Jefferies Group LLC
Form 10-Q
July 09, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended May 31, 2014

OR

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

For the transition period from __________ to __________

Commission file number 1-14947

JEFFERIES GROUP LLC

(Exact name of registrant as specified in its charter)

Delaware	**95-4719745**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
520 Madison Avenue, New York, New York	**10022**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (212) 284-2550

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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	x	Smaller reporting company	¨

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

The Registrant is a wholly-owned subsidiary of Leucadia National Corporation and meets the conditions set forth in General Instructions H(1)(a) and (b) of Form 10-Q and is therefore filing this Form 10-Q with a reduced disclosure format as permitted by Instruction H (2).

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JEFFERIES GROUP LLC

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MAY 31, 2014

PART I. FINANCIAL INFORMATION

PART II. OTHER INFORMATION

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JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (UNAUDITED)

(In thousands)

	May 31, 2014	November 30, 2013
ASSETS		
Cash and cash equivalents	$ 3,958,288	$ 3,561,119
Cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations	3,288,517	3,616,602
Financial instruments owned, at fair value, including securities pledged of $13,994,936 and $13,253,537 at May 31, 2014 and November 30, 2013, respectively	17,143,518	16,650,043
Investments in managed funds	75,369	57,285
Loans to and investments in related parties	508,570	701,873
Securities borrowed	6,097,098	5,359,846
Securities purchased under agreements to resell	4,609,422	3,746,920
Securities received as collateral	126,106	11,063
Receivables:		
Brokers, dealers and clearing organizations	2,588,654	2,119,279
Customers	1,805,451	1,046,945
Fees, interest and other	290,838	251,072
Premises and equipment	234,258	202,467
Goodwill	1,725,117	1,722,346
Other assets	1,158,780	1,130,136
Total assets	$ 43,609,986	$ 40,176,996
LIABILITIES AND EQUITY		
Short-term borrowings	$ 12,000	$ 12,000
Financial instruments sold, not yet purchased, at fair value	8,172,300	7,271,613
Collateralized financings:		
Securities loaned	2,901,159	2,506,122
Securities sold under agreements to repurchase	11,668,130	10,779,845
Other secured financings	240,288	234,711
Obligation to return securities received as collateral	126,106	11,063
Payables:		
Brokers, dealers and clearing organizations	1,475,140	1,281,253
Customers	5,623,278	5,208,768
Accrued expenses and other liabilities	1,135,000	1,217,141
Long-term debt	6,729,484	6,232,806
Total liabilities	38,082,885	34,755,322

EQUITY		
Member s paid-in capital	5,455,461	5,280,420
Accumulated other comprehensive income:		
Currency translation adjustments	37,984	21,341
Additional minimum pension liability	2,759	2,759
Total accumulated other comprehensive income	40,743	24,100
Total member s equity	5,496,204	5,304,520
Noncontrolling interests	30,897	117,154
Total equity	5,527,101	5,421,674
Total liabilities and equity	$ 43,609,986	$ 40,176,996

Continued on next page.

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JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION CONTINUED (UNAUDITED)

(In thousands)

The table below presents the carrying amount and classification of assets of consolidated variable interest entities (VIEs) that can be used only to settle obligations of the consolidated VIEs and the liabilities of consolidated VIEs for which creditors (or beneficial interest holders) do not have recourse to our general credit. The assets and liabilities of these consolidated VIEs are included in the Consolidated Statements of Financial Condition and are presented net of intercompany eliminations.

	May 31, 2014	November 30, 2013
Assets		
Cash and cash equivalents	$ 175	$ 176
Financial instruments owned, at fair value		
Loans and other receivables		97,500
Investments, at fair value	374	412
Total financial instruments owned, at fair value	374	97,912
Other assets		2,275
Total assets	$ 549	$ 100,363
Liabilities		
Other secured financings	$ 222,000	$ 226,000
Accrued expenses and other liabilities		706
Total liabilities	$ 222,000	$ 226,706

See accompanying notes to consolidated financial statements.

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JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS (UNAUDITED)

(In thousands, except per share amounts)

	Successor	
	Three Months Ended May 31, 2014	Three Months Ended May 31, 2013
Revenues:		
Commissions	$ 167,378	$ 162,759
Principal transactions	183,416	134,571
Investment banking	331,149	277,134
Asset management fees and investment income from managed funds	(3,101)	10,527
Interest	283,540	258,665
Other	8,404	26,245
Total revenues	970,786	869,901
Interest expense	247,794	211,463
Net revenues	722,992	658,438
Interest on mandatorily redeemable preferred interests of consolidated subsidiaries		3,368
Net revenues, less interest on mandatorily redeemable preferred interests of consolidated subsidiaries	722,992	655,070
Non-interest expenses:		
Compensation and benefits	404,876	373,880
Non-compensation expenses:		
Floor brokerage and clearing fees	54,020	48,902
Technology and communications	70,257	63,839
Occupancy and equipment rental	26,673	32,225
Business development	24,917	22,732
Professional services	25,345	29,519
Other	17,767	18,720
Total non-compensation expenses	218,979	215,937
Total non-interest expenses	623,855	589,817
Earnings before income taxes	99,137	65,253
Income tax expense	37,323	25,007
Net earnings	61,814	40,246

