LABRANCHE & CO INC
Form 10-Q
August 11, 2008
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended June 30, 2008

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from ______ to ______

Commission File Number: 001-15251

LABRANCHE & CO INC.

(Exact name of registrant as specified in its charter)

Delaware	**13-4064735**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

33 Whitehall Street, New York, New York 10004

(Address of principal executive offices) (Zip Code)

(212) 425-1144

(Registrant s telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

Large accelerated filer ¨ Accelerated filer x

Non-accelerated filer ¨ (Do not check if a smaller reporting company)

Smaller reporting company ¨

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

The number of shares of the registrant s common stock outstanding as of August 8, 2008 was 61,993,216.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

LaBRANCHE & CO INC. and SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(000 s omitted except per share data)

(unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
REVENUES:				
Net gain on principal transactions	$ 44,917	$ 64,014	$ 105,097	$ 112,933
Commissions and other fees	9,950	11,927	19,959	24,688
Net loss on investments	(36,344)	(53,673)	(117,769)	(58,528)
Interest income	17,469	67,348	47,394	132,005
Other	1,110	1,158	1,403	1,282
Total revenues	37,102	90,774	56,084	212,380
Interest expense:				
Debt	8,504	12,726	19,367	25,521
Inventory financing	20,808	79,230	51,620	150,159
Total interest expense	29,312	91,956	70,987	175,680
Total revenues, net of interest expense	7,790	(1,182)	(14,903)	36,700
EXPENSES:				
Employee compensation and related benefits	19,594	24,188	48,124	48,086
Exchange, clearing and brokerage fees	9,743	10,597	20,401	19,651
Lease of exchange memberships and trading license fees	416	630	843	1,312
Depreciation and amortization	907	3,617	1,797	7,129
Goodwill impairment		164,100		164,100
Specialist stock list impairment		335,264		335,264
Restructuring costs		849		1,073
Early extinguishment of debt	5,119		6,005	
Other	6,923	10,059	14,271	19,565
Total expenses	42,702	549,304	91,441	596,180
Loss before benefit for income taxes	(34,912)	(550,486)	(106,344)	(559,480)
BENEFIT FOR INCOME TAXES	(13,571)	(181,542)	(44,766)	(184,981)
Loss applicable to common stockholders	$ (21,341)	$ (368,944)	$ (61,578)	$ (374,499)
Weighted-average common shares outstanding:				
Basic	61,993	61,471	61,924	61,370
Diluted	61,993	61,471	61,924	61,370

Loss per share:								
Basic	$	(0.34)	$	(6.00)	$	(0.99)	$	(6.10)
Diluted	$	(0.34)	$	(6.00)	$	(0.99)	$	(6.10)

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

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LaBRANCHE & CO INC. and SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(000 s omitted except per share data)

	As of	
ASSETS	**June 30, 2008 (unaudited)**	**December 31, 2007 (1) (audited)**
Cash and cash equivalents	$ 276,877	$ 504,654
Cash and securities segregated under federal regulations	1,191	1,573
Receivable from brokers, dealers and clearing organizations	356,979	343,729
Financial instruments owned, at fair value	3,681,377	4,267,395
Commissions and other fees receivable		23
Exchange memberships owned, at adjusted cost (market value of $8,258 and $7,790, respectively)	1,315	1,315
Office equipment and leasehold improvements, at cost, less accumulated depreciation and amortization of $12,650 and $10,990, respectively	16,821	17,652
Intangible assets:		
Trade name	25,011	25,011
Goodwill	84,218	84,218
Income tax receivable	2,416	11,802
Other assets	36,651	41,219
Total assets	$ 4,482,856	$ 5,298,591
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Payable to brokers, dealers and clearing organizations	$ 181,157	$ 104,759
Payable to customers	36	93
Financial instruments sold, but not yet purchased, at fair value	3,529,085	4,062,995
Accrued compensation	25,844	16,729
Accounts payable and other accrued expenses	29,464	36,980
Other liabilities	12,277	12,583
Deferred tax liabilities, net	26,132	71,024
Short term debt		5,700
Long term debt	209,888	459,811
Total liabilities	4,013,883	4,770,674
Commitments and contingencies		
Common stock, $.01 par value, 200,000,000 shares authorized; 61,993,216 and 61,490,638 shares issued and outstanding at June 30, 2008 and December 31, 2007, respectively	620	615
Additional paid-in capital	700,407	699,099
Accumulated other comprehensive income (loss)	332	(989)
Accumulated deficit	(232,386)	(170,808)
Total stockholders equity	468,973	527,917
Total liabilities and stockholders equity	$ 4,482,856	$ 5,298,591

(1) Certain of the Company s December 31, 2007 balances have been reclassified to conform to the presentation in the current period, deferred tax assets were netted against deferred tax liabilities. This reclassification did not affect stockholders equity or earnings.

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

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LaBRANCHE & CO INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN

STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME

(000 s omitted)

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained (Deficit) Earnings	Accumulated Other Comprehensive (Loss)/Income	Total
BALANCE, December 31, 2006	60,734	$ 607	$ 694,434	$ 179,666		874,707
Net loss				(350,474)		(350,474)
Other comprehensive income:						
Cumulative translation adjustment, net of taxes					(989)	(989)
Comprehensive income						(351,463)
Issuance of restricted stock, shares for option exercises and related compensation, including excess tax benefit of $99 thousand	757	8	4,665			4,673
BALANCE, December 31, 2007	61,491	$ 615	$ 699,099	$ (170,808)	(989)	527,917
Net loss				(61,578)		(61,578)
Other comprehensive income:						
Cumulative translation adjustment, net of taxes					1,321	1,321
Comprehensive income						(60,257)
Issuance of restricted stock, shares for option exercises and related compensation	502	5	1,308			1,313
BALANCE, June 30, 2008	61,993	$ 620	$ 700,407	$ (232,386)	332	468,973

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

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LaBRANCHE & CO INC. and SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(000 s omitted)

	Six Months Ended June 30, 2008 (unaudited)	Six Months Ended June 30, 2007 (unaudited)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (61,578)	$ (374,499)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,797	7,129
Amortization of debt issuance costs and bond discount	814	997
Charge on early extinguishment of debt	6,005	
Stock-based compensation expense	2,109	2,661
Deferred tax benefit	(44,892)	(180,130)
Goodwill impairment		164,100
Stock list impairment		335,264
Changes in operating assets and liabilities:		
Cash and securities segregated under federal regulations	382	3,970
Securities purchased under agreements to resell		30,000
Receivable from brokers, dealers and clearing organizations	(13,250)	11,318
Receivable from customers		2,421
Financial instruments owned, at fair value	586,018	(560,191)
Commissions and other fees receivable	23	3,530
Income tax receivable	8,590	(4,437)
Other assets	2,767	1,219
Payable to brokers, dealers and clearing organizations	76,398	693,180
Payable to customers	(57)	(4,167)
Financial instruments sold, but not yet purchased, at fair value	(533,910)	(170,693)
Accrued compensation	9,115	6,967
Accounts payable and other accrued expenses	(7,516)	(7,353)
Other liabilities	(306)	(42)
Excess tax benefit from vesting of stock based compensation		(99)
Net cash provided by (used in) operating activities	32,509	(38,855)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Payments for purchases of office equipment and leasehold improvements	(966)	(2,305)
Payments for purchases of exchange memberships		(1)
Proceeds from sale of business unit		2,250
Net cash used in investing activities	(966)	(56)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Principal payments of short term debt	(5,700)	(17,338)
Early extinguishment of long term debt	(249,923)	
Premium on early extinguishment of debt	(3,739)	
Excess tax benefit from vesting of stock based compensation		99
Net cash used in financing activities	(259,362)	(17,239)
Effect of exchange rate changes on cash and cash equivalents	42	

Decrease in cash and cash equivalents	(227,777)	(56,150)
CASH AND CASH EQUIVALENTS, beginning of period	504,654	557,352
CASH AND CASH EQUIVALENTS, end of period	$ 276,877	$ 501,202
SUPPLEMENTAL DISCLOSURE OF CASH PAID DURING THE PERIOD FOR:		
Interest	$ 72,701	$ 179,164
Income taxes	$ 1,122	$ 2,268

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

LaBRANCHE & CO INC. and SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. ORGANIZATION AND DESCRIPTION OF BUSINESS

The condensed consolidated financial statements include the accounts of LaBranche & Co Inc., a Delaware corporation (the Holding Company), and its subsidiaries, LaBranche & Co. LLC, a New York limited liability company, LaBranche Financial Services, LLC, a New York limited liability company (LFS), LaBranche Structured Holdings, Inc., a Delaware corporation (LSHI), LABDR Services, Inc., a Delaware corporation (LABDR), and LaBranche & Co. B.V., a Netherlands private limited liability company (BV). The Holding Company is the sole member of LaBranche & Co. LLC and LFS, the 100% stockholder of LSHI and LABDR and the sole owner of BV. LSHI is a holding company that is the sole member of LaBranche Structured Products, LLC, a New York limited liability company (LSP), and LaBranche Structured Products Specialists LLC, a New York limited liability company (LSPS), the 100% owner of LaBranche Structured Products Europe Limited, a United Kingdom single member private company (LSPE), and LaBranche Structured Products Hong Kong Limited, a Hong Kong single member private company (LSPH), and the sole stockholder of LaBranche Structured Products Direct, Inc., a New York corporation (LSPD and collectively with the Holding Company, LaBranche & Co. LLC, LFS, LSHI, LABDR, BV, LSP, LSPS, LSPE, LSPD and LSPH, the Company).

LaBranche & Co. LLC is a registered broker-dealer that operates primarily as a specialist in equity securities and rights listed on the New York Stock Exchange (NYSE). LFS is a registered broker-dealer and a member of the NYSE and other exchanges and primarily provides securities execution and brokerage services to institutional investors. LSP is a registered broker-dealer that operates as a specialist in options, futures and Exchange-Traded Funds (ETFs) on several exchanges, and as a market-marker in options, ETFs and futures on several exchanges. LSPE operates as a market-maker for ETFs traded on the London Stock Exchange and the Euroex and Euronext exchanges, and is registered as a broker-dealer with the United Kingdom s Financial Services Authority. LSPH is registered as a market-maker for ETFs in Hong Kong and is registered as a broker-dealer with Hong Kong s Securities and Futures Commission. LSPD is a registered broker-dealer and Financial Industry Regulatory Authority (FINRA) member firm that was acquired by LSH in April 2006 and is primarily an institutional execution firm in equities and structured products. LABDR is an investment company with a minority ownership in a New Jersey aviation partnership. BV represented LaBranche & Co. LLC in European markets and provided client services to LaBranche & Co. LLC s European listed companies until June 30, 2007, when it ceased operations. LSPS has been inactive since October 31, 2007.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Certain of the Company s December 31, 2007 statement of financial condition balances have been reclassified to conform to the presentation in the current period. Pursuant to SFAS No. 109 the Company netted its deferred tax assets against deferred tax liabilities by taxing jurisdiction to determine net deferred taxes. This reclassification did not affect previously reported net income before provision for income taxes, net income applicable to common stockholders or stockholders equity.

Cash and Cash Equivalents

Cash and cash equivalents include all demand deposits held in banks, highly liquid investments with original maturities of 90 days or less and currency positions that are being held in the prime brokerage account at the Company s clearing broker for its specialist and market-making operations. Certain portions of these balances are used to meet regulatory requirements (see Note 5).

Use of Estimates

The use of generally accepted accounting principles requires management to make certain estimates and assumptions. In addition to the estimates we make in connection with fair value measurements and the accounting for goodwill and identifiable intangible assets, the use of estimates and assumptions is also important in determining provisions for potential losses that may arise from litigation and regulatory proceedings and tax audits.

A substantial portion of our compensation and benefits represents discretionary bonuses, which are determined at year end. We believe the most appropriate way to allocate estimated annual discretionary bonuses among interim periods is in proportion to the net revenues earned in such periods. In addition to the level of net revenues, our overall compensation expense in any given year is also influenced by, among other factors, prevailing labor markets, business mix and the structure of our share-based compensation programs.

Adoption of SFAS 157 Fair Value Measurements

The Company adopted SFAS No. 157, Fair Value Measurements (SFAS 157), as of January 1, 2008. SFAS 157 defines fair value, expands disclosure requirements around fair value and specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company s market assumptions (see Note 11).

3. INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND FINANCIAL INFORMATION

The unaudited interim condensed consolidated financial information as of June 30, 2008 and for the three months and six months ended June 30, 2008 and 2007 is presented in the accompanying condensed consolidated financial statements. The unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to

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Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial information. The unaudited interim condensed consolidated financial information reflects all adjustments which are, in the opinion of management, necessary for a fair presentation of the results for such periods. The preparation of condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates and assumptions. The unaudited interim condensed consolidated financial information as of June 30, 2008 should be read in conjunction with the audited consolidated financial statements and notes thereto as of December 31, 2007 included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007 filed with the Securities and Exchange Commission (SEC) on March 17, 2008 (the 2007 10-K). Results of the second quarter 2008 interim period are not necessarily indicative of results to be obtained for the full fiscal year.

4. INCOME TAXES

The Company accounts for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes and FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48). SFAS No. 109 requires the recognition of tax benefits or expenses based on the estimated future tax effects of temporary differences between the financial statement and tax bases of its assets and liabilities. Deferred tax assets and liabilities primarily relate to tax basis differences on unrealized gains on corporate equities, not readily marketable, stock-based compensation, other compensation accruals, amortization periods of certain intangible assets and differences between the financial statement and tax bases of assets acquired.

The components of the provision for income taxes reflected on the condensed consolidated statements of operations are set forth below (000 s omitted):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Current federal, state and local taxes	$ 1,180	$ (7,115)	$ 126	$ (4,851)
Deferred tax (benefit) provision	(14,751)	(174,427)	(44,892)	(180,130)
Total (benefit) provision for income taxes	$ (13,571)	$ (181,542)	$ (44,766)	$ (184,981)

Included in the current federal, state and local taxes are foreign taxes of $37 and $1,706 for the three months and six months ended June 30, 2008 respectively. The foreign taxes represent taxes payable to the United Kingdom for LSPE, the Company s single member private equity company in the UK that is a controlled foreign corporation as of January 1, 2008.

The Company has a $4.1 million federal net operating loss carryforward from 2007 expiring in 2027. In addition, the Company has the following state and city net operating loss carryforwards (000 s omitted):

Year	NYS	NYC	Expiring
2004	$ 20,549	$ 18,083	2024
2007	$ 34,478	$ 34,681	2027

5. CAPITAL AND NET LIQUID ASSET REQUIREMENTS

LaBranche & Co. LLC, as a specialist and member of the NYSE, is subject to the provisions of SEC Rule 15c3-1, as adopted and administered by the SEC and NYSE. LaBranche & Co. LLC is required to maintain minimum net capital, as defined, equivalent to the greater of $100,000 or $^{1}/_{15}$ of aggregate indebtedness, as defined.

As of June 30, 2008 and December 31, 2007, LaBranche & Co. LLC s net capital, as defined under SEC Rule 15c3-1, was $103.8 million and $306.8 million, respectively, which exceeded the minimum requirements by $103.4 million and $306.4 million, respectively. LaBranche & Co. LLC s aggregate indebtedness to net capital ratio on those dates was .05 to 1 and .02 to 1, respectively.

The NYSE generally requires its specialist firms to maintain a minimum dollar regulatory capital amount in order to establish that they can meet, with their own Net Liquid Assets (NLA), their position requirement. As of June 30, 2008 LaBranche & Co. LLC s NYSE minimum required dollar amount of NLA, as defined, was $69.8 million and its actual NLA, as defined, was $99.3 million. As of December 31, 2007, LaBranche & Co. LLC s NYSE minimum required dollar amount of NLA, as defined was $276.2 million, and LaBranche & Co. LLC s actual NLA, as defined was $300.1 million. As of June 30, 2008 and December 31, 2007, LaBranche & Co. LLC s actual NLA exceeded the NLA requirement, thus satisfying its NLA requirement as of each of those dates. LaBranche & Co. LLC s NLA as of June 30, 2008 and December 31, 2007 included approximately $72.1 million and $74.7 million, respectively, in NYX shares (after the risk-based haircuts required to be taken in connection with those securities).

