

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

ANNUAL AUDITED REPORT
FORM X-17A-5
PART III

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FACING PAGE

Information Required of Brokers and Dealers Pursuant to Section 17 of the
Securities Exchange Act of 1934 and Rule 17a-5 Thereunder

REPORT FOR THE PERIOD BEGINNING October 1, 2018 AND ENDING September 30, 2019
MM/DD/YY MM/DD/YY

A. REGISTRANT IDENTIFICATION

NAME OF BROKER-DEALER: National Securities Corporation

ADDRESS OF PRINCIPAL PLACE OF BUSINESS: (Do not use P.O. Box No.)

5000 T-Rex Avenue, Suite 300

OFFICIAL USE ONLY

FIRM I.D. NO.

(No. and Street)

Boca Raton

FL

33431

(City)

(State)

(Zip Code)

NAME AND TELEPHONE NUMBER OF PERSON TO CONTACT IN REGARD TO THIS REPORT

Natalia Watson

561-869-5215

(Area Code - Telephone Number)

B. ACCOUNTANT IDENTIFICATION

INDEPENDENT PUBLIC ACCOUNTANT whose opinion is contained in this Report*

EisnerAmper LLP

(Name - if individual, state last, first, middle name)

750 Third Avenue

New York

NY

10017

(Address)

(City)

(State)

(Zip Code)

CHECK ONE:



Certified Public Accountant



Public Accountant



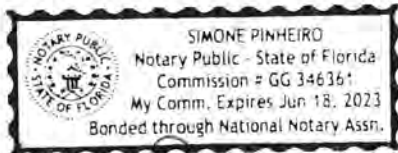
Accountant not resident in United States or any of its possessions.

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*Claims for exemption from the requirement that the annual report be covered by the opinion of an independent public accountant must be supported by a statement of facts and circumstances relied on as the basis for the exemption. See Section 240.17a-5(e)(2)

OATH OR AFFIRMATION

I, Natalia Watson, swear (or affirm) that, to the best of my knowledge and belief the accompanying financial statement and supporting schedules pertaining to the firm of National Securities Corporation, as of December 19, 20 19, are true and correct. I further swear (or affirm) that neither the company nor any partner, proprietor, principal officer or director has any proprietary interest in any account classified solely as that of a customer, except as follows:



Simone Pinheiro
Notary Public

Natalia Watson
Signature

Chief Financial Officer

Title

This report ** contains (check all applicable boxes):

- ☒ (a) Facing Page.
- ☒ (b) Statement of Financial Condition.
- ☐ (c) Statement of Income (Loss) or, if there is other comprehensive income in the period(s) presented, a Statement of Comprehensive Income (as defined in §210.1-02 of Regulation S-X).
- ☐ (d) Statement of Changes in Financial Condition.
- ☐ (e) Statement of Changes in Stockholders' Equity or Partners' or Sole Proprietors' Capital.
- ☐ (f) Statement of Changes in Liabilities Subordinated to Claims of Creditors.
- ☐ (g) Computation of Net Capital.
- ☐ (h) Computation for Determination of Reserve Requirements Pursuant to Rule 15c3-3.
- ☐ (i) Information Relating to the Possession or Control Requirements Under Rule 15c3-3.
- ☐ (j) A Reconciliation, including appropriate explanation of the Computation of Net Capital Under Rule 15c3-1 and the Computation for Determination of the Reserve Requirements Under Exhibit A of Rule 15c3-3.
- ☐ (k) A Reconciliation between the audited and unaudited Statements of Financial Condition with respect to methods of consolidation.
- ☒ (l) An Oath or Affirmation.
- ☐ (m) A copy of the SIPC Supplemental Report.
- ☐ (n) A report describing any material inadequacies found to exist or found to have existed since the date of the previous audit.

