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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 06/29/02 AND ENDING 06/27/03
MM/DD/YY MM/DD/YY

A. REGISTRANT IDENTIFICATION

NAME OF BROKER-DEALER: Southwest Securities, Inc.
ADDRESS OF PRINCIPAL PLACE OF BUSINESS: (Do not use P.O. Box No.)
1201 Elm Street, Suite 3500
(No. and Street)
Dallas, TX 75270
(City) (State) (Zip Code)

OFFICIAL USE ONLY
FIRM I.D. NO.

NAME AND TELEPHONE NUMBER OF PERSON TO CONTACT IN REGARD TO THIS REPORT
Laura Leventhal 214/859-1026
(Area Code - Telephone Number)

B. ACCOUNTANT IDENTIFICATION

INDEPENDENT PUBLIC ACCOUNTANT whose opinion is contained in this Report*
PricewaterhouseCoopers LLP
(Name - if individual, state last, first, middle name)
2001 Ross Avenue, Suite 1800, Dallas, TX 75201-2997
(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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THOMSON FINANCIAL

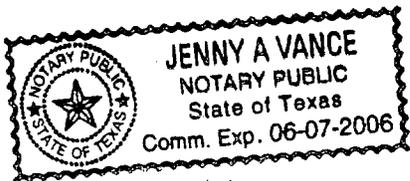
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*Claims for exemption from the requirement that the annual report be covered by the opinion of an independent public accountant must be supported by a statement of facts and circumstances relied on as the basis for the exemption. See Section 240.17a-5(e)(2)

Handwritten initials/signature

OATH OR AFFIRMATION

I, Daniel Leland, swear (or affirm) that, to the best of my knowledge and belief the accompanying financial statement and supporting schedules pertaining to the firm of Southwest Securities, Inc., as of June 27, 2003, 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:



Jenny A Vance
Notary Public

Signature: Daniel Leland
Title: President

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

- (a) Facing Page.
(b) Statement of Financial Condition.
(c) Statement of Income (Loss).
(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 15c3-3 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).



Southwest Securities, Inc.

(A Subsidiary of SWS Group, Inc.)

Financial Statements and Supplemental Schedules

Pursuant to Rule 17a-5 of the

Securities and Exchange Commission

For the Year Ended June 27, 2003

With Report of Independent Auditors

Report of Independent Auditors

To the Board of Directors and Stockholders of
Southwest Securities, Inc.

In our opinion, the accompanying statement of financial condition and the related statements of operations, stockholders' equity, changes in liabilities subordinated to claims of general creditors and cash flows present fairly, in all material respects, the financial position of Southwest Securities, Inc. (the "Company") (a subsidiary of SWS Group, Inc.) at June 27, 2003, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information contained in Schedules I, II and III is presented for purposes of additional analysis and is not a required part of the basic financial statements, but is supplementary information required by Rule 17a-5 under the Securities Exchange Act of 1934. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

PricewaterhouseCoopers LLP

July 31, 2003

Southwest Securities, Inc
(A Subsidiary of SWS Group, Inc.)
Statement of Financial Condition

June 27, 2003

(dollars in thousands, except par and redemption values)

ASSETS	
Cash	\$ 22,038
Assets segregated for regulatory purposes	441,184
Receivable from brokers, dealers and clearing organizations	2,487,962
Receivable from clients	297,238
Securities owned, at market value	113,122
Exchange memberships, at cost (market value of \$1,777)	240
Fixed assets, at cost, less accumulated depreciation of \$18,650	13,843
Goodwill, net of accumulated amortization of \$912	6,302
Other assets (including \$30,168 from affiliates)	53,542
Total assets	<u>\$ 3,435,471</u>
LIABILITIES AND STOCKHOLDERS' EQUITY	
Payable to brokers, dealers, and clearing organizations	\$ 2,407,070
Payable to clients	706,003
Drafts payable	29,332
Securities sold, not yet purchased, at market value	40,585
Capital lease obligation	1,248
Accrued expenses and other liabilities (including \$6,952 to affiliates)	57,260
	<u>3,241,498</u>
Liabilities subordinated to claims of general creditors	-
Stockholders' equity:	
Series A preferred stock, \$20 par value, \$1,000 redemption value; authorized 100,000 shares; issued and outstanding 150 shares	3
Class A voting common stock of \$1 par value; authorized 10,000 shares; issued and outstanding 2,820 shares	3
Class B nonvoting common stock of \$1 par value; authorized 10,000 shares; none issued	-
Additional paid-in capital	32,487
Retained earnings	161,480
	<u>193,973</u>
Total liabilities and stockholders' equity	<u>\$ 3,435,471</u>

