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 the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date:

As of May 10, 2001, there were 319,290,700 shares of common stock and 2,815,253 shares exchangeable into common stock outstanding. The Exchangeable Shares, which were issued by EGI Canada Corporation in connection with the acquisition of VERSUS Technologies, Inc. (renamed E*TRADE Technologies Corporation effective January 2, 2001), are exchangeable at any time into common stock on a one-for-one basis and entitle holders to dividend, voting, and other rights equivalent to holders of the registrant’s common stock.

---

**E*TRADE GROUP, INC.**

**FORM 10-Q QUARTERLY REPORT**

For the Quarter Ended March 31, 2001

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**Part I—Financial Information**

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</tbody>
</table>
### PART I.  FINANCIAL INFORMATION

#### Item 1.  Financial Statements

**E*TRADE GROUP, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF OPERATIONS**

(in thousands, except per share amounts)  
(unaudited)

<table>
<thead>
<tr>
<th></th>
<th>Three Months Ended</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>March 31, 2001</td>
<td>2000</td>
<td></td>
</tr>
<tr>
<td><strong>Revenues:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transaction revenues</td>
<td>$131,362</td>
<td>$254,596</td>
<td></td>
</tr>
<tr>
<td>Interest income</td>
<td>317,430</td>
<td>243,582</td>
<td></td>
</tr>
<tr>
<td>Global and institutional</td>
<td>36,841</td>
<td>49,676</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>64,492</td>
<td>16,711</td>
<td></td>
</tr>
<tr>
<td><strong>Gross revenues</strong></td>
<td>550,125</td>
<td>564,565</td>
<td></td>
</tr>
<tr>
<td>Interest expense</td>
<td>(219,101)</td>
<td>(146,609)</td>
<td></td>
</tr>
<tr>
<td>Provision for loan losses</td>
<td>(1,443)</td>
<td>(1,256)</td>
<td></td>
</tr>
<tr>
<td><strong>Net revenues</strong></td>
<td>329,581</td>
<td>416,700</td>
<td></td>
</tr>
<tr>
<td><strong>Cost of services</strong></td>
<td>142,435</td>
<td>135,579</td>
<td></td>
</tr>
<tr>
<td><strong>Operating expenses:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Selling and marketing</td>
<td>93,698</td>
<td>180,605</td>
<td></td>
</tr>
<tr>
<td>Technology development</td>
<td>22,281</td>
<td>45,335</td>
<td></td>
</tr>
<tr>
<td>General and administrative</td>
<td>60,242</td>
<td>52,551</td>
<td></td>
</tr>
<tr>
<td>Amortization of goodwill and other intangibles</td>
<td>7,999</td>
<td>5,297</td>
<td></td>
</tr>
<tr>
<td>Acquisition-related expenses</td>
<td>—</td>
<td>24,599</td>
<td></td>
</tr>
<tr>
<td><strong>Total operating expenses</strong></td>
<td>184,220</td>
<td>306,387</td>
<td></td>
</tr>
<tr>
<td><strong>Total cost of services and operating expenses</strong></td>
<td>326,655</td>
<td>441,966</td>
<td></td>
</tr>
<tr>
<td><strong>Operating income (loss)</strong>*</td>
<td>2,926</td>
<td>(25,266)</td>
<td></td>
</tr>
<tr>
<td><strong>Non-operating income (expense):</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Corporate interest income</td>
<td>5,778</td>
<td>3,620</td>
<td></td>
</tr>
<tr>
<td>Corporate interest expense</td>
<td>(11,228)</td>
<td>(7,128)</td>
<td></td>
</tr>
<tr>
<td>Gain (loss) on sale of investments</td>
<td>(2,531)</td>
<td>10,915</td>
<td></td>
</tr>
<tr>
<td>Equity in losses of investments</td>
<td>(3,341)</td>
<td>(736)</td>
<td></td>
</tr>
<tr>
<td>Unrealized loss on venture funds</td>
<td>(11,611)</td>
<td>(14,628)</td>
<td></td>
</tr>
<tr>
<td>Fair value adjustments of financial derivatives</td>
<td>334</td>
<td>—</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>(700)</td>
<td>(753)</td>
<td></td>
</tr>
<tr>
<td><strong>Total non-operating expense</strong></td>
<td>(23,299)</td>
<td>(8,710)</td>
<td></td>
</tr>
<tr>
<td><strong>Pretax loss</strong></td>
<td>(20,373)</td>
<td>(33,976)</td>
<td></td>
</tr>
<tr>
<td><strong>Income tax benefit</strong></td>
<td>(13,242)</td>
<td>(8,918)</td>
<td></td>
</tr>
<tr>
<td><strong>Minority interest in subsidiaries</strong></td>
<td>35</td>
<td>408</td>
<td></td>
</tr>
<tr>
<td><strong>Loss before extraordinary loss on early extinguishment of debt, net of tax (See Note 12)</strong></td>
<td>(7,166)</td>
<td>(25,466)</td>
<td></td>
</tr>
</tbody>
</table>

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*References to E*TRADE, Company, “we”, “us” and “our” in this Form 10-Q refer to E*TRADE Group, Inc. and its subsidiaries unless the context requires otherwise.

E*TRADE, the E*TRADE logo, etrade.com, E*TRADE Bank, ClearStation, Equity Edge, Equity Resource, OptionsLink, ShareData, Stateless Architecture, Power E*TRADE, Destination E*TRADE, and TELE*MASTER are registered service marks or trademarks of E*TRADE Group, Inc. or its subsidiaries in the United States. Some of these and other trademarks are registered outside the United States.
Extraordinary loss on early extinguishment of debt, net of tax

$ (2,037)

Net loss

$ (9,203)  $ (25,466)

Loss per share before extraordinary loss on early extinguishment of debt:

Basic  $ (0.02)  $ (0.09)

Diluted  $ (0.02)  $ (0.09)

Net loss per share:

Basic  $ (0.03)  $ (0.09)

Diluted  $ (0.03)  $ (0.09)

Shares used in computation of per share data (See Note 11):

Basic 317,242  298,026

Diluted 317,242  298,026

See notes to condensed consolidated financial statements.

E*TRADE GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(in thousands, except share amounts)

March 31, 2001 September 30, 2000

( unaudited)

ASSETS

Cash and equivalents  $ 156,094  $ 175,443

Cash and investments required to be segregated under Federal or other regulations  134,368  125,862

Brokerage receivables—net  4,562,003  6,542,508

Mortgage-backed securities  3,970,223  4,188,553

Loans receivable—net of allowance for loan losses of $13,821 at March 31, 2001 and $10,930 at September 30, 2000  6,345,377  4,172,754

Investments  1,722,330  985,218

Property and equipment—net  425,587  334,262

Goodwill and other intangibles  456,813  484,166

Other assets  642,740  308,671

Total assets  $18,415,535  $17,317,437

LIABILITIES AND SHAREOWNERS’ EQUITY

Liabilities:

Brokerage payables  $ 4,273,285  $ 6,055,530

Banking deposits  6,862,630  4,721,801

Borrowings by bank subsidiary  4,033,426  3,531,000

Convertible subordinated notes  650,000  650,000

Accounts payable, accrued and other liabilities  842,339  471,626

Total liabilities  16,661,680  15,429,957

Company-obligated mandatorily redeemable preferred capital securities of subsidiary trusts holding solely junior subordinated debentures of the Company (redemption value $32,400)  30,763  30,647

Total liabilities  16,692,443  15,459,594

Commitments and contingencies

Shareowners’ equity:

Preferred stock, shares authorized: 1,000,000; issued and outstanding: none at March 31, 2001 and September 30, 2000  —  —

Shares exchangeable into common stock, $.01 par value, shares authorized: 10,644,223; issued and outstanding: 3,293,840 at March 31, 2001 and 5,619,543 at September 30, 2000  33  56

Common stock, $.01 par value, shares authorized: 600,000,000; issued and outstanding: 318,908,996 at March 31, 2001 and 304,504,764 at September 30, 2000  3,189  3,045

Additional paid-in capital  1,907,837  1,814,581

Unearned Employee Stock Ownership Plan shares  (1,286)  (1,560)

Shareowners’ notes receivable  19,640  (19,103)

Deferred stock compensation  (13,088)  —

Accumulated deficit  (14,758)  (6,908)

Accumulated other comprehensive income (loss)  (139,195)  66,722

Total shareowners’ equity  1,723,092  1,856,833

Total liabilities and shareowners’ equity  18,415,535  17,317,437
### Condensed Consolidated Statements of Cash Flows

(in thousands)  
(unaudited)

<table>
<thead>
<tr>
<th>Three Months Ended</th>
<th>March 31,</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>2000</td>
<td></td>
</tr>
</tbody>
</table>

**Net cash used in operating activities**  
$ (92,546)  
(142,230)

**CASH FLOWS FROM INVESTING ACTIVITIES:**

- **Purchase of mortgage-backed securities, available-for-sale securities, and other investments, net of securities received in business acquisitions**:  
  \((6,709,043)\)  
  \((3,173,463)\)

- **Proceeds from sales, maturities of and principal payments on mortgage-backed securities, available-for-sale securities, and other investments**:  
  \(7,229,679\)  
  \(2,114,438\)

- **Net increase in loans receivable, net of loans received in business acquisitions**:  
  \((-928,813)\)  
  \((-631,803)\)

- **Increase (decrease) in restricted deposits**:  
  \(45\)  
  \((14,886)\)

- **Purchases of property and equipment, net of property and equipment received in business acquisitions**:  
  \((-62,715)\)  
  \((-47,911)\)

- **Other**:  
  \(1,460\)  
  \(943\)

**Net cash used in investing activities**  
\((-469,387)\)  
\((-1,752,682)\)

**CASH FLOWS FROM FINANCING ACTIVITIES:**

- **Net increase in banking deposits**:  
  \(1,112,421\)  
  \(578,728\)

- **Advances from the Federal Home Loan Bank of Atlanta**:  
  \(1,489,000\)  
  \(1,173,000\)

- **Payments on advances from the Federal Home Loan Bank of Atlanta**:  
  \((2,039,000)\)  
  \((668,000)\)

- **Net increase (decrease) in securities sold under agreements to repurchase**:  
  \((-45,927)\)  
  \(305,931\)

- **Net proceeds from convertible subordinated notes**:  
  \(-\)  
  \(631,312\)

- **Repayments on loans to related parties, net of loans issued**:  
  \(2,899\)  
  \(-\)

- **Proceeds from issuance of common stock from associate stock transactions**:  
  \(10,806\)  
  \(21,238\)

- **Proceeds from bank loans and lines of credit, net of transaction costs**:  
  \(2,172\)  
  \(75,000\)

- **Payments on bank loans and lines of credit**:  
  \((23,626)\)  
  \((150,589)\)

- **Repayment of capital lease obligations**:  
  \(34\)  
  \(1,134\)

**Net cash provided by financing activities**  
\(505,597\)  
\(1,965,717\)

**INCREASE (DECREASE) IN CASH AND EQUIVALENTS**  
\((-56,336)\)  
\(70,805\)

**CASH AND EQUIVALENTS—Beginning of period**  
\(212,430\)  
\(326,227\)

**CASH AND EQUIVALENTS—End of period**  
\($156,094\)  
\($397,032\)

**SUPPLEMENTAL DISCLOSURES:**

- **Non-cash investing and financing activities:**
  - **Unrealized loss on available-for-sale securities**:  
    \$ (73,614)  
    \$ (139,844)
  - **Tax benefit on exercise of stock options**:  
    \$ 3,029  
    \$ 3,385
  - **Tax effect of gain on available-for-sale securities**:  
    \$ (2,863)  
    \$ —
  - **Transfer of loans to REO**:  
    \$ (480)  
    \$ —
  - **Assets acquired under capital lease obligations**:  
    \$ 1,339  
    \$ —
  - **Change in financial derivatives recorded at fair market value**:  
    \$ (83,495)  
    \$ —
  - **Deferred stock compensation**:  
    \$ 14,510  
    \$ —
  - **Purchase acquisitions, net of cash acquired**:  
    - **Common stock issued and stock options assumed**:  
      \$ 52,008  
      \$ —
    - **Cash paid, less acquired (including acquisition costs)**:  
      \$ 1,521  
      \$ —
    - **Liabilities assumed**:  
      \$ 10  
      \$ —
    - **Reduction in payable for purchase of international subsidiary**:  
      \$ (12,341)  
      \$ —
    - **Carrying value of joint-venture investment**:  
      \$ 1,258  
      \$ —
    - **Fair value of assets acquired (including goodwill of $38,452 and $0)**:  
      \$ 42,456  
      \$ —

**See notes to condensed consolidated financial statements.**

**Notes to Condensed Consolidated Financial Statements**

**Note 1. Organization and Basis of Presentation**
The accompanying unaudited condensed consolidated financial statements include E*TRADE Group, Inc., referred to in this Form 10-Q as the Parent, a financial services holding company, and its subsidiaries, collectively referred to in this Form 10-Q as the Company or E*TRADE, including but not limited to E*TRADE Securities, Incorporated, referred to in this Form 10-Q as E*TRADE Securities, a securities broker-dealer, TIR (Holdings) Limited, referred to in this Form 10-Q as TIR, a provider of global securities brokerage and other related services to institutional clients, and E*TRADE Financial Corporation, referred to in this Form 10-Q as ETC, a provider of financial services whose primary business is conducted by E*TRADE Bank, referred to in this Form 10-Q as the Bank, a federally chartered savings bank that provides deposit accounts insured by the Federal Deposit Insurance Corporation, commonly referred to as the FDIC, to customers nationwide.

On January 22, 2001, the Company changed its fiscal year end from September 30 to December 31.

The unaudited condensed consolidated financial statements of the Company include the accounts of the Parent and its majority owned subsidiaries. Intercompany accounts and transactions are eliminated in consolidation. Affiliates in which there is at least a 20% ownership or in which there are other indicators of significant influence are generally accounted for by the equity method; those in which there is a less than 20% ownership are generally carried at cost.

These unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission, commonly referred to as the SEC, and, in the opinion of management, reflects adjustments consisting only of normal recurring adjustments necessary to present fairly the financial position, results of operations and cash flows for the periods presented in conformity with accounting principles generally accepted in the United States of America. These unaudited condensed consolidated financial statements should be read in conjunction with the audited annual consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended September 30, 2000.

Certain prior period items in these unaudited condensed consolidated financial statements have been reclassified to conform to the current period presentation.

NOTE 2.  BUSINESS COMBINATIONS

On February 1, 2001, the Company acquired LoansDirect, Inc., referred to in this Form 10-Q as LoansDirect, an online mortgage originator for an aggregate purchase price of approximately $36.0 million, comprised of approximately 3.0 million shares of the Company’s common stock valued at $33.0 million, the assumption of vested employee stock options of approximately $1.5 million, and acquisition costs of approximately $1.5 million. Through the acquisition of LoansDirect, the Company expects to gain strategic inroads into the consumer lending market, advancing its diversified online financial services model. The acquisition was accounted for using the purchase method of accounting, and the results of LoansDirect’s operations have been combined with those of the Company since the date of acquisition. The purchase price exceeded the fair value of the assets acquired by approximately $32.0 million, which was recorded as goodwill to be amortized over 15 years. The purchase price allocation at March 31, 2001 is preliminary and has been allocated based on the estimated fair value of net tangible and intangible assets acquired. Prior period results for LoansDirect were not material.

In October 2000, the Company completed the acquisition of PrivateAccounts, Inc., renamed E*TRADE Advisory Services, Inc. on March 26, 2001, and referred to in this Form 10-Q as E*TRADE Advisory Services, a Minneapolis-based developer of online separately managed accounts. The Company issued 618,057 shares of common stock valued at approximately $8.7 million in exchange for 100% of the outstanding shares of E*TRADE Advisory Services. The Company also issued an equal number of shares to be held in escrow until the completion of product and asset target milestones, whereby the Company would be required to issue up to an additional $31.0 million of the Company’s common stock and, if necessary, cash consideration as incentive consideration. In March 2001, E*TRADE Advisory Services achieved a product development milestone, resulting in the release of approximately 479,000 shares valued at approximately $4.3 million from escrow. The acquisition was accounted for using the purchase method of accounting, and the results of E*TRADE Advisory Services’ operations have been combined with those of the Company since the date of acquisition. The purchase price allocation at March 31, 2001 is preliminary and has been allocated based on the estimated fair value of net tangible and intangible assets acquired. Prior period results for E*TRADE Advisory Services were not material.

In October 1999, the Company entered into a joint venture agreement with Berliner Effektenbank AG and New York Broker Deutschland AG to form E*TRADE Germany AG, referred to in this Form 10-Q as E*TRADE Germany. The Company had a 60% ownership interest in this joint venture at September 30, 2000. The Company entered into an agreement to acquire the remaining 40% ownership interest in E*TRADE Germany for approximately 24.0 million Euros (approximately $20.2 million as of October 16, 2000, the closing date of the transaction). The additional investment was comprised of approximately $1.4 million in cash (paid in October 2000), 1.0 million shares of the Company’s common stock valued at approximately $6.6 million (paid in January 2001), and 9.8 million Euros (approximately $8.2 million as of October 16, 2000, the closing date of the transaction) payable in cash or shares of the Company’s common stock before the end of calendar year 2001. The purchase price exceeded the fair value of the assets acquired by $19.4 million, which was recorded as goodwill to be amortized over 20 years. The acquisition was accounted for using the purchase method of accounting, and the results of E*TRADE Germany’s operations have been combined with those of the Company since the date of the acquisition. The purchase price allocation at March 31, 2001 is preliminary and has been allocated based on the estimated fair value of net tangible assets acquired. Prior period results for E*TRADE Germany were not material.

NOTE 3.  SALE OF INTERNATIONAL SUBSIDIARY

In November 2000, the Company sold its ownership interest in E*TRADE @ Net Bourse S.A. for approximately 80.5 million Euros (approximately $68.0 million as of November 2000). Of this amount, approximately 8.2 million Euros (approximately $7.0 million as of November 2000) will be held in escrow for two years, of which 50% may be released after one year. In conjunction with this transaction, the Company reacquired its licensing rights to France, as well as the ownership interests in E*TRADE SARL, E*TRADE Italy and E*TRADE Benelux, previously held by E*TRADE @ Net Bourse S.A. No gain or loss resulted from this transaction.

NOTE 4.  BROKERAGE RECEIVABLES—NET AND PAYABLES

Brokerage receivables—net and payables consist of the following (in thousands):

NOTE 5.  INTEREST EARNED

The interest earned on cash and short-term investments is summarized as follows (in thousands):

NOTE 6.  LOANS

Includes the following information (in thousands):

NOTE 7.  INCOME TAXES

The Company’s effective tax rate for the periods presented was impacted by an increase in the Company’s non-U.S. tax rate, as well as the increased use of tax credits in the first quarter of 2001.

The Company has three domestic indefinite-life intangible assets, acquired primarily in connection with the LoansDirect and PrivateAccounts acquisitions: (i) customer lists, customer relationships, and software; (ii) goodwill; and (iii) an intangible asset related to the addition of a separately managed account platform. The carrying amount of these indefinite-life intangible assets was approximately $6.3 million at December 31, 2000, $15.2 million at March 31, 2001, and $31.8 million at September 30, 2001.

NOTE 13.  DISCONTINUED OPERATIONS

Certain prior period items in these unaudited condensed consolidated financial statements have been reclassified to conform to the current period presentation.

NOTE 14.  SUBSEQUENT EVENTS

As of the date of this Form 10-Q, the Company had the right to issue up to an additional $31.0 million of the Company’s common stock and, if necessary, cash consideration as incentive consideration. In addition, the Company had the right to issue 1.0 million additional shares of common stock as incentive consideration if the E*TRADE Germany operations met certain milestones.

The information contained in this Form 10-Q should be read in conjunction with the Company’s Annual Report on Form 10-K for the fiscal year ended September 30, 2000.
NOTE 5. INVESTMENTS

Investments are comprised of trading and available-for-sale debt and equity securities, as defined under the provisions of Statement of Financial Accounting Standard, referred to in this Form 10-Q as SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities. Also included in investments are investments in entities in which the Company owns between 20% and 50% or has the ability to exercise significant influence, which are accounted for under the equity method, as well as some investments accounted for under the cost method.

The carrying amounts of investments are shown below (in thousands):

<table>
<thead>
<tr>
<th>March 31, 2001</th>
<th>September 30, 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trading securities</td>
<td>$1,935</td>
</tr>
<tr>
<td>Available-for-sale investment securities(1)</td>
<td>1,537,421</td>
</tr>
<tr>
<td>Equity method and other investments:</td>
<td></td>
</tr>
<tr>
<td>Joint ventures</td>
<td>36,764</td>
</tr>
<tr>
<td>Venture capital funds</td>
<td>36,331</td>
</tr>
<tr>
<td>Wit Soundview</td>
<td>41,690</td>
</tr>
<tr>
<td>Archipelago</td>
<td>25,274</td>
</tr>
<tr>
<td>Other investments</td>
<td>42,915</td>
</tr>
<tr>
<td>Total investments</td>
<td>$1,722,330</td>
</tr>
</tbody>
</table>


Wit Soundview

At September 30, 2000 E*TRADE owned a 23.6% investment in E*OFFERING Corp., referred to in this Form 10-Q as E*OFFERING, a full service, Internet-based investment bank. On October 16, 2000, Wit Soundview Group, Inc., referred to in this Form 10-Q as Wit completed the acquisition of E*OFFERING. Under the terms of the agreement, the Company received approximately 5,324,000 shares of Wit common stock and warrants to purchase 534,705 and 1,821,936 shares of Wit common stock exercisable for $5.99 and $0.60 per share, respectively, exercisable immediately and expiring in February 2001 and January 2005, respectively, as well as the right to name one representative to Wit’s Board of Directors. The warrants to purchase 534,705 shares of Wit common stock expired unexercised in February 2001. Concurrently with this agreement, the Company and Wit entered into certain other collateral arrangements whereby the Company acquired Wit’s retail brokerage business and received 4,025,948 shares of Wit common stock and a warrant to purchase up to 2,000,000 shares of Wit common stock for $10.25 per share, as consideration for the Company entering into a strategic alliance agreement pursuant to which Wit is the exclusive source of initial public offerings, follow-on offerings, and other investment banking products to the Company for a five year term. The warrants are exercisable if the exclusivity provisions of the strategic alliance agreement have remained in effect during the fourth and fifth years of the agreement. If, following a change of control of the Company while the exclusivity provisions are still in effect, the Company or its successor breaches the strategic alliance agreement or the acquirer fails to acknowledge that it will cause the Company to honor the exclusivity provisions thereunder, the Company will be obligated to pay Wit $120 million less $3.33 million for each calendar month since October 2000, but in no event less than $80 million. If the Company received, in the change of control transaction, fully registered and freely marketable common or preferred stock, the Company may at its option make the payment in such securities instead of cash, applying the same valuation principles as in the change of control transaction. If the Company makes such election Wit may then elect to receive a number of shares of Wit common stock held by the Company equal in value to the payment due provided that each share of Wit common stock be valued at not less than $10.25. In addition, any shares of Wit common stock still in escrow under the terms...
of the merger would be transferred to Wit. Wit would also continue, for two years after the change of control, to have the right to provide securities to the Company’s retail customers on a non-exclusive basis but the exclusivity provisions would no longer be effective. In a related transaction the Company also purchased 2,000,000 shares of Wit common stock for $20.5 million in cash. The Company subsequently purchased 300,000 shares of Wit common stock for approximately $1.9 million on the open market. As a result of these transactions, the Company holds an approximate 10% ownership interest in Wit, excluding the warrants held, and accounts for its investment under the equity method.

