

LABRANCHE & CO INC
Form 10-Q
August 13, 2003

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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 June 30, 2003

OR

- o **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 | 13-4064735 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

One Exchange Plaza, New York, New York 10006

(Address of principal executive offices)

(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: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No []

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes [X] No []

The number of shares of the registrant's common stock outstanding as of August 12, 2003 was 59,556,605.

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LaBRANCHE & CO INC. and SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
(000 s omitted except per share data)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|------------------|---------------------------|------------------|
| | 2003 | 2002 | 2003 | 2002 |
| | (unaudited) | (unaudited) | (unaudited) | (unaudited) |
| REVENUES: | | | | |
| Net gain on principal transactions | \$ 60,103 | \$ 72,731 | \$ 111,906 | \$ 161,855 |
| Commissions | 24,859 | 22,420 | 47,375 | 43,393 |
| Other | 2,542 | 2,957 | 4,857 | 15,540 |
| Total revenues | 87,504 | 98,108 | 164,138 | 220,788 |
| EXPENSES: | | | | |
| Employee compensation and related benefits | 25,096 | 31,080 | 50,915 | 62,153 |
| Interest | 12,207 | 12,848 | 23,928 | 25,684 |
| Exchange, clearing and brokerage fees | 10,936 | 9,203 | 21,598 | 16,980 |
| Lease of exchange memberships | 6,186 | 6,398 | 12,655 | 13,107 |
| Depreciation & amortization of intangibles | 3,279 | 3,359 | 6,589 | 6,689 |
| Other | 7,767 | 6,996 | 15,147 | 14,435 |
| Total expenses | 65,471 | 69,884 | 130,832 | 139,048 |
| Income before minority interest and provision for income taxes | 22,033 | 28,224 | 33,306 | 81,740 |
| MINORITY INTEREST | 127 | | 127 | |
| Income before provision for income taxes | 21,906 | 28,224 | 33,179 | 81,740 |
| PROVISION FOR INCOME TAXES | 10,316 | 13,283 | 16,062 | 39,147 |
| Net income | \$ 11,590 | \$ 14,941 | \$ 17,117 | \$ 42,593 |
| Series A Preferred dividends and discount accretion | 942 | 1,741 | 2,109 | 3,817 |
| Net income available to common stockholders | \$ 10,648 | \$ 13,200 | \$ 15,008 | \$ 38,776 |
| Weighted average shares outstanding: | | | | |
| Basic | 59,525 | 58,859 | 59,510 | 58,782 |
| Diluted | 60,256 | 59,991 | 60,284 | 59,995 |
| Earnings per share: | | | | |
| Basic | \$ 0.18 | \$ 0.22 | \$ 0.25 | \$ 0.66 |
| Diluted | \$ 0.18 | \$ 0.22 | \$ 0.25 | \$ 0.65 |

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

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LaBRANCHE & CO INC. and SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(000 s omitted except share data)

| | As of | |
|---|--------------------|----------------------|
| | June 30, 2003 | December 31, 2002 |
| | (unaudited) | (audited) |
| ASSETS | | |
| Cash and cash equivalents | \$ 377,208 | \$ 77,033 |
| Cash and securities segregated under federal regulations | 20,946 | 16,012 |
| Securities purchased under agreements to resell | 11,000 | 26,000 |
| Receivable from brokers, dealers and clearing organizations | 223,420 | 145,387 |
| Receivable from customers | 6,518 | 12,425 |
| United States Government obligations | | 395,840 |
| Securities owned, at market value: | | |
| Corporate equities | 221,549 | 106,295 |
| Exchange-traded funds | 233,538 | 21,455 |
| Options | 59,585 | 61,478 |
| Commissions receivable | 4,836 | 4,379 |
| Exchange memberships contributed for use, at market value | 18,000 | 26,176 |
| Exchange memberships owned, at cost (market value of \$58,826 and \$78,337, respectively) | 77,828 | 77,815 |
| Office equipment and leasehold improvements, at cost, less accumulated depreciation and amortization of \$7,904 and \$6,987, respectively | 5,330 | 6,089 |
| Intangible assets, net of accumulated amortization: | | |
| Specialist stock list | 376,768 | 381,956 |
| Trade name | 25,011 | 25,011 |
| Goodwill | 470,537 | 470,598 |
| Other assets | 56,528 | 58,853 |
| | \$2,188,602 | \$ 1,912,802 |
| Total assets | \$2,188,602 | \$ 1,912,802 |

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| | As of | |
|--|-----------------------------|-----------------------------|
| | June 30, 2003 | December 31, 2002 |
| | (unaudited) | (audited) |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Liabilities: | | |
| Payable to brokers and dealers | \$ 32,667 | \$ 16,417 |
| Payable to customers | 14,022 | 21,971 |
| Securities sold, but not yet purchased, at market value: | | |
| Corporate equities | 287,836 | 106,685 |
| Exchange-traded funds | 141,239 | 4,359 |
| Options | 54,981 | 63,695 |
| Accrued compensation | 39,896 | 55,185 |
| Accounts payable and other accrued expenses | 50,245 | 52,268 |
| Income taxes payable | 11,880 | 13,201 |
| Deferred tax liabilities | 180,358 | 179,924 |
| Long term debt | 355,253 | 354,948 |
| Subordinated liabilities | | |
| Exchange memberships, at market value | 18,000 | 26,176 |
| Other subordinated indebtedness | 28,285 | 28,285 |
| | <u> </u> | <u> </u> |
| Total liabilities | 1,214,662 | 923,114 |
| | <u> </u> | <u> </u> |
| Minority Interest | 127 | |
| | <u> </u> | <u> </u> |
| Preferred stock, liquidation value of \$1,000 per share; 10,000,000 shares authorized; 39,186 and 63,836 shares issued and outstanding as of June 30, 2003 and December 31, 2002, respectively | 37,985 | 61,361 |
| Common stock, \$.01 par value, 200,000,000 shares authorized; 59,551,645 and 59,504,148 shares issued and outstanding as of June 30, 2003 and December 31, 2002, respectively | 596 | 595 |
| Additional paid-in-capital | 681,206 | 679,601 |
| Retained earnings | 254,550 | 249,065 |
| Unearned compensation | (524) | (934) |
| | <u> </u> | <u> </u> |
| Total stockholders equity | 973,813 | 989,688 |
| | <u> </u> | <u> </u> |
| Total liabilities and stockholders equity | \$ 2,188,602 | \$ 1,912,802 |
| | <u> </u> | <u> </u> |

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

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LaBRANCHE & CO INC. and SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(000 s omitted)

| | Six Months Ended | |
|---|------------------|---------------|
| | June 30, 2003 | June 30, 2002 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | \$ 17,117 | \$ 42,593 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Depreciation and amortization of intangibles | 6,589 | 6,689 |
| Amortization of bond discount and debt issuance costs | 1,053 | 1,044 |
| Minority interest in income of consolidated subsidiary | 127 | |
| Compensation expense related to stock-based compensation | 1,801 | 1,618 |
| Deferred tax provision | 1,153 | 4,738 |
| Acceleration of preferred stock discount accretion | 918 | 1,485 |
| Tax benefit related to employee stock transactions | 61 | 3,733 |
| Change in assets and liabilities: | | |
| Cash and securities segregated under federal regulations | (4,934) | 54,252 |
| Securities purchased under agreements to resell | 15,000 | 47,094 |
| Receivable from brokers, dealers and clearing organizations | (78,034) | (89,594) |
| Receivable from customers | 5,906 | 3,844 |
| United States Government obligations | 395,840 | 5,491 |
| Securities owned, Corporate equities | (115,254) | (41,878) |
| Securities owned, Exchange-traded funds | (212,083) | |
| Securities owned, Options and other | 1,894 | (6,847) |
| Commissions receivable | (457) | (392) |
| Other assets | 1,577 | (5,536) |
| Payable to brokers and dealers | 16,250 | (19,539) |
| Payable to customers | (7,949) | (29,505) |
| Securities sold, but not yet purchased, Corporate equities | 181,151 | 67,401 |
| Securities sold, but not yet purchased, Exchange-traded funds | 136,880 | |
| Securities sold, but not yet purchased, Options | (8,715) | 6,073 |
| Accrued compensation | (15,289) | (264) |
| Accounts payable and other accrued expenses | (1,030) | (18,573) |
| Income taxes payable | (2,041) | (16,004) |
| | 337,531 | 17,923 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Payments for office equipment and leasehold improvements | (641) | (1,779) |
| Payments for exchange memberships | (13) | |
| | (654) | (1,779) |

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| | Six Months Ended | |
|--|-------------------|-------------------|
| | June 30, 2003 | June 30, 2002 |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from the exercise of stock options | 216 | 4,196 |
| Payment of common stock dividends | (9,523) | |
| Payment of preferred stock dividends | (2,745) | (4,300) |
| Payment for preferred stock buyback | (24,650) | (28,164) |
| | <u> </u> | <u> </u> |
| Net cash used in financing activities | (36,702) | (28,268) |
| | <u> </u> | <u> </u> |
| Increase/(Decrease) in cash and cash equivalents | 300,175 | (12,124) |
| CASH AND CASH EQUIVALENTS, beginning of the period | 77,033 | 52,043 |
| | <u> </u> | <u> </u> |
| CASH AND CASH EQUIVALENTS, end of the period | \$ 377,208 | \$ 39,919 |
| | <u> </u> | <u> </u> |
| SUPPLEMENTAL DISCLOSURE OF CASH PAID FOR: | | |
| Interest | \$ 21,555 | \$ 22,485 |
| Income taxes | 16,193 | 48,960 |
| SUPPLEMENTAL NON-CASH FINANCING AND INVESTING ACTIVITIES: | | |
| Net increase in additional paid-in capital related to stock based awards | 2,016 | 5,811 |

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

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**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), LaBranche Financial Services, Inc., a New York corporation (LFSI), LaBranche Structured Products, LLC, a New York limited liability company (LSP), LABDR Services, Inc., a Delaware corporation (LABDR), and LaBranche & Co. B.V., a Netherlands private limited liability company (BV) and collectively with the Holding Company, LaBranche, LFSI, LSP and LABDR, the Company. The Holding Company is the sole member of LaBranche and LSP, the 100% stockholder of LFSI and LABDR, and the sole owner of BV. LaBranche is a registered broker-dealer and operates primarily as a specialist in equity securities and rights listed on the New York Stock Exchange (the NYSE) and in equity securities on the American Stock Exchange (the AMEX). LFSI is a registered broker-dealer and a member of the NYSE and other exchanges, and provides securities clearing, securities execution and other related services to its own retail customers, customers of introducing brokers and institutional customers, including traders, professional investors and broker-dealers. LFSI also provides direct-access floor brokerage services to institutional customers. LSP is a registered broker-dealer and operates as a specialist in options, Exchange Traded Funds (ETFs) and futures on the AMEX and the New York Board of Trade (NYBOT) and acts as a market-maker in ETFs on several exchanges. LABDR was recently incorporated to provide disaster recovery services and back-up facilities to other Holding Company subsidiaries. BV represents LaBranche in European markets and provides client services to LaBranche's European listed companies.

2. INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND FINANCIAL INFORMATION

The unaudited interim condensed consolidated financial information as of June 30, 2003 and for the six months ended June 30, 2003 and 2002 is presented in the accompanying condensed consolidated financial statements. The unaudited interim condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the 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 accounting principles generally accepted in the United States 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. This interim condensed consolidated financial information as of June 30, 2003 should be read in conjunction with the audited consolidated financial statements and notes thereto as of December 31, 2002 included in the Company's Form 10-K filed with the Securities and Exchange Commission (SEC) on March 20, 2003. Results of the interim periods are not necessarily indicative of results to be obtained for a full fiscal year.

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With the adoption of Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets on January 1, 2002, which was issued by the Financial Accounting Standards Board (FASB), the acquired trade name and goodwill are no longer amortized. The acquired specialist stock lists, however, will continue to be amortized over their respective lives. The Company tests the acquired trade name, goodwill and specialist stock lists for impairment at least annually or when events and circumstances indicate impairment testing may be necessary by applying a fair-value based test in accordance with SFAS No. 142 and No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. It is possible that in the future, after periodic testing, the Company may incur impairment charges related to the carrying value of acquired goodwill and intangible assets recorded in its financial statements.

The gross carrying amount, accumulated amortization and net carrying amount of the Company s acquired specialist stock lists are set forth below (000 s omitted):

| | As of June 30, 2003 | As of December 31, 2002 |
|--------------------------|-----------------------------|-----------------------------|
| | <u> </u> | <u> </u> |
| Gross carrying amount | \$406,190 | \$ 406,190 |
| Accumulated amortization | (29,422) | (24,234) |
| | <u> </u> | <u> </u> |
| Net carrying amount | \$376,768 | \$ 381,956 |
| | <u> </u> | <u> </u> |

Amortization expense associated with the Company s acquired specialist stock lists was \$2.6 million and \$5.2 million for each of the three-month and six-month periods ended June 30, 2003 and 2002, respectively. Estimated amortization expense for the existing specialist stock lists is \$10.4 million for each of the fiscal years ending December 31, 2004 through December 31, 2008.

4. INCOME TAXES

The Company accounts for taxes in accordance with SFAS No. 109, Accounting for Income Taxes, which requires the recognition of tax benefits or expenses on temporary differences between the financial reporting and tax bases of its assets and liabilities. Deferred tax assets and liabilities primarily relate to stock-based compensation, other compensation accruals, amortization periods of certain intangibles and differences between the financial and tax bases of assets acquired. The Company s effective tax rate differs from the combined federal, state and local statutory rates primarily due to its non-deductible amortization of intangible assets and the non-deductible expense recorded due to the acceleration of the discount accretion as a result of the repurchase of the Company s Series A preferred stock in 2002 and 2003.

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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 June 30, | | Six Months Ended June 30, | |
|---|-----------------------------|------------------|---------------------------|------------------|
| | 2003 | 2002 | 2003 | 2002 |
| Current federal, state and local taxes | \$ 10,813 | \$ 13,708 | \$ 14,909 | \$ 34,409 |
| Deferred tax (benefit)/provision | (497) | (425) | 1,153 | 4,738 |
| Total provision for income taxes | \$ 10,316 | \$ 13,283 | \$ 16,062 | \$ 39,147 |

5. CAPITAL AND NET LIQUID ASSET REQUIREMENTS

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

As of June 30, 2003 and December 31, 2002, LaBranche's net capital, as defined under SEC Rule 15c3-1, was \$473.9 million and \$472.0 million, respectively, which exceeded the minimum requirements by \$471.9 million and \$467.4 million, respectively. LaBranche's aggregate indebtedness to net capital ratio on those dates was .06 to 1 and .15 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, their position requirement.

As of June 30, 2003 and December 31, 2002, LaBranche's NYSE minimum required dollar amount of net liquid assets, as defined, was \$446.0 million, compared to actual net liquid assets, as defined, of \$483.0 million and \$465.2 million, respectively.

The AMEX generally requires its equity specialist firms to maintain a cash or liquid asset position of the greater of (a) \$600,000, or (b) an amount sufficient to assume a position of sixty trading units of each security in which the specialist is registered. Because LaBranche adheres to the NYSE's net liquid asset requirements, it automatically satisfies the AMEX liquid asset requirements.

As a registered broker-dealer and NYSE member firm, LFSI is also subject to SEC Rule 15c3-1, as adopted and administered by the NYSE and the SEC. Under the alternative method permitted by the rule, the minimum required net capital for LFSI is equal to the greater of \$1.5 million or 2% of aggregate debit items, as defined. As of June 30, 2003 and December 31, 2002, LFSI's net capital, as defined under SEC Rule 15c3-1, was \$16.5 million and \$19.4 million, respectively, which exceeded the minimum requirements by \$15.0 million and \$17.9 million, respectively.

As a registered broker-dealer and AMEX member firm, LSP is subject to SEC Rule 15c3-1, as adopted and administered by the AMEX and the SEC. LSP is required to maintain minimum net capital, as defined, equivalent to the greater of \$100,000 or 1/15 of aggregate indebtedness, as defined. As of June 30, 2003 and December 31, 2002, LSP's net capital, as defined under SEC Rule 15c3-1, was \$18.1 million and \$6.9 million, respectively, which exceeded minimum requirements by \$18.0 million and \$6.8 million, respectively.

Table of Contents**6. RECENT TRANSACTION**

On April 22, 2003, LSP formed an options specialist joint account on the AMEX (the Joint Account) with Botta Capital Management, LLC (Botta). LSP contributed \$1.5 million of capital for the operations of the Joint Account and manages the Joint Account s business on the trading floor of the AMEX. Botta contributed its right to act as specialist in certain AMEX option listings. Net profits of the Joint Account, on an annual basis, generated from specialist activities in the Joint Account s AMEX listed options are shared by LSP and Botta at a ratio of 66% and 34%, respectively. However, LSP is required to bear 100% of any net losses incurred on an annual basis. After the fourth anniversary of the formation of the Joint Account, Botta will no longer have any interest in the Joint Account or the AMEX option listings it contributed to the Joint Account.

The results of the Joint Account have been included in the Company s condensed consolidated financial statements since April 22, 2003, in accordance with FASB Interpretation No. (FIN) 46, Consolidation of Variable Interest Entities. Botta s share of the net income and net assets of the Joint Account are classified as minority interest on the condensed consolidated statements of operations and financial condition, respectively.

7. DERIVATIVE FINANCIAL INSTRUMENTS

LSP uses derivative financial instruments, including exchange-traded options, ETFs and domestic and foreign futures contracts, for trading purposes and to financially hedge other positions or transactions as part of its specialist and market-making business and overall risk management process. These financial instruments subject LSP to varying degrees of market, credit and foreign exchange risk. LSP records its derivative trading activities at market value, with corresponding gains or losses recorded in net gain on principal transactions. Any gains or losses from foreign currency transactions are recorded in other income. In order to minimize risk, management continually monitors positions, profit and loss, volatility and other standard risk measures on a real-time basis and communicates its risk tolerance to LSP s traders.

The following table indicates the fair value of LSP s ETFs, exchange-traded options and futures contracts:

| (000's omitted) | As of June 30, 2003 | | As of December 31, 2002 | |
|-------------------------|------------------------|-------------|----------------------------|-------------|
| | Assets | Liabilities | Assets | Liabilities |
| ETFs | \$233,538 | \$141,239 | \$21,455 | \$ 4,359 |
| Exchange-traded options | 59,585 | 54,981 | 61,478 | 63,695 |
| Futures contracts | 2,469 | 1,774 | 97 | 41 |

8. EARNINGS PER SHARE

Earnings per share (EPS) are computed in accordance with SFAS No. 128, Earnings Per Share. Basic EPS is calculated by dividing net income available to common stockholders by the weighted-average number of common shares outstanding. Diluted EPS includes the determinants of basic EPS and, in addition, gives effect to dilutive potential common shares.

