

CONSOLIDATED FINANCIAL STATEMENTS AND
SUPPLEMENTAL INFORMATION

TD Ameritrade, Inc.
(An Indirect Wholly Owned Subsidiary of TD Ameritrade Holding Corporation)
Year Ended September 30, 2016
With Report of Independent Registered Public Accounting Firm

This report is deemed **CONFIDENTIAL** in accordance with Rule 17a-5(e)(3).

Statement of Financial Condition bound separately has been filed with the Securities and Exchange Commission simultaneously herewith as a Public Document.

TD Ameritrade, Inc.
(An Indirect Wholly Owned Subsidiary of TD Ameritrade Holding Corporation)

Notes to the Consolidated Financial Statements

September 30, 2016

1. Basis of Presentation and Nature of Operations

The consolidated financial statements include the accounts of TD Ameritrade, Inc. and its wholly owned subsidiary (collectively, "the Company"). Intercompany balances and transactions have been eliminated. The Company is an indirect wholly owned subsidiary of TD Ameritrade Holding Corporation (the "Parent") through the Company's immediate parent, TD Ameritrade Online Holdings Corp. ("TDAOH"). The Company evaluated subsequent events through November 18, 2016, the date on which the consolidated financial statements were available to be issued.

The Company is an introducing securities broker-dealer and a registered investment advisor registered with the Securities and Exchange Commission ("SEC") and is a member of the Financial Industry Regulatory Authority ("FINRA"). The Company is required to comply with all applicable rules and regulations of the SEC and FINRA.

The Company clears its client securities transactions on a fully disclosed basis through TD Ameritrade Clearing, Inc. ("TDAC"), an indirect wholly owned subsidiary of the Parent.

2. Significant Accounting Policies

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles ("GAAP") requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Change in Accounting Policy

In the fourth quarter of fiscal year 2016, the Company elected to prospectively change the date of its annual goodwill and indefinite-lived acquired intangible asset impairment tests from September 30 to July 1 of each year, commencing on July 1, 2016. The change in the impairment testing date is preferable as it provides the Company with additional time to complete its annual impairment testing in advance of its year-end reporting. The change in the testing date did not impact the Company's financial statements.

Cash and Cash Equivalents

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

Securities Owned

Securities owned are recorded on a trade-date basis and carried at fair value, and the related changes in fair value are generally included in other revenues on the Consolidated Statement of Income.

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Notes to the Consolidated Financial Statements (continued)

Property and Equipment

Property and equipment is recorded at cost, net of accumulated depreciation and amortization. Depreciation is provided using the straight-line method over the estimated useful service lives of the depreciable property and equipment, which range from three to seven years. Leasehold improvements are amortized over the lesser of the economic useful life of the improvement or the term of the lease.

Goodwill

The Parent and TDAOH have recorded goodwill for purchase business combinations to the extent the purchase price of each completed acquisition exceeded the fair value of the net identifiable assets of the acquired company. Goodwill resulting from certain business combinations has been pushed down to the Company. The Company tests goodwill for impairment on an annual basis and more frequently as events occur or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. In performing the impairment tests, the Company utilizes quoted market prices of the Parent's common stock to estimate the fair value of the consolidated Parent. The consolidated Parent's estimated fair value is then allocated to the Parent's subsidiaries based on operating revenues and is compared with the book value of the subsidiaries. No impairment charges resulted from the annual impairment test.

Amortization of Acquired Intangible Assets

Acquired intangible assets pushed down to the Company are amortized on a straight-line basis over their estimated useful lives, ranging from 10 to 23 years.

Long-Lived Assets and Acquired Intangible Assets

The Company reviews its long-lived assets and finite-lived acquired intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. If based on that review, changes in circumstances indicate that the carrying amount of such assets may not be recoverable, the Company evaluates recoverability by comparing the undiscounted cash flows associated with the asset to the asset's carrying amount. The Company also evaluates the remaining useful lives of intangible assets to determine if events or trends warrant a revision to the remaining period of amortization.

