nine months ended September 30, 2012 and 2011, and the twelve months ended September 30, 2012, is described below. Inflows are composed solely of the investment of new or additional assets by new or existing clients. Outflows consist solely of redemptions of assets by existing clients.

Assets Under Management	For the Three Months Ended September 30, 2012	For the Three Months Ended September 30, 2011	For the Nine Months Ended September 30, 2012	For the Nine Months Ended September 30, 2011	For the Twelve Months Ended September 30, 2012
			(in billions)		
Institutional Accounts					
Assets					
Beginning of Period	$ 10.9	$ 12.9	$ 11.3	$ 12.5	$ 10.0
Inflows	0.3	0.3	0.7	1.3	1.3
Outflows	(0.7)	(0.4)	(2.3)	(1.6)	(2.7)
Net Flows	(0.4)	(0.1)	(1.6)	(0.3)	(1.4)
Market Appreciation/(Depreciation)	0.7	(2.8)	1.5	(2.2)	2.6
End of Period	$ 11.2	$ 10.0	$ 11.2	$ 10.0	$ 11.2
Retail Accounts					
Assets					
Beginning of Period Assets	$ 2.2	$ 3.0	$ 2.2	$ 3.1	$ 2.2
Inflows	3.3	0.2	3.5	0.8	3.8
Outflows	(0.3)	(0.4)	(0.7)	(1.3)	(1.2)
Net Flows	3.0	(0.2)	2.8	(0.5)	2.6
Market Appreciation/(Depreciation)	0.4	(0.6)	0.6	(0.4)	0.8
End of Period	$ 5.6	$ 2.2	$ 5.6	$ 2.2	$ 5.6
Total					
Assets					
Beginning of Period	$ 13.1	$ 15.9	$ 13.5	$ 15.6	$ 12.2
Inflows	3.6	0.5	4.2	2.1	5.1
Outflows	(1.0)	(0.8)	(3.0)	(2.9)	(3.9)
Net Flows	2.6	(0.3)	1.2	(0.8)	1.2
Market Appreciation/(Depreciation)	1.1	(3.4)	2.1	(2.6)	3.4
End of Period	$ 16.8	$ 12.2	$ 16.8	$ 12.2	$ 16.8

The following table describes the allocation of our AUM among our investment strategies, as of September 30, 2012 and 2011:

Investment Strategy	AUM at September 30, 2012	AUM at September 30, 2011
	(in billions)	

U.S. Value Strategies	$	10.8	$	7.4
Global Value Strategies		4.0		3.0
Non-U.S. Value Strategies		2.0		1.8
Total	$	16.8	$	12.2

During the twelve months ended September 30, 2012, our AUM increased $4.6 billion, or 37.7%, from $12.2 billion at September 30, 2011, to $16.8 billion at September 30, 2012. This increase is primarily due to large inflows in our retail Large Cap Diversified Value Strategy and market appreciation during the twelve months ended September 30, 2012.

At September 30, 2012, we managed $11.2 billion in institutional accounts and $5.6 billion in retail accounts, for a total of $16.8 billion in assets. For the three months ended September 30, 2012, we experienced total gross inflows of $3.6 billion, which were partially offset by total gross outflows of $1.0 billion. For the three months ended September 30, 2012, assets in institutional accounts increased by $0.3 billion, or 2.8%, due to $0.7 billion in market appreciation and $0.3 billion in gross inflows, partially offset by $0.7 billion in gross outflows. Assets in retail accounts increased by $3.4 billion, or 154.5%, as a result of $3.3 billion in inflows and $0.4 billion in market appreciation, partially offset by $0.3 billion in gross outflows. Retail inflows are primarily associated with our mandate to manage 28% of the Vanguard Windsor Fund as of the beginning of August 2012.

For the nine months ended September 30, 2012, we experienced total gross inflows of $4.2 billion, which were partially offset by total gross outflows of $3.0 billion. For the nine months ended September 30, 2012, assets in institutional accounts decreased by $0.1 billion, or 0.9%, due to $2.3 billion in gross outflows, partially offset by $0.7 billion in gross inflows and $1.5 billion in market appreciation. Assets in retail accounts increased by $3.4 billion, or 154.5%, as a result of $3.5 billion in gross inflows and $0.6 billion in market appreciation, partially offset by $0.7 billion in gross outflows. As mentioned above, retail inflows are primarily associated with our mandate to manage 28% of the Vanguard Windsor Fund as of the beginning of August 2012.

