LABRANCHE & CO INC
Form 10-K
March 16, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ý **Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

for the fiscal year ended December 31, 2004

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) (Zip Code)

(212) 425-1144

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:	**Common Stock, par value $0.01** **New York Stock Exchange**
Securities registered pursuant to Section 12(g) of the Act:	**None**

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 ý No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2. Yes ý No o

The aggregate market value of the Common Stock held by non-affiliates of the registrant, based upon the last sale price of the Common Stock reported on the New York Stock Exchange on June 30, 2004, was approximately $503,709,000.

The number of shares of Common Stock outstanding as of March 10, 2005 was 60,623,134.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s definitive Proxy Statement for the registrant s 2005 Annual Meeting of Stockholders to be held on May 17, 2005 are incorporated by reference in this Annual Report on Form 10-K in response to Part II, item 5 and Part III, items 10, 11, 12, 13 and 14.

PART I

This Annual Report on Form 10-K and the documents incorporated by reference contain forward-looking statements that have been made pursuant to the provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on current expectations, estimates and projections about the registrant s industry, management s beliefs and certain assumptions made by management. Words such as anticipates, expects, intends, plans, believes, seeks, estimates, variations of such words and similar expressions are inte identify such forward-looking statements. These statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to predict; therefore, actual results may differ materially from those expressed or forecasted in any such forward-looking statements. Unless required by law, the registrant undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. However, readers should carefully review the risk factors set forth herein and in other reports or documents the registrant files from time to time with the Securities and Exchange Commission (the SEC).

Item 1. **BUSINESS.**

Overview

LaBranche & Co Inc. is a holding company that is the sole member of LaBranche & Co. LLC, LaBranche Structured Products, LLC (LSP) and LaBranche Structured Products Specialists, LLC (LSPS), the sole stockholder of LaBranche Financial Services, Inc. (LFSI) and LABDR Services, Inc. (LABDR), and the sole owner of LaBranche & Co. B.V. (BV). Founded in 1924, LaBranche & Co. LLC 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, a registered broker-dealer and a member of the NYSE and other exchanges, provides securities clearing, securities execution and other related services to its own customers and customers of introducing brokers. LFSI also provides direct-access floor brokerage services to institutional customers. LSP is a registered broker-dealer that operates as a specialist in options, Exchange-Traded Funds (ETFs) and futures on the AMEX, the New York Board of Trade (NYBOT), and the Philadelphia Stock Exchange (PHLX), and as a market-maker in options, ETFs and futures on several exchanges. LSPS is a registered broker-dealer and operates as a specialist in ETFs traded on the NYSE. LABDR provides disaster recovery services and back-up facilities to other LaBranche subsidiaries. BV represents LaBranche & Co. LLC in European markets and provides client services to LaBranche & Co. LLC s European listed companies. In January 2005, LSP formed a wholly-owned subsidiary in the United Kingdom, LaBranche Structured Products Europe Limited (LSPE), to be a market-maker for ETFs traded on the London Stock Exchange and the Eurex and Euronext exchanges. LSPE has yet to commence operations.

We are a Delaware corporation that was incorporated in June 1999. Our principal executive offices are located at One Exchange Plaza, 25th Floor, New York, New York 10006, and our telephone number is (212) 425-1144. Our Internet address is www.labranche.com. We make available free of charge, on or through the investor relations section of our website, annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to such reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission (SEC). These filings also are available on the SEC s website at www.sec.gov.

Also available on our website are our Corporate Governance Guidelines, our Code of Conduct (applicable to all our directors, officers and employees) and the charters for our Audit Committee, Compensation Committee and Nominating & Corporate Governance Committee. Within the time period required by the SEC and the NYSE, if applicable, we will post any amendment and/or any waiver of our Code of Conduct.

We currently view our business as operating principally in two separate segments: the Specialist segment and the Execution and Clearing segment.

Our Specialist segment currently includes the operations of LaBranche & Co. LLC, LSP, LSPS, LABDR and BV. As of December 31, 2004, the entities within our Specialist segment were specialists on the NYSE, the AMEX, the NYBOT, and PHLX, as well as market-makers on several exchanges. Collectively, our Specialist segment is the specialist for 580 common stock listings and 13 ETFs on the NYSE and 104 common stock listings, 324 options listings, 5 futures and 3 ETFs on the AMEX, PHLX and NYBOT, and is a market-maker for 124 ETFs, 173 options and 19 futures on various exchanges.

Our Execution and Clearing segment currently includes the operations of LFSI, which provides securities execution and clearing services to retail and institutional clients and correspondents. LFSI s central focus is to bring the customer closer to the point of sale and provide price discovery at the highest possible speed and lowest possible cost.

Compensation and related benefits for certain employees and certain company-wide professional fees are allocated to our two principal business segments. However, certain revenues and administrative and corporate overhead expenses, which consist primarily of interest on our public debt, are not specifically allocated to our two principal business segments and thus are treated as other revenues and expenses. A description of our principal business segments is presented below.

Our Specialist Segment

The Specialist Industry

The NYSE is the largest equities market in the world. At year-end 2004, the global market capitalization of all shares listed on the NYSE was approximately $19.8 trillion and the NYSE had nearly 2,800 listed companies, including approximately 460 non-U.S. companies from approximately 47 countries.

The NYSE s average daily trading volume for 2004 was 1,456.7 million shares, up from 1,398.4 million shares in 2003.

All trading of securities on the NYSE is conducted through an auction process. The auction process for each security is managed by the exclusive specialist for that security. The specialist is a broker-dealer who applies for and, if accepted, is assigned the role to maintain a fair and orderly market in its specialist stocks. The number of specialist units on the NYSE has decreased substantially over the past several years due to consolidation within the industry. There are currently seven NYSE specialist firms, of which the five largest, as ranked by number of specialist stocks, were responsible for 95.1% and 95.6% of the average daily share volume traded on the NYSE in 2004 and 2003, respectively.

A specialist firm is granted an exclusive franchise by the NYSE to conduct the auction in each of its NYSE-listed stocks. Specialist firms conduct their auctions at specific trading posts located on the floor of the NYSE. Because the specialist firm runs the auction in its specialist stocks, it must consider all known buy and sell interest in its stocks in order to price its stocks appropriately.

Specialist firms compete for the original listing of stocks through an allocation process organized by the NYSE. As part of this allocation process, companies seeking a listing may select a specialist firm in one of two ways. Under the first method, the NYSE s allocation committee selects the specialist firm based on specific criteria. Under the second method, available since March 1997, the listing company requests that the allocation committee select three to five potential specialist firms suitable for the stock, based on criteria specified by the listing company. The listing company then has the opportunity to meet with representatives from each specialist firm identified by the allocation committee. Within one week after meeting the competing specialist firms, the listing company must select a specialist firm. Currently, substantially all companies seeking a listing on the NYSE opt to make the final choice of their own specialist firm under the second allocation method.

When assigned a particular stock, the specialist firm agrees to specific obligations. The specialist firm s role is to maintain, as far as practicable, trading in the stock that is fair and orderly. This implies that the trading will have reasonable depth and price continuity, so that, under normal circumstances, a customer may buy or sell stock in a manner consistent with market conditions. A specialist firm helps market participants achieve price improvement in their trades because the best bids and offers are discovered through the auction process. In performing its obligations, the specialist firm is exposed to all transactions that occur in each of its specialist stocks on the NYSE floor, either through electronic orders or floor brokers. In any given transaction, the specialist firm may act as:

an auctioneer by setting opening prices for its specialist stocks and by matching the highest bids with the lowest offers, permitting buyers and sellers to trade directly;

a facilitator bringing together buyers and sellers who do not know of each other in order to execute a trade which would not otherwise occur;

an agent for broker-dealers who wish to execute transactions as instructed by their customers (typically, these orders are limit orders entrusted to the specialist at prices above or below the current market price); or a principal using its own capital to buy or sell stocks for its own account.

The specialist firm s decision to buy or sell shares of its specialist stocks as principal for its own account may be based on obligation or inclination. For example, the specialist firm may be obligated to buy or sell its specialist stock to counter short-term imbalances in the prevailing market, thus helping to maintain a fair and orderly market in that stock. At other times, the specialist firm may be inclined to buy or sell the stock as principal based on market conditions. In actively-traded stocks, the specialist firm continually buys and sells its specialist stocks at varying prices throughout each trading day. The specialist firm s goal and expectation is to profit from differences between the prices at which it buys and sells these stocks. In fulfilling its specialist obligations, however, the specialist firm may, at times, be obligated to trade against the market, adversely impacting its profitability. In addition, the specialist firm s trading practices are subject to a number of restrictions, as described in NYSE and AMEX Rules Governing Our Specialist Activities.

Recent Trends in NYSE Trading

Specialist firms generate revenues by executing trades, either as agent or principal, in their specialist stocks. Accordingly, the specialist firms revenues are significantly impacted by the share volume of trading on the NYSE. Over the last three years, average daily trading volume on the NYSE has been flat at approximately 1.4 billion shares. This may be attributed to:

- a relatively slow return by the retail investor to the equity markets following the 2000-2002 bear market;

- popular interest in alternative investments, particularly residential real estate and commodities;

- significant changes in the regulatory environment facing institutional investors, including the rules relating to research and underwriting; and

- the continued emergence of a new class of investors, including hedge funds, that invest in non-traditional instruments.

In addition to the declining annual growth of trading volume on the NYSE, several other factors negatively impacted specialists revenues during 2004, including:

- declining volatility of stock prices as measured by the CBOE s Volatility Index®, a key measure of market expectation of near-term volatility and investor sentiment. As volatility in markets diminishes, the need for specialists to employ capital to mitigate volatility decreases, which in turn reduces specialists level of principal participation; and

- increased program trading as a percentage of total NYSE average daily share volume. Program trading often results in a number of smaller orders executed through the NYSE s SuperDOT® system. As a result, block-trading strategies have become less prevalent.

Despite increases in the major stock indices during 2004, including the Dow Jones Industrial Average, S&P 500 Index and the NYSE Composite Index, the combination of the aforementioned factors adversely affected our specialist operations.

The majority of trades in NYSE-listed stocks take place on the NYSE. In 2004, specialist firms handled 79.3% of trades in NYSE-listed stocks as compared to 79.5% in 2003. The percentage of trades in NYSE-listed stocks on the floor of the NYSE is affected as follows:

some stocks are listed on multiple exchanges, such as regional exchanges, and trades take place on those exchanges as well as in the over-the-counter market and through alternative trading systems (ATSs); and

at times, significant volume in NYSE-listed stocks takes place before and after regular NYSE trading hours.

Technological advances have contributed to increased trading through ATSs, such as electronic communications networks, or ECNs, and electronic crossing systems. While the first ECN was created in 1969, most of the ECNs currently in operation were started only during the past several years. These systems electronically facilitate the matching of buy and sell orders that are entered by their network members. If a match does not occur, some ATSs will forward unfilled orders to other ATSs or to exchanges such as the NYSE. Some of these networks also allow limited negotiation between members to facilitate a match. These ATSs generally limit trades over their systems to their members, who are typically large financial institutions, professional traders or brokerage firms. Additionally, some ATSs are being developed to facilitate trading by retail investors. In April 1999, the SEC ruled that these networks are allowed, and in specified cases are required, to register and become subject to regulation as stock exchanges.

Despite the presence of these ATSs, to date, there has been only a slight decline in the percentage of equity shares traded on the NYSE. The percentage of annual trading of NYSE-listed stocks on the NYSE has ranged from 79.3% to 84.0% for the past five years. It is unclear, however, how ATSs and other new technologies will affect the future percentages of trading in listed stocks conducted on the NYSE.

In response to the development of ATSs, in 2001 the NYSE launched Network NYSE, a suite of market information and auto-execution products offering new choices to different types of customers. Some examples of these products include:

NYSE Direct+®, an automatic execution service for limit orders up to 1,099 shares, enabling investors to automatically execute orders at the national best bid offer;

NYSE OpenBook(SM), an online market data product allowing subscribers to view information on the NYSE limit order books; and

Institutional Express(SM), an electronic gateway to satisfy large order requirements and the growing information needs of NYSE member firms and their institutional customers.

During 2004, the NYSE also proposed to institute a Hybrid Market system, which enables investors to choose how their orders are executed on the NYSE. As proposed, an investor interested in speed, certainty and anonymity of execution can choose the NYSE Direct+® automatic execution system. An investor interested in the opportunity for price improvement can choose the NYSE s auction process. Specifically, the NYSE Direct+® system will be enhanced by eliminating the rule requiring a delay of at least 30 seconds between orders for the same customer, eliminating the 1,099-share size limit for orders on NYSE Direct+® and allowing traders to sweep the book within a specified range, allowing execution at different price points.