Income Taxes

The Company files a consolidated U.S. income tax return with the Parent on a calendar year basis, combined returns for state tax purposes where required and separate state income tax returns where required. The Company determines and records income taxes as if it were a separate taxpayer, pursuant to a tax sharing agreement with the Parent. Deferred tax assets and liabilities are determined based on the difference between the financial statement carrying amounts and tax bases of assets and liabilities using enacted tax rates expected to apply to taxable income in the periods in which

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the deferred tax asset or liability is expected to be settled or realized. Uncertain tax positions are recognized if they are more likely than not to be sustained upon examination, based on the technical merits of the position. The amount of tax benefit recognized is the largest amount of benefit that is greater than 50% likely of being realized upon settlement. The Company recognizes interest and penalties, if any, related to income tax matters as part of the provision for income taxes on the Consolidated Statement of Income.

Commissions and Transaction Fees

Revenues and expenses related to client trades, including revenues from markups on riskless principal trades in fixed-income securities and an allocation of order routing revenues (also referred to as payment for order flow), are recorded on a trade-date basis, net of promotional allowances. Revenues are included in commissions and transaction fees and expenses are included in clearing and execution costs, including affiliate clearing fees, on the Consolidated Statement of Income.

Net Interest Revenue

Net interest revenue primarily consists of a share of income generated by client cash held in securities brokerage accounts and interest charged to clients on margin balances, net of interest paid to clients on their credit balances. Client cash held in securities brokerage accounts, margin balances and credit balances are held by TDAC.

Insured Deposit Account Fees

Insured deposit account fees consist of revenues resulting from the Insured Deposit Account ("IDA") agreement with TD Bank USA, N.A. ("TD Bank USA"), TD Bank, N.A. and The Toronto-Dominion Bank ("TD"). Under the IDA agreement, TD Bank USA and TD Bank, N.A., (together, the "TD Depository Institutions") make available to clients of the Company and TD Ameritrade Trust Company ("TDATC"), an indirect wholly owned subsidiary of the Parent, FDIC-insured money market deposit accounts as either designated sweep vehicles or as non-sweep deposit accounts. The Company and TDATC provide marketing and support services for the TD Depository Institutions, and TDAC acts as agent for clients of the Company and as recordkeeper for the TD Depository Institutions, in each case with respect to the money market deposit accounts. In exchange for providing these services, the TD Depository Institutions pay the Company, TDATC and TDAC (together, the "Ameritrade Companies"), collectively, an aggregate marketing fee based on the weighted average yield earned on the client IDA assets, less the actual interest paid to clients, a servicing fee to the TD Depository Institutions and the cost of FDIC insurance premiums. The IDA agreement is described further in Note 10.

Investment Product Fees

Investment product fee revenue consists of revenues earned on client assets invested in money market mutual funds, other mutual funds and certain Company-sponsored investment programs.

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Notes to the Consolidated Financial Statements (continued)

Advertising and Marketing

The Parent expenses advertising costs the first time the advertising takes place. Client cash offers are also characterized as advertising expense, rather than as a reduction of revenue, because there is generally little or no cumulative revenue associated with an individual client earning a cash offer at the time the consideration is recognized in the Consolidated Statement of Income. The Company is allocated advertising costs from entities related by common ownership.

Recently Issued Accounting Pronouncements

ASU 2016-13 — In June 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") 2016-13, *Measurement of Credit Losses on Financial Instruments*. The main objective of ASU 2016-13 is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by an entity at each reporting date. To achieve this objective, the amendments in this update replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to develop credit loss estimates. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, with early adoption permitted. Therefore, ASU 2016-13 will be effective for the Company's fiscal year beginning on October 1, 2020, using a modified retrospective approach. The Company is currently assessing the impact this ASU will have on the Company's financial statements.

ASU 2016-09 — In March 2016, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting*. The guidance in ASU 2016-09 simplifies several aspects of the accounting for share-based payment transactions, including: (1) all excess tax benefits and tax deficiencies should be recognized as income tax expense or benefit in the income statement; (2) tax effects of exercised or vested awards should be treated as discrete items in the period in which they occur; (3) excess tax benefits should be recognized regardless of whether the benefit reduces taxes payable in the current period; (4) excess tax benefits should be classified along with other income tax cash flows as an operating activity; (5) an entity can make an accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur; (6) the threshold to qualify for equity classification will permit withholding up to the maximum statutory rates in the applicable jurisdictions; and (7) cash paid by an employer when directly withholding shares for tax withholding purposes should be classified as a financing activity in the statement of cash flows. The transition requirements are dependent upon each amendment within this update and will be applied either prospectively, retrospectively or using a modified retrospective transition method. ASU 2016-09 is effective for annual periods beginning after December 15, 2016, with early adoption permitted. Therefore, ASU 2016-09 will be effective for the Company's fiscal year beginning October 1, 2017. The impact of ASU 2016-09 could be material to the Company's results of operations in future periods depending upon, among other things, the level of earnings and market price of the Parent's common stock.

