FIRST ALBANY COMPANIES INC
Form 10-Q
May 10, 2007

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

**FORM 10-Q**

[ X ] **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended March 31, 2007**

\- or -

[ ] **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from to**

Commission file number 014140

**F I R S T A L B A N Y C O M P A N I E S I N C.**

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **New York** | **22-2655804** |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| **677 Broadway, Albany, New York** | **12207** |
| (Address of principal executive offices) | (Zip Code) |
| **Registrant's telephone number, including area code** | **(518) 447-8500** |

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No ¨

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

Large Accelerated Filer ¨ Accelerated Filer þ Non-accelerated Filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No þ

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

16,372,817 shares of Common Stock were outstanding as of the close of business on April 30, 2007

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**FIRST ALBANY COMPANIES INC. AND SUBSIDIARIES**

FORM 10-Q

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FIRST ALBANY COMPANIES INC.
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(Unaudited)

## Part I – Financial Information

***Item 1. Financial Statements***

| *(In thousands of dollars)* As of | March 31 2007 | December 31 2006 |
|---|---|---|
| *Assets* | | |
| Cash | $ 3,977 | $ 4,192 |
| Cash and securities segregated for regulatory purposes | 6,700 | 5,200 |
| Securities purchased under agreement to resell | 15,910 | 14,083 |
| Receivables from: | | |
| Brokers, dealers and clearing agencies | 21,356 | 10,626 |
| Customers | 720 | 2,898 |
| Others | 6,777 | 6,933 |
| Securities owned | 276,852 | 276,167 |
| Investments | 12,322 | 12,250 |
| Office equipment and leasehold improvements, net | 4,195 | 4,516 |
| Intangible assets, including goodwill | 17,849 | 17,862 |
| Other assets | 3,755 | 2,391 |
| Total Assets | $ 370,413 | $ 357,118 |
| *Liabilities and Stockholders' Equity* | | |
| *Liabilities* | | |
| Short-term bank loans | $ 172,837 | $ 128,525 |
| Payables to: | | |
| Brokers, dealers and clearing agencies | 46,730 | 49,065 |
| Customers | 447 | 1,151 |
| Others | 10,146 | 8,996 |
| Securities sold, but not yet purchased | 51,395 | 52,120 |
| Accounts payable | 3,800 | 4,118 |
| Accrued compensation | 10,121 | 32,445 |
| Accrued expenses | 7,188 | 8,273 |
| Income taxes payable | - | 131 |
| Notes payable | 11,952 | 12,667 |
| Obligations under capitalized leases | 3,148 | 3,522 |
| Total Liabilities | 317,764 | 301,013 |
| *Commitments and Contingencies* | | |
| Temporary capital | 104 | 104 |
| Subordinated debt | 4,424 | 4,424 |
| *Stockholders' Equity* | | |
| Preferred stock; $1.00 par value; authorized 500,000 shares; none issued | | |
| Common stock; $.01 par value; authorized 50,000,000 shares; issued 17,669,641 and 17,613,827 respectively | 177 | 176 |

| | | |
|---|---|---|
| Additional paid-in capital | 154,249 | 152,573 |
| Deferred compensation | 2,694 | 2,647 |
| Accumulated deficit | (105,701) | (100,605) |
| Treasury stock, at cost (1,375,991 shares and 1,168,748 shares respectively) | (3,298) | (3,214) |
| Total Stockholders' Equity | 48,121 | 51,577 |
| Total Liabilities and Stockholders' Equity | $ 370,413 | $ 357,118 |

