



Robert W. Baird & Co. Incorporated

Consolidated Statement of Financial Condition

As of December 31, 2010

Together with Report of Independent Registered Public Accounting Firm

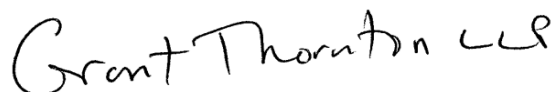
Report of Independent Registered Public Accounting Firm

Board of Directors
Robert W. Baird & Co. Incorporated

We have audited the accompanying consolidated statement of financial condition of Robert W. Baird & Co. Incorporated (a Wisconsin corporation) and its consolidated private equity partnerships (“Baird Private Equity Partnerships”) (collectively, the “Company”) as of December 31, 2010. This financial statement is the responsibility of the Company’s management. Our responsibility is to express an opinion on the financial statement based on our audit. We did not audit the financial statements of the Baird Private Equity Partnerships, which statements reflect total assets constituting 14% of the related consolidated total. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Baird Private Equity Partnerships, is based solely on the report of the other auditors.

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 statement of financial condition is 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 statement of financial condition, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall statement of financial condition presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, based on our audit and the report of the other auditors, the consolidated statement of financial condition referred to above presents fairly, in all material respects, the financial position of Robert W. Baird & Co. Incorporated as of December 31, 2010 in conformity with accounting principles generally accepted in the United States of America.



GRANT THORNTON LLP
New York, New York
March 11, 2011

Robert W. Baird & Co. Incorporated

Consolidated Statement of Financial Condition
As of December 31, 2010

(In Thousands)

| <u>Assets</u> | |
|--|---------------------|
| Cash and Cash Equivalents | \$ 230,326 |
| Cash Held by Baird Private Equity Partnerships | 567 |
| Securities Purchased Under Agreements to Resell | 863,134 |
| Deposits with Clearing Corporations | 14,511 |
| Receivables: | |
| Clients | 236,444 |
| Brokers and Dealers | 45,033 |
| Deposits Paid on Securities Borrowed | 55,378 |
| Other | 187,573 |
| | <u>524,428</u> |
| Securities Owned, at Fair Value | 538,569 |
| Securities Owned by Baird Private Equity Partnerships, at Fair Value | 359,217 |
| Furniture, Equipment, Leasehold Improvements and Capital Leases at Cost, Less Accumulated Depreciation and Amortization of \$98,596 | 45,158 |
| Goodwill | 27,561 |
| Intangible Assets, at Cost, Less Accumulated Amortization of \$8,547 | 12,012 |
| Other Assets, including \$3,947 of Net Deferred Tax Assets | <u>37,245</u> |
| Total Assets | <u>\$ 2,652,728</u> |

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

Robert W. Baird & Co. IncorporatedConsolidated Statement of Financial Condition
As of December 31, 2010

(In Thousands)

(Continued)

| <u>Liabilities and Stockholders' Equity</u> | |
|---|---------------------|
| <u>Liabilities:</u> | |
| Money Borrowed: | |
| Book Credit Balances in Bank Accounts | \$ 35,743 |
| Securities Sold Under Agreements to Repurchase | 1,060,560 |
| Payables: | |
| Clients | 107,903 |
| Brokers and Dealers | 16,940 |
| Deposits Received on Securities Loaned | 21,520 |
| | <u>146,363</u> |
| Securities Sold, Not Yet Purchased, at Fair Value | 51,198 |
| Accounts Payable, Accrued Expenses and Other Liabilities | 340,284 |
| Subordinated Liabilities | <u>254,075</u> |
| Total Liabilities | <u>1,888,223</u> |
| <u>Stockholders' Equity:</u> | |
| Common Stock | 26,374 |
| Preferred Stock | - |
| Additional Paid-In Capital | 115,450 |
| Restricted Stock Units | 2,072 |
| Retained Earnings | 265,899 |
| Treasury Stock, at Cost | (3,418) |
| Accumulated Other Comprehensive Income | 2,124 |
| Total Robert W. Baird & Co. Incorporated Stockholders' Equity | 408,501 |
| Noncontrolling Interests in Baird Private Equity Partnerships | <u>356,004</u> |
| Total Stockholders' Equity | <u>764,505</u> |
| Total Liabilities and Stockholders' Equity | <u>\$ 2,652,728</u> |

