

LABRANCHE & CO INC  
Form 10-Q  
November 10, 2008  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

**x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 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: 001-15251

**LABRANCHE & Co INC.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**13-4064735**  
(I.R.S. Employer  
Identification No.)

**33 Whitehall Street, New York, New York 10004**  
(Address of principal executive offices) (Zip Code)

**(212) 425-1144**  
(Registrant's telephone number, including area code)

**Not Applicable**  
(Former name, former address and former fiscal year, if changed since last report)

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 definition 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  (Do not check if a smaller reporting company)

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

The number of shares of the registrant's common stock outstanding as of November 7, 2008 was 60,347,426.

**Table of Contents**

**TABLE OF CONTENTS**

<u>PART I FINANCIAL INFORMATION</u>	3
<u>Item 1. Financial Statements</u>	3
<u>CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS</u>	3
<u>CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION</u>	4
<u>CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY AND COMPREHENSIVE LOSS</u>	5
<u>CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS</u>	6
<u>NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS</u>	7
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	22
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	47
<u>Item 4. Controls and Procedures</u>	55
<u>PART II OTHER INFORMATION</u>	55
<u>SIGNATURES</u>	58

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements.****LaBRANCHE & CO INC. and SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(000 s omitted except per share data)****(unaudited)**

	<b>For the Three Months Ended September 30,</b>		<b>For the Nine Months Ended September 30,</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
<b>REVENUES:</b>				
Net gain on principal transactions	\$ 84,634	\$ 33,345	\$ 189,731	\$ 146,278
Commissions and other fees	10,890	11,070	30,849	35,757
Net (loss) gain on investments	(35,343)	17,398	(153,112)	(41,130)
Interest income	16,129	54,874	63,523	186,879
Other	1,000	1,187	2,403	2,470
<b>Total revenues</b>	<b>77,310</b>	<b>117,874</b>	<b>133,394</b>	<b>330,254</b>
<b>Interest expense:</b>				
Debt	6,455	12,333	25,822	38,210
Inventory financing	23,841	63,825	75,461	213,628
<b>Total interest expense</b>	<b>30,296</b>	<b>76,158</b>	<b>101,283</b>	<b>251,838</b>
<b>Total revenues, net of interest expense</b>	<b>47,014</b>	<b>41,716</b>	<b>32,111</b>	<b>78,416</b>
<b>EXPENSES:</b>				
Employee compensation and related benefits	34,955	13,522	83,079	61,608
Exchange, clearing and brokerage fees	12,357	10,062	32,758	29,713
Lease of exchange memberships and trading license fees	429	614	1,272	1,926
Depreciation and amortization	925	1,000	2,722	8,128
Goodwill impairment				164,100
Specialist stock list impairment				335,264
Restructuring costs		25		1,098
Early extinguishment of debt			6,005	
Other	7,215	9,587	21,483	29,152
<b>Total expenses</b>	<b>55,881</b>	<b>34,810</b>	<b>147,319</b>	<b>630,989</b>
(Loss) income before (benefit) provision for income taxes	(8,867)	6,906	(115,208)	(552,573)
<b>(BENEFIT) PROVISION FOR INCOME TAXES</b>	<b>(3,280)</b>	<b>903</b>	<b>(48,046)</b>	<b>(184,077)</b>
(Loss) income applicable to common stockholders	\$ (5,587)	\$ 6,003	\$ (67,162)	\$ (368,496)
<b>Weighted-average common shares outstanding:</b>				
Basic	61,946	61,471	61,931	61,404
Diluted	61,946	61,645	61,931	61,404
(Loss) income per share:				

Edgar Filing: LABRANCHE & CO INC - Form 10-Q

Basic	\$ (0.09)	\$ 0.10	\$ (1.08)	\$ (6.00)
Diluted	\$ (0.09)	\$ 0.10	\$ (1.08)	\$ (6.00)

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

**Table of Contents****LaBRANCHE & CO INC. and SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

(000 s omitted except per share data)

	As of	
	September 30, 2008 (unaudited)	December 31, 2007 (1) (audited)
<b>ASSETS</b>		
Cash and cash equivalents	\$ 227,920	\$ 504,654
Cash and securities segregated under federal regulations	1,471	1,573
Receivable from brokers, dealers and clearing organizations	91,842	343,729
Financial instruments owned, at fair value	3,867,064	4,267,395
Commissions and other fees receivable		23
Exchange memberships owned, at adjusted cost (market value of \$6,705 and \$7,790 at September 30, 2008 and December 31, 2007, respectively)	1,315	1,315
Office equipment and leasehold improvements, at cost, less accumulated depreciation and amortization of \$13,416 and \$10,990 at September 30, 2008 and December 31, 2007, respectively	16,716	17,652
Intangible assets:		
Trade name	25,011	25,011
Goodwill	84,218	84,218
Income tax receivable	502	11,802
Other assets	41,898	41,219
<b>Total assets</b>	<b>\$ 4,357,957</b>	<b>\$ 5,298,591</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Liabilities:		
Payable to brokers, dealers and clearing organizations	\$ 412,783	\$ 104,759
Payable to customers	36	93
Financial instruments sold, but not yet purchased, at fair value	3,172,981	4,062,995
Accrued compensation	37,310	16,729
Accounts payable and other accrued expenses	35,039	36,980
Other liabilities	12,363	12,583
Deferred tax liabilities, net	17,578	71,024
Short term debt		5,700
Long term debt	209,888	459,811
<b>Total liabilities</b>	<b>3,897,978</b>	<b>4,770,674</b>
Commitments and contingencies		
Common stock, \$.01 par value, 200,000,000 shares authorized; 61,993,216 shares issued , 61,621,463 shares outstanding at September 30, 2008 and 61,490,638 shares issued and outstanding December 31, 2007	620	615
Treasury stock, 371,753 shares at September 30, 2008	(1,640)	
Additional paid-in capital	701,441	699,099
Accumulated other comprehensive loss	(2,472)	(989)
Accumulated deficit	(237,970)	(170,808)
<b>Total stockholders equity</b>	<b>459,979</b>	<b>527,917</b>
<b>Total liabilities and stockholders equity</b>	<b>\$ 4,357,957</b>	<b>\$ 5,298,591</b>

- (1) Certain of the Company's December 31, 2007 balances have been reclassified to conform to the presentation in the current period, deferred tax assets were netted against deferred tax liabilities and certain non-marketable investments were re-classed from Financial instruments owned, at fair value to Other assets. These reclassifications did not affect stockholders' equity or earnings.  
The accompanying notes are an integral part of these condensed consolidated financial statements.

**Table of Contents**

**LaBRANCHE & CO INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN**  
**STOCKHOLDERS EQUITY AND COMPREHENSIVE LOSS**

(000 s omitted)

	Common Stock Shares	Common Stock Amount	Treasury Stock	Additional Paid-in Capital	Retained (Deficit) Earnings	Accumulated Other Comprehensive Loss	Total
BALANCE, December 31, 2006	60,734	\$ 607	\$	\$ 694,434	\$ 179,666	\$	\$ 874,707
Net loss					(350,474)		(350,474)
Other comprehensive loss:							
Cumulative translation adjustment, net of taxes						(989)	(989)
Comprehensive loss							(351,463)
Issuance of restricted stock, shares for option exercises and related compensation, including excess tax benefit of \$99	757	8		4,665			4,673
BALANCE, December 31, 2007	61,491	\$ 615	\$	\$ 699,099	\$ (170,808)	\$ (989)	\$ 527,917
Net loss					(67,162)		(67,162)
Other comprehensive loss:							
Cumulative translation adjustment, net of taxes						(1,483)	(1,483)
Comprehensive loss							(68,645)
Treasury stock		(372)	(1,640)				(1,640)
Issuance of restricted stock, shares for option exercises and related compensation	502	5		2,342			2,347
BALANCE, September 30, 2008 (unaudited)	61,621	\$ 620	\$ (1,640)	\$ 701,441	\$ (237,970)	\$ (2,472)	\$ 459,979

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



**Table of Contents****LaBRANCHE & CO INC. and SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(000 s omitted)

	<b>Nine Months Ended September 30,</b>	
	<b>2008</b>	<b>2007</b>
	<b>(unaudited)</b>	<b>(unaudited)</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (67,162)	\$ (368,496)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	2,722	8,128
Amortization of debt issuance costs and bond discount	995	1,503
Charge on early extinguishment of debt	6,005	
Stock-based compensation expense	3,143	3,652
Deferred tax benefit	(53,446)	(172,051)
Goodwill impairment		164,100
Stock list impairment		335,264
Changes in operating assets and liabilities:		
Cash and securities segregated under federal regulations	102	5,972
Securities purchased under agreements to resell		35,000
Receivable from brokers, dealers and clearing organizations	251,887	(669,728)
Receivable from customers		2,859
Financial instruments owned, at fair value	400,331	222,693
Commissions and other fees receivable	23	3,543
Income tax receivable	10,504	(10,850)
Other assets	(4,595)	3,067
Payable to brokers, dealers and clearing organizations	308,024	(33,392)
Payable to customers	(57)	(4,718)
Financial instruments sold, but not yet purchased, at fair value	(890,014)	483,634
Accrued compensation	20,581	(3,871)
Accounts payable and other accrued expenses	(1,941)	5,809
Other liabilities	(220)	(1,365)
Excess tax benefit from vesting of stock based compensation		(99)
Net cash (used in) provided by operating activities	(13,118)	10,654
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Payments for purchases of office equipment and leasehold improvements	(1,786)	(3,086)
Payments for purchases of exchange memberships		(1)
Proceeds from sale of business unit		2,250
Net cash used in investing activities	(1,786)	(837)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Principal payments of short term debt	(5,700)	(25,338)
Early extinguishment of long term debt	(249,923)	
Premium on early extinguishment of debt	(3,739)	
Purchases of treasury stock	(1,640)	
Excess tax benefit from vesting of stock based compensation		99
Net cash used in financing activities	(261,002)	(25,239)

Edgar Filing: LABRANCHE & CO INC - Form 10-Q

Effect of exchange rate changes on cash and cash equivalents	(828)	
Decrease in cash and cash equivalents	(276,734)	(15,422)
CASH AND CASH EQUIVALENTS, beginning of period	504,654	557,352
<b>CASH AND CASH EQUIVALENTS, end of period</b>	<b>\$ 227,920</b>	<b>\$ 541,930</b>

**SUPPLEMENTAL DISCLOSURE OF CASH PAID DURING THE PERIOD FOR:**

Interest	\$ 96,325	\$ 243,546
Income taxes	\$ 2,093	\$ 2,554

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

---

**Table of Contents**

**LaBRANCHE & CO INC. and SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(UNAUDITED)**

**1. ORGANIZATION AND DESCRIPTION OF BUSINESS**

The condensed consolidated financial statements include the accounts of LaBranche & Co Inc., a Delaware corporation (the Holding Company ), and its subsidiaries, LaBranche & Co. LLC, a New York limited liability company, LaBranche Financial Services, LLC, a New York limited liability company ( LFS ), LaBranche Structured Holdings, Inc., a Delaware corporation ( LSHI ), LABDR Services, Inc., a Delaware corporation ( LABDR ), and LaBranche & Co. B.V., a Netherlands private limited liability company ( BV ). The Holding Company is the sole member of LaBranche & Co. LLC and LFS, the 100% stockholder of LSHI and LABDR and the sole owner of BV. LSHI is a holding company that is the sole member of LaBranche Structured Products, LLC, a New York limited liability company ( LSP ), and LaBranche Structured Products Specialists LLC, a New York limited liability company ( LSPS ), the 100% owner of LaBranche Structured Products Europe Limited, a United Kingdom single member private company ( LSPE ), and LaBranche Structured Products Hong Kong Limited, a Hong Kong single member private company ( LSPH ), and the sole stockholder of LaBranche Structured Products Direct, Inc., a New York corporation ( LSPD ) and collectively with the Holding Company, LaBranche & Co. LLC, LFS, LSHI, LABDR, BV, LSP, LSPS, LSPE, LSPD and LSPH, the Company ).

LaBranche & Co. LLC is a registered broker-dealer that operates primarily as a specialist in equity securities and rights listed on the New York Stock Exchange ( NYSE ). LFS is a registered broker-dealer and a member of the NYSE and other exchanges and primarily provides securities execution and brokerage services to institutional investors. LSP is a registered broker-dealer that operates as a specialist in options, futures and Exchange-Traded Funds ( ETFs ) on several exchanges, and as a market-maker in options, ETFs and futures on several exchanges. LSPE operates as a market-maker for ETFs traded on the London Stock Exchange and the Euroex and Euronext exchanges, and is registered as a broker-dealer with the United Kingdom s Financial Services Authority. LSPH is registered as a market-maker for ETFs in Hong Kong and is registered as a broker-dealer with Hong Kong s Securities and Futures Commission. LSPD is a registered broker-dealer and Financial Industry Regulatory Authority ( FINRA ) member firm that is primarily an institutional execution firm in equities and structured products. LABDR is an investment company with a minority ownership in a New Jersey aviation partnership. BV represented LaBranche & Co. LLC in European markets and provided client services to LaBranche & Co. LLC s European listed companies until June 30, 2007, when it ceased operations. LSPS has been inactive since October 31, 2007.

## **Table of Contents**

### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### ***Basis of Presentation***

Certain of the Company's December 31, 2007 statement of financial condition balances have been reclassified to conform to the presentation in the current period. Pursuant to Statement of Financial Accounting Standard (SFAS) No. 109, Accounting for Income Taxes, the Company netted its deferred tax assets against deferred tax liabilities by taxing jurisdiction to determine net deferred taxes. The Company also re-classed certain non-marketable investments from Financial instruments owned, at fair value to Other assets. These reclassifications did not affect previously reported net income before provision for income taxes, net income applicable to common stockholders or stockholders' equity.

#### ***Cash and Cash Equivalents***

Cash and cash equivalents include all demand deposits held in banks, highly liquid investments with original maturities of 90 days or less and currency positions that are being held in the prime brokerage account at the Company's clearing broker for its specialist and market-making operations. Certain portions of these balances are used to meet regulatory requirements (see Note 5).

#### ***Use of Estimates***

The use of generally accepted accounting principles requires management to make certain estimates and assumptions. In addition to the estimates we make in connection with fair value measurements and the accounting for goodwill and identifiable intangible assets, the use of estimates and assumptions is also important in determining provisions for potential losses that may arise from litigation and regulatory proceedings and tax audits. Actual results could differ from these estimates.

A substantial portion of our compensation and benefits represents discretionary bonuses, which are determined at year end. We believe the most appropriate way to allocate estimated annual discretionary bonuses among interim periods is in proportion to the net revenues earned in such periods. In addition to the level of net revenues, our overall compensation expense in any given year is also influenced by, among other factors, prevailing labor markets, business mix and the structure of our share-based compensation programs.

#### ***Adoption of SFAS No. 157 Fair Value Measurements***

The Company adopted SFAS No. 157, Fair Value Measurements (SFAS No. 157), as of January 1, 2008. SFAS No. 157 defines fair value, expands disclosure requirements around fair value and specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions (see Note 11).

### **3. INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND FINANCIAL INFORMATION**

The unaudited interim condensed consolidated financial information as of September 30, 2008 and for the three and nine months ended September 30, 2008 and 2007 is presented in the accompanying condensed consolidated financial statements. The unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the

**Table of Contents**

instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial information. The unaudited interim condensed consolidated financial information reflects all adjustments which are, in the opinion of management, necessary for a fair presentation of the results for such periods. The preparation of condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates and assumptions. The unaudited interim condensed consolidated financial information as of September 30, 2008 and for the three and nine months ended September 30, 2008 should be read in conjunction with the audited consolidated financial statements and notes thereto as of December 31, 2007 included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007 filed with the Securities and Exchange Commission (SEC) on March 17, 2008 (the 2007 10-K). Results of the third quarter 2008 interim period are not necessarily indicative of results to be obtained for the full fiscal year.

**4. INCOME TAXES**

The Company accounts for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes and FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48). SFAS No. 109 requires the recognition of tax benefits or expenses based on the estimated future tax effects of temporary differences between the financial statement and tax bases of its assets and liabilities. Deferred tax assets and liabilities primarily relate to tax basis differences on unrealized gains on corporate equities, not readily marketable, stock-based compensation, other compensation accruals, amortization periods of certain intangible assets and differences between the financial statement and tax bases of assets acquired.

The components of the provision for income taxes reflected on the condensed consolidated statements of operations are set forth below (000's omitted):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Current federal, state and local taxes	\$ 3,060	\$ (7,176)	\$ 4,073	\$ (12,026)
Deferred tax (benefit) provision	(6,340)	8,079	(52,119)	(172,051)
Total (benefit) provision for income taxes	\$ (3,280)	\$ 903	\$ (48,046)	\$ (184,077)

Included in the current federal, state and local taxes are foreign taxes of \$0.2 million and \$1.5 million for the three and nine months ended September 30, 2008 respectively. The foreign taxes represent taxes payable to the United Kingdom for LSPE the Company's single member private equity company in the UK that is a controlled foreign corporation as of January 1, 2008.

