

Linsco/Private Ledger Corp.

Statement of Financial Condition

June 30, 2006
(Unaudited)



FINANCIAL
SERVICES

Linsco/Private Ledger • Member NASD/SIPC

LINSKO/PRIVATE LEDGER CORP.**STATEMENT OF FINANCIAL CONDITION**
June 30, 2006 (Unaudited) (Dollars in thousands)

ASSETS	
Cash and cash equivalents	\$ 122,855
Cash and securities segregated under federal and other regulations	10
Receivable from:	
Customers, net of allowance of \$267	297,419
Product sponsors, broker/dealers and clearing organizations	78,811
Others, net of allowance of \$2,735	38,562
Securities borrowed	3,667
Securities owned—at market value (including \$2,349 pledged to clearing organizations)	9,500
Fixed assets, net of accumulated depreciation and amortization of \$60,139	39,483
Goodwill	421
Intangible assets, net of accumulated amortization of \$2,153	4,032
Income tax receivable from parent	15,209
Deferred income tax—net	2,070
Prepaid expenses	10,745
Due from affiliates	285
Other assets	272
TOTAL	<u>\$623,341</u>

LIABILITIES AND STOCKHOLDER'S EQUITY

LIABILITIES:	
Drafts payable	\$ 92,868
Payable to customers	171,444
Payable to broker/dealers and clearing organizations	29,935
Accrued commissions payable	62,621
Accounts payable and accrued liabilities	30,651
Securities sold but not yet purchased—at market value	2,498
Unearned revenue	30,989
Total liabilities	<u>421,006</u>

COMMITMENTS AND CONTINGENCIES (NOTE 9)**STOCKHOLDER'S EQUITY:**

Common stock, no par value—authorized, 7,500 shares; issued and outstanding, 4,900 shares	17
Additional paid-in capital	117,126
Retained earnings	85,192
Total stockholder's equity	<u>202,335</u>
TOTAL	<u>\$623,341</u>

NOTES TO THE STATEMENT OF FINANCIAL CONDITION

As of June 30, 2006 (Unaudited)

1. ORGANIZATION AND DESCRIPTION OF THE COMPANY

Linsco/Private Ledger Corp. ("Linsco" or the "Company"), headquartered in Boston and San Diego, is a clearing broker/dealer registered with the National Association of Securities Dealers, Inc. ("NASD") and the Securities and Exchange Commission ("SEC") pursuant to the Securities Exchange Act of 1934 and an investment adviser registered with the SEC pursuant to the Investment Advisers Act of 1940. The Company is also registered as a Futures Commission Merchant with the Commodity Futures Trading Commission and is a member of the National Futures Association. Additionally, the Company is a member of the Boston Stock Exchange. The Company is a wholly owned subsidiary of LPL Holdings, Inc. ("LPL"), a Massachusetts holding corporation.

The Company principally transacts business as an agent on behalf of customers in mutual funds, stocks, fixed income instruments, commodities, options, private and public partnerships, variable annuities, real estate investment trusts, and other investment products. The Company is licensed to operate in all 50 states and Puerto Rico and has an independent contractor sales force of approximately 6,700 licensed financial advisors dispersed throughout the United States.

On December 2005, LPL and its subsidiaries was acquired through a merger transaction with BD Acquisition, Inc., a wholly owned subsidiary of LPL Investment Holdings, Inc. ("LPLIH") (previously named BD Investment Holdings, Inc.). LPLIH was formed by investment funds affiliated with TPG Partners IV, L.P. and Hellman & Friedman Capital Partners V, L.P. (collectively, the "Sponsors"). The acquisition was accomplished through the merger of BD Acquisition, Inc. with and into LPL with LPL being the surviving entity (the "Acquisition"). As a result of the Acquisition, LPL became a wholly owned subsidiary of LPLIH.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation—This financial statement is prepared in accordance with accounting principles generally accepted in the United States of America ("generally accepted accounting principles"), which require the Company to make estimates and assumptions regarding the valuations of certain financial instruments, intangible assets, allowance for doubtful accounts, accruals for liabilities and income taxes, revenue and expense accruals, and other matters that affect the financial statement and related disclosures. Actual results could differ materially from those estimates.

See accompanying notes to the statement of financial condition.

Cash and Cash Equivalents—Cash and cash equivalents are composed of interest-bearing deposits and U.S. government obligations that meet the definition of a cash equivalent. Cash equivalents are highly liquid investments, with original maturities of less than 90 days that are not required to be segregated under federal or other regulations.

