Interactive Brokers Group, Inc.
Form 10-Q
June 15, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2007.

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

For the transition period from to

Commission File Number: **001-33440**

INTERACTIVE BROKERS GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**30-0390693**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One Pickwick Plaza

Greenwich, Connecticut 06830

(Address of principal executive office)

(203) 618-5800

(Registrant s telephone number, including area code)

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 o No x.

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

Large accelerated filer o	Accelerated filer o	Non-accelerated filer x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x.

As of June 15, 2007, there were 40,187,258 shares of the issuer s Class A common stock, par value $0.01 per share, outstanding and 100 shares of the issuer s Class B common stock, par value $0.01 per share, outstanding.

INTERACTIVE BROKERS GROUP, INC.

QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTER ENDED MARCH 31, 2007

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PART I: FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

Introductory Note

On May 3, 2007, Interactive Brokers Group, Inc., a Delaware corporation (IBG, Inc.), priced an initial public offering (the IPO) of shares of its Class A common stock, par value $0.01 per share (the Common Stock). In connection with the IPO, IBG, Inc. purchased 10% of the membership interests in IBG LLC, a Connecticut limited liability company, from IBG Holdings LLC, a Delaware limited liability company, became the sole managing member of IBG LLC and began to consolidate IBG LLC s financial results into its financial statements. Such transactions are collectively referred to herein as the Recapitalization are described in greater detail in Note 12 to the condensed consolidated financial statements. Because the Recapitalization occurred subsequent to the end of the period covered by this report, the historical condensed consolidated financial statements reflect the historical financial position, results of operations and cash flows of IBG LLC and subsidiaries (the Group) for all periods presented. Accordingly, the historical condensed consolidated financial statements do not reflect what the financial position, results of operations or cash flows of IBG, Inc. or the Group would have been had these companies been stand-alone public companies for the periods presented. Specifically, the historical financial statements of the Group do not give effect to the following matters:

- The Recapitalization.

- U.S. corporate federal income taxes, since the Group operates in the U.S. as a limited liability company that is treated as a partnership for U.S. federal income tax purposes. Historically, the Group s income was not subject to U.S. federal income taxes. Taxes related to income earned by partnerships represent obligations of the individual partners. Income taxes shown on the Group s condensed consolidated statements of income are primarily attributable to taxes incurred by non-U.S. entities. Outside the United States, the Group principally operates through subsidiary corporations and is subject to local income taxes. Foreign income taxes paid on dividends received are also reported as income taxes. State and local income taxes reported in the condensed consolidated statements of income represent taxes assessed by jurisdictions that do not recognize the Group s limited liability company status. Subsequent to the consummation of the IPO, the consolidated financial statements of IBG, Inc. will include U.S. federal income taxes on its allocable share of the results of operations of the Group, giving effect to the post-IPO structure.

- Minority interest reflecting IBG Holdings LLC s ownership of approximately 90% of the IBG LLC membership interests outstanding immediately after the IPO.

IBG LLC AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(Unaudited)

(dollars in thousands)	March 31 2007	December 31, 2006
Assets		
Cash and cash equivalents	$ 607,776	$ 669,271
Cash and securities segregated for regulatory purposes	3,427,864	3,111,795
Securities borrowed	10,533,021	10,479,231
Securities purchased under agreements to resell		97,740
Trading assets, at fair value:		
Financial instruments owned	7,261,800	7,485,879
Financial instruments owned and pledged as collateral	7,438,086	8,331,923
	14,699,886	15,817,802
Other receivables:		
Customers (net of allowance for doubtful accounts of $1,043 at March 31, 2007 and $1,031 at December 31, 2006)	1,081,663	848,448
Brokers, dealers and clearing organizations	1,682,564	856,957
Interest	63,657	62,772
	2,827,884	1,768,177
Other assets	152,257	136,502
Total assets	$ 32,248,688	$ 32,080,518
Liabilities and redeemable members interest		
Liabilities:		
Trading liabilities financial instruments sold but not yet purchased, at fair value	$ 14,719,628	$ 14,785,617
Securities sold under agreements to repurchase	17,286	
Securities loaned	7,003,580	8,026,468
Short-term borrowings	1,051,486	1,296,909
Other payables:		
Customers	4,591,418	3,914,037
Brokers, dealers and clearing organizations	1,381,951	743,339
Accounts payable, accrued expenses and other liabilities	163,202	161,812
Interest	49,180	49,821
	6,185,751	4,869,009
Senior notes payable	154,604	150,598
Senior secured credit facility	150,000	150,000
Commitments, contingencies and guarantees		
Redeemable members interests		
(including accumulated other comprehensive income of $103,308 at March 31, 2007 and $98,568 at December 31, 2006)	2,966,353	2,801,917
Total liabilities and redeemable members interest	$ 32,248,688	$ 32,080,518

See accompanying notes to the condensed consolidated financial statements.