**For conditions of confidential treatment of certain portions of this filing, see section 240.17a-5(e)(3).

National Securities Corporation

(a wholly owned subsidiary of
National Holdings Corporation)

STATEMENT OF FINANCIAL CONDITION

SEPTEMBER 30, 2019

National Securities Corporation
(a wholly owned subsidiary of National Holdings Corporation)

Statement of Financial Condition and Notes

Year ended September 30, 2019

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors
National Securities Corporation

Opinion on the Financial Statement

We have audited the accompanying statement of financial condition of National Securities Corporation (the "Company") as of September 30, 2019 and the related notes (collectively referred to as the "financial statement"). In our opinion, the financial statement presents fairly, in all material respects, the financial position of the Company as of September 30, 2019, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

This financial statement is the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statement based on our audit. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement, whether due to error or fraud. Our audit included performing procedures to assess the risks of material misstatement of the financial statement, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statement. Our audit also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statement. We believe that our audit provides a reasonable basis for our opinion.



We have served as the Company's auditor since 2019.

EISNERAMPER LLP
New York, New York
December 19, 2019

National Securities Corporation

Statement of Financial Condition September 30, 2019

ASSETS

Cash	\$27,894,130
Cash deposits with clearing organizations	435,767
Securities owned, at fair value	6,150,427
Receivables from broker dealers and clearing organizations	3,105,049
Forgivable loans receivable	1,833,659
Other receivables	4,009,537
Prepaid expenses	952,830
Property and equipment, net	1,269,028
Goodwill	5,702,000
Intangibles, net	2,210,899
Due from affiliates	419,715
Deposits and other assets	245,341
Deferred tax asset	200,176
TOTAL ASSETS	<u>\$54,428,558</u>

LIABILITIES AND SHAREHOLDER'S EQUITY

Liabilities

Accrued commissions and payroll	\$16,472,114
Accounts payable and other accrued expenses	5,701,400
Deferred clearing and marketing credits	366,667
Due to affiliates	42,402
Due to parent	3,729,085
Total Liabilities	<u>26,311,668</u>

Commitments and Contingencies (Note I)

Shareholder's Equity

Common stock \$0.02 par value, 5,000,000 shares authorized, 100 shares issued and outstanding	2
Additional paid-in-capital	24,733,101
Retained earnings	3,383,787
Total Shareholder's Equity	<u>28,116,890</u>

TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	<u>\$54,428,558</u>
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National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

NOTE A - DESCRIPTION OF BUSINESS

National Securities Corporation, ("National" or the "Company"), a wholly owned subsidiary of National Holdings Corporation ("Parent"), was incorporated under the laws of the State of Washington. Its primary business is to provide financial services and products to the general public and to the financial community as a registered broker-dealer. The Company has offices throughout the United States with main offices in New York City, New York and Boca Raton, Florida.

The Company is subject to regulation by, among others, the Securities and Exchange Commission ("SEC") and Financial Industry Regulatory Authority ("FINRA").

The Company does not hold customer funds or securities. The Company clears its transactions on a fully disclosed basis through National Financial Services, LLC ("NFS"), Axos Clearing ("Axos") formerly COR Clearing LLC and Raymond James ("RJ").

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

[1] Basis of presentation

The statement of financial condition is presented in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP").

[2] Use of estimates

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

[3] Income taxes

The Company accounts for income taxes in accordance with US GAAP which requires the recognition of tax benefits or expenses based on the estimated future tax effects of temporary differences between the financial statement and tax basis of its assets and liabilities. Valuation allowances are established to reduce deferred tax assets to an amount that is more likely than not to be realized.

FASB ASC 740 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements, requiring the Company to determine whether a tax position is more likely than not to be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. For tax positions meeting the more likely than not threshold, the tax amount recognized in the financial statements is reduced by the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant taxing authority. As of September 30, 2019, the Company had no unrecognized tax positions.

The Company is included in consolidated federal and certain combined state and local income tax returns with its Parent.

[4] Cash and cash equivalents

The Company has defined cash and cash equivalents as cash held at financial institutions and highly liquid investments with original maturities of less than three months that are not held for sale in the ordinary course of business. Cash and cash equivalents held at financial institutions, at times, may exceed the amount insured by the Federal Deposit Insurance Corporation.

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

[5] Receivables from broker dealers and clearing organizations

Receivables from broker dealers and clearing organizations represent net amounts due for fees and commissions associated with the Company's retail brokerage business.