The minimum required dollar amount of NLA fluctuates daily and is computed by adding two components. The first component is equal to $0.25 million for each one tenth of one percent (.1%) of the aggregate NYSE transaction dollar volume in a cash equities specialist organization s allocated securities, as adjusted at the beginning of each month based on the prior month transaction dollar volume. Prior to February 8, 2008 the first component was equal to $1.0 million for each one tenth of one percent (.1%). The second component is calculated either by multiplying the average haircuts on a specialist organization s proprietary positions over the most recent twenty days by three, or by using an NYSE-approved value at risk (VAR) model. Based on this two part calculation, LaBranche & Co. LLC s NLA requirement could increase or decrease in future periods based on its own trading activity and all other specialists trading as a respective percentage of overall NYSE transaction dollar volume. In February 2008, pursuant to the SEC approved reduction in the NLA requirement LaBranche & Co. LLC s NLA requirement was reduced by approximately $205.0 million. The majority of the amended NLA requirement is met by the shares of NYSE Euronext, Inc. common stock (the NYX shares) held by LaBranche & Co. LLC. The amended NLA requirements enabled LaBranche & Co. LLC to make a dividend distribution of $200.0 million to LaBranche & Co

Inc. in the first quarter of 2008. LaBranche & Co. LLC has approximately $27.2 million in cash and other liquid assets over and above the NYX shares used to meet its continuing NLA requirements. This $27.2 million includes a cushion over and above the required NLA to account for potential fluctuations in LaBranche & Co. LLC s NLA requirement, as well as fluctuations in the fair value of its NYX shares, as described above.

As a registered broker-dealer and member firm of the NYSE, LFS is subject to SEC Rule 15c3-1, as adopted and administered by the SEC and the NYSE. Under the alternative method permitted by this rule, the minimum required net capital is equal to the greater of $1.0 million or 2.0% of aggregate debit items, as defined. As of June 30, 2008 and December 31, 2007, LFS net capital, as defined, was $33.6 million and $16.6 million, respectively, which exceeded minimum requirements by $32.6 million and $15.6 million, respectively. In February 2008, the Company contributed an additional $20.0 million in capital to LFS in order to enable LFS to conduct increased trading activities in connection with its institutional execution business. A portion of the net capital at LFS is met with the value of the NYX shares held by that broker/dealer.

As a registered broker-dealer and AMEX member firm, LSP is subject to SEC Rule 15c3-1, as adopted and administered by the SEC and the AMEX. LSP is required to maintain minimum net capital, as defined, equivalent to the greater of $100,000 or $^{1}/_{15}$ of aggregate indebtedness, as defined. As of June 30, 2008 and December 31, 2007, LSP s net capital, as defined, was $107.9 million and $62.6 million, respectively, which exceeded minimum requirements by $106.1 million and $60.9 million, respectively. LSP s aggregate indebtedness to net capital ratio on those dates was .25 to 1 and .41 to 1, respectively.

As a registered broker-dealer and AMEX and FINRA member firm, LSPD is subject to SEC Rule 15c3-1, as adopted and administered by the SEC, AMEX and FINRA. LSPD is required to maintain minimum net capital, as defined, equivalent to the greater of $5,000 or $^{1}/_{15}$ of aggregate indebtedness, as defined. As of June 30, 2008 and December 31, 2007, LSPD s net capital, as defined, was $2.8 million and $3.0 million, respectively, which exceeded its minimum requirements by $2.8 million and $3.0 million, respectively.

As a registered broker dealer, LSPE is subject to the capital adequacy and capital resources as managed and monitored in accordance with the regulatory capital requirements of the Financial Services Authority (FSA) in the United Kingdom. In calculating regulatory capital, the Company s capital consists wholly of Tier 1 capital. Tier 1 capital is the core measure of a Company s financial strength from a regulator s point of view. It consists of the type of financial capital considered the most reliable and liquid, primarily Shareholder s Equity. As of June 30, 2008 Tier 1 capital, as defined, was $34.7 million which exceeded the total variable capital requirement by $3.7 million. At December 31, 2007 Tier 1 capital, as defined, was $14.2 million which resulted in a deficit of $1.2 million. The December 31, 2007 calculation did not include accumulated profits for the year ended December 31, 2007 which was in excess of the deficit. With those results now audited they can be included in Tier 1 regulatory capital. In addition, the Company had injected an additional $9.9 million of share capital in January 2008, further enhancing regulatory capital.

As a licensed corporation registered under the Hong Kong Securities and Futures Ordinance, LSPH is subject to the capital requirements of the Hong Kong Securities and Futures (Financial Resources) Rules (FRR). The minimum paid-up share capital requirement is HKD 5,000,000 ($0.6 million at June 30, 2008 and December 31, 2007) and the minimum liquid capital requirement is the higher of HKD 3,000,000 ($0.4 million at June 30, 2008 and December 31, 2007) and the variable required liquid capital as defined in the FRR. The company monitors its compliance with the requirements of the FRR on a daily basis. As of June 30, 2008 and December 31, 2007, LSPH s liquid capital, as defined was $0.9 and $0.7 million, respectively, which exceeded its minimum requirements by $0.5 and $0.3 million, respectively. In addition, the Company had injected an additional $0.5 million of share capital in June 2008 further enhancing regulatory capital.

6. LOSS PER SHARE

The computations of basic and diluted loss per share are set forth below (000 s omitted, except per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Numerator for basic and diluted loss per share net loss applicable to common stockholders	$ (21,341)	$ (368,944)	$ (61,578)	$ (374,499)
Denominator for basic loss per share weighted-average number of common shares outstanding	61,993	61,471	61,924	61,370
Dilutive shares:				
Stock options				
Restricted stock units				
Denominator for diluted loss per share weighted-average number of common shares outstanding	61,993	61,471	61,924	61,370
Loss per share:				
Basic	$ (0.34)	$ (6.00)	$ (0.99)	$ (6.10)
Diluted	$ (0.34)	$ (6.00)	$ (0.99)	$ (6.10)

Options to purchase an aggregate of 1,090,000 and 1,409,389 shares of common stock were outstanding at June 30, 2008 and 2007, respectively, but were not included in the computation of diluted earnings per share because the options exercise prices were greater than the market price of the Company s common stock. For the 2008 and 2007 second quarters, respectively, 932,564 and 837,184 potentially dilutive shares from restricted stock units were not included in the computation of diluted net loss per share because to do so would be anti-dilutive.

7. EMPLOYEE INCENTIVE PLANS

SFAS No. 123(R) requires compensation costs related to share-based payment transactions to be recognized in the financial statements over the period that an employee provides service in exchange for the award.

The following disclosures are also being provided pursuant to the requirements of SFAS No. 123(R):

The Company sponsors one share-based employee incentive plan the LaBranche & Co Inc. Equity Incentive Plan (the Plan), which provides for grants of incentive stock options, nonqualified stock options, restricted shares of common stock, restricted stock units, unrestricted shares and stock appreciation rights. The fair value of the restricted stock awards is determined by using the closing price of the Company s common stock on the respective dates on which the awards are granted. Grant date is determined to be the date the compensation committee of the Board of Directors approves the grant, except in circumstances where the approval by the compensation committee is contingent upon a future event, such as the negotiation and execution of an employment agreement, in which case the grant date is the date is the date the condition is satisfied. Amortization of compensation costs for grants awarded under the Plan recognized during the three and six months ended June 30, 2008 was approximately $1.0 million and $1.8 million compared to $1.0 million and $2.4 million for the same periods in 2007. The tax benefit realized in the Consolidated Statements of Operations for the Plan was approximately $0.4 million and $0.7 million for the three and six months ended June 30, 2008 compared to $0.4 million and $1.0 million for the same periods in 2007, respectively.

Unrecognized compensation cost related to the Company s non-vested stock option and restricted stock unit awards totaled $5.7 million at June 30, 2008 and $4.9 million at December 31, 2007. The cost of these non-vested awards is generally expected to be recognized over period of approximately three years.

SFAS No. 123(R) generally requires share-based awards granted to retirement-eligible employees to be expensed immediately. The Company did not grant any share-based awards prior to our adoption of SFAS No. 123(R) to retirement-eligible employees or those with non-substantive non-compete agreements. In addition, no grants of any stock options or RSUs were changed or amended after the Company s adoption of SFAS No. 123(R) to reflect retirement eligibility or non-compete agreements.

The total number of shares of the Company s common stock that may be issued under the Plan through fiscal 2009 may not exceed 7,687,500 shares. As of June 30, 2008 and December 31, 2007, 3,284,200 shares and 3,187,613 shares, respectively, were available for grant under the Plan.

Restricted Stock Units

All of the RSUs outstanding as of June 30, 2008 and 2007 require future service as a condition to the delivery of the underlying shares of common stock on their respective vesting dates. The RSUs are granted under the Company s Equity Incentive Plan and vest over varying numbers of years. An employee who receives RSUs does not have any ownership rights with respect to the underlying shares until the shares vest pursuant to the terms of an RSU agreement. In all cases, delivery of the underlying shares of common stock is conditioned on the grantees satisfying certain requirements outlined in the agreements. Generally, the RSUs become fully vested if the grantee s employment with the Company terminates by reason of

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death or disability prior to vesting. The grantee forfeits the unvested portion of the RSUs upon the termination of employment for any reason other than death or disability. When delivering the underlying shares of stock to employees, the Company generally issues new shares of common stock, as opposed to reissuing treasury shares.

The following table provides information about grants of RSUs:

	Number of Shares	Weighted Average Price per Share
RSUs Outstanding as of December 31, 2007	1,083,484	$ 9.44
Granted		
Vested	(444,340)	9.12
Forfeited	(24,997)	9.12
RSUs Outstanding as of March 31, 2008	614,147	$ 9.68
Granted	692,000	5.55
Vested		
Forfeited	(54,828)	9.43
RSUs Outstanding as of June 30, 2008	1,251,319	$ 7.41

Under SFAS No. 123(R), the Company is required to estimate forfeitures of RSUs for purposes of determining the Company s share-based award expense. Applying SFAS No. 123(R) as of June 30, 2008, for purposes of determining share-based award expense, RSUs with respect to 1,215,851 shares of the Company s common stock were expected to vest based on the original shares issued of 3,393,500, with a weighted average price of $7.92 per share.

Stock Options

As of June 30, 2008, all stock options granted to employees were fully vested and exercisable. In general, all stock options expire on the tenth anniversary of grant, although they may be subject to earlier termination or cancellation in certain circumstances under the Plan and the stock option agreement, such as death, disability or other termination of employment prior to the tenth anniversary of grant. The dilutive effect, if any, of the Company s outstanding stock options is included in Weighted Average Common Shares Outstanding Diluted on the Condensed Consolidated Statement of Operations.

The following table provides information about options to purchase the Company s common stock:

	Number of Shares	Weighted Average Exercise Price per Share
Options Outstanding as of December 31, 2007	1,165,000	$ 23.77
Options Granted		
Options Exercised		
Options Forfeited		
Options Outstanding as of March 31, 2008	1,165,000	$ 23.77
Options Granted		
Options Exercised		
Options Forfeited	(75,000)	27.50

Options Outstanding as of June 30, 2008	1,090,000	$ 23.51
Options Exercisable as of:		
March 31, 2008	1,165,000	$ 23.77
June 30, 2008	1,090,000	$ 23.51

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The following table summarizes information about stock options outstanding as of June 30, 2008:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	**Number of Shares**	**Weighted Average Remaining Contractual Life**	**Weighted Average Exercise Price per Share**	**Number of Shares**	**Weighted Average Exercise Price per Share**
$11.00 $20.99	600,000	1.14	$ 14.00	600,000	$ 14.00
$31.00 $40.99	490,000	3.52	$ 35.15	490,000	$ 35.15
	1,090,000			1,090,000	

No options were exercised during the six months ended June 30, 2008 and June 30, 2007.

8. BUSINESS SEGMENTS

Segment information is presented in accordance with SFAS No. 131, Disclosures About Segments of an Enterprise and Related Information. The Company s business segments are based upon the nature of the financial services provided, their revenue source and the Company s management organization.

The Company s Specialist and Market-Making segment operates as a specialist in equities and rights listed on the NYSE, as a specialist in equities, options, ETFs and futures on several exchanges as well as a market-maker in ETFs, futures and options on several exchanges. The Specialist and Market-Making segment currently includes the operations of LaBranche & Co. LLC, LSP, LSPE, LSPH and LSPD.

The Company s Institutional Brokerage segment (formerly called the Execution and Clearing segment) provides mainly securities execution and brokerage services to institutional investors, and currently includes the operations of LFS. Until June 8, 2007, the Institutional Brokerage segment also provided securities clearing services to its own customers and customers of introducing brokers, when it outsourced its clearing operations to a major Wall Street financial services firm.

The Company s Other segment is comprised primarily of the interest on the Holding Company s indebtedness, unallocated corporate administrative expenses, including professional and legal costs, unallocated revenues (primarily interest income) and elimination entries. This section also includes the investment entity, LABDR, and the inactive company, BV.

Revenues and expenses directly associated with each segment are included in determining its operating results. Other expenses, including corporate overhead, which are not directly attributable to a particular segment, generally are allocated to each segment based on

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its resource usage levels or other appropriate measures. Interest with respect to the Company s outstanding senior notes, certain administrative expenses, corporate overhead expenses and other sources of revenues are not specifically allocated by management when reviewing the Company s segments performance, and appear in the Other section. Selected financial information for each segment is set forth below (000 s omitted):

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Specialist and Market-Making Segment:				
Total Revenues, net of interest expense	$ 13,486	$ 6,909	$ 25	$ 48,591
Operating expenses	28,761	37,033	67,551	70,056
Goodwill impairment		164,100		164,100
Specialist stock list impairment		335,264		335,264
Depreciation and amortization	85	2,721	171	5,487
Loss before taxes	(15,360)	(532,209)	(67,697)	(526,316)
Segment goodwill	84,218	84,218	84,218	84,218
Segment assets	$ 4,203,195	$ 4,953,910	$ 4,203,195	$ 4,953,910
Institutional Brokerage Segment:				
Total, Revenues, net of interest expense	$ 1,708	$ 2,295	$ 1,063	$ 9,282
Operating expenses	6,354	7,573	12,195	15,771
Depreciation and amortization	13	56	37	121
Loss before taxes	(4,659)	(5,334)	(11,169)	(6,610)
Segment assets	51,824	69,874	$ 51,824	$ 69,874
Other:				
Total Revenues, net of interest expense	$ (7,404)	$ (10,386)	$ (15,991)	$ (21,173)
Operating expenses	1,561	1,715	3,893	3,860
Early extinguishment of debt	5,119		6,005	
Depreciation and amortization	809	842	1,589	1,521
Loss before taxes	(14,893)	(12,943)	(27,478)	(26,554)
Segment assets	$ 227,837	$ 276,985	$ 227,837	$ 276,985
Total:				
Total, Revenues, net of interest expense	$ 7,790	$ (1,182)	$ (14,903)	$ 36,700
Operating expenses	36,676	46,321	83,639	89,687
Goodwill impairment		164,100		164,100
Specialist stock list impairment		335,264		335,264
Early extinguishment of debt	5,119		6,005	
Depreciation and amortization	907	3,619	1,797	7,129
Loss before taxes	(34,912)	(550,486)	(106,344)	(559,480)
Goodwill	84,218	84,218	84,218	84,218
Assets	$ 4,482,856	$ 5,300,769	$ 4,482,856	$ 5,300,769

9. NYSE GROUP RESTRICTED STOCK EXCHANGE TRANSACTION

The Company holds, in aggregate, 3,126,903 NYX shares collectively through its subsidiaries, LaBranche & Co. LLC and LFSL.

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On April 4, 2007, the NYSE Group consummated its merger with Euronext N.V. (the NYSE/Euronext merger) to form NYSE Euronext, Inc., and the Company s 3,126,903 shares of NYSE Group, Inc. common stock were exchanged for an equal number of the NYX shares, all of which continue to be owned by LaBranche & Co. LLC and LFSL. Following the NYSE/Euronext merger, the restricted NYX shares continued to be subject to the same restrictions on transfer as had existed before the NYSE/Euronext merger. The restriction with respect to the second tranche of the NYX shares was removed by NYSE Euronext in June 2007. The restriction on the remaining one-third of the Company s restricted NYX shares will be removed on March 7, 2009, unless removed earlier by the board of directors of NYSE Euronext in its sole discretion.

