

The following table sets forth the plans' funded status and amounts recognized in the balance sheets at December 31:

	PENSION BENEFITS		OTHER POSTRETIREMENT BENEFITS	
	2002	2001	2002	2001
<b>CHANGE IN BENEFIT OBLIGATION</b>				
Benefit obligation at beginning of year	\$ 159,189	\$ 143,235	\$ 801	\$ -
Service cost	17,744	15,747	52	43
Interest cost	11,830	10,432	55	51
Amendments	1,587	1,659	-	-
Actuarial losses	12,321	(2,724)	(50)	-
Benefits paid	(22,794)	(11,877)	-	(17)
Curtailment/settlement gain	-	(1,301)	-	-
Loss due to change in discount rate	14,870	4,320	82	35
Other benefits/changes	987	(302)	-	689
Benefit obligation at end of year	\$ 195,734	\$ 159,189	\$ 940	\$ 801
<b>CHANGE IN PLAN ASSETS</b>				
Fair value of plan assets at beginning of year	\$ 102,247	\$ 100,743	\$ -	\$ -
Transfers between related parties	960	(462)	-	-
Actual return on plan assets	(12,708)	2,210	-	-
Company contributions	23,290	11,633	-	17
Participant contributions	-	-	-	-
Benefits paid	(22,794)	(11,877)	-	(17)
Fair value of plan assets at end of year	90,995	102,247	-	-
Funded status of the plan (underfunded)	(104,739)	(56,942)	\$ (940)	\$ (801)
Unrecognized net actuarial loss	62,373	15,580	64	35
Unrecognized prior service cost	3,829	3,258	-	-
Unrecognized transition obligation/(asset)	(1,038)	(1,252)	613	651
Amount recognized to reflect minimum liability	(4,341)	(3,425)	-	-
Net accrued benefit cost recorded in the consolidated balance sheets	\$ (43,916)	\$ (42,781)	\$ (263)	\$ (115)

## 2002 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in tables in thousands)

The net accrued pension cost as of December 31, 2002, as reflected above, consists of the accrued benefit cost from the underfunded ERP plans and the unfunded SERP.

The components of the accrued benefit cost for the Company's defined benefit pension plans as of December 31, 2002, and 2001 along with the location of these amounts in the consolidated balance sheets were as follows:

	DECEMBER 31,	
	2002	2001
ERP – included in accrued personnel costs	\$ (10,989)	\$ (4,344)
ERP – included in accrued pension and other postretirement benefit costs	(19,125)	(20,292)
SERP – included in accrued pension and other postretirement benefit costs	(13,802)	(18,145)
Accrued benefit costs	<u>\$ (43,916)</u>	<u>\$ (42,781)</u>

As of December 31, 2002 and 2001, the following is the funded status of each of NASD's defined benefit pension plans:

	DECEMBER 31,	
	2002	2001
<b>ERP</b>		
Projected benefit obligations	\$ 178,594	\$ 136,561
Accumulated benefit obligations	100,885	78,182
Fair value of plan assets	90,995	102,247
<b>SERP</b>		
Projected benefit obligations	\$ 17,140	\$ 22,628
Accumulated benefit obligations	13,742	17,600
Fair value of plan assets	-	-

During 2002, there was a settlement of \$1.2 million for employees included within the SERP plan due to early retirements. During 2001, there was a curtailment gain recognized of \$1.3 million in the pension plan to reflect the reduction in force on June 26, 2001.

Pursuant to the provisions of SFAS No. 87 "Employer's Accounting for Pensions," related to the SERP, an intangible asset of \$1.3 million and \$1.0 million, and a net adjustment to members' equity of \$3.1 million and \$1.0 million, were recorded as of December 31, 2002, and 2001, respectively, to recognize a minimum pension liability. Included within the net adjustment to accumulated other comprehensive income (loss) in the accompanying consolidated balance sheets is the portion of minimum pension liabilities from equity method affiliates.

	PENSION BENEFITS		OTHER POSTRETIREMENT BENEFITS	
	2002	2001	2002	2001
<b>WEIGHTED-AVERAGE ASSUMPTIONS</b>				
<b>AS OF DECEMBER 31:</b>				
Discount rate	6.75%	7.25%	6.75%	7.25%
Expected return on plan assets	9.0	9.0	-	-
Rate of increase (compensation or health care cost)	5.5	5.3	5.5	5.5
	PENSION BENEFITS		OTHER POSTRETIREMENT BENEFITS	
	2002	2001	2002	2001
<b>COMPONENTS OF NET PERIODIC BENEFIT COST, YEARS ENDED DECEMBER 31:</b>				
Service cost	\$ 17,744	\$ 15,747	\$ 52	\$ 43
Interest cost	11,830	10,432	55	51
Expected return on plan assets	(9,025)	(8,629)	-	-
Amortization of unrecognized transition asset	(57)	(215)	38	38
Recognized net actuarial (gains) losses	(57)	61	-	-
Prior service cost (income) recognized	947	698	-	-
Curtailment/settlement loss (gain) recognized	3,523	16	-	-
Other benefits/changes	-	760	-	-
Benefit cost (income)	\$ 24,747	\$ 18,870	\$ 145	\$ 132

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*(Dollars in tables in thousands)*

The assumptions for the annual increase in the composite health care cost trend rate are 7.5% and 8% for 2002 and 2001. The health care cost trend rate for 2002 was assumed to decrease gradually to an estimated annual increase of 5% in the year 2007 and thereafter. The assumed health care cost trend rate can have a significant effect on the amounts reported. A one-percentage point change in the assumed health care cost trend rate would not have a material impact on the benefit obligation, service costs and interest components.

