

# Advisory Services

**Financial Planning**



**Waddell & Reed, Inc.**  
**SEC File Number: 16720**  
**Part 2A of Form ADV: Firm Brochure**  
**Financial Planning Services Brochure**  
**The date of this Brochure is: December 26, 2016**

*This brochure provides information about the qualifications and business practices of Waddell & Reed, Inc. If you have any questions about the contents of this brochure, please contact us at (1-888-Waddell and/or [financialplanning@waddell.com](mailto:financialplanning@waddell.com)). The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission or by any state securities authority.*

Additional information about Waddell & Reed, Inc. is also available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

Waddell & Reed, Inc. is a Federally registered Investment Advisor and a broker-dealer and member of FINRA.

*Note: Registration with the SEC as an Investment Advisor does not imply a certain level of skill or training.*

This brochure and the services and fees described in this brochure are all subject to change without prior notice to you.

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For more information about Waddell & Reed, Inc. please visit our website at [www.waddell.com](http://www.waddell.com)

## **Summary of Changes**

Since our last Part 2A filing, Waddell & Reed has updated this brochure to include information related to its Financial Planning Activities. Items that have been updated include:

1. The addition of information which reflects that the firm recently entered into a consent order with the New Hampshire Bureau of Securities related to the actions of a New Hampshire investment advisory representative.

# Advisory Services

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## Advisory Business

The following discussion presents an overview of Waddell & Reed, Inc. and discusses generally the Financial Planning and related products and services we offer and our corporate structure. This section contains certain defined terms that will be used throughout the Brochure:

### Overview and Ownership

Waddell & Reed, Inc. (Waddell & Reed) is a securities broker-dealer and a registered investment advisor serving clients nationwide. Waddell & Reed was founded in 1937 and emphasizes comprehensive financial planning and provides a variety of personal financial services and investment opportunities. Through the financial planning process, Financial Advisors can help clients identify their unique financial goals and develop a plan to meet those goals. And, Financial Advisors have access to a broad array of investment and insurance products and services that can help satisfy their clients' planning needs.

Waddell & Reed is a wholly owned subsidiary of Waddell & Reed Financial, Inc., a publically held company (NYSE: WDR). Waddell & Reed provides highly competitive mutual fund offerings, including the Waddell & Reed Advisors Funds, the Ivy Funds, the Ivy Funds VIP offered within variable insurance products provided by our strategic insurance partners (currently Minnesota Life Insurance Company and Nationwide Life Insurance Companies (collectively the "Strategic Partners")) and the Waddell & Reed InvestEd Portfolios offered within Waddell & Reed's 529 Plan (collectively the "Waddell & Reed Mutual Funds").

As part of an organization that manages and offers the Waddell & Reed Mutual Funds, Financial Advisors have direct access to portfolio managers and other professionals who are involved in analyzing and managing the Waddell & Reed Mutual Funds on an ongoing basis. Therefore, Financial Advisors have the opportunity to know the Waddell & Reed Mutual Funds well. Waddell & Reed believes this close alignment between our Financial Advisors and mutual fund managers is of enormous benefit to the firm's Financial Advisors and, more importantly, to the firm's clients.

Of course, as needed or desired, Financial Advisors can offer Mutual Funds and other products that are not proprietary to Waddell & Reed. They may do so when the Waddell & Reed Mutual Funds may not satisfy your goals fully or it may be in your best interests to consider other investment options consistent with your personal and financial goals. Waddell & Reed investment philosophy has always been and continues to be today:

#### **Focus on growing and protecting investors' assets:**

a sound approach that seeks to capture asset appreciation when market conditions are favorable, and strives to manage risk consistent with the objectives of the Waddell & Reed Mutual Funds.

**Rigorous fundamental research:** an enduring investment culture that dedicates itself to analyzing companies on its own rather than relying solely on outside research and trends.

## Advisory Services Generally

Waddell & Reed believes that financial planning should be the cornerstone to a well-balanced investment program. That is why Financial Advisors are trained to encourage clients at every stage of life to create a comprehensive financial plan before deciding to purchase investment products and how to allocate those products among various asset classes. To be effective the financial planning process requires you and your Financial Advisor to each engage in the process in different ways.

### Your Financial Advisor will:

- Conduct an initial consultation to determine your personal concerns, priorities and financial goals.
- Determine the appropriate advisory service for your situation and the applicable fee.
- Schedule additional consultations to discuss your advisory needs and goals.
- Review and analyze the information you provide.
- Summarize your situation and develop specific strategies, solutions or actionable recommendations that will address your particular concerns, financial goals and advisory needs in the form of a written personal financial plan that your Financial Advisor will deliver to you.

### Financial Planning must be an interactive process to be successful. As such, you will:

- Work with your Financial Advisor to determine the appropriate financial planning goals to be addressed during the term of our engagement.
- Identify any material life events, economic factors, changes in your financial situation, goals or any other issues that may cause a change in the advice given by your Financial Advisor and notify your Financial Advisor of such changes.
- Pay a fee to your Financial Advisor for his or her financial planning services and attention to your financial goals and advisory needs. This fee is separate from any compensation you will pay or that your Financial Advisor may receive for or in connection with product sales, such as commissions.
- Understand the benefits of and limits to the financial planning process and form reasonable expectations with respect to the results to be obtained from your personal financial plan and recommended investment strategy.

Your Financial Advisor relies primarily on the information you provide to create your financial plan and to ensure the suitability of investment and insurance products that your Financial Advisor may recommend. Therefore, the accuracy of the recommendations made by your Financial Advisor will depend directly on the accuracy of the information you provide with respect to your personal data, assets and liabilities, income and expenses, assumed overall expected rates of interest and inflation, short-term and long-term financial and personal goals, risk tolerance and other relevant information requested by your Financial Advisor. In addition to your personal information, your Financial Advisor may use, as necessary, financial planning publications and tools, training courses and materials, prospectuses and regulatory filings, financial information prepared by product sponsors and issuers, marketing material prepared by product sponsors, and product analyses prepared by third parties.

A personal financial plan will address your financial planning goals and objectives as you describe them to your Financial Advisor. Your financial planning goals and potential strategies recommended to help meet your goals will be addressed in the context of your overall financial situation. Depending on the level of service you select, your Financial Advisor will provide an analysis and summary of your current situation, compare it to your stated financial goals, offer appropriate strategies or alternatives, and make actionable recommendations to help you achieve your financial goals.

**All investment illustrations included in your financial plan are hypothetical and do not reflect actual investment results or provide guarantees of future results. You are not obligated to implement any investment recommendations through your Financial Advisor or Waddell & Reed.**

## Financial Planning Services

This section describes the financial planning services currently offered by Waddell & Reed:

### FOCUSPlan<sup>SM</sup> Forecast

This level of service provides a limited analysis of accumulation and/or protection goals, centering on five possible basic modules: Financial Independence (Retirement), Education funding, Survivor Needs, Long-Term Care and Disability needs.

### FOCUSPlan<sup>SM</sup> Start-Up-Plan

This level of service provides a FOCUSPlan<sup>SM</sup> that includes a written analysis containing a Financial Profile and two or more other Select Modules, as described below, to address basic financial issues using simplified planning assumptions and calculations. You may choose whichever Select Modules pertain to your personal financial concerns, interests and needs.

### FOCUSPlan<sup>SM</sup>

This level of service provides a planning foundation that includes a written analysis containing a Financial Profile and three or more Select Modules (which are describe on the next page) to address specific financial issues. You may choose whichever Select Modules pertain to your personal financial concerns, interests and needs.

## Tax-Sensitive Planning Analysis

This level of service enhances a FOCUSPlan<sup>SM</sup>, as described above, by including tax-sensitive calculations. This service can generally analyze the potential impact of taxes on various accumulation and distribution strategies and the general tax treatment of investment returns, as well as the general tax status of individual assets as they are liquidated to provide income during life events. Any analysis of potential tax consequences associated with your investment and financial planning decisions should not be construed as tax advice or a substitute for advice regarding your personal situation from a qualified tax advisor. Please consult your tax advisor regarding the potential tax consequences associated with your investment and financial planning decisions.

## Detailed Cash Flow Analysis

This level of service enhances the FOCUSPlan<sup>SM</sup> and Tax Sensitive Planning Analysis, as described above, by including detailed analysis of current and future cash flows. This service allows for greater flexibility and accuracy of planning projections while planning for life events such as paying for college expenses, selling a home, divorce, the death of a spouse or retirement.

## FOCUSPlan<sup>SM</sup> Premier

This service is an in-depth financial planning service utilizing Waddell & Reed's home office planning staff. We provide detailed analysis of advanced retirement planning and/or estate planning strategies. In addition, this service can address almost any other financial consideration or concern, such as cash flow, education funding, disability income, survivor needs and stock options.

## FOCUSPlan<sup>SM</sup> Select Modules

Select Modules address financial planning considerations regarding specific financial issues or goals. You may select whichever Select Modules pertain to your personal financial concerns, interests and needs, as follows:

**Financial Profile:** This module includes a summary of your financial concerns and goals, current net worth and may include cash flow statements detailing sources of income and expenses. It may also include information when dealing with specific life changing events and may include graphs detailing allocation percentages and surplus income that may be available for financial goals and additional savings objectives.

**Financial Independence (Retirement):** This module analyzes projected retirement income and expenses based on defined retirement goals. The analysis outlines potential retirement shortages or surpluses and provides possible savings and investment combinations to help meet your retirement capital and income needs.

**Survivor Income Needs:** This module analyzes the potential financial impact of each person's death based on defined financial goals. It also outlines resources available, immediate expenses, survivor income needs and additional assets required to achieve stated financial goals under capital retention or depletion methods.

**Education Funding:** This module analyzes educational planning goals for specified education periods. The analysis may include current assets available, potential additional savings required under both level and inflation-adjusted savings methods, and the effect on cash flows if no savings are in place.

**Estate Review:** This module analyzes your current estate, including various existing estate planning techniques and strategies, such as wills, revocable trusts, irrevocable trusts, and gifting programs.

**Asset Allocation:** This module provides basic asset allocation strategies for specific financial objectives based on individual time horizons and risk tolerance levels. It also may be accompanied by specific recommendations made by Waddell & Reed in its capacity as a broker-dealer for investment products (including the Waddell & Reed Mutual Funds). It may also analyze your current mutual fund holdings and aid in developing asset allocation strategies specific to current and recommended Mutual Fund investments.

**Income Tax:** This module calculates and summarizes your projected federal and state tax brackets and estimated taxable income or potential tax refunds due based on current year tax and income information. It can also analyze the impact of various changes in tax strategy with regard to current tax planning alternatives and anticipated changes in income, filing status and qualified plan contributions. Waddell & Reed does not provide specific accounting or tax advice. Please consult your tax advisor for tax advice regarding your personal situation.

**Goal Funding:** This module analyzes specific financial goals. The analysis will include current savings, monthly additions to savings, and the affect on cash flows when no savings are present. The resulting analysis may also outline the additional lump sum or annual savings required under both a level savings and inflation-adjusted savings method.

**Disability Income:** This module analyzes the potential impact of a permanent disability on defined financial goals over specified time periods.

**Long-Term Care:** This module analyzes the potential impact of long-term care expenses on assets available for other financial goals and objectives.

## SUPPLEMENTAL SERVICES/STRATEGIES

The following services may be added to, or provided separate from, any of the above Waddell & Reed FOCUSPlan<sup>SM</sup> services:

**Investment Planning Services (INVESTMENTPlan):** This service provides advanced asset allocation strategies for specific financial objectives based on individual time horizons and risk tolerance levels.