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ASU 2016-02 — In February 2016, the FASB issued ASU 2016-02, *Leases*. This ASU will supersede the guidance in Accounting Standards Codification ("ASC") Topic 840, *Leases*. Under ASU 2016-02, for lease arrangements exceeding a 12-month term, a lessee will be required to recognize in the Statement of Financial Position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. ASU 2016-02 will retain a distinction between finance and operating leases; however, the principal difference from the previous guidance is that lease assets and liabilities arising from operating leases will be recognized in the Statement of Financial Position. The recognition, measurement and presentation of expenses and cash flows arising from a lease by a lessee will not significantly change from current GAAP. The accounting applied by a lessor will be largely unchanged from that applied under current GAAP. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, and will require an entity to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. Therefore, ASU 2016-02 will be effective for the Company's fiscal year beginning October 1, 2019. Early adoption is permitted. The Company is currently assessing the impact this ASU will have on the Company's financial statements.

ASU 2014-09 — In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*, to clarify the principles of recognizing revenue from contracts with customers and to improve financial reporting by creating common revenue recognition guidance for U.S. GAAP and International Financial Reporting Standards. This ASU will supersede the revenue recognition requirements in ASC Topic 605, *Revenue Recognition*, and most industry-specific guidance. Entities are required to apply the following steps when recognizing revenue under ASU 2014-09: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and, (5) recognize revenue when (or as) the entity satisfies a performance obligation. This ASU also requires additional disclosures related to the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts. An entity may apply the amendments by using one of the following two methods: (1) retrospective application to each prior reporting period presented or (2) a modified retrospective approach, requiring the standard be applied only to the most current period presented, with the cumulative effect of initially applying the standard recognized at the date of initial application. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017. Therefore, ASU 2014-09 will be effective for the Company's fiscal year beginning October 1, 2018. Early adoption is permitted for annual reporting periods beginning after December 15, 2016.

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Subsequent to issuing ASU 2014-09, the FASB issued the following standards for the purpose of clarifying certain aspects of ASU 2014-09:

- ASU 2016-08, *Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*;
- ASU 2016-10, *Identifying Performance Obligations and Licensing*; and
- ASU 2016-12, *Narrow-Scope Improvements and Practical Expedients*.

These subsequently issued ASU's have the same effective date and transition requirements as ASU 2014-09. The Company is currently assessing the impact that these revenue recognition standards will have on the Company's financial statements and is evaluating which adoption method to apply.

3. Property and Equipment

Property and equipment consists of the following as of September 30, 2016 (in millions):

Leasehold improvements	\$ 75
Computer equipment	6
Other equipment, furniture and fixtures	19
	<u>100</u>
Less accumulated depreciation and amortization	(65)
Property and equipment at cost, net	<u><u>\$ 35</u></u>

4. Goodwill and Acquired Intangible Assets

The following table summarizes changes in the Company's goodwill and acquired intangible assets for the fiscal year ended September 30, 2016 (in millions):

	<u>Goodwill</u>	<u>Acquired Intangible Assets, Net</u>
Balance as of September 30, 2015	\$ 2,297	\$ 498
Amortization of intangible assets	—	(75)
Balance as of September 30, 2016	<u><u>\$ 2,297</u></u>	<u><u>\$ 423</u></u>

Acquired intangible assets consist of the following as of September 30, 2016 (in millions):

	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
Client relationships	\$ 1,143	\$ (720)	\$ 423

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Estimated future amortization expense for acquired intangible assets outstanding as of September 30, 2016 is as follows (in millions):

<u>Fiscal Year</u>	<u>Estimated Amortization Expense</u>
2017	\$ 74
2018	70
2019	67
2020	62
2021	53
Thereafter (to 2025)	97
Total	<u>\$ 423</u>

5. Income Taxes

As of September 30, 2016, temporary differences between the consolidated financial statement carrying amounts and tax bases of assets and liabilities arise primarily from goodwill, acquired intangible assets, stock-based compensation, the federal impact of state uncertain tax positions, property and equipment and certain accrued liabilities. The Company's effective income tax rate differs from the statutory rate primarily as a result of state income taxes, and the tax benefit relating to certain federal income tax incentives.