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

FIRST ALBANY COMPANIES INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three Months Ended March 31 | |
|---|---|---|
| *(In thousands of dollars except for per share amounts and shares outstanding)* | 2007 | 2006 |
| *Revenues:* | | |
| Commissions | $ 1,753 | $ 3,471 |
| Principal transactions | 10,278 | 17,366 |
| Investment banking | 7,590 | 11,725 |
| Investment gains (losses) | 239 | (6,143) |
| Interest | 3,242 | 3,042 |
| Fees and other | 455 | 619 |
| Total revenues | 23,557 | 30,080 |
| Interest expense | 3,755 | 4,232 |
| Net revenues | 19,802 | 25,848 |
| *Expenses (excluding interest):* | | |
| Compensation and benefits | 14,998 | 26,685 |
| Clearing, settlement and brokerage costs | 1,298 | 1,709 |
| Communications and data processing | 2,867 | 2,944 |
| Occupancy and depreciation | 2,049 | 2,804 |
| Selling | 1,218 | 1,813 |
| Other | 1,701 | 1,782 |
| Total expenses (excluding interest) | 24,131 | 37,737 |
| Loss before income taxes | (4,329) | (11,889) |
| Income tax benefit | - | - |
| Loss from continuing operations | (4,329) | (11,889) |
| Loss from discontinued operations, net of taxes (see “Discontinued Operations” note) | (133) | (756) |
| Loss before cumulative effect of change in accounting principle | (4,462) | (12,645) |
| Cumulative effect of accounting change, net of taxes (see “Benefit Plans” note) | - | 427 |
| Net loss | $ (4,462) | $ (12,218) |
| | | |
| Per share data: | | |
| Basic earnings: | | |
| Continuing operations | $ (0.28) | $ (0.77) |
| Discontinued operations | (0.01) | (0.05) |
| Cumulative effect of accounting change | - | 0.03 |
| Net loss per share | $ (0.29) | $ (0.79) |
| Diluted earnings: | | |
| Continuing operations | $ (0.28) | $ (0.77) |
| Discontinued operations | (0.01) | (0.05) |
| Cumulative effect of accounting change | - | 0.03 |
| Net loss per share | $ (0.29) | $ (0.79) |
| Weighted average common and common equivalent shares outstanding: | | |
| Basic | 15,505,922 | 15,377,662 |
| Dilutive | 15,505,922 | 15,377,662 |

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

FIRST ALBANY COMPANIES INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| *(In thousands of dollars)* | Three months Ended March 31 2007 | 2006 |
|---|---|---|
| *Cash flows from operating activities:* | | |
| Net loss | $ (4,462) | $ (12,218) |
| *Adjustments to reconcile net loss to net cash used in operating activities:* | | |
| Depreciation and amortization | 486 | 710 |
| Amortization of warrants | - | 498 |
| Deferred compensation | 82 | 214 |
| Unrealized investment (gains)/losses | (372) | 7,959 |
| Realized losses (gains) on sale of investments | 133 | (1,816) |
| Loss on sale of fixed assets, including termination of office lease | - | 81 |
| Services provided in exchange for common stock | 1,435 | 1,537 |
| *Changes in operating assets and liabilities:* | | |
| Cash and securities segregated for regulatory purposes | (1,500) | 2,000 |
| Securities purchased under agreement to resell | (1,827) | 1,787 |
| Net receivables from customers | 1,474 | 5,311 |
| Securities owned, net | (1,357) | 29,497 |
| Other assets | (1,364) | (982) |
| Net payable to brokers, dealers and clearing agencies | (13,065) | (47,671) |
| Net payables to others | (51) | (1,639) |
| Accounts payable and accrued expenses | (24,238) | (10,860) |
| Income taxes payable, net | (131) | - |
| Net cash used in operating activities | (44,757) | (25,592) |
| *Cash flows from investing activities:* | | |
| Purchases of office equipment and leasehold improvements | (152) | (2,190) |
| Purchases of investments | - | (928) |
| Proceeds from sale of investments | 62 | 3,368 |
| Net cash (used in) provided by investing activities | (90) | 250 |
| *Cash flows from financing activities*: | | |
| Proceeds of short-term bank loans, net | 44,312 | 30,665 |
| Proceeds of notes payable | - | 9,023 |
| Payments of notes payable | (715) | (10,822) |
| Payments of obligations under capitalized leases | (374) | (459) |
| Proceeds from subordinated debt | - | 159 |
| Proceeds from issuance of common stock under stock option plans | - | 55 |
| Net increase (decrease) in drafts payable | 1,409 | (3,281) |
| Net cash provided by financing activities | 44,632 | 25,340 |
| Decrease in cash | (215) | (2) |
| Cash at beginning of the period | 4,192 | 1,926 |
| Cash at the end of the period | $ 3,977 | $ 1,924 |

**Non-Cash Investing and Financing Activities**

During the first three months of 2007 and 2006, the Company entered into capital leases for office and computer equipment totaling approximately $0.0 million and $0.2 million, respectively.