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

Robert W. Baird & Co. Incorporated

Notes to Consolidated Statement of Financial Condition
December 31, 2010

(In Thousands, Except Share and Per Share Amounts)

(1) Summary of Significant Accounting Policies

The Consolidated Statement of Financial Condition includes Robert W. Baird & Co. Incorporated (“RWB”) and its consolidated private equity partnerships as more fully discussed in Footnote 12 (together, the “Company”). The Company is registered as a securities broker dealer and an investment adviser with the Securities and Exchange Commission (“SEC”) under the Securities Exchange Act of 1934 and the Investment Advisers Act of 1940, and is also a member of the Financial Industry Regulatory Authority (“FINRA”) and various securities exchanges. 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 private wealth management, equity and fixed income capital markets, asset management and private equity businesses, including securities brokerage; investment advisory and asset management services; institutional equity and fixed income sales; research services; origination of and participation in underwritings and distribution of corporate and municipal securities issuances; municipal advisory services; merger and acquisition advisory services; private equity and venture capital investing; and market making and trading activities in equity, municipal and other fixed income securities. 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 Consolidated Statement of Financial Condition.

(a) Estimates

The preparation of the Consolidated Statement of Financial Condition 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 Consolidated Statement of Financial Condition. Actual results may differ from those estimates.

(b) Cash and Cash Equivalents

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

(c) Cash Held by Baird Private Equity Partnerships

Cash held by Baird Private Equity Partnerships represents cash and cash equivalents held by consolidated private equity partnerships. Such amounts are not available to fund the general liquidity needs of RWB.

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

The Company enters into 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.

(e) Receivables

Receivables: Clients - includes amounts receivable on cash and margin transactions which are generally collateralized by securities owned by clients.

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

The Company maintains an allowance for doubtful accounts based on an assessment of its ability to collect these receivables. Assessments include market conditions, aggregate balances as well as historical collection experience. When the review of these accounts indicates that further collection activity is highly unlikely, amounts are written off and the corresponding allowance for doubtful accounts is reduced. At December 31, 2010 the allowance was \$18,533.

(f) Securities Transactions

Revenue from 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.

(g) Fair Value Measurements

The Company follows Accounting Standards Codification (“ASC”) Topic 820, “*Fair Value Measurements*.” ASC Topic 820 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. ASC Topic 820 prescribes the methodology of observable 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 Company’s assets recorded in the Consolidated Statement of Financial Condition are categorized based upon the level of judgment associated with the inputs used to measure their fair value. The hierarchy, defined by ASC Topic 820, 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.

Cash and cash equivalents, deposits with clearing corporations and receivables are financial assets with carrying values that approximate fair value. Money borrowed, payables, accounts payable, accrued expenses and other liabilities, including deferred tax liability are financial liabilities with carrying values that approximate fair value. The carrying amount of subordinated liabilities approximates fair value based on current market conditions and interest rates available to the Company for similar financial instruments.

Valuation Techniques are based on the following:

- i. U.S. Government and Agency Obligations – U.S. Government and Agency Obligations are valued based on quoted prices from external data providers and market participants.
- ii. Municipal Bonds - Municipal Bonds are valued based on quoted prices from external data providers and market participants.
- iii. Corporate Bonds – Corporate Bonds are valued based on quoted prices from external data providers and market participants.