**Table of Contents**

The Company has a \$4.1 million federal net operating loss carryforward from 2007 expiring in 2027. In addition, the Company has the following state and city net operating loss carryforwards (000 s omitted):

Year	NYS	NYC	Expiring
2004	\$ 20,549	\$ 18,083	2024
2007	\$ 34,478	\$ 34,681	2027

During the third quarter the Company completed a multi year tax audit with the local taxing authorities resulting in a \$1.6 million payment for that period for both taxes and interest. This resulted in a \$2.1 million reduction in our FIN 48 reserve balances of which \$0.5 million was recorded as a tax benefit in the current quarter.

**5. CAPITAL AND NET LIQUID ASSET REQUIREMENTS**

LaBranche & Co. LLC, as a specialist and member of the NYSE, is subject to the provisions of SEC Rule 15c3-1, as adopted and administered by the SEC and NYSE. LaBranche & Co. LLC is required to maintain minimum net capital, as defined, equivalent to the greater of \$100,000 or <sup>1</sup>/<sub>15</sub> of aggregate indebtedness, as defined.

As of September 30, 2008 and December 31, 2007, LaBranche & Co. LLC s net capital, as defined under SEC Rule 15c3-1, was \$103.9 million and \$306.8 million, respectively, which exceeded the minimum requirements by \$102.9 million and \$306.4 million, respectively. LaBranche & Co. LLC s aggregate indebtedness to net capital ratio on those dates was 0.14 to 1 and 0.02 to 1, respectively.

The NYSE generally requires its specialist firms to maintain a minimum dollar regulatory capital amount in order to establish that they can meet, with their own Net Liquid Assets ( NLA ), their position requirement. As of September 30, 2008 LaBranche & Co. LLC s NYSE minimum required dollar amount of NLA, as defined, was \$76.1 million and its actual NLA, as defined, was \$88.9 million. As of December 31, 2007, LaBranche & Co. LLC s NYSE minimum required dollar amount of NLA, as defined was \$276.2 million, and LaBranche & Co. LLC s actual NLA, as defined was \$300.1 million. As of September 30, 2008 and December 31, 2007, LaBranche & Co. LLC s actual NLA exceeded the NLA requirement, thus satisfying its NLA requirement as of each of those dates. LaBranche & Co. LLC s NLA as of September 30, 2008 and December 31, 2007 included approximately \$32.8 million and \$74.7 million, respectively, in NYX shares (after the risk-based haircuts required to be taken in connection with those securities).

The minimum required dollar amount of NLA fluctuates daily and is computed by adding two components. The first component is equal to \$0.25 million for each one tenth of one percent (0.1%) of the aggregate NYSE transaction dollar volume in a cash equities specialist organization s allocated securities, as adjusted at the beginning of each month based on the prior month transaction dollar volume. Prior to February 8, 2008 the first component was equal to \$1.0 million for each one tenth of one percent (0.1%). The second component is calculated either by multiplying the average haircuts on a specialist organization s proprietary positions over the most recent twenty days by three, or by using an NYSE-approved value at

---

**Table of Contents**

risk ( VAR ) model. Based on this two part calculation, LaBranche & Co. LLC s NLA requirement could increase or decrease in future periods based on its own trading activity and all other specialists trading as a respective percentage of overall NYSE transaction dollar volume. In February 2008, pursuant to the SEC approved reduction in the NLA requirement LaBranche & Co. LLC s NLA requirement was reduced by approximately \$205.0 million. The majority of the amended NLA requirement is met by the shares of NYSE Euronext, Inc. common stock (the NYX shares ) held by LaBranche & Co. LLC. The amended NLA requirements enabled LaBranche & Co. LLC to make a dividend distribution of \$200.0 million to LaBranche & Co Inc. in the first quarter of 2008. LaBranche & Co. LLC has approximately \$56.1 million in cash and other liquid assets over and above the NYX shares used to meet its continuing NLA requirements. This \$56.1 million includes a cushion over and above the required NLA to account for potential fluctuations in LaBranche & Co. LLC s NLA requirement, as well as fluctuations in the fair value of its NYX shares, as described above.

As a registered broker-dealer and member firm of the NYSE and FINRA, LFS is subject to SEC Rule 15c3-1, as adopted and administered by the SEC and the NYSE. Under the alternative method permitted by this rule, the minimum required net capital is equal to the greater of \$1.0 million or 2.0% of aggregate debit items, as defined. As of September 30, 2008 and December 31, 2007, LFS net capital, as defined, was \$31.0 million and \$16.6 million, respectively, which exceeded minimum requirements by \$30.0 million and \$15.6 million, respectively. In February 2008, the Company contributed an additional \$20.0 million in capital to LFS in order to enable LFS to conduct increased trading activities in connection with its institutional execution business. A portion of the net capital at LFS is met with the value of the NYX shares held by that broker/dealer.

As a registered broker-dealer and American Stock Exchange ( AMEX ) member firm, LSP is subject to SEC Rule 15c3-1, as adopted and administered by the SEC and the AMEX. LSP is required to maintain minimum net capital, as defined, equivalent to the greater of \$100,000 or  $\frac{1}{15}$  of aggregate indebtedness, as defined. As of September 30, 2008 and December 31, 2007, LSP s net capital, as defined, was \$110.2 million and \$62.6 million, respectively, which exceeded minimum requirements by \$107.8 million and \$60.9 million, respectively. LSP s aggregate indebtedness to net capital ratio on those dates was 0.32 to 1 and 0.41 to 1, respectively.

As a registered broker-dealer and AMEX and FINRA member firm, LSPD is subject to SEC Rule 15c3-1, as adopted and administered by the SEC, AMEX and FINRA. LSPD is required to maintain minimum net capital, as defined, equivalent to the greater of \$5,000 or  $\frac{1}{15}$  of aggregate indebtedness, as defined. As of September 30, 2008 and December 31, 2007, LSPD s net capital, as defined, was \$2.8 million and \$3.0 million, respectively, which exceeded its minimum requirements by \$2.8 million and \$3.0 million, respectively.

As a registered broker dealer in the United Kingdom, LSPE is subject to the capital adequacy and capital resources as managed and monitored in accordance with the regulatory capital requirements of the Financial Services Authority ( FSA ) in the United Kingdom. In calculating regulatory capital, the Company s capital consists wholly of Tier 1 capital. Tier 1 capital is the core measure of a Company s financial strength from a regulator s point of view. It consists of the type of financial capital considered the most reliable and liquid,

**Table of Contents**

primarily Shareholder's Equity. As of September 30, 2008, Tier 1 capital, as defined, was \$31.0 million which exceeded the total variable capital requirement by \$12.3 million. At December 31, 2007, Tier 1 capital, as defined, was \$14.2 million which resulted in a deficit of \$1.2 million. The December 31, 2007 calculation did not include accumulated profits for the year ended December 31, 2007 which was in excess of the deficit. With those results now audited they can be included in Tier 1 regulatory capital. In addition, the Company had injected an additional \$9.9 million of share capital in January 2008, further enhancing regulatory capital.

As a licensed corporation registered under the Hong Kong Securities and Futures Ordinance, LSPH is subject to the capital requirements of the Hong Kong Securities and Futures (Financial Resources) Rules ( FRR ). The minimum paid-up share capital requirement is HKD 5,000,000 (\$0.6 million at September 30, 2008 and December 31, 2007) and the minimum liquid capital requirement is the higher of HKD 3,000,000 (\$0.4 million at September 30, 2008 and December 31, 2007) and the variable required liquid capital as defined in the FRR. The Company monitors its compliance with the requirements of the FRR on a daily basis. As of September 30, 2008 and December 31, 2007, LSPH's liquid capital, as defined was \$0.6 and \$0.7 million, respectively, which exceeded its minimum requirements by \$0.2 and \$0.3 million, respectively. In addition, the Company had injected an additional \$0.5 million of share capital in June 2008 further enhancing regulatory capital.

**6. LOSS PER SHARE**

The computations of basic and diluted loss per share are set forth below (000's omitted, except per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Numerator for basic and diluted (loss) income per share net (loss) income applicable to common stockholders	\$ (5,587)	\$ 6,003	\$ (67,162)	\$ (368,496)
Denominator for basic (loss) income per share weighted-average number of common shares outstanding	61,946	61,471	61,931	61,404
Dilutive shares:				
Stock options				
Restricted stock units		174		
Denominator for diluted (loss) income per share weighted-average number of common shares outstanding	61,946	61,645	61,931	61,404
Loss per share:				
Basic	\$ (0.09)	\$ 0.10	\$ (1.08)	\$ (6.00)
Diluted	\$ (0.09)	\$ 0.10	\$ (1.08)	\$ (6.00)

Options to purchase an aggregate of 990,000 and 1,195,000 shares of common stock were outstanding at September 30, 2008 and 2007, respectively, but were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the market price of the Company's common stock. For the 2008 third quarter, 446,267 potentially dilutive shares from restricted stock units were not included in the computation of diluted net loss per share because to do so would be anti-dilutive.



**Table of Contents**

**7. EMPLOYEE INCENTIVE PLANS**

SFAS No. 123(R), Share Based Payments requires compensation costs related to share-based payment transactions to be recognized in the financial statements over the period that an employee provides service in exchange for the award.

The following disclosures are also being provided pursuant to the requirements of SFAS No. 123(R):

The Company sponsors one share-based employee incentive plan the LaBranche & Co Inc. Equity Incentive Plan (the Plan ), which provides for grants of incentive stock options, nonqualified stock options, restricted shares of common stock, restricted stock units ( RSUs ), unrestricted shares and stock appreciation rights. The fair value of the restricted stock awards is determined by using the closing price of the Company s common stock on the respective dates on which the awards are granted. Grant date is determined to be the date the compensation committee of the Board of Directors approves the grant, except in circumstances where the approval by the compensation committee is contingent upon a future event, such as the negotiation and execution of an employment agreement, in which case the grant date is the date the condition is satisfied. Amortization of compensation costs for grants awarded under the Plan recognized during the three and nine months ended September 30, 2008 was approximately \$1.0 million and \$3.1 million compared to \$1.0 million and \$3.6 million for the same periods in 2007. The tax benefit realized in the Consolidated Statements of Operations for the Plan was approximately \$0.4 million and \$1.2 million for the three and nine months ended September 30, 2008 compared to \$0.4 million and \$1.4 million for the same periods in 2007, respectively.

Unrecognized compensation cost related to the Company s non-vested stock option and restricted stock unit awards totaled \$4.8 million at September 30, 2008 and \$4.9 million at December 31, 2007. The cost of these non-vested awards is generally expected to be recognized over a period of approximately three years.

SFAS No. 123(R) generally requires share-based awards granted to retirement-eligible employees to be expensed immediately. The Company did not grant any share-based awards prior to our adoption of SFAS No. 123(R) to retirement-eligible employees or those with non-substantive non-compete agreements. In addition, no grants of any stock options or RSUs were changed or amended after the Company s adoption of SFAS No. 123(R) to reflect retirement eligibility or non-compete agreements.

The total number of shares of the Company s common stock that may be issued under the Plan through fiscal year 2009 may not exceed 7,687,500 shares. As of September 30, 2008 and December 31, 2007, 3,394,199 shares and 3,187,613 shares, respectively, were available for grant under the Plan.

**Table of Contents***Restricted Stock Units*

All of the RSUs outstanding as of September 30, 2008 and 2007 require future service as a condition to the delivery of the underlying shares of common stock on their respective vesting dates. The RSUs are granted under the Company's Equity Incentive Plan and vest over varying numbers of years. An employee who receives RSUs does not have any ownership rights with respect to the underlying shares until the shares vest pursuant to the terms of an RSU agreement. In all cases, delivery of the underlying shares of common stock is conditioned on the grantees satisfying certain requirements outlined in the agreements. Generally, the RSUs become fully vested if the grantee's employment with the Company terminates by reason of death or disability prior to vesting. The grantee forfeits the unvested portion of the RSUs upon the termination of employment for any reason other than death or disability. When delivering the underlying shares of stock to employees, the Company generally issues new shares of common stock, as opposed to reissuing treasury shares.

The following table provides information about grants of RSUs:

	Number of Shares	Weighted Average Price per Share
RSUs Outstanding as of December 31, 2007	1,083,484	\$ 9.44
Granted		
Vested	(444,340)	9.12
Forfeited	(24,997)	9.12
RSUs Outstanding as of March 31, 2008	614,147	\$ 9.68
Granted	692,000	5.55
Vested		
Forfeited	(54,828)	9.43
RSUs Outstanding as of June 30, 2008	1,251,319	\$ 7.41
Granted		
Vested		
Forfeited	(9,999)	9.47
RSUs Outstanding as of September 30, 2008	1,241,320	\$ 7.39

Under SFAS No. 123(R), the Company is required to estimate forfeitures of RSUs for purposes of determining the Company's share-based award expense. Applying SFAS No. 123(R) as of September 30, 2008, for purposes of determining share-based award expense, RSUs with respect to 1,215,851 shares of the Company's common stock were expected to vest based on shares issued of 3,393,500, with a weighted average price of \$7.92 per share.

*Stock Options*

As of September 30, 2008, all stock options granted to employees were fully vested and exercisable. In general, all stock options expire on the tenth anniversary of grant, although they may be subject to earlier termination or cancellation in certain circumstances under the Plan and the stock option agreement, such as death, disability or other termination of employment prior to the tenth anniversary of grant. The dilutive effect, if any, of the Company's outstanding stock options is included in Weighted Average Common Shares Outstanding Diluted on the Condensed Consolidated Statement of Operations.

**Table of Contents**

The following table provides information about options to purchase the Company's common stock:

	Number of Shares	Weighted Average Exercise Price per Share
Options Outstanding as of December 31, 2007	1,165,000	\$ 23.77
Options Granted		
Options Exercised		
Options Forfeited		
Options Outstanding as of March 31, 2008	1,165,000	\$ 23.77
Options Granted		
Options Exercised		
Options Forfeited	(75,000)	27.50
Options Outstanding as of June 30, 2008	1,090,000	\$ 23.51
Options Granted		
Options Exercised		
Options Forfeited	(100,000)	35.00
Options Outstanding as of September 30, 2008	990,000	\$ 22.35
Options Exercisable as of:		
March 31, 2008	1,165,000	\$ 23.77
June 30, 2008	1,090,000	\$ 23.51
September 30, 2008	990,000	\$ 22.35

The following table summarizes information about stock options outstanding as of September 30, 2008:

Range of Exercise Prices	Number of Shares	Options Outstanding		Options Exercisable	
		Weighted Average Remaining Contractual Life	Weighted Average Exercise Price per Share	Number of Shares	Weighted Average Exercise Price per Share
\$11.00 - \$20.99	600,000	0.88	\$ 14.00	600,000	\$ 14.00
\$31.00 - \$40.99	390,000	3.26	\$ 35.19	390,000	\$ 35.19
	990,000			990,000	

No options were exercised during the nine months ended September 30, 2008 and September 30, 2007.

**8. BUSINESS SEGMENTS**

Segment information is presented in accordance with SFAS No. 131, Disclosures About Segments of an Enterprise and Related Information. The Company's business segments are based upon the nature of the financial services provided, their revenue source and the Company's management organization.

The Company's Specialist and Market-Making segment operates as a specialist in equities and rights listed on the NYSE, as a specialist in equities, options, ETFs and futures on several exchanges as well as a market-maker in ETFs, futures and options on several exchanges. The

Edgar Filing: LABRANCHE & CO INC - Form 10-Q

Specialist and Market-Making segment currently includes the operations of LaBranche & Co. LLC, LSP, LSPE, LSPH and LSPD.

-15-

**Table of Contents**

The Company's Institutional Brokerage segment (formerly called the Execution and Clearing segment) provides mainly securities execution and brokerage services to institutional investors, and currently includes the operations of LFS. Until June 8, 2007, the Institutional Brokerage segment also provided securities clearing services to its own customers and customers of introducing brokers, when it outsourced its clearing operations to a major Wall Street financial services firm.

The Company's Other segment is comprised primarily of the interest on the Holding Company's indebtedness, unallocated corporate administrative expenses, including professional and legal costs, unallocated revenues (primarily interest income) and elimination entries. This section also includes the investment entity, LABDR, and the inactive company, BV.