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

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|------------------------------------|-------------|----------------------------------|-------------|
| | 2003 | 2002 | 2003 | 2002 |
| Net income | \$ 11,590 | \$ 14,941 | \$ 17,117 | \$ 42,593 |
| Less preferred dividends and accretion | 942 | 1,741 | 2,109 | 3,817 |
| Numerator for basic and diluted earnings per share net income available to common stockholders | \$ 10,648 | \$ 13,200 | \$ 15,008 | \$ 38,776 |
| Denominator for basic earnings per share weighted-average number of common shares | 59,525 | 58,859 | 59,510 | 58,782 |
| Dilutive Shares | | | | |
| Stock options | 432 | 684 | 475 | 761 |
| Restricted stock | | 32 | | 36 |
| Restricted stock units | 299 | 416 | 299 | 416 |
| Denominator for diluted earnings per share weighted-average number of common shares | 60,256 | 59,991 | 60,284 | 59,995 |
| Basic earnings per share | \$ 0.18 | \$ 0.22 | \$ 0.25 | \$ 0.66 |
| Diluted earnings per share | \$ 0.18 | \$ 0.22 | \$ 0.25 | \$ 0.65 |

The exercise prices for options to purchase an aggregate of 1,807,500 and 1,732,500 shares of common stock exceeded the average market price of the Company's common stock for the three and six months ended June 30, 2003 and 2002, respectively. Accordingly the calculation of diluted earnings per share does not include the antidilutive effect of these options for the three and six months ended June 30, 2003 and 2002.

9. EMPLOYEE INCENTIVE PLANS

During March 2003, the board of directors of the Company approved, subject to the subsequent approval of the Company's shareholders, the adoption of the Senior Executive Bonus Plan, effective as of January 1, 2003. The purpose of the Senior Executive Bonus Plan is to provide for the payment to the Company's Chief Executive Officer and next four most highly compensated executive officers of bonuses which are exempt from the \$1.0 million deduction limitation imposed by Section 162(m) of the Internal Revenue Code of 1986, as amended. The adoption of the Senior Executive Bonus Plan was approved by a majority of the stockholders of the Company at its annual meeting of stockholders on May 20, 2003.

In December 2002, the FASB issued SFAS No. 148, Accounting for Stock-Based Compensation-Transition and Disclosure, an Amendment of FASB Statement No. 123. SFAS No. 148 provides two additional methods, the modified prospective and the retroactive restatement methods, for an entity that voluntarily changes to the fair-value based method of accounting for stock-based employee compensation, in addition to the prospective method required by SFAS No. 123. Prior to January 1, 2003, the Company elected to account for stock

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based employee compensation in accordance with Accounting Principles Board Opinion (APB) No. 25. Pursuant to APB No. 25, the Company did not recognize any compensation expense since, on the date of grant, the Company's stock options had no intrinsic value. On January 1, 2003, the Company adopted the prospective method provided by SFAS No. 148 to account for stock-based employee compensation. Accordingly, the Company expenses the fair value, as of the date of grant, of stock options issued to employees on or after January 1, 2003 over the related service periods. The Company has not issued any stock options since January 1, 2003.

If the Company had recognized compensation expense for options granted prior to January 1, 2003 under the fair-value based method of SFAS No. 123, its net income would have decreased by approximately \$1.8 million and \$1.9 million for the three months ended June 30, 2003 and 2002, respectively, and approximately \$3.6 million for each of the six-month periods ended June 30, 2003 and 2002, resulting in pro forma net income and earnings per share as follows:

| (000's omitted, except per share data) | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|-----------------------------|-----------|---------------------------|-----------|
| | 2003 | 2002 | 2003 | 2002 |
| Net income available to common stockholders, as reported | \$ 10,648 | \$ 13,200 | \$ 15,008 | \$ 38,776 |
| Add: Stock-based compensation expense included in reported net income (net of tax effect) | 510 | (235) | 928 | 838 |
| Less: Stock-based compensation expense under SFAS 123 (net of tax effect) | (2,303) | (1,693) | (4,514) | (4,436) |
| Pro forma net income available to common stockholders | 8,855 | 11,272 | 11,422 | 35,178 |
| Diluted EPS, as reported | 0.18 | 0.22 | 0.25 | 0.65 |
| Pro forma diluted EPS | 0.15 | 0.19 | 0.19 | 0.59 |

The effect of applying SFAS No. 123 in the pro forma disclosure above may not be representative of the potential effect stock-based compensation would have on net income in future periods.

10. BUSINESS SEGMENTS

Segment information is presented in accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. Currently, the Company views its business under two separate segments: the Specialist segment and the Execution and Clearing segment. The Company's business segments are based upon the nature of the financial services provided, their revenue sources and the Company's management organization.

The Company's Specialist segment operates as a specialist in equities and rights on the NYSE and in equities, options, ETFs and futures on the AMEX and the NYBOT and provides support services for the specialist activities. In addition, this segment acts as a market maker in ETFs on several exchanges. The Specialist segment currently includes the operations of LaBranche, LSP, LABDR and BV.

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The Company's Execution and Clearing segment provides securities execution, securities clearing and other related services to its own retail customers, customers of introducing brokers and institutional customers, including traders, professional investors and broker-dealers. This segment also provides direct access floor brokerage services to institutional customers. The Execution and Clearing segment currently includes the operations of LFSI.

Revenues and expenses directly associated with each segment are included in determining its operating results. Other expenses, such as certain employee compensation and company-wide professional fees, 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. Certain revenues, administrative expenses and corporate overhead expenses are not specifically allocated by management when reviewing the Company's segments' performance, and appear in the Other section. Selected financial information for each segment is set forth below (000's omitted):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|-----------------------------|-----------|---------------------------|------------|
| | 2003 | 2002 | 2003 | 2002 |
| Specialist Segment: | | | | |
| Revenues | \$ 74,598 | \$ 87,805 | \$ 139,373 | \$ 192,616 |
| Operating expenses | 33,394 | 40,163 | 66,704 | 78,492 |
| Depreciation and amortization expense | 2,920 | 3,082 | 5,879 | 6,142 |
| Income before minority interest and taxes | 38,284 | 44,560 | 66,790 | 107,982 |
| Segment Assets | 2,012,461 | 1,854,879 | 2,012,461 | 1,854,879 |
| Execution and Clearing Segment: | | | | |
| Revenues | \$ 12,907 | \$ 10,219 | \$ 24,401 | \$ 18,969 |
| Operating expenses | 15,307 | 12,338 | 29,888 | 24,533 |
| Depreciation and amortization expense | 343 | 273 | 689 | 539 |
| Loss before minority interest and taxes | (2,743) | (2,392) | (6,176) | (6,103) |
| Segment Assets | 76,474 | 123,977 | 76,474 | 123,977 |

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| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|-----------------------------|-----------|---------------------------|------------|
| | 2003 | 2002 | 2003 | 2002 |
| Other: (1) | | | | |
| Revenues | \$ (1) | \$ 84 | \$ 364 | \$ 9,203 |
| Operating expenses | 13,491 | 14,024 | 27,651 | 29,334 |
| Depreciation and amortization expense | 16 | 4 | 21 | 8 |
| Loss before minority interest and taxes | (13,508) | (13,944) | (27,308) | (20,139) |
| Segment Assets | 99,667 | 38,302 | 99,667 | 38,302 |
| Total: | | | | |
| Revenues | \$ 87,504 | \$ 98,108 | \$ 164,138 | \$ 220,788 |
| Operating expenses | 62,192 | 66,525 | 124,243 | 132,359 |
| Depreciation and amortization expense | 3,279 | 3,359 | 6,589 | 6,689 |
| Income before minority interest and taxes | 22,033 | 28,224 | 33,306 | 81,740 |
| Assets | 2,188,602 | 2,017,158 | 2,188,602 | 2,017,158 |

- (1) Other is comprised primarily of the interest on the Holding Company's indebtedness, unallocated corporate administrative expenses, including legal costs, unallocated revenues (primarily income from non-marketable investments as well as interest income), and elimination entries.

11. STOCKHOLDERS' EQUITY

On January 16, 2003, the board of directors declared an \$0.08 per share cash dividend payable on February 14, 2003 to holders of record of the Company's common stock on January 31, 2003. This dividend was paid on February 14, 2003.

On April 14, 2003, the board of directors declared an \$0.08 per share cash dividend payable on May 14, 2003 to holders of record of the Company's common stock on April 30, 2003. This dividend was paid on May 14, 2003.

During January 2003, the Company offered to repurchase up to 30,000 shares of its outstanding Series A preferred stock for \$1,000 per share, plus accrued and unpaid dividends up to but not including the date of purchase. On February 4, 2003, the offer expired, and on February 6, 2003, the Company purchased all of the approximately 24,650 shares that had been tendered for approximately \$24.8 million, including accrued but unpaid dividends. As a result of the purchase, the Company recorded an expense due to the acceleration of the discount accretion on the shares purchased of approximately \$0.9 million, which was included in other expenses.

12. COMMITMENTS AND CONTINGENCIES

The Company and, in particular, certain of the business operations conducted by LFSI's predecessor in interest, ROBB PECK McCOOEY Clearing Corporation, have been the target, from time to time, of various claims and lawsuits incidental to the ordinary course of their respective businesses. While the ultimate outcome of those claims and lawsuits which currently are pending cannot be predicted with certainty, the Company believes, based on its understanding of the facts of these proceedings, that their ultimate resolution, in the aggregate,

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will not have a material adverse effect on the Company's financial condition or results of operations.

On April 22, 2003, the NYSE announced that it was reviewing the trading practices of several specialist firms, including the Company's subsidiary specialist firm, LaBranche. The investigation presently focuses on the trading requirement that NYSE specialist firms not intervene in a natural match between a buyer and a seller.