Our revenues are generally correlated with the levels of our weighted average AUM. Our weighted average AUM fluctuates based on changes in the market value of accounts advised and managed by us, and on our fund flows. Since we are long-term fundamental investors, we believe that our investment strategies yield the most benefits, and are best evaluated, over a long-term timeframe. We believe that our investment strategies are generally evaluated by our clients and our potential future clients based on their relative performance since inception, and the previous one-year, three-year, and five-year periods. There has typically been a correlation between our strategies' investment performance and the size and direction of asset flows over the long term. To the extent that our returns for these periods outperform client benchmarks, we would generally anticipate increased asset flows over the long term. Correspondingly, negative returns relative to client benchmarks could cause existing clients to reduce their exposure to our products, or hinder new client acquisition.

In addition, an increase in weighted average AUM and in revenues typically results in higher operating income and net income while a decrease in weighted average AUM and in revenues typically results in lower operating income, net income, and operating margins. We would expect pressure on our operating income, net income, and operating margins in the future if average AUM and revenues were to decline.

Revenues

Our revenue from advisory fees earned on our institutional accounts and our retail accounts for the three and nine months ended September 30, 2012 and 2011 is described below:

Revenue	For the Three Months Ended September 30, 2012	For the Three Months Ended September 30, 2011	For the Nine Months Ended September 30, 2012	For the Nine Months Ended September 30, 2011
	(in thousands)			
Institutional Accounts	$ 15,741	$ 17,363	$ 49,110	$ 55,406
Retail Accounts	3,120	2,587	7,858	8,703
Total	$ 18,861	$ 19,950	$ 56,968	$ 64,109

Three Months Ended September 30, 2012 versus September 30, 2011

Our total revenue decreased $1.1 million, or 5.5%, to $18.9 million for the three months ended September 30, 2012, from $20.0 million for the three months ended September 30, 2011. This change was driven primarily by the lack of performance fees recognized during the three months ended September 30, 2012 compared to $1.1 million of performance fees recognized for the three months ended September 30, 2011.

Our weighted average fees were 0.508% and 0.560% for the three months ended September 30, 2012 and 2011, respectively. This decrease was primarily due to the decrease in performance fees recognized during the three months ended September 30, 2012 as discussed above combined with the partial period impact of a higher mix of assets in our retail Large Cap Diversified Value Strategy, which carries a lower fee rate.

Weighted average assets in institutional accounts decreased $0.8 billion, or 6.8%, to $10.9 billion for the three months ended September 30, 2012, from $11.7 billion for the three months ended September 30, 2011, and had weighted average fees of 0.575% and 0.597% for the three months ended September 30, 2012 and 2011, respectively. The decrease in weighted average fees in institutional accounts was primarily due to no performance fees being recognized during the third quarter of 2012.

Weighted average assets in retail accounts increased $1.3 billion, or 50%, to $3.9 billion for the three months ended September 30, 2012, from $2.6 billion for the three months ended September 30, 2011, and had weighted average fees of 0.321% and 0.395% for the three months ended September 30, 2012 and 2011, respectively. The decrease in weighted average fees in retail accounts was primarily due to a higher mix of assets in our retail Large Cap Diversified Value strategy, which carries a lower fee rate.

Nine Months Ended September 30, 2012 versus September 30, 2011

Our total revenue decreased $7.1 million, or 11.1%, to $57.0 million for the nine months ended September 30, 2012, from $64.1 million for the nine months ended September 30, 2011. This decrease was driven primarily by a $1.1 billion decrease in weighted average AUM, or 7.1%, to $14.4 billion for the nine months ended September 30, 2012, from $15.5 billion for the nine months ended September 30, 2011. The decrease was also attributable to a reduction in performance fees recognized during the nine months ended September 30, 2012. Such performance fees generated $0.3 million and $2.5 million for the nine months ended September 30, 2012 and 2011, respectively. As noted above, to the extent that we experience reductions in weighted average AUM, either through negative market performance or net client outflows, our revenue will be adversely affected.

Our weighted average fees were 0.529% and 0.553% for the nine months ended September 30, 2012 and 2011, respectively. This decrease was primarily due to the decrease in performance fees recognized during the nine months ended September 30, 2012 combined with the partial period impact of a higher mix of assets in our retail Large Cap Diversified Value Strategy, which carries a lower fee rate.

Weighted average assets in institutional accounts decreased $1.1 billion, or 8.8%, to $11.4 billion for the nine months ended September 30, 2012, from $12.5 billion for the nine months ended September 30, 2011, and had weighted average fees of 0.575% and 0.592% for the nine months ended September 30, 2012 and 2011, respectively. The decrease in weighted average fees in institutional accounts was primarily due to a decrease in performance fees recognized during the nine months ended September 30, 2012, partially offset by the decrease in weighted average institutional assets. Our tiered fee schedules typically charge higher rates as account size decreases.

