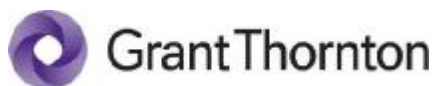


**Robert W. Baird & Co. Incorporated**

**Statement of Financial Condition**

**As of December 31, 2008**

**Together with Reports of Independent Certified Public Accountant**



**Report of Independent Certified Public Accountants**

To the Board of Directors of  
Robert W. Baird & Co. Incorporated:

We have audited the accompanying statement of financial condition of Robert W. Baird & Co. Incorporated (the "Company"), a Wisconsin corporation and a majority-owned subsidiary of Baird Financial Corporation as of December 31, 2008. This financial statement is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America as established by the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statement referred to above presents fairly, in all material respects, the financial position of Robert W. Baird & Co. Incorporated as of December 31, 2008 in conformity with accounting principles generally accepted in the United States of America.

*Grant Thornton LLP*

Milwaukee, Wisconsin  
February 26, 2009

**Robert W. Baird & Co. Incorporated**  
Statement of Financial Condition  
As of December 31, 2008

(In Thousands)

<u>Assets</u>	
Cash and Cash Equivalents	\$ 59,548
Securities Purchased Under Agreements to Resell	9,464
Deposits with Clearing Corporations	9,808
Receivables:	
Clients	255,445
Brokers and Dealers	5,197
Deposits Paid on Securities Borrowed	5,923
Other	170,056
	<u>436,621</u>
Securities Owned, at Fair Value	432,040
Furniture, Equipment and Leasehold Improvements, at Cost, Less Accumulated Depreciation and Amortization of \$91,042	31,444
Goodwill and Intangible Assets, at Cost, Less Accumulated Amortization of \$5,840	42,021
Other Assets, Including \$32,639 Net Deferred Tax Asset	<u>59,527</u>
Total Assets	<u>\$ 1,080,473</u>

The accompanying notes are an integral part of this financial statement.

**Robert W. Baird & Co. Incorporated**

Statement of Financial Condition  
As of December 31, 2008

(In Thousands)

(Continued)

Liabilities and Stockholders' Equity

Liabilities:

Money Borrowed:

Book Credit Balances in Bank Accounts	\$	26,224
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Payables:

Clients		106,940
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Brokers and Dealers		38,545
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Deposits Received on Securities Loaned		7,466
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		152,951
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Securities Sold, Not Yet Purchased, at Fair Value		25,247
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Accounts Payable, Accrued Expenses and Other Liabilities		264,081
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Subordinated Liabilities		274,913
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Total Liabilities		743,416
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Stockholders' Equity:

Common Stock		26,251
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Additional Paid-In Capital		117,748
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Restricted Stock Units		2,334
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Retained Earnings		189,988
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Treasury Stock, at Cost		(969)
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Accumulated Other Comprehensive Income		1,705
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Total Stockholders' Equity		337,057
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Total Liabilities and Stockholders' Equity		\$ 1,080,473
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The accompanying notes are an integral part of this financial statement.



**Robert W. Baird & Co. Incorporated**

Notes to Statement of Financial Condition  
December 31, 2008

(In Thousands, Except Share and Per Share Amounts)

(1) Summary of Significant Accounting Policies

Robert W. Baird & Co. Incorporated (the “Company”) is a registered broker dealer and an investment advisor with the Securities and Exchange Commission (“SEC”) under the Securities Exchange Act of 1934 and the Investment Advisors Act of 1940, and is also a member of various exchanges and the Financial Industry Regulatory Authority (“FINRA”). The Company owns a 48% ownership interest in Baird UK Ltd., the parent company of an affiliated broker and dealer in securities located principally in London, England. The Company engages in a broad range of activities in the securities brokerage, investment banking and asset management businesses, including private wealth management brokerage transactions; institutional equity and fixed income sales; research services; origination of and participation in underwritings and distribution of corporate and municipal securities issuances; merger and acquisition transactions; private equity and venture capital investing; market making and trading activities in corporate and municipal securities, government and governmental agency bonds; equity, balanced and fixed income investment advisory and asset management services; mutual fund distribution; and option transactions. The Company is a majority-owned subsidiary of Baird Financial Corporation (“BFC”), which is a majority-owned subsidiary of Baird Holding Company (“BHC” or the “Parent”).