In connection with this investigation, the NYSE's Division of Enforcement recently served LaBranche with a so-called Charge Memorandum as a result of LaBranche's refusal to furnish the NYSE's Division of Enforcement with copies of all personal e-mail messages sent or received by certain of its specialists and other employees since January 2002. LaBranche personnel have given a number of on-the-record interviews to the NYSE, and LaBranche has produced numerous documents, including many thousands of e-mail messages, but has not produced personal e-mail messages in order to protect its employees' privacy rights and because it does not believe that such messages have any bearing on any of LaBranche's business activities or are at all relevant to the pending NYSE investigation. LaBranche has sought to comply with the NYSE's Division of Enforcement inquiry by offering to furnish copies of the disputed e-mail messages to an independent third party for a determination of whether they are relevant to the ongoing investigation, but the NYSE's Division of Enforcement has refused this offer. The Company believes that it is fully cooperating with this ongoing investigation, but it intends to contest vigorously the NYSE's Division of Enforcement efforts to obtain copies of its specialists' and other employees' non-business e-mail messages. Toward this end, LaBranche filed with the NYSE on August 12, 2003 a formal answer to the Charge Memorandum, in which it denied the NYSE's Division of Enforcement charge that it has failed to cooperate with the NYSE's investigation.

While the Company believes that LaBranche has operated in accordance with all applicable requirements, the investigation is ongoing and there can be no assurance as to the outcome of the investigation or its effects, if any, on the Company's financial condition.

13. SUBSEQUENT EVENT

On July 17, 2003, the board of directors declared an \$0.08 per share cash dividend payable on August 14, 2003 to holders of record of the Company's common stock on July 31, 2003. The payment of future dividends is within the discretion of the board of directors and will depend on the Company's future earnings, capital requirements, applicable regulatory restrictions, financial condition and other relevant factors.

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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 discussion should be read in conjunction with the Company's Condensed Consolidated Financial Statements and the Notes thereto contained in this report.

General

We currently view our business as operating principally in two separate segments: the specialist segment and the execution and clearing segment. Our specialist segment operates as a specialist in equities and rights on the New York Stock Exchange (the NYSE) and in equities, options, Exchange Traded Funds (ETFs) and futures on the American Stock Exchange (the AMEX) and the New York Board of Trade (NYBOT), a market-maker in ETFs on several exchanges, and provides support services for our specialist activities. Our execution and clearing segment provides securities clearing, securities execution and other related services to its own retail customers, customers of introducing brokers and institutional customers, including traders, professional investors and broker-dealers. Our execution and clearing segment also provides direct access floor brokerage services to institutional customers. Certain revenues and administrative and corporate overhead expenses, which consist primarily of interest on our public debt, are not specifically related to our two principal segments, and thus are treated as other revenues and expenses. Our specialist segment currently includes the operations of our LaBranche & Co. LLC, LaBranche Structured Products, LLC (LSP), LABDR Services, Inc. (LABDR), and LaBranche & Co. B.V. (BV) subsidiaries. Our execution and clearing segment currently includes the operations of our LaBranche Financial Services, Inc. (LFSI) subsidiary.

Recent Developments

In January 2003, the Financial Accounting Standard Board (FASB) issued FASB Interpretation (FIN) No. 46, Consolidation of Variable Interest Entities. FIN 46 requires a company to consolidate a variable interest entity (VIE) if the company has variable interests that give it a majority of the expected losses or a majority of the expected residual returns of the entity. FIN 46 is effective immediately for VIEs created after January 31, 2003. For VIEs created prior to February 1, 2003, FIN 46 will apply in the first interim period or fiscal year beginning after June 15, 2003. The implementation of FIN 46 has not had a material impact on our financial statements.

In May 2003, the FASB issued Statement of Financial Standards (SFAS) No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity. SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS No. 150 is

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effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective for the interim period beginning after June 15, 2003. We have not entered into or modified any financial instruments with characteristics of both liabilities and equity as defined under SFAS No. 150 since May 31, 2003. The implementation of SFAS No. 150 has not had a material impact on our financial statements.

Critical Accounting Policies

All of our principal securities transactions and the related gains and losses are recorded on a trade date basis. Customer securities transactions are recorded on a settlement date basis and the related revenues and expenses are recorded on a trade date basis. Corporate equities, ETFs, options and other securities owned, and securities sold, but not yet purchased, are reflected at market value and unrealized gains and losses are reflected in net gain on principal transactions. United States Government obligations, together with related interest receivable as reported in other assets, are reflected at market value, with interest income included in other income. The market value for equity securities for which we act as specialist on both the AMEX and NYSE is based on the closing price posted by the exchange on which they are traded. The market value for ETFs and futures contracts is also based on the closing price posted on the exchanges on which they are traded. The market value of our exchange-traded options is based on the national best bid/offer as determined by our options clearing agent.

Investments in non-marketable securities consist of private equity, limited liability company and limited partnership investments, and are included in other assets on the statement of financial condition. These investments do not have readily available price quotations. These investments are accounted for under the equity method, which approximates fair value, or are accounted for at fair value as estimated by our management. In determining the estimated fair value, we consider all appropriate factors relevant to such investments and consistently apply industry standard methodology for arriving at fair value. Gains and losses for changes in fair value are included in other revenues in the accompanying consolidated statement of operations.

Our balance sheet contains significant intangible assets. These intangible assets are comprised of our specialist stock lists, trade name and goodwill acquired in connection with our various acquisitions and the limited partner buyout that occurred in 1999 in connection with our reorganization from partnership to corporate form. The allocations of purchase price and determinations of useful lives were based on independent appraisals for material acquisitions through March 2001. The useful lives of the acquired specialist stock lists were determined based on analysis of historical turnover characteristics of the specialist stocks comprising these lists. For acquisitions subsequent to March 2001, the allocations of purchase price and determinations of useful lives were based on management's analysis of revenues, consideration paid, common stock listings and other relevant data and ratios. This information was analyzed and compared with the results of the independent appraisals conducted on acquisitions prior to April 2001.

Since the implementation of SFAS No. 142, Goodwill and Other Intangible Assets, on January 1, 2002, acquired trade name and goodwill are no longer amortized. Our acquired specialist stock lists, however, continue to be amortized over their respective lives. We test

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goodwill for impairment at least annually or when events and circumstances indicate impairment testing may be necessary by applying a fair-value based test in accordance with SFAS No. 142 and No. 144, Accounting for Impairment or Disposal of Long-Lived Assets. The fair value test involves a comparison of the fair value of the reporting unit to the carrying value of the reporting unit. The fair value of the reporting unit is determined using both its market capitalization, when applicable, and the present value of its estimated future cash flows based on certain management assumptions. If the carrying amount of the reporting unit exceeds its estimated fair value, we will determine if impairment is necessary through additional testing. Additionally, we test our specialist stock lists and trade name intangible assets whenever events or circumstances indicate that their carrying amount may not be recoverable. If the carrying value of the specialist stock lists and trade name exceeds their fair value, an impairment loss would be recognized for the excess of carrying value over fair value. It is possible that in the future, as a result of periodic testing, we may incur impairment charges related to the carrying value of goodwill and intangible assets recorded in our financial statements.

Results of Operations*Specialist Segment Operating Results*

| (000's omitted) | For the Three | | For the Six | | Three | Six |
|---|--------------------------|----------|--------------------------|-----------|---------------------------|---------------------------|
| | Months Ended June 30, | | Months Ended June 30, | | Months 2003 vs 2002 | Months 2003 vs 2002 |
| | 2003 | 2002 | 2003 | 2002 | Percentage Change | Percentage Change |
| Revenues: | | | | | | |
| Net gain on principal transactions | \$60,103 | \$72,731 | \$111,906 | \$161,855 | (17.4)% | (30.9)% |
| Commissions | 12,358 | 13,004 | 23,631 | 26,197 | (5.0) | (9.8) |
| Other | 2,137 | 2,070 | 3,836 | 4,564 | 3.2 | (16.0) |
| Total segment revenues | 74,598 | 87,805 | 139,373 | 192,616 | (15.0) | (27.6) |
| Operating expenses | 36,314 | 43,245 | 72,583 | 84,634 | (16.0) | (14.2) |
| Income before minority interest and taxes | \$38,284 | \$44,560 | \$66,790 | \$107,982 | (14.1) | (38.1) |

Revenues from our specialist segment consist primarily of net gain earned from principal transactions in securities for which we act as specialist. Net gain on principal transactions represents trading gains net of trading losses and Securities and Exchange Commission (SEC) transaction fees, where applicable, and are earned by us when we act as principal buying and selling our specialist stocks, rights, options, ETFs and futures. Also included in net gain on principal transactions are accrued dividends receivable or payable on our stock positions, net gains and losses resulting from our market-making activities in ETFs, the trading of futures used to hedge our ETF positions, and the trading of equities underlying the rights, ETFs and options for which we act as specialist. These revenues are primarily affected by changes in share volume traded and fluctuations in price of our stocks, options, ETFs and futures, in which we are the specialist or in which we make a market.

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Commissions revenue generated by our specialist segment consists primarily of fees earned when our specialists act as agents by executing limit orders on behalf of brokers, professional traders and broker-dealers after a specified period of time; we do not earn commissions when we match market orders.

Other revenue at our specialist segment consists primarily of interest income, proprietary trading gains or losses and earnings or losses from an investment in a hedge fund by LaBranche & Co. LLC.

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002

Net gain on principal transactions decreased as a result of a decrease in the dollar value and share volume of principal shares traded during the second quarter of 2003 as compared to the same period in 2002. During the second quarter of 2003, the aggregate dollar value of principal trades decreased 26.0% to \$187.9 billion from \$253.9 billion for the same period in 2002, and the aggregate share volume of principal trades decreased 16.9% to 7.4 billion shares during the second quarter of 2003 from 8.9 billion shares for the same period in 2002. Of the total \$60.1 million and \$72.7 million of net gain on principal transactions during the second quarter of 2003 and 2002, respectively, \$5.2 million and (\$0.7) million, respectively, were from our derivative trading activities.

Commissions revenue earned by our specialist segment decreased, despite an increase in the share volume executed by us as agent, due to the competitive price pressures within the marketplace and our billing structure, which is designed to provide our customers with the lowest possible execution price. The total share volume executed by us as agent in our specialist stocks increased 15.0% to 2.3 billion shares for the three months ended June 30, 2003, from 2.0 billion shares for the same period in 2002.