The Company also maintains voluntary savings plans for eligible employees of its subsidiaries. Employees are immediately eligible to make contributions to the plan and are also eligible for an employer contribution match at an amount equal to 100% of the first 4% of eligible employee contributions. Eligible plan participants may also receive an additional discretionary match from the Company. Savings plan expense for 2002 and 2001 was \$9.0 million and \$11.7 million, respectively. The expense included a discretionary match totaling \$2.1 million for 2002 and \$2.6 million for 2001.

### 11. NASDAQ STOCK COMPENSATION, STOCK AWARDS AND CAPITAL STOCK

Effective December 5, 2000, as amended on January 23, 2002, NASDAQ adopted The NASDAQ Stock Market, Inc. Equity Incentive Plan (the "Plan"), under which nonqualified and qualified incentive stock options, restricted stock, restricted stock units, or other stock based awards may be granted to employees, directors, officers and consultants. A total of 24.5 million shares are authorized under the Plan. At December 31, 2002, 13.0 million shares were available for future grants under the Plan.

In 2002, NASDAQ granted 2.2 million stock options and 77 thousand shares of restricted stock to employees and officers and 65 thousand options to non-employee Board of Directors members pursuant to the Plan. During 2002, 0.9 million stock options and 49 thousand shares of restricted stock awards were forfeited.

Restricted stock awards are awarded in the name of the employee or officer at fair value on the date of the grant. The awards contain restrictions on sales and transfers, are generally subject to a five-year vesting period and are expensed over the vesting period. NASDAQ recognized \$2.0 million and \$4.1 million in amortization expense related to restricted stock during the years ended December 31, 2002, and December 31, 2001, respectively.

Stock options are granted with an exercise price equal to the estimated fair market value of the stock on the date of the grant. NASDAQ accounts for stock option grants in accordance with APB No. 25, and, accordingly, recognizes no compensation expense related to such grants.

Options granted generally vest over three years and expire 10 years from the date of grant. All options to date have been granted at fair market value on the date of grant. At December 31, 2002, options for 5.3 million shares were vested, and exercisable with a weighted-average exercise price of \$12.77. At December 31, 2001, options for 3.6 million shares were vested, and exercisable with a weighted-average exercise price of \$12.73.

Stock option activity during the year ended December 31, 2002, is set forth below:

	SHARES	PRICE PER SHARE	
		RANGE	WEIGHTED AVERAGE
Balance, January 1, 2002	9,625,587	\$ 10.25–13.00	\$ 12.70
Granted	2,220,279	\$ 13.00–19.70	\$ 13.65
Exercised	8,612	\$ 10.25–13.00	\$ 10.65
Forfeited	919,851	\$ 10.25–13.00	\$ 12.38
Balance, December 31, 2002	10,917,403	\$ 10.25–19.70	\$ 12.91

Stock option activity during the year ended December 31, 2001 is set forth below:

	SHARES	PRICE PER SHARE	
		RANGE	WEIGHTED AVERAGE
Balance, January 1, 2001	—	—	—
Granted	10,795,223	\$ 10.25–13.00	\$ 12.73
Exercised	—	—	—
Forfeited	1,169,636	\$ 10.25–13.00	\$ 12.98
Balance, December 31, 2001	9,625,587	\$ 10.25–13.00	\$ 12.70

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*(Dollars in tables in thousands)*

NASDAQ has an employee stock purchase plan for all eligible employees. Under the plan, shares of Common Stock may be purchased at six-month intervals (each, an "Offering Period") at 85% of the lower of the fair market value on the first or the last day of each Offering Period. Employees may purchase shares having a value not exceeding 10% of their annual compensation, subject to applicable annual IRS limitations. During 2002 and 2001, employees purchased an aggregate of 0.2 million and 0.3 million shares at a weighted-average price of \$10.22 and \$10.63 per share, respectively.