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

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Statement of Operations
Year Ended June 27, 2003
(dollars in thousands)

Revenues:	
Net revenues from clearing operations	\$ 20,660
Commissions	64,559
Interest	52,400
Investment banking, advisory and administrative fees	25,050
Net gains on principal transactions	15,062
Other	4,714
	<hr/>
Total revenue	182,445
Expenses:	
Commissions and other employee compensation	96,308
Interest	28,025
Occupancy, equipment and computer service costs	26,169
Communications	10,758
Floor brokerage and clearing organization charges	6,335
Advertising and promotional	3,355
Other	14,630
	<hr/>
	185,580
	<hr/>
Loss before income taxes	(3,135)
Income tax benefit	(1,350)
	<hr/>
Net loss	\$ (1,785)
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The accompanying notes are an integral part of these financial statements.

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Statement of Stockholders' Equity
Year Ended June 27, 2003
(dollars in thousands)

	Series A preferred stock		Class A voting common stock		Additional paid-in capital	Retained Earnings	Total
	Shares	Amount	Shares	Amount			
Balance at June 28, 2002	250	\$ 5	2,820	\$ 3	\$ 32,585	\$ 163,265	195,858
Net loss	-	-	-	-	-	(1,785)	(1,785)
Purchase of preferred stock	(100)	(2)	-	-	(98)	-	(100)
Balance at June 27, 2003	150	\$ 3	2,820	\$ 3	\$ 32,487	\$ 161,480	\$ 193,973

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

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
**Statement of Changes in Liabilities Subordinated
to Claims of General Creditors**
Year Ended June 27, 2003
(dollars in thousands)

Balance at June 28, 2002	\$	43,000
Note payment		<u>(43,000)</u>
Balance at June 27, 2003	\$	<u>-</u>

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

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Statement of Cash Flows
Year Ended June 27, 2003
(dollars in thousands)

Cash flows from operating activities:	
Net loss	\$ (1,785)
Adjustments to reconcile net loss to net cash provided by operating activities:	
Depreciation and amortization	4,241
Deferred income taxes	68
Provision for doubtful accounts	755
Changes in operating assets and liabilities:	
Assets segregated for regulatory purposes	1,473
Brokers, dealers and clearing organizations accounts, net	(78,307)
Clients accounts, net	127,138
Securities owned	(17,070)
Other assets	37,021
Drafts payable	(5,199)
Securities sold, not yet purchased	21,354
Accrued expenses and other liabilities	5,670
Net cash provided by operating activities	<u>95,359</u>
Cash flows from investing activities:	
Goodwill recognized	(927)
Purchase of fixed assets	(4,244)
Net cash used in investing activities	<u>(5,171)</u>
Cash flows from financing activities:	
Purchase of preferred stock	(100)
Repayment of subordinated debt	(43,000)
Repayment of capital lease obligation	(901)
Repayment of short-term borrowings	(37,600)
Net cash used in financing activities	<u>(81,601)</u>
Net change in cash	8,587
Cash at beginning of year	13,451
Cash at end of year	<u>\$ 22,038</u>
Supplemental cash flow disclosures	
Cash paid for interest	<u>\$ 28,801</u>
Cash paid for taxes	<u>\$ -</u>
Significant non-cash investing and financing activities	
Transfer of goodwill from parent	<u>\$ 5,190</u>
Capital lease obligation	<u>\$ 1,848</u>

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

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
(dollars in thousands, except par and redemption values)

1. Organization

Southwest Securities, Inc. ("Company"), a subsidiary of SWS Group, Inc. ("Parent"), is a registered broker/dealer in securities under the Securities Exchange Act of 1934 (Act).

The annual financial statements are prepared as of the close of business on the last Friday of June. Accordingly, the fiscal year for 2003 ended on June 27, 2003.

Pursuant to the Securities and Exchange Commission's ("SEC") Rule 11(a) of the Act, over 50% of the Company's revenues are comprised of Section 11(a) items, indicating the Company is primarily engaged in trading on behalf of customers.

2. Summary of Significant Accounting Policies

Securities Transactions

Proprietary securities transactions in regular-way trades are recorded on trade date, as if they had settled. Customers' securities and commodities transactions are reported on a settlement date basis with related commission income and expenses reported on a trade date basis.