Net earnings attributable to noncontrolling interests		488		738
Net earnings attributable to Jefferies Group LLC	$	61,326	$	39,508

See accompanying notes to consolidated financial statements.

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JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS CONTINUED (UNAUDITED)

(In thousands, except per share amounts)

	Successor		Predecessor
	Six Months Ended May 31, 2014	Three Months Ended May 31, 2013	Three Months Ended February 28, 2013
Revenues:			
Commissions	$ 329,441	$ 162,759	$ 146,240
Principal transactions	421,779	134,571	300,278
Investment banking	745,469	277,134	288,278
Asset management fees and investment income from managed funds	6,856	10,527	10,883
Interest	532,808	258,665	249,277
Other	31,473	26,245	27,004
Total revenues	2,067,826	869,901	1,021,960
Interest expense	445,806	211,463	203,416
Net revenues	1,622,020	658,438	818,544
Interest on mandatorily redeemable preferred interests of consolidated subsidiaries		3,368	10,961
Net revenues, less interest on mandatorily redeemable preferred interests of consolidated subsidiaries	1,622,020	655,070	807,583
Non-interest expenses:			
Compensation and benefits	912,775	373,880	474,217
Non-compensation expenses:			
Floor brokerage and clearing fees	103,533	48,902	46,155
Technology and communications	134,563	63,839	59,878
Occupancy and equipment rental	53,175	32,225	24,309
Business development	51,393	22,732	24,927
Professional services	50,164	29,519	24,135
Other	35,011	18,720	14,475
Total non-compensation expenses	427,839	215,937	193,879
Total non-interest expenses	1,340,614	589,817	668,096
Earnings before income taxes	281,406	65,253	139,487
Income tax expense	104,200	25,007	48,645

Net earnings	177,206	40,246	90,842
Net earnings attributable to noncontrolling interests	3,448	738	10,704
Net earnings attributable to Jefferies Group LLC/common stockholders	$ 173,758	$ 39,508	$ 80,138
Earnings per common share:			
Basic	N/A	N/A	$ 0.35
Diluted	N/A	N/A	$ 0.35
Dividends declared per common share	N/A	N/A	$ 0.075
Weighted average common shares:			
Basic	N/A	N/A	213,732
Diluted	N/A	N/A	217,844

See accompanying notes to consolidated financial statements.

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JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

(In thousands)

	Successor	
	Three Months Ended May 31, 2014	Three Months Ended May 31, 2013
Net earnings	$ 61,814	$ 40,246
Other comprehensive income (loss), net of tax:		
Currency translation adjustments	2,859	(11,466)
Total other comprehensive income (loss), net of tax (1)	2,859	(11,466)
Comprehensive income:	64,673	28,780
Net earnings attributable to noncontrolling interests	488	738
Comprehensive income attributable to Jefferies Group LLC	$ 64,185	$ 28,042

	Successor		Predecessor
	Six Months Ended May 31, 2014	Three Months Ended May 31, 2013	Three Months Ended February 28, 2013
Net earnings	$ 177,206	$ 40,246	$ 90,842
Other comprehensive income (loss), net of tax:			
Currency translation adjustments	16,643	(11,466)	(10,018)
Total other comprehensive income (loss), net of tax (1)	16,643	(11,466)	(10,018)
Comprehensive income:	193,849	28,780	80,824
Net earnings attributable to noncontrolling interests	3,448	738	10,704
Comprehensive income attributable to Jefferies Group LLC/ common stockholders	$ 190,401	$ 28,042	$ 70,120

(1) No other comprehensive income (loss) is attributable to noncontrolling interests.

See accompanying notes to consolidated financial statements.