The Company has accounted for its investment in NYX restricted shares as corporate equities not readily marketable at the estimated fair value of such restricted shares pursuant to SFAS No. 157, Fair Value Measurements (SFAS 157). At June 30, 2008, the NYSE closing market price for the NYX shares was $50.66 per share as compared to the closing price of NYX shares at March 31, 2008 which was $61.71 per share. This resulted in the Company s recognition of an unrealized pre-tax loss of $33.2 million for the quarter ended June 30, 2008, which includes the effects of a valuation allowance due to the share restrictions and is included in net loss on investments in the Company s condensed consolidated statement of operations. There is no valuation allowance on shares without transfer restrictions, which are reported in financial instruments owned, at fair value.

On June 11, 2008, a quarterly dividend of $0.30 per share was paid to shareholders of record of NYSE Euronext as of the close of business on June 11, 2008. The aggregate dividend payment with respect to the Company s 3,126,903 NYX shares was $0.9 million in the second quarter of 2008 and is reported in the Company s other revenues.

10. FINANCIAL INSTRUMENTS

Financial instruments owned and financial instruments sold, but not yet purchased, at fair value, were as follows (000 s omitted):

	June 30, 2008	December 31, 2007
FINANCIAL INSTRUMENTS OWNED:		
Corporate equities, not readily marketable	$ 48,853	$ 83,945
Corporate equities	1,690,544	2,016,380
Options	906,119	1,025,670
Exchange-traded funds	793,110	1,000,600
Government and corporate bonds	237,931	138,159
Investment in limited partnerships	4,820	2,641
	$ 3,681,377	$ 4,267,395
FINANCIAL INSTRUMENTS SOLD, BUT NOT YET PURCHASED:		
Corporate equities	$ 1,661,402	$ 1,980,040
Options	1,091,574	1,183,884
Exchange-traded funds	714,158	769,094
Government and corporate bonds	61,951	129,977
	$ 3,529,085	$ 4,062,995

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11. FAIR VALUE MEASUREMENTS

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards, or SFAS No. 157 Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 applies only to fair value measurements already required or permitted by other accounting standards and does not impose requirements for additional fair value measures. Our adoption of SFAS No. 157 did not have a material impact on our financial condition or results of operations. Pursuant to SFAS No. 157, the fair value of a financial instrument is defined as the amount that would be received to sell an asset or paid to transfer a liability, or the exit price, in an orderly transaction between market participants at the measurement date.

We use fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Our financial instruments owned and financial instruments sold, but not yet purchased are recorded at fair value on a recurring basis.

We may be required to record at fair value other assets or liabilities on a non-recurring basis, such as our trade name and goodwill. These non-recurring fair value adjustments involve the application of fair value measurements in assessing whether these and other nonfinancial assets or nonfinancial liabilities are impaired.

The Company has elected to apply the deferral provisions in FSP No. 157-2 and therefore have only partially applied the provisions of SFAS No. 157. FSP No. 157-2 defers the effective date for the disclosure fair value measurements related to nonfinancial assets and nonfinancial liabilities to fiscal years beginning after November 15, 2008.

SFAS No 157 outlines a fair value hierarchy. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets and liabilities (which are considered level 1 measurements) and the lowest priority to unobservable inputs (which are considered level 3 measurements). The three levels of the fair value hierarchy under SFAS No. 157 are as follows:

- Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level 2 Quoted prices for similar instruments in active markets, quoted prices in markets that are not active or financial instruments for which all significant inputs are observable, either directly or indirectly;
- Level 3 Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions would reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Such valuation techniques include the use of option pricing models, discounted cash flow models and similar techniques.

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The following table represents the Company s fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of June 30, 2008 (000 s omitted):

	Level 1	Level 2	Level 3	Total
ASSETS:				
Financial instruments owned, at fair value:				
Corporate equities	$ 1,601,383	$ 142,834	$	$ 1,744,217
Government and corporate bonds	143,466	94,465		237,931
Options	890,600	15,519		906,119
Exchange-traded funds	658,007	135,103		793,110
Total financial instruments owned	$ 3,293,456	$ 387,921	$	$ 3,681,377
Cash equivalents	190,525			190,525
Securities segregated under federal regulations	1,189			1,189
Total assets, at fair value	$ 3,485,170	$ 387,921	$	$ 3,873,091
LIABILITIES:				
Government and corporate bonds	$ 46,676	$ 15,276	$	$ 61,952
Corporate equities	1,634,369	27,033		1,661,402
Options	1,079,875	11,698		1,091,573
Exchange-traded funds	362,956	351,202		714,158
Total financial instruments sold, not yet purchased	$ 3,123,876	$ 405,209	$	$ 3,529,085

Determining the fair value of our financial securities was determined from a variety of sources as follows:

For corporate equities and ETFs, fair value was determined by the closing price of the primary exchanges and was included in Level 1 for those that are actively traded. Those classified in Level 2 represent either restricted shares or those not actively traded with quoted market prices.

For government and corporate bonds, the primary source for pricing fixed income instruments is derived from our clearing broker who determines prices through various third party pricing services. The Company confirms these values using independent observable sources. When pricing cannot be confirmed the positions will be valued using broker quotes and included in Level 2.

For options, the fair values are based on the NBBO mid point average. Those included in Level 2 are valued based on broker quotes when a price could not be confirmed due to the security not being actively traded.

12. CONTINGENCIES

There have been no material new developments in the Company s legal proceedings since the March 17, 2008 filing of its Annual Report on Form 10-K for the year ended December 31, 2007 (the 2007 10-K) and the May 12, 2008 filing of its Quarterly Report on Form 10-Q for the first quarter of 2008 (the First Quarter 10-Q).

The Company believes that the claims asserted against it by the plaintiffs in the pending proceedings described in the 2007 10-K and First Quarter 10-Q are without merit, and the Company denies all allegations of wrongdoing. There can be no assurance, however, as to the outcome or timing of the resolution of these proceedings. Therefore, the Company is unable to estimate the amount or potential range of any loss that may arise out of these proceedings. The range of possible resolutions could include determinations and judgments against the Company or settlements that could require substantial payments by the Company that could have a material adverse effect on the Company s financial condition, results of operations and cash flows.

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In addition to the proceedings described in the 2007 10-K and First Quarter 10-Q, the Company and its operating subsidiaries have been the target, from time to time, of various claims, lawsuits and regulatory inquiries in the ordinary course of their respective businesses. While the ultimate outcome of those claims and lawsuits which are currently pending cannot be predicted with certainty, the Company believes, based on its understanding of the facts of these proceedings, that their ultimate resolution will not, in the aggregate, have a material adverse effect on the Company s financial condition, results of operations or cash flows.

13. SUBSEQUENT EVENTS

On June 17, 2008, NYSE Euronext, Inc. and the American Stock Exchange (the AMEX) announced that members of the AMEX Membership Corporation (the AMC) approved the adoption of the merger agreement between AMC and NYSE Euronext and certain of their subsidiaries. In July 2008, the AMEX submitted proposed rule changes in connection with the trading of AMEX- listed securities following the merger, including on which market each class of securities will trade following the merger. The SEC must still approve the rule changes in connection with the transaction and related AMEX-proposed trading rules before the merger becomes final. We currently unable to estimate how those new rules will affect our operations until they are finalized by the SEC. Under the terms of the merger agreement, NYSE Euronext will pay $260 million in NYSE Euronext common stock for the Amex. In addition, Amex members will be entitled to receive additional shares of NYSE Euronext common stock calculated by reference to net proceeds, if any, from the expected sale of the AMEX s lower Manhattan headquarters. The Company owns one AMEX seat and, upon consummation of the merger, would be entitled to a pro rata portion of the NYX shares issued in the merger, based on the one seat it owns, plus its pro rata portion of any proceeds from the sale of the AMEX s lower Manhattan headquarters.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.
Unless the context otherwise requires, the Company or we shall mean LaBranche & Co Inc. and its wholly-owned subsidiaries.

This Management s Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended December 31, 2007 (the 2007 10-K) and our Condensed Consolidated Financial Statements and the Notes thereto contained in this report.

Executive Overview

For the second quarter of 2008, our US GAAP net loss was $21.3 million, or $0.34 per share, compared to a net loss of $368.9 million, or $6.00 per share for the same period in 2007. These GAAP earnings were affected by significant unrealized losses of $33.2 million and $54.6 million, in the second quarter of 2008 and 2007, respectively, in connection with the decline in value of our NYX shares, as well as by a $5.1 million pre-tax loss on early extinguishment of our senior indebtedness in the second quarter of 2008 and a non-cash pre-tax impairment charge related to the Company s goodwill and stock listing rights of $164.1 million and $335.3 million, respectively, in the second quarter of 2007. Excluding these losses in each quarter, our pro-forma net income for the second quarter of 2008 was $1.7 million, or $0.03 per share, compared to pro-forma net income for the second quarter of 2007 of $6.6 million, or $0.11 per share.

Excluding the unrealized losses on our NYX shares in the first half of 2008 and 2007, the tax losses on early extinguishment of our debt in 2008 and the non-cash pre-tax impairment charges in the second quarter of 2008, our pro-forma net income for the first six months of 2008 was $9.5 million, or $0.15 per diluted share, compared to pro-forma net income of $3.4 million, or $0.06 per share, for the first six months of 2007.

As noted in our analysis of cash flows, we generated positive cash of $25.0 million from operating income, the majority of which was derived from our Specialist and Market-Making segment. Our cash equities specialist business over the first six months of 2008 yielded positive results and continue to generate cash. In addition, our specialist and market-making operations outside of our traditional cash equities business also continue to generate strong earnings and continue to represent an increasing percentage of our total company revenues. We continue to believe that new trading venues will grow as the securities markets globalize and converge, and that global securities markets will increasingly interact with each other. As such, our liquidity-providing activities outside the NYSE floor operations are increasingly becoming a major component of our specialist and market-making operations, especially as we continue to rely upon and further develop electronic trading strategies to interact with the global electronic marketplace.

We are also continuing to build our Institutional Brokerage business. Although our Institutional Brokerage segment showed a loss in the second quarter of 2008, we believe much of these results are mainly attributable to start-up costs and our initial facilitation trading results. We have made key hires of sales and position traders that we believe are important to transform our Institutional Brokerage business into a more rounded operation that specializes in a range of high-touch services.

We are actively taking steps to reduce our operating expenses. The largest of these expenses is the interest on our public debt, which was approximately $47.6 million per year until 2008. Following the repurchases and retirement of $249.9 million of our outstanding in the first half of 2008, only $209.9 million of our 11% Senior Notes due 2012 remain outstanding, with a remaining annual interest expense of approximately $23.1 million versus $47.6 million in 2007. Historically, the operating expense related to our outstanding debt has been the negative carry on our debt, which is the interest we pay on our outstanding indebtedness, less the interest income we receive as a result of having that cash on-hand. Prior to the repurchases described above, our negative carry would have been $10.2 million per quarter, based on current short-term interest rates. Following our 2008 repurchases, the negative carry will be reduced to approximately $4.7 million per quarter, based on current short-term interest rates, for the second half of 2008. We also believe that we will have flexibility on our negative carry going forward, as we manage our balance sheet. The repurchase of our public debt also has enabled us to improve our consolidated fixed charge coverage ratio to 3.2:1 at June 30, 2008, which evidences our growing flexibility to strategically utilize our capital by considering a broader spectrum of opportunities.

As we have explained in the past, our ownership of 3,126,903 shares of NYSE Euronext Inc. common stock (the NYX shares) resulted from the exchange of our NYSE memberships, or seats in connection with the NYSE s mergers with Archipelago Holdings and Euronext. Before the exchange of our NYSE seats into the NYX shares, we believed that our seat ownership was integral to our position in the industry. Though the value of our NYX shares has been volatile over the past two years, the value of our seats prior to their exchange were volatile as well. Our management will remain flexible regarding our continued ownership of NYX shares, and we currently use a majority of the unrestricted NYX shares, rather than cash, to satisfy our regulatory capital requirements, thereby enabling us to more efficiently deploy our cash working capital. We are also mindful that our ownership of exchange seats and exchange-related securities, such as our NYX shares, have been beneficial to our company over time.

Our balance sheet is strong and very liquid. We believe we have ample capital to maintain and grow our business. We are continuing to concentrate on building our business in London and Hong Kong, in which we see trading opportunities in those markets in ETFs and other derivative products.

The NYSE has filed a proposed rule with the SEC to further change its market model, changing the role of specialists to designated market makers who will still provide liquidity, but without some of the negative and affirmative obligations that could, at times, adversely affect our profitability. The purported rule changes would change the timing of when the designated market-maker can see orders, but would provide us more flexibility in trading for our own account. We believe that some of these possible market structure changes would allow us to interact in the market more efficiently and also allow us to benefit from organizational changes and integration, because some of these changes presumably would remove the informational barriers that have caused us to maintain our specialist and market-making businesses as separate broker-dealers. We currently are unable to project if or when any of these market structure changes, or other informational barrier changes will be formally proposed or passed, if at all.

The restructuring of certain of our specialist and market-making subsidiaries has allowed us to develop those operations across various domestic and international exchanges and marketplaces. The organizational structure of our Specialist and Market-Making segment, therefore, is intended to enable us to better allocate and deploy our capital, workforce and technology across our operations in order to more efficiently seek out opportunities as they arise.

Regulation G Reconciliation of Non-GAAP Financial Measures

In evaluating our financial performance as described above in Executive Overview, management reviews operating results from operations, which excludes non-operating charges. Pro-forma earnings per share is a non-GAAP (generally accepted accounting principles) performance measure, but we believe that it is useful to assist investors in gaining an understanding of the trends and operating results for our core business. In this report, our pro-forma operating results in the periods presented exclude certain extraordinary and/or non-recurring items, such as, for example, the unrecognized loss on the Company s NYX shares and the costs associated with the early retirement of our Company s outstanding senior indebtedness, neither of which are, in management s belief, reflective of the Company s day-to-day operating performance or cash generation, and nether of which affect the Company s actual income or cash. Pro-forma earnings per share should be viewed in addition to, and not in lieu of our reported results under U.S. GAAP.

The following is a reconciliation of U.S. GAAP results to pro-forma results for the periods presented:

	Three Months Ended June 30,					
	2008			2007		
	Amounts as reported	(1) (2) Adjustments	Pro forma amounts	Amounts as reported	(1) Adjustments	Pro forma amounts
Revenues, net of interest expense	$ 7,790	$ 33,206(1)	$ 40,996	$ (1,182)	$ 54,618(1)	$ 53,436
Total expenses	42,702	(5,119)(2)	37,583	549,304	(499,364)(3)	49,940
(Loss) income before (benefit) provision for income taxes	(34,912)	38,325	3,413	(550,486)	553,982	3,496
(Benefit) provision for income taxes	(13,571)	15,330	1,759	(181,542)	178,425	(3,117)
Net (loss) income applicable to common stockholders	$ (21,341)	$ 22,995	$ 1,654	$ (368,944)	$ 375,557	$ 6,613
Basic per share	$ (0.34)	$ 0.37	$ 0.03	$ (6.00)	$ 6.11	$ 0.11
Diluted per share	$ (0.34)	$ 0.37	$ 0.03	$ (6.00)	$ 6.11	$ 0.11

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	Six Months Ended June 30, 2008 Amounts as reported	2008 (1) (2) Adjustments	2008 Pro forma amounts	2007 Amounts as reported	2007 (1) Adjustments	2007 Pro forma amounts
Revenues, net of interest expense	$ (14,903)	$ 112,452(1)	$ 97,549	$ 36,700	$ 58,787(1)	$ 95,487
Total expenses	91,441	(6,005)(2)	85,436	596,180	(499,364)(3)	96,816
(Loss) income before (benefit) provision for income taxes	(106,344)	118,457	12,113	(559,480)	558,151	(1,329)
(Benefit) provision for income taxes	(44,766)	47,383	2,617	(184,981)	180,239	(4,742)
Net (loss) income applicable to common stockholders	$ (61,578)	$ 71,074	$ 9,496	$ (374,499)	$ 377,912	$ 3,413
Basic per share	$ (0.99)	$ 1.14	$ 0.15	$ (6.10)	$ 6.16	$ 0.06
Diluted per share	$ (0.99)	$ 1.14	$ 0.15	$ (6.10)	$ 6.16	$ 0.06

(1) Revenue adjustment reflects loss in each accounting period, based on the change in fair market value of the Company s restricted and unrestricted NYX shares at the end of each such period versus the beginning of such period.