Cash and Securities Segregated under Federal and Other Regulations—As a broker/dealer carrying customer accounts, the Company is subject to requirements related to maintaining cash or qualified securities in a segregated reserve account for the exclusive benefit of its customer in accordance with SEC Rule 15c3-3. At June 30, 2006, the Company had \$10,000 in cash segregated in a special reserve bank account for the benefit of customers.

Receivable From and Payable to Customers—Receivable from and payable to customers include amounts due on cash and margin transactions. The Company extends credit to its customers to finance their purchases of securities on margin. The Company receives income from interest charged on such extensions of credit. The Company pays interest on certain customer-free credit balances held pending investment. Loans to customers are generally fully collateralized by customer securities, which are not included in the accompanying statement of financial condition.

To the extent that margin loans and other receivables from customers are not fully collateralized by customer securities, management establishes an allowance that it believes is sufficient to cover any probable losses. When establishing this allowance, management considers a number of factors including its ability to collect from the client and/or the customer's financial advisor and the Company's historical experience in collecting on such transactions. Allowances for uncollectible amounts from customers increased \$144,000 during the six months ended June 30, 2006. As of June 30, 2006, the allowance was \$267,000.

Receivable From Product Sponsors, Broker/Dealers and Clearing Organizations—Receivable from product sponsors, broker/dealers and clearing organizations primarily consists of commission and transaction-related receivables.

Receivable From Others—Receivable from others primarily consists of accrued fees from product sponsors, financial advisors, and others. The Company periodically extends credit to its financial advisors in the form of recruiting loans, commission advances, and other loans. The decisions to grant receivables to financial advisors are generally based on either the financial advisors' credit score, his/her ability to generate future commissions, or both. Management maintains an allowance for uncollectible amounts using an aging analysis that takes into account the financial advisor's registration status and the specific type of receivable. The aging thresholds and specific percentages used represent management's best estimates of probable losses. Management monitors the adequacy of these estimates through periodic evaluations against actual trends experienced.

The following schedule shows the Company's activity in providing for uncollectible receivables from others for the six months ended June 30, 2006 (in thousands):

Beginning balance—January 1	\$2,529
Provision	367
Charge-offs—net of recoveries	<u>(161)</u>
Ending balance—June 30	<u>\$2,735</u>

Securities Borrowed and Loaned—Securities borrowed and loaned are accounted for as collateralized financings and are recorded at the amount of the cash provided for securities borrowed transactions and cash received for securities loaned (generally in excess of market values). The adequacy of the collateral deposited for securities borrowed is continuously monitored and adjusted when considered necessary to minimize the risk associated with this activity. The collateral received for securities loaned is generally cash and is adjusted daily through the Depository Trust Company's ("DTC") net settlement process and is included in payable to broker/dealers and clearing organizations in the statement of financial condition.

Under Statement of Financial Accounting Standards ("SFAS") No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities—a replacement of FASB Statement No. 125*, ("SFAS No. 140") the Company is required to disclose the collateral received under securities borrowed, customer and noncustomer agreements that it has the ability to sell or repledge, and the amounts of collateral that have been pledged or resold. As of June 30, 2006, the Company had received collateral primarily in connection with securities borrowed and customer margin loans with a market value of approximately \$361.55 million, which it can sell or repledge. Of this amount, approximately \$144.86 million has been pledged or sold as of June 30, 2006, \$102.10 million was pledged to a bank in connection with an unutilized secured margin line of credit, \$28.78 million was pledged to various clearing organizations, and \$13.98 million was loaned to the Depository Trust Company through participation in the Stock Borrow Program.

Securities Owned and Sold but Not Yet Purchased—Securities owned and sold but not yet purchased are reflected on a trade-date basis at market value with realized and unrealized gains and losses being recorded in other revenues. Customers' securities transactions are recorded on a settlement-date basis, with related commission income and expense reported on a trade-date basis. Securities owned by customers held as collateral for the receivable balances are not reflected in the statement of financial condition.

Fixed Assets—Furniture, equipment, computers, purchased software, capitalized software, automobiles and leasehold improvements are recorded, net of accumulated depreciation and amortization. Depreciation is recognized using the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the lesser of their useful lives or the terms of the underlying leases, ranging up to 10 years. Equipment, furniture, fixtures and purchased software are depreciated over periods of 3 to 7 years. Automobiles have depreciable lives of 5 years. Management reviews fixed assets for impairment whenever events or changes in circumstances indicate the carrying amount of the assets may not be recoverable.