Deferred income taxes consist of the following as of September 30, 2016 (in millions):

Deferred tax liabilities	\$ 310
Deferred tax assets	(40)
Net deferred tax liabilities	<u>\$ 270</u>

The Company's income tax returns are subject to review and examination by federal, state and local taxing authorities. The federal returns for 2012 through 2015 remain open under the statute of limitations. The years open to examination by state and local government authorities vary by jurisdiction, but the statute of limitations is generally three to four years from the date the tax return is filed. It is reasonably possible that the gross unrecognized tax benefits as of September 30, 2016, could decrease by up to \$3 million (\$2 million net of the federal benefit on state matters) within the next 12 months as a result of settlements of certain examinations or expiration of the statute of limitations with respect to other tax filings.

No material amounts were recognized for interest and penalties expense during fiscal year 2016. As of September 30, 2016, accrued interest and penalties included in accounts payable and accrued liabilities was \$1 million.

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6. Capital Requirements

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

The Company computes net capital under the alternative method as permitted by Rule 15c3-1, which requires the Company to maintain minimum net capital of the greater of \$250,000 or 2% of aggregate debit balances. Under the alternative method, a broker-dealer may not repay any subordinated borrowings, pay cash dividends or make any unsecured advances or loans to its parent company or employees if such payment would result in a net capital amount of less than (a) 5% of aggregate debit balances or (b) 120% of its minimum dollar requirement.

As of September 30, 2016, the Company's net capital was \$139 million, which exceeded the \$250,000 required net capital by \$138 million.

7. Employee Benefit Plans

The Parent has a 401(k) and profit-sharing plan covering eligible employees of the Company, under which the Company's annual profit-sharing contributions are determined at the discretion of the Parent's Board of Directors. The Company also makes matching contributions pursuant to the plan document. Profit-sharing and matching contributions expense was \$18 million for the fiscal year ended September 30, 2016, which is included in employee compensation and benefits on the Consolidated Statement of Income. The Company's employees also participate in the Parent's stock option and incentive plans. The Company recognized compensation expense of \$26 million relating to the Parent's stock option and incentive plans during the fiscal year ended September 30, 2016. Of these costs, \$11 million is included in allocated costs from affiliates and \$15 million is included in employee compensation and benefits on the Consolidated Statement of Income.

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8. Commitments and Contingencies

Lease Commitments

The Company has various non-cancelable operating leases on facilities and certain office equipment requiring annual payments as follows (in millions):

<u>Fiscal Year</u>	<u>Minimum Lease Payments</u>
2017	\$ 30
2018	28
2019	25
2020	23
2021	21
Thereafter (to 2033)	100
Total	<u>\$ 227</u>

A majority of the leases for the Company's branch offices contain provisions for renewal at the Company's option. Rental expense was \$28 million for the fiscal year ended September 30, 2016.

Borrowing Arrangements

Parent Credit Agreement – On March 31, 2015, the Parent entered into a credit agreement with the Company, which will terminate on March 1, 2022. Under this agreement, the Company may borrow up to \$50 million in cash or securities from the Parent under a committed facility. In addition, the Parent is permitted, but under no obligation, to make loans of up to \$300 million in cash or securities to the Company under an uncommitted facility.

Loans under both the committed and uncommitted facilities must be repaid with interest on or before the termination date. The applicable interest rate is calculated as a per annum rate equal to, at the Company's option, (a) LIBOR plus an interest rate margin ("LIBOR loans") or (b) the federal funds effective rate plus an interest rate margin ("Fed Funds Rate loans"). The interest rate margin ranges from 0.75% to 1.50% for both LIBOR loans and Fed Funds Rate loans, determined by reference to the Parent's public debt ratings. As of September 30, 2016, the interest rate margin would have been 1.00% for both LIBOR loans and Fed Funds Rate loans, each determined by reference to the Parent's public debt ratings. There were no borrowings outstanding under the Parent credit agreement as of September 30, 2016.