Weighted average assets in retail accounts was $3.0 billion, relatively flat, for the nine months ended September 30, 2012 and 2011, and had weighted average fees of 0.352% and 0.388% for the nine months ended September 30, 2012 and 2011, respectively. The decrease in weighted average fees in retail accounts was primarily due to the higher mix of assets in our retail Large Cap Diversified Value Strategy, which carries a lower fee rate.

Expenses

Our operating expense is driven primarily by our compensation costs. The table below describes the components of our compensation expense for the three and nine months ended September 30, 2012 and 2011:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
	(in thousands)			
Cash Compensation and Other Benefits	$6,967	$6,688	$21,801	$20,973
Other Non-Cash Compensation	722	1,039	2,073	3,402
Total Compensation and Benefits Expense	7,689	7,727	23,874	24,375
General and Administrative Expense	1,764	1,969	5,383	5,972
Total Operating Expenses	$9,453	$9,696	$29,257	$30,347

Three Months Ended September 30, 2012 versus September 30, 2011

Total operating expense decreased by $0.2 million, or 2.5%, to $9.5 million for the three months ended September 30, 2012, from $9.7 million for the three months ended September 30, 2011. This decrease was primarily attributable to reductions in real estate expenses associated with the sublease of excess office space.

Compensation and benefits expense was $7.7 million, relatively flat, for the three months ended September 30, 2012 and 2011. Non-cash compensation decreased by $0.3 million, or 30.5%, to $0.7 million for the three months ended September 30, 2012, from $1.0 million for the three months ended September 30, 2011. This decrease was offset by an increase of $0.3 million in cash compensation, or 41.7%, to $7.0 million for the three months ended September 30, 2012, from $6.7 million for the three months ended September 30, 2011. These changes are attributable to the amortization of previously issued awards partially offset by a shift in compensation mix. We expect non-cash compensation expense in subsequent years to depend on the size and composition of awards granted under our equity incentive plans.

General and administrative expense decreased by $0.2 million, or 10.4%, to $1.8 million for the three months ended September 30, 2012, from $2.0 million for the three months ended September 30, 2011. This decrease was due largely to reductions in real estate expense associated with the sublease agreement we entered into in 2011.

Nine Months Ended September 30, 2012 versus September 30, 2011

Total operating expense decreased by $1.0 million, or 3.6%, to $29.3 million for the nine months ended September 30, 2012, from $30.3 million for the nine months ended September 30, 2011. This decrease was primarily attributable to reductions in real estate expenses associated with the sublease of excess office space and lower compensation costs.

Compensation and benefits expense decreased by $0.5 million, or 2.1%, to $23.9 million for the nine months ended September 30, 2012, from $24.4 million for the nine months ended September 30, 2011. This decrease was primarily attributable to a decrease in other non-cash compensation related to annual equity-based awards to our employee members, and arose in part as a result of the amortization of previously issued awards partially offset by a shift in compensation mix. We expect non-cash compensation expense in subsequent years to depend on the size and composition of awards granted under our equity incentive plans.

General and administrative expense decreased by $0.6 million, or 9.9%, to $5.4 million for the nine months ended September 30, 2012, from $6.0 million for the nine months ended September 30, 2011. This decrease was due largely to reductions in real estate expense associated with the sublease agreement we entered into in 2011.

Other (Expense)

Three Months Ended September 30, 2012 versus September 30, 2011

Other (expense) was $1.2 million for the three months ended September 30, 2012, and consisted primarily of $1.7 million in expense related to adjustments to our liability to our selling and converting shareholders. This was partially offset by $0.4 million of net realized and unrealized gains from investments and $0.1 million in dividend and interest income. Other (expense) was an expense of $1.2 million for the three months ended September 30, 2011, and consisted primarily of $1.2 million of net realized and unrealized losses from investments. As discussed further below, the liability to our selling and converting shareholders represents 85% of the amount of cash savings, if any, in U.S. federal, state and local income tax that we realize as a result of the amortization of the increases in tax basis generated from our purchase of operating company units from our selling shareholders.

Nine Months Ended September 30, 2012 versus September 30, 2011

Other (expense) was $1.1 million for the nine months ended September 30, 2012, and consisted primarily of $2.3 million in expense related to adjustments to our liability to our selling and converting shareholders. This was partially offset by $1.1 million of net realized and unrealized gains from investments and $0.2 million in dividend and interest income. Other (expense) was $3.0 million for the nine months ended September 30, 2011, and consisted primarily of $2.3 million of expense related to adjustments to our liability to our selling and converting shareholders, $0.7 million of net realized and unrealized losses from investments and $0.2 million in other (expense), partially offset by approximately $0.2 million in dividend and interest income.