**Publicly-Traded Equity Securities**

Included in available-for-sale securities are investments in several companies that are publicly-traded and carried at fair value. Unrealized gains related to these investments were $13,000 and $186,3 million at March 31, 2001 and September 30, 2000, respectively. Unrealized losses related to these investments were $11.6 million and $2.8 million at March 31, 2001 and September 30, 2000, respectively.

**Other Investments**

The Company has also made investments in non-public, venture capital-backed high technology companies with which it does business and which provide Internet-based services, as well as venture capital funds. These investments represent less than 20% of the outstanding shares of these companies and are accounted for under the cost method.

### NOTE 6. RELATED PARTY TRANSACTIONS

**Related Party Loans**

In March 2001, the Company made a loan to an executive officer of the Company in the aggregate principal amount of $0.1 million. The loan accrues interest at a rate of 4.68% annually. Accrued interest on the loan is due to be paid in March 2002, and the remaining interest and principal is due in March 2003. The loan is collateralized by shares of the Company’s common stock currently held in the name of the officer.

In February 2001, an executive officer of the Company repaid $2.9 million of his relocation loan. The remainder of the loan of $1.3 million, due in May 2005, is collateralized by shares of the Company’s common stock currently held in the name of the officer.

In November and December 2000, the Company made loans to two executive officers and a director of the Company in the aggregate principal amount of $30.5 million. The loans accrue interest at rates of between 6.09% and 6.10% annually. The principal amounts of $0.5 million, $15.0 million, and $15.0 million are due in December 2002, November 2005, and November 2010, respectively. One of the $15.0 million loans is collateralized by real property owned by an executive officer. The other $15.0 million loan is collateralized by equity interests in various limited liability companies and real property owned by a director.

Related party loans receivable are recorded in other assets ($38.3 million at March 31, 2001).

**Other**

In January 2001, a wholly owned subsidiary of the Company purchased residential property from a related party of the Company for a total purchase price of approximately $1.7 million paid in cash.

During fiscal 2000, a wholly-owned subsidiary of the Company purchased residential properties that it leases to certain of its executive officers with options to buy. Rental income in the quarter ended March 31, 2001 related to these properties was approximately $41,000. Rental income is recorded in other income.

See Note 8 for additional related party transactions.

### NOTE 7. LINE OF CREDIT AND OTHER BORROWINGS

In March 2001, the Company obtained a $2.0 million term loan from a financial institution due in twenty-four equal monthly installments commencing on May 1, 2001 that expires in April 2003. The term loan is collateralized by assets owned by the Company. Borrowings under the loan bear interest at 3.00% above LIBOR (total of 8.08% at March 31, 2001). The Company had approximately $2.0 million outstanding under this term loan at March 31, 2001, which is included in accounts payable, accrued and other liabilities.

In December 2000, the Company obtained two term loans from financial institutions that expire in March 31, 2001. The Company had $16.7 million outstanding under these term loans at March 31, 2001, which is included in accounts payable, accrued and other liabilities.

In November 2000, the Company renewed a $50 million line of credit under an agreement with a bank that expires in November 2001. The line of credit is collateralized by investment securities that are owned by the Company. Borrowings under the line of credit bear interest at 0.35% above LIBOR (total of 5.43% at March 31, 2001). The Company had no borrowings outstanding under this line of credit at March 31, 2001.

### NOTE 8. SHAREOWNERS’ EQUITY

**Shareowners’ Notes Receivable**

In December 2000, the Company made a full recourse loan to one of its executive officers for approximately $0.5 million. The proceeds from this loan were used to fund the purchase of shares of the Company’s common stock for the exercise and hold of stock options. The loan accrues interest at the rate of 6.15% per annum. The interest on the loan is due in December 2001 with all remaining unpaid interest due upon the payment of the principal in January 2002.
Deferred Stock Compensation

In January 2001, in connection with the issuance of restricted common stock to certain executive officers, the Company recorded deferred stock compensation of $14.5 million, the fair market value of the shares on the date of grant. This amount is being amortized to expense ratably over the period in which restrictions are removed on the related shares of restricted common stock, generally four years. Amortization of deferred stock compensation for the three months ended March 31, 2001 was $1.4 million.

NOTE 9. ASSOCIATE BENEFIT PLAN

Effective January 1, 2001, the Company’s Board of Directors adopted a Supplemental Executive Retirement Plan, referred to in this Form 10-Q as the SERP, for certain executive officers. The purpose of the SERP is to attract, retain and motivate certain executive officers of the Company who provide valuable services to the Company and to provide those officers with flexibility to meet their retirement and estate planning needs. Funding of the SERP by the Company is discretionary. Contributions to the SERP, if any, are due at the beginning of each calendar year and are deposited into a Rabbi Trust, to which the Company retains ownership until participant benefits vest and are distributed. To receive full benefits accrued under the SERP, at the time of retirement a participating individual must have fifteen years of participation in the plan. With the exception of the Company’s Chief Executive Officer, whose benefits vest immediately, no portion of a participant’s benefits will become vested unless the individual has participated in the plan for at least five years. Fifty percent of participation benefits vest after five years of participation in the SERP with the remaining benefits vesting over the next five years of participation. In January 2001, the Company contributed $12.1 million to fund its SERP obligations and will recognize related compensation expense during the three months ended March 31, 2001.

NOTE 10. COMPREHENSIVE LOSS

The reconciliation of net loss to comprehensive loss is as follows (in thousands):

<table>
<thead>
<tr>
<th>Three Months Ended March 31,</th>
<th>2001</th>
<th>2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net loss</td>
<td>$(9,203)</td>
<td>$(25,466)</td>
</tr>
<tr>
<td>Changes in other comprehensive loss:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unrealized loss on available-for-sale securities, net of tax</td>
<td>$(27,447)</td>
<td>$(81,030)</td>
</tr>
<tr>
<td>Unrealized loss on derivative instruments, net of tax (see Note 16)</td>
<td>$(49,548)</td>
<td>—</td>
</tr>
<tr>
<td>Cumulative translation adjustments</td>
<td>$(4,298)</td>
<td>$(1,455)</td>
</tr>
<tr>
<td>Total comprehensive loss</td>
<td>$(90,496)</td>
<td>$(107,951)</td>
</tr>
</tbody>
</table>

NOTE 11. NET LOSS PER SHARE

The following table sets forth the computation of the numerator and denominator used in the computation of basic and diluted net loss per share (in thousands):

<table>
<thead>
<tr>
<th>Three Months Ended March 31,</th>
<th>2001</th>
<th>2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic and diluted</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Numerator:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loss before extraordinary loss on early extinguishment of debt</td>
<td>$(7,166)</td>
<td>$(25,466)</td>
</tr>
<tr>
<td>Extraordinary loss on early extinguishment of debt, net of tax</td>
<td>(2,037)</td>
<td>—</td>
</tr>
<tr>
<td>Net loss</td>
<td>$(9,203)</td>
<td>$(25,466)</td>
</tr>
<tr>
<td>Denominator:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Weighted average shares outstanding</td>
<td>317,242</td>
<td>298,026</td>
</tr>
</tbody>
</table>

Because the Company reported a net loss for the three months ended March 31, 2001 and 2000, the calculation of diluted net loss per share does not include common stock equivalents as they are anti-dilutive and would result in a reduction of net loss per share. If the Company had reported net income for the three months ended March 31, 2001 and 2000, there would have been 10,294,000 and 18,103,000 additional shares for options outstanding, respectively, and 198,000 and 1,182,000 additional shares for warrants outstanding, respectively. Excluded from the calculation of diluted net loss per share for the three months ended March 31, 2001 and 2000 are approximately 27,542,000 and 13,317,000, respectively, shares of common stock issuable under convertible subordinated notes as the effect of applying the treasury stock method on an as-if-converted basis would be anti-dilutive in the calculation of diluted net loss per share.

The following options to purchase shares of common stock have not been included in the computation of diluted net loss per share because the options’ exercise price was greater than the average market price of the Company’s common stock for the periods stated, and therefore, the effect would be anti-dilutive (in thousands, except exercise price data):

<table>
<thead>
<tr>
<th>Three Months Ended March 31,</th>
</tr>
</thead>
</table>
Options excluded from computation of diluted net loss per share

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>$ 58.19</td>
<td>$ 58.75</td>
</tr>
<tr>
<td>Low</td>
<td>$ 10.53</td>
<td>$ 25.16</td>
</tr>
</tbody>
</table>

NOTE 12. EXTRAORDINARY LOSS ON EARLY EXTINGUISHMENT OF DEBT

Extraordinary loss on early extinguishment of debt was $2.0 million (net of tax benefits of $1.2 million) for the three months ended March 31, 2001 and was recorded as a result of the early redemption of $400 million of adjustable and fixed rate advances with the Federal Home Loan Bank of Atlanta, referred to in this Form 10-Q as the FHLB. The FHLB advances were entered into as a result of normal funding requirements of the Company’s banking operations. The loss consisted primarily of a prepayment penalty and costs associated with the early redemption.

NOTE 13. REGULATORY REQUIREMENTS

E*TRADE Securities is subject to the Uniform Net Capital Rule, referred to in this Form 10-Q as the Rule under the Securities Exchange Act of 1934 administered by the SEC and the National Association of Securities Dealers Regulation, Inc., commonly referred to as the NASD, which requires the maintenance of minimum net capital. E*TRADE Securities has elected to use the alternative method permitted by the Rule, which requires that E*TRADE Securities maintain minimum net capital equal to the greater of $250,000 or two percent of aggregate debit balances arising from customer transactions, as defined. E*TRADE Securities had amounts in relation to the Rule as follows (in thousands, except percentage data):

<table>
<thead>
<tr>
<th>March 31, 2001</th>
<th>September 30, 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net capital</td>
<td>$414,103</td>
</tr>
<tr>
<td>Percentage of aggregate debit balances</td>
<td>17.2%</td>
</tr>
<tr>
<td>Required net capital</td>
<td>$ 48,123</td>
</tr>
<tr>
<td>Excess net capital</td>
<td>$365,980</td>
</tr>
<tr>
<td>Net capital</td>
<td>$479,036</td>
</tr>
<tr>
<td>Percentage of aggregate debit balances</td>
<td>9.2%</td>
</tr>
<tr>
<td>Required net capital</td>
<td>$103,747</td>
</tr>
<tr>
<td>Excess net capital</td>
<td>$375,289</td>
</tr>
</tbody>
</table>

Under the alternative method, a broker-dealer may not repay subordinated borrowings, pay cash dividends or make any unsecured advances or loans to its parent or employees if such payment would result in net capital of less than 5% of aggregate debit balances or less than 120% of its minimum dollar amount requirement.

The table below summarizes the minimum excess capital requirements for the Company’s other U.S. broker-dealer subsidiaries (in thousands):

<table>
<thead>
<tr>
<th>March 31, 2001</th>
<th>September 30, 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Required Net Capital</td>
<td>Net Capital</td>
</tr>
<tr>
<td>-------------------</td>
<td>--------------</td>
</tr>
<tr>
<td>E*TRADE Institutional Securities, Inc.</td>
<td>$250</td>
</tr>
<tr>
<td>E*TRADE Investor Select, Inc.</td>
<td>$ 5</td>
</tr>
<tr>
<td>Marquette Securities, Inc.</td>
<td>$250</td>
</tr>
<tr>
<td>E*TRADE Capital Markets, Inc.</td>
<td>$174</td>
</tr>
<tr>
<td>E*TRADE Canada Securities Corporation</td>
<td>$ 56</td>
</tr>
</tbody>
</table>

The Company’s broker-dealer subsidiaries located in Canada, South Africa, Australia, Europe, and South East Asia, have various and differing capital requirements, all of which were met at March 31, 2001 and September 30, 2000. The aggregate net capital, required net capital, and excess net capital of these companies at March 31, 2001, was $66.4 million, $29.8 million, and $36.6 million, respectively. The aggregate net capital, required net capital, and excess net capital of these companies at September 30, 2000, was $48.4 million, $18.5 million, and $29.9 million, respectively.

The Bank is also subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory—and possibly additional discretionary—actions by regulators that, if undertaken, could have a direct material effect on the Bank’s financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank’s assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank’s capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of total and Tier I capital to risk-weighted assets and of Tier I capital to average assets. Management believes that, as of March 31, 2001 the Bank has met all capital adequacy requirements to which it was subject. As of March 31, 2001 and September 30, 2000, the Office of Thrift Supervision, commonly referred to as the OTS categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the institution’s category.

The Bank’s required and actual capital amounts and ratios are presented in the table below (dollars in thousands):

<table>
<thead>
<tr>
<th>Amount</th>
<th>Ratio</th>
<th>Amount</th>
<th>Ratio</th>
<th>Amount</th>
<th>Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Core Capital (to adjusted tangible assets)</td>
<td>$682,943</td>
<td>5.66%</td>
<td>$482,993</td>
<td>4.0%</td>
<td>$603,741</td>
</tr>
</tbody>
</table>

As of March 31, 2001:
As of September 30, 2000:

| Core Capital (to adjusted tangible assets) | $582,058 | 6.5% | $>359,874 | 4.0% | $>449,843 | 5.0% |
| Tangible Capital (to tangible assets) | $582,058 | 6.5% | $>134,953 | 1.5% | N/A | N/A |
| Tier I Capital (to risk weighted assets) | $582,058 | 16.8% | N/A | N/A | $>207,890 | 6.0% |
| Total Capital (to risk weighted assets) | $592,597 | 17.1% | $>277,186 | 8.0% | $>346,483 | 10.0% |

NOTE 15. SEGMENT INFORMATION

Segment Information

The Company has separated its financial services into four categories: domestic retail brokerage, banking, global and institutional, and asset gathering and other. During the quarter ended March 31, 2001, the banking segment was expanded to include the operations of LoansDirect (see Note 2). There have been no other changes to these categories from fiscal 2000. As the asset gathering and other operations business represents emerging activities which are not material to the consolidated results for segment reporting purposes, management has aggregated asset gathering and other with domestic retail brokerage to form one of three reportable segments, with banking and global and institutional comprising the other two segments currently considered by management when it evaluates Company performance.

Financial information for the Company’s reportable segments is presented in the table below, and the totals are equal to the Company’s consolidated amounts as reported in the unaudited condensed consolidated financial statements (in thousands):

<table>
<thead>
<tr>
<th>Domestic Retail Brokerage &amp; Other</th>
<th>Banking</th>
<th>Global and Institutional</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Three Months Ended March 31, 2001:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest income-net of interest expense</td>
<td>$ 59,648</td>
<td>$ 36,319</td>
<td>$ 2,362</td>
</tr>
<tr>
<td>Non-interest revenue-net of provision for loan losses</td>
<td>158,694</td>
<td>35,294</td>
<td>37,264</td>
</tr>
<tr>
<td>Net revenues</td>
<td>$ 218,342</td>
<td>$ 71,613</td>
<td>$ 39,626</td>
</tr>
</tbody>
</table>
### Operating Income (Loss)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Income (Loss)</td>
<td>$(8,181)</td>
</tr>
<tr>
<td>Three Months Ended March 31, 2000:</td>
<td></td>
</tr>
<tr>
<td>Interest income-net of interest expense</td>
<td>$66,385</td>
</tr>
<tr>
<td>Non-interest revenue-net of provision for loan losses</td>
<td>$269,080</td>
</tr>
<tr>
<td>Net revenues</td>
<td>$335,465</td>
</tr>
<tr>
<td>Operating loss</td>
<td>$(16,029)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Date</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>As of March 31, 2001:</td>
<td></td>
</tr>
<tr>
<td>Segment assets</td>
<td>$5,916,185</td>
</tr>
<tr>
<td>As of September 30, 2000:</td>
<td></td>
</tr>
<tr>
<td>Segment assets</td>
<td>$7,805,843</td>
</tr>
</tbody>
</table>

No single customer accounted for greater than 10% of total revenues in the three months ended March 31, 2001 or 2000, respectively.

### NOTE 16. ADOPTION OF NEW ACCOUNTING STANDARD

Effective October 1, 2000, the Company adopted SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. All derivatives, whether designated anew or in hedging relationships on October 1, 2000 or not, are required to be recorded on the balance sheet at fair value. If the derivative is designated as a fair value hedge, the changes in the fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in earnings. If the derivative is designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in other comprehensive income, referred to in this Form 10-Q as “OCI” and are recognized in the income statement when the hedged item affects earnings. Ineffective portions of changes in the fair value of cash flow hedges are recognized in earnings.

### Interest Rate Risk

The Company uses derivatives to provide a cost- and capital-efficient way to manage the interest rate risk exposure of the Company by synthetically modifying the repricing or maturity characteristics of certain assets and liabilities and by locking in the rates of certain forecasted issuances of debt. The primary derivative instruments used include interest rate swaps, caps, and floors. The Company enters into interest rate swap agreements to assume fixed-rate interest payments in exchange for variable market-indexed interest payments. Depending on the hedge relationship, the effects of these agreements are to (a) convert adjustable rate liabilities to longer-term fixed rate liabilities, (b) convert long-term fixed rate assets to shorter-term adjustable rate assets or (c) reduce the variability of future changes in interest rates on forecasted issuances of debt. The net payments of these agreements are charged to either interest expense or interest income, depending on whether the agreement is designated as an existing or forecasted liability or asset.

### Fair Value Hedges

The Company uses a combination of interest rate swaps, caps and floors to substantially offset the change in value of certain fixed rate assets. In calculating the effective portion of the fair value hedges under SFAS No. 133, the change in the fair value of the hedge agreement is recognized currently in earnings, as is the change in value of the hedged item. Accordingly, the net difference or hedge ineffectiveness, if any, is recognized currently in non-operating income (expense), included in fair value adjustments of financial derivatives. Fair value hedge ineffectiveness resulted in a gain of $1.5 million for the three months ended March 31, 2001.

Five fair value hedges were derecognized and therefore hedge accounting was discontinued during the period. Changes in the fair value of these derivative instruments after the discontinuance of fair value hedge accounting are recorded in other revenue in the consolidated statement of operations, which totaled $1.4 million of losses for the three months ended March 31, 2001. In addition, the Company recognized $0.4 million of hedge ineffectiveness expense in fair value adjustments of financial derivatives included in non-operating expense for the period in which these hedge relationships were accounted for as fair value hedges.

### Cash Flow Hedges

**Variable Rate Debt and Forecasted Issuances of Debt**

The Company also uses interest rate swaps to hedge the variability of future cash flows associated with existing variable rate debt and forecasted issuances of debt. In respect to the variable rate debt currently on the balance sheet, the Company uses interest rate swaps to hedge the risk of changes in the benchmark rate (LIBOR), which impacts the amount of future payments to be made on the variable rate debt. In relation to the hedging of the forecasted issuance of debt, the Company utilizes interest rate swaps with a longer maturity than the underlying variable rate debt. The use of an interest rate swap contract that is longer than the underlying debt allows the Company to hedge both the risk of changes in the benchmark rate (LIBOR) and the replacement of such debt upon maturity. These cash flow hedge relationships will be treated as effective hedges as long as the future issuances of debt remain probable and the cash flow hedge continues to meet the requirements of SFAS No. 133. The Company expects to hedge the forecasted issuance of debt over a maximum term of 7 years.

During the three months ended March 31, 2001 the Company reclassified $1.5 million of derivative losses from OCI to realized gain (loss) on trading activity recorded in other revenue in the consolidated statement of operations for forecasted transactions that had become probable of not occurring.

The Company measures ineffectiveness for these cash flow hedges in accordance with SFAS No. 133. The ineffectiveness for the three months ended March 31, 2001 had no material impact on earnings.

In accordance with the Company’s SFAS No. 133 accounting policy, the fair value of all interest rate swap agreements in cash flow hedge relationships are recorded at fair value on the balance sheet. OCI is adjusted to the balance that reflects the effective portion of the change in the fair value of the
derivative, net of tax. Gains or losses recorded in OCI are recognized in the income statement as the hedged item affects earnings.

Forward Commitments

The Company also uses forward commitments as cash flow hedges of the forecasted purchases or sales of securities. The Company measures ineffectiveness in accordance with the provisions of SFAS No. 133. For the three months ended March 2001, there was no significant ineffectiveness for these forward commitments. The effective portion of the change in fair value of these forward commitments is recorded in OCI, net of tax. The amounts recorded to OCI will be recognized in the statement of operations as the hedged forecasted transaction affects earnings.

Foreign Currency Risk

Certain forecasted revenues and expenses are exposed to foreign currency risk. The Company’s objective in hedging anticipated transactions is to mitigate the variability of operating and cash results from fluctuations in currency rates; hedging strategies are not speculative in nature. The Company primarily hedges against fluctuations in the foreign exchange rates of material, anticipated revenues/expenses of TIR which are denominated in non-functional currencies, typically the Japanese yen, the Euro, and the British pound. As the functional currency of TIR is the U.S. dollar and as TIR maintains customer accounts in over thirty currencies, current risk management policies allow authorized persons to enter into forward contracts and purchase options to hedge between 0-100% of exposures deemed material. Material exposures are assessed on the basis of cash flow projections prepared by TIR.

TIR uses forward contracts and purchase options to hedge a portion of forecasted revenue denominated in non-functional currencies for up to one year in the future. Forward contracts and purchase options are designated as cash flow hedging instruments.

