

INTERNATIONAL ASSETS HOLDING CORP
Form 10QSB
May 23, 2005
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U.S. Securities and Exchange Commission

Washington D.C. 20549

Form 10-QSB

**QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2005

Commission File Number 000-23554

INTERNATIONAL ASSETS HOLDING CORPORATION

(Exact name of small business issuer as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

59-2921318
(IRS Employer
Identification No.)

220 East Central Parkway, Suite 2060

Altamonte Springs, FL 32701

(Address of principal executive offices)

(407) 741-5300

(Issuer's telephone number)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No .

The issuer had 7,413,370 outstanding shares of common stock as of May 16, 2005.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Unaudited)

| | March 31, | September |
|---|------------------|--------------------|
| | 2005 | 30, |
| | | 2004 |
| | | as restated |
| <u>Assets</u> | | |
| Cash | \$ 3,060,707 | \$ 3,523,604 |
| Cash and cash equivalents deposited with brokers, dealers and clearing organization | 9,448,198 | 17,560,863 |
| Receivable from brokers, dealers and clearing organization | 11,759,767 | 7,699,450 |
| Receivable from customers | 13,564,972 | 12,358,412 |
| Financial instruments owned, at market value | 32,031,463 | 18,805,625 |
| Trust certificates, at cost | 29,739,902 | |
| Income taxes receivable | 163,105 | |
| Investment in asset management joint venture | 528,105 | 459,075 |
| Investment in INTL Consilium sponsored fund | 4,497,499 | 3,020,805 |
| Deferred income tax asset, net | 209,661 | 362,838 |
| Fixed assets and leasehold improvements at cost, net of accumulated depreciation and amortization | 469,138 | 465,023 |
| Intangible assets, net of accumulated amortization of \$58,333 at March 31, 2005 | 291,667 | 350,000 |
| Goodwill | 3,184,639 | 2,424,945 |
| Other assets | 851,066 | 661,641 |
| | <hr/> | <hr/> |
| Total assets | \$ 109,799,889 | \$ 67,692,281 |
| | <hr/> | <hr/> |
| <u>Liabilities and Stockholders' Equity</u> | | |
| Liabilities: | | |
| Accounts payable | \$ 205,202 | \$ 343,657 |
| Foreign currency sold, not yet purchased, at market value | 971,676 | 2,829,597 |
| Financial instruments sold, not yet purchased, at market value | 53,666,340 | 12,310,543 |
| Payable to banks under loans and overdrafts | 10,406,108 | 10,447,417 |
| Payable to brokers, dealers and clearing organization | 2,310,243 | 9,272,857 |
| Payable to customers | 10,638,671 | 4,665,183 |
| Accrued compensation and benefits | 1,180,130 | 2,102,055 |
| Accrued expenses | 734,566 | 562,263 |
| Income taxes payable | 477,601 | 224,396 |
| Deferred acquisition consideration payable | 1,046,074 | 286,380 |
| Other liabilities | 379,732 | 74,692 |
| | <hr/> | <hr/> |
| Total liabilities | 82,016,343 | 43,119,040 |
| | <hr/> | <hr/> |
| Minority owners interest in consolidated entity | 1,389,217 | |
| | <hr/> | <hr/> |
| Commitments and contingent liabilities | | |
| Stockholders' equity: | | |
| Preferred stock, \$.01 par value. Authorized 5,000,000 shares; no shares issued or outstanding | | |
| Common stock, \$.01 par value. Authorized 12,000,000 shares; issued and outstanding 7,409,873 shares at March 31, 2005 and 7,069,076 shares at September 30, 2004 | 74,099 | 70,691 |
| Additional paid-in capital | 27,994,817 | 27,168,617 |

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| | | |
|--|----------------|---------------|
| Retained deficit | (1,674,587) | (2,666,067) |
| Total stockholders' equity | 26,394,329 | 24,573,241 |
| Total liabilities and stockholders' equity | \$ 109,799,889 | \$ 67,692,281 |

See accompanying notes to condensed consolidated financial statements.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Operations

For the Six Months Ended March 31, 2005 and 2004

(Unaudited)

| | <u>2005</u> | <u>2004</u> |
|--|-------------------|---------------------|
| | | <u>as restated</u> |
| Revenues: | | |
| Net dealer inventory and investment gains | \$ 11,859,875 | \$ 11,208,334 |
| Commissions, net | 309,302 | 501,545 |
| Interest income | 131,264 | 63,771 |
| Dividend income (expense), net | (130,188) | (80,751) |
| Equity in income from asset management joint venture | 69,030 | |
| Other | 3,066 | 4,661 |
| | <u>12,242,349</u> | <u>11,697,560</u> |
| Total revenues | | |
| Interest expense | 472,659 | 161,820 |
| | <u>11,769,690</u> | <u>11,535,740</u> |
| Net revenues | | |
| Non-interest expenses: | | |
| Compensation and benefits | \$ 5,157,388 | \$ 4,278,447 |
| Clearing and related expenses | 3,135,201 | 3,410,658 |
| Wholesale commission expense | 14,138 | 4,800 |
| Occupancy and equipment rental | 360,278 | 240,556 |
| Professional fees | 245,416 | 164,078 |
| Depreciation and amortization | 152,566 | 113,172 |
| Business development | 380,113 | 157,313 |
| Insurance | 302,107 | 148,964 |
| Other | 446,369 | 172,005 |
| | <u>10,193,576</u> | <u>8,689,993</u> |
| Total non-interest expenses | | |
| Income before income tax expense and minority interest | 1,576,114 | 2,845,747 |
| Income tax expense | 571,668 | 1,223,409 |
| | <u>1,004,446</u> | <u>1,622,338</u> |
| Income before minority interest | | |
| Minority interest in income of consolidated entity | 12,966 | |
| | <u>\$ 991,480</u> | <u>\$ 1,622,338</u> |
| Net income | | |
| Earnings per share: | | |
| Basic | \$ 0.14 | \$ 0.34 |
| | <u>\$ 0.12</u> | <u>\$ 0.29</u> |
| Diluted | | |
| Weighted average number of common shares outstanding: | | |

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| | | |
|---------|-----------|-----------|
| Basic | 7,186,054 | 4,738,214 |
| Diluted | 8,037,059 | 5,546,596 |

See accompanying notes to condensed consolidated financial statements.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Operations

For the Three Months Ended March 31, 2005 and 2004

(Unaudited)

| | <u>2005</u> | <u>2004</u> |
|--|-------------------|--------------------|
| | | <u>as restated</u> |
| Revenues: | | |
| Net dealer inventory and investment gains | \$ 6,019,604 | 6,158,001 |
| Commissions, net | 151,950 | 255,709 |
| Interest income | 82,122 | 36,824 |
| Dividend income (expense), net | (129,309) | (87,455) |
| Equity in income from asset management joint venture | 29,672 | |
| Other | 3,011 | 5,855 |
| | <u>6,157,050</u> | <u>6,368,934</u> |
| Interest expense | 295,747 | 137,752 |
| | <u>5,861,303</u> | <u>6,231,182</u> |
| Net revenues | | |
| Non-interest expenses: | | |
| Compensation and benefits | 2,548,907 | 2,339,095 |
| Clearing and related expenses | 1,705,362 | 1,835,954 |
| Wholesale commission expense | 3,781 | 4,000 |
| Occupancy and equipment rental | 187,143 | 128,338 |
| Professional fees | 123,478 | 69,994 |
| Depreciation and amortization | 78,120 | 29,425 |
| Business development | 202,104 | 76,733 |
| Insurance | 169,700 | 77,633 |
| Other | 260,525 | 97,765 |
| | <u>5,279,120</u> | <u>4,658,937</u> |
| Total non-interest expenses | | |
| Income before income tax expense and minority interest | 582,183 | 1,572,245 |
| Income tax expense | 196,341 | 720,762 |
| | <u>385,842</u> | <u>851,483</u> |
| Income before minority interest | | |
| Minority interest in income of consolidated entity | 6,529 | |
| | <u>\$ 379,313</u> | <u>851,483</u> |
| Net income | | |
| Earnings per share: | | |
| Basic | \$ 0.05 | \$ 0.18 |
| | <u>\$ 0.05</u> | <u>\$ 0.15</u> |
| Diluted | | |
| Weighted average number of common shares outstanding: | | |
| Basic | 7,288,778 | 4,763,724 |

| | | |
|---------|-----------|-----------|
| Diluted | 8,075,465 | 5,654,402 |
|---------|-----------|-----------|

See accompanying notes to condensed consolidated financial statements.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

For the Six Months Ended March 31, 2005 and 2004

(Unaudited)

| | <u>2005</u> | <u>2004</u> |
|---|--------------------|--------------------|
| | | <u>as restated</u> |
| Cash flows from operating activities: | | |
| Net income | \$ 991,480 | 1,622,338 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Depreciation and amortization | 152,566 | 113,172 |
| Amortization of debt issuance costs | | 14,545 |
| Amortization of beneficial conversion feature | | 3,698 |
| Deferred income taxes | 153,177 | 294,312 |
| Equity in gain from asset management joint venture | (69,030) | |
| Amortization of stock option expense for consultant | | 12,375 |
| Unrealized investment gain from INTL Consilium sponsored fund | (87,477) | |
| Cash provided by (used in) changes in: | | |
| Receivable from brokers, dealers and clearing | (4,060,317) | (951,084) |
| Receivable from customers | (1,206,560) | |
| Other receivables | | 237,894 |
| Financial instruments owned, at market value | (13,225,838) | (17,346,303) |
| Income taxes receivable | 26,966 | |
| Other assets | (189,425) | (56,889) |
| Foreign currency sold, not yet purchased, at market value | (1,857,921) | 379,684 |
| Financial instruments sold, not yet purchased, at market value | 12,034,688 | 14,692,307 |
| Accounts payable | (138,455) | 20,621 |
| Payable to brokers, dealers and clearing | (6,962,614) | |
| Payable to customers | 5,554,695 | |
| Accrued compensation and benefits | (921,925) | 325,077 |
| Accrued expenses | 172,303 | 49,073 |
| Income taxes payable | 253,205 | 373,897 |
| Other liabilities | 305,040 | 3,815 |
| Net cash used in operating activities | <u>(9,075,442)</u> | <u>(211,468)</u> |
| Cash flows from investing activities: | | |
| Purchase of fixed assets and leasehold improvements | (98,348) | (16,685) |
| Net cash used in investing activities | <u>(98,348)</u> | <u>(16,685)</u> |
| Cash flows from financing activities: | | |
| Issuance of convertible subordinated notes payable, net of debt issuance costs settled in cash of \$997,706 | | 11,002,293 |
| Bank overdrafts | (41,309) | |
| Exercise of stock options | 639,537 | 270,640 |
| Net cash provided by financing activities | <u>598,228</u> | <u>11,272,933</u> |

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| | | |
|---|-----------------------------|-----------------------------|
| Net (decrease) increase in cash and cash equivalents | (8,575,562) | 11,044,780 |
| Cash and cash equivalents at beginning of period | 21,084,467 | 7,066,572 |
| | <u> </u> | <u> </u> |
| Cash and cash equivalents at end of period | \$ 12,508,905 | 18,111,352 |
| | <u> </u> | <u> </u> |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for interest | \$ 472,659 | 80,334 |
| | <u> </u> | <u> </u> |
| Income taxes paid | \$ 138,320 | 558,680 |
| | <u> </u> | <u> </u> |
| Supplemental disclosure of noncash investing and financing activities: | | |
| Assumption of trust certificates, at cost, with related financial instruments sold, not yet purchased, at market value and payable to customers (TRS) | \$ 29,739,902 | |
| | <u> </u> | <u> </u> |
| Consolidation of INTL Consilium sponsored fund | \$ 1,376,251 | \$ |
| | <u> </u> | <u> </u> |
| Issuance of warrants for placement agent services | \$ | \$ 893,121 |
| | <u> </u> | <u> </u> |

See accompanying notes to condensed consolidated financial statements.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

March 31, 2005

(Unaudited)

(1) Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions and requirements of Form 10-QSB and, therefore, do not include all information and footnotes necessary for a fair presentation of financial position, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States of America. In the opinion of management, such financial statements reflect all adjustments (consisting of normal recurring items) necessary for a fair statement of the results of operations, cash flows and financial position for the interim periods presented. Operating results for the interim periods are not necessarily indicative of the results that may be expected for the full year. These condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the fiscal year ended September 30, 2004, contained in the Company's amended Annual Report on Form 10-KSB/A for the fiscal year ended September 30, 2004 filed with the Securities and Exchange Commission.

Current Subsidiaries and Operations

As used in this Form 10-QSB, the term "Company" refers, unless the context requires otherwise, to International Assets Holding Corporation and its subsidiaries. The Company's subsidiaries are INTL Trading, Inc. ("INTL Trading"), INTL Assets, Inc. ("INTL Assets"), INTL Holdings (U.K.) Limited, INTL Global Currencies Limited (INTL Global Currencies) and IAHC (Bermuda) Ltd. The Company also owns a 50.1% limited liability company interest in INTL Consilium, LLC (INTL Consilium), an investment advisory firm that focuses on the emerging market asset class. INTL Consilium is accounted for using the equity method of accounting. All significant intercompany balances and transactions have been eliminated in consolidation.

The Company operates as a wholesale international financial firm in four business segments: international equities market making, international debt capital markets, foreign exchange/commodities trading and asset management. The Company acts as a market maker for equity securities, including American Depositary Receipts ("ADRs"), issued by non-U.S. issuers, and trades and invests in debt securities issued by non-U.S. issuers. These activities are primarily conducted through INTL Trading. During the quarter ended March 31, 2003, the Company also began to conduct fixed income trading and investing activities through IAHC Bermuda. During the quarter ended September 30, 2003, the Company began to conduct precious metals and foreign currency trading and investing activities through International Assets Holding Corporation.

On May 11, 2004 the Company signed a joint venture agreement with Consilium Investment Capital, Inc. ("CIC") of Fort Lauderdale, Florida and formed INTL Consilium, LLC. INTL Consilium, LLC is an investment management firm which primarily provides investment advice on emerging market securities.