Amounts receivable and payable for securities transactions that have not reached their contractual settlement date are recorded net on the statement of financial condition.

Marketable securities are valued at market value, based on quoted market prices, and securities not readily marketable are valued at fair value as determined by management.

Commissions

Commissions and related clearing expenses are recorded on a trade-date basis as securities transactions occur.

Fixed Assets

Fixed assets are comprised of furniture, equipment and leasehold improvements which are stated at cost and depreciated using the straight-line method over the estimated useful lives of the assets (3 to 9 years).

In fiscal year 2003, the Company wrote off fully depreciated assets of \$699.

Goodwill

The Parent transferred goodwill of \$5,190 (net of accumulated amortization of \$912) to the Company. The transfer was recorded through the intercompany accounts, and therefore was a non-cash transaction to the Company.

The Company adopted SFAS No. 142, "*Goodwill and Other Intangible Assets*", on June 29, 2002. SFAS No. 142 addresses financial accounting and reporting for acquired goodwill. This statement also addresses how goodwill and other intangibles should be accounted for after they have been initially recognized in the financial statements. SFAS No. 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead be tested for impairment at least annually. The statement also provides specific guidance for impairment testing.

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
(dollars in thousands, except par and redemption values)

The Company completed its initial and annual reviews during fiscal year 2003. Based on the results of these tests, the Company's goodwill balance is not impaired.

In accordance with SFAS No. 142, the Company ceased amortizing its goodwill at the date of adoption, and recorded no amortization expense for the year ended June 27, 2003.

Resale and Repurchase Agreements

Transactions involving purchases of securities under agreements to resell (reverse repurchase agreements or reverse repos) or sales of securities under agreements to repurchase (repurchase agreements or repos) are accounted for as collateralized financings except where the Company does not have an agreement to sell (or purchase) the same or substantially the same securities before maturity at a fixed or determinable price. It is the policy of the Company and subsidiaries to obtain possession of collateral with a market value equal to or in excess of the principal amount loaned under resale agreements. Collateral is valued daily, and the Company may require counterparties to deposit additional collateral or return collateral pledged when appropriate.

Securities-Lending Activities

Securities borrowed and securities loaned transactions are generally reported as collateralized financings except where letters of credit or other securities are used as collateral. Securities-borrowed transactions require the Company to deposit cash, letters of credit, or other collateral with the lender. With respect to securities loaned, the Company receives collateral in the form of cash or other collateral in an amount generally in excess of the market value of securities loaned. The Company monitors the market value of securities borrowed and loaned on a daily basis, with additional collateral obtained or refunded as necessary.

Investment Banking

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

Drafts Payable

In the normal course of business, the Company uses drafts to make payments relating to its brokerage transactions. These drafts are presented for payment through the Company's bank and are sent to the Company daily for review and acceptance. Upon acceptance, the drafts are paid and charged against cash.

Cash Flow Reporting

For purposes of the statement of cash flows, the Company considers cash to include cash on hand and in depository accounts. In addition, highly liquid debt instruments purchased with original maturities of three months or less are considered to be cash equivalents.

Assets segregated for regulatory purposes are not included as cash equivalents for purposes of the statement of cash flows because such assets are segregated for the benefit of customers only.

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
(dollars in thousands, except par and redemption values)

Federal Income Taxes

The Company files a consolidated Federal income tax return with its Parent. For purposes of these financial statements current income taxes are computed as if the Company filed a separate entity income tax return.

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Fair Value of Financial Instruments

Substantially all of the Company's financial assets and liabilities are carried at market value or at amounts which, because of their short-term nature, approximate current fair value.

Use of Estimates

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

3. Assets Segregated For Regulatory Purposes

At June 27, 2003, the Company had U.S. Treasury securities with a market value of approximately \$248,143, reverse repurchase agreements of approximately \$191,990, and related accrued interest of approximately \$51 segregated in special reserve bank accounts for the exclusive benefit of customers under Rule 15c3-3 of the Act. These reverse repurchase agreements were collateralized by U.S. Government securities with a market value of approximately \$194,647. The Company also had approximately \$1,000 in reverse repurchase agreements, in special reserve bank accounts for the Proprietary Accounts of Introducing Brokers ("PAIB") at June 27, 2003. The reverse repurchase agreements in the PAIB accounts were collateralized by U.S. Government securities with a market value of approximately \$1,003.

