TD AMERITRADE HOLDING CORP
Form 10-Q/A
February 10, 2006

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

FORM 10-Q/A
AMENDMENT NO. 1

(Mark One)

þ **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarterly Period Ended December 31, 2005**

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: 0-49992

TD AMERITRADE HOLDING CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	**82-0543156**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

4211 South 102nd Street, Omaha, Nebraska, 68127
(Address of principal executive offices) (Zip Code)
(402) 331-7856
(Registrant s telephone number, including area code)
AMERITRADE HOLDING CORPORATION
(Registrant s former name)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months, and (2) has been subject to such filing requirements for the past ninety days. Yes þ No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No þ
As of January 27, 2006, there were 603,585,433 outstanding shares of the registrant s common stock.

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Explanatory Note

This Amendment No. 1 to the Quarterly Report on Form 10-Q/A for the period ended December 31, 2005 amends the Quarterly Report on Form 10-Q filed on February 8, 2006 solely for the purpose of amending the disclosure in Item 2 of Part I of such report relating to projections for the second quarter of fiscal 2006 for average commissions and clearing fees, net interest revenue and other revenues. Except for the changes to Item 2 of Part I, no other information included in the original report on Form 10-Q is amended by this Form 10-Q/A. This Amendment No. 1 to the Quarterly Report continues to speak as of the date of the Quarterly Report, and Registrant has not updated the disclosures contained in this Amendment No. 1 to the Quarterly Report to reflect any events that occurred at a date subsequent to the filing of the Quarterly Report. The filing of this Amendment No. 1 to the Quarterly Report is not a representation that any statements contained in items of the Quarterly Report other than that information being amended hereby are true or complete as of any date subsequent to the date of the Quarterly Report.

TD AMERITRADE HOLDING CORPORATION

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Part I FINANCIAL INFORMATION

Item 1. Financial Statements

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors
TD AMERITRADE Holding Corporation

We have reviewed the condensed consolidated balance sheet of TD AMERITRADE Holding Corporation (the Company, formerly known as Ameritrade Holding Corporation) as of December 31, 2005, and the related condensed consolidated statements of operations and cash flows for the three-month period then ended. These financial statements are the responsibility of the Company s management. We did not make a similar review of these financial statements for the corresponding period of the prior year (2004).

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

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

/S/ ERNST & YOUNG LLP

Kansas City, Missouri
February 3, 2006

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TD AMERITRADE HOLDING CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands, except share amounts)

	December 31, 2005	September 30, 2005
ASSETS		
Cash and cash equivalents	$ 188,119	$ 171,064
Short-term investments	302,921	229,819
Cash and investments segregated in compliance with federal regulations	7,041,290	7,595,359
Receivable from brokers, dealers and clearing organizations	3,107,058	3,420,226
Receivable from clients and correspondents net of allowance for doubtful accounts	3,891,247	3,784,688
Property and equipment net of accumulated depreciation and amortization	32,671	33,259
Goodwill	769,212	769,215
Acquired intangible assets net of accumulated amortization	256,250	259,759
Investments in equity securities	81,534	68,575
Other assets	105,777	85,146
Total assets	$ 15,776,079	$ 16,417,110
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Payable to brokers, dealers and clearing organizations	$ 3,786,473	$ 4,449,686
Payable to clients and correspondents	10,039,673	10,095,837
Accounts payable and accrued liabilities	152,352	171,290
Securities sold, not yet purchased		26,002
Prepaid variable forward derivative instrument	32,126	20,423
Prepaid variable forward contract obligation	39,951	39,518
Capitalized lease and other long-term obligations	7,999	6,218
Deferred income taxes	90,157	89,269
Total liabilities	14,148,731	14,898,243
Commitments and contingencies		
Stockholders equity:		
Preferred stock, $0.01 par value; 100,000,000 shares authorized, none issued		
Common stock, $0.01 par value; 650,000,000 shares authorized; 435,081,860 shares issued	4,351	4,351
Additional paid-in capital	1,187,017	1,184,004

Retained earnings	738,739	652,742
Treasury stock, common, at cost Dec. 31, 2005 28,086,933 shares; Sept. 30, 2005 29,022,890 shares	(353,444)	(364,794)
Deferred compensation	1,007	952
Accumulated other comprehensive income	49,678	41,612
Total stockholders equity	1,627,348	1,518,867
Total liabilities and stockholders equity	$ 15,776,079	$ 16,417,110

See notes to condensed consolidated financial statements.

