

SCOTIA CAPITAL (USA) INC.
(A Wholly Owned Subsidiary of Scotia Holdings (US) Inc.)

Statement of Financial Condition

October 31, 2019

(With Report of Independent Registered Public Accounting Firm Thereon)



KPMG LLP
345 Park Avenue
New York, NY 10154-0102

Report of Independent Registered Public Accounting Firm

To the Stockholder and the Board of Directors
Scotia Capital (USA) Inc.:

Opinion on the Financial Statement

We have audited the accompanying statement of financial condition of Scotia Capital (USA) Inc. (a wholly owned subsidiary of Scotia Holdings (US) Inc.) (the Company) as of October 31, 2019, and the related notes (collectively, the financial statement). In our opinion, the financial statement presents fairly, in all material respects, the financial position of the Company as of October 31, 2019, in conformity with U.S. generally accepted accounting principles.

Basis for Opinion

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

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

KPMG LLP

We have served as the Company's auditor since 1988.

New York, New York
December 27, 2019

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(dollars in thousands, except share and per share amounts)

Assets	
Cash and cash equivalents	\$ 39,704
Cash on deposit with clearing organizations	165,659
Securities segregated under federal and other regulations, at fair value	342,577
Deposits paid for securities borrowed	17,346,350
Securities received as collateral, at fair value	6,052,462
Securities owned, at fair value (including \$461,092 pledged to creditors)	977,120
Receivable from brokers, dealers, and clearing organizations	246,717
Receivable from customers	14,203
Accrued fees, interest, and other receivables	87,998
Furniture, equipment, and leasehold improvements, at cost, net of accumulated depreciation and amortization of \$1,867	2,912
Goodwill	72,305
Other assets	34,273
Total assets	\$ 25,382,280
Liabilities and Stockholder's Equity	
Liabilities:	
Deposits received for securities loaned	\$ 10,718,069
Obligation to return securities received as collateral, at fair value	6,052,462
Securities sold under agreements to repurchase	5,500,000
Bank loan payable	277,292
Payable to customers	305,530
Payable to brokers, dealers, and clearing organizations	84,337
Securities sold, not yet purchased, at fair value	905,879
Accounts payable, accrued expenses, and other liabilities	163,386
Total liabilities	24,006,955
Commitments and contingencies (see Note 9)	
Stockholder's equity:	
Common stock par value, \$10 per share. Authorized, issued, and outstanding 3,000 shares	30
Additional paid-in capital	747,469
Retained earnings	627,826
Total stockholder's equity	1,375,325
Total liabilities and stockholder's equity	\$ 25,382,280

See accompanying notes to statement of financial condition.

SCOTIA CAPITAL (USA) INC.
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(1) Organization

Scotia Capital (USA) Inc. (the Company) is a wholly owned subsidiary of Scotia Holdings (US) Inc. (the Parent), whose ultimate parent is The Bank of Nova Scotia, a Canadian bank chartered under the *Bank Act* (Canada). The Company is a registered broker-dealer with the U.S. Securities and Exchange Commission (SEC) under the Securities Exchange Act of 1934 and is a member of the Financial Industry Regulatory Authority (FINRA), the Securities Investor Protection Corporation (SIPC), the Options Clearing Corp (OCC), the New York Stock Exchange (NYSE) as well as other exchanges. The Company is also a registered futures commission merchant with the Commodity Futures Trading Commission (CFTC) and a member of the National Futures Association (NFA). The Company's primary business activities include debt and equity securities underwriting, fixed income sales and trading, equity sales and trading, securities borrowing and lending, repurchase agreement activities, investment banking, and equity research. The Company's customers and counterparties comprise a diverse group of domestic and foreign corporations, governments, and institutional investors.

(2) Summary of Significant Accounting Policies

(a) Basis of Presentation

The Company's statement of financial condition is prepared in accordance with U.S. Generally Accepted Accounting Principles (U.S. GAAP), which requires management to make estimates and assumptions that may affect the amounts reported in the statement of financial condition and accompanying notes. These estimates and the underlying assumptions affect the amounts of assets and liabilities reported, and disclosures about contingent assets and liabilities. Such estimates, including the fair value of financial instruments, goodwill, and litigation reserves are, by their nature, based on judgment and available information and, therefore, may vary from actual results. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. The Company adjusts such estimates and assumptions when facts and circumstances dictate.