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
(dollars in thousands, except par and redemption values)

4. Receivable From and Payable to Brokers, Dealers and Clearing Organizations

At June 27, 2003, the Company had receivable from and payable to brokers, dealers and clearing organizations comprised of the following:

Receivable:	
Securities failed to deliver	\$ 55,337
Securities borrowed	2,401,664
Correspondent broker/dealers	18,104
Clearing organizations	5,717
Other	7,140
	<u>\$ 2,487,962</u>
Payable:	
Securities failed to receive	\$ 62,723
Securities loaned	2,303,994
Correspondent broker/dealers	16,016
Other	24,337
	<u>\$ 2,407,070</u>

Securities failed to deliver and receive represent the contract value of securities that have not been delivered or received subsequent to settlement date. Securities borrowed and loaned represent deposits made to or received from other broker/dealers relating to these transactions. These deposits approximate the market value of the underlying securities.

The Company clears securities transactions for correspondent broker/dealers. Settled securities and related transactions for these correspondents are included in the receivable from and payable to brokers, dealers and clearing organizations. The Company holds collateral for the receivables from correspondents.

The Company participates in the securities borrowing and lending business by borrowing and lending securities other than those of its clients. All open positions are adjusted to market values daily. The Company has received collateral of approximately \$2,401,664 under securities lending agreements, of which the Company has repledged approximately \$2,286,526 at June 27, 2003.

5. Receivable From and Payable to Clients

Receivable from and payable to clients include amounts due on cash and margin transactions. Included in these amounts are receivable from and payable to noncustomers (as defined by Rule 15c3-3 of the Act, principally officers, directors and related accounts), which aggregated approximately \$1,211 and \$3,827, respectively, at June 27, 2003. Securities accounts of noncustomers are subject to the same terms and regulations as those of customers. Securities owned by customers and noncustomers that collateralize the receivables are not reflected in the accompanying financial statements.

Southwest Securities, Inc.
 (A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
 (dollars in thousands, except par and redemption values)

The Company pledges client securities as collateral in conjunction with the Company's securities lending activities. At June 27, 2003, the Company has approximately \$389,240 of client securities under customer margin loans that are available to be pledged, of which the Company has repledged approximately \$16,753 under securities loan agreements.

The Company pays interest on certain customer "free credit" balances available for reinvestment. The aggregate balance of such funds was approximately \$620,140 at June 27, 2003. During fiscal year 2003, the interest rates paid on these balances ranged from 0.60% to 1.00%. While the Company pays interest on these funds at varying rates, the rate paid at June 27, 2003 was 0.60%. The weighted average interest rate paid during fiscal 2003 was 0.82%.

The Company maintains an allowance for doubtful accounts which represents amounts, in the judgment of management, that are necessary to adequately absorb losses from known and inherent risks in receivables from customers. Provisions made to this allowance are charged to operations. At June 27, 2003, all unsecured customer receivables had been provided for in this allowance.

6. Securities Owned and Securities Sold, not yet Purchased

At June 27, 2003, securities owned and securities sold, not yet purchased, both of which are carried at market value, included the following:

Securities owned:

U.S. Government and Government agency obligations	\$ 17,666
Municipal obligations	35,404
Corporate equity securities	5,856
Corporate obligations	46,240
Other	7,956
	<u>\$ 113,122</u>

Securities sold, not yet purchased:

U.S. Government and Government agency obligations	\$ 9,047
Municipal obligations	726
Corporate equity securities	1,515
Corporate obligations	29,040
Other	257
	<u>\$ 40,585</u>

Certain of the above securities have been collateralized to secure short-term borrowings or as security deposits at clearing organizations for the Company's clearing business. These collateralized securities amounted to approximately \$1,945 at June 27, 2003. Additionally, at June 23, 2003, the Company had pledged securities valued at \$242 in conjunction with securities lending activities.

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
(dollars in thousands, except par and redemption values)

7. Short-Term Borrowings

The Company has credit arrangements with commercial banks, which include broker loan lines up to \$275,000 at June 27, 2003 to finance securities owned, securities held for correspondent broker/dealer accounts, and receivables in customers' margin accounts. The lines may also be used to release pledged collateral against day loans. These credit arrangements are provided on an "as offered" basis and are not committed lines of credit. These arrangements can be terminated at any time by the lender. Any outstanding balances under these credit arrangements are due on demand and bear interest at rates indexed to the federal funds rate (1.06% at June 27, 2003). There were no amounts outstanding under these agreements at June 27, 2003.