In May and July 2000, restricted Common Stock and options on Common Stock of NASDAQ Japan were awarded to certain NASDAQ officers and key employees who devote substantial time to the operations of NASDAQ Japan. These awards contained restrictions and were subject to vesting provisions, generally three years. The options were granted at an exercise price of \$125 per share, the estimated fair market value of the Common Stock at the time of the award. The options were exercisable for a period of seven years. As of December 31, 2001 there were 784 stock options outstanding to purchase shares of NASDAQ Japan held by NASDAQ Global, 261 of them exercisable with an approximate value of \$6,175 per share. The restricted Common Stock award was for 1,900 shares at the estimated fair value of \$125 per share. Approximately one-third of the shares vested immediately while the remaining two-thirds were to vest over a two-year period. As of December 31, 2001, the restricted Common Stock had an approximate value of \$6,250 per share. All share and dollar amounts reflect a four-for-one stock split of NASDAQ Japan shares in April 2001.

The options and restricted Common Stock awards were marked to market, and the fair value was being expensed over the vesting periods. NASDAQ recorded \$2.8 million in compensation expense related to these awards in 2001. During the second quarter of 2002, NASDAQ recognized a \$15.2 million other-than-temporary impairment of its investment in NASDAQ Japan. Included in this impairment charge was a benefit for the revaluation of the stock based awards of \$7.9 million. As of December 31, 2002, the options outstanding have no value and effectively were cancelled. On August 16, 2002, the Board of Directors of NASDAQ Japan voted to take the company to dormant status, effectively ceasing operations. NASDAQ Japan is currently in liquidation status and is expected to be completely dissolved in the second quarter of 2003 (see Note 6).

## 12. LEASES

The Company leases certain office space and equipment in connection with its operations. The majority of these leases contain escalation clauses based on increases in property taxes and building operating costs. Certain of these leases also contain renewal options. Rent expense for operating leases was \$37.9 million in 2002 and \$39.4 million in 2001.

Future minimum lease payments under non-cancelable operating leases with initial or remaining terms of one year or more consisted of the following at December 31, 2002:

Year ending December 31,

2003		\$	33,020
2004			34,731
2005			33,355
2006			32,244
2007			29,538
Remaining years			282,031
Total minimum lease payments		\$	<u>444,919</u>

Future minimum lease payments under non-cancelable capital leases with initial or remaining terms of one year or more consisted of the following at December 31, 2002

Year ending December 31,

2003		\$	5,222
2004			5,222
2005			3,048
			<u>13,492</u>
Less: imputed interest			(1,361)
Total minimum lease payments		\$	<u>12,131</u>

## 2002 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

*(Dollars in tables in thousands)*

### 13. COMMITMENTS AND CONTINGENCIES

NASDAQ entered into a six-year \$600.0 million contract with WorldCom in 1997 to replace the data network that connected the NASDAQ market facilities to market participants. As part of that contract, NASDAQ provided a guaranteed revenue commitment to WorldCom of \$300.0 million. NASDAQ was permitted to renegotiate the contract once the minimum guarantee was satisfied. In June 2002, an amendment to the original contract was negotiated with WorldCom once the minimum usage level of \$300.0 million was achieved from the original contract. The amended contract supersedes the terms of the existing contract and is for \$182.0 million over three years commencing in June 2002. The three-year contract includes fixed and variable cost components for two years and permits NASDAQ to terminate the contract in certain circumstances after the second year. Although WorldCom declared bankruptcy in July 2002, NASDAQ does not foresee any interruption in service under the contract.

As of December 31, 2002, €21.3 million (\$22.3 million) was funded in the form of a loan from a commitment of €31.8 million (\$33.4 million) for NASDAQ Europe. Of the funded amount, €15.5 million (\$16.2 million) was used to finance the operations of NASDAQ Europe through 2002. The remaining €5.8 million (\$6.1 million) was used to enable NASDAQ Europe to invest in NASDAQ Deutschland AG, a venture among NASDAQ Europe, several German banks and two regional German exchanges. NASDAQ has agreed to convert the aggregate amount of outstanding loans from debt to equity if the majority of the European strategic partners also convert their debt to equity. In October 2002, NASDAQ Europe's strategic investors committed to convert 73.8% of NASDAQ Europe's external debt to equity (or 87.1% including intercompany debt with NASDAQ). The conversion was formally approved by NASDAQ Europe's Board in March 2003 and is expected to close in May 2003. An additional €10.5 million (\$11.1 million) is expected to be contributed in 2003 for NASDAQ Europe operations, which will fulfill NASDAQ's Boards funding approval of €31.8 million (\$33.4 million).

NASDAQ has agreed to guarantee the provision of certain support and maintenance services for the trading platform to be operated by NASDAQ Deutschland AG in the event NASDAQ Europe no longer provides such services due to circumstances including its liquidation or winding down. NASDAQ's obligation to provide services would continue for a period of 18 months from the date the guarantee is triggered, but in no event longer than three years from the date trading begins on the NASDAQ Deutschland exchange. NASDAQ will be obligated to perform under the guarantee only if NASDAQ Deutschland satisfies certain conditions, including minimum quarterly order flow requirements for periods starting in the fourth quarter of 2003. NASDAQ estimates the maximum cost of providing the services at €14.7 million (\$15.4 million) over the term of the guarantee.