The following is a summary of the significant accounting policies followed by the Company in the preparation of its financial statement:

(a) Cash and Cash Equivalents

Cash equivalents are defined as short-term investments with maturities generally of three months or less at time of purchase.

(b) Securities Purchased Under Agreements to Resell and Securities Sold Under Agreements to Repurchase

The Company invests in short-term securities purchased under agreements to resell (“reverse repurchase agreements”). Additionally, the Company enters into securities sold under agreements to repurchase (“repurchase agreements”). Both reverse repurchase and repurchase agreements are accounted for as collateralized financings and are carried at contractual amounts. It is the Company’s policy to obtain possession of collateral with a market value equal to or in excess of the principal amount loaned under the reverse repurchase agreements. To ensure the market value of the underlying collateral remains



sufficient, the collateral is valued daily, and the Company may require counterparties to deposit additional collateral (or may return collateral to counterparties) when necessary.

(c) Receivables

Receivables - clients include amounts receivable on cash and margin transactions. The receivables are reported at their outstanding principal balance, adjusted for any allowance for doubtful accounts.

Receivables - other primarily includes affiliate amounts as more fully discussed in Footnote 2 and loans to associates for recruiting purposes.

(d) Securities Transactions

Securities transactions are recorded on settlement date, which is not materially different from trade date.

In the normal course of business, the Company, similar to other firms in the securities industry, purchases and sells securities as both principal and agent. If the other party to the transaction fails to perform as agreed, the Company may incur a loss if the market value of the security is different from the contract amount of the transaction.

The Company's policy is to continually monitor its market exposure and counterparty risk. In addition, the Company has a policy of reviewing, as considered necessary, the credit standing of each counterparty and client with which it conducts business.

Securities Owned and Securities Sold, Not Yet Purchased are recognized on a trade date basis.

(e) Fair Value Measurements

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 157, "*Fair Value Measurements*". SFAS No. 157 defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the inputs used to measure fair value and enhances disclosure requirements for fair value measurements. SFAS No. 157 maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs be used when available.

Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect assumptions that market participants would use in pricing the asset or liability based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the transparency of inputs as follows:



Level I — Quoted prices are available in active markets for identical assets or liabilities as of the report date. A quoted price for an identical asset or liability in an active market provides the most reliable fair value measurement because it is directly observable to the market.

Level II — Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the report date. The nature of these securities include investments for which quoted prices are available but traded less frequently and investments that are fair valued using other securities, the parameters of which can be directly observed.

Level III — Securities that have little to no pricing observability as of the report date. These securities are measured using management's best estimate of fair value, where the inputs into the determination of fair value are not observable and require significant management judgment or estimation.

See Footnote 6 for further information.

(f) Valuation of Securities

When available, the Company values securities at observable market prices, observable market parameters, or broker or dealer prices (bid and ask prices). In the case of securities transacted on recognized exchanges, the observable market prices represent quotations for completed transactions from the exchange on which the financial instrument is principally traded.

For investments in illiquid or privately held securities that do not have readily determinable fair values, the determination of fair value requires the Company to estimate the value of the securities using the best information available. Among the factors that may be considered by the Company in determining the fair value of such securities are the cost, terms and liquidity of the investment, the financial condition and operating results of the issuer, the quoted market price of publicly traded securities with similar quality and yield, and other factors generally pertinent to the valuation of investments. In instances where a security is subject to transfer restrictions, the value of the security is based primarily on the quoted price of a similar security without restriction but may be reduced by an amount estimated to reflect such restrictions. In addition, even where the value of a security is derived from an independent source, certain assumptions may be required to determine the security's fair value. The actual value realized upon disposition could be different from the currently estimated fair value.