Software Development Costs—Software development costs are charged to operations as incurred. Software development costs include costs incurred in the development and enhancement of software used in connection with services provided by the Company that do not otherwise qualify for capitalization under the American Institute of Certified Public Accountants (“AICPA”) Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use* (“SOP 98-1”).

The costs of internally developed software that qualify for capitalization under SOP 98-1 are capitalized as fixed assets and subsequently amortized over the estimated useful life of the software generally ranging from 3 to 5 years. The costs of internally developed software are included in fixed assets at the point at which the conceptual formulation, design and testing of possible software project alternatives are complete and management authorizes and commits to funding the project. The Company does not capitalize pilot projects and projects where it believes that the future economic benefits are less than probable.

Goodwill—Goodwill represents the excess purchase price over the value of assets and liabilities assumed in a purchase business combination. In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, Goodwill is not amortized, but tested annually for impairment (in December), or more frequently if certain events having a material impact on the Company’s value occur.

Intangible Assets—Intangible assets are comprised primarily of relationships with the Company’s financial advisors. The relationships with the Company’s financial advisors are amortized over their estimated useful lives of 5 years, and will be tested for potential impairment whenever events or changes in circumstances suggest that an asset’s or asset group’s carrying value may not be fully recoverable in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (“SFAS No. 144”). An impairment loss, calculated as the difference between the estimated fair value and the carrying value of an asset or asset group, is recognized if the estimated fair value is less than the corresponding carrying value.

Fair Value of Financial Instruments—The Company’s financial assets and liabilities are carried at fair value or at amounts that, because of their short-term nature, approximate current fair value. Customer receivables, primarily consisting of floating rate margin loans collateralized by customer securities, are charged interest at rates similar to such other loans made within the industry.

Commitments and Contingencies—The Company recognizes liabilities for contingencies when analysis indicates it is both probable that a liability has been incurred and the amount of loss can be reasonably estimated. When a range of probable loss can be estimated, the Company accrues the most likely amount.

Management evaluates all available evidence about asserted and unsettled income tax contingencies and unasserted income tax contingencies caused by uncertain income tax positions taken in the Company’s income tax returns filed with the Internal Revenue Service and state and local tax authorities.

Contingencies that management believes are estimable and probable of payment, if successfully challenged by such tax authorities, are accrued for under the provisions of SFAS No. 5, *Accounting for Contingencies*.

Drafts Payable—Drafts payable represent customer withdrawals drawn against the Company under a sweep agreement with a bank, which have not yet cleared through the bank.

Legal Reserves—The Company records reserves for legal proceedings in accounts payable and accrued liabilities in the accompanying statement of financial condition. The determination of these reserve amounts requires significant judgment on the part of management. Management considers many factors including, but not limited to, the amount of the claim, the amount of the loss in the client’s account, the basis and validity of the claim, the possibility of wrongdoing on the part of a financial advisor, likely insurance coverage, previous results in similar cases, and legal precedents and case law. Each legal proceeding is reviewed with counsel in each accounting period and the reserve is adjusted as deemed appropriate by management. Any change in the reserve amount is recorded to earnings in such period of change in professional services.

Estimates of Effective Tax Rates, Deferred Taxes and Valuation Allowances—In preparing the financial statement, the Company estimates the income tax expense based on the various jurisdictions where the Company conducts business. The Company must then assess the likelihood that the deferred tax assets will be realized. A valuation allowance is established to the extent that it is more likely than not that such deferred tax assets will not be realized. When the Company establishes a valuation allowance or modifies the existing allowance in a certain reporting period, the Company generally records a corresponding increase or decrease to tax expense. Management makes significant judgments in determining the provision for income taxes, the deferred tax assets and liabilities, and any valuation allowances recorded against the net deferred tax asset. Changes in the estimate of these taxes occur periodically due to changes in the tax rates, changes in the business operations, implementation of tax planning strategies, resolution with taxing authorities of issues where the Company had previously taken tax positions, and newly enacted statutory, judicial, and regulatory guidance. These changes, when they occur, affect accrued taxes and can be material to the Company’s operating results for any particular reporting period.

Income Taxes—The Company is included in the consolidated federal income tax return filed by LPL. Federal income taxes are calculated as if the Company filed on a separate-return basis, and the amount of current tax or benefit calculated is either remitted to or received from LPL. Income taxes are provided for using the liability method, under which deferred tax assets and liabilities are recorded based on differences between the financial accounting and tax bases of assets and liabilities. The amount of current and deferred taxes payable or refundable is recognized as of the date of the financial statement, utilizing currently enacted tax laws and rates. Deferred tax expenses or benefits are recognized in the financial statement for the changes in deferred tax

liabilities or assets. Deferred tax liabilities resulting from the recognition of intangible assets will be amortized simultaneously with those intangible assets through income over their estimated useful life of 15 years.