The Board of Director's of NASDAQ have approved a capital contribution of up to \$25.0 million to the NQLX joint venture. NASDAQ made a \$2.0 million capital contribution in 2001. During 2002, NASDAQ made additional contributions to NQLX of \$16.0 million. An additional \$7.0 million is expected to be contributed in 2003, which will fulfill NASDAQ's Board's initial approval of \$25.0 million.

From the \$72.2 million in net proceeds NASD received for the sale of warrants and shares of NASDAQ Common Stock in Phase I, NASD established a \$25.0 million earmark for the benefit of Amex to support Amex business operations and meet NASD's obligations to Amex arising out of its acquisition of Amex. In October 2000, NASD funded this \$25.0 million to Amex in the form of a capital contribution. Additionally, from the Phase I proceeds, NASD established a \$25.0 million earmark for the benefit of NASDR to fund membership fee reductions. Member rebates given to NASD members were \$24.0 and \$17.0 in 2002 and 2001, respectively. Future cumulative fee reductions are expected to be \$90.0 million through 2006. NASD established additional earmarks of \$25.0 million each to Amex and NASDR from the \$113.4 million in net proceeds from Phase II. In May 2001, NASD funded \$15.0 million under the Amex earmark in the form of a capital contribution. Additionally, NASD may also establish additional earmarks from the proceeds received upon exercise of the warrants.

On June 1, 1999, NASD finalized a ten-year agreement with EDS Corporation (the "EDS Agreement") to establish an alliance, NasTech, through which EDS provides technology services to NASD and NASDR. NASD has an obligation to pay to EDS a minimum of \$47.9 million each year under the term of the EDS Agreement except for 2009, which will be prorated through the ending date of the EDS Agreement on May 31, 2009. Included in the total minimum obligation, NASD is required to acquire at least \$21.5 million in applications development services from EDS, and use EDS for all their production service and application maintenance needs. Additionally, in the event that NASD terminates the EDS Agreement for convenience, it is subject to a termination fee to EDS. The termination fee is based upon a formula, which considers total EDS billings and profit through the date of termination and remaining minimum payments after the date of termination. If the EDS Agreement was terminated effective December 31, 2002, NASD would have been obligated to pay EDS a termination fee estimated at \$81.3 million. NASD has recorded advances to EDS of \$34.3 million and \$28.6 million as of December 31, 2002, and 2001, respectively, which is included in other assets in the consolidated balance sheet, which will be used to satisfy obligations under the EDS Agreement during the years ended December 31, 2005 through 2009.

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*(Dollars in tables in thousands)*

In 2001, NASD entered into a series of incentive agreements with the City of New York resulting in potential incentives aggregating \$53.6 million on a net present value basis to NASD, NASDAQ, and Amex. During 2002 and 2001, the Company recognized benefits of \$1.1 million and \$1.1 million, respectively, in real estate tax abatement and \$0.3 million and \$1.2 million, respectively, in sales tax abatement under this agreement.

The Company may be subject to claims arising out of the conduct of its business. Currently, there are certain legal proceedings pending against the Company. Management believes, based upon the opinion of counsel, it has adequately provided for any liabilities or settlements arising from these proceedings. Management is not aware of any unasserted claims or assessments that would have a material adverse effect on the financial position and the results of operations of the Company.

### 14. REAL ESTATE DEVELOPMENTS

During the fourth quarter of 2001, as a result of the terrorist attacks on September 11, 2001, NASDAQ decided to relocate its New York City headquarters from One Liberty Plaza, which was adjacent to the site where the World Trade Center Towers stood, to a location closer to its Times Square MarketSite Building. As of December 31, 2001, NASDAQ was obligated under the terms of its One Liberty Plaza lease to pay \$106.9 million over the remaining life of the lease and recorded an estimated loss on the sublease of \$21.5 million, which was included in other expense in the consolidated statements of income.

NASDAQ signed a lease commencing May 1, 2002, at 1500 Broadway, directly across from the MarketSite building and began marketing the space at its One Liberty Plaza location. Due to the softening of the real estate market in lower Manhattan, NASDAQ reconsidered its decision to relocate to 1500 Broadway and decided to support the downtown Manhattan community and maintain its headquarters at One Liberty Plaza. As a result of the decision to remain at One Liberty Plaza, NASDAQ has reevaluated the loss recorded in 2001 for One Liberty Plaza as well as its original plans to move to 1500 Broadway. As of December 31, 2002, NASDAQ was obligated under the terms of its 1500 Broadway lease to pay \$84.5 million over the life of the lease. At December 31, 2002, the estimated loss on the sublease (including interest accretion) is \$23.2 million including leasehold improvements, which is included in other expense in the consolidated statements of income. The estimated loss was calculated using an 8.0% net discount rate and an estimated 22-year sublease commencing December 2003 at estimated market rates. NASDAQ will continue to evaluate its estimated loss on 1500 Broadway.