Legal and Regulatory Matters

Order Routing Matters – Five putative class action complaints were filed between August and October 2014 regarding the Company's routing of client orders. The cases were filed in, or transferred to, the U.S. District Court for the District of Nebraska: *Jay Zola et al. v. TD Ameritrade*,

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Inc., et al.; Tyler Verdieck v. TD Ameritrade, Inc.; Bruce Lerner v. TD Ameritrade, Inc.; Michael Sarbacker v. TD Ameritrade Holding Corporation, et al.; Gerald Klein v. TD Ameritrade Holding Corporation, et al. The complaints in *Zola*, *Klein* and *Sarbacker* allege that the defendants failed to provide clients with "best execution" and routed orders to the market venue that paid the most for its order flow. The complaints in *Verdieck* and *Lerner* allege that the defendant routed its clients' non-marketable limit orders to the venue paying the highest rates of maker rebates, and that clients did not receive best execution on these kinds of orders. The complaints variously include claims of breach of contract, breach of fiduciary duty, breach of the duty of best execution, fraud, negligent misrepresentation, violations of Section 10(b) and 20 of the Exchange Act and SEC Rule 10b-5, violation of Nebraska's Consumer Protection Act, violation of Nebraska's Uniform Deceptive Trade Practices Act, aiding and abetting, unjust enrichment and declaratory judgment. The complaints seek various kinds of relief including damages, restitution, disgorgement, injunctive relief, equitable relief and other relief. The Company moved to dismiss each of the five putative class action complaints. The Magistrate Judge subsequently entered Findings and Recommendations with respect to each of the five actions, recommending that the District Judge dismiss each of the five lawsuits. On March 23, 2016, the District Judge entered an order dismissing all of the state law claims in the five actions, denying the motion to dismiss the federal securities claims in the *Klein* case, and permitting the plaintiffs in the other four actions to amend their complaints to assert a federal securities claim. None of the plaintiffs in the other four actions filed an amended complaint. The plaintiffs in the *Zola*, *Sarbacker* and *Verdieck* cases filed notices of appeal. The plaintiff in the *Lerner* case did not file a notice of appeal and that case is considered closed. The *Klein* case is proceeding in the District Court. The Company intends to vigorously defend against these lawsuits. The Company is unable to predict the outcome or the timing of the ultimate resolution of these lawsuits, or the potential losses, if any, that may result.

Certain regulatory authorities are conducting examinations and investigations regarding the routing of client orders. The Company has received requests for documents and information from the regulatory authorities. The Company is cooperating with the requests.

Other Legal and Regulatory Matters – The Company is subject to a number of other lawsuits, arbitrations, claims and other legal proceedings in connection with its business. Some of these legal actions include claims for substantial or unspecified compensatory and/or punitive damages. In addition, in the normal course of business, the Company discusses matters with its regulators raised during regulatory examinations or otherwise subject to their inquiry. These matters could result in censures, fines, penalties or other sanctions. ASC 450, *Loss Contingencies*, governs the recognition and disclosure of loss contingencies, including potential losses from legal and regulatory matters. ASC 450 categorizes loss contingencies using three terms based on the likelihood of occurrence of events that result in a loss: "probable" means that "the future event or events are likely to occur;" "remote" means that "the chance of the future event or events occurring is slight;" and "reasonably possible" means that "the chance of the future event or events occurring is more than remote but less than likely." Under ASC 450, the Company accrues for losses that are considered both probable

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and reasonably estimable. The Company may incur losses in addition to the amounts accrued where the losses are greater than estimated by management, or for matters for which an unfavorable outcome is considered reasonably possible, but not probable.

The Company estimates that the aggregate range of reasonably possible losses in excess of amounts accrued is from \$0 to \$50 million as of September 30, 2016. This estimated aggregate range of reasonably possible losses is based upon currently available information for those legal and regulatory matters in which the Company is involved, taking into account the Company's best estimate of reasonably possible losses for those matters as to which an estimate can be made. For certain matters, the Company does not believe an estimate can currently be made, as some matters are in preliminary stages and some matters have no specific amounts claimed. The Company's estimate involves significant judgment, given the varying stages of the proceedings and the inherent uncertainty of predicting outcomes. The estimated range will change from time to time as the underlying matters, stages of proceedings and available information change. Actual losses may vary significantly from the current estimated range.

The Company believes, based on its current knowledge and after consultation with counsel, that the ultimate disposition of these legal and regulatory matters, individually or in the aggregate, is not likely to have a material adverse effect on the financial condition or cash flows of the Company. However, in light of the uncertainties involved in such matters, the Company is unable to predict the outcome or the timing of the ultimate resolution of these matters, or the potential losses, fines, penalties or equitable relief, if any, that may result, and it is possible that the ultimate resolution of one or more of these matters may be material to the Company's results of operations for a particular reporting period.