Additionally, the Company has an irrevocable letter of credit agreement aggregating \$57,000 at June 27, 2003, pledged to support its open option positions with an options clearing organization. The letter of credit bears interest at the broker call rate, if drawn, and is renewable annually. This letter of credit is fully collateralized by marketable securities held in customers' and noncustomers' margin accounts with values of approximately \$76,298 at June 27, 2003. The Company also has an unsecured letter of credit agreement aggregating \$2,250 at June 27, 2003, pledged to support its open positions with securities clearing organizations. The unsecured letter of credit bears interest at the prime rate plus 3%, if drawn, and is renewable semi-annually.

In addition, the Company has an unsecured line of credit aggregating \$10,000 that is due on demand and bears interest at rates indexed to the federal funds rate. There was no amount outstanding on this unsecured line of credit at June 27, 2003.

8. Capital Lease Obligation

The Company leases computer equipment through two capital leases. The two leases require monthly payments of \$11 and \$73 and expire on September 30, 2004 and 2005. The future minimum lease payments required under the capital leases (together with the present value of net minimum lease payments) at June 27, 2003 are as follows:

<u>Fiscal Year</u>	
2004	\$ 1,016
2005	255
	<hr/>
Total minimum lease payments	1,271
Less imputed interest	(23)
	<hr/>
Present value of net minimum lease payments	\$ 1,248

9. Income Taxes

The Company files a consolidated tax return with the Parent. For purposes of these financial statements, current income taxes are computed as if the Company files a separate entity income tax return.

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
(dollars in thousands, except par and redemption values)

Income tax benefit for the fiscal year ended June 27, 2003, (effective rate of 43.1% in 2003) differs from the amount that would otherwise have been calculated by applying the U.S. Federal corporate tax rate (35% in 2003) to loss before income taxes and is comprised of the following:

Income tax benefit at the statutory rate	\$ (1,097)
Tax-exempt interest	(495)
Non-deductible meals and entertainment expenses	279
Other, net	<u>(37)</u>
	<u>\$ (1,350)</u>

Income taxes as set forth in the statement of operations consist of the following components:

Current	\$ (1,418)
Deferred	<u>68</u>
Total income taxes	<u>\$ (1,350)</u>

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at June 27, 2003 are presented below:

Deferred tax assets:	
Expenses for book, not deductible until paid	\$ 4,236
Management incentive compensation	713
Loss on impairment of assets	1,072
Other	<u>399</u>
Total gross deferred tax asset	<u>6,420</u>
Deferred tax liabilities - other	<u>(250)</u>
Net deferred tax asset included in other assets	<u>\$ 6,170</u>

As a result of the Company's history of taxable income and the nature of the items from which deferred tax assets are derived, management believes that it is more likely than not that the Company will realize the benefit of the deferred tax assets.

10. Liabilities Subordinated to Claims of General Creditors

Liabilities subordinated to claims of general creditors represent loans from the Parent. The loans are covered by agreements approved by the New York Stock Exchange, Inc., and are thus available to the Company in computing net capital under the Securities and Exchange Commission's Uniform Net Capital Rule ("Rule 15c3-1"). The subordinated liabilities of \$43,000 were repaid during fiscal year 2003.

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
(dollars in thousands, except par and redemption values)

11. Net Capital Requirements

The Company is subject to the Securities and Exchange Commission's Uniform Net Capital Rule, which requires the maintenance of minimum net capital. The Company has elected to use the alternative method, permitted by the rule, which requires that it maintain minimum net capital, as defined in Rule 15c3-1 under the Act, equal to the greater of \$1,500 or 2% of aggregate debit balances, as defined in Rule 15c3-3 of the Act. At June 27, 2003, the Company had net capital of approximately \$102,736 which is approximately \$93,841 in excess of its minimum net capital requirement of approximately \$8,895 at that date. Additionally, Rule 15c3-1 provides that equity capital may not be withdrawn or cash dividends paid if resulting net capital would be less than 5% of aggregate debit items. At June 27, 2003, the Company had net capital of approximately \$80,498 in excess of 5% of aggregate debit items.

12. Affiliate Transactions

The Company clears all customer transactions and provides accounting and administrative services for three affiliates, SWS Financial Services, Inc. ("SWSFS"), Mydiscountbroker.com, Inc. ("MDB") and May Financial Corporation ("May"). Based on agreements with these entities, the Company receives a fee for clearing SWSFS, MDB and May trades. The amount of fees received by the Company for clearing trades for these entities' trades was approximately \$1,403 during fiscal year 2003.