In addition, on February 26, 2004, the SEC proposed new rules (Regulation NMS) which would require, subject to certain exceptions, that every order execution facility (i.e., every national securities exchange, national securities association that operates an order execution facility, alternative trading system, exchange specialist and market-maker, OTC market-maker, block positioner and any other broker or dealer that executes orders internally by trading as principal or crossing orders as agent), establish, maintain and enforce polices and procedures reasonably designed to prevent the execution of a trade-through (*viz*., the execution of an order at a price that is inferior to a price displayed in another market) in its market. As originally proposed, this requirement would apply to all incoming orders in NMS Stocks, including all NASDAQ, NYSE and AMEX-listed stocks and to any order execution facility that executes orders internally within its market, whether or not that market posts its best bid and offer in the consolidated quote system. The two major exceptions to this requirement, however, would have (1) allowed customers (and broker-dealers trading for their own accounts) to opt-out of the protections of the rule by providing informed consent to the execution of their orders, on an order-by-order basis, in one market without regard to the possibility of obtaining a better price in another market, and (2) taken into account the differences between the speed of execution in electronic versus manual markets by providing an automated market with the ability to trade-through a non-automated market at a price up to a certain amount away from the best bid or offer displayed by the non-automated market.

On December 16, 2004, after receiving numerous comments on proposed Regulation NMS, the SEC reproposed Regulation NMS (Reproposed Regulation NMS) and opened it for a 30-day comment period, which ended on January 26, 2005. Reproposed Regulation NMS includes the following refinements of the trade-through rule:

the establishment of intermarket protection against trade-throughs for all NMS stocks and protection of only those quotations that are immediately accessible through automatic execution. The revised rule also would limit investors' ability to opt out of the trade-through rule.

two alternative approaches to the scope of quotations to be protected:

The Market BBO Alternative, which would protect only the best bids and offers (BBOs) of each exchange trading a security, as well as the BBO of the NASD s Alternative Display Facility and NASDAQ s BBO; and

The Voluntary Depth Alternative, which would protect the BBOs of each market and would establish a mechanism for a market to voluntarily protect its quotations at prices below its best bid or above its best offer (depth-of-book) that are publicly displayed. Thus, the alternative rule would protect all publicly displayed quotes, or limit orders, and not just the best quote.

While the effect on our business operations of adoption of the NYSE s and SEC s proposed rule changes, either in their current form or in a modified form, cannot be predicted with certainty, we believe that the proposed enhancements to NYSE Direct+® should enable the NYSE to remain competitive for order flow by offering a combination of best price, high liquidity and fast execution.

Our Specialist Operations

Our NYSE and AMEX Equity Specialists

Our NYSE and AMEX equity specialist operations are conducted through our LaBranche & Co. LLC subsidiary. As a specialist in equity securities and rights listed on the NYSE and in equity securities on the AMEX, LaBranche & Co. LLC s role is to maintain, as far as practicable, a fair and orderly market in its specialist stocks. In doing so, it provides a service to its listed companies, and to the brokers, traders and investors who trade in its specialist stocks. As a result of our commitment to providing high quality specialist services, we have developed a solid reputation among our constituencies, including investors, members of the Wall Street community and our listed companies.

While our specialist business has grown considerably since our 1999 initial public offering, our operating results have weakened over the last two fiscal years. Revenues from our Specialist operations have decreased from $401.2 million in 2002 to $245.0 million in 2004. Since our initial public offering, we have increased the number of our listed companies and specialist market share both internally and through acquisitions. Since the NYSE implemented its new specialist allocation process in March 1997, we have been selected by 174 new listed companies, resulting from 408 listing interviews through December 31, 2004. In addition, we have acquired eleven specialist operations since 1997, adding approximately 500 NYSE common stocks and 52 AMEX common stocks. As a result of internal growth and selective acquisitions, our LaBranche & Co. LLC subsidiary currently is a leading NYSE specialist as illustrated by the following data:

the dollar volume traded of stocks for which LaBranche & Co. LLC was the specialist on the NYSE in 2004 was $2.8 trillion, or 25.4% of total 2004 NYSE dollar volume, and was $2.5 trillion in 2003, or 26.9% of total 2003 NYSE dollar volume;

the share volume traded of stocks for which LaBranche & Co. LLC was the specialist on the NYSE in 2004 was 96.1 billion, or 27.1% of total 2004 NYSE share volume, and was 94.5 billion in 2003, or 28.3% of total 2003 NYSE share volume; and

as of December 31, 2004, the total number of LaBranche & Co. LLC s NYSE common stock listings was 580, or 22.1% of all NYSE common stock listings, and as of December 31, 2003, its total number of NYSE common stock listings was 578, or 22.4% of all NYSE common stock listings.

By these three measurements, LaBranche & Co. LLC was one of the largest NYSE specialist firms as of December 31, 2004 and 2003. In addition, LaBranche & Co. LLC acted as the specialist for 243 other NYSE-listed securities (e.g., preferred stocks and derivative securities).

As of December 31, 2004, our LaBranche & Co. LLC subsidiary s listed companies included:

104 of the S&P 500 Index companies;

30 of the S&P 100 Index companies; and

7 of the 30 companies comprising the Dow Jones Industrial Average (DJIA). Our DJIA stocks are 3M Co., Altria Group, Inc., American Express Company, E.I. du Pont de Nemours and Company, Exxon Mobil Corporation, Merck & Co. Inc., and SBC Communications Inc.

Our Options/ETF Specialist and Market-Maker Operations

Through September 25, 2002, our AMEX specialist operations for both equities and options were conducted entirely by LaBranche & Co. LLC. Since then, we have conducted our options, ETFs and other derivatives specialist and market-making business activities on the AMEX, NYBOT, PHLX, Chicago Board Options Exchange® (CBOE), and other exchanges through our LSP subsidiary. Our equity specialist activities on the AMEX continue to be conducted by LaBranche & Co. LLC.

During 2004, LSP s operations continued to expand substantially. LSP revenues increased 92.4% from $18.4 million in 2003 to $35.4 million in 2004. In addition, LSP expanded its market-making activities to different derivative products as well as other financial markets. As of December 31, 2004, LSP acted as the specialist for 324 options, 5 futures and 3 ETFs listed on the AMEX, NYBOT, PHLX and other exchanges, and acted as a market-maker in 124 ETFs, 173 options and 19 futures on several other exchanges. Furthermore, during January 2005 and February 2005, LSP gained an additional 97 options listings on the AMEX, due to the reallocation of options formerly handled by another firm.

LSP is responsible for creating a fair and orderly market in the trading of its specialist options, ETFs and futures. In doing so, LSP may at times be obligated to trade against the market, adversely impacting the profitability of the trade or creating a position that may not necessarily be desired. To hedge the risk of its derivative positions, LSP may buy or sell the underlying asset(s). LSP also trades securities as principal out of both obligation and inclination.

As a registered market-maker in options, ETFs and futures, LSP generally engages in a course of dealings that is reasonably calculated to contribute to the maintenance of a fair and orderly market. LSP also may hedge these positions with the underlying assets or other financial instruments. In its market-making function, LSP brings immediacy and liquidity to the markets when it chooses to participate.

In January 2005, LSP also formed a wholly-owned subsidiary in the United Kingdom (UK), LSPE, to be a market-maker for ETFs traded on the London Stock Exchange, Eurex and Euronext exchanges. LSPE has yet to commence operations, but is in the process of registering as a broker-dealer with the UK s Financial Securities Authority (FSA). After it commences operations, we expect LSPE to also strengthen LSP s relationships with U.S. ETF issuers, which will help LSP diversify its exchange base and better manage its risk.

Our NYSE ETF Specialist Operations

In July 2004, LSPS commenced operations on the floor of the NYSE as an ETF specialist. As a specialist in ETFs listed on the NYSE, LSPS s role is to maintain, as far as practicable, a fair and orderly market in its ETFs. In doing so, it provides a critical service to brokers, traders and investors. As of December 31, 2004, LSPS acted as the specialist for 13 ETFs listed on the NYSE. For the year ended December 31, 2004, LSPS revenues were approximately $2.0 million and management expects further growth in this subsidiary through strategic resource allocation and anticipated increased market activity.

Our Specialist Support Services

In April 2002, BV was organized to represent LaBranche & Co. LLC in European markets and to provide client services to LaBranche & Co. LLC s European-listed companies. BV was established under Dutch law, and its office is in Amsterdam, The Netherlands. Through a services agreement, BV provides monitoring and trading services for LaBranche & Co. LLC s specialist stock positions, as specifically directed by appropriately designated LaBranche & Co. LLC personnel. In addition, BV markets the services of our specialist entities to existing and prospective European NYSE-listed issuers.

For detailed financial information in connection with our Specialist segment, please see Management s Discussion and Analysis of Financial Condition and Results of Operations Specialist Segment Operating Results and Note 17 to the Financial Statements filed herewith.

NYSE and AMEX Rules Governing Our Specialist Activities

Under NYSE and AMEX rules, a specialist has a duty to maintain, as far as practicable, a fair and orderly market in its specialist securities. In order to fulfill its obligations, the specialist must at times trade for its own account, even when it may adversely affect the specialist s profitability. In addition, under certain circumstances, the specialist is prohibited from making trades as principal in its specialist stocks. The specialist s obligations are briefly described below.

Requirement to Trade as Principal. A specialist must buy and sell securities as principal when necessary to minimize an actual or reasonably anticipated short-term imbalance between supply and demand in the auction market. The specialist must effect these transactions when their absence could result in an unreasonable lack of continuity and/or depth in its specialist stocks. The specialist is not expected to act as a barrier in a rising market or as support in a falling market, but must use its own judgment to try to keep such price increases and declines equitable and consistent with market conditions.

A specialist must make firm and continuous two-sided quotations that are timely and that accurately reflect market conditions. In making these quotations, the specialist s transactions are calculated to contribute to the maintenance of price continuity with reasonable depth.

Trading Restrictions. In trading for its own account, the specialist must avoid initiating a market-destabilizing transaction. All purchases and sales must be reasonably necessary to permit the specialist to maintain, as far as practicable, a fair and orderly market in its specialist stocks. In addition, the specialist must comply with the following trading requirements:

A specialist must first satisfy a customer s market buy order (an order to buy at the prevailing market price) before buying any stock for its own account. Similarly, a specialist must first satisfy a customer s market sell order (an order to sell at the prevailing market price) before selling any stock for its own account;

A specialist must first satisfy a customer s limit order held by it before buying or selling at the same price for its own account. A limit order is an order either to buy only at or below a specified price, or to sell only at or above a specified price. A specialist may not have priority over any customer s limit order. A specialist, however, may buy or sell at the same price as a customer limit order as long as that limit order is executed first;

If a public buyer wants to buy at a particular price and a seller wants to sell at the same price, the buyer and seller must be permitted to trade directly with each other, without specialist interaction;

The specialist does not charge commissions for trades in which it acts as a principal;

Except in some circumstances in less active markets, the specialist may not, without permission from an exchange official, initiate destabilizing trades for its own account which cause the stock price to rise or fall; and

Any transactions by the specialist for its own account must be effected in a reasonable and orderly manner in relation to the condition of the general market, the market in the particular stock and the adequacy of the specialist s position to the immediate and reasonably anticipated needs of the market.

In addition, the specialist cannot be in a control relationship with any of its listed companies. Generally, this means a specialist may not acquire more than 5% of any common or preferred issue of its specialist stocks and may not own 10% or more of any common or preferred stock. A specialist may not hold any position as an officer or director with, receive payments or loans from, or engage in certain business transactions with any of its listed companies.

New SEC-Proposed Market Rules. During fiscal 2004, the SEC proposed new rules, which are designed to modernize the regulatory structure of the U.S. equity markets. Refer to Recent Trends in NYSE Trading for a detailed discussion.

Listed Company Services

We are committed to providing our listed companies with a high level of service, in addition to our specialist functions on the trading floor. We have a Corporate Relations Department devoted to serving our listed companies. The most important function of the Corporate Relations Department is to provide current market information to our listed companies.

In addition, we keep management of our listed companies informed on general market trends. We organize an annual educational conference that reviews trends in the securities industry and equity markets. For newly listed companies on the NYSE, we provide additional investor relations support services to assist the companies with their transition to the NYSE. These services add significant value for companies considering a listing on the NYSE.