IBG LLC AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(dollars in thousands)	**Three months ended March 31, 2007**	**2006**
Revenues:		
Trading gains	$ 198,802	$ 225,369
Commissions and execution fees	56,335	39,364
Interest income	184,519	132,075
Other income	24,689	25,564
Total revenues	464,345	422,372
Interest expense	133,537	93,803
Total net revenues	330,808	328,569
Non-interest expenses:		
Execution and clearing	90,120	71,308
Employee compensation and benefits	32,793	28,687
Occupancy, depreciation and amortization	5,957	5,580
Communications	3,463	2,691
General and administrative	8,136	4,944
Total non-interest expenses	140,469	113,210
Income before income taxes	190,339	215,359
Income tax expense	6,143	9,184
Net income	$ 184,196	$ 206,175

See accompanying notes to the condensed consolidated financial statements.

IBG LLC AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(dollars in thousands)	**Three months ended March 31, 2007**	**2006**
Cash flows from operating activities:		
Net income	$ 184,196	$ 206,175
Adjustments to reconcile net income to net cash provided by operating activities:		
Translation (gains) losses	(7,677)	890
Deferred income taxes	(2,714)	
Depreciation and amortization	2,953	3,244
Loss (income) from equity investments in exchanges	591	(237)
Other	29	21
Change in operating assets and liabilities:		
Increase in cash and securities segregated for regulatory	(316,041)	(141,569)
Increase in securities borrowed	(38,693)	(1,256,581)
Decrease in securities purchased under agreements to resell	97,740	1,700
Decrease (increase) in trading assets	1,162,118	(1,464,304)
Increase in receivables from customers	(233,129)	(196,250)
(Increase) decrease in other receivables	(820,811)	79,827
Increase in other assets	(7,163)	(6,712)
(Decrease) increase in trading liabilities	(108,113)	1,268,701
Increase in securities sold under agreements to repurchase	17,093	45,180
(Decrease) increase in securities loaned	(1,030,296)	1,235,965
Increase in payable to customers	677,017	330,890
Increase in other payables	639,544	104,905
Net cash provided by operating activities	216,644	211,845
Cash flows from investing activities:		
Purchase of investments	(9,419)	(24,250)
Purchase of property and equipment	(4,048)	(2,425)
Net cash used in investing activities	(13,467)	(26,675)
Cash flows from financing activities:		
Issuance of senior notes	112,816	156,637
Redemptions from senior notes	(108,810)	(125,338)
Decrease in short-term borrowings, net	(243,224)	(118,093)
Members contributions		201
Members interests redeeemed		(1,504)
Dividends paid	(24,500)	(86,000)
Net cash used in financing activities	(263,718)	(174,097)
Effect of exchange rate changes on cash and cash equivalents	(954)	(329)
Net (decrease) increase in cash and cash equivalents	(61,495)	10,744
Cash and cash equivalents at beginning of period	669,271	408,232
Cash and cash equivalents at end of period	$ 607,776	$ 418,976
Supplemental disclosures of cash flow information:		
Refinancing of bridge loan receivable	$ 10,018	$
Interest paid	$ 134,178	$ 82,889
Taxes paid	$ 5,279	$ 6,563

See accompanying notes to the condensed consolidated financial statements.

IBG LLC AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF CHANGES

IN REDEEMABLE MEMBERS INTERESTS

Three months ended March 31, 2007

(Unaudited)

(dollars in thousands)	**Redeemable Members Interests and Accumulated Earnings**	**Accumulated Other Comprehensive Income**	**Total Redeemable Members Interests and Accumulated Other Comprehensive Income**
Balance, January 1, 2007	$ 2,703,349	$ 98,568	$ 2,801,917
Dividends	(24,500)		(24,500)
Members interests redeemed			
Members contributions			
Comprehensive income:			
Net income	184,196		184,196
Cumulative translation adjustment		4,740	4,740
Total comprehensive income	184,196	4,740	188,936
Balance, March 31, 2007	$ 2,863,045	$ 103,308	$ 2,966,353

See accompanying notes to the condensed consolidated financial statements.

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IBG LLC and Subsidiaries

Notes to Condensed Consolidated Financial Statements

(Unaudited)

(dollars in thousands, except per share amounts or unless otherwise noted)

1. Organization and Nature of Business

IBG LLC, formerly known as Interactive Brokers Group LLC, and subsidiaries (the Group) is an automated global market maker and electronic broker specializing in routing orders and processing trades in securities, futures and foreign exchange instruments.

IBG LLC is a Connecticut limited liability company that conducts its business through its operating subsidiaries (collectively called the Operating Companies): Timber Hill LLC (TH LLC), Timber Hill Europe AG (THE), Timber Hill Securities Hong Kong Limited (THSHK), Timber Hill Australia Pty Limited (THA), Timber Hill Canada Company (THC), Interactive Brokers Hungary KFT (IBH), IB Exchange Corp. (IBEC), Interactive Brokers LLC (IB LLC), Interactive Brokers Canada Inc. (IBC) and Interactive Brokers (U.K.) Limited (IBUK). The operations of Timber Hill Hong Kong Limited (THHK) were assumed by THSHK and THHK ceased operating in February 2004 and was liquidated in October 2005. Timber Hill (U.K.) Limited (THUK), a subsidiary of THE, transferred its operations to THE and THUK ceased operating on November 16, 2004.