During the first three months of 2007 and 2006, the Company converted $0.0 million and $0.2 million, respectively of accrued compensation to subordinated debt.

During the three months ended March 31, 2007 the company recorded a liability of $0.6 million related to the cumulative effect of adopting FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*. Refer to "Income Taxes" note for further details.

Refer to "Benefit Plans" note for non-cash financing activities related to restricted stock.
Refer to the "Investments" note for non-cash investing activities related to the Employee Investment Funds.

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

FIRST ALBANY COMPANIES INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

***1. Basis of Presentation***

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all normal, recurring adjustments necessary for a fair statement of results for such periods. The results for any interim period are not necessarily indicative of those for the full year. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes for the year ended December 31, 2006.

***2. Liquidity and Net Capital***

The Company has experienced recurring losses and as of March 31, 2007, the Company had cash of approximately $4.0 million and working capital of approximately $26 million. Continuing losses will impact the Company's liquidity and net capital. The Company believes that cash from operations and available credit lines will be sufficient to meet the Company's anticipated cash needs for working capital for the next 12 months. However, if the Company's estimates of revenues, expenses or capital or liquidity requirements change or are inaccurate, the Company may need to raise additional funds. The Company cannot be certain that it will be able to obtain additional financing on acceptable terms, or at all.

***3. Reclassifications***

Certain 2006 amounts on the Condensed Consolidated Statements of Operations have been reclassified to conform to the 2007 presentation. Expenses of $0.4 million related to investment banking business development were reclassified to Selling expense from Investment banking revenue. The reclassification results in investment banking revenue being recorded net of related unreimbursed expenses while unreimbursed expenses which have no related revenue are presented in selling expense.

***4. Earnings Per Common Share***

The Company calculates its basic and diluted earnings per shares in accordance with Statement of Financial Accounting Standards No. 128, *Earnings Per Share*. Basic earnings per share are computed based upon weighted-average shares outstanding. Dilutive earnings per share is computed consistently with basic while giving effect to all dilutive potential common shares that were outstanding during the period. The Company uses the treasury stock method to reflect the potential dilutive effect of unvested stock awards, warrants, unexercised options and any contingently issued shares (see "Temporary Capital" note). The weighted-average shares outstanding were calculated as follows:

| | Three Months Ended March 31 | |
|---|---|---|
| | 2007 | 2006 |
| Weighted average shares for basic earnings per share | 15,505,922 | 15,377,662 |
| Effect of dilutive common equivalent shares | - | - |
| Weighted average shares and dilutive common stock equivalents for dilutive earnings per share | 15,505,922 | 15,377,662 |

For the three months ended March 31, 2007 and 2006, the Company excluded approximately 0.3 million and 0.2 million common stock equivalents, respectively, in its computation of dilutive earnings per share because they were anti-dilutive. In addition, at March 31, 2007 and March 31, 2006, approximately 1.1 million and 1.3 million shares of restricted stock awards (see "Benefit Plans" note) which are included in shares outstanding are not included in the basic earnings per share computation because they are not vested as of March 31, 2007 and March 31, 2006, respectively.

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FIRST ALBANY COMPANIES INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

### *5. Receivables from and Payables to Brokers, Dealers and Clearing Agencies*

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

| *(In thousands of dollars)* | March 31 2007 | December 31 2006 |
|---|---|---|
| Adjustment to record securities owned on a trade date basis, net | $ 7,469 | $ - |
| Securities borrowed | - | 455 |
| Securities failed-to-deliver | 8,964 | 2,146 |
| Commissions receivable | 1,868 | 3,841 |
| Receivable from clearing organizations | 3,055 | 4,184 |
| Total receivables | $ 21,356 | $ 10,626 |
| Adjustment to record securities owned on a trade date basis, net | $ - | $ 2,173 |
| Payable to clearing organizations | 45,884 | 43,807 |
| Securities failed-to-receive | 846 | 3,085 |
| Total payables | $ 46,730 | $ 49,065 |

Proprietary securities transactions are recorded on trade date, as if they had settled. The related amounts receivable and payable for unsettled securities transactions are recorded net in receivables or payables to brokers, dealers and clearing agencies on the unaudited condensed consolidated statements of financial condition.