The Company, as clearing broker for its affiliates, has the right to charge customer losses back to the affiliates.

13. Profit Sharing

The Company has a defined contribution profit sharing/401(k) plan covering substantially all employees. Employer provided profit sharing benefits become fully vested after six years of service by the participant. Profit sharing contributions to the plan are accrued and funded at the Company's discretion. There was no profit sharing expense for the year ended June 27, 2003. The 401(k) portion of the plan began in January 2000, and the Company provides a match of up to 4% of eligible compensation. The Company's matching contributions vest immediately and the expense totaled approximately \$2,009 for the year ended June 27, 2003.

14. Commitments and Contingencies

The Company leases its offices under noncancelable operating lease agreements. During fiscal year 2003, the Company entered into various noncancelable operating lease agreements relating to data processing equipment used in the brokerage operations. Rental expense relating to the facilities and equipment leases for fiscal year 2003 aggregated approximately \$14,145.

Southwest Securities, Inc.
(A Subsidiary of SWS Group, Inc.)
Notes to Financial Statements
(dollars in thousands, except par and redemption values)

At June 27, 2003 the future rental payments for the noncancelable operating leases for each of the following five fiscal years and thereafter follows (in thousands):

2004	\$	8,421
2005		4,640
2006		4,608
2007		4,510
2008		3,899
Thereafter		1,276
	\$	<u>27,354</u>

In the general course of its brokerage business and the business of clearing for other brokerage firms, the Company has been named as a defendant in various lawsuits and arbitration proceedings. These claims allege violation of Federal and state securities laws. Management believes that resolution of these claims will not result in any material adverse effect on the Company's financial position or results of operations.

15. Financial Instruments with Off-Balance-Sheet Risk

In the normal course of business, the Company engages in activities involving the execution, settlement and financing of various securities transactions. These activities may expose the Company to off-balance-sheet credit and market risks in the event the customer or counterparty is unable to fulfill its contractual obligation. Such risks may be increased by volatile trading markets.

As part of its normal brokerage activities, the Company sells securities not yet purchased (short sales) for its own account. The establishment of short positions exposes the Company to market risk in the event prices increase, as the Company may be obligated to acquire the securities at prevailing market prices.

The Company seeks to control the risks associated with its customers' activities, including customer accounts of its correspondents for which it provides clearing services, by requiring customers to maintain margin collateral in compliance with various regulatory and internal guidelines. The required margin levels are monitored daily and, pursuant to such guidelines, customers are required to deposit additional collateral or to reduce positions when necessary.

A portion of the Company's customer activity involves short sales and the writing of option contracts. Such transactions may require the Company to purchase or sell financial instruments at prevailing market prices in order to fulfill the customers' obligations.

At times, the Company lends money using reverse repurchase agreements. All positions are collateralized by U.S. Government or U.S. Government agency securities. The Company generally has such securities deposited in a trustee account designated for the exclusive benefit of the Company's customers. Such transactions may expose the Company to off-balance-sheet risk in the event such borrowers do not repay the loans and the value of collateral held is less than that of the underlying receivable. These agreements provide the Company with the right to maintain the relationship between market value of the collateral and the receivable. At June 27, 2003, the Company had no repurchase agreements outstanding.

Southwest Securities, Inc.

(A Subsidiary of SWS Group, Inc.)

Notes to Financial Statements

(dollars in thousands, except par and redemption values)

The Company arranges secured financing by pledging securities owned and unpaid customer securities for short-term borrowings, securities loaned and to satisfy margin deposits of clearing organizations. The Company also actively participates in the borrowing and lending of securities other than those of its customers. In the event the counterparty in these and other securities loaned transactions is unable to return such securities pledged or repay the deposit placed with them, the Company may be exposed to the risks of acquiring the securities at prevailing market prices or holding collateral possessing a market value less than that of the related pledge securities. The Company seeks to control the risks by monitoring the market value of securities pledged and requiring adjustments of collateral levels where necessary.

