

WADDELL & REED FINANCIAL INC  
Form 10-Q  
August 02, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2012

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-13913

**WADDELL & REED FINANCIAL, INC.**

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(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction  
of incorporation or organization)

**51-0261715**  
(I.R.S. Employer  
Identification No.)

**6300 Lamar Avenue**

**Overland Park, Kansas 66202**

(Address, including zip code, of Registrant's principal executive offices)

**(913) 236-2000**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Shares outstanding of each of the registrant's classes of common stock as of the latest practicable date:

| Class                                 | Outstanding as of July 25, 2012 |
|---------------------------------------|---------------------------------|
| Class A common stock, \$.01 par value | 85,821,754                      |



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## Consolidated Balance Sheets

(in thousands)

|  | June 30,<br>2012<br>(unaudited) | December 31,<br>2011 |
|--|---------------------------------|----------------------|
| <b>Assets:</b>   |                                 |                      |
| Cash and cash equivalents  | \$ 346,940                      | 327,083              |
| Cash and cash equivalents - restricted   | 74,147                          | 50,569               |
| Investment securities  | 158,551                         | 135,497              |
| <b>Receivables:</b>  |                                 |                      |
| Funds and separate accounts  | 34,650                          | 31,842               |
| Customers and other  | 114,308                         | 116,996              |
| Deferred income taxes  | 8,064                           | 11,848               |
| Income taxes receivable  | 7,861                           | 15,067               |
| Prepaid expenses and other current assets  | 13,012                          | 10,709               |
| <b>Total current assets</b>  | <b>757,533</b>                  | <b>699,611</b>       |
| Property and equipment, net  | 68,584                          | 74,028               |
| Deferred sales commissions, net  | 70,565                          | 68,788               |
| Goodwill and identifiable intangible assets  | 221,210                         | 221,210              |
| Deferred income taxes  | 12,482                          | 4,878                |
| Other non-current assets   | 13,039                          | 13,681               |
| <b>Total assets</b>  | <b>\$ 1,143,413</b>             | <b>1,082,196</b>     |
| <b>Liabilities:</b>  |                                 |                      |
| Accounts payable   | \$ 39,852                       | 52,134               |
| Payable to investment companies for securities   | 125,417                         | 104,304              |
| Accrued compensation   | 38,284                          | 35,117               |
| Payable to third party brokers   | 50,832                          | 41,125               |
| Other current liabilities  | 58,699                          | 56,218               |
| <b>Total current liabilities</b>   | <b>313,084</b>                  | <b>288,898</b>       |
| Long-term debt   | 190,000                         | 190,000              |
| Accrued pension and postretirement costs   | 46,178                          | 56,548               |
| Other non-current liabilities  | 22,504                          | 23,107               |
| <b>Total liabilities</b>   | <b>571,766</b>                  | <b>558,553</b>       |
| <b>Commitments and contingencies</b>   |                                 |                      |
| <b>Stockholders' equity:</b>   |                                 |                      |
| Preferred stock-\$1.00 par value; 5,000 shares authorized; none issued   |                                 |                      |
| Class A Common stock-\$0.01 par value; 250,000 shares authorized; 99,701 shares issued; 85,825 shares outstanding (85,564 shares outstanding at December 31, 2011) | 997                             | 997                  |
| Additional paid-in capital   | 212,410                         | 216,426              |
| Retained earnings  | 767,322                         | 721,281              |
| Cost of 13,876 common shares in treasury (14,137 at December 31, 2011)   | (364,865)                       | (366,954)            |

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|  |    |           |           |
|--|----|-----------|-----------|
| Accumulated other comprehensive loss       |    | (44,217)  | (48,107)  |
| Total stockholders' equity                 |    | 571,647   | 523,643   |
| Total liabilities and stockholders' equity | \$ | 1,143,413 | 1,082,196 |

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents**WADDELL & REED FINANCIAL, INC. AND SUBSIDIARIES**

## Consolidated Statements of Income

(Unaudited, in thousands, except for per share data)

|  | For the three months<br>ended June 30, |                | For the six months<br>ended June 30, |                |
|--|--|----------------|--------------------------------------|----------------|
|  | 2012                                   | 2011           | 2012                                 | 2011           |
| <b>Revenues:</b>   |  |                |                                      |                |
| Investment management fees   | \$ 134,213                             | 138,985        | 269,113                              | 270,629        |
| Underwriting and distribution fees   | 139,944                                | 137,354        | 277,434                              | 270,117        |
| Shareholder service fees   | 34,051                                 | 33,606         | 68,279                               | 65,773         |
| <b>Total</b>   | <b>308,208</b>                         | <b>309,945</b> | <b>614,826</b>                       | <b>606,519</b> |
| <b>Operating expenses:</b>   |  |                |                                      |                |
| Underwriting and distribution  | 163,032                                | 157,219        | 322,507                              | 309,223        |
| Compensation and related costs (including<br>share-based compensation of \$12,293, \$12,960,<br>\$24,565 and \$22,828, respectively) | 42,973                                 | 42,092         | 88,376                               | 82,567         |
| General and administrative   | 25,095                                 | 19,500         | 44,419                               | 37,131         |
| Subadvisory fees   | 5,208                                  | 8,313          | 11,479                               | 16,393         |
| Depreciation   | 3,428                                  | 3,842          | 6,900                                | 7,446          |
| <b>Total</b>   | <b>239,736</b>                         | <b>230,966</b> | <b>473,681</b>                       | <b>452,760</b> |
| <b>Operating income</b>  | <b>68,472</b>                          | <b>78,979</b>  | <b>141,145</b>                       | <b>153,759</b> |
| Investment and other income  | 1,272                                  | 2,452          | 5,328                                | 3,455          |
| Interest expense   | (2,825)                                | (2,835)        | (5,652)                              | (5,735)        |
| <b>Income before provision for income taxes</b>  | <b>66,919</b>                          | <b>78,596</b>  | <b>140,821</b>                       | <b>151,479</b> |
| Provision for income taxes   | 25,201                                 | 28,626         | 51,716                               | 55,876         |
| <b>Net income</b>  | <b>\$ 41,718</b>                       | <b>49,970</b>  | <b>89,105</b>                        | <b>95,603</b>  |
| <b>Net income per share:</b>   |  |                |                                      |                |
| Basic  | \$ 0.48                                | 0.58           | 1.04                                 | 1.11           |
| Diluted  | \$ 0.48                                | 0.58           | 1.04                                 | 1.11           |
| <b>Weighted average shares outstanding:</b>  |  |                |                                      |                |
| Basic  | 86,093                                 | 86,264         | 85,848                               | 86,040         |
| Diluted  | 86,095                                 | 86,275         | 85,851                               | 86,057         |

See accompanying notes to the unaudited consolidated financial statements.

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## Consolidated Statements of Comprehensive Income

(Unaudited, in thousands)

|  | For the three months<br>ended June 30, |         | For the six months<br>ended June 30, |         |
|--|--|---------|--------------------------------------|---------|
|  | 2012                                   | 2011    | 2012                                 | 2011    |
| Net income   | \$ 41,718                              | 49,970  | 89,105                               | 95,603  |
| Other comprehensive income:  |  |         |                                      |         |
| Unrealized appreciation (depreciation) of available for sale investment securities during the period, net of income taxes of \$(1,023), \$(191), \$1,489 and \$471, respectively | (1,742)                                | (333)   | 2,548                                | 801     |
| Valuation allowance on investment securities deferred tax asset during the period  | (1,086)                                | (915)   | 867                                  | (256)   |
| Pension and postretirement benefits, net of income taxes of \$526, \$237, \$1,047 and \$432, respectively  | 891                                    | 436     | 1,548                                | 778     |
| Reclassification adjustment for amounts included in net income, net of income taxes of \$(62), \$(730), \$(623), and \$(730)   | (107)                                  | (1,256) | (1,073)                              | (1,256) |
| Comprehensive income   | \$ 39,674                              | 47,902  | 92,995                               | 95,670  |

See accompanying notes to the unaudited consolidated financial statements.



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## Consolidated Statement of Stockholders' Equity

For the Six Months Ended June 30, 2012

(Unaudited, in thousands)

|   | Shares | Common Stock<br>Amount | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Income (Loss) | Total<br>Stockholders<br>Equity |
|---|--------|------------------------|----------------------------------|----------------------|-------------------|--|---------------------------------|
| Balance at December 31, 2011  | 99,701 | \$ 997                 | 216,426                          | 721,281              | (366,954)         | (48,107)   | 523,643                         |
| Net income  |        |                        |                                  | 89,105               |                   |  | 89,105                          |
| Recognition of share-based<br>compensation                                |        |                        | 24,565                           |                      |                   |  | 24,565                          |
| Issuance of nonvested shares  |        |                        | (31,412)                         |                      | 31,412            |  |                                 |
| Dividends accrued, \$0.50 per<br>share                                    |        |                        |                                  | (43,064)             |                   |  | (43,064)                        |
| Excess tax benefits from<br>share-based payment<br>arrangements           |        |                        | 2,831                            |                      |                   |  | 2,831                           |
| Repurchase of common stock  |        |                        |                                  |                      | (29,323)          |  | (29,323)                        |
| Unrealized appreciation of<br>available for sale investment<br>securities |        |                        |                                  |                      |                   | 2,548  | 2,548                           |
| Valuation allowance on<br>investment securities - deferred<br>tax asset   |        |                        |                                  |                      |                   | 867  | 867                             |
| Pension and postretirement<br>benefits                                    |        |                        |                                  |                      |                   | 1,548  | 1,548                           |
| Reclassification adjustment for<br>amounts included in net income         |        |                        |                                  |                      |                   | (1,073)  | (1,073)                         |
| Balance at June 30, 2012  | 99,701 | \$ 997                 | 212,410                          | 767,322              | (364,865)         | (44,217)   | 571,647                         |

See accompanying notes to the unaudited consolidated financial statements.