(b) Cash and Cash Equivalents

Cash and cash equivalents include demand deposits held in banks with original maturities of 90 days or less.

(c) Cash on Deposit with Clearing Organizations

The Company is a member of various clearing organizations and exchanges at which it maintains cash required for the conduct of its day-to-day clearing activities. Cash on deposit with clearing organizations is considered restricted cash by the Company.

(d) Collateralized Financing Transactions

Securities borrowed and securities loaned transactions are reported as collateralized financings. Securities borrowed and loaned transactions are entered into with other broker-dealers or financial institutions and are recorded at the amount of cash collateral advanced or received. Securities borrowed transactions require the Company to deposit cash with the lender and are reflected in the statement of financial condition as Deposits paid for securities borrowed. With respect to securities loaned, the Company receives collateral in the form of cash in an amount in excess of the market value of securities loaned and is reflected in the statement of financial condition as Deposits received for securities loaned. The Company also acts as a securities lender in transactions where it receives securities collateral that can be pledged or sold and such transactions are reflected in the statement

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of financial condition as Securities received as collateral, at fair value with a corresponding obligation to return those securities reflected in Obligation to return securities received as collateral, at fair value. The Company monitors the market value of securities borrowed and loaned on a daily basis, with additional collateral obtained, posted, or refunded as necessary.

Securities sold under agreements to repurchase are also treated as collateralized financing transactions. The agreements provide that the transferor will receive substantially the same securities in return at the maturity of the agreement and that the transferor will obtain from the transferee sufficient cash or collateral to purchase such securities during the term of the agreement. The liabilities which result from these agreements are initially recognized at amortized cost in the accompanying statement of financial condition.

(e) *Securities Owned, Securities Sold, Not Yet Purchased at Fair Value*

Securities owned and securities sold, not yet purchased are recorded at fair value.

Amounts receivable and payable for regular-way securities transactions that have not yet reached their contractual settlement date are recorded net on the statement of financial condition in receivable or payable from broker, dealers, and clearing organizations.

(f) *Receivable from and Payables to Customers*

Receivables from and payables to customers include amounts due on cash and margin transactions, including balances related to futures transactions. Securities owned by customers, including those that collateralize margin or other similar transactions, are not reflected on the statement of financial condition.

(g) *Receivable and Payable – Brokers, Dealers, and Clearing Organizations*

Receivables from brokers, dealers and clearing organization include amounts receivable for securities failed to deliver by the Company to a purchaser by the settlement date, margin deposits, commissions, and balances related to futures transactions. Payable to brokers, dealers, and clearing organizations include amounts payable for securities failed to receive by the Company from a seller by the settlement date and also include balances related to futures transactions. Brokers, dealers, and clearing organization receivables and payables additionally include net receivables or net payables arising from unsettled regular-way transactions.

(h) *Income Taxes*

Income taxes are accounted for under the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as the estimated future tax consequences attributable to net operating losses and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to be applied to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date. If appropriate, deferred tax assets are adjusted by a valuation allowance, which reflects expectations to the extent which such assets will be realized.

The Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that

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is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs.

(i) ***Furniture, Equipment, and Leasehold Improvements***

Following is a summary of the carrying value and accumulated depreciation of furniture, equipment, and leasehold improvements at October 31, 2019:

(dollars in thousands)

	Accumulated Depreciation	Carrying Value
Furniture and Equipment	\$ 1,257	742
Leasehold Improvements	610	2,170
	\$ 1,867	2,912

(j) ***Goodwill***

Goodwill is the excess of purchase price over the fair value of net identifiable assets acquired. Goodwill is reviewed for impairment annually, or whenever events or circumstances suggest that it may be more likely than not the fair value of the reporting unit is below its carrying amount. Goodwill impairment tests may involve judgments in determining the estimate of future cash flows, discount rates, long-term growth rates, economic forecasts, similar guideline companies, control premiums, and other assumptions.

The Company performed its goodwill impairment test as of June 30, 2019 and qualitatively determined that there was no impairment. The carrying amount of goodwill was \$72.3 million at October 31, 2019.

(k) ***Accounting Standards***

Recently Adopted

ASU 2016-01, Financial Instruments – Overall – Recognition and Measurement of Financial Assets and Financial Liabilities

Effective November 1, 2018 the Company adopted a new accounting standard for recognition and measurement of financial assets and financial liabilities. The standard made targeted updates to the accounting for equity instruments, and the presentation and disclosure requirements for financial instruments. The new standard did not have a material impact on the Company's financial position.