It also may be accompanied by specific recommendations made by Waddell & Reed in its capacity as a broker-dealer regarding selection of a model portfolio or custom optimization to create a personalized asset mix for investment positions and monthly savings. This may include a recommendation to invest in one or more of the Waddell & Reed Mutual Funds. It may also provide advanced classification of your current and recommended holdings and aid in developing asset allocation strategies specific to current and recommended investments.

**Wealth Forecasting Service (Monte Carlo Analysis):** This service analyzes the probability of success of your current and proposed financial plans and investment strategies, using a statistical analysis that considers the impact and likelihood of various economic uncertainties, including investment volatility.

**Estate Planning Strategies:** This service analyzes your current estate and the effects of implementing various estate planning techniques and strategies, such as wills, revocable trusts, irrevocable trusts and gifting programs. Waddell & Reed provides neither legal or tax advice. Please consult your tax advisor for tax advice regarding your personal situation.

**Business Planning Strategies:** This service analyzes the value of a business under multiple valuation methods. It can also address issues important to business continuity planning and assist with executive compensation planning. It does not address business funding or the issuance of securities by the business, such as stock, debt, partnership interests, LLC interests, etc.

## Re-FOCUSPlan<sup>SM</sup>

This service re-examines your current financial situation with regard to any Waddell & Reed financial planning services purchased and delivered within the preceding 24 months. This service enables you to update your original financial plan to reflect changes in your financial situation, previous assumptions or goals.

## FOCUSPlan<sup>SM</sup> Step-Up

At any time within 90 days after the completion of any financial planning services, you may purchase additional planning services to upgrade the original planning services to a higher level.

During the financial planning process, your Financial Advisor may review and evaluate assets maintained in your retirement plans (i.e. 401(k), 457 and 403(b) plan accounts) and in brokerage or other accounts held at financial services firms other than Waddell & Reed or its affiliates. These accounts may contain individual stocks and bonds or other securities. Although your Financial Advisor may consider these assets in their comprehensive financial planning process, they cannot actively manage these assets. They can only actively manage assets held in a W&R investment advisory fee-based account or program.

## FINANCIAL ANALYSIS TOOLS

The financial planning service(s) you select may be prepared using one or more of the following tools:

**The projections or other information generated by the financial planning software tools used by Financial Advisors that include the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investments and are not guarantees of future results.**

**Financial Planning Tools:** The financial planning service(s) you select may be implemented using financial planning software tools developed by Waddell & Reed or third parties.

**Asset Allocation Tools:** Asset allocation tools may assist you in determining if you have an appropriate mix of investments for your personal situation. Development of a personalized asset allocation is designed to assist you in positioning your assets, based on your financial objectives, time horizons and risk tolerance. You may receive a report that contains hypothetical illustrations using assumed rates of return that are based on information you have provided to your Financial Advisor and from sources believed to be reliable. Depicted rates of return are not representative of the actual rate of return that you will experience with any particular insurance or investment product. Such illustrations may be based on the concepts of Modern Portfolio Theory, which states that through diversification you may be able to minimize the effects of investment risks and that gains in one investment class may help offset losses in another. There is no certainty that any investment or strategy will be profitable or successful in achieving your specific investment objectives. Principal values of your investments will fluctuate and, when redeemed, may be worth more or less than your original investment. Asset allocation does not ensure a profit or protect against losses in a declining market.

Asset mixes in this analysis are derived using available historical information for each asset class based on the selected index for that class. They are meant only to illustrate the relative experience between asset classes and portfolios. Other asset classes and indices may have characteristics similar or superior to those being analyzed in any given scenario.

If you have a substantial percentage of your net worth concentrated in a given asset or asset class, the asset allocation process may prompt your Financial Advisor to recommend that you sell a significant portion of that asset or asset class in order to potentially reduce risk by reducing the concentrated positions within your portfolio. This is particularly true if the asset in question is stock of your employer, given that both your income and investment could be tied to the fortunes of your employer. Before you actually sell any assets, it is very important that you consult with your legal and tax advisors regarding the tax and other implications of any such sale. There is a significant risk of adverse tax consequences if your proposed transactions have not properly been evaluated by your legal and tax advisors. Your legal and tax advisors should ensure that the proposed transactions have been properly structured to

minimize tax effects. Neither Waddell & Reed nor your Financial Advisor, in his or her capacity as a registered representative or an investment advisor representative, provide the specialized, detailed legal or tax advice necessary to ensure that you avoid adverse tax consequences.

The optimal portfolio mix for a particular client is determined based on a variety of factors, including age, risk tolerance, goals and objectives, time horizon and historical performance of different asset classes. However, the analysis does not provide a comprehensive financial analysis of your ability to reach your goals, and it does not identify the impact of your investment strategy on your tax and estate planning situations. These components of financial planning are more appropriately handled by a comprehensive financial analysis. Generally, periodic rebalancing of your portfolio and re-optimization among the asset classes is recommended. Waddell & Reed does not provide discretionary money management services as part of its FOCUSPlan<sup>SM</sup> services.

**Monte Carlo Engine:** Your Financial Advisor may use a tool with a Monte Carlo simulation engine. Monte Carlo engines are based on different assumptions that lead to varying probabilities of success among various investment scenarios. When interpreting your probability of success, it is important to review the underlying assumptions included in your financial plan, to determine if and how those assumptions may apply to your actual personal financial situation. The assumptions used to generate your personal financial plan are likely different than the assumptions found in other Monte Carlo simulations. As a result, you are likely to receive a substantially different simulation success rate when you use our Monte Carlo simulation engine. Additionally, the results you achieve using our Monte Carlo engine may vary with each subsequent use and over time. The probability of success may also vary from one planning period to the next due to your changing circumstances and updated market information. Results are hypothetical and reflect only one point in time. Therefore, we strongly recommend that you revisit your Monte Carlo simulation analysis at least annually to accommodate these changes and updates.

The probability of success is only one factor to consider in financial planning. Other important factors include recommendations of your Financial Advisor and other professionals, your personal and financial goals and objectives, your investment risk tolerance, your desired lifestyle currently and in retirement and your needs for special protections, such as insurance or investment products intended to meet specific needs.

Other Advisory Services

Waddell & Reed also offers fee-based asset allocation and wrap fee programs. These investment programs are tailored to your individual needs. You may impose reasonable restrictions on investing in certain types of securities in these programs. These asset allocation and wrap fee programs are described in significant detail in separate brochures used to offer these unique products. In addition, clients may pay a separate fee for a financial plan prior to investing in a wrap fee program that may include certain bundled financial planning services at no additional charge.

Fees and Compensation

**Financial Planning Fees and Compensation:** Waddell & Reed charges different fees for each Financial Planning Service. Our fixed and variable fee schedules are presented below.

Fixed Fees

Certain Waddell & Reed Financial Advisors charge fixed fees for financial planning services. Those fees are listed below. Fixed fees are not negotiable.

Service	Fee
FOCUSPlan <sup>SM</sup> Premier	\$3,000
FOCUSPlan <sup>SM</sup> with Tax-Sensitive Planning Analysis and Detailed Cash Flow Analysis	\$900
Includes a Financial Profile plus a Tax-Sensitive Planning Analysis and Detailed Cash Flow Analysis of three (3) or more of the Select Modules below, depending on your situation and needs.	
FOCUSPlan <sup>SM</sup> with Tax-Sensitive Planning Analysis	\$700
Includes the Financial Profile plus a Tax-Sensitive Planning Analysis of three (3) or more of the Select Modules below, depending on your situation and needs.	
FOCUSPlan <sup>SM</sup>	\$500
Includes a Financial Profile plus three (3) or more of the Select Modules below, depending on your situation and needs.	
FOCUSPlan <sup>SM</sup> Start-Up Plan	\$300
Includes a Financial Profile and an analysis of two (2) or more Select Modules, as described below, depending on your situation and needs.	
FOCUSPlan <sup>SM</sup> Forecast	\$200
Includes a Financial Profile and a limited analysis on two (2) or more of the following analyses: Financial Independence (Retirement), Education funding, Survivor Needs, Long-Term Care and Disability needs.	



## FOCUSPlan<sup>SM</sup> Select Modules \$200 per module

Includes the Financial Profile at no cost with the purchase of one or two of the modules listed below:

Financial Profile (no cost)  
Income Tax  
Financial Independence (Retirement)  
Goal Funding  
Survivor Income Needs  
Disability Income  
Education Funding  
Long-Term Care  
Estate Review  
Asset Allocation

## Supplemental Services/Strategies

The following Supplemental Services and Strategies may be added to, or purchased separately from, the FOCUSPlan<sup>SM</sup> services:

<b>Investment Planning Services (INVESTMENTPlan)</b>	<b>\$400</b>
<b>Wealth Forecasting Service</b>	<b>\$200</b>
<b>Estate Planning Strategies</b>	<b>\$500</b>
<b>Business Planning Strategies</b>	<b>\$300</b>
<b>Re- FOCUSPlan<sup>SM</sup></b>	

Re-FOCUSPlan fees vary. A discount, up to 50% off the Fixed Fees listed above, may be offered if the same services were purchased and delivered within the previous 24 months. A minimum Re-FOCUSPlan fee of \$200 applies.

## FOCUSPlan<sup>SM</sup> Step-Up

Step-Up fee will be the difference between the applicable charges for the financial planning services desired and the fees paid for financial planning service(s) received within the past 90 days.

## Variable Fees

Waddell & Reed permits certain Financial Advisors to charge variable fees for financial planning services. Such fees are negotiable and are subject to acceptance by the client. Among the factors that may be taken into consideration in determining a variable fee are:

- (1) The amount of time the Financial Advisor expects to spend completing the particular financial planning services involved and providing related advice and assistance,
- (2) The complexity of the client's financial planning issues and needs,
- (3) The extensiveness and complexity of the data needed regarding the client's income, expenses, assets and liabilities,
- (4) The client's net worth or the value of the client's investment accounts and/or other assets that are the subject of the financial planning services provided, and
- (5) Special circumstances related to life change, marital status, health or special income needs, and growth or decline of a personal business.

The fees charged may vary from one client to another and from one Financial Advisor to another, depending on various factors, including differences in:

- (1) The client's situations,
- (2) The levels of experience of the Financial Advisors,
- (3) The geographic locations of the clients and Financial Advisors, and
- (4) The extent of supplemental services rendered in connection with the financial planning services provided.

Certain Financial Advisors are permitted to charge variable fees for financial planning services. Variable fees are negotiable and must not exceed the maximum fee for the respective service provided, as set forth below:

<u>Service</u>	<u>Maximum Fee</u>
<b>FOCUSPlan<sup>SM</sup> Premier</b>	<b>\$15,000*</b>

*\*Under certain circumstances and only with prior approval of the Financial Advisors Division in the home office, fees may exceed \$15,000 for highly complex financial planning situations.*

<b>FOCUSPlan<sup>SM</sup> with Tax-Sensitive Planning Analysis And Detailed Cash Flow Analysis</b>	<b>\$5,000</b>
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Includes the Financial Profile plus Tax-Sensitive Planning Analysis and Detailed Cash Flow Analysis of three (3) or more of the Select Modules below, depending on your situation and needs.

<b>FOCUSPlan<sup>SM</sup> with Tax-Sensitive Planning Analysis</b>	<b>\$4,000</b>
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Includes the Financial Profile plus a Tax-Sensitive Analysis of three (3) or more of the Select Modules below, depending on your situation and needs.

