

NATIONAL HOLDINGS CORP  
Form 10-Q  
August 14, 2009

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 Commission File  
June 30, 2009 Number 001-12629

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

Delaware 36-4128138  
(State or (I.R.S.  
other Employer  
jurisdiction of  
incorporation Identification  
or No.)  
organization)

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 12, 2009 there were 17,150,704 shares of the registrant's common stock outstanding.

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NATIONAL HOLDINGS CORPORATION  
FORM 10-Q  
QUARTERLY PERIOD ENDED JUNE 30, 2009

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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  
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

## ASSETS

|   | June 30,<br>2009 | September 30,<br>2008 |
|---|------------------|-----------------------|
|   | (unaudited)      | (see note<br>below)   |
| Cash  | \$ 5,921,000     | \$ 7,387,000          |
| Deposits with clearing organizations  | 1,261,000        | 1,210,000             |
| Receivables from broker dealers and clearing organizations  | 4,342,000        | 3,691,000             |
| Other receivables, net of allowance for uncollectible accounts of \$198,000 and \$164,000 at June 30, 2009 and September 30, 2008, respectively | 913,000          | 580,000               |
| Advances to registered representatives  | 3,529,000        | 4,463,000             |
| Securities owned - at fair market value   | 632,000          | 1,024,000             |
| Fixed assets, net   | 1,290,000        | 1,243,000             |
| Secured demand note   | 500,000          | 500,000               |
| Intangible assets, net  | 2,484,000        | 2,950,000             |
| Other assets  | 1,134,000        | 1,429,000             |
| Total Assets  | \$ 22,006,000    | \$ 24,477,000         |

## LIABILITIES AND STOCKHOLDERS' EQUITY

|   |            |            |
|---|------------|------------|
| Payable to broker dealers and clearing organizations  | \$ 279,000 | \$ 730,000 |
| Securities sold, but not yet purchased, at market   | 76,000     | 63,000     |
| Accounts payable, accrued expenses and other liabilities  | 13,356,000 | 12,335,000 |
| Convertible notes payable, net of debt discounts of \$1,135,000 and \$1,431,000 at June 30, 2009 and September 30, 2008, respectively | 4,865,000  | 4,569,000  |
| Notes payable, net of debt discount of \$0 and \$41,000 at June 30, 2009 and September 30, 2008, respectively                         | 500,000    | 959,000    |
| Total Liabilities   | 19,076,000 | 18,656,000 |

|                         |         |         |
|-------------------------|---------|---------|
| Subordinated borrowings | 600,000 | 500,000 |
|-------------------------|---------|---------|

## Stockholders' Equity

|   |   |   |
|---|---|---|
| Preferred stock, \$.01 par value, 200,000 shares authorized; 50,000 shares designated as Series A and 20,000 shares designated as Series B  |   |   |
| Series A 9% cumulative convertible preferred stock, \$.01 par value, 50,000 shares authorized; 42,957 shares issued and outstanding (liquidation preference: \$4,295,700) at June 30, 2009 and 37,550 shares issued and outstanding (liquidation preference: \$3,755,000) at September 30, 2008 | - | - |
| Series B 9% cumulative convertible preferred stock, \$.01 par value, 20,000 shares authorized; 0 shares issued and outstanding (liquidation preference: \$0) at June 30, 2009 and September 30, 2008  | - | - |
| Common stock, \$.02 par value, 50,000,000 shares authorized; 17,150,704   |   |   |

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shares issued and outstanding at June 30, 2009 and 16,421,538

|   |               |               |
|---|---------------|---------------|
| shares issued and outstanding at September 30, 2008 | 342,000       | 328,000       |
| Additional paid-in capital                          | 40,211,000    | 39,279,000    |
| Accumulated deficit                                 | (38,223,000)  | (34,286,000)  |
| Total Stockholders' Equity                          | 2,330,000     | 5,321,000     |
| Total Liabilities and Stockholders' Equity          | \$ 22,006,000 | \$ 24,477,000 |

Note: The balance sheet at September 30, 2008 has been derived from the audited consolidated financial statements at that date.

See accompanying notes to unaudited condensed consolidated financial statements

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NATIONAL HOLDINGS CORPORATION AND  
SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF  
OPERATIONS  
(Unaudited)

|  | ----- Three Months Ended ----- |                     | ----- Nine Months Ended ----- |                       |
|--|--------------------------------|---------------------|-------------------------------|-----------------------|
|  | June 30,<br>2009               | June 30,<br>2008    | June 30,<br>2009              | June 30,<br>2008      |
| <b>Revenues:</b>                                     |                                |                     |                               |                       |
| Commissions  | \$ 22,337,000                  | \$ 11,428,000       | \$ 50,308,000                 | \$ 34,644,000         |
| Net dealer inventory gains                           | 5,077,000                      | 3,202,000           | 19,016,000                    | 11,035,000            |
| Investment banking                                   | 896,000                        | 1,210,000           | 2,046,000                     | 1,277,000             |
| <b>Total commission and fee revenues</b>             | <b>28,310,000</b>              | <b>15,840,000</b>   | <b>71,370,000</b>             | <b>46,956,000</b>     |
| Interest and dividends                               | 252,000                        | 837,000             | 1,285,000                     | 2,647,000             |
| Transfer fees and clearing services                  | 3,847,000                      | 1,105,000           | 9,516,000                     | 3,378,000             |
| Other  | 1,121,000                      | 897,000             | 3,783,000                     | 2,347,000             |
| <b>Total Revenues</b>                                | <b>33,530,000</b>              | <b>18,679,000</b>   | <b>85,954,000</b>             | <b>55,328,000</b>     |
| <b>Expenses:</b>                                     |                                |                     |                               |                       |
| Commissions  | 26,061,000                     | 14,695,000          | 64,524,000                    | 43,449,000            |
| Employee compensation and related expenses           | 2,985,000                      | 1,786,000           | 9,029,000                     | 6,334,000             |
| Clearing fees  | 1,523,000                      | 541,000             | 3,890,000                     | 1,676,000             |
| Communications                                       | 1,245,000                      | 299,000             | 3,137,000                     | 907,000               |
| Occupancy and equipment costs                        | 954,000                        | 831,000             | 3,786,000                     | 2,564,000             |
| Professional fees                                    | 483,000                        | 546,000             | 1,790,000                     | 1,597,000             |
| Interest   | 291,000                        | 176,000             | 925,000                       | 319,000               |
| Taxes, licenses, registration                        | 414,000                        | 123,000             | 1,016,000                     | 330,000               |
| Other administrative expenses                        | 442,000                        | 591,000             | 1,795,000                     | 1,590,000             |
| <b>Total Expenses</b>                                | <b>34,398,000</b>              | <b>19,588,000</b>   | <b>89,892,000</b>             | <b>58,766,000</b>     |
| Net loss   | (868,000)                      | (909,000)           | (3,938,000)                   | (3,438,000)           |
| Preferred stock dividends                            | (96,000)                       | (84,000)            | (265,000)                     | (253,000)             |
| <b>Net loss attributable to common stockholders</b>  | <b>\$ (964,000)</b>            | <b>\$ (993,000)</b> | <b>\$ (4,203,000)</b>         | <b>\$ (3,691,000)</b> |
| <b>Net loss per common share</b>                     |                                |                     |                               |                       |
| <b>Basic:</b>  |                                |                     |                               |                       |
| Net loss attributable to common stockholders         | \$ (0.06)                      | \$ (0.12)           | \$ (0.25)                     | \$ (0.43)             |
| <b>Diluted:</b>                                      |                                |                     |                               |                       |
| Net loss attributable to common stockholders         | \$ (0.06)                      | \$ (0.12)           | \$ (0.25)                     | \$ (0.43)             |
| <b>Weighted average number of shares outstanding</b> |                                |                     |                               |                       |
| Basic  | 16,930,924                     | 8,622,628           | 16,635,442                    | 8,611,602             |
| Diluted  | 16,930,924                     | 8,622,628           | 16,635,442                    | 8,611,602             |