Other revenue earned by our specialist segment increased slightly as a result of additional interest income related to stock-borrow transactions from our expanded LSP operations and an increase in earnings from our hedge fund investment. This increase was partially offset by a decline in interest income at LaBranche & Co. LLC due to significantly lower interest rates for our short-term treasury investments and stock-borrow transactions.

Operating expenses for our specialist segment decreased primarily due to a reduction in employee compensation and related benefits expense, interest expense and lease of exchange membership expense. These decreases were partially offset by an increase in exchange, clearing and brokerage fees expense. For a further discussion of operating expenses, see [Operating Expenses](#) below.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002

Net gain on principal transactions decreased as a result of the unfavorable market conditions resulting from global economic and geopolitical uncertainties during the first quarter of 2003 as compared to the same period in 2002. The decrease in the dollar value and share volume of principal trades throughout the first six months of 2003 also contributed to this decline. The aggregate dollar value of principal trades decreased 26.2% to \$379.7 billion for

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the six months ended June 30, 2003 from \$514.4 billion for the same period in 2002, and the aggregate share volume of principal trades decreased 15.3% to 15.0 billion shares for the six months ended June 30, 2003, from 17.7 billion shares for the same period in 2002. Of the total \$111.9 million and \$161.9 million of net gain on principal transactions, during the first six months of 2003 and 2002, respectively, \$7.0 million and (\$0.4) million, respectively, were from our derivative trading activities.

Commissions revenue earned by our specialist segment decreased, despite an increase in the share volume executed by us as agent, as a result of our billing structure, which is designed to provide our customers with the lowest possible execution price. The total share volume executed by us as agent in our specialist stocks increased 10.0% to 4.4 billion shares for the six months ended June 30, 2003, from 4.0 billion shares for the same period in 2002.

Other revenue earned by our specialist segment decreased primarily due to a decline in interest income as a result of significantly lower interest rates for our short-term treasury investments and stock-borrow transactions. The decrease in other revenue was partially offset by an increase in proprietary trading revenues, as well as an increase in interest income related to stock-borrow transactions at our LSP subsidiary due to expanded trading activities.

Operating expenses for our specialist segment decreased primarily due to a reduction in employee compensation and related benefits expense, interest expense and lease of exchange membership expense. These decreases were partially offset by an increase in exchange, clearing and brokerage fees expense. For a further discussion of operating expenses, see *Operating Expenses* below.

Execution and Clearing Segment Operating Results

| (000 \$ omitted) | For the Three Months Ended June 30, | | For the Six Months Ended June 30, | | Three Months | Six Months |
|---|--|------------|--------------------------------------|------------|--------------------------------------|---|
| | 2003 | 2002 | 2003 | 2002 | 2003 vs 2002 Percentage Change | 2003 vs 2002 Percentage Change |
| Revenues: | | | | | | |
| Commissions | \$ 12,501 | \$ 9,416 | \$ 23,744 | \$ 17,196 | 32.8% | 38.1% |
| Other | 406 | 803 | 657 | 1,773 | (49.4) | (62.9) |
| Total segment revenues | 12,907 | 10,219 | 24,401 | 18,969 | 26.3 | 28.6 |
| Operating expenses | 15,650 | 12,611 | 30,577 | 25,072 | 24.1 | 22.0 |
| Loss before minority interest and taxes | \$ (2,743) | \$ (2,392) | \$ (6,176) | \$ (6,103) | 14.7 | 1.2 |

Our execution and clearing segment's commissions revenue includes fees charged to customers for execution, clearance and direct-access floor brokerage services.

Our execution and clearing segment's other revenues consist of interest income, proprietary trading gains or losses and fees charged to customers for the use of our proprietary front-end order execution system.

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Commissions revenue from our execution and clearing segment increased primarily due to the growth and expansion of our institutional execution services. This increase was partially offset by a decrease in commission income from clearance activities and retail execution services.

Other revenue from our execution and clearing segment decreased primarily due to a decline in interest income as a result of significantly lower interest rates for our short-term investments and reduced margin balances, as well as a decline in proprietary trading revenues. This decrease was also due to a decline in fees received from customers using our proprietary front-end order execution system.

The increase in operating expenses for our execution and clearing segment was primarily due to an increase in employee compensation and related benefits expense and other expenses. For a further discussion of operating expenses, see *Operating Expenses* below.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002

Commissions revenue from our execution and clearing segment increased primarily due to the growth and expansion of our institutional execution services. This increase was partially offset by a reduction in commission income from clearance activities.

Other revenue from our execution and clearing segment decreased primarily due to a decline in interest income as a result of significantly lower interest rates for our short-term investments and reduced margin balances, as well as a decline in proprietary trading revenues. This decrease was also due to a decline in fees received from customers using our proprietary front-end order execution system.

The increase in operating expenses for our execution and clearing segment was primarily due to an increase in employee compensation and related benefits expense, exchange, clearing and brokerage fees and other expenses. For a further discussion of operating expenses, see *Operating Expenses* below.

Other Operating Results

| (000 s omitted) | For the Three Months Ended June 30, | | For the Six Months Ended June 30, | | Three Months | Six Months |
|---|--|------------|--------------------------------------|------------|--------------------------------------|---|
| | 2003 | 2002 | 2003 | 2002 | 2003 vs 2002 Percentage Change | 2003 vs 2002 Percentage Change |
| Other Revenues | \$ (1) | \$ 84 | \$ 364 | \$ 9,203 | (101.2)% | (96.0)% |
| Total segment revenues | (1) | 84 | 364 | 9,203 | (101.2) | (96.0) |
| Operating expenses | 13,507 | 14,028 | 27,672 | 29,342 | (3.7) | (5.7) |
| Loss before minority interest and taxes | \$(13,508) | \$(13,944) | \$(27,308) | \$(20,139) | (3.1) | 35.6 |

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The portion of our revenues that is not generated from our two principal business segments consists primarily of appreciation or depreciation of our non-marketable investments and interest income.

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002

Other revenue decreased due to a decline in interest income as a result of significantly lower interest rates for our short to medium term investments.

Operating expenses decreased primarily due to a decline in interest expense. For a further discussion of operating expenses see, *Operating Expenses* below.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002

Other revenue decreased due to an approximately \$8.7 million appreciation in the value of our non-marketable investments during the first quarter of 2002. Other revenues also decreased due to a decline in interest income as a result of significantly lower interest rates for our short to medium term investments.

Operating expenses decreased primarily due to a decline in interest expense as well as a reduction in charges related to the repurchases of our Series A preferred stock. For a further discussion of operating expenses see, *Operating Expenses* below.

Operating Expenses

| (000's omitted) | For the Three | | For the Six | | Three Months 2003 vs 2002 Percentage Change | Six Months 2003 vs 2002 Percentage Change |
|---|--------------------------|-----------|--------------------------|-----------|--|---|
| | Months Ended June 30, | | Months Ended June 30, | | | |
| | 2003 | 2002 | 2003 | 2002 | | |
| Expenses: | | | | | | |
| Employee compensation and related benefits | \$25,096 | \$31,080 | \$ 50,915 | \$ 62,153 | (19.3)% | (18.1)% |
| Interest | 12,207 | 12,848 | 23,928 | 25,684 | (5.0) | (6.8) |
| Exchange, clearing and brokerage fees | 10,936 | 9,203 | 21,598 | 16,980 | 18.8 | 27.2 |
| Other operating expenses | 17,232 | 16,753 | 34,391 | 34,231 | 2.9 | 0.5 |
| Total expenses before minority interest and taxes | 65,471 | 69,884 | 130,832 | 139,048 | (6.3) | (5.9) |
| Provision for income taxes | \$ 10,316 | \$ 13,283 | \$ 16,062 | \$ 39,147 | (22.3) | (59.0) |

Our largest operating expense is employee compensation and related benefits. Our specialist segment's employee compensation and related benefits expense consists of salaries, wages and profitability-based compensation paid to our floor traders and related support staff. The employee compensation and related benefits expense related to our execution and clearing segment consists of salaries, wages and profitability-based compensation paid to our execution and clearing professionals, as well as compensation based on commissions earned by various trading professionals. Profitability-based compensation may include cash awards and stock-based compensation paid or granted to managing directors, trading professionals and other employees based on our profitability.

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Interest expense is primarily generated from the indebtedness not allocated to either of our two principal segments. This indebtedness was incurred in connection with our reorganization from partnership to corporate form in 1999, our subsequent acquisitions and the issuance of promissory notes in exchange for our preferred stock. The interest expense at our specialist segment is primarily the result of subordinated indebtedness that has been approved by the NYSE for inclusion in our net capital as well as margin interest expense related to our derivative specialist and market-making business. Customer's free credit balances and bank loans generate interest expense at our execution and clearing segment.

Exchange, clearing and brokerage fees expense at our specialist segment consists primarily of fees paid by us to the NYSE, AMEX, 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, an allocation fee requiring specialist firms to share the cost of newly allocated listings, technology fees, a flat annual fee and execution and clearing fees. Our execution and clearing segment's exchange, clearing and brokerage fees expense consists of commissions paid to third parties for introduction of customers, use of certain proprietary information and third party execution fees.

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002

Employee compensation and related benefits expense decreased as a result of a reduction in profitability-based compensation accruals and other employee benefit accruals. The decrease was partially offset by an increase in employee salaries due to the hiring of additional trading and support personnel for LSP's trading activities and for LFSI's institutional execution services group, which increased our average number of employees by approximately 29 individuals for the three months ended June 30, 2003, as compared to the same period in 2002. Employee compensation and related benefits expense decreased to 28.7% of total revenues for the three months ended June 30, 2003, from 31.7% of total revenues for the same period in 2002.