[6] Forgivable loans

Forgivable loans represent loans to primarily newly recruited independent financial advisors as an incentive for their affiliation. The notes receivable balance is comprised of unsecured non-interest-bearing and interest-bearing loans (interest ranging up to 9%). These forgivable loans are amortized over time. The Company provides an allowance for doubtful accounts on the notes based on historical collection experience and continually evaluates the receivables for collectability and possible write-offs where a loss is deemed probable. As of September 30, 2019, no allowance was considered to be required.

[7] Property and equipment, net

Property and equipment are recorded at cost net of accumulated depreciation and amortization.

[8] Deferred clearing and marketing credits

Deferred clearing and marketing credits represent clearing fee and marketing rebates from NFS. At September 30, 2019, the remaining deferred clearing and marketing rebates amounted to approximately \$250,000 and \$117,000, respectively.

[9] Goodwill and other intangible assets

Goodwill, which is not subject to amortization, is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset may be impaired. As the Company has only one reporting unit, the impairment test consists of a comparison of the fair value of the Company with the carrying amount of its net assets, including goodwill. Fair value is typically based upon estimated future cash flows discounted at a rate commensurate with the risk involved or market-based comparables. If the carrying amount of the Company's net assets exceeds the fair value of the Company, then an analysis will be performed to compare the implied fair value of goodwill with the carrying amount of goodwill. An impairment loss will be recognized in an amount equal to the excess of the carrying amount over its implied fair value. After an impairment loss is recognized, the adjusted carrying amount of goodwill is its new accounting basis. Accounting guidance on the testing of goodwill for impairment allows entities testing goodwill for impairment the option of performing a qualitative assessment to determine the likelihood of goodwill impairment and whether it is necessary to perform such two-step impairment test. The annual impairment test performed on September 30, 2019 based on a quantitative assessment did not indicate any impairment of goodwill.

Intangible assets with indefinite lives consisting of brand name are carried at cost, are not amortized and are subject to impairment testing on an annual basis through a comparison of the fair value of the assets to its carrying value. Based on the impairment test performed at September 30, 2019, there was no impairment of the brand name intangible asset. The Company utilized the relief-from-royalty method in determining the fair value of the brand name.

Intangible assets with finite lives including customer relationships are being amortized over their estimated useful lives on a straight-line basis and are tested for recoverability whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The Company assesses the recoverability of its finite-lived intangible assets by determining whether the unamortized balance can be recovered over the assets' remaining useful life through undiscounted estimated future cash flows. If undiscounted estimated future cash flows indicate that the unamortized amounts will not be recovered, an adjustment will be made to reduce such amounts to fair value based on estimated future cash flows discounted at a rate commensurate with the risk associated with achieving such cash flows. Estimated future cash flows

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

are based on trends of historical performance and the Company's estimate of future performance, giving consideration to existing and anticipated competitive and economic conditions.

[10] New accounting guidance

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers (Topic 606) which creates a single, principle-based model for revenue recognition and expands and improves disclosures about revenue. The new guidance was effective for the Company beginning October 1, 2018, and was adopted using modified retrospective approach. The Company adopted the new revenue standard on October 1, 2018 and recognized a decrease of \$135,000 to retained earnings as the cumulative effect of adoption of this accounting change. The impact of adoption is primarily related to the Company's investment banking advisory fees that were recognized as of September 30, 2018 under the previously existing accounting guidance, which would have been deferred in prior periods under the new revenue standard. Accordingly, the new revenue standard will be applied prospectively in the Company's financial statements from October 1, 2018 forward.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which supersedes the existing guidance for lease accounting, Leases (Topic 840). ASU 2016-02 requires lessees to recognize leases on their balance sheets, and leaves lessor accounting largely unchanged. The recognition of these lease assets and lease liabilities represents a change from previous US GAAP requirements, which did not require lease assets and lease liabilities to be recognized for most leases. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee, have not significantly changed from previous US GAAP requirements. The amendments in this ASU are effective for the Company beginning October 1, 2019 and interim periods within those fiscal years. As of September 30, 2019, the Company has identified its arrangements that are within the scope of the new guidance and has evaluated its portfolio of leases, which is primarily comprised of operating real estate leases for its respective offices. The Company adopted the package of practical expedients and will recognize the right to use lease assets and related lease liabilities as of the adoption date using FASB's modified retrospective approach. Prior period information will not be restated.