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TD AMERITRADE HOLDING CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands, except per share amounts)

	Three Months Ended December 31, 2005	Three Months Ended December 31, 2004
Revenues:		
Commissions and clearing fees	$ 129,799	$ 153,546
Interest revenue	177,354	113,100
Brokerage interest expense	(49,754)	(24,679)
Net interest revenue	127,600	88,421
Other	19,862	20,014
Net revenues	277,261	261,981
Expenses:		
Employee compensation and benefits	44,892	43,989
Clearing and execution costs	5,966	6,528
Communications	8,754	9,446
Occupancy and equipment costs	15,047	11,005
Depreciation and amortization	3,483	2,603
Amortization of acquired intangible assets	3,509	3,670
Professional services	9,593	9,567
Interest on borrowings	648	557
Gain on disposal of property	(206)	(98)
Other	7,009	3,946
Advertising	26,563	23,110
Unrealized fair value adjustments of derivative instruments	11,703	13,006
Total expenses	136,961	127,329
Pre-tax income	140,300	134,652
Provision for income taxes	54,303	50,243
Net income	$ 85,997	$ 84,409
Earnings per share basic	$ 0.21	$ 0.21
Earnings per share diluted	$ 0.21	$ 0.20

Weighted average shares outstanding	basic	406,560	405,664
Weighted average shares outstanding	diluted	417,063	414,701

See notes to condensed consolidated financial statements.

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

	Three Months Ended	
	December 31, 2005	**December 31, 2004**
Cash flows from operating activities:		
Net income	$ 85,997	$ 84,409
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,483	2,603
Amortization of acquired intangible assets	3,509	3,670
Deferred income taxes	(4,093)	(4,350)
Gain on disposal of property	(206)	(98)
Unrealized fair value adjustments of derivative instruments	11,703	13,006
Other non-cash expenses, net	2,111	1,957
Changes in operating assets and liabilities:		
Cash and investments segregated in compliance with federal regulations	554,069	(345,346)
Brokerage receivables	206,620	(1,620,349)
Other assets	(20,631)	210,365
Brokerage payables	(719,377)	1,716,370
Accounts payable and accrued liabilities	(18,637)	16,882
Securities sold, not yet purchased	(26,002)	
Net cash flows provided by operating activities	78,546	79,119
Cash flows from investing activities:		
Purchase of property and equipment	(196)	(2,452)
Proceeds from sale of property and equipment	8	
Cash paid in business combinations, net		(17,500)
Purchase of short-term investments	(370,325)	
Proceeds from sale of short-term investments	297,223	17,950
Net cash flows used in investing activities	(73,290)	(2,002)
Cash flows from financing activities:		
Proceeds from notes payable		280,000
Principal payments on notes payable		(280,000)
Principal payments on capital leases and other long-term obligations	(916)	
Proceeds from exercise of stock options	6,924	2,369
Purchase of treasury stock		(46,387)
Excess tax benefits on stock option exercises	5,715	

Net cash flows provided by (used in) financing activities	11,723	(44,018)
Effect of exchange rate changes on cash and cash equivalents	76	378
Net increase in cash and cash equivalents	17,055	33,477
Cash and cash equivalents at beginning of period	171,064	137,392
Cash and cash equivalents at end of period	$ 188,119	$ 170,869
Supplemental cash flow information:		
Interest paid	$ 48,179	$ 20,308
Income taxes paid	$ 55,692	$ 26,659
Tax benefit on exercise of stock options	$ 5,718	$ 2,052
Noncash investing and financing activities:		
Issuance of capital lease and other long-term obligations	$ 2,697	$

See notes to condensed consolidated financial statements.

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TD AMERITRADE HOLDING CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
For the Three-Month Periods Ended December 31, 2005 and December 31, 2004
(Unaudited)
(Columnar amounts in thousands, except per share amounts)

1. BASIS OF PRESENTATION

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

These financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and, in the opinion of management, reflect all adjustments, which are all of a normal recurring nature, necessary to present fairly the financial position, results of operations and cash flows for the periods presented in conformity with U.S. generally accepted accounting principles. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s annual report filed on Form 10-K for the fiscal year ended September 30, 2005.