(g) Securities Lending Activities

Securities borrowed and securities loaned are recorded at the amount of cash collateral advanced or received. Securities borrowed transactions require the Company to deposit cash, letters of credit or other collateral with the lender. With respect to securities loaned, the



Company receives collateral in the form of cash in an amount in excess of the market value of securities loaned. The Company monitors the market value of securities borrowed and loaned on a daily basis. Additional collateral is obtained or refunded as necessary.

(h) Derivative Financial Instruments

The Company has limited involvement with derivative financial instruments. The Company enters into forward, option and future transactions as more fully discussed in Footnote 17.

(i) Income Taxes

Certain income and expense items are accounted for in different periods for financial reporting purposes than for income tax purposes. Appropriate provisions are made in the Company's financial statement for deferred income taxes in recognition of these temporary differences.

The Company is under continuous examination by various tax authorities in jurisdictions in which the Company has significant business operations. The Company regularly evaluates the likelihood of additional assessments in each of the tax jurisdictions resulting from these examinations.

(j) Furniture, Equipment and Leasehold Improvements

Furniture, equipment and leasehold improvements are stated at cost less accumulated depreciation. Depreciation is provided using the straight-line method over the estimated useful lives of the assets, which range from three years for software and computer equipment to seven years for furniture and other equipment.

Additions, improvements and expenditures for repairs and maintenance that significantly extend the useful life of an asset are capitalized, as more fully disclosed in Footnote 3. Other expenditures for repairs and maintenance are charged to expense in the period incurred.

(k) Goodwill and Intangible Assets

Goodwill and intangible assets with indefinite lives are not amortized but are reviewed at least annually for impairment. Intangibles with finite lives are amortized on a straight-line basis over their respective lives as more fully disclosed in Footnote 4.

(l) Stock-Based Compensation

The Company has an incentive stock option and a restricted stock plan which provide for the issuance of Company common stock. The Company accounts for such stock and stock options under SFAS No. 123(R), "Accounting for Stock-Based Compensation."

(m) Estimates

The preparation of the financial statement in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statement. Actual results may differ from those estimates.

(n) Foreign Currency Translation

In accordance with SFAS No. 52, "*Foreign Currency Translation*," assets and liabilities of the Company's foreign investment are translated at the current exchange rate. Net exchange gains or losses resulting from the translation of foreign financial statements are credited or charged directly to a separate component of Stockholders' Equity titled "Accumulated Other Comprehensive Income."

(o) Reclassification

Certain prior year amounts have been reclassified to conform to the current year presentation.

(p) New Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board issued SFAS No. 160, "*Noncontrolling Interest in Consolidated Financial Statements*" ("SFAS No. 160"). SFAS No. 160 requires noncontrolling interests to be treated as a separate component of equity, not as a liability or other item outside of permanent equity. This statement is applicable to the accounting for noncontrolling interests and transactions with noncontrolling interest holders in consolidated financial statements and is effective for the Company in 2009. The Company is currently evaluating the impact the adoption of SFAS No. 160 will have on its financial statement.

In December 2008, the FASB issued FASB Staff Position (FSP) FIN 48-3, "*Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises*." FSP FIN 48-3 permits an entity within its scope to defer the effective date of FASB Interpretation 48 ("Interpretation 48"), "*Accounting for Uncertainty in Income Taxes*," to its annual financial statements for fiscal years beginning after December 15, 2008. The Company has elected to defer the application of Interpretation 48 for the year ending December 31, 2008. The Company evaluates its uncertain tax positions using the provisions of SFAS No. 5, "*Accounting for Contingencies*." Accordingly, a loss contingency is recognized when it is probable that a liability has been incurred as of the date of the financial statements and the amount of the loss can be reasonably estimated. The amount recognized is subject to estimate and management judgment with respect to the likely outcome of each uncertain tax position. The amount that is ultimately sustained for an individual uncertain tax position or for all uncertain tax positions in the aggregate could differ from the amount recognized.