Income Tax Expense

Our results for the three and nine months ended September 30, 2012 and 2011 included the effects of adjustments related to our tax receivable agreement and the associated liability to selling and converting shareholders. Our effective corporate tax rate, exclusive of these adjustments, was 42.9% and 42.6%, respectively, for the three and nine months ended September 30, 2012. For each of the three and nine months ended September 30, 2011, our effective corporate tax rate, exclusive of these adjustments, was 42.9%. The change in the effective rate was due to one-time prior period adjustments recognized during the nine months ended September 30, 2012.

Non-GAAP income before corporate income taxes used to calculate our income before income taxes for the three and nine months ended September 30, 2012 and 2011 are as follows:

	For the Three Months Ended September 30, 2012	2011	For the Nine Months Ended September 30, 2012	2011
	(in thousands)			
Income Before Income Taxes	$ 8,169	$ 9,094	$ 26,640	$ 30,758
Change in Liability to Selling and Converting Shareholders	1,684	50	2,342	2,307
Unincorporated Business Taxes	(594)	(596)	(1,778)	(2,062)
Net Income Attributable to Non-Controlling Interests	(7,733)	(7,097)	(22,803)	(26,178)
Non-GAAP Income Before Income Taxes	$ 1,526	$ 1,451	$ 4,401	$ 4,825

Our non-GAAP effective corporate tax rate, which is exclusive of adjustments related to our tax receivable agreement and the associated liability to selling and converting shareholders, was determined as follows:

	For the Three Months Ended September 30, 2012 Tax (in thousands)	% of Non-GAAP Pre-tax Income	2011 Tax (in thousands)	% of Non-GAAP Pre-tax Income
Federal Corporate Tax	$ 519	34.0 %	$ 493	34.0 %
State and Local Taxes, Net of Federal Benefit	135	8.9 %	129	8.9 %
Non-GAAP Effective Taxes	$ 654	42.9 %	$ 622	42.9 %

	For the Nine Months Ended September 30, 2012 Tax (in thousands)	% of Non-GAAP Pre-tax Income	2011 Tax (in thousands)	% of Non-GAAP Pre-tax Income
Federal Corporate Tax	$ 1,496	34.0 %	$ 1,641	34.0 %
State and Local Taxes, Net of Federal Benefit	389	8.9 %	427	8.9 %
Prior Period Adjustments	(12)	(0.3)%	-	-
Non-GAAP Effective Taxes	$ 1,873	42.6 %	$ 2,068	42.9 %

Three Months Ended September 30, 2012 versus September 30, 2011

Income tax (benefit)/expense increased $2.3 million, from an income tax expense of $1.5 million for the three months ended September 30, 2011, to an income tax benefit of $0.8 million for the three months ended September 30, 2012. The income tax benefit for the three months ended September 30, 2012 included $2.1 million of benefit associated with adjustments to the valuation allowance recorded against our deferred tax asset related to our initial public offering and subsequent exchanges of operating company Class B units for shares of our Class A common stock. The income tax expense for the three months ended September 30, 2011 included $0.3 million of expense associated with such adjustments. Exclusive of these adjustments, the remaining income tax expense for three months ended September 30, 2012 consisted of $0.6 million in operating company unincorporated business taxes and $0.7 million of corporate income taxes. On a similar basis, the remaining income tax expense for the three months ended September 30, 2011 consisted of $0.6 million in both operating company unincorporated business taxes and corporate income taxes. A comparison of the GAAP effective tax rates for the three months ended September 30, 2012 and 2011 is not meaningful due to the valuation allowance adjustments.

Nine Months Ended September 30, 2012 versus September 30, 2011

Income tax expense decreased $0.6 million, from $1.6 million for the nine months ended September 30, 2011, to $1.0 million for the nine months ended September 30, 2012. The income tax expense for the nine months ended September 30, 2012 included $2.7 million of benefit associated with adjustments to the valuation allowance recorded against our deferred tax asset. The income tax expense for the nine months ended September 30, 2011 included $2.6 million of benefit associated with such adjustments. Exclusive of these adjustments, the remaining income tax expense for the nine months ended September 30, 2012 consisted of $1.8 million in operating company unincorporated business taxes and $1.9 million of corporate income taxes. On a similar basis, the remaining income tax expense for the nine months ended September 30, 2011 consisted of $2.1 million in both operating company unincorporated business taxes and corporate income taxes. The decrease in these taxes is attributable primarily to a decrease in taxable income. A comparison of the GAAP effective tax rates for the nine months ended September 30, 2012 and 2011 is not meaningful due to the valuation allowance adjustments.