## 15. DISCONTINUED OPERATIONS

In connection with NASD's overall corporate restructuring, NASD and Amex's Boards agreed that it was appropriate to begin the process of separating Amex from NASD and in December 2001, NASD and Amex's Boards appointed a committee composed of members of each Board to advise the Boards regarding separation. During 2002, NASD engaged an investment banker to assist with the various alternatives related to the separation of Amex. Significant progress on the Amex separation was made during 2002 and as of December 31, 2002, Amex met the requirements under the provisions of SFAS No. 144 to be reported as a discontinued operation. Management believes it's probable that the sale of Amex will be completed within one year and that it is unlikely that significant changes will be made to the plan to sell.

At December 31, 2002, the assets and liabilities of Amex are segregated on the consolidated balance sheets and the net operations of Amex have been reported within discontinued operations on the consolidated statements of income. Amex was previously reported by NASD as a separate segment under the provisions of SFAS No. 131, "Disclosure about Segments of an Enterprise and Related Information." Total revenues for Amex for the years ended December 31, 2002, and 2001 was \$252.5 million and \$281.1 million, respectively. Including intercompany expenses, Amex's net loss for the years ended December 31, 2002, and 2001 was (\$4.3) million and (\$2.6) million.

For the years ended December 31, 2002, and 2001, NASD recorded a net (loss) income from discontinued operations of (\$121.2) million and \$12.0 million, respectively. Included in the net (loss) income from discontinued operations are net income, after income taxes and excluding intercompany expenses, associated with Amex of \$13.4 million and \$12.0 million, for the years ended December 31, 2002, and 2001, respectively, and an estimated loss at disposal recorded as of December 31, 2002, of \$134.6 million (net of tax benefit of \$8.8 million). The estimated loss at disposal was calculated as the adjustment of carrying value to estimated fair value less costs to sell and includes amounts expected to be funded to Amex by NASD to settle certain remaining commitments and contingencies, an estimate of minimum working capital requirements, employee and severance costs, and liabilities to be assumed by NASD. The commitments and contingencies include the remaining obligation under the Member Equity Program discussed below, and the technology transfer agreement included within the Master Agreement (see Note 17).

In addition, the following commitments and contingencies exist with respect to Amex.

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*(Dollars in tables in thousands)*

The transaction agreement entered into by NASD related to the acquisition of Amex included a Member Equity Program (the "Program") to support the value of Amex members' seats. On October 30, 1998, the closing date of NASD's acquisition of Amex, NASD committed \$30.0 million to support seat prices with an additional \$10.0 million commitment effective on January 1, 1999. This fund can grow through a 5.0% return on the account, which is offset by seat purchases made by NASD.

Under the Program, an elected Seat Committee monitors the effectiveness of the Program at 18 months and 60 months from the acquisition date. At the time of the reviews, the Seat Committee determines, subject to a majority vote of the Amex members, the disbursement of portions of the initial commitment amount in one of the following ways: to owners of membership interests in Amex; as a reduction of Amex Exchange fees; and/or for investments in technology. Additionally, the Seat Committee may elect a rollover option under which it would not disburse funds until the next review date. After five years, the undistributed amount will be eligible for distribution to the Amex Members, reduction of Amex fees or investments in technology as determined by a membership vote. Every two years after that, the remainder will be eligible for distribution in the same manner until the commitment has been fully paid. The commitment will be funded from operations of NASD.

At the time of the 18-month review in June 2000, the Seat Committee recommended, and the members approved a disbursement of \$15.0 million to the Amex membership. This \$15.0 million distribution was funded by a capital contribution from NASD to Amex with Amex making the subsequent payments to the Amex membership. As of December 31, 2002, ten seats were purchased by NASD under the Program or a total of \$2.1 million. Accordingly, as of December 31, 2002, \$22.9 million remains outstanding under this commitment plus accrued interest of \$6.4 million. As of December 31, 2002, NASD accrued for their remaining obligation under this agreement, which is included within (loss) income from discontinued operations in the consolidated financial statements.

As a condition of NASD's acquisition of Amex, a Member Supplement Fund was established under which annual distributions may be made by NASD based upon 15.0% of the amount, if any, that the net income of Amex exceeds established thresholds for the years 1999 through 2008. Funds will be distributed to owners of membership interests in Amex or used to pay for investments in technology as determined by a Member Supplement Fund Committee. No payments were required to be made for 2002 and 2001 under the Member Supplement Fund formula.

At December 31, 2002, the rights to trade on Amex LLC were embodied through The American Stock Exchange, Inc. ("Amex Corp") in the 864 memberships (the "Members"). In accordance with the Limited Liability Company Agreement of Amex LLC, in the event of liquidation of Amex LLC, Amex Corp. will satisfy all obligations of the company and distribute any remaining cash as follows: (1) each existing regular member shall receive an equal distribution up to \$26 thousand; (2) each options principal member shall then receive an equal distribution up to \$15 thousand; (3) the remainder shall then be distributed in a manner such that each regular member will receive from such remaining assets two times the amount distributed to each options principal member. The total amount to be distributed to the members is capped at \$140.0 million.