### *6. Receivables from and Payables to Customers*

At March 31, 2007, receivables from customers are mainly comprised of the purchase of securities by institutional clients. Delivery of these securities is made only when the Company is in receipt of the funds from the institutional clients.

The majority of the Company's non-institutional customers securities transactions, including those of officers, directors, employees and related individuals, are cleared through a third party under a clearing agreement. Under this agreement, the clearing agent executes and settles customer securities transactions, collects margin receivables related to these transactions, monitors the credit standing and required margin levels related to these customers and, pursuant to margin guidelines, requires the customer to deposit additional collateral with them or to reduce positions, if necessary. In the event the customer is unable to fulfill its contractual obligations, the clearing agent may purchase or sell the financial instrument underlying the contract, and as a result may incur a loss.

If the clearing agent incurs a loss, it has the right to pass the loss through to the Company which, as a result, exposes the Company to off-balance-sheet risk. The Company has retained the right to pursue collection or performance from customers who do not perform under their contractual obligations and monitors customer balances on a daily basis along with the credit standing of the clearing agent. As the potential amount of losses during the term of this contract has no maximum, the Company believes there is no maximum amount assignable to this indemnification. At March 31, 2007, substantially all customer obligations were fully collateralized and the Company has not recorded a liability related to the clearing agent's right to pass losses through to the Company.

FIRST ALBANY COMPANIES INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

### 7. *Securities Owned and Sold, but Not Yet Purchased*

Securities owned and sold, but not yet purchased consisted of the following at:

| | March 31, 2007 | | December 31, 2006 | |
|---|---|---|---|---|
| *(In thousands of dollars)* | Owned | Sold, but not yet Purchased | Owned | Sold, but not yet Purchased |
| *Marketable Securities* | | | | |
| U.S. Government and federal agency obligations | $ 80,018 | $ 48,153 | $ 90,652 | $ 51,393 |
| State and municipal bonds | 151,017 | 2,963 | 139,811 | 26 |
| Corporate obligations | 33,247 | 155 | 31,146 | 84 |
| Corporate stocks | 10,747 | 12 | 12,989 | 456 |
| Options | 172 | 112 | 258 | 161 |
| *Not Readily Marketable Securities* | | | | |
| Securities with no publicly quoted market | 1,116 | - | 1,008 | - |
| Securities subject to restrictions | 535 | - | 303 | - |
| Total | $ 276,852 | $ 51,395 | $ 276,167 | $ 52,120 |

Securities not readily marketable include investment securities (a) for which there is no market on a securities exchange or no independent publicly quoted market, (b) that cannot be publicly offered or sold unless registration has been effected under the Securities Act of 1933, or (c) that cannot be offered or sold because of other arrangements, restrictions or conditions applicable to the securities or to the Company.

### 8. *Intangible Assets, Including Goodwill*

| *(In thousands of dollars)* | March 31 2007 | December 31 2006 |
|---|---|---|
| Intangible assets | | |
| Customer related (amortizable): | | |
| Descap Securities, Inc. - Acquisition | $ 641 | $ 641 |
| Accumulated amortization | (156) | (143) |
| Institutional convertible bond arbitrage advisory group - Acquisition | 1,017 | 1,017 |
| Accumulated amortization | (382) | (382) |
| Impairment loss | (635) | (635) |
| | 485 | 498 |
| Goodwill (unamortizable): | | |
| Descap Securities, Inc. - Acquisition | 25,250 | 25,250 |
| Impairment loss | (7,886) | (7,886) |
| Institutional convertible bond arbitrage advisory group - Acquisition | 964 | 964 |
| Impairment loss | (964) | (964) |
| | 17,364 | 17,364 |
| Total Intangible Assets | $ 17,849 | $ 17,862 |

