

TD AMERITRADE HOLDING CORP
Form 10-Q
February 05, 2009

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

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended December 31, 2008

OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from _____ to _____

Commission file number: 0-49992

TD AMERITRADE HOLDING CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

82-0543156

(I.R.S. Employer Identification Number)

4211 South 102nd Street, Omaha, Nebraska, 68127

(Address of principal executive offices) (Zip Code)

(402) 331-7856

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months, and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No
As of January 30, 2009, there were 589,318,526 outstanding shares of the registrant's common stock.

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Part I FINANCIAL INFORMATION

Item 1. Financial Statements

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors

TD AMERITRADE Holding Corporation

We have reviewed the condensed consolidated balance sheet of TD AMERITRADE Holding Corporation (the Company) as of December 31, 2008, and the related condensed consolidated statements of income and cash flows for the three-month periods ended December 31, 2008 and 2007. These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of TD AMERITRADE Holding Corporation as of September 30, 2008, and the related consolidated statements of income, stockholders' equity, and cash flows for the year then ended (not presented herein) and in our report dated November 25, 2008, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of September 30, 2008, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ ERNST & YOUNG LLP

Chicago, Illinois

February 5, 2009

TD AMERITRADE HOLDING CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)

	December 31, 2008 (Unaudited)	September 30, 2008
ASSETS		
Cash and cash equivalents	\$ 1,154,155	\$ 674,135
Short-term investments	118,148	369,133
Cash and investments segregated in compliance with federal regulations	1,869,120	260,000
Receivable from brokers, dealers and clearing organizations	1,856,800	4,177,149
Receivable from clients net of allowance for doubtful accounts	4,031,917	6,933,926
Receivable from affiliates	123,200	179,633
Other receivables net of allowance for doubtful accounts	80,716	89,486
Securities owned, at fair value	56,674	60,645
Property and equipment net of accumulated depreciation and amortization	153,622	153,208
Goodwill	1,946,761	1,947,102
Acquired intangible assets net of accumulated amortization	998,141	1,013,679
Deferred income taxes	24,187	17,158
Other investments	11,996	12,768
Other assets	69,785	63,500
Total assets	\$ 12,495,222	\$ 15,951,522
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Payable to brokers, dealers and clearing organizations	\$ 2,221,046	\$ 5,769,676
Payable to clients	5,075,356	5,070,671
Accounts payable and accrued liabilities	641,816	571,425
Payable to affiliates	3,359	3,637
Long-term debt	1,434,625	1,444,000
Capitalized lease obligations	235	544
Deferred income taxes	40,695	166,531
Total liabilities	9,417,132	13,026,484
Stockholders equity:		
Preferred stock, \$0.01 par value; 100 million shares authorized, none issued		
Common stock, \$0.01 par value; one billion shares authorized; 631,381,860 shares issued; December 31, 2008 590,232,231 shares outstanding;		
September 30, 2008 593,130,521 shares outstanding	6,314	6,314

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Additional paid-in capital	1,619,775	1,613,700
Retained earnings	2,070,810	1,886,412
Treasury stock, common, at cost December 31, 2008 41,149,629 shares; September 30, 2008 38,251,339 shares	(617,299)	(580,664)
Deferred compensation	147	146
Accumulated other comprehensive loss	(1,657)	(870)
Total stockholders' equity	3,078,090	2,925,038
Total liabilities and stockholders' equity	\$ 12,495,222	\$ 15,951,522

See notes to condensed consolidated financial statements.

TD AMERITRADE HOLDING CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(In thousands, except per share amounts)