On July 9, 2004, the Company acquired the foreign exchange business of Global Currencies Limited ("Global") through the purchase of two wholly-owned subsidiaries of Global, INTL Global Currencies Limited and INTL Holdings (U.K.) Limited. Both INTL Global Currencies and INTL Holdings (U.K.) Limited are designated as U.S. dollar denominated companies under the laws of the United Kingdom. Accordingly, the

functional currency for these companies is the U.S. dollar.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

(2) **Restatement**

The Company restated its financial statements for the fiscal years ended September 30, 2002, 2003 and 2004, and for the fiscal quarter ended December 31, 2004. The restatement was made with respect to the following three items:

- a) Subsequent to the issuance of its financial statements for the year ended September 30, 2004, the Company determined that it should have accounted for the discount arising from the beneficial conversion feature in the 7% convertible notes (the Notes) issued in March 2004 and converted in August 2004, in compliance with FASB Emerging Issues Task Force (EITF) Issue No. 98-5, *Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratio*, as amended by EITF Issue No. 00-27, *Application of Issue No. 98-5 to Certain Convertible Instruments*. Since the conversion price of \$5.75 per share was lower than the fair value of the Company's stock on the relevant commitment date, the difference should have been accounted for as a discount to the debt issue and an increase in additional paid-in capital. The discount should have been amortized over the life of the notes and, upon conversion, the remaining balance of the discount should have been written off, with both passing through the consolidated statement of operations and classified as interest expense. The total effect for the year ended September 30, 2004 of the beneficial conversion feature restatement was to increase additional paid in capital by \$2,483,478 and to increase interest expense and the retained deficit by the same amount. The effect for the fiscal quarter ended March 31, 2004 of the beneficial conversion feature restatement was to increase interest expense by \$3,698. The interest expense is not deductible for tax purposes. The restatement included a change from the treasury method to the if-converted method for calculation of the dilutive effect of the convertible notes on earnings per share.

- b) The Company had previously treated the interest paid to holders of the 7% notes for the period between their issuance in March 2004 and their conversion in August 2004 as deductible for income tax purposes. The Company has now concluded that there is insufficient certainty that the Internal Revenue Service will recognize this interest, amounting to \$378,243, as deductible. The restatement adjusted for this by increasing the income tax expense by \$154,096 for the year ended September 30, 2004 and increasing income taxes payable by a corresponding amount.

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- c) Following a review of its lease accounting policies, the Company determined that it was appropriate to restate its financial statements for the years ended September 30, 2002, 2003 and 2004, and for the fiscal quarter ended December 31, 2004. In the past, while the benefits of certain periods of free or reduced rental had been spread across the lease term, the Company had not properly allocated scheduled rent escalations across the lease terms. The restatement increased rent expense to spread scheduled rent escalations on a straight-line basis over the contractual lease terms, in accordance with FAS 13, *Accounting for Leases*. As a result of this restatement, rental expense for the fiscal year ended September 30, 2004 was increased by \$10,104 and for the fiscal quarter ended March 31, 2004 by \$2,526. These adjustments resulted in decreases in the Company's tax charge in each of the applicable periods, calculated at its marginal income tax rate, and corresponding decreases in liability for income tax. Since these adjustments resulted in *timing differences* of rental charges, they resulted in an increase in the Company's deferred tax balances.

The restatements had no effect on total cash flows from operating activities, investing activities or financing activities for the six months ended March 31, 2004 and 2005. The tables below summarize the impact of the restatements on the fiscal quarter ended March 31, 2004 and on the year ended September 30, 2004:

| | Quarter Ended March 31, 2004 | Quarter Ended March 31, 2004 | Quarter Ended March 31, 2004 | Sept. 30, 2004 | Sept. 30, 2004 | Sept. 30, 2004 |
|---|---------------------------------------|---------------------------------------|---------------------------------------|------------------------|---------------------------|-------------------|
| | previously reported | restatement adjustment | as restated | previously reported | restatement adjustment | as restated |
| Interest expense | 134,054 | 3,698 | 137,752 | | | |
| Net revenues | 6,234,880 | (3,698) | 6,231,182 | | | |
| Occupancy and equipment rental | 123,286 | 2,526 | 125,812 | | | |
| Non-interest expenses | 4,656,411 | 2,526 | 4,658,937 | | | |
| Income (loss) before income taxes | 1,578,469 | (6,224) | 1,572,245 | | | |
| Income tax expense | 696,026 | 24,736 | 720,762 | | | |
| Net income (loss) | 882,443 | (30,960) | 851,483 | | | |
| Net income (loss) per share - basic | \$ 0.19 | | \$ 0.18 | | | |
| Net income (loss) per share - diluted | \$ 0.15 | | \$ 0.15 | | | |
| Weighted average number of common shares outstanding: | | | | | | |
| Diluted | 5,740,733 | (86,331) | 5,654,402 | | | |
| Deferred income tax asset, net | 33,087 | 13,087 | 46,174 | 332,429 | 30,409 | 362,838 |
| Income taxes receivable | | | | 57,881 | (57,881) | |
| Total assets | 47,980,191 | 13,087 | 47,993,278 | 67,719,753 | (27,472) | 67,692,281 |
| Income taxes payable | 348,132 | 25,765 | 373,897 | 112,917 | 111,479 | 224,396 |
| Other liabilities | 42,402 | 32,121 | 74,523 | 37,519 | 37,173 | 74,692 |
| Debt discount, net | | (2,479,780) | (2,479,780) | | | |
| Total liabilities | 35,850,932 | (2,421,894) | 33,429,038 | 42,970,388 | 148,652 | 43,119,040 |
| Additional paid-in capital | 12,958,317 | 2,483,478 | 15,441,795 | 24,685,139 | 2,483,478 | 27,168,617 |
| Retained deficit | (877,025) | (48,497) | (925,522) | (6,465) | (2,659,602) | (2,666,067) |
| Total stockholders' equity | 12,129,259 | 2,434,981 | 14,564,240 | 24,749,365 | (176,124) | 24,573,241 |

Table of Contents**(3) Stock-Based Employee Compensation**

In October 1995, the Financial Accounting Standards Board (FASB) issued SFAS No. 123, Accounting for Stock-Based Compensation, which generally permits entities to recognize as expense over the vesting period the fair value of all stock-based awards calculated on the date of grant. Alternatively, SFAS No. 123 allows entities to continue to apply the provisions of APB Opinion No. 25, which provides that compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price and if disclosure is made on a pro forma basis of the expense which would have been recognized if the fair-value-based method defined in SFAS No. 123 had been applied. The Company has elected to continue to apply the provisions of APB Opinion No. 25 and provide the required pro forma disclosure.

If the Company had determined compensation cost based on the fair value at the grant date for its stock options under SFAS No. 123, the Company's net income and earnings per share, on a pro forma basis, would have been the amounts indicated below:

For the six months ended March 31,

| | <u>2005</u> | <u>2004</u> |
|----------------------------|-------------|---------------|
| | | (as restated) |
| Net income | | |
| As reported | \$ 991,480 | 1,622,338 |
| Pro forma | \$ 772,295 | 1,333,063 |
| Basic earnings per share | | |
| As reported | \$ 0.14 | 0.34 |
| Pro forma | \$ 0.11 | 0.28 |
| Diluted earnings per share | | |
| As reported | \$ 0.12 | 0.29 |
| Pro forma | \$ 0.10 | 0.24 |

For the three months ended March 31,

| | <u>2005</u> | <u>2004</u> |
|----------------------------|-------------|---------------|
| | | (as restated) |
| Net income | | |
| As reported | \$ 379,313 | 851,483 |
| Pro forma | \$ 278,051 | 705,363 |
| Basic earnings per share | | |
| As reported | \$ 0.05 | 0.18 |
| Pro forma | \$ 0.04 | 0.15 |
| Diluted earnings per share | | |
| As reported | \$ 0.05 | 0.15 |
| Pro forma | \$ 0.03 | 0.12 |

Pro forma net income reflects only options granted from 1996 to the present date. Therefore, the full impact of calculating compensation expense for stock options under SFAS No. 123 is not reflected in the pro forma net income amounts presented above because compensation expense is reflected over the options' expected life ranging from immediate vesting to 8.5 years and compensation expense for options granted prior to October 1, 1995 is not considered.

(4) Effects of Recent Accounting Pronouncements and Interpretations

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In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (revised 2004), Share-Based Payment (SFAS No. 123R). This statement requires the recognition of the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award in its financial statements. It also requires the cost to be recognized over the period during which an employee is required to provide service in exchange for the award (usually the vesting period). SFAS No. 123R replaces SFAS No. 123 and supersedes APB Opinion No. 25, and its related

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interpretations. SFAS No. 123R is effective for annual periods beginning after June 15, 2005. Small-business issuers (the Company presently qualifies as a small business issuer) must apply SFAS No. 123R for annual periods beginning after December 15, 2005. In the Company's case, this will be the fiscal year commencing on October 1, 2006. The Company is reviewing the impacts of the adoption of this statement including the transition options provided by SFAS No. 123R.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

On October 13, 2004, the Financial Accounting Standards Board (FASB) ratified the consensus reached by the Emerging Issues Task Force (EITF) on EITF issue 04-10, Determining Whether to Aggregate Operating Segments that do not meet the Quantitative Thresholds. The task force concluded that operating segments that do not meet the quantitative thresholds established by Statement of Financial Accounting Standard (SFAS) No. 131, Disclosures about Segments of an Enterprise and Related Information, can be aggregated only if aggregation is consistent with the objective and basic principles of SFAS No. 131, the segments have similar economic characteristics, and the segments share a majority of the aggregation criteria listed in SFAS No. 131. This EITF becomes applicable for fiscal years ending after October 13, 2004. The adoption of this EITF will not have a material effect on the Company s disclosure.

In January 2003, the FASB issued Interpretation No. 46 (FIN 46), Consolidation of Variable Interest Entities, which provides guidance on the consolidation of certain entities in which the equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. Such entities are referred to as variable interest entities (VIE s). FIN 46 requires that a VIE be consolidated by a business enterprise if that enterprise is deemed to be the primary beneficiary of the VIE. The FASB revised FIN 46 through the issuance of Interpretation No. 46 (revised December 2003 and referred to as FIN 46R). FIN 46R contains technical corrections and extends the effective date of FIN 46 to the first reporting period that ended after March 15, 2004. The issuance of FIN 46 and FIN 46R had no material impact on the Company s consolidated financial statements. The Company has one VIE with an impact on total assets of \$1,389,217 as at March 31, 2005. The Company has consolidated this VIE, which involves an investment in a hedge fund managed by INTL Consilium. The effect of the consolidation is to recognize a minority interest of \$1,389,217 on the Condensed Consolidated Balance Sheets at March 31, 2005 and a minority interest in the income of the VIE of \$12,966 on the Condensed Consolidated Statements of Operations for the six months ended March 31, 2005.

(5) Basic and Diluted Earnings Per Share

Basic earnings per share for the six months and three months ended March 31, 2005 and 2004 have been computed by dividing net income by the weighted average number of common shares outstanding.

Common stock equivalents (including options, warrants and convertible subordinated notes) to purchase 53,750 and 2,307,056 shares of common stock were excluded from the calculation of diluted earnings per share for the six months ended March 31, 2005 and 2004, respectively, because the exercise prices of these options exceeded the average market price of the common stock for the period (i.e. they were anti-dilutive). Common stock equivalents to purchase 53,750 and 9,200 shares of common stock were excluded from the calculation of diluted earnings per share for the three months ended March 31, 2005 and 2004, respectively, because the exercise prices of these options exceeded the average market price of the common stock for the period.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

For the six months ended March 31,

| | <u>2005</u> | <u>2004</u> |
|--|------------------|------------------|
| | | (as restated) |
| Diluted earnings per share | | |
| Numerator: | | |
| Net income | \$ 991,480 | 1,622,338 |
| Denominator: | | |
| Weighted average number of: | | |
| Common shares outstanding | 7,186,054 | 4,738,214 |
| Dilutive potential common shares outstanding | 851,005 | 808,382 |
| | <u>8,037,059</u> | <u>5,546,596</u> |
| Diluted earnings per share | \$ 0.12 | 0.29 |

For the three months ended March 31,

| | <u>2005</u> | <u>2004</u> |
|--|------------------|------------------|
| | | (as restated) |
| Diluted earnings per share | | |
| Numerator: | | |
| Net income | \$ 379,313 | 851,483 |
| Denominator: | | |
| Weighted average number of: | | |
| Common shares outstanding | 7,288,778 | 4,763,724 |
| Dilutive potential common shares outstanding | 786,687 | 890,678 |
| | <u>8,075,465</u> | <u>5,654,402</u> |
| Diluted earnings per share | \$ 0.05 | 0.15 |

(6) Issuance of Convertible Subordinated Notes, Conversion of Subordinated Notes in Common Shares, related Debt Issuance Costs and Beneficial Conversion Feature

On March 12, 2004, the Company issued \$12,000,000 in principal amount of the Company's 7% convertible subordinated notes (the Notes) due December 31, 2014. The Notes were issued at par and bore interest at the rate of 7% per annum, payable semi-annually on June 30 and December 31 of each year. They were redeemable, in whole or in part at the option of the Company, at any time on or after December 31, 2009 at a redemption price in cash equal to 115% of the principal balance. The Notes were general unsecured obligations of the Company. The conversion features of the Notes were approved by the shareholders on March 26, 2004. The Notes were convertible by the holders at any time prior to the maturity date of December 31, 2014 into shares of the Company's common stock at a conversion price of \$5.75 per share. The Company was authorized to cause the outstanding principal balance of the Notes to be converted, in whole or in part, into shares of common stock at any time during the 90 days following the occurrence of all of the following three events: (i) the closing price of the common stock exceeding \$8.00 per share (proportionately adjusted to reflect adjustments to conversion price) for 20 consecutive days; (ii) the Company filing a registration statement under the Securities Act to register the issuance of the common stock pursuant to the conversion of the Notes; and, (iii) such registration statement being declared effective by the SEC.

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On August 13, 2004, the Company converted the outstanding Notes into shares of the Company's common stock because the Company had fulfilled the necessary conditions set forth in the Notes allowing for such conversion. As a result of the conversion, the Company issued 2,086,923 shares of common stock to the holders of the Notes, in exchange for the cancellation of \$12,000,000 in outstanding debt.

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Debt issuance costs of \$1,890,828 were incurred in connection with the issuance of the Notes. This total included \$997,706 of costs settled in cash for commissions, placement agent fees, professional fees and state filing fees. This total also included \$893,121 for the Black-Scholes valuation (\$6.00 strike price, 3 year life, risk free rate 2.27%) for the 200,000 warrants issued to the placement agent for placement agent services. Prior to the conversion, the total debt issuance costs were being amortized over the life of the Notes (through December 31, 2014) and charged to interest expense. Upon conversion of the Notes, these debt issuance costs (\$1,812,004) were charged to additional paid in capital as part of the capitalization of the newly issued 2,086,923 common shares.