- iv. Collateralized Mortgage Obligations – Collateralized Mortgage Obligations are valued based on quoted prices from external data providers and market participants. For certain securities where there is limited activity or less transparency around significant inputs, the securities are valued as determined by the Company by reference to available market information.
- v. Auction Rate Securities – Auction Rate Securities (“ARS”) include securities backed by pools of student loans, securities issued by municipalities, and auction rate preferred securities issued by closed end mutual funds. ARS are measured using market data provided by external service providers, as available. For certain securities where there is limited activity or less transparency around significant inputs, the securities are valued as determined by the Company by reference to available market information.
- vi. Other Securities – Other Securities consist principally of corporate stocks and investments in partnership interests. Corporate stocks are primarily publicly traded with observable prices in active markets; any corporate stock not actively traded is valued with unobservable inputs.
- vii. Securities Owned by Baird Private Equity Partnerships - Partnership interest valuations are based on prices or valuation techniques that require inputs that are both significant to the fair value and unobservable, and thus, are considered Level III. In the absence of readily ascertainable market values, valuation techniques include but are not limited to, EBITDA multiples based on public company comparables or comparable transactions, discounted cash flows, and forward looking multiples.

See Footnote 6 for further information.

(h) 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.

(i) Derivative Financial Instruments

The Company accounts for gains and losses resulting from changes in the fair values of derivatives depending on the use of the derivative and whether it qualifies for hedge accounting.

The Company enters into forward, option and future transactions as more fully discussed in Footnote 17.

(j) 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 statements for deferred income taxes in recognition of these temporary differences as more fully disclosed in Footnote 9.

(k) Furniture, Equipment, Leasehold Improvements and Capital Leases

Furniture, equipment, leasehold improvements and capital leases are stated at cost less accumulated depreciation. Depreciation is provided by 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.

(l) Goodwill and Intangible Assets

Goodwill and intangible assets with indefinite lives are not amortized but are reviewed at least annually for impairment. At December 31, 2010, there was no impairment identified by the Company. Intangibles with finite lives are amortized on a straight-line basis over their respective lives as more fully disclosed in Footnote 4.

(m) 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 ASC Topic 718, "*Accounting for Stock-Based Compensation*" as more fully disclosed in Footnote 11.

(n) Foreign Currency Translation

In accordance with ASC Topic 830, "*Foreign Currency Translation*," assets and liabilities of the Company's foreign investment are generally translated at the current exchange rate, and the related revenues and expenses are translated at the average monthly exchange rates in effect. 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." These gains or losses are the only component of Accumulated Other Comprehensive Income.

(o) Commitments and Contingencies

The Company regularly enters into office space and other equipment lease arrangements, some of which are noncancelable for the term of the lease. In addition, the Company is occasionally involved in legal and regulatory proceedings, arbitrations, underwriting commitments, private equity capital commitments and various other contingent obligations as more fully disclosed in Footnote 14.

(p) Consolidation

The Consolidated Statement of Financial Condition includes the accounts of RWB and those entities in which the Company has a controlling interest as a general partner or in which the Company is the primary beneficiary of a variable interest entity (“VIE”). In evaluating whether the Company has a controlling financial interest in entities in which the Company would consolidate, the Company considers the following: (1) for voting interest entities, the Company consolidates those entities in which the Company owns a majority of the voting interests; (2) for VIEs that meet the criteria for deferral under Financial Accounting Standards Board (“FASB”) Accounting Standards Update (“ASU”) 2010-10, the Company consolidates those entities in which the Company is considered the primary beneficiary because the Company (i) has the direct or indirect ability through voting rights or similar rights to make decisions about the VIE’s activities that have a significant effect on its success and (ii) absorbs the majority of the VIE’s expected losses, receives a majority of the VIE’s expected residual returns, or both; and (3) for limited partnership entities that are not considered VIEs, the Company consolidates those entities if the Company is the general partner of such entities and for which no substantive kick-out rights (the rights underlying the limited partners’ ability to dissolve the limited partnership or otherwise remove the general partners are collectively referred to as “kick-out” rights) or participating rights exist. All material intercompany accounts and transactions have been eliminated in consolidation.

FASB ASU 2010-10 defers the consolidation requirements of ASC Topic 810 resulting from the issuance of FASB Statement 167 for a reporting entity’s interest in an entity that has all the attributes of an investment company.