Recently Issued Accounting Pronouncements—In May 2005, the Financial Accounting Standards Board (“FASB”) issued SFAS No. 154, *Accounting Changes and Error Corrections—a replacement of APB Opinion No. 20 and FASB Statement No. 3* (“SFAS No. 154”). SFAS No. 154 changes the accounting for and reporting of a change in accounting principle. The provisions of SFAS No. 154 require, unless impracticable, retrospective application to prior periods’ financial statements of (1) all voluntary changes in accounting principles and (2) changes required by a new accounting pronouncement, if a specific transition is not provided. SFAS No. 154 also requires that a change in depreciation, amortization, or depletion method for long-lived, nonfinancial assets be accounted for as a change in accounting estimate, which requires prospective application of the new method. SFAS No. 154 is effective for all accounting changes made in fiscal years beginning after December 15, 2005. The implementation of SFAS No. 154 did not have a material impact on our financial statement as no accounting changes have been made since January 1, 2006.

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109* (“FIN 48”). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 requires that the tax effects of a position be recognized only if it is “more-likely-than-not” to be sustained based solely on its technical merits as of the reporting date. The more-likely-than-not threshold represents a positive assertion by management that a company is entitled to the economic benefits of a tax position. If a tax position is not considered more-likely-than-not to be sustained based solely on its technical merits, no benefits of the position are to be recognized. Moreover, the more-likely-than-not threshold must continue to be met in each reporting period to support continued recognition of a benefit. At adoption, companies must adjust their financial statement to reflect only those tax positions that are more-likely-than-not to be sustained as of the adoption date. Any necessary adjustment would be recorded directly to retained earnings in the period of adoption and reported as a change in accounting principle. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is evaluating FIN 48 and has not yet determined the impact of its adoption on its financial statement.

3. RECEIVABLE FROM PRODUCT SPONSORS, BROKER/DEALERS, AND CLEARING ORGANIZATIONS AND PAYABLE TO BROKER/DEALERS AND CLEARING ORGANIZATIONS

At June 30, 2006, the receivable from product sponsors, broker/dealers and clearing organizations and payable to broker/dealers and clearing organizations was as follows (in thousands):

	RECEIVABLE FROM	PAYABLE TO
Securities failed-to-deliver/receive	\$5,301	\$ 8,208
Receivable from/payable to product sponsors and broker/dealers	6,808	4,812
Receivable from/payable to clearing organizations	6,289	2,931
Securities loaned to clearing organization		13,984
Commissions receivable from product sponsors and others	60,413	
	<u>\$78,811</u>	<u>\$29,935</u>

Securities loaned represents amounts due to DTC for collateral received in participation with its securities lending program.

4. SECURITIES OWNED AND SECURITIES SOLD BUT NOT YET PURCHASED

At June 30, 2006, the components of securities owned and securities sold but not yet purchased were as follows (in thousands):

	OWNED	SOLD BUT NOT YET PURCHASED
Marketable Securities at Market Value		
Mutual funds	\$6,032	\$2,443
U.S. government obligations	2,349	
Stocks and warrants	438	18
Certificate of deposits	350	
Variable annuities	209	
Money market funds	77	
Unit investment trusts	45	37
	<u>\$9,500</u>	<u>\$2,498</u>

5. FIXED ASSETS

The components of fixed assets at June 30, 2006, were as follows (in thousands):

Computers and software	\$38,759
Internally developed software	37,173
Leasehold improvements	12,692
Furniture and equipment	10,718
Automobiles	280
Total fixed assets	99,622
Accumulated depreciation and amortization	(60,139)
Fixed assets—net	<u>\$39,483</u>

6. INTANGIBLE ASSETS

Intangible assets representing relationships with independent financial advisors were obtained from LPL through its acquisition of certain broker/dealers in prior years. The Company amortizes such intangible assets over an expected life of approximately 5 years.