See accompanying notes to unaudited condensed consolidated financial  
statements



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

|  | Nine Months Ended<br>June 30, |                |
|--|-------------------------------|----------------|
|  | 2009                          | 2008           |
| Cash flows from operating activities   |                               |                |
| Net loss   | \$ (3,938,000)                | \$ (3,438,000) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities |                               |                |
| Depreciation and amortization  | 1,017,000                     | 146,000        |
| Amortization of deferred financing costs   | 41,000                        | 15,000         |
| Amortization of note discount  | 296,000                       | 98,000         |
| Compensatory element of common stock options issuance                                    | 678,000                       | 361,000        |
| Unrealized loss on securities owned  | (142,000)                     | -              |
| Changes in assets and liabilities  |                               |                |
| Deposits with clearing organizations   | (51,000)                      | -              |
| Receivables from broker-dealers, clearing organizations and others                       | (651,000)                     | 891,000        |
| Other receivables  | (333,000)                     | -              |
| Advances to registered representatives   | 934,000                       | -              |
| Securities owned: marketable, at market value  | 541,000                       | 850,000        |
| Securities owned: non-marketable, at fair value  | (7,000)                       | -              |
| Other assets   | 295,000                       | (133,000)      |
| Accounts payable and accrued expenses  | 1,022,000                     | (3,748,000)    |
| Payable to broker dealers and clearing organizations                                     | (451,000)                     | -              |
| Securities sold, but not yet purchased, at market  | 13,000                        | 229,000        |
| Net cash used in operating activities  | (736,000)                     | (4,729,000)    |
| Cash flows from investing activities   |                               |                |
| Purchase of fixed assets   | (598,000)                     | (142,000)      |
| Net cash used in investing activities  | (598,000)                     | (142,000)      |
| Cash flows from financing activities   |                               |                |
| Repayment of notes payable   | (500,000)                     | -              |
| Net proceeds from issuance of convertible notes payable                                  | -                             | 6,000,000      |
| Net proceeds from subordinated borrowings  | 100,000                       | -              |
| Proceeds from sale of common stock   | 502,000                       | (181,000)      |
| Costs associated with sale of common stock   | (234,000)                     | (449,000)      |
| Exercise of stock options  | -                             | 8,000          |
| Net cash (used in) provided by financing activities                                      | (132,000)                     | 5,378,000      |
| Net decrease (increase) in cash  | (1,466,000)                   | 507,000        |
| Cash balance   |                               |                |
| Beginning of the period  | 7,387,000                     | 4,957,000      |
| End of the period  | \$ 5,921,000                  | \$ 5,464,000   |

## Supplemental disclosures of cash flow information

Cash paid during the period for:

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|  |    |         |    |           |
|--|----|---------|----|-----------|
| Interest   | \$ | 574,000 | \$ | 162,000   |
| Income taxes   | \$ | 80,000  | \$ | 37,000    |
| Supplemental disclosures of noncash financing activities |    |         |    |           |
| Warrants issued in connection with debt                  | \$ | -       | \$ | 1,184,000 |
| Preferred stock dividends                                | \$ | 676,000 | \$ | -         |

See accompanying notes to unaudited condensed consolidated financial statements

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NATIONAL HOLDINGS CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2009  
(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 condensed consolidated financial statements as of June 30, 2009 and for the periods ended June 30, 2009 and June 30, 2008 are unaudited. The results of operations for the interim periods are not necessarily indicative of the results of operations for the fiscal year. These condensed 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, 2008.

NOTE 2. CONSOLIDATION

The condensed 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 brokerage servicing approximately 45,000 accounts, consisting of retail, 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 3,500 micro and small cap 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”). vFinance Investments is also a member 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 2008, 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 second 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. RECENT ACCOUNTING PRONOUNCEMENTS

In December 2007, the FASB issued SFAS No. 141 (revised 2007), “Business Combinations” (“SFAS 141(R)”), which is a revision of SFAS 141, “Business Combinations”. The primary requirements of SFAS 141(R) are as follows:

- upon initially obtaining control, the acquiring entity in a business combination must recognize 100% of the fair values of the acquired assets, including goodwill, and assumed liabilities, with only limited exceptions even if the acquirer has not acquired 100% of its target—as a consequence, the current step acquisition model will be eliminated;
- contingent consideration arrangements will be fair valued at the acquisition date and included in the purchase price consideration—the concept of recognizing contingent consideration at a later date when the amount of that consideration is determinable beyond a reasonable doubt will no longer be applicable;
- for prior business combinations, adjustments for recognized changes in acquired tax uncertainties are to be recognized in accordance with the provisions of FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes — An Interpretation of FASB No. 109,” and adjustments for recognized changes in the valuation allowance for acquired deferred tax assets are to be recognized in income tax expense in accordance with the provisions of SFAS No. 109, “Accounting for Income Taxes;” and
- all transaction costs will be expensed as incurred.

In April 2009, the FASB issued FSP No. FAS 141(R)-1, “Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies” (“FSP FAS 141(R)-1”). FSP FAS 141(R)-1 amends and clarifies SFAS 141(R) to address application issues raised about the initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination. SFAS 141(R) and FSP FAS 141(R)-1 apply prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008.

In December 2007, the FASB issued SFAS No. 160, “Non-controlling Interests in Consolidated Financial Statements — An Amendment of ARB No. 51” (“SFAS 160”). SFAS 160 establishes new accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 requires non-controlling interests or minority interests to be treated as a separate component of equity and any changes in the parent’s ownership interest (in which control is retained) are to be accounted for as equity transactions. However, a change in ownership of a consolidated subsidiary that results in deconsolidation triggers gain or loss recognition, with the establishment of a new fair value basis in any remaining non-controlling ownership interests. SFAS 160 also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the non-controlling interests. SFAS 160 is effective for fiscal years beginning on or after December 15, 2008. We are currently evaluating the impact that the adoption of SFAS 160 will have on our financial condition, results of operations, and disclosures.

In April 2008, the FASB issued FSP No. FAS 142-3, “Determination of the Useful Life of Intangible Assets” (“FSP FAS 142-3”). FSP FAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, “Goodwill and Other Intangible Assets” (“SFAS 142”). The intent of the position is to improve the consistency between the useful life of a recognized intangible asset under SFAS 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141(R), and other GAAP. FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008. We are currently evaluating the impact that the adoption of FSP FAS 142-3 will have on our financial condition,

results of operations and disclosures.

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NOTE 3. RECENT ACCOUNTING PRONOUNCEMENTS

-Continued-

In May 2008, the FASB issued SFAS No. 162, “The Hierarchy of Generally Accepted Accounting Principles” (“SFAS 162”). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP. This statement is not expected to change existing practices but rather reduce the complexity of financial reporting. This statement was effective 60 days following the Securities and Exchange Commission’s approval of the Public Company Accounting Oversight Board amendments to AU Section 411, “The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles.” The provisions in SFAS 162 did not have a material impact on our financial condition, results of operations, or disclosures.

In June 2008, the FASB issued FSP No. Emerging Issues Task Force (“EITF”) 03-6-1, “Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities” (“FSP EITF 03-6-1”). FSP EITF 03-6-1 clarifies whether unvested share-based payment awards that entitle holders to receive non-forfeitable dividends or dividend equivalents (whether paid or unpaid) are considered participating securities and should be included in the computation of earnings per share pursuant to the two-class method. The two-class method of computing earnings per share is an earnings allocation formula that determines earnings per share for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. FSP EITF 03-6-1 requires retrospective application and is effective for fiscal years beginning after December 15, 2008, and interim periods within those years. We do not believe the adoption of FSP EITF 03-6-1 will have a material impact on our calculation of earnings per share and related disclosures.