The beginning balance of stockholders’ equity was restated to correct an error related to the consolidation of the Baird Private Equity Funds and to include non-controlling interests, which represent the component of partnership capital in consolidated entities held by third party investors. Further disclosure about these consolidated funds is included in Footnote 12.

(q) Noncontrolling Interests in Baird Private Equity Partnerships

Noncontrolling Interests in Baird Private Equity Partnerships represent the component of partnership capital in consolidated entities held by third party investors.

(2) Related-Party Transactions

As of December 31, 2010 there was \$64,988 of receivables from affiliates included in Receivables Other on the Consolidated Statement of Financial Condition.

As of December 31, 2010 there was \$16,524 of payables to affiliates included in Accounts Payable, Accrued Expenses and Other Liabilities on the Consolidated Statement of Financial Condition.

The Company makes loans or pays advances to associates primarily for recruiting purposes. Receivables from associates at December 31, 2010 were \$92,346 and are included in Receivables Other on the Consolidated Statement of Financial Condition.

(3) Furniture, Equipment, Leasehold Improvements, and Capital Leases

Furniture, Equipment, Leasehold Improvements and Capital Leases as of December 31, 2010 consist of the following:

| | <u>2010</u> |
|--|-------------------------|
| Furniture and Fixtures | \$ 34,113 |
| Equipment | 32,514 |
| Software | 21,672 |
| Leasehold Improvements | <u>50,589</u> |
| | 138,888 |
| Less Accumulated Depreciation | <u>(96,717)</u> |
| Furniture, Equipment and Leasehold Improvements, Net | 42,171 |
| Capital Leases | 4,866 |
| Less Accumulated Amortization | <u>(1,879)</u> |
| Furniture, Equipment, Leasehold Improvements and Capital Leases, Net | <u><u>\$ 45,158</u></u> |

(4) Goodwill and Intangible Assets

At December 31, 2010 goodwill and intangible assets consist of the following:

| | <u>Useful Life</u> | <u>2010</u> |
|-----------------------------|--------------------|------------------|
| Finite Life Intangibles | | |
| Client lists | 8 Years | \$ 10,490 |
| Noncompete agreements | 5 Years | <u>240</u> |
| | | 10,730 |
| Accumulated Amortization | | |
| Client lists | | (8,413) |
| Noncompete agreements | | <u>(134)</u> |
| | | <u>(8,547)</u> |
| Net Finite Life Intangibles | | 2,183 |
| Indefinite Life Intangibles | | |
| Trade Names | N/A | <u>9,829</u> |
| Net Intangibles | | 12,012 |
| Goodwill | N/A | <u>27,561</u> |
| | | <u>\$ 39,573</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 \$260,000 at December 31, 2010. The Company had no outstanding balances under its lines of credit at December 31, 2010. 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 \$35,743 at December 31, 2010 in credit balances at certain banks with which it does business. The Company does not have a right of offset regarding these balances and, as a result, they are classified as Money Borrowed on the Consolidated Statement of Financial Condition.

(6) Fair Value of Financial Instruments

The following table summarizes the fair value of Securities Owned and Securities Sold, Not Yet Purchased in accordance with ASC Topic 820 standards as of December 31, 2010:

| | Level I | Level II | Level III | Total |
|--|------------|------------|------------|------------|
| Money Market Funds (included in Cash and Cash Equivalents) | \$ 199,000 | \$ - | \$ - | \$ 199,000 |
| Securities Owned | | | | |
| U.S. Government and Agency Obligations | \$ - | \$ 146,644 | \$ - | \$ 146,644 |
| Municipal Bonds | - | 129,403 | - | 129,403 |
| Corporate Bonds | - | 52,253 | 31,653 | 83,906 |
| Collateralized Mortgage Obligations | - | 82,096 | 4,017 | 86,113 |
| Auction Rate Securities | - | - | 52,025 | 52,025 |
| Other Securities | 35,394 | - | 5,084 | 40,478 |
| Total Securities Owned | \$ 35,394 | \$ 410,396 | \$ 92,779 | \$ 538,569 |
| Securities Owned by Baird Private Equity Partnerships | \$ - | \$ - | \$ 359,217 | \$ 359,217 |
| Securities Sold, Not Yet Purchased | | | | |
| U.S. Government and Agency Obligations | \$ - | \$ 48,920 | \$ - | \$ 48,920 |
| Municipal Bonds | - | 443 | - | 443 |
| Corporate Bonds | - | 1,079 | - | 1,079 |
| Other Securities | 756 | - | - | 756 |
| Total Securities Sold, Not Yet Purchased | \$ 756 | \$ 50,442 | \$ - | \$ 51,198 |