Recently Issued

ASU 2016-02, Leases

In February 2016, the FASB issued a new lease accounting standard that requires lessees to recognize operating leases in the balance sheet resulting in the recognition of a right-of-use asset and a lease liability. On November 1, 2019, the Company adopted the standard using the modified retrospective approach. Upon adoption, the right-of-use asset and lease liability was determined based on the present value of the remaining minimum lease payments resulting in the recognition of right-of-use assets and lease liabilities. The new standard did not have a material impact on the Company's financial position.

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ASU 2016-13, Financial Instruments – Credit Losses

In June 2016, the FASB issued a new accounting update that impacts the impairment model for certain financial assets measured at amortized cost by requiring a current expense credit loss (CECL) methodology to estimate expected credit losses over the entire life of the financial asset, recoded at inception or purchase. CECL will replace the current incurred loss model. We are currently evaluating the effects of the new standard and expect the impact will primarily result from collateralized financing transactions, margin loans and other receivables measured at amortized cost. The amendments in this update are effective for the Company on November 1, 2020.

(3) Related-Party Transactions

The Company has financing transactions with affiliates and The Bank of Nova Scotia, loans with The Bank of Nova Scotia, and other arrangements with The Bank of Nova Scotia. For further information refer to the Collateralized Financing Transactions (Note 5), Credit Facility (Note 6), Subordinated Borrowings (Note 7) and Commitment and Contingencies (Note 9) notes herein.

Included in the accompanying statement of financial condition are the following related party balances:

(dollars in thousands)

<u>Description</u>	<u>Total</u>
<u>Assets</u>	
Cash and cash equivalents	\$ 1,738
Deposits paid for securities borrowed	10,902,982
Securities received as collateral, at fair value	11,459
Securities owned, at fair value	13,157
Receivable from brokers, dealers, and clearing organizations	22,901
Receivable from customers	1,676
Accrued fees, interest and other receivables	31,332
Total	\$ 10,985,245

(dollars in thousands)

<u>Description</u>	<u>Total</u>
<u>Liabilities</u>	
Deposits received for securities loaned	\$ 4,325,303
Obligation to return securities received as collateral, at fair value	11,459
Securities sold, not yet purchased, at fair value	71,316
Bank loan payable	277,292
Payable to customers	240,779
Payable to brokers, dealers, and clearing organizations	2,884
Accounts payable, accrued expenses, and other liabilities	33,732
Total	\$ 4,962,765

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(4) Receivable From and Payable to Brokers, Dealers, and Clearing Organizations

Amounts receivable from and payable to brokers, dealers, and clearing organizations at October 31, 2019 consist of the following:

(dollars in thousands)

	<u>Receivable</u>	<u>Payable</u>
Receivable from/payable to clearing organizations	\$ 148,895	—
Receivable from/payable to brokers and dealers	49,179	43,366
Securities failed-to-deliver/receive	48,643	29,072
Unsettled regular-way transactions, net	—	11,899
	<u>\$ 246,717</u>	<u>84,337</u>

(5) Collateralized Financing Transactions

The Company enters into collateralized financing transactions to meet customers' needs, settle other securities obligations and finance its inventory positions.

To maintain reliable funding under a wide range of market conditions, including under periods of stress, the Company manages these activities by taking into consideration the quality of the underlying collateral, and stipulating financing tenor. Additionally, the Company manages liquidity risk related to these transactions by maintaining counterparty diversification through assessing counterparty reliability and stability under stress. It is the Company's policy to have a perfected, first priority security interest over the underlying collateral, monitor its market value relative to the amounts due under the agreements and, when necessary, require prompt transfer of additional collateral in order to maintain contractual margin protection.

For repurchase agreements, when necessary, the Company posts additional collateral in order to maintain contractual margin protection. With respect to securities loaned, the Company receives cash and securities collateral in an amount generally in excess of the market value of the securities loaned. The Company monitors the market value of securities borrowed and securities loaned on a daily basis and obtains or posts additional collateral in order to maintain contractual margin protection.