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## Consolidated Statements of Cash Flows

(Unaudited, in thousands)

|  |           |                 |                 |
|--|-----------|-----------------|-----------------|
| <b>Cash flows from operating activities:</b>   |           |                 |                 |
| Net income   | \$        | 89,105          | 95,603          |
| <b>Adjustments to reconcile net income to net cash provided by operating activities:</b> |           |                 |                 |
| Depreciation and amortization  |           | 7,754           | 7,742           |
| Amortization of deferred sales commissions   |           | 27,018          | 26,601          |
| Share-based compensation   |           | 24,565          | 22,828          |
| Excess tax benefits from share-based payment arrangements                                |           | (2,831)         | (7,499)         |
| Gain on sale of available for sale investment securities                                 |           | (1,697)         | (1,986)         |
| Net purchases and sales or maturities of trading securities                              |           | (12,277)        | 71,301          |
| Unrealized gain on trading securities  |           | (3,078)         | (962)           |
| Loss on sale and retirement of property and equipment                                    |           | 4,863           | 49              |
| Deferred income taxes  |           | (4,866)         | (662)           |
| <b>Changes in assets and liabilities:</b>  |           |                 |                 |
| Cash and cash equivalents - restricted   |           | (23,578)        | 1,219           |
| Receivables from funds and separate accounts   |           | (2,808)         | (4,112)         |
| Other receivables  |           | 2,688           | (14,973)        |
| Other assets   |           | (1,661)         | (3,261)         |
| Deferred sales commissions   |           | (28,795)        | (33,382)        |
| Accounts payable and payable to investment companies                                     |           | 8,831           | 6,478           |
| Other liabilities  |           | 16,949          | 7,312           |
| <b>Net cash provided by operating activities</b>   | <b>\$</b> | <b>100,182</b>  | <b>172,296</b>  |
| <b>Cash flows from investing activities:</b>   |           |                 |                 |
| Purchases of available for sale investment securities                                    |           | (15,796)        | (79,167)        |
| Proceeds from sales and maturities of available for sale investment securities           |           | 11,281          | 84,053          |
| Additions to property and equipment  |           | (6,354)         | (8,351)         |
| Proceeds from sales of property and equipment  |           | 35              |                 |
| <b>Net cash used in investing activities</b>   | <b>\$</b> | <b>(10,834)</b> | <b>(3,465)</b>  |
| <b>Cash flows from financing activities:</b>   |           |                 |                 |
| Dividends paid   |           | (42,999)        | (34,459)        |
| Repurchase of common stock   |           | (29,323)        | (37,663)        |
| Exercise of stock options  |           |                 | 4,722           |
| Excess tax benefits from share-based payment arrangements                                |           | 2,831           | 7,499           |
| <b>Net cash used in financing activities</b>   | <b>\$</b> | <b>(69,491)</b> | <b>(59,901)</b> |
| <b>Net increase in cash and cash equivalents</b>   |           | <b>19,857</b>   | <b>108,930</b>  |
| Cash and cash equivalents at beginning of period   |           | 327,083         | 195,315         |
| <b>Cash and cash equivalents at end of period</b>  | <b>\$</b> | <b>346,940</b>  | <b>304,245</b>  |

See accompanying notes to the unaudited consolidated financial statements.



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**WADDELL & REED FINANCIAL, INC.**

**NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**1. Description of Business and Significant Accounting Policies**

*Waddell & Reed Financial, Inc. and Subsidiaries*

Waddell & Reed Financial, Inc. and subsidiaries (hereinafter referred to as the Company, we, our and us) derive revenues from investment management, investment product underwriting and distribution, and shareholder services administration provided to the Waddell & Reed Advisors Group of Mutual Funds (the Advisors Funds), Ivy Funds (the Ivy Funds), Ivy Funds Variable Insurance Portfolios (the Ivy Funds VIP), and InvestEd Portfolios (InvestEd) (collectively, the Advisors Funds, Ivy Funds, Ivy Funds VIP and InvestEd are referred to as the Funds), and institutional and separately managed accounts. The Funds and the institutional and separately managed accounts operate under various rules and regulations set forth by the United States Securities and Exchange Commission (the SEC). Services to the Funds are provided under investment management agreements, underwriting agreements and shareholder servicing and accounting service agreements that set forth the fees to be charged for these services. The majority of these agreements are subject to annual review and approval by each Fund's board of trustees and shareholders. Our revenues are largely dependent on the total value and composition of assets under management. Accordingly, fluctuations in financial markets and composition of assets under management can significantly impact revenues and results of operations.

*Basis of Presentation*

We have prepared the accompanying unaudited consolidated financial statements included herein pursuant to the rules and regulations of the SEC. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to such rules and regulations, although we believe that the disclosures are adequate to enable a reasonable understanding of the information presented. The information in this Quarterly Report on Form 10-Q should be read in conjunction with Part I, Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations and our audited financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2011 (the 2011 Form 10-K).

The accompanying unaudited consolidated financial statements are prepared consistently with the accounting policies described in Note 2 to the consolidated financial statements included in our 2011 Form 10-K, which include the following: use of estimates, cash and cash equivalents, disclosures about fair value of financial instruments, investment securities and investments in mutual funds, property and equipment, software developed for internal use, goodwill and identifiable intangible assets, deferred sales commissions, revenue recognition, advertising and promotion, share-based compensation and accounting for income taxes.

In our opinion, the accompanying unaudited consolidated financial statements reflect all adjustments (consisting of only a normal and recurring nature) necessary to present fairly our financial position at June 30, 2012, the results of operations for the three and six months ended June 30, 2012 and 2011, and cash flows for the six months ended June 30, 2012 and 2011 in conformity with accounting principles generally accepted in the United States.

**2. Cash and Cash Equivalents**

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

Table of Contents**3. Investment Securities**

Investment securities at June 30, 2012 and December 31, 2011 are as follows:

| June 30, 2012                         | Amortized<br>cost | Unrealized<br>gains | Unrealized<br>losses | Fair value |
|---------------------------------------|-------------------|---------------------|----------------------|------------|
| (in thousands)                        |                   |                     |                      |            |
| <b>Available for sale securities:</b> |                   |                     |                      |            |
| Mortgage-backed securities            | \$ 9              | 1                   |                      | 10         |
| Municipal bonds                       | 2,362             | 24                  |                      | 2,386      |
| Corporate bonds                       | 45,360            | 447                 | (8)                  | 45,799     |
| Affiliated mutual funds               | 57,739            | 2,007               | (2,701)              | 57,045     |
|                                       | \$ 105,470        | 2,479               | (2,709)              | 105,240    |
| <b>Trading securities:</b>            |                   |                     |                      |            |
| Mortgage-backed securities            |                   |                     |                      | 45         |
| Municipal bonds                       |                   |                     |                      | 501        |
| Corporate bonds                       |                   |                     |                      | 17,262     |
| Common stock                          |                   |                     |                      | 34         |
| Affiliated mutual funds               |                   |                     |                      | 35,469     |
|                                       |                   |                     |                      | 53,311     |
| Total investment securities           |                   |                     |                      | \$ 158,551 |
| <br>                                  |                   |                     |                      |            |
| December 31, 2011                     | Amortized<br>cost | Unrealized<br>gains | Unrealized<br>losses | Fair value |
| (in thousands)                        |                   |                     |                      |            |
| <b>Available for sale securities:</b> |                   |                     |                      |            |
| Mortgage-backed securities            | 9                 | 2                   |                      | 11         |
| Municipal bonds                       | 2,549             |                     | (13)                 | 2,536      |
| Corporate bonds                       | 45,893            | 170                 | (89)                 | 45,974     |
| Affiliated mutual funds               | 51,456            | 2,738               | (5,379)              | 48,815     |
|                                       | \$ 99,907         | 2,910               | (5,481)              | 97,336     |
| <b>Trading securities:</b>            |                   |                     |                      |            |
| Mortgage-backed securities            |                   |                     |                      | 63         |
| Municipal bonds                       |                   |                     |                      | 500        |
| Corporate bonds                       |                   |                     |                      | 17,319     |
| Common stock                          |                   |                     |                      | 37         |
| Affiliated mutual funds               |                   |                     |                      | 20,242     |
|                                       |                   |                     |                      | 38,161     |
| Total investment securities           |                   |                     |                      | \$ 135,497 |

Purchases of trading securities during the six months ended June 30, 2012 were \$26.2 million; \$25.0 million represented seed money for the Ivy Global Equity Income Fund, a new fund launched in the second quarter. Sales of trading securities were \$13.9 million for the same period.