Other Securities consist principally of corporate stocks. In addition, there were no transfers into or out of Levels I, II or III during these periods.

The valuation of equity ownership in privately owned companies, the type of investment principally included in Securities Owned by Baird Private Equity Partnerships, requires significant management judgment due to the absence of quoted market prices, inherent lack of liquidity and long-term nature of these assets. As a result, these values cannot be determined with precision and the calculated fair value estimates may not be realizable in a current sale or immediate settlement of the instrument.

The following table summarizes the change in fair values associated with ASC Topic 820 Level III assets during 2010:

| | Securities Owned | Securities Owned by Baird Private Equity Partnerships |
|---------------------------|---------------------|--|
| | <u> </u> | <u> </u> |
| Balance December 31, 2009 | \$ 85,850 | \$ 294,275 |
| Purchase and (Sales), Net | 3,570 | 38,755 |
| Realized Gains | 1,619 | - |
| Unrealized Gains | 1,740 | 26,187 |
| Balance December 31, 2010 | <u>\$ 92,779</u> | <u>\$ 359,217</u> |

(7) 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, 2010, the Company’s net capital percentage was 107% of aggregate debit items, and net capital, as defined, was \$279,200, which was \$273,993, in excess of the required minimum amount. Net capital after anticipated withdrawals as a percentage of aggregate debits was 67%.

(8) Subordinated Liabilities

The Company had \$254,075 of subordinated notes, including \$212,000 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, 2010. The following schedule discloses the major components including repayment terms:

| | <u>2010</u> |
|--|-------------------|
| Payable to BFC | |
| Series A Subordinated Note, 6.75%, due May 2014. | |
| Scheduled principal payments began in May 2010. | \$ 112,000 |
| Subordinated Note, variable interest rate (4.0% at | |
| December 31, 2010), due June 2011. | 75,000 |
| Subordinated Notes, variable interest rate (0.75% | |
| at December 31, 2010), due August 2011. | <u>25,000</u> |
| | 212,000 |
| Payable to Associates | <u>42,075</u> |
| | <u>\$ 254,075</u> |

Subordinated Liabilities mature as follows at December 31, 2010:

| | |
|------------|-------------------|
| 2011 | \$ 128,000 |
| 2012 | 35,142 |
| 2013 | 35,980 |
| 2014 | 38,549 |
| 2015 | 9,259 |
| Thereafter | <u>7,145</u> |
| | <u>\$ 254,075</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, 2010, 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.

(9) Income Taxes

(a) Uncertain Tax Provisions

The Company accounts for tax contingencies in accordance with ASC Topic 740, “*Income Taxes*.” As required by the uncertain tax position guidance in that Topic, the Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

The Company is included in the consolidated income tax returns of Baird Holding Company in the U.S. federal jurisdiction and various consolidated states. It also files separate income tax returns in various states and local jurisdictions. The income tax returns for the years prior to 2006 are no longer subject to examination by income tax authorities, unless subsequently amended.

The Company’s unrecognized tax benefits are analyzed and monitored to ensure they are adequate and reflective of known events. The Company does not believe there will be a material change in the balance within the subsequent 12 month period.