2. BUSINESS COMBINATION

On January 24, 2006, the Company completed the acquisition of TD Waterhouse Group, Inc. (TD Waterhouse), a Delaware corporation, pursuant to an Agreement of Sale and Purchase, dated June 22, 2005, as amended (the Purchase Agreement), with the Toronto-Dominion Bank (TD). The Company purchased from TD (the Share Purchase) all of the capital stock of TD Waterhouse in exchange for 196,300,000 shares of Company common stock and $20,000 in cash. The shares of common stock issued to TD in the Share Purchase represented approximately 32.5 percent of the outstanding shares of the Company after giving effect to the transaction. Upon the completion of the transaction, the Company changed its name to TD AMERITRADE Holding Corporation and the authorized shares of common stock of the Company were increased from 650 million to one billion. In addition, on January 24, 2006, the Company completed the sale of Ameritrade Canada, Inc. to TD for $60 million in cash. The Company has agreed not to compete or own any portion of a business that competes with TD in Canada (including in the retail securities brokerage business) after the consummation of the Share Purchase. The purchase price for the acquisition of TD Waterhouse and the sale price for the sale of Ameritrade Canada are subject to cash adjustments based on the closing date balance sheets of the Company, TD Waterhouse and Ameritrade Canada.

Pursuant to the Purchase Agreement, prior to the consummation of the Share Purchase, TD Waterhouse conducted a reorganization in which it transferred its Canadian retail securities brokerage business and TD Waterhouse Bank, N.A. to TD such that, at the time of consummation of the Share Purchase, TD Waterhouse retained only its United States retail securities brokerage business. TD Waterhouse also distributed to TD excess capital of TD Waterhouse above certain thresholds prior to the consummation of the Share Purchase. As contemplated in the Purchase Agreement, on January 24, 2006, the Company commenced payment of a special cash dividend of $6.00 per share in respect of the shares of Company common stock outstanding prior to the consummation of the Share Purchase. The total amount of the dividend was approximately $2.4 billion.

In connection with the Purchase Agreement, TD was given rights to have its shares of common stock of the Company registered for resale and TD licensed the Company to use the TD name in connection with the operation of the Company s business. The parties also entered into agreements regarding bank sweep accounts and mutual funds.

In connection with the Purchase Agreement, the Company, TD and J. Joe Ricketts, the Company s Chairman and Founder, and certain of his affiliates also entered into a Stockholders Agreement (the Stockholders Agreement). The Stockholders Agreement sets forth certain governance arrangements and contains various provisions relating to stock ownership, voting, election of directors and other matters. The Company s certificate of incorporation and bylaws were amended and restated as of January 24, 2006 to give effect to and facilitate the provisions contained in the Stockholders Agreement.

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3. GOODWILL AND ACQUIRED INTANGIBLE ASSETS

The Company has recorded goodwill for purchase business combinations to the extent the purchase price of each acquisition exceeded the fair value of the net identifiable assets of the acquired company. The following table summarizes changes in the carrying amount of goodwill for the three months ended December 31, 2005:

	Total
Balance as of September 30, 2005	$ 769,215
Tax benefit of option exercises (1)	(3)
Balance as of December 31, 2005	$ 769,212

(1) Represents the tax benefit of exercises of replacement stock options that were issued in connection with the Datek Online Holdings Corp. (Datek) merger. The tax benefit of an option exercise is recorded as a reduction of goodwill to the extent the Company recorded fair value of the replacement option in the purchase accounting. To the extent any gain realized on an option exercise exceeds the fair value of the replacement option recorded in the purchase accounting, the tax benefit on the excess is

recorded as
additional
paid-in capital.

The Company s acquired intangible assets consist primarily of client relationship intangible assets and had a carrying value of $256.2 million, net of $41.8 million of accumulated amortization as of December 31, 2005. The Company estimates amortization expense on acquired intangible assets outstanding as of December 31, 2005 will be $10.4 million for the remainder of fiscal 2006 and approximately $13.8 million for each of the five succeeding fiscal years. These amounts do not include amortization of any intangible assets to be recorded in connection with the acquisition of TD Waterhouse.

4. INVESTMENTS IN EQUITY SECURITIES

The Company s investments in equity securities consist primarily of ownership of approximately 7.9 million common shares of Knight Capital Group, Inc. (Knight), representing approximately eight percent of Knight s outstanding common shares as of December 31, 2005. The Company accounted for its investment in Knight as a marketable equity security available-for-sale. As of December 31, 2005 and September 30, 2005, the Company s investment in Knight was valued at $78.2 million and $65.7 million, respectively. The Company s cost basis was $0.7 million; therefore the gross unrealized gain was $77.5 million and $65.0 million at December 31, 2005 and September 30, 2005, respectively, which is reflected in other comprehensive income, net of taxes, on the Condensed Consolidated Balance Sheets. The Company liquidated its position in Knight and the prepaid variable forward contracts described below in January 2006, resulting in a one-time pre-tax net gain of approximately $79 million that will be recorded in the fiscal quarter ending March 31, 2006.