<b>FOCUSPlan<sup>SM</sup></b>	<b>\$3,000</b>
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Includes the Financial Profile plus three (3) or more of the Select Modules below, depending on your situation and needs.

<b>FOCUSPlan<sup>SM</sup> Start-Up Plan</b>	<b>\$1,500</b>
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Includes a Financial Profile and an analysis of two (2) or more Select Modules, as described below, depending on your situation and needs.

<b>FOCUSPlan<sup>SM</sup> Forecast</b>	<b>\$1,000</b>
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Includes a Financial Profile and a limited analysis on two (2) or more of the following analyses: Financial Independence (Retirement), Education funding, Survivor Needs, Long-Term Care and Disability needs.

<b>FOCUSPlan<sup>SM</sup> Select Modules</b>	<b>\$1,000 per module</b>
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Includes the Financial Profile at no cost with the purchase of one or two of the select modules listed below:

Financial Profile (no cost)  
Income Tax  
Financial Independence (Retirement)  
Goal Funding  
Survivor Income Needs  
Disability Income  
Education Funding  
Long-Term Care  
Estate Review  
Asset Allocation

## Supplemental Services/Strategies

The following Supplement Services and Strategies may be added to, or purchased separately from the FOCUSPlan<sup>SM</sup> services:

**Investment Planning Services (INVESTMENTPlan)** \$2,500

**Wealth Forecasting Service** \$1,000

**Estate Planning Strategies** \$3,000

**Business Planning Strategies** \$1,500

**Re-FOCUSPlan<sup>SM</sup>** **Varies\*\***

Fee varies, a discount off the current charges for the planning services selected may apply if the same planning services were purchased and delivered within the previous 24 months.

### FOCUSPlan<sup>SM</sup> Step-Up

Step-Up fee will be the difference between the applicable charges for the financial planning services desired and the fees paid for financial planning service(s) received within the past 90 days.

*\*\* Please refer to the range of fees for each FOCUSPlan<sup>SM</sup> service listed above.*

## Fee Payment

### Fixed and Variable Fees

Fixed and variable fees for FOCUSPlan<sup>SM</sup> services are payable in full at the time you execute your Financial Planning Services Agreement, except in certain unique situations approved by Waddell & Reed to facilitate periodic payments, organizational programs or other special arrangements agreed to by you and your Financial Advisor. All FOCUSPlan services must be rendered and resulting financial planning documents delivered to you no later than 6 months from the date you execute your Financial Planning Services Agreement or such earlier date as you and your Financial Advisor agree. However, in certain circumstances, FOCUSPlan Premier cases may require more than 6 months to complete due to their complexity.

### Method of Payment and Refunds

Fixed and variable fees may be withdrawn directly from certain Waddell & Reed mutual fund accounts, paid by a credit card approved by Waddell & Reed, or paid by check payable to Waddell & Reed. Checks should not be made payable to your Financial Advisor or to any entity other than Waddell & Reed. Fees may not be withdrawn from accounts where such withdrawal would result in a tax penalty, accounts contain class B and C shares where such withdrawal would cause a CDSC, or sub accounts of variable insurance products.

Cash payments are not accepted. Payments made in advance for any services will be refunded in full to any client who enters into a Financial Planning Services Agreement but decides to terminate the Agreement prior to receipt of any services. Payment for services will be refunded in full to any client who is not fully satisfied with the financial planning services ultimately received, provided the client notifies Waddell & Reed in writing within sixty (60) days after receipt of all financial planning services purchased, but not later than one (1) year from the date of the Financial Planning Services Agreement. As a condition to receiving a refund after all services are received, clients may be required to provide certain information to enable Waddell & Reed to determine the reasons for dissatisfaction. Waddell & Reed will refund any payment made in advance for a Financial Plan and/or module or strategy if the planning document(s)

is not delivered to you within 6 months from the date you sign the Financial Planning Services Agreement. For some FOCUSPlan Premier cases, additional time may be needed to complete the plan due to the complex nature of these plans. In some situations, and only with prior approval of the Financial Advisors Division in the home office, the 6 month delivery requirement may be extended.

A Financial Planning Services Agreement may be terminated at any time by you or Waddell & Reed upon the date a written termination notice is received from you by Waddell & Reed or on the date such notice is sent by Waddell & Reed to you at your address shown on the Financial Planning Services Agreement being terminated. Additional information regarding fees is contained in the Financial Planning Services Agreement.

## Fee Discounts, Free Services and Fee Changes

Fees are non-negotiable, except as described above regarding variable fees. Waddell & Reed may offer organizational discounts to certain individuals who are affiliated with organizations that are determined in Waddell & Reed's sole discretion to be eligible for such discounts. The discount rates offered and the terms of eligibility for organizational discounts are subject to change.

Waddell & Reed may offer financial planning services free of charge to employees and retirees of Waddell & Reed Financial, Inc. (Waddell & Reed's parent company) and its subsidiaries, to Financial Advisors and account representatives of Waddell & Reed and its affiliates, to directors and officers of the registered investment companies for which Waddell & Reed or an affiliate serves as distributor, and to the spouse, children, parents, children's spouses and spouse's parents of each such employee and/or retiree, Financial Advisor, account representative, director and officer. "Child" includes stepchild; "parent" includes stepparent. Waddell & Reed may offer financial planning services free of charge or at a reduced fee for promotional and charitable purposes and in connection with certain asset allocation programs it may create from time to time. Waddell & Reed may accept payment for the performance of financial planning services from persons other than the recipient of the services, through a referral arrangement or otherwise. Fees are subject to change.

## Other Fees and Compensation

If you implement our Financial Planning recommendations through your Financial Advisor by agreeing to purchase securities, insurance, or other financial products offered through Waddell & Reed, you will pay commissions, asset-based fees, internal expenses of certain products you select such as mutual funds and variable insurance products, and in some cases trust company or custodian fees if you invest through a retirement plan account such as an IRA, 457 or 403(b) plan account.

Financial Advisors may recommend the Waddell & Reed Mutual Funds (i.e. the proprietary Mutual Funds sponsored by Waddell & Reed or one of its affiliates). The Waddell & Reed Mutual Funds your Financial Advisor recommends may charge front-end commissions or a back-end CDSC. The investment managers who manage these Mutual Funds and Financial Advisors are part of the same parent organization – Waddell & Reed Financial, Inc. Throughout more than 70 years of serving investors, Waddell & Reed has developed a business structure that combines both the creation and management of the Waddell & Reed Mutual Funds and their sale to retail investors through Waddell & Reed in its capacity as a broker-dealer and its Financial Advisors. We believe this business structure provides significant value to our clients but also presents certain conflicts, which are discussed more fully below.

Higher revenue from the sale of the Waddell & Reed Mutual Funds and the variable insurance products distributed through the Strategic Partners, which contain the Waddell & Reed Mutual Funds in the sub accounts, generally results in greater profitability for Waddell & Reed and its affiliates. Employee compensation (including management and field leader compensation) and operating goals at all levels of the company are tied to varying degrees of Waddell & Reed's financial success. As such, management, sales leaders and other employees generally spend more of their time and resources promoting Waddell & Reed Mutual Funds and related products and services.

Both Waddell & Reed and your Financial Advisor are compensated when you buy Mutual Funds and variable insurance products through Waddell & Reed. Generally, your Financial Advisor receives a substantial portion of the sales charge and distribution and shareholder service (12b-1) fees paid in connection with your purchase. Sales charges and 12b-1 fees vary among products and, for mutual funds, among share classes. In addition to sales charges discussed above, you will also pay a portion of the product's internal operating expenses.

Sales charges are paid to compensate Waddell & Reed and your Financial Advisor for the assistance they provide in helping you select suitable investments and ongoing costs associated with servicing your Waddell & Reed investment accounts.

Operating expenses include: fees paid for investment management (research, trading, portfolio manager compensation, administrative services and technology), distribution and shareholder services fees paid for ongoing service provided by Waddell & Reed and your Financial Advisor, and other expenses such as record keeping, portfolio accounting, regulatory reporting, audit, legal and other non-investment expenses. A significant portion of the distribution and service fees will be paid to your Financial Advisor as additional compensation on an ongoing basis.

For additional information, you should review carefully the prospectus and, where applicable, statement of additional information for the particular mutual fund you are considering. Waddell & Reed also offers wrap fee and asset allocation fee-

based services - Strategic Portfolio Allocation (SPA) and Managed Allocation Portfolios (MAP). If you invest in SPA or a MAP program you will pay an additional ongoing advisory fee for advice concerning the investment of your assets in these programs. These advisory fees are separate from, and in addition to, your financial planning fee. It is possible that you will pay a financial planning fee for a financial plan that, among other things, recommends the use of more than one SPA or more than one MAP program, in which case you will pay fees for participating in one or more of these programs.

The fact that your Financial Advisor may recommend the purchase of Waddell & Reed Mutual Funds and variable insurance products distributed through the Strategic Partners presents a conflict of interest and gives your Financial Advisor an incentive to recommend these products. Other investment alternatives having similar or better risk and return characteristics and lower costs may be available to you through other broker-dealers or Investment Advisors.

Before purchasing investment products from your Financial Advisor you should consider that most of Waddell & Reed's revenue is generated from the sale of Mutual Funds and variable insurance products that charge commissions. Typically, this commission revenue is generated by the sale of the Waddell & Reed Mutual Funds and variable insurance products distributed through the Strategic Partners.

If you wish to purchase securities in a brokerage account through your Financial Advisor, you will be required to open a brokerage account at Pershing LLC. Waddell & Reed clears its general securities business exclusively through Pershing LLC on a fully disclosed basis. You will incur certain fees, expenses and trading costs if you conduct your Waddell & Reed brokerage business through a brokerage account maintained at Pershing LLC. You will receive a complete list of these fees, expenses and trading costs when you establish your Waddell & Reed brokerage account. The fees, expenses and trading costs you incur in your Waddell & Reed brokerage account may be more than the same fees, expenses and trading costs charged by other broker-dealers for similar services.

## Performance-Based Fees and Side-By-Side Management

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Waddell & Reed does not charge performance-based fees or engage in side-by-side investment management.

## Types of Clients

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Waddell & Reed typically provides investment advice to the following clients:

- Individuals
- Certain pension and professional plans
- Trusts, estates and charitable organizations
- Certain corporations and business entities not included in the categories above

## Methods of Analysis, Investment Strategies and Risk of Loss

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Waddell & Reed typically recommends as part of its overall financial planning process that clients broadly allocate their assets among a number of common asset classes. The financial plans we create will contain general asset allocation recommendations. Nevertheless, Financial Advisors, if requested by our clients, may recommend specific investment and insurance products to implement the asset class allocation developed through the financial plan. Clients should consider that asset allocation alone cannot ensure gains in up markets or protect accounts against loss in down markets. As discussed above, Financial Advisors generally recommend the Waddell & Reed Mutual Funds. We believe that these securities do not involve significant or unusual risks to our clients.

## Disciplinary Information

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On April 12, 2000, a letter of Acceptance, Waiver and Consent (No. C11000007) was approved by NASD Regulation, Inc. ("NASD") relating to conduct of three (3) of Waddell & Reed's Financial Advisors with respect to their misuse of account transaction request forms. The NASD found Waddell & Reed failed to establish, maintain and enforce written supervisory procedures reasonably designed to achieve compliance with the applicable securities laws and regulations and with applicable NASD rules relating, among other things, to forgery, unauthorized transactions and misappropriation. The NASD also found Waddell & Reed failed to respond adequately, and take appropriate action, to supervise its registered representatives, when confronted with evidence of problems in the above-referenced areas, that was reasonably designed to prevent the violations by the registered representatives.