	Three Months Ended December	
	31,	
	2008	2007
Revenues:		
Transaction-based revenues:		
Commissions and transaction fees	\$ 287,113	\$ 260,269
Asset-based revenues:		
Interest revenue	92,514	250,210
Brokerage interest expense	(7,675)	(101,119)
Net interest revenue	84,839	149,091
Money market deposit account fees	163,230	155,840
Investment product fees	69,166	68,005
Total asset-based revenues	317,235	372,936
Other revenues	6,381	8,411
Net revenues	610,729	641,616
Expenses:		
Employee compensation and benefits	117,390	106,015
Fair value adjustments of compensation-related derivative instruments		764
Clearing and execution costs	15,628	12,066
Communications	18,744	17,524
Occupancy and equipment costs	30,127	25,008
Depreciation and amortization	11,503	7,695
Amortization of acquired intangible assets	15,538	13,723
Professional services	27,339	19,282
Interest on borrowings	15,637	25,726
Other	11,564	12,370
Advertising	46,697	45,456
Total expenses	310,167	285,629
Income before other income and income taxes	300,562	355,987
Other income:		
Gain on sale of investments		644

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Pre-tax income	300,562	356,631
Provision for income taxes	116,164	115,792
Net income	\$ 184,398	\$ 240,839
Earnings per share basic	\$ 0.31	\$ 0.40
Earnings per share diluted	\$ 0.31	\$ 0.40
Weighted average shares outstanding basic	591,748	594,915
Weighted average shares outstanding diluted	600,601	604,388

See notes to condensed consolidated financial statements.

TD AMERITRADE HOLDING CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Three Months Ended December	
	31,	
	2008	2007
Cash flows from operating activities:		
Net income	\$ 184,398	\$ 240,839
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	11,503	7,695
Amortization of acquired intangible assets	15,538	13,723
Deferred income taxes	(132,638)	(44,188)
Gain on sale of investments		(644)
Loss on disposal of property	1,273	193
Fair value adjustments of derivative instruments		764
Stock-based compensation	6,382	5,340
Other, net	73	
Changes in operating assets and liabilities:		
Cash and investments segregated in compliance with federal regulations	(1,609,120)	(82,000)
Receivable from brokers, dealers and clearing organizations	2,320,349	607,488
Receivable from clients, net	2,902,009	(1,089,860)
Receivable from/payable to affiliates, net	56,382	(38,798)
Other receivables, net	8,742	(50,065)
Securities owned	3,971	(118,225)
Other assets	(6,285)	(5,160)
Payable to brokers, dealers and clearing organizations	(3,548,630)	852,738
Payable to clients	4,685	(261,515)
Accounts payable and accrued liabilities	70,764	(10,431)
 Net cash provided by operating activities	 289,396	 27,894
 Cash flows from investing activities:		
Purchase of property and equipment	(13,190)	(11,475)
Purchase of short-term investments		(251,740)
Proceeds from sale of short-term investments		328,540
Proceeds from redemption of money market funds	250,934	
Proceeds from sale of other investments available-for-sale	140	4,336
Other		9
 Net cash provided by investing activities	 237,884	 69,670

See notes to condensed consolidated financial statements.

TD AMERITRADE HOLDING CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(Unaudited)
(In thousands)

	Three Months Ended December	
	2008	2007
Cash flows from financing activities:		
Principal payments on long-term debt	\$ (9,375)	\$ (6,250)
Principal payments on capital lease obligations	(309)	(791)
Proceeds from exercise of stock options; Three months ended December 31, 2008 80,976 shares; 2007 1,246,433 shares	372	2,600
Purchase of treasury stock; Three months ended December 31, 2008 2,980,563 shares; 2007 1,030,000 shares	(37,584)	(19,505)
Excess tax benefits on stock-based compensation	271	6,871
 Net cash used in financing activities	 (46,625)	 (17,075)
 Effect of exchange rate changes on cash and cash equivalents	 (635)	 41
 Net increase in cash and cash equivalents	 480,020	 80,530
 Cash and cash equivalents at beginning of period	 674,135	 413,787
 Cash and cash equivalents at end of period	 \$ 1,154,155	 \$ 494,317
 Supplemental cash flow information:		
Interest paid	\$ 30,840	\$ 125,615
Income taxes paid	\$ 109,470	\$ 113,940

See notes to condensed consolidated financial statements.

TD AMERITRADE HOLDING CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
For the Three-Month Periods Ended December 31, 2008 and 2007
(Unaudited)

1. BASIS OF PRESENTATION

The condensed consolidated financial statements include the accounts of TD AMERITRADE Holding Corporation and its wholly-owned subsidiaries (collectively, the Company). Intercompany balances and transactions have been eliminated.

These financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and, in the opinion of management, reflect all adjustments, which are all of a normal recurring nature, necessary to present fairly the financial position, results of operations and cash flows for the periods presented in conformity with U.S. generally accepted accounting principles. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's annual report filed on Form 10-K for the fiscal year ended September 30, 2008.

Reclassifications:

Approximately \$0.2 million has been reclassified from receivable from affiliates to receivable from brokers, dealers and clearing organizations as of September 30, 2008 on the Condensed Consolidated Balance Sheets. Approximately \$15.0 million has been reclassified from payable to affiliates to payable to brokers, dealers and clearing organizations as of September 30, 2008 on the Condensed Consolidated Balance Sheets. Each of the aforementioned reclassifications was made in order to conform to the current financial statement presentation.

Recently Adopted Accounting Pronouncements:

SFAS No. 157 On October 1, 2008, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, for financial assets and liabilities and nonfinancial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis. The Company will not adopt this statement until October 1, 2009 for nonfinancial assets and liabilities that are not recognized or disclosed at fair value in the financial statements on a recurring basis. SFAS No. 157 clarifies the definition of fair value and the methods used to measure fair value and expands disclosures about fair value measurements. The adoption of SFAS No. 157 did not have a material impact on the Company's financial position, results of operations or cash flows. See Note 10 FAIR VALUE DISCLOSURES for additional information.

Recently Issued Accounting Pronouncements:

SFAS No. 141R In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 141 (revised 2007), *Business Combinations*. SFAS No. 141R generally requires an acquirer to recognize the identifiable assets acquired, liabilities assumed, contingent purchase consideration and any noncontrolling interest in the acquiree at fair value on the date of acquisition. It also requires an acquirer to recognize as expense most transaction and restructuring costs as incurred, rather than include such items in the cost of the acquired entity. For the Company, SFAS No. 141R will apply prospectively to business combinations for which the acquisition date is on or after October 1, 2009. The Company will evaluate the impact of SFAS No. 141R on any potential future business combinations that may occur on or after the effective date.

2. BUSINESS COMBINATIONS

On January 8, 2009, the Company entered into a definitive agreement to acquire thinkorswim Group Inc. (thinkorswim) for approximately 28 million shares of Company common stock and approximately \$225 million in cash. thinkorswim offers online brokerage, investor education and related financial products and services for self-directed investors and active traders. Upon the closing of the acquisition, each share of thinkorswim common stock will be exchanged for \$3.34 in cash and 0.3980 shares of the Company's common stock. In connection with the acquisition, the Company also announced its intent to initiate a new stock repurchase program that will equal the approximately 28 million shares issued in the acquisition. The closing of the acquisition is subject to customary conditions, including regulatory and thinkorswim stockholder approvals, and is expected to occur during fiscal 2009.

On February 4, 2008, the Company completed the acquisition of Fiserv Trust Company, an investment support services business and wholly-owned subsidiary of Fiserv, Inc. (Fiserv). The Company paid \$274.5 million in cash during fiscal 2008 for this acquisition. Pursuant to the stock purchase agreement, an additional earn-out payment of up to \$100 million in cash could be payable following the first anniversary of the acquisition based on the achievement of revenue targets. Based on revenues through December 31, 2008, the Company expects the earn-out payment to be between \$40 million and \$45 million. The Company's condensed consolidated financial statements include the results of operations for Fiserv Trust Company beginning February 5, 2008.

3. GOODWILL AND ACQUIRED INTANGIBLE ASSETS

The Company has recorded goodwill for purchase business combinations to the extent the purchase price of each completed acquisition exceeded the fair value of the net identifiable tangible and intangible assets of each acquired company. The following table summarizes changes in the carrying amount of goodwill for the three months ended December 31, 2008 (dollars in thousands):

Balance as of September 30, 2008	\$ 1,947,102
Purchase accounting adjustments, net of income taxes (1)	(330)
Tax benefit of option exercises (2)	(11)
Balance as of December 31, 2008	\$ 1,946,761

(1) Purchase accounting adjustments primarily consist of adjustments to liabilities related to the acquisition of Fiserv Trust Company in fiscal 2008.