In September 2000, Amex entered into a stipulation with the Department of Justice pursuant to which a decree was entered and an offer of settlement pursuant to which the SEC entered an order which, together, resolved investigations into options listing activity at Amex and other exchanges. Contemporaneous to these investigations, class action lawsuits were filed against Amex, other exchanges, and others. Amex entered into an agreement to settle these class action lawsuits in August 2000, with one-third of the total agreed upon settlement amount paid in August 2000, one-third paid in June 2001, and the remaining one-third to be paid in July 2002. Amex accrued for the remaining settlement payments in 2000 with the signing of the settlement agreement. The exact amount of Amex's settlement is confidential. The settlement is subject to the approval of the court, which declined to grant such approval for jurisdictional reasons in April 2001. That decision is currently on appeal.

SIAC, an affiliated company, has a lease agreement for a data processing site. The NYSE as majority owner of SIAC has guaranteed SIAC's performance under the terms of the lease, which has a remaining obligation of \$145.8 million over the next eight years. Amex has agreed to indemnify the NYSE for a portion of losses, if any, sustained by the NYSE in the event of a default by SIAC. The Amex's share of potential losses (\$35.0 million, or 24%, at December 31, 2002) is based upon its utilization of SIAC services for the preceding three years, and is adjusted annually. Amex has not made any payments under this indemnification agreement to date and no amounts are reflected in the accompanying financial statements for this guarantee.

In October 2002, Amex received a \$3.0 million grant from the New York State Urban Development Corporation d/b/a Empire State Development Corporation ("ESDC"). The terms of this grant require Amex to maintain a set number of full time employees within New York City annually until January 1, 2012. If Amex does not meet the required headcount as summarized in this grant, Amex will be required to pay back to ESDC a portion of the grant received. Further, if Amex were to relocate employees outside of New York City, they may be required to pay back the full amount of the grant plus additional penalties associated with such relocation, depending on when such relocation occurred. As of and for the year ended December 31, 2002,

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Amex recorded \$2.3 million as a deferred liability associated with this agreement and recognized \$0.8 million as a reduction to compensation expense since it met the annual requirements under the grant as of the balance sheet date. No accrual has been recorded for relocation related penalties, since management believes the risk of such relocation is remote.

### 16. BUSINESS SEGMENT INFORMATION

In accordance with SFAS No. 131, NASD manages two primary business segments: NASDAQ and NASD. As described in the summary of significant accounting policies, NASDAQ represents a separate identifiable organization. NASD includes NASD, NASDR, and NASD DR.

#### SEGMENT INCOME OR LOSS

NASD's accounting policies for segments are the same as those described in the summary of significant accounting policies. Management evaluates segment performance based on net operating income. Prior year segment information has been restated to conform to the current composition of reportable segments. Transfers between segments are accounted for at cost.

	2002				
	NASDAQ	NASD	DISCONTINUED OPERATIONS	CONSOLIDATING ADJUSTMENTS	CONSOLIDATED
Revenues, principally from external customers	\$ 799,343	\$ 446,587	\$ -	\$ (8,458)	\$ 1,237,472
Total operating expenses	707,667	430,752	-	10,048	1,148,467
Net operating income (loss)	91,676	15,835	-	(18,506)	89,005
Total assets	1,175,914	1,652,987	174,206	(261,163)	2,741,944
Long lived assets	361,225	177,513	-	-	538,738
Depreciation & amortization	\$ 97,911	\$ 54,726	\$ -	\$ (60)	\$ 152,577

	2001				
	NASDAQ	NASD	DISCONTINUED OPERATIONS	CONSOLIDATING ADJUSTMENTS	CONSOLIDATED
Revenues, principally from external customers	\$ 859,884	\$ 409,431	\$ -	\$ (2,317)	\$ 1,266,998
Total operating expenses	781,486	383,053	-	11,973	1,176,512
Net operating income (loss)	78,398	26,378	-	(14,290)	90,486
Total assets	1,327,630	1,596,752	269,900	(543,538)	2,650,744
Long lived assets	380,213	216,095	-	-	596,308
Depreciation & amortization	\$ 93,400	\$ 55,721	\$ -	\$ -	\$ 149,121

#### 17. PARENT COMPANY ONLY STATEMENTS -- CONDENSED

The following condensed consolidated balance sheets, statements of income and statements of cash flows as of and for the years ended December 31, 2002, and 2001 present the information for the entities that Company management consider to be the parent company for NASD. This information includes: 1) the consolidated information for NASD, NASDR and NASD DR (the "Parent Entities"), and 2) NASD's investments in its NASDAQ and Amex subsidiaries (not consolidated). As disclosed in Note 1, NASD is in the process of a Restructuring relating to its ownership interests in NASDAQ, which upon completion will reduce NASD's ownership of NASDAQ to 0%. In addition, NASD has reached an agreement with the Amex Board of Directors on the ultimate separation of Amex from NASD. Accordingly, the following presentation of "Parent Company Only Statements" reflects the financial position, results of operations and cash flow for the Parent Entities, assuming deconsolidation of its NASDAQ and Amex subsidiaries.