On April 29, 2005, Waddell & Reed entered into a Decision & Order of Offer of Settlement with the NASD Department of Enforcement ("DOE") settling a regulatory action brought by the DOE on January 14, 2004 (Case No. CAF040002) alleging that Waddell & Reed violated NASD Conduct Rules 2110, 2310, 3010 and 3110, and § 17(a)(1) of the Securities Exchange Act of 1934 and Rule 17a-3(A)(6) hereunder, relating to exchanges made by certain of its clients of their variable annuity policies. The DOE alleged that Waddell & Reed failed to take adequate steps to determine whether there were reasonable grounds for the clients to enter into the exchanges, such as determining whether the clients were likely to benefit or lose money from the exchanges, failed to

establish sufficient guidance for the sales force to use in determining the suitability of the exchanges, failed to establish and maintain supervisory procedures or a system to supervise the activities of its advisors that was reasonably designed to achieve compliance with the requirements of the NASD's suitability rule, and failed to maintain books and records regarding orders for unexecuted variable annuity exchanges. Without admitting or denying the allegations, Waddell & Reed agreed to be censured, pay a fine of \$5 million and pay client restitution of \$11 million. Waddell & Reed also entered into a global settlement with state regulators in connection with the NASD settlement. Without admitting or denying the state's allegations, Waddell & Reed agreed to pay \$2 million fine and additional client restitution.

On July 24, 2006, Waddell & Reed entered into settlements with the U.S. Securities and Exchange Commission ("SEC"), the Attorney General of the State of New York ("NYAG") and the Kansas Securities Commissioner ("KSC") resolving their investigations into alleged market timing activities of shareholders of certain mutual funds for which Waddell & Reed serves as principal underwriter and distributor (the "Funds"). Based upon its investigation, the SEC alleged that a subsidiary of Waddell & Reed, Waddell & Reed Investment Management Company ("WRIMCO"), violated Sections 206(1) and 206(2) of the Investment Advisers Act of 1940 (the "Advisers Act") by following certain Fund Shareholders to engage in frequent trading of Fund shares in exchange for fees paid to Waddell & Reed and another Waddell & Reed subsidiary, Waddell & Reed Services Company ("WRSCO"), and that WRIMCO allowed such trading in the Waddell & Reed Advisors International Growth Fund (the "International Fund") despite having been notified that the shareholders were harming the International Fund through dilution and failed to disclose the conflict of interest to the Funds' Board of Directors and shareholders. The SEC also alleged that Waddell & Reed and WRSCO aided and abetted and caused WRIMCO's alleged violations of Sections 206(1) and 206(2) of the Advisers Act by negotiating agreements with the shareholders allowing their trading of the Funds within certain defined limits and receiving financial benefit therefrom, and that WRIMCO, Waddell & Reed and WRSCO violated Section 17(d) of the Investment Company Act of 1940 (the "40 Act") and Rule 17d-1 thereunder by participating in and effecting transactions in connection with joint arrangements in which the Funds were participants without filing an application with or receiving approval from the SEC. The NYAG alleged that Waddell & Reed's conduct violated the Martin Act, Article 23-A of the General Business Law, § 349 of the General Business Law and § 63(12) of the Executive Law of the State of New York, and the KSC alleged that the conduct of Waddell & Reed, WRIMCO and/or WRSCO violated K.S.A 17-1253(a), 17-1253(b), 17-1254(m)(7), K.A.R. 81-3-1(i)(1) and/or 81-14-5(a). Without admitting or denying the alleged violations, Waddell & Reed agreed with the SEC, together with WRIMCO and WRSCO, to a censure, to cease and desist from violating Sections 206(1) and 206(2) of the Advisers Act, Section 17(d) of the 40 Act and Rule 17d-1 thereunder, to pay to the SEC \$40 million in disgorgement and a \$10 million civil penalty that will be distributed to Fund shareholders, and to implement certain compliance undertakings. Waddell & Reed also agreed with the NYAG to reduce the investment management fees on certain of the Funds by \$5 million per year for five years and to certain Fund governance undertakings, and Waddell & Reed, WRIMCO and WRSCO agreed with the KSC to pay a fine of \$2 million to be used for the education of consumers in matters concerning securities regulation and investments.

On January 15, 2013, a Letter of Acceptance Waiver and Consent (No. 2011029075101) was approved by FINRA relating to the

failure of the firm to deliver purchase confirmations for a period of time. The firm failed to deliver numerous purchase confirmations for mutual-fund asset-allocation products accounts (MAP), during a period, and those confirmations would have confirmed multiple mutual fund share purchases that occurred in numerous investment-advisory accounts. Although the failure to deliver purchase confirmations resulted from the actions of a third-party service provider, the firm remained responsible at all times for compliance with its obligations under all applicable securities laws and regulations. The firm's investment-advisory offerings include several MAP accounts. The firm contracts with its subsidiary to act as the transfer agent for the mutual funds that can be held in the MAP accounts and the subsidiary was obligated to send purchase confirmations on behalf of the firm to MAP-account customers. The firm's subsidiary, in turn, contracts with a third-party service provider to generate and deliver those confirmations. Until a certain date, all purchase transactions in MAP accounts resulted in the delivery of contemporaneous trade confirmations. On that date, however, the third-party service provider made a coding change to the software system that it provided to the subsidiary and other entities. The third party did not intend for the coding change to affect the MAP accounts in any way, and neither the subsidiary nor the firm requested the change. Nonetheless, one effect of the coding change was to prevent customers from receiving confirmations when cash in a MAP account was allocated to individual mutual funds. Thereafter, a MAP-account customer contacted a representative of the firm to ask why the firm was no longer issuing fund-allocation confirmations. The representative contacted the subsidiary, but did not alert the firm's compliance department of the situation. The subsidiary conducted an internal review and determined that the subsidiary's coding change had created the problem. The subsidiary also did not apprise the firm's compliance department of the situation at that time. Thereafter, the subsidiary began researching the issue and working on a solution. The subsidiary's initial work did not completely solve the problem and it implemented a second fix, which through subsequent testing verified that the problem was fully resolved. Without admitting or denying FINRA's allegations, Waddell and Reed agreed to a censure and fine of \$75,000 to settle the regulatory action.

On June 19, 2015 the State of New Hampshire, Department of State, Bureau of Securities (the "Bureau") received a complaint from a New Hampshire resident and former client of Waddell, which raised concerns regarding certain financial planning fees charged by an investment advisor representative of Waddell. Based on the content of the complaint, the Bureau initiated an investigation. During the course of its investigation, the Bureau determined that the investment advisor representative in question engaged in several violations of New Hampshire securities law, including verbally misrepresenting to his clients the nature of financial planning fees he charged those clients. The Bureau also noted certain deficiencies in Waddell's supervision of the investment advisor representative in question. The Bureau noted that over the past two years, Waddell has taken steps to enhance its supervision of the financial planning conducted by its investment advisor representatives and these enhancements will be finalized during the second quarter of 2017. All of the Bureau's allegations against Waddell are limited to investment advisory activities.

Pursuant to Waddell's Financial Planning Refund Program, Waddell agreed to refund a portion of certain financial planning fees paid by the clients of the investment advisor representative in question, in the amount of \$2,012,615.80. Waddell also agreed to pay the Bureau's costs of investigation in the amount of Three Hundred Thousand Dollars (\$300,000), an administrative fine in the amount of Three Hundred Thousand Dollars (\$300,000), and a contribution to the Bureau's investor education fund in the amount of Three Hundred Thousand Dollars (\$300,000).

## Other Financial Industry Activities and Affiliations

Waddell & Reed is registered as a broker-dealer and its investment advisor. Investment advisor representatives are also registered representatives of the broker-dealer. As such, your Financial Advisor may offer both our financial planning services, various asset allocations and wrap programs, some of which are sponsored by Waddell & Reed and general securities products including:

- Equities
- Certain Municipal Securities
- Certain Commercial Paper
- Certain Corporate Debt Securities
- Certain Brokered CDs
- Variable Life Insurance
- Variable Annuities
- Mutual Fund Shares
- U.S. Government and Certain Agency Securities
- Options on Securities

Waddell & Reed has material relationships and arrangements with the following:

**Pershing LLC** - Waddell & Reed clears its brokerage business exclusively through Pershing LLC on a fully disclosed basis. Clients that establish brokerage accounts with Waddell & Reed must establish those accounts at Pershing LLC. Clients will be subject to the various account and transaction related costs and fees assessed by Pershing LLC, which may be higher than those charged by other broker-dealers for similar services. Also, Waddell & Reed receives a share of certain charges imposed by Pershing LLC on the brokerage accounts they carry for us.

**Waddell & Reed Mutual Funds:** Please read carefully the discussion above under "Other Fees and Compensation" regarding the conflicts of interest inherent in the relationship between Waddell & Reed and the Waddell & Reed Mutual Funds. Also, the investment managers for the Waddell & Reed Mutual Funds are wholly owned subsidiaries of Waddell & Reed.

**W&R Insurance Agency:** Waddell & Reed distributes certain fixed and variable insurance products through its affiliate, W&R Insurance Agency. These products include the insurance products created for Waddell & Reed by the Strategic Partners.

**Strategic Partners:** We discuss our relationship with the Strategic Partners under Advisory Business, Overview and Ownership above. Most of the variable insurance products we sell are created by our Strategic Partners. We earn standard commissions on the sale of these products. We also receive a percent of the value of the assets held in the sub-accounts on an ongoing basis.

**Lockwood Advisors, Inc.:** Lockwood Advisors, Inc. is an affiliate of Pershing LLC. Waddell & Reed uses Lockwood Advisors, Inc. as a platform for several of the fee-based asset allocation and wrap programs we offer as an investment advisor. Waddell & Reed pays various fees to Lockwood Advisors, Inc. for its services. Waddell & Reed offers its investment advisory clients SMA and UMA products sponsored and/or managed by Lockwood Advisors, Inc. Waddell & Reed receives a portion of the fees charged to clients by the managers of these products. See Appendix I to Form ADV Part 2 for more information about this relationship.

## Code of Ethics

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Waddell & Reed has adopted a Code of Ethics. The Code of Ethics is primarily intended to establish specific standards of business conduct and to avoid any actual or potential conflict of interest or any abuse of the positions of trust and responsibility of certain persons considered "Access Persons".

Under the Code of Ethics, Access Persons are, among other things, required to report certain personal securities transactions and holdings, must pre-clear certain securities transactions, are restricted with respect to the timing of certain securities transactions, and are prohibited from making certain investments, all as more specifically provided in the Code of Ethics.

Waddell & Reed, its affiliates and their employees, directors and associated persons are prohibited from misusing, for their personal benefit or for the benefit of other, material nonpublic information.

Persons who violate any portion of the Code of Ethics, including the prohibitions against the misuse of nonpublic information, are subject to sanction, up to and including termination.

Waddell & Reed will provide a copy of its Code of Ethics to any client or prospective client upon written request. Copies of the Code of Ethics may be obtained by writing to :

Waddell & Reed, Inc.  
Legal Department  
Attention: Code of Ethics  
6300 Lamar Avenue  
Shawnee Mission, KS 66202

## Brokerage Practices

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Waddell & Reed does not receive research or soft dollar benefits from a broker-dealer in connection with client securities transactions.