Revenues and expenses directly associated with each segment are included in determining its operating results. Other expenses, including corporate overhead, which are not directly attributable to a particular segment, generally are allocated to each segment based on its resource usage levels or other appropriate measures. Interest with respect to the Company's outstanding senior notes, certain administrative expenses, corporate overhead expenses and other sources of revenues are not specifically allocated by management when reviewing the Company's segments' performance, and appear in the Other segment. Selected financial information for each segment is set forth below (000's omitted):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
<b>Specialist and Market-Making Segment:</b>				
Total Revenues, net of NYX and interest expense	\$ 79,518	\$ 28,051	\$ 183,344	\$ 130,907
Net (loss) gain on NYX	(29,480)	15,579	(133,282)	(38,687)
Operating expenses	45,483	24,970	113,029	95,025
Goodwill impairment				164,100
Specialist stock list impairment				335,264
Depreciation and amortization	81	127	253	5,613
Income (loss) before taxes	\$ 4,474	\$ 18,533	\$ (63,220)	\$ (507,782)
Segment goodwill	\$ 84,218	\$ 84,218	\$ 84,218	\$ 84,218
Segment assets	\$ 4,081,617	\$ 4,867,904	\$ 4,081,617	\$ 4,867,904
<b>Institutional Brokerage Segment:</b>				
Total Revenues, net of NYX and interest expense	\$ 5,576	\$ 5,913	\$ 15,291	\$ 19,716
Net (loss) gain on NYX	(2,457)	1,298	(11,107)	(3,224)
Operating expenses	7,418	6,845	19,614	22,616
Depreciation and amortization	14	31	51	152
(Loss) income before taxes	\$ (4,313)	\$ 335	\$ (15,481)	\$ (6,276)
Segment assets	\$ 47,839	\$ 47,190	\$ 47,839	\$ 47,190
<b>Other:</b>				
Total Revenues, net of interest expense	\$ (6,143)	\$ (9,125)	\$ (22,135)	\$ (30,296)
Operating expenses	2,055	1,995	5,949	5,856
Early extinguishment of debt			6,005	
Depreciation and amortization	830	842	2,418	2,363
Loss before taxes	\$ (9,028)	\$ (11,962)	\$ (36,507)	\$ (38,515)
Segment assets	\$ 228,501	\$ 321,154	\$ 228,501	\$ 321,154
<b>Total:</b>				
Total Revenues, net of NYX and interest expense	\$ 78,951	\$ 24,839	\$ 176,500	\$ 120,327
Net (loss) gain on NYX	(31,937)	16,877	(144,389)	(41,911)
Operating expenses	54,956	33,810	138,592	123,497

Edgar Filing: LABRANCHE & CO INC - Form 10-Q

Goodwill impairment				164,100
Specialist stock list impairment				335,264
Early extinguishment of debt			6,005	
Depreciation and amortization	925	1,000	2,722	8,128
(Loss) income before taxes	\$ (8,867)	\$ 6,906	\$ (115,208)	\$ (552,573)
Goodwill	\$ 84,218	\$ 84,218	\$ 84,218	\$ 84,218
Assets	\$ 4,357,957	\$ 5,236,248	\$ 4,357,957	\$ 5,236,248

-16-

**Table of Contents**

**9. NYSE GROUP RESTRICTED STOCK EXCHANGE TRANSACTION**

The Company holds, in aggregate, 3,126,903 NYX shares collectively through its subsidiaries, LaBranche & Co. LLC and LFSL (see Note 13 for additional share information related to NYSE merger with the AMEX).

On April 4, 2007, the NYSE Group consummated its merger with Euronext N.V. (the NYSE/Euronext merger) to form NYSE Euronext, Inc., and the Company's 3,126,903 shares of NYSE Group, Inc. common stock were exchanged for an equal number of the NYX shares, all of which continue to be owned by LaBranche & Co. LLC and LFSL. Following the NYSE/Euronext merger, the restricted NYX shares continued to be subject to the same restrictions on transfer as had existed before the NYSE/Euronext merger. The restriction with respect to the second tranche of the NYX shares was removed by NYSE Euronext in June 2007. The restriction on the remaining one-third of the Company's restricted NYX shares was removed on October 1, 2008 upon the completion of the NYSE Group, Inc acquisition of the American Stock Exchange.

The Company has accounted for its investment in NYX restricted shares as corporate equities not readily marketable at the estimated fair value of such restricted shares pursuant to SFAS No. 157. At September 30, 2008, the NYSE closing market price for the NYX shares was \$39.18 per share as compared to the closing price of NYX shares at June 30, 2008 which was \$50.66 per share. This resulted in the Company's recognition of an unrealized pre-tax loss of \$31.9 million, which is net of a gain of \$4.0 million for the reversal of the 7.5% valuation allowance related to the removal of the restriction on the last one third of restricted shares, for the quarter ended September 30, 2008 and is included in net loss on investments in the Company's condensed consolidated statements of operations.

On September 30, 2008, a quarterly dividend of \$0.30 per share was paid to shareholders of record of NYSE Euronext as of the close of business on September 15, 2008. The aggregate dividend payment with respect to the Company's 3,126,903 NYX shares was \$0.9 million in the third quarter of 2008 and is reported in the Company's other revenues.

**Table of Contents****10. FINANCIAL INSTRUMENTS**

Financial instruments owned and financial instruments sold, but not yet purchased, at fair value, were as follows (000 s omitted):

	September 30, 2008	December 31, 2007
<b>FINANCIAL INSTRUMENTS OWNED:</b>		
Corporate equities, not readily marketable	\$ 40,837	\$ 83,945
Corporate equities	1,719,240	2,016,380
Options	1,238,010	1,025,670
Exchange-traded funds	630,110	1,000,600
Government and corporate bonds	233,881	138,159
Investment in limited partnerships	4,986	2,641
	\$ 3,867,064	\$ 4,267,395
<b>FINANCIAL INSTRUMENTS SOLD, BUT NOT YET PURCHASED:</b>		
Corporate equities	\$ 1,276,011	\$ 1,980,040
Options	1,247,937	1,183,884
Exchange-traded funds	608,177	769,094
Government and corporate bonds	40,856	129,977
	\$ 3,172,981	\$ 4,062,995

**11. FAIR VALUE MEASUREMENTS**

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards, or SFAS No. 157 Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 applies only to fair value measurements already required or permitted by other accounting standards and does not impose requirements for additional fair value measures. Our adoption of SFAS No. 157 did not have a material impact on our financial condition or results of operations. Pursuant to SFAS No. 157, the fair value of a financial instrument is defined as the amount that would be received to sell an asset or paid to transfer a liability, or the exit price, in an orderly transaction between market participants at the measurement date.

We use fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Our financial instruments owned and financial instruments sold, but not yet purchased are recorded at fair value on a recurring basis.

We may be required to record at fair value other assets or liabilities on a non-recurring basis, such as our trade name and goodwill. These non-recurring fair value adjustments involve the application of fair value measurements in assessing whether these and other nonfinancial assets or nonfinancial liabilities are impaired.

The Company has elected to apply the deferral provisions in FSP No. 157-2 and therefore have only partially applied the provisions of SFAS No. 157. FSP No. 157-2 defers the effective date for the disclosure fair value measurements related to nonfinancial assets and nonfinancial liabilities to fiscal years beginning after November 15, 2008. FSP No. 157-3 clarifies the application of FASB 157 in a market that is not active. FSP No. 157-3 is effective upon issuance.



**Table of Contents**

SFAS No. 157 outlines a fair value hierarchy. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets and liabilities (which are considered level 1 measurements) and the lowest priority to unobservable inputs (which are considered level 3 measurements). The three levels of the fair value hierarchy under SFAS No. 157 are as follows:

- Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level 2 Quoted prices for similar instruments in active markets, quoted prices in markets that are not active or financial instruments for which all significant inputs are observable, either directly or indirectly;
- Level 3 Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions would reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Such valuation techniques include the use of option pricing models, discounted cash flow models and similar techniques.

The following table represents the Company's fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of September 30, 2008 (000's omitted):

	Level 1	Level 2	Level 3	Total
<b>ASSETS:</b>				
Financial instruments owned, at fair value:				
Corporate equities	1,750,571	14,492	\$	1,765,063
Government and corporate bonds	190,212	43,669		233,881
Options	1,227,454	10,556		1,238,010
Exchange-traded funds	630,092	18		630,110
<b>Total financial instruments owned</b>	<b>\$ 3,798,329</b>	<b>\$ 68,735</b>	<b>\$</b>	<b>\$ 3,867,064</b>
Government obligations	996			996
Securities segregated under federal regulations	1,342			1,342
<b>Total assets, at fair value</b>	<b>\$ 3,800,667</b>	<b>\$ 68,735</b>	<b>\$</b>	<b>\$ 3,869,402</b>
<b>LIABILITIES:</b>				
Government and corporate bonds	\$ 35,881	\$ 4,975	\$	\$ 40,856
Corporate equities	1,275,772	239		1,276,011
Options	1,243,378	4,559		1,247,937
Exchange-traded funds	608,173	4		608,177
<b>Total financial instruments sold, not yet purchased</b>	<b>\$ 3,163,204</b>	<b>\$ 9,777</b>	<b>\$</b>	<b>\$ 3,172,981</b>

Determining the fair value of our financial securities was determined from a variety of sources as follows:

For corporate equities and ETFs, fair value was determined by the closing price of the primary exchanges and was included in Level 1 for those that are actively traded. Those classified in Level 2 represent those not actively traded with quoted market prices.

## **Table of Contents**

For government and corporate bonds, the primary source for pricing fixed income instruments is derived from our clearing broker who determines prices through various third party pricing services. The Company confirms these values using independent observable sources. When pricing cannot be confirmed the positions will be valued using broker quotes and included in Level 2.

For options, the fair values are based on the NBBO mid point average. Those included in Level 2 are valued based on broker quotes when a price could not be confirmed due to the security not being actively traded.

## **12. STOCKHOLDERS EQUITY**

On April 17, 2008, our Board of Directors authorized the repurchase of up to \$40.0 million in shares of our common stock. In the third quarter of 2008, we repurchased 371,753 shares at a cost of approximately \$1.6 million. The average cost per repurchased share was \$4.41 (see Note 14 for subsequent repurchase information).

## **13. CONTINGENCIES**

There have been no material new developments in the Company's legal proceedings since the March 17, 2008 filing of its Annual Report on Form 10-K for the year ended December 31, 2007 (the 2007 10-K), the May 12, 2008 filing of its Quarterly Report on form 10-Q for the first quarter of 2008 (the First Quarter 10-Q), and the August 11, 2008 filing of its Quarterly Report on Form 10-Q for the second quarter of 2008 (the Second Quarter 10-Q), except as follows:

In re LaBranche Securities Litigation. As previously reported, on February 8, 2008, the Company entered into an agreement in principle to settle the action for \$13 million, to be paid entirely by the Company's insurers, subject to completion of a usual and customary settlement agreement, notice to the class, and approval by the Court. On September 19, 2008, the parties submitted a settlement agreement to the Court. On September 22, 2008, the Court preliminary approved the settlement. Notice has been provided to the class, and the settlement remains subject to final approval by the Court.

Sea Carriers, L.P. v. NYSE Euronext, et al. On August 20, plaintiff voluntarily dismissed this action without prejudice. No payment was made by the Company or any other defendant in the case.

The Company believes that the claims asserted against it by the plaintiffs in the pending proceedings described in the 2007 10-K, the First Quarter 10-Q, the Second Quarter 10-Q and above are without merit, and the Company denies all allegations of wrongdoing. There can be no assurance, however, as to the outcome or timing of the resolution of these proceedings. Therefore, the Company is unable to estimate the amount or potential range of any loss that may arise out of these proceedings. The range of possible resolutions could include determinations and judgments against the Company or settlements that could require substantial payments by the Company that could have a material adverse effect on the Company's financial condition, results of operations and cash flows.

## **Table of Contents**

In addition to the proceedings described in the 2007 10-K, the First Quarter 10-Q, the Second Quarter 10-Q and above, the Company and its operating subsidiaries have been the target, from time to time, of various claims, lawsuits and regulatory inquiries in the ordinary course of their respective businesses. While the ultimate outcome of those claims and lawsuits which are currently pending cannot be predicted with certainty, the Company believes, based on its understanding of the facts of these proceedings, that their ultimate resolution will not, in the aggregate, have a material adverse effect on the Company's financial condition, results of operations or cash flows.

### **14. SUBSEQUENT EVENTS**

On June 17, 2008, NYSE Euronext, Inc. and the American Stock Exchange (the "AMEX") announced that members of the AMEX Membership Corporation (the "AMC") approved the adoption of the merger agreement between AMC and NYSE Euronext and certain of their subsidiaries. In July 2008, the AMEX submitted proposed rule changes in connection with the trading of AMEX listed securities following the merger, including on which market each class of securities will trade following the merger. We currently are unable to estimate how those new rules will affect our operations, and although the rule changes have been approved by the SEC, it is the Company's understanding that the rules will not take effect until 2009 when the AMEX trading is expected to be moved to the NYSE and NYSE ARCA Exchange. On October 1, 2008, under the terms of the merger agreement, the Company received 8,138 shares of NYSE Euronext common stock in exchange for the AMEX seat we owned with fractional shares paid in cash. In addition, AMEX members will be entitled to receive additional shares of NYSE Euronext common stock calculated by reference to net proceeds, if any, from the expected sale of the AMEX's lower Manhattan headquarters if such sale occurs prior to the date which is four years and 240 days following the date on which the NYSE Euronext/Amex merger is completed and certain other conditions are satisfied.

In conjunction with the merger, the Board of Directors of NYSE Euronext approved the removal of the transfer restrictions as of October 1, 2008 on the remaining shares issued as part of the business combination between the NYSE and Archipelago Holdings, Inc. which was completed on March 7, 2006. These shares were previously restricted until March 7, 2009.

On October 9, 2008 the Company purchased an aggregate of \$7.6 million aggregate principal amount of its outstanding 11% Senior Notes due May 2012 below par. The purchase of the debt will result in an annual interest savings of \$0.8 million. The accrued interest payable at the date of purchase was \$0.3 million and a gain on repurchase, net of debt issuance costs, of \$0.2 was realized. The Company has \$202.3 million of its 11% senior notes outstanding after this purchase. Management continues to monitor opportunities to purchase senior notes at or below the call price for the debt.

In October 2008, the Company repurchased an aggregate of 1,292,702 million shares of its outstanding common stock at total price of \$5.6 million, or an average price of \$4.37 per share. Management continues to monitor opportunities to repurchase stock. These purchases were in addition to purchases made by the Company in September 2008 of an aggregate of 371,753 shares of its common stock in connection with the previously-announced authorization by its board of directors to purchase up to \$40.0 million of the Company's outstanding common stock in April 2008.

---

**Table of Contents**

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

*Unless the context otherwise requires, the Company or we shall mean LaBranche & Co Inc. and its wholly-owned subsidiaries.*

*This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended December 31, 2007 (the 2007 10-K ) and our Condensed Consolidated Financial Statements and the Notes thereto contained in this report.*

**Executive Overview**

For the third quarter of 2008, our US GAAP net loss was \$5.6 million, or \$0.09 per share, compared to net income of \$6.0 million, or \$0.10 per share for the same period in 2007. These GAAP earnings were affected by a significant unrealized loss of \$19.2 million in the third quarter of 2008 and a significant unrealized gain of \$10.1 million in the third quarter of 2007 in connection with the change in value of our NYX shares. Excluding these items in each quarter, our pro-forma net income for the third quarter of 2008 was \$13.6 million, or \$0.22 per share, compared to a pro-forma net loss for the third quarter of 2007 of \$4.1 million, or \$0.07 per share.

These results include unrealized changes in the mark-to-market value of our NYX shares in the first nine months of 2008 and 2007, a \$3.6 million loss on early extinguishment of our debt in 2008 and the non-cash charges related to the impairment of our goodwill and stock listing rights of \$344.7 in the second quarter of 2007. Absent these amounts, our pro-forma net income for the first nine months of 2008 was \$23.1 million, or \$0.37 per diluted share, compared to a pro-forma net loss of \$0.7 million, or \$0.01 per share, for the first nine months of 2007.

Virtually all of the markets in which we provide liquidity experienced higher levels of volatility in the third quarter of 2008, with periods of extreme volatility in September. We believe that there is a continued need for market makers, especially in these market conditions, and that our liquid balance sheet puts us in a strong position to provide added liquidity in securities markets. In the third quarter in particular, our financial condition, combined with market volatility, allowed us to take advantage of opportunities to provide greater liquidity to the markets. While our newer business lines performed well and constituted a majority of our revenues, our traditional cash equities specialist business posted its best results since the introduction of the NYSE's HYBRID market. In addition, the steps we have taken in reducing costs and overhead during past years have enabled us to improve cash flows at our operating companies.

We believe that new trading venues will continue to converge and that global securities markets will increasingly interact with each other. We continue to look for opportunities in markets outside our traditional cash equities specialist business. As a result our newer businesses today represent the majority of our specialist and market-making revenues, especially as we rely upon and further develop our electronic trading strategies to interact with the global electronic marketplace.

## Table of Contents

We are also continuing to build our Institutional Brokerage business. Although our Institutional Brokerage segment showed a loss in the second and third quarters of 2008, we believe much of these results are mainly attributable to start-up costs and our initial facilitation trading results. We have made key hires of sales and position traders that we believe will help us build our Institutional Brokerage business into an operation that meets the needs of today's institutional customers.

We are actively taking steps to further reduce our operating expenses. The largest of these expenses is the interest on our public debt, which was approximately \$47.6 million per year until 2008. Following the repurchases and retirement of \$249.9 million of our outstanding debt in the first half of 2008, \$209.9 million of our 11% Senior Notes due 2012 remained outstanding until October 2008 when we repurchased an additional \$7.6 million of our remaining notes. Following this October 2008 repurchase, our remaining annual interest expense is approximately \$22.3 million versus \$47.6 million in 2007. Historically, the operating expense related to our outstanding debt has been the negative carry on our debt, which is the interest we pay on our outstanding indebtedness, less the interest income we receive as a result of having that cash on-hand. Prior to the repurchases described above, our negative carry would have been \$10.2 million per quarter, based on current short-term interest rates. Following our repurchases to date in 2008, the negative carry will be reduced to approximately \$5.1 million per quarter, based on current short-term interest rates. The repurchase of our public debt also has enabled us to improve our consolidated fixed charge coverage ratio to 3.7:1 at September 30, 2008, which evidences our growing flexibility to strategically utilize our capital by considering a broader spectrum of opportunities.