Competition in the Specialist Industry

We obtain each of our new listings on the NYSE and AMEX by participating in an allocation process. As part of this process, either the allocation committee of the NYSE or AMEX or the listing company chooses the specialist firm. We compete with other specialist firms based on a number of factors, including:

- the strength of our capital base;
- our willingness to commit our own capital and trade for our own account while conducting our specialist operations; and
- the ancillary services we offer our specialist companies, such as providing information on the trading activities in their stocks.

The specialist industry experienced a vast and accelerated consolidation over the past several years with the five largest specialist units, as ranked by their number of specialist stock listings, accounting for 95.1% of the daily share volume traded on the NYSE in 2004 as compared to 95.6% in 2003. The competition for obtaining newly listed companies is intense. We expect competition to continue and intensify as some of our competitors may have greater financial resources and product service offerings.

Our Specialist Segment s Competitive Position

We are committed to providing the highest quality service to our various constituencies. Our strong competitive position is based on the following factors:

Leading Position in the Specialist Market. We have a long-standing reputation as a leading specialist firm. We have successfully grown our business and improved our services through widely varying market conditions. Trading in the stocks for which we were the specialist during 2004 accounted for 25.4% of the dollar value and 27.1% of the share volume traded on the NYSE. By these measures, we were the largest specialist firm on the NYSE. As of December 31, 2004, we were the specialist for 580 common stocks and 13 ETFs listed on the NYSE and 104 common stocks, 324 options, 5 futures, and 3 ETFs listed on the AMEX, PHLX and NYBOT. Of our NYSE common stock listings, 127 were non-U.S. listings as of December 31, 2004.

Diverse and High Quality Specialist Stocks. Our listed companies operate in a variety of industries, including financial services, media, oil and gas, retail, technology and telecommunications. Many of our listed companies are leaders in their respective fields. They range in market capitalization from some of the smallest on the NYSE and AMEX to some of the largest and most well-known. Being the specialist in the stocks of industry leaders could benefit us as these leading companies expand their businesses through internal growth and acquisitions.

Strong Skills. We utilize our trading skills to actively participate as principal in trading our specialist stocks. We significantly improve liquidity in our specialist stocks, particularly during periods of market volatility. In 2004, approximately 20.6% of our trades were as principal as compared to an average of approximately 20.4% for all NYSE specialists.

Innovative Customer-Oriented Services. In addition to our specialist functions on the trading floor, we provide our listed companies with a high level of service (e.g., detailed information on the trading activity of their stocks), as well as customized support services to assist in their investor relations efforts.

Completed Acquisitions. Since 1997, we have acquired eleven specialist operations adding approximately 500 NYSE common stocks and 52 AMEX common stocks, solidifying our position as one of the leading NYSE specialist firms, as well as establishing and expanding our presence on the AMEX.

Our Execution and Clearing Segment

Recent Trends in Execution and Clearing Industry

The traditional clearing industry has, over the last few years, consolidated down to a small number of highly capitalized and extremely focused competitors. Mostly owned by or affiliated with large investment or commercial banks, these few top competitors command the dominant share of the fully-disclosed correspondent clearing market. As a result, barriers to entry have risen and the capital expenditures necessary to maintain market share have increased.

As the result of years of advances in order delivery and execution technology, trading costs for customers across all categories (retail, institutional, etc.) have dropped dramatically. These advances in trading technologies, and the resulting economies afforded the customer, have also engendered an entirely new style of investment management, where algorithms embedded in servers generate, direct and account for orders with only a modicum of human interaction. Orders generated and delivered over purely electronic platforms now account for more than 50% of NYSE volume.

In addition, there have arisen a number of non-traditional execution venues that bypass the traditional exchanges and ECN s in which institutions can trade directly with each other without exposing orders to market-wide price verification.

Our Execution and Clearing Operations

LFSI, our execution and clearing segment, provides clearance and execution services to a range of clients. To our broker dealer correspondents, we provide traditional clearance services. To our own customers, which include institutions and individuals, we provide a range of customized execution services, including direct-access brokerage.

LFSI does not focus on commoditized bulk clearance and execution. LFSI targets businesses where flexibility, technological expertise and a versatile execution and clearance platform provides us with a competitive advantage.

Our Institutional Executive Group (IEG) provides institutions with highly customized service built around special execution needs. IEG focuses on timely executions with minimal market impact. IEG handles and clears trades on every major domestic exchange with straight through processing from order origination to trade execution. IEG also provides soft dollar execution and other administrative services to institutional customers.

IEG has also developed a purely electronic trading system to execute a wide range of institutional strategies. With offices in Massachusetts and Minnesota, IEG plans to grow head count and expand geographically. IEG has active relationships with over 220 institutional accounts and is developing its business nationwide.

For detailed financial information in connection with our Execution and Clearing segment, please see Management s Discussion and Analysis of Financial Condition and Results of Operations Execution and Clearing Segment Operating Results and Note 17 to the Financial Statements filed herewith.

Regulatory Matters

The securities industry in the United States is subject to regulation under both Federal and state laws. In addition, the SEC, NYSE, AMEX and other regulatory organizations require compliance with their rules and regulations.

Our broker-dealer subsidiaries, LaBranche & Co. LLC, LFSI, LSP and LSPS are subject to regulations concerning operational and financial aspects of their respective businesses. They are subject to registration requirements of various government entities and self-regulatory organizations (commonly referred to as SROs) with which they must comply before they may conduct business. Our broker-dealer subsidiaries are also subject to laws, rules and regulations requiring them to comply with financial reporting rules, trade practices, capital structure obligations and record retention requirements. Failure, or even the assertion by a regulatory organization of failure, by any of our broker-dealer subsidiaries to comply with any of these laws, rules or regulations could result in censure, fine, the issuance of cease-and-desist orders or the suspension or disqualification of its directors, officers or employees and other negative consequences, which could have an adverse effect on our business.

Refer to Legal Proceedings Specialist Trading Investigations. From time to time, in the ordinary course of business, we have been subject to other fines for violations of such laws, rules or regulations.

Our trading subsidiaries are under constant review by the NYSE and other exchanges on which they conduct operations on all aspects of their operations and financial condition. In particular, as part of the price discovery mechanism implemented by the NYSE, every NYSE specialist transaction is published immediately and broadcast worldwide. The NYSE s Market Surveillance Division employs sophisticated monitoring and requires adherence to stringent rules approved by the SEC in its examination of NYSE specialists trading in all stocks.

The USA PATRIOT Act of 2001 (the PATRIOT Act) contains anti-money laundering and financial transparency laws and mandates the implementation of various new regulations that apply to broker-dealers and other U.S. financial institutions, including procedures for verifying client identification at account opening, and obligations to monitor client transactions and report suspicious activities. Through its provisions, the PATRIOT Act seeks to promote cooperation among U.S. financial services companies, regulators and law enforcement officials in identifying parties that may be involved in terrorism or money laundering. The increased obligations of financial institutions, including our broker-dealer subsidiaries, require the implementation and maintenance of internal control procedures which have increased our costs and may subject us to liability.

Capital Requirements

Our broker-dealer subsidiaries are also subject to net capital requirements as required by SEC Rule 15c3-1, and net liquid asset requirements as required by the NYSE and AMEX. Please refer to Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources section for our broker-dealer subsidiaries capital requirements and actual amounts.

Failure by any of our broker-dealer subsidiaries to maintain the required net capital and/or net liquid assets may subject it to suspension or revocation of SEC registration or suspension or expulsion by the respective exchanges of which it is a member.

Employees

As of December 31, 2004, we had 525 full-time employees, of which 381 were employed at our Specialist segment, 104 were employed at our Execution and Clearing segment, and 40 were employed at the holding company.

Risk Factors

The following risk factors should be carefully considered in evaluating our business and us because they have a significant impact on our business, operating results, financial condition, and cash flows. If any of these risks actually occurs, our business, financial condition, operating results and/or cash flows could be adversely affected.

The market structure in which we operate may change, making it difficult for us to maintain our levels of profitability.

The market structure in which we operate is subject to changes that could adversely affect our financial condition and results of operations. Most notably, the NYSE s recent proposed changes in its automated trade execution system and the SEC s recent proposed structural changes in the U.S. equity trading markets may have an adverse effect on our business.

In February 2004 and again on August 2, 2004, the NYSE proposed to expand its Direct+® trading system to eliminate the current limits on size, timing and types of orders that currently may be executed electronically through the Direct+® system and thereby create a so-called hybrid market intended to incorporate a number of new trade execution options while preserving the option of access to auction price discovery and deep liquidity. Specifically, the NYSE s proposals would eliminate the 1,099-share restriction on NYSE Direct+® orders, as well as the prohibition against entering orders for the same account within 30 seconds, and would permit market orders and immediate-or-cancel orders to be eligible for Direct+® execution. In addition, the NYSE s proposals contain a number of other new features designed to create a liquidity pool accessible for electronic and auction price discovery; the opportunity for benefits associated with human judgment at the point of sale; and accountable performance with focused communication by specialists. The NYSE has indicated that it already has begun the technological work necessary to implement its proposed changes in the NYSE Direct+® system and has estimated that, subject to approval of its proposed changes by the SEC, a pilot or phased start of the new Direct+® system will get underway sometime in 2005.

In February 2004, the SEC proposed new rules which would require, subject to certain exceptions, that every order execution facility (*i.e.*, every national securities exchange, national securities association that operates an order execution facility, alternative trading system, exchange specialist and market maker, OTC market maker, block positioner and any other broker or dealer that executes orders internally by trading as principal or crossing orders as agent) establish, maintain and enforce polices and procedures reasonably designed to prevent the execution of a trade through (*viz*., the execution of an order at a price that is inferior to a price displayed in another market) in its market. As originally proposed, this requirement would apply to all incoming orders in NMS Stocks, including all NASDAQ, NYSE and AMEX-listed stocks and any order execution facility that executes orders internally within its market, whether or not that market posts its best bid and offer, and would have (1) allowed customers (and broker dealers trading for their own accounts) to opt-out of the protections of the rule by providing informed consent to the execution of their orders, on an order-by-order basis, in one market without regard to the possibility of obtaining a better price in another market, and (2) taken into account the differences between the speed of execution in electronic versus manual markets by providing an automated market with the ability to trade through a non-automated market at a price up to a certain amount away from the best bid or offer displayed by the non-automated market.

On December 16, 2004, after receiving numerous comments on its proposed Regulation NMS rules, the SEC reproposed Regulation NMS (Reproposed Regulation NMS) and opened it for a 30-day comment period that ended on January 26, 2005. Reproposed Regulation NMS includes the following refinements of the trade-through rule:

the establishment of intermarket protection against trade-throughs for all NMS stocks and protection of only those quotations that are immediately accessible through automatic execution. The revised rule also would limit investors' ability to opt out of the trade-through rule.

two alternative approaches to the scope of quotations to be protected:

The Market BBO Alternative, which would protect only the best bids and offers (BBOs) of each exchange trading a security, as well as the BBO of the NASD s Alternative Display Facility and NASDAQ s BBO; and

The Voluntary Depth Alternative, which would protect the BBOs of each market and would establish a mechanism for a market to voluntarily protect its quotations at prices below its best bid or above its best offer (depth-of-book) that are publicly displayed. Thus, the alternative rule would protect all publicly displayed quotes, or limit orders, and not just the best quote.

We are subject to extensive regulation under federal and state laws that could result in investigations, fines or other penalties.

On March 29, 2004, we entered into a definitive agreement with the NYSE and the SEC to settle investigations by the NYSE and the SEC concerning specialist trading activity. The findings, neither admitted nor denied, include violations of Section 11(b) of the Exchange Act and rules promulgated thereunder concerning specialist trading, including the requirement that a specialist maintain a fair and orderly market, violation of various NYSE rules and violations of Section 15(b)(4)(E) of the Exchange Act, including failure to supervise with respect to certain transactions in which one or more employees allegedly violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder. Pursuant to the agreement, and without admitting or denying any wrongdoing, we paid on April 7, 2004 a total of $63.5 million for certain trades that occurred during the five-year period from 1999 through 2003. This settlement resolved the NYSE and the SEC investigations of specialist trading activity concerning us for all periods through 2003. The settlement represented a subsequent event reportable for 2003 under accounting principles generally accepted in the United States of America, and we recorded a $63.5 million pre-tax charge for 2003. The four other largest NYSE specialist firms also settled the investigations concerning their specialist trading activity during the 1999 through 2003 period at the same time. The two smaller NYSE specialist firms later settled the investigations concerning their specialist trading activity during the 1999 through 2003 period. More recently, in December 2004, our LaBranche & Co. LLC subsidiary received a notice from the NASD Amex Regulation Division stating a preliminary determination by the NASD Amex Regulation Division s staff to seek disciplinary action against LaBranche & Co. LLC for violations of certain federal securities laws and the Amex s Constitution and Rules, including Sections 10(b), 9A and

17(a) of the Securities Exchange Act of 1934, in connection with manual book freezes effected in one of LaBranche & Co. LLC s Amex specialist stocks during the period March 8, 2004 through October 21, 2004.