During fiscal 2003, the Company executed a series of prepaid variable forward contracts on the Knight shares. Before the recent liquidation, these forward contracts were scheduled to mature on various dates in fiscal years 2006 and 2007. The forward contracts each contained a zero-cost embedded collar on the value of the Knight shares, with a weighted average floor price of $5.13 per share and a weighted average cap price of $6.17 per share. As of December 31, 2005 and September 30, 2005, the total fair value of the embedded collars was approximately $32.1 million and $20.4 million, respectively, and was included under the caption Prepaid variable forward derivative instrument on the Condensed Consolidated Balance Sheets. Changes in the fair value of the embedded collars are included under the caption Unrealized fair value adjustments of derivative instruments in the Condensed Consolidated Statements of Operations.

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The following table summarizes the Company s investments in equity securities, liabilities associated with the prepaid variable forward contracts, and related deferred income tax effects:

	December 31, 2005	September 30, 2005	Difference
Assets			
Investment in Knight	$ 78,204	$ 65,710	$ 12,494
Investment in International Securities Exchange, Inc.	3,109	2,644	465
Total marketable equity securities	81,313	68,354	12,959
Other investments	221	221	
Total investments in equity securities	$ 81,534	$ 68,575	$ 12,959
Liabilities			
Prepaid variable forward derivative instrument	$ (32,126)	$ (20,423)	$ (11,703)
Prepaid variable forward contract obligation	$ (39,951)	$ (39,518)	$ (433)
Deferred income taxes on unrealized (gains)/losses:			
Marketable equity securities	$ (30,852)	$ (25,863)	$ (4,989)
Derivative instrument	12,369	7,863	4,506
Deferred income taxes on unrealized (gains)/losses, net	$ (18,483)	$ (18,000)	$ (483)

5. ACQUISITION EXIT LIABILITIES

The following table summarizes activity in the Company s acquisition exit liabilities for the three-month period ended December 31, 2005, which are included in accounts payable and accrued liabilities in the Condensed Consolidated Balance Sheets:

	Three Months Ended December 31, 2005			
	Balance at Sept. 30, 2005	Restructuring Charges	Paid and Charged Against Liability	Balance at Dec. 31, 2005
Employee compensation and benefits	$ 121	$	$ 2	$ 119
Occupancy and equipment costs	3,217		174	3,043
Total acquisition exit liabilities	$ 3,338	$	$ 176	$ 3,162

Acquisition employee compensation liabilities are expected to be paid over contractual periods ending in fiscal 2009. Remaining acquisition occupancy and equipment exit liabilities are expected to be utilized over the respective lease periods through fiscal 2011.

6. CREDIT FACILITIES

On December 13, 2004, the Company entered into an amendment to its revolving credit agreement. The revolving credit agreement, as amended, permitted borrowings of up to $105 million through December 12, 2005, and was secured primarily by the Company s stock in its subsidiaries and personal property. On December 9, 2005, the lenders under the Company s revolving credit agreement agreed to extend the length of the agreement, on substantially the same terms, to the earlier of (a) March 12, 2006 and (b) the initial borrowing under a new syndicated loan facility to be entered into in connection with the acquisition of TD Waterhouse and payment of the special dividend. The interest rate on borrowings was equal to one month LIBOR (determined monthly) plus a spread (determined quarterly) of 1.75 percent or 2.00 percent based on a specified financial ratio. At December 31, 2005, the interest rate on the revolving credit agreement would have been 6.06 percent. The Company also paid a commitment fee of 0.25 percent of the unused credit facility through the maturity date. The Company had no outstanding indebtedness under the revolving credit agreement at December 31, 2005 or September 30, 2005. The revolving credit agreement contained certain covenants and restrictions, including maintenance of a minimum level of net worth, requiring prior written consent of the revolving lenders for certain business combinations and investments, and prohibiting the payment of cash dividends to stockholders. The Company was in compliance with or obtained waivers for all covenants under the revolving credit agreements.

The revolving credit agreement, as extended, terminated upon the initial borrowing under the new syndicated loan facility on January 23, 2006, as described below.