(2) Expense adjustment reflects costs associated with early extinguishment of debt in accounting period.

(3) Relates to the write-down of the carrying value of the Company s goodwill and stock listing rights to reflect the results of the Company s impairment evaluation under SFAS No s 142 and 144.

New Accounting Developments

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value and enhances disclosures about fair value measurements required under other accounting pronouncements, but does not change existing guidance as to whether or not an instrument is carried at fair value. SFAS 157 nullifies the guidance in EITF 02-3 which precluded the recognition of a trading profit at the inception of a derivative contract, unless the fair value of such derivative is obtained from a quoted market price, or other valuation technique incorporating observable market data. SFAS 157 also precludes the use of a liquidity or block discount, when measuring instruments traded in an active market at fair value. SFAS 157 requires that costs related to acquiring financial instruments carried at fair value should not be capitalized, but rather should be expensed as incurred. SFAS 157 also clarifies that an issuer s credit standing should be considered when measuring liabilities at fair value. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and was adopted by the Company as of January 1, 2008. SFAS 157 must be applied prospectively, except that the provisions related to block discounts and the guidance in EITF 02-3 are to be applied as a one time cumulative effect adjustment to opening retained earnings in the first interim period for the fiscal year in which SFAS 157 is initially applied. The adoption of SFAS 157 resulted in no cumulative change to the retained deficit. Please refer to Footnote 11 of our Condensed Consolidated Financial Statements for additional information and disclosure.

In February of 2008, the FASB issued FSP FAS 157-2 which delays the effective date of Statement 157 to all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in an entity s financial statements on a recurring basis (at least annually to fiscal years beginning after November 15, 2008. Such items include a) nonfinancial assets acquired and liabilities assumed in purchase business combinations and b) intangible assets and goodwill.

Accounting for Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159, Accounting for Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. We currently report the majority of our financial assets and liabilities at fair value in compliance with industry guidelines for brokers and dealers in securities. The company elected not to apply the fair value option for any applicable assets or liabilities.

Derivative Instruments and Hedging Activities

In April 2007, the FASB issued a Staff Position (FSP) FIN No. 39-1, Amendment of FASB Interpretation No. 39. FSP FIN No. 39-1 defines right of setoff and specifies what conditions must be met for a derivative contract to qualify for this right of setoff. It also addresses the applicability of a right of setoff to derivative instruments and clarifies the circumstances in which it is appropriate to offset amounts recognized for those instruments in the statement of financial position. In addition, this FSP permits offsetting of fair value amounts recognized for multiple derivative instruments executed with the same counterparty under a master netting arrangement and fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) arising from the same master netting arrangement as the derivative instruments. The provisions of this FSP are consistent with our current accounting practice. This interpretation is effective for fiscal years beginning after November 15, 2007, with early application permitted. The adoption of FSP FIN No. 39-1 did not have a material impact on our consolidated financial statements.

In March 2008, the FASB issued FASB Statement No 161, Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement 133. SFAS 161 amends and expands the disclosures required by SFAS 133 so that they provide an enhanced understanding of 1) how and why an entity uses derivative instruments, 2) how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and 3) how derivative instruments affect an entity s financial position, financial performance, and cash flows. SFAS 161 is effective for both interim and annual reporting periods beginning after November 15, 2008, with early adoption encouraged. The Company is not subject to SFAS 133 at this time. Since this amendment relates solely to disclosures related to SFAS 133, there is no potential effect on the financial position of the Company.

The Hierarchy of Generally Accepted Accounting Principles

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles (SFAS 162). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (GAAP) in the United States (the GAAP hierarchy). SFAS 162 is effective 60 days following the SEC s approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles.* The Adoption of SFAS 162 will not have a material effect on the Consolidated Financial Statements.

Critical Accounting Estimates

Goodwill and Other Intangible Assets

We determine the fair value of each of our reporting units and the fair value of each reporting unit s goodwill under the provisions of SFAS No. 142, Goodwill and Other Intangible Assets. In determining fair value, we use standard analytical approaches to business enterprise valuation (BEV), such as the market comparable approach and the income approach. The market comparable approach is based on comparisons of the subject company to similar companies engaged in an actual merger or acquisition or to public companies whose stocks are actively traded. As part of this process, multiples of value relative to financial variables, such as earnings or stockholders equity, are developed and applied to the appropriate financial variables of the subject company to indicate its value. The income approach involves estimating the present value of the subject company s future cash flows by using projections of the cash flows that the business is expected to generate, and discounting these cash flows at a given rate of return. Each of these BEV methodologies requires the use of management estimates and assumptions. For example, under the market comparable approach, we assigned a certain control premium to the public market price of our common stock as of the valuation date in estimating the fair value of our specialist reporting unit. Similarly, under the income approach, we assumed certain growth rates for our revenues, expenses, earnings before interest, income taxes, depreciation and amortization, returns on working capital, returns on other assets and capital expenditures, among others. We also assumed certain discount rates and certain terminal growth rates in our calculations. Given the subjectivity involved in selecting which BEV approach to use and in determining the input variables for use in our analyses, it is possible that a different valuation model and the selection of different input variables could produce a materially different estimate of the fair value of our goodwill.

We review the reasonableness of the carrying value of our goodwill annually as of December 31, unless an event or change in circumstances requires an interim reassessment of impairment. During the six months ended June 30, 2008, there were no changes in circumstances that necessitated goodwill impairment testing prior to our required year-end test date. We cannot provide assurance that a change in circumstances requiring an interim assessment or future goodwill impairment testing will not result in impairment charges in subsequent periods.

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Another of our intangible assets, as defined under SFAS No. 142, is our trade name. We determine the fair value of our trade name by applying the income approach using the royalty savings methodology. This method assumes that the trade name has value to the extent we are relieved of the obligation to pay royalties for the benefits received from it. Application of this methodology requires estimating an appropriate royalty rate, which is typically expressed as a percentage of revenue. Estimating an appropriate royalty rate includes reviewing evidence from comparable licensing agreements and considering qualitative factors affecting the trade name. Given the subjectivity involved in selecting which BEV approach to use and in determining the input variables for use in our analyses, it is possible that a different valuation model and the selection of different input variables could produce a materially different estimate of fair value of our trade name.

We review the reasonableness of the carrying amount of our trade name on an annual basis in conjunction with our goodwill impairment assessment. During the six months ended June 30, 2008, there were no changes in circumstances that necessitated trade name impairment testing prior to our required year-end test date. We cannot provide assurance that a change in circumstances requiring an interim assessment or future trade name and stock listing rights impairment testing will not result in impairment charges in subsequent periods.

Financial Instruments

Financial instruments owned, at fair value and Financial instruments sold, but not yet purchased, at fair value are reported in our consolidated financial statements, at fair value, on a recurring basis. Pursuant to SFAS No. 157, the fair value of a financial instrument is defined as the amount that would be received to sell an asset or paid to transfer a liability, or the exit price, in an orderly transaction between market participants at the measurement date.

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards, or SFAS, No. 157 Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 outlines a fair value hierarchy that is used to determine the value to be reported. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets and liabilities (which are considered level 1 measurements) and the lowest priority to unobservable inputs (which are considered level 3 measurements). The three levels of the fair value hierarchy under SFAS No. 157 are as follows:

Level 1	Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
Level 2	Quoted prices for similar instruments in active markets, quoted prices in markets that are not active or financial instruments for which all significant inputs are observable, either directly or indirectly;
Level 3	Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions would reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Such valuation techniques include the use of option pricing models, discounted cash flow models and similar techniques.

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Non-Marketable Securities

The measurement of non-marketable investments is a critical accounting estimate. Investments in non-marketable securities consist of investments in equity securities of private companies and limited liability company interests and are included in other assets in the condensed consolidated statements of cash flows. Certain investments in non-marketable securities are initially carried at cost, unless there are third-party transactions evidencing a change in value. For certain other investments in non-marketable investments we adjust their carrying value by applying the equity method of accounting pursuant to APB 18. Under the equity method the investor recognizes its share of the earnings and losses of an investee in the periods for which they are reported by the investee in its financial statements. The assets included in this section represent limited liability companies that are service providers and whose value is affected by nonfinancial components. In addition, if and when available, management considers other relevant factors relating to non-marketable investments in estimating their value, such as the financial performance of the entity, its cash flow forecasts, trends within that entity s industry and any specific rights associated with our investment such as conversion features among others.

Non-marketable investments are tested for potential impairment whenever events or changes in circumstances suggest that such investment s carrying value may be impaired.

Use of Estimates

The use of generally accepted accounting principles requires management to make certain estimates. In addition to the estimates we make in connection with fair value measurements and the accounting for goodwill and identifiable intangible assets, the use of estimates is also important in determining provisions for potential losses that may arise from litigation, regulatory proceedings and tax audits.

We estimate and provide for potential losses that may arise out of litigation, regulatory proceedings and tax audits to the extent that such losses are probable and can be estimated, in accordance with SFAS No. 5, Accounting for Contingencies and FIN 48, Accounting for Uncertainty in Income Taxes . Significant judgment is required in making these estimates and our final liabilities may ultimately be materially different. Our total liability in respect of litigation and regulatory proceedings is determined on a case-by-case basis and represents an estimate of probable losses after considering, among other factors, the progress of each case or proceeding, our experience and the experience of others in similar cases or proceedings, and the opinions and views of legal counsel. Given the inherent difficulty of predicting the outcome of our litigation and regulatory matters, particularly in cases or proceedings in which substantial or indeterminate damages or fines are sought, we cannot estimate losses or ranges of losses for cases or proceedings where there is only a reasonable possibility that a loss may be incurred. See Legal Proceedings in Part II, Item 1 of this Quarterly Report on Form 10-Q for information on our judicial, regulatory and arbitration proceedings.

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Completed Purchases of Outstanding Indebtedness

On May 23, 2008, we completed the optional redemption of all of our remaining outstanding 9 1/2% Senior Notes due 2009, in the aggregate principal amount of $169.1 million, at a redemption price of 102.375%, plus accrued and unpaid interest thereon. The repurchase will result in the reduction of our annual interest expense by approximately $16.1 million. Prior to the optional redemption, in January and February 2008, we also purchased an aggregate of $30.7 million aggregate principal amount of our then-outstanding 9 1/2% Senior Notes due 2009 and $50.1 million aggregate principal amount of our outstanding 11% Senior Notes due 2012. The purchase of the debt resulted in an annual interest savings of approximately $8.4 million. Following the redemption and the above-described January and February 2008 purchases, approximately $209.9 million of our 11% Senior Notes due 2012 remain outstanding under the indenture. Our management and board of directors continue to monitor the opportunities to purchase our remaining outstanding 11% Senior Notes due 2012 at or below the call price.

On June 3, 2008, we extinguished all of our remaining outstanding subordinated debt in the amount of $3.0 million, plus accrued and unpaid interest. Therefore, we no longer have any subordinated debt outstanding as of June 30, 2008.

Results of Operations

Specialist and Market-Making Segment Operating Results

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		Three Months 2008 vs. 2007 Percentage Change	Six Months 2008 vs. 2007 Percentage Change
(000 s omitted)	**2008**	**2007**	**2008**	**2007**		
Revenues:						
Net gain on principal transactions	$ 44,671	$ 63,754	$ 104,154	$ 112,649	(29.9)%	(7.5)%
Commissions and other fees	3,839	6,145	9,108	12,184	(37.5)	(25.2)
Net loss on investments	(31,308)	(49,267)	(106,472)	(53,972)	(36.5)	97.3
Interest income	15,966	64,323	43,877	125,947	(75.2)	(65.2)
Other	1,181	1,026	1,148	1,061	15.1	8.2
Total segment revenues	34,349	85,981	51,814	197,869	(60.1)	(73.8)
Fixed interest on debt	58	123	176	(23)	(52.8)	(865.2)
Inventory financing	20,805	78,949	51,613	149,301	(73.6)	(65.4)
Revenues, net of interest expense	13,486	6,909	25	48,591	95.2	(99.9)
Goodwill impairment		164,100		164,100	(100.0)	(100.0)
Specialist stock list impairment		335,264		335,264	(100.0)	(100.0)
Operating expenses	28,846	39,754	67,722	75,543	(27.4)	(10.4)
Loss before taxes	$ (15,360)	$ (532,209)	$ (67,697)	$ (526,316)	(97.1)%	(87.1)%

Revenues from our Specialist and Market-Making segment consist primarily of net gains and losses resulting from our specialist activities in stocks and options, market-making activities in ETFs, options and futures, the net gains and losses resulting from trading of foreign currencies, futures and equities underlying the rights, ETFs and options for which we act as specialist, and accrued dividends receivable or payable on our equity positions.

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Additionally, a significant component of the overall trading revenues is revenue generated by our Specialist and Market-Making segment consisting primarily of interest earned in securities lending transactions and inventory financing in connection with our trading in options, futures and ETFs which is aggregated with interest income and interest expense, respectively. These revenues are primarily affected by changes in share volume traded and fluctuations in prices of stocks, rights, options, ETFs and futures in which we are the specialist or in which we make a market.

Net gain on principal transactions represents trading gains net of trading losses and certain exchange imposed trading activity fees, where applicable, and are earned by us when we act as principal buying and selling our specialist stocks, rights, options, ETFs and futures.

Commissions and other fees revenue generated by our Specialist and Market-Making segment consists primarily of fees earned by our cash equity specialists for providing liquidity on the NYSE and, through July 9, 2007, for executing limit orders on the AMEX. The other fees in this line item are related to a specialist liquidity provision payment (the LPP) program implemented on September 1, 2007, which varies month-to-month depending on our principal trading activities on the NYSE and an interim specialist allocation pool payment to us in the amount of $2.1 million per month by the NYSE for the period from December 2006 through August 2007. The new LPP system involves a two tier fee structure based on (1) the firms proportional share of 100% of the consolidated tape revenue earned by the NYSE for quoting at the national best bid and offer, and (2) a subjective allocation from the NYSE of the LPP pool which consists of 25% of the NYSE s listed stock transaction revenue on matched volume. This monthly payment, in the aggregate, has been approximately $1.5 million for each of the first six months of 2008.

Net loss on investments reflects the aggregate losses generated from our investments in restricted and unrestricted NYX shares and other investments not derived specifically from specialist and market-making activities.

Other revenue at our Specialist and Market-Making segment consists primarily of miscellaneous receipts not derived specifically from specialist and market-making activities.

Interest expense attributable to our Specialist and Market-Making segment is the result of inventory financing costs relating to positions taken in connection with our options, futures and ETFs specialist and market-making operations and interest on subordinated indebtedness that has been approved by the NYSE for inclusion in the net capital of LaBranche & Co. LLC.

Generally, an increase in the average daily share volume on the NYSE, an increase in volatility (as measured by the average closing price of the CBOE s Volatility Index®, or the VIX), an increase in the dollar value and share volume of our principal shares or a decrease in program trading enables us to increase our level of principal participation and thus our ability to realize net gain on principal transactions. While we monitor these metrics each period, they are not the sole indicators or factors in any given period that determine our level of revenues, profitability or overall performance. Other factors, such as extreme price movements, unanticipated company news and events and other uncertainties may influence our financial performance either positively or negatively.

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Three Months Ended June 30, 2008 versus June 30, 2007

The decrease in our net gain on principal transactions was attributable to a decline in our option and ETF specialist and market-making principal trading revenue for the three months ended June 30, 2008 as compared to the same period in 2007. This decrease in principal trading revenues was directly related to challenging trading conditions.

Commission and other fees revenue during the second quarter of 2008 decreased as the result of the NYSE rule change in December 2006 implementing the rebate program for certain specialist limit order transactions. In 2007, we received a specialist allocation pool payment in the amount of $2.1 million per month from the NYSE, versus the average monthly commission in the second quarter of 2008 of approximately $1.3 million.