As we have explained in the past, our ownership of 3,126,903 shares of NYSE Euronext Inc. common stock (the NYX shares) resulted from the exchange of our NYSE memberships, or seats, in connection with the NYSE's mergers with Archipelago Holdings and Euronext. Before the exchange of our NYSE seats into the NYX shares, we believed that our seat ownership was integral to our position in the industry. Though the value of our NYX shares has been volatile over the past two years, the value of our seats prior to their exchange were volatile as well. Our management will remain flexible regarding our continued ownership of NYX shares. We are also mindful that our ownership of exchange seats and exchange-related securities, such as our NYX shares, have been beneficial to our Company over time.

Our balance sheet is strong and very liquid. We believe we have ample capital to maintain and grow our business. We are continuing to concentrate on building our business in London and Hong Kong, in which we see trading opportunities in those markets in ETFs and other products.

In October 2008, the SEC approved an NYSE proposal to further change its market model, changing the role of specialists to designated market makers, or DMMs, who will still provide liquidity, but without the bulk of the negative and affirmative obligations that could, at times, adversely affect our profitability. The rule changes would change the timing of when the designated market-maker can see orders, but would provide us more flexibility in

**Table of Contents**

trading for our own account. We believe that some of these possible market structure changes would allow us to interact in the market more efficiently and also allow us to benefit from organizational changes and integration, because some of these changes presumably would remove the informational barriers that have caused us to maintain our specialist and market-making businesses as separate broker-dealers. We currently are unable to project if or when any of these market structure changes, or other informational barrier changes will be formally implemented, if at all.

The restructuring of certain of our specialist and market-making subsidiaries has allowed us to develop those operations across various domestic and international exchanges and marketplaces. The organizational structure of our Specialist and Market-Making segment, therefore, is intended to enable us to better allocate and deploy our capital, workforce and technology across our operations in order to more efficiently seek out opportunities as they arise.

*Regulation G Reconciliation of Non-GAAP Financial Measures*

In evaluating our financial performance as described above in Executive Overview, management reviews operating results from operations, which excludes non-operating charges. Pro-forma earnings per share is a non-GAAP (generally accepted accounting principles) performance measure, but we believe that it is useful to assist investors in gaining an understanding of the trends and operating results for our core business. In this report, our pro-forma operating results in the periods presented exclude certain extraordinary and/or non-recurring items, such as, for example, the unrecognized loss on the Company's NYX shares and the costs associated with the early retirement of our Company's outstanding senior indebtedness, neither of which are, in management's belief, reflective of the Company's day-to-day operating performance or cash generation, and neither of which affect the Company's actual income or cash. Pro-forma earnings per share should be viewed in addition to, and not in lieu of our reported results under U.S. GAAP.

The following is a reconciliation of U.S. GAAP results to pro-forma results for the periods presented:

	Three Months Ended September 30,					
	Amounts as reported	2008 (1) (2) Adjustments	Pro forma amounts	Amounts as reported	2007 (1) Adjustments	Pro forma amounts
Revenues, net of interest expense	\$ 47,014	\$ 31,937(1)	\$ 78,951	\$ 41,716	\$ (16,877)(1)	\$ 24,839
Total expenses	55,881		55,881	34,810		34,810
(Loss) income before (benefit) provision for income taxes	(8,867)	31,937	23,070	6,906	(16,877)	(9,971)
(Benefit) provision for income taxes	(3,280)	12,775	9,495	903	(6,751)	(5,848)
Net (loss) income applicable to common stockholders	\$ (5,587)	\$ 19,162	\$ 13,575	\$ 6,003	\$ (10,126)	\$ (4,123)
Basic per share	\$ (0.09)	\$ 0.31	\$ 0.22	\$ 0.10	\$ (0.17)	\$ (0.07)
Diluted per share	\$ (0.09)	\$ 0.31	\$ 0.22	\$ 0.10	\$ (0.17)	\$ (0.07)

**Table of Contents**

	Nine Months Ended September 30,					
	2008			2007		
	Amounts as reported	(1) (2) Adjustments	Pro forma amounts	Amounts as reported	(1) Adjustments	Pro forma amounts
Revenues, net of interest expense	\$ 32,111	\$ 144,389(1)	\$ 176,500	\$ 78,416	\$ 41,910(1)	\$ 120,326
Total expenses	147,319	(6,005)(2)	141,314	630,989	(499,364)(3)	131,625
(Loss) income before (benefit) provision for income taxes	(115,208)	150,394	35,186	(552,573)	541,274	(11,299)
(Benefit) provision for income taxes	(48,046)	60,158	12,112	(184,077)	173,488	(10,589)
Net (loss) income applicable to common stockholders	\$ (67,162)	\$ 90,236	\$ 23,074	\$ (368,496)	\$ 367,786	\$ (710)
Basic per share	\$ (1.08)	\$ 1.45	\$ 0.37	\$ (6.00)	\$ 5.99	\$ (0.01)
Diluted per share	\$ (1.08)	\$ 1.45	\$ 0.37	\$ (6.00)	\$ 5.99	\$ (0.01)

- (1) Revenue adjustment reflects loss (gain) in each accounting period, based on the change in fair market value of the Company's restricted and unrestricted NYX shares at the end of each such period versus the beginning of such period.
- (2) Expense adjustment reflects costs associated with early extinguishment of debt in accounting period.
- (3) Relates to the write-down of the carrying value of the Company's goodwill and stock listing rights to reflect the results of the Company's impairment evaluation under SFAS Nos. 142 and 144.

**New Accounting Developments***Fair Value Measurements*

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value and enhances disclosures about fair value measurements required under other accounting pronouncements, but does not change existing guidance as to whether or not an instrument is carried at fair value. SFAS 157 nullifies the guidance in EITF 02-3 which precluded the recognition of a trading profit at the inception of a derivative contract, unless the fair value of such derivative is obtained from a quoted market price, or other valuation technique incorporating observable market data. SFAS 157 also precludes the use of a liquidity or block discount, when measuring instruments traded in an active market at fair value. SFAS 157 requires that costs related to acquiring financial instruments carried at fair value should not be capitalized, but rather should be expensed as incurred. SFAS 157 also clarifies that an issuer's credit standing should be considered when measuring liabilities at fair value. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and was adopted by the Company as of January 1, 2008. SFAS 157 must be applied prospectively, except that the provisions related to block discounts and the guidance in EITF 02-3 are to be applied as a one time cumulative effect adjustment to opening retained earnings in the first interim period for the fiscal year in which SFAS 157 is initially applied. The adoption of SFAS 157 resulted in no cumulative change to the accumulated deficit. Please refer to Footnote 11 of our Condensed Consolidated Financial Statements for additional information and disclosure.

## **Table of Contents**

In February 2008, the FASB issued FSP FAS 157-2 which delays the effective date of Statement 157 to all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in an entity's financial statements on a recurring basis (at least annually to fiscal years beginning after November 15, 2008. Such items include a) nonfinancial assets acquired and liabilities assumed in purchase business combinations and b) intangible assets and goodwill.

In October of 2008, the FASB issued FSP FAS 157-3 which clarifies the application of FASB 157, *Fair Value Measurement*, in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that asset is not active. The FSP shall be effective upon issuance, including prior periods for which financial statements have not been issued. Revisions resulting from a change in the valuation technique or its application shall be accounted for as a change in accounting estimate pursuant to FASB 154. The disclosure provisions of Statement 154 for a change in accounting estimate are not required for revisions resulting from a change in valuation technique or its application. As of September 30, 2008, we do not hold any securities that would be subject to change based on FSP FAS 157-3.

### *Accounting for Fair Value Option for Financial Assets and Financial Liabilities*

In February 2007, the FASB issued SFAS No. 159, *Accounting for Fair Value Option for Financial Assets and Financial Liabilities* ( SFAS 159 ). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. We currently report the majority of our financial assets and liabilities at fair value in compliance with industry guidelines for brokers and dealers in securities. The Company elected not to apply the fair value option for any applicable assets or liabilities.

### *Derivative Instruments and Hedging Activities*

In April 2007, the FASB issued a Staff Position ( FSP ) FIN No. 39-1, *Amendment of FASB Interpretation No. 39*. FSP FIN No. 39-1 defines *right of setoff* and specifies what conditions must be met for a derivative contract to qualify for this right of setoff. It also addresses the applicability of a right of setoff to derivative instruments and clarifies the circumstances in which it is appropriate to offset amounts recognized for those instruments in the statement of financial position. In addition, this FSP permits offsetting of fair value amounts recognized for multiple derivative instruments executed with the same counterparty under a master netting arrangement and fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) arising from the same master netting arrangement as the derivative instruments. The provisions of this FSP are consistent with our current accounting practice. This interpretation is effective for fiscal years beginning after November 15, 2007, with early application permitted. The adoption of FSP FIN No. 39-1 did not have a material impact on our consolidated financial statements.



---

## **Table of Contents**

In March 2008, the FASB issued FASB Statement No 161, Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement 133. SFAS 161 amends and expands the disclosures required by SFAS 133 so that they provide an enhanced understanding of 1) how and why an entity uses derivative instruments, 2) how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and 3) how derivative instruments affect an entity's financial position, financial performance, and cash flows. SFAS 161 is effective for both interim and annual reporting periods beginning after November 15, 2008, with early adoption encouraged. The Company is not subject to SFAS 133 at this time. Since this amendment relates solely to disclosures related to SFAS 133, there is no potential effect on the financial position of the Company.

### *The Hierarchy of Generally Accepted Accounting Principles*

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles (SFAS 162). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (GAAP) in the United States (the GAAP hierarchy). SFAS 162 is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles*. The Adoption of SFAS 162 will not have a material effect on the Consolidated Financial Statements.

### **Critical Accounting Estimates**

#### *Goodwill and Other Intangible Assets*

We determine the fair value of each of our reporting units and the fair value of each reporting unit's goodwill under the provisions of SFAS No. 142, Goodwill and Other Intangible Assets. In determining fair value, we use standard analytical approaches to business enterprise valuation (BEV), such as the market comparable approach and the income approach. The market comparable approach is based on comparisons of the subject company to similar companies engaged in an actual merger or acquisition or to public companies whose stocks are actively traded. As part of this process, multiples of value relative to financial variables, such as earnings or stockholders' equity, are developed and applied to the appropriate financial variables of the subject company to indicate its value. The income approach involves estimating the present value of the subject company's future cash flows by using projections of the cash flows that the business is expected to generate, and discounting these cash flows at a given rate of return. Each of these BEV methodologies requires the use of management estimates and assumptions. For example, under the market comparable approach, we assigned a certain control premium to the public market price of our common stock as of the valuation date in estimating the fair value of our specialist reporting unit. Similarly, under the income approach, we assumed certain growth rates for our revenues, expenses, earnings before interest, income taxes, depreciation and amortization, returns on working capital, returns on other assets and capital expenditures, among others. We also assumed certain discount rates and certain terminal growth rates in our calculations. Given the subjectivity involved in

**Table of Contents**

selecting which BEV approach to use and in determining the input variables for use in our analyses, it is possible that a different valuation model and the selection of different input variables could produce a materially different estimate of the fair value of our goodwill.

We review the reasonableness of the carrying value of our goodwill annually as of December 31, unless an event or change in circumstances requires an interim reassessment of impairment. During the nine months ended September 30, 2008, there were no changes in circumstances that necessitated goodwill impairment testing prior to our required year-end test date. We cannot provide assurance that a change in circumstances requiring an interim assessment or future goodwill impairment testing will not result in impairment charges in subsequent periods.

Another of our intangible assets, as defined under SFAS No. 142, is our trade name. We determine the fair value of our trade name by applying the income approach using the royalty savings methodology. This method assumes that the trade name has value to the extent we are relieved of the obligation to pay royalties for the benefits received from it. Application of this methodology requires estimating an appropriate royalty rate, which is typically expressed as a percentage of revenue. Estimating an appropriate royalty rate includes reviewing evidence from comparable licensing agreements and considering qualitative factors affecting the trade name. Given the subjectivity involved in selecting which BEV approach to use and in determining the input variables for use in our analyses, it is possible that a different valuation model and the selection of different input variables could produce a materially different estimate of fair value of our trade name.

We review the reasonableness of the carrying amount of our trade name on an annual basis in conjunction with our goodwill impairment assessment. During the nine months ended September 30, 2008, there were no changes in circumstances that necessitated trade name impairment testing prior to our required year-end test date. We cannot provide assurance that a change in circumstances requiring an interim assessment or future trade name and stock listing rights impairment testing will not result in impairment charges in subsequent periods.

*Financial Instruments*

Financial instruments owned, at fair value and Financial instruments sold, but not yet purchased, at fair value are reported in our consolidated financial statements, at fair value, on a recurring basis. Pursuant to SFAS No. 157, the fair value of a financial instrument is defined as the amount that would be received to sell an asset or paid to transfer a liability, or the exit price, in an orderly transaction between market participants at the measurement date.

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards, or SFAS, No. 157 Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 outlines a fair value hierarchy that is used to determine the value to be reported. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets and liabilities (which are considered level 1 measurements) and the lowest priority to unobservable inputs (which are considered level 3 measurements). The three levels of the fair value hierarchy under SFAS No. 157 are as follows:

- Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level 2 Quoted prices for similar instruments in active markets, quoted prices in markets that are not active or financial instruments for which all significant inputs are observable, either directly or indirectly;
- Level 3 Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions would reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Such valuation techniques include the use of option pricing models, discounted cash flow models and similar techniques.

## **Table of Contents**

### *Non-Marketable Securities*

The measurement of non-marketable investments is a critical accounting estimate. Investments in non-marketable securities consist of investments in equity securities of private companies and limited liability company interests and are included in other assets in the condensed consolidated statements of financial condition. Certain investments in non-marketable securities are initially carried at cost, unless there are third-party transactions evidencing a change in value. For certain other investments in non-marketable investments we adjust their carrying value by applying the equity method of accounting pursuant to APB 18. Under the equity method the investor recognizes its share of the earnings and losses of an investee in the periods for which they are reported by the investee in its financial statements. The assets included in this section represent limited liability companies that are service providers and whose value is affected by nonfinancial components. In addition, if and when available, management considers other relevant factors relating to non-marketable investments in estimating their value, such as the financial performance of the entity, its cash flow forecasts, trends within that entity's industry and any specific rights associated with our investment such as conversion features among others.

Non-marketable investments are tested for potential impairment whenever events or changes in circumstances suggest that such investment's carrying value may be impaired.

### **Use of Estimates**

The use of generally accepted accounting principles requires management to make certain estimates. In addition to the estimates we make in connection with fair value measurements and the accounting for goodwill and identifiable intangible assets, the use of estimates is also important in determining provisions for potential losses that may arise from litigation, regulatory proceedings and tax audits.

We estimate and provide for potential losses that may arise out of litigation, regulatory proceedings and tax audits to the extent that such losses are probable and can be estimated, in accordance with SFAS No. 5, Accounting for Contingencies and FIN 48, Accounting for Uncertainty in Income Taxes. Significant judgment is required in making these estimates and

---

## **Table of Contents**

our final liabilities may ultimately be materially different. Our total liability in respect of litigation and regulatory proceedings is determined on a case-by-case basis and represents an estimate of probable losses after considering, among other factors, the progress of each case or proceeding, our experience and the experience of others in similar cases or proceedings, and the opinions and views of legal counsel. Given the inherent difficulty of predicting the outcome of our litigation and regulatory matters, particularly in cases or proceedings in which substantial or indeterminate damages or fines are sought, we cannot estimate losses or ranges of losses for cases or proceedings where there is only a reasonable possibility that a loss may be incurred. See *Legal Proceedings* in Part II, Item 1 of this Quarterly Report on Form 10-Q for information on our judicial, regulatory and arbitration proceedings.

### **Recent Regulatory Developments**

#### *Regulation SHO and Short Selling Rules.*

On October 14, 2008, the Securities and Exchange Commission adopted several final rules concerning short selling practices in US securities markets. Among the rules were (a) an interim final temporary rule that extends, until July 31, 2009, the recently imposed Rule 204T requiring that firms buy or borrow securities to close-out any fail to deliver position in an equity security resulting from a long or a short sale by the beginning of regular trading hours on the next settlement day following the date the fail to deliver position arose; (b) a rule eliminating the options market maker exception to the close-out requirement for short sales under Regulation SHO; and (c) an antifraud rule prohibiting misrepresentations by a short seller regarding its ability or intention to deliver securities by the settlement date in connection with both long and short sales. The rules are generally consistent with the series of emergency orders issued by the SEC in September and October 2008. Included in the interim final temporary Rule 204T are certain exemptions and extends the time to deliver securities to cover such short sales by up to two trading days for certain bona fide market makers (such as our specialist and market-making businesses) in connection with their bona fide market-making activities. Although we believe these new rules and emergency orders have contributed to a more volatile and active securities market place in September and October 2008, possibly creating more opportunities to trade, we currently are unable to make a determination as to whether and how such new rules will affect our business in the future. We believe that the new rules' exemptions and additional time to cover failed short positions has enabled our market-making business to comply with the new requirements of Regulation SHO while maintaining our market-making and liquidity provision obligations, but cannot provide assurance that these provisions will continue to work for our benefit.