On adoption, the Company currently expects to recognize right-of-use assets and corresponding lease liabilities ranging from approximately \$5,500,000 to \$6,500,000 on the Company's statement of financial condition for its leases, with terms greater than twelve months. Adoption of the standard will not materially impact the Company's statement of operations or statement of cash flows.

The Company does not believe the new standard will have a material impact on its liquidity. This expectation may change as the Company's assessment is finalized.

The Company is in the process of evaluating changes to its business processes, systems and controls needed to support recognition and disclosure under the new standard. Further, the Company is continuing to assess any incremental disclosures that will be required in the Company's financial statements.

In May 2017, the FASB issued ASU 2017-09, Scope of Modification Accounting. This ASU clarifies when changes to the terms or conditions of a share-based payment award must be accounted for as modifications. Under the new guidance, modification accounting is required only if the fair value, the vesting conditions, or the classification of the award (as equity or liability) changes as a result of the change in terms or conditions. The Company adopted ASU No. 2017-09 as of October 1, 2018. The adoption of this update did not impact the Company's financial statements and related disclosures.

In August 2018, the FASB issued ASU 2018-13, "Fair Value Measurement - Disclosure Framework - Changes to the Disclosure Requirements for the Fair Value Measurement," which removes or modifies certain current disclosures, and adds additional disclosures. The changes are meant to provide more relevant information regarding valuation techniques and inputs used to arrive at measures of fair value, uncertainty in the fair value measurements, and how changes in fair value measurements impact an entity's performance and cash flows. Certain disclosures in ASU 2018-13 will need to be applied on a retrospective basis and others on a

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

prospective basis. The standard is effective for the Company beginning October 1, 2020 for both interim and annual periods. Early adoption is permitted. The company is currently assessing the impact that the adoption of ASU 2018-13 will have on its financial statements.

In August 2018, the FASB issued ASU 2018-15, "Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement that is a Service Contract". The guidance on the accounting for implementation, setup, and other upfront costs (collectively referred to as implementation costs) applies to entities that are a customer in a hosting arrangement that is a service contract. The amendments align the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by the guidance in this ASU. The standard is effective for the Company beginning October 1, 2020, should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption, and early adoption is permitted. The company early adopted ASU 2018-15 in 2019.

NOTE C – FAIR VALUE OF ASSETS AND LIABILITIES

Authoritative accounting guidance defines fair value, establishes a framework for measuring fair value, and establishes a fair value hierarchy which prioritizes the inputs to valuation techniques. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market. Valuation techniques that are consistent with the market, income or cost approach are used to measure fair value.

The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Financial assets and liabilities carried at fair value are classified and disclosed in one of the following three categories:

- Level 1 Unadjusted quoted prices in active markets for identical assets or liabilities.
- Level 2 Inputs other than quoted market prices that are observable, either directly or indirectly, and reasonably available. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability and are developed based on market data obtained from sources independent of the Company.
- Level 3 Unobservable inputs which reflect the assumptions that the Company develops based on available information about what market participants would use in valuing the asset or liability.

The following table presents the carrying values and estimated fair values at September 30, 2019 of financial assets and liabilities, excluding financial instruments that are carried at fair value on a recurring basis, and information is provided on their classification within the fair value hierarchy. Such instruments are carried at amounts that approximate fair value due to their short-term nature and generally negligible credit risk.

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

<u>Assets</u>	September 30, 2019			
	<u>Carrying Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Total Estimated Fair Value</u>
Cash	\$ 27,894,130	\$ 27,894,130	\$	\$ 27,894,130
Cash deposits with clearing organizations	435,767	435,767		435,767
Receivables from broker dealers and clearing organizations	3,105,049		3,105,049	3,105,049
Forgivable loans receivable	1,833,659		1,833,659	1,833,659
Other receivables	4,009,537		4,009,537	4,009,537
Due from affiliates	419,715		419,715	419,715
	<u>\$ 37,697,857</u>	<u>\$ 28,329,897</u>	<u>\$ 9,367,960</u>	<u>\$ 37,697,857</u>
<u>Liabilities</u>				
Accrued commissions and payroll	\$ 16,472,114		\$ 16,472,114	\$ 16,472,114
Accounts payable and other accrued expenses	5,701,400		5,701,400	5,701,400
Due to affiliates	42,402		42,402	42,402
Due to parent	3,729,085		3,729,085	3,729,085
	<u>\$ 25,945,001</u>		<u>\$ 25,945,001</u>	<u>\$ 25,945,001</u>

