

NATIONAL HOLDINGS CORP  
Form 10-Q  
August 15, 2011

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

FORM 10-Q

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

For the Quarter Ended June 30, 2011  
Number 001-12629

Commission File

NATIONAL HOLDINGS CORPORATION  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other  
jurisdiction of  
incorporation or  
organization)

36-4128138  
(I.R.S. Employer  
Identification No.)

120 Broadway, 27th Floor, New York, NY 10271  
(Address including zip code of principal executive offices)  
Registrant's telephone number, including area code: (212) 417-8000

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 ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

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

Large Accelerated Filer ☐

Accelerated Filer ☐

Non-Accelerated Filer ☐

Smaller Reporting Company ☒

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ☐ NO ☒

As of August 11, 2011 there were 20,446,704 shares of the registrant's common stock outstanding.



NATIONAL HOLDINGS CORPORATION

FORM 10-Q  
QUARTERLY PERIOD ENDED JUNE 30, 2011

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## FORWARD-LOOKING STATEMENTS

The following information provides cautionary statements under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 (the Reform Act). We identify important factors that could cause our actual results to differ materially from those projected in forward-looking statements we make in this report or in other documents that reference this report. All statements that express or involve discussions as to: expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, identified through the use of words or phrases such as we or our management believes, expects, anticipates or hopes and words or phrases such as will result, are expected to, will continue, is anticipated, estimated, projection and outlook, and words of similar import) are not statements of historical facts and may be forward-looking. These forward-looking statements are based largely on our expectations and are subject to a number of risks and uncertainties including, but not limited to, economic, competitive, regulatory, growth strategies, available financing and other factors discussed elsewhere in this report and in the documents filed by us with the Securities and Exchange Commission ("SEC"). Many of these factors are beyond our control. Actual results could differ materially from the forward-looking statements we make in this report or in other documents that reference this report. In light of these risks and uncertainties, there can be no assurance that the results anticipated in the forward-looking information contained in this report or other documents that reference this report will, in fact, occur.

These forward-looking statements involve estimates, assumptions and uncertainties, and, accordingly, actual results could differ materially from those expressed in the forward-looking statements. These uncertainties include, among others, the following: (i) the inability of our broker-dealer operations to operate profitably in the face of intense competition from larger full service and discount brokers; (ii) a general decrease in merger and acquisition activities and our potential inability to receive success fees as a result of transactions not being completed; (iii) increased competition from business development portals; (iv) technological changes; (v) our potential inability to implement our growth strategy through acquisitions or joint ventures; and (vi) our potential inability to secure additional debt or equity financing.

Any forward-looking statement speaks only as of the date on which such statement is made, and we undertake no obligation to update any forward-looking statement or statements to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time and it is not possible for our management to predict all of such factors, nor can our management assess the impact of each such factor on the business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

PART I.	FINANCIAL INFORMATION
ITEM I.	FINANCIAL STATEMENTS

NATIONAL HOLDINGS CORPORATION AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION  
ASSETS

	June 30, 2011 (Unaudited)	September 30, 2010
Current Assets		
Cash	\$ 7,163,000	\$ 5,390,000
Deposit with clearing organizations	1,157,000	1,159,000
Receivables from broker dealers and clearing organizations	3,536,000	3,518,000
Other receivables, net of allowance for uncollectible accounts of \$310,000 and \$324,000, respectively	991,000	804,000
Advances to registered representatives - Current portion	649,000	1,026,000
Securities owned: marketable – at market value	1,728,000	680,000
Securities owned: nonmarketable – at fair value	53,000	57,000
Total Current Assets	15,277,000	12,634,000
Advances to registered representatives - Long term portion	472,000	415,000
Fixed assets, net	911,000	1,127,000
Secured demand note	-	500,000
Intangible assets, net	1,242,000	1,708,000
Investment in unconsolidated joint venture	501,000	-
Other assets	876,000	996,000
Total Assets	\$ 19,279,000	\$ 17,380,000

LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities		
Accounts payable, accrued expenses and other liabilities	\$ 11,931,000	\$ 11,079,000
Derivative liabilities	-	4,331,000
Payable to broker dealers and clearing organizations	157,000	169,000
Securities sold, but not yet purchased, at market	21,000	21,000
Convertible notes payable, net of debt discount of \$345,000	5,655,000	-
Notes payable	-	500,000
Total Current Liabilities	17,764,000	16,100,000
Accrued expenses and other liabilities - Long term portion	541,000	864,000
Convertible notes payable, net of debt discount of \$642,000	-	5,358,000
Total Liabilities, before subordinated borrowings and other liabilities	18,305,000	22,322,000
Subordinated borrowings	130,000	750,000
Preferred Stock, \$0.01 par value, 134,500 shares authorized; 94,167 shares designated as Series C and D issued and outstanding	-	537,000

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Total Liabilities	18,435,000	23,609,000
National Holdings Corporation Stockholders' Equity (Deficit)		
Series A 9% cumulative convertible preferred stock, \$.01 par value, 50,000 shares authorized; 46,050 shares issued and outstanding (liquidation preference: \$4,605,000) at June 30, 2011 and September 30, 2010	-	-
Series C and D, convertible preferred stock, \$.01 par value, 10,000,000 shares authorized, 94,167 issued and outstanding	6,156,000	-
Common stock, \$.02 par value, 150,000,000 shares authorized; 20,446,704 and 17,276,704 shares issued and outstanding at June 30, 2011 and September 30, 2010, respectively	409,000	346,000
Additional paid-in capital	45,058,000	43,132,000
Subscription receivable	-	(1,334,000 )
Accumulated deficit	(50,797,000 )	(48,415,000 )
Total National Holdings Corporation Stockholders' Equity (Deficit)	826,000	(6,271,000 )
Non Controlling Interest	18,000	42,000
Total Liabilities and Stockholders' Equity (Deficit)	\$ 19,279,000	\$ 17,380,000

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

NATIONAL HOLDINGS CORPORATION AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three-month Period Ended June 30,		Nine-month Period Ended June 30,	
	2011	2010	2011	2010
<b>Revenues</b>				
Commissions	\$ 20,392,000	\$ 19,416,000	\$ 67,608,000	\$ 56,634,000
Net dealer inventory gains	3,650,000	3,336,000	11,241,000	11,199,000
Investment banking	3,124,000	1,427,000	6,395,000	4,940,000
Total commission and fee revenues	27,166,000	24,179,000	85,244,000	72,773,000
Interest and dividends	870,000	746,000	2,718,000	1,856,000
Transfer fees and clearing services	1,834,000	1,912,000	6,823,000	6,672,000
Other	2,170,000	1,643,000	5,882,000	4,401,000
Total Revenues	32,040,000	28,480,000	100,667,000	85,702,000
<b>Operating Expenses</b>				
Commissions, compensation, and fees	28,708,000	26,375,000	89,890,000	77,856,000
Clearing fees	483,000	576,000	1,641,000	982,000
Communications	1,132,000	1,124,000	3,401,000	3,307,000
Occupancy, equipment and other administrative costs	976,000	848,000	3,072,000	3,146,000
Professional fees	410,000	687,000	1,399,000	1,785,000
Interest	280,000	459,000	864,000	1,056,000
Taxes, licenses, registration	399,000	442,000	1,202,000	1,306,000
Total Operating Expenses	32,388,000	30,511,000	101,469,000	89,438,000
Net Income (Loss) from Operations	(348,000 )	(2,031,000 )	(802,000 )	(3,736,000 )
<b>Other Expense</b>				
Increase in fair value of derivative liabilities	-	-	(1,603,000 )	-
Total Other Expense	-	-	(1,603,000 )	-
Net income (loss) before non-controlling interest	(348,000 )	(2,031,000 )	(2,405,000 )	(3,736,000 )
Non-controlling interest	(21,000 )	-	(24,000 )	-
Net income (loss)	(327,000 )	(2,031,000 )	(2,381,000 )	(3,736,000 )
Preferred stock dividends	(103,000 )	(103,000 )	(310,000 )	(391,000 )
Net income (loss) attributable to common stockholders	\$ (430,000 )	\$ (2,134,000 )	\$ (2,691,000 )	\$ (4,127,000 )



**INCOME (LOSS) PER  
COMMON SHARE**

Net income (loss) attributable  
to common stockholders: Basic      \$   (0.02        )        \$   (0.12        )        \$   (0.06        )        \$   (0.24        )

Diluted:

Net income (loss) attributable  
to common stockholders:  
Diluted                                      \$   (0.02        )        \$   (0.12        )        \$   (0.06        )        \$   (0.24        )

Weighted average number of shares outstanding: Basic	20,446,704	17,276,704	19,444,396	17,209,396
Weighted average number of shares outstanding: Diluted	20,446,704	17,276,704	19,444,396	17,209,396

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

NATIONAL HOLDINGS CORPORATION AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

	Nine-month period ended June 30,	
	2011	2010
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net loss	\$(2,381,000 )	\$(3,736,000 )
Adjustments to reconcile net loss to net cash provided by (used in) operating activities		
Depreciation and amortization	944,000	1,005,000
Amortization of forgivable loans to brokers	316,000	1,105,000
Amortization of deferred financing costs	-	22,000
Amortization of note discount	297,000	796,000
Fair value of options	257,000	409,000
Fair value of warrant issuance	-	152,000
Provision bad debt	(14,000 )	(30,000 )
Net realized and unrealized gain on securities	(71,000 )	44,000
Non-controlling interest	(24,000 )	-
Increase in fair value of derivative liabilities	1,603,000	-
Changes in assets and liabilities		
Deposits with clearing organizations	2,000	52,000
Receivables from broker-dealers, clearing organizations and others	(18,000 )	1,784,000
Other receivables	(173,000 )	(156,000 )
Advances to registered representatives	4,000	81,000
Securities owned: marketable, at market value	(977,000 )	(207,000 )
Securities owned: non-marketable, at fair value	4,000	(16,000 )
Other assets	120,000	(63,000 )
Accounts payable, accrued expenses and other liabilities	529,000	(4,429,000 )
Payable to broker dealers and clearing organizations	(12,000 )	74,000
Securities sold, but not yet purchased, at market	-	159,000
Net cash provided by (used in) operating activities	406,000	(2,954,000 )
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Redemption of note receivable	500,000	-
Investment in unconsolidated joint venture	(501,000 )	-
Purchase of fixed assets	(262,000 )	(341,000 )
Net cash used in investing activities	(263,000 )	(341,000 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net proceeds from subordinated borrowings	(620,000 )	1,700,000
Principal repayment of notes payable	(500,000 )	(500,000 )
Proceeds from issuance of common stock	1,585,000	-
Proceeds from issuance of preferred stock	1,334,000	-
Payment of financing costs	(169,000 )	-
Net cash provided by financing activities	1,630,000	1,200,000
<b>NET INCREASE (DECREASE) IN CASH</b>	<b>1,773,000</b>	<b>(2,095,000 )</b>
<b>CASH BALANCE</b>		

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Beginning of the fiscal year	5,390,000	6,493,000
End of the period	\$7,163,000	\$4,398,000
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>		
Cash paid during the period for:		
Interest	\$170,000	\$578,000
Income taxes	\$-	\$-
<b>SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING ACTIVITIES</b>		
Preferred stock dividends	\$310,000	\$391,000
Reclassification of liability contracts to equity	\$6,464,000	\$-
Embedded conversion features upon issuance	\$530,000	\$-

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

NATIONAL HOLDINGS CORPORATION AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2011  
(UNAUDITED)

NOTE 1. BASIS OF PRESENTATION

The accompanying condensed consolidated financial statements of National Holdings Corporation ("National" or the "Company") have been prepared in accordance with generally accepted accounting principles for interim financial statements and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and disclosures required for annual financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The consolidated financial statements as of June 30, 2011 and for the periods ended June 30, 2011 and December 31, 2010 are unaudited. The results of operations for the interim periods are not necessarily indicative of the results of operations for the fiscal year. These consolidated financial statements should be read in conjunction with the consolidated financial statements and related footnotes included thereto in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2010.