In April 2009, in response to the current credit crisis, FASB issued three new FSPs to address fair value measurement concerns as follows:

- FSP No. FAS 157-4, “Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly” (“FSP FAS 157-4”), provides additional guidance on measuring the fair value of financial instruments when market activity has decreased and quoted prices may reflect distressed transactions;
- FSP No. FAS 115-2 and FAS 124-2, “Recognition and Presentation of Other-Than-Temporary Impairments” (“FSP FAS 115-2 and 124-2”), amends the other-than-temporary impairment guidance for debt securities. Under FSP FAS 115-2 and 124-2, an other-than-temporary impairment is now triggered when there is intent to sell the security, it is more likely than not that the security will be required to be sold before recovery in value, or the security is not expected to recover the entire amortized cost basis of the security. If an entity does not intend to sell the security, credit related losses on debt securities that exist will be considered an other-than-temporary impairment recognized in earnings, and any other losses due to a decline in fair value relative to the amortized cost deemed not to be other-than-temporary will be recorded in other comprehensive income; and
- FSP No. FAS 107-1 and APB No. 28-1, “Interim Disclosures about Fair Value of Financial Instruments” (“FSP FAS 107-1 and APB 28-1”), expands the fair value disclosures required for financial instruments to interim reporting periods for publicly traded companies, including disclosure of the significant assumptions used to estimate the fair value of those financial instruments.





NOTE 3. RECENT ACCOUNTING PRONOUNCEMENTS

-Continued-

FSP 157-4 and FSP FAS 115-2 and 124-2 are effective for interim and annual periods ending after June 15, 2009 and are effective for us during our annual period ending August 31, 2009. FSP FAS 107-1 and APB 28-1 is effective for interim periods ending after June 15, 2009. Early adoption is permitted for periods ending after March 15, 2009 only if all three FSPs are adopted together. We have not elected to early adopt these FSPs. We do not believe that the adoption of FSP FAS 157-4, FSP FAS 115-2 and 124-2, and FSP FAS 107-1 and APB 28-1 will have a material impact on our financial condition, results of operations, and disclosures.

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events" ("SFAS 165"), which provides guidance to establish general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. SFAS 165 also requires entities to disclose the date through which subsequent events were evaluated as well as the rationale for why that date was selected. SFAS 165 is effective for interim and annual periods ending after June 15, 2009. We do not believe that the adoption of SFAS 165 will have a material impact on our financial condition, results of operations, and disclosures.

In June 2009, the FASB issued SFAS No. 166, "Accounting for Transfers of Financial Assets — an amendment of FASB Statement No. 140" ("SFAS 166"), which requires additional information regarding transfers of financial assets, including securitization transactions, and where companies have continuing exposure to the risks related to transferred financial assets. SFAS 166 eliminates the concept of a "qualifying special-purpose entity," changes the requirements for derecognizing financial assets, and requires additional disclosures. SFAS 166 is effective for fiscal years beginning after November 15, 2009. We are currently evaluating the impact that the adoption of SFAS 166 will have on our financial condition, results of operations, and disclosures.

In June 2009, the FASB issued SFAS No. 167, "Amendments to FASB Interpretation No. 46(R)" ("SFAS 167"), which modifies how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. SFAS 167 clarifies that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly impact the entity's economic performance. SFAS 167 requires an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity. SFAS 167 also requires additional disclosures about a company's involvement in variable interest entities and any significant changes in risk exposure due to that involvement. SFAS 167 is effective for fiscal years beginning after November 15, 2009. We are currently evaluating the impact that the adoption of SFAS 167 will have on our financial condition, results of operations, and disclosures.

In June 2009, the FASB approved the "FASB Accounting Standards Codification" ("Codification") as the single source of authoritative nongovernmental U.S. GAAP to be launched on July 1, 2009. The Codification does not change current U.S. GAAP, but is intended to simplify user access to all authoritative U.S. GAAP by providing all the authoritative literature related to a particular topic in one place. All existing accounting standard documents will be superseded and all other accounting literature not included in the Codification will be considered non-authoritative. The Codification is effective for interim and annual periods ending after September 15, 2009. The Codification will not have an impact on our financial condition or results of operations. We are currently evaluating the impact to our financial reporting process of providing Codification references in our public filings.

## NOTE 4. STOCK BASED COMPENSATION

Effective October 1, 2005, the Company adopted FASB Statement of Financial Accounting Standard (“SFAS”) No. 123R “Share Based Payment.” This statement is a revision of SFAS Statement No. 123 and supersedes APB Opinion No. 25, and its related implementation guidance. SFAS 123R 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 SFAS 123R, 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 Company granted 40,000 and 180,000 options during the nine months ended June 30, 2009 and June 30, 2008, respectively. A charge of approximately \$237,000 and \$710,000 was recorded in the three and nine months ended June 30, 2009, respectively, and a charge of approximately \$149,000 and \$361,000 was recorded in the three and nine months ended June 30, 2008, respectively, relating to the amortization of the fair value associated with stock option grants and restricted stock grants.

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. In management's opinion, this valuation model does not necessarily provide a reliable single measure of the fair value of its employee stock options.

A summary of the stock option activity as of June 30, 2009, and changes during the nine month period then ended is presented below:

|                                   | Shares    | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term (Yrs) | Aggregate<br>Intrinsic<br>Value |
|-----------------------------------|-----------|--|---|---------------------------------|
| Outstanding at September 30, 2008 | 6,887,640 | \$ 1.58                                  | 3.98  | \$ -                            |
| Granted                           | 50,000    | \$ 0.64                                  | 5.00  |                                 |
| Expired                           | 467,675   | \$ 1.52                                  | 0.95  |                                 |
| Outstanding at June 30, 2009      | 6,469,965 | \$ 1.58                                  | 3.38  | \$ -                            |
| Exerciseable at June 30, 2009     | 3,372,524 | \$ 1.48                                  | 2.46  | \$ -                            |

As of June 30, 2009, there was approximately \$1,000,000 of total unrecognized deferred compensation costs related to share-based compensation arrangements. The Company has experienced a historic forfeiture rate of approximately 38% on previously granted stock options and expects that future forfeitures will be consistent with this experience.

## NOTE 4. STOCK BASED COMPENSATION

- Continued -

A summary of the status of the Company's non-vested shares as of June 30, 2009, and changes during the three month period then ended is presented below:

| Nonvested Shares                | Shares    | Weighted<br>Average<br>Grant Date<br>Fair Value |
|---------------------------------|-----------|---|
| Nonvested at September 30, 2008 | 3,828,774 | \$ 0.92   |
| Granted                         | 50,000    | 0.61  |
| Vested                          | (489,131) | 0.85  |
| Expired                         | (292,202) | 0.92  |
| Nonvested at June 30, 2009      | 3,097,441 | 0.79  |

## NOTE 5. SECURITIES OWNED AND SECURITIES SOLD, BUT NOT YET PURCHASED

The following table shows the quoted market values of securities owned by the Company as of June 30, 2009 and September 30, 2008 respectively:

|                        | Securities owned |                       |
|------------------------|------------------|-----------------------|
|                        | June 30, 2009    | September 30,<br>2008 |
| Corporate stocks       | \$ 88,000        | \$ 454,000            |
| Corporate bonds        | 68,000           | 6,000                 |
| Government obligations | 422,000          | 516,000               |
| Restricted Securities  | 54,000           | 48,000                |
|                        | \$ 632,000       | \$ 1,024,000          |

The following table shows the quoted market values of securities sold, but not yet purchased by the Company as of June 30, 2009 and September 30, 2008 respectively:

|                        | Securities sold, but<br>not yet purchased |                       |
|------------------------|---|-----------------------|
|                        | June 30, 2009                             | September 30,<br>2008 |
| Corporate stocks       | \$ 76,000                                 | \$ 9,000              |
| Corporate bonds        | -   | 10,000                |
| Government obligations | -   | 44,000                |
|                        | \$ 76,000                                 | \$ 63,000             |

## NOTE 5. SECURITIES OWNED AND SECURITIES SOLD, BUT NOT YET PURCHASED

- Continued -

## Fair Value Measurements

As of June 30, 2009

## Securities owned at fair value

|                        | Level 1    | Level 2   | Level 3 | Total      |
|------------------------|------------|-----------|---------|------------|
| Corporate stocks       | \$ 88,000  | \$ -      | \$ -    | \$ 88,000  |
| Corporate bonds        | 68,000     | -         | -       | 68,000     |
| Government obligations | 422,000    | -         | -       | 422,000    |
| Restricted stock       | -          | 54,000    | -       | 54,000     |
|                        | \$ 578,000 | \$ 54,000 | \$ -    | \$ 632,000 |