Interest expense decreased as the result of our repayment of \$20.0 million senior subordinated notes during 2002, as well as the repayment of \$33.1 million principal amount of subordinated indebtedness and promissory notes during the second half of 2002. This decrease was partially offset by an increase in margin interest charges as a result of the growth and expansion of derivative trading activities, as well as the interest expense related to the \$8.0 million aggregate principal amount of notes issued by us in August 2002 in exchange for 8,000 shares of our Series A preferred stock. Interest expense increased to 14.0% of total revenues for the three months ended June 30, 2003, from 13.1% of total revenues for the same period in 2002.

Exchange, clearing and brokerage fees expense increased primarily at our specialist segment due to the expansion of our derivative trading business, which led to an increase in commission expense, as well as a new NYSE technology fee that became effective as of January 1, 2003. Exchange, clearing and brokerage fees expense increased to 12.5% of total

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revenues for the three months ended June 30, 2003, from 9.4% of total revenues for the same period in 2002.

Other operating expenses increased primarily due to an increase in communication expenses due to the growth and expansion of our exchange and clearing segment. This increase was partially offset by a decline in lease of exchange memberships expense, the result of a slight decrease in the number of NYSE seats leased during the three months ended June 30, 2003, as well as a reduction in average seat rental cost on the AMEX.

Provision for income taxes decreased due to the decline in our income before provision for income taxes.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002

Employee compensation and related benefits expense decreased as a result of a reduction in profitability-based compensation accruals and other employee benefit accruals. The decrease was partially offset by an increase in employee salaries due to the hiring of additional trading and support personnel for LSP's trading activities and for LFSI's institutional execution services group, which increased our average number of employees by approximately 35 individuals for the six months ended June 30, 2003, as compared to the same period in 2002. Employee compensation and related benefits expense increased to 31.0% of total revenues for the six months ended June 30, 2003, from 28.2% of total revenues for the same period in 2002.

Interest expense decreased as the result of our repayment of \$20.0 million senior subordinated notes during 2002, as well as the repayment of \$34.8 million principal amount of subordinated indebtedness and promissory notes. This decrease was partially offset by an increase in margin interest charges as a result of the growth and expansion of our derivative trading activities, as well as the interest expense related to the \$8.0 million aggregate principal amount of notes issued by us in August 2002 in exchange for 8,000 shares of our Series A preferred stock. Interest expense increased to 14.6% of total revenues for the six months ended June 30, 2003, from 11.6% of total revenues for the same period in 2002.

Exchange, clearing and brokerage fees expense increased at our specialist segment due to the expansion of our derivative trading business, which led to an increase in commission expense, a new NYSE technology fee that became effective as of January 1, 2003, as well as an increase in NYSE allocation fees. This increase was also due to the growth and expansion of our execution and clearing segment. Exchange, clearing and brokerage fees expense increased to 13.2% of total revenues for the six months ended June 30, 2003, from 7.7% of total revenues for the same period in 2002.

Other operating expenses increased primarily due to an increase in communication and directed brokerage arrangement expenses due to the growth and expansion of our exchange and clearing segment. This increase was partially offset by a decline in legal and professional fees, as well as lease of exchange memberships expense, which was the result of a slight decrease in

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the number of NYSE seats leased during the six months ended June 30, 2003, as well as a reduction in average seat rental cost on the AMEX.

Provision for income taxes decreased due to the decline in our income before provision for income taxes.

Liquidity

As of June 30, 2003, we had \$2,188.6 million in assets, of which \$409.2 million consisted of cash and short-term investments primarily in United States Government obligations maturing within three months, cash and securities segregated under federal regulations and overnight repurchase agreements. As of June 30, 2003 cash and cash equivalents increased as a result of investing cash in United States Government obligations with maturities within three months, which are classified as cash and cash equivalents.

In October 2002, our LaBranche & Co. LLC subsidiary amended and restated its \$200.0 million committed line-of-credit agreement with a U.S. commercial bank, and extended the line-of-credit to October 31, 2003. The line-of-credit may be extended by LaBranche & Co. LLC, subject to the bank's approval, for additional one-year terms by giving written notice to the bank at least 30 days prior to the then-current scheduled termination date. Amounts outstanding under the U.S. commercial bank credit facility would be secured by our inventory of specialist stocks and bear interest at the U.S. commercial bank's broker loan rate. To date, we have not utilized this facility. In order to maintain the availability of funds under this credit facility, we must comply with certain financial and other covenants.

In connection with our acquisition of ROBB PECK McCOOEY Financial Services, Inc. (RPM), we assumed its liabilities and obligations under its deferred compensation plan. The deferred compensation plan provides for the payment, on or before December 15, 2007, of approximately \$30.2 million, plus interest at 8.0% per year, to certain former employees of RPM. While the payment of benefits under this deferred compensation plan may be accelerated in certain circumstances, no more than \$6.0 million in deferred compensation benefits (including interest) may be paid in any 12 consecutive month period beginning March 15, 2001. During the first quarter of 2003, we paid \$3.6 million in deferred compensation plan benefits. If the plan is terminated, the deferred compensation benefits (including interest) of all participants, to the extent not previously paid, must be distributed to the participants in one lump sum. The amounts payable under this deferred compensation plan may be reduced to satisfy certain indemnification obligations of the plan participants to us under the agreements governing our acquisition of RPM.

We also assumed RPM's liabilities and obligations under its retention bonus pool. The retention bonus pool requires \$9.0 million to be paid as bonus compensation on March 15, 2004 to as many as 31 former employees of RPM, provided they are still employed on the payment date. The portion of this retention bonus pool payable to each of these former employees will be determined by the majority vote of a committee consisting of Robert M. Murphy, George E. Robb, Jr. and Michael LaBranche or their respective successors.

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In connection with our acquisition of RPM, we also issued 100,000 shares of our nonconvertible Series A preferred stock to the former stockholders of RPM. Each outstanding share of our Series A preferred stock entitles the holder to cumulative preferred cash dividends at an annual rate of 8.0% of the liquidation preference per share until March 15, 2005, 10.0% until March 15, 2006, and 10.8% thereafter. Dividends are payable on the first day of January and the first day of July of each year (or if such date is not a regular business day, then the next business day thereafter), with the first payment made on July 1, 2001. Dividends on the issued and outstanding shares of Series A preferred stock are preferred and cumulative and accrue daily from the date on which they were originally issued. We have made all dividend payments to the holders of shares of our Series A preferred stock on the appropriate dates since issuance.

On January 6, 2003, we offered to repurchase up to 30,000 shares of our outstanding Series A preferred stock for \$1,000 per share, plus accrued and unpaid dividends up to but not including the date of purchase. On February 4, 2003, the offer expired, and on February 6, 2003, we purchased all of the approximately 24,650 shares that had been tendered for approximately \$24.8 million, including accrued but unpaid dividends. As a result of the purchase, we recorded an expense due to the acceleration of the discount accretion on the shares purchased of approximately \$0.9 million, which was included in other expenses. As of June 30, 2003, approximately 39,186 shares of our Series A preferred stock were outstanding. Of these remaining shares, 9,760 shares are held in escrow in order to satisfy the potential indemnification obligations of the former RPM stockholders to us under the agreements governing our acquisition of RPM.

On January 16, 2003, our board of directors declared an \$0.08 per share cash dividend payable on February 14, 2003 to holders of record of our common stock on January 31, 2003. This dividend was paid on February 14, 2003. On April 14, 2003, our board of directors declared an \$0.08 per share cash dividend payable on May 14, 2003 to holders of record of our common stock on April 30, 2003. This dividend was paid on May 14, 2003. On July 17, 2003, our board of directors declared an \$0.08 per share cash dividend payable on August 14, 2003 to holders of record of our common stock on July 31, 2003. The payment of future dividends is within the discretion of our board of directors and will depend on our future earnings, capital requirements, applicable regulatory restrictions, financial condition and other relevant factors.

As of June 30, 2003, the subordinated indebtedness of LaBranche & Co. LLC aggregated \$28.3 million (excluding subordinated liabilities related to contributed exchange memberships) and consisted of senior subordinated notes, junior subordinated notes and a secured demand note obligation. These notes mature on various dates between February 2004 and June 2008, and bear interest at annual rates ranging from 7.69% to 11.0%. In July 2003, LaBranche & Co. LLC prepaid, without penalty, the secured demand note in the principal amount of \$8.0 million, plus accrued interest. The note had an annual interest rate of 11.0% on the cash collateral and 4.0% on the non-cash collateral securing the note. The junior subordinated notes have automatic rollover provisions, which extend the maturities for an additional year, unless the lender provides at least seven months advance notice prior to maturity. LaBranche & Co. LLC is also entitled to prepay the junior subordinated notes without penalty under the terms of the agreements relating thereto.

As of June 30, 2003, \$10.0 million of our outstanding indebtedness consisted of one note of \$2.0 million, which matures in June 2004 and bears interest at an annual rate of 8.0%. The remaining notes in the aggregate principal amount of \$8.0 million mature in August 2007

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and bear interest at annual rates ranging from 9.0% to 10.0%.

On August 24, 1999, we issued \$100.0 million aggregate principal amount of Senior Notes. The Senior Notes bear interest at a rate of 9.5% annually and mature in August 2004. The indenture covering the Senior Notes includes certain covenants that, among other things, limit our ability to borrow money, pay dividends on our stock or purchase our stock, make 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.

On March 2, 2000, we issued \$250.0 million aggregate principal amount of Senior Subordinated Notes. These Senior Subordinated Notes bear interest at a rate of 12.0% annually and mature in March 2007. The indenture covering the Senior Subordinated Notes includes certain covenants that, among other things, limit our ability to borrow money, pay dividends on our stock or purchase our stock, make 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.