Net loss on investments is mainly the result of the unrealized loss on our NYX shares of $33.2 million, net of a valuation allowance for transfer restrictions, which represents the decline in the fair value of the NYX shares since March 31, 2008.

Interest income decreased primarily due to decreased trade finance interest income from stock borrow activity and lower interest rates during the second quarter of 2008 as compared to the second quarter of 2007.

Other revenue is mainly comprised of our receipt of the second quarterly dividend declared in June 2008 by the NYSE Euronext with respect to its common stock.

Interest expense decreased primarily as a result of decreased inventory financing costs relating to a decrease in our positions and lower interest rates relating to inventory financing costs such as margin interest.

Six Months Ended June 30, 2008 versus June 30, 2007

The decrease in our net gain on principal transactions reflects a decline in our option and ETF specialist principal trading revenue for the six months ended June 30, 2008 as compared to the same period in 2007. This decrease in principal trading revenues was directly related to challenging trading conditions.

Commission and other fees revenue during the first half of 2008 decreased as the result of the NYSE rule change in December 2006 implementing the rebate program for certain specialist limit order transactions. In 2007, we received a specialist allocation pool payment in the amount of $2.1 million per month from the NYSE, versus the average monthly commission in the first half of 2008 of approximately $1.5 million.

Net (loss) gain on investments is directly related to a decrease in the share price of the NYX stock during the second half 2008.

Stock borrow interest decreased mainly due to the decreased trading inventories for our non-cash equities specialist and market-making activities.

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Other revenue is mainly comprised of gains on non trading investments and our receipt of the NYSE quarterly dividend declared in June 2007.

For a discussion of operating expenses, see Our Operating Expenses below.

Institutional Brokerage Segment Operating Results

(000 s omitted)	For the Three Months Ended June 30, 2008	For the Three Months Ended June 30, 2007	For the Six Months Ended June 30, 2008	For the Six Months Ended June 30, 2007	Three Months 2008 vs. 2007 Percentage Change	Six Months 2008 vs. 2007 Percentage Change
Revenues:						
Net gain on principal transactions	$ 246	$ 260	$ 944	$ 284	(5.4)%	232.4%
Commissions	6,111	5,782	10,851	12,504	5.7	(13.2)
Net loss on investments	(4,905)	(4,201)	(11,137)	(4,522)	16.8	146.3
Interest income	161	744	221	1,854	(78.4)	(88.1)
Other	97	32	191	62	203.1	208.1
Total segment revenues	1,710	2,617	1,070	10,182	(34.7)	(89.5)
Inventory financing	2	322	7	900	(99.4)	(99.2)
Revenues, net of interest expense	1,708	2,295	1,063	9,282	(25.6)	(88.5)
Operating expenses	6,367	7,629	12,232	15,892	(16.5)	(23.0)
Loss before taxes	$ (4,659)	$ (5,334)	$ (11,169)	$ (6,610)	(12.7)%	69.0%

Our Institutional Brokerage segment s commission revenue for 2007 includes fees charged to customers for execution, clearance (through June 8, 2007) and direct-access floor brokerage activities.

Net loss on investments reflects the aggregated losses generated from our investments in restricted and unrestricted NYX shares and other investments not derived specifically from institutional brokerage activities.

Three Months Ended June 30, 2008 versus June 30, 2007

Commissions revenue increased primarily as a result of an increase of our institutional execution group s order-flow and trading volume.

Net loss on investments is directly related to a decrease in the share price of shares of NYX stock during the second quarter of 2008 as well as proprietary trading losses.

Effective June 8, 2007, LFS exited the clearing business. Therefore, there were no more stock borrow/loan transactions generating interest income/expense in 2008.

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Six Months Ended June 30, 2008 versus June 30, 2007

Net gain on principal transactions increased as a result of LFS trading and market making activity in OTC Bulletin Board and Pink Sheet securities containing six months of activity in 2008 compared to two months in 2007.

Commissions revenue decreased primarily as a result of a reduction in the number of our direct access customers. This decrease was partially offset by our growing institutional execution business commencing in May 2008 and the increase in commissions order flow in connection with this growing business.

Net loss on investments is directly related to a decrease in the share price of shares of NYX stock during the first six months of 2008 as well as proprietary trading losses.

Effective June 8, 2007, LFS exited the clearing business. Therefore, there were no more stock borrow/loan transactions generating interest income/expense in 2008.

For a discussion of operating expenses, see Our Operating Expenses below.

Other Segment Operating Results

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		Three Months 2008 vs. 2007 Percentage Change	Six Months 2008 vs. 2007 Percentage Change
(000 s omitted)	2008	2007	2008	2007		
Interest	$ 1,342	$ 2,282	$ 3,296	$ 4,205	(41.2)%	(21.6)%
Net loss on investments	(131)	(204)	(159)	(34)	(35.8)	367.6
Other	(168)	100	64	159	(268.0)	(59.7)
Total segment revenues	1,043	2,178	3,201	4,330	(52.1)	(26.1)
Fixed interest on debt	8,447	12,564	19,192	25,503	(32.8)	(24.7)
Revenues, net of interest expense	(7,404)	(10,386)	(15,991)	(21,173)	(28.7)	(24.5)
Early extinguishment of debt	5,119	&#1style="font-size:1.0pt;">	17,902			
Earnings per common share, basic	$ .23	$ .54	$ .53	$ .69		
Earnings per common share, diluted	$ .23	$ .54	$ .53	$ .69		
Net income attributable to One Liberty Properties, Inc. common stockholders,	$ 4,517	$ 9,972	$ 10,368	$ 12,837		

net of
non-controlling
interests

(a) Represents an allocation of distributed earnings to unvested restricted stock which, as participating securities, are entitled to receive dividends.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 4 Real Estate Acquisitions

The following chart details the Company s acquisitions of real estate during the six months ended June 30, 2018 (amounts in thousands):

Description of Property	**Date Acquired**	**Contract Purchase Price**	**Terms of Payment**	**Capitalized Third Party Real Estate Acquisition Costs**
Campania International/U.S. Tape industrial facility, Pennsburg, PA	March 28, 2018	$ 12,675	All cash	$ 227
[redacted]				
Plymouth, MN	June 7, 2018	5,500	All cash	50
Totals		$ 18,175		$ 277

The Company determined that with respect to each of these acquisitions, the gross assets acquired are concentrated in a single identifiable asset. Therefore, these transactions do not meet the definition of a business and are accounted for as asset acquisitions. As such, direct transaction costs associated with these asset acquisitions have been capitalized to real estate assets and depreciated over their respective useful lives.

The following chart details the allocation of the purchase price for the Company s acquisitions of real estate during the six months ended June 30, 2018 (amounts in thousands):

Description of Property	**Land**	**Building**	**Building Improvements**	**Total**
Campania International/U.S. Tape industrial facility, Pennsburg, PA	$ 1,776	$ 10,399	$ 727	$ 12,902
[redacted]				
Plymouth, MN	1,121	4,306	123	5,550
Totals	$ 2,897	$ 14,705	$ 850	$ 18,452

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 5 Sale of Property

On January 1, 2018, the Company adopted ASU No. 2017-05, *Other Income Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets*, using the modified retrospective transition method. As leasing is the Company s primary activity, the Company determined that its sales of real estate, which are nonfinancial assets, are sold to noncustomers and fall within the scope of ASC 610-20. The Company re-assessed and determined there were no open contracts or partial sales and as such, the adoption of this ASU did not (i) result in a cumulative adjustment as of January 1, 2018, and (ii) have any impact on the Company s consolidated financial statements.

On January 30, 2018, the Company sold a property located in Fort Bend, Texas, owned by a consolidated joint venture in which the Company held an 85% interest, for $8,958,000, net of closing costs, and paid off the $4,410,000 mortgage. This property accounted for 1.1% of the Company s rental income, net, during each of the three and six months ended June 30, 2017. The sale resulted in a gain of $2,408,000 which was recorded as Gain on sale of real estate, net, in the consolidated statement of income for the six months ended June 30, 2018. The non-controlling interest s share of the gain was $776,000. The Company determined it would recognize the full gain on the sale of the Fort Bend, Texas property in accordance with ASC 610-20 as the Company has no (i) controlling financial interest in the property and (ii) continuing interest or obligation with respect to the property sold.

Note 6 Variable Interest Entities, Contingent Liabilities and Consolidated Joint Ventures

Variable Interest Entities Ground Leases

The Company determined that with respect to the properties identified in the table below, it has a variable interest through its ground leases and the three owner/operators (which are affiliated with one another) are VIEs because their equity investment at risk is insufficient to finance its activities without additional subordinated financial support. The Company further determined that it is not the primary beneficiary of any of these VIEs because the Company has shared power over certain activities that most significantly impact the owner/operator s economic performance (*i.e.*, shared rights on the sale of the property) and therefore, does not consolidate these VIEs for financial statement purposes. Accordingly, the Company accounts for these investments as land and the revenues from the ground leases as Rental income, net. Such rental income amounted to $941,000 and $1,947,000 for the three and six months ended June 30, 2018, respectively, and $917,000 and $1,804,000 for the three and six months ended June 30, 2017, respectively.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 6 Variable Interest Entities, Contingent Liabilities and Consolidated Joint Ventures (Continued)

The following chart details the VIEs through the Company s ground leases and the aggregate carrying amount and maximum exposure to loss as of June 30, 2018 (dollars in thousands):

Description of Property(a)	**Date Acquired**	**Land Contract Purchase Price**	**# Units in Apartment Complex**	**Owner/ Operator Mortgage from Third Party(b)**	**Type of Exposure**	**Carrying Amount and Maximum Exposure to Loss**
The Meadows Apartments, Lakemoor, Illinois	March 24, 2015	$ 9,300	496	$ 51,331(c)	Land	$ 9,592
The Briarbrook Village Apartments, Wheaton, Illinois	August 2, 2016	10,530	342	39,411	Land	10,536
The Vue Apartments, Beachwood, Ohio	August 16, 2016	13,896	348	67,444	Land	13,901
Totals		$ 33,726	1,186	$ 158,186		$ 34,029

(a) Simultaneously with each purchase, the Company entered into a triple net ground lease with affiliates of Strategic Properties of North America, the owner/operators of these properties.

(b) Simultaneously with the closing of each acquisition, the owner/operator obtained a mortgage from a third party which, together with the Company s purchase of the land, provided substantially all of the funds to acquire the complex. The Company provided its land as collateral for the respective owner/operator s mortgage loans; accordingly, each land position is subordinated to the applicable mortgage. No other financial support has been provided by the Company to the owner/operator.

(c) In November 2017, the owner/operator closed on a $7,556 supplemental mortgage (the original mortgage was for $43,824). In connection therewith, the Company agreed to subordinate its fee interest to this second mortgage in exchange for a payment by the owner/operator to the Company of $5,906 as a fixed rent payment which was recorded as deferred income and will be included in rental income over the term of the lease. The fixed rent payment balance was $5,762 and $5,870 at June 30, 2018 and December 31, 2017, respectively, and is included in Accrued expenses and other liabilities on the consolidated balance sheets.

Pursuant to the terms of the ground lease for the Wheaton, Illinois property, the owner/operator is obligated to make certain unit renovations as and when units become vacant. Cash reserves to cover such renovation work, received by the Company in conjunction with the purchase of the property, are disbursed when the unit renovations are completed. The related cash reserve balance for this property was $416,000 and $443,000 at June 30, 2018 and December 31, 2017, respectively, and is classified as Restricted cash on the consolidated balance sheets.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 6 Variable Interest Entities, Contingent Liabilities and Consolidated Joint Ventures (Continued)

Variable Interest Entity Consolidated Joint Ventures

With respect to the five consolidated joint ventures in which the Company holds between a 90% to 95% interest, the Company has determined such ventures are VIEs because the non-controlling interests do not hold substantive kick-out or participating rights.

In each of these consolidated joint ventures, the Company has determined it is the primary beneficiary of the VIE as it has the power to direct the activities that most significantly impact each joint venture s performance including management, approval of expenditures, and the obligation to absorb the losses or rights to receive benefits. Accordingly, the Company consolidates the operations of these joint ventures for financial statement purposes. The joint ventures creditors do not have recourse to the assets of the Company other than those held by these joint ventures.

The following is a summary of the consolidated VIEs carrying amounts and classification in the Company s consolidated balance sheets, none of which are restricted (amounts in thousands):

	June 30, 2018	December 31, 2017 (a)
Land	14,722	$ 17,844
Buildings and improvements, net of accumulated depreciation of $3,615 and $3,811, respectively	28,145	31,789
Cash	839	1,145
Unbilled rent receivable	1,166	1,011
Unamortized intangible lease assets, net	975	1,241
Escrow, deposits and other assets and receivables	687	948
Mortgages payable, net of unamortized deferred financing costs of $423 and $442, respectively	27,411	32,252
Accrued expenses and other liabilities	538	870
Unamortized intangible lease liabilities, net	1,848	2,015
Accumulated other comprehensive income (loss)	90	(1)
Non-controlling interests in consolidated joint ventures	1,422	1,742

(a) Includes a consolidated joint venture, in which the Company held an 85% interest, located in Fort Bend, Texas which was sold in January 2018 (see Note 5).

At June 30, 2018 and December 31, 2017, MCB Real Estate, LLC and its affiliates (MCB) are the Company s joint venture partner in four consolidated joint ventures in which the Company has aggregate equity investments of approximately $9,734,000 and $9,705,000, respectively.

Distributions to each joint venture partner are determined pursuant to the applicable operating agreement and may not be pro rata to the equity interest each partner has in the applicable venture.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 7 Investment in Unconsolidated Joint Ventures

On April 5, 2018, an unconsolidated joint venture sold its building and a portion of its land, located in Savannah, Georgia for $2,600,000, net of closing costs. The Company s 50% share of the gain from this sale was $71,000, which is included in Equity in earnings from sale of unconsolidated joint venture property on the consolidated statements of income for the three and six months ended June 30, 2018. The unconsolidated joint venture retained approximately five acres of land at this property.

At June 30, 2018 and December 31, 2017, the Company s five unconsolidated joint ventures each owned and operated one property. The Company s equity investment in such unconsolidated joint ventures at such dates totaled $11,214,000 and $10,723,000, respectively. In addition to the equity in earnings from the sale of property of $71,000 in 2018, the Company recorded equity in earnings of $348,000 and $543,000 for the three and six months ended June 30, 2018, respectively, and $206,000 and $451,000 for the three and six months ended June 30, 2017, respectively. Included in equity in earnings from unconsolidated joint ventures for the three and six months ended June 30, 2018 is $110,000 related to the discontinuance of hedge accounting on a mortgage swap related to an unconsolidated joint venture property, located in Milwaukee, Wisconsin, that was sold in July 2018 (see below and Note 14).

At June 30, 2018, MCB is the Company s joint venture partner in one of these unconsolidated joint ventures in which the Company has an equity investment of $8,408,000.

On July 31, 2018, an unconsolidated joint venture sold its property located in Milwaukee, Wisconsin for approximately $12,800,000, net of closing costs and paid off the related $6,970,000 mortgage. The Company anticipates its 50% share of the gain from this sale will be approximately $2,000,000, which will be recognized in the three months ending September 30, 2018.

Note 8 Allowance for Doubtful Accounts

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of a tenant to make required rent and other payments. If the financial condition of a specific tenant were to deteriorate, adversely impacting its ability to make payments, allowances may be required. At June 30, 2018 and December 31, 2017, there was no balance in allowance for doubtful accounts.

The Company records bad debt expense as a reduction of rental income and/or tenant reimbursements. There was no bad debt expense in the three and six months ended June 30, 2018. During the three and six months ended June 30, 2017, the Company recorded bad debt expense of

$15,000 and $310,000, respectively, related to tenant reimbursements due from former tenants that filed for Chapter 11 bankruptcy protection. In connection with these tenants, the Company wrote-off (i) $362,000 of unbilled straight-line rent receivable and $67,000 of unamortized intangible lease assets as a reduction to rental income and (ii) $884,000 of tenant origination costs as an increase to depreciation expense.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 9 Debt Obligations

Mortgages Payable

The following table details the Mortgages payable, net, balances per the consolidated balance sheets (amounts in thousands):

	June 30, 2018	December 31, 2017
Mortgages payable, gross	$ 395,357	$ 396,946
Unamortized deferred financing costs	(3,758)	(3,789)
Mortgages payable, net	$ 391,599	$ 393,157

Line of Credit

The Company has a credit facility with Manufacturers & Traders Trust Company, People s United Bank, VNB New York, LLC, and Bank Leumi USA, pursuant to which the Company may borrow up to $100,000,000, subject to borrowing base requirements. The facility, which matures December 31, 2019, provides that the Company pay an interest rate equal to the one month LIBOR rate plus an applicable margin ranging from 175 basis points to 300 basis points depending on the ratio of the Company s total debt to total value, as determined pursuant to the facility. At June 30, 2018 and 2017, the applicable margin was 175 basis points. An unused facility fee of .25% per annum applies to the facility. The average interest rate on the facility was approximately 3.54% and 2.67% for the six months ended June 30, 2018 and 2017, respectively. The Company was in compliance with all covenants at June 30, 2018.