NOTE 2. CONSOLIDATION

The consolidated financial statements include the accounts of National and its wholly owned subsidiaries. National operates primarily through National Securities Corporation ("National Securities"), vFinance Investments, Inc. ("vFinance Investments") and EquityStation, Inc. ("EquityStation") (collectively, the "Broker Dealer Subsidiaries"). The Broker Dealer Subsidiaries conduct a national securities brokerage business through its main offices in New York, New York, Boca Raton, Florida, and Seattle, Washington.

Through its Broker Dealer Subsidiaries, the Company offers (1) full service retail brokerage to approximately 45,000 high net worth and institutional clients, (2) provides investment banking, merger, acquisition and advisory services to micro, small and mid-cap high growth companies, and (3) engages in trading securities, including making markets in over 5,000 small and micro-cap listed stocks and provides liquidity in the United States Treasury marketplace. The Broker Dealer Subsidiaries are introducing brokers and clear all transactions through clearing organizations on a fully disclosed basis. They are registered with the Securities and Exchange Commission ("SEC"), are members of the Financial Industry Regulatory Authority, Inc. ("FINRA") (formerly the National Association of Securities Dealers) and Securities Investor Protection Corporation ("SIPC"). National Securities and vFinance Investments are also members of the National Futures Association ("NFA").

In July 1994, National Securities formed a wholly owned subsidiary, National Asset Management, Inc., a Washington corporation ("NAM"). NAM is a federally-registered investment adviser providing asset management advisory services to high net worth clients for a fee based upon a percentage of assets managed. In March 2009, all of the issued and outstanding stock of NAM was transferred from National Securities to National. National formed a new wholly owned subsidiary, National Insurance Corporation, a Washington corporation ("National Insurance") in the third quarter of fiscal year 2006. National Insurance provides fixed insurance products to its clients, including life insurance, disability insurance, long term care insurance and fixed annuities. National Insurance finalized certain requisite state registrations during the third quarter of fiscal year 2007 and commenced business operations that to date have been de minimus. vFinance Lending Services, Inc. ("vFinance Lending"), originally formed as a wholly owned subsidiary of vFinance, Inc. was established in May 2002. It is a mortgage lender focused primarily on the commercial sector, providing bridge loans and commercial mortgages through its nationwide network of lenders. Its operations to date have been de minimus. All significant inter-company accounts and transactions have been eliminated in consolidation.



### NOTE 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Principles of Consolidation

The consolidated financial statements include the accounts of National and its wholly owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation. We account for our investment in a joint venture using the equity method.

#### Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### Reclassifications

Certain items in the 2010 financial statements have been reclassified to conform to the presentation in the 2011 financial statements. Such reclassifications did not have a material impact on the presentation of the overall financial statements.

#### Revenue Recognition

The Company generally acts as an agent in executing customer orders to buy or sell listed and over-the-counter securities in which it may or may not make a market, and charges commissions based on the services the Company provides to its customers. In executing customer orders to buy or sell a security in which the Company makes a market, the Company may sell to, or purchase from, customers at a price that is substantially equal to the current inter-dealer market price plus or minus a mark-up or mark-down. The Company may also act as agent and execute a customer's purchase or sale order with another broker-dealer market-maker at the best inter-dealer market price available and charge a commission. Mark-ups, mark-downs and commissions are generally priced competitively based on the services it provides to its customers. In each instance the commission charges, mark-ups or mark-downs, are in compliance with guidelines established by FINRA.

Customer security transactions and the related commission income and expense are recorded on a trade date basis. Customers who are financing their transaction on margin are charged interest. The Company's margin requirements are in accordance with the terms and conditions mandated by its clearing firms, National Financial Services LLC ("NFS"), Penson Financial Services, Inc. ("Penson"), Legent Clearing LLC ("Legent"), ICBC (formerly known as Fortis Securities, LLC ("ICBC")) and Rosenthal Collins Group, LLC. ("Rosenthal"). The interest is billed on the average daily balance of the margin account.

Investment banking revenues include gains, losses, and fees, net of syndicate expenses, arising from securities offerings in which the Company acts as an underwriter or agent. Investment banking revenues also include fees earned from providing financial advisory services. Investment banking management fees are recorded on the offering date, sales concessions on the settlement date, and underwriting fees at the time the underwriting is completed and the income is reasonably determinable.

Net trading profits result from mark-ups and mark-downs in securities transactions entered into for the account of the Company. Some of these transactions may involve the Company taking a position in securities that may expose the company to losses. Net trading profits are recorded on a trade date basis.

Clearing and other brokerage income are fees charged to the broker on customer's security transactions and are recognized as of the trade date.

Other revenue consists primarily of investment advisory fees which are account management fees for high net worth clients. These fees are determined based on a percentage of the customers assets under management, are billed monthly in arrears, quarterly in arrears and are recognized when collected. Some fees are collected quarterly in advance, and those are accounted for as deferred revenue until earned.

#### Cash and Cash Equivalents

The Company considers all highly liquid temporary cash investments with an original maturity of three months or less when purchased to be cash equivalents.

#### Fixed Assets

Fixed assets are recorded at cost. Depreciation is calculated using the straight-line method based on the estimated useful lives of the related assets, which range from three to five years. Leasehold improvements are amortized using the straight-line method over the shorter of the estimated useful lives of the assets or the terms of the leases. Maintenance and repairs are charged to expense as incurred; costs of major additions and betterments that extend the useful life of the asset are capitalized. When assets are retired or otherwise disposed of, the costs and related accumulated depreciation or amortization are removed from the accounts and any gain or loss on disposal is recognized.

#### Income Taxes

The Company recognizes deferred tax assets and liabilities based on the difference between the financial statements carrying amounts and the tax basis of assets and liabilities, using the effective tax rates in the years in which the differences are expected to reverse. A valuation allowance related to deferred tax assets is also recorded when it is more likely than not that some or all of the deferred tax asset may not be realized.

#### Fair Value of Financial Instruments

Effective January 1, 2008, the Company adopted FASB ASC 820-Fair Value Measurements and Disclosures, or ASC 820, for assets and liabilities measured at fair value on a recurring basis. ASC 820 establishes a common definition for fair value to be applied to existing generally accepted accounting principles that require the use of fair value measurements establishes a framework for measuring fair value and expands disclosure about such fair value measurements. The adoption of ASC 820 did not have an impact on the Company's financial position or operating results, but did expand certain disclosures.

ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Additionally, ASC 820 requires the use of valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. These inputs are prioritized below:

- |          |   |
|----------|---|
| Level 1: | Observable inputs such as quoted market prices in active markets for identical assets or liabilities                              |
| Level 2: | Observable market-based inputs or unobservable inputs that are corroborated by market data  |
| Level 3: | Unobservable inputs for which there is little or no market data, which require the use of the reporting entity's own assumptions. |

The Company did not have any Level 2 or Level 3 assets or liabilities as of June 30, 2011 and September 30, 2010, with the exception of its subordinated borrowings and securities owned- nonmarketable. The carrying amounts of the



convertible promissory notes at June 30, 2011 and September 30, 2010 approximate their respective fair value based on the Company's incremental borrowing rate.

Cash and cash equivalents include money market securities that are considered to be highly liquid and easily tradable as of June 30, 2011 and September 30, 2010, respectively. These securities are valued using inputs observable in active markets for identical securities and are therefore classified as Level 1 within our fair value hierarchy. The fair value of the derivative liabilities is based on the quoted market prices of the Company's stock.

In addition, FASB ASC 825-10-25 Fair Value Option, or ASC 825-10-25, was effective for January 1, 2008. ASC 825-10-25 expands opportunities to use fair value measurements in financial reporting and permits entities to choose to measure many financial instruments and certain other items at fair value. The Company did not elect the fair value options for any of its qualifying financial instruments. The fair value of the derivative liabilities are classified as Level 2 within our fair value hierarchy.

#### Impairment of Long-Lived Assets

The Company reviews long-lived assets for impairment at least once a year or earlier if circumstances and situations change such that there is an indication that the carrying amounts may not be recovered, in accordance with professional standards. In such circumstances, the Company will estimate the future cash flows expected to result from the use of the asset and its eventual disposition. Future cash flows are the future cash inflows expected to be generated by an asset less the future outflows expected to be necessary to obtain those inflows. If the sum of the expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the asset, the Company will recognize an impairment loss to adjust to the fair value of the asset.

#### Common Stock Purchase Warrants

The Company accounts for the issuance of common stock purchase warrants issued in connection with capital financing transactions in accordance with professional standards for "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock". In accordance with professional standards, the Company classifies as equity any contracts that (i) require physical settlement or net-share settlement or (ii) gives the Company a choice of net-cash settlement or settlement in its own shares (physical settlement or net-share settlement). The Company classifies as assets or liabilities any contracts that (i) require net-cash settlement (including a requirement to net-cash settle the contract if an event occurs and if that event is outside the control of the Company) or (ii) gives the counterparty a choice of net-cash settlement or settlement in shares (physical settlement or net-share settlement).

The Company assessed the classification of its derivative financial instruments as of June 30, 2011, which consist of common stock purchase warrants, and determined that such warrants are equity contracts.

#### Convertible Instruments

The Company evaluates and accounts for conversion options embedded in its convertible instruments in accordance with professional standards for "Accounting for Derivative Instruments and Hedging Activities".