On January 23, 2006, the Company entered into a credit agreement for $2.2 billion in senior credit facilities with a syndicate of lenders. The senior credit facilities include: (a) a senior secured term loan facility in the aggregate principal amount of $250 million (the Term A Facility), (b) a senior secured term loan facility in the aggregate principal amount of $1.65 billion (the Term B Facility) and (c) a senior secured revolving credit facility in the aggregate principal amount of $300 million (the Revolving Facility) (together, the Financings). The maturity date of the Term A Facility is December 31, 2011. The maturity date of the Term B Facility is December 31, 2012. The maturity date of the Revolving Facility is December 31, 2010. The Financings are subject to certain mandatory prepayments, which include prepayments based on amounts of excess cash flow and from the net cash proceeds of asset sales and debt issuances, subject to certain exceptions. Pursuant to the Financings, the Company may prepay borrowings without penalty.

The Company used $1.6 billion of the proceeds from the Term A Facility and Term B Facility to fund a portion of the $6 per share special cash dividend paid in connection with the acquisition of TD Waterhouse and $300 million for working capital purposes. No initial borrowings were made on the Revolving Facility, which will be used for general corporate purposes.

The applicable interest rate under the Revolving Facility and the Term A Facility is calculated as a per annum rate equal to, at the Company s option, (a) LIBOR plus an interest rate margin (LIBOR loans) or (b) (i) the greater of (x) the prime rate or (y) the federal funds effective rate plus 0.50 percent plus (ii) an interest rate margin (Base Rate loans). With respect to the Revolving Facility and the Term A Facility the interest rate margin for LIBOR loans is 1.50 percent if the consolidated leverage ratio (as defined in the Financings) of the Company is 1.75 to 1.00 or higher, 1.25 percent if the consolidated leverage ratio of the Company is less than 1.75 to 1.00 but greater than or equal to 1.00 to 1.00, and 1.00 percent if the consolidated leverage ratio of the Company is less than 1.00 to 1.00. The interest rate margin for Base Rate loans under the Revolving Facility and the Term A Facility is 1.00 percent less than the interest rate margin for LIBOR loans. The applicable interest rate under the Term B Facility is calculated as a per annum rate equal to (a) LIBOR plus 1.50 percent or (b) (i) the greater of (x) the prime rate or (y) the federal funds effective rate plus 0.50 percent plus (ii) 0.50 percent. On January 26, 2006, the applicable interest rate on both the Term A Facility and the Term B Facility was 6.04 percent, based on LIBOR. The Financings also provide that the Company is obligated to pay from time to time letter of credit fees equal to the applicable margin in respect of LIBOR advances on each outstanding letter of credit under the Revolving Credit Facility. In addition, the Financings provide that the Company pays fees to the issuing bank in respect of the Letters of Credit in an amount agreed to by the Company and the issuing bank. A commitment fee at the rate of 0.375 percent per annum will accrue on any unused amount of the Revolving Facility.

The obligations under the Financings are guaranteed by the Company s material subsidiaries, other than broker-dealer subsidiaries, with certain exceptions, and are secured by a lien on substantially all of the assets of each guarantor, including a pledge of the ownership interests in each first-tier broker-dealer subsidiary held by a guarantor and 65 percent of the ownership interests in each first-tier foreign subsidiary held by a guarantor, with certain exceptions. On January 24, 2006, concurrently with the closing of the TD Waterhouse Transaction, TD Waterhouse was added as an additional guarantor to the Financings and TD Waterhouse granted a lien on substantially all of its assets (including its ownership interest in each of its first-tier broker dealer subsidiaries) as additional security for the Financings.

The Financings contain certain covenants that limit or restrict the incurrence of liens, investments (including acquisitions), sales of assets, indebtedness and mergers and consolidations, subject to certain exceptions. The Financings also restrict the payment of dividends on the Company s outstanding capital stock and repurchases or redemptions of the Company s outstanding capital stock, subject to certain exceptions. The Company is also required to maintain compliance with a maximum consolidated leverage ratio covenant and a minimum consolidated interest coverage ratio covenant, and the Company s broker-dealer subsidiaries are required to maintain compliance with a minimum regulatory net capital covenant.