## 2002 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in tables in thousands)

BALANCE SHEETS:	DECEMBER 31,	
	2002	2001
<b>ASSETS</b>		
Cash and cash equivalents		
Investments, available-for-sale	\$ 269,566	\$ 267,477
Receivables, net	869,899	515,744
Receivable from related parties	27,645	22,315
Other current assets	35,273	47,392
Total current assets	11,450	11,689
	1,213,833	864,617
Total property and equipment, net		
	177,513	216,095
Investment in NASDAQ		
Net assets— discontinued operations	209,398	357,170
Other assets	—	102,349
Total assets	52,243	56,521
	\$ 1,652,987	\$ 1,596,752
<b>LIABILITIES AND MEMBERS' EQUITY</b>		
Payable to related parties		
Net liabilities— discontinued operations	\$ 6,866	\$ 35,340
Current liabilities	7,407	—
Other liabilities	410,593	311,853
Total liabilities	53,565	207,525
	478,431	554,718
Members' equity		
	1,174,556	1,042,034
Total liabilities and members' equity	\$ 1,652,987	\$ 1,596,752



**STATEMENTS OF INCOME:****REVENUES:**Revenues, net of member rebates of \$24,000 in 2002  
and \$17,000 in 2001**EXPENSES:**Compensation and benefits  
Professional and contract services  
Depreciation and amortization  
Other, including support charge allocated to related parties  
Total operating expenses  
Net operating income**OTHER INCOME (EXPENSE):**Equity in earnings of NASDAQ  
Other (expense) income  
Gain on NASDAQ warrants  
(Loss) income from discontinued operations  
Gain from NASDAQ shares sold by NASD  
Net (loss) incomeYEARS ENDED DECEMBER 31,  
2002 2001

\$ 446,587	\$ 409,431
233,962	223,555
134,118	135,133
54,726	55,721
7,946	(31,356)
430,752	383,053
15,835	26,378
25,927	30,159
(28,703)	12,007
104,667	-
(121,206)	12,010
-	31,445
\$ (3,480)	\$ 111,999

**STATEMENTS OF CASH FLOWS:**CASH FLOWS FROM OPERATING ACTIVITIES  
CASH FLOWS FROM INVESTING ACTIVITIES  
CASH FLOWS FROM FINANCING ACTIVITIES  
Increase in cash and cash equivalents  
Cash and cash equivalents at beginning of year  
CASH AND CASH EQUIVALENTS AT END OF YEARYEARS ENDED DECEMBER 31,  
2002 2001

\$ 203,638	\$ 120,905
(129,264)	65,824
(72,285)	(148,999)
2,089	37,730
267,477	229,747
\$ 269,566	\$ 267,477

## 2002 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

*(Dollars in tables in thousands)*

During 2002 and 2001, the repurchases by NASDAQ of NASDAQ stock held by NASD with gross proceeds of \$439.0 million and \$240.0 million resulted in NASD realizing proceeds in excess of its basis in the underlying shares of NASDAQ of \$277.5 million and \$134.4 million, respectively. As a result of these reductions in NASDAQ equity resulting from this transaction, NASD realized a reduction in its proportionate remaining ownership of NASDAQ of \$154.6 million and \$93.9 million, respectively. Accordingly, the net effect of this transaction is reflected as a \$122.9 million and \$40.5 million increase to NASD equity in the consolidated statements of changes in members' equity for the years ending December 31, 2002, and 2001, respectively. These transactions represent another element of the continuing plan of corporate reorganization with regard to NASD's investment in NASDAQ.

### RELATED PARTY TRANSACTIONS

On February 6, 2002, NASD, NASDAQ and Amex (the "Parties") entered into a Master Agreement that would establish provisions for the ongoing relationships of the Parties. The parties submitted the Master Agreement to the SEC and Department of Justice for review prior to final agreement and execution. Summarized below are some of the significant provisions contained in the Master Agreement.

NASD and NASDAQ have agreed to fund a portion of the necessary expenses related to the separation of software, hardware, and data under a plan to transition technology applications and support from NASD and NASDAQ to Amex. NASD originally integrated NASDAQ and Amex technology subsequent to the acquisition of Amex by NASD in October 1998. The total estimated cost of the separation has been set at a maximum of \$29.0 million, and is to be shared evenly between NASDAQ and NASD. In 2002 and 2001, Amex incurred \$4.3 million and \$3.8 million, respectively, of costs under this agreement, for which Amex was reimbursed \$7.4 million from NASD in 2002 in the form of a capital contribution. The Technology Steering Committee consists of one representative each from NASD, NASDAQ and Amex and was established to supervise the performance of the Parties pursuant to the technology transition. NASD and NASDAQ expect to fund this commitment up to its \$29.0 maximum, at the cost of \$14.5 million each. As of December 31, 2002, NASD accrued for their remaining obligation under this agreement, which is included within (loss) income from discontinued operations in the consolidated statement of income.