In calculating the ineffective portion of the Company’s hedge performance under SFAS No. 133, the Company excludes the time value component related to any option premiums paid and discounts or premiums on forward contracts and recognizes the amount in other income during the life of the contract. These amounts have not been material in the three months ended March 31, 2001. Hedge ineffectiveness related to the Company’s foreign currency hedge instruments, determined in accordance with SFAS No.133, had no impact on earnings for the three months ended March 31, 2001. No foreign exchange cash flow hedges were derecognized or discontinued for the three months ended March 31, 2001.

Derivative gains and losses included in OCI are reclassified into global and institutional revenues at the time forecasted revenue is recognized. During the three months ended March 31, 2001, TIR settled all remaining forward contracts and purchase options, recognizing $402,000 in revenues, including $163,000 which was reclassified from OCI. TIR has resumed its hedging activities during the month of April 2001.

Other Derivatives

The Company owns warrants to purchase shares of common stock of Wit (see Note 5). The adjustment to the fair value of these warrants of $1.1 million is reflected in non-operating income at March 31, 2001. The Company also holds 2.0 million unvested warrants to purchase shares of common stock of Wit received in connection with a strategic alliance agreement. Because vesting of these warrants is subject to future performance, their value will not be recognized until such criteria are met.

The Company engages in originating and selling mortgage loans as part of its mortgage banking business. As a result of mortgage banking activities, the Company records two different derivatives, Interest Rate Lock Commitments for mortgage loans that will be held for resale, commonly referred to as IRLCs, and forward sale agreements. Both the IRLCs and forward sale agreements are recorded on the balance sheet at fair value. Changes in the fair value of these derivatives are shown in the statement of operations as gains (losses) on loans held for sale, recorded in other revenue. Changes in the fair value of IRLCs resulted in income of $1.0 million for the three months ended March 31, 2001. Changes in the fair value of forward sales agreements resulted in a loss of $1.0 million for the three months ended March 31, 2001.

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

Forward-Looking Statements

Statements in this document, other than statements of historical information, are forward-looking statements that are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements, as well as other oral and written forward-looking statements made by us or on our behalf from time to time, including statements contained in our filings with the Securities and Exchange Commission, commonly referred to as the SEC, and our reports to shareowners, involve known and unknown risks and other factors which may cause our actual results to differ materially from those expressed in any forward-looking statements. Any such statement is qualified by reference to the risks and factors discussed below under the headings “Liquidity and Capital Resources” and “Risk Factors,” as well as in our filings with the SEC, which are available from the SEC or which you may request from us.

We caution that the risks and factors discussed below and in such filings are not exclusive. We do not undertake to update any forward-looking statement that may be made from time to time by or on behalf of E*TRADE. You are urged to carefully review and consider the various disclosures in this report and in our other reports filed with the SEC, including our Annual Report on Form 10-K/A as filed with the SEC on November 22, 2000, that attempt to advise you of certain risks and factors that may affect our business. You are cautioned not to place undue reliance on these forward-looking statements to reflect events or circumstances occurring after the date hereof. The following should be read in conjunction with our consolidated financial statements and notes to these consolidated financial statements.

Results of Operations

Key Performance Indicators

The following table sets forth several key performance indicators which management utilizes in measuring our performance and in explaining the results of our operations for the comparative three months presented (dollars in thousands except cost per new account, average commission per domestic brokerage transaction and rebates per domestic brokerage transaction):

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Three Months Ended March 31,</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The table above provides a summary of key performance indicators for the three months ended March 31, 2001, compared to the same period in 2000.
The following table sets forth the components of both gross and net revenues and percentage change information related to certain items on our Consolidated Statements of Operations for the periods indicated (dollars in thousands):

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2000</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Active domestic brokerage accounts</strong></td>
<td>3,223,404</td>
<td>2,423,076</td>
<td>33 %</td>
</tr>
<tr>
<td><strong>Active banking accounts</strong></td>
<td>404,765</td>
<td>170,584</td>
<td>137 %</td>
</tr>
<tr>
<td><strong>Active global and institutional accounts</strong></td>
<td>96,952</td>
<td>50,925</td>
<td>90 %</td>
</tr>
<tr>
<td><strong>Total active accounts at period end</strong></td>
<td>3,725,121</td>
<td>2,644,585</td>
<td>41 %</td>
</tr>
<tr>
<td><strong>Net new domestic brokerage accounts</strong></td>
<td>111,036</td>
<td>547,173</td>
<td>(80) %</td>
</tr>
<tr>
<td><strong>Net new banking accounts</strong></td>
<td>42,148</td>
<td>39,949</td>
<td>6 %</td>
</tr>
<tr>
<td><strong>Net new global and institutional accounts</strong></td>
<td>12,928</td>
<td>23,559</td>
<td>(45) %</td>
</tr>
<tr>
<td><strong>Total net new accounts</strong></td>
<td>166,112</td>
<td>610,681</td>
<td>(73) %</td>
</tr>
<tr>
<td><strong>Cost per new account</strong></td>
<td>$ 387</td>
<td>$ 258</td>
<td>50 %</td>
</tr>
<tr>
<td><strong>Total assets in domestic brokerage accounts</strong></td>
<td>$39,995,040</td>
<td>$61,569,597</td>
<td>(35) %</td>
</tr>
<tr>
<td><strong>Total deposits in banking accounts</strong></td>
<td>6,771,024</td>
<td>3,201,194</td>
<td>112 %</td>
</tr>
<tr>
<td><strong>Total assets in global and institutional accounts</strong></td>
<td>1,102,736</td>
<td>1,142,355</td>
<td>(3) %</td>
</tr>
<tr>
<td><strong>Total assets/deposits in customer accounts at period end</strong></td>
<td>$47,868,800</td>
<td>$65,913,146</td>
<td>(27) %</td>
</tr>
<tr>
<td><strong>Total domestic brokerage transactions</strong></td>
<td>8,084,849</td>
<td>14,242,052</td>
<td>(43) %</td>
</tr>
<tr>
<td><strong>Daily average domestic brokerage transactions</strong></td>
<td>130,401</td>
<td>226,064</td>
<td>(42) %</td>
</tr>
<tr>
<td><strong>Average commission per domestic brokerage transaction</strong></td>
<td>$ 13.62</td>
<td>$ 15.85</td>
<td>(14) %</td>
</tr>
<tr>
<td><strong>Rebates per domestic brokerage transaction</strong></td>
<td>$ 2.62</td>
<td>$ 2.02</td>
<td>30 %</td>
</tr>
</tbody>
</table>

Revenues

Gross revenues decreased 3% and net revenues decreased 21% from the prior year quarter. The decreases are mainly due to decreases in our brokerage-related activities, including transaction revenues and interest income, which have been impacted by the significant volatility in the securities market during the twelve months ended March 31, 2001. The Nasdaq composite index reached a record high in March 2000, compared to a dramatic decline through the period ended March 31, 2001, losing approximately 60% of its value. The sharp decline in the value of publicly traded securities has significantly impacted the total assets in our domestic brokerage accounts, which declined by 35% from the prior year quarter. Gross revenues consist principally of commission revenues from domestic retail brokerage transactions, payments for order flow, interest income, institutional transaction execution fees, international brokerage-related transaction revenue and, to a lesser degree, revenue from services, gains on the sale of loans and securities, and royalty revenues.
Transaction Revenues

Transaction revenues decreased 48% from the prior year quarter primarily due to the stock market downturn experienced since September 2000. Transaction revenues consist of commission revenues from domestic retail brokerage transactions and payments for order flow.

Commission revenues, which are earned as customers execute domestic securities trades, decreased 51% from the prior year quarter. These revenues are primarily affected by domestic brokerage transaction volume and the average commission per domestic brokerage transaction. Daily average domestic brokerage transactions decreased 42% from the prior year quarter, largely reflective of the market downturn and the decrease in the average commission per domestic transaction from $15.85 in the three months ended March 31, 2000 to $13.62 in the three months ended March 31, 2001. The decline in average commission per domestic brokerage transaction is primarily a result of promotional activities and the mix of revenue generating transactions, reflecting a higher percentage of trading by Power E*TRADE customers, our high volume traders. During the market downturn, the volume of transactions from our Power E*TRADE customers has declined less than the volume from our other customers. Power E*TRADE customers pay commissions as low as $4.95 per equity transaction compared with other customers who pay commissions of $14.95 or $19.95.

Revenue from order flow is comprised of rebate income from various market makers and market centers for processing transactions through them. We use other broker-dealers to execute our customers’ orders and have derived a significant portion of our transaction revenues from these broker-dealers for such order flow. This practice of receiving payment for order flow is widespread in the securities industry. Under applicable SEC regulations, receipt of these payments requires disclosure of such payments by us to our customers. Revenues from order flow decreased 26% from the prior year quarter primarily due to the market downturn. Payments for order flow as a percentage of transaction revenues were 16% and 11% in the three months ended March 31, 2001 and 2000, respectively, as evidenced by our rebates per transaction which increased from $2.02 for the three months ended March 31, 2000 to $2.62 for the three months ended March 31, 2001. The increase in rebates per transaction in the quarter ended March 31, 2001 is primarily due to the renegotiation of contracts with our primary market makers and market centers for processing transactions through them in the three months ended March 31, 2001. We cannot be certain that rebates per transaction will continue at the same levels in future periods. Also, reflected in the three month period ended March 31, 2001 is $2.6 million in revenues from option order flow, or approximately 12.4% of total order flow revenue. We initiated the acceptance of option order flow payments in October 2000.

Impacting future revenues from order flow, the listed marketplace, with the exception of the Nasdaq, implemented the move from fractional based trading to decimals (“decimalization”) in January 2001 and in March 2001, the Nasdaq initiated decimalization. With the advent of decimalization, certain market makers have announced plans to reduce payments for order flow, while others are taking a “wait and see” approach. As a majority of our order flow revenues is derived from Nasdaq listed securities, the impact of decimalization during the quarter ended March 31, 2001 has not been significant. Going forward, we expect a decrease in revenue from order flow due to decimalization; however, at this time, we are unable to quantify the future impact on net revenues. Further, there can be no assurance that we will be able to continue our present relationships and terms for such payments for order flow. In addition, there can be no assurance that payments for order flow will continue to be permitted by the SEC, the NASDR or other regulatory agencies, courts or governmental units. Loss of any or all of these revenues could have a material adverse effect on our business, financial condition and operating results. See “Item 2. Risk factors—Restrictions on the ability of or decreased willingness of third parties to make payments for order flow could reduce our profitability.”

Overall, transaction revenues as a percentage of net revenues have decreased from 45% in the three months ended March 31, 2000 to 24% in the three months ended March 31, 2001 due in part to the market downturn and also due to our efforts to diversify revenue streams.

Interest Income and Expense

Interest income from brokerage-related activities is comprised of interest earned by our brokerage subsidiaries on credit extended to customers to finance their purchases of securities on margin and fees on customer assets invested in money market accounts. Interest expense from brokerage-related activities is comprised of interest paid to customers on certain deposits, advances from the FHLB, and other borrowings. Interest expense from banking-related activities is comprised of interest-bearing banking liabilities that include customer credit extended to customers to finance their purchases of securities on margin and fees on customer assets invested in money market accounts. Interest expense from brokerage-related activities reflects interest earned on assets, consisting primarily of interest-bearing banking liabilities coupled with an increase in the average cost of the borrowings. Average interest-bearing

<table>
<thead>
<tr>
<th>Three Months Ended March 31</th>
<th>2001</th>
<th>2000</th>
<th>Percentage Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average customer margin balances</td>
<td>$2,866</td>
<td>$4,877</td>
<td>(41)%</td>
</tr>
<tr>
<td>Average customer money market fund balances</td>
<td>$8,596</td>
<td>$6,698</td>
<td>28%</td>
</tr>
<tr>
<td>Average customer credit balances</td>
<td>$1,373</td>
<td>$1,530</td>
<td>(10)%</td>
</tr>
<tr>
<td>Average stock loan balances</td>
<td>$2,594</td>
<td>$4,385</td>
<td>(41)%</td>
</tr>
</tbody>
</table>

Banking interest income increased 96% from the prior year quarter. Increases in banking interest income reflect overall growth in our banking segment including the increases in the average interest-earning banking asset balances, customer accounts, and customer deposits, partially offset by a decline in the average yield. Average interest-earning banking assets increased 104% from the prior year quarter. The average yield on interest-earning banking assets decreased to 7.47% in the three months ended March 31, 2001 from 7.76% in the three months ended March 31, 2000. Total deposits in banking accounts increased 112% from the prior year quarter. Banking interest expense increased 123% from the prior year quarter. The increase in banking interest expense reflects an increase in the average interest-bearing banking liabilities coupled with an increase in the average cost of the borrowings. Average interest-bearing
banking liabilities increased 108% from the prior year quarter. The average cost of borrowings increased to 6.62% in the three months ended March 31, 2001 from 6.13% in the three months ended March 31, 2000. The decrease in the average net interest spread from 1.63% in the three months ended March 31, 2000 to 0.85% in the three months ended March 31, 2001 is primarily a result of the overall tightening of spread in the market place coupled with an increase in the costs of retail deposits.

The following table presents average balance data and income and expense data for our banking operations and the related interest yields and rates for the three months ended March 31, 2001 and March 31, 2000. The table also presents information with respect to net interest margin, an indicator of profitability. Another indicator of profitability is net interest spread, which is the difference between the weighted average yield earned on interest-earning banking assets and weighted average rate paid on interest-bearing banking liabilities (dollars in thousands):

<table>
<thead>
<tr>
<th>Three Months Ended March 31, 2001</th>
<th>Three Months Ended March 31, 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Average Balance</strong></td>
<td><strong>Interest Income/Expense</strong></td>
</tr>
<tr>
<td>Loans receivable, net</td>
<td>$5,705,108</td>
</tr>
<tr>
<td>Interest-bearing deposits</td>
<td>39,825</td>
</tr>
<tr>
<td>Mortgage-backed and related available-for-sale securities</td>
<td>4,803,455</td>
</tr>
<tr>
<td>Available-for-sale investment securities</td>
<td>843,772</td>
</tr>
<tr>
<td>Investment in FHLB stock</td>
<td>83,358</td>
</tr>
<tr>
<td>Trading securities</td>
<td>128,797</td>
</tr>
<tr>
<td><strong>Total interest-earning banking assets</strong></td>
<td>11,604,315</td>
</tr>
<tr>
<td>Non-interest-earning banking assets</td>
<td>303,709</td>
</tr>
<tr>
<td><strong>Total banking assets</strong></td>
<td>$11,908,024</td>
</tr>
<tr>
<td>Interest-bearing banking liabilities:</td>
<td></td>
</tr>
<tr>
<td>Retail deposits</td>
<td>$6,169,462</td>
</tr>
<tr>
<td>Brokerced callable certificates of deposit</td>
<td>91,644</td>
</tr>
<tr>
<td>FHLB advances</td>
<td>1,625,322</td>
</tr>
<tr>
<td>Other borrowings</td>
<td>3,160,833</td>
</tr>
<tr>
<td><strong>Total interest-bearing banking liabilities</strong></td>
<td>11,047,261</td>
</tr>
<tr>
<td>Non-interest-bearing banking liabilities</td>
<td>208,214</td>
</tr>
<tr>
<td><strong>Total banking liabilities</strong></td>
<td>11,255,475</td>
</tr>
<tr>
<td><strong>Total banking shareholders equity</strong></td>
<td>652,549</td>
</tr>
<tr>
<td><strong>Total banking liabilities and shareholders equity</strong></td>
<td>$11,908,024</td>
</tr>
<tr>
<td>Excess of interest-earning banking assets over interest-bearing banking liabilities/net interest income</td>
<td>$557,054</td>
</tr>
<tr>
<td><strong>Net interest spread</strong></td>
<td>0.85%</td>
</tr>
<tr>
<td><strong>Net interest margin (net yield on interest-earning banking assets)</strong></td>
<td>1.26%</td>
</tr>
<tr>
<td><strong>Ratio of interest-earning banking assets to interest-bearing banking liabilities</strong></td>
<td>105.04%</td>
</tr>
<tr>
<td><strong>Return on average total banking assets</strong></td>
<td>0.44%</td>
</tr>
<tr>
<td><strong>Return on average net banking assets</strong></td>
<td>8.12%</td>
</tr>
<tr>
<td><strong>Equity to total banking assets</strong></td>
<td>5.48%</td>
</tr>
</tbody>
</table>

* Ratios calculated by excluding Employee Stock Ownership Plan and merger related costs of $0.2 million and $13.8 million in the three months ended March 31, 2001 and 2000.

**Global and Institutional**

Global and institutional revenues decreased 26% from the prior year quarter. Global and institutional revenues are comprised primarily of revenues from institutional operations of $31.2 million, as well as brokerage-related transaction revenue from our international subsidiaries of $5.7 million. The overall decrease is primarily attributable to a slowdown in the institutional business that was consistent with market conditions in the three months ended March 31, 2001, partially offset by the emerging online brokerage market in Canada and account growth in our international subsidiaries.
Other

Other revenues increased $47.8 million or 286% from the prior year quarter. Of this increase, $18.4 million is due to revenues generated by entities acquired subsequent to March 31, 2000 and accounted for under the purchase method of accounting, $17.3 million is due to net gains on available for sale and trading securities primarily resulting from the reclassification of our Bank loan portfolio, and $8.4 million is due to the implementation of a $15 quarterly maintenance fee for low-balance, inactive accounts which was instituted in December 2000. In future periods, net gains on investments may fluctuate. We expect to continue our policy of assessing maintenance fees for low-balance, inactive accounts. Revenues from our purchase acquisitions will fluctuate and may decrease. Purchase acquisitions included the acquisitions of E*TRADE Access, in May 2000 and LoansDirect in February 2001. Also included in other revenue are Business Solutions Group revenue, mutual fund revenues, and brokerage and banking-related fees for services, which in the aggregate have remained flat in the three months ended March 31, 2001 as compared to the prior year quarter.

Provision for loan losses

The provision for loan losses recorded reflects increases in our allowance for loan losses based upon management’s review and assessment of the risk in our loan portfolio, as well as the level of charge-offs as a portion of our allowance for loan losses. The provision for loan losses increased 15% from the prior year quarter. The increase in the provision for loan losses primarily reflects the growth in and composition of our banking loan portfolio. As of March 31, 2001 and September 30, 2000, the total loan loss allowance was $13.8 million, or 0.22% of total loans outstanding and $10.9 million, or 0.26% of total loans outstanding, respectively. As of March 31, 2001, the unallocated loan loss allowance was $13.0 million, or 75% of total non-performing assets of $17.3 million. As of September 30, 2000, the unallocated loan loss allowance was $10.5 million, or 87% of total non-performing assets of $12.1 million.

Operating Expenses

The following table sets forth the components of cost of services and operating expenses and percentage change information for the three months ended March 31, 2001 and 2000 (dollars in thousands):

<table>
<thead>
<tr>
<th>Cost of services and operating expenses</th>
<th>Three Months Ended March 31,</th>
<th>Percentage Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2001</td>
<td>2000</td>
</tr>
<tr>
<td>Cost of services</td>
<td>$142,435</td>
<td>$135,579</td>
</tr>
<tr>
<td>Cost of services as a percentage of net revenues</td>
<td>43%</td>
<td>33%</td>
</tr>
<tr>
<td>Selling and marketing</td>
<td>93,698</td>
<td>180,605</td>
</tr>
<tr>
<td>Technology development</td>
<td>22,281</td>
<td>43,335</td>
</tr>
<tr>
<td>General and administrative</td>
<td>60,242</td>
<td>52,551</td>
</tr>
<tr>
<td>Amortization of goodwill and other intangibles</td>
<td>7,999</td>
<td>5,297</td>
</tr>
<tr>
<td>Acquisition-related expenses</td>
<td>—</td>
<td>24,599</td>
</tr>
<tr>
<td>Total operating expenses</td>
<td>$184,220</td>
<td>$306,387</td>
</tr>
</tbody>
</table>

Cost of Services

Cost of services as a percentage of net revenues was 43% and 33% in the three months ended March 31, 2001 and 2000, respectively. The increase in cost of services as a percentage of net revenues is primarily a result of increased headcount in the cost of services area due to the acquisition of LoansDirect, the launch of Club E*TRADE in the three months ended December 31, 2000 and an increase in amortization expense related to internally developed software as significant projects were placed into production in November 2000, coupled with the decrease in net revenues from the prior year quarter. Cost of services increased 5% from the prior year quarter. Cost of services includes expenses related to our brokerage clearing operations, customer service activities, web site content costs, systems maintenance, and amortization expenses related to internally developed and purchased software. The slight increase in cost of services, primarily reflecting increased headcount, was offset by savings as we began integration of customer support staff for our banking and brokerage businesses and improved average speed to answer customer calls in the three months ended March 31, 2001 as compared to the three months ended March 31, 2000. In addition, during the three months ended March 31, 2001, we implemented system changes which have further improved the stability of our transaction enabling systems, reducing costs attributed to system outages and improving operational automation leading to efficiencies expected to benefit future periods. Looking forward, we plan to continue to identify and implement cost savings strategies in this area, including the full integration of our bank and brokerage customer service and the implementation of a tiered customer service strategy across the organization which will include improved interactive voice response call servicing and a tier-focused automated call routing system.