7. INCOME TAXES

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

The components of the net deferred tax assets included in the statement of financial condition is presented below (in thousands):

Deferred tax assets:	
Reserves for litigation, vacation, and bonuses	\$ 1,477
Deferred rent	2,259
Provision for bad debts	1,087
Intangible assets	21
Stock-based compensation	2,684
Regulatory fees and related matters	2,361
Total deferred tax assets	<u>9,889</u>
Deferred tax liabilities:	
Fixed assets	7,679
State taxes	119
Other	21
Total deferred tax liabilities	<u>7,819</u>
Deferred income taxes—net	<u><u>\$ 2,070</u></u>

A valuation allowance against deferred tax assets at the balance sheet date is not considered necessary because it is more likely than not the deferred tax asset will be fully realized.

8. BANK LOANS PAYABLE

The Company maintains uncommitted, secured lines of credit totaling \$305.00 million, which did not have outstanding balances at June 30, 2006.

9. COMMITMENTS AND CONTINGENCIES

Leases—The Company leases certain office space and equipment at its headquarter locations under various operating leases. These leases are generally subject to scheduled base rent and maintenance cost increases, which are recognized on a straight-line basis over the period of the leases.

Future minimum payments under leases and lease commitments with remaining terms greater than one year as of June 30, 2006 are approximately as follows (in thousands):

2006—remainder	\$ 4,256
2007	9,053
2008	9,228
2009	9,491
2010	9,508
Thereafter	17,099
	<u><u>\$58,635</u></u>

Guarantees—The Company also provides guarantees to securities clearing houses and exchanges under their standard membership agreements, which require a member to guarantee the performance of other members. Under these agreements, if a member becomes unable to satisfy its obligations to the clearing houses and exchanges, all other members would be required to meet any shortfall. The Company's liability under these arrangements is not quantifiable and may exceed the cash and securities it has posted as collateral. However, the potential requirement for the Company to make payments under these agreements is remote. Accordingly, no liability has been recognized for these transactions.

Litigation—The Company has been named as a defendant in various legal actions, mostly arbitrations. In view of the inherent difficulty of predicting the outcome of such matters, particularly in cases in which claimants seek substantial or indeterminate damages, the Company cannot predict with certainty what the eventual loss or range of loss related to such matters will be. The Company believes, based on current knowledge and after consultation with counsel, and consideration of insurance, if any, that the outcome of such matters will not have a material adverse effect on the financial condition of the Company or its results of operations.

Regulatory—In May 2005, the Company entered into an Acceptance Waiver and Consent ("AWC") with the NASD regarding certain sales of Class B and Class C mutual fund shares. In its investigation, the NASD questioned whether certain sales of Class B and Class C mutual fund shares since January 1, 2002, were appropriate on the basis of cost differences among share classes. The AWC provides for payment to clients impacted by certain transactions and imposition of a monetary penalty. In December 2005, the AWC was counter signed by the NASD. The Company paid a fine in the amount of \$2.40 million and agreed to remediate certain transactions occurring since January 1, 2002, based on the criteria outlined in the AWC. In prior years, the Company had also accrued \$5.36 million for estimated client settlements related to this matter. In June 2006, the Company completed programming required to calculate the actual cost of remediation, which resulted in a change in accounting estimate for the total related settlements of \$(1.19) million. As of June 30, 2006, the Company's remaining accrual was \$2.72 million, which is included in the Company's accrued liabilities in the accompanying statement of financial condition.

Other Commitments—The Company is required to maintain deposits with certain clearing organizations. At June 30, 2006, the Company had pledged \$26.34 million of customer-owned securities on deposit with the Options Clearing Corporation and \$2.44 million of customer-owned securities on deposit with other clearing organizations.

As part of its brokerage operations, the Company periodically enters into when-issued and delayed delivery transactions on behalf of its customers. Settlements of these transactions after June 30, 2006, did not have a material effect on the statement of financial condition of the Company.

10. EMPLOYEE BENEFIT PLANS

The Company has a 401(k) defined contribution plan. All employees meeting minimum age and length of service requirements are eligible to participate. The Company has an employer matching program whereby employer contributions are made to the 401(k) plan in an amount equal to 50% of the lesser of the amount designated by the employee for withholding and contribution to the 401(k) plan or 8% of the employee's total compensation.

Certain employees, officers, and directors also participate in stock option plans (the "Plans") of LPLIH (previously, Plans of the Company). The Plans were assumed by LPLIH in conjunction with the Acquisition and provide for the granting of shares of incentive stock options, shares of nonqualified stock options, and an unspecified number of stock appreciation rights. Stock options granted under the stock option plans have an exercise period of 10 years and generally vest 33-1/3% on the fifth anniversary of the grant date, and an additional 33-1/3% on each of the sixth and seventh anniversaries of that date.