Beginning in 2002, Amex began paying NASDAQ an annual fee for the right to list, trade and market the NASDAQ-100 Index Tracking Stock, otherwise known as QQQ. For the year ended December 31, 2002, this fee was \$2.0 million.

As consideration for certain benefits that NASDAQ agreed to provide to Amex, the Parties agreed that (1) NASDAQ is entitled to realize the \$15.1 million of tax loss carryforwards related to the assignment by Market Group of its interest in Amex to New NASD Holding, Inc. and (2) NASD is required to repay NASDAQ \$5.6 million in cash NASDAQ paid to NASD relating to NASDAQ's use of federal tax losses allocated by Amex to Market Group for the period beginning November 1, 1998, and ending on June 30, 2000. NASD paid NASDAQ \$5.6 million on February 20, 2002. NASDAQ treated the payment as a contribution and reflected it in additional paid-in capital on its consolidated balance sheet. Pursuant to this transaction, NASD recognized a net reduction in equity of \$2.5 million related to the minority partner's share of this contribution to NASDAQ.

In June 2002, NASD granted Amex a \$50.0 million revolving line of credit. Interest on this line of credit is LIBOR plus .45%. The line of credit agreement matures on April 30, 2004. As of December 31, 2002, NASD had an outstanding receivable from Amex under this agreement of \$50.0 million.

In December 2002, NASD sold its 50.0% interest in the NASD Insurance Agency, LLC (subsequently renamed the NASDAQ Insurance Agency, LLC ("NIA")) to NASDAQ for an initial payment of \$0.5 million and up to \$5.1 million based on the NASD Insurance Agency's stream of contingent cash flow through 2011. NASDAQ will pay (a) 20% of NIA's cash flows until NASDAQ has paid NASD \$2.3 million from cash flows; (b) 10% of NIA's cash flows until NASDAQ has paid NASD a cumulative amount of \$3.0 million from cash flows; (c) 5% of NIA's cash flows until NASDAQ has paid NASD the full cumulative amount of \$5.1 million from cash flows. Pursuant to this transaction, NASD recognized a net increase in equity of \$0.2 million related to the minority partner's share of this payment from NASDAQ.

## 2002 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in tables in thousands)

### 18. SUBSEQUENT EVENTS

In January 2003, NASDR censured a large investment banking NASD member firm and directed it to pay \$14.0 million to the SEC and \$14.0 million to NASDR in monetary sanctions for receiving inflated commissions from more than 100 client accounts in exchange for the allocation of "hot" initial public offerings ("IPO") in 1999 and 2000 during the height of the IPO boom. On January 15, 2003, the \$14.0 million was received by NASDR and recorded as fines revenue in 2003.

On April 1, 2003, NASD and EDS entered into a new service agreement ("2003 EDS Agreement"), which supersedes the existing EDS Agreement. The new agreement included several modifications including a more detailed statement of work, enhanced service levels, improved pricing, and an extended term. The 2003 EDS agreement expires on December 31, 2012, representing an extension of 3.5 years. Under the 2003 EDS Agreement, NASD is obligated to pay EDS a minimum of \$24.0 million for the first year, (prorated for a 9-month period during 2003 commencing on the effective date), which is reduced ratably to \$16.0 million in the final year, for both applications development and maintenance services. NASD is also required to use EDS for all its production service needs. Furthermore, NASD cannot terminate the 2003 EDS Agreement until April 1, 2005, at which point, the termination fee is based on a fixed fee schedule versus the formula-based approach in the initial agreement. As consideration for the 2003 EDS Agreement, NASD agreed to forgive the \$34.3 million deposit with EDS. This deposit will be deferred and amortized into income over the term of the new agreement.

On May 30, 2003, NASD agreed in principle to sell its interest in Amex to a Chicago-based private equity firm, GTCR Golder Rauner LLC. The terms of this specific agreement are subject to the completion of definitive sale documents and approvals by NASD's Board of Governors, Amex's Board of Governors, Amex membership, and the Securities and Exchange Commission ("SEC").

On June 26, 2003, the SEC notified Amex that it had commenced a formal investigation into certain issues arising from an inspection of its regulatory programs by the SEC's Office of Compliance Inspections and Examinations ("OCIE") related to customer options order handling. As part of the investigation, the SEC has asked Amex to provide information relating to this matter. Amex is cooperating fully with the SEC's requests. At this time Amex cannot predict the outcome of this investigation and whether such outcome will have a material financial statement impact.

On June 26, 2003, NASDAQ announced several strategic initiatives with the ultimate intent to focus on its U.S. operations. The most significant initiative is the decision to close the market operated by NASDAQ Europe. The final plans on winding down this operation along with the calculation of the costs to complete an orderly wind down is currently in process.



A PEOPLE-FOCUSED,  
PERFORMANCE DRIVEN ORGANIZATION

NASD

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