We are subject to extensive regulation under both federal and state laws. In addition, the SEC, the NYSE, the NASD, the AMEX, other self-regulatory organizations, more commonly known as SROs, and state securities commissions require strict compliance with their respective rules and regulations. As a result of our acquisitions since 1997 and the consequent increase in the size of our business and in the number of our employees, the risk that we will not detect or prevent employee misconduct has increased. Employee misconduct that may be difficult to detect could result in losses. Misconduct by employees could include, among other things, binding us to transactions that exceed authorized limits or present unacceptable risks, or hiding from us unauthorized or unsuccessful activities, which, in either case, may result in unknown and unmanaged risks or losses. Employee misconduct could also involve the improper use or disclosure of confidential information, which could result in regulatory sanctions and serious reputation or financial harm.

If there are any additional investigations or actions against us or any of our subsidiaries, such investigations or actions could result in settlements, determinations or judgments requiring substantial payments by us, including the costs of defending such investigations or actions, the imposition of substantial sanctions, fines or penalties and the suspension or revocation of our registration with the SEC as a broker dealer or our suspension or expulsion as a member firm of the NYSE and the AMEX, in which case we would be unable to operate our business.

It also may be difficult for us to comply with other new or revised legislation or regulations imposed by the SEC, other U.S. or foreign governmental regulatory authorities and SROs, including the NYSE and the AMEX. Failure to comply would have an adverse effect on our business, financial condition and/or operating results. Other changes in the interpretation or enforcement of existing laws and rules by the SEC, these governmental authorities and SROs also could have an adverse effect on our business, financial condition and/or operating results.

Failure to comply with undertakings set forth in the settlement with the NYSE and SEC could adversely affect us.

In connection with the settlement of the NYSE and the SEC investigations concerning our NYSE specialist trading activity, we agreed to, and we are complying with, the following undertakings:

implementation of systems and procedures to ensure appropriate follow up and review with regard to information provided to LaBranche & Co. LLC on a daily basis by the NYSE with regard to specialists override of the Principal Inhibitor function, which identifies specialist principal trades that may have been effected while an executable agency order was reflected in the order book on the same side of the market;

creation of a committee, including LaBranche & Co. LLC s chief compliance officer and at least two members of senior management, specifically charged with meeting periodically (no less frequently than monthly) to evaluate specialist rule compliance;

development and/or enhancement of systems and procedures to track and maintain records identifying the individuals acting as specialist and clerk for each security at all times throughout each trading day;

annual certification, through LaBranche & Co. LLC s chief executive officer, that a review has been conducted by the chief compliance officer of trading in LaBranche & Co. LLC s principal account for the purpose of detecting interpositioning, trading ahead and unexecuted limit order violations;

bi-annual assessment of, and reports on, the adequacy of the resources devoted to LaBranche & Co. LLC s compliance function, and devotion of adequate funds and staffing to the compliance department; and

retention of an independent consultant to review and evaluate LaBranche & Co. LLC s compliance systems, policies and procedures reasonably designed to ensure that LaBranche & Co. LLC is in compliance with federal securities laws and NYSE rules with regard to specialist trading.

If we are, in the future, unable to satisfy or maintain compliance with any of these undertakings for reasons that we cannot foresee, such failure could have a material adverse effect on our business and our regulatory compliance structure.

We also are subject to the risks of securities laws liability and related civil litigation.

Many aspects of our business involve substantial risks of legal liability. A specialist is exposed to substantial risks of liability under federal and state securities laws, other federal and state laws and court decisions, as well as rules and regulations promulgated by the SEC, the NYSE and the AMEX.

The above-described NYSE and SEC investigations of our NYSE specialist trading practices have also resulted in the initiation of purported class action and derivative action proceedings against us and certain of our officers and directors in the United States District Court for the Southern District of New York and other proceedings in other courts, all of which are described under Business Legal Proceedings. We have continued to receive requests for information from the SEC and also have received requests for information from the United States Attorney s Office for the Southern District of New York as part of an industry-wide investigation relating to activities of NYSE floor specialists in recent years. Two additional actions have been commenced by entities against four national securities exchanges and 35 securities brokers (including our LSP subsidiary) in the United States District Court for the Northern District of Illinois, alleging that LSP conspired with the other defendants by allegedly failing to execute orders, canceling orders and refusing to cancel orders for the purchase and sale of options.

While we deny the allegations of wrongdoing against us in these actions, there can be no assurance as to the ultimate outcome or timing of their resolution. The range of possible resolutions could include determinations and judgments against us or settlements that could require substantial payments by us, including the costs of defending such investigations and suits, which could have a material adverse effect on our financial condition, results of operations and

19

cash flows.

We also are subject to the risk of civil litigation, employment claims and other actions in the ordinary course of our business operations. In particular, LFSI, as successor in interest to ROBB PECK McCOOEY Clearing Corporation, or RPMCC, has been the target, from time to time, of various claims and lawsuits incidental to the ordinary course of RPMCC s business operations. It is possible that we could incur significant legal expenses in defending ourselves against these and future lawsuits or claims. An adverse resolution of any future lawsuits or claims against us could have an adverse effect on our business, financial condition and/or operating results.

We may have insufficient capital in the future and may be unable to secure additional financing when we need it.

Our business depends on the availability of adequate capital. We cannot be sure that we will have sufficient capital in the future or that additional financing will be available on a timely basis, or on terms favorable to us. Historically, we have satisfied these needs with internally generated funds, the issuance of subordinated debt by our operating subsidiaries and the issuance of common stock and notes representing our indebtedness. While we currently anticipate that our available cash resources will be sufficient to meet our anticipated working capital, regulatory capital and capital expenditure requirements through at least the next twelve months, we may need to raise additional funds to:

- increase the capital available to us for our inventory positions;
- expand or diversify our operations;
- acquire complementary businesses; or
- respond to unanticipated capital requirements.

We may be required to obtain this additional financing on short notice as a result of rapid, unanticipated developments, such as a steep market decline.

Our revenues may decrease due to changes affecting the economy or changes affecting the securities markets, such as decreased volume, volatility or liquidity.

Adverse changes affecting the economy and/or the securities markets could result in a further decline in market volatility or liquidity, thus negatively impacting revenues at our specialist and execution and clearing segments. Many elements of our cost structure do not decline if we experience reductions in our revenues and we may be unable to adjust our cost structure on a timely basis, or at all, and we could suffer losses.

The lack of growth in share volume, rising program trading and low levels of volatility on the NYSE over the past three years have negatively affected our results of operations and may adversely affect our operations in the future. Although U.S. equity prices generally recovered in

2003 and 2004, adverse changes in the economy and the securities markets could return, resulting in:

- losses from declines in the market value of securities held in our accounts;
- a decline in trading volume on the NYSE, the AMEX and other exchanges;
- a decline in volatility in the securities markets in which we act as a specialist;
- the failure of buyers and sellers of securities to fulfill their settlement obligations; and
- further increases in claims and litigation.

Whether market and economic conditions will continue to improve and whether we will be able to adequately protect our interests and maintain revenues in the future is uncertain.

Risks associated with our trading transactions could result in trading losses.

A majority of our Specialist segment s revenues are derived from trading by us as principal. We may incur trading losses relating to these activities, since each such trade primarily involves the purchase, sale or short sale of securities for our own account. In any period, we may incur trading losses in a significant number of our specialist stocks, options, rights and ETFs for a variety of reasons, including price declines, lower trading volumes and the required performance of our specialist obligations. From time to time, we have large position concentrations in securities of a single issuer or issuers engaged in a specific industry. In general, because our inventory of securities is marked-to-market on a daily basis, any downward price movement in these securities results in an immediate reduction of our revenues and operating results. LSP s specialist and market-maker trading in options, ETFs, futures, other derivative instruments and foreign currencies also exposes it to certain additional risks associated with such factors as price fluctuations, foreign exchange currency movements, changes in the liquidity of markets, volatility and counterparty credit. Although we have adopted and carry out risk management procedures, we cannot be sure that these procedures have been formulated properly to identify or completely limit our risks and, even if formulated properly, we cannot be sure that we will successfully implement these procedures. As a result, we may not be able to manage our risks successfully or avoid trading losses.

Our securities transactions are conducted as principal and agent with broker-dealer counterparties located in the United States. While the NYSE, the AMEX and the clearing houses monitor the credit standing of the counterparties with which we conduct business, we cannot be certain that any of these counterparties will not default on their obligations. If any do, our business, financial condition and/or operating results could be adversely affected.

Specialist and market-maker rules require us to make unprofitable trades and refrain from making profitable trades.

Our roles as a specialist and market maker, at times, require us to make trades that adversely affect our operating results. In addition, as a specialist and market-maker, we are at times required to refrain from trading for our own account in circumstances in which it may be to our advantage to trade. For example, we may be obligated to act as a principal when buyers or sellers outnumber each other and take a position counter to the market, buying or selling shares to support an orderly market in the affected stocks. In addition, specialists and market-makers generally may not trade for their own account when public buyers are meeting public sellers in an orderly fashion and may not compete with public orders at the same price. By having to support an orderly market, maintain inventory positions and refrain from trading under some favorable conditions, we are subject to risk. In addition, one consequence of the SEC and the NYSE investigations of NYSE specialist trading practices may be amendments by the NYSE and, possibly, the AMEX, of the rules, practices and procedures governing our specialist and market-making activities in a manner that could adversely affect our trading revenues.

Failure to comply with net capital and net liquid asset requirements may result in the revocation of our registration with the SEC or our expulsion from the NYSE and/or the AMEX.

The SEC, the NYSE, the AMEX and various other regulatory agencies have stringent rules with respect to the maintenance of minimum levels of capital and net liquid assets by securities broker-dealers and specialist firms. Currently, LaBranche & Co. LLC and LSPS are required to maintain minimum combined net liquid assets of approximately $447.0 million. Failure by any of our broker-dealer and specialist subsidiaries to maintain its required level of net capital and net liquid assets may subject it to suspension or revocation of its SEC registration or suspension or expulsion by the NYSE and/or the AMEX. If this occurs, we would be unable to operate our business. In addition, a change in these rules, the imposition of new rules or any unusually large capital requirement or charge against the regulatory capital of any of our broker-dealer subsidiaries could limit those areas of our operations which require intensive use of capital. These rules also could restrict our ability to withdraw capital from our broker-dealer subsidiaries, thus limiting our ability to expand, diversify or even maintain our present levels of business, pay dividends, repay debt and repurchase shares of our outstanding common stock.

We depend primarily on our specialist activities, and if they fail to generate revenues as anticipated, it would adversely affect our financial condition and results of operations.

We derive the vast majority of our revenues from specialist activities. If demand for our specialist services fails to grow, grows more slowly than we currently anticipate or declines, our financial condition and results of operations would be adversely affected. We expect our specialist activities to continue to account for the vast majority of our revenues for the foreseeable future. Our future success will depend on:

- continued growth in the volume of trading and the number of listings on the NYSE, the AMEX and other exchanges;
- being chosen as the specialist for additional listing companies;
- our ability to respond to regulatory and technological changes; and

our ability to respond to changing demands in the marketplace.

This, in turn, could have an adverse effect on our revenues. Over the past few years, a number of alternative trading systems have been developed or emerged. These alternative trading systems may compete with specialists by increasing trading in NYSE-listed and AMEX-listed securities off the NYSE and the AMEX trading floors. In addition, as described above, the SEC and the NYSE s recently proposed market structure rule changes could result in increased trading of NYSE-listed and AMEX-listed securities in electronically-matched orders and thus reduce levels of trading of such securities through specialists.

Historically, a relatively small number of listed companies have accounted for a significant portion of our revenues from our NYSE specialist trading activities. The loss of any of these listed companies could have an adverse effect on our revenues. For the years ended December 31, 2002, 2003 and 2004, transactions in our 10 most actively traded NYSE specialist stocks accounted for approximately 27.5%, 19.0% and 16.8% of our total NYSE principal trading revenues, respectively. The composition of these ten most actively traded specialist stocks changes frequently. We cannot be certain that we will be able to retain these or any other of our top listed companies. We can lose these listed companies if they cease to be traded on the NYSE as a result of being acquired or otherwise delisted. In addition, under NYSE procedures allowing listed companies greater latitude to request a change in their specialist or if the NYSE were to determine that we have failed to fulfill our obligations as specialist for a listed company, our registration as the specialist for that listed company could be canceled or suspended.