#### *SEC Approval of New NYSE Market Model.*

On October 24, 2008, the SEC approved a rule change proposed by the NYSE to establish a new market model that will implement significant changes in NYSE's market structure, including, among other things, (a) the phasing out of the specialist system and adopting a Designated Market Maker (DMM) structure; (b) the alteration of NYSE's priority and parity rules, including those that will allow DMMs to trade on parity with orders on NYSE's display book; and (iii) the introduction of new order functionality, including the DMM Capital Commitment Schedule (CCS) and hidden orders. In order to achieve parity trading

**Table of Contents**

for the DMMs, the new market model is expected to eliminate the order-by-order advance look specialists currently receive, but the DMM would also be relieved of their negative obligation to not trade for its own account unless reasonably necessary to the maintenance of a fair and orderly market. The NYSE has stated that this change will give the DMM greater freedom to manage the trading risks associated with their reduced responsibilities to the NYSE market. In addition, under the changed rule, DMMs would continue to be able to generate orders through an algorithm that interacts directly with the NYSE's display book. Furthermore, the DMMs will be able to commit additional liquidity in advance to fill incoming orders via the CCS, which is a liquidity schedule setting forth various price points where the DMM is willing to interact with incoming orders. We are continuing to develop our trading technologies to interact in this new market model and are participating in a pilot program for selected securities under the new market model until the market model is fully implemented. We currently do not know when the new market model will be fully implemented on the NYSE, but we do believe the model will present us with additional opportunity to trade and provide liquidity in the market. It is too early to estimate the effects of this new market model on our future results, if any.

**Completed Purchases of Outstanding Indebtedness**

As of September 30, 2008, our remaining outstanding indebtedness consisted of \$209.9 million aggregate principal amount of our 11% Senior Notes due 2012 (the 2012 Notes). In October 2008, we purchased an aggregate of \$7.6 million aggregate principal amount of the 2012 Notes. The Company also purchased \$50.1 million of our outstanding 2012 Notes earlier in 2008. Following these purchases, approximately \$202.3 million of our 2012 Notes remain outstanding under the indenture. Our management and board of directors continue to monitor the opportunities to purchase our remaining outstanding 2012 Notes at or below the call price.

**Results of Operations****Specialist and Market-Making Segment Operating Results**

(000 \$ omitted)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,		Three Months 2008 vs. 2007	Nine Months 2008 vs. 2007
	2008	2007	2008	2007	Percentage Change	Percentage Change
<b>Revenues:</b>						
Net gain on principal transactions	\$ 84,089	\$ 32,876	\$ 188,242	\$ 145,525	155.8%	29.4%
Commissions and other fees	3,920	5,938	13,029	18,123	(34.0)	(28.1)
Net (loss) gain on investments	(30,489)	16,182	(136,962)	(37,791)	(288.4)	262.4
Interest income	15,195	51,418	59,071	177,364	(70.4)	(66.7)
Other	1,157	1,180	2,304	2,241	(1.9)	2.8
<b>Total segment revenues</b>	<b>73,872</b>	<b>107,594</b>	<b>125,684</b>	<b>305,462</b>	<b>(31.3)</b>	<b>(58.9)</b>
Fixed interest on debt		152	175	129	(100.0)	35.7
Inventory financing	23,834	63,812	75,447	213,113	(62.6)	(64.6)
<b>Revenues, net of interest expense</b>	<b>50,038</b>	<b>43,630</b>	<b>50,062</b>	<b>92,220</b>	<b>14.7</b>	<b>(45.7)</b>
Goodwill impairment				164,100		(100.0)
Specialist stock list impairment				335,264		(100.0)
Operating expenses	45,564	25,097	113,282	100,638	81.6	12.6
<b>Income (loss) before taxes</b>	<b>\$ 4,474</b>	<b>\$ 18,533</b>	<b>\$ (63,220)</b>	<b>\$ (507,782)</b>	<b>(75.9)%</b>	<b>(87.5)%</b>

## **Table of Contents**

Revenues from our Specialist and Market-Making segment consist primarily of net gains and losses resulting from our specialist activities in stocks and options, market-making activities in ETFs, options and futures, the net gains and losses resulting from trading of foreign currencies, futures and equities underlying the rights, ETFs and options for which we act as specialist, and accrued dividends receivable or payable on our equity positions.

Additionally, a significant component of the overall trading revenues is revenue generated by our Specialist and Market-Making segment consisting primarily of interest earned in securities lending transactions and inventory financing in connection with our trading in options, futures and ETFs which is aggregated with interest income and interest expense, respectively. These revenues are primarily affected by changes in share volume traded and fluctuations in prices of stocks, rights, options, ETFs and futures in which we are the specialist or in which we make a market.

Net gain on principal transactions represents trading gains net of trading losses and certain exchange imposed trading activity fees, where applicable, and are earned by us when we act as principal buying and selling our specialist stocks, rights, options, ETFs and futures.

Commissions and other fees revenue generated by our Specialist and Market-Making segment consists primarily of fees earned by our cash equity specialists for providing liquidity on the NYSE and, through July 9, 2007, for executing limit orders on the AMEX. The other fees in this line item are related to a specialist liquidity provision payment (the LPP ) program implemented on September 1, 2007, which varies month-to-month depending on our principal trading activities on the NYSE and an interim specialist allocation pool payment to us in the amount of \$2.1 million per month by the NYSE for the period from December 2006 through August 2007. The new LPP system involves a two tier fee structure based on (1) the firms proportional share of 100% of the consolidated tape revenue earned by the NYSE for quoting at the national best bid and offer, and (2) a subjective allocation from the NYSE of the LPP pool which consists of 25% of the NYSE s listed stock transaction revenue on matched volume. This monthly payment, in the aggregate, has been approximately \$1.4 million for each of the first nine months of 2008.

Net loss on investments reflects the aggregate losses generated from our investments in restricted and unrestricted NYX shares and other investments not derived specifically from specialist and market-making activities.

Other revenue at our Specialist and Market-Making segment consists primarily of miscellaneous receipts not derived specifically from specialist and market-making activities.

Interest expense attributable to our Specialist and Market-Making segment is the result of inventory financing costs relating to positions taken in connection with our options, futures and ETFs specialist and market-making operations and interest on subordinated indebtedness, up to June 3, 2008, that has been approved by the NYSE for inclusion in the net capital of LaBranche & Co. LLC.

## **Table of Contents**

Generally, an increase in the average daily share volume on the NYSE, an increase in volatility (as measured by the average closing price of the CBOE's Volatility Index<sup>®</sup>, or the VIX<sup>®</sup>), an increase in the dollar value and share volume of our principal shares or a decrease in program trading enables us to increase our level of principal participation and thus our ability to realize net gain on principal transactions. While we monitor these metrics each period, they are not the sole indicators or factors in any given period that determine our level of revenues, profitability or overall performance. Other factors, such as extreme price movements, unanticipated news and events and other uncertainties may influence our financial performance either positively or negatively.

### **Three Months Ended September 30, 2008 versus September 30, 2007**

The increase in our net gain on principal transactions was attributable to gains in our stock, option and ETF specialist and market-making principal trading revenue for the three months ended September 30, 2008 as compared to the same period in 2007. This increase in principal trading revenues was directly related to volatile trading conditions noted during the third quarter 2008, especially during the month of September 2008 when both the CBOE VIX Index and trading volumes increased simultaneously.

Commission and other fees revenue during the third quarter of 2008 decreased as the result of the NYSE rule change in December 2006 implementing the rebate program for certain specialist limit order transactions. In 2007, we received a specialist allocation pool payment in the amount of \$2.1 million per month from the NYSE, versus the average monthly commission in the third quarter of 2008 of approximately \$1.4 million.

Net (loss) gain on investments is mainly the result of the unrealized loss on our NYX shares of \$29.5 million, which represents the decline in the fair value of the NYX shares since June 30, 2008.

Interest income decreased primarily due to decreased trade finance interest income from stock borrow activity and lower interest rates during the third quarter of 2008 as compared to the third quarter of 2007.

Other revenue is mainly comprised of our receipt of the third quarterly dividend declared in September 2008 by the NYSE Euronext with respect to its common stock.

Interest expense decreased primarily as a result of decreased inventory financing costs relating to a decrease in our positions and lower interest rates relating to inventory financing costs such as margin interest.

**Table of Contents****Nine Months Ended September 30, 2008 versus September 30, 2007**

The increase in our net gain on principal transactions is directly related to our stock, option and ETF specialist and market making principal trading revenue for the nine months ended September 30, 2008 as compared to the same period in 2007. This increase in principal trading revenues was directly related to volatile trading conditions noted during the third quarter of 2008.

Commission and other fees revenue for the nine months ending September 2008 decreased as the result of the NYSE rule change in December 2006 implementing the rebate program for certain specialist limit order transactions. In 2007, we received a specialist allocation pool payment in the amount of \$2.1 million per month from the NYSE, versus the average monthly commission in the nine months of 2008 of approximately \$1.4 million.

Net (loss) gain on investments is directly related to a decrease in the share price of the NYX stock.

Stock borrow interest decreased mainly due to the decreased trading inventories for our non-cash equities specialist and market-making activities and lower interest rates during the first nine months of 2008.

Other revenue is mainly comprised of our receipt of the NYSE quarterly dividend.

For a discussion of operating expenses, see [Our Operating Expenses](#) below.

**Institutional Brokerage Segment Operating Results**

(000 s omitted)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,		Three Months 2008 vs. 2007	Nine Months 2008 vs. 2007
	2008	2007	2008	2007	Percentage Change	Percentage Change
<b>Revenues:</b>						
Net gain on principal transactions	\$ 545	\$ 469	\$ 1,489	\$ 752	16.2%	98.0%
Commissions	6,969	5,132	17,820	17,635	35.8	1.0
Net (loss) income on investments	(4,577)	1,298	(15,713)	(3,224)	(452.6)	387.4
Interest income	84	404	306	2,258	(79.2)	(86.4)
Other	105	(80)	296	(16)	(231.3)	(1950.0)
<b>Total segment revenues</b>	<b>3,126</b>	<b>7,223</b>	<b>4,198</b>	<b>17,405</b>	<b>(56.7)</b>	<b>(75.9)</b>
Inventory financing	7	12	14	913	(41.7)	(98.5)
<b>Revenues, net of interest expense</b>	<b>3,119</b>	<b>7,211</b>	<b>4,184</b>	<b>16,492</b>	<b>(56.7)</b>	<b>(74.6)</b>
Operating expenses	7,432	6,876	19,665	22,768	8.1	(13.6)
<b>(Loss) income before taxes</b>	<b>\$ (4,313)</b>	<b>\$ 335</b>	<b>\$ (15,481)</b>	<b>\$ (6,276)</b>	<b>(1387.5)%</b>	<b>146.7%</b>

Our Institutional Brokerage segment's commission revenue for 2007 includes fees charged to customers for execution, clearance (through June 8, 2007) and direct-access floor brokerage activities.



**Table of Contents**

Net loss on investments reflects the aggregated losses generated from our investments in restricted and unrestricted NYX shares as well as proprietary trading losses. Proprietary trading began in March 2008.

**Three Months Ended September 30, 2008 versus September 30, 2007**

Commission revenue increased primarily as a result of an increase of our institutional execution group's order-flow and trading volume.

Net loss on investments is directly related to a decrease in the share price of shares of NYX stock during the third quarter of 2008 as well as proprietary trading losses. The losses relating to the investment in NYX stock and to proprietary trading were \$2.5 million and \$2.1 million, respectively.

**Nine Months Ended September 30, 2008 versus September 30, 2007**

Net gain on principal transactions increased as a result of LFS trading and market making activity in OTC Bulletin Board and Pink Sheet securities containing nine months of activity in 2008 compared to five months in 2007.

Commission revenue decreased primarily as a result of a reduction in the number of our direct access customers. This decrease was offset by our growing institutional execution business commencing in May 2008 and the increase in commissions order flow in connection with this growing business.

Net loss on investments is directly related to a decrease in the share price of shares of NYX stock during the first nine months of 2008 as well as proprietary trading losses. The losses relating to the investment in NYX stock and to proprietary trading were \$11.1 million and \$4.6 million, respectively.

Effective June 8, 2007, LFS exited the clearing business. Therefore, there were no more stock borrow/loan transactions generating interest income/expense in 2008.

For a discussion of operating expenses, see [Our Operating Expenses](#) below.

**Other Segment Operating Results**

(000 \$ omitted)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,		Three Months 2008 vs. 2007	Nine Months 2008 vs. 2007
	2008	2007	2008	2007	Percentage Change	Percentage Change
Interest	\$ 851	\$ 3,051	\$ 4,146	\$ 7,257	(72.1)%	(42.9)%
Net loss on investments	(277)	(82)	(437)	(115)	237.8	280.0
Other	(262)	87	(197)	246	(401.1)	(180.1)
Total segment revenues	312	3,056	3,512	7,388	(89.8)	(52.5)
Fixed interest on debt	6,455	12,181	25,647	37,684	(47.0)	(31.9)
Revenues, net of interest expense	(6,143)	(9,125)	(22,135)	(30,296)	(32.7)	(26.9)
Early extinguishment of debt			6,005			100.0
Operating expenses	2,885	2,837	8,367	8,219	1.7	1.8
Loss before taxes	\$ (9,028)	\$ (11,962)	\$ (36,507)	\$ (38,515)	(24.5)%	(5.2)%

**Table of Contents**

The portion of our revenues that is not generated from our two principal business segments consists primarily of unrealized gains or losses on our non-marketable investments and interest income from short-term investments of our excess cash.

Revenues, net of interest expense, of our Other segment is calculated after netting revenues by the interest expense related to our public debt and interest accrued on reserves.

Interest expense mainly relates to the effective yield on our public debt inclusive of our debt issuance costs.

Operating expenses mainly relate to finance, accounting, tax, legal, treasury and human resource expenditures as well as related insurance and corporate governance costs and fees.

**Three Months Ended September 30, 2008 versus September 30, 2007**

Interest revenues decreased primarily as a result of cash balances decreasing by approximately \$91.1 million due to the repurchase of our 9.5% outstanding debt offset by return of capital from subsidiaries, as well as decreases in interest rates on our short term investments.

Net loss on investments increased as a result of increased losses on our non-marketable investments.

**Nine Months Ended September 30, 2008 versus September 30, 2007**

Interest revenues decreased primarily as a result of cash balances decreasing by approximately \$91.1 million due to the repurchase of our 9.5% outstanding debt offset by return of capital from subsidiaries, as well as decreases in interest rates on our short term investments.

Net loss on investments increased as a result of increased losses on our non-marketable investments.

**Table of Contents**

For a discussion of operating expenses, see [Our Operating Expenses](#) below.

**Our Operating Expenses**

(000 s omitted)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,		Three months 2008 vs. 2007	Nine months 2008 vs. 2007
	2008	2007	2008	2007	Percentage Change	Percentage Change
<b>Expenses:</b>						
Employee compensation and related benefits	\$ 34,955	\$ 13,522	\$ 83,079	\$ 61,608	158.5%	34.9%
Exchange, clearing and brokerage fees	12,357	10,062	32,758	29,713	22.8	10.2
Lease of exchange memberships and trading license fees	429	614	1,272	1,926	(30.1)	(34.0)
Depreciation and amortization	925	1,000	2,722	8,128	(7.5)	(66.5)
Goodwill impairment				164,100		(100.0)
Specialist stock list impairment				335,264		(100.0)
Restructuring		25		1,098	(100.0)	(100.0)
Extinguishment of debt			6,005			100.0
Other	7,215	9,587	21,483	29,152	(24.7)	(26.3)
<b>Total expenses</b>	<b>55,881</b>	<b>34,810</b>	<b>147,319</b>	<b>630,989</b>	<b>60.5</b>	<b>(76.7)</b>
(Benefit) provision for income taxes	\$ (3,280)	\$ 903	\$ (48,046)	\$ (184,077)	(463.2)%	(73.9)%

Our Specialist and Market-Making segment's employee compensation and related benefits expense consists of salaries, wages and performance-based compensation paid to our traders and related support staff based on operating results. The employee compensation and related benefits expense associated with our Institutional Brokerage segment consists of salaries, wages and performance-based compensation paid to certain institutional brokerage personnel based on their earned commissions or operating results. Performance-based compensation may include cash compensation and stock-based compensation granted to managing directors, trading professionals and other employees.

Exchange, clearing and brokerage fees expense at our Specialist and Market-Making segment consists primarily of fees paid by us to the NYSE, AMEX, other exchanges, the Depository Trust Clearing Corporation ( DTCC ) and to third party execution and clearing companies. The fees paid by us to these entities are primarily based on the volume of transactions executed by us as principal and as agent, a fee based on exchange seat use, technology fees, a flat annual fee and execution and clearing fees. Our Institutional Brokerage segment's exchange, clearing and brokerage fees expense consists of floor brokerage fees paid to direct-access floor brokers, fees paid for executions including those paid to exchanges and ECNs, and fees paid to our clearing firm.