Clients that decide to purchase securities in connection with their financial planning experience with Waddell & Reed need not purchase securities through Waddell & Reed or its Financial Advisors. They may purchase these securities through any broker-dealer or through fee-based accounts at any Investment Advisor. Nevertheless, clients that decide to purchase securities in brokerage accounts through Waddell & Reed must do so only through brokerage accounts carried for Waddell & Reed by Pershing LLC. All transactions effected in these brokerage accounts will be executed by Pershing LLC. By directing brokerage executions through Pershing LLC, we may be unable to achieve most favorable execution for your transactions and it may cost more to execute transactions through Pershing LLC than through other broker-dealers. Nevertheless, Waddell & Reed continually monitors the quality of executions in accounts held at Pershing LLC. We believe Pershing LLC provides highly competitive execution quality based on (i) speed and certainty; (ii) price improvement; and (iii) overall execution quality.

## Review of Accounts

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All financial plans are reviewed by a supervisory principal of Waddell & Reed to ensure that they are appropriate for the individual client given their stated personal financial situation, life stage, investment and financial objectives and risk tolerance.

## Client Referrals and Other Compensation

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From time to time Waddell & Reed may enter into referral arrangements with financial institutions, such as banks and credit unions, CPAs, attorneys and certain others. These referral sources will be paid compensation either directly or indirectly to refer clients to Waddell & Reed for investment advisory services. The fee, if any, paid to referral sources will be disclosed to you in writing at the time of referral.

## Custody

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You will receive statements reflecting your account holdings on a quarterly basis and more frequently if you have transactions in your account. You will receive confirmations and statements from our transfer agency if your purchase, sell, or hold the Waddell & Reed Mutual Funds direct with our transfer agency. You will receive confirmations and statements from the product sponsor if you hold other mutual funds direct at the fund or variable insurance products direct at the carrier. You will receive confirmations and statements from Pershing LLC if you purchase, sell, or hold securities in a brokerage account. Your Financial Advisor is permitted to send our Compass report account summary and related performance reports. However, these are merely unofficial account summaries and must not be relied upon as an accurate, complete statement of your account holdings or activity.

## Investment Discretion

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We do not accept discretionary authority from clients to manage their securities accounts. We do exercise discretion indirectly within our MAP asset allocation programs only to the extent necessary to rebalance your portfolio periodically to remain consistent with the investment model you select.

## Voting Client Securities

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Waddell & Reed does not accept authority to vote client securities proxies.

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**WADDELL & REED, INC. AND SUBSIDIARIES**  
(A Wholly Owned Subsidiary of Waddell & Reed Financial, Inc.)

Consolidated Balance Sheet

December 31, 2015

(With Report of Independent Registered Public Accounting Firm Thereon)





**KPMG LLP**  
Suite 1000  
1000 Walnut Street  
Kansas City, MO 64106-2162

## **Report of Independent Registered Public Accounting Firm**

The Board of Directors  
Waddell & Reed, Inc.:

We have audited the accompanying consolidated balance sheet of Waddell & Reed, Inc. and subsidiaries (the Company), a wholly owned subsidiary of Waddell & Reed Financial, Inc. as of December 31, 2015. The consolidated financial statement is the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statement based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statement referred to above presents fairly, in all material respects, the financial position of Waddell & Reed, Inc. and subsidiaries as of December 31, 2015, in conformity with U.S. generally accepted accounting principles.

**KPMG LLP**

Kansas City, Missouri  
February 25, 2016

KPMG LLP is a Delaware limited liability partnership,  
the U.S. member firm of KPMG International Cooperative  
("KPMG International"), a Swiss entity.

**WADDELL & REED, INC. AND SUBSIDIARIES**  
(A Wholly Owned Subsidiary of Waddell & Reed Financial, Inc.)

Consolidated Balance Sheet

December 31, 2015

(In thousands)

**Assets**

Cash and cash equivalents	\$ 337,143
Cash and cash equivalents – restricted	66,880
Investment securities	71,396
Receivables:	
Funds and separate accounts	29,008
Customers and other	220,106
Due from affiliates	9,938
Prepaid expenses and other current assets	25,657
Income taxes receivable	3,620
	<hr/>
Total current assets	763,748
Property and equipment, net	104,125
Deferred sales commissions, net	13,588
Deferred income taxes	32,194
Goodwill and identifiable intangible asset	35,095
Other assets	15,448
	<hr/>
Total assets	\$ 964,198

**Liabilities and Stockholder's Equity**

Accounts payable	\$ 28,225
Payable to investment companies for securities	113,648
Payable to third party brokers	14,373
Payable to customers	120,420
Accrued compensation	36,978
Other current liabilities	39,944
	<hr/>
Total current liabilities	353,588
Accrued pension and postretirement costs	39,579
Other non-current liabilities	20,519
	<hr/>
Total liabilities	413,686
Commitments and contingencies	
Stockholder's equity:	
Common stock, \$1.00 par value: 1,000 shares authorized, issued, and outstanding.	1
Additional paid-in capital	252,843
Retained earnings	346,224
Accumulated other comprehensive loss	(48,556)
	<hr/>
Total stockholder's equity	550,512
	<hr/>
Total liabilities and stockholder's equity	\$ 964,198

See accompanying notes to consolidated balance sheet.

**WADDELL & REED, INC. AND SUBSIDIARIES**  
(A Wholly Owned Subsidiary of Waddell & Reed Financial, Inc.)

Notes to Consolidated Balance Sheet

December 31, 2015

**(1) Summary of Significant Accounting Policies**

**(a) Organization**

Waddell & Reed, Inc. (W&R Inc.), a broker-dealer and investment adviser, and subsidiaries (the Company, we, our, and us) derive revenues primarily from investment management, investment product underwriting and distribution, and shareholder services administration provided to the Waddell & Reed Advisors Funds (the Advisors Funds), Ivy Funds Variable Insurance Portfolios (the Ivy Funds VIP), Ivy Funds, which are underwritten by an affiliate, and Ivy Funds InvestEd (InvestEd) (collectively, the Funds), and institutional and separately managed accounts. The Funds and the institutional and separately managed accounts operate under various rules and regulations set forth by the United States Securities and Exchange Commission (the SEC). Services to the Funds are provided under investment management agreements, underwriting agreements, and shareholder servicing and accounting agreements that set forth the fees to be charged for these services. The majority of these agreements are subject to annual review and approval by each Fund's board of trustees and shareholders. Our revenues are largely dependent on the total value and composition of assets under management. Accordingly, fluctuations in financial markets and composition of assets under management can significantly impact revenues and results of operations. The Company is an indirect wholly owned subsidiary of Waddell & Reed Financial, Inc. (WDR), a publicly traded company.

The Company's underwriting agreements with the Funds allow the Company the exclusive right to distribute redeemable shares of the Funds on a continuous basis. The Company has entered into a limited number of selling agreements authorizing third parties to offer certain of the Funds. In addition, the Company receives Rule 12b-1 asset-based service and distribution fees from certain of the Funds for purposes of advertising and marketing the shares of such funds and for providing shareholder-related services. The Company must pay certain costs associated with underwriting and distributing the Funds, including commissions and other compensation paid to financial advisors, sales force management, and other marketing personnel, compensation paid to other broker-dealers, plus overhead expenses relating to field offices, sales programs, and the costs of developing and producing sales literature and printing of prospectuses, which may be either partially or fully reimbursed by certain of the Funds. The Funds are sold in various classes that are structured in ways that conform to industry standards (i.e., front-end load, back-end load, level-load, and institutional).

The Company operates its investment advisory business and its transfer agency and accounting services business through its primary subsidiaries, Waddell & Reed Investment Management Company and Waddell & Reed Services Company, respectively.

**(b) Basis of Presentation**

The accompanying consolidated balance sheet is prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and include the accounts of the Company and its subsidiaries, all of which are wholly owned. All significant intercompany accounts and transactions have been eliminated in consolidation. Amounts in the accompanying balance sheet and notes are rounded to the nearest thousand unless otherwise stated.

(Continued)

**WADDELL & REED, INC. AND SUBSIDIARIES**  
(A Wholly Owned Subsidiary of Waddell & Reed Financial, Inc.)

Notes to Consolidated Balance Sheet

December 31, 2015

The company has evaluated subsequent events through February 25, 2016, the date that this balance sheet statement was issued and determined there are no other items to disclose.

**(c) Consolidation**

We provide seed capital to our new investment products at the time we launch the products. These investment products include certain of the Advisors Funds and the Ivy Funds ("1940 Act Mutual Funds"), Ivy Global Investors Funds (IGI) and limited liability companies ("LLCs"). The primary purpose of providing seed capital is to generate an investment performance track record to attract third-party investors. Our seed investment in a new product represents 100% ownership in that product when the product is launched.

Assessing if an entity is a variable interest entity ("VIE") or voting interest entity ("VOE") involves judgment and analysis on an entity by entity basis. Factors included in this assessment include the legal organization of the entity, the company's contractual involvement with the entity and any implications resulting from or associated with related parties' involvement with the entity.

Seeded investments in 1940 Act Mutual Funds are organized under a series fund structure, whereby each open-ended mutual fund represents a separate share class of a legal entity organized under a statutory trust. The Company has determined that the 1940 Act Mutual Funds are VOEs because the structure of the investment product is such that the voting rights held by the equity holders provide for equality among equity investors. To the extent material, these investment products would be consolidated if Company ownership, directly or indirectly, represents a majority interest.

The privately offered funds seeded by the Company are structured as investment companies in the legal form of LLCs. The Company is the managing member of these LLCs. For the majority of these LLCs, the Company's investment represents an ownership of less than 3%. Generally, limited partnerships and similar entities in which the general partner does not have substantive equity at risk and the other limited partners do not have substantive rights to remove the general partner would be considered VIEs. During the fourth quarter of 2015, the LLC agreements were amended so that all of the members of the Company's privately offered funds now hold substantive kick-out and participation rights. They also have the ability to remove the managing member and to dissolve the LLC. Given the substantive rights afforded the members, the Company has concluded the LLCs are VOEs. These investment products would be consolidated, if material, if a majority interest is held, directly or indirectly, by the Company.

The Company has determined the SICAV to be a VOE, as its legal structure and the powers of its equity investors prevents the SICAV from meeting the characteristics of being a VIE. To the extent material, the Company would be required to consolidate the SICAV if ownership of the SICAV, directly or indirectly, represents more than 50% of the outstanding voting shares of the SICAV.

**(d) Use of Estimates**

GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities in the consolidated balance sheet and accompanying notes, and related disclosures of

(Continued)

**WADDELL & REED, INC. AND SUBSIDIARIES**  
(A Wholly Owned Subsidiary of Waddell & Reed Financial, Inc.)

Notes to Consolidated Balance Sheet

December 31, 2015

commitments and contingencies. Estimates are used for, but are not limited to depreciation and amortization, income taxes, valuation of assets, pension and postretirement obligations, and contingencies. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment. Actual results could differ from those estimates.

**(e) Cash and Cash Equivalents**

Cash and cash equivalents include cash on hand and short-term investments. We consider all highly liquid investments with maturities upon acquisition of 90 days or less to be cash equivalents. Cash and cash equivalents-restricted represents cash held for the benefit of customers and non-customers segregated in compliance with federal and other regulations.

**(f) Disclosures about Fair Value of Financial Instruments**

Fair value of cash and cash equivalents, receivables, and payables approximates carrying value. Fair values for investment securities are based on quoted market prices, where available. Otherwise, fair values for investment securities are based on Level 2 or Level 3 inputs detailed in Note 3.