We cannot be sure that we will be able to compete effectively with current or future competitors. Our failure to compete effectively would have an adverse effect on our operating results. We obtain all our new listings on the NYSE by going through an allocation process. In this process, either a committee of the NYSE or the listing company chooses the specialist. The competition for obtaining new listing companies is intense. We expect competition to continue and further intensify in the future. Some of our competitors may have significantly greater financial and other resources than we have and may have greater name recognition. These competitors may be able to respond more quickly to new or evolving opportunities and listing company requirements. They also may be able to undertake more extensive promotional activities to attract new listing companies, especially those which are not publicly-traded specialist firms.

We have significant debt obligations.

We have a significant amount of debt. As of December 31, 2004, our total debt outstanding was $500.7 million, excluding subordinated liabilities related to contributed exchange memberships. LaBranche & Co. LLC also may borrow, subject to certain conditions, up to $200.0 million to finance its specialist security positions under a committed line-of-credit with a U.S. commercial bank. Our significant level of debt could have important consequences, including the following:

our ability to obtain additional financing to fund growth, working capital, capital expenditures, debt service requirements or other purposes may be impaired;

our ability to use operating cash flow in other areas of our business may be limited because we dedicate a substantial portion of these funds to service our debt; and

limitation on our flexibility to adjust to changing market conditions, changes in our industry and economic downturns.

Our ability to take certain actions is restricted by the terms of our outstanding indebtedness.

The covenants in the indenture governing our outstanding 9.5% Senior Notes due 2009, in the aggregate principal amount of $199.9 million, and our outstanding 11.0% Senior Notes due 2012, in the aggregate principal amount of $260.0 million (collectively, the outstanding senior notes), LaBranche & Co. LLC s $200.0 million committed line of credit agreement with a bank and subordinated note purchase agreements (under which $12.0 million remains outstanding), as well as any future financing agreements, may adversely affect our ability to finance future operations or capital needs or to engage in other business activities. These covenants limit or restrict our ability and the ability of our subsidiaries to:

incur additional debt;

pay dividends and make distributions;

repurchase our common stock or subordinated indebtedness prior to maturity;

make certain investments;

create liens on our assets;

transfer or sell assets;

enter into transactions with affiliates;

- issue or sell stock of subsidiaries; or

- merge or consolidate.

The subordinated note purchase agreements also require LaBranche & Co. LLC to comply with certain financial ratios. LaBranche & Co. LLC s ability to comply with these ratios may be affected by events beyond our or its control. If any of the covenants in our indebtedness are breached, or if LaBranche & Co. LLC is unable to comply with required financial ratios, we or it may be in default under such agreements. A significant portion of our indebtedness then may become immediately due and payable. We are not certain whether we would have, or be able to obtain, sufficient funds to make these accelerated payments, including payments on the outstanding senior notes.

We may not be able to generate sufficient cash flows to meet our debt service obligations, including payments on the outstanding senior notes.

Our ability to generate sufficient cash flows from operations to make scheduled payments on our debt obligations will depend on our future financial performance, which will be, to an extent, subject to general economic, financial, competitive, regulatory and other factors that are beyond our control.

We cannot provide assurance that our business will generate sufficient cash flows or that future borrowings will be available to us in an amount sufficient to enable us to pay our debt, including the outstanding senior notes, or to fund our other liquidity needs. If our future cash flows from operations are insufficient to pay our obligations as they mature or to fund our liquidity needs, we may be forced to sell assets, obtain additional equity capital or restructure or refinance all or a portion of our debt, including the outstanding senior notes, on or before maturity. We cannot assure you that we will be able to repay or refinance our debt, including the outstanding senior notes, on a timely basis or on satisfactory terms, if at all.

We may not be able to finance a change of control offer required by the indenture governing the outstanding senior notes.

If we were to experience a change of control, we would be required to offer to repurchase all outstanding senior notes then-outstanding, as well as all of our then-outstanding 12.0% senior subordinated notes due 2007, in the aggregate principal amount of approximately $13.6 million (the 2007 notes), in each case at a price equal to 101.0% of their principal amount, plus accrued and unpaid interest, if any, to the date of repurchase. This purchase requirement may delay or make it harder for others to obtain control of us. If a change of control were to occur, it is possible that we would not have sufficient funds to repurchase these notes or that restrictions in the credit agreement and LaBranche & Co. LLC s subordinated note purchase agreements and such other notes would not allow such repurchases. If we do not have sufficient funds at the time of a repurchase obligation or cannot meet any obligations under the credit agreement, the subordinated note purchase agreements, the indenture governing the outstanding senior notes, or the indenture governing the 2007 notes, we would be forced to seek additional third-party financing. However, it is possible that we would not be able to obtain such financing on favorable terms, or at all.

Our success depends on our ability to accurately process and record our transactions, and any failure to do so could subject us to losses.

Our specialist, market-making and clearing and execution activities require us to accurately record and process a very large number of transactions on a daily basis. Any failure or delay in recording or processing transactions could cause substantial losses for brokers, their customers and/or us and could subject us to claims for losses. We rely on our staff to operate and maintain our information and communications systems properly, and we depend on the integrity and performance of those systems. Our recording and processing of trades is subject to human and processing errors. Moreover, extraordinary trading volume or other events could cause our information and communications systems to operate at an unacceptably low speed or even fail.

Any significant degradation or failure of our information systems or any other systems in the trading process could cause us to fail to complete transactions or could cause brokers who place trades through us to suffer delays in trading.

Any information or communication systems failure or decrease in information or communications systems performance that causes interruptions in our operations could have an adverse effect on our business, financial condition and/or operating results. Our systems may fail as a result of a hardware, software, power or telecommunications failure. In addition, our offices are located in close proximity to the site of the September 11, 2001 terrorist attacks on the World Trade Center. The aftermath of the attacks on the World Trade Center required us to close our operations and temporarily operate from our disaster recovery site. The NYSE also was forced to stop operating for four consecutive trading days, which caused our operations to halt. It is possible that additional terrorist attacks or acts of war may occur in the future and that such attacks could compromise or disable our systems. Although we have established back-up disaster recovery centers in New Jersey and New York, they may not be effective in preventing an interruption of our business.

We also are dependent on the proper and timely function of complex information and communications systems maintained and operated by or for the NYSE, the AMEX and clearing and depositary institutions. Failures or inadequate or slow performance of any of these systems could adversely affect our ability to operate and complete trades. The failure to complete trades on a timely basis could subject us to losses and claims for losses of brokers and their customers.

Our future success will depend on the ability to upgrade information and communications systems, and any failure to do so could harm our business and profitability.

The development of complex communications and new technologies, including Internet-based technologies, may render our existing information and communications systems outdated. In addition, our information and communications systems must be compatible with those of the NYSE and the AMEX. As a result, when and if the NYSE or the AMEX upgrades its systems, we will need to make corresponding upgrades. Our future success will depend on our ability, on a cost-effective basis, to timely respond to changing technologies. Our failure to do so could have an adverse effect on our business, financial condition and/or operating results.

The NYSE s ability to develop information and communications systems and complex computer and other technology systems has been instrumental in its growth and success. We are dependent on the continuing development of technological advances by the NYSE and the AMEX, a process over which we have no control. If the NYSE for any reason is unable to continue its history of computer-related and other technological developments and advances, it could have an adverse effect on the success of the NYSE, including its ability to grow, to manage its trading volumes and to attract new listings. Any such developments can be expected to adversely affect our operations, financial condition and operating results.

If we lose the services of our key personnel or cannot hire additional qualified personnel, our business will be harmed.

Our future success depends on the continued service of key employees, particularly George M.L. LaBranche, IV, our Chairman, Chief Executive Officer and President. The loss of the services of any of our key personnel or the inability to identify, hire, train and retain other qualified personnel in the future could have an adverse effect on our business, financial condition and/or operating results. Competition for key personnel and other highly qualified management, trading, compliance and technical personnel is intense. We cannot assure you that we will be able to attract or retain highly qualified personnel in the future.

In connection with our 1999 reorganization from partnership to corporate form and initial public offering of our common stock, a number of our current managing directors received substantial amounts of our common stock in exchange for their partnership interests. Because the shares of common stock were received in exchange for partnership interests, ownership of the shares is not dependent upon the continued employment of those managing directors. In addition, in and subsequent to our 1999 reorganization, many of our employees who are not managing directors have received grants of stock options and restricted stock units. The steps we have taken to encourage the continued service of these individuals, who include key senior personnel, may not be effective.

Our current and prospective employees may experience uncertainty about their future roles with us and our business prospects. This uncertainty may adversely affect our ability to attract and retain key personnel, which would adversely affect our business and results of operations.

We may have difficulty successfully managing our growth.

Our business has grown since 1997, primarily due to acquisitions we have made since then. The growth of our business has increased the demands upon our management and operations. This growth has required, and will continue to require, an increase in investment in management personnel, financial and management systems and controls and facilities. The scope of procedures for assuring compliance with applicable rules and regulations has changed as the size and complexity of our business has increased. In response, we have implemented formal compliance procedures that are regularly updated. Our future operating results will depend on our ability to continue:

- to improve our systems for operations, financial control and communication and information management;
- to refine our compliance procedures and enhance our compliance oversight;
- to maintain strong relationships with, and attract new, listed companies; and
- to retain and incentivize our employees.

Three of our current or former executive officers are in a position to substantially control matters requiring a stockholder vote.

27

Certain of our current and former managing directors who currently own a significant amount of our outstanding common stock have entered into a stockholders agreement under which they have agreed, among other things, that their shares of our common stock will be voted, for as long as they own their shares, as directed by a majority vote of George M.L. LaBranche, IV, our Chairman, Chief Executive Officer and President, Alfred O. Hayward, Jr., our executive officer, director and Chief Executive Officer of LaBranche & Co. LLC and James G. Gallagher, a former executive officer and director. Accordingly, these individuals have the ability to substantially control most matters requiring approval by our common stockholders. These matters include the election and removal of directors and the approval of any merger, consolidation or sale of all or substantially all our assets. This concentration of ownership could have the effect of delaying, deferring or preventing a change in control, a merger or consolidation, a takeover or another business combination.

Item 2. PROPERTIES.

Our offices are located at One Exchange Plaza, New York, New York, where we lease approximately 36,000 square feet under two separate leases expiring in January 2008, and at 120 Broadway, New York, New York, where we lease approximately 45,000 square feet under a sublease expiring in March 2006. We also lease five trading posts on the floor of the NYSE, approximately 8,600 square feet of additional space at locations in New York, New Jersey and Boston under leases expiring between June 2005 and September 2012. In addition, we lease approximately 1,000 square feet in Amsterdam, The Netherlands, under a lease expiring in April 2009, and a workstation (approximately 25 square feet) in London, England, under a month-to-month operating lease. We believe that our current leased space is suitable and adequate for the operation of our business as presently conducted and as contemplated to be conducted in the near future.

Item 3. LEGAL PROCEEDINGS.

Specialist Trading Investigations. On March 30, 2004, LaBranche & Co. LLC and other NYSE specialist firms entered into agreements with the SEC and NYSE to settle the SEC and NYSE investigations concerning alleged improper specialist trading practices by specialists on the NYSE. Pursuant to the settlement, LaBranche & Co. LLC consented, without admitting or denying any wrongdoing, to an SEC order instituting administrative cease-and-desist proceedings, making findings, and imposing remedial sanctions and a cease-and-desist order. The SEC s findings, neither admitted nor denied, included violations by LaBranche & Co. LLC of Section 11(b) of the Exchange Act and Rule 11b-1 promulgated thereunder, NYSE Rules 104, 92, 123B, 401 and 342, and Section 15(b)(4)(E) of the Exchange Act. The Section 15(b)(4)(E) finding includes a failure reasonably to supervise individual specialists who, the finding states, violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder with respect to transactions in six particular stocks. Pursuant to the settlement, LaBranche & Co. LLC paid $41.6 million in restitution and $21.9 million in a civil money penalty, which we accrued for the year ended December 31, 2003, in connection with trades that occurred during the years 1999 through 2003 and has agreed to undertakings stated in the SEC s order. We have continued to receive requests for information from the SEC and also have received requests for information from the United States Attorney s Office for the Southern District of New York as part of an industry-wide investigation relating to activities of NYSE floor specialists in recent years. We are cooperating with the requests.