Other operating expenses primarily are comprised of occupancy costs, such as office space and equipment leases and utilities, communications costs, insurance, professional, legal and consulting fees and restructuring costs.

**Three Months Ended September 30, 2008 versus September 30, 2007**

Employee compensation and related benefits increased primarily as a result of our bonus and incentive compensation being higher than the prior year based on an increase in trading results. This was partially offset by reduction to the base component of salary resulting from a reduction of headcount.

Exchange, clearing and brokerage fees increased primarily as a result of our increased trading activity.

Lease of exchange memberships and trading license fees decreased due to the reduced headcount in our cash equity specialist operations, which resulted in a decrease of the number of our NYSE trading licenses, and a decrease in the monthly fee per license.



## **Table of Contents**

The decrease in other operating expenses was due to decreases in legal fees, insurance, occupancy and communications.

### **Nine Months Ended September 30, 2008 versus September 30, 2007**

Employee compensation and related benefits increased primarily as a result of our bonus and incentive compensation being higher than the prior year based on an increase in trading results. This was partially offset by reduction to the base component of salary resulting from a reduction of headcount.

Exchange, clearing and brokerage fees increased primarily as a result of our increased trading activity.

Lease of exchange memberships and trading license fees decreased due to the reduced headcount in our cash equity specialist operations, which resulted in a decrease of the number of our NYSE trading licenses, and a decrease in the monthly fee per license.

Depreciation and amortization decreased as a result of the elimination of amortization related to our specialist stock list due to impairment in 2007.

Goodwill and stock list impairment charges were the result of interim impairment testing triggered by the sale of our AMEX cash equity specialist operations for below carrying value and changing market conditions associated with the HYBRID market.

Restructuring charges were the result of the planned reduction of workforce and related severance costs due to the automation of markets, general cost reductions and the outsourcing of the Institutional Brokerage segment's clearing operations to a major Wall Street firm in the earlier period.

Extinguishment of debt expenses are due to the acceleration of debt issuance costs and a call premium on the early retirement of portions of our public debt in the current period.

The decrease in other operating expenses was due to decreases in legal fees, insurance, occupancy and communications.

### **Liquidity and Capital Resources**

As of September 30, 2008, we had \$4,358 million in assets, of which \$229.4 million consisted of cash and short-term investments, primarily in overnight time deposits, government obligations maturing within thirty days and cash and securities segregated under federal regulations. To date, we have financed our operations primarily with cash flows from operations and proceeds from our debt and equity offerings. Due to the nature of the securities business and our role as a specialist, market-maker and execution agent, the amount of our cash and short-term investments, as well as operating cash flow, may vary considerably due to a number of factors, including the dollar value of our positions as principal, whether we are net

**Table of Contents**

buyers or sellers of securities, the dollar volume of executions by our customers and clearing house requirements, among others. Certain regulatory requirements constrain the use of a portion of our liquid assets for financing, investing or operating activities. Similarly, the nature of our business lines, the capital necessary to maintain current operations and our current funding needs subject our cash and cash equivalents to different requirements and uses.

As of September 30, 2008, our most significant long-term indebtedness was the \$209.9 million aggregate principal amount of our outstanding 11% Senior Notes that mature in May 2012. On October 9, 2008 the Company purchased an aggregate of \$7.6 million aggregate principal amount of its outstanding 11% Senior Notes due May 2012 below par. In the first quarter of 2008, we purchased and cancelled \$30.8 million of our outstanding 9 1/2% senior notes due 2009 and \$50.1 million of our 11% senior notes due 2012 in open market transactions. On May 23, 2008 the Company redeemed of all of the remaining outstanding 9 1/2% senior notes due 2009, in the aggregate principal amount of \$169.1 million, at a redemption price of 102.375%, plus accrued and unpaid interest thereon, pursuant to the optional redemption provisions of the indenture governing the notes.

At September 30, 2008, our net cash capital position was \$183.8 million. Fluctuations in net cash capital are common and are a function of variability in our total assets, balance sheet composition and total capital. We attempt to maintain cash capital sources in excess of our aggregate longer-term funding requirements (*i.e.*, positive net cash capital). Over the previous 12 months, our net cash capital has averaged above \$254.1 million.

	(\$ millions)	
	9/30/2008	9/30/2007
<b>Cash Capital Available:</b>		
Stockholders' equity	\$ 460.0	\$ 509.9
Subordinated debt		5.7
Long term debt > 1 year	209.9	459.8
Other holding company liabilities	40.2	38.9
<b>Total cash capital available</b>	<b>\$ 710.1</b>	<b>\$ 1,014.3</b>
<b>Cash Capital Required:</b>		
Regulatory capital (1)	\$ 79.4	\$ 224.3
Working capital	157.1	140.0
NYX unrestricted shares	81.7	165.0
Illiquid assets/long-term investments	197.8	191.5
Subsidiary intercompany	10.3	18.6
<b>Total Cash Capital Required</b>	<b>\$ 526.3</b>	<b>\$ 739.4</b>
<b>Net Cash Capital</b>	<b>\$ 183.8</b>	<b>\$ 274.9</b>

(1) In February 2008, our regulatory capital was reduced by \$200.0 million in connection with the NYSE's 75% reduction of the NLA specialist capital requirement. This amount was paid as a dividend to our holding company.

Cash Capital Available is mainly comprised of stockholders' equity, long term debt, subordinated debt and other liabilities of our parent holding company which, in the aggregate, constitute the currency used to purchase our assets and provide our working capital. This amount will principally be affected as debt matures or is refinanced and as earnings are retained or paid as dividends. Cash Capital Required mainly consists of the assets used in our

**Table of Contents**

businesses. Regulatory capital is defined as capital required by the SEC and applicable exchanges to be maintained by broker-dealers. It is principally comprised of cash, net equities, other investments and net receivables from other broker-dealers. Working capital constitutes liquid assets provided to our subsidiaries in excess of the required regulatory capital. Illiquid assets and long term investments are mainly comprised of exchange memberships, intangible assets, such as goodwill, tradename, deposits, deferred taxes and non-marketable investments. Net Cash Capital is considered to be the excess of Cash Capital Available over Cash Capital Required, or free cash, which we can utilize to fund our business needs.

We also monitor alternative funding measures in addition to our available net cash. The alternative funding measures are significant transactions and actions we could take in a short-term time frame to generate cash to meet debt maturities or other business needs. More precisely, as of September 30, 2008, we have identified the following alternative funding measures to support future debt maturity requirements:

Liquidation of available net invested capital at certain subsidiaries:

Reduction of excess capital at LaBranche & Co. LLC to only required NLA (i.e., declare and pay a dividend to the holding company of excess NLA):

Further reduction of NLA requirements by the NYSE and SEC: and

Our restricted and unrestricted NYX shares, as previously discussed, can be either sold or held as qualifying regulatory capital as their restrictions are removed. If the shares are held as qualifying regulatory capital, cash can be displaced from its current use as NLA capital.

<b>Alternative Funding Measures</b>	
<b>\$ millions</b>	
Net cash capital	\$ 183.8
Excess regulatory capital at subsidiaries (3)	62.0
NYX shares (1) (2)	40.8
 Total cash available from alternative funding measures	 \$ 286.6

(1) Computed on an after-tax basis and after a \$20.0 million reduction for NYX shares used as regulatory capital.

(2) Based on NYX price of \$39.18 per share on September 30, 2008.

(3) Subject to regulatory approval prior to distribution to the holding company.

Following our 2008 repurchases of senior and subordinated debt, the Company maintains its ability to repurchase in whole or in part the remaining senior notes at any time up to the maturity date without impacting the current operations at any of its trading subsidiaries. Moreover, we anticipate that the final removal of the NYX share restrictions in October 2008 will provide us a level of flexibility in managing debt servicing payments concurrently with the funding of our subsidiaries trading operations.

In addition to the alternative funding measures above, we monitor the maturity profile of our unsecured debt to minimize refinancing risk, and maintain relationships with debt investors and bank creditors. Strong relationships with a diverse base of creditors and debt investors are critical to our liquidity. We also maintain available sources of short-term funding that exceed actual utilization, thus allowing us to accommodate changes in investor appetite and credit capacity for our debt obligations.

---

**Table of Contents**

With respect to the management of refinancing risk, the maturity profile of our long-term debt portfolio is monitored on an ongoing basis. In 2004, we strategically refinanced our outstanding indebtedness and created two new series of senior notes maturing in 2009 and 2012 which represented a significant portion of our outstanding debt. On May 23, 2008, the Company redeemed all of its remaining outstanding 9 1/2% senior notes due 2009, in the aggregate principal amount of \$169.1 million, at a price of 102.375%, plus accrued and unpaid interest thereon, pursuant to the optional redemption provisions of the indenture governing the notes. Following the redemption, \$209.9 million of the Company's 11% Senior Notes due 2012 remains outstanding at September 30, 2008 under the indenture. Subsequently, on October 9, 2008 the Company purchased an aggregate of \$7.6 million aggregate principal amount of its outstanding 11% Senior Notes due May 2012. Our annual interest expense related to those remaining outstanding senior notes going forward is expected to be approximately \$22.3 million, excluding debt issuance cost amortization expense. The debt has available maturities and calls over the five-year period 2008 through 2012 to allow us maximum flexibility in satisfying the debt servicing payments and/or sufficient time to refinance the long-term debt, if necessary. The debt is redeemable at redemption prices of 105.50% on or after May 15, 2008, 102.75% on or after May 15, 2009 and 100.0% on or after May 15, 2010.

Our outstanding senior notes were issued pursuant to an indenture which includes certain covenants that, among other things, limit our ability to make certain investments, engage in transactions with stockholders and affiliates, create liens on our assets and sell assets or engage in mergers and consolidations, except in accordance with certain specified conditions. In addition, our ability to make so-called restricted payments, such as incurring additional indebtedness (other than certain permitted indebtedness), paying dividends, redeeming stock or repurchasing subordinated indebtedness prior to maturity, is limited if our consolidated fixed charge coverage ratio is at or below a threshold of 2.00:1. The consolidated fixed charge coverage ratio reflects a comparison between (1) our consolidated earnings before interest, taxes, depreciation and amortization expenses, or EBITDA, and (2) the sum of our consolidated interest expense and a tax-effected multiple of any dividend payments with respect to our preferred stock, and this ratio is calculated as of the end of the most recently completed fixed quarter on a trailing four quarter basis. As of September 30, 2008, our consolidated fixed charge coverage ratio, as defined, was 3.7:1. This ratio was impacted by the repurchase of the senior notes during the first half of 2008, because the indenture allows us to deem any indebtedness purchased in the trailing four quarter period as not outstanding throughout the period, thus giving pro-forma effect to the consolidated interest expense versus fixed debt.

While our fixed charge ratio is above 2.00:1, the indenture governing our outstanding senior notes enable us to make cumulative restricted payments in an amount that is not greater than (i) the sum of (A) 50.0% of our cumulative consolidated net income, as defined in the indenture, since July 1, 2004 (or, if such calculation is a loss, minus 100.0% of such loss) and (B) 100.0% of the net cash proceeds received from any issuance or sale of our capital stock since July 1, 2004, plus (ii) \$15.0 million. If our cumulative restricted payments since May 18, 2004



**Table of Contents**

at any time exceeds this restricted payment calculation, we will not be able to make any additional restricted payments. However, this calculation is recomputed each quarterly calendar period as allowed under the covenants in the indenture. As of September 30, 2008, 50% of our cumulative consolidated net income since July 1, 2004 was \$56.6 million, and we had received approximately \$1.4 million upon the exercise of options since July 1, 2004. When these amounts are added to the \$15 million allowance, as of September 30, 2008, we were entitled to make restricted payments of \$71.4 million, excluding the stock repurchases we made during the third quarter of \$1.6 million. We cannot be sure if, when or to what extent this covenant will prevent or limit us from making restricted payments in the future.

In April of 2008, the Board of Directors of the Company authorized a \$40.0 million share repurchase plan. While the restricted payment allowance would allow us to repurchase the full amount of shares under the plan, we have repurchased 371,753 of our shares under this plan during the first nine months of 2008 in the amount of \$1.6 million, or an average price of \$4.41 per share. In October 2008, we repurchased an additional 1,292,703 shares of our common stock for a total of purchase price of \$5.6 million, or an average of \$4.37 per share. We have funded, and will continue to fund, our share repurchases through a combination of cash from operations and excess cash at our holding company, dependent upon market conditions. As discussed above, the indenture governing our outstanding senior notes permits us to redeem some or all of the senior notes due 2012 on or after May 15, 2008 at varying redemption prices, depending on the date of redemption. In addition, under the terms of the indenture, if we sell substantially all our assets or experience specific kinds of changes in control, we will be required to offer to repurchase outstanding senior notes, on a pro rata basis, at a price in cash equal to 101.0% of their principal amount, plus accrued and unpaid interest, if any, to the date of purchase.

Any time we repurchase our outstanding senior notes, our fixed-term interest payments are correspondingly reduced. During 2008 we repurchased an aggregate of \$199.8 million aggregate principal amount of our outstanding 9 1/2% Senior Notes due 2009 and an aggregate of \$50.1 million aggregate principal amount of our outstanding 11% Senior Notes due 2012. These purchases of our outstanding senior notes resulted in annual interest savings of approximately \$24.5 million. Subsequently, on October 9, 2008 the Company purchased an aggregate of \$7.6 million aggregate principal amount of its outstanding 11% Senior Notes due May 2012 below par which will result in annual interest savings of approximately \$0.8 million. To the extent we repurchase any remaining outstanding 11% Senior Notes due 2012 in connection with future corporate strategic initiatives, our fixed-term interest payments would be correspondingly reduced.

As of September 30, 2008, the subordinated indebtedness of LaBranche & Co. LLC was repurchased and terminated in its entirety. This subordinated debt was comprised of senior subordinated notes and junior subordinated notes, which matured on various dates between June 2008 and April 2009 and bore interest at annual rates ranging from 7.7% to 10.0%. The senior subordinated notes were originally issued in the aggregate principal amount of \$15.0 million, and, in accordance with their terms, \$3.0 million in principal amount must be repaid on June 3 in each of the years 2004 through 2008. LaBranche & Co. LLC repaid \$3.0 million in accordance with these terms in each of June 2004 through 2008. In the second quarter of 2008, we repaid the remaining \$1.7 million in junior subordinated notes plus accrued and unpaid interest thereon.

## **Table of Contents**

As of September 30, 2008 and December 31, 2007, we had a tax receivable of \$0.5 million and \$11.8 million, respectively. The December 31, 2007 balance mainly relates to a Federal NOL carryback claim. In the second quarter 2008, the Company received an \$11.0 million federal tax refund for the 2007 net operating loss carry-back claim filed.

Our Other liabilities of \$12.4 million reflected on the accompanying 2008 consolidated statement of financial condition are principally comprised of tax contingencies pursuant to FIN 48. Such contingencies are considered long term, as there is no present obligation to pay such liabilities in the foreseeable future. During the third quarter the company completed a multi year tax audit with the local taxing authorities resulting in a \$1.6 million payment for that period for both taxes and interest. This resulted in a \$2.1 million reduction in our FIN 48 reserve balances of which \$0.5 million was recorded as a tax benefit in the current quarter.

### *Regulated Subsidiaries*

As a specialist and market-maker, we are required to maintain certain levels of capital and liquid assets as promulgated by various regulatory agencies which regulate our business. As part of our overall risk management procedures (for further discussion, refer to Part I, Item 3.

Quantitative and Qualitative Disclosures about Market Risk ), we attempt to balance our responsibility as specialist, market-maker and broker-dealer with our overall capital resources. These requirements restrict our ability to make use of cash and other liquid assets for corporate actions, such as repaying our debt, repurchasing stock or making acquisitions.

As a broker-dealer, LaBranche & Co. LLC is subject to regulatory requirements intended to ensure the general financial soundness and liquidity of broker-dealers and requiring the maintenance of minimum levels of net capital, as defined in SEC Rule 15c3-1. LaBranche & Co. LLC is required to maintain minimum net capital, as defined, equivalent to the greater of \$100,000 or  $\frac{1}{15}$  of aggregate indebtedness, as defined. NYSE Rule 326(c) also prohibits a broker-dealer from repaying subordinated borrowings, paying cash dividends, making loans to any parent, affiliates or employees, or otherwise entering into transactions which would result in a reduction of its total net capital to less than 150.0% of its required minimum capital. Moreover, broker-dealers are required to notify the SEC prior to repaying subordinated borrowings, paying dividends and making loans to any parent, affiliates or employees, or otherwise entering into transactions which, if executed, would result in a reduction of 30.0% or more of their excess net capital (net capital less minimum requirement). The SEC has the ability to prohibit or restrict such transactions if the result is deemed detrimental to the financial integrity of the broker-dealer. As of September 30, 2008, LaBranche & Co. LLC's net capital, as defined, was \$103.8 million, which exceeded the minimum requirements by \$102.9 million.