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A summary of available for sale debt securities and affiliated mutual funds with fair values below carrying values at June 30, 2012 and December 31, 2011 is as follows:

| June 30, 2012                         | Less than 12 months |                   | 12 months or longer          |                   | Total      |                   |
|---------------------------------------|---------------------|-------------------|------------------------------|-------------------|------------|-------------------|
|                                       | Fair value          | Unrealized losses | Fair value<br>(in thousands) | Unrealized losses | Fair value | Unrealized losses |
| Corporate bonds                       | \$ 5,909            | (8)               |                              |                   | 5,909      | (8)               |
| Affiliated mutual funds               | 33,272              | (1,176)           | 17,267                       | (1,525)           | 50,539     | (2,701)           |
| Total temporarily impaired securities | \$ 39,181           | (1,184)           | 17,267                       | (1,525)           | 56,448     | (2,709)           |

| December 31, 2011                     | Less than 12 months |                   | 12 months or longer          |                   | Total      |                   |
|---------------------------------------|---------------------|-------------------|------------------------------|-------------------|------------|-------------------|
|                                       | Fair value          | Unrealized losses | Fair value<br>(in thousands) | Unrealized losses | Fair value | Unrealized losses |
| Municipal bonds                       | \$ 16,769           | (89)              | 2,536                        | (13)              | 2,536      | (13)              |
| Corporate bonds                       | 36,801              | (5,362)           | 209                          | (17)              | 37,010     | (5,379)           |
| Total temporarily impaired securities | \$ 53,570           | (5,451)           | 2,745                        | (30)              | 56,315     | (5,481)           |

Based upon our assessment of these corporate bonds and affiliated mutual funds, the time frame investments have been in a loss position, our intent to hold affiliated mutual funds until they have recovered and our history of holding bonds until maturity, we determined that a write-down was not necessary at June 30, 2012.

Mortgage-backed securities, municipal bonds and corporate bonds accounted for as available for sale and held as of June 30, 2012 mature as follows:

|                                    | Amortized cost<br>(in thousands) | Fair value |
|------------------------------------|----------------------------------|------------|
| Within one year                    | \$ 21,436                        | 21,651     |
| After one year but within 10 years | 25,303                           | 25,543     |
| After 10 years                     | 992                              | 1,001      |
|                                    | \$ 47,731                        | 48,195     |

Mortgage-backed securities, municipal bonds and corporate bonds accounted for as trading and held as of June 30, 2012 mature as follows:

|                                    | Fair value<br>(in thousands) |
|------------------------------------|------------------------------|
| Within one year                    | \$ 5,064                     |
| After one year but within 10 years | 12,712                       |
| After 10 years                     | 32                           |
|                                    | \$ 17,808                    |





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

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

Assets classified as Level 2 can have a variety of observable inputs, including, but not limited to, benchmark yields, reported trades, broker quotes, benchmark securities and bid/offer quotations. These observable inputs are collected and utilized, primarily by an independent pricing service, in different evaluated pricing approaches, depending upon the specific asset, to determine a value. Securities' values classified as Level 3 are primarily determined through the use of a single quote (or multiple quotes) from dealers in the securities using proprietary valuation models. These quotes involve significant unobservable inputs, and thus, the related securities are classified as Level 3 securities.

The following tables summarize our investment securities as of June 30, 2012 and December 31, 2011 that are recognized in our consolidated balance sheets using fair value measurements based on the differing levels of inputs:

| June 30, 2012              | Level 1 | Level 2        | Level 3 | Total   |
|----------------------------|---------|----------------|---------|---------|
|                            |         | (in thousands) |         |         |
| Mortgage-backed securities | \$      | 55             |         | 55      |
| Municipal bonds            |         | 2,887          |         | 2,887   |
| Corporate bonds            |         | 63,061         |         | 63,061  |
| Common stock               |         | 34             |         | 34      |
| Affiliated mutual funds    |         | 92,514         |         | 92,514  |
| Total                      | \$      | 92,548         | 66,003  | 158,551 |

| December 31, 2011          | Level 1 | Level 2        | Level 3 | Total  |
|----------------------------|---------|----------------|---------|--------|
|                            |         | (in thousands) |         |        |
| Mortgage-backed securities | \$      | 74             |         | 74     |
| Municipal bonds            |         | 3,036          |         | 3,036  |
| Corporate bonds            |         | 63,293         |         | 63,293 |
| Common stock               |         | 37             |         | 37     |
| Affiliated mutual funds    |         | 69,057         |         | 69,057 |

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|       |    |        |        |         |
|-------|----|--------|--------|---------|
| Total | \$ | 69,094 | 66,403 | 135,497 |
|-------|----|--------|--------|---------|

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Table of Contents**4. Property and Equipment**

During the second quarter of 2012, we recorded a pre-tax charge of \$5.0 million to reflect the impairment of certain capitalized software development costs. This charge is included in general and administrative expenses in the statement of income. Our ongoing assessment and changes to our enterprise information technology infrastructure and software resulted in the decision to discontinue the usage of certain software.

**5. Goodwill and Identifiable Intangible Assets**

Goodwill represents the excess of purchase price over the tangible assets and identifiable intangible assets of an acquired business. Our goodwill is not deductible for tax purposes. As of June 30, 2012, the Company's annual impairment test indicated that goodwill and identifiable intangible assets were not impaired. Goodwill and identifiable intangible assets (all considered indefinite lived) are as follows:

|  | <b>June 30,<br/>2012</b> | <b>December 31,<br/>2011</b> |
|--|--------------------------|------------------------------|
|  | (in thousands)           |                              |
| Goodwill                                     | \$ 202,518               | 202,518                      |
| Accumulated amortization                     | (36,307)                 | (36,307)                     |
| Total goodwill                               | 166,211                  | 166,211                      |
| Mutual fund management advisory contracts    | 38,699                   | 38,699                       |
| Mutual fund management subadvisory contracts | 16,300                   | 16,300                       |
| Total identifiable intangible assets         | 54,999                   | 54,999                       |
| Total  | \$ 221,210               | 221,210                      |

**6. Indebtedness**

Debt is reported at its carrying amount in the consolidated balance sheets. The fair value of the Company's outstanding indebtedness is approximately \$199.9 million at June 30, 2012 compared to the carrying value of \$190.0 million. Fair value is calculated based on Level 2 inputs.

**7. Income Tax Uncertainties**

As of January 1, 2012 and June 30, 2012, the Company had unrecognized tax benefits, including penalties and interest, of \$9.8 million (\$6.9 million net of federal benefit) and \$10.8 million (\$7.6 million net of federal benefit), respectively, that if recognized, would impact the Company's effective tax rate. Unrecognized tax benefits that are not expected to be settled within the next 12 months are included in other liabilities in the consolidated balance sheets; unrecognized tax benefits that are expected to be settled within the next 12 months are included in

income taxes payable.

The Company's accounting policy with respect to interest and penalties related to income tax uncertainties is to classify these amounts as income taxes. As of January 1, 2012, the total amount of accrued interest and penalties related to uncertain tax positions recognized in the consolidated balance sheet was \$2.3 million (\$1.8 million net of federal benefit). The total amount of penalties and interest, net of federal benefit, related to income tax uncertainties recognized in the statement of income for the six month period ended June 30, 2012 was \$0.3 million. The total amount of accrued penalties and interest related to uncertain tax positions at June 30, 2012 of \$2.6 million (\$2.1 million net of federal benefit) is included in the total unrecognized tax benefits described above.

In the ordinary course of business, many transactions occur for which the ultimate tax outcome is uncertain. In addition, respective tax authorities periodically audit our income tax returns. These audits examine our significant tax filing positions, including the timing and amounts of deductions and the allocation of income among tax jurisdictions. The 2008 through 2011 federal income tax returns are open tax years that remain subject to potential future audit. The 2005 through 2007 federal tax years also remain

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open to a limited extent due to capital loss carryback claims. State income tax returns for all years after 2007, and in certain states, income tax returns prior to 2008, are subject to potential future audit by tax authorities in the Company's major state tax jurisdictions.

The Company is currently being audited in various state jurisdictions. It is reasonably possible that the Company will settle the audits in these jurisdictions within the next 12-month period. It is estimated that the Company's liability for unrecognized tax benefits, including penalties and interest, could decrease by approximately \$0.5 million to \$3.2 million (\$0.3 million to \$2.1 million net of federal benefit) upon settlement of these audits. Such settlements are not anticipated to have a significant impact on the results of operations.

## 8. Pension Plan and Postretirement Benefits Other Than Pension

We provide a non-contributory retirement plan that covers substantially all employees and certain vested employees of our former parent company (the Pension Plan). Benefits payable under the Pension Plan are based on employees' years of service and compensation during the final 10 years of employment. We also sponsor an unfunded defined benefit postretirement medical plan that covers substantially all employees, as well as Waddell & Reed and Legend advisors. The medical plan is contributory with participant contributions adjusted annually. The medical plan does not provide for post age 65 benefits with the exception of a small group of employees that were grandfathered when such plan was established.

The components of net periodic pension and other postretirement costs related to these plans are as follows:

|  | Pension Benefits   |         | Other Postretirement Benefits |      | Pension Benefits |         | Other Postretirement Benefits |      |
|--|--------------------|---------|-------------------------------|------|------------------|---------|-------------------------------|------|
|  | Three months ended |         | Three months ended            |      | Six months ended |         | Six months ended              |      |
|  | 2012               | 2011    | 2012                          | 2011 | 2012             | 2011    | 2012                          | 2011 |
|  | June 30,           |         | June 30,                      |      | June 30,         |         | June 30,                      |      |
|  | (in thousands)     |         | (in thousands)                |      | (in thousands)   |         | (in thousands)                |      |
| Components of net periodic benefit cost: |                    |         |                               |      |                  |         |                               |      |
| Service cost                             | \$ 2,478           | 1,850   | 173                           | 140  | 4,687            | 3,551   | 346                           | 279  |
| Interest cost                            | 1,973              | 1,861   | 100                           | 100  | 3,785            | 3,598   | 200                           | 201  |
| Expected return on plan assets           | (2,273)            | (2,196) |                               |      | (4,400)          | (4,382) |                               |      |
| Actuarial loss amortization              | 1,260              | 518     | 3                             |      | 2,281            | 902     | 6                             |      |
| Prior service cost amortization          | 139                | 139     | 14                            | 14   | 278              | 278     | 28                            | 28   |
| Transition obligation amortization       | 2                  | 1       |                               |      | 3                | 2       |                               |      |
| Total                                    | \$ 3,579           | 2,173   | 290                           | 254  | 6,634            | 3,949   | 580                           | 508  |

During the first six months of 2012, we contributed \$15.0 million to the Pension Plan. We do not expect to make additional contributions for the remainder of 2012.