16. Preferred Stock

On October 17, 1997, the Company's Board of Directors ("Board") authorized 100,000 shares of preferred stock. Simultaneously, the Board designated 5,000 shares of the authorized preferred stock as Series A Preferred Stock. Up to 50 shares of the Series A Preferred Stock, which has a par value of \$20, can be issued to each of up to 100 qualified participants. Qualified participants are broker/dealers registered under the Act who clear their proprietary transactions through the Company and who represent that they are subject to net capital rules of the SEC and other self-regulatory organizations to which such broker/dealers report. The Series A Preferred Stock is nonvoting and nonconvertible to common stock, and it is entitled to noncumulative cash dividends when, as and if declared by the Board. The Series A Preferred Stock is redeemable at any time by the Company at a redemption price of \$1,000 per share. During fiscal year 2003, the Company bought back 100 shares of the Series A Preferred Stock.

17. PAIB Reserve Requirements

At June 27, 2003, the company had a PAIB reserve requirement of \$1,546 and after a deposit of \$1,700, made after year end but within the timeframe required by the rule, had a deposit of \$2,700.

Southwest Securities, Inc.**(A Subsidiary of SWS Group, Inc.)****Schedule I – Computation of Net Capital Pursuant to Rule 15c3-1 of the Securities Exchange Act of 1934****(dollars in thousands)**

Total stockholders' equity from statement of financial condition		\$	193,973
Add liabilities subordinated to claims of general creditors allowable in computation of net capital			<u>-</u>
Total capital and allowable subordinated liabilities			<u>193,973</u>
Deductions and /or charges:			
Receivable from affiliates	\$	(30,168)	
Fixed assets, net		(13,843)	
Other nonallowable assets		(29,888)	
Aged fails to deliver		(176)	
Aged short security differences		(1,195)	
Other deductions and/or charges		<u>(5,913)</u>	<u>(81,183)</u>
Net capital before haircuts on securities positions			112,790
Haircuts on securities positions			<u>(10,054)</u>
Net Capital			102,736
Net capital requirement:			
Greater of 2% of aggregate debit items as shown in computation of special reserve requirement on Schedule II ($\$444,760 \times 2\% = \$8,895$) or \$1,500			<u>8,895</u>
Excess net capital			<u>\$ 93,841</u>
Net capital in excess of the greater of 5% of aggregate debit items or \$1,800			<u>\$ 80,498</u>

Note: The above computation does not differ materially from the computation of net capital prepared by the Company as of June 27, 2003 and filed with the New York Stock Exchange, Inc. on July 23, 2003 on Form X-17A-5.

Southwest Securities, Inc.

(A Subsidiary of SWS Group, Inc.)

Schedule II – Computation for Determination of Reserve Requirements

Pursuant to Rule 15c3-3 of the Securities Exchange Act of 1934

(dollars in thousands)

Credit balances:

Free credit balances and other credit balances in customers' security accounts	\$	732,507
Monies borrowed collateralized by securities carried for the accounts of customers		348
Monies payable against customers' securities loaned		17,468
Customers' securities failed to receive		55,243
Credit balances in firm accounts which are attributable to principal sales to customers		2,050
Market value of stock dividends, stock splits and similar distributions receivable outstanding over 30 calendar days		316
Market value of short securities and credits in all suspense accounts over 30 calendar days		849
Transfers in excess of 40 calendar days		476
Other		53,406
Total credits		862,663

Debit balances:

Debit balances in customers' cash and margin accounts excluding unsecured accounts and accounts doubtful of collection		295,648
Securities borrowed to effectuate short sales by customers and securities borrowed to make delivery on customers' securities failed to deliver		51,860
Failed to deliver of customers' securities not older than 30 calendar days		50,919
Margin required and on deposit with the Options Clearing Corporation for all option contracts with or purchased in customer accounts		46,333
Total debits		444,760
Less 3% haircut		(13,343)
Total debits		431,417
Excess of total credits over total debits	\$	431,246

Reserve requirement at June 27, 2003:

Amount of securities held in "Reserve Bank Accounts" at June 27, 2003	\$	440,184
Deposit made within required time frames of qualified securities		14,200
Amount of securities held in "Reserve Bank Accounts"	\$	454,384

Note: The above computation does not differ materially from the computation of special reserve requirement prepared by the Company as of June 27, 2003 and filed with the New York Stock Exchange, Inc. on July 23, 2003 on Form X-17A-5.