As a result of annual impairment testing, the goodwill related to the acquisition of Descap Securities, Inc. (“Descap”) was determined to be impaired as of December 31, 2006. Fair value of the Descap reporting unit was determined using both the income and market approaches. The income approach determines fair value using a discounted cash flow analysis based on management’s projections. The market approach analyzes and compares the operations performance and financial conditions of the reporting unit with those of a group of selected publicly-traded companies that can be used for comparison. The valuation gives equal weight to the two approaches to arrive at the fair value of the reporting unit. As a result of the valuation, as of December 31, 2006, the carrying value of goodwill was greater than the implied value of goodwill resulting in a goodwill impairment loss of $7.9 million recognized in the caption “Impairment” on the Statements of Operations for the year ended December 31, 2006.

FIRST ALBANY COMPANIES INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

A plan approved by the Board of Directors on September 28, 2006 to discontinue operations of the Institutional Convertible Bond Arbitrage Advisory Group (the "Group") triggered an impairment test in the third quarter of 2006 in accordance with SFAS No. 142 *Goodwill and Other Intangible Assets.* Fair value of the Group was determined using the income approach. The income approach determines fair value using a discounted cash flow analysis based on management's projections. Based on the impairment test, a goodwill impairment loss of $1.0 was recognized in discontinued operations for the year ended December 31, 2006. As a result of impairment testing of the disposal group in accordance with SFAS No. 144 *Accounting for the Impairment or Disposal of Long-Lived Assets*, it was determined that amortizable customer related intangibles were also impaired. An impairment loss of $0.6 million was recognized related to amortizable intangible assets in discontinued operations for the year ended December 31, 2006. The group ceased operations in April 2007.

Customer related intangible assets are being amortized over 12 years. Future amortization expense is estimated as follows:

| *(In thousands of dollars)* | | |
|---|---|---|
| 2007 (remaining) | $ | 40 |
| 2008 | | 53 |
| 2009 | | 53 |
| 2010 | | 53 |
| 2011 | | 53 |
| 2012 | | 53 |
| Thereafter | | 180 |
| Total | $ | 485 |

***9. Investments***

The Company's investment portfolio includes interests in privately held companies. Information regarding these investments has been aggregated and is presented below.

| *(In thousands of dollars)* | | March 31 2007 | | December 31 2006 |
|---|---|---|---|---|
| Carrying Value | | | | |
| Private | $ | 10,918 | $ | 10,866 |
| Consolidation of Employee Investment Funds, net of Company's ownership interest | | 1,404 | | 1,384 |
| Total carrying value | $ | 12,322 | $ | 12,250 |

Investment gains (losses) were comprised of the following:

| | Three Months Ended March 31 | | | |
|---|---|---|---|---|
| *(In thousands of dollars)* | | 2007 | | 2006 |
| Public (net realized and unrealized gains and losses) | $ | - | $ | (6,030) |
| Private (net realized gains and losses) | | (133) | | 83 |
| Private (net unrealized gains and losses) | | 372 | | (196) |

| | | |
|---|---|---|
| Investment gains (losses) | $ 239 | $ (6,143) |

The Company's public investments as of March 31, 2006 consisted of investments in iRobot ("IRBT") and Mechanical Technology Incorporated ("MKTY"). Both investments were completely liquidated during the year ended December 31, 2006.

FIRST ALBANY COMPANIES INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Privately held investments include an investment of $10.3 million in FA Technology Ventures L.P. (the "Partnership"), which represented the Company's maximum exposure to loss in the Partnership at March 31, 2007. The Partnership's primary purpose is to provide investment returns consistent with the risk of investing in venture capital. At March 31, 2007 total Partnership capital for all investors in the Partnership equaled $40.6 million. The Partnership is considered a variable interest entity. The Company is not the primary beneficiary, due to other investors' level of investment in the Partnership. Accordingly, the Company has not consolidated the Partnership in these financial statements, but has only recorded the value of its investment. FA Technology Ventures Inc. ("FATV"), a wholly-owned subsidiary, is the investment advisor for the Partnership. Revenues derived from the management of this investment and the Employee Investment Funds for the three-month period ended March 31, 2007 and 2006 were $0.3 million and $0.4 million in consolidation, respectively.