Table of Contents**9. Stockholders Equity***Earnings per Share*

The components of basic and diluted earnings per share were as follows:

|   | Three months ended<br>June 30,           |        | Six months ended<br>June 30, |        |
|---|--|--------|------------------------------|--------|
|   | 2012                                     | 2011   | 2012                         | 2011   |
|   | (in thousands, except per share amounts) |        |                              |        |
| Net income                                    | \$ 41,718                                | 49,970 | 89,105                       | 95,603 |
| Weighted average shares outstanding - basic   | 86,093                                   | 86,264 | 85,848                       | 86,040 |
| Dilutive potential shares from stock options  | 2  | 11     | 3                            | 17     |
| Weighted average shares outstanding - diluted | 86,095                                   | 86,275 | 85,851                       | 86,057 |
| <b>Earnings per share:</b>                    |  |        |                              |        |
| Basic   | \$ 0.48                                  | 0.58   | 1.04                         | 1.11   |
| Diluted                                       | \$ 0.48                                  | 0.58   | 1.04                         | 1.11   |

*Anti-dilutive Securities*

There were no anti-dilutive options for the three and six months ended June 30, 2012 or 2011.

*Dividends*

On April 18, 2012, the Board of Directors (the Board) approved a dividend on our common stock in the amount of \$0.25 per share to stockholders of record as of July 11, 2012 to be paid on August 1, 2012. The total dividend to be paid is approximately \$21.5 million and is included in other current liabilities in the consolidated balance sheet at June 30, 2012.

*Common Stock Repurchases*

The Board has authorized the repurchase of our common stock in the open market and/or private purchases. The acquired shares may be used for corporate purposes, including shares issued to employees in our stock-based compensation programs.



There were 944,988 shares and 782,316 shares repurchased in the open market or privately during the three months ended June 30, 2012 and 2011, respectively, which included 412,988 shares and 339,815 shares repurchased from employees tendering shares to cover their minimum income tax withholdings with respect to vesting of stock awards during the three months ended June 30, 2012 and 2011, respectively. There were 945,354 shares and 957,673 shares repurchased in the open market or privately during the six months ended June 30, 2012 and 2011, respectively, which included 413,354 shares and 340,172 shares repurchased from employees tendering shares to cover their minimum income tax withholdings with respect to vesting of stock awards during each of these two periods.

Table of Contents**10. Share-Based Compensation**

A summary of stock option activity and related information for the six months ended June 30, 2012 is presented in the table below. All options outstanding expire prior to December 31, 2013.

|                                | Options  |    | Weighted<br>average<br>exercise price |
|--------------------------------|----------|----|---------------------------------------|
| Outstanding, December 31, 2011 | 27,595   | \$ | 28.64                                 |
| Granted                        |          |    |                                       |
| Exercised                      |          |    |                                       |
| Terminated/Cancelled           | (16,224) | \$ | 33.94                                 |
| Outstanding, June 30, 2012     | 11,371   | \$ | 21.09                                 |
| Exercisable, June 30, 2012     | 11,371   | \$ | 21.09                                 |

On April 2, 2012, we granted 1,205,698 shares of nonvested stock with a fair value of \$33.23 per share under the Company's 1998 Stock Incentive Plan, as amended and restated (the "SI Plan"). The value of those shares at the grant date, aggregating \$40.1 million, will be amortized to expense over a four year vesting period.

**11. Contingencies**

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

*Michael E. Taylor, Kenneth B. Young, individuals, on behalf of themselves individually and on behalf of others similarly situated v. Waddell & Reed, Inc., a Delaware Corporation; and DOES 1 through 10 inclusive; Case No. 09-CV-2909 DMS WVG; in the United States District Court for the Southern District of California.*

In this action filed December 28, 2009, the Company was sued in an individual action, class action and Fair Labor Standards Act ( "FLSA" ) nationwide collective action by two former advisors asserting misclassification of financial advisors as independent contractors instead of employees. Plaintiffs, on behalf of themselves and a purported class of Waddell & Reed, Inc. financial advisors, assert claims under the FLSA for minimum wages and overtime wages, and under California Labor Code Statutes for timely payment of wages, minimum wages, overtime compensation, meal periods, reimbursement of losses and business expenses and itemized wage statements and a claim for Unfair Business Practices under §17200 of the California Business & Professions Code. Plaintiffs seek declaratory and injunctive relief and monetary damages.

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Plaintiffs moved for conditional collective action certification under the FLSA. The Company opposed this motion and additionally moved for summary judgment on Plaintiffs' individual FLSA claims. The Court issued an order on January 3, 2012 granting the Company's summary judgment motions, holding that Plaintiffs' individual FLSA claims fail as a matter of law, and denying Plaintiffs' motion for conditional collective action certification under the FLSA as moot. This ruling effectively removes all nationwide FLSA claims from the case.

Plaintiffs intend to continue to pursue the California claims. An adverse determination in this matter could have a material adverse impact on the financial position and results of operations of the Company. The Company intends to continue to vigorously defend against plaintiffs' claims.

At this stage in this litigation, based upon the information currently available to the Company, the Company is not able to determine that an unfavorable outcome is remote, reasonably possible, or probable, and the Company has determined that it cannot reasonably estimate either the amount or the range of

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possible losses that would result if plaintiffs were to prevail, therefore, the Company has not made any accruals with respect to this matter in its consolidated financial statements.

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

*This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which reflect the current views and assumptions of management with respect to future events regarding our business and industry in general. These forward-looking statements include all statements, other than statements of historical fact, regarding our financial position, business strategy and other plans and objectives for future operations, including statements with respect to revenues and earnings, the amount and composition of assets under management, distribution sources, expense levels, redemption rates and the financial markets and other conditions. These statements are generally identified by the use of such words as may, could, should, would, believe, anticipate, forecast, estimate, expect, intend, plan, project, outlook, statements of a future or forward-looking nature. Readers are cautioned that any forward-looking information provided by or on behalf of the Company is not a guarantee of future performance. Actual results may differ materially from those contained in these forward-looking statements as a result of various factors, including but not limited to those discussed below. If one or more events related to these or other risks, contingencies or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may differ materially from those forecasted or expected. Certain important factors that could cause actual results to differ materially from our expectations are disclosed in the Risk Factors section of our Annual Report on Form 10-K for the year ended December 31, 2011, which include, without limitation:*

- *The introduction of legislative or regulatory proposals or judicial rulings that change the independent contractor classification of our financial advisors at the federal or state level for employment tax or other employee benefit purposes;*
- *The adverse ruling or resolution of any litigation, regulatory investigations and proceedings, or securities arbitrations by a federal or state court or regulatory body;*
- *The loss of existing distribution channels or inability to access new distribution channels;*
- *A reduction in assets under our management on short notice, through increased redemptions in our distribution channels or our Funds, particularly those Funds with a high concentration of assets, or investors terminating their relationship with us or shifting their funds to other types of accounts with different rate structures;*
- *Our inability to implement new information technology and systems, or inability to complete such implementation in a timely or cost effective manner;*
- *Non-compliance with applicable laws or regulations and changes in current legal, regulatory, accounting, tax or compliance requirements or governmental policies;*

- *A decline in the securities markets or in the relative investment performance of our Funds and other investment portfolios and products as compared to competing funds; and*
- *Our inability to hire and retain senior executive management and other key personnel.*

*The foregoing factors should not be construed as exhaustive and should be read together with other cautionary statements included in this and other reports and filings we make with the Securities and Exchange Commission, including the information in Item 1 Business and Item 1A Risk Factors of Part I and Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations of Part II to our Annual Report on Form 10-K for the year ended December 31, 2011 and as updated in our quarterly reports on Form 10-Q for the year ending December 31, 2012. All forward-looking statements speak only as the date on which they are made and we undertake no duty to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.*

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**Overview**

Founded in 1937, we are one of the oldest mutual fund complexes in the United States, with expertise in a broad range of investment styles and across a variety of market environments. Our earnings and cash flows are heavily dependent on financial market conditions. Significant increases or decreases in the various securities markets can have a material impact on our results of operations, financial condition and cash flows.

We derive our revenues from providing investment management, investment product underwriting and distribution, and shareholder services administration primarily to mutual funds and institutional and separately managed accounts. Investment management fees are based on the amount of average assets under management and are affected by sales levels, financial market conditions, redemptions and the composition of assets. Our underwriting and distribution revenues consist of commissions derived from sales of investment and insurance products, Rule 12b-1 asset-based service and distribution fees, distribution fees on certain variable products, fees earned on fee-based asset allocation products, and related advisory services. The products sold have various commission structures and the revenues received from those sales vary based on the type and amount sold. Shareholder service fee revenue includes transfer agency fees, custodian fees from retirement plan accounts, and portfolio accounting and administration fees, and is earned based on assets under management or number of client accounts. Our major expenses are underwriting and distribution-related commissions, employee compensation, amortization of deferred sales commissions, subadvisory fee expenses and information technology expense.