(2) Represents the tax benefit of exercises of replacement stock options that were issued in connection with the Datek Online Holdings Corp. merger in fiscal 2002. The tax benefit of an option exercise is recorded as a

reduction of goodwill to the extent the Company recorded fair value of the replacement option in the purchase accounting. To the extent any gain realized on an option exercise exceeds the fair value of the replacement option recorded in the purchase accounting, the tax benefit on the excess is recorded as additional paid-in capital.

The Company's acquired intangible assets consist of the following as of December 31, 2008 (dollars in thousands):

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Client relationships	\$ 1,062,046	\$ (209,579)	\$ 852,467
Trademark license	145,674		145,674
Totals	\$ 1,207,720	\$ (209,579)	\$ 998,141

The Company estimates that amortization expense on acquired intangible assets outstanding as of December 31, 2008 will be approximately \$46.2 million for the remainder of fiscal 2009 and approximately \$61.6 million for each of the five succeeding fiscal years.

4. CASH AND CASH EQUIVALENTS

The Company's cash and cash equivalents is summarized in the following table (dollars in thousands):

	December 31, 2008	September 30, 2008
Corporate	\$ 203,883	\$ 184,632
Broker-dealer subsidiaries	838,061	418,626
Trust company subsidiaries	99,173	61,430
Investment advisory subsidiaries	13,038	9,447
Total	\$ 1,154,155	\$ 674,135

Capital requirements may limit the amount of cash available for dividend from the broker-dealer and trust company subsidiaries to the parent company. Cash and cash equivalents of the investment advisory subsidiaries is generally not available for corporate purposes.

5. SHORT-TERM INVESTMENTS

Short-term investments consist of the following (dollars in thousands):

	December 31, 2008	September 30, 2008
Money market mutual funds	\$ 117,051	\$ 368,066
Federal National Mortgage Association discount notes	1,097	1,067
Total short-term investments	\$ 118,148	\$ 369,133

As of September 30, 2008, the Company had holdings with a fair value of approximately \$585.5 million in the Primary Fund, a money market mutual fund managed by The Reserve, an independent mutual fund company. In September 2008, the net asset value of the Primary Fund declined below \$1.00 per share and the fund announced it was liquidating under the supervision of the SEC. In order to facilitate an orderly liquidation, the SEC allowed the fund to suspend redemptions until the fund could liquidate portfolio securities without further impairing the net asset value. As of September 30, 2008, the Company classified approximately \$217.4 million of its Primary Fund holdings as cash and cash equivalents, based on its estimated share of the partial redemption. The remaining \$368.1 million of the Company's Primary Fund holdings was reclassified to short-term investments, due to uncertainty as to whether these holdings could be converted to cash within three months. During the first quarter of fiscal 2009, the Company received \$468.4 million of cash as The Reserve redeemed approximately 79% of the shares of the fund. The Company's remaining Primary Fund holdings with a fair value of \$117.1 million remain classified as short-term investments, due to uncertainty as to whether the holdings can be converted to cash within three months.

6. ACQUISITION EXIT LIABILITIES

The following table summarizes activity in the Company's acquisition exit liabilities, which are included in accounts payable and accrued liabilities in the Condensed Consolidated Balance Sheets (dollars in thousands):

	Three Months Ended December 31, 2008		
	Balance at Sept. 30, 2008	Utilized	Balance at Dec. 31, 2008
Employee compensation and benefits	\$ 2,575	\$ (249)	\$ 2,326

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Occupancy and equipment costs	12,742	(510)	12,232
Total acquisition exit liabilities	\$ 15,317	\$ (759)	\$ 14,558

The exit liabilities primarily relate to the acquisition of TD Waterhouse Group, Inc. (TD Waterhouse) during fiscal 2006. Employee compensation exit liabilities are expected to be paid over contractual periods ending in fiscal 2013. Remaining occupancy and equipment exit liabilities are expected to be utilized over the related lease periods through fiscal 2016.