The Notes were convertible by investors at a price lower than the fair value of the Company's stock on March 26, 2004 (the date that the Company's shareholders approved the conversion terms of the Notes), requiring accounting recognition of this beneficial conversion feature as a debt discount against the Notes. This gave rise to an increase in the Company's additional paid-in capital of \$2,483,478 and a matching expense item that was classified as interest, resulting in reduced net income for the year but having no effect on total stockholders' equity at September 30, 2004. For the period prior to conversion, the total debt discount was amortized over the life of the Notes (through December 31, 2014) and charged to interest expense. During the quarter ended March 31, 2004, amortization of \$3,698 was charged to interest expense. During the quarter ended June 30, 2004 and upon conversion of the Notes remainder of the debt discount (\$2,479,780) was charged to interest expense.

(7) Reclassifications

Certain prior period amounts have been reclassified to conform to current period presentation.

(8) Investment in Asset Management Joint Venture

On May 11, 2004, the Company entered into an agreement with Consilium Investment Capital, Inc. (CIC) of Fort Lauderdale, Florida to form INTL Consilium, LLC (INTL Consilium). INTL Consilium is an investment management firm which primarily provides investment advice with respect to emerging market securities. In June 2004 the Company made a capital contribution of \$500,000 and CIC a capital contribution of \$100,000 to INTL Consilium. The Company's total capital contribution was allocated as \$100,401 share capital and \$399,599 excess capital. The excess capital contribution was made by the Company in recognition of the asset management skills and relationships contributed by CIC. The excess capital contribution has a liquidation preference of three years. The Company is entitled to receive 50.1% of the profits and losses of INTL Consilium. The Company and CIC are each entitled to appoint two of the four directors of INTL Consilium. Two principals of CIC actively manage the business of INTL Consilium. The Company has assessed the joint venture using the consolidation criteria in FIN 46R and concluded that INTL Consilium is not a variable interest entity. Accordingly, the Company assessed the consolidation criteria established by EITF 96-16 by reviewing the voting rights of each investor in INTL Consilium and, due to certain specified operating matters that require board approval, concluded that its investment in INTL Consilium should be accounted for utilizing the equity method of accounting.

For the six months and three months ended March 31, 2005 the Company has recorded revenue of \$69,030 and \$29,672, representing the Company's equity in the net income of INTL Consilium.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued**INTL Consilium, LLC****Condensed Statement of Operations****For the Six Months Ended March 31, 2005**

| | |
|---|------------|
| Revenues: | |
| Management and investment advisory fees | \$ 567,428 |
| Interest | 2,334 |
| Other | 2,307 |
| | <hr/> |
| Total revenues | 572,069 |
| Non-interest expenses: | |
| Compensation and benefits | 300,021 |
| Occupancy and equipment rental | 22,232 |
| Professional fees | 32,761 |
| Depreciation | 4,206 |
| Business development | 23,087 |
| Insurance | 21,330 |
| Other | 28,153 |
| | <hr/> |
| Total non-interest expenses | 431,790 |
| | <hr/> |
| Net income | \$ 140,279 |
| | <hr/> |

INTL Consilium, LLC**Condensed Statement of Operations****For the Three Months Ended March 31, 2005**

| | |
|---|------------|
| Revenues: | |
| Management and investment advisory fees | \$ 298,935 |
| Interest | 1,151 |
| Other | |
| | <hr/> |
| Total revenues | 300,086 |
| Non-interest expenses: | |
| Compensation and benefits | 160,951 |
| Occupancy and equipment rental | 11,537 |
| Professional fees | 18,900 |
| Depreciation | 2,765 |
| Business development | 16,076 |
| Insurance | 11,259 |

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| | |
|-----------------------------|-----------|
| Other | 16,877 |
| Total non-interest expenses | 238,365 |
| Net income | \$ 61,721 |

Table of Contents**INTL Consilium, LLC****Condensed Balance Sheet**

| | March 31, 2005 |
|---|---------------------------|
| <u>Assets</u> | |
| Cash | 306,633 |
| Receivable from clients | 148,231 |
| Investment in INTL Consilium sponsored fund | 176,472 |
| Property and equipment, net | 32,032 |
| Other assets | 11,612 |
| | <hr/> |
| Total assets | \$ 674,980 |
| | <hr/> |
| <u>Liabilities and Members' Equity</u> | |
| Liabilities: | |
| Accounts payable | 5,084 |
| Accrued compensation and benefits | 13,799 |
| | 18,883 |
| Members' equity | |
| Common stock | 200,401 |
| Excess capital contribution | 399,599 |
| Retained earnings | 56,097 |
| | <hr/> |
| Total members' equity | 656,097 |
| | <hr/> |
| Total liabilities and members' equity | \$ 674,980 |
| | <hr/> |

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued**(9) Investment in INTL Consilium Sponsored Fund**

Investment in INTL Consilium Sponsored Fund consists of the Company's investment in a hedge fund managed by INTL Consilium. The fund primarily invests in emerging market debt securities. At March 31, 2005 the Company owned approximately 69% of the total assets of the fund. Accordingly, the Company has consolidated the fund under the provisions of FIN 46R at March 31, 2005.

As indicated in note 8, the Company owns 50.1% of INTL Consilium, the fund's investment manager, through a joint venture agreement. The Company invested \$3,000,000 in the fund in July 2004. Change in the net asset value is included in Net dealer inventory and investment gains in the Condensed Consolidated Statements of Operations. Investment withdrawals require ninety days' written notice to the manager of the fund as well as additional limitations on the amount of withdrawal. The manager may waive the withdrawal limitations in its sole discretion.

| | March 31, 2005 |
|--|---------------------------|
| Investment in INTL Consilium Sponsored Fund | |
| International Assets Holding Corporation | \$ 3,108,282 |
| Minority owners' interest | 1,389,217 |
| Investment in INTL Consilium Sponsored Fund | 4,497,499 |
| Percentage of fund owned by International Assets Holding Corporation | 69% |

(10) Acquisition of the Foreign Exchange Business of Global Currencies Limited

On July 9, 2004 the Company completed the acquisition of the foreign exchange business of Global Currencies Limited through the purchase of all of the shares of INTL Holdings (U.K.) Limited. INTL Holdings (U.K.) Limited is a U.K. holding company that owns 100% of INTL Global Currencies Limited (INTL Global Currencies). The primary reason for the acquisition was to accelerate the Company's efforts to establish a foreign exchange business. Consolidated results of operations have been included for the period from July 9, 2004 through September 30, 2004. The Company made cash payments of \$4,594,440 and issued 150,000 common shares of the Company valued at \$1,471,500 as of the date of the purchase. The cash payments consisted of \$1,000,000 cash premium paid to the sellers, \$3,577,375 for the value of the net assets received, less negotiation differences of \$49,982 related to fixed asset amounts and stamp duty adjustments. In addition, the Company paid \$67,047 for legal and accounting related fees.

The Company is obligated to make certain earn-out payments to the sellers. In particular, the Company is obligated to pay the Sellers an amount equal to 20% of the gross foreign exchange trading profits generated by the Company during the 30 months ending on December 31, 2006 (up to a maximum of \$4.0 million). Additionally, the Company is obligated to pay the Sellers 10% of the gross foreign exchange trading profits in excess of \$10.0 million per year for the 12 months ended June 30, 2005 and June 30, 2006, and 10% of such profits in excess of \$5.0 million for the 6 months ended December 31, 2006.

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The Company negotiated a purchase price that resulted in recognition of goodwill based on factors including anticipated revenues, cash flows, profitability and synergistic human resource sharing including trading staff, operations, administration and management.

The Company funded the acquisition from its existing working capital, which included amounts previously generated from the Company's issuance of \$12,000,000 of Notes in March 2004.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

| | |
|--|---------------|
| Receivable from brokers, dealers and clearing | \$ 15,309,696 |
| Receivable from customers | 3,763,377 |
| Fixed assets | 45,511 |
| | <hr/> |
| Total assets | 19,118,584 |
| | <hr/> |
| Payable to brokers, dealers and clearing organizations | 79,745 |
| Payable to customers | 8,097,688 |
| Demand loan payable | 7,215,486 |
| Accrued expenses | 115,127 |
| Income taxes payable | 33,163 |
| | <hr/> |
| Total liabilities | 15,541,209 |
| | <hr/> |
| Total net assets acquired | \$ 3,577,375 |
| | <hr/> |

(11) Goodwill and Intangible Assets

The purchase price paid by the Company for the acquisition of the foreign exchange business of Global Currencies Limited exceeded the net asset value received by \$2,488,565. This amount was treated as goodwill. The Company has accrued additional goodwill of \$1,046,074 under the earnout provisions of the purchase agreement. This accrual is reported as deferred acquisition consideration payable.

The goodwill related to the INTL Global Currencies acquisition is as follows:

| | |
|---|--------------|
| Cash premium paid to sellers | \$ 1,000,000 |
| Cash paid for net assets received | 3,577,375 |
| Negotiation differences for fixed assets and stamp duty | (49,982) |
| Legal and accounting fees | 67,047 |
| Value of 150,000 common shares at \$9.81 per share | 1,471,500 |
| | <hr/> |
| Total payments of cash and shares | 6,065,940 |
| Less: Fair value of net assets received | 3,577,375 |
| Less: Intangible assets identified by independent valuation | 350,000 |
| | <hr/> |
| Initial goodwill | 2,138,565 |
| Additional goodwill under earnout based on foreign exchange revenues from July 9, 2004 through March 31, 2005 | 1,046,074 |
| | <hr/> |
| Total goodwill as of March 31, 2005 | \$ 3,184,639 |
| | <hr/> |

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The additional goodwill will be calculated for each period as each earnout payment is earned and an adjustment will be recorded to goodwill. The additional payments will be due one year after the closing date of July 9, 2004 and each six months thereafter, until December 2006.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

The intangible assets identified by an independent valuation related to the INTL Global Currencies acquisition are as follows:

| | March 31, 2005 |
|---|---------------------------|
| Intangible assets | |
| Noncompete agreement | \$ 150,000 |
| Trade name | 100,000 |
| Customer base | 100,000 |
| Total intangible assets | 350,000 |
| Less: Amortization of intangible assets | 58,333 |
| Intangible assets, net | 291,667 |

The intangible assets are amortized over their useful lives of three years.

(12) Commission Revenue and Wholesale Commission Expense

Commission revenues of \$309,302 and \$501,545 were reported for the six months ended March 31, 2005 and 2004, respectively. These revenues were primarily related to introducing broker fees that the Company received in connection with its wholesale debt trading activities.

| For the six months ended March 31, | 2005 | 2004 |
|---|-------------|-------------|
| Wholesale commission revenue | \$ 501,918 | 942,573 |
| Amounts paid to wholesale third party | (192,616) | (441,028) |
| Net wholesale commission revenue | 309,302 | 501,545 |
| For the three months ended March 31, | 2005 | 2004 |
| Wholesale commission revenue | \$ 230,339 | 476,860 |
| Amounts paid to wholesale third party | (78,389) | (221,151) |
| Net wholesale commission revenue | 151,950 | 255,709 |

(13) Related Party Transactions

In November 2004 one of the Company's principal shareholders increased its investment in a hedge fund managed by INTL Consilium from \$50,000,000 to \$89,000,000. In November 2004, an executive of this shareholder was elected to the Board of Directors of the Company.

(14) Financial Instruments Owned and Financial Instruments Sold, Not Yet Purchased, at Market Value

Financial instruments owned and financial instruments sold, not yet purchased, at March 31, 2005 and September 30, 2004 consisted of trading and investment financial instruments at market values as follows:

| | <u>Owned</u> | <u>Sold, not yet purchased</u> |
|--|----------------------|--|
| March 31, 2005: | | |
| Common stock and American Depository Receipts | \$ 2,515,182 | 2,514,828 |
| Foreign ordinary stocks, paired with their respective American Depository Receipts | 9,210,375 | 9,277,734 |
| Corporate and municipal bonds | 603,453 | 69,032 |
| Foreign government obligations | 4,699,019 | 409,929 |
| Negotiable instruments (promissory notes) | 2,835,396 | |
| U.S. Treasury Bonds under total return swap transactions | | 29,321,109 |
| Options and futures | 1,387,554 | 1,342,708 |
| Commodities | 10,731,009 | 10,731,000 |
| Other investments | 49,475 | |
| | <u>\$ 32,031,463</u> | <u>53,666,340</u> |

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

| | <u>Owned</u> | <u>Sold, not yet purchased</u> |
|--|----------------------|--|
| September 30, 2004: | | |
| Common stock and American Depository Receipts | \$ 1,546,117 | 1,401,367 |
| Foreign ordinary stocks, paired with their respective American Depository Receipts | 8,851,358 | 8,935,260 |
| Corporate and municipal bonds | 2,085,122 | |
| Foreign government obligations | 1,529,410 | 454,025 |
| Negotiable instruments (promissory notes) | 2,905,812 | |
| Options and futures | 1,762,052 | 1,519,891 |
| Commodities | 55,076 | |
| U.S. Government obligations | 17,194 | |
| Other investments | 53,484 | |
| | <u>\$ 18,805,625</u> | <u>12,310,543</u> |

(15) Trust Certificates and Total Return Swap

During the quarter ended December 31, 2004, the Company entered into a series of financial transactions (the Transactions) with an unaffiliated financial institution in Latin America for a transaction fee. These Transactions involved three distinct and simultaneous steps:

- a) the acquisition by the Company of beneficial interests (Trust Interests) in certain trusts (the Trusts) in exchange for the assumption of a liability to deliver securities, at a transaction value of \$29,739,902. This step did not require any prior purchase or delivery of securities by the Company. The Trusts were previously established by the financial institution to hold a variety of assets;
- b) the entry into a repurchase agreement under the terms of which the Company notionally repurchased these undelivered securities for cash, at a price of \$29,739,902;
- c) the entry into a total return swap (TRS) agreement.
 - i) Under the TRS agreement the Company received, on a notional basis, the cash amount of \$29,739,902 as collateral for the potential liability of the financial institution to the Company.
 - ii) Receivables or payables arising from the TRS should leave the Company unaffected by any changes in the values of the Trust Interests or securities deliverable.
 - iii) When the Transactions terminate in December 2005 and November 2007 the Company intends to sell the Trust Interests at their then prevailing market values. As part of the Transactions, the gain or loss arising from the change in market value of the Trust Interests will be passed to the financial institution.