Professional standards generally provides three criteria that, if met, require companies to bifurcate conversion options from their host instruments and account for them as free standing derivative financial instruments. These three criteria include circumstances in which (a) the economic characteristics and risks of the embedded derivative instrument are not clearly and closely related to the economic characteristics and risks of the host contract, (b) the hybrid instrument that embodies both the embedded derivative instrument and the host contract is not re-measured at fair value under otherwise applicable generally accepted accounting principles with changes in fair value reported in earnings as they occur and (c) a separate instrument with the same terms as the embedded derivative instrument would be considered a derivative instrument. Professional standards also provide an exception to this rule when the host instrument is deemed to be conventional as defined under professional standards as "The Meaning of "Conventional Convertible Debt

Instrument”. The Company accounts for convertible instruments (when it has determined that the embedded conversion options should not be bifurcated from their host instruments) in accordance with professional standards when “Accounting for Convertible Securities with Beneficial Conversion Features,” as those professional standards pertain to “Certain Convertible Instruments.” Accordingly, the Company records, when necessary, discounts to convertible notes for the intrinsic value of conversion options embedded in debt instruments based upon the differences between the fair value of the underlying common stock at the commitment date of the note transaction and the effective conversion price embedded in the note. Debt discounts under these arrangements are amortized over the term of the related debt to their earliest date of redemption. The Company also records when necessary deemed dividends for the intrinsic value of conversion options embedded in preferred shares based upon the differences between the fair value of the underlying common stock at the commitment date of the note transaction and the effective conversion price embedded in the note.

The Company evaluated the conversion option embedded in the series A Preferred Stock and determined, in accordance with the provisions of these statements, that such conversion option does not meet the criteria requiring bifurcation of these instruments. The characteristics of the common stock that is issuable upon a holder's exercise of the conversion option embedded in the convertible preferred stock are deemed to be clearly and closely related to the characteristics of the preferred shares. Additionally, the Company's conversion options, if free standing, would not be considered derivatives subject to the accounting guidelines prescribed in accordance with professional standards.

ASC 815-40 provides that, among other things, generally, if an event is not within the entity's control could require net cash settlement, then the contract shall be classified as an asset or a liability.

Pursuant to 815-40-25-22, if the number of currently authorized but unissued shares, less the maximum number of shares that could be required to be delivered during the contract period under existing commitments, including outstanding convertible debt or instruments, outstanding stock options and warrants, exceeds the maximum number of shares that could be required to be delivered under share settlement of the contract. The warrants issued pursuant to the Series D transactions, even if not all vested, triggered this excess, at the date of issuance. Accordingly, the share settlement of the exercise of such warrants was not within the control of the Company and was classified as liability.

Additionally, the Company needs to determine whether the instruments issued in the transactions are considered indexed to the Company's own stock. While the Series C and Series D preferred Stock transactions do not provide variability involving sales volume, stock index, commodity price, revenue targets, among other things, they do provide for variability involving future equity offerings and issuance of equity-linked financial instruments. While the instruments do not contain an exercise contingency, other than the passage of time for the warrants, the settlement of the warrants associated with Series C and D and the Series C and D Preferred Stock would not equal the difference between the fair value of a fixed number of the Company's common stock and a fixed stock price. Accordingly, they were not indexed to the Company's stock price.

The Company accounted for the embedded conversion features included in its Series C and Series D preferred Stock as well as the related warrants and the warrants issued in connection with the issuance of the Company's shares of Common stock during 2010 as derivative liabilities through March 31, 2011. At March 31, 2011, all such financial instruments were reclassified as equity contracts.

## Net Loss per Common Share

Basic net loss per share is computed on the basis of the weighted average number of common shares outstanding. Diluted net income (loss) per share is computed on the basis of the weighted average number of common shares outstanding plus the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted.

	Three months ended		Nine months ended	
	June 30, 2011	June 30, 2010	June 30, 2011	June 30, 2010
Numerator:				
Net loss	\$ (327,000 )	\$ (2,031,000 )	\$ (2,381,000 )	\$ (3,736,000 )
Preferred stock dividends	(103,000 )	(103,000 )	(310,000 )	(391,000 )
Increase in fair value of derivative liabilities	-	-	1,603,000	-
Numerator for basic earnings per share- loss attributable to common stockholders - as adjusted	(430,000 )	(2,134,000 )	(1,088,000 )	(4,127,000 )
Numerator for diluted earnings per share-net income (loss) attributable to common stockholders - as adjusted	\$ (430,000 )	\$ (2,134,000 )	\$ (1,088,000 )	\$ (4,127,000 )
Denominator:				
Denominator for basic earnings per share--weighted average shares	20,446,704	17,276,704	19,444,396	17,209,396
Effect of dilutive securities:				
Assumed conversion of Series A preferred stock	-	-	-	-
Assumed conversion of Series C and D preferred stock	-	-	-	-
Stock options	-	-	-	-
Warrants	-	-	-	-
Dilutive potential common shares	-	-	-	-
Denominator for diluted earnings per share--adjusted weighted-average shares and assumed conversions	20,446,704	17,276,704	19,444,396	17,209,396
Loss per share:				
Net loss available to common stockholders Basic and diluted	\$ (0.02 )	\$ (0.12 )	\$ (0.06 )	\$ (0.24 )

The weighted-average anti-dilutive common share equivalents are as follows:

	Three-month period ended June 30,		Nine-month period ended June 30,	
	2011	2010	2011	2010
Series A Preferred Stock	3,684,000	3,560,280	3,684,000	3,519,040
Series C and D Preferred Stock	9,416,692	-	9,416,692	-
Convertible notes payable	3,375,000	3,375,000	3,375,000	3,375,000
Options	4,077,625	3,420,446	4,421,231	5,585,879
Warrants	15,773,941	1,719,250	14,067,275	1,842,991
	36,327,258	12,074,976	34,964,198	14,322,910

The anti-dilutive common shares outstanding at June 30, 2011 and 2010 are as follows:

	2011	2010
Series A Preferred Stock	3,684,000	3,684,000
Series C and D Preferred Stock	9,416,692	-
Convertible notes payable	3,375,000	3,375,000
Options	3,880,973	5,259,593
Warrants	15,173,941	2,437,250
	35,530,606	14,755,843

### Stock-Based Compensation

Effective October 1, 2005, the Company adopted ASC Topic 718 accounting for “Share Based Payment.” This topic addresses all forms of share based payment (“SBP”) awards including shares issued under employee stock purchase plans, stock options, restricted stock and stock appreciation rights. Under Topic 718, SBP awards will result in a charge to operations that will be measured at fair value on the awards grant date, based on the estimated number of awards expected to vest over the service period.

The Black-Scholes option valuation model is used to estimate the fair value of the options granted. The model includes subjective input assumptions that can materially affect the fair value estimates. The model was developed for use in estimating the fair value of traded options that have no vesting restrictions and that are fully transferable. For example, the expected volatility is estimated based on the most recent historical period of time equal to the weighted average life of the options granted. Options issued under the Company's option plans have characteristics that differ from traded options.

The Company granted 340,000 options during the nine-month period ended June 30, 2010.

The fair value of such options is based on the Black Scholes Model using the following assumptions:

Exercise price:	\$0.69-0.75
Market price at date of grant:	\$0.69-0.75
Volatility :	71.3%
Expected dividend rate:	0%

Expected terms: 5 years

Risk-free interest 2.55%  
rate:

The Company did not grant any options during the nine-month period ended June 30, 2011.

The following activity occurred under our plan:

	Three-month period ended June 30,	
	2011	2010
Weighted-average grant-date fair value of options granted	N/A	N/A
Fair value of options recognized as expense:	\$57,000	\$113,000
	Nine-month period ended June 30,	
	2011	2010
Weighted-average grant-date fair value of options granted	N/A	\$0.50
Fair value of options recognized as expense:	\$257,000	\$409,000

The total compensation cost related to non-vested options not yet recognized amounted to approximately \$24,000 at June 30, 2011 and the Company expects that it will be recognized over the following weighted-average period of 11 months.

#### Concentrations of Credit Risk

The Company is engaged in trading and providing a broad range of securities brokerage and investment services to a diverse group of retail and institutional clientele, as well as corporate finance and investment banking services to corporations and businesses. Counterparties to the Company's business activities include broker-dealers and clearing organizations, banks and other financial institutions. The Company primarily uses clearing brokers to process transactions and maintain customer accounts on a fee basis for the Company. The Company uses three clearing brokers for substantially all of its business. The Company permits the clearing firms to extend credit to its clientele secured by cash and securities in the client's account. The Company's exposure to credit risk associated with the non-performance by its customers and counterparties in fulfilling their contractual obligations can be directly impacted by volatile or illiquid trading markets, which may impair the ability of customers and counterparties to satisfy their obligations to the Company. The Company has agreed to indemnify the clearing brokers for losses they incur while extending credit to the Company's clients. It is the Company's policy to review, as necessary, the credit standing of its customers and counterparty. Amounts due from customers that are considered uncollectible by the clearing broker are charged back to the Company by the clearing broker when such amounts become determinable. Upon notification of a charge back, such amounts, in total or in part, are then either (i) collected from the customers, (ii) charged to the broker initiating the transaction and included in other receivables in the accompanying consolidated statements of financial condition, and/or (iii) charged as an expense in the accompanying consolidated statements of financial condition, based on the particular facts and circumstances.

The Company maintains cash with major financial institutions. All interest bearing accounts are insured up to \$250,000. On October 14, 2008 the FDIC announced its temporary Transaction Account Guarantee Program, which provides full coverage for non-interest bearing transaction deposit accounts at FDIC-insured institutions that agree to participate in the program. The transaction account guarantee applies to all personal and business checking deposit accounts that do not earn interest at participating institutions. This unlimited insurance coverage is temporary and will remain in effect for participating institutions until December 31, 2012. As a result of this coverage the Company believes it is not exposed to any significant credit risks for cash.





### Other Receivables

The Company extends unsecured credit in the normal course of business to its registered representatives. The determination of the amount of uncollectible accounts is based on the amount of credit extended and the length of time each receivable has been outstanding, as it relates to each individual registered representative. The allowance for doubtful accounts reflects the amount of loss that can be reasonably estimated by management is included in operating expenses in the accompanying consolidated statements of operations.

### Advances to Registered Representatives

Advances are given to certain registered representatives as an incentive for their affiliation with the Broker Dealer Subsidiaries. The representative signs an independent contractor agreement with the Broker Dealer Subsidiaries for a specified term, typically a three-year period. The advance is then amortized on a straight-line basis over the life of the broker's agreement with the Broker Dealer Subsidiaries, and is included in commission expense in the accompanying consolidated statements of operations. In the event a representative's affiliation terminates prior to the fulfillment of their contract, the representative is required to repay the unamortized balance.