Non-Controlling Interests

Three Months Ended September 30, 2012 versus September 30, 2011

Net income attributable to non-controlling interests was $7.7 million for the three months ended September 30, 2012, and consisted of $7.5 million associated with our employees' and outside investors' approximately 83.4% weighted average interest in the income of the operating company, and a $0.2 million gain related to outside interests of our consolidated investment partnerships. Net income attributable to non-controlling interests was $7.1 million for the three months ended September 30, 2011, and consisted of $7.8 million associated with our employees' and outside investors' approximately 84.5% weighted average interest in the income of the operating company, partially offset by a $0.7 million loss related to our consolidated investment partnerships. The change in net income attributable to non-controlling interests reflects improved results in our consolidated investment partnerships during the three months ended September, 30, 2012 compared to the year ago period. This increase was partially offset by the decrease in performance fees recognized during the three months ended September 30, 2012, which had a corresponding negative impact on operating company revenues and income, as well as the decrease in our employees' and outside investors' weighted average interest in the income of the operating company. The decrease in weighted average interest in the income of the operating company is due to the August 31, 2012 exchange of 722,521 of employees' and outside investors' Class B units for an equivalent number of shares of Class A common stock.

Nine Months Ended September 30, 2012 versus September 30, 2011

Net income attributable to non-controlling interests was $22.8 million for the nine months ended September 30, 2012, and consisted of $22.2 million associated with our employees' and outside investors' approximately 83.6% weighted-average interest in the income of the operating company, and a $0.6 million gain related to our consolidated investment partnerships. Net income attributable to non-controlling interests was $26.2 million for the nine months ended September 30, 2011, and consisted of our $26.8 million associated with our employees' and outside investors' approximately 84.9% weighted-average interest in the income of the operating company, partially offset by a $0.7 million loss related to our consolidated investment partnerships. The decrease in net income attributable to non-controlling interests reflects primarily the decrease in performance fees recognized during the nine months ended September 30, 2012, which had a corresponding negative impact on operating company revenues and income, as well as the decrease in our employees' and outside investors' weighted average interest in the income of the operating company. The decrease in weighted average interest in the income of the operating company is due to the August 31, 2012 exchange of 722,521 of employees' and outside investors' Class B units for an equivalent number of shares of Class A common stock.

Liquidity and Capital Resources

Historically, the working capital needs of our business have primarily been met through the cash generated by our operations. Distributions to members of our operating company have been our largest use of cash from financing activities. Investing activities have historically been investments in our own investment strategies, purchases and sales of investments to fund our deferred compensation program, and, to a lesser extent, capital expenditures.

At September 30, 2012, our cash and cash equivalents was $38.1 million, inclusive of $0.8 million in cash held by our consolidated subsidiaries. Advisory fees receivable was $14.6 million. We also had approximately $2.9 million in investments set aside to satisfy our obligations under our deferred compensation program.

We expect to fund the liquidity needs of our business in the next twelve months, and over the long-term, primarily through cash generated from operations. As an investment management firm, our business has been materially affected by conditions in the global financial markets and economic conditions throughout the world. Our liquidity is highly dependent on the revenue and income from our operations, which is directly related to our levels of AUM. For the three months ended September 30, 2012, our weighted average AUM increased by 3.5% and revenues decreased by 5.5%, compared to our weighted average AUM and revenues for the three months ended September 30, 2011. For the nine months ended September 30, 2012, our weighted average AUM and revenues decreased by 7.1% and 11.1%, respectively, compared to our weighted average AUM and revenues for the nine months ended September 30, 2011.

In determining the sufficiency of liquidity and capital resources to fund our business, we regularly monitor our liquidity position, including, among other things, cash, working capital, investments, long-term liabilities, lease commitments, debt obligations, and operating company distributions. Compensation is our largest expense. To the extent we deem necessary and appropriate to run our business, recognizing the need to retain our key personnel, we have the ability to change the absolute levels of our compensation packages, as well as change the mix of their cash and non-cash components. Historically, we have not tied our level of compensation directly to revenue, as many Wall Street firms do. Correspondingly, there is not a linear relationship between our compensation and the revenues we generate. This generally has the effect of increasing operating margins in periods of increased revenues, but can reduce operating margins when revenue declines.