Selling and Marketing

Selling and marketing expenses decreased 48% from the prior year quarter. The selling and marketing expenditures reflect expenditures for advertising placements, creative development and collateral materials resulting from a variety of advertising campaigns directed at expanding brand identity, growing the customer base and increasing market share. Selling and marketing expenditures also include selling efforts in support of our global and institutional business segment and costs to sell products of our asset gathering business segment. The decrease in selling and marketing expenses from the prior year quarter is primarily due to reductions in customer acquisition spending, including advertising and direct mailing and promotional activities, which are expected to remain at lower than prior year levels. Cost per new account increased from $258 in the three months ended March 31, 2000 to $387 in the three months ended March 31, 2001, due to fewer new entrants into the market during the market downturn, as well as account attrition. Going forward, our focus will be on developing current customer households, reviewing metrics such as value per household, assets per household and share of wallet instead of cost per new account. Looking forward, we expect that marketing expenditure levels will be in the range of 20% to 23% of net revenues, significantly lower than during the fiscal year ended September 30, 2000. If general market conditions improve, we will explore the possibility of increasing our spending. We believe that our reduction in selling and marketing expenditures will not significantly impact our competitive position because substantial investment in marketing efforts has already been made to build a strong brand identity and because we are focusing marketing and sales resources on cross selling our services to our existing customer base, which is a less expensive way to generate and maintain business.
Technology Development

Technology development expenses decreased 49% from the prior year quarter. The expense for technology development was incurred to enhance our existing product offerings, including maintenance of our web site and development costs of our E*TRADE Insight technology incurred prior to the achievement of technological feasibility. Technology development costs in the three months ended March 31, 2001 as compared to the prior year quarter have decreased, primarily due to a reduction in the use of outside consultants as we refocused our efforts on fewer projects with higher anticipated benefits, and a conversion of consultants to full time associates where appropriate. Furthermore, as ongoing projects such as our Insight project progress, the achievement of technological feasibility results in the capitalization of expenses incurred from the date technological feasibility is achieved through the implementation date. During the six months ended March 31, 2001, significant phases of our Insight project reached technological feasibility. With management’s continuing focus on cost savings initiatives, technology development expenses are expected to remain at least flat with the quarter ended March 31, 2001 as we continue our integration efforts and continue to convert remaining consultants to full time associates. Our reduction in technology development spending is not expected to harm our ability to operate competitively when the market regains momentum, as improvements implemented to date provide us with sufficient excess capacity to meet currently anticipated needs of the business.

General and Administrative

General and administrative expenses increased 15% from the prior year quarter. General and administrative expenses increased primarily as a result of a $10.1 million compensation charge, $9.6 million of which is non-recurring, recognized in the three months ended March 31, 2001 related to the vesting of funds contributed to our Supplemental Executive Retirement Plan. Also contributing to the increase are personnel additions and the development of corporate functions, such as legal and finance, resulting from our investment in infrastructure, particularly as we expand our asset gathering and global and institutional operations. Looking forward, we expect that general and administrative expenses will remain at least flat with the three months ended March 31, 2001, allowing for possible reductions as we integrate our business acquisitions, continue our efforts to reengineer and reorganize our business to realize operating efficiencies, and review expenses in response to current and future market conditions. We will continue to actively manage our headcount with a focus on responsible hiring, attrition, efficient use of our associates and performance-based management.

Amortization of Goodwill and Other Intangibles

Amortization of goodwill and other intangibles was $8.0 million and $5.3 million in the three months ended March 31, 2001 and 2000, respectively. The significant increase in the amortization of goodwill and other intangibles primarily consists of the amortization of goodwill related to the purchase acquisitions of several of our foreign affiliates and E*TRADE Access, which were acquired during fiscal 2000, the acquisition of E*TRADE Germany AG, which was acquired during the three months ended December 31, 2001, and the acquisition of LoansDirect, which was acquired in February 2001. Goodwill is amortized over 5 to 20 years. Other intangibles are not significant.

Acquisition-Related Expenses

Acquisition-related expenses were $24.6 million for the three months ended March 31, 2000, and primarily represent transaction costs associated with acquisitions accounted for as poolings of interests.

Non-Operating Income (Expenses)

Corporate interest income was $5.8 million and $3.6 million in the three months ended March 31, 2001 and 2000, respectively. Corporate interest income includes interest income earned on corporate investment balances, restricted cash balances, and related party notes. The increase in corporate interest income was primarily due to interest income earned on related party notes, which were entered into during the period from March 2000 through June 2000.

Corporate interest expense was $11.2 million and $7.1 million in the three months ended March 31, 2001 and 2000, respectively. Corporate interest expense in the three months ended March 31, 2001 and 2000 primarily relates to interest expense resulting from the issuance of $650 million in convertible subordinated notes during the three months ended March 31, 2000.

Realized loss on sale of investments was $2.5 million and realized gain on the sale of investments was $10.9 million in the three months ended March 31, 2001 and 2000, respectively. In the three months ended March 31, 2001, we liquidated a portion of our investment portfolio, recognizing realized losses on the sale of a publicly-traded equity security. In the three months ended March 31, 2000, we liquidated a portion of our investment portfolio, recognizing realized gains as a result of the sale of publicly-traded equity securities. The Company has investments in other non-public entities, several of which have subsequently gone public. These investments have been classified as available-for-sale under the provisions of SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities.

Equity in losses of investments was $3.3 million and $0.7 million in the three months ended March 31, 2001 and 2000, respectively, which resulted from our minority ownership in investments that are accounted for under the equity method. These investments primarily include E*TRADE Japan KK and Wit, Inc in the three months ended March 31, 2001 and E*TRADE Japan KK in the three months ended March 31, 2000. We expect that these companies will continue to invest in the development of their products and services and may incur operating losses that will result in future charges to reflect our proportionate share of those losses.

In the three months ended March 31, 2001 and 2000, we recorded unrealized losses on venture funds of $11.6 million and $14.6 million, respectively, primarily due to our participation in Softbank Capital Partners, L.P., E*TRADE eCommerce Fund, L.P. and E*TRADE eCommerce Fund II, L.P. These changes represent market fluctuations on public investments held by the funds and changes in the estimated value of the non-public investments.

In the three months ended March 31, 2001, we recorded a $0.3 million pre-tax gain for the fair value adjustments of financial derivatives. The gain represents a $1.4 million gain representing the ineffective portions of changes in the fair value of fair value hedges offset by a $1.1 million loss on the valuation of warrants.

Other non-operating expense was $0.7 million and $0.8 million in the three months ended March 31, 2001 and 2000, respectively. Other non-operating
expense, which is primarily comprised of foreign exchange gains/losses, was recorded primarily as a result of fluctuations in foreign exchange rates for assets and liabilities held on our balance sheet that are denominated in non-functional currencies. In the three months ended March 31, 2001, foreign exchange losses resulted from the fluctuation in the foreign exchange rate on the Euro payable for the acquisition of E*TRADE Germany AG, offset by the Euro receivable held in escrow from the sale of E*TRADE @ NetBourse S.A. In the three months ended March 31, 2000, these foreign exchange losses primarily reflect fluctuations in the Japanese yen impacting assets held by TIR.

Income Tax Benefit

Income tax benefit represents the benefit for federal and state income taxes at an effective tax rate of 65.0% and 26.2% for the three months ended March 31, 2001 and 2000, respectively. The rate for the three months ended March 31, 2001 reflects an increase in the tax benefit due to federal and state research and development income tax credits, a decrease of the tax benefit for the amortization of goodwill and differences between our statutory and foreign effective tax rates. The rate for the three months ended March 31, 2000 reflects the tax impact of non-deductible acquisition-related expenses and amortization of goodwill arising from foreign acquisitions.

Minority Interest in Subsidiaries

Minority interest in subsidiaries was $35,000 and $0.4 million in the three months ended March 31, 2001 and 2000, respectively. Minority interest in subsidiaries results primarily from ETFC’s interest payments to subsidiary trusts which have issued Company-obligated mandatorily redeemable capital securities and which hold junior subordinated debentures of the Company. Also included in minority interest in subsidiaries for the three months ended March 31, 2001 and 2000 is the net loss attributed to a minority interest in one of our international affiliates.

Extraordinary Loss on Early Extinguishment of Debt

Extraordinary loss on early extinguishment of debt was $2.0 million (net of tax benefits of $1.2 million) for the three months ended March 31, 2001 and was recorded as a result of the early redemption of $400 million of adjustable and fixed rate advances with the FHLB. The FHLB advances were entered into as a result of normal funding requirements of the Company’s banking operations. The loss consisted primarily of a prepayment penalty and costs associated with the early redemption.

Liquidity and Capital Resources

We have financing facilities totaling $346.9 million to meet the needs of E*TRADE Securities. These facilities, if used, would be collateralized by customer securities or restricted cash included in other assets. There was $71.9 million in borrowings outstanding under these lines as of March 31, 2001, collateralized by restricted cash included in other assets. In addition, we have a short-term line of credit for up to $50 million, collateralized by marketable securities owned by us, of which there were no outstanding borrowings as of March 31, 2001. We also have three term loans collateralized by equipment owned by us, of which $18.7 million was outstanding as of March 31, 2001. We have also entered into numerous agreements with other broker-dealers to provide financing under our stock loan program.

We currently anticipate that our available cash resources, credit facilities, and liquid portfolio of equity securities will be sufficient to meet our presently anticipated working capital and capital expenditure requirements for at least the next 12 months. However, as a result of the substantial market decline of technology stocks since December 31, 2000, the value of our equity investments in technology companies, recorded in our investment portfolio, has deteriorated. The recognition of unrealized losses of $11.6 million related to these equity investments impacts our liquidity. Depreciation in the market value of our portfolio impacts our financing strategies that could result in higher interest expense if alternative financing strategies are used. We may need to raise additional funds in order to support more rapid expansion, develop new or enhanced services and products, respond to competitive pressures, acquire complementary businesses or technologies or take advantage of unanticipated opportunities. Our future liquidity and capital requirements will depend upon numerous factors, including costs and timing of expansion of technology development efforts and the success of such efforts, the success of our existing and new service offerings and competing technological and market developments. Our forecast of the period of time through which our financial resources will be adequate to support our operations is a forward-looking statement that involves risks and uncertainties, and actual results could vary. If additional funds are raised through the issuance of equity securities, the percentage ownership of the shareholders in our company will be reduced, shareholders may experience additional dilution in net book value per share or such equity securities may have rights, preferences or privileges senior to those of the holders of our common stock. There can be no assurance that additional financing will be available when needed on terms favorable to our Company, if at all. See “Item 2. Risk factors—If we are unable to quickly introduce new products and services that satisfy changing customer needs, we could lose customers and have difficulty attracting new customers.”

If adequate funds are not available on acceptable terms, we may be unable to develop or enhance our services and products, take advantage of future opportunities or respond to competitive pressures, any of which could harm our business. See “Item 2. Risk factors—If we are unable to quickly introduce new products and services that satisfy changing customer needs, we could lose customers and have difficulty attracting new customers.”

Cash used in operating activities, net of effects from acquisitions was $92.5 million for the three months ended March 31, 2001. Cash used in operating activities resulted primarily from an excess of purchases of banking-related assets over the net sale/maturity of banking-related assets of $196.6 million and an increase in other assets of $55.7 million, partially offset by depreciation, amortization and accretion of $36.1 million and an increase in brokerage-related liabilities in excess of assets, net of effects from acquisitions of $111.4 million. Cash used in operating activities, net of effects from acquisitions and net of the effects of realized gains on the sale of available-for-sale securities of $10.9 million, was $142.2 million for the three months ended March 31, 2000. Cash used in operating activities resulted primarily from an increase in brokerage-related assets in excess of liabilities, net of effects from acquisitions, of $239.3 million, an increase in other assets of $113.7 million, offset by an increase in accounts payable, accrued and other liabilities of $202.9 million.

Cash used in investing activities was $469.4 million and $1,752.7 million for the three months ended March 31, 2001 and 2000, respectively. For the three months ended March 31, 2001 and 2000, cash used in investing activities resulted primarily from an increase in loans receivable and purchases of property and equipment, partially offset by an excess of the net sale/maturity of investments over the purchases of investments.

Cash provided by financing activities was $505.6 million and $1,965.7 million for the three months ended March 31, 2001 and 2000, respectively. For the three months ended March 31, 2001 and 2000, cash provided by financing activities primarily resulted from an increase in banking deposits and net advances from the FHLB, offset by payments on advances from the FHLB and decreases in securities sold under agreements to repurchase.
Recent Accounting Pronouncements

In September 2000, the FASB issued SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. SFAS No. 140 replaces SFAS No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. It revises the standard for accounting for securitizations and other transfers of financial assets and collateral and requires certain disclosures, but it carries over most of SFAS No. 125’s provisions without reconsideration. SFAS No. 140 is effective for transactions after March 31, 2001. We are currently evaluating the impact of SFAS No. 140 on our consolidated financial statements.

RISK FACTORS

RISKS RELATING TO THE NATURE OF THE ONLINE FINANCIAL SERVICES BUSINESS

We face competition from competitors, some of whom have significantly greater financial, technical, marketing and other resources, which could cause us to lower our prices or to lose a significant portion of our market share.

The market for financial services over the Internet is new, rapidly evolving and intensely competitive. We expect competition to continue and intensify in the future. We face direct competition from financial institutions, brokerage firms, banks, mutual fund companies, Internet portals and other organizations, including among others:

- American Express Company
- AOL Time Warner Inc.
- Ameritrade, Inc.
- Bank of America Corporation
- Charles Schwab & Co., Inc.
- CSFBdirect (formerly DLJ direct)
- J.P. Morgan Chase & Co.
- Citigroup Inc.
- Datek Online Holdings Corporation
- Fidelity Investments
- FleetBoston Financial Corporation
- Intuit Inc.
- Merrill Lynch, Pierce, Fenner & Smith Incorporated
- Microsoft MoneyCentral
- Morgan Stanley Dean Witter & Co.
- National Discount Brokers Corporation (which is owned by Deutsche Bank)
- NetBank, Inc.
- PaineWebber Group, Inc. (which is owned by UBS AG)
- Salomon Smith Barney, Inc. (which is owned by Citigroup)
- TD Waterhouse Group, Inc.
- Wells Fargo & Company
- WingspanBank.com (a division of First USA Bank, N.A.)
- Yahoo! Inc.

Many of our competitors have longer operating histories and significantly greater financial, technical, marketing and other resources than we do. In addition, many of our competitors offer a wider range of investment banking, advisory and other financial services and products than we do, and thus may be able to respond more quickly to new or changing opportunities, technologies and customer preferences and requirements. Many of our competitors also have greater name recognition and larger customer bases that could be leveraged, thereby gaining market share from us. These competitors may conduct more extensive promotional activities and offer better terms and lower prices to customers than we do, possibly even sparking a price war in the online financial services industry. Moreover, some of our competitors have established cooperative relationships among themselves or with third parties to enhance their services and products. It is possible that new competitors or alliances among existing competitors may significantly reduce our market share.

General financial success within the financial services industry over the past several years has strengthened existing competitors and may continue to attract new competitors, such as software development companies, insurance companies and others, as such companies expand their financial product lines. Commercial banks and other financial institutions have become more competitive with our brokerage operations by offering their customers certain corporate and individual financial services traditionally provided by securities firms. The current trend toward consolidation in the commercial banking industry could
further increase competition in all aspects of our business. While we cannot predict the type and extent of competitive services that commercial banks and other financial institutions ultimately may offer, we may be adversely affected by such competition. To the extent our competitors are able to attract and retain customers, our business or ability to grow could be adversely affected.

There can be no assurance that we will be able to compete effectively with current or future competitors or that this competition will not significantly harm our business.

The security of our computers or confidential customer information transmitted over public networks could be breached, which could deter customers from using our services and significantly damage our reputation

Because we rely heavily on electronic communications and secure transaction processing in our securities, banking and ATM businesses, we must protect our computer systems and network from physical break-ins, security breaches and other disruptions caused by unauthorized access. We must also provide for the secure transmission of confidential information over public networks. The open nature of the Internet makes protecting against these threats more difficult. Unauthorized access to our computers could jeopardize the security of information stored in and transmitted through our computer systems and network, which could harm our ability to retain or attract customers, damage our reputation and subject us to litigation and financial losses. We have in the past, and could in the future, be subject to denial of service, vandalism and other attacks on our systems. We rely on encryption and authentication technology, including cryptography technology licensed from RSA Data Security, Inc., to provide secure transmission of confidential information over public networks. Advances in computer and decryption capabilities or other developments could compromise the methods we use to protect customer transaction data, which could harm our ability to retain or attract customers. In addition, we must guard against damage by persons with authorized access to our computer systems. The security and encryption technology and the operational procedures we implement to prevent break-ins, damage and failures may be unable to prevent future disruptions of our operations. Our insurance coverage may be insufficient to cover losses that may result from these events.

As a significant portion of our revenues come from online investing services, downturns in the securities industry have harmed and could further significantly harm our business, including by reducing transaction volumes and margin borrowing and increasing our dependence on our more active customers who receive lower prices

A significant portion of our revenues in recent years has been from online investing services, and although we continue to diversify our revenue sources we expect this business to continue to account for a significant portion of our revenues in the foreseeable future. We, like other financial services firms, are directly affected by economic and political conditions, broad trends in business and finance and changes in volume and price levels of securities and futures transactions. The U.S. securities markets are characterized by considerable fluctuation and downturns in these markets have harmed our operating results, including our transaction volume and the rate of growth of new accounts, and could continue to do so in the future. Significant downturns in the U.S. securities markets occurred in October 1987 and October 1989, and a significant downturn has been occurring since March 2000. Consequently, transaction volume has decreased industry-wide including a substantial decrease in the past quarter, and many broker-dealers, including E*TRADE Securities, have been adversely affected. The decrease in transaction volume has been more significant with respect to our less active customers, increasing our dependence on our more active Power E*TRADE customers who receive more favorable pricing based on their transaction volume. When transaction volume is low, our operating results are harmed in part because some of our overhead costs remain relatively fixed. We cannot assure you that U.S. securities markets will not continue to be volatile or that prices and transaction volume will not continue to move downward, either of which could harm our business going forward. Some of our competitors with more diverse product and service offerings might withstand such a downturn in the securities industry better than we would. See “Item 2. Risk Factors—If we are unable to compete effectively against our competitors, some of whom have significantly greater financial, technical, marketing and other resources, our business may suffer.”

Downturns in the securities markets increase the risk that parties to margin lending transactions with us will fail to honor their commitments and that the value of the collateral we hold in connection with those transactions will not be adequate, increasing our risk of losses from our margin lending activities

We sometimes allow customers to purchase securities on margin, and we are therefore subject to risks inherent in extending credit. This risk is especially great when the market is rapidly declining and the value of the collateral we hold could fall below the amount of a customer’s indebtedness. Under specific regulatory guidelines, any time we borrow or lend securities, we must correspondingly disburse or receive cash deposits. If we fail to maintain adequate cash deposit levels at all times, we run the risk of loss if there are sharp changes in market values of many securities and parties to the borrowing and lending transactions fail to honor their commitments. Any such losses could harm our financial position and results of operations.

Our inability to retain and hire skilled personnel and senior management could seriously harm our ability to maintain and grow our business

Over the past year, we hired a significant number of additional skilled personnel, including persons with experience in the computer, brokerage and banking industries, and persons with Series 7 or other broker-dealer licenses. If the number of accounts and transaction volume increases significantly over current volume, there could be a shortage of qualified and, in some cases, licensed personnel that we may then be seeking to hire which could cause a backlog in the handling of banking transactions or the processing of brokerage orders that need review, and that could harm our business, financial condition and operating results. Competition for such personnel is intense when trading volumes are high, and there can be no assurance that we will be able to retain or hire technical persons or licensed representatives in the future.

In addition, our future success depends to a significant degree on the skills, experience and efforts of our Chief Executive Officer, President and Chief Operating Officer, Chief Financial Officer, and other key management personnel. The loss of the services of any of these individuals could compromise our ability to effectively operate our business.

If our ability to correctly process customer transactions is slowed or interrupted, we could be subject to customer litigation and our reputation could be harmed

We process customer transactions mostly through the Internet, online service providers, touch-tone telephones and our computer systems, and we depend heavily on the integrity of the communications and computer systems supporting these transactions, including our internal software programs and computer systems. A degradation or interruption in the operation of these systems could subject us to significant customer litigation and could materially harm our reputation. Our systems or any other systems in the transaction process could slow down significantly or fail for a variety of reasons including:
undetected errors in software programs or computer systems,

our inability to effectively resolve any errors in our internal software programs or computer systems once they are detected, or

heavy stress placed on systems in the transaction process during certain peak trading times.

If our systems or any other systems in the transaction process slow down or fail even for a short time, our customers could suffer delays in transaction processing, which could cause substantial customer losses and may subject us to claims for these losses or to litigation. The NASDR defines a "system failure" as a shutdown of our mission critical systems (defined as those necessary for the acceptance and execution of online securities orders) which causes the customers' use of these systems to equal or exceed system capacity during regular market hours, or a shutdown of any system application necessary for the acceptance and execution of online securities orders for a period of 15 continuous minutes that affects 25% or more of the customers on the system from effecting securities transactions during regular market hours. We have experienced systems failures and degradation in the past. Systems failures and degradations could occur with respect to U.S. markets or foreign markets where we must implement new transaction processing infrastructures. To date, during our systems failures, we were able to take orders by telephone; however, with respect to our brokerage transactions, only associates with securities brokers' licenses can accept telephone orders. An adequate number of such associates may not be available to take customer calls in the event of a future systems failure, and we may not be able to increase our customer service personnel and capabilities in a timely and cost-effective manner. To promote customer satisfaction and protect our brand name, we have, on certain occasions, compensated customers for verifiable losses from such failures.

Increases in prevailing and anticipated interest rates would reduce the value of the Bank's fixed rate investments and may decrease the Bank's profitability by increasing the expense of variable rate interest-bearing liabilities without a corresponding increase in income from assets bearing a fixed rate of interest

The results of operations for the Bank depend in large part upon the level of its net interest income, that is, the difference between interest income from interest-earning assets, such as loans and mortgage-backed securities, and interest expense on interest-bearing liabilities, such as deposits and borrowings. Changes in market interest rates (and the yield curve) could reduce the value of the Bank’s financial assets and thereby reduce net interest income. Fixed-rate investments, mortgage-backed and related securities and mortgage loans generally decline in value as interest rates rise. Many factors cause changes in interest rates, including governmental monetary policies and domestic and international economic and political conditions.

The Bank attempts to mitigate this interest rate risk by using derivative contracts that are designed to offset, in whole or in part, the variability in value or cash flow of various assets or liabilities caused by changes in interest rates. There can be no assurances that these derivative contracts move either directionally or proportionately as intended. SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, which the Company adopted on October 1, 2000, requires that the hedge ineffectiveness, or the change in value of the hedged item versus the change in value of the hedging instruments, be recognized in earnings as of the reporting date. Our financial results may prove to be more volatile due to this new reporting requirement.

If we are unsuccessful in managing the effects of changes in interest rates, our financial condition and results of operations could suffer.

The Bank’s asset diversification to include higher yielding investments which carry a higher inherent risk of default in its portfolio may increase the risk of charge-offs which could reduce our profitability

As the Bank diversifies its investment portfolio through purchases of new higher yielding investment classes, we will have to manage assets that carry a higher inherent risk of default than experienced with our existing portfolio. Consequently, the level of charge-offs associated with these assets may be higher than previously experienced. If expectations of future charge-offs increase, a simultaneous increase in the amount of our loss reserves would be required. The increased level of charge-offs recorded to meet additional reserve requirements could harm the results of our operations if those higher yields do not cover the charge-offs.