### Securities Owned

Marketable securities which consist of publicly traded unrestricted common stock and bonds are valued at the closing price on the valuation date. Non-marketable securities which consist partly of restricted common stock and of non-tradable warrants exercisable into freely trading common stock of public companies are carried at fair value as determined in good faith by management, is partly based on the underlying security upon the presence of an actual value in the open market.

### Other Assets

Other assets consist primarily of reimbursable prepaid expenses and lease deposits.

### Legal and Other Contingencies

The outcomes of legal proceedings and claims brought against us are subject to significant uncertainty. ASC 450-20, Accounting for Contingencies, requires that an estimated loss from a loss contingency such as a legal proceeding or claim should be accrued by a charge to income if it is probable that an asset has been impaired or a liability has been incurred and the amount of the loss can be reasonably estimated. Disclosure of a contingency is required if there is at least a reasonable possibility that a loss has been incurred. In determining whether a loss should be accrued we evaluate, among other factors, the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate of the amount of loss. Changes in these factors could materially impact our results of operations, financial position, or our cash flows.

### Recent Accounting Pronouncements

In May 2011, the FASB issued guidance and clarification about the application of existing fair value measurements and disclosure requirements. This guidance will be effective for interim and fiscal periods beginning after December 15, 2011. We will review the requirements under the standard to determine what impacts, if any, the adoption would have on our consolidated financial statements.



NOTE 4. CLEARING AGREEMENTS

On February 1, 2010, National Securities Corporation and vFinance Investments, Inc. entered into separate but coterminous clearing agreements with National Financial Services, LLC. with a termination date of February 1, 2015. The clearing agreement includes a termination fee if either broker dealer terminates the agreement without cause. The Broker Dealer Subsidiaries currently have clearing agreements with NFS, Penson, Legent, ICBC and Rosenthal.

NOTE 5. BROKER-DEALERS AND CLEARING ORGANIZATIONS RECEIVABLES AND PAYABLES

At June 30, 2011 and September 30, 2010, the receivables of \$3,536,000 and \$3,518,000, respectively, from broker-dealers and clearing organizations represent net amounts due for fees and commissions. At June 30, 2011 and September 30, 2010, the amounts payable to broker-dealers and clearing organizations of \$157,000 and \$169,000, respectively, represent amounts owed to clearing firms or other broker dealers for fees on transactions and payables to other broker dealers associated with tri-party clearing agreements.

## NOTE 6. SECURITIES OWNED AND SECURITIES SOLD, BUT NOT YET PURCHASED AT FAIR VALUE

The following tables show the fair market values of securities owned by the Company, and securities sold but not yet purchased by the Company, as of June 30, 2011 and September 30, 2010:

## Fair Value Measurements

As of June 30, 2011

Securities owned at fair value	Level 1	Level 2	Level 3	Total
Corporate stocks	\$ 170,000	-	-	\$ 170,000
Corporate bonds	-	-	-	-
Government obligations	1,558,000	-	-	1,558,000
Restricted stock	-	53,000	-	53,000
	\$ 1,728,000	\$ 53,000	\$ -	\$ 1,781,000

Securities sold, but not yet purchased at fair value

	Level 1	Level 2	Level 3	Total
Corporate stocks	\$ 21,000	-	-	\$ 21,000
Corporate bonds	-	-	-	-
Government obligations	-	-	-	-
Restricted stock	-	-	-	-
	\$ 21,000	\$ -	\$ -	\$ 21,000

As of September 30, 2010

Securities owned at fair value	Level 1	Level 2	Level 3	Total
Corporate stocks	\$ 72,000	-	-	\$ 72,000
Corporate bonds	-	-	-	-
Government obligations	608,000	-	-	608,000
Restricted stock	-	57,000	-	57,000
	\$ 680,000	\$ 57,000	\$ -	\$ 737,000

Securities sold, but not yet purchased at fair value

	Level 1	Level 2	Level 3	Total
Corporate stocks	\$ 21,000	-	-	\$ 21,000
Corporate bonds	-	-	-	-
Government obligations	-	-	-	-
Restricted stock	-	-	-	-
	\$ 21,000	\$ -	\$ -	\$ 21,000

## NOTE 7. INVESTMENT IN UNCONSOLIDATED JOINT VENTURE

During January 2011, the Company finalized its joint venture with Opus Point Partners, LLC (“Opus”), one of the Company’s significant stockholders. The Company received a 50% interest in the joint venture in consideration of an initial capital contribution of \$1 million. The Company is in its early stage of implementing the joint venture agreement and expects that it will formalize its structure and operations within the next few months. The joint venture will initially provide investment banking services focused on the global life science sector. The joint venture may be terminated at will by both parties.

During June 2011, the Company made a cash contribution of \$501,000 in the joint venture. Opus has not earned revenues or incurred expenses since inception.

Summarized information from the balance sheet and statement of operations for Opus as of June 30, 2011 and from of the date of inception (January 2011) through June 30, 2011 were as follows:

	2011
Balance sheet	
Current Assets	\$ 501,000
Non-current assets	-
Current liabilities	-
Non-current liabilities	-
Statement of Operations	
Revenues	-
Income (loss) from operations	-
Net income (loss)	-

## NOTE 8. OTHER ASSETS

Other assets consist of the following:

	June 30, 2011	September 30, 2010
Pre-paid expenses	\$ 586,000	\$ 579,000
Deposits	90,000	184,000
Investments in unaffiliated entity	162,000	162,000
Deferred financing costs	38,000	71,000
Total	\$ 876,000	\$ 996,000

## NOTE 9. ACCOUNTS PAYABLE, ACCRUED EXPENSES AND OTHER LIABILITIES

Accounts payable, accrued expenses and other liabilities consist of the following:

	June 30, 2011	September 30, 2010
Commissions payable	7,675,000	\$ 6,037,000
Deferred clearing fee credits	392,000	210,000
Telecommunications vendors payable	63,000	80,000
Legal payable	540,000	575,000
Deferred rent payable	272,000	373,000
Accrued compensation	670,000	702,000
Capital lease liability	457,000	540,000
Other vendors	2,403,000	3,426,000
Total	\$ 12,472,000	\$ 11,943,000

## NOTE 10. DERIVATIVE LIABILITIES

During fiscal 2010, the Company issued shares of Preferred Stock Series C and D and associated warrants. The terms of the Preferred Stock C and D and associated warrants include a subsequent financing reset provision which lapses in July 2011 and March 2011, respectively. Additionally, holders of the warrants issued pursuant to Series D have a right to net settle their warrants in cash if there aren't enough shares of common stock authorized to cover the issuance of shares pursuant to the exercise of such warrants. The net settlement effective price per warrant is the difference between the fair value as defined and the effective exercise price. Furthermore, the maximum number of shares required to be delivered during the period under which the warrants issued pursuant to the Series D transaction, together with all outstanding convertible debt, stock options, warrants, and series A, C and D Preferred shares, exceeded the amount of authorized shares at September 29, 2010, their date of issuance. Furthermore, the warrants issued in connection with the sale of the Company's common stock in December 2010 also exceeded the amount of authorized shares at the date of issuance.

During April 2011, the Company's shareholders approved an increase of its authorized shares of common stock from 50,000,000 to 150,000,000 and its authorized shares of preferred stock from 200,000 to 10,000,000. Additionally, the subsequent financing reset provision of Preferred Stock D and related warrants lapsed in March 2011. Furthermore, the Company believes that, as of March 31, 2011, the likelihood that it will enter into any financing terms which would trigger resets of the conversion price of the Preferred Stock Series C and of the exercise price of the related warrants prior to July 2011 is remote.

The Company accounted for the embedded conversion features included in its Series C and Series D preferred Stock as well as the related warrants and the warrants issued in connection with the issuance of the Company's shares of Common stock during 2010 as derivative liabilities through March 31, 2011. At March 31, 2011, all such financial instruments were reclassified as equity contracts.

The aggregate fair value of derivative liabilities at June 30, 2011, and September 30, 2010 amounted to \$0 and \$4,331,000, respectively.

The reclassification of the Series C and D Preferred Stock and aforementioned warrants, previously accounted for as liability, to equity contracts, including the fair value of derivative liabilities of \$6,465,000 and the carrying value of the Preferred Stock C and D of \$513,000 resulted in the following increases at June 30, 2011:

Preferred Stock C and D	\$6,156,000
Additional paid-in capital	846,000

During the nine-month period ended June 30, 2011, the Company issued 2,820,000 warrants which were accounted for as liability contracts. The fair value of the warrants at their date of issuance amounted to \$530,000 and was offset against the proceeds of the issuance of the Company's common stock.

The fair value of the embedded conversion features and warrants were based on the Company's quoted traded price and the Black Scholes method, respectively, at each measurement date.

The fair value of the derivative instruments were based on the following assumptions:

	March 31, 2011 (prior to reclassification)	Issuance during the nine-month period ended June 30, 2011	September 30, 2010
Embedded Conversion Features:			
Exercise price	\$ 0.50	N/A	\$ 0.40
market value	\$ 0.50	N/A	\$ 0.40
Warrants:			
Effective Exercise price	\$ 0.50	\$ 0.50	\$ 0.50
Effective Market price	\$ 0.48-\$0.50	\$ 0.34-\$0.35	\$ 0.34-\$0.40
Volatility	75%	75%	76%
Risk-free interest	2.24%	2.06%	1.27%
Terms	4.25-4.75 years	5 years	5 years
Expected dividend rate	0%	0%	0%

The fair value of derivative liabilities increased by \$1.6 million between measurement dates during the nine-month period ended June 30, 2011. Such increase is recorded as other expense in the accompanying statement of operations.

#### NOTE 11. CONVERTIBLE NOTES PAYABLE

On June 30, 2008, the Company completed a financing transaction under which an investor made an investment in the Company by purchasing a convertible promissory note in the principal amount of \$3.0 million, with a warrant to purchase 375,000 shares of common stock at an exercise price of \$2.50 per share. The promissory note matures in March 2012, is convertible into common stock at a price of \$2.00 per share and has a stated interest rate of 10% per annum. Using professional standards, the relative fair value of the warrant was calculated using the Black-Scholes Option Valuation Model. The Company also recorded an additional debt discount for the beneficial conversion feature of the instrument. These amounts, totaling approximately \$791,000, have been recorded as a debt discount that will be charged to interest expense over the life of the promissory note.

On June 30, 2008, the Company completed a financing transaction under which the same investor made an additional investment in the Company by purchasing a convertible promissory note in the principal amount of \$3.0 million, with



a warrant to purchase 468,750 shares of common stock at an exercise price of \$2.00 per share. The promissory note matures in June 2012, is convertible into common stock at a price of \$1.60 per share and has a stated interest rate of 10% per annum. Under professional standards, the relative fair value of the warrant was calculated using the Black-Scholes Option Valuation Model. The Company also recorded an additional debt discount for the beneficial conversion feature of the instrument. These amounts, totaling approximately \$789,000, have been recorded as a debt discount that will be charged to interest expense over the life of the promissory note.