The Operating Companies are members of various securities and commodities exchanges in the United States, Europe and the Asia/Pacific region. Other than IB LLC, IBUK and IBC, the Operating Companies do not carry securities accounts for customers or perform custodial functions relating to customer securities.

IB LLC, a U.S. broker-dealer and futures commission merchant, conducts electronic brokerage services for customers. IB LLC carries customer securities and commodity accounts and is subject to the regulatory requirements of the U.S. Securities Exchange Act of 1934, as amended (the Exchange Act), and the U.S. Commodities Exchange Act.

2. Significant Accounting Policies

Basis of Presentation

The unaudited condensed consolidated financial statements of IBG LLC are presented in U.S. dollars and have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC) regarding interim financial reporting with respect to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States (U.S. GAAP) for complete financial statements and should be read in conjunction with the audited consolidated financial statements and notes thereto included in IBG, Inc. s final prospectus filed with the SEC on May 4, 2007 (the Prospectus) for the offering of Class A common stock, par value $0.01 per share (the Common Stock). See Note 12 to the condensed consolidated financial statements for information regarding the Recapitalization (as defined in Note 12) and the IPO.

In management s opinion, the unaudited condensed consolidated financial statements reflect all normal, recurring adjustments to present fairly the Group s financial position, results of operations and cash flows for the interim periods presented. The consolidated results of operations and cash flows for the three month period ended March 31, 2007 are not necessarily indicative of the results to be expected for any future period or for the full year. Gains and losses from foreign currency transactions are included in trading gains and losses where related to market making activities or in other income where related to electronic brokerage activities in the condensed consolidated statements of income. Non-U.S. subsidiaries have a functional currency (i.e., the currency in which activities are primarily conducted) that is other than the U.S. dollar. Such subsidiaries assets and liabilities are translated to U.S. dollars at period-end exchange rates, while revenues and expenses are translated at average exchange rates during the year. Adjustments that result from translating amounts from a subsidiary s functional currency to the U.S. dollar are reported in redeemable members interests as a component of accumulated other comprehensive income.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts and disclosures in the condensed consolidated financial

IBG LLC and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

(dollars in thousands, except per share amounts or unless otherwise noted)

statements and accompanying notes. Estimates, by their nature, are based on judgment and available information. Therefore, actual results could differ materially from those estimates. Such estimates include the estimated fair value of financial instruments, the estimated useful lives of property and equipment, including capitalized internally developed software, compensation accruals, tax liabilities and estimated contingency reserves.

Fair Value

At March 31, 2007 and December 31, 2006, substantially all of the Group s assets and liabilities were carried at fair value or at amounts that approximate fair value. The fair value amounts for financial instruments are disclosed in each respective note to the condensed consolidated financial statements.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Group and its majority and wholly owned subsidiaries. The Group s policy is to consolidate all entities of which it owns more than 50% unless it does not have control. All intercompany balances and transactions have been eliminated. At March 31, 2007 and December 31, 2006, there was a minority interest of $550 and $506, respectively, which was included in accounts payable, accrued expenses and other liabilities in the condensed consolidated statements of financial condition. Pursuant to the revised Financial Accounting Standards Board (FASB) Interpretation (FIN) No. 46, Consolidation of Variable Interest Entities, the Group would also consolidate any Variable Interest Entities (VIEs) of which it is the primary beneficiary. The Group currently is not the primary beneficiary of any such entities and therefore no VIEs are included in the condensed consolidated financial statements.

Redeemable Members Interests

Redeemable members interests represent member interests in IBG LLC that are entitled to share in the condensed consolidated profits and losses of the Group. IBG LLC is a private entity owned by the members holding such member interests.

IBG LLC has applied guidance within Emerging Issues Task Force (EITF) Topic D-98 Classification and Measurement of Redeemable Securities, which requires securities or equity interests of a company whose redemption is outside the control of the company to be classified outside of permanent capital in the statement of financial condition. Historically, the member interests in IBG LLC could be redeemed by the members at book value at their option. Because this redemption right is deemed to be outside of its control, IBG LLC has classified all members capital outside of permanent capital as redeemable members interests in the condensed consolidated statements of financial condition.

Prior to January 2, 2006, selected employees had been granted non-transferable fully vested member interests in IBG LLC. Grants issued before January 1, 2006 were accounted for pursuant to Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees and EITF Issue No. 00-23, Issues Related to the Accounting for Stock Compensation under APB Opinion No. 25 and FIN No. 44. IBG LLC recorded a fixed dollar amount of expense for member interest grants at the date of grant based on management s estimate of fair value, which is book value (as defined in IBG LLC s Agreement as to Member Interest Purchase Rights). Member interests confer ownership rights in IBG LLC and entitle the holder to proportionate rights to future allocable profits and losses of IBG LLC. Under the terms of the agreement, member-employees could only sell their interests back to IBG LLC at any time at book value. Member interest grants were initially accounted for as liabilities until six months elapsed from the date of grant, at which time such liabilities were reclassified to redeemable members interests as members contributions.