The Company has consolidated its Employee Investment Funds (EIF). The EIF are limited liability companies, established by the Company for the purpose of having select employees invest in private equity securities. The EIF is managed by FAC Management Corp., a wholly-owned subsidiary, which has contracted with FATV to act as an investment advisor with respect to funds invested in parallel with the Partnership. The Company's carrying value of this EIF is $0.3 million excluding the effects of consolidation. The Company has outstanding loans of $0.3 million from the EIF and is also committed to loan an additional $0.2 million to the EIF. The effect of consolidation was to increase Investments by $1.4. million, decrease Receivable from Others by $0.3 million and increase Payable to Others by $1.1 million. The amounts in Payable to Others relates to the value of the EIF owned by employees.

***10. Payables to Others***

Amounts payable to others consisted of the following at:

| *(In thousands of dollars)* | March 31 2007 | December 31 2006 |
|---|---|---|
| Drafts payable | $ 7,351 | $ 5,942 |
| Payable to Employees for the Employee Investment Funds (see "Investments" footnote) | 1,058 | 1,039 |
| Payable to Sellers of Descap Securities, Inc. (see "Commitments and Contingencies" footnote) | 1,036 | 1,036 |
| Others | 701 | 979 |
| Total | $ 10,146 | $ 8,996 |

The Company maintains a group of "zero-balance" bank accounts which are included in payables to others on the Statements of Financial Condition. Drafts payable represent the balances in these accounts related to outstanding checks that have not yet been presented for payment at the bank. The Company has sufficient funds on deposit to clear these checks, and these funds will be transferred to the "zero-balance" accounts upon presentment. The Company maintains one "zero-balance" account which is used as a cash management technique, permitted under Rule 15c3-3 of the Securities and Exchange Commission, to obtain federal funds for a fee, which is lower than prevailing interest rates, in amounts equivalent to amounts in customers' segregated funds accounts with a bank.

***11. Short-Term Bank Loans and Notes Payables***

Short-term bank loans are made under a variety of bank lines of credit totaling $210 million of which approximately $173 million is outstanding at March 31, 2007. These bank lines of credit consist of credit lines that the Company has been advised are available solely for financing securities inventory but for which no contractual lending obligation exist and are repayable on demand. These loans are collateralized by eligible securities, including Company-owned securities, subject to certain regulatory formulas. Typically, these lines of credit will allow the Company to borrow up to 85% to 90% of the market value of the collateral. These loans bear interest at variable rates based primarily on the Federal Funds interest rate. The weighted average interest rates on these loans were 5.78% and 5.74% at March 31, 2007 and December 31, 2006, respectively. At March 31, 2007, short-term bank loans were collateralized by Company-owned securities, which are classified as securities owned, of $191 million.

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FIRST ALBANY COMPANIES INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The Company's notes payable include a $12.0 million Term Loan to finance the acquisition of Descap. Interest rate is 2.40% over the 30-day London InterBank Offered Rate ("LIBOR") (5.32% at March 31, 2007). Interest only was payable for the first six months, and thereafter monthly payments of $238 thousand in principal and interest over the life of the loan which matures on May 14, 2011. The Term Loan agreement contains various covenants, as defined in the agreement. The Agreement requires that the Company's modified total funded debt to EBITDAR not to exceed 1.75 to 1 (for the twelve-month period ending March 31, 2007, modified total funded indebtedness EBITDAR ratio was 0.52 to 1). In addition, the modified Term Loan agreement requires operating cash flow to total fixed charges (as defined) to be not less than 1.15 to 1 (for the twelve-month period ending March 31, 2007, the operating cash flow to total fixed charge ratio was 2.08 to 1). EBITDAR is defined as earnings before interest, taxes, depreciation, amortization and lease expense plus pro forma adjustments. The definition of operating cash flow includes the payment of cash dividends; therefore, the Company's ability to pay cash dividends in the future may be impacted by the covenant.