## Securities sold, but not yet purchased at fair value

|                        | Level 1   | Level 2 | Level 3 | Total     |
|------------------------|-----------|---------|---------|-----------|
| Corporate stocks       | \$ 76,000 | \$ -    | \$ -    | \$ 76,000 |
| Corporate bonds        | -         | -       | -       | -         |
| Government obligations | -         | -       | -       | -         |
|                        | \$ 76,000 | \$ -    | \$ -    | \$ 76,000 |

As of September 30, 2008

## Securities owned at fair value

|                        | Level 1    | Level 2   | Level 3 | Total        |
|------------------------|------------|-----------|---------|--------------|
| Corporate stocks       | \$ 454,000 | \$ -      | \$ -    | \$ 454,000   |
| Corporate bonds        | 6,000      | -         | -       | 6,000        |
| Government obligations | 516,000    | -         | -       | 516,000      |
| Restricted stock       | -          | 48,000    | -       | 48,000       |
|                        | \$ 976,000 | \$ 48,000 | \$ -    | \$ 1,024,000 |

| Securities sold, but<br>not yet purchased at fair<br>value | Level 1   | Level 2 | Level 3 | Total     |
|--|-----------|---------|---------|-----------|
| Corporate stocks   | \$ 9,000  | \$ -    | \$ -    | \$ 9,000  |
| Corporate bonds  | 10,000    | -       | -       | 10,000    |
| Government obligations                                     | 44,000    | -       | -       | 44,000    |
|  | \$ 63,000 | \$ -    | \$ -    | \$ 63,000 |

## NOTE 6. COMMITMENTS AND CONTINGENCIES

### Operating Leases

In February 2009, the Company's office lease on its Military Trail office in Boca Raton, Florida had expired. Thereafter, the Company made arrangements with the landlord of this space to holdover until April 30, 2009 paying rent on a month to month basis at the then current rate per square foot.

In March 2009, the Company negotiated a simultaneous termination of its existing lease for the 1200 North Federal Highway Location and a new lease for the same space. This resulted in a savings of approximately \$350,000. The Company relocated all of its employees from its Military Trail office to this location in May. The new lease terminates on August 15, 2015 and the Landlord provided a rent holiday for the first four months of the lease and reimbursement of build-out costs to a maximum of \$150,000.

### Litigation and Regulatory Matters

On March 4, 2008, vFinance received a customer arbitration (FINRA Case No.08-00472) from Donald and Patricia Halfmann, alleging that Jeff Lafferty, a former registered representative of vFinance, misappropriated approximately \$110,000 of the Halfmanns' funds via check alteration, and that vFinance ought to be liable for an additional \$150,000 for other dishonest and fraudulent acts committed after he left vFinance. On August 6, 2009 the arbitrators' ruled that vFinance Investments must pay for losses, interest, attorneys costs and punitive damages totaling approximately \$780,000. The firm has made a claim against its fidelity bond carrier, and is completing its analysis as to whether to seek to have the entire arbitration award, or any part of that award, vacated.

In October, 2008, vFinance and others were named as defendants in a civil action (Case No. 09-CV-9008 United Stated District Court, Southern District of New York), wherein The Pinnacle Fund, L.P. and others alleged securities law violations and other causes of action stemming from a private placement transaction into a public company which vFinance acted as placement agent. Plaintiffs alleged damages in excess of \$12,000,000 in compensatory damages. vFinance asserted its indemnification rights against a one of the co-defendants, and has thus far received reimbursement of most of the attorneys fees and costs incurred. The parties have reached a settlement and the action was dismissed with prejudice and vFinance Investments, Inc. was indemnified as to all costs in this matter.

The Company's subsidiaries are defendants in various arbitrations and administrative proceedings, lawsuits and claims together alleging damages in excess of \$11,100,000. The Company estimates, to the extent that it can, that based on discussions with legal counsel and prior experience, its aggregate liability from these pending actions may be less than \$450,000 (exclusive of fees, costs and unspecified punitive damages related to certain claims and inclusive of expected insurance coverage). These matters arise in the normal course of business. The Company intends to vigorously defend itself in these actions, and based on discussions with counsel 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, 2009 and 2008, is \$290,000 and \$40,000 (inclusive of legal fees and estimated claims), 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 \$176,000 and \$170,000 for the third quarter of fiscal year 2009 and 2008, respectively, and \$460,000 and \$660,000 for the first nine months of fiscal year 2009 and 2008, respectively.

## NOTE 7. DIVIDENDS ON CONVERTIBLE 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. In the quarter and nine months ended June 30, 2009, the Company accumulated \$96,000 and \$265,000, respectively, of dividends on its Series A preferred stock. In March 2009, the Company's Board of Directors declared an in-kind dividend in the aggregate of 5,407 shares of Series A preferred stock, in payment of approximately \$676,000 of dividends accrued through March 31, 2009. At June 30, 2009, the accumulated dividend on the Company's 42,957 issued and outstanding shares of Series A preferred stock was \$96,000.

## NOTE 8. LOSS PER COMMON SHARE

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

For both the three and nine month periods ended June 30, 2009, 12,163,057 common share equivalents were excluded from the calculation of diluted net loss per share because their inclusion would have been anti-dilutive. For both the three and nine month periods ended June 30, 2008, 10,014,750 common share equivalents were excluded from the calculation of diluted net loss per share because their inclusion would have been anti-dilutive.

The following table sets forth the common share equivalents that were excluded from the calculation:

|   | Three Months Ended |                   | Nine Months Ended |                   |
|---|--------------------|-------------------|-------------------|-------------------|
|   | June 30,<br>2009   | June 30,<br>2008  | June 30,<br>2009  | June 30,<br>2008  |
| Stock options                           | 3,373,524          | 2,092,000         | 3,373,524         | 2,092,000         |
| Warrants                                | 1,977,973          | 1,543,750         | 1,977,973         | 1,543,750         |
| Assumed conversion of:                  |                    |                   |                   |                   |
| Series A Preferred Stock                | 3,436,560          | 3,004,000         | 3,436,560         | 3,004,000         |
| Notes                                   | 3,375,000          | 3,375,000         | 3,375,000         | 3,375,000         |
| <b>Dilutive potential common shares</b> | <b>12,163,057</b>  | <b>10,014,750</b> | <b>12,163,057</b> | <b>10,014,750</b> |

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

Accounts payable, accrued expenses and other liabilities as of June 30, 2009 and September 30, 2008, respectively, consist of the following:

|                                    | June 30, 2009        | September 30,<br>2008 |
|------------------------------------|----------------------|-----------------------|
| Commissions payable                | \$ 7,198,000         | \$ 6,537,000          |
| Deferred clearing fee credits      | 508,000              | 578,000               |
| Telecommunications vendors payable | 176,000              | 209,000               |
| Legal payable                      | 758,000              | 646,000               |
| Deferred rent payable              | 259,000              | 313,000               |
| Accrued compensation               | 651,000              | 679,000               |
| Capital lease liability            | 778,000              | 613,000               |
| Other vendors                      | 3,028,000            | 2,760,000             |
| <b>Total</b>                       | <b>\$ 13,356,000</b> | <b>\$ 12,335,000</b>  |

## NOTE 10. 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. The alternative method precludes National Securities from having to maintain a ratio of aggregate indebtedness to net capital. At June 30, 2009, National Securities had net capital of approximately \$542,000 which exceeded its requirement by approximately \$261,000.