The following table details the Line of credit, net, balances per the consolidated balance sheets (amounts in thousands):

	June 30, 2018	December 31, 2017
Line of credit, gross	$ 20,300	$ 9,400
Unamortized deferred financing costs	(468)	(624)
Line of credit, net	$ 19,832	$ 8,776

At August 2, 2018, there was an outstanding balance of $3,300,000 (before unamortized deferred financing costs) under the facility.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 10 Related Party Transactions

Compensation and Services Agreement

Pursuant to the compensation and services agreement with Majestic Property Management Corp. (Majestic), the Company pays fees to Majestic and Majestic provides to the Company the services of all affiliated executive, administrative, legal, accounting, clerical and property management personnel, as well as property acquisition, sale and lease consulting and brokerage services, consulting services with respect to mortgage financings and construction supervisory services. Majestic is wholly-owned by the Company s vice-chairman and certain of the Company s executive officers are officers of, and are compensated by, Majestic. The fee the Company pays Majestic is negotiated each year by Majestic and the Compensation and/or Audit Committees of the Company s Board of Directors, and is approved by such committees and the independent directors.

In consideration for the services described above, the Company paid Majestic $689,000 and $1,367,000 for the three and six months ended June 30, 2018 respectively, and $664,000 and $1,329,000 for the three and six months ended June 30, 2017, respectively. Included in these fees are $309,000 and $608,000 of property management costs for the three and six months ended June 30, 2018, respectively, and $284,000 and $570,000 for the three and six months ended June 30, 2017, respectively. The property management fee portion of the compensation and services agreement is paid based on 1.5% and 2.0% of the rental payments (including tenant reimbursements) actually received by the Company from net lease tenants and operating lease tenants, respectively. The Company does not pay Majestic property management fees with respect to properties managed by third parties. Majestic credits against the fees due to it under the compensation and services agreement any management or other fees received by it from any joint venture in which the Company is a joint venture partner. The compensation and services agreement also provides for an additional payment to Majestic of $54,000 and $108,000 in each of the three and six months ended June 30, 2018 and 2017, respectively, for the Company s share of all direct office expenses, including rent, telephone, postage, computer services, internet usage and supplies. The Company does not pay any fees or expenses to Majestic for such services except for the fees described in this paragraph.

Executive officers and others providing services to the Company under the compensation and services agreement were awarded shares of restricted stock and RSUs under the Company s stock incentive plans (described in Note 13). The related expense charged to the Company s operations was $432,000 and $849,000 for the three and six months ended June 30, 2018, respectively, and $386,000 and $768,000 for the three and six months ended June 30, 2017, respectively.

The fees paid under the compensation and services agreement (except for the property management fees which are included in Real estate expenses) and the costs of the stock incentive plans are included in General and administrative expense on the consolidated statements of income for the three and six months ended June 30, 2018 and 2017.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 10 Related Party Transactions (Continued)

Joint Venture Partners and Affiliates

The Company paid an aggregate of $22,000 and $65,000 for the three and six months ended June 30, 2018, respectively, and $33,000 and $82,000 for the three and six months ended June 30, 2017, respectively, to its consolidated joint venture partners or their affiliates (none of whom are officers, directors or employees of the Company) for property management fees, which are included in Real estate expenses on the consolidated statements of income.

The Company s unconsolidated joint ventures paid management fees of $45,000 and $96,000 for the three and six months ended June 30, 2018, respectively, and $42,000 and $87,000 for the three and six months ended June 30, 2017, respectively, to the other partner of the venture, which reduced Equity in earnings of $23,000 and $48,000 for the three and six months ended June 30, 2018, respectively, and $21,000 and $44,000 for the three and six months ended June 30, 2017, respectively.

Other

During 2018 and 2017, the Company paid quarterly fees of $69,000 to the Company s chairman and $27,500 to the Company s vice-chairman. These fees are included in General and administrative expenses on the consolidated statements of income.

The Company obtains its property insurance in conjunction with Gould Investors L.P. (Gould Investors), a related party, and reimburses Gould Investors annually for the Company s insurance cost relating to its properties. Included in Real estate expenses on the consolidated statements of income is insurance expense of $206,000 and $404,000 for the three and six months ended June 30, 2018, respectively, and $174,000 and $347,000 for the three and six months ended June 30, 2017, respectively of amounts reimbursed to Gould Investors in prior periods.

Note 11 Common Stock Cash Dividend

On June 13, 2018, the Board of Directors declared a quarterly cash dividend of $.45 per share on the Company s common stock, totaling $8,652,000. The quarterly dividend was paid on July 6, 2018 to stockholders of record on June 25, 2018.

Note 12 Shares Issued through Equity Offering Program

During the six months ended June 30, 2018, the Company sold 93,417 shares for proceeds of $2,303,000, net of commissions of $23,000, and incurred offering costs of $45,000 for professional fees.

One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 13 Stock Based Compensation

The Company s 2016 Incentive Plan (Plan), approved by the Company s stockholders in June 2016, permits the Company to grant, among other things, stock options, restricted stock, RSUs, performance share awards and dividend equivalent rights and any one or more of the foregoing to its employees, officers, directors and consultants. A maximum of 750,000 shares of the Company s common stock is authorized for issuance pursuant to this Plan. As of June 30, 2018, (i) restricted stock awards with respect to 284,850 shares had been issued, of which 200 shares were forfeited and 3,000 shares had vested, and (ii) as further described below, RSUs with respect to 76,250 shares had been issued and are outstanding.

Under the Company s 2012 Incentive Plan, as of June 30, 2018, 500,700 shares had been issued, of which 3,400 shares were forfeited and 127,450 shares had vested. No additional awards may be granted under this plan.

For accounting purposes, the restricted stock is not included in the shares shown as outstanding on the balance sheet until they vest; however, dividends are paid on the unvested shares. The restricted stock grants are charged to General and administrative expense over the respective vesting periods based on the market value of the common stock on the grant date. Unless earlier forfeited because the participant s relationship with the Company terminated, unvested restricted stock awards vest on the fifth anniversary of the grant date, and under certain circumstances may vest earlier.

In each of 2017 and July 2018, the Company granted RSUs exchangeable for up to 76,250 shares of common stock upon satisfaction, through June 30, 2020 and June 30, 2021, respectively, of specified conditions. Specifically, up to 50% of these RSUs vest upon achievement of metrics related to average annual total stockholder return (the TSR Awards), which metrics meet the definition of a market condition, and up to 50% vest upon achievement of metrics related to average annual return on capital (the ROC Awards), which metrics meet the definition of a performance condition. The holders of the RSUs are not entitled to dividends or to vote the underlying shares until such RSUs vest and shares are issued. Accordingly, the shares underlying these RSUs are not included in the shares shown as outstanding on the balance sheet. For the ROC Awards, the performance assumptions are re-evaluated quarterly. Expense is not recognized on the RSUs which the Company does not expect to vest as a result of service conditions or the Company s performance expectations.

Based on performance and market assumptions, the total amount recorded as deferred compensation for the 2017 grant of RSUs is $1,005,000, and such sum will be charged to General and administrative expense over the three year performance cycle. None of these RSUs were forfeited or vested during the six months ended June 30, 2018.

In 2010, RSUs exchangeable for up to 200,000 shares of common stock were awarded pursuant to the Company s 2009 Incentive Plan. The holders of RSUs were not entitled to dividends or to vote the underlying shares until the RSUs vested and the underlying shares were issued.

During 2017, 113,584 shares of common stock underlying the RSUs were deemed to have vested and were issued. RSUs with respect to the balance of 86,416 shares were forfeited.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 13 Stock Based Compensation (Continued)

The following is a summary of the activity of the equity incentive plans:

	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Six Months Ended June 30, 2018	Six Months Ended June 30, 2017
Restricted stock:				
Number of shares			144,750	140,100
Average per share grant price			$ 25.31	$ 24.75
Deferred compensation to be recognized over vesting period			$ 3,664,000	$ 3,467,000
Number of non-vested shares:				
Non-vested beginning of period	651,650	626,400	612,900	591,750
Grants			144,750	140,100
Vested during period		(13,500)	(106,000)	(118,450)
Forfeitures	(150)		(150)	(500)
Non-vested end of period	651,500	612,900	651,500	612,900
RSU grants:				
Number of underlying shares				
Average per share grant price				
Deferred compensation to be recognized over vesting period				
Number of non-vested shares:				
Non-vested beginning of period	76,250	200,000	76,250	200,000
Grants				
Vested during period		(113,584)		(113,584)
Forfeitures		(86,416)		(86,416)
Non-vested end of period	76,250		76,250	
Restricted stock and RSU grants:				
Weighted average per share value of non-vested shares (based on grant price)	$ 23.56	$ 22.75	$ 23.56	$ 22.75
Value of stock vested during the period (based on grant price)	$	$ 1,248,000	$ 2,289,000	$ 3,008,000
Weighted average per share value of shares forfeited during the period (based on grant price)	$ 23.93	$ 8.29	$ 23.93	$ 8.37
The total charge to operations:				

Outstanding restricted stock grants	$ 765,000	$ 878,000	$ 1,500,000	$ 1,571,000
Outstanding RSUs	91,000	37,000	182,000	86,000
Total charge to operations	$ 856,000	$ 915,000	$ 1,682,000	$ 1,657,000

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 13 Stock Based Compensation (Continued)

As of June 30, 2018, total compensation costs of $8,349,000 and $728,000 to non-vested restricted stock awards and RSUs, respectively, have not yet been recognized. These compensation costs will be charged to General and administrative expense over the remaining respective vesting periods. The weighted average vesting period is 2.7 years for the restricted stock and 2.0 years for the RSUs.

Note 14 Fair Value Measurements

The Company measures the fair value of financial instruments based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, a fair value hierarchy distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity and the reporting entity s own assumptions about market participant assumptions. In accordance with the fair value hierarchy, Level 1 assets/liabilities are valued based on quoted prices for identical instruments in active markets, Level 2 assets/liabilities are valued based on quoted prices in active markets for similar instruments, on quoted prices in less active or inactive markets, or on other observable market inputs and Level 3 assets/liabilities are valued based significantly on unobservable market inputs.

The carrying amounts of cash and cash equivalents, restricted cash, escrow, deposits and other assets and receivables (excluding interest rate swaps), dividends payable, and accrued expenses and other liabilities (excluding interest rate swaps), are not measured at fair value on a recurring basis, but are considered to be recorded at amounts that approximate fair value.

At June 30, 2018, the $389,903,000 estimated fair value of the Company s mortgages payable is less than their $395,357,000 carrying value (before unamortized deferred financing costs) by approximately $5,454,000 assuming a blended market interest rate of 4.50% based on the 8.5 year weighted average remaining term to maturity of the mortgages. At December 31, 2017, the $397,103,000 estimated fair value of the Company s mortgages payable is greater than their $396,946,000 carrying value (before unamortized deferred financing costs) by approximately $157,000 assuming a blended market interest rate of 4.25% based on the 8.7 year weighted average remaining term to maturity of the mortgages.

At June 30, 2018 and December 31, 2017, the carrying amount of the Company s line of credit (before unamortized deferred financing costs) of $20,300,000 and $9,400,000, respectively, approximates its fair value.

The fair value of the Company s mortgages payable and line of credit are estimated using unobservable inputs such as available market information and discounted cash flow analysis based on borrowing rates the Company believes it could obtain with similar terms and maturities. These fair value measurements fall within Level 3 of the fair value hierarchy.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 14 Fair Value Measurements (Continued)

Considerable judgment is necessary to interpret market data and develop estimated fair value. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

Fair Value on a Recurring Basis

The fair value of the Company s derivative financial instruments, using Level 2 inputs, was determined to be the following (amounts in thousands):

	As of	Carrying and Fair Value	
Financial assets:			
Interest rate swaps	June 30, 2018	$	4,032
	December 31, 2017		1,615
Financial liabilities:			
Interest rate swaps	June 30, 2018	$	109
	December 31, 2017		1,492

The Company does not own any financial instruments that are measured on a recurring basis and that are classified as Level 1 or 3.

The Company s objective in using interest rate swaps is to add stability to interest expense. The Company does not use derivatives for trading or speculative purposes.

Fair values are approximated using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of the derivatives. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves and implied volatilities.

Although the Company has determined the majority of the inputs used to value its derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with it use Level 3 inputs, such as estimates of current credit spreads, to evaluate the likelihood of default by the Company and its counterparty. As of June 30, 2018, the Company has assessed and determined the impact of the credit valuation adjustments on the overall valuation of its derivative positions is not significant. As a result, the Company determined its derivative valuation is classified in Level 2 of the fair value hierarchy.

As of June 30, 2018, the Company had entered into 28 interest rate derivatives, all of which were interest rate swaps, related to 28 outstanding mortgage loans with an aggregate $131,103,000 notional amount and mature between 2019 and 2028 (weighted average remaining term to maturity of 6.6 years). Such interest rate swaps, all of which were designated as cash flow hedges, converted LIBOR based variable rate mortgages to fixed annual rate mortgages (with interest rates ranging from 3.02% to 5.38% and a weighted average interest 4.13% at June 30, 2018). The fair values of the Company s derivatives in asset and liability positions are reflected as other assets or other liabilities on the consolidated balance sheets.

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 14 Fair Value Measurements (Continued)

One of the Company s unconsolidated joint ventures, in which a wholly-owned subsidiary of the Company is a 50% partner, had an interest rate derivative outstanding at June 30, 2018 which was designated as a cash flow hedge. This interest rate swap with a $6,983,000 notional amount has an interest rate of 3.49% and matures in 2022. See discussion below for the discontinuation of hedge accounting on this interest rate swap during the three months ended June 30, 2018.

In connection with the sale of an unconsolidated joint venture property in Savannah, Georgia, the Company terminated an interest rate swap with a $3,402,000 notional amount and a 5.81% interest rate when the related mortgage was paid off at its maturity in April 2018 (see Note 7).

The following table presents the effect of the Company s derivative financial instruments on the consolidated statements of income for the periods presented (amounts in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	**2017**	**2018**	**2017**
One Liberty Properties, Inc. and Consolidated subsidiaries				
Amount of gain (loss) recognized on derivatives in Other comprehensive income	$ 1,009	$ (1,055)	$ 3,509	$ (986)
Amount of reclassification from Accumulated other comprehensive income into Interest expense	(95)	(545)	(291)	(1,054)
Unconsolidated Joint Ventures (Company s share)				
Amount of gain (loss) recognized on derivatives in Other comprehensive income	$ 22	$ (21)	$ 69	$ (12)
Amount of reclassification from Accumulated other comprehensive income into Equity in earnings of unconsolidated joint ventures	110	(16)	103	(35)

During the three months ended June 30, 2018 and 2017, the Company (including one of its unconsolidated joint ventures) discontinued hedge accounting on two interest rate swaps as the forecasted hedged transactions were no longer probable of occurring. As a result, during the three months ended June 30, 2018 and 2017, the Company reclassified $110,000 and $118,000 of realized gain and loss, respectively, from Accumulated other comprehensive income to earnings. No gain or loss was recognized with respect to amounts excluded from effectiveness testing on the Company s cash flow hedges for the three and six months ended June 30, 2018 and 2017.

During the twelve months ending June 30, 2019, the Company estimates an additional $222,000 will be reclassified from other Accumulated other comprehensive income as a decrease to Interest expense.