One of our distinctive qualities is that we are a significant distributor of investment products. Our retail products are distributed through our Advisors channel sales force of independent financial advisors or through our Wholesale channel, which includes third-parties such as other broker/dealers, registered investment advisors, and various retirement platforms. We also market our investment advisory services to institutional investors, either directly or through consultants, through our Institutional channel.

**Second Quarter Highlights**

- We broadened our product line by launching the Ivy Global Equity Income Fund and modifying an existing fund to bring to market Ivy Global Income Allocation Fund. These funds enhance our global product lineup and provide additional global equity and income allocation choices for investors.
- Our assets under management decreased 5% during the quarter, from \$93.8 billion to \$89.1 billion, driven by market depreciation.
- Net income decreased 17% compared to the second quarter of 2011, and our operating margin was 22.2%.
- We recorded a pre-tax charge of \$5.0 million to reflect the impairment of certain capitalized software development costs.

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- We recorded gains of \$1.1 million from the sale of trading and available for sale mutual fund holdings. Due to these gains, income tax expense was reduced by \$0.3 million.
  
- Our balance sheet remains solid, and we ended the quarter with cash and investments of \$505.5 million.

Table of Contents**Assets Under Management**

During the second quarter, assets under management decreased to \$89.1 billion compared to \$93.8 billion on March 31, 2012 due to market depreciation of \$5.0 billion and minimal net flows.

**Change in Assets Under Management(1)**

|                                      | Advisors  | Second Quarter 2012        |               | Total   |
|--------------------------------------|-----------|----------------------------|---------------|---------|
|                                      |           | Wholesale<br>(in millions) | Institutional |         |
| Beginning Assets                     | \$ 35,073 | 46,738                     | 11,981        | 93,792  |
| Sales (net of commissions)           | 1,046     | 3,864                      | 567           | 5,477   |
| Redemptions                          | (961)     | (3,535)                    | (1,058)       | (5,554) |
| Net Sales                            | 85        | 329                        | (491)         | (77)    |
| Net Exchanges                        | (49)      | 48                         |               | (1)     |
| Reinvested Dividends & Capital Gains | 147       | 249                        | 58            | 454     |
| Net Flows                            | 183       | 626                        | (433)         | 376     |
| Market Depreciation                  | (1,410)   | (2,985)                    | (654)         | (5,049) |
| Ending Assets                        | \$ 33,846 | 44,379                     | 10,894        | 89,119  |

|                                      | Advisors  | Second Quarter 2011        |               | Total   |
|--------------------------------------|-----------|----------------------------|---------------|---------|
|                                      |           | Wholesale<br>(in millions) | Institutional |         |
| Beginning Assets                     | \$ 34,922 | 44,742                     | 10,407        | 90,071  |
| Sales (net of commissions)           | 1,011     | 4,211                      | 556           | 5,778   |
| Redemptions                          | (1,058)   | (2,566)                    | (709)         | (4,333) |
| Net Sales                            | (47)      | 1,645                      | (153)         | 1,445   |
| Net Exchanges                        | (56)      | 55                         |               | (1)     |
| Reinvested Dividends & Capital Gains | 128       | 117                        | 28            | 273     |
| Net Flows                            | 25        | 1,817                      | (125)         | 1,717   |
| Market Appreciation (Depreciation)   | (104)     | (1)                        | 64            | (41)    |
| Ending Assets                        | \$ 34,843 | 46,558                     | 10,346        | 91,747  |

(1) Includes all activity of the Funds and institutional and separate accounts, including money market funds and transactions at net asset value, accounts for which we receive no commissions.





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Assets under management increased to \$89.1 billion on June 30, 2012 compared to \$83.2 billion on December 31, 2011 due to market appreciation of \$4.3 billion and net flows of \$1.7 billion.

|                                      | Advisors  | Year to Date 2012          |               | Total    |
|--------------------------------------|-----------|----------------------------|---------------|----------|
|                                      |           | Wholesale<br>(in millions) | Institutional |          |
| Beginning Assets                     | \$ 31,709 | 40,954                     | 10,494        | 83,157   |
| Sales (net of commissions)           | 2,076     | 8,297                      | 1,219         | 11,592   |
| Redemptions                          | (2,003)   | (6,981)                    | (1,565)       | (10,549) |
| Net Sales                            | 73        | 1,316                      | (346)         | 1,043    |
| Net Exchanges                        | 54        | (56)                       |               | (2)      |
| Reinvested Dividends & Capital Gains | 214       | 336                        | 88            | 638      |
| Net Flows                            | 341       | 1,596                      | (258)         | 1,679    |
| Market Appreciation                  | 1,796     | 1,829                      | 658           | 4,283    |
| Ending Assets                        | \$ 33,846 | 44,379                     | 10,894        | 89,119   |

|                                      | Advisors  | Year to Date 2011          |               | Total   |
|--------------------------------------|-----------|----------------------------|---------------|---------|
|                                      |           | Wholesale<br>(in millions) | Institutional |         |
| Beginning Assets                     | \$ 33,181 | 40,883                     | 9,609         | 83,673  |
| Sales (net of commissions)           | 2,075     | 8,930                      | 1,333         | 12,338  |
| Redemptions                          | (2,048)   | (5,728)                    | (1,240)       | (9,016) |
| Net Sales                            | 27        | 3,202                      | 93            | 3,322   |
| Net Exchanges                        | (118)     | 117                        |               | (1)     |
| Reinvested Dividends & Capital Gains | 182       | 117                        | 44            | 343     |
| Net Flows                            | 91        | 3,436                      | 137           | 3,664   |
| Market Appreciation                  | 1,571     | 2,239                      | 600           | 4,410   |
| Ending Assets                        | \$ 34,843 | 46,558                     | 10,346        | 91,747  |

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Average assets under management, which are generally more indicative of trends in revenue for providing investment management services than the quarter over quarter change in ending assets under management, are presented below.

*Average Assets Under Management*

| Asset Class: | Advisors  | Second Quarter 2012 |               | Total     |
|--------------|-----------|---------------------|---------------|-----------|
|              |           | Wholesale           | Institutional |           |
|              |           | (in millions)       |               |           |
| Equity       | \$ 23,897 | 37,597              | 10,651        | \$ 72,145 |
| Fixed Income | 8,788     | 6,991               | 766           | 16,545    |
| Money Market | 1,308     | 185                 |               | 1,493     |
| Total        | \$ 33,993 | 44,773              | 11,417        | \$ 90,183 |

| Asset Class: | Advisors  | Second Quarter 2011 |               | Total     |
|--------------|-----------|---------------------|---------------|-----------|
|              |           | Wholesale           | Institutional |           |
|              |           | (in millions)       |               |           |
| Equity       | \$ 26,049 | 41,767              | 9,713         | \$ 77,529 |
| Fixed Income | 7,512     | 3,478               | 782           | 11,772    |
| Money Market | 1,157     | 281                 |               | 1,438     |
| Total        | \$ 34,718 | 45,526              | 10,495        | \$ 90,739 |

| Asset Class: | Advisors  | Year to Date 2012 |               | Total     |
|--------------|-----------|-------------------|---------------|-----------|
|              |           | Wholesale         | Institutional |           |
|              |           | (in millions)     |               |           |
| Equity       | \$ 24,091 | 38,249            | 10,525        | \$ 72,865 |
| Fixed Income | 8,599     | 6,380             | 776           | 15,755    |
| Money Market | 1,312     | 205               |               | 1,517     |
| Total        | \$ 34,002 | 44,834            | 11,301        | \$ 90,137 |

| Asset Class: | Advisors  | Year to Date 2011 |               | Total     |
|--------------|-----------|-------------------|---------------|-----------|
|              |           | Wholesale         | Institutional |           |
|              |           | (in millions)     |               |           |
| Equity       | \$ 25,821 | 40,504            | 9,516         | \$ 75,841 |
| Fixed Income | 7,382     | 3,280             | 775           | 11,437    |
| Money Market | 1,195     | 276               |               | 1,471     |
| Total        | \$ 34,398 | 44,060            | 10,291        | \$ 88,749 |

Table of Contents**Results of Operations Three and Six Months Ended June 30, 2012 as Compared with Three and Six Months Ended June 30, 2011***Net Income*

|                           |    | <b>Three months ended<br/>June 30,</b> |             |                 |
|---------------------------|----|--|-------------|-----------------|
|                           |    | <b>2012</b>                            | <b>2011</b> | <b>Variance</b> |
| Net Income (in thousands) | \$ | 41,718                                 | 49,970      | -17%            |
| Earnings per share:       |    |  |             |                 |
| Basic                     | \$ | 0.48                                   | 0.58        | -17%            |
| Diluted                   | \$ | 0.48                                   | 0.58        | -17%            |
| Operating Margin          |    | 22.2%                                  | 25.5%       | -13%            |

|                           |    | <b>Six months ended<br/>June 30,</b> |             |                 |
|---------------------------|----|--------------------------------------|-------------|-----------------|
|                           |    | <b>2012</b>                          | <b>2011</b> | <b>Variance</b> |
| Net Income (in thousands) | \$ | 89,105                               | 95,603      | -7%             |
| Earnings per share:       |    |                                      |             |                 |
| Basic                     | \$ | 1.04                                 | 1.11        | -6%             |
| Diluted                   | \$ | 1.04                                 | 1.11        | -6%             |
| Operating Margin          |    | 23.0%                                | 25.4%       | -9%             |

We reported net income of \$41.7 million, or \$0.48 per diluted share, for the second quarter of 2012 compared to \$50.0 million, or \$0.58 per diluted share, for the second quarter of 2011. For the six months ended June 30, 2012, net income was \$89.1 million, or \$1.04 per diluted share, compared to \$95.6 million, or \$1.11 per diluted share, for the six months ended June 30, 2011.