- iv) The Company has obtained legal advice on the Transactions and believes that the TRS agreement has been structured in such a way as to fully offset any changes in the value of the Trust Interests against its liability to deliver certain securities to the financial institution.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

Under FIN 39 the nominal payment and receipt of an equal amount of cash as described in b) and c) i) above have a net effect of zero on the Company's cash position, represent transactions with a single counterparty and may therefore be offset. Under FIN 39 the asset of securities receivable under the repurchase agreement in b) may be offset against the collateral liability of the Company in c) ii), since they involve an asset and liability position with a single counterparty.

The net result is that the Company reports the effects of a) above as an increase in assets of \$29,739,902 (represented by the Trust Interests), and the assumption of a liability to deliver securities. Over time, as the values of the Trust Interests and securities deliverable may change, the Company will experience equal and offsetting changes in the values of the TRS receivables or payables. Although the Transactions will temporarily increase the Company's assets and liabilities until termination, the Company expects that the only impact of the transactions on the Company's net cash flow will be the Company's receipt of fee revenue.

The total fees received and to be received on the Transactions, as well as the associated variable compensation payable, are spread on a straight-line basis over the terms of the Transactions. Non-refundable fees received but not yet recognized as revenue, amounting to \$280,755, appear as a liability on the Condensed Consolidated Balance Sheets as at March 31, 2005 under "Other liabilities". Non-recoverable costs incurred in connection with the Transactions but not yet recognized as expenses, amounting to \$84,227, appear as an asset under "Other assets" at the same date.

(16) Financial Instruments with Off-Balance Sheet Risk and Concentrations of Credit Risk

The Company is party to certain financial instruments with off-balance sheet risk in the normal course of business as a registered securities broker-dealer and from its market making and proprietary trading in the foreign exchange and commodities trading business. The Company has sold financial instruments that it does not currently own and will therefore be obligated to purchase such financial instruments at a future date. The Company has recorded these obligations in the consolidated financial statements at March 31, 2005 at market values of the related financial instruments (totaling \$53,666,340). The Company will incur losses if the market value of the financial instruments increases subsequent to March 31, 2005. The total of \$53,666,340 includes \$1,342,708 for options and futures contracts, which represent a liability to the Company based on their market value as of March 31, 2005.

Listed below is the fair value of trading-related derivatives as of March 31, 2005 and September 30, 2004. Assets represent net unrealized gains and liabilities represent net unrealized losses.

| | March 31, 2005 | | September 30, 2004 | |
|------------------------------|----------------|--------------|--------------------|--------------|
| | Assets | Liabilities | Assets | Liabilities |
| Interest Rate Derivatives | \$ 6,925 | \$ | \$ | \$ 984 |
| Foreign Exchange Derivatives | \$ 22,041 | \$ 1,861 | \$ 48,822 | \$ 3,350 |
| Commodity Price Derivatives | \$ 1,358,588 | \$ 1,340,847 | \$ 1,713,230 | \$ 1,515,557 |
| Total | \$ 1,387,554 | \$ 1,342,708 | \$ 1,762,052 | \$ 1,519,891 |

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Options and futures contracts held by the Company result from its customer market-making and proprietary trading activities in the foreign exchange/commodities trading business segment. The Company assists its

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commodities clients in protecting the value of their future production (precious or base metals) by selling them put options on an OTC basis. The Company also provides its commodities clients with sophisticated option products, including combinations of buying and selling puts and calls. The Company mitigates its risk by effecting offsetting OTC options with market counterparties or through the purchase or sale of commodities futures traded through the COMEX division of the New York Mercantile Exchange. The risk mitigation of offsetting options is not within the documented hedging designation requirements of FAS 133.

These derivative contracts are traded along with cash transactions because of the integrated nature of the markets for such products. The Company manages the risks associated with derivatives on an aggregate basis along with the risks associated with its proprietary trading and market-making activities in cash instruments as part of its firm-wide risk management policies.

In the normal course of business, the Company purchases and sells financial instruments and foreign currency as either principal or agent on behalf of its customers. If either the customer or a counterparty fails to perform, the Company may be required to discharge the obligations of the nonperforming party. In such circumstances, the Company may sustain a loss if the market value of the financial instrument or foreign currency is different from the contract value of the transaction.

The majority of the Company's transactions and, consequently, the concentration of its credit exposure is with customers, broker-dealers and other financial institutions. These activities primarily involve collateralized and uncollateralized arrangements and may result in credit exposure in the event that the counterparty fails to meet its contractual obligations. The Company's exposure to credit risk can be directly impacted by volatile financial markets, which may impair the ability of counterparties to satisfy their contractual obligations. The Company seeks to control its credit risk through a variety of reporting and control procedures, including establishing credit limits based upon a review of the counterparties financial condition and credit ratings. The Company monitors collateral levels on a daily basis for compliance with regulatory and internal guidelines and requests changes in collateral levels as appropriate.

(17) Interest Income and Interest Expense

For the six months ended March 31,

| | <u>2005</u> | <u>2004</u> |
|---|-------------|---------------|
| | | (as restated) |
| Interest income and interest expense: | | |
| Interest income | \$ 131,264 | 63,771 |
| Interest expense: | | |
| Borrowing to support foreign exchange business | \$ 197,994 | |
| Short securities trading position balances | 240,005 | 80,334 |
| Convertible subordinated notes payable | | 63,243 |
| Amortization of debt issuance costs | | 14,545 |
| Amortization of debt discount from beneficial conversion feature of convertible notes | | 3,698 |
| Other | 34,660 | |
| Interest expense | \$ 472,659 | 161,820 |

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| For the three months ended March 31, | 2005 | 2004 |
|---|-------------------|-------------------|
| | <u> </u> | <u> </u> |
| | | (as restated) |
| Interest income and interest expense: | | |
| Interest income | \$ 82,122 | 36,824 |
| | <u> </u> | <u> </u> |
| Interest expense: | | |
| Borrowing to support foreign exchange business | \$ 97,964 | |
| Short securities trading position balances | 168,862 | 56,266 |
| Convertible subordinated notes payable | | 63,243 |
| Amortization of debt discount from beneficial conversion feature of convertible notes | | 3,698 |
| Amortization of debt issuance costs | | 14,545 |
| Other | 28,921 | |
| | <u> </u> | <u> </u> |
| Interest expense | \$ 295,747 | 137,752 |
| | <u> </u> | <u> </u> |

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued**(18) Dividend Income and Expense, net**

For the six months ended March 31,

| | <u>2005</u> | <u>2004</u> |
|---------------------------------|---------------------|-----------------|
| Dividend income (expense), net: | | |
| Dividend income | \$ 113,723 | 59,832 |
| Dividend expense | (243,911) | (140,583) |
| Dividend (expense) income, net | <u>\$ (130,188)</u> | <u>(80,751)</u> |

For the three months ended March 31,

| | <u>2005</u> | <u>2004</u> |
|---------------------------------|---------------------|-----------------|
| Dividend income (expense), net: | | |
| Dividend income | \$ 28,755 | 28,058 |
| Dividend expense | (158,064) | (115,513) |
| Dividend (expense) income, net | <u>\$ (129,309)</u> | <u>(87,455)</u> |

(19) Receivables From and Payable to Brokers, Dealers and Clearing Organization

Amounts receivable from and payable to brokers, dealers and clearing organization at March 31, 2005 and September 30, 2004 consisted of the following:

| | <u>Receivables</u> | <u>Payable</u> |
|--|----------------------|------------------|
| March 31, 2005: | | |
| Open securities transactions with clearing organization, net | \$ 1,064,297 | |
| Securities clearing fees and related charges payable with clearing organization, net | | 101,623 |
| Open foreign currency transactions | 10,634,070 | 2,208,620 |
| Open commodities transactions | 2,379 | |
| Introducing fee receivable | 59,021 | |
| | <u>\$ 11,759,767</u> | <u>2,310,243</u> |
| September 30, 2004: | | |
| Open securities transactions with clearing organization, net | \$ | 6,314,652 |
| Securities clearing fees and related charges payable with clearing organization, net | | 58,402 |
| Open foreign currency transactions | 7,552,215 | 2,899,803 |
| Introducing fee receivable | 147,235 | |

| | | |
|--|------------------|------------------|
| | <u>7,699,450</u> | <u>9,272,857</u> |
|--|------------------|------------------|

Receivables and payables to brokers, dealers and clearing organization result from open trading activities between the Company and other financial institutions including banks, securities broker-dealers, market makers and counter-parties. Receivables and payables to certain organizations are reported net, when a right of setoff exists with the broker, dealer or clearing organization. As these amounts are short-term in nature, the carrying amount is a reasonable estimate of fair value.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued**(20) Receivable From and Payable to Customers**

Amounts receivable from and payable to customers at March 31, 2005 and September 30, 2004 consisted of the following:

| | <u>Receivables</u> | <u>Payable</u> |
|---|----------------------|-------------------|
| March 31, 2005: | | |
| Open transactions- foreign currency trading | \$ 11,550,673 | 10,003,704 |
| Open transactions other debt structures | 27,549 | 418,793 |
| Margin deposits held - commodities trading | | 216,174 |
| Pledge receivable - commodities trading | 1,986,750 | |
| | <u>\$ 13,564,972</u> | <u>10,638,671</u> |
| September 30, 2004: | | |
| Open transactions- foreign currency trading | \$ 11,018,572 | 4,613,147 |
| Open transactions other debt structures | | 41,000 |
| Margin deposits held - metals trading | | 11,036 |
| Pledge receivable - commodities trading | 1,339,840 | |
| | <u>\$ 12,358,412</u> | <u>4,665,183</u> |

Receivables and payables to customers result from open trading activities between the Company and its customers which are not financial institutions or broker-dealers. Receivables and payables to certain customers are reported net, when a right of setoff exists with the customer.

(21) Other Assets

Other assets at March 31, 2005 and September 30, 2004 consisted of the following:

| | <u>March 31, 2005</u> | <u>September 30, 2004</u> |
|------------------------------------|---------------------------|-------------------------------|
| Other receivables | \$ 4,041 | 32,651 |
| Deposit with clearing organization | 500,000 | 500,000 |
| Prepaid expenses and other assets | 347,025 | 128,990 |
| | <u>\$ 851,066</u> | <u>661,641</u> |

(22) Payable to Banks Under Loans and Overdrafts

At March 31, 2005, the Company had lines of credit with three commercial banks totaling \$23,000,000. Each credit facility is secured by certain assets. In addition, the Company has a \$3,000,000 on-demand overdraft facility with one U.S. commercial bank.

At September 30, 2004, INTL Global Currencies had a multi-currency on-demand overdraft facility of up to \$7,000,000 with a commercial bank based in the United Kingdom. The overdraft facility provided a right of set-off between amounts borrowed in one or more currencies against positive balances in one or more other currencies. Amounts borrowed bear interest at the London Interbank Offered Rates (LIBOR) for each currency plus 2%. The overdraft facility was guaranteed by International Assets Holding Corporation. At September 30, 2004, the net borrowings of INTL Global Currencies exceeded its credit facility limit by \$3,447,417. This excess borrowing was guaranteed by a cross-lending guarantee from the former owner of the foreign exchange trading business of INTL Global Currencies. The former owner of the foreign exchange business was not obligated by any written agreement to provide access to this additional credit. The guarantee terminated during the quarter ended December 31, 2004. This on-demand facility was terminated during the quarter ended March 31, 2005.

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At March 31, 2005 the Company had the following credit facilities:

| | |
|-----------------------------|---|
| Amount | \$10,000,000 |
| Borrowing at March 31, 2005 | \$5,925,409 |
| Allocation | Supports Foreign Exchange Trading |
| Borrower | INTL Global Currencies Limited |
| Security | Certain foreign exchange assets |
| Duration | 1 Year |
| Executed | 1/18/2005 |
| Amount | \$3,000,000 |
| Borrowing at March 31, 2005 | \$1,295,925 |
| Allocation | Supports Commodities Trading |
| Borrower | International Assets Holding Corporation |
| Security | Certain commodities assets |
| Duration | On demand |
| Executed | 1/24/2005 |
| Amount | \$10,000,000 |
| Borrowing at March 31, 2005 | \$0 |
| Allocation | Supports Other Debt (trade finance) Trading |
| Borrower | International Assets Holding Corporation |
| Security | Certain other debt trading assets |
| Duration | On demand |
| Executed | 2/1/2005 |

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

At March 31, 2005 and September 30, 2004, the U.S. dollar equivalent of the components of the net borrowing payable to banks were as follows:

| | 2005 | 2004 |
|-------------------------------------|---------------------------------|---------------------------------|
| | Positive balance (overdraft) | Positive balance (overdraft) |
| | U.S. dollar equivalent | U.S. dollar equivalent |
| | <u> </u> | <u> </u> |
| Payable to Banks: | \$ | |
| Lines of Credit | | |
| Commodities trading | | |
| United States Dollar | (1,295,925) | |
| Foreign exchange trading | | |
| Australian Dollar | (131,694) | |
| Danish Krona | (295) | |
| Japanese Yen | (66,745) | |
| Singapore Dollar | (2,862) | |
| United Kingdom Pound Sterling | (259,057) | |
| United States Dollar | (5,464,756) | |
| | <u> </u> | <u> </u> |
| Total Payable under lines of credit | \$ (7,221,334) | |
| | <u> </u> | <u> </u> |

Continued,

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| | March 31, 2005 | September 30, 2004 |
|---|---------------------------------|---------------------------------|
| | Positive balance (overdraft) | Positive balance (overdraft) |
| | U.S. dollar equivalent | U.S. dollar equivalent |
| Payable to Banks: | | |
| Overdraft facility with one U.S. Bank | | |
| United States Dollar | (3,000,000) | |
| Overdraft with other financial institutions | | |
| Indian Rupee | (2,954) | |
| Indonesian Rupiah | (7,354) | |
| Japanese Yen | (112,575) | |
| Namibian Dollar | (601) | |
| Singapore Dollar | (8,874) | |
| United Kingdom Pound Sterling | (52,416) | |
| | <u>(3,184,774)</u> | |
| Overdraft, subtotal | | |
| | <u>(3,184,774)</u> | |
| Overdraft facility with set-off limits (terminated during March 31, 2005 quarter) | | |
| Australian Dollar | \$ | |
| Canadian Dollar | | 698,967 |
| Danish Krona | | 196 |
| Euro | | (2,826,520) |
| Indian Rupee | | (511,067) |
| Indonesian Rupiah | | 2,452 |
| Japanese Yen | | 175 |
| Mexican Peso | | 4,244 |
| Namibian Dollar | | (4,897) |
| Norwegian Krona | | 441 |
| South African Rand | | 12,325 |
| Swedish Krona | | 5,770 |
| Swiss Franc | | (76,697) |
| United Kingdom Pound Sterling | | (2,202,841) |
| United States Dollar | | (5,549,965) |
| | | <u>(10,447,417)</u> |
| Overdraft with one U.K. bank | | <u>(10,447,417)</u> |
| Summary: | | |
| Total due to banks under overdraft | (3,184,774) | (10,447,417) |
| Total due to banks under lines of credit | (7,221,334) | |
| | <u>(10,406,108)</u> | <u>(10,447,417)</u> |
| Total Payable to Banks Under Loans and Overdrafts | <u>(10,406,108)</u> | <u>(10,447,417)</u> |

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued**(23) Capital and Cash Reserve Requirements**

INTL Trading is subject to the net capital rules imposed by the Securities and Exchange Commission under SEC Rule 15c3-1. This rule requires maintenance of minimum net capital of an amount equal to the greater of \$100,000, 6²/₃ percent of aggregate indebtedness, or \$2,500 for each security in which a market is made with a bid price over \$5 and \$1,000 for each security in which a market is made with a bid price of \$5 or less with a ceiling of \$1,000,000. Rule 15c3-1 also requires that the ratio of aggregate indebtedness to net capital not exceed 15 to 1. As of March 31, 2005, the Company had excess net capital of \$2,899,660, a ratio of aggregate indebtedness to net capital of 1.53 to 1 and a percentage of debt to debt-equity total computed in accordance with Rule 15c3-1(d) of 28%.