Due to its market maker status, vFinance Investments is required to maintain a minimum net capital of \$1,000,000 and EquityStation is required to maintain \$100,000. 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, 2009, vFinance Investments had net capital of approximately \$1,421,000 which was approximately \$421,000 in excess of its required net capital of \$1,000,000 and its percentage of aggregate indebtedness to net capital was 471%. At June 30, 2009, EquityStation had net capital of approximately \$211,000 which was approximately \$111,000 in excess of its required net capital of \$100,000 and its percentage of aggregate indebtedness to net capital was 251%. 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 11. PRO FORMA

Had the acquisition of vFinance, Inc. occurred on October 1, 2007, the results would have been as follows:

|   | For the nine<br>months ended<br>June 30, 2008 |
|---|---|
| Total Revenue                           | \$ 94,172,000                                 |
| Net loss                                | (7,544,000)                                   |
| Basic and diluted loss per common share | (0.71)  |

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

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, 2008. 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") and EquityStation, Inc. ("EquityStation", and collectively with National Securities and vFinance Investments, 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 is a member of the Securities Investor Protection Corporation ("SIPC"). vFinance Investments is 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, 2009, we had approximately 918 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 84 other registered offices are owned and operated by independent owners who maintain all appropriate licenses and are responsible for all office overhead and expenses. Because these independent operators, many of whom are financial planners, are required to pay their own expenses, we generally pay them a much greater percentage of the commissions and fee income they generate, typically 70% - 90%.

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.

#### Difficult Market Conditions

The U.S. and global economies have continued to deteriorate and are now in a recession, which could be long-term. We, like other companies in the financial services sector, are exposed to volatility and trends in the securities markets and the economy, generally. The market downturn and poor economic conditions have reduced overall investment banking and client activity levels. It is difficult to predict when conditions will change. Given difficult market and economic conditions, we have focused on reducing redundancies and unnecessary expense. At the same time, however, we continue to seek to selectively upgrade our talent pool given the availability of experienced professionals.

#### 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 shareholders and/or may increase our leverage. 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.

#### Acquisition of vFinance, Inc.

In July 2008, we acquired vFinance, Inc. through a merger with a newly formed wholly-owned subsidiary. The assets and liabilities acquired as well as the financial results of vFinance were included in our consolidated financial statements after the close of business on July 1, 2008, the acquisition date. The aggregate acquisition price was approximately \$17.6 million, which consisted of approximately 7,788,910 shares of Company common stock issued in exchange for all of the issued and outstanding common stock of vFinance, and direct expenses of \$0.6 million in legal fees, valuation fees, severance costs and contract cancellation costs. We accounted for the acquisition of vFinance under the provisions of Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 141 "Business Combinations."

Since July 1, 2008, our management team has been focused on the task of eliminating duplicative overhead and services, and eliminating unnecessary costs in an effort to improve bottom line performance. As of the date of this report, the Company has made considerable progress on cost cutting measures, and these savings are exceeding \$6 million dollars on an annualized basis. We fully intend to continue our efforts to conserve capital and keep costs low in an effort to improve the Company's profitability.



## RESULTS OF OPERATIONS

Three Months Ended June 30, 2009 Compared to Three Months Ended June 30, 2008

The Company's third quarter of fiscal year 2009 resulted in an increase in revenues, but a greater increase in expenses compared to the same period last year. As a result, the Company reported a net loss of \$868,000 compared with a net loss of \$909,000 for the third quarters of fiscal years 2009 and 2008, respectively.

|                                      | Three Months Ended |               | Increase (Decrease) |         |
|--------------------------------------|--------------------|---------------|---------------------|---------|
|                                      | 2009               | 2008          | Amount              | Percent |
| Commissions                          | \$ 22,337,000      | \$ 11,428,000 | \$ 10,909,000       | 95%     |
| Net dealer inventory gains           | 5,077,000          | 3,202,000     | 1,875,000           | 59%     |
| Investment banking                   | 896,000            | 1,210,000     | (314,000)           | -26%    |
| Interest and dividends               | 252,000            | 837,000       | (585,000)           | -70%    |
| Transfer fees and clearance services | 3,847,000          | 1,105,000     | 2,742,000           | 248%    |
| Other                                | 1,121,000          | 897,000       | 224,000             | 25%     |
|                                      | \$ 33,530,000      | \$ 18,679,000 | \$ 14,851,000       | 80%     |

Total revenues increased \$14,851,000, or 80%, in the third quarter of fiscal year 2009 to \$33,530,000 from \$18,679,000 in the third quarter of fiscal year 2008. Commission revenue increased \$10,909,000, or 95%, to \$22,337,000 from \$11,428,000 during the third quarter of fiscal year 2009 compared with the same period in fiscal year 2008. Net dealer inventory gains which includes profits on proprietary trading, market making activities and customer mark-ups and mark-downs, increased \$1,875,000, or 59%, to \$5,077,000 from \$3,202,000 during the third quarter of fiscal year 2009 compared with the same period in fiscal year 2008. The increase in total revenues, commission revenues and net dealer inventory gains were all primarily due to the addition of vFinance revenues as a result of the merger.

Investment banking revenue decreased \$314,000, or 26%, in the third quarter of fiscal year 2009 to \$896,000 from \$1,210,000 in the third quarter of fiscal year 2008. This decrease in revenues was primarily attributed to less favorable market conditions during the quarter in comparison to the same quarter of last year. The Company completed a capital raise during the third quarter of 2009, and received modest fee income. Interest and dividend income decreased by \$585,000 or 70%, to \$252,000 from \$837,000 in the third quarter of fiscal year 2009 compared with the same period last year. The decrease in interest income is attributable to generally lower customer margin account balances, lower customer free cash balances and lower prevailing interest rates during the quarter. Transfer fees and clearance service fee income increased \$2,742,000 or 248%, to \$3,847,000 in the third quarter of fiscal year 2009 from \$1,105,000 in the third quarter of fiscal year 2008. The increase is due primarily to the addition of vFinance revenues as a result of the merger.

Other revenue, consisting of asset management fees, miscellaneous transaction fees and trading fees and other investment income, increased \$224,000, or 25%, to \$1,121,000 from \$897,000 during the third quarter of fiscal year 2009 compared to the third quarter of fiscal year 2008. The increase is due primarily to the addition of vFinance revenues as a result of the merger.

In comparison with the 80% increase in total revenues, total expenses increased 76% or \$14,810,000 to \$34,398,000 for the third quarter of fiscal year 2009 compared to \$19,588,000 in the third quarter of fiscal year 2008. The increase in total expenses is primarily a result of the addition of vFinance expenses as a result of the merger.

|                                  | Three Months Ended |               | Increase (Decrease) |         |
|----------------------------------|--------------------|---------------|---------------------|---------|
|                                  | 2009               | 2008          | Amount              | Percent |
| Commissions                      | \$ 26,061,000      | \$ 14,695,000 | \$ 11,366,000       | 77%     |
| Employee compensation            | 2,985,000          | 1,786,000     | 1,199,000           | 67%     |
| Clearing fees                    | 1,523,000          | 541,000       | 982,000             | 182%    |
| Communications                   | 1,245,000          | 299,000       | 946,000             | 316%    |
| Occupancy and equipment costs    | 954,000            | 831,000       | 123,000             | 15%     |
| Professional fees                | 483,000            | 546,000       | (63,000)            | -12%    |
| Interest                         | 291,000            | 176,000       | 115,000             | 65%     |
| Taxes, licenses and registration | 414,000            | 123,000       | 291,000             | 237%    |
| Other administrative expenses    | 442,000            | 591,000       | (149,000)           | -25%    |
|                                  | \$ 34,398,000      | \$ 19,588,000 | \$ 14,810,000       | 76%     |

Commission expense, which primarily includes expenses related to commission revenue, net dealer inventory gains and investment banking, increased \$11,366,000, or 77%, to \$ 26,061,000 in the third quarter of fiscal year 2009 from \$14,695,000 in the third quarter of fiscal year 2008. The increase is primarily attributable to an increase in the related commission revenues from the vFinance merger and is consistent with the increase in commission revenues. Commission expense includes the amortization of advances to registered representatives of \$391,000 and \$240,000 for the third quarter of fiscal years 2009 and 2008, 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 our Broker Dealer Subsidiaries.