Income Taxes

The Company's federal and state income tax returns are subject to examination by taxing authorities. Because the application of tax laws and regulations to many types of transactions is subject to varying interpretations, amounts reported in the consolidated financial statements could be significantly changed at a later date upon final determinations by taxing authorities.

Guarantees

In the ordinary course of business, securities transactions for brokerage clients are introduced by the Company and cleared on a fully disclosed basis through TDAC. These activities may expose the Company to credit risk in the event the clients are unable to fulfill their contractual obligations. Pursuant to the clearing agreement between the Company and TDAC, TDAC charges the Company for unsecured losses that result from a client's failure to complete such transactions. As of September 30, 2016, the total amount of client margin loan balances maintained by TDAC and subject to such indemnification was approximately \$11.9 billion. TDAC seeks to mitigate the risks associated with client margin activities by requiring clients to maintain margin collateral in compliance with various regulatory and internal guidelines. The Company does not expect losses

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under the indemnification to be material to the Company's financial condition, results of operations or cash flows.

See "Insured Deposit Account Agreement" in Note 10 for a description of a guarantee included in that agreement.

9. Fair Value Disclosures

Fair Value Measurement — Definition and Hierarchy

ASC 820-10, *Fair Value Measurement*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants at the measurement date.

ASC 820-10 establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability, developed based on market data obtained from sources independent of the Company. Unobservable inputs reflect the Company's own assumptions about the assumptions market participants would use in pricing the asset or liability, developed based on the best information available in the circumstances.

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels, as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. This category includes active exchange-traded funds, money market mutual funds, mutual funds and equity securities.
- Level 2 – Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Such inputs include quoted prices in markets that are not active, quoted prices for similar assets and liabilities in active and inactive markets, inputs other than quoted prices that are observable for the asset or liability and inputs that are derived principally from or corroborated by observable market data by correlation or other means. This category includes most debt securities and other interest-sensitive financial instruments.
- Level 3 – Unobservable inputs for the asset or liability, where there is little, if any, observable market activity or data for the asset or liability.

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The following table presents the Company's fair value hierarchy for assets measured at fair value on a recurring basis as of September 30, 2016 (in millions):

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Fair Value</u>
Assets				
Cash equivalents:				
Money market mutual funds	\$ 271	\$ —	\$ —	\$ 271
Securities owned:				
U.S. government debt securities	—	100	—	100
Other	—	5	—	5
Subtotal - Securities owned	—	105	—	105
Total assets at fair value	<u>\$ 271</u>	<u>\$ 105</u>	<u>\$ —</u>	<u>\$ 376</u>

There were no transfers between any levels of the fair value hierarchy during fiscal year 2016.

Valuation Techniques

In general, and where applicable, the Company uses quoted prices in active markets for identical assets or liabilities to determine fair value. This pricing methodology applies to the Company's Level 1 assets and liabilities. If quoted prices in active markets for identical assets and liabilities are not available to determine fair value, then the Company uses quoted prices for similar assets and liabilities or inputs other than the quoted prices that are observable, either directly or indirectly. This pricing methodology applies to the Company's Level 2 assets and liabilities.

Level 2 Measurements:

Debt Securities – Fair values for debt securities are based on prices obtained from an independent pricing vendor. The primary inputs to the valuation include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in markets that are not active, contractual cash flows, benchmark yields and credit spreads. The Company validates the vendor pricing by periodically comparing it to pricing from another independent pricing service. The Company has not adjusted prices obtained from the independent pricing vendor because no significant pricing differences have been observed.

Level 3 Measurements:

The Company has no material assets or liabilities classified as Level 3 of the fair value hierarchy.

Fair Value of Financial Instruments Not Recorded at Fair Value

Receivable from affiliated clearing broker-dealer, receivable from/payable to affiliates, other receivables, and accounts payable and accrued liabilities are short-term in nature and accordingly are carried at amounts that approximate fair value. Receivable from affiliated clearing broker-

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dealer, receivable from/payable to affiliates, other receivables and accounts payable and accrued liabilities are recorded at or near their respective transaction prices and historically have been settled or converted to cash at approximately that value (categorized as Level 2 of the fair value hierarchy).