INTL Trading is exempt from the customer reserve requirements and providing information relating to possession or control of securities pursuant to SEC Rule 15c3-3 because INTL Trading meets the exemption set forth in SEC Rule 15c3-3(k)(2)(ii).

(24) Leases

The Company leases approximately 5,100 square feet of office space at 220 E. Central Parkway in Altamonte Springs, Florida. This lease commenced on February 1, 2002 and expires on July 31, 2009. The Company leases approximately 5,300 square feet of office space at 708 Third Avenue in New York, New York. This lease commenced on December 13, 2002, and expires on September 30, 2009. The Company leases approximately 1,500 square feet of office space at Nedbank House, 20 Abchurch Lane, London. This lease commenced on October 1, 2003 and expires on January 31, 2006. The London office space is shared with the previous owners of the foreign exchange business under a shared cost apportionment arrangement. During 2004 the Company leased approximately 310 square feet of office space at 1111 Brickell Avenue in Miami, Florida. This lease commenced on December 18, 2002, and expired on January 31, 2004.

The Company is obligated under various noncancelable operating leases for the rental of office facilities, service obligations and certain office equipment. The expense associated with operating leases amounted to \$474,200 and \$295,157 for the six months ended March 31, 2005 and 2004, respectively. The expense associated with the operating leases and service obligations are reported in the statements of operations in occupancy and equipment rental, clearing and related and other expenses.

Future minimum lease payments under noncancelable operating leases as of March 31, 2005 are as follows:

| | |
|--|------------|
| Fiscal Year (12 month period) ending September 30, | |
| 2005 | \$ 804,400 |
| 2006 | 564,100 |
| 2007 | 369,400 |
| 2008 | 328,000 |
| 2009 | 303,100 |
| Thereafter | 700 |

| | |
|-------------------------------------|--------------|
| Total future minimum lease payments | \$ 2,369,700 |
|-------------------------------------|--------------|

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued**(25) Stock Options**

During the six months ended March 31, 2005, the Company granted incentive stock options covering 124,650 shares of common stock. During the six months ended March 31, 2005, incentive stock options covering 264,889 shares of common stock were exercised and 44,518 shares were forfeited. During the six months ended March 31, 2005, 80,900 shares of common stock were exercised under existing nonqualified stock options. As of March 31, 2005, the Company had outstanding total options covering 1,016,349 shares of common stock and the Company has 275,000 shares available for issuance under its existing option plans.

Incentive Stock Options (Granted during the six months ended March 31, 2005)

| Options | | Exercise Price | | | |
|----------------|-------------------|-----------------------|--|------------------------|--------------------|
| Granted | Grant Date | Per Share | | Expiration Date | Exercisable |
| 52,500 | 11/18/04 | \$ 7.45 | | 11/18/08 | (a) |
| 50,000 | 11/18/04 | \$ 8.568 | | 11/18/08 | (b) |
| 20,000 | 12/01/04 | \$ 7.35 | | 12/01/08 | (a) |
| 2,150 | 02/01/05 | \$ 8.39 | | 02/28/05 | (c) |
| 124,650 | | | | | |

- (a) Exercisable at 33% after year one, 33% after year two and 34% after year three.
(b) Exercisable at 33% on January 2 2006, 33% on November 18, 2006 and 34% on November 18, 2007.
(c) 100% Exercisable on February 1, 2005. 2,150 shares were exercised by February 28, 2005.

The Company did not recognize any compensation expense in connection with the grant of incentive stock options covering 124,650 shares during the six months ended March 31, 2005, because the exercise price on the date of grant for each option was equal to or greater than the fair market value of the common stock on the date of grant.

(26) Commitments and Contingent Liabilities

The Company has entered into employment agreements with two officers, effective October 1, 2004 and December 1, 2004 respectively, that each have an indefinite term. Under the terms of the agreements each officer will receive specified annual compensation and have the right to receive bonuses as determined by the Board of Directors. In the event of termination of either agreement by the Company other than for cause, or if the officer concerned resigns as a result of a breach by the Company, each agreement provides for payments equal to 100% of total compensation for 120 days following date of termination.

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The employment of the Company's former Chief Operating Officer, who resigned from that office in November 2004, terminated effective as of March 15, 2005, but he continues to receive an amount equal to his salary for a period of six months from that date under an existing contractual arrangement.

(27) Segment Analysis

International Assets Holding Corporation and its subsidiaries form a financial services group focused on select international securities, foreign exchange and commodities markets. The Company's activities are currently divided into four functional areas: international equities market making, international debt capital markets, foreign exchange/commodities trading and asset management. During May 2004, the Company expanded into the asset management business through its investment in INTL Consilium. The Company's asset management activities will not be separately reported until certain asset and revenue levels are achieved.

International Equities Market making:

Through INTL Trading, the Company acts as a wholesale market maker in select foreign securities including unlisted American Depositary Receipts (ADRs) and foreign ordinary shares. INTL Trading provides execution and liquidity to national broker-dealers, regional broker-dealers and institutional investors.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

International Debt Capital Markets:

The Company actively trades a wide variety of international debt instruments. The Company also invests in international debt instruments on a proprietary basis and arranges international debt transactions. The Company trades and invests in international bonds, including both investment grade and higher yielding emerging market bonds. The Company generally focuses on smaller issues, such as emerging market sovereign, corporate and bank bonds that trade worldwide on an over-the-counter basis. Through its customer relationships, the Company periodically identifies opportunities to arrange, purchase or sell debt transactions that fall outside the parameters of established financial markets. These transactions generally involve negotiable emerging market debt and may be documented by promissory notes, bills of exchange, loan agreements, accounts receivable and other types of debt instruments. The revenues, expenses, assets and liabilities relating to the Trust Certificate and Total Return Swap discussed in note 15 are included in this segment.

Foreign Exchange/ Commodities Trading:

The Company trades select illiquid currencies of developing countries. The Company's target customers are financial institutions, multi-national corporations, governmental and charitable organizations operating in these developing countries. In addition, the Company executes trades based on the foreign currency flows inherent in the Company's existing international securities activities. The Company primarily acts as a principal in buying and selling foreign currencies on a spot basis. The Company derives revenue from the difference between the purchase and sale prices. The Company periodically holds foreign currency positions for longer periods to create liquidity for customers or generate proprietary earnings potential.

The Company provides a full range of trading and hedging capabilities to select producers, consumers, recyclers and investors in precious metals and some base metals. Acting as a principal, the Company commits its own capital to buy and sell the metals on a spot and forward basis.

Other:

All other transactions that do not relate to the operating segments above are classified as Other. Certain cash accounts and balances were maintained to support administrative as well as all of the operating segments. These multi-segment assets were allocated to Other. Revenue reported for Other includes all the Company's interest income but not interest expense; and the gain or loss on the Company's asset management joint venture, which is accounted for by the equity method.

Segment data includes the profitability measure of net contribution by segment. Net contribution is one of the key measures used by management to assess the performance of each segment and for decisions regarding the allocation of the Company's resources. Net contribution is calculated as revenue less direct clearing and clearing related charges and variable trader compensation. Variable trader compensation represents a fixed percentage of an amount equal to revenues produced less clearing and related charges, base salaries and an overhead allocation.

Inter-segment revenues, charges, receivables and payables are eliminated between segments, excepting revenues and costs related to foreign currency transactions done at arm's length by the foreign exchange trading business for the equity and debt trading business. The foreign exchange trading business competes for this business as it does for any other business. If its rates are not competitive the equity and debt trading businesses buy or sell their foreign currency through other market counter-parties. The profit or loss made by the foreign exchange trading business on these transactions is not quantifiable.

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INTERNATIONAL ASSETS HOLDING CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements, continued

Information concerning operations in these segments of business is shown in accordance with SFAS 131 as follows:

For the six months ending March 31,

| | 2005 | 2004 |
|---|----------------------|-------------------|
| | | (as restated) |
| Revenues: | | |
| International equities market-making | \$ 5,683,000 | 9,704,000 |
| International debt capital markets | 1,112,000 | 1,505,000 |
| Foreign exchange/commodities trading | 5,147,000 | 421,000 |
| Other | 300,000 | 68,000 |
| Total | \$ 12,242,000 | 11,698,000 |
| Net contribution: | | |
| (Revenue less clearing and related expenses and variable trader bonus compensation): | | |
| International equities market-making | \$ 2,465,000 | 5,044,000 |
| International debt capital markets | 777,000 | 1,106,000 |
| Foreign exchange/commodities trading | 3,874,000 | 307,000 |
| Other | | |
| Total | \$ 7,116,000 | 6,457,000 |
| Reconciliation of net contribution to income before income taxes and minority interest | | |
| Net contribution allocated to segments | \$ 7,116,000 | 6,457,000 |
| Fixed costs not allocated to operating segments | 5,540,000 | 3,611,000 |
| Income before income taxes and minority interest | \$ 1,576,000 | 2,846,000 |

For the three months ending March 31,

| | 2005 | 2004 |
|--|---------------------|------------------|
| | | (as restated) |
| Revenues: | | |
| International equities market-making | \$ 3,166,000 | 5,305,000 |
| International debt capital markets | 484,000 | 828,000 |
| Foreign exchange/commodities trading | 2,341,000 | 193,000 |
| Other | 166,000 | 43,000 |
| Total | \$ 6,157,000 | 6,369,000 |
| Net contribution: | | |
| (Revenue less clearing and related expenses and variable trader bonus compensation): | | |
| International equities market-making | \$ 1,409,000 | 2,767,000 |

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| | | |
|--|-------------------|-------------------|
| International debt capital markets | 333,000 | 616,000 |
| Foreign exchange/commodities trading | 1,743,000 | 140,000 |
| Other | | |
| | <u> </u> | <u> </u> |
| Total | \$ 3,485,000 | 3,523,000 |
| | <u> </u> | <u> </u> |
| Reconciliation of net contribution to income before income taxes and minority interest | | |
| Net contribution allocated to segments | \$ 3,485,000 | 3,523,000 |
| Fixed costs not allocated to operating segments | 2,903,000 | 1,951,000 |
| | <u> </u> | <u> </u> |
| Income before income taxes and minority interest | \$ 582,000 | 1,572,000 |
| | <u> </u> | <u> </u> |

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| March 31, | 2005 | 2004 |
|--------------------------------------|-----------------------------|-----------------------------|
| | | (as restated) |
| Total assets: | | |
| International equities market-making | \$ 17,898,000 | 27,997,000 |
| International debt capital markets | 39,232,000 | 3,198,000 |
| Foreign exchange/commodities trading | 46,008,000 | 3,214,000 |
| Other | 6,662,000 | 13,584,000 |
| | <u> </u> | <u> </u> |
| Total | \$ 109,800,000 | 47,993,000 |
| | <u> </u> | <u> </u> |

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

The following discussion and analysis should be read in conjunction with the financial statements and notes thereto appearing elsewhere in this report. This Quarterly Report on Form 10-QSB contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements involve known and unknown risks and uncertainties, many of which are beyond the Company's control, including adverse changes in economic, political and market conditions, losses from the Company's market making and trading activities arising from counter-party failures and changes in market conditions, the possible loss of key personnel, the impact of increasing competition, the impact of changes in government regulation, the possibility of liabilities arising from violations of federal and state securities laws and the impact of changes in technology in the securities and commodities brokerage industries. Although the Company believes that its forward-looking statements are based upon reasonable assumptions regarding its business and future market conditions, there can be no assurances that the Company's actual results will not differ materially from any results expressed or implied by the Company's forward-looking statements. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Readers are cautioned that any forward-looking statements are not guarantees of future performance.

Principal Activities

The Company's principal activities include market making and trading in international financial instruments, foreign currencies and commodities and asset management. The markets in which the Company operates are highly competitive and volatile. The Company has little or no control over many of the factors which affect its operations. As a result, the Company's earnings are subject to potentially wide fluctuations. The Company seeks to counteract many of these influences by focusing on niche, uncorrelated markets and, when possible, linking the Company's expenses to revenues.

The following have been notable events since the beginning of 2004:

In the second quarter of fiscal 2004, the Company raised \$12,000,000 from the issuance of the Company's 7% convertible subordinated notes. The proceeds have been utilized to continue the expansion of the Company's trading businesses.