**(g) Investment Securities and Investments in Sponsored Funds**

Our investments are comprised of state and government obligations, corporate debt securities, common stock and investments in sponsored funds. Sponsored funds, which include the Funds, the IGI Funds and the LLCs, are investments we have made for both general corporate investment purposes and to provide seed capital for new investment products. The Company has classified its investments in certain sponsored funds as either equity method investments (when the Company owns between 20% and 50% of the fund) or as available for sale investments (when the Company owns less than 20% of the fund) as described in Note 3. Investments held by our broker/dealer entity or certain investments that are anticipated to be purchased and sold on a more frequent basis are classified as trading.

Unrealized holding gains and losses on securities available for sale, net of related tax effects, are excluded from earnings until realized and are reported as a separate component of comprehensive income. For trading securities, unrealized holding gains and losses are included in earnings. Realized gains and losses are computed using the specific identification method for investment securities, other than sponsored funds. For sponsored funds, realized gains and losses are computed using the average cost method. Substantially all of the Company's equity method investees are investment companies which record their underlying investments at fair value. Therefore, under the equity method of accounting, our share of the investee's underlying net income or loss is predominantly representative of fair value adjustments in the investments held by the equity method investee. Our share of the investee's net income or loss is based on the most current information available and is recorded as a net gain or loss on investments within investment and other income (loss).

Our available for sale investments are reviewed each quarter and adjusted for other than temporary declines in value. We consider factors affecting the issuer and the industry the issuer operates, general market trends including interest rates, and our ability and intent to hold an investment until it

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(Continued)

**WADDELL & REED, INC. AND SUBSIDIARIES**  
(A Wholly Owned Subsidiary of Waddell & Reed Financial, Inc.)

Notes to Consolidated Balance Sheet

December 31, 2015

has recovered. Consideration is given to the length of time an investment's market value has been below carrying value and prospects for recovery to carrying value. When a decline in the fair value of equity securities is determined to be other than temporary, the unrealized loss recorded net of tax in other comprehensive income is realized as a charge to net income, and a new cost basis is established for financial reporting purposes. When a decline in the fair value of debt securities is determined to be other than temporary, the amount of the impairment recognized in earnings depends on whether the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss. If so, the other than temporary impairment recognized in earnings is equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If not, the portion of the impairment related to the credit loss is recognized in earnings while the portion of the impairment related to other factors is recognized in other comprehensive income, net of tax.

**(h) *Property and Equipment***

Property and equipment are carried at cost. The costs of improvements that extend the life of a fixed asset are capitalized, while the costs of repairs and maintenance are expensed as incurred. Depreciation and amortization are calculated and recorded using the straight-line method over the estimated useful life of the related asset (or lease term if shorter), generally three to 10 years for furniture and fixtures; one to 10 years for computer software; one to five years for data processing equipment; one to 40 years for buildings; three to 26 years for other equipment; and up to 15 years for leasehold improvements, which is the lesser of the lease term or expected life.

**(i) *Software Developed for Internal Use***

Certain internal costs incurred in connection with developing or obtaining software for internal use are capitalized in accordance with ASC 350, "Intangibles – Goodwill and Other Topic." Internal costs capitalized are included in property and equipment, net in the consolidated balance sheets, and were \$13.8 million as of December 31, 2015. Amortization begins when the software project is complete and ready for its intended use and continues over the estimated useful life, generally one to 10 years.

**(j) *Goodwill and Identifiable Intangible Asset***

Goodwill represents the excess of the cost of the Company's investment in the net assets of acquired companies over the fair value of the underlying identifiable net assets at the dates of acquisition. Goodwill is not amortized, but is reviewed annually for impairment in the second quarter of each year and when events or circumstances occur that indicate that goodwill might be impaired. Factors that the Company considers important in determining whether an impairment of goodwill or intangible assets might exist include significant continued underperformance compared to peers, the likelihood of termination or non-renewal of a mutual fund advisory or subadvisory contract or substantial changes in revenues earned from such contracts, significant changes in our business and products, material and ongoing negative industry or economic trends, or other factors specific to each asset being evaluated.

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The Company has one reporting unit for goodwill, investment management and related services. This unit's goodwill was recorded as part of the spin-off of WDR from its former parent, and to a lesser extent, was recorded as part of subsequent business combinations that were merged into the existing investment management operations.

To determine the fair value of the Company's reporting unit, our review process uses the market and income approaches. In performing the analyses, the Company uses the best information available under the circumstances, including reasonable and supportable assumptions and projections.

The market approach employs market multiples for comparable publicly-traded companies in the financial services industry. Estimates of fair values of the reporting units are established using multiples of earnings before interest, taxes, depreciation and amortization ("EBITDA"). The Company believes that fair values calculated based on multiples of EBITDA are an accurate estimation of fair value.

If the fair value coverage margin calculated under the market approach is not considered significant, the Company utilizes a second approach, the income approach, to estimate fair values and averages the results under both methodologies. The income approach employs a discounted free cash flow approach that takes into account current actual results, projected future results, and the Company's estimated weighted average cost of capital.

The Company compares the fair value of the reporting unit to its carrying amount, including goodwill. If the carrying amount of the reporting unit exceeds its calculated fair value, goodwill is considered impaired and a second step is performed to measure the amount of impairment loss, if any.

Indefinite-lived intangible asset represent an advisory contract for managed assets obtained in an acquisition. The Company considers this contract to be an indefinite-lived intangible asset as it is expected to be renewed without significant cost or modification of terms. The Company also tests this asset for impairment annually and when events or circumstances occur that indicate that the indefinite-lived intangible asset might be impaired. If the carrying value of a management contract acquired exceeds its fair value, an impairment loss is recognized equal to that excess.

**(k) *Deferred Sales Commissions***

We defer certain costs, principally sales commissions and related compensation, which are paid to financial advisors and broker/dealers in connection with the sale of certain mutual fund shares sold without a front-end load sales charge. The costs incurred at the time of the sale of Class B shares sold prior to January 1, 2014 are amortized on a straight-line basis over five years, which approximates the expected life of the shareholders' investments. Effective January 1, 2014, the Company suspended sales of Class B shares. The costs incurred at the time of the sale of Class C shares are amortized on a straight-line basis over 12 months. Prior to June 16, 2014, the costs incurred at the time of the sale of shares for certain fee-based asset allocation products were deferred and amortized on a straight-line basis, not to exceed three years. We recover deferred sales commissions and related compensation through Rule 12b-1 and other distribution fees, which are

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paid on the Class B and Class C shares of the Advisors Funds and Ivy Funds, along with contingent deferred sales charges (“CDSCs”) paid by shareholders who redeem their shares prior to completion of the specified holding period (three years for shares of certain fee-based asset allocation products sold prior to June 16, 2014, six years for a Class B share and 12 months for a Class C share), as well as through client fees paid on the asset allocation products sold prior to June 16, 2014. Effective June 16, 2014 we no longer assess a CDSC to investors upon early redemption of fee-based asset allocation products and amounts deferred for sales commissions and related compensation are classified in the prepaid and other current asset and other non-current assets in our consolidated balance sheet. Should we lose our ability to recover deferred sales commissions through distribution fees or CDSCs, the value of these assets would immediately decline, as would future cash flows. We periodically review the recoverability of the deferred sales commission assets as events or changes in circumstances indicate that their carrying amount may not be recoverable and adjust them accordingly. Impairment adjustments are recognized in operating income as a component of amortization of deferred sales commissions.

**(I) Revenue Recognition**

*Investment Management and Advisory Fees*

We recognize investment management fees as earned over the period in which services are rendered. We charge the Funds daily based upon average daily net assets under management in accordance with investment management agreements between the Funds and the Company. The majority of investment and/or advisory fees earned from institutional and separate accounts are charged either monthly or quarterly based upon an average of net assets under management in accordance with such investment management agreements. The Company may waive certain fees for investment management services at its discretion, or in accordance with contractual expense limitations, and these waivers are reflected as a reduction to investment management fees on the consolidated statement of income.

Our investment advisory business receives research products and services from broker/dealers through “soft dollar” arrangements. Consistent with the “soft dollar” safe harbor established by Section 28(e) of the Securities Exchange Act of 1934, as amended, the investment advisory business does not have any contractual obligation requiring it to pay for research products and services obtained through soft dollar arrangements with brokers. As a result, we present “soft dollar” arrangements on a net basis.

The Company has contractual arrangements with third parties to provide subadvisory services. Investment advisory fees are recorded gross of any subadvisory payments and are included in investment management fees based on management’s determination that the Company is acting in the capacity of principal service provider with respect to its relationship with the Funds. Any corresponding fees paid to subadvisors are included in operating expenses.

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*Distribution, Underwriter and Service Fees*

Underwriting and distribution commission revenues resulting from the sale of investment products are recognized on the trade date. When a client purchases Class A or Class E shares (front-end load), the client pays an initial sales charge of up to 5.75% of the amount invested. The sales charge for Class A or Class E shares typically declines as the investment amount increases. In addition, investors may combine their purchases of all fund shares to qualify for a reduced sales charge. When a client invests in a fee-based asset allocation product, Class A shares are purchased at net asset value and we do not charge an initial sales charge.

Under a Rule 12b-1 service plan, the Funds may charge a maximum fee of 0.25% of the average daily net assets under management for Class B and C shares for expenses paid to broker/dealers and other sales professionals in connection with providing ongoing services to the Funds' shareholders and/or maintaining the Funds' shareholder accounts, with the exception of Class Y shares, which do not charge a service fee. The Funds' Class B and Class C shares may charge a maximum of 0.75% of the average daily net assets under management under a Rule 12b-1 distribution plan to compensate broker/dealers and other sales professionals for their services in connection with distributing shares of that class. The Fund's Class A shares may charge a maximum fee of 0.25% of the average daily net assets under management under a Rule 12b-1 service and distribution plan for expenses detailed previously. The Company receives 12b-1 fees for Ivy funds sold by our financial advisors. The Rule 12b 1 plans are subject to annual approval by the Funds' board of trustees, including a majority of the disinterested members, by votes cast in person at a meeting called for the purpose of voting on such approval. All Funds may terminate the service and distribution plans at any time with approval of fund trustees or portfolio shareholders (a majority of either) without penalty.

Fee-based asset allocation revenues are charged quarterly based upon average daily net assets under management. For certain types of investment products, primarily variable annuities, distribution revenues are generally calculated based upon average daily net assets under management and are recognized monthly. Fees collected from advisors for services related to technology and errors and omissions insurance are recorded in underwriting and distribution fees on a gross basis, as the Company is the primary obligor in these arrangements.

Shareholder service fees are recognized monthly and are calculated based on the number of accounts or assets under management as applicable. Other administrative service fee revenues are recognized when contractual obligations are fulfilled or as services are provided.

Through a revenue sharing allocation agreement with affiliates, the Company receives 25 basis points on gross sales of assets and 10 basis points on average assets under management for Ivy Funds sold by our financial advisors. In addition, the Company receives revenue for providing accounting, information technology, legal, marketing, rent and other administrative services to affiliated companies.

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**(m) Leases**

The Company leases office space under various leasing arrangements. Most lease agreements contain renewal options, rent escalation clauses and/or other inducements provided by the landlord. As leases expire, they are typically renewed or replaced in the ordinary course of business.

**(n) Income Taxes**

The Company files consolidated federal income tax returns with WDR. The Company's provision for income taxes has been made on the same basis as if the Company filed separate federal income tax returns using the maximum statutory rate applicable to the consolidated group. The Company is included in the combined state returns filed by WDR and also files separate state income tax returns in other state jurisdictions in which the Company operates that do not allow or require the affiliated group to file on a combined basis.