The following table presents the financial assets and liabilities measured at fair value on a recurring basis at September 30, 2019:

		September 30, 2019			
<u>Assets</u>	<u>Carrying Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total Estimated Fair Value</u>
Securities owned:					
Corporate stocks	\$ 13,755	\$ 13,755			\$ 13,755
Municipal Bonds	19,950	19,950			19,950
Restricted common stock	724,792		724,792		724,792
Warrants	5,391,930		1,466,618	3,925,312	5,391,930
	\$ 6,150,427	\$ 33,705	\$2,191,410	\$3,925,312	\$ 6,150,427

Changes in Level 3 assets measured at fair value on a recurring basis for the year ended September 30, 2019:

	<u>Beginning Balance as of September 30, 2018</u>	<u>Net Realized Gain or (losses)</u>	<u>Net Change in Unrealized Appreciation (Depreciation)</u>	<u>Purchases</u>	<u>Sales</u>	<u>Transfer into Level 3 (a)</u>	<u>Transfer Out of Level 3 (b)</u>	<u>Ending Balance as of September 30, 2019</u>
<u>Assets</u>								
Warrants	3,279,000	-	(72,471)	-	-	882,741	(163,958)	3,925,312

(a) The Company received warrants as part of investment banking transactions.

(b) Transfers out consist of a transfer to Level 2 of a warrant as the underlying security became a publicly registered security and a warrant exercise.

The table below presents information on the valuation techniques, significant unobservable inputs and their ranges for our financial assets measured at fair value on a recurring basis with a significant Level 3 balance.

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

Financial Instruments Owned	Fair Value	Valuation Technique	Significant Unobservable Input(s)	Input/Range
Warrants	\$ 3,925,312	Market approach	Discount for lack of marketability	21% - 44%
			Volatility	55% - 120%

Certain positions in common stock and warrants were received as compensation for investment banking services. Restricted common stock and warrants may be freely traded only upon the effectiveness of a registration statement covering them or upon the satisfaction of the requirements of Rule 144, including the requisite holding period.

Warrants are carried at fair value as determined by using the Black-Scholes option pricing model. This model takes into account the underlying securities current market values, the underlying securities market volatility, the terms of the warrants, exercise prices, and risk-free return rate. The market value of the underlying securities' market value is discounted based on the value of a protective put.

NOTE D – OTHER RECEIVABLES

Other receivables represent principally employee receivables, investment banking transactions and trailing fees due from product sponsors.

NOTE E – FORGIVABLE LOANS RECEIVABLE

From time to time, the Company may make loans, evidenced by promissory notes, primarily to newly recruited independent financial advisors as an incentive for their affiliation. The notes receivable balance is comprised of unsecured non-interest-bearing and interest-bearing loans (interest ranging up to 9%). These notes have various schedules for repayment or forgiveness based on production or retention requirements being met and mature at various dates through 2026. In the event the advisor's affiliation with the National terminates, the advisor is required to repay the unamortized balance of the note.

The Company provides an allowance for doubtful accounts on the notes based on historical collection experience and continually evaluates the receivables for collectability and possible write-offs where a loss is deemed probable. As of September 30, 2019, no allowance was considered to be required.

NOTE F – INTANGIBLES

At September 30, 2019, intangibles consisted of the following:

	Estimated Useful Life (years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Brand name	indefinite	\$ 410,000	-	\$ 410,000
Customer relationships	10	4,300,000	2,517,768	1,782,232
Software license	3	44,800	26,133	18,667
		<u>\$ 4,754,800</u>	<u>\$ 2,543,901</u>	<u>\$ 2,210,899</u>

NOTE G - NET CAPITAL AND OTHER REGULATORY REQUIREMENTS

The Company is subject to the Securities and Exchange Commission Uniform Net Capital Rule (Rule 15c3-1), which, among other things, requires the maintenance of minimum net capital. At September 30, 2019, the Company had net capital of \$5,887,912, which was \$4,887,912 in excess of its required net capital of \$1,000,000.