The Group adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), Share-Based Payment, a revision of SFAS No. 123, Accounting for Stock-Based Compensation as of January 1, 2006 (SFAS 123R). The Group continued to account for all grants of member interests granted subsequent to December 31, 2005 as liability awards.

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IBG LLC and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

(dollars in thousands, except per share amounts or unless otherwise noted)

Cash and Cash Equivalents

The Group defines cash equivalents as short-term, highly liquid securities and cash deposits with original maturities of three months or less, other than those used for trading purposes. At March 31, 2007 and December 31, 2006, foreign currency owned of $362,174 and $279,501 is included in cash and cash equivalents and foreign currency sold of $4,407 and $11,837 is included in short-term borrowings, respectively, and are carried at fair value.

Cash and Securities Segregated for Regulatory Purposes

As a result of customer activities, certain Operating Companies are obligated by rules mandated by their primary regulators including the SEC and the Commodities Futures Trading Commission (CFTC) in the United States and the Financial Services Authority in the United Kingdom to segregate or set aside cash or qualified securities to satisfy such regulations, which regulations have been promulgated to protect customer assets. In addition, substantially all of the Operating Companies are members of various clearing organizations at which cash or securities are deposited as required to conduct day-to-day clearance activities.

Securities Borrowed and Securities Loaned

Securities borrowed and securities loaned are recorded at the amount of cash collateral advanced or received. Securities borrowed transactions require the Group to provide counterparties with collateral, which may be in the form of cash, letters of credit, or other securities. With respect to securities loaned, the Group receives collateral, which may be in the form of cash or other securities in an amount generally in excess of the fair value of the securities loaned.

The Group monitors the market value of securities borrowed and loaned on a daily basis, with additional collateral obtained or refunded as required contractually. Receivables and payables with the same counterparty are not offset in the condensed consolidated statements of financial condition. For these transactions, the fees received or paid by the Group are recorded as interest income or interest expense in the condensed consolidated statements of income.

Securities Purchased Under Agreements to Resell and Securities Sold Under Agreements to Repurchase

Securities purchased under agreements to resell and securities sold under agreements to repurchase are treated as collateralized financing transactions and are recorded at contract value, plus accrued interest, which approximates fair value. The Group s policy is to obtain possession of collateral with a fair value equal to or in excess of the principal amount loaned under resale agreements. To ensure that the fair value of the underlying collateral remains sufficient, this collateral is valued daily with additional collateral obtained or excess collateral returned, as required under contractual provisions.

Financial Instruments Owned and Sold, Not Yet Purchased

Stocks, government and corporate bonds, futures and options transactions are reported in the condensed consolidated financial statements on a trade date basis. Substantially all financial instruments owned and financial instruments sold, not yet purchased are recorded at fair value based upon quoted market prices. All firm-owned financial instruments pledged to counterparties where the counterparty has the right, by contract or custom, to sell or repledge the financial instruments are classified as financial instruments owned and pledged as collateral in the condensed consolidated statements of financial condition.

The Group also enters into cross-currency swap transactions. These transactions, which are also reported on a trade date basis, are agreements to exchange a fixed amount of one currency for a specified amount of a second currency at the outset and at completion of the swap term. Unrealized mark-to-market gains and losses on cross-currency swap transactions are reported as components of financial instruments owned or financial instruments sold,

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IBG LLC and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

(dollars in thousands, except per share amounts or unless otherwise noted)

not yet purchased in the condensed consolidated statements of financial condition. Net earnings or losses are reported as components of interest income in the condensed consolidated statements of income.

Customer Receivables and Payables

Customer securities transactions are recorded on a settlement date basis and customer commodities transactions are recorded on a trade date basis. Receivables from and payables to customers include amounts due on cash and margin transactions, including futures contracts transacted on behalf of the Group s customers. Securities owned by customers, including those that collateralize margin loans or other similar transactions, are not reported in the condensed consolidated statements of financial condition.

Receivables from and Payables to Brokers, Dealers and Clearing Organizations

Receivables from brokers, dealers and clearing organizations include amounts receivable for securities not delivered by the Group to the purchaser by the settlement date (fails to deliver) and margin deposits. Payables to brokers, dealers and clearing organizations include amounts payable for securities not received by the Group from a seller by the settlement date (fails to receive). Receivables and payables to brokers, dealers and clearing organizations also include amounts related to futures contracts executed on behalf of the Group s customers as well as net payables and receivables from unsettled trades.