Employee compensation expense increased \$1,199,000, or 67%, to \$2,985,000 in the third quarter of fiscal year 2009 from \$1,786,000 in the third quarter of fiscal year 2008. The increase is primarily attributable to costs from vFinance due to the merger. Employee compensation includes the amortization of the fair value associated with stock based compensation of \$237,000 and \$149,000 in third quarter of fiscal years 2009 and 2008, respectively. Overall, combined commission and employee compensation expense, as a percentage of total revenue decreased to 87% from 88% in the third quarter of fiscal year 2009 and 2008, respectively as a result of cost cutting plans implemented due to economic conditions.

Clearing fees increased \$982,000 or 182%, to \$1,523,000 in the third quarter of fiscal year 2009 from \$541,000 in the third quarter of fiscal year 2008. The increase in clearing fees is primarily attributable to costs from vFinance due to the merger. The greater increase in clearing fees as compared to the increase in commission revenue is attributable to lower average commission revenue per ticket in the third quarter of fiscal year 2009 and new fees charged by the Company's clearings firms.

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Communication expenses increased \$946,000 or 316%, to \$1,245,000 from \$299,000 in the third quarter of fiscal year 2009 compared to the third quarter of fiscal year 2008. The increase is partly due to costs from vFinance due to the merger and the need for additional network connectivity between corporate offices. Occupancy costs increased \$123,000, or 15%, to \$954,000 from \$831,000 in the third quarter of fiscal year 2009 compared to the third quarter of fiscal year 2008. The increase in occupancy expense is due to annual rent increases contained in the Company's office leases and the addition of rented office space due to the vFinance merger. The Company anticipates a savings of in excess of \$600,000 on an annualized basis as a result of eliminating one of its leased spaces in Boca Raton, Florida in May 2009.

Professional fees decreased \$63,000, or 12%, to \$483,000 from \$546,000 in the third quarter of fiscal year 2009 compared to the third quarter of fiscal year 2008. The decrease in professional fees is primarily a result of higher than normal professional fees in the third quarter of 2008 due to legal costs incurred in the defense of an arbitration, in addition to costs incurred for the merger and the filing of a registration statement.

Interest expense increased \$115,000, or 65%, to \$291,000 from \$176,000 in the third quarter of fiscal year 2009 compared to the third quarter of fiscal year 2008. The increase in interest expense is attributable to new convertible notes issued in June of fiscal year 2008. Included in interest expense is the amortization of deferred financing costs of \$110,000 and \$58,000 for the third quarter of fiscal years 2009 and 2008, respectively. Taxes, licenses and registration increased \$291,000, or 237%, to \$414,000 from \$123,000 in the third quarter of fiscal year 2009 compared to the third quarter of fiscal year 2008. The increase in taxes, licenses and registration is due to primarily to costs from vFinance due to the merger. Other administrative expenses decreased \$149,000 or 25% to \$442,000 from \$591,000 in the third quarter of fiscal year 2009 compared to the third quarter of fiscal year 2008. The decrease is primarily attributable to costs from vFinance due to the merger.

The Company reported a net loss of \$868,000 in the third quarter of fiscal year 2009 compared to a net loss of \$909,000 in the third quarter of fiscal year 2008. The net loss attributable to common stockholders in the third quarter of fiscal year 2009 was \$964,000, or \$0.06 per common share, as compared to a net loss attributable to common stockholders in the third quarter of fiscal year 2008 of \$993,000, or \$.12 per common share. The net loss attributable to common stockholders for the third quarter of fiscal year 2009 and 2008 reflects \$96,000 and \$84,000, respectively, of cumulative preferred stock dividends on the Company's preferred stock.

Nine Months Ended June 30, 2009 Compared to Nine Months Ended June 30, 2008

The Company's first nine months of fiscal year 2009 resulted in an increase in revenues, but a greater increase in expenses compared to the same period last year. As a result, the Company reported a net loss of \$3,937,000 compared with a net loss of \$3,438,000 for the first nine months of fiscal years 2009 and 2008, respectively.

|                                      | Nine Months Ended |               | Increase (Decrease) |         |
|--------------------------------------|-------------------|---------------|---------------------|---------|
|                                      | 2009              | 2008          | Amount              | Percent |
| Commissions                          | \$ 50,308,000     | \$ 34,644,000 | \$ 15,664,000       | 45%     |
| Net dealer inventory gains           | 19,016,000        | 11,035,000    | 7,981,000           | 72%     |
| Investment banking                   | 2,046,000         | 1,277,000     | 769,000             | 60%     |
| Interest and dividends               | 1,285,000         | 2,647,000     | (1,362,000)         | -51%    |
| Transfer fees and clearance services | 9,516,000         | 3,378,000     | 6,138,000           | 182%    |
| Other                                | 3,783,000         | 2,347,000     | 1,436,000           | 61%     |
|                                      | \$ 85,954,000     | \$ 55,328,000 | \$ 30,626,000       | 55%     |





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Total revenues increased \$30,626,000, or 55%, in the first nine months of fiscal year 2009 to \$85,954,000 from \$55,328,000 in the first nine months of fiscal year 2008. The increase in revenues is due primarily to the addition of vFinance revenues as a result of the merger. Commission revenue increased \$15,664,000, or 45%, to \$50,308,000 from \$34,644,000 during the first nine months of fiscal year 2009 compared with the same period in fiscal year 2008, which is due primarily to the addition of vFinance revenues as a result of the merger. Net dealer inventory gains which includes profits on proprietary trading, market making activities and customer mark-ups and mark-downs, increased \$7,981,000, or 72%, to \$19,016,000 from \$11,035,000 during the first nine months of fiscal year 2009 compared with the same period in fiscal year 2008. The increase is due primarily to the addition of vFinance revenues as a result of the merger.

Investment banking revenue increased \$769,000, or 60%, in the first nine months of fiscal year 2009 to \$2,046,000 from \$1,277,000 in the first nine months of fiscal year 2008. These revenues were attributable to the closing of a few smaller private placements as well as advisory and consulting services provided during the nine month period. Interest and dividend income decreased by \$1,362,000 or 51%, to \$1,285,000 from \$2,647,000 in the first nine months of fiscal year 2009 compared with the same period last year. The decrease in interest income is attributable to generally lower customer margin account balances, lower customer free cash balances and lower prevailing interest rates during the quarter. Transfer fees and clearance services increased \$6,138,000 or 182%, to \$9,516,000 in the first nine months of fiscal year 2009 from \$3,378,000 in the first nine months of fiscal year 2008. The increase is due primarily to the addition of vFinance revenues as a result of the merger.

Other revenue, consisting of asset management fees, miscellaneous transaction fees and trading fees and other investment income, increased \$1,436,000, or 61%, to \$3,783,000 from \$2,347,000 during the first nine months of fiscal year 2009 compared to the first nine months of fiscal year 2008. The increase is due primarily to the addition of vFinance revenues as a result of the merger.

In comparison with the 55% increase in total revenues, total expenses increased 53% or \$31,126,000 to \$89,892,000 for the first nine months of fiscal year 2009 compared to \$58,766,000 in the first nine months of fiscal year 2008. The increase in total expenses is primarily a result of the addition of vFinance expenses as a result of the merger.

|                                  | Nine Months Ended |               | Increase (Decrease) |         |
|----------------------------------|-------------------|---------------|---------------------|---------|
|                                  | 2009              | 2008          | Amount              | Percent |
| Commissions                      | 64,524,000        | \$ 43,449,000 | \$ 21,075,000       | 49%     |
| Employee compensation            | 9,029,000         | 6,334,000     | 2,695,000           | 43%     |
| Clearing fees                    | 3,890,000         | 1,676,000     | 2,214,000           | 132%    |
| Communications                   | 3,137,000         | 907,000       | 2,230,000           | 246%    |
| Occupancy and equipment costs    | 3,786,000         | 2,564,000     | 1,222,000           | 48%     |
| Professional fees                | 1,790,000         | 1,597,000     | 193,000             | 12%     |
| Interest                         | 925,000           | 319,000       | 606,000             | 190%    |
| Taxes, licenses and registration | 1,016,000         | 330,000       | 686,000             | 208%    |
| Other administrative expenses    | 1,795,000         | 1,590,000     | 205,000             | 13%     |
|                                  | \$ 89,892,000     | \$ 58,766,000 | \$ 31,126,000       | 53%     |

Commission expense, which includes expenses related to commission revenue, net dealer inventory gains and investment banking, increased \$21,075,000, or 49%, to \$64,524,000 in the first nine months of fiscal year 2009 from \$43,449,000 in the first nine months of fiscal year 2008. The increase is primarily attributable to an increase in the related commission revenues from the vFinance merger. Commission expense includes the amortization of advances to registered representatives of \$1,158,000 and \$1,044,000 for the first nine months of fiscal years 2009 and 2008, 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 our Broker Dealer Subsidiaries.