Collateralized financing transactions are documented under industry standard agreements that allow the prompt close-out of all transactions (including the liquidation of securities held) and the offsetting of obligations to return cash or securities by the non-defaulting party, following a payment default or other type of default under the relevant master agreement. The counterparty that receives the securities in these transactions is generally unrestricted in its use of the securities, with the exception of transactions executed on a tri-party basis, where the collateral is maintained by a custodian. At October 31, 2019, the approximate fair value of securities collateral accepted and securities borrowed by the Company was \$23.4 billion, of which \$16.9 billion was sold or repledged.

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Offsetting of Certain Financing Transactions

As of October 31, 2019 (dollars in thousands)

	Gross Amounts	Amounts Offset	Net Amounts Presented	Financial Instruments ¹	Net Amounts
Deposits paid for securities borrowed	\$ 17,346,350	-	17,346,350	(16,754,660)	591,690
Securities received as collateral, at fair value	6,052,462	-	6,052,462	(6,052,462)	-
Total	\$ 23,398,812	-	23,398,812	(22,807,122)	591,690

As of October 31, 2019 (dollars in thousands)

	Gross Amounts	Amounts Offset	Net Amounts Presented	Financial Instruments ¹	Net Amounts
Securities sold under agreements to repurchase	\$ 5,500,000	-	5,500,000	(4,445,000)	1,055,000
Deposits received for securities loaned	10,718,069	-	10,718,069	(10,471,448)	246,621
Obligation to return securities received as collateral, at fair value	6,052,462	-	6,052,462	(6,052,462)	-
Total	\$ 22,270,531	-	22,270,531	(20,968,910)	1,301,621

¹ Amount includes securities collateral received or pledged subject to a legally enforceable master netting agreement. Although shown as a reduction to Net Amounts Presented they are not offset in the statement of financial condition. Amount does not include securities collateral received or pledged where the legal enforceability of the master netting agreement is uncertain.

Maturities and Collateral Pledged

Gross Financing Transaction Balances by Remaining Contractual Maturity

As of October 31, 2019 (dollars in thousands)

	Overnight and Continuous	Up to 30 Days	31-90 Days	Greater than 90 Days ¹	Total
Securities sold under agreements to repurchase	\$ 4,415,000	85,000	700,000	300,000	5,500,000
Deposits received for securities loaned	10,456,860	261,209	-	-	10,718,069
Obligation to return securities received as collateral, at fair value	6,052,462	-	-	-	6,052,462
Total	\$ 20,924,322	346,209	700,000	300,000	22,270,531

¹ Remaining contractual maturity is less than one year.

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Gross Financing Transaction Balances by Class of Collateral Pledged

As of October 31, 2019 (dollars in thousands)

	Securities sold under agreements to repurchase	Deposits received for securities loaned	Obligation to return securities received as collateral, at fair value	Total
U.S. and Canadian government obligations	\$ -	563,776	1,153,195	1,716,971
Corporate debt obligations	2,721,752	1,152,133	50,295	3,924,180
Common stock	2,774,043	9,002,160	4,848,972	16,625,175
Other foreign government obligations	4,205	-	-	4,205
Total	\$ 5,500,000	10,718,069	6,052,462	22,270,531

(6) Credit Facility

The Company has established borrowing agreements with The Bank of Nova Scotia in the normal course of business. Amounts outstanding under these arrangements are included within Bank loan payable. The arrangements are summarized below:

A \$600 million 12-month revolving senior unsecured line of credit. Interest on the line of credit is based on prevailing short-term market rates. The credit line matures on March 25, 2020, but may be renewed by the Company for an additional 364 days upon written notice to The Bank of Nova Scotia at least 91 days prior to the expiration date. At October 31, 2019, \$117 million was outstanding on the line of credit.

A \$500 million 12-month revolving senior unsecured line of credit. Interest on the line of credit is based on prevailing short-term market rates. The credit line matures on March 26, 2020, but may be renewed by the Company for an additional 364 days upon written notice to The Bank of Nova Scotia at least 91 days prior to the expiration date. At October 31, 2019, \$14 million was outstanding on the line of credit.

A \$1.05 billion overnight overdraft line of credit. Interest on the line of credit is based on prevailing short-term market rates. The Bank of Nova Scotia reserves the right to withdraw the line with 91 days prior written notice. At October 31, 2019, \$146 million was outstanding on the line of credit.