Income tax expense is based on pre-tax financial accounting income, including adjustments made for the recognition or derecognition related to uncertain tax positions. The recognition or derecognition of income tax expense related to uncertain tax positions is determined under the guidance as prescribed by ASC 740, "*Income Taxes Topic*." Deferred tax assets and liabilities are recognized for the future tax attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. A valuation allowance is recognized for deferred tax assets if, based on available evidence, it is more likely than not that all or some portion of the asset will not be realized. Deferred tax assets and deferred tax liabilities are measured using enacted tax rates expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in earnings in the period that includes the enactment date.

The Company recognizes tax benefits from equity awards in WDR stock granted to its employees and financial advisors (our sales force) who are independent contractors. These tax benefits are reflected as an increase to additional paid-in capital with a corresponding increase to income taxes receivable. The excess tax benefits from share-based payments were \$4.0 million for 2015.

**(2) New Accounting Guidance**

*Accounting Guidance Adopted During Fiscal Year 2015*

During the fourth quarter of 2015, the Company adopted ASU 2015-07, "*Fair Value Measurement*," which eliminates the requirement to categorize investments in the fair value hierarchy if their fair value is measured at net asset value ("NAV") per share (or its equivalent) using the practical expedient.

During the fourth quarter of 2015, the Company adopted ASU 2015-17, "*Income Taxes*," which requires an entity to classify all deferred tax assets and liabilities as noncurrent on the balance sheet. Prior to implementation of this ASU, the Company classified deferred tax assets and liabilities as either current or non-current assets and liabilities.

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*New Accounting Guidance Not Yet Adopted*

In May 2014, the Financial Accounting Standards Board (“FASB”) issued ASU 2014-09, “*Revenue from Contracts with Customers*.” ASU 2014-09 requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. This standard also specifies the accounting for certain costs to obtain or fulfill a contract with a customer. This ASU will supersede much of the existing revenue recognition guidance in accounting principles generally accepted in the United States and is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period; early application is permitted for the first interim period within annual reporting periods beginning after December 15, 2016. ASU 2014-09 permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating which transition method to apply and the estimated impact the adoption of this ASU will have on our consolidated balance sheet and related disclosures.

In February 2015, the FASB issued ASU 2015-02, “*Amendments to the Consolidation Analysis*.” The amendments in this ASU will affect all companies that are required to evaluate whether they should consolidate another entity. Additionally, the amendments in this ASU rescind the indefinite deferral of FASB Statement 167, “*Amendments to FASB Interpretation No. 46(r)*” included in ASU 2010-10. ASU 2015-02 will be effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period. This standard permits the use of either a full retrospective or a modified retrospective approach. The Company believes that the adoption of this ASU on January 1, 2016, will result in an immaterial impact to our consolidated balance sheet and related disclosures regarding our seeded investments in the 1940 Act Funds and LLCs. The Company has concluded that the SICAV will be deemed a VIE due to the lack of equity investment at risk at the SICAV legal entity level. The sub-funds of the SICAV are deemed silos and evaluated individually for consolidation. Because the decisions regarding key activities of the sub-fund reside at the SICAV level, the shareholders of the sub-funds lack the ability to control the key decision-making processes that most directly affect the performance of the sub-funds. As such, each sub-fund is a VIE with the primary beneficiary evaluation being an analysis of economic interest. The Company will be the primary beneficiary and will consolidate any sub-fund of the SICAV in which it owns a majority interest.

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**(3) Investment Securities**

Investments at December 31, 2015 are as follows (in thousands):

Available-for-sale securities:	
Sponsored privately offered funds	\$ <u>825</u>
Total available-for-sale securities	<u>825</u>
Trading securities:	
Mortgage-backed securities	20
Common stock	87
Sponsored funds	564
Corporate bonds	<u>5</u>
Total trading securities	<u>676</u>
Equity method securities:	
Sponsored funds	66,722
Sponsored privately offered funds	<u>3,173</u>
Total equity method securities	<u>69,895</u>
Total investment securities	<u>\$ 71,396</u>

The following is a summary of the gross unrealized gains related to securities classified as available for sale at December 31, 2015:

	<u>Amortized cost</u>	<u>Unrealized gains</u>	<u>Unrealized losses</u>	<u>Fair value</u>
Sponsored privately offered funds	\$ 500	325	—	825
Total available-for-sale securities	<u>\$ 500</u>	<u>325</u>	<u>—</u>	<u>825</u>

*Sponsored Funds*

The Company has classified its investments in certain sponsored funds as either equity method investments (when the Company owns between 20% and 50% of the fund) or as available for sale investments (when the Company owns less than 20% of the fund). We do not hold a majority interest in any of our sponsored funds as of December 31, 2015. As a result, there are no sponsored funds consolidated in our balance sheet.

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*Sponsored privately offered funds*

The Company holds voting interests in certain sponsored privately offered funds that are structured as investment companies in the legal form of LLCs. The Company held investments in these funds totaling \$4.0 million as of December 31, 2015, which is our maximum loss exposure.

During, 2015, \$77.0 million of investments previously classified as available for sale securities were classified as equity method securities, representing seed investments in which the Company owned between 20% and 50% of the fund. As a result of this classification change, during 2015, \$2.9 million of unrealized gains were reclassified from other comprehensive income and recognized in the consolidated statement of income.

The corporate bond accounted for as trading matures in 2018. Mortgage-backed securities accounted for as trading and held as of December 31, 2015 mature in 2022.

Investment securities accounted for as equity method and as trading, with a fair value of \$3.0 million and \$51 thousand, respectively, were sold during 2015. Net realized losses resulting from these sales were \$296 thousand and one thousand, respectively.

Accounting standards establish a framework for measuring fair value and a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of the asset. Inputs may be observable or unobservable and refer broadly to the assumptions that market participants would use in pricing the asset. An individual investment's fair value measurement is assigned a level based upon the observability of the inputs that are significant to the overall valuation. The three-tier hierarchy of inputs is summarized as follows:

- Level 1 – Investments are valued using quoted prices in active markets for identical securities.
- Level 2 – Investments are valued using other significant observable inputs, including quoted prices in active markets for similar securities.
- Level 3 – Investments are valued using significant unobservable inputs, including the Company's own assumptions in determining the fair value of investments.

Assets classified as Level 2 can have a variety of observable inputs. These observable inputs are collected and utilized, primarily by an independent pricing service, in different evaluated pricing approaches depending upon the specific asset to determine a value. The fair value of municipal bonds is measured based on pricing models that take into account, among other factors, information received from market makers and broker/dealers, current trades, bid-wants lists, offerings, market movements, the callability of the bond, state of issuance and benchmark yield curves. The fair value of corporate bonds is measured using various techniques, which consider recently executed transactions in securities of the issuer or comparable issuers, market price quotations (where observable), bond spreads and fundamental data relating to the issuer. The fair value of equity derivatives is measured based on active market broker quotes, evaluated broker quotes and evaluated prices from vendors.

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Securities' values classified as Level 3 are primarily determined through the use of a single quote (or multiple quotes) from dealers in the securities using proprietary valuation models. These quotes involve significant unobservable inputs, and thus, the related securities are classified as Level 3 securities.

The following table summarizes our investment securities as of December 31, 2015 that are recognized in our consolidated balance sheet using fair value measurements based on the differing levels of inputs.

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
	(In thousands)			
<b>Available for sale securities:</b>				
Sponsored privately offered funds				
measured at net asset value <sup>(2)</sup>	\$ —	—	—	825
<b>Trading Securities:</b>				
Mortgage-backed securities	—	20	—	20
Corporate bonds	—	5	—	5
Common stock	87	—	—	87
Sponsored funds	564	—	—	564
<b>Equity Method Securities:</b> <sup>(1)</sup>				
Sponsored funds	66,722	—	—	66,722
Sponsored privately offered funds				
measured at net asset value <sup>(2)</sup>	—	—	—	3,173
Total	\$ 67,373	25	—	71,396

(1) Substantially all of the Company's equity method investments are investment companies which record their underlying investments at fair value. Fair value is measured using the Company's share of the investee's underlying net income or loss, which is predominately representative of fair value adjustments in the investments held by the equity method investee.

(2) Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheet.

**(4) Goodwill and Identifiable Intangible Asset**

Goodwill represents the excess of purchase price over the tangible assets and the identifiable intangible asset of acquired business. Our goodwill is not deductible for tax purposes. Goodwill and the identifiable intangible asset (all considered indefinite-lived) at December 31, 2015 are as follows (in thousands):

Goodwill	\$ 8,242
Identifiable intangible asset	26,853
Total	\$ 35,095

In 2015, the Company's annual impairment test indicated that goodwill and the identifiable intangible asset summarized in the table above were not impaired.

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**(5) Property and Equipment**

A summary of property and equipment at December 31, 2015 is as follows (in thousands):

		<u>Estimated useful lives</u>
Furniture and fixtures	\$ 28,385	3 – 10 years
Data processing equipment	19,836	1 – 5 years
Computer software	92,327	1 – 10 years
Equipment	20,671	3 – 26 years
Leasehold improvements	21,630	1 – 15 years
Building	12,860	1 – 40 years
Land	<u>3,804</u>	
Property and equipment, at cost	199,513	
Accumulated depreciation	<u>(95,388)</u>	
Property and equipment, net	<u>\$ 104,125</u>	

At December 31, 2015, we have property and equipment under capital lease with a cost of \$2.1 million and accumulated depreciation of \$1.1 million.

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**(6) Income Taxes**

The tax effect of temporary differences that give rise to significant portions of deferred tax liabilities and deferred tax assets at December 31, 2015 is presented as follows (in thousands):

Deferred tax liabilities:	
Deferred sales commissions	(44)
Property and equipment	(9,494)
Benefit plans	(13,974)
Identifiable intangible asset	(8,221)
Prepaid expenses	(1,795)
	<hr/>
Total gross deferred liabilities	(33,528)
	<hr/>
Deferred tax assets:	
Additional pension and postretirement liability	28,675
Accrued compensation	10,349
Other accrued expenses	5,225
Unrealized losses on investment securities	1,715
Nonvested stock	18,065
State net operating loss carryforwards	3,315
Federal benefit on state liabilities	1,694
Unused state tax credits	1,468
Other	80
	<hr/>
Total gross deferred assets	70,586
	<hr/>
Valuation allowance	(4,864)
	<hr/>
Net deferred tax asset	\$ 32,194
	<hr/>

As of December 31, 2015, the Company had a valuation allowance against deferred tax assets for capital losses and state net operating loss carryforwards of \$1.7 million and \$3.2 million, respectively.

As of December 31, 2015, the Company had a deferred tax asset for unrealized losses on investment securities and partnerships of \$1.7 million that would be capital losses for tax purposes if realized. Due to the character of the loss and the limited carryforward period permitted by law upon realization, the Company may not realize the full tax benefit of the loss. Management believes it is not more likely than not that the Company will generate sufficient future capital gains to realize the full benefit of these capital losses and accordingly, a valuation allowance in the amount of \$1.7 million has been recorded as of December 31, 2015. During 2015, decreases in the fair value of the Company's available for sale securities portfolio and equity method investments resulted in an increase in the valuation allowance of \$1.7 million. Of this amount, \$1.5 million was recorded as an increase to income tax expense and \$0.2 million was recorded as an increase in accumulated other comprehensive loss.