We rely on a number of third parties to process our transactions, and their inability to expand their technology to meet our needs, or our inability to expand our own technology in the event of a significant increase in demand, could impair our ability to acquire new customers and otherwise grow our business

We rely on a number of third parties to process our transactions, including online and Internet service providers, back office processing organizations, other service providers and market-makers, all of which may need to expand the scope of the operations they perform for us. Any backlog caused by a third party’s inability to expand sufficiently to meet our needs could harm our business. In addition, in the past rapid growth in the use of our services has strained our own ability to adequately expand technologically to meet increased demand.

If we are unable to quickly introduce new products and services that satisfy changing customer needs, we could lose customers and have difficulty attracting new customers

Our future profitability depends significantly on our ability to develop and enhance our services and products. There are significant challenges to such development and enhancement, including technical risks. There can be no assurance that we will be successful in achieving any of the following:

- effectively using new technologies,
- adapting our services and products to meet emerging industry standards,
- developing, introducing and marketing service and product enhancements, or
- developing, introducing and marketing new services and products to meet customer demand.

Additionally, these new services and products, if they are developed, may not adequately meet the requirements of the marketplace or achieve market acceptance. If we are unable to develop and introduce enhanced or new services and products quickly enough to respond to market or customer requirements, or if they do not achieve market acceptance, our business could be harmed.
If our Business Solutions Group products fail or produce inaccurate results we could be subject to litigation and our reputation may be harmed

BSG provides products and services to assist companies to work effectively with their own professional legal, accounting and tax advisors to comply with the laws, regulations, and rules pertaining to equity compensation. BSG provides products and services that, by their nature, are highly technical and intricate, and that deal with issues which could result in significant accounting and tax reporting inaccuracies. If BSG’s efforts to protect itself from liability arising from product design limitations and/or potential human error prove inadequate, these inaccuracies could subject BSG to customer litigation and damage our reputation.

The size of our market and our results of operations depend heavily upon the growing acceptance of the Internet as a commercial marketplace for financial services

Because the electronic provision of financial services is currently the most significant part of our business, sales of most of our services and products will depend on consumers continuing to adopt the Internet as a method of doing business and, in particular, as a method of obtaining financial services. Several factors could adversely affect the acceptance and growth of online commerce. For example, there can be no assurance that the Internet infrastructure will continue to be able to support the demands placed on it by growing usage. In addition, the Internet could be adversely affected by the slow development or adoption of standards and protocols to handle increased Internet activity or by increased governmental regulation. Moreover, critical Internet issues including privacy, security, reliability, cost, ease of use, accessibility and quality of service remain unresolved, which could negatively affect the growth of Internet use or commerce on the Internet.

Even if Internet commerce grows generally, the online market for financial services could grow more slowly or even shrink in size. Adoption of online commerce for financial services by individuals who have relied upon traditional delivery channels in the past will require such individuals to accept new and different methods of conducting business.

If our international efforts are not successful, our business growth will be harmed and our resources will not have been used efficiently

One component of our strategy is a planned increase in efforts to attract more international customers. To date, we have limited experience in providing brokerage services internationally, and E*TRADE Access has had only limited experience providing banking services to customers outside the United States. There can be no assurance that we and/or our international licensees will be able to market our branded services and products successfully in international markets.

In order to expand our services globally, we must comply with the regulatory controls of each specific country in which we conduct business. Our international expansion could be limited by the compliance requirements of other regulatory jurisdictions, including the EU’s Privacy Directive regulating the use and transfer of customer data. We intend to rely primarily on local third parties and our subsidiaries for regulatory compliance in foreign jurisdictions.

In addition, there are certain risks inherent in doing business in international markets, particularly in the heavily regulated brokerage and banking industries, such as:

- unexpected changes in regulatory requirements and trade barriers,
- difficulties in staffing and managing foreign operations,
- the level of investor interest in cross-border trading,
- authentication of online customers,
- political instability,
- fluctuations in currency exchange rates,
- reduced protection for intellectual property rights in some countries,
- seasonal reductions in business activity during the summer months in Europe and certain other parts of the world,
- the level of adoption of the Internet in international markets, and
- potentially adverse tax consequences.

Any of the foregoing could harm our international operations. In addition, because some of these international markets are served through license arrangements with others, we rely upon these third parties for a variety of business and regulatory compliance matters. We have limited control over the management and direction of these third parties. We run the risk that their action or inaction could harm our operations and/or our reputation. Additionally, our international licensees have the right to grant sublicenses. Generally, we have less control over sublicensees than we do over licensees. As a result, the risk to our operations and goodwill is higher.

Our failure to successfully integrate the companies that we acquire into our existing operations could harm our business.

We recently acquired E*TRADE Access, Electronic Investing Corporation, PrivateAccounts Inc., renamed E*TRADE Advisory Services, Inc. on January 2, 2001, E*TRADE Technologies, LoansDirect and several of our international affiliates. We may also acquire other companies or technologies in the future, and we regularly evaluate such opportunities. Acquisitions entail numerous risks, including, but not limited to:

- difficulties in the assimilation and integration of acquired operations and products,
- diversion of management’s attention from other business concerns,
- failure to achieve anticipated cost savings,
amortization of acquired intangible assets, with the effect of reducing our reported earnings, and
potential loss of key associates of acquired companies.

No assurance can be given as to our ability to integrate successfully any operations, technology, personnel, services or new businesses or products that might be acquired in the future. Failure to successfully assimilate acquired organizations could harm our business. In addition, there can be no assurance that we will realize a positive return on any of these investments.

Any failure to maintain our relationships with strategic partners or loss in value of the investments we make could harm our business

We have established a number of strategic relationships with online and Internet service providers, as well as software and information service providers and retail companies. There can be no assurance that any such relationships will be maintained, or that if they are maintained, they will be successful or profitable. Additionally, we may not be able to develop new relationships of this type in the future.

We also make investments, either directly or through affiliated private investment funds, in equity securities of other companies without acquiring control of those companies. There may be no public market for the securities of the companies in which we invest, and we may not be able to sell these securities at a profit, or at all.

If we fail to protect our intellectual property rights or face a claim of intellectual property infringement by a third party, we could lose our intellectual property rights, be liable for significant damages, or incur significant costs and expenses regardless of the merits of the claims against us

Our ability to compete effectively is dependent to a significant degree on our brand and proprietary technology. We rely primarily on copyright, trade secret and trademark law to protect our technology and our brand. Effective trademark protection may not be available for our trademarks. Although we have registered the trademark “E*TRADE” in the United States and a number of other countries, and have other registered trademarks, there can be no assurance that we will be able to secure significant protection for these trademarks. Our competitors or others may adopt product or service names similar to “E*TRADE,” thereby impeding our ability to build brand identity and possibly leading to customer confusion. Our inability to adequately protect the name “E*TRADE” could harm our business. Despite any precautions we take, a third party may be able to copy or otherwise obtain and use our software or other proprietary information without authorization or to develop similar software independently. Policing unauthorized use of our technology is made especially difficult by the global nature of the Internet and difficulty in controlling the ultimate destination or security of software or other data transmitted on it. The laws of other countries may afford us little or no effective protection for our intellectual property. There can be no assurance that the steps we take will prevent misappropriation of our technology or that agreements entered into for that purpose will be enforceable. In addition, litigation may be necessary in the future to:

- enforce our intellectual property rights,
- protect our trade secrets,
- determine the validity and scope of the proprietary rights of others, or
- defend against claims of infringement or invalidity.

Such litigation, whether successful or unsuccessful, could result in substantial costs and divert resources, either of which could harm our business.

We have received in the past, and may receive in the future, notices of claims of infringement of other parties’ proprietary rights. There can be no assurance that claims for infringement or invalidity—or any indemnification claims based on such claims—will not be asserted or prosecuted against us. Any such claims, with or without merit, could be time consuming and costly to defend or litigate, divert our attention and resources or require us to enter into royalty or licensing agreements. There can be no assurance that such licenses would be available on reasonable terms, if at all.

RISKS RELATING TO THE REGULATION OF OUR BUSINESS

If changes in government regulation favor our competition or restrict our business practices, our ability to attract customers and our profitability may suffer

The securities industry in the United States is subject to extensive regulation under both federal and state laws. The banking industry in the United States is subject to extensive federal regulation. Broker-dealers are subject to regulations covering all aspects of the securities business, including:

- sales methods,
- recommendations of securities,
- trading practices among broker-dealers,
- execution of customers’ orders,
- use and safekeeping of customers’ funds and securities,
- capital structure,
- record keeping,
- advertising,
- conduct of directors, officers and employees, and
Because we are a self-clearing broker-dealer, we have to comply with many additional laws and rules. These include rules relating to possession and control of customer funds and securities, margin lending and execution and settlement of transactions. Our ability to comply with these rules depends largely on the establishment and maintenance of a qualified compliance system.

Similarly, the Parent and ETFC, as savings and loan holding companies, and the Bank, as a federally chartered savings bank and subsidiary of ETFC, are subject to extensive regulation, supervision and examination by the OTS, and, in the case of the Bank, the FDIC. Such regulation covers all aspects of the banking business, including lending practices, safeguarding deposits, capital structure, record keeping, and conduct and qualifications of personnel.

Because of our international presence, we are also subject to the regulatory controls of each specific country in which we conduct business.

Because we operate in an industry subject to extensive regulation, the competitive landscape in our industry can change significantly as a result of new regulation, changes in existing regulation, or changes in the interpretation or enforcement of existing laws and rules. For example, in November 1999, the Gramm-Leach-Bliley Act was enacted into law. This act reduces the legal barriers between banking, securities and insurance companies, and will make it easier for financial holding companies to compete directly with our securities business, as well as for our competitors in the securities business to diversify their revenues and attract additional customers through entry into the banking and insurance businesses. The Gramm-Leach-Bliley Act may have a material impact on the competitive landscape that we face.

There can be no assurance that federal, state or foreign agencies will not further regulate our business. We anticipate that we may be required to comply with record keeping, data processing and other regulatory requirements as a result of proposed federal legislation or otherwise. We may also be subject to additional regulation as the market for online commerce evolves. Because of the growth in the electronic commerce market, Congress has held hearings on whether to regulate providers of services and transactions in the electronic commerce market. As a result, federal or state authorities could enact laws, rules or regulations affecting our business or operations. We may also be subject to federal, state or foreign money transmitter laws and state and foreign sales or use tax laws. If such laws are enacted or deemed applicable to us, our business or operations could be rendered more costly or burdensome, less efficient or even impossible. Any of the foregoing could harm our business, financial condition and operating results.

### If we fail to comply with applicable securities and banking regulations, we could be subject to disciplinary actions, damages, penalties or restrictions that could significantly harm our business

The SEC, the NASDR or other self-regulatory organizations and state securities commissions can censure, fine, issue cease-and-desist orders or suspend or expel a broker-dealer or any of its officers or employees. The OTS may take similar action with respect to our banking activities. Our ability to comply with all applicable laws and rules is largely dependent on our establishment and maintenance of a system to ensure such compliance, as well as our ability to attract and retain qualified compliance personnel. Our growth has placed considerable strain on our ability to ensure such compliance. We could be subject to disciplinary or other actions due to claimed noncompliance in the future, which could harm our business.

### If we do not maintain the capital levels required by regulators, we may be fined or forced out of business

The SEC, NASDR, OTS and various other regulatory agencies have stringent rules with respect to the maintenance of specific levels of net capital by securities broker-dealers and regulatory capital by banks. Net capital is the net worth of a broker or dealer (assets minus liabilities), less deductions for certain types of assets. If a securities firm fails to maintain the required net capital it may be subject to suspension or revocation of registration by the SEC and suspension or expulsion by the NASDR, and could ultimately lead to the firm’s liquidation. In the past, our broker-dealer subsidiaries have depended largely on capital contributions by us in order to comply with net capital requirements. If such net capital rules are changed or expanded, or if there is an unusually large charge against net capital, operations that require the intensive use of capital could be limited. Such operations may include investing activities, marketing and the financing of customer account balances. Also, our ability to withdraw capital from brokerage subsidiaries could be restricted, which in turn could limit our ability to pay dividends, repay debt and redeem or purchase shares of our outstanding stock. A large operating loss or charge against net capital could adversely affect our ability to expand or even maintain our present levels of business, which could harm our business.

The table below summarizes the minimum net capital requirements for our domestic broker-dealer subsidiaries as of March 31, 2001 (in thousands):

<table>
<thead>
<tr>
<th>Subsidiary</th>
<th>Required Net Capital</th>
<th>Net Capital</th>
<th>Excess Net Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>E*TRADE Securities Incorporated.</td>
<td>$48,123</td>
<td>$414,103</td>
<td>$365,980</td>
</tr>
<tr>
<td>E*TRADE Institutional Securities, Inc.</td>
<td>$250</td>
<td>$2,779</td>
<td>$2,529</td>
</tr>
<tr>
<td>E*TRADE Investor Select, Inc.</td>
<td>$5</td>
<td>$230</td>
<td>$225</td>
</tr>
<tr>
<td>Marquette Securities, Inc.</td>
<td>$250</td>
<td>$795</td>
<td>$545</td>
</tr>
<tr>
<td>E*TRADE Capital Markets, Inc.</td>
<td>$174</td>
<td>$14,126</td>
<td>$13,952</td>
</tr>
<tr>
<td>E*TRADE Canada Securities Corporation</td>
<td>$56</td>
<td>$192</td>
<td>$136</td>
</tr>
</tbody>
</table>

Similarly, banks, such as the Bank, are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could harm a bank’s operations and financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, a bank must meet specific capital guidelines that involve quantitative measures of a bank’s assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. A bank’s capital amounts and classification are also subject to qualitative judgments by the regulators about the strength of components of the bank’s capital, risk weightings of assets and off-balance-sheet transactions, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require a bank to maintain minimum amounts and ratios of total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets. To be categorized as well capitalized, a bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the following table.

The table below summarizes the capital adequacy requirements for the Bank as of March 31, 2001 (dollars in thousands):

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Risk-Based Capital</td>
<td>$21,421</td>
</tr>
<tr>
<td>Tier 1 Risk-Based Capital</td>
<td>$13,247</td>
</tr>
<tr>
<td>Tier 1 Leverage Ratio</td>
<td>3.39%</td>
</tr>
<tr>
<td>Total Capital Adequacy Ratio</td>
<td>11.65%</td>
</tr>
<tr>
<td>Tier 1 Capital Adequacy Ratio</td>
<td>8.22%</td>
</tr>
</tbody>
</table>

The table above presents a summary of the capital adequacy requirements for the Bank as of March 31, 2001. The figures represent the required capital adequacy ratios as defined by regulatory agencies. The Bank must maintain these ratios to be considered adequately capitalized. The table also indicates the actual capital adequacy ratios as of the reporting date, which are compared to the required ratios to assess the Bank’s capital position. The ratios are calculated based on the Bank’s risk-weighted assets and average total assets, respectively. If the Bank fails to meet the required capital adequacy ratios, regulatory actions such as restrictions on dividends, loan or investment limits, or imposition of regulatory sanctions may be initiated.
Restrictions on the ability of or decreased willingness of third parties to make payments for order flow could reduce our profitability

Order flow revenue is comprised of rebate income from various market makers and market centers for processing transactions through them. There can be no assurance that payments for order flow will continue to be permitted by the SEC, the NASD or other regulatory agencies, courts or governmental units. In addition, the listed marketplaces other than Nasdaq moved from trading using fractional share prices to trading using decimals in January 2001 and the Nasdaq initiated decimalization in March 2001. With the advent of decimalization, certain market makers have announced plans to reduce payments for order flow, while others are taking a “wait and see” approach. As a majority of our order flow revenues is derived from Nasdaq listed securities, the impact of decimalization during the quarter ended March 31, 2001 has not been significant, but the impact of decimalization on future revenues cannot be accurately predicted at this time, and a general decrease in these revenues is expected. Further, there can be no assurance that we will be able to continue our present relationships and terms for payments for order flow. Loss of any or all of these revenues could harm our business.

Regulatory review of our advertising practices could hinder our ability to operate our business and result in fines and other penalties

All marketing activities by E*TRADE Securities are regulated by the NASD, and all marketing materials must be reviewed by an E*TRADE Securities Series 24 licensed principal prior to release. The NASD has in the past asked us to revise certain marketing materials. We are currently the subject of a formal NASD investigation and an informal SEC inquiry into our advertising practices. The NASD can impose certain penalties for violations of its advertising regulations, including:

- censure or fines,
- suspension of all advertising,
- the issuance of cease-and-desist orders, or
- the suspension or expulsion of a broker-dealer or any of its officers or employees.

In addition, the federal banking agencies impose restrictions on bank advertising of non-deposit investment products to minimize the likelihood of customer confusion.

If we were to solicit orders from our customers or make investment recommendations, we would become subject to additional regulations that could be burdensome and subject us to fines and other penalties

We do not currently solicit orders from our customers or make investment recommendations. However, if we were to engage in such activities, we would become subject to additional rules and regulations governing, among other things, sales practices and the suitability of recommendations to customers. Compliance with these regulations could be burdensome, and, if we fail to comply, we could be subject to fines and other penalties. We are continuing to develop technology, through a joint venture, that may enable us to provide financial advice for online investors in the future.

Due to the increasing popularity of the Internet, laws and regulations may be passed dealing with issues such as user privacy, pricing, content and quality of products and services and those regulations could adversely affect the growth of the online financial services industry

As required by the Gramm-Leach-Bliley Act, the SEC and OTS have recently adopted regulations on financial privacy which will take effect in July 2001 that will require E*TRADE Securities and the Bank to notify consumers about the circumstances in which they may share consumers’ personal information with unaffiliated third parties and to give consumers the right to prohibit such information sharing in specified circumstances. Although E*TRADE Securities and the Bank already provide such opt-out rights in our privacy policies, the regulations will require us to modify the text and the form of presentation of our privacy policies and to incur additional expense to ensure ongoing compliance with the regulations.

In addition, several recent reports have focused attention on the online brokerage industry. For example, the New York Attorney General investigated the online brokerage industry and issued a report in November 1999, citing consumer complaints about delays and technical difficulties in companies conducting online stock trading. SEC Commissioner Laura Unger also issued a report in November 1999 on issues raised by online brokerage, including suitability and marketing issues. Most recently, the United States General Accounting Office issued a report citing a need for better investor protection information on brokers’ Web sites and, on January 25, 2001, the SEC issued a report summarizing its findings and recommendations following an examination of broker-dealers offering online trading.

Increased attention focused upon these issues could hurt the growth of the online financial services industry, which could, in turn, decrease the demand for our services or could otherwise harm our business.

Due to our acquisition of ETFC, we are subject to regulations that could restrict our ability to take advantage of good business opportunities and that may be burdensome to comply with

Upon the completion of our acquisition of ETFC and its subsidiary, the Bank, on January 12, 2000, we became subject to regulation as a savings and loan holding company. As a result, we, as well as the Bank, are required to file periodic reports with the OTS, and are subject to examination by the OTS. The OTS also has certain types of enforcement power over ETFC and us, including the ability to issue cease-and-desist orders, up to and including forcing divestiture of the Bank, and civil money penalties, for violating the Savings and Loan Holding Company Act. In addition, under the Graham-Leach-Bliley Act, we are subject to regulations that could restrict our ability to take advantage of good business opportunities and that may be burdensome to comply with.

<table>
<thead>
<tr>
<th>Actual</th>
<th>To Be Well Capitalized Under Prompt Corrective Action Provision</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount</td>
<td>Ratio</td>
</tr>
<tr>
<td>$682,943</td>
<td>5.66%</td>
</tr>
<tr>
<td>$682,943</td>
<td>11.57%</td>
</tr>
<tr>
<td>$696,595</td>
<td>11.80%</td>
</tr>
</tbody>
</table>
Act, our activities are now restricted to activities that are financial in nature and certain real estate-related activities. We may also make merchant banking investments in companies whose activities are not financial in nature, if those investments are engaged in for the purpose of appreciation and ultimate resale of the investment, and we do not manage or operate the company. Such merchant banking investments may be subject to maximum holding periods and special recordkeeping and risk management requirements.

We believe that all of our existing activities and investments are permissible under the new legislation, but the OTS has not interpreted these provisions. Even if all of our existing activities and investments are permissible, under the new legislation we will be constrained in pursuing future new activities that are not financial in nature. We are also limited in our ability to invest in other savings and loan holding companies. These restrictions could prevent us from pursuing certain activities and transactions that could be beneficial to us.

In addition to regulation of us and ETFC as savings and loan holding companies, federal savings banks such as the Bank are subject to extensive regulation of their activities and investments, their capitalization, their risk management policies and procedures, and their relationship with affiliated companies. In addition, as a condition to approving our acquisition of ETFC, the OTS imposed various notice and other requirements, primarily a requirement that the Bank obtain prior approval from the OTS of any future material changes to the Bank’s business plan. These regulations and conditions, and our inexperience with them, could affect our ability to realize synergies from the acquisition, and could negatively affect both us and the Bank following the acquisition and could also delay or prevent the development, introduction and marketing of new products and services.

We may incur costs to avoid investment company status and our business would suffer significant harm if we were deemed to be an investment company

We may incur significant costs to avoid investment company status and may suffer other adverse consequences if we are deemed to be an investment company under the Investment Company Act of 1940, commonly referred to as the 1940 Act.

A company may be deemed to be an investment company if it owns investment securities with a value exceeding 40% of its total assets, subject to certain exclusions. After giving effect to the sale of 6% convertible subordinated notes, we will have substantial short-term investments until the net proceeds from the sale can be deployed. In addition, we and our subsidiaries have made minority equity investments in other companies that may constitute investment securities under the 1940 Act. In particular, many of our publicly-traded equity investments, which are owned directly or indirectly by us or through related venture funds, are deemed to be investment securities. Although our investment securities currently comprise less than 40% of our total assets, the value of these minority investments has fluctuated in the past, and substantial appreciation in some of these investments or a decline in our total assets may, from time to time, cause the value of our investment securities to exceed 40% of our total assets. These factors may result in us being treated as an “investment company” under the 1940 Act.