7. INCOME TAXES

The Company's effective income tax rate for the three months ended December 31, 2008 was 38.6%, compared to 32.5% for the three months ended December 31, 2007. The provision for income taxes for the three months ended December 31, 2007 was unusually low due to \$7.2 million of favorable resolutions of state income tax matters and \$11.1 million of adjustments to current and deferred income taxes resulting from a revision to estimated state income tax expense. The revision was based on the Company's actual state income tax returns filed for calendar year 2006 and similar adjustments applied to estimated state income tax rates for 2007 and future years. These items favorably impacted the Company's earnings for the three months ended December 31, 2007 by approximately \$0.03 per share.

8. CAPITAL REQUIREMENTS

The Company's broker-dealer subsidiaries are subject to the SEC Uniform Net Capital Rule (Rule 15c3-1 under the Securities Exchange Act of 1934 (the Exchange Act)), which requires the maintenance of minimum net capital, as defined. Net capital is calculated for each broker-dealer subsidiary individually. Excess net capital of one broker-dealer subsidiary may not be used to offset a net capital deficiency of another broker-dealer subsidiary. Net capital and the related net capital requirement may fluctuate on a daily basis.

Net capital and net capital requirements for the Company's broker-dealer subsidiaries are summarized in the following table (dollars in thousands):

	December 31, 2008			September 30, 2008		
	Net Capital	Minimum Net Capital Required	Excess Net Capital	Net Capital	Minimum Net Capital Required	Excess Net Capital
TD AMERITRADE Clearing, Inc.	\$ 1,087,338	\$ 92,187	\$ 995,151	\$ 836,531	\$ 157,458	\$ 679,073
TD AMERITRADE, Inc.	63,049	500	62,549	44,039	250	43,789
Totals	\$ 1,150,387	\$ 92,687	\$ 1,057,700	\$ 880,570	\$ 157,708	\$ 722,862

TD AMERITRADE Clearing, Inc. (TDA Clearing) is a clearing broker-dealer and TD AMERITRADE, Inc. (TDA Inc.) is an introducing broker-dealer.

The Company's non-depository trust company subsidiary, TD AMERITRADE Trust Company (TDATC), is subject to capital requirements established by the State of Maine, which requires TDATC to maintain minimum Tier 1 capital, as defined. TDATC's Tier 1 capital was \$111.3 million and \$112.4 million as of December 31, 2008 and September 30, 2008, respectively, which exceeded the required Tier 1 capital by \$101.3 million and \$102.4 million, respectively.

9. COMMITMENTS AND CONTINGENCIES

Spam Litigation A purported class action, captioned *Elvey v. TD Ameritrade, Inc.*, was filed on May 31, 2007 in the United States District Court for the Northern District of California. The complaint alleges that there was a breach in TDA Inc.'s systems, which allowed access

to e-mail addresses and other personal information of account holders, and that as a result account holders received unsolicited e-mail from spammers promoting certain stocks and have been subjected to an increased risk of identity theft. The complaint requests unspecified damages and injunctive and other equitable relief. A second lawsuit, captioned *Zigler v. TD Ameritrade, Inc.*, was filed on September 26, 2007, in the same jurisdiction on behalf of a purported nationwide class of account holders. The factual allegations of the complaint and the relief sought are substantially the same as those in the first lawsuit. The cases were consolidated under the caption *In re TD Ameritrade Accountholders Litigation*. The Company hired an independent consultant to investigate whether identity theft occurred as a result of the breach. The consultant has conducted four investigations since August 2007 and reported that it found no evidence of identity theft. The parties entered into an agreement to settle the lawsuits on a class basis subject to court approval. A hearing on a motion requesting preliminary approval of the proposed settlement was held

on June 12, 2008. The court denied the motion without prejudice. After additional submissions were made by the parties, the Court held a further hearing on October 7, 2008. The Court has not yet issued a ruling on the matter.