The following table summarizes convertible notes payable at June 30, 2011 and September 30, 2010:

	June 30, 2011	September 30, 2010
10% convertible notes payable	\$ 6,000,000	\$ 6,000,000
Less: Debt discount	(345,000 )	(642,000 )
	\$ 5,655,000	\$ 5,358,000

The Company incurred interest expense related to its convertible notes of approximately \$148,000 and \$148,000 for the three-month period ended June 30, 2011 and 2010, respectively, and \$448,000 and \$448,000 for the nine-month period ended June 30, 2011 and 2010, respectively.

#### NOTE 12. NOTES PAYABLE – RELATED PARTY

In February 2007, the Company completed a financing transaction under which certain investors purchased 10% promissory notes in the principal amount of \$1.0 million, with warrants to purchase an aggregate of 250,000 shares of common stock at an exercise price of \$1.40 per share. The promissory notes matured in February 2009, and had a stated interest rate of 10% per annum. The Company obtained forbearance agreements from the lenders and as a result, re-priced some of the warrants down to an exercise price of \$0.75 per share. The Company recalculated the fair value of the warrants and took an incremental charge of approximately \$46,000 recorded as interest expense, in accordance with professional standards.

During 2009 the Company repaid \$500,000 of the notes payable and the other \$500,000 has been extended to a new maturity of May 2010. In June 2010, the remaining lender agreed to extend the maturity date to June 30, 2011, in consideration of a warrant grant to purchase an aggregate of 225,000 shares of common stock at an exercise price of \$0.50.

This note is made by Christopher Dewey, one of the Company's former directors. The Company paid the balance owed on this note in March 2011. Interest expense of \$6,000 and \$17,000 was recorded related to this note for the nine month period ended June 30, 2011 and 2010, respectively.

#### NOTE 13. SECURED DEMAND NOTE / SUBORDINATED BORROWINGS

Subordinated borrowings represent a secured demand note that was entered into by National Securities, a registered broker-dealer. The secured demand note was entered into in accordance with the form prescribed by the FINRA, and it is accounted for in accordance with broker-dealer accounting SEC rule 15c3-1d. Accordingly, our balance sheet includes both an asset ("Secured demand note") and the corresponding liability ("Subordinated borrowings") in an identical amount. The secured demand note is available to compute net capital under SEC rule 15c3-1. The borrowings are subordinated to the claims of present and future creditors of the Company and cannot be repaid where such repayment will cause the Company to fail to meet its minimum net capital requirements in accordance with SEC rule 15c3-1.

National Securities entered into a secured demand note collateral agreement with an employee of National Securities and a former Director of the Company, to borrow securities that can be used by the Company for collateral agreements. These securities have been pledged through an unrelated broker-dealer, and have a borrowing value totaling \$500,000. This note bears interest at 5% per annum with interest paid monthly. In fiscal year 2009, upon the maturity of the aforementioned note, the lender opted to not renew the note and as such, the note is presently in "Suspended Repayment" status, as defined in the original note. Certain of the securities, totaling \$168,000, have been pledged as collateral for security deposits for office leases under two letters of credit. No amounts have been drawn

on either of these letters of credit. The holder also entered into a warrant agreement to purchase 150,000 shares of common stock at a price of \$1.25 per share. This warrant expired on July 31, 2009. In December 2010, this Secured demand note was repaid with all accrued interest due through the repayment.

In June 2009, National Securities was approved by the FINRA to receive a Subordinated loan from Legent for \$100,000. This loan was granted subsequent to National Securities signing a clearing agreement with Legent to clear a portion of the business. This loan was forgiven in June 2010 after National Securities completed the contractual obligations required by the contract.

In July 2009, National Securities was approved by the FINRA to receive an additional Subordinated loan from Legent for \$250,000, also bearing interest at the rate of 4.5% payable monthly. This loan was granted subsequent to National Securities signing a clearing agreement with Legent to clear a portion of the business. This loan began principal repayment at a minimum of \$10,000 per month or \$10 per transaction, whichever is greater, starting July 31, 2010. Some or all of this repayment may be funded by transactional credits depending on the amount of business conducted through Legent on a monthly basis.

#### NOTE 14. COMMITMENTS AND CONTINGENCIES

During the quarter ended June 30, 2011, there were no significant developments in the Company's legal proceedings. For a detailed discussion of the Company's legal proceedings, please refer to the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2010.

In September 2010, Ms. Lambeth, a Florida resident, sent a letter alleging that her accounts at NSC had experienced significant declines based on unsuitable, high risk investments recommended by Eric Elliott, a broker formerly registered with NSC. Ms. Lambeth sought damages of approximately \$3,400,000 in one account and \$250,000 in a trust account, on theory that Mr. Elliott was liable for them and that NSC is vicariously liable for Mr. Elliott's conduct. NSC denied all claims, and the parties reached a settlement for \$1,150,000 on August 10, 2011, of which the Company's Errors and Omissions policy will contribute \$1,000,000 (the policy per event limit) to the settlement. The Company has accounted for its contribution to this settlement (\$150,000) as of June 30, 2011.

The Company's subsidiaries are defendants in various arbitrations and administrative proceedings and lawsuits. Damages alleged in these matters, to the extent they can be quantified, were approximately \$12,225,000 as of June 30, 2011. These matters arise in the normal course of business. The Company intends to vigorously defend itself in these actions, and believes that the eventual outcome of these matters will not have a material adverse effect on the Company. However, the ultimate outcome of these matters cannot be determined at this time. The amounts related to such matters that are reasonably estimable and which have been accrued at June 30, 2011 and September 30, 2010, is \$370,000 and \$265,000 (primarily legal fees), respectively, and have been included in "Accounts Payable, Accrued Expenses and Other Liabilities" in the accompanying consolidated statements of financial condition. The Company has included in "Professional fees" litigation and FINRA related expenses of approximately \$388,000 and \$311,000 for the three-month period ended June 30, 2011 and 2010, respectively and \$762,000 and \$655,000 during the nine month period ended June 30, 2011 and 2010, respectively.

## NOTE 15. STOCKHOLDERS' EQUITY

### Issuance of shares of common stock and warrants pursuant to a private placement

During the nine-month period ended June 30, 2011, the Company generated gross proceeds of \$1,585,000 by issuing 3,170,000 shares of its common stock. The Company paid \$169,000 in costs in connection with the issuance of shares. Additionally, the Company recognized derivative liabilities of \$530,000 in connection with this transaction, which was offset against the proceeds. Furthermore, the Company issued 3,170,000 warrants to the investors participating in this private placement and 200,000 warrants to brokers. The warrants have an exercise price of \$0.50 per share. The warrants expire in December 2016.

### Receipt of subscription receivable

During the nine-month period ended June 30, 2011, the Company received the remaining proceeds of its Series D preferred Stock offering which amounted to \$1,334,000.

### Dividends on Series A Preferred Stock

The holders of the Company's Series A convertible preferred stock, that are convertible into the Company's common stock at \$1.25 per share, are entitled to receive dividends on a quarterly basis at a rate of 9% per annum, per share. Such dividends are cumulative and accumulate whether or not declared by the Company's Board of Directors, but are payable only when and if declared by the Company's Board of Directors. During the three-month period ended June 30, 2011 and 2010, the Company recognized approximately \$103,000 and \$103,000 of dividends on its Series A preferred stock, and at June 30, 2011, the total amount of accumulated dividends on the Company's 46,050 issued and outstanding shares of Series A preferred stock was approximately \$414,000.

### Reclassification of liability contracts to equity contracts

At June 30, 2011, we reclassified certain Series C and D Preferred Stock and related warrants and certain warrants issued in connection with a private placement from liability contracts to equity contracts.

The reclassification of the Series C and D Preferred Stock and aforementioned warrants, previously accounted for as a liability to equity contracts, resulted in the following increases at June 30, 2011:

Preferred Stock C and D	\$6,156,000
Additional paid-in capital	\$ 846,000

## NOTE 16. NET CAPITAL REQUIREMENTS

National Securities, as a registered broker-dealer, is subject to the SEC's Uniform Net Capital Rule 15c3-1 that requires the maintenance of minimum net capital. National Securities has elected to use the alternative standard method permitted by the rule. This requires that National Securities maintain minimum net capital equal to the greater of \$250,000 or a specified amount per security based on the bid price of each security for which National Securities is a market maker. At June 30, 2011, National Securities had net capital of approximately \$1,545,000 which exceeded its requirement by approximately \$1,295,000.

In addition to the net capital requirements, each of vFinance Investments and EquityStation are required to maintain a ratio of aggregate indebtedness to net capital, as defined, of not more than 15 to 1 (and the rule of the "applicable" exchange also provides that equity capital may not be withdrawn or cash dividends paid if the resulting net capital

ratio would exceed 10 to 1). At June 30, 2011, vFinance Investments had net capital of approximately \$1,486,000 which was approximately \$486,000 in excess of its required net capital of \$1,000,000 and its percentage of aggregate indebtedness to net capital was 296%. At June 30, 2011, EquityStation had net capital of approximately \$209,000 which was approximately \$109,000 in excess of its required net capital of \$100,000 and its percentage of aggregate indebtedness to net capital was 107%. Each of the Broker Dealer subsidiaries qualifies under the exemptive provisions of Rule 15c3-3 under Section (k)(2)(ii) of the Rule, as none of them carry the accounts of their customers on their books nor perform custodial functions related to customer securities.

Advances, dividend payments and other equity withdrawals from its broker dealer subsidiaries are restricted by the regulations of the SEC, and other regulatory agencies. These regulatory restrictions may limit the amounts that a subsidiary may dividend or advance to the Company.

#### NOTE 17. SUBSEQUENT EVENTS

In September 2010, Ms. Lambeth, a Florida resident, sent a letter alleging that her accounts at NSC had experienced significant declines based on unsuitable, high risk investments recommended by Eric Elliott, a broker formerly registered with NSC. Ms. Lambeth sought damages of approximately \$3,400,000 in one account and \$250,000 in a trust account, on theory that Mr. Elliott was liable for them and that NSC is vicariously liable for Mr. Elliott's conduct. NSC denied all claims, and the parties reached a settlement for \$1,150,000 on August 10, 2011, of which the Company's Errors and Omissions policy will contribute \$1,000,000 (the policy per event limit) to the settlement. The Company has accounted for its contribution to this settlement (\$150,000) as of June 30, 2011.