We believe we are primarily engaged in a business other than investing, reinvesting, owning, holding, or trading securities for our account and, therefore, are not an investment company within the meaning of the 1940 Act. However, in the event that the 40% limit were to be exceeded (including through fluctuations in the value of our investment securities), we may need to reduce our investment securities as a percentage of our total assets. This reduction can be attempted in a number of ways, including the sale of investment securities and the acquisition of non-investment security assets, such as cash, cash equivalents and U.S. government securities. If we sell investment securities, we may sell them sooner than we intended. These sales may be at depressed prices and we may never realize anticipated benefits from, or may incur losses on, these investments. Some investments may not be sold due to normal contractual or legal restrictions or the inability to locate a suitable buyer. Moreover, we may incur tax liabilities if we sell these assets. We may also be unable to purchase additional investment securities that may be important to our operating strategy. If we decide to acquire non-investment security assets, we may not be able to identify and acquire suitable assets, and will likely realize a lower return on any such investments.

If we were deemed to be an investment company, we could become subject to substantial regulation under the 1940 Act with respect to our capital structure, management, operations, affiliate transactions and other matters. As a consequence, we could be barred from engaging in business or issuing our securities as we have in the past and might be subject to civil and criminal penalties for noncompliance. In addition, some of our contracts might be voidable, and a court-appointed receiver could take control of us and liquidate our business in certain circumstances.

Risks relating to owning our stock

Our historical quarterly results have fluctuated and do not reliably indicate future operating results

We do not believe that our historical operating results should be relied upon as an indication of our future operating results. We expect to experience large fluctuations in future quarterly operating results that may be caused by many factors, including the following:

- Fluctuations in the fair market value of our equity investments in other companies, including through existing or future private investment funds managed by us,
- Fluctuations in interest rates, which will impact our investment and loan portfolios,
- Changes in trading volume in securities markets,
- The success of, or costs associated with, acquisitions, joint ventures or other strategic relationships,
- Changes in key personnel,
- Seasonal trends,
- Purchases and sales of securities and other assets as part of the Bank’s portfolio restructuring efforts,
- Customer acquisition costs, which may be affected by competitive conditions in the marketplace,
- The timing of introductions or enhancements to online financial services and products by us or our competitors,
- Market acceptance of online financial services and products,
domestic and international regulation of the brokerage, banking and Internet industries,
accounting for derivative instruments and hedging activities,
changes in domestic or international tax rates,
changes in pricing policies by us or our competitors,
fluctuation in foreign exchange rates, and
changes in the level of operating expenses to support projected growth.

We have also experienced fluctuations in the average number of customer transactions per day. Thus, the rate of growth in customer transactions at any given time is not necessarily indicative of future transaction activity.

We have incurred losses in the past and we cannot assure you that we will achieve profitability

We have a long history of incurring operating losses in each fiscal year and we may incur operating losses in the future. We incurred net losses of $402,000 in fiscal 1998 and $56.8 million in fiscal 1999. Although we achieved profitability in fiscal 2000 due in part to sales of investment securities, we cannot assure you that profitability will be sustained.

The market price of our common stock may continue to be volatile which could cause litigation against us and the inability of shareowners to resell their shares at or above the prices at which they acquire them

Since January 1, 2000, the price per share of our common stock has ranged from a high of $15.38 to a low of $5.32. The market price of our common stock has been, and is likely to continue to be, highly volatile and subject to wide fluctuations due to various factors, many of which may be beyond our control, including:

- quarterly variations in operating results,
- volatility in the stock market,
- volatility in the general economy,
- changes in interest rates,
- announcements of acquisitions, technological innovations or new software, services or products by us or our competitors, and
- changes in financial estimates and recommendations by securities analysts.

In addition, there have been large fluctuations in the prices and trading volumes of securities of many technology, Internet and financial services companies. This volatility is often unrelated or disproportionate to the operating performance of these companies. Broad market and industry factors may decrease the market price of our common stock. In the past, volatility in the market price of a company’s securities has often led to securities class action litigation. Such litigation could result in substantial costs to us and divert our attention and resources, which could harm our business. Declines in the market price of our common stock or failure of the market price to increase could also harm our ability to retain key associates, our access to capital and other aspects of our business, which also could harm our business.

We may need additional funds in the future which may not be available and which may result in dilution of the value of our common stock

In the future, we may need to raise additional funds for various purposes, including to expand our technology resources, to hire additional associates, to make acquisitions or to increase the Bank’s total assets or deposit base. Additional financing may not be available on favorable terms, if at all. If adequate funds are not available on acceptable terms, we may be unable to fund our business growth plans. In addition, if funds are available, the result of our issuing securities could be to dilute the value of shares of our common stock and cause the market price to fall.

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

For quantitative and qualitative disclosures about market risk, we have evaluated such risk for our domestic retail brokerage, banking, global and institutional, and asset gathering and other segments separately. The following discussion about our market risk disclosures includes forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements as a result of certain factors, including those set forth in the section entitled “Risk factors” and elsewhere in this filing.

Domestic Retail Brokerage, Global and Institutional, and Asset Gathering and Other

Our domestic retail brokerage, global and institutional, and asset gathering and other operations are exposed to market risk related to changes in interest rates, foreign currency exchange rates and equity security price risk. However, we do not believe any such exposures are material. To reduce certain risks, we utilize derivative financial instruments; however, we do not hold derivative financial instruments for speculative or trading purposes.

Interest Rate Sensitivity

During the quarter ended March 31, 2001, we had a variable rate bank line of credit and three variable rate term loans. As of March 31, 2001, we had no borrowings outstanding under this line of credit and $18.7 million outstanding under these term loans. The line of credit and term loans and the monthly interest payments are subject to interest rate risk. If market interest rates were to increase immediately and uniformly by one percent at March 31, 2001, the interest payments would increase by an immaterial amount.
Foreign Currency Exchange Risk

A portion of our operations consist of brokerage and investment services outside of the United States. As a result, our results of operations could be adversely affected by factors such as changes in foreign currency exchange rates or economic conditions in the foreign markets in which we provide our services. We are primarily exposed to changes in exchange rates on the Japanese yen, the British pound, the Canadian dollar and the Euro. When the U.S. dollar strengthens against these currencies, the U.S. dollar value of non-U.S. dollar-based revenues decreases. When the U.S. dollar weakens against these currencies, the U.S. dollar value of non-U.S. dollar-based revenues increases. Correspondingly, the U.S. dollar value of non-U.S. dollar-based costs increases when the U.S. dollar weakens and decreases when the U.S. dollar strengthens. We are a net payer of British pounds and, as such, benefit from a stronger dollar, and are adversely affected by a weaker dollar relative to the British pound. However, we are a net receiver of currencies other than British pounds, and as such, benefit from a weaker dollar, and are adversely affected by a stronger dollar relative to these currencies. Accordingly, changes in exchange rates may adversely affect our consolidated sales and operating margins as expressed in U.S. dollars.

To mitigate the short-term effect of changes in currency exchange rates on our non-U.S. dollar-based revenues and operating expenses, we routinely hedge our material net non-U.S. dollar-based exposures by entering into foreign exchange forward and option contracts. Currently, hedges of transactions do not extend beyond twelve months and are immaterial. Given the short-term nature of our foreign exchange forward and option contracts, our exposure to risk associated with currency market movement on the instruments is not material.

Equity Price Risk

We have investments in publicly-traded equity securities which, in conjunction with cash provided from operations and financing arrangements, are utilized to meet forecasted liquidity needs. The fair value of these securities at March 31, 2001 was $221.1 million. As a result of significant market volatility during the quarter ended March 31, 2001, the fair value of our equity portfolio was subjected to significant fluctuations. As we account for these securities as available-for-sale, unrealized gains and losses resulting from changes in the fair value of these securities are reflected as a change in shareholders’ equity, and not reflected in the determination of operating results until the securities are sold. Depreciation in the market value of our portfolio impacts our financing strategies which could result in higher interest expense if alternative financing strategies are used. At March 31, 2001, unrealized gains on these securities were $13,000 million and unrealized losses on these securities were $11.6 million.

Financial Instruments

For our working capital and reserves, which are required to be segregated under Federal or other regulations, we primarily invest in money market funds, resale agreements, certificates of deposit, and commercial paper. Money market funds do not have maturity dates and do not present a material market risk. The other financial instruments are fixed rate investments with short maturities and do not present a material interest rate risk.

Banking Operations

We manage our banking related interest rate risk through the use of derivatives such as interest rate cap, swap and floor agreements. We use these instruments to ensure that the market value of equity and net interest income are protected from the impact of changes in interest rates. During the quarter, changes in interest rates, increasing prepayments, portfolio restructurings, and additional hedging activity substantially changed our market risk.

We employ various techniques to implement the asset-liability committee’s strategies directed toward managing the variability of the fair value of equity by controlling the relative sensitivity of market value of interest-earning assets and interest-bearing liabilities. The sensitivity of changes in market value of assets and liabilities is affected by factors, including the level of interest rates, market expectations regarding future interest rates, projected related loan prepayments and the repricing characteristics of interest-bearing liabilities. We use hedging techniques to reduce the variability of fair value of equity and its overall interest rate risk exposure over a one- to seven-year period.

We also monitor our assets and liabilities by examining the extent to which such assets and liabilities are interest rate sensitive and by monitoring the interest rate sensitivity gap. An asset or liability is said to be interest rate sensitive within a specific period if it will mature or reprice within that period. The interest rate sensitivity gap is defined as the difference between the amount of interest-earning assets maturing or repricing within a specific time period and the amount of interest-bearing liabilities maturing or repricing within the same time period. A gap is considered positive when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities and is considered negative when the amount of interest rate sensitive liabilities exceeds the amount of interest rate sensitive assets. Generally, during a period of rising interest rates, a negative gap would adversely affect net interest income, while a positive gap would result in an increase in net interest income.

The following assumptions were used to prepare our gap table at March 31, 2001. Non-amortizing investment securities are shown in the period in which they contractually mature. Investment securities that contain embedded options such as puts or calls are shown in the period in which that security is currently expected to be put or called or to mature. The table assumes that adjustable-rate residential mortgage loans and mortgage-backed securities prepay at an annual rate of between 10% and 40%, based on estimated future prepayment rates for comparable market benchmark securities and the Bank’s prepayment history. The table also assumes that fixed-rate, residential loans and mortgage-backed securities prepay at an annual rate of between 8% and 35%. The above assumptions were applied on a pool-by-pool basis depending on the pools characteristics which include, but are not limited to, the following: product type, coupon rate, rate adjustment frequency, periodic cap, lifetime cap and net coupon reset margin. Time deposits are shown in the period in which they contractually mature, and savings deposits are shown to reprice immediately. The interest rate sensitivity of our assets and liabilities could vary substantially if different assumptions were used or if actual experience differs from the assumptions used.

The following table sets forth our gap at March 31, 2001 (dollars in thousands):

<table>
<thead>
<tr>
<th>Interest-earning banking assets:</th>
<th>Balance at March 31, 2001</th>
<th>Percent of Total</th>
<th>Repricing Within 0-3 Months</th>
<th>Repricing Within 4-12 Months</th>
<th>Repricing Within 1-5 Years</th>
<th>Repricing in More Than 5 Years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loans receivable, net</td>
<td>$ 6,345,377</td>
<td>54.26%</td>
<td>$ 485,201</td>
<td>$1,431,295</td>
<td>$3,656,471</td>
<td>$ 772,410</td>
</tr>
<tr>
<td>Mortgage-backed securities, available-for-sale and trading</td>
<td>3,972,033</td>
<td>33.97%</td>
<td>359,337</td>
<td>813,316</td>
<td>1,877,965</td>
<td>921,415</td>
</tr>
</tbody>
</table>
Investment securities, available-for-sale and FHLB stock

1,327,805 11.35 161,441 149,929 587,111 429,324

Federal funds sold and interest bearing deposits

49,356 0.42 — 9,871 39,485 —

Total interest-earning banking assets

11,694,571 100.00% $1,005,979 $2,404,411 $6,161,032 $2,123,149

Non-interest-earning banking assets

378,842

Total banking assets

$12,073,413

Interest-bearing banking liabilities:

Savings deposits $ 1,279,438 11.75% $ — $ — $ 1,279,438 $ —

Time deposits 5,583,191 51.24 221,675 3,861,950 1,416,375 83,191

FHLB advances 1,887,000 10.89 987,000 — 50,000

Other borrowings 2,846,426 26.12 2,846,426 — — —

Total interest-bearing banking liabilities

10,896,055 100.00% $4,055,101 $3,861,950 $2,845,813 $133,191

Non-interest-bearing banking liabilities

456,828

Total banking liabilities

$11,352,883

As of March 31, 2001, the Bank’s cumulative one-year gap and five-year gap of positive 87.1% and positive 55.9% have increased from negative 12.8% and negative 21.5% as of September 30, 2000. The changes are due largely to additional hedging activity and the shortening of duration of the mortgage assets as a result of lower interest rates and faster prepayment assumptions.

PART II. OTHER INFORMATION

Item 1. Legal and Administrative Proceedings

Reference is made to the information reported in prior filings with the Securities and Exchange Commission under Item 3. Legal and Administrative Proceedings in our Annual Report on Form 10-K, as amended, for the year ended September 30, 2000, and under Part II Item 1. Legal and Administrative Proceedings in our Transition Report on Form 10Q1 for the quarter ended December 31, 2000.

With respect to the putative class action filed in the Superior Court of California, County of Santa Clara, by Eile Wurtman on March 11, 1999, the plaintiff filed her second amended complaint on or about March 21, 2001. On April 3, 2001, we filed our answer to plaintiff’s second amended complaint denying plaintiff’s allegations. At this time, we are unable to predict the ultimate outcome of this proceeding.

From time to time, we have been threatened with, or named as a defendant in, lawsuits, arbitrations and administrative claims involving both securities related and non-securities related matters. We are also subject to periodic regulatory audits and inspections. Compliance and trading problems that are reported to regulators such as the SEC or the NASDR by dissatisfied customers or others are investigated by such regulators, and may, if pursued, result in formal arbitration claims being filed against us by customers and/or disciplinary action being taken against us by regulators. Any such claims or disciplinary actions that are decided against us could have a material adverse effect on our business, financial condition and results of operations. The securities industry is subject to extensive regulation under federal, state and applicable international laws. As a result, we are required to comply with many complex laws and rules and our ability to do so comply is dependent in large part upon the establishment and maintenance of a qualified compliance system.

We maintain insurance in such amounts and with such coverages, deductibles and policy limits as management believes are reasonable and prudent. The principal risks that we insure against are comprehensive general liability, commercial property damage, hardware/software damage, directors and officers, Fidelity (crime) Bond, and errors and omissions liability. We believe that such insurance coverage is adequate for the purpose of our business.

Item 2. Changes in Securities and Use of Proceeds

On February 1, 2001, the Company authorized the issuance of 2,997,951 shares of its common stock in connection with the acquisition of LoansDirect as consideration for all the issued and outstanding capital stock of LoansDirect. No underwriters were involved, and there were no underwriting discounts or commissions. The securities were issued in reliance upon the exemption from registration provided under Section 4(2) of the Securities Act based on the fact that the common stock was sold by the issuer in a transaction not involving a public offering. On March 20, 2001, the Company filed a registration statement with the Securities and Exchange Commission for the resale of these 2,997,951 shares. The registration statement has not yet been declared effective.

On February 22, 2001, the Company authorized the issuance of 191,250 shares of common stock in connection with its acquisition of Confluent, Inc. pursuant to the Agreement and Plan of Reorganization dated September 20, 1999. No underwriters were involved, and there were no underwriting discounts or commissions. The securities were issued in reliance upon the exemption from registration provided under Section 4(2) of the Securities Act based on the fact that the common stock was sold by the issuer in a transaction not involving a public offering.

On March 12, 2001, the Company authorized the issuance of 1,416,586 shares of common stock in connection with the acquisition of E*TRADE Germany AG, as part of the consideration for all of the capital shares of E*TRADE Germany AG. No underwriters were involved, and there were no underwriting discounts or commissions. The securities were issued in reliance upon the exemption from registration provided under Section 4(2) of the
Securities Act based on the fact that the common stock was sold by the issuer in a transaction not involving a public offering. On March 16, 2001, the Company filed a registration statement with the Securities and Exchange Commission for the resale of these 1,416,586 shares. The registration statement has not yet been declared effective.

On March 12, 2001, the Company authorized the issuance of an aggregate of 618,057 shares of unregistered common stock in connection with the acquisition of PrivateAccounts, Inc. (renamed “E*TRADE Advisory Services Inc.” on January 2, 2001). The shares were deposited into escrow pursuant to the terms of the merger agreement as a portion of the consideration for the merger. No underwriters were involved, and there were no underwriting discounts or commissions. The securities were issued in reliance upon the exemption from registration provided under Section 4(2) of the Securities Act based on the fact that the common stock was sold by the issuer in a transaction not involving a public offering. On March 20, 2001, the Bank of New York as escrow agent authorized the release from escrow of 478,500 of the shares of common stock.

On March 14, 2001, the Company authorized the issuance of an aggregate of 78,928 shares of common stock in connection with the acquisition of E*TRADE Nordic AB, referred to in this Form 10-Q as E*TRADE Nordic as consideration for the purchase pursuant to a forward agreement of shares of E*TRADE Nordic held by E*TRADE Nordic shareholders upon the exercise of E*TRADE Nordic stock options held by them. No underwriters were involved and there were no underwriting discounts or commissions. The securities were issued in reliance upon the exemption from registration provided under Section 4(2) of the Securities Act based on the fact that the common stock was sold by the issuer in a transaction not involving a public offering. On April 23, 2001, the Company filed an amended registration statement with the Securities and Exchange Commission for the resale of these 78,928 shares. The registration statement has not yet been declared effective.

Item 3. Defaults Upon Senior Securities—Not applicable.

Item 4. Submission of Matters to a Vote of Security Holders—None

Item 5. Other Information—None

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

<table>
<thead>
<tr>
<th>Exhibit Number</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>*10.1</td>
<td>Form of Stock Pledge Agreement by and between the Company and Charles W. Thomson dated February 28, 2001</td>
</tr>
<tr>
<td>*10.2</td>
<td>Form of Loan, Note and Stock Pledge Agreements by and between the Company and Pamela Kramer dated March 30, 2001</td>
</tr>
<tr>
<td>*10.3</td>
<td>Form of Residential Lease with option to buy entered into between B.R.E. Holdings LLC, a wholly-owned subsidiary of the Company, and each of Jerry Gramaglia and Charles W. Thomson, as lessees</td>
</tr>
</tbody>
</table>

* Filed herewith.

(b) Reports on Form 8-K

On January 19, 2001, the Company filed a Current Report on Form 8-K to report a change in the independent accountants for E*TRADE Financial Corporation, a wholly owned subsidiary of the Company. On January 16, 2001, the Company formally engaged Deloitte & Touche LLP to replace Arthur Andersen as the independent accountants of E*TRADE Financial Corporation.


On January 25, 2001, the Company filed a Current Report on Form 8-K to report a change in the Company’s fiscal year end. On October 25, 2000, the Board of Directors of the Company unanimously approved a resolution delegating to the Company’s Chief Executive Officer the unilateral authority to determine if and/or when the Company’s fiscal year end was to change from September 30. On January 22, 2001, the Chief Executive Officer of the Company decided to change the Company’s fiscal year end from September 30 to December 31.

On February 12, 2001, by filing a Form 8-K/A (Amendment No. 2), the Company amended the Current Report on Form 8-K as previously filed on January 19, 2001 and as amended by Form 8-K/A filed on January 23, 2001. The Form 8-K/A (Amendment No. 2) amends items 4 and 7 to supplement the information provided in those items.

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.

E*TRADE Group, Inc.
(Registrant)

Dated: May 15, 2001
By: /s/ CHRISTOS M. COTSAKOS

Christos M. Cotsakos
Chairman of the Board and Chief Executive Officer
(Principal Executive Officer)

By: /s/ LEONARD C. PURKIS

Leonard C. Purkis
Chief Financial Officer
(Principal Financial and Accounting Officer)
E*TRADE GROUP, INC.

STOCK PLEDGE AGREEMENT

THIS STOCK PLEDGE AGREEMENT is made as of February 28, 2001 by and between E*TRADE Group, Inc., a Delaware corporation (the "Corporation"), and Charles W. Thomson ("Pledgor").

RECITALS

A. In connection with the purchase of residential real estate located at 1850 Brookvale Ave., Hillsborough, CA 94010 (the "Property"), Pledgor has issued that certain promissory note (the "Note") dated May 8, 2000 payable to the order of the Corporation in the principal amount of $4,217,365.63, such Note secured by an interest in the Property.

B. Pledgor has paid the principal amount of $2,899,072.26 on the Note following the sale of the Property and has a balance due on the Note in the principal amount of $1,318,293.37.

C. Pledgor wishes to pledge additional collateral for the balance due on the Note upon the terms set forth in this Agreement.

NOW, THEREFORE, it is hereby agreed as follows:

1. Grant of Security Interest. Pledgor hereby grants the Corporation a security interest in, and assigns, transfers to and pledges with the Corporation, the following securities and other property (collectively, the "Collateral"):

   (i) (a) 50,000 shares of the Corporation's Common Stock issued to Pledgor as restricted stock on January 2, 2001 (denominated "Option No. 00014385"); (b) fully vested options to purchase 100,000 shares of the Corporation's Common Stock granted to Pledgor on April 5, 2000 (denominated "Option No. 00007874"); and (c) fully vested options to purchase 150,000 shares of the Corporation's Common Stock granted to Pledgor on August 23, 2000 (denominated "Option No. 00008236"), (collectively, the "Pledged Shares") which shall be delivered to and/or retained by the Corporation as collateral for the Note;

   (ii) any and all new, additional or different securities or other property subsequently distributed with respect to the Pledged Shares which are to be delivered to and deposited with the Corporation pursuant to the requirements of Paragraph 3 of this Agreement;

   (iii) any and all other property and money which is delivered to or comes into the possession of the Corporation pursuant to the terms of this Agreement; and

   (iv) the proceeds of any sale, exchange or disposition of the property and securities described in subparagraphs (i), (ii) or (iii) above.

2. Warranties. Pledgor hereby warrants that Pledgor is the owner of the Collateral and has the right to pledge the Collateral and that the Collateral is free from all liens, adverse claims and other security interests (other than those created hereby).

3. Duty to Deliver. Any new, additional or different securities or other property (other than regular cash dividends) which may now or hereafter become distributable with respect to the Collateral by reason of (i) any stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the Common Stock as a class without the Corporation's receipt of consideration or (ii) any merger, consolidation or other reorganization affecting the capital structure of the Corporation shall, upon receipt by Pledgor, be promptly delivered to and deposited with the Corporation as part of the Collateral hereunder. Any such securities shall be accompanied by one or more properly-endorsed stock power assignments.