The Senior Subordinated Notes also require us, within 150 days after the end of each fiscal year, to offer to redeem from all holders of the Senior Subordinated Notes a principal amount equal to our Excess Cash Flow at a price equal to 103.0% of the principal amount being offered for purchase plus accrued and unpaid interest, if any, to the date of redemption. Each holder is entitled to be offered his or her pro rata share based upon his or her ownership percentage of the outstanding Senior Subordinated Notes. Excess Cash Flow is defined for this purpose as 40.0% of the amount by which our consolidated EBITDA exceeds the sum of our interest expense, tax expense, increase in net capital or net liquid asset requirements, capital expenditures, any cash amounts related to acquisitions of NYSE specialists or any cash payments related to our payment at maturity of the principal amount of our existing or certain other indebtedness. On May 13, 2003, we offered to purchase approximately \$30.5 million aggregate principal amount of Senior Subordinated Notes based on our Excess Cash Flow for the year ended December 31, 2002. This offer expired on June 11, 2003 without the tender of any Senior Subordinated Notes.

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 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

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financial integrity of the broker-dealer. As of June 30, 2003, LaBranche & Co. LLC's net capital, as defined under SEC Rule 15c3-1, was \$473.9 million, which exceeded the minimum requirements by \$471.9 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 net liquid assets, their position requirement. As of June 30, 2003, LaBranche & Co. LLC's NYSE minimum required dollar amount of net liquid assets, as defined, was \$446.0 million, compared to actual net liquid assets, as defined, of \$483.0 million.

The AMEX generally requires its equity specialist firms to maintain a cash or liquid asset position of the greater of (a) \$600,000, or (b) an amount sufficient to assume a position of sixty trading units of each security in which the specialist is registered. Because LaBranche & Co. LLC adheres to the NYSE's net liquid asset requirements, it automatically satisfies the AMEX liquid asset requirements.

As a registered broker-dealer and member firm of the NYSE, LFSI also is subject to SEC Rule 15c3-1, as adopted and administered by the NYSE and the SEC. Under the alternative method permitted by the rule, the minimum required net capital of LFSI as of June 30, 2003 was equal to the greater of \$1.5 million or 2.0% of aggregate debit items as defined. As of June 30, 2003, LFSI's net capital, as defined under SEC Rule 15c3-1, was \$16.5 million and exceeded minimum net capital requirements by \$15.0 million.

As a registered broker-dealer and AMEX member firm, LSP is subject to SEC Rule 15c3-1, as adopted and administered by the AMEX and the SEC. LSP is required to maintain minimum net capital, as defined, equivalent to the greater of \$100,000 or 1/15 of aggregate indebtedness, as defined. As of June 30, 2003, LSP's net capital, as defined under SEC Rule 15c3-1, was \$18.1 million, which exceeded minimum net capital requirements by \$18.0 million.

Failure by any of our broker-dealer subsidiaries to maintain its required net capital and net liquid assets, where appropriate, may subject it to suspension or revocation of its SEC registration or its suspension or expulsion by the NYSE and/or AMEX.

We currently anticipate that our available cash resources and credit facilities will be sufficient to meet our working capital, regulatory capital and capital expenditure requirements through at least the next twelve months.

Table of Contents***Credit Ratings***

Our \$100.0 million Senior Notes and our \$250.0 million Senior Subordinated Notes were both sold to public investors on their respective issuance dates. The following table sets forth the credit ratings on both of these issues as of June 30, 2003:

| | <u>Moody's Investors Services</u> | <u>Standard & Poor's</u> |
|---------------------------|---------------------------------------|----------------------------------|
| Senior Notes | Baa3 | BB+ |
| Senior Subordinated Notes | Ba1 | BB- |

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

Because our specialist equity activities on the NYSE and AMEX expose our capital to significant risks, managing these risks is a constant priority for us. Our central role in the auction process helps us to reduce risks by enabling us to incorporate up-to-date market information in the management of our inventory, subject to our specialist obligations. We have developed a risk management process which is designed to balance our ability to profit from our specialist activities with our exposure to potential losses. Our risk management process includes participation by our executive operating committee, our floor management committee, our floor team captains and our specialists.

Executive Operating Committee. Our executive operating committee is composed of four executive officers of LaBranche & Co. LLC. This committee is responsible for approving all risk management policies and trading guidelines for particular specialist stocks, after receiving input and proposals by the 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 floor management committee is composed of seven senior floor specialists. This committee is responsible for formulating and overseeing our overall risk management policies and risk guidelines for each of our specialist stocks. In arriving at these policies and guidelines, our floor management committee considers the advice and input of our floor team captains. Our floor management committee meets with all floor team captains no less than once a month to review and, if necessary, revise the risk management policies for LaBranche & Co. LLC and/or for particular specialist stocks. In addition, a member of our floor management committee is always available on the trading floor to review and assist with any unusual situations reported by a captain. Our floor management committee reports to our executive operating committee about each of these situations.

Floor Team Captains. We have 24 floor team captains who monitor the activities of LaBranche & Co. LLC's specialists throughout the trading day from various positions at LaBranche & Co. LLC's trading posts. The captains observe trades and constantly review trading positions on a real-time basis through our information systems. In addition, the captains are readily available to assist LaBranche & Co. LLC's specialists in determining when to deviate from our policies and guidelines to react to any unusual situations or market conditions. The captains must report these unusual situations to management, including any deviations from our policies and guidelines. Captains meet with each specialist at least once a week to evaluate the specialist's adherence to our risk management policies and guidelines. Captains

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also meet among themselves at least twice weekly to review risk policies and guidelines and, if appropriate, make new recommendations to the floor management committee.

Specialists. LaBranche & Co. LLC's specialists conduct auctions based on the conditions of the marketplace. In doing so, specialists observe our risk management policies and guidelines notwithstanding their responsibility to create a fair and orderly market. Specialists must immediately notify a captain of any unusual situations or market conditions requiring a deviation from our policies and guidelines.

Our equity specialist operations on the AMEX are conducted by five equity specialists. We have one floor captain on the AMEX, who monitors the trading activities of the AMEX equity specialists by observing trades and reviewing positions on a real time basis. In addition, we have an off-floor manager that monitors the AMEX equity positions and gains and losses on a real-time basis. The floor captain and manager regularly communicate with management and seek to ensure that our AMEX equity specialists adhere to all risk management policies set by LaBranche & Co. LLC's executive operating committee.

Circuit Breaker Rules. The NYSE and AMEX have instituted certain circuit breaker rules intended to halt trading in all NYSE/AMEX 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 opportunity to insure compliance with our risk management policies.

Equity Market Risk

As a specialist on the NYSE, a high concentration of LaBranche & Co. LLC's trading revenue is generated from its ten and twenty-five most profitable specialist stocks. However, the percentage of LaBranche & Co. LLC's specialist trading revenue generated from its ten most profitable specialist stocks has decreased from 28.1% to 20.4% and 25.2% to 20.1% of total principal trading revenue for the three and six months ended June 30, 2002 and 2003, respectively. The percentage of LaBranche & Co. LLC's specialist trading revenue generated from its twenty-five most profitable specialist stocks has decreased from 48.5% to 38.0% and 45.4% to 38.3% of total principal trading revenue for the three and six months ended June 30, 2002 and 2003, respectively. LaBranche & Co. LLC is not overly reliant on a particular group of specialist stocks, as the composition of its ten and twenty-five most profitable specialist stocks changes continuously.

Our specialist 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 in our specialist stocks for a variety of reasons, including price fluctuations of our specialist stocks, lack of trading volume in our specialist stocks and the performance of our specialist obligations. From time to time, we may have large position concentrations in securities of a

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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 a reduction of our revenues and operating profits.

We have developed a risk management process which is intended to balance our ability to profit from our 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 management instant access to specific trading information at any time during the trading day, including our aggregate long and short positions, 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 our principal trading revenues.

Derivatives Market Risk

As a specialist and market maker in options, ETFs and futures, LSP is responsible for creating a fair and orderly market, and trades securities as principal out of both obligation and inclination. As is true with LaBranche & Co. LLC's equity trading, LSP's options, ETFs, futures and foreign currency trading exposes it to certain risks, such as price fluctuations, foreign currency movements and changes in the liquidity of markets. In addition, these derivative instruments expose LSP to volatility, credit and foreign exchange risk, among other types of risks.

In order to manage these risks, LSP has a risk management team. These individuals utilize a third party software application to monitor LSP's positions on a real-time basis. By monitoring actual and theoretical profit and loss, volatility and other standard risk measures, these individuals seek to ensure that all LSP traders are within the parameters set by management. LSP's traders use futures, the stocks underlying certain positions and foreign currencies in an attempt to hedge market and foreign currency risk. LSP's aggregate risk is under constant evaluation by both the risk management team and traders, and all significant trading strategies and positions are discussed between both groups. LSP's option, future and ETF trading is executed solely on national and foreign exchanges. These trades clear through the Options Clearing Corporation, the National Securities Clearing Corporation or the applicable exchange clearing organization, thereby reducing potential credit risk.

The following chart illustrates how the specified movements in the underlying securities prices of LSP's entire portfolio would have impacted profits and losses from its trading activities:

| (000's omitted) | Profit or (Loss) if the underlying securities move: | | | | |
|------------------|---|--------------|-----------|--------------|---------------|
| | <u>-15.0%</u> | <u>-5.0%</u> | <u>0%</u> | <u>+5.0%</u> | <u>+15.0%</u> |
| Portfolio as of: | | | | | |
| March 31, 2003 | \$ 610 | \$ 396 | \$ (5) | \$ 194 | \$ (44) |
| June 30, 2003 | (930) | (47) | (7) | 295 | 610 |

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The numbers in the above table are based on certain theoretical assumptions and thus do not fully represent the profit or loss exposure to changes in volatility, interest rates and dividends. The zero percent change column represents the loss LSP would experience on a daily basis if the market remained unchanged.