During the second quarter of 2012, we recorded a pre-tax charge of \$5.0 million (\$3.1 million net of taxes, or \$0.04 per diluted share) to reflect the impairment of certain capitalized software development costs. This charge is included in general and administrative expenses. Our ongoing assessment and changes to our enterprise information technology infrastructure and software resulted in the decision to discontinue the usage of certain software.

Table of Contents*Total Revenues*

Total revenues decreased 1% to \$308.2 million for the three months ended June 30, 2012 compared to the three months ended June 30, 2011 due to a decrease in average assets under management of 1% and a decrease in gross sales of 5%. For the six months ended June 30, 2012, total revenues increased \$8.3 million, or 1% compared to the same period in the prior year due to an increase in average assets under management of 2%, offset by a decrease in gross sales of 6%.

|  | Three months ended<br>June 30, |         |         | Variance |
|--|--------------------------------|---------|---------|----------|
|  | 2012                           | 2011    |         |          |
| (in thousands, except percentage data) |                                |         |         |          |
| Investment management fees             | \$                             | 134,213 | 138,985 | -3%      |
| Underwriting and distribution fees     |                                | 139,944 | 137,354 | 2%       |
| Shareholder service fees               |                                | 34,051  | 33,606  | 1%       |
| Total revenues                         | \$                             | 308,208 | 309,945 | -1%      |

|  | Six months ended<br>June 30, |         |         | Variance |
|--|------------------------------|---------|---------|----------|
|  | 2012                         | 2011    |         |          |
| (in thousands, except percentage data) |                              |         |         |          |
| Investment management fees             | \$                           | 269,113 | 270,629 | -1%      |
| Underwriting and distribution fees     |                              | 277,434 | 270,117 | 3%       |
| Shareholder service fees               |                              | 68,279  | 65,773  | 4%       |
| Total revenues                         | \$                           | 614,826 | 606,519 | 1%       |

*Investment Management Fee Revenues*

Investment management fee revenues are earned for providing investment advisory services to the Funds and to institutional and separate accounts. Investment management fee revenues decreased \$4.8 million, or 3%, from last year's second quarter. For the six month period ended June 30, 2012, investment management fee revenues decreased \$1.5 million, or 1%, compared to the same period in 2011.

Revenues from investment management services provided to our retail mutual funds, which are distributed through the Advisors, Wholesale and Institutional channels, were \$123.5 million for the quarter ended June 30, 2012. Revenues decreased \$5.0 million, or 4%, compared to the second quarter of 2011, while the related retail average assets decreased 2% to \$78.8 billion. Investment management fee revenues decreased more than the related retail average assets due to a shift in assets to products with lower than average management fee rates. For the six months ended June 30, 2012, revenues from investment management services provided to our retail mutual funds were \$247.8 million. Revenues decreased \$2.3 million, or 1%, compared to the first six months of 2011, while the related retail average assets increased 1% to \$78.8 billion. Investment management fee revenues decreased more than the related retail average assets due in part to a shift in assets toward products with lower than average management fee rates and also due to the effect of recording management fee waivers, mostly for money market funds, as an offset to investment management fees.

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Institutional account revenues were \$10.7 million for the second quarter of 2012, representing an increase of \$0.3 million, or 2%, from the second quarter of 2011, while average assets increased 9%. For the six month period ended June 30, 2012, institutional account revenues were \$21.3 million, an increase of 4% compared to the same period in 2011, and average assets increased 10%. For both periods, account revenues increased less than the related average assets due to a decline in the average management fee rate.

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Long-term redemption rates (which exclude money market fund redemptions) in the Advisors channel were 9.1% in the second quarter of 2012 and 9.6% year-to-date, compared to 10.1% in the second quarter of 2011 and 9.9% for the first six months of 2011. In the Wholesale channel, long-term redemption rates were 31.5% for the quarter ended June 30, 2012, compared to 22.3% in the second quarter of 2011. For the six months ended June 30, 2012, the Wholesale channel's long-term redemption rate increased to 31.1% compared to 25.8% for the same period in 2011. We expect the Advisors channel long-term redemption rate to remain lower than that of the Wholesale channel due to the personal and customized nature in which our financial advisors provide service to our clients. Long-term redemption rates for our Institutional channel were 37.3% and 27.1% for the second quarter of 2012 and 2011, respectively, and 27.9% for the six month period ended June 30, 2012 compared to 24.3% for the same period in 2011.

Our overall redemption rate of 22.7% for the first six months of 2012 compares positively to the current year to date industry average of approximately 25%, based on data from the Investment Company Institute.

Table of Contents*Underwriting and Distribution Fee Revenues and Expenses*

The following tables summarize our underwriting and distribution fee revenues and expenses segregated by distribution method within the respective Advisors or Wholesale channel:

|                                 | Advisors   | Second Quarter 2012<br>Wholesale<br>(in thousands) | Total    |
|---------------------------------|------------|--|----------|
| Revenue                         | \$ 79,779  | 60,165   | 139,944  |
| Expenses                        |            |  |          |
| Direct                          | 55,813     | 66,142   | 121,955  |
| Indirect                        | 26,755     | 14,322   | 41,077   |
|                                 | 82,568     | 80,464   | 163,032  |
| Net Underwriting & Distribution | \$ (2,789) | (20,299)   | (23,088) |

|                                 | Advisors   | Second Quarter 2011<br>Wholesale<br>(in thousands) | Total    |
|---------------------------------|------------|--|----------|
| Revenue                         | \$ 74,018  | 63,336   | 137,354  |
| Expenses                        |            |  |          |
| Direct                          | 52,422     | 69,376   | 121,798  |
| Indirect                        | 23,724     | 11,697   | 35,421   |
|                                 | 76,146     | 81,073   | 157,219  |
| Net Underwriting & Distribution | \$ (2,128) | (17,737)   | (19,865) |

|                                 | Advisors   | Year to Date 2012<br>Wholesale<br>(in thousands) | Total    |
|---------------------------------|------------|--|----------|
| Revenue                         | \$ 156,459 | 120,975  | 277,434  |
| Expenses                        |            |  |          |
| Direct                          | 109,489    | 131,979  | 241,468  |
| Indirect                        | 53,122     | 27,917   | 81,039   |
|                                 | 162,611    | 159,896  | 322,507  |
| Net Underwriting & Distribution | \$ (6,152) | (38,921)   | (45,073) |

|                                 | Advisors   | Year to Date 2011<br>Wholesale<br>(in thousands) | Total    |
|---------------------------------|------------|--|----------|
| Revenue                         | \$ 146,573 | 123,544  | 270,117  |
| Expenses                        |            |  |          |
| Direct                          | 103,294    | 135,967  | 239,261  |
| Indirect                        | 46,515     | 23,447   | 69,962   |
|                                 | 149,809    | 159,414  | 309,223  |
| Net Underwriting & Distribution | \$ (3,236) | (35,870)   | (39,106) |





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Underwriting and distribution revenues earned in the second quarter of 2012 increased \$2.6 million, or 2%, compared with the second quarter of 2011 as a result of increased revenues in our Advisors channel of \$5.8 million, partially offset by lower revenues in our Wholesale channel of \$3.2 million. Revenues from fee-based asset allocation products increased \$7.3 million compared to the prior year. Technology fees collected from our advisors of \$0.9 million during the second quarter of 2012 resulted in an increase period over period as fees were netted in expense during the second quarter of 2011. Partially offsetting these increases, variable annuity revenues decreased \$0.9 million and financial plan revenues decreased \$0.5 million. Rule 12b-1 asset-based service and distribution fee revenues decreased \$4.0 million, or 6%, as a result of a decrease in average mutual fund assets under management.

For the six months ended June 30, 2012, underwriting and distribution revenues increased \$7.3 million, or 3%, compared with the six months ended June 30, 2011. The increase was comprised of an increase in the Advisors channel of \$9.9 million and a \$2.6 million decrease in Wholesale channel revenues period over period. Revenues from fee-based asset allocation products increased \$15.6 million compared to the prior year. Technology fees collected from our advisors of \$1.9 million during the first half of 2012 resulted in an increase period over period as fees were netted in expense during 2011. Partially offsetting these increases, variable annuity revenues decreased \$3.5 million compared to the prior year, other front-load product sales revenues decreased \$1.6 million and financial plan revenues decreased \$0.8 million. Rule 12b-1 asset-based service and distribution fee revenues decreased \$4.4 million, or 3%, due to a decrease in average mutual fund assets under management.

Underwriting and distribution expenses increased by \$5.8 million, or 4%, compared to the second quarter of 2011. Direct expenses in the Advisors channel increased \$3.4 million, or 6%, compared to the second quarter of 2011 due to increased commissions related to the sale of fee-based asset allocation products of \$5.1 million and higher amortization expense of deferred sales commissions of \$1.1 million, partially offset by decreased commissions on variable annuity product sales of \$0.9 million and decreased Rule 12b-1 asset-based service and distribution expenses of \$0.9 million. Direct expenses in the Wholesale channel decreased by \$3.2 million, due to decreased Rule 12b-1 asset-based service and distribution expenses of \$2.3 million, lower dealer compensation paid to third party distributors and lower wholesaler commissions of \$0.2 million from lower sales volumes. Indirect expenses increased \$5.7 million compared to the quarter ended June 30, 2011 due primarily to increased employee compensation and benefits expenses, pension expenses and marketing costs. The second quarter of 2012 also included costs for an electronic books and records conversion initiative in our Advisors channel, which is expected to be complete during the third quarter of 2012.