Principal payments for the Term Loan are due as follows:

| *(In thousands of dollars)* | | |
|---|---|---|
| 2007 (remaining) | $ | 2,142 |
| 2008 | | 2,857 |
| 2009 | | 2,857 |
| 2010 | | 2,857 |
| 2011 | | 1,239 |
| Total principal payments remaining | $ | 11,952 |

***12. Obligations Under Capitalized Leases***

The following is a schedule of future minimum lease payments under capital leases for office equipment together with the present value of the net minimum lease payments at March 31, 2007:

| *(In thousands of dollars)* | | |
|---|---|---|
| 2007 (remaining) | $ | 1,165 |
| 2008 | | 999 |
| 2009 | | 676 |
| 2010 | | 460 |
| 2011 | | 213 |
| 2012 | | 11 |
| Total minimum lease payments | | 3,524 |
| Less: amount representing interest | | 376 |
| Present value of minimum lease payments | $ | 3,148 |

***13. Commitments and Contingencies***

Commitments: As of March 31, 2007, the Company had a commitment to invest up to an additional $3.8 million in FA Technology Ventures, LP (the "Partnership"). The investment period expired in July 2006, however, the General Partner may continue to make capital calls up through July 2011 for additional investments in portfolio companies and for the payment of management fees. The Company intends to fund this commitment from operating cash flow. The

Partnership's primary purpose is to provide investment returns consistent with risks of investing in venture capital. In addition to the Company, certain other limited partners of the Partnership are officers or directors of the Company. The majority of the commitments to the Partnership are from non-affiliates of the Company.

FIRST ALBANY COMPANIES INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The General Partner for the Partnership is FATV GP LLC. The General Partner is responsible for the management of the Partnership, including among other things, making investments for the Partnership. The members of the General Partnership are George McNamee, Chairman of the Company, First Albany Enterprise Funding, Inc., a wholly owned subsidiary of the Company, and other employees of the Company or its subsidiaries. Mr. McNamee is required under the Partnership agreement to devote a majority of his business time to the conduct of the affairs of the Partnership and any parallel funds. Subject to the terms of the Partnership agreement, under certain conditions, the General Partnership is entitled to share in the gains received by the Partnership in respect of its investment in a portfolio company. The General Partner will receive a carried interest on customary terms. The General Partner has contracted with FATV to act as investment advisor to the General Partner.

As of March 31, 2007, the Company had an additional commitment to invest up to $0.3 million in funds that invest in parallel with the Partnership, which it intends to fund, at least in part, through current and future Employee Investment Funds (EIF). The investment period expired in July 2006, but the General Partner may continue to make capital calls up through July 2011 for additional investments in portfolio companies and for the payment of management fees. The Company anticipates that the portion of the commitment that is not funded by employees through the EIF will be funded by the Company through operating cash flow.

Contingent Consideration: On May 14, 2004, the Company acquired 100 percent of the outstanding common shares of Descap, a New York-based broker-dealer and investment bank. Per the acquisition agreement, the Sellers can receive future contingent consideration (“Earnout Payment”) based on the following: for each of the years ending May 31, 2006 and May 31, 2007, if Descap’s Pre-Tax Net Income (as defined) (i) is greater than $10 million, the Company shall pay to the Sellers an aggregate amount equal to fifty percent (50%) of Descap’s Pre-Tax Net Income for such period, or (ii) is equal to or less than $10 million, the Company shall pay to the Sellers an aggregate amount equal to forty percent (40%) of Descap’s Pre-Tax Net Income for such period. Each Earnout Payment shall be paid in cash, provided that Buyer shall have the right to pay up to seventy-five percent (75%) of each Earnout Payment in the form of shares of Company Stock. The amount of any Earnout Payment that the Company elects to pay in the form of Company Stock shall not exceed $3.0 million for any Earnout Period and in no event shall such amounts exceed $6.0 million in the aggregate for all Earnout Payments. Based upon Descap’s Pre-Tax Net Income from June 1, 2005 through May 31, 2006, $1.0 million of contingent consideration has been accrued at March 31, 2007. Also, based upon Descap’s pre-tax net income from June 1, 2006 to March 31, 2007, no contingent consideration would be payable to the Sellers.