In re LaBranche Securities Litigation. On or about October 16, 2003 through December 16, 2003, nine purported class action lawsuits were filed by purchasers of our common stock in the United States District Court for the Southern District of New York, including Sofran v. LaBranche & Co Inc., et al., No. 03 CV 8201, Semon v. LaBranche & Co Inc., et al., No. 03 CV 8255, Haug v. LaBranche & Co. Inc., et al., No. 03 CV 8265, Labul v. LaBranche & Co Inc., et al., No. 03 CV 8365, Murphy v. LaBranche & Co Inc., et al., No. 03 CV 8462, Strain v. LaBranche & Co Inc., et al., No. 03 CV 8509, Yopp v. LaBranche & Co Inc., et al., No. 03 CV 8783, Ferris v. LaBranche & Co Inc., et al., No. 03 CV 8806, and Levin v. LaBranche & Co Inc., et al., No. 03 CV 8918. On March 22, 2004, the court consolidated these lawsuits under the caption In re LaBranche Securities Litigation, No. 03 CV 8201. The court named the following lead plaintiffs: Anthony Johnson, Clyde Farmer, Edwin Walthall, Donald Stahl and City of Harper Woods Retirement System.

On June 7, 2004, plaintiffs filed a Consolidated Class Action Complaint. On July 12, 2004, plaintiffs filed a Corrected Consolidated Class Action Complaint. Plaintiffs allege that they represent a class consisting of persons and entities that purchased or otherwise acquired our common stock during the period beginning on August 19, 1999 and concluding on October 15, 2003. Plaintiffs allege that we, LaBranche & Co. LLC, and certain of our and/or LaBranche & Co. LLC s past or present officers and/or directors, including George M.L. LaBranche, IV, William J. Burke, III, James G. Gallagher, Alfred O. Hayward, Jr., Robert M. Murphy and Harvey S. Traison, violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder and Section 20(a) of the Exchange Act by failing to disclose improper specialist trading. Plaintiffs also allege that two other of our past or present officers and/or directors, S. Lawrence Prendergast and George E. Robb, Jr., also violated Section 20(a) of the Exchange Act. Plaintiffs seek unspecified money damages, attorneys fees and reimbursement of expenses.

In re NYSE Specialists Securities Litigation. On or about October 16, 2003 through December 16, 2003, four purported class action lawsuits were brought by persons or entities who purchased and/or sold shares of stocks of NYSE-listed companies for which LaBranche & Co. LLC and any other NYSE specialist firm acted as specialist, including Pirelli v. LaBranche & Co Inc., et al., No. 03 CV 8264, Marcus v. LaBranche & Co Inc., et al., No. 03 CV 8521, Empire v. LaBranche & Co Inc., et al., No. 03 CV 8935, and the California Public Employees Retirement System (CalPERS) v. The New York Stock Exchange, Inc., et al., No. 03 CV 9968. On March 11, 2004, a fifth action asserting similar claims, Rosenbaum Partners, LP v. The New York Stock Exchange, Inc., et al., No. 04 CV 2038, was filed in the United States District Court for the Southern District of New York by an individual plaintiff who does not allege to represent a class. On May 27, 2004, the court consolidated these lawsuits under the caption In re NYSE Specialists Securities Litigation, No. CV 8264. The court named the following lead plaintiffs: California Public Employees Retirement System (CalPERS) and Empire Programs, Inc.

On September 15, 2004, plaintiffs filed a Consolidated Complaint for Violation of the Federal Securities Laws and Breach of Fiduciary Duty alleging that they represent a class consisting of all public investors who purchased and/or sold shares of stock listed on the NYSE from October 17, 1998 to October 15, 2003. Plaintiffs allege that we, LaBranche & Co. LLC, Mr. LaBranche and other NYSE specialist firms and their respective parents and affiliates violated Section 10(b), Rule 10b-5 and Section 20(a) by failing to disclose improper specialist trading, improperly profiting on purchases and/or sales of NYSE-listed securities and breaching and/or aiding and abetting breaches of fiduciary duty. Plaintiffs also name the NYSE as a defendant. Plaintiffs seek unspecified money damages, restitution, forfeiture of fees, commissions and other compensation, equitable and/or injunctive relief, including an accounting of and the imposition of a constructive trust and/or asset freeze on trading proceeds, and attorneys fees and reimbursement of expenses.

Posner. On or about December 4, 2003, an action brought by Michele Posner, who purports to act on behalf of the general public, Posner v. LaBranche & Co Inc., et al., No. BC307099, was filed in the Superior Court of the State of California, County of Los Angeles. Plaintiff alleges that we, Messrs. LaBranche, Burke, Hayward, Murphy and Traison, other NYSE specialist firms, the parents and affiliates of other specialist firms and individuals at other specialist firms violated California Business and Professions Code § 17200 by engaging in improper specialist trading. Plaintiff sought an order permanently enjoining the alleged misconduct, restitution, an order declaring acts and practices to be unlawful, unfair and/or fraudulent, an accounting to determine the amount to be returned by defendants and the amounts to be refunded to members of the public, the creation of an administrative process for defendants customers to recover their losses, and attorneys fees. On February 27, 2004, the defendants in the action removed the action to the United States District Court for the Central District of California (No. CV04-1345). On May 17, 2004, the action was transferred to the United States District Court for the Southern District of New York (No. 04 CV 3966). On December 8, 2004, plaintiff voluntarily dismissed the action.

Brown. On or about November 6, 2003, a purported shareholder derivative action, Brown v. George M. L. LaBranche IV, et al., No. 03 603512, was filed by Norman and Florence Brown, who purport to be two of our shareholders, and who purport to act on behalf of us, against certain of our past or present directors and officers, including Messrs. LaBranche, Hayward, Murphy and Traison and Thomas E. Dooley, E. Margie Filter (who is deceased), James G. Gallagher, David A. George, Donald E. Kiernan, S. Lawrence Prendergast and George E. Robb, Jr., in the Supreme Court of the State of New York, New York County. Plaintiffs allege breaches of fiduciary duty arising out of statements by us concerning our specialist trading business that are alleged to have been false and misleading because we failed to disclose alleged violations of NYSE rules. According to plaintiffs, [a]t least a majority of the Individual Defendants had knowledge of, or were reckless in not knowing of these false and misleading statements and the improper transactions concealed by such statements, and failed to establish and maintain adequate policies, systems and procedures reasonably designed to detect and prevent such improper transactions. Plaintiffs seek damages, return of all compensation received by the defendants for periods during which they allegedly breached their fiduciary duties, an order requiring implementation of corrective measures to prevent repetition of the alleged wrongful conduct, and attorneys fees and reimbursement of expenses.

On November 8, 2004, the court dismissed the action due to plaintiffs failure to make a pre-litigation demand. The court s decision states that the dismissal is without prejudice to the bringing of a new action, if a pre-suit demand is either rejected or not considered within a reasonable amount of time.

On January 31, 2005, plaintiffs made a demand, alleging improper transactions in connection with [LaBranche & Co. LLC s] role as a specialist on the New York Stock Exchange and further alleging that the Board of Directors breached its fiduciary duties by . . . failing to exercise reasonable and prudent supervision over the management policies, practices, controls, and financial affairs of LaBranche, and demanding the following: (1) the appointment of new independent directors who will form a special committee to investigate the alleged managerial, financial, trading and accounting improprieties, (2) modification of the definition of outside director, (3) separation of the office of chairman and chief executive officer and the election by outside directors of an outside director to serve as chairman, (4) the special committee must seek restitution and/or monetary damages on behalf of the Company, by lawsuit if necessary, from Messrs. LaBranche, Burke, Dooley, Gallagher, George, Hayward, Kiernan, Murphy, Prendergast, Robb and Traison and Ms. Filter and any other current or former officer, director or employee, for any and all costs incurred by the Company as a result of the alleged improprieties including, but not limited to, any damages incurred as a result of the federal securities lawsuits, (5) an investigation by outside auditors of accounting and controls, following which our board must ensure that any and all deficiencies or weaknesses in the Company s accounting and controls are promptly remedied, (6) creation of a chief ethics officer position and mandatory ethics training, and (7) a recommendation by the special committee of the resignation or dismissal from office of any and all officers, directors or employees found to have breached any fiduciary duty to the Company, or any law, regulation or internal Company rules. The letter states that the Brown s counsel intend to file a shareholder derivative complaint on behalf of the Browns and for the benefit of LaBranche if, after the expiration of ninety (90) days from the date of this demand, the Board has not responded to the demand or has otherwise failed to satisfy controlling law.

Henik. On or about February 1, 2005, a purported shareholder derivative action, Henik v. LaBranche, et al., No. 05 CV 1087, was filed by Diane Henik, who purports to be one of our stockholders, and who purports to act on behalf of us, against certain of our past or present directors and officers, including Messrs. LaBranche, Burke, Dooley, Gallagher, George, Hayward, Kiernan, Murphy, Prendergast, Robb and Traison and Ms. Filter, in the United States District Court for the Southern District of New York. Plaintiff alleges breaches of fiduciary duty arising out of alleged improper specialist trading and violations of NYSE rules. According to plaintiff, the defendants engaged in numerous acts, and on some occasions, failed to act, both of which caused LaBranche to suffer damages, were extremely reckless with respect to LaBranche s internal controls, its corporate governance practices, and their own formal oversight responsibility, it [is] likely that some or all defendants actually directed, knew of, acquiesced after the fact, or could have easily discovered the alleged improper trading, there were numerous red flags . . . that were deliberately ignored that suggest that the Board actually knew of the misconduct alleged herein or that could have alerted a conscientious director that something was amiss, and that the defendants either knowingly breached their fiduciary duties to LaBranche and its shareholders, or at the very least, engaged in extremely reckless conduct which also was a breach of fiduciary duties. Plaintiff seeks unspecified money damages, attorneys fees and reimbursement of expenses.

Last Atlantis and Rule. On January 20, 2004, five entities that allege that they are purchasers and sellers of options commenced an action in the United States District Court for the Northern District of Illinois, Last Atlantis Capital LLC v. Chicago Board of Options Exchange, Inc., et al., No. 04 C 0397, against four national securities exchanges (the American Stock Exchange, the Chicago Board Options Exchange, the Philadelphia Stock Exchange and Pacific Exchange) and 35 alleged securities brokers and/or dealers, including our LSP subsidiary, who, plaintiffs allege, made markets in options on the named exchanges. Plaintiffs allege that we and LSP conspired with other defendants by allegedly failing to execute orders, canceling orders, and refusing to cancel orders allegedly submitted by plaintiffs for the purchase and sale of options. Plaintiffs allege violations of federal antitrust laws (Section 1 of the Sherman Act), and securities law (Section 10(b) of the Exchange Act and Rule 10b-5), breach of contract, common law fraud, breach of fiduciary duty, violations of an Illinois consumer fraud and deceptive business practices statute, and tortious interference with plaintiffs business. Injunctive relief and damages (including punitive damages) in an unspecified amount are sought. On January 28, 2005, an individual represented by the same counsel who represent the plaintiffs in the Last Atlantis case commenced a substantially similar action in the United States District Court for the Northern District of Illinois, Rule v. Chicago Board of Options Exchange, Inc., et al., No. 05 C 0539, making substantially the same allegations and seeking the same relief against the same defendants, including LSP and us. To our knowledge, the complaint in the Rule case has not been served.

NASD/AMEX Notice of Disciplinary Action. On December 15, 2004, LaBranche & Co. LLC received a notice from the NASD Amex Regulation Division stating a preliminary determination has been made by the NASD Amex Regulation Division s staff to seek disciplinary action against LaBranche & Co. LLC for violations of certain federal securities laws and the Amex Constitution and Rules, including Sections 10(b), 9A and 17(a) of the Exchange Act, in connection with manual book freezes effected in one of LaBranche & Co. LLC s Amex specialist stocks during the period March 8, 2004 through October 21, 2004. Prior to receiving this notice, we had determined that the individual specialist responsible for the book freezes failed to adhere to company policy and had terminated that employee. We have submitted a response to the staff of the NASD Amex Regulation Division setting forth the reasons why disciplinary action should not be brought against LaBranche & Co. LLC and we are cooperating with the NASD Amex Regulation Division in this matter.

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

In addition to the proceedings described above, we and our operating subsidiaries have been the target, from time to time, of various claims and lawsuits incidental to the ordinary course of our and their respective businesses, including, in particular, three separate employment discrimination proceedings currently pending against LaBranche & Co. LLC before the United States Equal Employment Opportunity Commission. While the ultimate outcome of those claims and lawsuits which currently are pending cannot be predicted with certainty, we believe, based on our understanding of the facts of these proceedings, that their ultimate resolution will not, in the aggregate, have a material adverse effect on our financial condition, results of operations or cash flows.