4. Payment of Taxes and Other Charges. Pledgor shall pay, prior to the delinquency date, all taxes, liens, assessments and other charges against the Collateral, and in the event of Pledgor's failure to do so, the Corporation may at its election pay any or all of such taxes and other charges without contesting the validity or legality thereof. The payments so made shall become part of the indebtedness secured hereunder and until paid shall bear interest at the minimum per annum rate, compounded semi-annually, required to avoid the imputation of interest to Pledgor under the Federal tax laws.

5. Stockholder Rights. So long as there exists no event of default under Paragraph 10 of this Agreement, Pledgor may exercise all stockholder voting rights and be entitled to receive any and all regular cash dividends paid on the Collateral and all proxy statements and other stockholder materials pertaining to the Collateral.

6. Rights and Powers of Corporation. The Corporation may, without obligation to do so, exercise at any time and from time to time one or more of the following rights and powers with respect to any or all of the Collateral:

   (i) subject to the applicable limitations of Paragraph 9, accept in its discretion other property of Pledgor in exchange for all or part of the Collateral and release Collateral to Pledgor to the extent necessary to effect such exchange, and in such event the other property received in the exchange shall become part of the Collateral hereunder;

   (ii) perform such acts as are necessary to preserve and protect the Collateral and the rights, powers and remedies granted with respect to such Collateral by this Agreement; and

   (iii) transfer record ownership of the Collateral to the Corporation or its nominee and receive, endorse and give receipt for, or collect by legal proceedings or otherwise, dividends or other distributions made or paid with respect to the Collateral, provided and only if there exists at the time an outstanding event of default under Paragraph 10 of this Agreement. Any cash

sums which the Corporation may so receive shall be applied to the payment of the Note and any other indebtedness secured hereunder, in such order of application as the Corporation deems appropriate. Any remaining cash shall be paid over to Pledgor.
Any action by the Corporation pursuant to the provisions of this Paragraph 6 may be taken without notice to Pledgor. Expenses reasonably incurred in connection with such action shall be payable by Pledgor and form part of the indebtedness secured hereunder as provided in Paragraph 12.

7. Care of Collateral. The Corporation shall exercise reasonable care in the custody and preservation of the Collateral. However, the Corporation shall have no obligation to (i) initiate any action with respect to, or otherwise inform Pledgor of, any conversion, call, exchange right, preemptive right, subscription right, purchase offer or other right or privilege relating to or affecting the Collateral, (ii) preserve the rights of Pledgor against adverse claims or protect the Collateral against the possibility of a decline in market value or (iii) take any action with respect to the Collateral requested by Pledgor unless the request is made in writing and the Corporation determines that the requested action will not unreasonably jeopardize the value of the Collateral as security for the Note and other indebtedness secured hereunder.

Subject to the limitations of Paragraph 9, the Corporation may at any time release and deliver all or part of the Collateral to Pledgor, and the receipt thereof by Pledgor shall constitute a complete and full acquittance for the Collateral so released and delivered. The Corporation shall accordingly be discharged from any further liability or responsibility for the Collateral, and the released Collateral shall no longer be subject to the provisions of this Agreement.

8. Transfer of Collateral. In connection with the transfer or assignment of the Note (whether by negotiation, discount or otherwise), the Corporation may transfer all or any part of the Collateral, and the transferee shall thereupon succeed to all the rights, powers and remedies granted the Corporation hereunder with respect to the Collateral so transferred. Upon such transfer, the Corporation shall be fully discharged from all liability and responsibility for the transferred Collateral.

9. Release of Collateral. Provided all indebtedness secured hereunder (other than payments not yet due and payable under the Note) shall at the time have been paid in full and there does not otherwise exist any event of default under Paragraph 10, the Pledged Shares, together with any additional Collateral which may hereafter be pledged and deposited hereunder, shall be released from pledge and returned to Pledgor in accordance with the following provisions:

(i) Upon payment or prepayment of principal under the Note, together with payment of all accrued interest to date on the principal amount so paid or prepaid, one or more of the Pledged Shares held as Collateral hereunder shall (subject to the applicable limitations of Paragraphs 9(iii) and 9(v) below) be released at the time of such payment or prepayment. The number of the shares to be so released shall be equal to the number obtained by multiplying

(i) the total number of Pledged Shares held under this Agreement at the time of the payment or prepayment, by (ii) a fraction, the numerator of which shall be the amount of the principal paid or prepaid and the denominator of which shall be the unpaid principal balance of the Note immediately prior to such payment or prepayment. In no event, however, shall any fractional shares be released.

(ii) Any additional Collateral which may hereafter be pledged and deposited with the Corporation (pursuant to the requirements of Paragraph 3) with respect to the Pledged Shares shall be released at the same time the particular shares of Common Stock to which the additional Collateral relates are to be released in accordance with the applicable provisions of Paragraph 9(i) or 9(vi).

(iii) Under no circumstances, however, shall any Pledged Shares or any other Collateral be released if previously applied to the payment of any indebtedness secured hereunder. In addition, in no event shall any Pledged Shares or other Collateral be released pursuant to the provisions of Paragraph 9(i), 9(ii) or 9(v) if, and to the extent, the fair market value of the Common Stock and all other Collateral which would otherwise remain in pledge hereunder after such release were effected would be less than the unpaid principal and accrued interest under the Note.

(iv) For all valuation purposes under this Agreement, the fair market value per share of Common Stock on any relevant date shall be determined in accordance with the following provisions:

(A) If the Common Stock is at the time traded on the Nasdaq National Market, the fair market value shall be the average of the high and low selling prices per share of Common Stock on the date in question, as such prices are reported by the National Association of Securities Dealers on the Nasdaq National Market. If there is no average of the high and low selling prices for the Common Stock on the date in question, then the average of the high and low selling prices on the last preceding date for which such quotation exists shall be determinative of fair market value.

(B) If the Common Stock is at the time listed on the American Stock Exchange or the New York Stock Exchange, then the fair market value shall be the average of the high and low selling prices selling per share of Common Stock on the date in question on the securities exchange serving as the primary market for the Common Stock, as such prices are officially quoted in the composite tape of transactions on such exchange. If there is no average of the high and low selling prices of Common Stock on such exchange on the date in question, then the fair market value shall be the average of the high and low selling prices on the exchange on the last preceding date for which such quotation exists.

(C) If the Common Stock is at the time neither listed on any securities exchange nor traded on the Nasdaq National Market, the fair market value shall be determined by the Corporation's Board of Directors after taking into account such factors as the Board shall deem appropriate.

(v) So long as the Collateral is in whole or in part comprised of "margin stock" within the meaning of Section 221.2 of Regulation U of the Federal Reserve Board, then no Collateral shall be substituted for any Collateral under the provisions of Paragraph 6(i) or be released under Paragraph 9(i), 9(ii) or 9(vi), unless there is compliance with each of the following additional requirements:
(A) The substitution or release must not increase the amount by which the indebtedness secured hereunder at the time of such substitution or release exceeds the maximum loan value (as defined below) of the Collateral immediately prior to such substitution or release.

(B) The substitution or release must not cause the amount of indebtedness secured hereunder at the time of such substitution or release to exceed the maximum loan value of the Collateral remaining after such substitution or release is effected.

(C) For purposes of this Paragraph 9(v), the maximum loan value of each item of Collateral shall be determined on the day the substitution or release is to be effected and shall, in the case of the shares of Common Stock and any additional Collateral (other than margin stock), equal the good faith loan value thereof (as defined in Section 221.2 of Regulation U) and shall, in the case of all margin stock (other than the Common Stock), equal fifty percent (50%) of the current market value of such margin stock.

(vi) The Compensation Committee of the Corporation's Board of Directors shall have the discretion, exercisable upon such terms and conditions as the Compensation Committee deems advisable, to authorize the release of one or more shares of Common Stock from pledge hereunder in the event the maximum loan value of the Collateral pledged hereunder (as such value is determined pursuant to subparagraph 9(v)(C)) should substantially exceed the outstanding indebtedness at the time secured hereunder. Any such release of the pledged shares of Common Stock shall, however, be effected in compliance with the requirements of subparagraphs (iii) and (v) of this Paragraph 9.

10. **Events of Default.** The occurrence of one or more of the following events shall constitute an event of default under this Agreement:

(i) the failure of Pledgor to pay, when due under the Note, any installment of principal or accrued interest; or

(ii) the occurrence of any other acceleration event specified in the Note; or

(iii) the failure of Pledgor to perform any obligation imposed upon Pledgor by reason of this Agreement; or

(iv) the breach of any warranty of Pledgor contained in this Agreement.

Upon the occurrence of any such event of default, the Corporation may, at its election, declare the Note and all other indebtedness secured hereunder to become immediately due and payable and may exercise any or all of the rights and remedies granted to a secured party under the provisions of the California Uniform Commercial Code (as now or hereafter in effect), including (without limitation) the power to dispose of the Collateral by public or private sale or to accept the Collateral in full payment of the Note and all other indebtedness secured hereunder.

Any proceeds realized from the disposition of the Collateral pursuant to the foregoing power of sale shall be applied first to the payment of expenses incurred by the Corporation in connection with the disposition, then to the payment of the Note and finally to any other indebtedness secured hereunder. Any surplus proceeds shall be paid over to Pledgor. However, in the event such proceeds prove insufficient to satisfy all obligations of Pledgor under the Note, then Pledgor shall remain personally liable for the resulting deficiency.

11. **Other Remedies.** The rights, powers and remedies granted to the Corporation pursuant to the provisions of this Agreement shall be in addition to all rights, powers and remedies granted to the Corporation under any statute or rule of law. Any forbearance, failure or delay by the Corporation in exercising any right, power or remedy under this Agreement shall not be deemed to be a waiver of such right, power or remedy. Any single or partial exercise of any right, power or remedy under this Agreement shall not preclude the further exercise thereof, and every right, power and remedy of the Corporation under this Agreement shall continue in full force and effect unless such right, power or remedy is specifically waived by an instrument executed by the Corporation.

12. **Costs and Expenses.** All costs and expenses (including reasonable attorneys fees) incurred by the Corporation in the exercise or enforcement of any right, power or remedy granted it under this Agreement shall become part of the indebtedness secured hereunder and shall constitute a personal liability of Pledgor payable immediately upon demand and bearing interest until paid at the minimum per annum rate, compounded semi-annually, required to avoid the imputation of interest income to the Corporation and compensation income to Pledgor under the Federal tax laws.

13. **Applicable Law.** This Agreement shall be governed by and construed in accordance with the laws of the State of California without resort to that State's conflict-of-laws rules.

14. **Successors.** This Agreement shall be binding upon the Corporation and its successors and assigns and upon Pledgor and the executors, heirs and legateses of Pledgor's estate.

15. **Severability.** If any provision of this Agreement is held to be invalid under applicable law, then such provision shall be ineffective only to the extent of such invalidity, and neither the remainder of such provision nor any other provisions of this Agreement shall be affected thereby.

**IN WITNESS WHEREOF,** this Agreement has been executed by Pledgor and the Corporation on this 28th day of February, 2001.

/s/ Charles W. Thomson

Charles W. Thomson, Pledgor
AGREED TO AND ACCEPTED BY:

E*TRADE GROUP, INC.

By: /s/ Christos M. Cotsakos
Title: Chief Executive Officer
Dated: February 28, 2001

ASSIGNMENT SEPARATE FROM CERTIFICATE

FOR VALUE RECEIVED, ______________ hereby sells, assigns and transfers unto E*TRADE Group, Inc. (the "Corporation"), __________(__) shares of the Common Stock of the Corporation standing in his name on the books of the Corporation represented by Certificate No. herewith and does hereby irrevocably constitute and appoint Attorney to transfer the said stock on the books of the Corporation with full power of substitution in the premises.

Dated: __________

Signature: /s/ Charles W. Thomson
Charles W. Thomson

Instruction: Please do not fill in any blanks other than the signature line. Please sign exactly as you would like your name to appear on the issued stock certificate.
LOAN AGREEMENT

This Loan Agreement ("Agreement") is made effective this 30th day of March, 2001, by and between Pamela Kramer ("Borrower") and E*TRADE Group, Inc., a Delaware corporation ("Lender"), with reference to the following:

A. Borrower, an executive employee of Lender, desires to borrow from Lender and Lender is willing to loan to Borrower the principal amount of One Hundred Thousand Dollars ($100,000) upon the terms set forth herein.

NOW, THEREFORE, in consideration of the foregoing, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Borrower and Lender agree as follows:

1. **Loan Agreement.** Subject to the terms and conditions of this Agreement, and in reliance upon the representations and warranties of Borrower set forth in this Agreement, Lender agrees to make to Borrower, and Borrower agrees to accept from Lender, a loan (the "Loan") in the principal amount of One Hundred Thousand Dollars ($100,000).

2. **Loan Terms.** The Loan shall be evidenced by a Promissory Note in the form of Exhibit A to this Agreement (the "Note") and the related Stock Pledge Agreement executed by Borrower on this date (the "Stock Pledge Agreement"). The Loan shall bear interest at the rate per annum specified in the Note and Borrower shall pay the Note in accordance with the terms thereof.

3. **Notices.** All notices, requests, demands, and other communications required or permitted to be given under this Agreement shall be in writing and shall be sent by United States mail, postage prepaid, certified return receipt requested, or by personal delivery, or by overnight courier, addressed to the other party as set forth below or at such other places as may be designated in notice to the other party given as hereinbefore. Notice shall be deemed effective upon delivery of notice as set forth above, or on the third day following deposit in the United States mail in the manner described above.

   **Borrower:**
   Pamela Kramer
   519 Placitas Ave.
   Menlo Park, CA 94025

   **Lender:**
   E*TRADE Group, Inc.
   4500 Bohannon Drive
   Menlo Park, CA 94025
   Attention: Theodore J. Theophilos

4. **Loan Not to Affect Employment.** Borrower agrees and understands that nothing in this Agreement shall confer any right with respect to the termination of her employment with Lender or any of its subsidiaries, nor shall this Agreement interfere in any way with her right or Lender's right to terminate her employment at any time, with or without cause, in accordance with the Management Continuity Agreement dated October 25, 2000, between Borrower and Lender (the "Employment Agreement").

5. **Acceleration.** The amount of all advances of principal and all interest accrued under the Note shall become immediately due and payable within thirty (30) calendar days following any termination of Borrower's employment by Lender.

6. **Entire Agreement.** The foregoing, including the Promissory Note and the Stock Pledge Agreement, constitutes the entire agreement between the parties relating to the Loan and may be modified only by writing signed by Borrower and Lender. There are no agreements, representations, or warranties between the parties with regard to the Loan other than those expressly set forth in this Agreement and the Employment Agreement.

7. **Representation of the Parties.** Borrower acknowledges that (i) she has been advised by attorneys for Lender to consult with her separate legal, tax and financial counsel about the terms of this Loan, including but not limited to the tax effects of any forgiveness of principal or interest due under the Note, and (ii) she has had an adequate opportunity to consult with such separate counsel before executing this Agreement.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first written above.

   **Borrower:**
   Pamela Kramer
   _/s/ Pamela Kramer_

   **Lender:**
   E*TRADE Group, Inc.
   _/s/ Christos M. Cotsakos_
   By
   Christos M. Cotsakos
   Chairman and Chief Executive Officer

EXHIBIT A

FORM OF PROMISSORY NOTE

PROMISSORY NOTE

$100,000.00

For value received, Pamela Kramer ("Borrower") promises to pay to the order of E*TRADE Group, Inc., a Delaware corporation ("Lender"), the principal sum of One Hundred Thousand Dollars ($100,000.00) (the "Principal"), in lawful money of the United States of America, with interest thereon to be computed from date of the funding of this Note at the Interest Rate defined below, in accordance with the terms of this Note. The place of payment shall be 4500 Bohannon Drive, Menlo Park, Calif., or at such other place as the holder of this Note may from time to time require.

Accrued interest on this Note shall be due and payable on March 30, 2002, with the entire principal balance of this Note, together with any remaining accrued and unpaid interest due and payable on March 30, 2003 (the "Maturity Date"), except as expressly provided in this Note and that certain Loan Agreement between Borrower and Lender of even date herewith (the "Loan Agreement").
The term Interest Rate as used in this Note shall mean a rate of interest equal to four and eighty-six hundredths percent (4.86%) per annum, compounded and paid annually. All computations of interest shall be made on the basis of a year of 360 days for the actual number of days occurring in the period for which such interest is payable.

Payment of this Note shall be secured by a pledge of Borrower's interest in to be executed this date by Borrower. Borrower, however, shall remain personally liable for payment of this Note, and assets of the Borrower, in addition to the collateral under the Unit Pledge Agreement, may be applied to the satisfaction of Borrower's obligations hereunder.

All amounts payable under this Note are payable in lawful money of the United States. Checks constitute payment only when collected. This Note may be prepaid, in whole or in part, without penalty.

This Note is subject to the terms and conditions of the Loan Agreement, which, among other things, contains provisions for acceleration of the maturity of this Note.

This Note is governed by the laws of the State of California.

If Lender delays in exercising or fails to exercise any of its rights under this Note, that delay or failure shall not constitute a waiver of any of Lender's rights, or of any breach, default or failure of condition of or under this Note. No waiver by Lender of any of its rights, or of any such breach, default or failure of condition shall be effective, unless the waiver is expressly stated in a writing signed by Lender.

Notwithstanding anything to the contrary contained in this Note or the Loan Agreement, the interest rate applicable to this Loan and each advance hereunder shall be not less than the Applicable Federal Rate set by the U.S. Treasury for determining below market loans pursuant to Section 7872 of the Internal Revenue Code of 1986, as now in effect (the "Internal Revenue Code"). This Loan is not intended as a "below market loan" as such term is used in Section 7872 of the Internal Revenue Code, or any comparable applicable state tax law ("Below Market Loan"). The parties hereby agree that if any court or governmental taxing authority having jurisdiction over Borrower or Lender shall determine that this Loan is a Below Market Loan, the interest rate payable under this Note shall then be increased to the extent necessary to remove this Loan from any otherwise applicable definition of a Below Market Loan.

This Note inures to and binds the heirs, legal representatives, successors and permitted assigns of Borrower and Lender; provided, however, that Borrower may not assign this Note or any Loan funds, or assign or delegate any of his rights or obligations hereunder, without the prior written consent of Lender in each instance. Lender in its sole discretion may transfer this Note on the terms and subject to the conditions of the Loan Agreement, without the consent of Borrower.

IN WITNESS WHEREOF, Borrower has duly executed and delivered this Note to Lender as of the date first above written.

Borrower: /s/ Pamela Kramer

E*TRADE GROUP, INC.

STOCK PLEDGE AGREEMENT

THIS STOCK PLEDGE AGREEMENT is made effective as of March 30, 2001 by and between E*TRADE Group, Inc., a Delaware corporation (the "Corporation"), and Pamela Kramer ("Pledgor").

RECEALS

A. The Corporation has made a loan to Pledgor in the principal amount of One Hundred Thousand Dollars ($100,000.00) as evidenced by the Loan Agreement and Promissory Note executed herewith (the "Note").

B. Pledgor wishes to pledge her interest in certain shares of common stock of the Corporation upon the terms set forth in this Agreement.

NOW, THEREFORE, it is hereby agreed as follows:

1. Grant of Security Interest. Pledgor hereby grants the Corporation a security interest in, and assigns, transfers to and pledges with the Corporation, the following securities and other property (collectively, the "Collateral"): (i) 40,000 shares of the Corporation's Common Stock currently held in the name of Pledgor, (the "Pledged Shares") which shall be delivered to and deposited with the Corporation as collateral for the Note; (ii) any and all new, additional or different securities or other property subsequently distributed with respect to the Pledged Shares which are to be delivered to and deposited with the Corporation pursuant to the requirements of Paragraph 3 of this Agreement; (iii) any and all other property and money which is delivered to or comes into the possession of the Corporation pursuant to the terms of this Agreement; and (iv) the proceeds of any sale, exchange or disposition of the property and securities described in subparagraphs (i), (ii) or (iii) above.

2. Warranties. Pledgor hereby warrants that Pledgor is the owner of the Collateral and has the right to pledge the Collateral and that the Collateral is free from all liens, adverse claims and other security interests (other than those created hereby).

3. Duty to Deliver. Any new, additional or different securities or other property (other than regular cash dividends) which may now or hereafter become distributable with respect to the Collateral by reason of (i) any stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the Common Stock as a class without the Corporation's receipt of consideration or (ii) any merger, consolidation or other reorganization affecting the capital structure of the Corporation shall, upon receipt by Pledgor, be promptly delivered to and deposited with the Corporation.
as part of the Collateral hereunder. Any such securities shall be accompanied by one or more properly-endorsed stock power assignments.

4. **Payment of Taxes and Other Charges.** Pledgor shall pay, prior to the delinquency date, all taxes, liens, assessments and other charges against the Collateral, and in the event of Pledgor's failure to do so, the Corporation may at its election pay any or all of such taxes and other charges without contesting the validity or legality thereof. The payments so made shall become part of the indebtedness secured hereunder and until paid shall bear interest at the minimum per annum rate, compounded semi-annually, required to avoid the imputation of interest income to the Corporation and compensation income to Pledgor under the Federal tax laws.

5. **Stockholder Rights.** So long as there exists no event of default under Paragraph 10 of this Agreement, Pledgor may exercise all stockholder voting rights and be entitled to receive any and all regular cash dividends paid on the Collateral and all proxy statements and other stockholder materials pertaining to the Collateral.

6. **Rights and Powers of Corporation.** The Corporation may, without obligation to do so, exercise at any time and from time to time one or more of the following rights and powers with respect to any or all of the Collateral:

(i) subject to the applicable limitations of Paragraph 9, accept in its discretion other property of Pledgor in exchange for all or part of the Collateral and release Collateral to Pledgor to the extent necessary to effect such exchange, and in such event the other property received in the exchange shall become part of the Collateral hereunder;

(ii) perform such acts as are necessary to preserve and protect the Collateral and the rights, powers and remedies granted with respect to such Collateral by this Agreement; and

(iii) transfer record ownership of the Collateral to the Corporation or its nominee and receive, endorse and give receipt for, or collect by legal proceedings or otherwise, dividends or other distributions made or paid with respect to the Collateral, provided and only if there exists at the time an outstanding event of default under Paragraph 10 of this Agreement. Any cash sums which the Corporation may so receive shall be applied to the payment of the Note and any other indebtedness secured hereunder, in such order of application as the Corporation deems appropriate. Any remaining cash shall be paid over to Pledgor.