(2) Related-Party Transactions

Included on the Statement of Financial Condition is \$81,940 as of December 31, 2008 of receivables from affiliates included in Receivables Other and \$47,635 as of December 31, 2008 of payables to affiliates included in Accounts Payable, Accrued Expenses and Other Liabilities.

(3) Furniture, Equipment, and Leasehold Improvements

Furniture, Equipment, and Leasehold Improvements as of December 31, 2008 consist of the following:

Furniture and Fixtures	\$ 25,956
Equipment	31,910
Software	20,119
Leasehold Improvements	40,735
Capital Leases	3,766
	<u>122,486</u>
Less Accumulated Depreciation	<u>(91,042)</u>
Furniture, Equipment and Leasehold Improvements, Net	<u>\$ 31,444</u>

(4) Goodwill and Intangible Assets

At December 31, 2008 goodwill and intangible assets consist of the following:

Goodwill	\$ 27,400
Amortizing Intangibles	4,792
Indefinite Life Intangibles	9,829
	<u>\$ 42,021</u>

(5) Money Borrowed(a) Bank Loans

The Company has a committed unsecured credit facility. In addition, it also has several uncommitted unsecured lines of credit with various banks payable on demand. The aggregate lines of credit available were \$210,000 at December 31, 2008. The Company has no



amounts outstanding under its lines of credit at December 31, 2008. Lending under the uncommitted unsecured facilities is subject to the discretion of the bank involved.

(b) Book Credit Balances in Bank Accounts

The Company has \$26,224 in credit balances at certain banks with which it does business at December 31, 2008. The Company does not have a right of offset regarding these balances and, as a result, they are classified as money borrowed on the Statement of Financial Condition.

(6) Fair Value of Financial Instruments

The following table summarizes Securities Owned and Securities Sold, Not Yet Purchased by SFAS No. 157 levels as of December 31, 2008:

	Securities Owned	Securities Sold, Not Yet Purchased
Level I	\$ 25,945	\$ 18,033
Level II	391,475	7,214
Level III	14,620	-
	<u>\$ 432,040</u>	<u>\$ 25,247</u>

Level I generally includes equities, mutual funds, and US government securities. Level II generally includes corporate bonds, municipal bonds, and government agency mortgage backed bonds. Level III includes primarily investments in nonpublic companies and private equity partnerships.

The following table summarizes the change in fair values associated with SFAS No. 157 level III assets:

Balance as of December 31, 2007	\$ 28,612
Purchases and (Sales), net	(22,713)
Realized Gains	6,307
Unrealized Gains	2,414
Balance as of December 31, 2008	<u>\$ 14,620</u>

Net unrealized gains relate to those securities held by the Company at December 31, 2008.

(7) Securities Owned and Securities Sold, Not Yet Purchased

At December 31, 2008 Securities Owned and Securities Sold, Not Yet Purchased, consist of trading and investment securities at fair value, as follows:

	Securities Owned	Securities Sold, Not Yet Purchased
<u>2008</u>		
U.S. Government and Agency Obligations	\$ 316,495	\$ 17,388
Municipal Bonds	52,948	50
Corporate Bonds	24,304	7,164
Corporate Stocks	23,241	645
Other Securities	15,052	-
	<u>\$ 432,040</u>	<u>\$ 25,247</u>

Other Securities consists principally of investments in partnership interests and corporate stocks that are not readily marketable. Investments in partnership interests are carried at an estimated fair value of \$8,353 at December 31, 2008. Certain associates have purchased limited partnership interests on a basis consistent with other investors in the partnerships. The Company serves as the general partner or limited partner in the partnerships. In connection with these partnerships, the Company has made commitments to invest up to an additional \$4,491 at December 31, 2008.