The NYSE generally requires its specialist firms to maintain a minimum dollar regulatory capital amount in order to establish that they can meet, with their own NLA, their position requirement. As of September 30 2008, LaBranche & Co. LLC's NYSE minimum

---

**Table of Contents**

required dollar amount of NLA, as defined, was \$76.1 million, and its actual NLA, as defined, was \$88.9 million. As of December 31, 2007, LaBranche & Co. LLC's minimum required dollar amount of NLA, as defined, was \$276.2 million and its actual NLA, as defined, was \$300.1 million. LaBranche & Co. LLC thus satisfied its NLA requirement as of each of those dates.

The minimum required dollar amount of NLA fluctuates daily and is computed by adding two components. The first component is equal to \$0.25 million for each one tenth of one percent (.1%), prior to February 2008 the first component was equal to \$1.0 million for each one tenth of one percent (.1%), of the aggregate NYSE transaction dollar volume in a cash equities specialist organization's allocated securities, as adjusted at the beginning of each month based on the prior month transaction dollar volume. The second component is calculated either by multiplying the average haircuts on a specialist organization's proprietary positions over the most recent twenty days by three, or by using an NYSE-approved value at risk (VAR) model. Based on this two part calculation, LaBranche & Co. LLC's NLA requirement could increase or decrease in future periods based on its own trading activity and all other specialists' respective percentages of overall NYSE transaction dollar volume.

In February 2008, the SEC approved, with immediate effect, an approximate 75% reduction in the required NLA that need to be maintained by cash equity specialists to transact business on the NYSE. This resulted in a reduction of our required NLA by approximately \$205.0 million, of which \$200.0 million was moved at such time to our holding company for other current or future corporate purposes. In May 2008, LaBranche & Co. LLC distributed \$10.0 million of excess NLA to the holding company. Pursuant to these NLA rules, LaBranche & Co. LLC is entitled to use unrestricted shares of NYX stock as NLA, instead of cash for regulatory capital, subject to risk-based haircuts. As a result, LaBranche & Co. LLC's NLA as of September 30, 2008 includes approximately \$32.8 million in NYX shares (after the risk-based haircuts). Since our \$205.0 million NLA reduction was implemented in February 2008, the majority of the amended NLA requirement can be met by the NYX shares held by LaBranche & Co. LLC. The amended NLA requirements enabled LaBranche & Co. LLC to declare a dividend distribution of \$200.0 million to us, which was paid in February and March 2008, and which left LaBranche & Co. LLC with \$12.8 million in cash as a cushion over and above the NYX shares used to satisfy the continuing NLA requirement.

As a registered broker-dealer and member firm of the NYSE, LFS is also subject to SEC Rule 15c3-1, as adopted and administered by the SEC and the NYSE. Under the alternative method permitted by this rule, the minimum required net capital is equal to the greater of \$1.0 million or 2.0% of aggregate debit items, as defined. As of September 30, 2008 and December 31, 2007, LFS' net capital, as defined, was \$31.0 million and \$16.6 million, respectively, which exceeded minimum requirements by \$30.0 million and \$15.6 million, respectively.

LFS is also subject to SEC Rule 15c3-3 because it maintains a soft dollar program that may result in credit balances to such clients. As of October 2, 2008, to comply with its September 30, 2008 requirement, cash and U.S. Treasury Bills in the amount of \$1.5 million were segregated in a special reserve account for the exclusive benefit of customers, thus

---

**Table of Contents**

exceeding actual requirements by \$0.2 million. As of January 3, 2008, to comply with its December 31, 2007 requirement, cash and U.S. Treasury Bills in the amount of \$1.6 million were segregated in a special reserve account for the exclusive benefit of customers, exceeding actual requirements by \$0.2 million.

As a registered broker-dealer and AMEX member firm, LSP is subject to SEC Rule 15c3-1, as adopted and administered by the SEC and the AMEX. LSP is required to maintain minimum net capital, as defined, equivalent to the greater of \$100,000 or  $\frac{1}{15}$  of aggregate indebtedness, as defined. As of September 30, 2008 and December 31, 2007, LSP's net capital, as defined, was \$110.2 million and \$62.6 million, respectively, which exceeded minimum requirements by \$107.8 million and \$60.9 million, respectively. LSP's aggregate indebtedness to net capital ratio on those dates was .32 to 1 and .41 to 1, respectively.

As a registered broker-dealer and AMEX and FINRA member firm, LSPD is subject to SEC Rule 15c3-1, as adopted and administered by the SEC, AMEX and FINRA. LSPD is required to maintain minimum net capital, as defined, equivalent to the greater of \$5,000 or  $\frac{1}{15}$  of aggregate indebtedness, as defined. As of September 30, 2008 and December 31, 2007, LSPD's net capital, as defined, was \$2.8 million and \$3.0 million, respectively, which exceeded its minimum requirement by \$2.8 million and \$3.0 million, respectively. LSPD's aggregate indebtedness to net capital ratio on those dates was .01 to 1 and .001 to 1, respectively.

As a registered broker dealer in the United Kingdom, LSPE is subject to the capital adequacy and capital resources as managed and monitored in accordance with the regulatory capital requirements of the Financial Services Authority ( FSA ). In calculating regulatory capital, the Company's capital consists wholly of Tier 1 capital. Tier 1 capital is the core measure of a Company's financial strength from a regulator's point of view. It consists of the type of financial capital considered the most reliable and liquid, primarily Shareholder's Equity. As of September 30, 2008 Tier 1 capital, as defined, was \$31.0 million which exceeded the total variable capital requirement by \$12.3 million. At December 31, 2007 Tier 1 capital, as defined, was \$14.2 million which resulted in a deficit of \$1.2 million. The December 31, 2007 calculation did not include accumulated profits for the year ended December 31, 2007 which was in excess of the deficit. With those results now audited they can be included in Tier 1 regulatory capital. In addition, the Company had injected an additional \$9.9 million of share capital in January 2008 further enhancing regulatory capital.

As a licensed corporation registered under the Hong Kong Securities and Futures Ordinance, LSPH is also subject to the capital requirements of the Hong Kong Securities and Futures (Financial Resources) Rules ( FRR ). The minimum paid-up share capital requirement is HKD 5,000,000 (\$0.6 million at September 30, 2008 and December 31, 2007) and the minimum liquid capital requirement is the higher of HKD 3,000,000 (\$0.4 million at September 30, 2008 and December 31, 2007) and the variable required liquid capital as defined in the FRR. The Company monitors its compliance with the requirements of the FRR on a daily basis. As of September 30, 2008 and December 31, 2007, LSPH's liquid capital, as defined was \$0.6 and \$0.7 million, respectively, which exceeded its minimum requirements by \$0.2 and \$0.3 million, respectively. In addition, we had injected an additional \$0.5 million of share capital in June 2008 further enhancing regulatory capital.

## **Table of Contents**

Failure by any of our broker-dealer subsidiaries to maintain its required net capital and NLA, where applicable, may subject it to suspension or revocation of its SEC registration or its suspension or expulsion by the NYSE, the AMEX and/or any other exchange of which it is a member firm.

As evidenced by the foregoing requirements, our broker-dealer subsidiaries require a substantial amount of capital. In particular, even as amended, LaBranche & Co. LLC's NLA requirement limits our ability to utilize a substantial portion of our liquid assets for other corporate purposes.

### *Cash Flows*

Our cash and cash equivalents decreased \$276.7 million to \$227.9 million at the end of the third quarter of 2008. The decrease was primarily the result of the aggregate net effects of \$259.4 million repayments of debt, \$1.6 million for the purchase of treasury stock, \$1.8 million for capital asset additions and a \$13.1 million net decrease from operating activities comprised of cash flow of \$47.0 million from operating income and a \$60.1 million increase in working capital.

### **Credit Ratings**

Our outstanding senior notes were originally sold in private sales to institutional investors on May 18, 2004, and substantially all these senior notes were subsequently exchanged for substantially identical senior notes registered under the Securities Act of 1933, as amended, pursuant to the terms of our May 2004 debt refinancing.

In September 2007, Moody's Investor Services changed its credit rating of our outstanding senior notes from B1 to B2 but continued a stable outlook due to our high quality balance sheet and improved liquidity.

In August 2008, the Management of the Company determined that only one rating agency was necessary to provide a rating for the outstanding senior notes. As such, the Company terminated its relationship for credit rating services from Standard & Poor's Investor Services. The Company still engages the credit rating services from Moody's.

### **Off-Balance Sheet Arrangements**

We have no off-balance sheet arrangements that have a material current effect or that are reasonably likely to have a material future effect on our financial position or results of operations.

### **Contractual Obligations**

During the first nine months of 2008, there were no significant changes in our reported payments due under contractual obligations and disclosed contingent contractual obligations at December 31, 2007, as described in our 2007 Form 10-K.

## **Table of Contents**

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk.**

Due to regulatory requirements that prescribe communication barriers between our broker-dealer subsidiaries, we employ different compliance risk management procedures at each such subsidiary. These risk processes are set forth below:

#### *Our Cash Equities Specialist Risk Management Process*

Because our cash equities specialist activities on the NYSE expose our capital to significant risks, managing these risks is a constant priority for us. Our central role in the HYBRID market helps us to manage risks by incorporating up-to-date market information in the management of our inventory, subject to our specialist obligations. We have developed a risk management process at our LaBranche & Co. LLC subsidiary that is designed to balance our ability to profit from our specialist activities with our exposure to potential losses and compliance risk. This risk management process includes participation by our corporate compliance committee, executive operating committee, floor management committee, post managers, floor captains, specialists and chief risk officer. These parties' roles are as follows:

*Corporate Compliance Committee.* LaBranche & Co. LLC's corporate compliance committee consists of representatives from executive and senior management, compliance personnel, including our on-floor compliance officer, our general counsel, our chief regulatory officer and several additional senior floor specialists, known as post managers. The role of the corporate compliance committee is to monitor and report to senior management on the statutory and regulatory compliance efforts of our specialist business. The corporate compliance committee also advises the compliance department in establishing, reviewing and revising our policies and procedures governing LaBranche & Co. LLC's regulatory compliance structure.

*Executive Operating Committee.* Our executive operating committee is composed of two executive officers. This committee is responsible for approving all risk management procedures and trading guidelines for our specialist stocks, after receiving recommendations from our floor management committee. In addition, our executive operating committee reviews all unusual situations reported to it by our floor management committee.

*Floor Management Committee.* Our NYSE floor management committee is currently composed of one senior floor manager, six post managers, one wheel manager and one floor administrative personnel manager. This committee is responsible for formulating and overseeing our overall risk management procedures and trading guidelines for each of our specialist stocks. In determining these procedures and guidelines, the floor management committee considers the recommendations of the floor captains. The post managers generally meet with their respective floor captains on a weekly basis to review and, if necessary, revise the risk management procedures and trading guidelines for particular specialist stocks. The wheel managers ensure that the floor is adequately staffed at all times. In addition, post managers, wheel managers and floor captains are always available on the trading floor to review and assist with any unusual trading situations reported by a floor captain, and the swat-team manager is available to assess and provide assistance on break-out, or intense trading situations. Our floor management committee reports to our executive operating committee.

## **Table of Contents**

about each of these trading situations as they occur. Our floor management committee also trains other specialists and trading assistants on a regular basis on new rules and/or interpretations from the NYSE with respect to our specialist obligations and guidelines, with the assistance of our compliance department.

*Floor Captains.* We currently employ four floor captains who monitor the activities of our cash equities specialists throughout the trading day from various positions at our trading posts. The floor captains observe trades and constantly review trading activities on a real-time basis. In addition, the floor captains are readily available to assist our specialists in determining when to deviate from procedures and guidelines in reacting to any unusual situations or market conditions. The floor captains report these unusual situations and any deviations from these procedures and guidelines to their respective post managers. Floor captains meet with each specialist at least once a week to evaluate each specialist's adherence to our risk management procedures and trading guidelines, as well as to review compliance reports generated by the compliance department in monitoring and reviewing specialist trading activities. Floor captains also meet to review risk procedures and guidelines and, if appropriate, make recommendations to the floor management committee.

*Specialists.* Our specialists conduct electronic and, at times, manual auctions of our specialist stocks based upon the conditions of the marketplace. In doing so, specialists observe our risk management procedures and trading guidelines in tandem with their responsibility to create and maintain a fair and orderly market. Specialists promptly notify a floor captain of any unusual situations or market conditions requiring a deviation from our procedures and guidelines.

*On-Floor Compliance Officer.* We also have an on-floor compliance officer that monitors the specialists' compliance with NYSE rules throughout the day on an ad hoc basis. The on-floor compliance officer reports his findings and on general on-floor compliance initiatives on a daily basis to our equity specialist unit's Chief Compliance Officer and Chief Executive Officer and provides summary updates of these efforts to the Corporate Compliance Committee on a monthly basis. In addition, we have at least one trading assistant at each post on the NYSE floor who is compliance-registered and able to review trading activities to monitor compliance with rules. Many of our compliance and risk management activities flow from the efforts of our on-floor compliance initiative.

*Electronic Exception Reports.* We have implemented a system of electronic rule exception reports at our LaBranche & Co. LLC subsidiary to monitor our compliance with NYSE and SEC rules. These reports are generated on a daily basis, from one to three days after each trading day, and are the result of significant development efforts from our technology group, with advice of our compliance and legal staff. Our compliance staff reviews these exception reports daily, and in the event an exception is detected, the exception is researched in detail by our on-floor compliance officer or another compliance officer to determine if a compliance issue is found. If a compliance issue is detected, we make an effort to correct the problem and conduct training of our specialists and/or distribute compliance bulletins to ensure our specialists understand the rule and processes going forward. Certain detected issues are discussed at monthly compliance committee meetings.

## **Table of Contents**

We believe that enhancements we have made to our compliance procedures and guidelines, and on a continuous basis as circumstances warrant, have continued to improve our risk management process.

*Circuit Breaker Rules.* The NYSE has instituted certain circuit breaker rules intended to halt trading in all NYSE listed stocks in the event of a severe market decline. The circuit breaker rules impose temporary halts in trading when the Dow Jones Industrial Average drops a certain number of points. Current circuit breaker levels are set quarterly at 10, 20 and 30 percent of the Dow Jones Industrial Average closing values of the previous month, rounded to the nearest 50 points. These rules provide investors extra time to respond to severe market declines and provide us an additional opportunity to assure compliance with our risk management procedures.

### *Equity Market Financial Risk*

We have developed a risk management process, which is intended to balance our ability to profit from our equity specialist activities with our exposure to potential losses. We have invested substantial capital, along with the NYSE, in real-time, on-line systems which give our management, including our chief risk officer, access to specific trading information during the trading day, including our aggregate long and short positions and our capital and profit-and-loss information on an aggregate or per issue basis. Subject to the specialist's obligation to maintain a fair and orderly market and to applicable regulatory requirements, we constantly seek to manage our trading positions relative to existing market conditions.

Our equity specialist trading activities are subject to a number of risks, including risks of price fluctuations, rapid changes in the liquidity of markets and foreign exchange risk related to American Depositary Receipts ( ADRs ). In any period, we may incur trading losses or gains in our specialist stocks for a variety of reasons, including price fluctuations of our specialist stocks and fulfillment of our specialist obligations. Quantification of such losses or gains would not be meaningful as standard market studies do not capture our specialist obligations. From time to time, we may have large position concentrations in securities of a single issuer or issuers engaged in a specific industry. In general, because our inventory of securities is marked-to-market on a daily basis, any significant price movement in these securities could result in an immediate reduction of our revenues and operating profits.

### *Our Options, Futures and ETFs Specialist and Market-Making Risk Management Process*

As specialists in options, ETFs and futures in our LSH group of entities, we have a responsibility to maintain a fair and orderly market, and trade securities as principal out of both obligation and inclination. Our options, ETFs, futures, U.S. Government obligations and foreign currency specialist trading exposes us to certain risks, such as price and interest rate fluctuations, volatility risk, credit risk, foreign currency movements and changes in the liquidity of markets.

Additionally, as a market-maker in options, ETFs and futures through our LSH Group of entities, we also trade as principal. In our market-making function, we bring immediacy and liquidity to the markets when we participate. Our market-making activities expose us to certain risks, including, but not limited to, price fluctuations and volatility.



**Table of Contents**

In connection with our specialist and market-making activities, we are engaged in various securities trading and lending activities and assume positions in stocks, rights, options, ETFs, U.S. Government securities, futures and foreign currencies for which we are exposed to credit risk associated with the nonperformance of counterparties in fulfilling their contractual obligations pursuant to these securities transactions. We are also exposed to market risk associated with the sale of securities not yet purchased, which can be directly impacted by volatile trading on the NYSE, the AMEX and other exchanges. Additionally, in the event of nonperformance and unfavorable market price movements, we may be required to purchase or sell financial instruments at a loss.