Leases: The Company's headquarters and sales offices, and certain office and communication equipment, are leased under non-cancelable operating leases, certain of which contain renewal options and escalation clauses, and which expire at various times through 2015. To the extent the Company is provided tenant improvement allowances funded by the lessor, they are amortized over the initial lease period and serve to reduce rent expense. To the extent the Company is provided free rent periods, the Company recognizes the rent expense over the entire lease term on a straightline basis.

Future minimum annual lease payments, and sublease rental income, are as follows:

| *(In thousands of dollars)* | Future Minimum Lease | Sublease Rental Income | Net Lease Payments |
|---|---|---|---|

| | Payments | | |
|---|---|---|---|
| 2007 (remaining) | $ 5,604 | $ 769 | $ 4,835 |
| 2008 | 6,175 | 809 | 5,366 |
| 2009 | 2,829 | 100 | 2,729 |
| 2010 | 2,517 | 100 | 2,417 |
| 2011 | 2,439 | 100 | 2,339 |
| 2012 | 2,417 | 100 | 2,317 |
| Thereafter | 4,376 | 91 | 4,285 |
| Total | $ 26,357 | $ 2,069 | $ 24,288 |

Litigation: In 1998, the Company was named in lawsuits by Lawrence Group, Inc. and certain related entities (the "Lawrence Parties") in connection with a private sale of Mechanical Technology Inc. stock from the Lawrence Parties that was previously approved by the United States Bankruptcy Court for the Northern District of New York (the "Bankruptcy Court"). The Company acted as placement agent in that sale, and a number of employees and officers of the Company, who have also been named as defendants, purchased shares in the sale. The complaints alleged that the defendants did not disclose certain information to the sellers and that the price approved by the court was therefore not proper. The cases were initially filed in the Bankruptcy Court and the United States District Court for the Northern District of New York (the "District Court"), and were subsequently consolidated in the District Court. The District Court dismissed the cases, and that decision was subsequently vacated by the United States Court of Appeals for the Second Circuit, which remanded the cases for consideration of the plaintiffs' claims as motions to modify the Bankruptcy Court sale order. The plaintiffs' claims have now been referred back to the Bankruptcy Court for such consideration. Discovery is currently underway. The Company believes that it has strong defenses to and intends to vigorously defend itself against the plaintiffs' claims, and believes that the claims lack merit. However, an unfavorable resolution could have a material adverse effect on the Company's financial position, results of operations and cash flows in the period resolved.

The Company's wholly owned subsidiary Descap acted as the seller in a series of purchases by a large institutional customer of collateralized mortgage securities (the "Bonds") from April through June 2006. In these transactions, Descap acted as "riskless principal," insofar as it purchased the Bonds from a third party and immediately resold them to the customer. The customer who purchased the Bonds has claimed that Descap misled the customer through misrepresentations and omissions concerning certain fundamental elements of the Bonds and that the customer would not have purchased the Bonds had it not been misled by Descap. By letter of September 14, 2006, the customer claimed that the Company and Descap are liable to the customer for damages in an amount in excess of $21 million and has threatened litigation if the dispute is not resolved. The Company and Descap have denied that Descap is responsible for the customer's damages and intend to defend vigorously any litigation that the customer may commence. The Company and Descap have held discussions with the customer in an attempt to resolve the dispute. In addition, Descap has taken steps that the Company and Descap believe have mitigated substantially any losses that the customer may have suffered as a result of its purchase of the Bonds. No legal proceedings have been brought to date. The outcome of this dispute is highly uncertain, however, and an unfavorable resolution could have a material adverse effect on the Company's financial position, results of operations and cash flows in the period resolved.

In the normal course of business, the Company has been named a defendant, or otherwise has possible exposure, in several claims. Certain of these are class actions, which seek unspecified damages that could be substantial. Although there can be no assurance as to the eventual outcome of litigation in which the Company has been named as a defendant or otherwise has possible exposure, the Company has provided for those actions most likely to have an adverse disposition. Although further losses are possible, the opinion of management, based upon the advice of its attorneys, is that such litigation will not, in the aggregate, have a material adverse effect on the Company's liquidity, financial position or cash flow, although it could have a material