Other than disclosed above, the Company has evaluated subsequent events through August 15, 2011, which is the date the financial statements were issued, and has concluded that no such events or transactions took place which would require disclosure herein.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. This Quarterly Report may contain certain statements of a forward-looking nature relating to future events or future business performance. Any such statements that refer to the Company's estimated or anticipated future results or other non-historical facts are forward-looking and reflect the Company's current perspective of existing trends and information. These statements involve risks and uncertainties that cannot be predicted or quantified and, consequently, actual results may differ materially from those expressed or implied by such forward-looking statements. Such risks and uncertainties include, among others, risks and uncertainties detailed in the Company's Annual Report on Form 10-K, filed with the Securities and Exchange Commission on December 29, 2010. Any forward-looking statements contained in or incorporated into this Quarterly Report speak only as of the date of this Quarterly Report. The Company undertakes no obligation to update publicly any forward-looking statement, whether as a result of new information, future events or otherwise.

### OVERVIEW

We are engaged in investment banking, equity research, institutional sales and trading, independent brokerage and advisory services and asset management services through our principal subsidiaries, National Securities Corporation ("National Securities"), vFinance Investments, Inc. ("vFinance Investments") EquityStation, Inc. ("EquityStation") and National Asset Management Inc. (EquityStation, collectively with National Securities and vFinance Investments, are the "Broker Dealer Subsidiaries"). We are committed to establishing a significant presence in the financial services industry by meeting the varying investment needs of our retail, corporate and institutional clients.

Each of the Broker Dealer Subsidiaries is subject to regulation by, among others, the Securities and Exchange Commission ("SEC"), the Financial Industry Regulatory Authority ("FINRA"), the Municipal Securities Rulemaking Board ("MSRB") and each is a member of the Securities Investor Protection Corporation ("SIPC"). vFinance Investments and National Securities are also subject to regulation by the National Futures Association ("NFA"). In addition, each of the Broker Dealer Subsidiaries is licensed to conduct its brokerage activities in all 50 states, plus the District of Columbia and Puerto Rico, with vFinance Investments also being licensed in the U.S. Virgin Islands.

As of June 30, 2011, we had approximately 963 associated personnel serving retail and institutional customers, trading and investment banking clients. With the exception of our New York, New Jersey, Florida, Washington and Illinois branches, our approximately 91 other registered offices are owned and operated by independent owners who maintain all appropriate licenses and are responsible for all office overhead and expenses. These independent operators, many of whom are financial planners, are required to pay their own expenses. This independent contractor model calls for a much higher payout percentage, (typically in the 70-90% range) than the traditional employee model of brokerage which typically only pays between 25-50% of production.

Our registered representatives offer a broad range of investment products and services. These products and services allow us to generate both commissions (from transactions in securities and other investment products) and fee income (for providing investment advisory services, namely managing a client's account). The investment products and services offered include but are not limited to stocks, bonds, mutual funds, annuities, insurance, and managed money accounts.

### Business Environment in the Nine Months of Fiscal 2011

The financial markets seemed to strengthen during the first nine months of our fiscal year, as U.S. economic critical data showed some very early indications of economic recovery. Merger and acquisitions markets continue to show signs of rebound; however the extent and timing of a significant rise in transactions is uncertain.





Volatility in the financial markets remains due to uncertainties related to bank regulation, the effect of the Federal Reserve quantitative easing programs resulting in risk of inflation which may lead to higher interest rates and impact the valuation of corporate stocks and bonds and government obligations as asset classes. The potential tightening of credit and regulation of banks and other financial institutions stemming from the Dodd-Frank Act may have a detrimental impact on the markets.

The results of our operations during the first nine months of 2011 were impacted by the volatility in the financial markets yet clearly show signs of improvement over our recently recorded results. As these results are highly dependent on the environment in which our businesses operate, our quarterly results may not necessarily be indicative of future performance.

### Growth Strategy

We continue to evaluate opportunities to grow our businesses, including potential acquisitions or mergers with other securities, investment banking and investment advisory firms, and by adding to our base of independent representatives organically. These acquisitions may involve payments of material amounts of cash, the incurrence of a significant amount of debt or the issuance of significant amounts of our equity securities, which may be dilutive to our existing stockholders and/or may increase our leverage. For example, we finalized our agreement on a joint venture with Opus Point Partners LLC in which our initial investment is \$1.0 million for a 50% interest in an investment banking operations focusing on the global life science industry. We cannot assure you that we will be able to consummate any such potential acquisitions at all or on terms acceptable to us or, if we do, that any acquired business will be profitable. There is also a risk that we will not be able to successfully integrate acquired businesses into our existing business and operations.

### Key Indicators of Financial Performance for Management

Management periodically reviews and analyzes our financial performance across a number of measurable factors considered to be particularly useful in understanding and managing our business. Key metrics in this process include productivity and practice diversification of representatives, top line commission and advisory services revenues, gross margins, operating expenses, legal costs, taxes and earnings per share.

## RESULTS OF OPERATIONS

### Three Months Ended June 30, 2011 Compared to Three Months Ended June 30, 2010

Our third quarter of fiscal year 2011 resulted in an increase in revenues, with a lower increase in expenses compared to the same period last year. As a result, we reported a net operating loss of \$348,000 compared with a net operating loss of \$2,031,000 for the third quarters of fiscal years 2011 and 2010, respectively.

	Three Months Ended June 30,		Increase (Decrease)	
	2011	2010	Amount	Percent
Commissions	\$ 20,392,000	\$ 19,416,000	\$ 976,000	5%
Net dealer inventory gains	3,650,000	3,336,000	314,000	9%
Investment banking	3,124,000	1,427,000	1,697,000	119%
Interest and dividends	870,000	746,000	124,000	17%
Transfer fees and clearance services	1,834,000	1,912,000	(78,000 )	-4%
Other	2,170,000	1,643,000	527,000	32%
	\$ 32,040,000	\$ 28,480,000	\$ 3,560,000	13%

Total revenues increased \$3,560,000, or 13%, in the third quarter of fiscal year 2011 to \$32,040,000 from \$28,480,000 in the third quarter of fiscal year 2010. The increase in revenues is primarily due to more favorable market conditions. Commission revenue increased \$976,000, or 5%, to \$20,392,000 from \$19,416,000 during the third quarter of fiscal year 2011 compared with the same period in fiscal year 2010, which is attributable to generally more favorable market conditions for corporate securities. Net dealer inventory gains, which includes profits on proprietary trading, market making activities and customer mark-ups and mark-downs, increased \$314,000, or 9%, to \$3,650,000 from \$3,336,000 during the third quarter of fiscal year 2011 compared with the same period in fiscal year 2010. The increase is primarily due to more favorable trading conditions affecting our market making and fixed income trading activities in the quarter ended June 30, 2011 as compared to the same quarter in 2010.

Investment banking revenue increased \$1,697,000, or 119% to \$3,124,000 from \$1,427,000 during the third quarter of 2011 compared to the same period in fiscal year 2010. This increase was attributable to a larger number of successful completion of capital raising for clients, advisory and consulting services provided during the quarter. Interest and dividend income increased by \$124,000 or 17%, to \$870,000 from \$746,000 in the third quarter of fiscal year 2011 compared with the same period in fiscal year 2010. The increase is primarily attributable to generally higher customer margin account balances, higher customer free cash balances and slightly higher prevailing interest rates during the quarter. Transfer fees and clearance services decreased \$78,000 or 4%, to \$1,834,000 in the third quarter of fiscal year 2011 from \$1,912,000 in the third quarter of fiscal year 2010.

Other revenue, consisting of asset management fees, miscellaneous transaction fees and trading fees and other investment income, increased \$527,000, or 32%, to \$2,170,000 from \$1,643,000 during the third quarter of fiscal year 2011 compared to the third quarter of fiscal year 2010. The increase is due primarily to slightly more favorable market conditions resulting in generally higher assets under management in our Registered Investment Advisory firm, National Asset Management.

In comparison with the 13% increase in total revenues, total expenses increased by \$1,877,000, or 6%, to \$32,388,000 for the third quarter of fiscal year 2011 compared to \$30,511,000 in the third quarter of fiscal year 2010. This increase in total expenses is primarily a result of an increase in commission expense which is consistent with the increase in commission and investment banking revenues.

	Three Months Ended		Increase (Decrease)	
	2011	2010	Amount	Percent
Commissions, compensation, and fees	\$ 28,708,000	\$ 26,375,000	\$ 2,333,000	9%
Clearing fees	483,000	576,000	(93,000 )	-16%
Communications	1,132,000	1,124,000	8,000	1%
Occupancy, equipment and other administrative expenses	976,000	848,000	128,000	15%
Professional fees	410,000	687,000	(277,000 )	-40%
Interest	280,000	459,000	(179,000 )	-39%
Taxes, licenses and registration	399,000	442,000	(43,000 )	-10%
	\$ 32,388,000	\$ 30,511,000	\$ 1,877,000	6%

Commissions, compensation, and fees, which includes expenses related to commission revenue, net dealer inventory gains and investment banking, increased \$2,333,000, or 9%, to \$28,708,000 in the third quarter of fiscal year 2011 from \$26,375,000 in the third quarter of fiscal year 2010. The increase is primarily attributable to an increase in the related commission and investment banking revenues. Commission expense also includes the amortization of advances to registered representatives and the fair value of stock-based compensation aggregating of \$88,000 and \$187,000 for the third quarter of fiscal year 2011 and 2010, respectively. These amounts fluctuate based upon the amounts of advances outstanding and the time period for which the registered representatives have agreed to be affiliated with National Securities. Employee compensation includes the amortization of the fair value associated with stock based compensation of \$58,000 and \$113,000 in third quarter of fiscal years 2011 and 2010, respectively.

Commission, compensation, and fees, as a percentage of revenue decreased by 3% to 90% in the third quarter of fiscal year 2011 from the comparable prior year period, primarily from an increase in investment banking and other revenues, which have higher margins and, to a lesser extent, the higher amount of amortization of advances to registered representatives recognized during the third quarter of fiscal 2010.

Clearing fees decreased \$93,000, or 16%, to \$483,000 in the third quarter of fiscal year 2011 from \$576,000 in the third quarter of fiscal year 2010. The decrease in clearing fees is commensurate with a decrease in clearance services revenues in the third quarter of fiscal year 2011.

Communications expenses increased by \$8,000, or 1% to \$1,132,000 in the third quarter of fiscal year 2011 from \$1,124,000 in the third quarter of fiscal year 2010. These expenses are at comparable levels during both third quarter of fiscal year 2011 and 2010. Occupancy, equipment and other administrative expenses increased \$128,000, or 15%, to \$976,000 from \$848,000 in the third quarter of fiscal year 2011 compared to the third quarter of fiscal year 2010. This increase in such expenses is primarily attributable to settlements of two claims offset by a decrease in occupancy costs due primarily to our focus on reducing the cost of operations, including square footage rented as well as negotiating slightly better rental agreements during the third quarter of 2011 when compared to the prior year period.