The derivative agreements in effect at June 30, 2018 provide that if the wholly-owned subsidiary of the Company which is a party to the agreement defaults or is capable of being declared in default on any of its indebtedness, then a default can be declared on such subsidiary s derivative obligation. In addition, the Company is a party to the derivative agreements and if there is a default by the subsidiary on the loan subject to the derivative

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 14 Fair Value Measurements (Continued)

agreement to which the Company is a party and if there are swap breakage losses on account of the derivative being terminated early, then the Company could be held liable for such swap breakage losses, if any.

As of June 30, 2018 and December 31, 2017, the fair value of the derivatives in a liability position, including accrued interest of $9,000 and $53,000, respectively, but excluding any adjustments for nonperformance risk, was approximately $126,000 and $1,638,000, respectively. In the event the Company breaches any of the contractual provisions of the derivative contracts, it would be required to settle its obligations thereunder at their termination liability value of $126,000 and $1,638,000 as of June 30, 2018 and December 31, 2017, respectively. This termination liability value, net of adjustments for nonperformance risk of $8,000 and $93,000, is included in Accrued expenses and other liabilities on the consolidated balance sheet at June 30, 2018 and December 31, 2017, respectively.

Note 15 Commitments

The Company is contractually required to expend approximately $7,800,000 through 2018 for building expansion and improvements at its property tenanted by L-3 Communications, located in Hauppauge, New York, of which $6,261,000 has been spent through June 30, 2018.

Note 16 New Accounting Pronouncements

In June 2018, the FASB issued ASU No. 2018-07, *Compensation - Stock Compensation (Topic 718), Improvements to Nonemployee Share-Based Payment Accounting,* which provides additional guidance related to share-based payment transactions for acquiring goods or services from nonemployees. The guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Company is evaluating this new guidance but does not expect it to have a material impact on the Company s consolidated financial statements.

In August 2017, the FASB issued ASU No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*, which amends the presentation and disclosure requirements for hedge accounting and changes how companies assess hedge effectiveness. This ASU is intended to more closely align hedge accounting with companies risk management strategies, simplify the application of hedge accounting, and increase transparency as to the scope and results of hedging programs. The Company early adopted this guidance on January 1, 2018 using the modified retrospective transition method and its adoption did not have any impact on the Company s previously reported income from operations, net income or accumulated undistributed net income for the periods presented.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. The guidance replaces the current incurred loss model with an expected loss approach. The guidance is effective for fiscal years, and

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One Liberty Properties, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2018 (Continued)

Note 16 New Accounting Pronouncements (Continued)

interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted after December 2018. The Company is evaluating the new guidance to determine if, and to the extent, it will impact the consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, which amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets and making targeted changes to lessor accounting. In July 2018, the FASB issued ASU No. 2018-10, *Codification Improvements to Topic 842, Leases,* which seeks to clarify aspects of ASU No. 2016-02 and correct unintended application of such guidance. The effective date of these standards will be fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, and early adoption is permitted. The new leases standard requires a modified retrospective transition approach for all leases existing at, or entered into after, the date of initial application, with an option to use certain transition relief. The Company is currently evaluating these new standards but does not expect them to have a significant effect on its consolidated financial statements. The Company anticipates adopting these standards effective as of January 1, 2019 and will apply the modified retrospective approach.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which outlines a new, single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. The new model requires revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration a company expects to receive in exchange for those goods or services. In July 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which delays the effective date of ASU No. 2014-09 by one year. In March 2016, the FASB issued ASU No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*, which is intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations. ASU No. 2014-09, ASU No. 2015-14 and ASU No. 2016-08 are herein collectively referred to as the New Revenue Recognition Standards . The Company adopted the New Revenue Recognition Standards on January 1, 2018 using the modified retrospective transition method. The Company s main revenue streams are rental revenues and tenant reimbursements. Such revenues are related to lease contracts with tenants which currently fall within the scope of ASC Topic 840, and will fall within the scope of ASC Topic 842 upon the adoption of ASU No. 2016-02 on January 1, 2019 (the Company s sales of real estate are within the scope of ASU No. 2017-05, see Note 5). Accordingly, the adoption of the New Revenue Recognition Standards did not (i) result in a cumulative adjustment as of January 1, 2018, and (ii) have any impact on the Company s consolidated financial statements.

Note 17 Subsequent Events

Subsequent events have been evaluated and except as disclosed herein, there were no other events relative to the consolidated financial statements that require additional disclosure.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. We intend such forward-looking statements to be covered by the safe harbor provision for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and include this statement for purposes of complying with these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe our future plans, strategies and expectations, are generally identifiable by use of the words may, will, could, believe, expect, intend, anticipate, estimate, project, or similar expressions or variations thereof. Forward-looking statements should not be relied on since they involve known and unknown risks, uncertainties and other factors which are, in some cases, beyond our control and which could materially affect actual results, performance or achievements. Investors are encouraged to review the risk factors included in our Annual Report on Form 10-K for the year ended December 31, 2017 under the caption Item 1A. Risk Factors for a discussion of certain factors which may cause actual results to differ materially from current expectations and are cautioned not to place undue reliance on any forward-looking statements.

Overview

We are a self-administered and self-managed real estate investment trust, or REIT, incorporated in Maryland in 1982. To qualify as a REIT, under the Internal Revenue Code of 1986, as amended, we must meet a number of organizational and operational requirements, including a requirement that we distribute currently at least 90% of ordinary taxable income to our stockholders. We intend to comply with these requirements and to maintain our REIT status.

We acquire, own and manage a geographically diversified portfolio consisting primarily of industrial, retail (including furniture stores and supermarkets), restaurant, health and fitness and theater properties, many of which are subject to long-term net leases. As of June 30, 2018, we own 120 properties (including five properties owned by consolidated joint ventures and five properties owned by unconsolidated joint ventures) located in 30 states. Based on square footage, our occupancy rate at June 30, 2018 is approximately 99.1%.

We face a variety of risks and challenges in our business. Among other things, we face the possibility that we will not be able to acquire accretive properties on acceptable terms, lease our properties on terms favorable to us or at all, our tenants may not be able to pay their rental and other obligations and we may not be able to renew or relet, on acceptable terms, leases that are expiring or otherwise terminating.

We seek to manage the risk of our real property portfolio and the related financing arrangements by diversifying among types of properties, industries, locations, tenants, scheduled lease expirations, mortgage maturities and lenders, and by seeking to minimize our exposure to interest rate fluctuations. Substantially all of our mortgage debt either bears interest at fixed rates or is subject to interest rate swaps, limiting our exposure to fluctuating interest rates on our outstanding mortgage debt.

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We monitor the risk of tenant non-payments through a variety of approaches tailored to the applicable situation. Generally, based on our assessment of the credit risk posed by our tenants, we monitor a tenant s financial condition through one or more of the following actions: reviewing tenant financial statements or other financial information, obtaining other tenant related information, regular contact with tenant s representatives, tenant credit checks and regular management reviews of our tenants. We may sell a property if the tenant s financial condition is unsatisfactory.

In acquiring properties, we balance an evaluation of the terms of the leases and the credit of the existing tenants with a fundamental analysis of the real estate to be acquired, which analysis takes into account, among other things, the estimated value of the property, local demographics and the ability to re-rent or dispose of the property on favorable terms upon lease expiration or early termination.

We are sensitive to the risks facing the retail industry as a result of the growth of e-commerce. We are addressing our exposure to the retail industry by seeking to acquire industrial properties that we believe capitalize on e-commerce activities, such as e-commerce distribution and warehousing facilities, and by being especially selective in acquiring retail properties. Approximately 39.0% of our contractual rental income (as described below) is derived from retail tenants (including 8.8%, 4.2% and 3.3% from tenants engaged in retail furniture, supermarkets and office supply activities, respectively) and 38.4%, 5.3%, 4.9%, 4.5%, 3.2% and 4.7% from industrial (*e.g.*, distribution and warehouse facilities), residential ground leases, restaurant, health and fitness, theaters and other properties, respectively.

Our contractual rental income is approximately $69.0 million and represents, after giving effect to any abatements, concessions or adjustments, the base rent payable to us during the twelve months ending June 30, 2019 under leases in effect at June 30, 2018. Contractual rental income excludes: (i) approximately $589,000 of straight-line rent and $1.1 million of amortization of intangibles; and (ii) our share of the rental income payable to our unconsolidated joint ventures, which is approximately $1.7 million (excluding $658,000 of rental income from a property sold in July 2018).

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The following table sets forth scheduled expirations of leases for our properties as of June 30, 2018 for the periods indicated below:

Lease Expiration (1) 12 Months Ending June 30,	Number of Expiring Leases	Approximate Square Footage Subject to Expiring Leases (2)		Contractual Rental Income Under Expiring Leases	Percentage of Contractual Rental Income Represented by Expiring Leases
2019	13	257,917	$	1,256,206	1.8
2020	8	181,386		1,906,403	2.8
2021	17	473,150		3,928,474	5.7
2022	21	1,351,812		8,032,439	11.6
2023	19	1,491,689		10,444,761	15.1
2024	11	568,272		5,140,610	7.4
2025	10	484,815		5,085,781	7.4
2026	8	230,189		3,523,673	5.1
2027	8	415,981		2,765,415	4.0
2028	10	1,079,941		7,541,607	10.9
2029 and thereafter	26	3,198,997		19,405,228	28.2
	151	9,734,149	$	69,030,597	100.0

(1) Lease expirations assume tenants do not exercise existing renewal or termination options.

(2) Excludes an aggregate of 67,891 square feet of vacant space.

Property Transactions During the Three Months Ended June 30, 2018

On April 5, 2018, an unconsolidated joint venture sold its building and a portion of its land, located in Savannah, Georgia for $2.6 million, net of closing costs. Our 50% share of the gain from this sale, which was recognized in the three and six months ended June 30, 2018, is $71,000. In connection with the sale of this property, the joint venture and its affiliates repaid the $3.4 million mortgage balance which encumbered their contiguous properties.

On June 7, 2018, we acquired an industrial facility in Plymouth, Minnesota for $5.6 million, including $50,000 of transaction costs that were capitalized. The facility is net leased to Plymouth Industries through 2033. We estimate that commencing July 1, 2018, the quarterly rental income and depreciation expense from this property will be $117,000 and $29,000, respectively.

Property Transaction Subsequent to June 30, 2018

On July 31, 2018, an unconsolidated joint venture sold its only property, located in Milwaukee, Wisconsin, for $12.8 million, net of closing costs. We anticipate that our 50% share of the gain from this sale, which will be recognized in the three months ending September 30, 2019, will be approximately $2.0 million. In connection with the sale of this property, the joint venture repaid its $7.0 million mortgage. Equity in earnings from unconsolidated joint ventures for the three and six months ended June 30, 2018 includes the recognition of $110,000, representing our 50% share of the realized gain that was reclassified from accumulated other comprehensive income as a result of the discontinuance of hedge accounting on its mortgage interest rate swap. This joint venture accounted for $172,000 of our Equity in earnings of unconsolidated joint ventures during the six months ended June 30, 2017.

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Results of Operations

Revenues

The following table compares revenues for the periods indicated:

(Dollars in thousands)	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Increase (Decrease)	% Change	Six Months Ended June 30, 2018	Six Months Ended June 30, 2017	Increase (Decrease)	% Change
Revenues:								
Rental income, net	$ 17,718	$ 16,720	$ 998	6.0	$ 35,308	$ 33,553	$ 1,755	5.2
Tenant reimbursements	2,034	1,693	341	20.1	3,978	3,332	646	19.4
Total revenues	$ 19,752	$ 18,413	$ 1,339	7.3	$ 39,286	$ 36,885	$ 2,401	6.5

Rental income, net. The increases during the three and six months ended June 30, 2018 are due primarily to $270,000 and $281,000, respectively, generated by two properties acquired in 2018 and $660,000 and $1.5 million, respectively, generated by four properties acquired in 2017. Same store properties (as defined below) contributed $349,000 and $578,000, respectively, during the three and six months ended June 30, 2018, primarily due to the re-tenanting of two properties that were vacant in the corresponding prior year periods. Offsetting the increases in rental income during the three and six months ended June 30, 2018 are decreases of $281,000 and $576,000, respectively, representing the 2017 rental income from properties sold during 2018 and 2017. Same store properties refer to properties that were owned for the entirety of the periods being presented.

Tenant reimbursements. Real estate tax and operating expense reimbursements increased during the three and six months ended June 30, 2018 due primarily to reimbursements of (i) $219,000 and $394,000, respectively, from several same store properties and (ii) $218,000 and $395,000, respectively, from properties acquired in 2018 and 2017. Offsetting the increases during the three and six months ended June 30, 2018 are decreases of $96,000 and $143,000, respectively, representing tenant reimbursements in 2017 from the Fort Bend, Texas property sold in January 2018. Tenant reimbursements generally relate to real estate expenses incurred in the same period.

Operating Expenses

The following table compares operating expenses for the periods indicated:

			Increase	%			Increase	%

(Dollars in thousands)	Three Months Ended June 30, 2018	2017	(Decrease)	Change	Six Months Ended June 30, 2018	2017	(Decrease)	Change
Operating expenses:								
Depreciation and amortization	$ 5,250	$ 5,190	$ 60	1.2	$ 10,432	$ 10,743	$ (311)	(2.9)
General and administrative	2,969	2,893	76	2.6	5,928	5,708	220	3.9
Real estate expenses	2,515	2,371	144	6.1	5,182	5,075	107	2.1
Federal excise and state taxes	154	224	(70)	(31.3)	227	312	(85)	(27.2)
Leasehold rent	77	77			154	154		
Total operating expenses	10,965	10,755	210	2.0	$ 21,923	21,992	(69)	(.3)
Operating income	$ 8,787	$ 7,658	$ 1,129	14.7	$ 17,363	$ 14,893	$ 2,470	16.6

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Depreciation and amortization. The decrease in the six months ended June 30, 2018 is due primarily to (i) $947,000 from the sales of properties in 2017 and 2018 and (ii) the inclusion, during the six months ended June 30, 2017, of $219,000 for the write-off of tenant origination costs related to a vacant property. Offsetting the decrease is an increase of $763,000 in depreciation and amortization expense on the properties acquired in 2018 and 2017.

General and administrative. The increase in the six months ended June 30, 2018 was due primarily to (i) an increase in professional fees, including a one-time $110,000 fee and (ii) higher compensation levels and an additional employee.

Real estate expenses. The increases during the three and six months ended June 30, 2018 are primarily due to $215,000 and $406,000, respectively, from properties acquired in 2017 and 2018; substantially all these expenses are rebilled to tenants and are included in Tenant reimbursements. Same store properties contributed net increases of $113,000 and $149,000, respectively, during the three and six months ended June 30, 2018. These increases were offset by decreases of $184,000 and $448,000 related to properties sold during 2018 and 2017.

Other Income and Expenses

The following table compares our other income and expenses for the periods indicated:

	Three Months Ended June 30,				Six Months Ended June 30,			
(Dollars in thousands)	**2018**	**2017**	**Increase (Decrease)**	**% Change**	**2018**	**2017**	**Increase (Decrease)**	**% Change**
Other income and expenses:								
Equity in earnings of unconsolidated joint ventures	$ 348	$ 206	$ 142	68.9	$ 543	$ 451	$ 92	20.4
Equity in earnings from sale of unconsolidated joint venture property	71		71	100.0	71		71	100.0
Other income	6	320	(314)	(98.1)	10	342	(332)	(97.1)
Interest:								
Expense	(4,445)	(4,532)	(87)	(1.9)	(8,747)	(8,921)	(174)	(2.0)
Amortization and write-off of deferred financing costs	(221)	(227)	(6)	(2.6)	(449)	(454)	(5)	(1.1)

Equity in earnings of unconsolidated joint ventures. The increases in the three and six months ended June 30, 2018 were due primarily to the recognition of $110,000, which represents our 50% share of the realized gain reclassified from accumulated other comprehensive income as a result of the discontinuance of hedge accounting on a mortgage interest rate swap in connection with the July 31, 2018 sale of the Milwaukee, Wisconsin property.

Other income. The three and six months ended June 30, 2017 includes $243,000 paid to us by a former tenant in connection with the resolution of a dispute.