We continuously evaluate our staffing requirements and compensation levels with reference to our own liquidity position and external peer benchmarking data. The result of this review directly influences management’s recommendations to our Board of Directors with respect to such staffing and compensation levels.

We anticipate that tax allocations and dividend equivalent payments to the members of our operating company, which consisted of our employees, certain unaffiliated persons, former employees, and us, will continue to be a material financing activity. Cash distributions to operating company members for partnership tax allocations would increase should the taxable income of the operating company increase. Dividend equivalent payments will depend on our dividend policy and the discretion of our Board of Directors, as discussed below.

We currently do not have any material need for cash in excess of that derived from our operations. Although we are comfortable with our current capital structure, in the current economic environment, it is uncertain whether additional or alternative sources of debt or equity financing would be available on acceptable terms, if required.

We do not anticipate meaningful outlays for internal investment or capital expenditures over the next twelve months.

We believe that our lack of long-term debt, and ability to vary cash compensation levels, have provided us with an appropriate degree of flexibility in providing for our liquidity needs.

Dividend Policy

We are a holding company and have no material assets other than our ownership of membership interests in our operating company. As a result, we depend upon distributions from our operating company to pay any dividends that our Board of Directors may declare to be paid to our Class A common stockholders. When, and if, our Board of Directors declares any such dividends, we then cause our operating company to make distributions to us in an amount sufficient to cover the dividends declared. Our dividend policy has certain risks and limitations, particularly with respect to liquidity. We may not pay dividends to our Class A common shareholders in amounts that have been paid to them in the past, or at all, if, among other things, we do not have the cash necessary to pay our intended dividends. To the extent we do not have cash on hand sufficient to pay dividends in the future, we may decide not to pay dividends. By paying cash dividends rather than investing that cash in our future growth, we risk slowing the pace of our growth, or not having a sufficient amount of cash to fund our operations or unanticipated capital expenditures, should the need arise.

On an annual basis, our Board of Directors has targeted a cash dividend payout ratio of approximately 70% to 80% of our non-GAAP net income, subject to growth initiatives and other funding needs. Our ability to pay dividends is subject to the Board of Directors' discretion and may be limited by our holding company structure and applicable provisions of Delaware law.

Tax Receivable Agreement

Our purchase of membership units of our operating company concurrent with our initial public offering, and the subsequent and future exchanges by holders of Class B units of our operating company for shares of our Class A common stock (pursuant to the exchange rights provided for in the operating company's operating agreement), has resulted in, and is expected to continue to result in, increases in our share of the tax basis of the tangible and intangible assets of our operating company at the time of our acquisition and these subsequent and future exchanges, which will increase the tax depreciation and amortization deductions that otherwise would not have been available to us. These increases in tax basis and tax depreciation and amortization deductions have reduced, and are expected to continue to reduce, the amount of cash taxes that we would otherwise be required to pay in the future. We have entered into a tax receivable agreement with the current members of our operating company, the one member of our operating company immediately prior to our initial public offering who sold all of its membership units to us in connection with our initial public offering, and any future holders of Class B units, that requires us to pay them 85% of the amount of cash savings, if any, in U.S. federal, state and local income tax that we actually realize (or are deemed to realize in the case of an early termination payment by us, or a change in control, as described in the tax receivable agreement) as a result of the increases in tax basis described above and certain other tax benefits related to entering into the tax receivable agreement, including tax benefits attributable to payments under the tax receivable agreement.

Cash Flows

Operating activities provided $11.8 million and $18.5 million in cash flows for the three months ended September 30, 2012 and 2011, respectively. The year-over-year decrease in cash flows from operating activities was driven primarily by changes in working capital, partially offset by an increase in net income, exclusive of the adjustments related to our tax receivable agreement and the associated liability to selling and converting shareholders.

Operating activities provided $33.2 and $44.5 million in cash flows for the nine months ended September 30, 2012 and 2011, respectively. The decrease in cash flows from operating activities was driven primarily by a decrease in net income and working capital, exclusive of the adjustments related to our tax receivable agreement and associated liability to our selling and converting shareholders.

Investing activities consist primarily of capital expenditures, mutual fund contributions to, and redemptions from, our deferred compensation program, and related party activity. For the three months ended September 30, 2012, investing activities used $0.1 million. For the three months ended September 30, 2011, investing activities used less than $0.1 million. Investing activities used approximately $0.1 million and $0.7 million in cash for the nine months ended September 30, 2012 and 2011, respectively. The decrease in cash used in investing activities was primarily due to a decrease of $0.9 million in purchases of investments in our deferred compensation plan and a decrease of $0.1 million in purchases of property and equipment, partially offset by a decrease of $0.3 million in proceeds from our deferred compensation plan.