10. Related-Party Transactions

Allocated Costs from Affiliates Based on Services and Expense Allocation Agreements

The Company has system maintenance, marketing and software licensing agreements with certain affiliates. In addition, the Company is allocated certain costs from entities related by common ownership.

The expenses associated with these agreements and the allocated costs from affiliates during the fiscal year ended September 30, 2016, were as follows (in millions):

Advertising and marketing	\$ 345
Corporate overhead ⁽¹⁾	230
Technology	210
Total	<u>\$ 785</u>

⁽¹⁾ Allocated corporate overhead primarily includes costs for employee compensation and benefits, facilities, professional services and communications.

Clearing Agreement

The Company clears its clients' securities transactions through TDAC on a fully disclosed basis and receives a share of transaction fees and net interest from TDAC pursuant to the revenue sharing provisions of a clearing agreement. The Company earned \$60 million of transaction fee revenue and \$281 million of net interest revenue from TDAC during the fiscal year ended September 30, 2016, which are reflected in commissions and transaction fees and net interest revenue, respectively, on the Consolidated Statement of Income. The Company incurred clearing costs to TDAC pursuant to the provisions of the clearing agreement of \$284 million for the fiscal year ended September 30, 2016, which is included in clearing and execution costs on the Consolidated Statement of Income.

Income Taxes

The Company settles consolidated and combined current income tax payables and receivables with the Parent periodically, as amounts become due to or from the taxing authorities. Receivable from affiliates on the Consolidated Statement of Financial Condition includes \$35 million of income taxes receivable from the Parent, partially offset by other amounts due to the Parent, as of September 30, 2016.

TD Ameritrade, Inc.
(An Indirect Wholly Owned Subsidiary of TD Ameritrade Holding Corporation)

Notes to the Consolidated Financial Statements (continued)

Transactions with The Toronto-Dominion Bank and Affiliates

TD is an affiliate of the Parent, owning approximately 42% of the Parent's common stock as of September 30, 2016. The Company transacts business and has extensive relationships with TD and certain of its affiliates. Transactions with TD and its affiliates are discussed and summarized below.

Insured Deposit Account Agreement

Under the IDA agreement, the TD Depository Institutions make available to clients of the Company and TDATC FDIC-insured money market deposit accounts as either designated sweep vehicles or as non-sweep deposit accounts. The Company and TDATC provide marketing and support services for the TD Depository Institutions, and TDAC acts as agent for the clients of the Company and as recordkeeper for the TD Depository Institutions, in each case with respect to the money market deposit accounts. In exchange for providing these services, the TD Depository Institutions pay the Ameritrade Companies, collectively, an aggregate marketing fee based on the weighted average yield earned on the client IDA assets, less the actual interest paid to clients, a servicing fee to the TD Depository Institutions and the cost of FDIC insurance premiums.

The current IDA agreement became effective as of January 1, 2013 and has an initial term expiring July 1, 2018. It is automatically renewable for successive five-year terms, provided that it may be terminated by either the Ameritrade Companies or the TD Depository Institutions by providing written notice of non-renewal at least two years prior to the initial expiration date or the expiration date of any subsequent renewal period. As of July 1, 2016, notice of non-renewal was not provided by either party, therefore the IDA agreement will automatically renew on July 1, 2018.

The fee earned on the IDA agreement is calculated based on two primary components: (a) the yield on fixed-rate "notional" investments, based on prevailing fixed rates for identical balances and maturities in the interest rate swap market (generally LIBOR-based) at the time such investments were added to the IDA portfolio (including any adjustments required to adjust the variable rate leg of such swaps to a one-month reset frequency and the overall swap payment frequency to monthly) and (b) the yield on floating-rate investments. As of September 30, 2016, the IDA portfolio was comprised of approximately 68% fixed-rate notional investments and 32% floating-rate investments.