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Interest expense. The following table details the components of interest expense for the periods indicated:

(Dollars in thousands)	Three Months Ended June 30, 2018	2017	Increase (Decrease)	% Change	Six Months Ended June 30, 2018	2017	Increase (Decrease)	% Change
Interest expense:								
Credit line interest	$ 219	$ 115	$ 104	90.4	$ 346	$ 221	$ 125	56.6
Mortgage interest	4,226	4,417	(191)	(4.3)	8,401	8,700	(299)	(3.4)
Total	$ 4,445	$ 4,532	$ (87)	(1.9)	$ 8,747	$ 8,921	$ (174)	(2.0)

Credit line interest

The increase in the three and six months ended June 30, 2018 were due primarily to increases of $10.5 million and $5.6 million, respectively, in the weighted average balance outstanding under our line of credit and increases of 85 (from 2.81% to 3.66%) and 87 basis points (from 2.67% to 3.54%), respectively, in the average interest rate due to the increase in the one month LIBOR rate.

Mortgage interest

The following table reflects the average interest rate on the average principal amount of outstanding mortgage debt for the periods indicated:

(Dollars in thousands)	Three Months Ended June 30, 2018	2017	Increase (Decrease)	% Change	Six Months Ended June 30, 2018	2017	Increase (Decrease)	% Change
Average interest rate on mortgage debt	4.27%	4.32%	(.05)	(1.2)	4.25%	4.31%	(.06)	(1.4)
Average principal amount of mortgage debt	$ 395,643	$ 397,935	$ (2,292)	(.6)	$ 395,277	$ 398,121	$ (2,844)	(.7)

The decreases are due primarily to decreases in the average interest rates on outstanding mortgage debt and the average principal amount of mortgage debt outstanding. The decreases in the average interest rates are due to the financing (including financings effectuated in connection with acquisitions) or refinancing in 2018 and 2017 of $34.8 million of gross mortgage debt (including $2.9 million of refinanced amounts) with an average interest rate of approximately 4.0%. The net decreases in the average balance outstanding are due principally to scheduled amortization payments and the payoff of several mortgages in connection with property sales.

Gain on sale of real estate, net. The gain in the six months ended June 30, 2018 was realized from the sale of the Fort Bend, Texas property. The non-controlling interest s share of the gain was $776,000. The gain in the three and six months ended June 30, 2017 was realized from the sale of the Greenwood Village, Colorado property in May 2017.

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Liquidity and Capital Resources

Our sources of liquidity and capital include cash flow from operations, cash and cash equivalents, borrowings under our revolving credit facility, refinancing existing mortgage loans, obtaining mortgage loans secured by our unencumbered properties, issuance of our equity securities and property sales. Our available liquidity at August 2, 2018, was $99.2 million, including $2.5 million of cash and cash equivalents (net of the credit facility s required $3.0 million deposit maintenance balance) and, subject to borrowing base requirements, up to $96.7 million available under our revolving credit facility.

Liquidity and Financing

We expect to meet our (i) operating cash requirements (including debt service and dividends) principally from cash flow from operations and (ii) capital requirements of $1.5 million of building expansion and improvements at our property tenanted by L-3 located in Hauppauge, New York, from cash flow from operations, our available cash and cash equivalents, proceeds from the sale of our common stock and, to the extent permitted, our credit facility. We and our joint venture partner are also contemplating a significant redevelopment of our multi-tenant shopping center in Manahawkin, New Jersey we anticipate that the capital expenditures that may be incurred if such property is redeveloped will be funded by the foregoing sources as well as equity contributions from us and our joint venture partner.

At June 30, 2018, excluding mortgage indebtedness of our unconsolidated joint ventures, we had 68 outstanding mortgages payable secured by 85 properties, in the aggregate principal amount of $395.4 million (before netting unamortized deferred financing costs). These mortgages represent first liens on individual real estate investments with an aggregate carrying value of $626.6 million, before accumulated depreciation of $88.4 million. After giving effect to interest rate swap agreements, the mortgage payments bear interest at fixed rates ranging from 3.02% to 6.45% (a 4.25% weighted average interest rate) and mature between 2018 and 2042 (an 8.5 year weighted average remaining term to maturity).

The following table sets forth, as of June 30, 2018, information with respect to our mortgage debt that is payable from July 1, 2018 through December 31, 2021 (excluding our unconsolidated joint ventures):

(Dollars in thousands)	2018	2019	2020	2021	Total
Amortization payments	$ 5,179	$ 11,824	$ 12,633	$ 13,046	$ 42,682
Principal due at maturity	2,890	3,485		8,463	14,838
Total	$ 8,069	$ 15,309	$ 12,633	$ 21,509	$ 57,520

At June 30, 2018, our unconsolidated joint ventures had first mortgages on two properties with outstanding balances aggregating $31.2 million, bearing interest rates of 3.49% and 4.0% (*i.e.*, a 3.89% weighted average interest rate) and maturing in 2022 and 2025. The mortgage in principal amount of $7.0 million, an interest rate of 3.49% and maturing in 2022, was paid off in connection with the July 2018 sale of the joint venture property in Milwaukee, Wisconsin.

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We intend to make debt amortization payments from operating cash flow and, though no assurance can be given that we will be successful in this regard, generally intend to refinance, extend or payoff the mortgage loans which mature in 2018 through 2021. We intend to repay the amounts not refinanced or extended from our existing funds and sources of funds, including our available cash, proceeds from the sale of our common stock and our credit facility (to the extent available).

We continually seek to refinance existing mortgage loans on terms we deem acceptable to generate additional liquidity. Additionally, in the normal course of our business, we sell properties when we determine that it is in our best interests, which also generates additional liquidity. Further, since each of our encumbered properties is subject to a non-recourse mortgage (with standard carve-outs), if our in-house evaluation of the market value of such property is less than the principal balance outstanding on the mortgage loan, we may determine to convey, in certain circumstances, such property to the mortgagee in order to terminate our mortgage obligations, including payment of interest, principal and real estate taxes, with respect to such property.

Typically, we utilize funds from our credit facility to acquire a property and, thereafter secure long-term, fixed rate mortgage debt on such property. We apply the proceeds from the mortgage loan to repay borrowings under the credit facility, thus providing us with the ability to re-borrow under the credit facility for the acquisition of additional properties.

Credit Facility

Subject to borrowing base requirements, we can borrow up to $100.0 million pursuant to our revolving credit facility which is available to us for the acquisition of commercial real estate, repayment of mortgage debt, property improvements and general working capital purposes; provided, that if used for property improvements and working capital purposes, the amount outstanding for such purposes will not exceed the lesser of $15.0 million and 15% of the borrowing base and if used for working capital purposes, will not exceed $10.0 million. The facility matures December 31, 2019 and bears interest equal to the one month LIBOR rate plus the applicable margin. The applicable margin ranges from 175 basis points if our ratio of total debt to total value (as calculated pursuant to the facility) is equal to or less than 50%, increasing to a maximum of 300 basis points if such ratio is greater than 65%. The applicable margin was 175 basis points at June 30, 2018 and 2017. At June 30, 2018 and 2017, the interest rate was 3.80% and 2.87%, respectively. There is an unused facility fee of 0.25% per annum on the difference between the outstanding loan balance and $100 million. The credit facility requires the maintenance of $3.0 million in average deposit balances.

The terms of our revolving credit facility include certain restrictions and covenants which limit, among other things, the incurrence of liens, and which require compliance with financial ratios relating to, among other things, the minimum amount of tangible net worth, the minimum amount of debt service coverage, the minimum amount of fixed charge coverage, the maximum amount of debt to value, the minimum level of net income, certain investment limitations and the minimum value of unencumbered properties and the number of such properties. Net proceeds received from the sale, financing or refinancing of properties are generally required to be used to repay amounts outstanding under our credit facility. At June 30, 2018, we were in compliance with the covenants under this facility.

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Off-Balance Sheet Arrangements

We are not a party to any off-balance sheet arrangements other than with respect to our properties located in Lakemoor and Wheaton, Illinois and Beachwood, Ohio. These properties are ground leases improved by multi-family properties and generated $1.9 million of rental income during the six months ended June 30, 2018. At June 30, 2018, our maximum exposure to loss with respect to these properties is $34.0 million, representing the carrying value of the land; such leasehold positions are subordinate to an aggregate of $158.2 million of mortgage debt incurred by our tenants, the owner/operators of the multi-family properties. These owner/operators are affiliated with one another. We do not believe this type of off-balance sheet arrangement has been or will be material to our liquidity and capital resource positions. See Note 6 to our consolidated financial statements for additional information regarding these arrangements.

Funds from Operations and Adjusted Funds from Operations

We compute funds from operations, or FFO, in accordance with the White Paper on Funds From Operations issued by the National Association of Real Estate Investment Trusts (NAREIT) and NAREIT s related guidance. FFO is defined in the White Paper as net income (computed in accordance with generally accepting accounting principles), excluding gains (or losses) from sales of property, plus real estate depreciation and amortization (including amortization of deferred leasing costs), plus impairment write-downs of depreciable real estate and after adjustments for unconsolidated partnerships and joint ventures. Adjustments for unconsolidated partnerships and joint ventures will be calculated to reflect funds from operations on the same basis. In computing FFO, we do not add back to net income the amortization of costs in connection with our financing activities or depreciation of non-real estate assets. We compute adjusted funds from operations, or AFFO, by adjusting from FFO for our straight-line rent accruals and amortization of lease intangibles, deducting lease termination fees and gain on extinguishment of debt and adding back amortization of restricted stock compensation, amortization of costs in connection with our financing activities (including our share of our unconsolidated joint ventures) and debt prepayment costs. Since the NAREIT White Paper does not provide guidelines for computing AFFO, the computation of AFFO may vary from one REIT to another.

We believe that FFO and AFFO are useful and standard supplemental measures of the operating performance for equity REITs and are used frequently by securities analysts, investors and other interested parties in evaluating equity REITs, many of which present FFO and AFFO when reporting their operating results. FFO and AFFO are intended to exclude GAAP historical cost depreciation and amortization of real estate assets, which assumes that the value of real estate assets diminish predictability over time. In fact, real estate values have historically risen and fallen with market conditions. As a result, we believe that FFO and AFFO provide a performance measure that when compared year over year, should reflect the impact to operations from trends in occupancy rates, rental rates, operating costs, interest costs and other matters without the inclusion of depreciation and amortization, providing a perspective that may not be necessarily apparent from net income. We also consider FFO and AFFO to be useful to us in evaluating potential property acquisitions.

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FFO and AFFO do not represent net income or cash flows from operations as defined by GAAP. FFO and AFFO and should not be considered to be an alternative to net income as a reliable measure of our operating performance; nor should FFO and AFFO be considered an alternative to cash flows from operating, investing or financing activities (as defined by GAAP) as measures of liquidity. FFO and AFFO do not measure whether cash flow is sufficient to fund all of our cash needs, including principal amortization, capital improvements and distributions to stockholders.

Management recognizes that there are limitations in the use of FFO and AFFO. In evaluating our performance, management is careful to examine GAAP measures such as net income and cash flows from operating, investing and financing activities.

The table below provides a reconciliation of net income in accordance with GAAP to FFO and AFFO for the periods indicated (dollars in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
GAAP net income attributable to One Liberty Properties, Inc.	$ 4,517	$ 9,972	$ 10,368	$ 12,837
Add: depreciation and amortization of properties	5,165	5,111	10,263	10,585
Add: our share of depreciation and amortization of unconsolidated joint ventures	191	219	407	441
Add: amortization of deferred leasing costs	85	79	169	158
Deduct: gain on sale of real estate		(6,568)	(2,408)	(6,568)
Deduct: equity in earnings from sale of unconsolidated joint venture property	(71)		(71)	
Adjustments for non-controlling interests	(27)	(35)	722	(69)
NAREIT funds from operations applicable to common stock	9,860	8,778	19,450	17,384
Deduct: straight-line rent accruals and amortization of lease intangibles	(499)	(218)	(1,025)	(404)
Add: our share of straight-line rent accruals and amortization of lease intangibles of unconsolidated joint ventures	10	8	20	16
Add: amortization of restricted stock compensation	856	915	1,682	1,657
Add: amortization and write-off of deferred financing costs	222	227	449	454
Add: our share of amortization and write-off of deferred financing costs of unconsolidated joint ventures	6	6	12	13
Adjustments for non-controlling interests	12	3	26	8
Adjusted funds from operations applicable to common stock	$ 10,467	$ 9,719	$ 20,614	$ 19,128

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The table below provides a reconciliation of net income per common share (on a diluted basis) in accordance with GAAP to FFO and AFFO:

	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Six Months Ended June 30, 2018	Six Months Ended June 30, 2017
GAAP net income per common share attributable to One Liberty Properties, Inc.	$ .23	$ .54	$ .53	$ .69
Add: depreciation and amortization of properties	.27	.27	.54	.57
Add: our share of depreciation and amortization of unconsolidated joint ventures	.01	.01	.02	.02
Add: amortization of deferred leasing costs			.01	.01
Deduct: gain on sale of real estate		(.35)	(.13)	(.35)
Deduct: equity in earnings from sale of unconsolidated joint venture property				
Adjustments for non-controlling interests			.04	
NAREIT funds from operations per share of common stock	.51	.47	1.01	.94
Deduct: straight-line rent accruals and amortization of lease intangibles	(.03)	(.01)	(.05)	(.02)
Add: our share of straight-line rent accruals and amortization of lease intangibles of unconsolidated joint ventures				
Add: amortization of restricted stock compensation	.05	.05	.09	.09
Add: amortization and write-off of deferred financing costs	.01	.01	.02	.02
Add: our share of amortization and write-off of deferred financing costs of unconsolidated joint ventures				
Adjustments for non-controlling interests				
Adjusted funds from operations per share of common stock	$ .54	$ .52	$ 1.07	$ 1.03

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our primary market risk exposure is the effect of changes in interest rates on the interest cost of draws on our revolving variable rate credit facility and the effect of changes in the fair value of our interest rate swap agreements. Interest rates are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control.

We use interest rate swaps to limit interest rate risk on variable rate mortgages. These swaps are used for hedging purposes-not for speculation. We do not enter into interest rate swaps for trading purposes. At June 30, 2018, our aggregate liability in the event of the early termination of our swaps was $126,000.

At June 30, 2018, we had 29 interest rate swap agreements outstanding (including one held by an unconsolidated joint venture). The fair market value of the interest rate swaps is dependent upon existing market interest rates and swap spreads, which change over time. As of June 30, 2018, if there had been an increase of 100 basis points in forward interest rates, the fair market value of the interest rate swaps would have increased by approximately $6.7 million and the net unrealized gain on derivative instruments would have increased by $6.7 million. If there were a decrease of 100 basis points in forward interest rates, the fair market value of the interest rate swaps would have decreased by approximately $7.2 million and the net unrealized

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gain on derivative instruments would have decreased by $7.2 million. These changes would not have any impact on our net income or cash.

Our mortgage debt, after giving effect to interest rate swap agreements, bears interest at fixed rates and accordingly, the effect of changes in interest rates would not impact the amount of interest expense that we incur under these mortgages.

Our variable rate credit facility is sensitive to interest rate changes. At June 30, 2018, a 100 basis point increase of the interest rate on this facility would increase our related interest costs over the next twelve months by approximately $203,000 and a 100 basis point decrease of the interest rate would decrease our related interest costs over the next twelve months by approximately $203,000.

The fair market value of our long-term debt is estimated based on discounting future cash flows at interest rates that our management believes reflect the risks associated with long term debt of similar risk and duration.

Item 4. Controls and Procedures

Based on their evaluation as of the end of the period covered by this report, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act)) are effective.

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) promulgated under the Exchange Act) during the three months ended June 30, 2018 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Part II - OTHER INFORMATION

Item 6. Exhibits

Exhibit No.	Title of Exhibit
10.1	Form of Performance Award Agreement granted July 2018.
31.1	Certification of President and Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Senior Vice President and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of President and Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Senior Vice President and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Definition Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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ONE LIBERTY PROPERTIES, INC.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	ONE LIBERTY PROPERTIES, INC. (Registrant)
Date: August 6, 2018	/s/ Patrick J. Callan, Jr. Patrick J. Callan, Jr. President and Chief Executive Officer (principal executive officer)
Date: August 6, 2018	/s/ David W. Kalish David W. Kalish Senior Vice President and Chief Financial Officer (principal financial officer)