Employee compensation expense increased \$2,695,000, or 43%, to \$9,029,000 in the first nine months of fiscal year 2009 from \$6,334,000 in the first nine months of fiscal year 2008. The increase is primarily attributable to costs from vFinance due to the merger. Employee compensation includes the amortization of the fair value associated with stock based compensation of \$730,000 and \$442,000 in first nine months of fiscal years 2009 and 2008, respectively. Overall, combined commission and employee compensation expense, as a percentage of revenue decreased to 86% from 90% in the first nine months of fiscal year 2009 and 2008, respectively as a result of cost cutting plans implemented due to economic conditions.

Clearing fees increased \$2,214,000 or 132%, to \$3,890,000 in the first nine months of fiscal year 2009 from \$1,676,000 in the first nine months of fiscal year 2008. The increase in clearing fees is primarily attributable to costs from vFinance due to the merger. The greater increase in clearing fees as compared to the increase in commission revenue is attributable to lower average commission revenue per ticket in the first nine months of fiscal year 2009.

Communication expenses increased \$2,230,000 or 246%, to \$3,137,000 from \$907,000 in the first nine months of fiscal year 2009 compared to the first nine months of fiscal year 2008. The increase is due to costs from vFinance due to the merger. Occupancy costs increased \$1,222,000, or 48%, to \$3,786,000 from \$2,564,000 in the first nine months of fiscal year 2009 compared to the first nine months of fiscal year 2008. The increase in occupancy expense is due to annual rent increases contained in the Company's office leases and the addition of rented office space due to the vFinance merger.

Professional fees increased \$193,000, or 12%, to \$1,790,000 from \$1,597,000 in the first nine months of fiscal year 2009 compared to the first nine months of fiscal year 2008. The increase in professional fees is primarily a result of the filing of a registration statement and slightly higher legal costs associated with the merger with vFinance.

Interest expense increased \$606,000, or 190%, to \$925,000 from \$319,000 in the first nine months of fiscal year 2009 compared to the first nine months of fiscal year 2008. The increase in interest expense is attributable to new convertible notes issued in March and June of fiscal year 2008. Included in interest expense is the amortization of deferred financing costs of \$337,000 and \$113,000 the first nine months of fiscal years 2009 and 2008, respectively. Taxes, licenses and registration increased \$686,000, or 208%, to \$1,016,000 from \$330,000 in the first nine months of fiscal year 2009 compared to the first nine months of fiscal year 2008. The increase in taxes, licenses and registration is due to primarily attributable to costs from vFinance due to the merger. Other administrative expenses increased \$205,000 or 13% to \$1,795,000 from \$1,590,000 in the first nine months of fiscal year 2009 compared to the first nine months of fiscal year 2008. The increase is primarily attributable to costs from vFinance due to the merger.

The Company reported a net loss of \$3,938,000 in the first nine months of fiscal year 2009 compared to a net loss of \$3,438,000 in the first nine months of fiscal year 2008. The net loss attributable to common stockholders in the first nine months of fiscal year 2009 was \$4,203,000 or \$0.25 per common share, as compared to a net loss attributable to common stockholders in the first nine months of fiscal year 2008 of \$3,691,000, or \$0.43 per common share. The net loss attributable to common stockholders for the first nine months of fiscal year 2009 and 2008 reflects \$265,000 and \$253,000, respectively, of cumulative preferred stock dividends on the Company's preferred stock.



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

Management considers 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 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 and nine months ended June 30, 2009, EBITDA, as adjusted, was \$431,000 and \$(21,000), respectively. In the three and nine months ended June 30, 2008, EBITDA, as adjusted, was (\$274,000) and (\$1,935,000), respectively. This improvement of \$705,000 and \$1,914,000 in both the three and nine months ended June 30, 2009 over 2008 result from increased revenues, lower average payout per dollar of commission earned, and significant reductions in operating expenses.

The following table presents a reconciliation of EBITDA, as adjusted, to net income as reported.

|                                  | Three Months Ended<br>June 30, |              | Nine Months Ended<br>June 30, |                |
|----------------------------------|--------------------------------|--------------|-------------------------------|----------------|
|                                  | 2009                           | 2008         | 2009                          | 2008           |
| Net income loss, as reported     | \$ (868,000)                   | \$ (909,000) | \$ (3,938,000)                | \$ (3,438,000) |
| Interest expense                 | 291,000                        | 176,000      | 926,000                       | 319,000        |
| Taxes                            | 29,000                         | 63,000       | 106,000                       | 169,000        |
| Depreciation                     | 189,000                        | 45,000       | 551,000                       | 146,000        |
| Amortization                     | 162,000                        | -            | 466,000                       | -              |
| EBITDA                           | (197,000)                      | (625,000)    | (1,889,000)                   | (2,804,000)    |
| Non-cash compensation<br>expense | 237,000                        | 54,000       | 710,000                       | 83,000         |
| Forgivable loan write down       | 391,000                        | 297,000      | 1,158,000                     | 786,000        |
| EBITDA, as adjusted              | \$ 431,000                     | \$ (274,000) | \$ (21,000)                   | \$ (1,935,000) |

Earnings before interest, taxes, depreciation and amortization, or 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 under the Securities Act of 1933, as amended.

## Liquidity and Capital Resources

For the periods ended June 30, 2009 and September 30, 2008, 55% and 54% of our total assets consisted of cash and cash equivalents, marketable securities owned and receivables from clearing brokers and other broker dealers. The level of cash used in each asset class is subject to fluctuation based on market volatility, revenue production and trading activity in the marketplace. Allocation of cash into marketable securities classes are dependent upon overall market activity, but the majority of our securities owned are in municipal securities and common stock.

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, 2008, National Securities' net capital exceeded the requirement by \$261,000. Due to its market maker status, vFinance Investments is required to maintain a minimum net capital of \$1,000,000 and EquityStation is required to maintain \$100,000, and at June 30, 2009 the firms had excess net capital of \$421,000 and \$111,000, respectively.

Cash used in operations for the nine months ended June 30, 2009 was \$736,000 which was primarily due to our net loss of \$3,938,000, reduced by non cash adjustments of \$1,017,000 in depreciation and amortization and \$678,000 in stock compensation expense. An increase in receivables from our clearing firms of \$651,000, an increase in other receivables of \$333,000, and a decrease of the payable to broker dealers and clearing organizations of \$451,000 further decreased cash but was offset by an increase in accounts payable and accrued expenses of \$1,021,000, a decrease in advances to brokers of \$934,000 and a decrease in long securities owned at market value of \$541,000. Investing activities used \$598,000 due to the need to purchase fixed assets under mostly capital leases due to the move of our vFinance Boca Raton data center into a co-location in Miami, Florida and the move of our Boca Raton office to a new location.

Financing activities used \$132,000 due in part to the repayment of indebtedness to certain principal stockholders of \$500,000. But a private placement of our securities (net of costs) and securing a subordinated loan brought in about \$368,000.

The Company has historically satisfied its capital needs with cash generated from operations or from financing activities. The Company believes that it will have sufficient funds to maintain its current level of business activities during fiscal year 2009. If market conditions should weaken, the Company would need to consider curtailing certain of its business activities, reducing its fixed overhead costs and/or seek additional sources of financing.