(b) Deferred Income Tax

The major deferred tax items, as computed under ASC Topic 740, are as follows:

| | <u>2010</u> |
|--------------------------------------|------------------------|
| Deferred Tax Assets: | |
| Deferred Compensation Plans | \$ 6,931 |
| Accrued Expenses | <u>8,352</u> |
| | 15,283 |
| Deferred Tax Liabilities: | |
| Margin Debt | 1,198 |
| Goodwill and Intangibles | 6,606 |
| Equipment and Leasehold Improvements | 2,733 |
| Securities Owned | 223 |
| Other | <u>576</u> |
| | <u>11,336</u> |
| Net Deferred Tax Asset | <u><u>\$ 3,947</u></u> |

No valuation allowance, as defined in ASC Topic 740, is required as management believes it is more likely than not that the deferred tax assets are realizable.

(10) Stockholders' Equity

During 2010, the following share transactions took place:

| | Shares of Common Stock; \$1 Stated Value | Shares of Common Treasury Stock |
|--------------------------------------|--|---------------------------------------|
| Balance, December 31, 2009 | 26,374,422 | 212,863 |
| Exercise of Options | - | (132,745) |
| Conversion of Restricted Stock Units | - | (6,924) |
| Sales of Treasury Stock | - | (173,692) |
| Purchases of Treasury Stock | - | 209,008 |
| Balance, December 31, 2010 | <u>26,374,422</u> | <u>108,510</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 2010. The shares of the Company are subject to strict transfer restrictions.

(11) 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 two thousand dollars contributed by each eligible participant annually. Employer profit sharing contributions are made annually at the discretion of the Company's Board of Directors.

(b) Non-Qualified Compensation

The Company has three non-qualified compensation plans, entitled the Baird Capital Participation Plan (“BCPP”), the Financial Advisors Deferred Compensation Plan (“FADCP”) and the Baird Long Term Incentive Plan (“LTIP”). The BCPP no longer grants awards and all balances in the Plan are fully vested. For services performed, the FADCP and LTIP grant awards to certain associates. The awards, which vest after seven years, are expensed at the date of grant as no future services are required, subject to continued employment. However, any award under the BCPP, FADCP or LTIP granted in 2004 or prior years vested after five years. Associates have the ability to allocate their unvested 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 2010 is as follows:

| | <u>Shares</u> |
|--------------------------------|----------------|
| Outstanding, December 31, 2009 | 286,092 |
| Conversion to Common Stock | <u>(6,924)</u> |
| Outstanding, December 31, 2010 | <u>279,168</u> |

The Company issued no RSUs during 2010. In connection with the RSUs, the Company has reserved 279,168 shares of Company common stock at December 31, 2010, to cover the ultimate conversion of the RSUs.

(c) Incentive Stock Option Plans

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 stock option grants up to the discretion of the stock option committee of the Company’s Board of Directors. The stock 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 stock option granted under the Incentive Plan shall generally be 10 years. The stock options immediately vest and become exercisable upon a change in control, as defined in the Incentive Plan of the Parent or of the Company. The stock options and shares issued upon exercise of the stock options are subject to strict transfer restrictions.

There were no non-vested options as of December 31, 2010.

Stock option activity during 2010 was as follows:

| | <u>Baird Options</u> | <u>Weighted Average Exercise Price</u> | <u>Weighted Average Remaining Contractual Term (Years)</u> |
|----------------------------------|--------------------------|--|--|
| Outstanding, December 31, 2009 | 430,368 | \$ 17.24 | 3.1 |
| Exercised | (114,548) | 16.05 | |
| Forfeited | <u>(2,800)</u> | 22.94 | |
| Outstanding, December 31, 2010 | <u>313,020</u> | 17.63 | 2.3 |
| Exercisable at December 31, 2010 | 313,020 | 17.63 | 2.3 |

Cash received from the exercise of stock options for the year ended December 31, 2010 was \$1,131. The tax benefit realized for the tax deductions from stock option exercises was \$206 for the year ended December 31, 2010, and is recorded in Additional Paid-In Capital on the Consolidated Statement of Financial Condition.