For the six months ended June 30, 2012, underwriting and distribution expenses increased by \$13.3 million, or 4%, compared to the first six months of 2011. Direct expenses in the Advisors channel increased \$6.2 million, or 6%, compared to 2011 due to increased commissions related to the sale of fee-based asset allocation products of \$9.9 million and higher amortization expense of deferred sales commissions of \$2.6 million, partially offset by decreased Rule 12b-1 asset-based service and distribution expenses of \$2.0 million and decreased commissions of \$2.7 million on variable annuity product sales. Direct expenses in the Wholesale channel decreased by \$4.0 million, due to decreased Rule 12b-1 asset-based service and distribution expenses of \$2.0 million, lower dealer compensation paid to third party distributors and lower wholesaler commissions of \$0.7 million from lower sales volumes. For the six months ended June 30, 2012, indirect expenses increased \$11.1 million compared to the same period in 2011 due primarily to increased employee compensation and benefits expenses, pension expenses and marketing costs. The first six months of 2012 also included costs for an electronic books and records conversion initiative in our Advisors channel, which is expected to be complete during the third quarter of 2012.

*Shareholder Service Fee Revenue*

Shareholder service fee revenue primarily includes transfer agency fees, custodian fees from retirement plan accounts, and portfolio accounting and administration fees. Portfolio accounting and administration fees are asset-based revenues or account-based revenues, while transfer agency fees and custodian fees from retirement plan accounts are based on the number of client accounts. During the second quarter of 2012,

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shareholder service fee revenue increased \$0.4 million, or 1%, over the second quarter of 2011. An increase of \$0.5 million due to higher asset-based fees quarter over quarter in certain share classes was partially

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offset by a \$0.1 million decrease attributable to account-based revenues due to a 1% decrease in the average number of accounts. For the six month period ended June 30, 2012, shareholder service fee revenue increased \$2.5 million, or 4%, compared to the same period in 2011. Of this increase, \$1.9 million is due to higher asset-based fees in certain share classes and \$0.6 million is attributable to account-based revenues due to a 3% increase in the average number of accounts.

*Total Operating Expenses*

Operating expenses increased \$8.8 million, or 4%, in the second quarter of 2012 compared to the second quarter of 2011, primarily due to increased underwriting and distribution expenses and general and administrative expenses, partially offset by lower subadvisory fees. For the six months ended June 30, 2012, operating expenses increased \$20.9 million, or 5%, compared to the first six months of 2011, primarily due to increased underwriting and distribution expenses, compensation and related costs, and general and administrative expenses, partially offset by lower subadvisory fees. Underwriting and distribution expenses are discussed above.

|                                | <b>Three Months Ended<br/>June 30,</b>        |             |  | <b>Variance</b> |
|--------------------------------|---|-------------|--|-----------------|
|                                | <b>2012</b>                                   | <b>2011</b> |  |                 |
|                                | <b>(in thousands, except percentage data)</b> |             |  |                 |
| Underwriting and distribution  | \$ 163,032                                    | 157,219     |  | 4%              |
| Compensation and related costs | 42,973  | 42,092      |  | 2%              |
| General and administrative     | 25,095  | 19,500      |  | 29%             |
| Subadvisory fees               | 5,208   | 8,313       |  | -37%            |
| Depreciation                   | 3,428   | 3,842       |  | -11%            |
| Total operating expenses       | \$ 239,736                                    | 230,966     |  | 4%              |

|                                | <b>Six Months Ended<br/>June 30,</b>          |             |  | <b>Variance</b> |
|--------------------------------|---|-------------|--|-----------------|
|                                | <b>2012</b>                                   | <b>2011</b> |  |                 |
|                                | <b>(in thousands, except percentage data)</b> |             |  |                 |
| Underwriting and distribution  | \$ 322,507                                    | 309,223     |  | 4%              |
| Compensation and related costs | 88,376  | 82,567      |  | 7%              |
| General and administrative     | 44,419  | 37,131      |  | 20%             |
| Subadvisory fees               | 11,479  | 16,393      |  | -30%            |
| Depreciation                   | 6,900   | 7,446       |  | -7%             |
| Total operating expenses       | \$ 473,681                                    | 452,760     |  | 5%              |

*Compensation and Related Costs*

On April 2, 2012, we granted 1,205,698 shares of nonvested stock with a fair value of \$33.23 per share under the SI Plan. The value of those shares at the grant date, aggregating \$40.1 million, will be amortized to expense over a four year vesting period.

Compensation and related costs increased \$0.9 million, or 2%, compared to the second quarter of 2011, due to higher base salaries of \$1.5 million associated with increased headcount and annual salary increases and higher pension costs of \$0.9 million. Partially offsetting these increases, incentive compensation decreased \$1.1 million compared to the second quarter of 2011, \$0.1 million of which related to lower

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earnings on portfolio manager deferred compensation plans. Share-based compensation decreased \$0.7 million primarily due to a decrease in non-employee advisor (independent contractor) stock award amortization expense.

For the six months ended June 30, 2012, compensation and related costs increased \$5.8 million, or 7%, compared to the first six months of 2011, due to higher base salaries of \$3.1 million associated with increased headcount and annual salary increases, higher pension costs of \$1.7 million and decreased capitalized software development activities of \$0.6 million. Share-based compensation increased \$1.7

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million compared to the first half of 2011 due to higher amortization expense associated with our April 2012 and December 2011 grants of nonvested stock compared to grants that became fully vested in 2011. Partially offsetting these increases, incentive compensation decreased \$1.5 million compared to the first six months of 2011, \$0.3 million of which related to lower earnings on portfolio manager deferred compensation plans.

*General and Administrative Costs*

General and administrative expenses increased \$5.6 million to \$25.1 million for the second quarter of 2012 compared to the second quarter of 2011. During the second quarter of 2012, we recorded a pre-tax charge of \$5.0 million to reflect the impairment of certain capitalized software development costs. Our ongoing assessment and changes to our enterprise information technology infrastructure and software resulted in the decision to discontinue the usage of certain software. Excluding this charge, general and administrative costs increased \$0.6 million. The variance is due to increased dealer services costs and higher costs for temporary office staff.

For the six months ended June 30, 2012, general and administrative expenses increased \$7.3 million compared to the same period in 2011. Excluding the \$5.0 million charge recorded in 2012, general and administrative expenses increased \$2.3 million, due to increased dealer services costs of \$2.0 million and higher costs for temporary office staff, partially offset by lower costs incurred for our national branding campaign that was launched in the first quarter of 2011, and reduced legal expenses.

*Subadvisory Fees*

Subadvisory fees represent fees paid to other asset managers for providing advisory services for certain mutual fund portfolios. These expenses reduce our operating margin since we pay out approximately half of our management fee revenue received from subadvised products. Gross management fee revenues for products subadvised by others were \$10.3 million for the three months ended June 30, 2012 compared to \$16.5 million for the second quarter of 2011 due to a 39% decrease in average net assets. For the six months ended June 30, 2012, gross management fee revenues for products subadvised by others were \$22.8 million compared to \$32.6 million for the same period in 2011 due to a 31% decrease in average net assets. Subadvisory expenses followed the same pattern of decrease compared to 2011.

*Other Income and Expenses*

*Investment and Other Income, Interest Expense and Taxes*

Investment and other income was \$1.3 million for the quarter ended June 30, 2012, compared to \$2.5 million in the same period a year ago. We recorded gains of \$0.2 million from the sale of available for sale mutual fund holdings during the second quarter of 2012, compared to gains of \$2.0 million for the same period in 2011. In our mutual fund trading portfolio, we recorded gains of \$0.9 million during the quarter, compared to gains of \$0.3 million in the second quarter of 2011.

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For the six months ended June 30, 2012 and 2011, investment and other income was \$5.3 million and \$3.5 million, respectively. In our mutual fund trading portfolio, we recorded gains of \$2.9 million in 2012, compared to gains of \$0.9 million in 2011. We also recorded gains of \$1.7 million from the sale of available for sale mutual fund holdings during the first six months of 2012, compared to \$2.0 million during the first six months of 2011. Included in 2012 were interest and gains related to debt securities of \$0.7 million.

Interest expense was \$2.8 million in the second quarter of both 2012 and 2011, and \$5.7 million for the six month periods ended June 30, 2012 and 2011.

Our effective income tax rate was 37.7% for the second quarter of 2012, compared to 36.4% for the second quarter of 2011. Due to the sale of a subsidiary in 2009, the Company has deferred tax assets related to capital loss carryforwards that are available to offset current and future capital gains. In 2009, a valuation allowance was recorded on a portion of these capital losses due to the limited carryforward period permitted by law on losses of this character. The higher effective tax rate in 2012 as compared to 2011 was attributable in part to a smaller release of this valuation allowance through income tax expense in 2012. An increase in the fair value of the Company's trading securities portfolio and realized capital gains on

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securities classified as available for sale in the second quarter of 2012 allowed for a release of the valuation allowance, thereby reducing income tax expense by \$0.3 million. Realized capital gains on securities classified as available for sale in the second quarter of 2011 allowed for the release of the valuation allowance, thereby reducing income tax expense by \$0.8 million.