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JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (UNAUDITED)

(In thousands, except per share amounts)

	Successor		Predecessor
	Six Months Ended May 31, 2014	Nine Months Ended November 30, 2013	Three Months Ended February 28, 2013
Common stock, par value $0.0001 per share			
Balance, beginning of period	$	$	$ 20
Issued			1
Balance, end of period	$	$	$ 21
Member s paid-in capital			
Balance, beginning of period	$ 5,280,420	$ 4,754,101	$
Contributions		362,255	
Net earnings to Jefferies Group LLC	173,758	161,191	
Tax benefit for issuance of share-based awards	1,283	2,873	
Balance, end of period	$ 5,455,461	$ 5,280,420	$
Additional paid-in capital			
Balance, beginning of period	$	$	$ 2,219,959
Benefit plan share activity (1)			3,138
Share-based expense, net of forfeitures and clawbacks			22,288
Proceeds from exercise of stock options			57
Acquisitions and contingent consideration			2,535
Tax deficiency for issuance of share-based awards			(17,965)
Dividend equivalents on share-based plans			1,418
Balance, end of period	$	$	$ 2,231,430
Retained earnings			
Balance, beginning of period	$	$	$ 1,281,855
Net earnings to common shareholders			80,138
Dividends			(17,217)
Balance, end of period	$	$	$ 1,344,776
Accumulated other comprehensive income (loss) (2) (3)			
Balance, beginning of period	$ 24,100	$	$ (53,137)

Currency adjustment		16,643		21,341		(10,018)
Pension adjustment, net of tax				2,759		
Balance, end of period	$	40,743	$	24,100	$	(63,155)
Treasury stock, at cost						
Balance, beginning of period	$		$		$	(12,682)
Purchases						(166,541)
Returns / forfeitures						(1,922)
Balance, end of period	$		$		$	(181,145)
Total member s / common stockholders equity	$	5,496,204	$	5,304,520	$	3,331,927
Noncontrolling interests						
Balance, beginning of period	$	117,154	$	356,180	$	346,738
Net earnings attributable to noncontrolling interests		3,448		8,418		10,704
Contributions		31,076		100,210		
Distributions				(25)		(1,262)
Redemptions				(347,629)		
Deconsolidation of asset management entity		(120,781)				
Balance, end of period	$	30,897	$	117,154	$	356,180
Total equity	$	5,527,101	$	5,421,674	$	3,688,107

(1) Includes grants related to the Incentive Plan, Deferred Compensation Plan and Directors Plan.

(2) The components of other comprehensive income (loss) are attributable to Jefferies Group LLC (formerly Jefferies Group, Inc.). None of the components of other comprehensive income (loss) are attributable to noncontrolling interests.

(3) There were no reclassifications out of Accumulated other comprehensive loss during the six months ended May 31, 2014 and nine months ended November 30, 2013.

See accompanying notes to consolidated financial statements.

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JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(In thousands)

	Successor		Predecessor
	Six Months Ended May 31, 2014	Three Months Ended May 31, 2013	Three Months Ended February 28, 2013
Cash flows from operating activities:			
Net earnings	$ 177,206	$ 40,246	$ 90,842
Adjustments to reconcile net earnings to net cash (used in) provided by operating activities:			
Depreciation and amortization	(10,052)	(1,511)	17,393
(Gain) loss on conversion option	(5,679)	7,109	
Interest on mandatorily redeemable preferred interests of consolidated subsidiaries		3,368	10,961
Accruals related to various benefit plans and stock issuances, net of forfeitures			23,505
Income on loans to and investments in related parties	(37,893)	(28,540)	
Distributions received on investments in related parties	41,260	19,353	
Other adjustments	(3,909)	(1,329)	(1,154)
Net change in assets and liabilities:			
Cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations	329,559	671,426	352,891
Receivables:			
Brokers, dealers and clearing organizations	(466,846)	(845,322)	(1,027,671)
Customers	(756,884)	(144,938)	(130,543)
Fees, interest and other	(39,072)	(39,832)	(29,149)
Securities borrowed	(732,449)	(47,036)	(224,557)
Financial instruments owned	(661,495)	1,116,683	229,394
Loans to and investments in related parties			(197,166)
Investments in managed funds	12,469	4,835	(2,213)
Securities purchased under agreements to resell	(852,859)	106,129	(224,418)
Other assets	(31,835)	36,500	25,489
Payables:			
Brokers, dealers and clearing organizations	192,375	205,037	(1,031,335)
Customers	406,233	(18,807)	(111,139)
Securities loaned	390,165	780,579	(28,138)
Financial instruments sold, not yet purchased	1,071,678	(2,979,532)	2,327,667
Securities sold under agreements to repurchase	878,120	1,521,605	(197,493)

Accrued expenses and other liabilities	(88,488)	151,616	(267,336)
Net cash (used in) provided by operating activities	(188,396)	557,639	(394,170)
Cash flows from investing activities:			
Contributions to loans to and investments in related parties	(941,725)	(345,955)	
Distributions from loans to and investments in related parties	1,131,661	644,666	
Net payments on premises and equipment	(59,595)	(10,071)	(10,706)
Deconsolidation of asset management entity	(137,856)		
Cash received from contingent consideration	3,979	1,284	1,203
Net cash (used in) provided by investing activities	(3,536)	289,924	(9,503)