The Company, through its wholly owned broker-dealer subsidiary Ameritrade, Inc., had access to secured uncommitted credit facilities with financial institutions of up to $180 million as of December 31, 2005 and

September 30, 2005. Ameritrade, Inc. also had access to an unsecured uncommitted credit facility of up to $310 million as of December 31, 2005 and September 30, 2005. The financial institutions may make loans under line of credit arrangements or, in some cases, issue letters of credit under these facilities. The secured credit facilities require the Company to pledge qualified client securities to secure outstanding obligations under these facilities. Borrowings under the secured and unsecured credit facilities bear interest at a variable rate based on the federal funds rate. There were no borrowings outstanding or letters of credit issued under the secured or unsecured credit facilities as of December 31, 2005 or September 30, 2005. As of December 31, 2005 and September 30, 2005, approximately $490 million was available to Ameritrade, Inc. for either loans or, in some cases, letters of credit.

7. NET CAPITAL

The Company s broker-dealer subsidiaries are subject to the SEC Uniform Net Capital Rule (Rule 15c3-1 under the Securities Exchange Act of 1934 (the Exchange Act)), which requires the maintenance of minimum net capital, as defined. Net capital and the related net capital requirement may fluctuate on a daily basis.

The Company s broker-dealer subsidiaries had aggregate net capital of $345.7 million and $321.7 million as of December 31, 2005 and September 30, 2005, respectively, which exceeded aggregate minimum net capital requirements by $256.0 million and $234.2 million, respectively.

8. STOCK OPTION AND INCENTIVE PLANS

The Company has four stock incentive plans. The Ameritrade Holding Corporation 1996 Long-Term Incentive Plan (the Long-Term Incentive Plan) and the 1996 Directors Incentive Plan (the Directors Plan) were established by the Company. The Ameritrade Holding Corporation 1998 Stock Option Plan (the 1998 Plan) (formerly known as the Datek Online Holdings Corp. 1998 Stock Option Plan) and the Ameritrade Holding Corporation 2001 Stock Incentive Plan (the 2001 Plan) (formerly known as the Datek Online Holdings Corp. 2001 Stock Incentive Plan) were established by Datek Online Holdings Corp. (Datek) and amended and restated by the Company effective September 9, 2002 in connection with the Datek merger.

The Long-Term Incentive Plan authorizes the award of options to purchase common stock, common stock appreciation rights, shares of common stock and performance units. The Long-Term Incentive Plan has reserved 42,104,174 shares of the Company s common stock for issuance to eligible employees. The Directors Plan authorizes the award of options to purchase common stock and shares of common stock. The Directors Plan has reserved 2,531,393 shares of the Company s common stock for issuance to non-employee directors. Options are generally granted by the Company at not less than the fair market value at grant date, vest over a one-to four-year period, and expire 10 years after the grant date.

The 1998 Plan and 2001 Plan authorize the award of options to purchase common stock. The 1998 Plan has reserved 15,502,818 shares of the Company s common stock for issuance to employees or consultants of the Company; non-employee directors of the Company; or employees of a corporation or other business enterprise which has been acquired by the Company, who hold options to purchase the acquired company s stock, if the Company has agreed to assume those options. The 2001 Plan has reserved 18,628,031 shares of the Company s common stock for issuance to directors or non-voting observers to the Board of Directors, officers and employees of the Company.

Effective October 1, 2005, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), *Share-Based Payment* (No. 123R) using a modified version of the prospective transition method. Under the transition method, compensation cost is recognized on or after the required effective date for the portion of outstanding awards for which the requisite service has not yet been rendered, based on the grant-date fair value of those awards calculated under SFAS No. 123 for either recognition or pro forma disclosures. Stock-based employee compensation expense for the three months ended December 31, 2005 and December 31, 2004 was $1.7 million and $0.4 million, respectively. The cumulative effect of initially adopting SFAS No. 123R was not material. As of December 31, 2005, the total compensation cost related to nonvested stock option awards was approximately $9.1 million and is expected to be recognized over a weighted average period of 12 months.

The fair value of stock options granted was estimated using a Black-Scholes valuation model with the following assumptions:

	Three Months Ended December 31,	
	2005	**2004**
Risk-free interest rate	4.4%	3.5%
Expected dividend yield	0%	0%
Expected volatility	58%	62%
Expected option life (years)	5.0	5.0

The risk free interest rate assumptions are based on 5-year U.S. Treasury note yields. The expected volatility is based on historical daily price changes of the Company s stock since April 2001. The expected option life is the average number of years that the Company estimates that options will be outstanding, based primarily on historical employee option exercise behavior.

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The following is a summary of option activity in the Company s stock incentive plans for the three months ended December 31, 2005:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at beginning of period	21,483	$ 6.38		
Granted	10	$22.17		
Exercised	(933)	$ 7.42		
Canceled	(183)	$15.90		
Outstanding at end of period	20,377	$ 6.26		