The second quarter 2012 and 2011 effective income tax rates, removing the effects of the valuation allowance, would have been 38.1% and 37.4%, respectively. The increase in the adjusted effective income tax rate is primarily due to lower income before taxes in 2012, which increases the impact of non-deductible expenses on the effective income tax rate. Additionally, the rate was lower in the second quarter of 2011 due to the recognition of a tax position previously considered partially uncertain.

Our effective income tax rate was 36.7% for the six months ended June 30, 2012, as compared to 36.9% for the six months ended June 30, 2011. Excluding the \$1.6 million decrease to the valuation allowance recorded through the statement of income for the six months ended June 30, 2012, the effective income tax rate would have been 37.9%. Excluding the \$1.0 million decrease to the valuation allowance recorded through the statement of income for the six months ended June 30, 2011, the effective income tax rate would have been 37.6%. The increase in the adjusted effective income tax rate is primarily due to lower income before taxes in 2012, which increases the impact of non-deductible expenses on the effective income tax rate.

The Company expects its future effective tax rate, exclusive of any increases or reductions to the valuation allowance, state tax incentives, unanticipated state tax legislative changes, and unanticipated fluctuations in earnings to range from 37% to 39%.

**Liquidity and Capital Resources**

Our operations provide much of the cash necessary to fund our priorities, as follows:

- Finance internal growth
  
- Pay dividends
  
- Repurchase our stock

*Finance Internal Growth*



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We use cash to fund growth in our distribution channels. Our Wholesale channel, which has a higher cost to gather assets, requires cash outlays for wholesaler commissions and commissions to third parties on deferred load product sales. We continue to invest in our Advisors channel by providing additional support to our advisors through wholesaling efforts and enhanced technology tools.

### *Pay Dividends*

We paid quarterly dividends on our common stock that resulted in financing cash outflows of \$43.0 million and \$34.5 million for the first six months of 2012 and 2011, respectively. The Board approved an increase in the quarterly dividend on our common stock from \$0.20 per share to \$0.25 per share beginning with our fourth quarter 2011 dividend, paid on February 1, 2012.

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*Repurchase Our Stock*

We repurchased 945,354 shares and 957,673 shares of our common stock in the open market during the six months ended June 30, 2012 and 2011, respectively, resulting in cash outflows of \$29.3 million and \$37.7 million, respectively.

**Operating Cash Flows**

Cash from operations is our primary source of funds and decreased \$72.1 million for the six months ended June 30, 2012 compared to the previous year. The decrease is primarily due to net purchases of trading securities in 2012 compared to significant net sales of trading securities in 2011.

During the first six months of 2012, we contributed \$15.0 million to our Pension Plan. We do not expect to make additional contributions for the remainder of 2012.

**Investing Cash Flows**

Investing activities consist primarily of the purchase, sale and maturities of available for sale investment securities, as well as capital expenditures. We expect our 2012 capital expenditures to be in the range of \$12.0 to \$15.0 million.

**Financing Cash Flows**

As noted previously, dividends and stock repurchases accounted for a majority of our financing cash outflows in the first six months of 2012 and 2011.

**Future Capital Requirements**

Management believes its available cash, marketable securities and expected cash flow from operations will be sufficient to fund its short-term operating and capital requirements. Expected short-term uses of cash include dividend payments, interest payments on outstanding debt, income tax payments, seed money for new investment products, share repurchases, payment of deferred commissions to our financial advisors and third parties, capital expenditures and home office leasehold improvements, and could include strategic acquisitions.

Expected long-term capital requirements include indebtedness, operating leases and purchase obligations, and potential recognition of tax liabilities. Other possible long-term discretionary uses of cash could include capital expenditures for enhancement of technology infrastructure and home office expansion, strategic acquisitions, payment of dividends, income tax payments, seed money for new investment products, payment of upfront fund commissions for Class B shares, Class C shares and certain fee-based asset allocation products, pension funding and repurchases of our common stock.

### **Critical Accounting Policies and Estimates**

Management believes certain critical accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements. The Company's critical accounting policies and estimates are disclosed in the Critical Accounting Policies and Estimates section of our 2011 Form 10-K.

As of June 30, 2012, the Company's annual impairment test indicated that goodwill and identifiable intangible assets were not impaired. Related to goodwill, the fair value of the investment management and related services reporting unit exceeded its carrying value by more than 100% and the fair value of the Legend reporting unit exceeded its carrying value by 40%. The fair value of our indefinite-life intangible assets exceeded their respective carrying values by 80%.

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|  | Second<br>Quarter<br>2012 | Second<br>Quarter<br>2011 | Change | Year to<br>Date<br>2012 | Year to<br>Date<br>2011 | Change |
|--|---------------------------|---------------------------|--------|-------------------------|-------------------------|--------|
| <b>Redemption rates - long term (annualized)</b> |                           |                           |        |                         |                         |        |
| Advisors   | 9.1%                      | 10.1%                     |        | 9.6%                    | 9.9%                    |        |
| Wholesale  | 31.5%                     | 22.3%                     |        | 31.1%                   | 25.8%                   |        |
| Institutional                                    | 37.3%                     | 27.1%                     |        | 27.9%                   | 24.3%                   |        |
| Total  | 23.9%                     | 18.2%                     |        | 22.7%                   | 19.6%                   |        |
| Gross revenue per advisor (000 \$)               | 42.2                      | 40.2                      | 5.0%   | 82.5                    | 79.4                    | 3.9%   |
| Number of financial advisors                     | 1,764                     | 1,751                     | 0.7%   |                         |                         |        |
| Average number of financial advisors             | 1,767                     | 1,737                     | 1.7%   | 1,775                   | 1,750                   | 1.4%   |
| Number of shareholder accounts (000 \$)          | 4,139                     | 4,087                     | 1.3%   |                         |                         |        |
| Number of shareholders                           | 823,875                   | 819,368                   | 0.6%   |                         |                         |        |

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

The Company has had no significant changes in its Quantitative and Qualitative Disclosures About Market Risk from that previously reported in the Company's 2011 Form 10-K.

**Item 4. Controls and Procedures**

The Company maintains a system of disclosure controls and procedures that is designed to provide reasonable assurance that information, which is required to be timely disclosed, is accumulated and communicated to management in a timely fashion. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. The Company's Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this quarterly report, have concluded that the Company's disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure and are effective to provide reasonable assurance that such information is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

The Company's internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f) and 15d-15(f)) is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. There were no changes in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. However, because of the inherent limitations in all control systems, no evaluation of

controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected.

Table of Contents**Part II. Other Information****Item 1. Legal Proceedings**

The Company is involved from time to time in various legal proceedings, regulatory investigations and claims incident to the normal conduct of business, which may include proceedings that are specific to us and others generally applicable to the business practices within the industries in which we operate. A substantial legal liability or a significant regulatory action against us could have an adverse effect on our business, financial condition and on the results of operations in a particular quarter or year. Information required to be reported under this Part II., Item 1. has been previously disclosed in Note 11 to the consolidated financial statements in Part I. above and is incorporated herein by reference.

**Item 1A. Risk Factors**

The Company has had no material changes to its Risk Factors from those previously reported in the Company's 2011 Form 10-K.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table sets forth certain information about the shares of common stock we repurchased during the second quarter of 2012.

| Period             | Total Number of Shares Purchased (1) | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Program | Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Program |
|--------------------|--------------------------------------|------------------------------|--|--|
| April 1 - April 30 | 512,743                              | \$ 32.77                     | 512,743  | n/a(1)   |
| May 1 - May 31     | 357,245                              | 29.36                        | 357,245  | n/a(1)   |
| June 1 - June 30   | 75,000                               | 26.95                        | 75,000   | n/a(1)   |
| Total              | 944,988                              | \$ 31.02                     | 944,988  |  |

(1) On August 31, 1998, we announced that our Board of Directors approved a program to repurchase shares of our common stock on the open market. Under the repurchase program, we are authorized to repurchase, in any seven-day period, the greater of (i) 3% of our outstanding common stock or (ii) \$50 million of our common stock. We may repurchase our common stock through the New York Stock Exchange, other national or regional market systems, electronic communication networks or alternative trading systems. Our stock repurchase program does not have an expiration date or an aggregate maximum number or dollar value of shares that may be repurchased. Our Board of Directors reviewed and ratified the stock repurchase program in July 2004. During the second quarter of 2012, all stock repurchases were made pursuant to the repurchase program and 412,988 shares, reflected in the table above, were purchased in connection with funding employee income tax withholding obligations arising from the vesting of nonvested shares.



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**Item 6.**

**Exhibits**

31.1 Section 302 Certification of Chief Executive Officer

31.2 Section 302 Certification of Chief Financial Officer

32.1 Section 906 Certification of Chief Executive Officer

32.2 Section 906 Certification of Chief Financial Officer

101 Materials from the Waddell & Reed Financial, Inc. Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, formatted in Extensible Business Reporting Language (XBRL): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statement of Stockholders' Equity, (v) Consolidated Statements of Cash Flows, and (vi) related Notes to the Unaudited Consolidated Financial Statements, tagged in detail.



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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, this 2nd day of August 2012.

**WADDELL & REED FINANCIAL, INC.**

By: /s/ Henry J. Herrmann  
Chief Executive Officer, Chairman of the Board and  
Director  
(Principal Executive Officer)

By: /s/ Daniel P. Connealy  
Senior Vice President  
and Chief Financial Officer  
(Principal Financial Officer)

By: /s/ Brent K. Bloss  
Senior Vice President - Finance and Treasurer  
(Principal Accounting Officer)