Professional fees decreased \$277,000, or 40% to \$410,000 from \$687,000 in the third quarter of fiscal year 2011 compared to the third quarter of fiscal year 2010. The decrease in professional fees is primarily a result of a refund from errors and omission insurance company offset by slightly higher costs to defend arbitrations and civil actions as well as general corporate legal services.

Interest expense decreased by \$179,000, or 39%, to \$280,000 from \$459,000 in the third quarter of fiscal year 2011 compared to the third quarter of fiscal year 2010. The decrease is primarily due to the fair value of warrants issued in June 2010 to extend the maturity of our note payable and lower weighted-average principal of interest-bearing debt resulting from a repayment of notes payable of \$500,000 during the second quarter of fiscal year 2011. Taxes, licenses and registration decreased \$43,000, or 10%, to \$399,000 from \$442,000 in the third quarter of fiscal year 2011 compared to the third quarter of fiscal year 2010. This decrease in taxes, licenses and registration is due to a general decrease in fees paid to regulators and other governmental agencies during this quarter.

#### Nine Months Ended June 30, 2011 Compared to Nine Months Ended June 30, 2010

Our first half of fiscal year 2011 resulted in an increase in revenues, with a lower increase in operating expenses compared to the same period last year. As a result, we reported a net operating loss of \$802,000 compared with a net operating loss of \$3,736,000 for the nine-month period ended June 30, 2011 and 2010, respectively.

	Nine Month Ended June 30,		Increase (Decrease)	
	2011	2010	Amount	Percent
Commissions	\$ 67,608,000	\$ 56,634,000	\$ 10,974,000	19%
Net dealer inventory gains	11,241,000	11,199,000	42,000	0%
Investment banking	6,395,000	4,940,000	1,455,000	29%
Interest and dividends	2,718,000	1,856,000	862,000	46%
Transfer fees and clearance services	6,823,000	6,672,000	151,000	2%
Other	5,882,000	4,401,000	1,481,000	34%
	\$ 100,667,000	\$ 85,702,000	\$ 14,965,000	17%

Total revenues increased \$14,965,000 or 17%, in the nine-month period ended June 30, 2011 to \$100,667,000 from \$85,702,000 in the nine-month period ended June 30, 2010. The increase in revenues is primarily due to more favorable market conditions. Commission revenue increased \$10,974,000 or 19%, to \$67,608,000 from \$56,634,000 during the nine-month period ended June 30, 2011 compared with the same prior year period, which is attributable to generally more favorable market conditions. Net dealer inventory gains, which includes profits on proprietary trading, market making activities and customer mark-ups and mark-downs, increased \$42,000, or less than 1%, to \$11,241,000 from \$11,199,000 during the nine month period ended June 30, 2011 compared with the same prior year period. The increase is primarily due the addition of market making in foreign ADR's on our market making desk as well as more favorable trading conditions affecting our municipal bond trading in the first half of fiscal year 2011.

Investment banking revenue increased \$1,455,000, or 29% in the nine-month period ended June 30, 2011 to \$6,395,000 from \$4,940,000 compared to the same period in fiscal year 2010. This increase was attributable to a larger number of successful completion of capital raising for clients, advisory and consulting services provided during the nine-month period ended June 30, 2011. Interest and dividend income increased by \$862,000 or 46%, to \$2,718,000 from \$1,856,000 in the nine-month period ended June 30, 2011 compared with the same prior year period. The increase is primarily attributable to generally higher customer margin account balances, higher customer free cash balances and slightly higher prevailing interest rates during the nine-month period ended June 30, 2011. Transfer fees and clearance services increased \$151,000 or 2%, to \$6,823,000 in the nine-month period ended June 30, 2011 from \$6,672,000 in the same prior year period. The increase is due to higher transactional volume as well as slightly higher year-end fees charged in 2011 than in 2010.

Other revenue, consisting of asset management fees, miscellaneous transaction fees and trading fees and other investment income, increased \$1,481,000, or 34%, to \$5,882,000 from \$4,401,000 during the nine-month period ended June 30, 2011 compared to the same prior year period. The increase is due primarily to slightly more favorable business conditions and generally higher assets under management in our registered investment advisory firm, National Asset Management.

In comparison with the 17% increase in total revenues, total expenses increased but to a lesser extent proportionately with revenues, up by \$12,013,000, or 13%, to \$101,469,000 for the nine-month period ended June 30, 2011 compared to \$89,438,000 for the same period the prior year. This increase in total expenses is primarily a result of an increase in commission expense, consistent with the increase in commission revenues, offset by reductions in most other expense categories, as a result of management's focus on cost cutting.

	Nine Months Ended June 30,		Increase (Decrease)	
	2011	2010	Amount	Percent
Commissions, compensation, and fees	\$89,890,000	\$77,856,000	\$12,034,000	15%
Clearing fees	1,641,000	982,000	659,000	67%
Communications	3,401,000	3,307,000	94,000	3%
Occupancy, equipment and other administrative expenses	3,072,000	3,146,000	(74,000)	-2%
Professional fees	1,399,000	1,785,000	(386,000)	-22%
Interest	864,000	1,056,000	(192,000)	-18%
Taxes, licenses and registration	1,202,000	1,306,000	(104,000)	-8%
	\$101,469,000	\$89,438,000	\$12,031,000	13%

Commission, compensation, and fees, which includes expenses related to commission revenue, net dealer inventory gains and investment banking, increased \$12,034,000, or 15%, to \$89,890,000 in the nine-month period ended June 30, 2011 from \$77,856,000 in the nine-month period ended June 30, 2010. The increase is primarily attributable to an increase in the related commission revenues. Commission expense also includes the amortization of advances to registered representatives of \$316,000 and \$1,106,000 for the nine-month period ended June 30, 2011 and 2010, respectively. These amounts fluctuate based upon the amounts of advances outstanding and the time period for which the registered representatives have agreed to be affiliated with National Securities. Employee compensation includes the amortization of the fair value associated with stock based compensation of \$257,000 and \$409,000 in the nine-month period ended June 30, 2011 and 2010, respectively.

Commissions, compensation and fees, as a percentage of revenue decreased by 2%, to 89% during the nine-month period ended June 30, 2011 from 91% during the nine-month ended June 30, 2010. The decrease of commissions, compensation, and fees, as a percentage of revenues, is primarily attributable to the higher amount of amortization of advances to registered representatives recognized during the nine-month period ended June 30, 2010.

Clearing fees increased \$659,000 or 67%, to \$1,641,000 in the nine-month period ended June 30, 2011 from \$982,000 in the comparable prior year period. The increase in clearing fees is primarily due to a write-off of deferred revenues of \$456,000 during the third quarter of fiscal 2010 as well as a general increase in transactional costs due to the increase in transactions commensurate with the increase in revenues. The write off of deferred revenue was attributable to the termination of our clearing agreement with NFS.

Communication expenses increased \$94,000 or 3%, to \$3,401,000 from \$3,307,000 in the nine-month period ended June 30, 2011 when compared to the prior year period. The increase was not significant. Occupancy, equipment and other administrative expenses decreased \$74,000, or 2%, to \$3,072,000 from \$3,146,000 in the nine-month period ended June 30, 2011 when compared to the prior year period. The decrease in these expenses is due primarily to our focus on reducing the cost of operations, including square footage rented as well as negotiating slightly better rental agreements, offset by the settlement of two claims which occurred during the third quarter of 2011.

Professional fees decreased \$386,000, or 22% to \$1,399,000 from \$1,785,000 in the nine-month period ended June 30, 2011 when compared to the prior year period. The decrease in professional fees is primarily a result of slightly lower costs to defend arbitrations and civil actions.

Interest expense decreased by \$192,000, or 18%, to \$864,000 from \$1,056,000 in the nine-month period ended June 30, 2011 when compared to the prior year period. The decrease is primarily due to the fair value of warrants issued in June 2010 to extend the maturity of our note payable and lower weighted-average principal of interest-bearing debt resulting from a repayment of notes payable of \$500,000 during the second quarter of fiscal year 2011. Taxes, licenses and registration decreased \$104,000, or 8%, to \$1,202,000 from \$1,306,000 in in the nine-month period ended June 30, 2011 when compared to the prior year period.. This decrease in taxes, licenses and registration is due to a general decrease in fees paid to regulators and other governmental agencies.

The fair value of derivative liabilities, as computed between measurement dates, increased by \$1,603,000 during the nine-month period ended June 30, 2011. We did not have any derivative liabilities outstanding during the nine-month period ended June 30, 2010. The increase in fair value of derivative liabilities is primarily due an increase in our quoted price per share between measurement dates, which is one of the main assumptions in our computation of derivative liabilities.



## NON-G.A.A.P. INFORMATION

Management considers earnings before interest, taxes, depreciation and amortization, or EBITDA, as adjusted, an important indicator in evaluating our business on a consistent basis across various periods. Due to the significance of non-recurring items, EBITDA, as adjusted, enables our board of directors and management to monitor and evaluate our business on a consistent basis. We use EBITDA, as adjusted, as a primary measure, among others, to analyze and evaluate financial and strategic planning decisions regarding future operating investments and potential acquisitions. We believe that EBITDA, as adjusted, eliminates items that are not part of our core operations, such as interest expense and amortization expense associated with intangible assets, or items that do not involve a cash outlay, such as stock-related compensation. EBITDA, as adjusted should be considered in addition to, rather than as a substitute for, pre-tax income, net income and cash flows from operating activities. For the three months ended June 30, 2011 and 2010, EBITDA, as adjusted, was \$451,000 and \$(930,000), respectively. This improvement of \$1,381,000 in the three months ended June 30, 2011 over 2010 resulted from an increase in revenues and a lower increase in expenses. Most other general operating expenses decreased as a result of cost cutting efforts on the part of management. For the nine-month period ended June 30, 2011 and 2010, EBITDA, as adjusted, was \$1,737,000 and \$(63,000) respectively. This improvement of \$1,743,000 in the nine months ended June 30, 2011 over 2010 resulted from an increase in sales offset by a corresponding increase in commissions and clearing costs and a decrease in general operating expenses as a result of cost cutting efforts on the part of management.

The following table presents a reconciliation of EBITDA, as adjusted, to net loss as reported in accordance with generally accepted accounting principles, or GAAP.

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2011	2010	2011	2010
Net loss, as reported	\$ (327,000 )	\$ (2,031,000 )	\$ (2,381,000 )	\$ (3,736,000 )
Interest expense	280,000	409,000	864,000	1,056,000
Taxes	46,000	47,000	110,000	132,000
Depreciation	151,000	182,000	478,000	540,000
Amortization	155,000	162,000	489,000	487,000
EBITDA	305,000	(1,231,000 )	(440,000 )	(1,521,000 )
Non-cash compensation expense	58,000	113,000	258,000	409,000
Forgivable loan write down	88,000	188,000	316,000	1,106,000
Change in fair value of derivative	-	-	1,603,000	-
EBITDA, as adjusted	\$ 451,000	\$ (930,000 )	\$ 1,737,000	\$ (6,000 )

EBITDA, adjusted for gains or losses on sales of assets, non-cash compensation expense and loss on extinguishment of debt, is a key metric we use in evaluating our business. EBITDA is considered a non-GAAP financial measure as defined by Regulation G promulgated by the SEC.