Investments

The Group makes certain strategic investments and accounts for these investments under the equity method of accounting. Investments are accounted for under the equity method of accounting when the Group has significant influence over the investee as required under APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock. Investments accounted for under the equity method are recorded at the amount of the Group s investment and adjusted each period for the Group s share of the investee s income or loss. The Group s share of the income or losses from equity investments is reported as a component of other income in the condensed consolidated statements of income and the Group s equity investments, which are included in other assets in the condensed consolidated statements of financial condition, increase or decrease accordingly. Distributions received from equity investees are recorded as reductions to the respective investment balance.

A judgmental aspect of accounting for investments is evaluating whether an other-than-temporary decline in the value of an investment has been sustained. The evaluation of an other-than-temporary impairment is dependent on specific quantitative and qualitative factors and circumstances surrounding an investment, including recurring operating losses, credit defaults and subsequent rounds of financing. As none of the Group s investments have readily determinable market values, the primary factor considered by Group management in assessing if an other-than-temporary impairment of value has occurred is the financial condition of the investee company. All investments are reviewed for changes in circumstances or occurrence of events that suggest the Group s investment may not be recoverable. If an unrealized loss on any investment is considered to be other than temporary, the loss is recognized in the period the determination is made.

The Group also holds exchange memberships and investments in equity securities of certain exchanges as required to qualify as a clearing member. Such investments are recorded at cost or, if an other-than-temporary impairment in value has occurred, at a value that reflects management s estimate of the impairment, and are included in other assets in the condensed consolidated statements of financial condition. Dividends are recognized as a component of other income as such dividends are received.

Property and Equipment

Property and equipment consist of purchased technology hardware and software, internally developed software, leasehold improvements and office furniture and equipment. Property and equipment are recorded at historical cost, less accumulated depreciation and amortization. Additions and improvements that extend the lives of assets are capitalized, while expenditures for repairs and maintenance are expensed as incurred. Depreciation and amortization are computed using the straight-line method. Equipment is depreciated over the estimated useful lives

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IBG LLC and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

(dollars in thousands, except per share amounts or unless otherwise noted)

of the assets, while leasehold improvements are amortized over the lesser of the estimated economic useful life of the asset or the term of the lease, generally three to seven years. Computer equipment is depreciated over three to five years and office furniture and equipment are depreciated over five to seven years. Qualifying costs for internally developed software are capitalized and amortized over the expected useful life of the developed software, not to exceed three years.

Comprehensive Income

Comprehensive income consists of two components: net income and other comprehensive income. Other comprehensive income refers to revenues, expenses, gains and losses that are included in redeemable members interests but are excluded from net income. The Group s other comprehensive income is comprised of foreign currency translation adjustments.

The local currency is designated as the functional currency for the Group s international operating companies. Accordingly, assets and liabilities are translated into U.S. dollars at year-end exchange rates, and revenues and expenses are translated at average exchange rates prevailing during the year. Translation gains and losses, from market making activities, are included in trading gains in the accompanying condensed consolidated statements of income. Adjustments that result from translating amounts from a subsidiary s functional currency are reported as a component of redeemable members interests.

Revenue Recognition

Trading Gains

Trading gains and losses are recorded on trade date, and are reported on a net basis. Net trading gains are comprised of changes in the fair value of trading assets and liabilities (i.e., unrealized gains and losses) and realized gains and losses. Dividends are integral to the valuation of stocks bought and sold and, accordingly, are reported on a net basis as a component of trading gains in the accompanying condensed consolidated statements of income.

Commissions and Execution Fees

Commissions charged for executing and clearing customer transactions are accrued on a trade date basis and are reported as commissions and execution fees in the condensed consolidated statements of income, and the related expenses are reported as execution and clearing expenses, also on a trade date basis.

Income Taxes

The Group accounts for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes, which requires the recognition of tax benefits or expenses on the temporary differences between the financial reporting and tax bases of assets and liabilities. In June 2006, the FASB issued FIN No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 . FIN No. 48 clarifies the accounting for uncertainty of income tax positions recognized in financial statements in accordance with SFAS No. 109. FIN No. 48 prescribes a more likely than not threshold and measurement attribute for recognition in the financial statements of an asset or liability resulting from a tax position taken or expected to be taken in an income tax return.

FIN No. 48 was adopted by the Group as of January 1, 2007. As a result of adoption and as of and for the three months ended March 31, 2007, the Group had no unrecognized tax benefits. Accordingly, no adjustments were required to be made to existing income tax assets or liabilities and no new income tax assets or liabilities were recognized.

The Group operates in the United States as a limited liability company that is treated as a partnership for U.S. federal income tax purposes. Accordingly, the Group s income is not subject to U.S. federal income taxes. Taxes related to income earned by partnerships represent obligations of the individual partners.

Income taxes shown on the Group s condensed consolidated statements of income are primarily attributable to taxes incurred in non-U.S. entities. State and local income taxes reported in the condensed consolidated statements of income represent taxes assessed by jurisdictions that do not recognize the Group s limited liability company

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IBG LLC and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

(dollars in thousands, except per share amounts or unless otherwise noted)

status. Outside the United States, the Group principally operates through subsidiary corporations and is subject to local income taxes. Foreign income taxes paid on dividends received are also reported as income taxes.