The Plans and the underlying option agreements also provide for accelerated vesting upon certain changes in control, including a public offering. The Acquisition discussed in Note 1 qualified as a change in control event that triggered the acceleration provisions in the Plans. Immediately prior to that transaction and in accordance with the Plans, each employee's unvested stock options became 33-1/3% vested and exercisable with the unvested portion vesting in equal increments on the first and second anniversary dates following. Certain employees and officers of the Company elected to exercise their vested options or convert them along with any unvested options into options for common shares of LPLIH, retaining the same terms and conditions of the original Plans.

11. RELATED-PARTY TRANSACTIONS

The Company provides facilities for and performs certain accounting and management services for the Independent Advisors Group Corporation, a wholly owned subsidiary of LPL. In exchange for these services, the Company receives a monthly administration and per-account fee.

The Company also has an agreement with the Private Trust Company, N.A., ("PTC") an indirect wholly owned subsidiary of LPL, which provides custodial trust services for its individual retirement accounts. In exchange for these services, the Company pays \$125,000 per month.

The Company also receives and pays mortgage brokerage commissions to its financial advisors on mortgage services offered through Innovex Mortgage, Inc., a wholly owned subsidiary of LPL.

12. REGULATORY REQUIREMENTS

As a registered broker/dealer, the Company is subject to the SEC's Uniform Net Capital Rule, which requires the maintenance of minimum net capital. The Company uses the alternative method, permitted by the rule, which requires that it maintain minimum net capital, as defined, equal to the greater of \$250,000 or 2% of aggregate debit balances arising from customers' transactions, as defined. The Company is also subject to the Commodity Futures Trading Commission's minimum financial requirements, which require that it maintain net capital, as defined, equal to 4% of customer funds required to be segregated pursuant to the Commodity Exchange Act, less the market value of certain commodity options, all as defined. At June 30, 2006, the Company had net capital of \$74.34 million, which was \$68.07 million in excess of its minimum required net capital.

13. FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET CREDIT RISK AND CONCENTRATION OF CREDIT RISK

The Company's customer securities activities are transacted on either a cash or margin basis. In margin transactions, the Company extends credit to the customer, subject to various regulatory and internal margin requirements, collateralized by cash and securities in the customer's account. As customers write options contracts or sell securities short, the Company may incur losses if the customers do not fulfill their obligations and the collateral in the clients' accounts is not sufficient to fully cover losses that clients may incur from these strategies. To control this risk, the Company monitors margin levels daily and clients are required to deposit additional collateral, or reduce positions, when necessary.

The Company is obligated to settle transactions with brokers and other financial institutions even if its customers fail to meet their obligation to the Company. Customers are required to complete their transactions on the settlement date, generally three business days after the trade date. If customers do not fulfill their contractual obligations, the Company may incur losses. The Company has established procedures to reduce this risk by generally requiring that customers deposit cash and/or securities into their account prior to placing an order.

The Company may at times maintain inventories in equity securities on both a long and short basis that are recorded on the accompanying statement of financial condition at market value. While long inventory positions represent the Company's ownership of securities, short inventory positions represent obligations of the Company to deliver specified

securities at a contracted price, which may differ from market prices prevailing at the time of completion of the transaction. Accordingly, both long and short inventory positions may result in losses or gains to the Company as market values of securities fluctuate. To mitigate the risk of losses, long and short positions are marked-to-market daily and are continuously monitored by the Company.

14. SUBSEQUENT EVENT

In conjunction with the remediation of certain Class B and Class C share mutual fund transactions (see Note 9 under "Regulatory") as required by the Acceptance Waiver and Consent ("A WC") signed with the NASD, we identified those purchase transactions that according to the terms of that AWC, were eligible for conversion to Class A shares. Clients holding the shares resulting from those transactions were given the opportunity to convert their Class B or Class C shares in accordance with the terms outlined in that AWC. The AWC prescribed the time period during which clients could evaluate and accept the conversion offer. The opportunity to elect conversion expired on July 24, 2006, subsequent to the current reporting period. Based on client responses to the conversion offer, we have determined that our liability for the remaining remediation costs has decreased by approximately \$1.3 million.

The Statement of Financial Condition filed pursuant to Rule 17a-5(e)(3) under the Securities Exchange Act of 1934 and Regulation 1.10(g) under the Commodity Exchange Act is available for inspection at the principal office of the Company and at the Boston Regional Office of the Commission.



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**FINANCIAL
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AP-00223-06