Auction Rate Securities Matters Beginning in March 2008, lawsuits were filed against various financial services firms by customers related to their investments in auction rate securities (ARS). The plaintiffs in these lawsuits allege that the defendants made material misrepresentations and omissions in statements to customers about investments in ARS and the manner in which the ARS market functioned in violation of provisions of the federal securities laws. Two purported class

action complaints have been filed alleging such conduct with respect to TDA Inc. and TD AMERITRADE Holding Corporation. The putative class actions are captioned *Humphrys v. TD Ameritrade Holding Corp. et al.* and *Silverstein v. TD Ameritrade Holding Corp. et al.* The complaints seek an unspecified amount of compensatory damages, injunctive relief, interest and attorneys' fees. Both cases are pending in the U.S. District Court for the Southern District of New York. A motion was filed by some plaintiffs requesting that the proceedings in the lawsuits against the various financial services firms in effect be consolidated for pretrial proceedings before one judge. The Company and parties in other cases filed oppositions to the motion. The Judicial Panel on Multidistrict Litigation denied the motion in October 2008.

The SEC and other regulatory authorities are conducting investigations regarding the sale of ARS. TDA Inc. has received subpoenas and other requests for documents and information from the regulatory authorities. The Company is cooperating with the investigations and requests. The Company and regulatory authorities are in discussions regarding the possible resolution of the investigations with respect to TDA Inc., which could include the Company offering to purchase certain client ARS over time. As of February 2, 2009, the Company's clients held ARS with an aggregate par value of approximately \$694 million in TDA Inc. accounts, including \$192 million custodied for clients of independent registered investment advisors.

Reserve Fund Matters During September 2008, The Reserve, an independent mutual fund company, announced that the net asset value of two of its money market mutual funds (the Primary Fund and the International Liquidity Fund) declined below \$1.00 per share. In addition, The Reserve announced that the net asset value of the Reserve Yield Plus Fund, which is not a money market mutual fund but sought to maintain a stable net asset value of \$1.00 per share, declined below \$1.00 per share. TDA Inc.'s clients hold shares in these funds, which The Reserve announced are being liquidated. From October 31, 2008 through February 2, 2008, Primary Fund, International Liquidity Fund and Yield Plus Fund shareholders have received distributions totaling approximately \$0.79 per share, \$0.65 per share and \$0.69 per share, respectively. The SEC and other regulatory authorities are conducting investigations regarding TDA Inc.'s offering of The Reserve funds to clients. TDA Inc. has received subpoenas and other requests for documents and information from the regulatory authorities. TDA Inc. is cooperating with the investigations and requests.

In November and December 2008 two purported class action lawsuits were filed with respect to the Yield Plus Fund. The lawsuits are captioned *Ross v. Reserve Management Company, Inc. et al.* in the U.S. District Court for the Southern District of New York and *Hamilton v. TD Ameritrade, Inc. et al.* in the U.S. District Court for the Northern District of Georgia. The lawsuits are on behalf of persons who purchased shares of Reserve Yield Plus Fund. Both complaints name as defendants a number of entities and individuals related to The Reserve. The Company is named as a defendant in both cases and TDA Inc. is named as a defendant in the Hamilton case. The complaints allege claims of violations of the federal securities laws and other claims based on allegations that false and misleading statements and omissions were made in the Reserve Yield Plus Fund prospectus and in other statements regarding the fund. The complaints seek an unspecified amount of compensatory damages, interest and attorneys' fees.

Other Legal and Regulatory Matters The Company is subject to lawsuits, arbitrations, claims and other legal proceedings in connection with its business. Some of the legal actions include claims for substantial or unspecified compensatory and/or punitive damages. A substantial adverse judgment or other unfavorable resolution of these matters could have a material adverse effect on the Company's financial condition, results of operations and cash flows. Management believes the Company has adequate legal defenses with respect to the legal proceedings to which it is a defendant or respondent and the outcome of these pending proceedings is not likely to have a material adverse effect on the financial condition, results of operations or cash flows of the Company. However, the Company is unable to predict the outcome of these matters.

In the normal course of business, the Company discusses matters with its regulators raised during regulatory examinations or otherwise subject to their inquiry. These matters could result in censures, fines or other sanctions. Management believes the outcome of any resulting actions will not be material to the Company's financial condition, results of operations or cash flows. However, the Company is unable to predict the outcome of these matters.