In the third quarter of fiscal 2004, the Company and an unrelated third party formed INTL Consilium, LLC, an asset management joint venture. The Company received a 50.1% interest in exchange for a \$500,000 capital contribution. INTL Consilium established a hedge fund in July 2004 and currently employs five individuals and manages more than \$96 million on behalf of investors in the fund.

In the fourth quarter of fiscal 2004, the Company acquired INTL Global Currencies, a specialist foreign exchange trading business based in London. Further details are provided below.

In the fourth quarter of fiscal 2004, the Company exercised its right to convert its outstanding 7% subordinated notes into 2,086,923 shares of the Company's common stock.

The Company believes that it continues to make significant progress in its effort to build a diversified financial services firm focusing on niche markets. During the last two years, the Company has successfully acquired or established businesses in key product areas and geographic locations. The Company's activities are currently divided into international equities market making, international debt capital markets, foreign

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exchange/ commodities trading and asset management. Although most of the Company's revenues over the past two fiscal years were generated by international equities market making, foreign exchange trading revenue from the recently-acquired INTL Global Currencies has shifted the balance and, together with growth in other business segments, has produced a more balanced and diversified revenue stream. As a result, the Company believes that it is now less vulnerable to market cycles which affect each of the Company's principal business activities. The Company believes that its strategy of linking expenses to revenues will also help to lessen the negative impact of adverse market conditions which occur periodically in international securities and financial markets.

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The Company is currently focused on increasing revenue and market share for each of its principal business activities. The equities market making activities were expanded during the quarter ended December 31, 2004, by the addition of trading in over-the-counter Bulletin Board stocks and the recruitment of a specialist trader in equity securities of Latin American issuers. During April and May 2005 the Company's international debt capital markets business has hired three sales and trading individuals and four individuals to develop origination, structuring and distribution.

Acquisition of Foreign Exchange Business of Global Currencies Limited

On July 9, 2004, the Company completed the acquisition of the foreign exchange business of Global Currencies Limited through the purchase of all the shares of INTL Holdings (U.K.) Limited. INTL Holdings (U.K.) Limited is a U.K. holding company that owns 100% of INTL Global Currencies Limited. The Company undertook this acquisition in order to expand its foreign exchange business. The results of operations from acquired businesses have been included in the Company's results of operations since July 9, 2004 (the date of the acquisition).

Under the terms of the purchase agreement for the acquisition of Global, the Company made a cash payment of \$4,594,000, and issued 150,000 shares of the Company's common stock (which were valued at \$1,472,000 on the date of the purchase). The cash payment consisted of a \$1,000,000 cash premium paid to the Sellers, and \$3,577,000 for the value of the net assets received, less negotiated differences of \$50,000 related to fixed assets amounts and stamp duties. In addition, the Company paid \$67,000 in legal and accounting fees.

The Company is obligated to make earn-out payments to the sellers of Global. In particular, the Company is obligated to pay an amount equal to 20% of the gross foreign exchange trade profits generated by the Company during the 30 months ending on December 31, 2006 (up to a maximum of \$4,000,000). In addition, the Company is obligated to pay the sellers ten percent (10%) of the gross foreign exchange trading profits in excess of \$10,000,000 per year for the 12 months ending June 30, 2005 and June 30, 2006, and ten percent (10%) of such profits in excess of \$5,000,000 for the six (6) months ended December 31, 2006.

The Company funded the acquisition by utilizing its existing working capital, which included cash received from the Company's private placement of \$12,000,000 in notes of March 2004.

The Company believes that the acquisition of the foreign exchange business of Global will materially increase the Company's revenues and net income from the foreign exchange business based upon the historical financial results of this business.

As noted above, the Company's acquisition of Global utilized approximately \$4,594,000 in cash in connection with the payment of the initial purchase price. The Company expects to make future payments to the sellers of Global pursuant to the earnout provisions of the purchase agreement. The Company expects to fund these payments from working capital generated by the foreign exchange business.

The operations of Global's foreign exchange business, which have been integrated into the Company's existing foreign exchange business, are expected to increase both the Company's net current assets and cash flow in the future.

Results of Operations

Set forth below is the Company's discussion of its results of operations for the first six months of the fiscal years ended September 30, 2005 and 2004, and the fiscal quarters ended March 31, 2005 and 2004. The Company's total revenues for the quarter ended March 31, 2005 (Q2 2005) decreased 3% to \$6,157,000 from \$6,369,000 for the quarter ended March 31, 2004 (Q2 2004). Total non-interest expenses for Q2 2005 were 13% higher than those in Q2 2004, while interest expense increased by \$138,000. The Company's net income decreased from \$851,000 during Q2 2004 to \$379,000 during Q2 2005.

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During Q2 2005 the Company's revenues were adversely affected by relatively difficult market conditions in its securities business and in particular the international equity trading business. The adverse effect of these conditions were offset by a substantial increase in revenues from the Company's foreign currency trading business. The increased foreign exchange trading revenue was due to the inclusion of the results of INTL Global Currencies for the full period. The Company believes that these difficult conditions reflect the cyclical nature of international debt and equity markets generally, and are not necessarily indicative of any long term market trends. The increase in non-interest expenses was attributable mainly to the expanded foreign exchange trading activities and, to a lesser extent, administrative infrastructure to support continued growth.

Table of Contents**Six Months Ended March 31, 2005 (YTD 2005) Compared to Six Months Ended March 31, 2004 (YTD 2004)**

The following table reflects the principal components of the Company's revenues and interest expense as a percentage of total revenue for YTD 2005 and YTD 2004.

| | Percentage | | |
|---|--------------------------------|--------------------------------|-----------------------------------|
| | Percentage of Total Revenue | Percentage of Total Revenue | Change from YTD '04 to YTD '05 |
| | YTD 2005 | YTD 2004 | |
| Trading revenue (Net dealer inventory and investment gains) | 96.9% | 95.8% | 5.8% |
| Commissions | 2.5% | 4.3% | -38.3% |
| Interest income | 1.1% | Less than 1% | 105.8% |
| Dividend income (expense), net | -1.1% | Less than -1% | -61.2% |
| Asset management joint venture income (expense) | Less than 1% | 0% | Not Meaningful |
| Other revenues | Less than 1% | Less than 1% | -34.2% |
| Total revenue | 100% | 100% | 4.7% |
| Interest expense | 3.9% | 1.4% | 192% |
| Net revenue | 96.1% | 98.6% | 2.0% |

The following table reflects the sources of the Company's revenues as a percentage of the Company's total revenue for YTD 2005 and YTD 2004.

| | Percentage | | |
|---------------------------------------|---------------------------------|---------------------------------|-----------------------------------|
| | Percentage of Total Revenues | Percentage of Total Revenues | Change from YTD '04 to YTD '05 |
| | YTD 2005 | YTD 2004 | |
| Equity market making | 47% | 83% | -41% |
| Debt capital markets | 9% | 13% | -26% |
| Foreign exchange/ commodities trading | 42% | 4% | Not Meaningful |
| Other | 2% | Less than 1% | 341% |
| Total revenues | 100% | 100% | 5% |

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The following table reflects the net contribution by percentage of each of the Company's principal business activities for YTD 2004 and YTD 2005. Net contribution consists of revenues from each business activity, less direct clearing and clearing related changes and variable trader compensation.

| | <u>% of Total Net Contribution</u> | <u>% of Total Net Contribution</u> | <u>% Change 2004 to 2005</u> |
|-------------------------------|--|--|--------------------------------------|
| | YTD 2005 | YTD 2004 | |
| Equity market making | 35% | 78% | -51% |
| Debt capital markets | 11% | 17% | -30% |
| Foreign exchange/commodities | 54% | 5% | Not Meaningful |
| Total Net Contribution | 100% | 100% | 10% |

The following table reflects the principal components of the Company's non-interest expenses as a percentage of the Company's total non-interest expenses for YTD 2005 and YTD 2004.

| | <u>Percentage of Total Non- interest Expenses</u> | <u>Percentage of Total Non- interest Expenses</u> | <u>Percentage Change from YTD 04 to YTD 05</u> |
|------------------------------------|---|---|--|
| | YTD 2005 | YTD 2004 | |
| Compensation and benefits | 50.6% | 49.2% | 20.5% |
| Clearing and related expenses | 30.8% | 39.3% | -8.1% |
| Wholesale commission expense | Less than 1% | Less than 1% | Not meaningful |
| Occupancy and equipment rental | 3.5% | 2.8% | 49.8% |
| Professional fees | 2.4% | 1.9% | 49.6% |
| Depreciation and amortization | 1.5% | 1.3% | 34.8% |
| Business Development | 3.7% | 1.8% | 141.6% |
| Insurance | 3.0% | 1.7% | 102.8% |
| Other expenses | 4.4% | 2.0% | 159.5% |
| Total non-interest expenses | 100% | 100% | 17.2% |

Net Income. The Company reported net income of \$991,000 for the six months ended March 31, 2005 (YTD 2005), which equates to \$0.14 per basic share and \$0.12 per diluted share. This compares to net income of \$1,622,000, or \$0.34 per basic share and \$0.29 per diluted share, for the six months ended March 31, 2004 (YTD 2004).

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Total Revenues. The Company's total revenues increased 4.7% to \$12,242,000 for YTD 2005 compared to \$11,698,000 for YTD 2004. The most significant change has been the relative change in the source of the Company's income resulting from the acquisition in July 2004 of INTL Global Currencies. Foreign exchange/commodities trading produced \$5,147,000, or 42% of total revenue for YTD 2005, compared to \$421,000, or 4% of total revenue for YTD 2004. The relative increase in foreign exchange/commodities trading revenue is also attributable to the decline in equity market making revenue. Equity market making revenue fell from \$9,704,000 for YTD 2004 to \$5,683,000 for YTD 2005 as a result of difficult securities trading market conditions. Equity market making revenues decreased from 83% of total revenue for YTD 2004 to 46% of total revenue for YTD 2005. International debt capital markets revenue decreased from \$1,505,000 for YTD 2004 to \$1,112,000 for YTD 2005. Debt trading and commission revenues were lower because of less volatility in the markets (which reduced the opportunity for profitable trades), and tighter interest spreads (which reduced trading volume).

Trading Revenues (Net Dealer Inventory and Investment Gains). The Company had trading income of \$11,860,000 for YTD 2005, compared to \$11,208,000 for YTD 2004. The increase in trading revenue primarily reflected the expansion of the foreign exchange/commodities trading business discussed above. The commodities trading revenues grew by 292% from YTD 2004 to YTD 2005, due to increased business and increased volatility in the price movements of gold and silver. The large growth in this business was partially offset by a 41% reduction in equity market making revenue and a 26% reduction in debt trading revenue.

Total trading revenue includes the trading profits earned by the Company before the related expense deduction for American Depositary Receipt conversion fees. These ADR fees are included in the statement of operations as part of clearing and related expenses.

Commission Revenues. The Company generated commission revenue of \$309,000 for YTD 2005, compared to \$502,000 for YTD 2004. Wholesale brokerage of debt securities declined during YTD 2005 because of tighter interest spreads.

Interest Income. The Company's interest income for YTD 2005 was \$131,000 compared to \$64,000 for YTD 2004. The majority of this interest income is paid by the Company's clearing organization to the Company's broker-dealer subsidiary.

Dividend Income (Expense). The Company's net dividend expense for YTD 2005 was \$130,000 compared to net dividend expense of \$81,000 for YTD 2004. Dividend income or expense is generated when the Company's equity business holds long or short equity positions, respectively, over a dividend declaration date.

Equity in Income from Asset Management Joint Venture. The Company recognized revenue of \$69,000 from the asset management joint venture formed during Q3 2004 and in which the Company has a 50.1% interest. INTL Consilium has achieved early profitability due to the significant level of assets invested in the hedge fund established by INTL Consilium. In this connection, one of the Company's principal shareholders has invested \$89,000,000 into the fund.

Net Contribution. Net contribution consists of revenues less direct clearing and clearing related charges and variable trader compensation. Net contribution is one of the key measures used by management to assess the performance of each segment and for decisions regarding the allocation of the Company's resources. The net contribution allocated to segments for YTD 2005 is \$7,116,000 compared to \$6,457,000 for YTD 2004. The relative changes in net contribution between the equity market making business and the foreign exchange/commodities trading business principally reflects the effects of the acquisition of INTL Global Currencies, together with the revenue decline in the equity business between YTD 2004 and YTD 2005. Equity market making revenues are stated before deduction of ADR conversion fees, while net contribution is stated after these fees.

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Interest Expense. The Company's interest expense was \$473,000 for YTD 2005, compared to \$162,000 for YTD 2004. The expense for YTD 2005 consisted of \$198,000 in interest paid to banks in the INTL Global Currencies business and \$240,000 of interest on financial instruments sold, not yet purchased, due to an increase in ADR conversion activity. Borrowings related to other segments for YTD 2005 consisted of \$35,000.

Total Non-interest Expenses. The Company's total non-interest expenses increased by approximately 17% to \$10,194,000 for YTD 2005 from \$8,690,000 for YTD 2004. This increase was directly attributable to the expansion of the Company's business, which resulted in higher personnel, rents, business development and insurance costs.

Compensation and Benefits. The Company's compensation and benefit expense increased 21% from \$4,278,000 for YTD 2004 to \$5,161,000 for YTD 2005. The increase was primarily a consequence of higher staff levels resulting from the expanded foreign exchange business.

Clearing and Related Expenses. Clearing and related expenses decreased by 8% from \$3,411,000 for YTD 2004 to \$3,135,000 for YTD 2005. The decrease was primarily due to the absence for YTD 2005 of the large, one-time ADR conversion-related charges that were paid for YTD 2004. The decrease was partially offset by an increase in foreign settlement fees, relating to changes in the composition of the equity trading activities, and a large increase in bank charges, relating to the INTL Global Currencies business. The total ADR conversion fees were \$1,041,000 and \$2,014,000 for YTD 2005 and YTD 2004, respectively.

Occupancy and Equipment Rental. Occupancy and equipment rental expense increased by 50% from \$241,000 for YTD 2004 to \$360,000 for YTD 2005. This increase is primarily due to increased occupancy as a result of expansion of the New York office space and the addition of the INTL Global Currencies office space in London; and an increase in information systems equipment corresponding to the increase in the number of employees.

Professional Fees. Professional fees principally consist of legal, taxation and accounting fees. These fees increased 50% from \$164,000 for YTD 2004 to \$245,000 for YTD 2005 mainly as a result of larger accruals for accounting and audit fees in fiscal 2005.