The Group recognizes interest related to income tax matters as interest expense and penalties related to income tax matters as income tax expense.

Recently Issued Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 requires companies to disclose the fair value of financial instruments according to a fair value hierarchy (i.e., levels 1, 2, and 3, as defined). Additionally, companies are required to provide enhanced disclosure regarding instruments in the level 3 category, including a reconciliation of the beginning and ending balances separately for each major category of assets and liabilities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and for interim periods within those fiscal years. Adoption of SFAS No. 157 is not expected to have a material effect on the Group s condensed consolidated statements of financial condition, income or cash flows.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, Including an amendment of FASB Statement No. 115. SFAS No. 159 permits entities to choose, at specified election dates, to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS No. 159 is effective for financial statements issued for an entity s first fiscal year beginning after November 15, 2007. Adoption of SFAS No. 159 is not expected to have a material effect on the Group s condensed consolidated statements of financial condition, income or cash flows.

3. Trading Activities and Related Risks

The Group s trading activities include providing securities market maker and brokerage services. Trading activities expose the Group to market and credit risks. These risks are managed in accordance with established risk management policies and procedures. To accomplish this, management has established a risk management process that includes:

- A regular review of the risk management process by executive management as part of its oversight role;
- Defined risk management policies and procedures supported by a rigorous analytic framework; and
- Articulated risk tolerance levels as defined by executive management that are regularly reviewed to ensure that the Group s risk-taking is consistent with its business strategy, capital structure, and current and anticipated market conditions.

Market Risk

IBG LLC is exposed to various market risks. Exposures to market risks arise from equity price risk, foreign currency exchange rate fluctuations and changes in interest rates which impact our variable rate debt obligations.

The Group seeks to mitigate market risk associated with trading inventories by employing hedging strategies that correlate rate, price and spread movements of trading inventories and related financing and hedging activities. The Group uses a combination of cash instruments and exchange traded derivatives to hedge its market exposures. The following discussion describes the types of market risk faced by the Group:

Equity Price Risk

Equity price risk arises from the possibility that equity security prices will fluctuate, affecting the value of equity securities and other instruments that derive their value from a particular stock, a defined basket of stocks, or a stock index. The Group is subject to equity price risk primarily in securities owned and

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(dollars in thousands, except per share amounts or unless otherwise noted)

securities sold, not yet purchased. The Group attempts to limit such risks by diversifying its portfolio across many different options, futures and underlying securities and avoiding concentrations of positions based on the same underlying security.

Currency Risk

Currency risk arises from the possibility that fluctuations in foreign exchange rates will impact the value of financial instruments. Exchange rate contracts include cross-currency swaps and currency futures contracts. Currency swaps are agreements to exchange future payments in one currency for payments in another currency. These agreements are used to effectively convert assets or liabilities denominated in different currencies. Currency futures are contracts for delayed delivery of currency at a specified future date. The Group uses currency swaps to manage the levels of its non-U.S. dollar currency balances and currency cash and futures to hedge its global exposure.

Interest Rate Risk

Interest rate risk arises from the possibility that changes in interest rates will affect the value of financial instruments. The Group is exposed to interest rate risk on variable-rate debt, cash and margin balances and positions carried in equity securities, options and futures. These risks are managed through investment policies and by entering into interest rate futures contracts.

Credit Risk

The Group is exposed to risk of loss if an individual, counterparty or issuer fails to perform its obligations under contractual terms (default risk). Both cash instruments and derivatives expose the Group to default risk. The Group has established policies and procedures for mitigating credit risk on principal transactions, including reviewing and establishing limits for credit exposure, maintaining collateral, and continually assessing the creditworthiness of counterparties.

In the normal course of business, the Group executes, settles and finances various customer securities transactions. Execution of these transactions includes the purchase and sale of securities by the Group that exposes the Group to default risk arising from the potential that customers or counterparties may fail to satisfy their obligations. In these situations, the Group may be required to purchase or sell financial instruments at unfavorable market prices to satisfy obligations to customers or counterparties. The Group seeks to control the risks associated with its customer margin activities by requiring customers to maintain collateral in compliance with regulatory and internal guidelines.

Liabilities to other brokers and dealers related to unsettled transactions (i.e., securities failed-to-receive) are recorded at the amount for which the securities were purchased, and are paid upon receipt of the securities from other brokers or dealers. In the case of aged securities failed-to-receive, the Group may purchase the underlying security in the market and seek reimbursement for any losses from the counterparty.

The Group enters into securities purchased under agreements to resell and securities sold under agreements to repurchase transactions (repos) in addition to securities borrowing and lending arrangements, all of which may result in credit exposure in the event the counterparty to a transaction is unable to fulfill its contractual obligations. In accordance with industry practice, repos are collateralized by securities with a market value in excess of the obligation under the contract. Similarly, securities borrowed and loaned agreements are collateralized by deposits of cash. The Group attempts to minimize credit risk associated with these activities by monitoring collateral values on a daily basis and requiring additional collateral to be deposited with or returned to the Group when deemed necessary.