(8) Net Capital Requirements

The Company is subject to the requirements of Rule 15c3-1 (the “net capital rule”) under the Securities Exchange Act of 1934. The basic concept of the net capital rule is liquidity, its objective being to require a broker and dealer to maintain adequate net capital, as defined. The Company has elected to operate under the alternative net capital requirement as allowed by the net capital rule, which requires that net capital exceed 2% of aggregate debit items as those terms are defined. Withdrawal of equity capital may be restricted if net capital is less than 5% of such aggregate debit items.

At December 31, 2008 the Company’s net capital percentage was 88% of aggregate debit items, and net capital, as defined, was \$255,473, which is \$249,660 in excess of the required minimum amount.

(9) Subordinated Liabilities

The Company has \$274,913 of subordinated notes, including \$240,000 payable to BFC, covered by agreements approved by the FINRA that are available in computing adjusted net capital under the net capital rule at December 31, 2008. The following schedule discloses the major components including repayment terms:

Payable to BFC	
Series A Subordinated Note, 6.75%, due May 2014.	
Scheduled principal payments begin in May 2010.	\$ 140,000
Subordinated Note, variable interest rate 4.0% at December 31, 2008 due June 2011.	75,000
Subordinated Notes, variable interest rate 2.5% at December 31, 2008 due August 2011.	25,000
	<u>240,000</u>
Payable to Associates	34,913
	<u>\$ 274,913</u>

To the extent that such notes are required for the Company's continued compliance with minimum net capital requirements, they may not be repaid. At December 31, 2008 the Company had sufficient capital that such restrictions did not apply. The right of the note holders to receive any payment from the Company under the terms of the notes is subordinated to the claims of all present and future creditors of the Company that arise prior to maturity and is dependent on approval by the FINRA.

(10) Deferred Income Tax

The major deferred tax items, as computed under SFAS No. 109, "Accounting for Income Taxes," are as follows:

Deferred Tax Assets:	
Deferred Compensation Plans	\$ 22,915
Equipment and Leasehold Improvements	7,071
Accrued Expenses	10,215
Other	3,310
	<u>43,511</u>
Deferred Tax Liabilities:	
Margin Debt	1,862
Goodwill and Intangibles	7,636
Other	1,374
	<u>10,872</u>
Net Deferred Tax Assets	<u>\$ 32,639</u>



No valuation allowance, as defined in SFAS No. 109, is required as management believes it is more likely than not that the deferred tax asset is realizable.

(11) Stockholders' Equity

During 2008 the following share transactions took place:

	<u>Shares of Common Stock \$1 Stated Value</u>	<u>Shares of Treasury Stock</u>
Balance, December 31, 2007	25,925,282	26,298
Exercise of Options	325,988	(87,918)
Conversion of Restricted Stock Units	-	(396)
Purchases of Treasury Stock, Net	-	96,134
Balance, December 31, 2008	<u>26,251,270</u>	<u>34,118</u>

The Company has authorized 72,450,000 shares of \$1 stated value common stock. The Company has also authorized 1,000 shares of no par value, cumulative, nonvoting preferred stock. No shares of preferred stock were issued or outstanding in 2008.

The shares of the Company are subject to strict transfer restrictions.

On December 5, 2007 the directors of the Company approved a 2-for-1 stock split of the common and preferred stock. The stock split occurred on February 19, 2008. The above schedule takes into account the stock split as if it occurred as of December 31, 2007.

(12) Associate Compensation and Retirement Plans

(a) The Baird Profit Sharing and Savings Plan

Substantially all associates of the Company are eligible to participate in the Robert W. Baird & Co. Incorporated Profit Sharing and Savings Plan. The plan complies with Section 401(k) of the Internal Revenue Code. The Company matches 100% of the first one thousand two hundred dollars contributed by each participant annually plus 25% of any additional contributions up to 2.5% of eligible compensation.

Employer profit sharing contributions are made annually at the discretion of the Company's Board of Directors.