A \$1.5 billion 31 day evergreen revolving senior unsecured line of credit. Interest on the line of credit is based on prevailing short-term market rates. The credit line matures on June 25, 2020, but may be renewed by the Company for an additional 364 days upon written notice to The Bank of Nova Scotia at least 60 days prior to the expiration date. At October 31, 2019, no borrowings were outstanding on the line of credit.

A CAD\$100 million 12-month revolving senior unsecured line of credit. Interest on the line of credit is based on prevailing short-term market rates. The credit line matures on August 13, 2020 if The Bank of Nova Scotia gives written notice of termination at least 60 days prior to the expiration, otherwise the term of the Agreement shall automatically renew for an additional 364 days. At October 31, 2019, no borrowings were outstanding on the line of credit.

(7) Subordinated Borrowings

The Company has a revolving note and cash subordination agreement (the note) with The Bank of Nova Scotia amounting to \$1.2 billion. The note, which has been approved for regulatory capital purposes, bears

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a market rate (LIBOR plus a market-based spread) of interest on the amount drawn and is scheduled to mature on October 31, 2022. No borrowings were outstanding at October 31, 2019.

(8) Employee Benefit and Incentive Plans

The Company participates in defined contribution, defined benefit, postretirement benefit plans and incentive plans provided by The Bank of Nova Scotia.

Defined Contribution Plan

The Company participates in a 401(k) salary deferral and profit sharing plan sponsored by The Bank of Nova Scotia (the 401(k) plan) covering eligible employees. Employees are permitted within limitations imposed by tax law to make pretax contributions to the 401(k) plan pursuant to salary reduction agreements. The Company matches the employee's contributions up to a maximum of 4.5% of the employee's salary.

Defined Benefit and Postretirement Benefit Plans

The Company participates in defined benefit and postretirement benefit plans sponsored by The Bank of Nova Scotia. The defined benefit expense covering the employees of the Company is recorded by The Bank of Nova Scotia and allocated to the Company.

Incentive Plans

The Company participates in incentive plans sponsored by The Bank of Nova Scotia. The expense covering the employees of the Company is recorded by The Bank of Nova Scotia and allocated to the Company.

(9) Commitments and Contingencies

The Bank of Nova Scotia provides the Company with office space in New York, Houston, San Francisco, and Boston. The Company also leases office space in New Orleans under an operating lease.

The Company's future minimum obligation under the aforementioned arrangements as of October 31, 2019 is as follows:

<i>(dollars in thousands)</i>		
2020	\$	7,608
2021		7,650
2022		7,673
2023		7,709
2024		7,226
Thereafter		10,581
	\$	<u>48,447</u>

The Company provides representations and warranties to counterparties in connection with a variety of commercial transactions and occasionally indemnifies them against potential losses caused by the breach of those representations and warranties. These indemnifications generally are standard contractual terms and are entered into in the normal course of business. The maximum potential amount of future payments that the Company could be required to make under these indemnifications cannot be estimated. However,

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the Company believes that it is unlikely it will have to make material payments under these arrangements and has not recorded any contingent liability in the statement of financial condition for these indemnifications.

The Company is a member of various exchanges that trade and clear securities or futures contracts or both. Associated with its membership, the Company may be required to pay a proportionate share of the financial obligations of another member who may default on its obligations to the exchange. Although the rules governing different exchange memberships vary, in general the Company's guarantee obligations would arise only if the exchange had previously exhausted its resources. In addition, any such guarantee obligation would be apportioned among the other non-defaulting members of the exchange. Any potential contingent liability under these membership agreements cannot be estimated. The Company has not recorded any contingent liability in the statement of financial condition for these agreements and believes that any potential requirement to make payments under these agreements is remote.

In the normal course of business, the Company, from time to time, may be named as a defendant in litigation actions, including actions relating to its underwriting business. The Company is also subject to various governmental and regulatory examinations and information-gathering requests. Where available information indicates that it is probable a liability had been incurred at the date of the statement of financial condition and the Company can reasonably estimate the amount of that loss, the Company accrues an estimated loss. After reviewing these actions with its counsel, management does not believe that the outcome of such actions will have any material effect on its financial position.