Our traders purchase and sell futures, options, the stocks underlying certain ETF and options positions, U.S. Government securities and foreign currencies in an attempt to hedge market and foreign currency risk. Certain members of management, including our chief risk officer, who oversee our options, futures and ETFs specialist and market making activities are responsible for monitoring these risks. These managers utilize a third-party software application, as well as information received directly from the traders, to monitor specialist and market-making positions on a real-time basis. By monitoring actual and theoretical profit and loss, volatility and other standard risk measures, these individuals seek to insure that our traders operate within the parameters set by management. Furthermore, our aggregate risk in connection with our options, futures and ETFs trading is under constant evaluation by certain members of management and our traders, and all significant trading strategies and positions are closely monitored. When an unusual or large position is observed by the chief risk officer, he communicates the issue to senior management, who communicate with the trader to understand the strategy and risk management behind the trade and, if necessary, determine avenues to mitigate our risk exposure. Our options, futures and ETFs trading is executed on national and foreign exchanges. These trades clear through the Options Clearing Corporation, the National Securities Clearing Corporation or the applicable exchange clearing organization, which reduces potential credit risk.

The following chart illustrates how specified movements in the underlying securities prices of the options, futures and ETFs in our specialist and market-making portfolios would have impacted profits and losses:

(000 s omitted)	Profit or (Loss) if the underlying securities move:				
	-15.0%	-5.0%	0%	+5.0%	+15.0%
<b>Portfolio as of:</b>					
December 31, 2007	\$ (5,193)	\$ (443)	\$ 0	\$ 3,903	\$ 12,259
March 31, 2008	\$ (3,331)	\$ (897)	\$ 0	\$ 4,295	\$ 24,456
June 30, 2008	\$ 49,381	\$ 9,122	\$ 0	\$ (57)	\$ 14,997
September 30, 2008	\$ 25,142	\$ 6,234	\$ 0	\$ (3,247)	\$ (1,632)

The modeling of the risk characteristics of our trading positions involves a number of assumptions and approximations. While management believes that these assumptions and approximations are reasonable, there is no standard methodology for estimating this risk, and

**Table of Contents**

different methodologies would produce materially different estimates. The zero percent change column represents the profit or loss our options, futures and ETFs specialist operations would experience on a daily basis if the relevant market remained unchanged.

*Foreign Currency Risk & Interest Rate Risk*

In connection with the trading of U.S.-registered shares of foreign issuers in connection with our cash equities specialist operations, we are exposed to varying degrees of foreign currency risk. The pricing of these securities is based on the value of the ordinary securities as denominated in their local currencies. Thus, a change in a foreign currency exchange rate relative to the U.S. dollar will result in a change in the value of U.S.-registered shares in which we are the specialist.

Our ETF specialists and market-makers trade international ETFs that are denominated and settled in U.S. dollars, but the pricing of these ETFs is also affected by changes in the relevant foreign currency rates. We, therefore, hold various foreign currencies in order to lessen the risks posed by changing foreign currency exchange rates. In addition, LSP trades derivatives denominated in foreign currencies, which creates exposure to foreign currency risk.

The following chart illustrates how the specified movements in foreign currencies relative to the U.S. dollar to which our specialist and market-making activities are exposed would have impacted our profits and losses:

(000 s omitted)	Profit or (Loss) if the foreign currencies relative to the U.S. dollar move:			
	-15.0%	-5.0%	+5.0%	+15.0%
<b>Portfolio as of:</b>				
December 31, 2007	\$ (1,930)	\$ (643)	\$ 643	\$ 1,930
March 31, 2008	\$ 7,398	\$ 2,466	\$ (2,466)	\$ (7,398)
June 30, 2008	\$ 7,616	\$ 2,539	\$ (2,539)	\$ (7,616)
September 30, 2008	\$ 5,664	\$ 1,888	\$ (1,888)	\$ (5,664)

The information in the above table is based on certain assumptions and it does not fully represent the profit and loss exposure to changes in foreign currency exchange rates, security prices, volatility, interest rates and other related factors.

As specialists and market makers in options, ETFs and futures, we generally maintain large specialist and market maker positions. Historically, we have been operating in a low and moderate interest rate market. As such, we may be sensitive to interest rate increases or decreases and/or widening credit spreads may create a less favorable operating environment for this line of business.

*Concentration Risk*

We are subject to concentration risk by holding large positions or committing to hold large positions in certain types of securities. As of September 30, 2008, our largest unhedged proprietary position is our NYX shares. This concentration does not arise in the normal course of business.

## **Table of Contents**

### *Institutional Brokerage Risk*

Our Institutional Brokerage segment, through the normal course of business, enters into various securities transactions acting in an agency or principal basis. The execution of these transactions can result in unrecorded market risk and concentration of credit risk. Our Institutional Brokerage activities involve execution and financing of various customer securities transactions on a cash or margin basis. These activities may expose us to risk in the event the customer or other broker is unable to fulfill its contractual obligations and we have to purchase or sell securities at a loss. For margin transactions, we may be exposed to significant market risk in the event margin requirements are not sufficient to fully cover losses that customers may incur in their accounts.

### *Institutional Brokerage Risk Management Process*

Our institutional brokerage activities require that we execute transactions in accordance with customer instructions and accurately record and process the resulting transactions. Any failure, delay or error in executing, recording and processing transactions, whether due to human error or failure of our information or communication systems, could cause substantial losses for brokers, customers and/or us and could subject us to claims for losses. We also, at times, execute orders as principal in order to facilitate customer transactions. To monitor the risk in these positions, we use an internally developed desk-top system that is constantly running on the desktop screens of our institutional brokerage firm's senior management, chief compliance officer and trading systems manager. Upon escalation to other members of senior management, research and diligence is performed as to the positions and risk and determinations are made as to how to limit the exposure. Once a position is established, our traders may attempt to manage the risk associated with the position by use of ETF strategies, futures on the S&P 500, or with an industry/sector comparable security or other method approved by senior management. Despite these risk management efforts, these facilitation positions may result in trading losses that could adversely affect our commission revenues.

Since June 8, 2007 our customer margin transactions have been cleared through a major Wall Street firm. These customer margin transactions are financed by the clearing firm based on our instructions. We are liable to the clearing firm for any losses incurred by the clearing firm in connection with our customers' margin transactions.

Our past clearing activities (through June 8, 2007) included settling each transaction with both the contra broker and the customer. In connection with our institutional and direct access floor brokerage activities, a transaction was settled either when the customer paid for securities purchased and took delivery, or delivered securities sold for payment. Settling transactions for retail customers and professional investors involved financing the transaction until the customer made payment or, for margin accounts, advancing credit to the customer within regulatory and internal guidelines. Clearing direct access brokers' transactions included guaranteeing their transactions to the contra broker on the exchange floor.

**Table of Contents**

These clearing activities may have exposed us to off-balance sheet risk in the event customers or brokers were unable to fulfill their contractual obligations and it was necessary to purchase or sell securities at a loss. For margin transactions, we may have been exposed to off-balance sheet risk in the event margin requirements were not sufficient to fully cover losses that customers may have incurred in their accounts.

The amount of risk related to our execution and clearance activities was linked to the size of the transaction, market volatility and the creditworthiness of customers and brokers. Our largest transactions involved those for institutional and direct access floor brokerage customers.

We systematically monitor our open transaction risk in connection with our institutional brokerage activities, starting when the transaction occurs and continuing until the designated settlement date. Transactions that remain unsettled after settlement date are scrutinized and necessary action to reduce risk is taken. Even under our new clearing arrangement with a major Wall Street firm, credit risk that could result from contra brokers defaulting is minimized since much of the settlement risk for transactions with brokers is essentially transferred to the National Stock Clearing Corporation. The credit risk associated with institutional and direct access clearing customers is minimized since these customers have been qualified by the Depository Trust Company ( DTC ) or the DTC participants or have met the prime broker qualification standards at other brokerage firms. Before conducting business with a prospective customer, senior management that oversees our institutional brokerage operations, in conjunction with the related compliance department, reviews the prospective customer's experience in the securities industry, financial condition and personal background, including a background check with a risk reporting agency, although some of this responsibility now is undertaken by our outsourced clearing firm.

The following chart illustrates how specified movements in the underlying securities prices in our institutional brokerage portfolios would have impacted profits and losses:

(000 s omitted)	Profit or (Loss) if the underlying securities move:				
	-15.0%	-5.0%	0%	+5.0%	+15.0%
<b>Portfolio as of:</b>					
December 31, 2007	\$ (53)	\$ (18)	\$ 0	\$ 18	\$ 53
March 31, 2008	\$ (113)	\$ (37)	\$ 0	\$ 37	\$ 113
June 30, 2008	\$ 501	\$ 167	\$ 0	\$ (167)	\$ (501)
September 30, 2008	\$ (965)	\$ (321)	\$ 0	\$ 321	\$ 965

*Operational and Technology Risk*

Operational risk relates to the risk of loss from external events, and from failures in internal processes or information systems. In each of our business segments, we rely heavily on our information systems in managing our risk. Accordingly, working in conjunction with the NYSE and other exchanges, we have made significant investments in our trade processing and execution systems. Our use of, and dependence on, technology has allowed us to sustain our growth over the past several years. Management members and floor captains at our NYSE cash equities specialist operations constantly monitor our positions and transactions in order to mitigate our risks and identify troublesome trends should they occur. The substantial capital we have invested, along with the NYSE, in real-time, on-line systems affords management instant access to specific trading information at any time during the trading day, including:

our aggregate long and short positions;

**Table of Contents**

the various positions of each of our trading professionals;

our overall position in a particular stock; and

capital and profit-and-loss information on an aggregate, per specialist or per issue basis.

Our information systems send and receive data from the NYSE through dedicated data feeds. The NYSE supplies us with specialist position reporting system terminals both on the trading floor and in our offices. These terminals allow us to monitor our NYSE specialist trading profits and losses, as well as our positions. Our options, futures and ETFs specialist and market-making operations utilize a third-party software application to monitor our positions and profits and losses on a real-time basis.

We internally develop and use significant proprietary trading technologies in our specialist and market-making segment in order to enhance our principal trading capabilities and manage risk in the increasingly evolving electronic marketplace. Our trading technologies are developed and maintained by our information technology personnel and their development process is subject to policies and procedures designed to mitigate the risk of technology design flaws and programming errors. These policies and procedures include, but are not limited to, policies concerning the techniques and manner by which new or enhanced trading technologies are implemented, segregation of duties among the developers, the quality assurance personnel and the individual who enters new trading technologies into production and, when possible, independent review of these technologies and procedures. Although these, and other, policies and procedures are designed to mitigate the risk of design, coding or other flaws or errors in our current and future trading technologies, we cannot assure you that these policies and procedures will successfully be followed or will timely and effectively detect such flaws or errors.

We have developed and implemented a business continuity plan, which includes a comprehensive disaster recovery plan. We have a back-up disaster recovery center in New York, outside of Manhattan as well as redundant trading facilities in London, England and Hong Kong.

*Legal and Regulatory Risk*

Substantial legal liability or a significant regulatory action against us could have a material adverse effect on our financial condition or cause significant harm to our reputation, which in turn could negatively affect our business prospects.

Our registered broker-dealer subsidiaries are subject to certain regulatory requirements intended to insure their general financial soundness and liquidity. These broker-dealers are subject to SEC Rules 15c3-1, 15c3-3 and other requirements adopted and administered by the SEC and the NYSE.

## **Table of Contents**

The USA PATRIOT Act of 2001 requires U.S. financial institutions, including banks, broker-dealers, futures commission merchants and investment companies, to implement policies, procedures and controls which are reasonably designed to detect and report instances of money laundering and the financing of terrorism. We actively monitor and update our anti-money laundering practices.

### **Item 4. Controls and Procedures**

As of the end of the period covered by this report, an evaluation of the effectiveness of our disclosure controls and procedures was performed under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that these disclosure controls and procedures were effective as of the end of the period covered by this report. In addition, no change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934) occurred during the quarter ended September 30, 2008 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## **PART II OTHER INFORMATION**

### **Item 1. Legal Proceedings**

There have been no material new developments in our legal proceedings since the March 17, 2008 filing of the 2007 Form 10-K, the May 12, 2008 filing of the First Quarter 10-Q1 and the August 11, 2008 filing of the Second Quarter 10-Q, except as follows:

In re LaBranche Securities Litigation. As previously reported, on February 8, 2008, we entered into an agreement in principle to settle the action for \$13 million, to be paid entirely by our insurers, subject to completion of a usual and customary settlement agreement, notice to the class, and approval by the Court. On September 19, 2008, the parties submitted a settlement agreement to the Court. On September 22, 2008, the Court preliminary approved the settlement. Notice has been provided to the class, and the settlement remains subject to final approval by the Court.

Sea Carriers, L.P. v. NYSE Euronext, et al. On August 20, plaintiff voluntarily dismissed this action without prejudice. No payment was made by us or any other defendant in the case.

We believe that the claims asserted against us by the plaintiffs in the pending proceedings described in the 2007 Form 10-K, the First Quarter 10-Q, the Second Quarter Form 10-Q and above are without merit, and we deny all allegations of wrongdoing. There can be no assurance, however, as to the outcome or timing of the resolution of these proceedings. We therefore are unable to estimate the amount or potential range of any loss that may arise out of these proceedings. The range of possible resolutions could include determinations and judgments against us or settlements that could require substantial payments by us that could have a material adverse effect on our financial condition, results of operations and cash flows.

**Table of Contents**

In addition to the proceedings described in the 2007 Form 10-K, the First Quarter 10-Q, the Second Quarter Form 10-Q and above, we and our operating subsidiaries have been the target, from time to time, of various claims, lawsuits and regulatory inquiries in the ordinary course of our and their respective businesses. While the ultimate outcome of those claims and lawsuits which currently are pending cannot be predicted with certainty, we believe, based on our understanding of the facts of these proceedings, that their ultimate resolution will not, in the aggregate, have a material adverse effect on our financial condition, results of operations or cash flows.

**Item 1A. Risk Factors**

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in the 2007 Form 10-K, which could materially affect our business, financial condition or future results. There have been no material changes in the Risk Factors disclosed in our 2007 Form 10-K. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

On April 17, 2008, our Board of Directors authorized the repurchase of up to \$40.0 million in shares of our common stock. In the third quarter of 2008, we repurchased 371,753 shares at a cost of approximately \$1.6 million. We have funded, and will continue to fund, our share repurchases through a combination of cash from operations, and excess cash at our holding company, dependent upon market conditions.

<b>Purchase Period</b>	<b>Total Number of Shares Purchased</b>	<b>Average Price Paid per Share (1)</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs</b>
September 1 - September 30, 2008	371,753	\$ 4.41	371,753	(2)
Total	371,753	\$ 4.41	371,753	(2)

(1) Average Price Paid per Share excludes transaction costs.

(2) Since board approval of repurchases is based on dollar amount, the Company cannot estimate the number of shares yet to be purchased.

## **Table of Contents**

### **Item 5. Other Information**

We have included in this Form 10-Q filing, and from time to time our management may make, statements which may constitute forward-looking statements within the meaning of the safe harbor provisions of The Private Securities Litigation Reform Act of 1995. Our quarterly and annual operating results are affected by a wide variety of factors that could materially and adversely affect actual results, including a decrease in trading volume on the exchanges on which we operate, changes in volatility in the equity and others securities markets and changes in the value of our securities positions. As a result of these and other factors, we may experience material fluctuations in future operating results on a quarterly or annual basis, which could materially and adversely affect our business, financial condition, operating results and stock price. An investment in us involves various risks, including those mentioned above and those that are detailed from time to time in our SEC filings.

Certain statements contained in this report, including without limitation, statements containing the words believe, intend, expect, anticipate and words of similar import, also may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Readers are cautioned that any such forward-looking statements are not guarantees of future performance, and since such statements involve risks and uncertainties, our actual results and performance and the performance of the specialist industry as a whole, may turn out to be materially different from the results expressed or implied by such forward-looking statements. Given these uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements. We also disclaim any obligation to update our view of any such risks or uncertainties or to publicly announce the result of any revisions to the forward-looking statements made in this report.

### **Item 6. Exhibits.**

- 31.1 Certification of George M.L. LaBranche, IV, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Jeffrey A. McCutcheon, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of George M.L. LaBranche, IV, Chairman, Chief Executive Officer and President, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, regarding the information contained in LaBranche & Co Inc. s Quarterly Report on Form 10-Q for the period ended September 30, 2008.
- 32.2 Certification of Jeffrey A. McCutcheon, Senior Vice President and Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, regarding the information contained in LaBranche & Co Inc. s Quarterly Report on Form 10-Q for the period ended September 30, 2008.



**Table of Contents**

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

November 10, 2008

LABRANCHE & Co INC.

By: /s/ Jeffrey A. McCutcheon

Name: Jeffrey A. McCutcheon

Title: Senior Vice President and Chief Financial Officer

-58-

**Table of Contents**

EXHIBIT INDEX

<b>Exhibit No.</b>	<b>Description of Exhibit</b>
31.1	Certification of George M.L. LaBranche, IV, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Jeffrey A. McCutcheon, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of George M.L. LaBranche, IV, Chairman, Chief Executive Officer and President, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, regarding the information contained in LaBranche & Co Inc. s Quarterly Report on Form 10-Q for the period ended September 30, 2008.
32.2	Certification of Jeffrey A. McCutcheon, Senior Vice President and Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, regarding the information contained in LaBranche & Co Inc. s Quarterly Report on Form 10-Q for the period ended September 30, 2008.