Any action by the Corporation pursuant to the provisions of this Paragraph 6 may be taken without notice to Pledgor. Expenses reasonably incurred in connection with such action shall be payable by Pledgor and form part of the indebtedness secured hereunder as provided in Paragraph 12.

7. **Care of Collateral.** The Corporation shall exercise reasonable care in the custody and preservation of the Collateral. However, the Corporation shall have no obligation to (i) initiate any action with respect to, or otherwise inform Pledgor of, any conversion, call, exchange right, preemptive right, subscription right, purchase offer or other right or privilege relating to or affecting the Collateral, (ii) preserve the rights of Pledgor against adverse claims or protect the Collateral against the possibility of a decline in market value or (iii) take any action with respect to the Collateral requested by Pledgor unless the request is made in writing and the Corporation determines that the requested action will not unreasonably jeopardize the value of the Collateral as security for the Note and other indebtedness secured hereunder.

Subject to the limitations of Paragraph 9, the Corporation may at any time release and deliver all or part of the Collateral to Pledgor, and the receipt thereof by Pledgor shall constitute a complete and full acquittance for the Collateral so released and delivered. The Corporation shall accordingly be discharged from any further liability or responsibility for the Collateral, and the released Collateral shall no longer be subject to the provisions of this Agreement.

8. **Transfer of Collateral.** In connection with the transfer or assignment of the Note (whether by negotiation, discount or otherwise), the Corporation may transfer all or any part of the Collateral, and the transferee shall thereupon succeed to all the rights, powers and remedies granted the Corporation hereunder with respect to the Collateral so transferred. Upon such transfer, the Corporation shall be fully discharged from all liability and responsibility for the transferred Collateral.

9. **Release of Collateral.** Provided all indebtedness secured hereunder (other than payments not yet due and payable under the Note) shall at the time have been paid in full and there does not otherwise exist any event of default under Paragraph 10, the Pledged Shares, together with any additional Collateral which may hereafter be pledged and deposited hereunder, shall be released from pledge and returned to Pledgor in accordance with the following provisions:

(i) Upon payment or prepayment of principal under the Note, together with payment of all accrued interest to date on the principal amount so paid or prepaid, one or more of the Pledged Shares held as Collateral hereunder shall (subject to the applicable limitations of Paragraphs 9(iii) and 9(iv) below) be released at the time of such payment or prepayment. The number of the shares to be so released shall be equal to the number obtained by multiplying (i) the total number of Pledged Shares held under this Agreement at the time of the payment or prepayment, by (ii) a fraction, the numerator of which shall be the amount of the principal paid or prepaid and the denominator of which shall be the unpaid principal balance of the Note immediately prior to such payment or prepayment. In no event, however, shall any fractional shares be released.

(ii) Any additional Collateral which may hereafter be pledged and deposited with the Corporation (pursuant to the requirements of Paragraph 3) with respect to the Pledged Shares shall be released at the same time the particular shares of Common Stock to which the additional Collateral relates are to be released in accordance with the applicable provisions of Paragraph 9(i) or 9(vi).

(iii) Under no circumstances, however, shall any Pledged Shares or any other Collateral be released if previously applied to the payment of any indebtedness secured hereunder. In addition, in no event shall any Pledged Shares or other Collateral be released pursuant to the provisions of Paragraph 9(iii) or 9(vi) if, and to the extent, the fair market value of the Common Stock and all other Collateral which would otherwise remain in pledge hereunder after such release were effected would be less than the unpaid principal and accrued interest under the Note.
(iv) For all valuation purposes under this Agreement, the fair market value per share of Common Stock on any relevant date shall be determined in accordance with the following provisions:

(A) If the Common Stock is at the time traded on the Nasdaq National Market, the fair market value shall be the average of the high and low selling prices per share of Common Stock on the date in question, as such prices are reported by the National Association of Securities Dealers on the Nasdaq National Market. If there is no average of high and low selling prices for the Common Stock on the date in question, then the average of the high and low selling prices on the last preceding date for which such quotation exists shall be determinative of fair market value.

(B) If the Common Stock is at the time listed on the American Stock Exchange or the New York Stock Exchange, then the fair market value shall be the average of the high and low selling prices selling prices per share of Common Stock on the date in question on the securities exchange serving as the primary market for the Common Stock, as such prices are officially quoted in the composite tape of transactions on such exchange. If there is no average of the high and low selling prices of Common Stock on such exchange on the date in question, then the fair market value shall be the average of the high and low selling prices on the exchange on the last preceding date for which such quotation exists.

(C) If the Common Stock is at the time neither listed on any securities exchange nor traded on the Nasdaq National Market, the fair market value shall be determined by the Corporation's Board of Directors after taking into account such factors as the Board shall deem appropriate.

(v) So long as the Collateral is in whole or in part comprised of "margin stock" within the meaning of Section 221.2 of Regulation U of the Federal Reserve Board, then no Collateral shall be substituted for any Collateral under the provisions of Paragraph 6(i) or be released under Paragraph 9(ii), 9(iii) or 9(vi), unless there is compliance with each of the following additional requirements:

(A) The substitution or release must not increase the amount by which the indebtedness secured hereunder at the time of such substitution or release exceeds the maximum loan value (as defined below) of the Collateral immediately prior to such substitution or release.

(B) The substitution or release must not cause the amount of indebtedness secured hereunder at the time of such substitution or release to exceed the maximum loan value of the Collateral remaining after such substitution or release is effected.

(C) For purposes of this Paragraph 9(v), the maximum loan value of each item of Collateral shall be determined on the day the substitution or release is to be effected and shall, in the case of the shares of Common Stock and any additional Collateral (other than margin stock), equal the good faith loan value thereof (as defined in Section 221.2 of Regulation U) and shall, in the case of all margin stock (other than the Common Stock), equal fifty percent (50%) of the current market value of such margin stock.

(vi) The Compensation Committee of the Corporation's Board of Directors shall have the discretion, exercisable upon such terms and conditions as the Compensation Committee deems advisable, to authorize the release of one or more shares of Common Stock from pledge hereunder in the event the maximum loan value of the Collateral pledged hereunder (as such value is determined pursuant to subparagraph 9(v)(C)) should substantially exceed the outstanding indebtedness at the time secured hereunder. Any such release of the pledged shares of Common Stock shall, however, be effected in compliance with the requirements of subparagraphs (iii) and (v) of this Paragraph 9.

10. **Events of Default.** The occurrence of one or more of the following events shall constitute an event of default under this Agreement:

   (i) the failure of Pledgor to pay, when due under the Note, any installment of principal or accrued interest; or

   (ii) the occurrence of any other acceleration event specified in the Note; or

   (iii) the failure of Pledgor to perform any obligation imposed upon Pledgor by reason of this Agreement; or

   (vi) the breach of any warranty of Pledgor contained in this Agreement.

Upon the occurrence of any such event of default, the Corporation may, at its election, declare the Note and all other indebtedness secured hereunder to become immediately due and payable and may exercise any or all of the rights and remedies granted to a secured party under the provisions of the California Uniform Commercial Code (as now or hereafter in effect), including (without limitation) the power to dispose of the Collateral by public or private sale or to accept the Collateral in full payment of the Note and all other indebtedness secured hereunder.

Any proceeds realized from the disposition of the Collateral pursuant to the foregoing power of sale shall be applied first to the payment of expenses incurred by the Corporation in connection with the disposition, then to the payment of the Note and finally to any other indebtedness secured hereunder. Any surplus of proceeds shall be paid over to Pledgor. However, in the event such proceeds prove insufficient to satisfy all obligations of Pledgor under the Note, then Pledgor shall remain personally liable for the resulting deficiency.

11. **Other Remedies.** The rights, powers and remedies granted to the Corporation pursuant to the provisions of this Agreement shall be in addition to all rights, powers and remedies granted to the Corporation under any statute or rule of law. Any forbearance, failure or delay by the Corporation in exercising any right, power or remedy under this Agreement shall not be deemed to be a waiver of such right, power or remedy. Any single or partial exercise of any right, power or remedy under this Agreement shall not preclude the further exercise thereof, and every right, power and remedy of the Corporation under this Agreement shall continue in full force and effect unless such right, power or remedy is specifically waived by an instrument executed by the Corporation.

12. **Costs and Expenses.** All costs and expenses (including reasonable attorneys' fees) incurred by the Corporation in the exercise or enforcement of any right, power or remedy granted it under this Agreement shall become part of the indebtedness secured hereunder and shall constitute a personal liability of Pledgor payable immediately upon demand and bearing interest until paid at the minimum per annum rate, compounded semi-annually, required to avoid the imputation of interest income to the Corporation and compensation income to Pledgor under the Federal tax laws.
13. **Applicable Law.** This Agreement shall be governed by and construed in accordance with the laws of the State of California without resort to that State's conflict-of-laws rules.

14. **Successors.** This Agreement shall be binding upon the Corporation and its successors and assigns and upon Pledgor and the executors, heirs and legatees of Pledgor's estate.

15. **Severability.** If any provision of this Agreement is held to be invalid under applicable law, then such provision shall be ineffective only to the extent of such invalidity, and neither the remainder of such provision nor any other provisions of this Agreement shall be affected thereby.

**IN WITNESS WHEREOF,** this Agreement has been executed by Pledgor and the Corporation on this 30th day of March, 2001.

<table>
<thead>
<tr>
<th>Pamela Kramer, Pledgor</th>
</tr>
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<tbody>
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<td>Address:</td>
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**AGREED TO AND ACCEPTED BY:**

**E*TRADE GROUP, INC.**

By:  
Title:  
Dated: March 30, 2001

**ASSIGNMENT SEPARATE FROM CERTIFICATE**

FOR VALUE RECEIVED, _________ hereby sells, assigns and transfers unto E*TRADE Group, Inc. (the "Corporation"), _________ (____) shares of the Common Stock of the Corporation standing in his name on the books of the Corporation represented by Certificate No. _________ herewith and does hereby irrevocably constitute and appoint _________ Attorney to transfer the said stock on the books of the Corporation with full power of substitution in the premises.

Dated: ___________________________  Signature: ___________________________

Pamela Kramer

**Instruction:** Please do not fill in any blanks other than the signature line. Please sign exactly as your name appears on the issued stock certificate.
RESIDENTIAL LEASE

This Residential Lease is made and entered into by and between [Tenant] ("Tenant") and B.R.E. Holdings LLC, a California limited liability company ("Owner") as of [date], with respect to the premises situated in the City of [ ], California, described as [address] (the "Premises").

Tenant and Owner agree to lease the Premises upon the following terms and conditions:

1. TERM: The term ("Term") will commence on [date] and continue until the earlier to occur of (i) [one year from date of lease], or (ii) the date of termination of employment of [employee] by E*TRADE Group, Inc., a Delaware corporation, or any of its subsidiaries ("E*TRADE"). The Term may be extended in accordance with paragraph 21 below.

2. RENT: Rent will be $[_________] per month ("Rent"), payable in advance, upon the first day of each calendar month to Owner or its authorized agent, at 10951 White Rock Road, Rancho Cordova, California 95670 (Attn: Ryan Stroub), or at such other places as may be designated by Owner from time to time.

3. UTILITIES: Tenant will be responsible for the payment of all utilities and services to the Premises.

4. USE: The Premises will be used exclusively as a residence.

5. ORDINANCES AND STATUTES: Tenant will comply with all statutes, ordinances, and requirements of all municipal, state and federal authorities now in force, or which may later be in force, regarding the premises.

6. ASSIGNMENT AND SUBLETTING: Tenant will not assign this Lease or sublet any portion of the Premises. This provision is intended to be an absolute prohibition on Tenant's transfer of this Lease or any interest therein. The option rights of Tenant, as provided in paragraphs 21 and 22 below, are personal to Tenant and may not be transferred to any other party.

7. MAINTENANCE, REPAIRS, OR ALTERATIONS: Tenant acknowledges that the Premises are in good order and repair, unless otherwise indicated. Tenant will, at his or her own expense, maintain the Premises in good repair and in a clean and sanitary manner including all equipment, appliances, smoke detectors, plumbing, heating and air conditioning, and will surrender the same, at termination, in as good condition as received, normal wear and tear excepted. Tenant will be responsible for damages caused by his or her negligence and that of his or her family, invitees, and guests. Tenant will not paint, paper or otherwise redecorate or make alterations to the Premises without the prior written consent of the Owner. Tenant will irrigate and maintain the grounds of the Premises, including lawns, trees and shrubbery. Tenant will not commit any waste or nuisance upon the Premises.

8. INVENTORY: The following furnishings and/or equipment are to be furnished by Owner: refrigerator, oven, microwave, dishwasher, trash compactor, and garage door openers. Tenant will keep such furnishings and equipment in good condition and repair, and will be responsible for any damage to them other than normal wear and tear.

9. DAMAGE TO PREMISES: If the Premises are damaged by fire or from any other cause which renders the Premises untenantable, either party will have the right to terminate this Lease as of the date on which the damage occurs. Written notice of termination will be given to the other party within fifteen days after occurrence of such damage. Should such damage or destruction occur as the result of the negligence of Tenant, or his or her invitees, then only the Owner will have the right to terminate. Should this right be exercised by either Owner or Tenant, then Rent for the current month will be prorated between the parties as of the date the damage occurred. If this Lease is not terminated, then Owner will promptly repair the Premises and there will be a proportionate reduction of Rent until the Premises are repaired and ready for Tenant's occupancy. Such proportionate reduction will be based on the extent which repairs interfere with Tenant's reasonable use of the Premises.

10. ENTRY AND INSPECTION: Owner will have the right to enter the Premises: (a) in case of emergency; (b) to make necessary or agreed repairs, decorations, alterations, improvements, supply necessary or agreed services, show the Premises to prospective or actual buyers, lenders, tenants, workers or contractors; and (c) when Tenant has abandoned or surrendered the Premises. Except under (a) and (c), entry may be made only during normal business hours, and with at least twenty-four (24) hours' prior notice to Tenant.

11. INDEMNIFICATION: Owner will not be liable for any damage or injury to Tenant, or any other person, or to any property, occurring on the Premises, unless such damage is the legal result of the negligence or willful misconduct of Owner, its agents, or employees. Tenant agrees to hold Owner harmless from any claims for damages, no matter how caused, except for injury or damages caused by negligence or willful misconduct of Owner, its agents or employees. It is understood that Owner's insurance does not cover Tenant's personal property or improvements.

12. PHYSICAL POSSESSION: If Owner is unable to deliver possession of the Premises at the commencement date of the Term, as set forth above, Owner will not be liable for any damage caused, nor will this Lease be void or voidable, but Tenant will not be liable for any Rent until possession is delivered.

13. DEFAULT: If Tenant fails to pay Rent when due, or perform any provision of this Lease, after not less than three (3) days written notice of such default is given in the manner required by law, the Owner, at its option, may terminate all rights of Tenant, unless Tenant, within said time, cures such default. If Tenant abandons or vacates the Premises while in default of this Lease, Owner may consider any property left on the Premises to be abandoned and may dispose of the same in any manner allowed by law. In the event that Owner reasonably believes that such abandoned property has no value, it may be discarded.

14. WAIVER: Failure of Owner to enforce any provision of this Lease will not be deemed a waiver. The acceptance of Rent by Owner will not waive its right to enforce any provision of this Lease.

15. NOTICES: Unless otherwise provided, any notice which either party may give or is required to give shall be in writing and shall be sent by United States mail, postage prepaid, certified, or by personal delivery, or by overnight courier, addressed to Tenant at the Premises or to Owner at the address shown below or at such other places as may be designated in notice to the other party given as provided herein. Notice will be deemed effective upon actual receipt, if personally delivered, one business day following deposit with Federal Express or other reputable overnight courier that provides a receipt, or on the third day following deposit in the United States mail in the manner described above. Owner's address for notices is: B.R.E. Holdings LLC, 4500 Bohannon Drive, Menlo Park, CA; Attention: Brigitte VanBaalen.

16. HOLDING OVER: Any holding over after expiration of this Lease, with the consent of Owner, will be a month-to-month tenancy at a monthly rent
of 150% of the then applicable Rent, payable in advance and otherwise subject to the terms of this Lease, as applicable, until either party terminates the same by giving the other party thirty days' advance written notice.

17. TIME. Time is of the essence of this Lease.

18. ATTORNEY'S FEES: In any action or proceeding involving a dispute between Owner and Tenant arising out of this Lease, the prevailing party will be entitled to reasonable attorneys' fees and costs incurred.

19. FAIR HOUSING: Owner and Tenant understand that the state and federal housing laws prohibit discrimination in the sale, rental, appraisal, financing or advertising of housing on the basis of race, religion, color, sex, familial status, sexual preference, handicap, or national origin.

20. INSURANCE: Upon execution of this Lease, Tenant shall provide Owner with evidence of (i) property insurance against "All Risks" of physical loss covering the replacement costs of all of Tenant's personal property located upon the Premises, and (ii) general liability insurance, each with such terms, coverages and insurers as Owner may reasonably require. Owner shall be named as additional insured with respect to Tenant's general liability policy.

21. OPTION TO EXTEND LEASE: Tenant shall have the option, for so long as [employee] shall be employed by E*TRADE, to extend the term of this Lease (the "Extension Option") for successive terms of one year each (the "Option Terms") upon and subject to the terms and conditions of this paragraph 21. Each Extension Option shall be exercised, if at all, by notice (the "Option Exercise Notice") given to Owner not earlier than four months nor later than two months prior to the expiration date of the Term. If Tenant exercises an Extension Option, each of the terms, covenants and conditions of the Lease shall apply during such Option Term as though the expiration date of the Option Term was the date originally set forth herein as the expiration date, except that the Rent for such Option Term shall be the fair market rental for the Property as reasonably determined by Owner ("Fair Market Rental"). Notwithstanding the foregoing, if Tenant (i) fails to timely exercise any Extension Option, or (ii) cancels an Option Exercise Notice as provided below, the remaining Extension Options shall automatically be null and void. If Tenant is in default under any of the terms, covenants or conditions of this Lease either at the time Tenant exercises an Extension Option or at any time thereafter prior to the commencement date of the Option Term, Owner shall have, in addition to all of Owners' other rights and remedies provided in this Lease, the right to terminate the Extension Option upon notice to Tenant. Within ten business days after Owner's receipt of an Option Exercise Notice, Owner shall give notice to Tenant of its determination of Fair Market Rental for such option period ("Rental Notice"). Tenant may, by notice delivered to Owner within ten business days following receipt of a Rental Notice, cancel his or her Option Exercise Notice, in which case this Lease shall terminate at the end of the then current term. In no event shall any provision of this paragraph be construed to extend the term of the Lease beyond the date of termination of [employee] employment by E*TRADE.

22. OPTION TO PURCHASE THE PREMISES:

(a) Grant of Option. Subject to the terms and conditions hereinafter set forth, Owner hereby grants to Tenant an exclusive option ("Option") to purchase the Premises.

(b) Term. The Option shall be effective for a term (the "Purchase Option Term") commencing on [date], and expiring upon the termination of this Lease.

(c) Exercise of Option. Provided Tenant is not then in default under any term or provision of the Lease, this Option may be exercised by Tenant's delivery to Owner of written notice (the "Option Notice") of Tenant's exercise of the Option prior to the expiration of the Purchase Option Term. The Option Notice shall state without condition or qualification that the Option is exercised.

(d) Terms of Sale and Option Notice. Upon Tenant's exercise of the Option, Owner shall sell to Tenant and Tenant shall purchase from Owner the Premises upon the terms and conditions set forth in the Standard Residential Purchase Agreement attached hereeto as Exhibit A (the "Purchase Agreement"). The Purchase Price for the Premises shall be [Dollars ($__________)]. The total amount of Rent paid by Purchaser as Tenant under the Lease shall be applied to the Purchase Price and credited as a deposit under paragraph 1A of the Purchase Agreement. There shall be no brokers or salespersons involved in the purchase and sale of the Premises as provided herein and all references to brokers or agents in the Purchase Agreement are deemed deleted. The word "acceptance" as used in the Purchase Agreement to describe the date Seller accepts the offer shall mean the date of delivery of the Option Notice.

(e) Memorandum of Option. Contemporaneously with the execution hereto, Owner and Tenant shall execute and acknowledge a Memorandum of Option substantially in the form of Exhibit B attached hereto, and promptly cause recordation of same in the Official Records of [county where property is located], California.

23. LEASE NOT TO AFFECT EMPLOYMENT: Tenant agrees and understands that nothing in this Lease shall confer any right with respect to [employee]' continuation of employment with E*TRADE, nor shall it interfere in any way with his right or the right of E*TRADE, to terminate his employment at any time, with or without cause, in accordance with his employment agreement with E*TRADE.

24. REPRESENTATION OF THE PARTIES: Owner has been represented by its independent attorneys in connection with this Lease. Tenant acknowledges that he and she have been advised by attorneys for Owner of their right to consult with his or her separate legal, tax and financial counsel about the terms of this Lease, and that Tenant has had an adequate opportunity to consult with such separate counsel before signing this Lease.

25. ENTIRE AGREEMENT: The foregoing constitutes the entire agreement between the parties and may be modified only in writing signed by all parties. This Lease and any modifications, including any photocopy or facsimile, may be signed in one or more counterparts, each of which will be deemed an original and all of which taken together will constitute one and the same instrument.

Tenant hereby acknowledges receipt of a copy of this Lease.

Tenant: [employee]

Owner: B.R.E. Holdings LLC

By: ________________________________

EXHIBIT B
MEMORANDUM OF AGREEMENT

This Memorandum of Agreement is made and entered into as of [date], by and between [Tenant] as "Tenant" and B.R.E. Holdings LLC as "Owner."

Tenant and Owner entered into a certain Residential Lease-Rental Agreement and Deposit Receipt dated [date] (the "Agreement") pursuant to which the Owner agreed to certain purchase option rights in favor of Tenant affecting Owner's interest in that certain real property commonly known as [address] and more particularly described in Exhibit A attached hereto.

For further particulars as to the terms, covenants and conditions of said Agreement, all of the provisions thereof are hereby referred to by this reference made a part hereof.

IN WITNESS WHEREOF, the undersigned have executed this document so that third parties might have notice of the rights, obligations and restrictions contained in the Agreement.

B.R.E. Holdings LLC

By: _______________________  
    Tenant

Signatures must be notarized.

EXHIBIT A

[Legal description of property]