(10) Regulatory Requirements

The Company is a registered broker-dealer and registered futures commission merchant and, accordingly, is subject to the net capital requirements of SEC Rule 15c3-1 (SEC Net Capital Rule), FINRA, and Regulation 1.17 of the Commodity Exchange Act (CFTC Rule). The Company has elected to use the alternative method permitted by the SEC Net Capital Rule, which requires that it maintain minimum net capital of the greater of \$1,500,000 or 2% of aggregate debit items arising from customer transactions, plus excess margin collateral on reverse repurchase agreements or the CFTC Rule requirement representing the sum of 8% of customer risk maintenance margin requirement and 8% of non-customer risk maintenance margin requirement, as defined.

FINRA may require a member firm to reduce its business if net capital is less than 4% of such aggregate debit items and may prohibit a firm from expanding its business if net capital is less than 5% of such aggregate debit items. In addition, the Company is subject to certain notification requirements related to withdrawals of excess net capital. At October 31, 2019, the Company's net capital was \$881.6 million which was \$794.2 million in excess of its required net capital of \$87.4 million as of October 31, 2019.

(11) Income Taxes

The Company provides for income taxes in accordance with the asset and liability method of accounting and recognizes deferred income taxes for the expected future tax consequences of differences in the book and tax basis of assets and liabilities.

At October 31, 2019, the deferred tax assets of \$9.7 million were composed of temporary differences due to deferred compensation accruals and post retirement expenses. As of October 31, 2019, management has not recorded a valuation allowance against its deferred tax assets as management believes it is more likely than not that they will be realized through future taxable earnings.

At October 31, 2019 the deferred tax liability of \$9.6 million was composed of temporary differences principally due to the tax effect of non-depreciable goodwill.

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The Tax Cuts and Jobs Act (Tax Act), was enacted on December 22, 2017. As part of the Tax Act, the Company was subject to the new 21% corporate tax rate as of January 1, 2018. The Company has evaluated the significant provisions of the law and has not identified any material impact these provisions had on the Company for the year ended October 31, 2019. The Company will continue to monitor the application of these provisions and make necessary policy elections if and when needed.

The Company remains open to Federal, California, New York State, Louisiana, Texas, Massachusetts, New Jersey and New York City examinations for the years ended October 31, 2016 and forward. The Company does not anticipate any settlements that would result in a material change to the statement of financial condition.

The reconciliation of the beginning unrecognized tax benefits balance to the ending balance is presented below.

(dollars in thousands)

Balance at October 31, 2018	\$	1,587
Increases related to prior year tax positions		317
Decreases related to prior year tax positions		(698)
Increases related to current year tax positions		112
Settlements		-
Lapse of statute		(65)
Balance at October 31, 2019	\$	1,253

(12) Fair Value Measurements

Fair value 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.

In determining fair value, the Company uses various valuation techniques and establishes a hierarchy for inputs used in measuring fair value.

The Company’s securities owned, securities segregated under federal and other regulations, securities received as collateral, securities sold, but not yet purchased, and obligation to return securities received as collateral are recorded at fair value on a recurring basis.

Fair Value Hierarchy

The fair value hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure an asset or a liability fall to different levels within the hierarchy, the classification of the entire asset or liability will be based on the lowest level input that is significant to the overall fair value measurement of the asset or liability. The Company categorizes assets and liabilities based on the inputs to the valuation techniques used to measure fair value 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.

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Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions would reflect the Company’s 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.

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 October 31, 2019:

(dollars in thousands)

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Assets:				
U.S. and Canadian government obligations	\$ 46,810	-	-	46,810
Corporate debt obligations	-	855,704	-	855,704
Common and preferred stock	8,705	16,466	-	25,171
Other foreign government obligations	-	49,435	-	49,435
Total securities owned	<u>55,515</u>	<u>921,605</u>	<u>-</u>	<u>977,120</u>
Securities segregated under				
federal and other regulations	342,577	-	-	342,577
Securities received as collateral	<u>6,002,167</u>	<u>50,295</u>	<u>-</u>	<u>6,052,462</u>
Total assets at fair value	<u>\$ 6,400,259</u>	<u>971,900</u>	<u>-</u>	<u>7,372,159</u>
Liabilities:				
U.S. and Canadian government obligations	\$ 69,825	-	-	69,825
Corporate debt obligations	-	486,539	-	486,539
Common and preferred stock	322,945	-	-	322,945
Other foreign government obligations	-	26,570	-	26,570
Total securities sold, not yet purchased	<u>392,770</u>	<u>513,109</u>	<u>-</u>	<u>905,879</u>
Obligation to return securities				
received as collateral	<u>6,002,167</u>	<u>50,295</u>	<u>-</u>	<u>6,052,462</u>
Total liabilities at fair value	<u>\$ 6,394,937</u>	<u>563,404</u>	<u>-</u>	<u>6,958,341</u>

The fair value of the Company’s securities was determined using a variety of sources as follows:

For Common and preferred stock, fair value was determined by the closing price of the primary exchanges and is included in Level 1 and from observable trades and/or external quotes for those included in Level 2.