Concentrations of Credit Risk

The Group s exposure to credit risk associated with its trading and other activities is measured on an individual counterparty basis, as well as by groups of counterparties that share similar attributes. Concentrations of credit risk can be affected by changes in political, industry, or economic factors. To reduce the potential for risk

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concentration, credit limits are established and exposure is monitored in light of changing counterparty and market conditions.

Off-Balance Sheet Risks

The Group may be exposed to a risk of loss not reflected in the condensed consolidated financial statements for certain derivative instruments, including equity options and futures products and for securities sold, but not yet purchased, which represent obligations of the Group to deliver specified securities at contracted prices, which may create a liability to repurchase them in the market at prevailing prices. Accordingly, these transactions result in off-balance sheet risk as the Group s cost to liquidate such securities and futures contracts may exceed the amount reported in the Group s condensed consolidated statements of financial condition.

4. Financial Instruments Owned and Sold, But Not Yet Purchased, at Fair Value

Financial instruments owned and sold, but not yet purchased consisted of securities, at quoted market prices, as follows:

	March 31, 2007		December 31, 2006	
	Owned	Sold, But Not Yet Purchased	Owned	Sold But Not Yet Purchased
Stocks	$ 9,179,372	$ 9,748,920	$ 10,596,252	$ 9,761,798
Options	4,875,714	4,964,282	4,597,737	5,022,253
U.S. and foreign government obligations	506,696		494,362	
Warrants	79,035		83,322	
Corporate bonds	4,428	59	4,862	54
Discount certificates	50,162		41,040	1,408
Currency forward contracts	4,479	6,367	227	104
	$ 14,699,886	$ 14,719,628	$ 15,817,802	$ 14,785,617

5. Investments and Notes Receivable

The Group has made strategic investments in electronic trading exchanges Boston Options Exchange, LLC, OneChicago LLC, ISE Stock Exchange, LLC and CBOE Stock Exchange, LLC.

In December 2006, the Group lent $10 million to W.R. Hambrecht + Co., Inc. (Hambrecht) under a senior secured promissory note at the rate of 15% per annum and maturing on January 23, 2007. The original maturity was subsequently extended to February 5, 2007 at which date it matured. The Group also had a commitment to lend Hambrecht $16 million as part of a three-year senior secured promissory note at December 31, 2006.

At March 31, 2007, the Group had notes receivable from Hambrecht with a par amount of $19.2 million. The notes receivable bear interest at 8% per annum, payable semi-annually. In conjunction with the notes receivable, the Group received warrants to purchase Series C common stock of Hambrecht at $0.01 per share, representing 25.48% of the fully diluted common shares of Hambrecht s capital stock and two seats on Hambrecht s board of directors.

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IBG LLC and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

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6. Senior Notes Payable

At March 31, 2007 and December 31, 2006, IBG LLC had $154,604 and $150,598 of 7% per annum, senior notes outstanding, which were privately placed to certain qualified customers of IB LLC. All of the senior notes outstanding at March 31, 2007 have either a 15-month or an 18-month maturity. IBG LLC may, solely at its option, redeem the senior notes at any time on or after a specified date in the third month or the sixth month, respectively, after the date on which the senior notes are issued and sold (the Optional Redemption Date), at a redemption price equal to 100% of the principal amount of the senior notes to be redeemed plus accrued interest. Historically, IBG LLC has redeemed these senior notes at their Optional Redemption Dates which makes these notes short-term in nature. The carrying value of the senior notes approximates their fair value.

7. Senior Secured Credit Facility

In May 2006, the Group entered into a 3-year $300 million revolving credit facility with a syndicate of banks, of which $150 million was borrowed in May 2006. As of March 31, 2007, the interest rate on the credit facility, which is indexed to LIBOR, was 5.92% per annum. The carrying value of the credit facility approximates its fair value since borrowings under the facility could be paid down at any time from available funds, making such borrowings short-term in nature. The credit facility is secured by a first priority interest in all of the capital stock of each entity owned directly by IBG LLC (subject to customary limitations with respect to foreign subsidiaries), and loans and advances to, and other intercompany obligations owed by, each entity owned directly or indirectly by IBG LLC.

The financial covenants on the Group under the terms of the credit facility are:

- minimum net worth (redeemable members interests) of $1.5 billion, with quarterly increases equal to 25% of positive consolidated net income;

- maximum total debt to capitalization (including redeemable members interests) ratio of 30%;

- minimum liquidity (unencumbered marketable securities and other liquid financial assets divided by unsecured short-term (maturities of less than one year) liabilities) ratio of 1.0 to 1.0; and

- maximum total debt to net consolidated regulatory capital ratio of 35%.

As of March 31, 2007, the Group was in compliance with all of the covenants under the credit facility.