Depreciation and Amortization. Depreciation and amortization increased 35% from \$113,000 for YTD 2004 to \$153,000 for YTD 2005. The Company incurred additional depreciation and amortization costs in YTD 2005 due to depreciation of additional fixed assets in the New York office and depreciation of the fixed assets and amortization of goodwill arising from the acquisition of INTL Global Currencies in July 2004. However, these items were more than offset by the absence of amortization of capitalized software development costs that were fully amortized in fiscal 2004.

Business Development Expense. Business development expense increased 142% from \$157,000 for YTD 2004 to \$380,000 for YTD 2005. Most of this increase relates to the business development activities of INTL Global Currencies, while the balance relates to expanded marketing efforts for the other businesses of the Company.

Insurance Expense. Insurance expense increased 103% from \$149,000 for YTD 2004 to \$302,000 for YTD 2005. The increase was primarily due to increases in the cost of health insurance caused by higher staff levels and increased cost per employee.

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Other Operating Expenses. Other operating expenses increased 160% from \$172,000 for YTD 2004 to \$446,000 for YTD 2005. The increase was primarily related to increased office expenses resulting from expanded staff levels, higher technology and license fees, and value added taxes payable in the United Kingdom by INTL Global Currencies.

Tax Expense. The Company recognized income tax expense of \$572,000 for YTD 2005 compared with \$1,223,000 for YTD 2004. The Company's effective income tax rate was approximately 36% for YTD 2005 compared with 43% for YTD 2004, largely as a result of the lower rate of corporate income tax applicable in the United Kingdom than that in the United States.

Three Months Ended March 31, 2005 Compared to Three Months Ended March 31, 2004

The following table reflects the principal components of the Company's revenues and interest expense as a percentage of total revenue for Q2 2005 and Q2 2004.

| | Percentage of Total Revenue | Percentage of Total Revenue | Percentage Change from Q1 '04 to Q1 '05 |
|---|--------------------------------|--------------------------------|---|
| | Q2 2005 | Q2 2004 | |
| Trading revenue (Net dealer inventory and investment gains) | 97.8% | 96.7% | -2.3% |
| Commissions | 2.5% | 4.0% | -40.6% |
| Interest income | 1.3% | Less than 1% | Not meaningful |
| Dividend income (expense), net | -2.1% | -1.4% | -47.9% |
| Asset management joint venture income (expense) | Less than 1% | 0% | Not Meaningful |
| Other revenues | Less than 1% | Less than 1% | -48.6% |
| Total revenue | 100% | 100% | (3.3%) |
| Interest expense | 4.8% | 2.5% | 87.9% |
| Net revenue | 95.2% | 97.6% | (5.7%) |

The following table reflects the sources of the Company's revenues as a percentage of the Company's total revenue for Q2 2005 and Q2 2004.

| | Percentage of Total Revenues | Percentage of Total Revenues | Percentage Change from Q1 '04 to Q1 '05 |
|---------------------------------------|---------------------------------|---------------------------------|---|
| | Q2 2005 | Q2 2004 | |
| Equity market making | 51% | 83% | -40% |
| Debt capital markets | 8% | 13% | -42% |
| Foreign exchange/ commodities trading | 38% | 3% | Not meaningful |
| Other | 3% | Less than 1% | 286% |

| | | | |
|----------------|------|------|-----|
| Total revenues | 100% | 100% | -3% |
|----------------|------|------|-----|

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The following table reflects the net contribution by percentage of each of the Company's principal business activities for Q2 2004 and Q2 2005. Net contribution consists of revenues from each business activity, less direct clearing and clearing related changes and variable trader compensation.

| | <u>% of Total Net Contribution</u> | <u>% of Total Net Contribution</u> | <u>% Change 2004 to 2005</u> |
|-------------------------------|--|--|----------------------------------|
| | Q2 2005 | Q2 2004 | |
| Equity market making | 40% | 79% | -49% |
| Debt capital markets | 10% | 17% | -46% |
| Foreign exchange/commodities | 50% | 4% | Not Meaningful |
| Total Net Contribution | 100% | 100% | -1% |

The following table reflects the principal components of the Company's non-interest expenses as a percentage of the Company's total non-interest expenses in Q2 2005 and Q2 2004.

| | <u>Percentage of Total Non- interest Expenses</u> | <u>Percentage of Total Non- interest Expenses</u> | <u>Percentage Change from Q1 04 to Q1 05</u> |
|------------------------------------|---|---|--|
| | Q2 2005 | Q2 2004 | |
| Compensation and benefits | 48.4% | 50.2% | 9.1% |
| Clearing and related expenses | 32.3% | 39.5% | -7.2% |
| Wholesale commission expense | Less than 1% | Less than 1% | -5.5% |
| Occupancy and equipment rental | 3.5% | 2.8% | 45.8% |
| Professional fees | 2.3% | 1.5% | 76.4% |
| Depreciation and amortization | 1.5% | Less than 1% | 165.5% |
| Business Development | 3.8% | 1.7% | 163.4% |
| Insurance | 3.2% | 1.7% | 118.6% |
| Other expenses | 4.9% | 2.1% | 166.5% |
| Total non-interest expenses | 100% | 100% | 13.3% |

Net Income. The Company reported net income of \$379,000 for the three months ended March 31, 2005 (Q2 2005), which equates to \$0.05 per basic share and \$0.05 per diluted share. This compares to net income of \$851,000, or \$0.18 per basic share and \$0.15 per diluted share, for the three months ended March 31, 2004 (Q2 2004).

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Total Revenues. The Company's total revenues decreased 3% to \$6,157,000 for Q2 2005 from \$6,369,000 for Q2 2004. The most significant change has been the relative change in the source of the Company's income resulting from the acquisition in July 2004 of INTL Global Currencies. Foreign exchange/commodities trading produced \$2,341,000, or 38% of total revenue for Q2 2005, compared to \$193,000, or 3% of total revenue for Q2 2004. The relative increase in foreign exchange/commodities trading revenue is also attributable to the decline in equity market making revenue. Equity market making revenue fell from \$5,305,000 for Q2 2004 to \$3,166,000 for Q2 2005 as a result of difficult market conditions. Equity market making revenues decreased from 83% of total revenue for Q2 2004 to 51% of total revenue for Q2 2005. International debt capital markets revenue decreased from \$828,000 for Q2 2004 to \$484,000 for Q2 2005. Debt trading and commission revenues were lower because of less volatility in the markets (which reduced the opportunity for profitable trades) and because of rising US interest rates, resulting in tighter spreads, decreased issuer and client activity.

Trading Revenues (Net Dealer Inventory and Investment Gains). The Company had trading income of \$6,020,000 for Q2 2005, compared to \$6,158,000 for Q2 2004. The decrease in trading revenue primarily reflected the difficult equity market conditions. The commodities trading revenues grew by 71% from Q2 2004 to Q2 2005, due to increased business and increased volatility in the price movements of gold and silver. The large overall growth in the foreign exchange/commodities business as a result of the INTL Global Currencies acquisition was partially offset by a 40% reduction in equity market making revenue and a 42% reduction in debt trading revenue.

Total trading revenue includes the trading profits earned by the Company before the related expense deduction for American Depositary Receipt conversion fees. These ADR fees are included in the statement of operations as part of clearing and related expenses.

Commission Revenues. The Company generated commission revenue of \$152,000 for Q2 2005, compared to \$256,000 in Q2 2004. Wholesale brokerage of debt securities declined during Q2 2005 because of tighter interest spreads.

Interest Income. The Company's interest income for Q2 2005 was \$82,000 compared to \$37,000 for Q2 2004. The majority of this interest income is paid by the Company's clearing organization to the Company's broker-dealer subsidiary.

Dividend Income (Expense). The Company's net dividend expense for Q2 2005 was \$129,000 compared to net dividend expense of \$87,000 for Q2 2004. Dividend income or expense is generated when the Company's equity business holds long or short equity positions, respectively, over a dividend declaration date.

Equity in Income from Asset Management Joint Venture. The Company recognized revenue of \$30,000 from the asset management joint venture formed during Q3 2004 and in which the Company has a 50.1% interest. INTL Consilium has achieved early profitability due to the significant level of assets invested in the hedge fund established by INTL Consilium. In this connection, one of the Company's principal shareholders has invested \$89,000,000 into the fund.

Net Contribution. Net contribution consists of revenues, less direct clearing and clearing related charges and variable trader compensation. Net contribution is one of the key measures used by management to assess the performance of each segment and for decisions regarding the allocation of the Company's resources. The net contribution allocated to segments for Q2 2005 is \$3,485,000 compared to \$3,523,000 for Q2 2004. The relative changes in net contribution between the equity market making business and the foreign exchange/commodities trading business principally reflects the effects of the acquisition of INTL Global Currencies, together with the revenue decline in the equity business between YTD 2004 and YTD 2005. Equity market making revenues are stated before deduction of ADR conversion fees, while net contribution is stated after these fees.

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Interest Expense. The Company's interest expense was \$296,000 for Q2 2005, compared to \$158,000 for Q2 2004. The expense in Q2 2005 consisted of \$98,000 in interest paid to banks in the INTL Global Currencies business and \$169,000 of interest on financial instruments sold, not yet purchased, due to an increase in ADR conversion activity. Borrowings related to other segments for Q2 2005 consisted of \$29,000.

Total Non-interest Expenses. The Company's total non-interest expenses increased by approximately 13% to \$5,279,000 for Q2 2005 from \$4,659,000 for Q2 2004. This increase was directly attributable to the expansion of the Company's business, resulting in higher personnel, rents, business development and insurance costs.

Compensation and Benefits. The Company's compensation and benefit expense increased 9% from \$2,339,000 for Q2 2004 to \$2,553,000 for Q2 2005. The increase was primarily a consequence of higher staff levels resulting from the expanded foreign exchange business.

Clearing and Related Expenses. Clearing and related expenses decreased by 7% from \$1,838,000 for Q2 2004 to \$1,705,000 for Q2 2005. The decrease was primarily due to the absence in Q2 2005 of the large, one-time ADR conversion-related charges that were paid in Q2 2004. The decrease was partially offset by an increase in foreign settlement fees, relating to changes in the composition of the equity trading activities, and a large increase in bank charges, relating to the INTL Global Currencies business. The total ADR conversion fees were \$556,000 and \$1,063,000 for Q2 2005 and Q2 2004, respectively.

Occupancy and Equipment Rental. Occupancy and equipment rental expense increased by 46% from \$129,000 for Q2 2004 to \$187,000 for Q2 2005. This increase is primarily due to increased occupancy as a result of expansion of the New York office space and the addition of the INTL Global Currencies office space in London; and an increase in information systems equipment corresponding to the increase in the number of employees.

Professional Fees. Professional fees principally consist of legal, taxation and accounting fees. These fees increased 76% from \$70,000 for Q2 2004 to \$123,000 for Q2 2005 mainly as a result of larger accruals for accounting and audit fees.

Depreciation and Amortization. Depreciation and amortization increased 165% from \$29,000 for Q2 2004 to \$78,000 for Q2 2005. The Company incurred additional depreciation and amortization costs in Q2 2005 due to depreciation of additional fixed assets in the New York office and depreciation of the fixed assets and amortization of goodwill arising from the acquisition of INTL Global Currencies in Q4 2004. However, these items were more than offset by the absence of amortization of capitalized software development costs that were fully amortized in fiscal 2004.

Business Development Expense. Business development expense increased 163% from \$77,000 for Q2 2004 to \$202,000 for Q2 2005. Most of this increase relates to the business development activities of INTL Global Currencies, while the balance relates to expanded marketing efforts for the other businesses of the Company.

Insurance Expense. Insurance expense increased 119% from \$78,000 in Q2 2004 to \$170,000 in Q2 2005. The increase was primarily due to increases in the cost of health insurance caused by higher staff levels and increased cost per employee.

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Other Operating Expenses. Other operating expenses increased 166% from \$98,000 in Q2 2004 to \$261,000 for Q2 2005. The increase was primarily related to increased office expenses resulting from expanded staff levels, higher technology and license fees, and value added taxes payable in the United Kingdom by INTL Global Currencies.

Tax Expense. The Company recognized income tax expense of \$196,000 for Q2 2005 compared with \$721,000 for Q2 2004. The Company's effective income tax rate was approximately 34% for Q2 2005 compared with 46% for Q2 2004, largely as a result of the lower rate of corporate income tax in the United Kingdom than that in the United States.

Liquidity and Capital Resources

A substantial portion of the Company's assets are liquid. The majority of the assets consist of financial instrument inventories, which fluctuate depending on the level of customer business. At March 31, 2005, approximately 87% of the Company's assets (excluding the Trust Interests of \$29,740,000 disclosed in total assets under Trust certificates, at cost, which are offset by a liability of an equal amount as discussed in note 15 above) consisted of cash, cash equivalents, receivables from brokers, dealers and clearing organization and marketable financial instruments. All assets are financed by the Company's equity capital, demand loans from banks, short-term borrowings from financial instruments sold, not yet purchased and other payables.

The Company's ability to receive distributions from INTL Trading, the Company's broker-dealer subsidiary, is restricted by regulations of the SEC and the NASD. The Company's right to receive distributions from its subsidiaries is also subject to the rights of the subsidiaries' creditors, including customers of INTL Trading.

INTL Trading is subject to the net capital requirements of the SEC and the NASD relating to liquidity and net capital levels. At March 31, 2005, INTL Trading had regulatory net capital of \$3,900,000, which was \$2,900,000 in excess of its minimum net capital requirement on that date. INTL Trading's net capital at March 31, 2005 included two subordinated loans made by the Company to INTL Trading. A loan of \$500,000 was made on January 31, 2003, has a scheduled maturity date of February 28, 2006, and has an interest rate of 3%. A second loan of \$2,500,000 was made on May 10, 2004, has a scheduled maturity date of June 30, 2005, and has an interest rate of 3%. The Company has requested from the NASD an extension of the maturity date of the \$2,500,000 loan to June 30, 2006. The Company believes that the NASD will approve the extension. INTL Trading is not obligated to repay the loans at scheduled maturity if repayment would cause INTL Trading to violate its net capital requirements. If this occurs, INTL Trading's obligation to repay the loan is deferred until these requirements can be satisfied. These inter-company loans, and the related interest income and income expense, have been eliminated from the consolidated balance sheet and statements of operations of the Company as of March 31, 2005.