Item 4. **SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

There were no matters submitted to a vote of security holders during the fourth quarter of our fiscal year ended December 31, 2004.

PART II

Item 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES.

Market Information

Our common stock is quoted on the NYSE under the symbol LAB. The following table sets forth the range of high and low closing sales prices for our common stock on the NYSE for the periods indicated:

	Fiscal 2003		Fiscal 2004	
	High	**Low**	**High**	**Low**
First Quarter	$ 26.99	$ 15.51	$ 12.10	$ 8.97
Second Quarter	$ 22.75	$ 16.29	$ 11.19	$ 8.20
Third Quarter	$ 23.26	$ 14.60	$ 8.58	$ 7.69
Fourth Quarter	$ 13.83	$ 7.60	$ 9.12	$ 7.09

Holders

As of February 1, 2005, we had 87 stockholders of record of our common stock and an estimated 7,200 beneficial owners. The closing sale price of our common stock on February 1, 2005 was $9.69 per share.

Dividends

Until 2003, we did not pay dividends on our common stock. In the first three fiscal quarters of 2003, however, we paid a quarterly cash dividend in the amount of $.08 per share to the holders of record of our common stock as of January 31, 2003, April 30, 2003 and July 31, 2003. On October 20, 2003, our Board of Directors suspended the payment of dividends with respect to our common stock because of the decline in our profitability and because earnings were not sufficient to support payment of further dividends in compliance with certain of the financial covenants contained in the indentures governing our then-outstanding senior indebtedness.

We do not expect to declare or pay any dividends on our common stock in the foreseeable future, but instead intend to retain all earnings, if any, to invest in our operations and service our debt obligations. 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, the application of the financial covenants contained in the indentures governing our currently outstanding debt obligations and other relevant factors.

Securities Authorized for Issuance under Equity Compensation Plans

The information set forth under the caption Executive Compensation in our definitive Proxy Statement to be used in connection with our 2005 Annual Meeting of Stockholders to be held on May 17, 2005, which will be filed within 120 days of the end of our fiscal year ended December 31, 2004 (the 2005 Proxy Statement), is incorporated herein by reference.

Item 6. SELECTED FINANCIAL DATA.

The selected financial data set forth below for the years ended December 31, 2004, 2003 and 2002 and as of December 31, 2004, 2003 and 2002 have been derived from our consolidated financial statements, which have been audited by KPMG LLP, independent auditors, and are included elsewhere in this filing. The selected financial data set forth below for the years ended December 31, 2001 and 2000 and as of December 31, 2001 and 2000 have been derived from our consolidated financial statements, audited by Arthur Andersen LLP, independent public auditors, which are not included elsewhere in this filing. The selected financial data set forth below should be read in conjunction with the consolidated financial statements and related notes thereto and with Management s Discussion and Analysis of Financial Condition and Results of Operations, which are included elsewhere in this filing.

	For Year Ended December 31,				
(000 s omitted)	**2004**	**2003**	**2002**	**2001**	**2000**
STATEMENT OF OPERATIONS DATA:					
Revenues:					
Net gain on principal transactions	$ 182,535	$ 202,207	$ 342,400	$ 340,795	$ 282,948
Commissions	96,045	94,443	92,044	62,866	45,381
Realized gain from sale of Lava investment	24,900				
Other	15,567	9,339	18,401	20,469	16,480
Total revenues	319,047	305,989	452,845	424,130	344,809
Expenses:					
Employee compensation and benefits	99,310	99,123	131,511	110,832	88,759
Interest	63,789	48,188	48,589	52,049	41,893
Restitution and fines		63,519			
Goodwill impairment	37,600	170,302			
Exchange memberships impairment	18,327	515			
Debt repurchase premium	49,029				
Other	106,461	109,416	106,621	104,538	47,580
Total expenses	374,516	491,063	286,721	267,419	178,232
Income (loss) before minority interest and provision (benefit) for income taxes	$ (55,469)	$ (185,074)	$ 166,124	$ 156,711	$ 166,577
Net income (loss)	$ (43,780)	$ (179,389)	$ 87,226	$ 71,587	$ 81,923

(000 s omitted)	2004	2003	As of December 31, 2002	2001	2000
BALANCE SHEET DATA:					
Total assets	$ 2,055,097	$ 1,963,090	$ 1,912,802	$ 2,000,837	$ 1,004,122
Total long term obligations (1)	498,733	275,891	383,233	429,205	397,828
Stockholders equity	$ 692,986	$ 772,964	$ 989,688	$ 928,358	$ 370,901

(1) Includes obligations under our subordinated debt (excluding those related to contributed exchange memberships).

	2004	2003	For Year Ended December 31, 2002	2001	2000
COMMON SHARE DATA:					
Earnings (loss) per share (diluted)	$ (0.77)	$ (3.08)	$ 1.34	$ 1.13	$ 1.69
Cash dividends declared per share		$ 0.24			

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

You should read the following discussion of our financial condition and results of operations together with the financial statements and the notes to such statements included elsewhere in this filing. This discussion contains forward-looking statements based on our current expectations, assumptions, estimates and projections about us and our industry. These forward-looking statements involve risks and uncertainties including, but not limited to those discussed in Risk Factors set forth in Item 1 of this annual report. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors. We undertake no obligation to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.

Executive Overview

For the year ended December 31, 2004, we reported a loss of $46.0 million, or $0.77 per share, which included a $24.6 million gain on the sale of our investment in Lava Trading, Inc., an exchange membership impairment charge of $18.3 million, a debt repurchase charge of $55.9 million, a goodwill impairment charge of $37.6 million and a preferred stock discount accretion charge of $0.5 million. Excluding the Lava sale and the exchange membership impairment, debt repurchase, goodwill impairment charges and preferred stock discount accretion, our net income available to common stockholders for the full year 2004 was $16.7 million, or $0.28 per diluted share.

The key drivers that contributed to the decreased revenues at our NYSE equity specialist subsidiary for 2004 included declining principal share volume and dollar value traded, lower market volatility and an increasing rate of program trading as a percentage of total trading volume on the NYSE. The decline in market volatility and rise in program trading resulted in fewer market imbalances, which lowered our rate of capital participation. Although this caused a 19.3% decrease in principal trading revenues at our LaBranche & Co. LLC subsidiary in 2004 versus 2003, our LSP and LSPS subsidiaries principal trading revenues grew 95.3% through expansion into new marketplaces and diversification of its specialist and market-making product offerings.

Throughout 2004, we continued to improve operational efficiencies by reducing headcount and related operating expenses and further enhancing our compliance and trading systems. We believe these changes have streamlined our organization without sacrificing our ability to respond to developments in the marketplace. If implemented, we anticipate that the NYSE s proposed changes to its automated trade execution system and the SEC s proposed market structure changes will provide more challenges. We are confident that our organization will successfully adapt to meet its future needs.

During 2004, we successfully completed a refinancing of certain of our indebtedness by repurchasing a substantial portion of our then-outstanding senior and senior subordinated notes and issuing $460.0 million aggregate principal amount of 9.5% senior notes due 2009 (the Original 2009 Notes) and 11.0% senior notes due 2012 (the Original 2012 Notes and collectively with the Original 2009 Notes, the Original Senior Notes). Although this refinancing increased the aggregate principal amount of our outstanding indebtedness, the interest rates on the Original Senior Notes and the third-quarter repurchase of all remaining shares of our outstanding Series B preferred stock with a portion of the proceeds of the Original Senior Notes issuance have enabled us to extend the maturities of our debt without increasing our overall combined after-tax annual interest and dividends expense.

On March 29, 2004, we entered into an agreement with the NYSE and the SEC to settle their investigations concerning our NYSE specialist trading activity. This settlement resolved the NYSE and the SEC investigations of our NYSE specialist trading activity for all periods through 2003. As part of the settlement with the NYSE and the SEC, we have agreed to comply with the following undertakings:

implementation of systems and procedures to ensure appropriate follow-up and review with regard to information provided to LaBranche & Co. LLC on a daily basis by the NYSE with regard to specialists override of the Principal Inhibitor function, which identifies specialist principal trades that may have been effected while an executable agency order was reflected in the order book on the same side of the market;

creation of a committee, including LaBranche & Co. LLC s chief compliance officer and at least two members of senior management, specifically charged with meeting periodically (no less frequently than monthly) to evaluate specialist rule compliance;

development and/or enhancement of systems and procedures to track and maintain records identifying the individuals acting as specialist and clerk for each security at all times throughout each trading day;

annual certification, through LaBranche & Co. LLC s chief executive officer, that a review has been conducted by the chief compliance officer of trading in LaBranche & Co. LLC s principal account for the purpose of detecting interpositioning, trading ahead and unexecuted limit order violations;

bi-annual assessment of, and reports on, the adequacy of the resources devoted to LaBranche & Co. LLC s compliance function, and devotion of adequate funds and staffing to the compliance department; and

retention of an independent consultant to review and evaluate LaBranche & Co. LLC s compliance systems, policies and procedures reasonably designed to ensure that LaBranche & Co. LLC is in compliance with federal securities laws and NYSE rules with regard to specialist trading.

We are complying with these undertakings and do not expect these changes or enhancements to adversely affect our principal trading revenues. Instead, our fulfillment of these undertakings should enhance our risk management activities related to our specialist trading activity.

New Accounting Developments

In December 2003, the FASB issued FIN 46(R), Consolidation of Variable Interest Entities, An Interpretation of ARB No. 51. FIN 46(R) 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, or both, of the entity. FIN 46(R) was effective no later than the end of the first reporting period that ended after March 15, 2004. As of December 31, 2004, we have determined that none of our investments are considered a VIE under the guidance provided in FIN 46(R), and therefore, the implementation of FIN 46(R) has had no impact on our consolidated financial statements.

In December 2004, the FASB issued a revision to SFAS No. 123, Accounting for Stock-Based Compensation, SFAS No. 123(R), Share Based Payment. SFAS No. 123(R) will require compensation costs related to share-based payment transactions to be recognized in the financial statements over the period that an employee provides service in exchange for the award. SFAS No. 123(R) replaces SFAS No. 123 and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees. SFAS No. 123(R) will be effective for our third quarter of fiscal 2005. We are currently evaluating the effect of adoption of SFAS No. 123(R), but we do not expect it to have a material effect on our financial condition, results of operations or cash flows.

Critical Accounting Estimates

Goodwill and Other Intangible Assets

We determine the fair value of each of our reporting units and the fair value of each reporting unit s goodwill under the provisions of Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets. In determining fair value, we use standard analytical approaches to business enterprise valuation (BEV), such as the market comparable approach and the income approach. The market comparable approach is based on comparisons of the subject company to similar companies engaged in an actual merger or acquisition or to public companies whose stocks are actively traded. As part of this process, multiples of value relative to financial variables, such as earnings or stockholders equity, are developed and applied to the appropriate financial variables of the subject company to indicate its value. The income approach involves estimating the present value of the subject company s future cash flows by using projections of the cash flows that the business is expected to generate, and discounting these cash flows at a given rate of return. Each of these BEV methodologies requires the use of management estimates and assumptions. For example, under the market comparable approach, we assigned a certain control premium to the public market price of our common stock as of the valuation date of our 2004 third quarter impairment test, as well as our 2004 year-end impairment test, in estimating the fair value of our specialist reporting unit. Similarly, under the income approach, we assumed certain growth rates for our revenues, expenses, earnings before interest, income taxes, depreciation and amortization, returns on working capital, returns on other assets and capital expenditures, among others. We also assumed certain discount rates and certain terminal growth rates in our calculations. For our third quarter and year-end 2004 goodwill impairment tests, we engaged an independent business valuation firm to assist us in our BEV analyses. Given the subjectivity involved in selecting which BEV approach to use and in determining the input variables for use in our analyses, it is possible that a different valuation model and the selection of different input variables could produce a materially different estimate of fair value of our goodwill.