(b) Deferred Compensation

The Company has two deferred compensation plans, entitled the Baird Capital Participation Plan (“BCPP”), and the Financial Advisors Deferred Compensation Plan (“FADCP”). The BCPP no longer grants awards and all balances in the Plan are fully vested. The FADCP grants deferred compensation awards to certain associates, which vest after seven years, and are expensed at the date of grant. However, any award under the BCPP or FADCP granted in 2004 or prior years vests after five years. Associates have the ability to allocate their unvested deferred compensation awards among several investment options.

Certain BCPP participants own restricted stock units (“RSUs”). The RSUs are fully vested in accordance with the terms of the BCPP and are ultimately convertible into Company common stock. BCPP participants owning RSUs are entitled to cumulative distributions and dividends issued by the Company on its common stock. The RSUs become payable in full upon a change in control, as defined in the offering circular, of the Parent or of the Company. The RSUs and shares issued on conversion of the RSUs are subject to strict transfer restrictions.

A summary of the activity relating to the RSUs in 2008 is as follows:

	<u>Shares</u>
Outstanding, December 31, 2007	<u>314,928</u>
Conversion to Common Stock	(396)
Outstanding, December 31, 2008	<u><u>314,532</u></u>

The Company issued no RSUs during 2008. In connection with the RSUs, the Company has reserved 314,532 shares of Company common stock as of December 31, 2008 to cover the ultimate conversion of the outstanding RSUs. As described in Footnote 11, the directors of the Company approved a 2-for-1 stock split that occurred on February 19, 2008. The above schedule takes into account the stock split as if it occurred on December 31, 2007.

(c) Incentive Stock Option Plan

The Company has established the Robert W. Baird & Co. Incorporated 1997 Incentive Stock Option Plan (the “Incentive Plan”) for selected associates. The maximum number of stock options that may be granted under the Incentive Plan is 50% of the shares authorized for issuance to Company associates. The Incentive Plan does not require or set forth any specific vesting periods for the stock options, leaving the vesting provisions of individual option grants up to the discretion of the stock option committee of the Company’s Board of Directors. The option exercise price per share under the Incentive Plan may not be less than 100% of the fair market value of the Company’s stock on the date the option is granted.

The term of each option granted under the Incentive Plan shall generally be 10 years. The options immediately vest and become exercisable upon a change in control, as defined in the offering circular, of the Parent or of the Company. The options and shares issued upon exercise of the options are subject to strict transfer restrictions.

The Company did not grant options in 2008.

As described in Footnote 11, the directors of the Company approved a 2-for-1 stock split that occurred on February 19, 2008. The schedule below takes into account the stock split as if it occurred as of December 31, 2007.

Option activity during 2008 was as follows:

	<u>Baird Shares</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Term (Years)</u>
Outstanding, December 31, 2007	822,864	\$ 14.76	4.0
Exercised	(222,724)	10.78	
Forfeited	<u>(6,200)</u>	17.70	
Outstanding, December 31, 2008	<u>593,940</u>	16.22	3.7
Exercisable at December 31, 2008	554,740	15.74	3.4
Exercisable at December 31, 2007	761,704	14.11	3.6

Cash received from the exercise of stock options for the year ended December 31, 2008 was \$1,993. The tax benefit realized for the tax deductions from option exercises was \$650 for the year ended December 31, 2008 and is recorded in Additional Paid-In Capital on the Statement of Financial Condition.

(13) Baird UK Ltd.

The Company reports the results of its investment in Baird UK Ltd. using the equity method of accounting. At December 31, 2008 the Company's investment in Baird UK Ltd. was \$13,872 and is included in Other Assets on the Statement of Financial Condition.



(14) Commitments and Contingencies

(a) Leases

The Company occupies office space and leases equipment under cancelable and noncancelable operating lease arrangements. The aggregate minimum annual rental expense related to noncancelable leases is as follows:

2009	\$	20,562
2010		18,193
2011		14,804
2012		12,428
2013		10,165
Thereafter		62,843
	\$	<u>138,995</u>

(b) Letters of Credit

The Company has obtained letters of credit of \$44,000 as of December 31, 2008 secured by client securities held in margin accounts, of which the Company utilized \$33,289 to meet margin requirements of a clearing corporation as of December 31, 2008.