For U.S. and Canadian government obligations, fair value was determined based on quoted prices in active markets and are included in Level 1.

For Corporate debt obligations and Other foreign government obligations, fair value was determined using prices from independent market data providers or third party broker quotes and are included in Level 2.

For Securities received as collateral and the Obligation to return securities received as collateral, fair value was determined by the closing price of the primary exchanges for those included in Level 1 and from third party broker quotes for those included in Level 2.

Securities segregated under federal and other regulations are comprised of U.S. government obligations. Fair value was determined based on quoted prices in active markets and are included in Level 1.

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There were no transfers in or out of Levels 1, 2 or 3.

Financial Instruments Not Measured at Fair Value

The carrying value approximates fair value for the following financial instruments: cash and cash equivalents, cash on deposits with clearing organizations, deposits paid for securities borrowed, receivables and payables from brokers, dealers, clearing organizations and customers, deposits received for securities loaned, securities sold under agreements to repurchase, and bank loan payables.

Under the fair value hierarchy, cash and cash equivalents and cash on deposit with clearing organizations are classified as Level 1. Deposits paid for securities borrowed, receivables and payables from brokers, dealers, clearing organizations and customers, deposits received for securities loaned, securities sold under agreements to repurchase, accounts payable, accrued expenses, and other liabilities, and bank loan payables are classified as Level 2.

(13) Off-Balance-Sheet Credit Risk

As a securities broker-dealer, the Company is engaged in securities trading and brokerage activities with a diverse group of domestic and foreign corporations, governments, and institutional investors, including other broker-dealers, commercial banks, insurance companies, pension plans, mutual funds, and other financial institutions. The Company's customer securities activities are generally processed on a delivery versus payment and receipt versus payment (DVP/RVP) basis. The Company records these transactions on a settlement-date basis, which is generally one business day for U.S. government securities transactions and three business days for equity and debt securities transactions.

As a result, the Company is exposed to risk of loss on these transactions in the event of the customer's inability to meet the terms of the contracts, in which case, the Company may be required to purchase or sell the underlying securities at prevailing market prices. In connection with the Company's customer and proprietary financing and securities settlement activities, the Company pledges securities as collateral in support of various secured financing sources such as bank loans and securities loaned. In the event the counterparty is unable to meet its contracted obligation to return securities pledged as collateral, the Company may be exposed to the risk of acquiring securities at prevailing market prices in order to satisfy its obligations. The Company controls this risk by monitoring the market value of securities pledged on a daily basis and by requiring adjustments of collateral levels in the event of excess market exposure. At October 31, 2019, the market value of securities pledged under these secured financing transactions approximated the amount due, which is recorded as Deposits received for securities loaned in the statement of financial condition.

As a securities broker-dealer, the Company is engaged in various securities trading and brokerage activities as principal. In the normal course of business, the Company has sold securities that it does not currently own and will, therefore, be obligated to purchase such securities at a future date. The Company has recorded this \$906 million obligation in the accompanying statement of financial condition at the October 31, 2019 fair value of the related securities. The Company will incur a trading loss on the securities if the market price increases, and a trading gain if the market price decreases subsequent to October 31, 2019. In security sales transactions, the Company is subject to risk if the security is not received and the market value has increased over the contract amount of the transaction.

As a securities broker-dealer, the Company is engaged in various securities trading activities and substantially all of the Company's financial assets and liabilities are carried at or approximate fair value.

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(14) Subsequent Events

The Company has evaluated whether any events or transactions occurred subsequent to the date of the statement of financial condition and through the issuance date of the statement of financial condition.

In December 2019, the Company provided written notice to The Bank of Nova Scotia to extend the \$600 million and \$500 million 12-month revolving senior unsecured lines of credit.

In December 2019, the Company borrowed \$250 million under its subordinated line of credit with The Bank of Nova Scotia.

There were no other material events or transactions that would require recognition or disclosure in the statement of financial condition.