Financing activities consist primarily of borrowing arrangements and contributions from, and distributions to, non-controlling interests, which represent tax allocations and dividend equivalents paid to the members of the operating company, as well as withdrawals made by our consolidated investment partnerships. Financing activities used $5.5 million for the three months ended September 30, 2012, and used $6.8 million for the three months ended September 30, 2011. The $1.3 million decrease in cash used in financing activities is primarily due to a decrease in tax allocations paid to the members of the operating company as a result of the decrease in taxable earnings of the operating company and a reduction of contributions from non-controlling interests, partially offset by the repurchase and retirement of Class A common stock and class B units during the three months ended September 30, 2012.

Financing activities used $30.1 million and $23.3 million, respectively, for the nine months ended September 30, 2012 and 2011. The $6.8 million increase in cash used in financing activities is primarily due to the timing of dividend and dividend equivalent payments made in March of 2012 and the repurchase and retirement of Class A Common stock and Class B units during the nine months ended September 30, 2012.

Our Board of Directors announced a share repurchase program in April of 2012 and authorized a repurchase of an aggregate of $10 million of our outstanding Class A common stock and Class B units of the operating company. The timing, number and value of common shares and units repurchased are subject to our discretion. In the three months ended September 30, 2012, we repurchased 24,666 shares of Class A common stock for $0.1 million at an average price per share of $5.15 and 3,131 Class B units for less than $0.1 million at an average price per share of $5.03. In the nine months ended September 30, 2012, we repurchased 53,120 shares of Class A common stock for $0.3 million at an average price per share of $4.74 and 3,131 Class B units less than $0.1 million at an average price per share of $5.03.

Off-Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of September 30, 2012.

Critical Accounting Policies and Estimates

The preparation of our consolidated financial statements in accordance with U.S. generally accepted accounting principles (GAAP), requires management to make estimates and judgments that affect our reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under current circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily available from other sources. We evaluate our estimates on an ongoing basis. Actual results may differ from these estimates under different assumptions or conditions.

Accounting policies are an integral part of our financial statements. A thorough understanding of these accounting policies is essential when reviewing our reported results of operations and our financial condition. Management believes that the critical accounting policies discussed below involve additional management judgment due to the sensitivity of the methods and assumptions used.

Consolidation

Our policy is to consolidate all majority-owned subsidiaries in which we have a controlling financial interest and variable-interest entities of which we are deemed to be the primary beneficiary. We also consolidate non-variable-interest entities which we control as the general partner or managing member. We assess our consolidation practices regularly, as circumstances dictate. All significant inter-company transactions and balances have been eliminated.

Investments in private investment partnerships in which we have a minority interest and exercise significant influence are accounted for using the equity method. Such investments, if any, are reflected on the consolidated statements of financial condition as investments in affiliates and are recorded at the amount of capital reported by the respective private investment partnerships. Such capital accounts reflect the contributions paid to, distributions received from, and the equity earnings of, the private investment partnerships.

Income Taxes

We are a “C” corporation under the Internal Revenue Code, and thus liable for federal, state and local taxes on the income derived from our economic interest in our operating company. The operating company is a limited liability company that has elected to be treated as a partnership for tax purposes. Our operating company has not made a provision for federal or state income taxes because it is the responsibility of each of the operating company’s members (including us) to separately report their proportionate share of the operating company’s taxable income or loss. Similarly, the income of our consolidated investment partnerships is not subject to income taxes, as such income is allocated to each partnership’s individual partners. The operating company has made a provision for New York City Unincorporated Business Tax (UBT).

We recognize deferred tax assets and liabilities for the future tax consequences attributable to differences between the carrying amounts of existing assets and liabilities and their respective tax bases, net operating loss carryforwards and tax credits. A valuation allowance is maintained for deferred tax assets that we estimate are more likely than not to go unrealizable based on available evidence at the time the estimate is made. Determining the valuation allowance requires management to make significant judgments and assumptions. In determining the valuation allowance, we use historical and forecasted future operating results, based upon approved business plans, including a review of the eligible carryforward periods, tax planning opportunities and other relevant considerations. Each quarter, we re-evaluate our estimate related to the valuation allowance, including our assumptions about future taxable income.

We believe that the accounting estimate related to the $60.3 million valuation allowance, recorded against the deferred tax asset associated with our acquisition of operating company membership units, is a critical accounting estimate because the underlying assumptions can change from period to period. For example, tax law changes, or variances in future projected operating performance, could result in a change in the valuation allowance. If we are not able to realize all or part of our net deferred tax assets in the future, an adjustment to our deferred tax asset valuation allowance would be charged to income tax expense in the period such determination was made.