8. Defined Contribution and Employee Incentive Plans

Defined Contribution Plan

The Group offers substantially all employees of U.S.-based Operating Companies who have met minimum service requirements the opportunity to participate in defined contribution retirement plans qualifying under the provisions of Section 401(k) of the Internal Revenue Code. The general purpose of these plans is to provide employees with an incentive to make regular savings in order to provide additional financial security during retirement. These plans provide for the Group to match 50% of the employee s pre-tax contributions, up to a maximum of 10% of eligible earnings. Employees become vested in the matching contributions incrementally over six years.

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Employee Incentive Plans

See Note 12 to the condensed consolidated financial statements for information regarding changes to the Group s employee incentive plans and the adoption of new plans by IBG, Inc. subsequent to March 31, 2007 in connection with the Recapitalization and the IPO.

Return on Investment Dollar Units (ROI Dollar Units): Since 1998, IBG LLC has granted all non-member employees ROI Dollar Units, which are redeemable under the amended provisions of the plan, and in accordance with regulations issued by the Internal Revenue Service (Section 409A of the Internal Revenue Code). Upon redemption, the grantee is entitled to accumulated earnings on the face value of the certificate, but not the actual face value. For grants made in 1998 and 1999, grantees may redeem the ROI Dollar Units after vesting on the fifth anniversary of the date of their grant and prior to the tenth anniversary of the date of their grant. For grants made between January 1, 2000 and January 1, 2005, grantees must elect to redeem the ROI Dollar Units upon the fifth, seventh or tenth anniversary date. These ROI Dollar Units will vest upon the fifth anniversary of the date of their grant and will continue to accumulate earnings until the elected redemption date. For grants made on or after January 1, 2006, all ROI Dollar Units shall vest on the fifth anniversary date of their grant and will be automatically redeemed.

As of March 31, 2007 and December 31, 2006, payables to employees for ROI Dollar Units were $36,149 and $39,644, respectively, of which $18,984 and $14,003, respectively, were vested. These amounts are included in accounts payable, accrued expenses and other liabilities in the condensed consolidated statements of financial condition.

Redeemable Members Interests: Prior to January 2, 2006, selected employees had been granted non-transferable member interests in IBG LLC, which conferred ownership rights in IBG LLC and entitled the holders to their proportionate share of the consolidated profits and losses of IBG LLC based on their holding percentages beginning on the date of the grant.

The Agreement as to Member Interest Purchase Rights (the Agreement) gave IBG LLC the right to repurchase any member s interests at its discretion at any time which, in particular, was triggered by the termination of employment of a member-employee, and also permitted members to sell their interests back to IBG LLC at any time, in every case for an amount equal to management s estimate of fair value, which is book value as defined in the Agreement. Because IBG LLC places a high value on the retention of its key employees, payment for a portion of redeemed interests was contingent on a post-redemption consulting services requirement that, among other conditions, required that a member-employee not compete with IBG LLC in any area of its businesses for five years following the date of redemption. In order to enforce these terms, payment for one-half of the redeemed interests was, under normal conditions, made within five months after the redemption date. Payment for the remaining one-half of the redeemed interests was made five years hence, subject to satisfaction of the consulting services and non-compete provisions of the Agreement. IBG LLC recognized compensation expense equal to the granted interest at the time of grant. If and when the terms of the five-year consulting and non-compete period were satisfied, IBG LLC recorded a distribution of redeemable members interests at such time as the remaining payment was made to the member-employee. Should any portion of a member-employee s interests be forfeited, such forfeited member interests would be redistributed among the remaining members in proportion to their holding percentages.

9. Commitments, Contingencies and Guarantees

Litigation

The Group is subject to certain pending and threatened legal actions which arise out of the normal course of business. Litigation is inherently unpredictable, particularly in proceedings where claimants seek substantial or indeterminate damages, or which are in their early stages. The Group cannot predict with certainty the actual loss or range of loss related to such legal proceedings, the manner in which they will be resolved, the timing of final resolution or the ultimate settlement. Consequently, the Group cannot estimate losses or ranges of losses related to such legal matters, even in instances where it is reasonably possible that a future loss will be incurred. In the opinion of management, after consultation with counsel, the resolution of all ongoing legal proceedings will not have a material adverse effect on the condensed consolidated financial condition, results of operations or cash flows of the Group. The Group accounts for potential losses related to litigation in accordance with SFAS No. 5

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Accounting for Contingencies. As of March 31, 2007 and December 31, 2006, reserves provided for potential losses related to litigation matters were not material.

Leases

Operating Companies have non-cancelable operating leases covering office space. All but one of the office space leases are subject to escalation clauses based on specified costs incurred by the respective landlords and contain renewal elections. In November 2005, the leases on the primary U.S. office space for the Group and its affiliates were renegotiated through January 2014, with renewal options through January 2026.

As of March 31, 2007, the Group s minimum annual lease commitments are as follows:

Year		
2007 (remaining)	$	