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As of December 31, 2015, the Company has net operating loss carryforwards in certain states in which the Company files on a separate company basis and has recognized a deferred tax asset for such loss carryforwards. The deferred tax asset, net of federal tax effect, related to the carryforwards is approximately \$3.3 million at December 31, 2015. The carryforwards, if not utilized, will expire between 2016 and 2032. Management believes it is not more likely than not that the Company will generate sufficient future taxable income in certain states to realize the benefit of the net operating loss carryforwards, and accordingly, a valuation allowance in the amount of \$3.2 million has been recorded at December 31, 2015. The Company has state tax credits of \$1.5 million as of December 31, 2015 that can be utilized in future tax years. Of these state tax credit carryforwards, \$1.3 million will expire between 2024 and 2031 if not utilized and \$0.2 million will expire in 2026 if not utilized. The Company anticipates these credits will be fully utilized prior to their expiration dates.

The unrecognized tax benefits that are not expected to be settled within the next 12 months are included in other liabilities in the accompanying consolidated balance sheet; unrecognized tax benefits that are expected to be settled within the next 12 months are included in income taxes receivable; and unrecognized tax benefits that reduce a net operating loss, similar tax loss or tax credit carryforward are presented as a reduction to noncurrent deferred income taxes.

The total amount of accrued penalties and interest related to uncertain tax positions at December 31, 2015 of \$2.0 million (\$1.6 million net of federal benefit) is included in the total unrecognized tax benefits described above.

The following table summarizes the Company's reconciliation of unrecognized tax benefits (excluding penalties and interest) for the year ended December 31, 2015 (in thousands):

	<b>Unrecognized tax benefits</b>
Balance at January 1, 2015	\$ 4,427
Increases during the year:	
Gross increases – tax positions in prior period	442
Gross increases – current period tax positions	317
Decreases during the year:	
Gross decreases – tax positions in prior period	(311)
Decreases due to settlements with taxing authorities	(281)
Decreases due to lapse of statute of limitations	(504)
Balance at December 31, 2015	<u>\$ 4,090</u>

In the ordinary course of business, many transactions occur for which the ultimate tax outcome is uncertain. In addition, respective tax authorities periodically audit our income tax returns. These audits examine our significant tax filing positions, including the timing and amounts of deductions and the allocation of income among tax jurisdictions. The 2012 through 2015 federal income tax returns are the only open tax years that remain subject to potential future audit. State income tax returns for all years after

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2011 and, in certain states, income tax returns for 2011, are subject to potential future audit by tax authorities in the Company's major state tax jurisdictions.

**(7) Pension Plan and Postretirement Benefits Other Than Pension**

The Company participates in the WDR sponsored non-contributory retirement plan (the Plan) that covers substantially all employees. Benefits payable under the Plan are based on an employee's years of service and compensation during the final ten years of employment. WDR allocates pension expense to the Company for the Plan.

The total projected benefit obligation of the Plan is \$210.8 million, of which \$182.4 million relates to the Company. The total pension benefits liability (representing the projected benefit obligation in excess of the pension plan assets) recorded on the consolidated balance sheet of WDR at December 31, 2015 is \$36.9 million, of which \$31.9 million is included in accrued pension and postretirement costs on the Company's consolidated balance sheet.

The Company also participates in the WDR sponsored unfunded defined benefit postretirement medical plan (medical plan) that covers substantially all employees and Waddell & Reed advisors. The medical plan is contributory with retiree contributions adjusted annually. All contributions to the medical plan are voluntary as it is not funded and is not subject to any minimum regulatory funding requirements. The contributions for each year represent claims paid for medical expenses. Net accrued medical plan costs in the amount of \$8.4 million are recorded on the consolidated balance sheet of WDR at December 31, 2015, of which \$8.0 million relates to the Company. Of the Company's total liability at December 31, 2015, \$315 thousand is included in other current liabilities, while the remainder is long term in nature and is included in accrued pension and postretirement costs..

**(8) Employee Savings Plan**

The Company participates in the WDR sponsored defined contribution plan that qualifies under Section 401(k) of the Internal Revenue Code to provide retirement benefits to substantially all of our employees. As allowed under Section 401(k), the plan provides tax-deferred salary deductions for eligible employees. The Company's matching contributions to the plan for the year ended December 31, 2015 were \$5.5 million.

**(9) Uniform Net Capital Rule Requirements**

The Company is subject to the SEC Uniform Net Capital Rule (Rule 15c3-1), which requires the maintenance of minimum net capital and requires that the ratio of aggregate indebtedness to net capital, both as defined, shall not exceed 15.0 to 1.0. A broker/dealer may elect to not be subject to the Aggregate Indebtedness Standard of paragraph (a)(1)(i) of Rule 15c3-1, in which case net capital must exceed the greater of \$250 thousand or 2% of aggregate debit items computed in accordance with the Formula for Determination of Reserve Requirements for broker/dealers. The Company made this election and is not subject to the aggregate indebtedness ratio as of December 31, 2015. At December 31, 2015, the Company had net capital of \$21.7 million that was \$21.5 million in excess of its required net capital of \$250 thousand. The primary difference between net capital and stockholder's equity are the nonallowable

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assets, including equity in subsidiaries, that are excluded from net capital. See Schedule I for additional information regarding net capital.

**(10) Rule 15c3-3 Exemption**

The Company does not hold customer funds or safekeep customer securities and is therefore exempt from Rule 15c3-3 of the SEC under subsection (k)(1), (k)(2)(i) and (k)(2)(ii). The Company did not have any customers' fully paid securities and excess margin securities that were not in the Company's possession or control as of December 31, 2015 for which instructions to reduce to possession or control had been issued as of December 31, 2015, but for which the required action was not taken by the Company within the time frames specified under Rule 15c3-3 of the Securities Exchange Act of 1934. The Company also did not have any customers' fully paid securities and excess margin securities for which instructions to reduce to possession or control had not been issued as of December 31, 2015, excluding items arising from "temporary lags that result from normal business operations" as permitted under Rule 15c3-3 of the Securities Exchange Act of 1934.

**(11) Share-Based Compensation**

WDR allocates expenses for nonvested shares of WDR stock to the Company that, in turn, are granted to certain key personnel of the Company under its stock incentive plans. Nonvested stock awards are valued on the date of grant, have no purchase price and vest over four years in 33⅓% increments on the second, third, and fourth anniversaries of the grant date. Under WDR's stock plans, shares of nonvested stock may be forfeited upon the termination of employment with the Company, dependent upon the circumstances of termination. Except for restrictions placed on the transferability of nonvested stock, holders of nonvested stock have full stockholders' rights during the term of restriction, including voting rights and the rights to receive cash dividends. The Company pays WDR for expense related to these awards.

**(12) Lease Commitments**

We lease certain home office buildings, certain sales and other office space and equipment under long-term operating leases. Future minimum rental commitments under non-cancelable operating leases are as follows:

<u>Year</u>	<u>Commitments</u> <u>(in thousands)</u>
2016	\$ 21,368
2017	17,646
2018	13,622
2019	8,971
2020	4,606
Thereafter	12,195
	<u>\$ 78,408</u>

(Continued)

**WADDELL & REED, INC. AND SUBSIDIARIES**  
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New leases are expected to be executed as existing leases expire. Thus, future minimum lease commitments are not expected to be materially different than those in 2015.

**(13) Related Party Transactions**

The current amounts due from affiliates at December 31, 2015 includes noninterest-bearing advances for current operating expenses and commissions due from the sales of affiliates' products. The current amounts due to affiliates at December 31, 2015 include amounts due for administrative and other services.

The amount classified as income tax receivable at December 31, 2015 consists entirely of amounts due from WDR for tax allocations.

We earn investment management fee revenues from the Advisors Funds and Ivy Funds VIP for which we also act as an investment adviser, pursuant to an investment management agreement with each Fund. In addition, we have agreements with the Advisors Funds and Ivy Funds VIP pursuant to Rule 12b-1 under the Investment Company Act of 1940, as amended, pursuant to which distribution and service fees are collected from the Advisor Funds and Ivy Funds VIP for distribution of mutual fund shares, for costs such as advertising and commissions paid to broker/dealers, and for providing ongoing services to shareholders of the Advisor Funds and Ivy Funds VIP and/or maintaining shareholder accounts. We also earn service fee revenues by providing various services to the Advisor Funds and their shareholders pursuant to a shareholder servicing agreement with each Fund and an accounting service agreement with the Advisor Funds and Ivy Funds VIP. These agreements are approved or renewed on an annual basis by each Fund's board of trustees, including a majority of the disinterested members. Funds and separate accounts receivable includes amounts due from the Funds for aforementioned services.

The Company earns point of sale commissions and Rule 12b-1 fees on sales of the Ivy Funds by the Company's licensed financial advisors. The Company is program manager for a 529 plan and earns point of sale commission from the sale of Class E shares of certain Ivy Funds by the Company's licensed financial advisors and financial intermediaries that have entered into 529 plan selling agreements with the Company.

Through revenue sharing allocation agreements with affiliates, the Company receives 25 basis points on gross sales of assets and 10 basis points on average assets under management for Ivy Funds sold through the Advisor channel. The Company also receives 10 basis points on gross sales of assets and 10 basis points on average assets under management for separately managed account relationships established by the institutional channel.

**(14) Contingencies**

The Company is involved from time to time in various legal proceedings, regulatory investigations and claims incident to the normal conduct of business, which may include proceedings that are specific to us and others generally applicable to business practices within the industries in which we operate. A substantial legal liability or a significant regulatory action against us could have an adverse effect on our business, financial condition and results of operations in a particular quarter or year.

The Company establishes reserves for litigation and similar matters when those matters present material loss contingencies that management determines to be both probable and reasonably estimable in

(Continued)

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accordance with Accounting Standards Codification 450, "*Contingencies Topic*" ASC 450. These amounts are not reduced by amounts that may be recovered under insurance or claims against third parties, but undiscounted receivables from insurers or other third parties may be accrued separately. The Company regularly revises such accruals in light of new information. The Company discloses the nature of the contingency when management believes it is reasonably possible the outcome may be significant to the Company's consolidated balance sheet and, where feasible, an estimate of the possible loss. For purposes of our litigation contingency disclosures, "significant" includes material matters as well as other items that management believes should be disclosed. Management's judgment is required related to contingent liabilities because the outcomes are difficult to predict.

In an action filed on February 18, 2016 in the United States District Court for the District of Kansas, *Saket Kapor(sic), Peter Brockett and Hieu Phan v. Ivy Investment Management Company, et. al.* (Case No. 2:16-cv-02106-JWL-TJJ), W&R Inc.'s registered investment advisor subsidiary, the trustees of two of the Company's affiliated mutual funds, and an officer of a W&R Inc.'s subsidiary were sued in a putative derivative action by three mutual fund shareholders alleging breach of fiduciary duty and breach of contract claims relating to investments held in the affiliated mutual funds. On behalf of the mutual funds, Plaintiffs seek monetary damages and demand a jury trial. To date, no responsive pleading has been filed and no discovery has taken place.

In the opinion of management, the ultimate resolution and outcome of this matter is uncertain. Given the preliminary nature of the proceedings and the Company's dispute over the merits of the claims, the Company is unable to estimate a range of reasonably possible loss, if any, that such matter may represent. While the ultimate resolution of this matter is uncertain, an adverse determination against the Company could have a material adverse impact on our business, financial condition and results of operations.

**(15) Concentration of Credit Risk**

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents held. The Company maintains cash and cash equivalents with various financial institutions. Cash deposits maintained at financial institutions may exceed the federally insured limit.

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