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

The Company claims exemption from the provisions of the SEC's Rule 15c3-3 pursuant to paragraphs (k) (2) (i) and (ii) since the Company is an introducing broker dealer that clears all transactions on a fully disclosed basis and promptly transmits all customer funds and securities to clearing brokers.

NOTE H - INCOME TAXES

The Company is included in the consolidated federal and certain combined state and local income tax returns with its Parent. For financial reporting purposes, the Company determines its income tax provision on a separate company basis. Taxes currently payable by the Company on a separate company basis will be paid to its Parent, or reduce amounts due to its parent.

Deferred tax amounts are comprised of the following at September 30, 2019:

Deferred tax assets:	
Federal net operating loss carryforwards	\$ 15,057
Stock-based compensation	839,710
Accrued compensation	641,678
Other accruals	553,474
Total deferred tax assets	<u>2,049,919</u>
Deferred tax liability:	
Property and equipment	(113,961)
Securities	(1,160,886)
Intangibles	(574,896)
Total deferred tax liability	<u>(1,849,743)</u>
Net	<u>\$ 200,176</u>

At September 30, 2019, the Company, on a separate company basis, has Federal net operating loss carryforwards of approximately \$72,000, which expires in various years from 2021 through 2031.

NOTE I - COMMITMENTS AND CONTINGENCIES

[1] Leases

The Company is obligated under several non-cancelable operating lease agreements for office space, expiring in various years through 2030. Minimum lease payments are as shown in the table below.

In October 2018, the Company entered into an agreement to lease equipment under a capital lease for 24 months. The equipment under the lease is collateral for the lease obligation and is included within fixed assets in the statement of financial condition. The leased equipment is amortized on a straight line basis over 7 years. The interest rate related to the lease obligation is 5.6 percent and the maturity date is September 2020. The capital lease obligation is included within accounts payable and other accrued expenses in the statement of financial condition.

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

Year Ending September 30,	Operating Leases	Capital Lease
2020	\$807,000	\$297,000
2021	842,000	-
2022	845,000	-
2023	865,000	-
2024	821,000	-
Thereafter	3,311,000	-
Total minimum lease payments	7,491,000	297,000
Less: Amounts representing interest not yet incurred		10,000
Present value of minimum lease payments		287,000

[2] Litigation and regulatory matters

The Company is a defendant or respondent in various pending and threatened arbitrations, administrative proceedings and lawsuits seeking compensatory damages. Several cases have no stated alleged damages. Claim amounts are infrequently indicative of the actual amounts the Company will be liable for, if any. Further, the Company has a history of collecting amounts awarded in these types of matters from its brokers that are still affiliated, as well as from those that are no longer affiliated. Many of these claimants also seek, in addition to compensatory damages, punitive or treble damages, and all seek interest, costs and fees. These matters arise in the normal course of business. The Company intends to vigorously defend itself in these actions, and the ultimate outcome of these matters cannot be determined at this time.

On July 3, 2019, a lawsuit was filed against the Company, the Parent and certain of its subsidiaries, the Parent's current board members and certain former board members, certain officers of the Parent, John Does 1–10, and the Parent as a nominal defendant, in the United States District Court for the Southern District of New York, captioned *Kay Johnson v. National Securities Corporation, et al.*, Case No. 1:19-cv-06197-LTS. The complaint presents three purported derivative causes of action on behalf of the Company, and five causes of action by the plaintiff directly. As part of the derivative claims, the complaint generally alleges that certain of the individual defendants failed to establish and maintain adequate internal controls to ensure that the Board acted in accordance with its fiduciary duties to prevent and uncover alleged legal and regulatory misconduct and wrongdoing on the part of a National officer. As part of its claims brought directly by the plaintiff, the complaint generally alleges that certain individual and corporate defendants wrongfully terminated the employment of the plaintiff in violation of the Dodd-Frank Act and applicable common law, or conspired to do so. The complaint further alleges that certain corporate defendants violated the Equal Pay Act with regards to the plaintiff's compensation. The complaint seeks monetary damages in favor of the Company, an order directing the Company's board members to take actions to enhance the Company's governance, compensatory and punitive damages in favor of the plaintiff, and attorneys' fees and costs. The Company has notified its insurer of the lawsuit and believes it has valid defenses to the asserted claims of the complaint.