Advances, dividend payments and other equity withdrawals from the Company's subsidiary 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. During the quarter ended June 30, 2009 the Company did not have any equity withdrawals.

The Company extends unsecured credit in the normal course of business to its 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 the Company has ready access to sufficient funds to meet commitments, fund deposit withdrawals and efficiently provide for the credit needs of customers.

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. In February 2008, upon the maturity of the previously issued note, National Securities and the holder entered into a new \$500,000 secured demand note collateral agreement with a maturity date of March 1, 2009 at which time the holder also entered into a warrant agreement to purchase 150,000 shares of common stock at a price of \$1.25 per share, with an expiration date of July 31, 2009. The note collateral agreement automatically renewed on March 1, 2009 and is set to mature on March 1, 2010.

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, which notes matured in February 2009. The Company recorded a debt discount of approximately \$195,000 that is being charged to interest expense over the life of the debt. The investment included \$500,000 by Christopher C. Dewey and \$250,000 by St. Cloud Capital Partners, L.P. ("St. Cloud"). Mr. Dewey, and Marshall S. Geller, the Senior Managing Partner of St. Cloud, are each members of the Company's board of directors. In February 2009, we entered into forbearance agreements with the investors as previously reported on our Current Report on Form 8-K, as filed with the SEC on March 2, 2009, and on April 6, 2009 we amended our forbearance agreement with St. Cloud, as filed with the SEC on April 10, 2009. The St. Cloud note was repaid in full on April 30, 2009.

On May 6, 2009, we entered into amendments to the existing forbearance agreements with the remaining investors, as previously reported on our Current Report on Form 8-K, as filed with the SEC on May 6, 2009, whereby the remaining investors agreed not exercise any of their rights under their notes until May 12, 2009. On May 14, 2009, we entered into second amendments to the existing forbearance agreements with the remaining investors whereby the remaining investors agreed not exercise any of their rights under their notes until May 22, 2009. On May 29, 2009 we repaid \$250,000 owed to Bedford Oak Partners, L.P., a principal stockholder of the Company, and on May 29, 2009 we entered into a third amendment to the forbearance agreement with Mr. Dewey as previously reported on our Current Report on Form 8-K, as filed with the SEC on May 29, 2009, whereby Mr. Dewey agreed to not exercise any of his rights under his note until June 1, 2010 and agreed to lower the interest rate on his note from 10% to 7% per annum.

On March 31, 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. Under accounting guidance provided by EITF No 98-5 and EITF No. 00-27 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 accounting guidance provided by EITF No 98-5 and EITF No. 00-27 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.



In April 2005, National Securities entered into a clearing agreement with National Financial Services LLC (“NFS”) that became effective in June 2005. In the first quarter of fiscal year 2007, NFS paid National Securities a \$750,000 general business credit that is being amortized over an eight year period ending November 2014, corresponding with the expiration date of the clearing agreement. In the second quarter of fiscal year 2007, NFS provided National Securities a \$250,000 clearing fee waiver that is being amortized over a two year period ending December 2008, corresponding with the time period that certain performance standards were to be achieved. The clearing agreement includes a termination fee if National Securities terminates the agreement without cause. The Broker Dealer Subsidiaries currently have clearing agreements with NFS, Penson Financial Services, Inc., Legent Clearing LLC and Fortis Securities, LLC. The Company believes that the overall effect of its clearing relationships has been beneficial to the Company’s cost structure, liquidity and capital resources.

In June 2009, National Securities was approved by the FINRA to receive a Subordinated loan from Legent Clearing 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 is forgivable after one year and National Securities bringing over a certain number of assets to the Legent clearing platform.

#### Contractual Obligations

In May 2009 the Company ceased using its Military Trail office in Boca Raton, Florida and relocated all of its employees from this location to space it already had under lease on North Federal Highway in Boca Raton. The original lease on the Federal Highway location was terminated and a new lease was signed for the Company to begin use in May. In addition to extending the term of the lease by approximately one year, the Landlord gave a rent holiday for the first four months of the lease and provided reimbursement of build-out costs to a maximum of \$150,000.

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

The Company's primary market risk arises from the fact that it engages in proprietary trading and historically made dealer markets in equity securities. Accordingly, the Company may be required to maintain certain amounts of inventories in order to facilitate customer order flow. The Company 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. The Company is not subject to direct market risk due to changes in foreign exchange rates. However, the Company is subject to market risk as a result of changes in interest rates and equity prices, which are affected by global economic conditions. The Company manages its exposure to market risk by limiting its net long or short positions. Trading and inventory accounts are monitored daily by management and the Company has instituted position limits.

Credit risk represents the amount of accounting loss the Company could incur if counterparties to its 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, the Company maintains more stringent requirements to further reduce its exposure. The Company monitors its exposure to counterparty risk on a daily basis by using credit exposure information and monitoring collateral values. The Company maintains 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, requiring the transfer of the account to another broker-dealer.



The Company monitors its market and credit risks daily through internal control procedures designed to identify and evaluate the various risks to which the Company is exposed. There can be no assurance, however, that the Company's 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 owned ("long") and securities sold but not yet purchased ("short") the Company as of June 30, 2009:

|                        | Long       | Short     |
|------------------------|------------|-----------|
| Corporate stocks       | \$ 88,000  | \$ 76,000 |
| Corporate bonds        | 68,000     | -         |
| Government obligations | 422,000    | -         |
|                        | \$ 578,000 | \$ 76,000 |

#### 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 and control procedures are also designed to ensure that such information is accumulated and communicated to management, including the chief executive officer and principal accounting officer, to allow timely decisions regarding required disclosures. 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 the evaluation of the Company's 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), the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were adequate and effective to ensure that material information relating to the Company and its 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.

We have continually had in place systems relating to internal control over financial reporting. There were no significant changes in the Company's internal controls over financial reporting or in other factors during the last fiscal quarter to which this Quarterly Report on Form 10-Q relates that could significantly affect those controls and procedures subsequent to the date of our evaluation nor any significant deficiencies or material weaknesses in such internal controls and procedures requiring corrective actions.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On March 4, 2008, vFinance received a customer arbitration (FINRA Case No.08-00472) from Donald and Patricia Halfmann, alleging that Jeff Lafferty, a former registered representative of vFinance, misappropriated approximately \$110,000 of the Halfmanns' funds via check alteration, and that vFinance ought to be liable for an additional \$150,000 for other dishonest and fraudulent acts committed after he left vFinance. On August 6, 2009 the arbitrators' ruled that vFinance Investments must pay for losses, interest, attorneys costs and punitive damages totaling approximately \$780,000. The firm has made a claim against its fidelity bond carrier, and is completing its analysis as to whether to seek to have the entire arbitration award, or any part of that award, vacated.

In October, 2008, vFinance and others were named as defendants in a civil action (Case No. 09-CV-9008 United Stated District Court, Southern District of New York), wherein The Pinnacle Fund, L.P. and others alleged securities law violations and other causes of action stemming from a private placement transaction into a public company which vFinance acted as placement agent. Plaintiffs alleged damages in excess of \$12,000,000 in compensatory damages. vFinance asserted its indemnification rights against a one of the co-defendants, and has thus far received reimbursement of most of the attorneys fees and costs incurred. The parties have reached a settlement and the action was dismissed with prejudice and vFinance Investments, Inc. was indemnified as to all costs in this matter.

During the quarter ended June 30, 2009, there were no other significant developments in the Company's legal proceedings except those already discussed in Note 6 to the financial statements entitled Commitments and Contingencies. For a detailed discussion of the Company's legal proceedings, please refer to Note 6 herein, and the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2008.

ITEM 1A. RISK FACTORS

There are no material changes from the risk factors previously disclosed in the Company's Form 10-K for the fiscal year ended September 30, 2008.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

10.34 Amendment No.2 to Forbearance Agreement, dated as of May 29, 2009, by and between National Holdings Corporation and Christopher C. Dewey.

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.

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 14, 2009

/s/ Mark Goldwasser  
Mark Goldwasser  
Chief Executive Officer

August 14, 2009

By:

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