We review the reasonableness of the carrying value of our goodwill on an annual calendar basis (i.e., December 31) unless an event or change in circumstances would require an interim reassessment of impairment. During the nine months ended September 30, 2004, certain changes in circumstances occurred, which management believed necessitated goodwill impairment testing. The two primary factors we analyzed, which indicated a need for us to reassess the reasonableness of the carrying value of our goodwill at September 30, 2004, were the prolonged downward trend in our principal trading revenues at our Specialist reporting unit and the continued decline in the public trading price of our common stock through September 30, 2004. In our third quarter 2004 SFAS No. 142 test, we compared the fair value of our Specialist reporting unit and the fair value of our Specialist reporting unit s goodwill based on the methods described above to their respective carrying values in two separate steps under SFAS No. 142 guidelines to arrive at the $37.6 million impairment charge we recognized during the third quarter. Notwithstanding our interim valuation of goodwill as of September 30, 2004, SFAS No. 142 requires us to test goodwill on an annual calendar basis. Accordingly, we updated our valuation models through and including our annual testing date, or December 31, 2004, and noted no further impairment of our goodwill. We cannot provide assurance that future goodwill impairment testing will not result in impairment charges in subsequent periods.

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

We review the reasonableness of the carrying amount of our trade name on an annual basis in conjunction with our goodwill impairment assessment. As of September 30, 2004, the fair value of our trade name determined in accordance with the methodology described above exceeded its carrying amount. During our 2004 fiscal fourth quarter, no events or changes in circumstances occurred that required us to reassess the fair value of our trade name. Therefore, no impairment of our trade name exists at December 31, 2004. We cannot provide assurance that future trade name impairment testing will not result in impairment charges in subsequent periods.

Non-Marketable Securities

The use of fair value to measure certain non-marketable investments is a critical accounting estimate. Investments in non-marketable securities consist of investments in equity securities of private companies, limited liability company interests and limited partnership interests, which do not have readily available price quotations. Certain investments in non-marketable securities are initially carried at cost, as an approximation of fair value. Adjustments to carrying value are made if there are third-party transactions evidencing a change in value. For certain other investments in non-marketable securities, we adjust their carrying value by applying the equity method of accounting, and for our investment in a limited partnership interest, we adjust its carrying value by recognizing our share of the partnership s quarterly results of operations. In addition, if and when available, management considers other relevant factors relating to non-marketable investments in estimating their fair value, such as the financial performance of the entity, its cash flow forecasts, trends within that entity s industry and any specific rights associated with our investment such as conversion features among others.

Given management s judgment involved in valuing certain of our non-marketable securities, it is possible, as of a given point in time, that a third-party could reach a different conclusion of fair value utilizing the same variables as we have in our analysis.

Other-Than-Temporary Impairment of Exchange Memberships

The determination of the fair value of our exchange memberships is a critical accounting estimate. Exchange memberships owned by us are originally carried at cost, pursuant to the American Institute of Certified Public Accountants (AICPA) *Audit and Accounting Guide Brokers and Dealers in Securities*. Adjustments to carrying value are made if we deem that an other-than-temporary decline in value, as defined in Emerging Issues Task Force (EITF) Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments,* and in Section M of Topic 5 of the SEC staff accounting bulletin series (SAB No. 59), has occurred. In determining whether the value of our owned exchange memberships is impaired (*i.e*., fair market value is below cost) and whether such impairment is temporary or other-than-temporary, we consider many factors, including, but not limited to, information regarding recent sale and lease prices of exchange memberships, historical trends of sale and lease prices of memberships on a particular exchange and their duration, the current condition of the particular exchange s market structure, legal and regulatory developments affecting the particular exchange s market structure and earnings capability, trends in new listings on the particular exchange, general global and national economic factors and our knowledge and judgment of the specialist and execution and clearing industries and the securities market as a whole.

As a result of our analysis of the above-mentioned factors for the three and six month periods ended December 31, 2004, the difference between the fair value of our NYSE exchange memberships and their carrying value at December 31, 2004 is deemed temporary. For the years ended December 31, 2004 and 2003, we recorded other-than-temporary impairment charges of $18.3 million and $0.5 million, respectively, to reduce the carrying value (or cost basis) of our NYSE (fiscal 2004) and AMEX (fiscal 2003) exchange memberships.

We cannot provide assurance that the consistent application of this accounting policy to future reporting periods will not result in further adjustments to the carrying value of our exchange memberships.

Off Balance Sheet Arrangements

LFSI, through the normal course of business, enters into various securities transactions as agent. The execution, settlement and financing of these transactions can result in off-balance sheet risk and concentration of credit risk. LFSI s execution and clearing activities 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 the customer or other broker is unable to fulfill its contractual obligations and LFSI 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.

May 2004 Refinancing of Our Indebtedness

On May 18, 2004, in connection with the refinancing of certain of our indebtedness, we repurchased approximately $93.1 million of our then-outstanding $100.0 million aggregate principal amount 9.5% senior notes due 2004 (the 2004 Notes) and approximately $236.4 million of our then-outstanding $250.0 million aggregate principal amount 12.0% senior subordinated notes due 2007 (the 2007 Notes and, together with the 2004 Notes, the Old Notes), and paid for related consents delivered by the holders of the Old Notes on or prior to April 19, 2004. The aggregate purchase price we paid for the Old Notes was approximately $386.9 million, which included the purchase price, premium and consent payments of approximately $49.0 million and accrued but unpaid interest on the Old Notes up to, but not including, the settlement date. Upon the completion of this refinancing, the indentures governing the remaining outstanding Old Notes were stripped of substantially all restrictive covenants, certain events of default and other related provisions.

In order to fund the repurchase of the Old Notes, we issued the Original Senior Notes. The indenture governing the Original Senior Notes contains provisions similar to the indentures that governed the Old Notes prior to their amendment. For a more complete description of the restrictive covenants in the indenture governing the Original Senior Notes, please see Liquidity and Capital Resources.

In connection with our purchase of the Old Notes and our payment for the related consents that were delivered on or prior to April 19, 2004, we recorded a charge of approximately $55.9 million in the second quarter of 2004 for premium and consent payments, accelerated debt issuance cost amortization and discount accretion and other related fees. In connection with the issuance of the Original Senior Notes, we capitalized certain costs in the aggregate amount of approximately $12.7 million, and are amortizing these costs over the life of these notes.

Repayment of Remaining 2004 Notes

On August 16, 2004, we repaid the $6.9 million aggregate principal amount of 2004 Notes that remained outstanding after our May 2004 refinancing, plus all accrued and unpaid interest thereon, for an aggregate of $7.2 million. No 2004 Notes remain outstanding and the indenture governing the 2004 Notes was terminated.

Completed Exchange Offer

On September 10, 2004, pursuant to a registration rights agreement between the initial purchaser of the Original Senior Notes and us, we offered to exchange (i) our 9.5% Senior Notes due 2009 that have been registered under the Securities Act of 1933, as amended (the 2009 Senior Notes), for an equal principal amount of outstanding Original 2009 Notes and (ii) our 11.0% Senior Notes due 2012 that have been registered under the Securities Act of 1933, as amended (the 2012 Senior Notes, and together with the 2009 Senior Notes, the Senior Notes), for an equal principal amount of outstanding Original 2012 Notes.

The exchange offer expired on October 22, 2004, with the holders of 98.5%, or $197.0 million aggregate principal amount, of Original 2009 Notes having tendered their Original 2009 Notes for exchange, and the holders of 100.0%, or $260.0 million aggregate principal amount, of the Original 2012 Notes having tendered their Original 2012 Notes for exchange. The Senior Notes represent the same indebtedness as the Original Senior Notes that were exchanged and have been issued under the same indenture. All subsequent references in this Report to the term 2009 Senior Notes shall include the $3.0 million principal amount of Original 2009 Notes that were not tendered in the exchange offer and remain outstanding.

Completed Excess Proceeds Offer

To the extent we did not use the net proceeds of the sale of the Original Senior Notes to repurchase Old Notes in connection with the May 2004 debt refinancing, repurchase the then-outstanding shares of our Series B preferred stock before September 15, 2004 and pay related fees and expenses, the Senior Notes indenture required us to offer to use such excess proceeds to repurchase an equal principal amount of Senior Notes at a price of 101.0%, on a pro rata basis.

Based on the aggregate principal amount of Old Notes that we repurchased in May 2004, the repurchase of our Series B preferred stock in July 2004 (see Completed Preferred Stock Exchange Offer and Subsequent Repurchase) and the fees and expenses incurred in connection therewith, the excess proceeds amount was approximately $18.2 million. Accordingly, on

November 1, 2004, we commenced an offer to purchase Senior Notes in the aggregate principal amount of up to approximately $18.2 million. This excess proceeds offer expired on December 1, 2004, with approximately $0.1 million principal amount, including accrued and unpaid interest, of 2009 Senior Notes having been tendered.

Completed Preferred Stock Exchange Offer and Subsequent Repurchase

On January 21, 2004, we completed an exchange offer pursuant to an exemption from registration under Section 3(a)(9) of the Securities Act of 1933, as amended, pursuant to which we exchanged one share of a newly-created Series B preferred stock for each share of our then-issued and outstanding Series A preferred stock. In the exchange offer, all of the approximately 39,186 shares of Series A preferred stock were exchanged by the fourteen holders of record for shares of our Series B preferred stock. Issuance of the newly-created shares of Series B preferred stock was contingent upon the tender for exchange of 100% of the issued and outstanding shares of Series A preferred stock.

On June 14, 2004, we commenced an offer to purchase any and all of the approximately 39,186 then-outstanding shares of our Series B preferred stock. On July 12, 2004, the offer expired with 100% of the then-outstanding shares of Series B preferred stock having been tendered. On July 13, 2004, we purchased all of the tendered shares at a price of $1,000 per share, plus accrued and unpaid dividends up to but not including the date of purchase for approximately $42.6 million and all then-outstanding shares of our Series B preferred stock were retired. As a result of the purchase, we recorded an expense in the third quarter of 2004 of approximately $0.5 million due to the acceleration of the discount accretion on the shares that were purchased.

Of the approximately 39,186 then-outstanding shares of our Series B preferred stock, approximately 9,760 shares had been held in escrow in order to secure the indemnification obligations of the former stockholders of ROBB PECK McCOOEY Financial Services, Inc. (RPM) in connection with our acquisition of RPM in March 2001. In connection with the completion of the offer to purchase all then-outstanding shares of our Series B preferred stock, this escrow arrangement was terminated in order to facilitate our objective of repurchasing and retiring all outstanding shares of our Series B preferred stock without forfeiting any material right to indemnification under the merger agreement governing our acquisition of RPM.

Results of Operations

Specialist Segment Operating Results

(000 s omitted)	For the Years Ended December 31, 2004	2003	2002	2004 vs. 2003 Percentage Change	2003 vs. 2002 Percentage Change
Revenues:					
Net gain on principal transactions	$ 182,535	$ 202,206	$ 342,400	(9.7)%	(40.9)%
Commissions	48,781	47,450	50,653	2.8	(6.3)
Other	13,707	6,927	8,116	97.9	(14.7)
Total segment revenues	245,023	256,583	401,169	(4.5)	(36.0)
Operating expenses	148,799	144,731	176,704	2.8	(18.1)
Goodwill impairment	37,600	166,250		(77.4)	
Exchange memberships impairment	16,300				
Restitution and fines		63,519		(100.0)	
Pre-tax income (loss)	$ 42,324	$ (117,917)	$ 224,465	135.9%	(152.5)%

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 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 net gains and losses resulting from our market-making activities in ETFs, options and futures, the net gains and losses resulting from trading of foreign currencies, futures and equities underlying the rights, ETFs and options for which we act as specialist, and accrued dividends receivable or payable on our equity positions. These revenues are primarily affected by changes in share volume traded and fluctuations in price of stocks, rights, options, ETFs and futures in which we are the specialist or in which we make a market.

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 or when we act as a market-maker.

Other revenue at our Specialist segment consists primarily of interest income, proprietary trading gains or losses and gains or losses from an investment in a hedge fund.

Key Metrics of our LaBranche & Co. LLC Specialist Business When assessing the performance and financial results of a specific period, management examines certain metrics to ascertain their impact on our LaBranche & Co. LLC specialist s financial results. Some of the key metrics that we review, and their values for 2004, 2003 and 2002, are as follows:

	2004	2003	2002	2004 vs. 2003 Percentage Change	2003 vs. 2002 Percentage Change
NYSE average daily share volume (in millions)	1,456.7	1,398.4	1,441.0	4.2%	(3.0)%
LAB share volume on the NYSE (in billions)	96.1	94.5	102.1	1.7%	(7.4)%
LAB dollar value on the NYSE (in billions)	$ 2,819.1	$ 2,477.4	$ 2,686.5	13.8%	(7.8)%
Share volume of principal shares traded (in billions)	22.3	27.6	35.7	(19.2)%	(22.7)%
Dollar value of principal shares traded (in billions)	$ 682.7	$ 725.1	$ 983.4	(5.8)%	(26.3)%
Average closing price of the CBOE Volatility Index	15.5	22.0	27.3	(29.5)%	