Liabilities for potential losses from complaints, legal actions, government investigations and proceedings are established where management believes that it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. In making these decisions, management bases its judgments on its knowledge of the situations, consultations with legal counsel and its historical experience in resolving similar matters. In many lawsuits, arbitrations and regulatory proceedings, it is not possible to determine whether a liability has been incurred or to estimate the amount of that liability until the matter is close to resolution. However, accruals are reviewed regularly and are adjusted to reflect management's estimates of the impact of developments, rulings, advice of counsel and any other information pertinent to a particular matter. Because of the inherent difficulty in predicting the ultimate outcome of legal and regulatory actions,

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

management cannot predict with certainty the eventual loss or range of loss related to such matters. As of September 30, 2019, the Company accrued approximately \$1,817,000 for these matters which is included in accounts payable and other accrued expenses in the statement of financial condition. Awards ultimately paid, if any, may be covered by our errors and omissions insurance policy. While the Company will vigorously defend itself in these matters, and will assert insurance coverage and indemnification to the maximum extent possible, there can be no assurance that such matters will not have a material adverse impact on the Company's financial position, results of operations or cash flows.

NOTE J - OFF-BALANCE-SHEET RISK AND CONCENTRATIONS OF CREDIT RISK

The Company is engaged in trading and providing a broad range of securities brokerage and investment services to a diverse group of retail and institutional clientele, as well as corporate finance and investment banking services to corporations and businesses. Counterparties to the Company's business activities include broker-dealers and clearing organizations, banks and other financial institutions. The Company uses clearing brokers to process transactions and maintain customer accounts for the Company on a fee basis. The Company permits the clearing firms to extend credit to its clientele secured by cash and securities in the client's account. The Company's exposure to credit risk associated with the non-performance by its customers and counterparties in fulfilling their contractual obligations can be directly impacted by volatile or illiquid trading markets, which may impair the ability of customers and counterparties to satisfy their obligations to the Company. The Company has agreed to indemnify the clearing brokers for losses they incur while extending credit to the Company's customers.

It is the Company's policy to review, as necessary, the credit standing of its customers and counterparties. Amounts due from customers that are considered uncollectible by the clearing broker are charged back to the Company by the clearing broker when such amounts become determinable. Upon notification of a charge back, such amounts, in total or in part, are then either (i) collected from the customers, (ii) charged to the broker initiating the transaction, and/or (iii) charged to operations, based on the particular facts and circumstances.

The Company maintains cash in bank deposit accounts which, at times, may exceed federally insured limits. The Company has not experienced and does not expect to experience any losses on such accounts.

To the extent the Company invests in marketable securities, the Company is subject to various market risks related to the portfolio.

NOTE K - RELATED PARTY TRANSACTIONS

The Company entered into a service agreement, as amended in November 2015, with its Parent, whereby the Parent charges the Company for certain employees, insurance and benefits coverage, rent and utilities, software, equipment, email services, office supplies and travel costs as needed.

The Company entered into a service agreement, as amended in November 2015, with its affiliate, National Tax and Financial Services ("National Tax"), a wholly owned subsidiary of the Parent, whereby National Tax provides the Company with certain services related to its former brokerage operation, which the Parent transferred to the Company in November 2013, principally for accounting, compliance, supervision, information technology, human resources and corporate administrative support services. Additionally, rent and related utilities, advertising, recruiting, general insurance, office supplies, postage and overnight delivery and meals and entertainment may also be furnished as needed.

National Securities Corporation

Notes to Statement of Financial Condition September 30, 2019

NOTE L – PROPERTY AND EQUIPMENT

At September 30, 2019, property and equipment consisted of the following:

	September 30, 2019	Estimated Useful Lives
Equipment and software	\$ 535,991	3 - 6
Furniture and fixtures	203,407	5
Capital leases	509,483	3 - 7
Leasehold improvements	565,792	Lesser of useful life or term of lease
	1,814,673	
Less accumulated depreciation and amortization	(545,645)	
Property and equipment, net	<u>\$ 1,269,028</u>	