Execution, Clearing and Operational Risk

As a specialist on the NYSE and AMEX and a market maker for certain securities, LaBranche & Co. LLC and LSP are engaged in various securities trading and lending activities. In connection with their activities as specialists and market makers, LaBranche & Co. LLC and LSP assume positions in stocks, rights, options, ETFs, futures and foreign currencies. LaBranche & Co. LLC and LSP are exposed to credit risk associated with the nonperformance of counterparties in fulfilling their contractual obligations pursuant to these securities transactions. LaBranche & Co. LLC and LSP also are exposed to market risk associated with the sale of securities not yet purchased, which can be directly impacted by volatile trading on the NYSE, AMEX and other exchanges. Additionally, in the event of nonperformance and unfavorable market price movements, LaBranche & Co. LLC and LSP may be required to purchase or sell financial instruments, which may result in a loss.

LFSI's execution and clearing services involve settlement and financing of various customer securities transactions on a cash or margin basis. These activities may expose LFSI to off-balance sheet risk in the event customers or other brokers are unable to fulfill their contractual obligations and it has to purchase or sell securities at a loss. For margin transactions, LFSI may be exposed to significant off-balance sheet risk in the event margin requirements are not sufficient to fully cover losses that customers may incur in their accounts.

Before conducting business with a prospective customer, LFSI reviews the prospective customer's experience in the securities industry, financial condition and personal background. For current customers, LFSI seeks to control the risks associated with customer activities by requiring customers to maintain margin collateral in compliance with various regulatory and internal guidelines. LFSI monitors margin levels daily and pursuant to such guidelines, requires customers to deposit additional collateral or to reduce positions when necessary. In addition, LFSI performs a background check on every customer.

In each of our segments, we rely heavily on our information systems in conducting our risk management. Accordingly, working in conjunction with the NYSE, 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 significant growth over the past several years. Management members and floor captains at our NYSE and AMEX operations must constantly monitor our positions and transactions in order to mitigate our risks and identify troublesome trends as they occur. The substantial capital we have invested, along with the NYSE, in real-time, on-line systems give management instant access to specific trading information at any time during the trading day, including:

our aggregate long and short positions;

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the various positions of each of our trading professionals;

our overall position in a particular stock;

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

average position size.

Our information systems send and receive data from the NYSE and AMEX 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 trading profits and losses as well as our positions. For our AMEX equity operations, our in-house technology staff has developed applications to monitor our current positions and profits and losses. Our derivative trading operation utilizes a third-party software application to monitor its positions and profits and losses on a real-time basis.

During 2002, we developed and implemented a business continuity plan which includes a comprehensive disaster recovery plan. We have a back-up disaster recovery center in New Jersey which has connectivity with our LaBranche & Co. LLC, LFSI and LSP subsidiaries. We are in the process of establishing a second back-up facility which will serve our LFSI and LSP subsidiaries in another New York state location and also will act as a secondary disaster recovery facility for our LaBranche & Co. LLC operations. We expect this second site to be fully operational by September 30, 2003.

Regulatory Risk

As registered broker-dealers, LaBranche & Co. LLC, LFSI and LSP are subject to certain regulatory requirements intended to insure their general financial soundness and liquidity. These subsidiaries are subject to SEC Rule 15c3-1, 15c3-3 and other requirements as adopted and administered by both the NYSE and AMEX.

LFSI must comply with the rules and regulations related to the custody of customers' assets issued under the Securities Exchange Act of 1934 and by the exchanges of which it is a member. In addition, the recently-enacted USA Patriot Act 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. As a result of this legislation, in July 2002, LFSI hired a compliance professional to establish and monitor LFSI's anti-money laundering practices.

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Item 4. Controls and Procedures

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-14 of the Securities Exchange Act of 1934 (the Exchange Act). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective, in all material respects, with respect to the recording, processing, summarizing and reporting, within the time periods specified in the Securities and Exchange Commission's rules and forms, of information required to be disclosed by us in the reports that we file or submit under the Exchange Act.

There have not been any changes in our internal control over financial reporting during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II OTHER INFORMATION

Item 1. Legal Proceedings

The Company and, in particular, certain of the business operations conducted by LFSI's predecessor in interest, ROBB PECK McCOOEY Clearing Corporation, have been the target, from time to time, of various claims and lawsuits incidental to the ordinary course of 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, in the aggregate, will not have a material adverse effect on our financial condition or results of operations.

On April 22, 2003, the NYSE announced that it was reviewing the trading practices of several specialist firms, including our subsidiary specialist firm, LaBranche & Co. LLC. The investigation presently focuses on the trading requirement that NYSE specialist firms not intervene in a natural match between a buyer and a seller.

In connection with this investigation, the NYSE's Division of Enforcement recently served our LaBranche & Co. LLC subsidiary with a so-called Charge Memorandum as a result of LaBranche & Co. LLC's refusal to furnish the NYSE's Division of Enforcement with copies of all personal e-mail messages sent or received by certain of its specialists and other employees since January 2002. LaBranche & Co. LLC personnel have given a number of on-the-record interviews to the NYSE, and LaBranche & Co. LLC has produced numerous documents, including many thousands of e-mail messages, but has not produced personal e-mail messages in order to protect its employees' privacy rights and because it does not believe that such messages have any bearing on any of LaBranche & Co. LLC's business activities or are at all relevant to the pending NYSE investigation. LaBranche & Co. LLC has sought to comply with the NYSE's Division of Enforcement inquiry by offering to furnish copies of the disputed e-mail messages to an independent third party for a determination of whether they are relevant to the ongoing investigation, but the NYSE's Division of Enforcement has refused this offer. We believe that we are fully cooperating with this ongoing investigation, but we intend to contest vigorously the NYSE's Division of Enforcement efforts to obtain copies of its specialists' and other employees' non-business e-mail messages. Toward this end, LaBranche & Co. LLC filed with the NYSE on August 12, 2003 a formal answer to the Charge Memorandum, in which it denied the NYSE's Division of Enforcement charge that it has failed to cooperate with the NYSE's investigation.

While we believe that LaBranche & Co. LLC has operated in accordance with all applicable requirements, the investigation is ongoing and there can be no assurance as to the outcome of the investigation or its effects, if any, on our financial condition.

Believing that it is inappropriate for him to continue to serve as Vice Chairman and Director of the NYSE while the NYSE's investigation of LaBranche & Co. LLC's trading practices is ongoing and particularly in the aftermath of the issuance by the NYSE's Division of Enforcement of the Charge Memorandum described above, Robert M. Murphy, the Chief Executive Officer of LaBranche & Co. LLC, resigned from his positions with the NYSE on August 7, 2003.

Table of Contents**Item 4. Submission of Matters to a Vote of Security Holders.**

The Company's Annual Meeting of Stockholders was held on May 20, 2003. The following proposals were adopted by the margins indicated:

- To elect three Class I directors, each of whom is to serve for a term of three years.

| | Number of Shares | |
|------------------------|------------------|-----------------------|
| | For | Withheld Authority |
| Michael LaBranche | 48,783,658 | 490,570 |
| Alfred O. Hayward, Jr. | 48,342,815 | 931,413 |
| Robert M. Murphy | 48,833,438 | 440,790 |

- To approve the Senior Executive Bonus Plan which provides for the payment to the Company's Chief Executive Officer and next four most highly compensated executive officers of bonuses which are exempt from \$1.0 million deduction limitation imposed by Section 162(m) of the Internal Revenue Code of 1986, as amended.

| | |
|---------|------------|
| For | 37,251,424 |
| Against | 4,730,871 |
| Abstain | 49,996 |

- To approve our appointment of KPMG LLP as our independent auditors for the fiscal year ending December 31, 2003.

| | |
|---------|------------|
| For | 49,017,049 |
| Against | 250,563 |
| Abstain | 6,616 |

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. The Company's 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 NYSE or the AMEX, excessive volatility in the equity securities market 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

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materially and adversely affect our business, financial condition, operating results and stock price. An investment in the Company 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, the actual results and performance of the Company and the specialist industry 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. The Company also disclaims any obligation to update its 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 and Reports on Form 8-K.*(a) Exhibits.*

| <u>Exhibit No.</u> | <u>Description of Exhibit</u> |
|--------------------|--|
| 31.1 | Certification of George M.L. LaBranche, IV, Chairman, Chief Executive Officer and President, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Harvey S. Traison, Senior Vice President and Chief Financial Officer, 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's Quarterly Report on Form 10-Q for the period ended June 30, 2003. |
| 32.2 | Certification of Harvey S. Traison, Senior Vice President and Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, regarding the information contained in LaBranche's Quarterly Report on Form 10-Q for the period ended June 30, 2003. |

(b) Reports on Form 8-K.

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(i) On April 3, 2003, we filed a Form 8-K, dated April 3, 2003, with respect to the announcement of our expected financial results for the first quarter of 2003.

(ii) On April 15, 2003, we filed a Form 8-K, dated April 15, 2003, with respect to our first quarter earnings announcement.
All other items of this report are inapplicable.

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SIGNATURES

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

August 12, 2003

LABRANCHE & CO INC.

By: /s/ Harvey S. Traison

Name: Harvey S. Traison
Title: Senior Vice President and Chief
Financial Officer

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EXHIBIT INDEX

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| 31.1 | Certification of George M.L. LaBranche, IV, Chairman, Chief Executive Officer and President, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Harvey S. Traison, Senior Vice President and Chief Financial Officer, 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's Quarterly Report on Form 10-Q for the period ended June 30, 2003. |
| 32.2 | Certification of Harvey S. Traison, Senior Vice President and Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, regarding the information contained in LaBranche's Quarterly Report on Form 10-Q for the period ended June 30, 2003. |