## Liquidity and Capital Resources

Our Broker Dealer Subsidiaries are subject to the SEC's Uniform Net Capital Rule 15c3-1, which is designed to measure the general financial integrity and liquidity of a broker-dealer and requires the maintenance of minimum net capital. Net capital is defined as the net worth of a broker-dealer subject to certain adjustments. In computing net capital, various adjustments are made to net worth that exclude assets not readily convertible into cash. Additionally, the regulations require that certain assets, such as a broker-dealer's position in securities, be valued in a conservative manner so as to avoid over-inflation of the broker-dealer's net capital. National Securities has elected to use the alternative standard method permitted by the rule. This requires that National Securities maintain minimum net capital equal to the greater of \$250,000 or a specified amount per security based on the bid price of each security for which National Securities is a market maker. At June 30, 2011, National Securities' net capital exceeded the requirement by \$1,295,000. Due to its market maker status, vFinance Investments is required to maintain minimum net capital of \$1,000,000, and at June 30, 2011 vFinance Investments' net capital exceeded the requirement by \$486,000. EquityStation is required to maintain minimum net capital of \$100,000, and at June 30, 2011 EquityStation's net capital exceeded the requirement by \$109,000.

Advances, dividend payments and other equity withdrawals from our subsidiaries are restricted by the regulations of the SEC and other regulatory agencies. These regulatory restrictions may limit the amounts that a subsidiary may pay as dividend or advance to us. During the nine-month period ended June 30, 2011 we did not have any equity withdrawals.

We extend unsecured credit in the normal course of business to our brokers. The determination of the appropriate amount of the reserve for uncollectible accounts is based upon a review of the amount of credit extended, the length of time each receivable has been outstanding, and the specific individual brokers from whom the receivables are due. The objective of liquidity management is to ensure that we have ready access to sufficient funds to meet commitments, fund deposit withdrawals and efficiently provide for the credit needs of customers.

Our primary sources of liquidity include our cash flow from operations, the sale of our securities and other financing activities. We believe that we have sufficient funds from operations to fund our ongoing operating requirements through at least fiscal year 2011. If market conditions should weaken, we would need to consider curtailing certain of our business activities, reducing fixed overhead costs and/or seek additional sources of financing.

Our cash and working capital at June 30, 2011 amount to \$7,163,000 and (\$2,556,000), respectively.

Cash provided by our operating activities for the nine-month period ended June 30, 2011 amounted to \$406,000, which was primarily due to our net loss of \$2,381,000, adjusted by non-cash adjustments of \$944,000 in depreciation and amortization, \$316,000 in amortization of forgivable loans to brokers, \$257,000 in stock compensation expense, \$297,000 in amortization of note discount and an increase in fair value of derivative liabilities of \$1,603,000.

Additionally, our operating assets and liabilities varied as follows:

- a decrease in other receivables of \$173,000, which is primarily attributable to the return of a security deposit on our space at 880 3rd Ave in New York;
- an increase in securities owned at market value of \$977,000, which is primarily due to the timing of securities purchased for inventory;
- an increase in accounts payable and accrued expenses of \$529,000, which is primarily due to an increase in accrued compensation commensurate with our increased revenues.



Cash used in investing activities for the nine-month period ended June 30, 2011 amounted to \$263,000, which was primarily due to the redemption of a note receivable of \$500,000, offset by recurring purchases of computer equipment of \$262,000 and an investment in an unconsolidated joint venture of \$501,000.

Cash provided by financing activities for the nine-month period ended June 30, 2011 amounted to \$1,630,000 and was primarily due to net proceeds from the issuance of Series D Preferred Stock and our shares of common stock aggregating \$2,750,000, offset by principal repayments aggregating \$1,120,000 of subordinated borrowings and notes payable.

Cash used in operating activities for the nine-month period ended June 30, 2010 amounted to \$3,454,000, which was primarily due to our net loss of \$3,736,000, reduced by non-cash adjustments of \$1,005,000 in depreciation and amortization, \$1,105,000 reduction of loans to registered representatives, \$409,000 in stock compensation expense, \$296,000 in amortization of note discount,

Additionally, our operating assets and liabilities varied as follows:

- a decrease in receivables from our clearing firms of \$1,784,000 resulted from a corresponding decrease in revenues; and,
- an increase in our securities owned; marketable at fair value of \$207,000, which is primarily due to the timing of securities purchased for inventory; and,
- a decrease in accounts payable and accrued expenses of \$4,429,000 due to lower commissions and general accounts payable consistent with lower revenues.

Cash used in investing activities for the nine-month period ended June 30, 2010 amounted to \$341,000, which was due to recurring purchases of Computer and office equipment.

Cash provided by financing activities for the nine-month period ended June 30, 2010 amounted to \$1,200,000 resulting from the issuance of subordinated borrowings to certain investors and existing board members of \$1,700,000 offset by a repayment of notes payable for \$500,000.

Two of our convertible notes, aggregating \$6,000,000, mature during the third quarter of fiscal 2012. Such notes are convertible at a weighted average rate of \$1.78 per share, at the option of the holders. Our plan is to satisfy our obligations under such convertible notes by either: 1) providing incentives to the holders to either extend the maturity of the notes or convert the notes in our shares of Common Stock, 2) securing additional financing between now and the maturity dates to repay the notes, 3) repay the notes in cash and other available current assets at maturity, or 4) a combination of the aforementioned options. While the Company is confident that it will ultimately satisfy its obligations under such convertible notes, it cannot guarantee that it will be able to do so at favorable terms, or at all.

#### OFF-BALANCE SHEET ARRANGEMENTS

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a material current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

#### NEW ACCOUNTING PRONOUNCEMENTS

See Note 3 of Notes to Condensed Consolidated Financial Statements.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our primary market risk arises from the fact that we engage in proprietary trading and historically have made dealer markets in equity securities. Accordingly, we may be required to maintain certain amounts of inventories in order to facilitate customer order flow. We may incur losses as a result of price movements in these inventories due to changes in interest rates, foreign exchange rates, equity prices and other political factors. We are not subject to direct market risk due to changes in foreign exchange rates. However, we are subject to market risk as a result of changes in interest rates and equity prices, which are affected by global economic conditions. We manage our exposure to market risk by limiting its net long or short positions. Trading and inventory accounts are monitored daily by management and we have instituted position limits.

Credit risk represents the amount of accounting loss we could incur if counterparties to our proprietary transactions fail to perform and the value of any collateral proves inadequate. Although credit risk relating to various financing activities is reduced by the industry practice of obtaining and maintaining collateral, we maintain more stringent requirements to further reduce our exposure. We monitor our exposure to counterparty risk on a daily basis by using credit exposure information and monitoring collateral values. We maintain a credit committee, which reviews margin requirements for large or concentrated accounts and sets higher requirements or requires a reduction of either the level of margin debt or investment in high-risk securities or, in some cases, requires the transfer of the account to another broker-dealer.

We monitor our market and credit risks daily through internal control procedures designed to identify and evaluate the various risks to which we are exposed. There can be no assurance, however, that our risk management procedures and internal controls will prevent losses from occurring as a result of such risks.

The following table shows the quoted market values of marketable securities we owned ("long"), securities we sold but have not yet purchased ("short"), and net positions as of June 30, 2011:

	Long	Short	Net
Corporate stocks	\$ 170,000	\$ 21,000	\$ 149,000
Government obligations	1,558,000	-	1,558,000
	\$ 1,728,000	\$ 21,000	\$ 1,707,000

## ITEM 4. CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures.

Disclosure controls and procedures are our controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act, is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding disclosure.

Based on our evaluation of disclosure controls and procedures (as defined in the Exchange Act Rules 13a-15(e) and 15d-15(e)) required by the Exchange Act Rules 13a-15(b) or 15d-15(b), our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were adequate and effective to ensure that material information relating to us and our consolidated subsidiaries would be made known to them by others within those entities, particularly during the period in which this quarterly report on Form 10-Q was being prepared.



Changes in internal controls.

There were no changes in our internal control over financial reporting during the quarter ended June 30, 2011, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II – OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

In September 2010, Ms. Lambeth, a Florida resident, sent a letter alleging that her accounts at NSC had experienced significant declines based on unsuitable, high risk investments recommended by Eric Elliott, a broker formerly registered with NSC. Ms. Lambeth sought damages of approximately \$3,400,000 in one account and \$250,000 in a trust account, on theory that Mr. Elliott was liable for them and that NSC is vicariously liable for Mr. Elliott's conduct. NSC denied all claims, and the parties reached a settlement for \$1,150,000 on August 10, 2011, of which the Company's Errors and Omissions policy will contribute \$1,000,000 (the policy per event limit) to the settlement. The Company has accounted for its contribution to this settlement (\$150,000) as of June 30, 2011.

Other than described above, there were no significant developments in our legal proceedings during the quarter ended June 30, 2011.

### ITEM 1A. RISK FACTORS

There are no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the fiscal year ended September 30, 2010.

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

### ITEM 4. (REMOVED AND RESERVED)

### ITEM 5. OTHER INFORMATION

None.

### ITEM 6. EXHIBITS

3.1 The Company's Certificate of Incorporation, as amended, previously filed as Exhibit 3.5 to Form 10-Q in May 2004, and hereby incorporated by reference.

3.2 The Company's Bylaws, as amended, previously filed as Exhibit 3.3 to Form 10-Q in February 2002, and hereby incorporated by reference.

31.1 Chief Executive Officer's Certificate pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Chief Financial Officer's Certificate pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Chief Executive Officer's Certificate pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Chief Financial Officer's Certificate pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101.INS\*\* XBRL Instance

101.SCH\*\* XBRL Taxonomy Extension Schema

101.CAL\*\* XBRL Taxonomy Extension Calculation

101.DEF\*\* XBRL Taxonomy Extension Definition

101.LAB\*\* XBRL Taxonomy Extension Labels

101.PRE\*\* XBRL Taxonomy Extension Presentation



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XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

SIGNATURES

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

NATIONAL HOLDINGS CORPORATION AND SUBSIDIARIES

August 15, 2011

By:

/s/ Mark Goldwasser  
Mark Goldwasser  
Chief Executive Officer

August 15, 2011

By:

/s/ Alan B. Levin  
Alan B. Levin  
Chief Financial Officer