The Company's assets and liabilities may vary significantly from period to period because of changes relating to customer needs and economic and market conditions. The Company's operating activities generate or utilize cash resulting from net income or loss earned during each period and fluctuations in its assets and liabilities. The most significant fluctuations arise from changes in the level of customer activity and financial instruments inventory changes resulting from proprietary arbitrage trading strategies dictated by prevailing market conditions. The Company's total assets at March 31, 2005 and September 30, 2004, were \$109,800,000 and \$67,692,000, respectively. Of the increase in assets over the quarter, \$29,740,000 of assets and an equal value of liabilities relate to total return swap (TRS) transactions. The TRS-related assets and liabilities are of equal amounts, thus having no effect on liquidity. The Company expects that the only net cash flow arising from the TRS transactions will be the Company's receipt of fee revenue. During Q2 2005 the Company recognized \$60,000 of fee revenue from these transactions. The total fee revenue is spread on a straight-line basis over the contractual terms of the TRS transactions.

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In addition to normal operating requirements, capital is required to satisfy financing and regulatory requirements. The Company's overall capital needs are continually reviewed to ensure that its capital base can appropriately support the anticipated capital needs of its operating subsidiaries. The excess regulatory net capital of the Company's broker-dealer subsidiary may fluctuate throughout the year reflecting changes in inventory levels and/or composition and balance sheet components.

In July 2004 the Company completed the acquisition of INTL Global Currencies. The Company is obligated to make certain earn-out payments to the sellers. In particular, the Company is obligated to pay the sellers an amount equal to 20% of the gross foreign exchange trading profits generated by the Company during the 30 months ending on December 31, 2006 (up to a maximum of \$4.0 million). Additionally, the Company is obligated to pay the sellers 10% of the gross foreign exchange trading profits in excess of \$10.0 million per year for the 12 months ended June 30, 2005 and June 30, 2006, and 10% of such profits in excess of \$5.0 million for the 6 months ended December 31, 2006. The Company anticipates that the additional contingent purchase consideration will be funded from working capital. At March 31, 2005 the Company recognized a liability for deferred acquisition consideration payable of \$1,046,000.

Cash Flows

The Company's cash and cash equivalents decreased from \$21,084,000 at September 30, 2004 to \$12,509,000 at March 31, 2005.

The major sources of cash were:

The Company's net cash income for the six months ended March 31, 2005 of \$1,141,000 (consisting of net income of \$991,000, adjusted upwards by \$149,000 for the net effect of non-cash items such as depreciation and amortization, deferred taxes, equity in the gain in INTL Consilium and the unrealized gain on investment in the INTL Consilium sponsored fund).

A \$4,348,000 increase in the Company's net amount payable to customers and receivable from customers.

The major uses of cash were:

A \$11,023,000 increase in the Company's net amount of receivables from and payables to brokers, dealers and clearing organization. At March 31, 2005 and September 30, 2004 these organizations owed/(were owed by) the Company \$9,450,000 and (\$1,573,000), net, respectively.

A \$3,049,000 increase in the Company's net financial instruments position (i.e. financial instruments owned, foreign currency sold, not yet purchased and financial instruments owned, not yet purchased).

Cash and cash equivalents were reduced in aggregate by \$8,576,000.

Quantitative and Qualitative Disclosures about Market Risk

The Company conducts its market-making and trading activities predominantly as a principal, which subjects its capital to significant risks. These risks include, but are not limited to, absolute and relative price movements, price volatility and changes in liquidity, over which the Company has virtually no control. The Company's exposure to market risk varies in accordance with the volume of client-driven market-making transactions, the size of the proprietary positions and the volatility of the financial instruments traded.

We seek to mitigate exposure to market risk by utilizing a variety of qualitative and quantitative techniques:

Diversification of business activities and instruments

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Limitations on positions

Allocation of capital and limits based on estimated weighted risks

Daily monitoring of positions and mark-to-market profitability

The Company utilizes derivative products in a trading capacity as a dealer, to satisfy client needs and mitigate risk. The Company manages risks from both derivatives and non-derivative cash instruments on a consolidated basis. The risks of derivatives should not be viewed in isolation, but in aggregate with the Company's other trading activities.

Management believes that the volatility of earnings is a key indicator of the effectiveness of its risk management techniques. The graph below summarizes volatility of daily revenue during the six months ended March 31, 2005.

In the Company's securities market-making and trading activities, the Company maintains inventories of equity and debt securities. In the Company's commodities market-making and trading activities, the Company's positions include physical inventories, forwards, futures and options. The Company's commodity trading activities are managed as one consolidated book for each commodity encompassing both cash positions and derivative instruments. The Company monitors the aggregate position for each commodity in equivalent physical ounces. The table below illustrates, for the six months ended March 31, 2005, the Company's average, greatest long, greatest short and minimum day-end positions by business segment. Due to integration issues related to the acquisition of the INTL Global Currencies foreign exchange business, this information is not available for the Company's foreign exchange activities.

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| Six months ended March 31, 2005 | Average | Greatest Long | Greatest Short | Minimum Exposure |
|--|----------|------------------|-------------------|---------------------|
| Equity Aggregate of Long and Short (\$ millions) | \$ 4.8 | \$ 7.0 | n/a | \$ 2.9 |
| Equity Net of Long and Short (\$ millions) | \$ 0 | \$ 2.6 | \$ (1.9) | \$ 0 |
| Debt Aggregate of Long and Short (\$ millions) | \$ 4.9 | \$ 7.4 | n/a | \$ 2.6 |
| Debt Net of Long and Short (\$ millions) | \$ 2.7 | \$ 6.4 | \$ (1.1) | \$ 0 |
| Gold (Equivalent Oz) | (21,164) | 753,578 | (750,571) | 0 |
| Silver (Equivalent Oz) | (3,538) | 59,735 | (59,605) | 0 |

Critical Accounting Policies

The Company's Condensed Consolidated Financial Statements are prepared in accordance with generally accepted accounting principles. The Company's significant accounting policies are described in the Summary of Significant Accounting Policies in the Consolidated Financial Statements set forth in the Company's 10-KSB/A for the year ended September 30, 2004. The Company believes that of its significant accounting policies, those described below may, in certain instances, involve a high degree of judgment and complexity. These critical accounting policies may require estimates and assumptions that affect the amounts of assets, liabilities, revenues and expenses reported in the Consolidated Financial Statements. Due to their nature, estimates involve judgment based upon available information. Actual results or amounts could differ from estimates and the difference could have a material impact on the financial statements. Therefore, understanding these policies is important in understanding the reported results of operations and the financial position of the Company.

Valuation of Financial Instruments and Foreign Currencies. Substantially all financial instruments are reflected in the financial statements at fair value or amounts that approximate fair value. These financial instruments include: cash, cash equivalents, and financial instruments purchased under agreements to resell; deposits with clearing organizations; financial instruments owned; and financial instruments sold but not yet purchased. Unrealized gains and losses related to these financial instruments are reflected in net earnings. Where available, the Company uses prices from independent sources such as listed market prices, or broker or dealer price quotations. Fair values for certain derivative contracts are derived from pricing models that consider current market and contractual prices for the underlying financial instruments or commodities, as well as time value and yield curve or volatility factors underlying the positions. In addition, even where the value of a financial instrument is derived from an independent market price or broker or dealer quote, certain assumptions may be required to determine the fair value. However, these assumptions may be incorrect and the actual value realized upon disposition could be different from the current carrying value. The value of foreign currencies, including foreign currencies sold, not yet purchased, are converted into its U.S. dollar equivalents at the foreign exchange rates in effect at the close of business at the end of the accounting period. For foreign currency transactions completed during each reporting period, the foreign exchange rate in effect at the time of the transaction is used.

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The application of the valuation process for financial instruments and foreign currencies is critical because these items represent a significant portion of the Company's total assets. The accuracy of the valuation process allows the Company to report accurate financial information. Valuations for substantially all of the financial instruments held by the Company are available from independent publishers of market information. The valuation process may involve estimates and judgments in the case of certain financial instruments with limited liquidity and over-the-counter derivatives. Given the wide availability of pricing information, the high degree of liquidity of the majority of the Company's assets, and the relatively short periods for which they are typically held in inventory, there is insignificant sensitivity to changes in estimates and insignificant risk of changes in estimates having a material effect on the Company. The basis for estimating the valuation of any financial instruments has not undergone any change.

Revenue Recognition. The revenues of the Company are derived principally from realized and unrealized trading income in securities, foreign currencies and commodities purchased or sold for the Company's account. Realized and unrealized trading income is recorded on a trade date basis. Securities owned and securities sold, not yet purchased and foreign currencies sold, not yet purchased, are stated at market value with related changes in unrealized appreciation or depreciation reflected in net dealer inventory and investment gains. Interest income is recorded on the accrual basis and dividend income is recognized on the ex-dividend date.

The critical aspect of revenue recognition for the Company is recording all known transactions as of the trade date of each transaction for the financial period. The Company has developed systems for each of its businesses to capture all known transactions. Recording all known transactions involves reviewing trades that occur after the financial period that relate to the financial period. The accuracy of capturing this information is dependent upon the completeness and accuracy of the operations systems including personnel and the Company's clearing firm.

Deferred Tax Asset and Liability. The Company recognizes deferred tax assets and liabilities for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply 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 income in the period that includes the enactment date. The Company also establishes valuation allowances when necessary to reduce deferred tax assets to an amount that, in the opinion of management, is more likely than not to be realized. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income or the reversal of deferred tax liabilities during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. As of March 31, 2005, based upon the projections for future taxable income, management believes it is more likely than not that the Company will realize the full benefits of these deductible differences and net operating loss carryforward. The carrying value of the net operating loss carryforward is \$35,000 as of March 31, 2005.

The recognition of deferred tax assets and liabilities involves estimates that management has calculated and relied upon. The various tax rates that jurisdictions impose and the proportion of the Company's taxable income assessed in each of those jurisdictions may differ from management's assumptions. As the Company expands into new tax jurisdictions these estimates become increasingly critical.

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Effects of Inflation

Because the Company's assets are, to a large extent, liquid in nature, they are not significantly affected by inflation. Increases in the Company's expenses, such as compensation and benefits, clearing and related expenses, occupancy and equipment rental, due to inflation, may not be readily recoverable from increasing the prices of services offered by the Company. In addition, to the extent that inflation results in rising interest rates or has other adverse effects on the financial markets and on the value of the financial instruments held in inventory, it may adversely affect the Company's financial position and results of operations.

ITEM 3. CONTROLS AND PROCEDURES

In May 2005, the Company's management and the Audit Committee of the Company's Board of Directors concluded that the Company needed to restate certain of the Company's financial statements to correct errors in the application of accounting principles with respect to the accounting for: (i) the beneficial conversion feature embedded in the \$12,000,000 convertible notes issued by the Company in March 2004; (ii) the recognition of rental expense for certain office leases; and (iii) the treatment of interest paid on the convertible notes for tax purposes. As a result, the Company has restated its historical financial statements for the fiscal years ended September 30, 2002, 2003 and 2004, and the fiscal quarters ended December 31, 2003 and 2004.

The above restatements are described in more detail in Note 2 to the condensed consolidated financial statements included in this Form 10-QSB.

Controls over the application of accounting policies are within the scope of internal controls. Therefore, management has concluded that there were material weaknesses in the Company's internal controls, as defined by the Public Company Accounting Oversight Board. The Company expects that the material weakness related to the issues described above will be remediated as a result of processes that have been implemented subsequent to December 31, 2004.

In connection with the filing of this Form 10-QSB, the Company's management, including the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of March 31, 2005. Because of the issues discussed above, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were not effective as of March 31, 2005.

There were no changes in the Company's internal controls over financial reporting that materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting during the fiscal quarter ended March 31, 2005.

It should be noted that a control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. As a result, there can be no assurance that a control system will succeed in preventing all possible instances of error and fraud. The Company's disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives, and the conclusions of our Chief Executive Officer and Chief Financial Officer are made at the reasonable assurance level.

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PART II - OTHER INFORMATION

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company's annual meeting of shareholders was held on March 3, 2005. The shareholders elected the following seven persons to serve as directors: Diego J. Veitia, Sean M. O'Connor, Scott J. Branch, Robert A. Miller, John Radziwill, Justin R. Wheeler and John M. Fowler. The shareholders also ratified the appointment of KPMG LLP to audit the consolidated financial statements of the Company and its subsidiaries for the fiscal year ending September 30, 2005.

The number of shares voted with respect to each matter considered at the annual meeting were as follows:

| Election of Directors | Votes For | Votes Withheld |
|------------------------------|----------------------|---------------------------|
| Diego J. Veitia | 5,606,023 | 4,944 |
| Sean M. O'Connor | 5,607,327 | 3,640 |
| Scott J. Branch | 5,607,327 | 3,640 |
| Robert A. Miller | 5,584,676 | 26,291 |
| John Radziwill | 5,603,628 | 7,339 |
| Justin R. Wheeler | 5,607,523 | 3,444 |
| John M. Fowler | 5,607,523 | 3,444 |

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| | <u>Votes For</u> | <u>Votes Against</u> | <u>Votes Abstain</u> |
|--------------------------------------|----------------------|--------------------------|--------------------------|
| Ratification of KPMG LLP as auditors | 5,560,867 | 47,534 | 2,566 |

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

a) Exhibits

- (31.1) Certification of Chief Executive Officer, pursuant to Rule 13a 14(a).
- (31.2) Certification of Chief Financial Officer, pursuant to Rule 13a 14(a).
- (32.1) Certification of Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- (32.2) Certification of Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

b) Reports on Form 8-K

On February 14, 2005 the Company filed a Current Report on Form 8-K to report on the release of operations for the fiscal year ended September 30, 2005 and the fiscal quarter ended December 31, 2004.

On May 17, 2005 the Company filed a Current Report in Form 8-K to report on the release announcing that it would restate its financial statements for the fiscal years 2002 through 2004 and for the first quarter of fiscal 2005.

Signatures

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date 05/23/2005

INTERNATIONAL ASSETS HOLDING CORPORATION

/s/ Sean M. O Connor

Sean M. O Connor
Chief Executive Officer

Date 05/23/2005

/s/ Brian T. Sephton

Brian T. Sephton
Chief Financial Officer and Treasurer

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Exhibit Index

| <u>Exhibit No.</u> | <u>Description</u> |
|---------------------------|---|
| (31.1) | Certification of Chief Executive Officer, pursuant to Rule 13a 14(a). |
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