(12) Partnership Consolidation

The following table presents information about the carrying value of the assets, liabilities and equity of the partnerships which are consolidated and included within the Consolidated Statement of Financial Condition. The noncontrolling interests presented in this table represent the portion of these net assets which are not the Company's.

| | <u>2010</u> |
|---|-------------------|
| Assets: | |
| Cash Held by Baird Private Equity Partnerships | \$ 567 |
| Receivables, Other | 5,720 |
| Securities Owned by Baird Private Equity Partnerships | 359,217 |
| Other Assets | 750 |
| Total Assets | <u>\$ 366,254</u> |
| Liabilities and Stockholders' Equity: | |
| Accounts Payable, Accrued Expenses and Other Liabilities | \$ 2,514 |
| Intercompany Payable | 2,646 |
| Total Liabilities | <u>5,160</u> |
| Stockholders' Equity Attributable to the Company | 5,090 |
| Stockholders' Equity Attributable to Noncontrolling Interests in Baird Private Equity Partnerships | 356,004 |
| Total Equity | <u>361,094</u> |
| Total Liabilities and Stockholders' Equity | <u>\$ 366,254</u> |

Certain Baird Private Equity Partnerships are not consolidated pursuant to the accounting rules previously mentioned under the consolidation footnote. Net assets of the partnerships not consolidated were \$59 million at December 31, 2010. These partnerships were determined to be Variable Interest Entities (VIE) and the general partner (an affiliate) was determined not to be the primary beneficiary. The general partner ownership interest in these partnerships was 0.2% at December 31, 2010.

(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, 2010, the Company's investment in Baird UK Ltd. was \$20,003, and is included in Other Assets on the Consolidated 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. These lease arrangements include escalating clauses which are recognized on a straight-line basis over the life of the lease. Capital leases consist of computers, servers and other computer related items. Future minimum lease payments are as follows:

| | Capital | Operating | Total |
|---|----------|------------|------------|
| 2011 | \$ 1,353 | \$ 20,544 | \$ 21,897 |
| 2012 | 1,288 | 19,568 | 20,856 |
| 2013 | 518 | 17,581 | 18,099 |
| 2014 | 46 | 15,978 | 16,024 |
| 2015 | - | 14,115 | 14,115 |
| Thereafter | - | 49,685 | 49,685 |
| | \$ 3,205 | \$ 137,471 | \$ 140,676 |
| Less amounts representing interest | (144) | | |
| Present value of minimum lease payments | \$ 3,061 | | |

The capital lease obligation was \$3,061 at December 31, 2010, and is recorded in Accounts Payable, Accrued Expenses and Other Liabilities on the Consolidated Statement of Financial Condition.

(b) Letters of Credit

The Company has obtained letters of credit of \$33,000 as of December 31, 2010, secured by client securities held in margin accounts. The Company utilized \$24,016 to meet margin requirements of a clearing corporation as of December 31, 2010.

(c) Other

The Company is involved in legal actions from time to time that are incidental to its securities business, including without limitation, client complaints and arbitrations, employment related disputes, regulatory investigations and proceedings, securities class action claims arising from underwriting activity, and claims brought against the Company in connection with its recruitment of associates from other firms. Pursuant to ASC Topic 450, "*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 financial condition of the Company.

In the normal course of business, the Company enters into underwriting commitments. Transactions relating to underwriting commitments that were open as of December 31, 2010 were not material.

RWB serves as the general partner or limited partner in various partnerships. RWB has commitments to invest up to an additional \$4,435 at December 31, 2010 in partnerships.

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 Consolidated Statement 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. At December 31, 2010 the fair value of securities accepted as collateral was \$920,643.

(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 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. 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 the client fails to satisfy its obligations, the Company may be required to purchase or sell financial instruments at prevailing market prices to fulfill the client's 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 Consolidated 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 \$171,288 and \$222,747, respectively, as of December 31, 2010. The market value of forward purchase and forward sale transactions was \$170,169 and \$221,599 respectively, as of December 31, 2010. 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 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 may use 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, 2010.

(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.

(19) Subsequent Events

The Company evaluated its December 31, 2010 Consolidated Statement of Financial Condition for subsequent events through March 11, 2011, the date that the financial statements were available to be issued. The Company is not aware of any subsequent events which would require recognition or disclosure in the Consolidated Statement of Financial Condition.