Southwest Securities, Inc.
 (A Subsidiary of SWS, Inc.)
Schedule III – Information for Possession or Control Requirements
Pursuant to Rule 15c3-3 of the Securities Exchange Act of 1934
 (dollars in thousands)

State the market valuation and the number of items of:

- 1. Customers' fully paid securities and excess margin securities not in the respondent's possession or control as of June 27, 2003 for which instructions to reduce to possession or control had been issued as of June 27, 2003 but for which the required action was not taken by respondent within the time frames specified under Rule 15c3-3

Number of items	19
Market Value	\$ 226

- 2. Customers' fully paid securities and excess margin securities for which instructions to reduce to possession or control had not been issued as of June 27, 2003 excluding items arising from "temporary lags which result from normal business operations" as permitted under Rule 15c3-3

Number of items	-
Market Value	\$ -

**Independent Auditors Report on Internal Control Required
By SEC Rule 17a-5 and CFTC Regulation 1.16**

To the Board of Directors
Southwest Securities, Inc.

In planning and performing our audit of the financial statements and supplemental schedules of Southwest Securities, Inc. (the "Company") (a subsidiary of SWS Group, Inc.) for the fiscal year ended June 27, 2003, we considered its internal control, including control activities for safeguarding securities, in order to determine our auditing procedures for the purpose of expressing our opinion on the statements and not to provide assurance on the internal control.

Also, as required by Rule 17a-5(g)(1) of the Securities and Exchange Commission (the "SEC"), and Regulation 1.16 of the Commodity Futures Trading Commission, (the "CFTF") (collectively, the "Commissions"), we have made a study of the practices and procedures followed by the Company, including tests of compliance with such practices and procedures, that we considered relevant to the objectives stated in Rule 17a-5(g) and CFTC Regulation 1.16, in the following:

1. Making the periodic computations of aggregate indebtedness and net capital under Rule 17a-3(a)(11) and the reserve required by Rule 15c3-3(e);
2. Making the quarterly securities examinations, counts, verifications, and comparisons, and the recordation of differences required by Rule 17a-13;
3. Complying with the requirements for prompt payment for securities under Section 8 of Federal Reserve Regulation T of the Board of Governors of the Federal Reserve System;
4. Obtaining and maintaining physical possession or control of all fully paid and excess margin securities of customers as required by Rule 15c3-3; and
5. Making the periodic computations of minimum financial requirements pursuant to Regulation 1.17.

Because the Company does not carry commodity accounts for customers or perform custodial functions relating to customers' commodity accounts; we did not review the practices and procedures followed by the Company in any of the following:

1. Making the daily computations of the segregation requirements of Section 4d(2) of the Commodity Exchange Act and the regulations thereunder, and the segregation of funds based upon such computations; and
2. Making the daily computations of the foreign futures and foreign options secured amount requirements pursuant to Regulation 30.7 of the CFTC.

The management of the Company is responsible for establishing and maintaining internal control and the practices and procedures referred to in the preceding paragraph. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control and of the practices and procedures referred to in the preceding paragraph, and to assess whether those practices and procedures can be expected to achieve the Commissions' above-mentioned objectives. Two of the objectives of internal control and the practices and procedures are to provide management with

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reasonable, but not absolute, assurance that assets for which the Company has responsibility are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Rule 17a-5(g) and Regulation 1.16 list additional objectives of the practices and procedures listed in the preceding paragraph.

Because of inherent limitations in internal control or the practices and procedures referred to above, errors or fraud may occur and not be detected. Also, projection of any evaluation of internal control to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the effectiveness of their design and operation may deteriorate.

Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the specific internal control components does not reduce to a relatively low level the risk that error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving internal control, including procedures for safeguarding customer and firm assets, including securities, that we consider to be material weaknesses as defined above.

We understand that practices and procedures that accomplish the objectives referred to in the second paragraph of this report are considered by the Commissions to be adequate for its purposes in accordance with the Securities Exchange Act of 1934, the Commodity Exchange Act and related regulations, and that practices and procedures that do not accomplish such objectives in all material respects indicate a material inadequacy for such purposes. Based on this understanding and on our study, we believe that the Company's practices and procedures were adequate at June 27, 2003 to meet the Commissions' objectives.

This report is intended solely for the information and use of the Board of Directors, management, the SEC, the CFTC, the National Association of Securities Dealers, Inc., the New York Stock Exchange, the National Futures Association and other regulatory agencies that rely on Rule 17a-5(g) under the Securities Exchange Act of 1934 in their regulation of registered brokers and dealers, or Regulation 1.16 under the Commodity Exchange Act, and is not intended to be and should not be used by anyone other than these specified parties.

PriceWaterhouseCoopers LLP

July 31, 2003