The IDA agreement provides that the Company may designate amounts and maturity dates for the fixed-rate notional investments in the IDA portfolio, subject to certain limitations. For example, if the Company designates that \$100 million of deposits be invested in 5-year fixed-rate investments, and on the day such investment is confirmed by the TD Depository Institutions the prevailing fixed yield for the applicable 5-year U.S. dollar LIBOR-based swaps is 1.45%, then the Ameritrade Companies will collectively earn a gross fixed yield of 1.45% on that portion of the portfolio (before any deductions for interest paid to clients, the servicing fee to the TD Depository Institutions and the cost of FDIC insurance premiums). In the event that (1) the federal funds effective rate is established at 0.75% or greater and (2) the rate on 5-year U.S. dollar interest rate swaps is equal to or greater than 1.50% for 20 consecutive business days, then the rate earned by the Ameritrade

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Notes to the Consolidated Financial Statements (continued)

Companies on new fixed-rate notional investments will be reduced by 20% of the excess of the 5-year U.S. dollar swap rate over 1.50%, up to a maximum of 0.10%.

The yield on floating-rate investments is calculated daily based on the greater of the following rates published by the Federal Reserve: (1) the interest rate paid by Federal Reserve Banks on balances held in excess of required reserve balances and contractual clearing balances under Regulation D and (2) the daily effective federal funds rate.

The interest rates paid to clients are set by the TD Depository Institutions and are not linked to any index. The servicing fee to the TD Depository Institutions under the IDA agreement is equal to 25 basis points on the aggregate average daily balance in the IDA accounts, subject to adjustment as it relates to deposits of less than or equal to \$20 billion kept in floating-rate investments or in fixed-rate notional investments with a maturity of up to 24 months ("short-term fixed-rate investments"). For such floating-rate and short-term fixed-rate investments, the servicing fee is equal to the difference of the interest rate earned on the investments less the FDIC premiums paid (in basis points), divided by two. The servicing fee has a floor of 3 basis points (subject to adjustment from time to time to reflect material changes to the TD Depository Institutions' leverage costs) and a maximum of 25 basis points.

In the event the marketing fee computation results in a negative amount, the Ameritrade Companies collectively must pay the TD Depository Institutions the negative amount. This effectively results in the Ameritrade Companies guaranteeing the TD Depository Institutions revenue equal to the servicing fee on the IDA agreement, plus the reimbursement of FDIC insurance premiums. The marketing fee computation under the IDA agreement is affected by many variables, including the type, duration, principal balance and yield of the fixed-rate and floating-rate investments, the prevailing interest rate environment, the amount of client deposits and the yield paid on client deposits. Because a negative marketing fee computation would arise only if there were extraordinary movements in many of these variables, the maximum potential amount of future payments the Company could be required to make under this arrangement cannot be reasonably estimated. Management believes the potential for the marketing fee calculation to result in a negative amount is remote. Accordingly, no contingent liability is carried on the Consolidated Statement of Financial Condition for the IDA agreement.

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Notes to the Consolidated Financial Statements (continued)

In addition, the Company has various other services agreements and transactions with TD and its affiliates. The following tables summarize revenues and expenses resulting from transactions with TD and its affiliates for the fiscal year ended September 30, 2016 (in millions):

Description	Statement of Income Classification	Revenue from TD and Affiliates
Insured Deposit Account Agreement	Insured deposit account fees . . .	\$ 550
Referral and Strategic Alliance Agreement	Various	14
Mutual Fund Agreements	Investment product fees	7
Other	Other revenues	1
Total revenues		<u>\$ 572</u>

Description	Statement of Income Classification	Expenses to TD and Affiliates
Canadian Call Center Services Agreement	Various ⁽¹⁾	\$ 22
Referral and Strategic Alliance Agreement	Various	2
Total Expenses		<u>\$ 24</u>

⁽¹⁾ On September 30, 2016, the Company notified TD of its intent to not extend or renew the Canadian Call Center Services Agreement. Of the \$22 million of expenses related to this agreement, \$19 million is included in professional services and \$3 million of contract termination costs are included in other expense on the Consolidated Statement of Income for the fiscal year ended September 30, 2016. The Company expects that services with the Canadian Call Center will be completed by September 30, 2017.

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Notes to the Consolidated Financial Statements (continued)

Receivables from and Payables to Affiliates

The following table summarizes the classification and amount of receivables from and payables to affiliates on the Consolidated Statement of Financial Condition resulting from related-party transactions as of September 30, 2016 (in millions):

Assets

Receivable from affiliated clearing broker-dealer		\$ 41
Receivable from affiliates:		
Receivable from TD and affiliates	\$ 3	
Receivable from entities related by common ownership	29	
Total		\$ 32

Liabilities

Payable to affiliates:		
Payable to TD and affiliates		\$ 7

Receivables from and payables to affiliates are generally settled in cash on a monthly basis.