Management judgment is required in determining our provision for income taxes, evaluating our tax positions and establishing deferred tax assets and liabilities. The calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax regulations. If our estimate of tax liabilities proves to be less than the ultimate assessment, a further charge to earnings would result.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Market Risk

Our exposure to market risk is directly related to our role as investment adviser for the institutional separate accounts we manage and the retail clients for which we act as sub-investment adviser. As noted in Item 1A, “Risk Factors,” of our Form 10-K for the year ended December 31, 2011, filed with the SEC on March 14, 2012, we experienced declines in AUM during the last three quarters of 2011, largely due to the volatility and disruption in the capital and credit markets. During this period, we experienced declines in revenue and profitability, and there can be no assurance that there will not be declines in our AUM, revenue and profitability should volatility and disruption in the capital and credit markets occur again in the future. A renewed economic downturn, and continued volatility in the global financial markets, could also significantly affect the estimates, judgments, and assumptions used in the valuation of our financial instruments.

Our revenue for the three months ended September 30, 2012 and 2011 was generally derived from advisory fees, which are typically based on the market value of our AUM, which can be affected by adverse changes in interest rates, foreign currency exchange and equity prices. Accordingly, a decline in the prices of securities would cause our revenue and income to decline, due to a decrease in the value of the assets we manage. In addition, such a decline could cause our clients to withdraw their funds in favor of investments offering higher returns or lower risk, which would cause our revenue and income to decline further.

We are also subject to market risk due to a decline in the value of the holdings of our consolidated subsidiaries, which consist primarily of marketable securities and investments in mutual funds. At September 30, 2012, the fair value of these assets was $2.2 million and $2.9 million, respectively. Assuming a 10% increase or decrease, the fair value would have increased or decreased by $0.2 million and $0.3 million, respectively, at September 30, 2012.

Interest Rate Risk

Since the Company does not have any debt that bears interest at a variable rate, it does not have any direct exposure to interest rate risk at September 30, 2012.

Item 4. Controls and Procedures.

During the course of their review of our consolidated financial statements as of September 30, 2012, our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of September 30, 2012, our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) were effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

There have not been any changes in our internal control over financial reporting during the three months ended September 30, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The table below sets forth information regarding purchases of our Class A Common Stock and Class B Units on a monthly basis during the three months ended September 30, 2012.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

Period	(a) Total Number of Shares of Class A Common Stock Purchased	(b) Average Price Paid per Share of Class A Common Stock	(c) Total Number of Shares Purchased of Publicly Announced Plans or Programs(1)	(d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (2) (in millions)
July 1, 2012 through July 31, 2012	-	$ -	-	$ 9.9
August 1, 2012 through August 31, 2012	4,010	4.98	4,010	9.9
September 1, 2012 through September 30, 2012	20,656	5.18	20,656	9.7
Total	24,666	$ 5.15	24,666	$ 9.7

(1) Our current share repurchase program was announced on April 24, 2012. The Board of Directors authorized us to repurchase an aggregate of $10 million of our outstanding Class A common stock and the operating company's Class B units on the open market and in private transactions in accordance with applicable securities laws. The timing, number and value of common sthares and units repurchased are subject to the Company's discretion. The Company's share repurchase program is not subject to an expiration date and may be suspended, discontinued, or modified at any time, for any reason.
(2) Total Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs also reflects the repurchase of 3,131 operating company's Class B units during August 2012 at an average price of $5.03 per share.

Item 6. Exhibits.

Exhibit	Description of Exhibit
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a)/15d-14(a)
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a)/15d-14(a)
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	

	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	Materials from the Pzena Investment Management, Inc. Quarterly Report on Form 10-Q for the quarter ended September 30, 2012, formatted in Extensible Business Reporting Language (XBRL): (i) Consolidated Statements of Financial Condition, (ii) Consolidated Statements of Operations, (iii) Consolidated Statement of Changes in Equity, (iv) Consolidated Statements of Cash Flows, and (vi) related Unaudited Notes to the Consolidated Financial Statements, tagged in detail (furnished herewith).

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: November 5, 2012

PZENA INVESTMENT MANAGEMENT, INC.

By:	/s/ RICHARD S. PZENA	
	Name:	Richard S. Pzena
	Title:	Chief Executive Officer
By:	/s/ GARY J. BACHMAN	
	Name:	Gary J. Bachman
	Title:	Chief Financial Officer (Principal Financial and Accounting Officer)