(c) Other

The Company and other securities dealers have been named as codefendants in certain suits purportedly brought for the benefit of large classes of securities investors and seeking substantial amounts in damages under Federal and state securities laws and common law. These suits arise in connection with the Company's role as a participating underwriter in various securities offerings. The Company is also involved in other actions incidental to its securities business. Pursuant to SFAS No. 5, "*Accounting for Contingencies*," the Company has established reserves against such contingencies. Based on its understanding of the facts and the advice of legal counsel, management believes that resolution of these various actions will not result, after taking into account the reserves, in any material adverse effect on the Company.

In the normal course of business, the Company enters into underwriting commitments. Transactions relating to underwriting commitments that were open at December 31, 2008 were not material.

The Company is a member of numerous exchanges and clearinghouses. Under the membership agreements, members are generally required to guarantee performance of other members. Additionally, if a member becomes unable to satisfy its obligations to the clearinghouse, other members would be required to meet these shortfalls. To mitigate these performance risks, the exchanges and clearinghouses often require members to post



collateral. The Company's maximum potential liability under these arrangements cannot be quantified. However, the potential for the Company to be required to make payments under these arrangements is remote. Accordingly, no contingent liability is recorded on the Statements of Financial Condition for these arrangements.

(15) Transfers of Financial Assets

The Company receives and delivers collateral in connection with its broker and dealer activities. Under many agreements, the Company is permitted to repledge securities held as collateral. There were no securities accepted as collateral at December 31, 2008.

(16) Financial Instruments With Off-Balance Sheet Risk

In the normal course of business, the Company's client securities activities involve the execution, settlement and financing of various client securities transactions. These activities may expose the Company to off-balance sheet risk in the event that the client or other broker is unable to fulfill its contracted obligations and the Company has to purchase or sell the financial instrument underlying the contract at a loss.

The Company's client securities activities are transacted on either a cash or margin basis. In margin transactions, the Company extends credit to its clients, subject to various regulatory and internal margin requirements, collateralized by cash and securities in the clients' accounts. In connection with these activities, the Company executes and clears client transactions involving the sale of securities not yet purchased, substantially all of which are transacted on a margin basis subject to individual exchange regulations. Such transactions may expose the Company to significant off-balance sheet risk in the event margin requirements are not sufficient to fully cover losses clients may incur. In the event clients fail to satisfy their obligations, the Company may be required to purchase or sell financial instruments at prevailing market prices to fulfill the clients' obligations.

The Company seeks to control the risks associated with its client activities by requiring clients to maintain margin collateral in compliance with various regulatory and internal guidelines. The Company monitors required margin levels daily and, pursuant to such guidelines, requires the client to deposit additional collateral or to reduce security positions when necessary. Such collateral is appropriately not reflected in the accompanying Statement of Financial Condition.

(17) Derivatives

The Company enters into security transactions involving future settlement. The Company has entered into forward purchase and forward sale transactions with a contract value of \$115,688 and \$245,652, respectively, as of December 31, 2008. The market value of forward purchase and forward sale transactions was \$116,489 and \$246,969 respectively, as of December 31, 2008. Transactions involving future settlement give rise to market risk if a counterparty fails to meet its obligations, which represents the potential loss that can be caused by a change in the market value of a particular financial instrument. The Company's exposure to market risk is determined by a



-15-

number of factors, including but not limited to the size, composition and diversification of positions held, the absolute and relative levels of interest rates, and market volatility.

The Company uses financial futures and options to manage market risk related to trading securities. The Company did not have open futures or options positions as of December 31, 2008.

(18) Federal Deposit Insurance Corporation

The Company has certain cash deposit accounts with financial institutions in which the balances occasionally exceed the Federal Deposit Insurance Corporation (FDIC) insured limit. The Company has not experienced any losses in such accounts and management believes it is not exposed to any significant risk.