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JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS CONTINUED (UNAUDITED)

(In thousands)

	Successor		Predecessor
	Six Months Ended May 31, 2014	Three Months Ended May 31, 2013	Three Months Ended February 28, 2013
Cash flows from financing activities:			
Excess tax benefits from the issuance of share-based awards	$ 1,364	$ 1,857	$ 5,682
Proceeds from short-term borrowings	6,081,157	3,838,000	6,744,000
Payments on short-term borrowings	(6,081,157)	(3,938,000)	(6,794,000)
Proceeds from secured credit facility	655,000	265,000	900,000
Payments on secured credit facility	(790,000)	(450,000)	(990,007)
Net proceeds from other secured financings	5,577	105,000	60,000
Payments on mandatorily redeemable preferred interest of consolidated subsidiaries		(64)	(61)
Payments on repurchase of common stock			(166,541)
Payments on dividends			(15,799)
Proceeds from exercise of stock options, not including tax benefits			57
Net proceeds from issuance of senior notes, net of issuance costs	681,222		991,469
Proceeds from contributions of noncontrolling interests	31,076	27,200	
Payments on distributions to noncontrolling interests		(306,830)	(1,262)
Net cash provided by (used in) financing activities	584,239	(457,837)	733,538
Effect of exchange rate changes on cash and cash equivalents	4,862	(4,205)	(4,502)
Net increase in cash and cash equivalents	397,169	385,521	325,363
Cash and cash equivalents at beginning of period	3,561,119	3,017,958	2,692,595
Cash and cash equivalents at end of period	$ 3,958,288	$ 3,403,479	$ 3,017,958
Supplemental disclosures of cash flow information:			
Cash paid (received) during the period for:			

Interest	$ 460,219	$ 195,409	$ 178,836
Income taxes paid (refunds), net	60,220	(7,475)	(34,054)

Noncash financing activities:

In connection with the transaction with Leucadia National Corporation, Jefferies Group LLC recorded acquisition accounting adjustments which resulted in changes to equity. Refer to Note 4, Leucadia and Related Transactions, for further details.

On March 31, 2013, Leucadia contributed its mandatorily redeemable preferred interests in JHYH to Jefferies Group, LLC. The contribution was recorded as a capital contribution and increased member s equity by $362.3 million. Refer to Note 4, Leucadia and Related Transactions, for further details.

See accompanying notes to consolidated financial statements.

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JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

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JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Organization and Basis of Presentation

Organization

Jefferies Group LLC and its subsidiaries operate as a global full service, integrated securities and investment banking firm. Jefferies Group LLC was previously known as Jefferies Group, Inc., which on March 1, 2013 was converted into a limited liability company and renamed Jefferies Group LLC. In addition, certain subsidiaries of Jefferies Group, Inc. also converted into limited liability companies. The accompanying Consolidated Financial Statements therefore refer to Jefferies Group LLC and represent the accounts of Jefferies Group, Inc., as it was formerly known, and all our subsidiaries (together we or us). The subsidiaries of Jefferies Group LLC include Jefferies LLC (Jefferies), Jefferies Execution Services, Inc. (Jefferies Execution), Jefferies Bache, LLC, Jefferies International Limited, Jefferies Bache Limited, Jefferies Hong Kong Limited, Jefferies Bache Financial Services, Inc., Jefferies Mortgage Funding, LLC and Jefferies Leveraged Credit Products, LLC and all other entities in which we have a controlling financial interest or are the primary beneficiary.

On March 1, 2013, Jefferies Group LLC, through a series of transactions, became an indirect wholly owned subsidiary of Leucadia National Corporation (Leucadia) (referred to herein as the Leucadia Transaction). Each outstanding share of Jefferies Group LLC was converted into 0.81 of a share of Leucadia common stock (the Exchange Ratio). Leucadia did not assume nor guarantee any of our outstanding debt securities. Our 3.875% Convertible Senior Debentures due 2029 are now convertible into Leucadia common shares at a price that reflects the Exchange Ratio and the 3.25% Series A Convertible Cumulative Preferred Stock of Jefferies Group, Inc. was exchanged for a comparable series of convertible preferred shares of Leucadia. Jefferies Group LLC continues to operate as a full-service investment banking firm and as the holding company of its various regulated and unregulated operating subsidiaries, retain a credit rating separate from Leucadia and remain an SEC reporting company, filing annual, quarterly and periodic financial reports. Richard Handler, our Chief Executive Officer and Chairman, was also appointed the Chief Executive Officer of Leucadia, as well as a Director of Leucadia. Brian Friedman, our Chairman of the Executive Committee, was appointed Leucadia s President and a Director of Leucadia.

We operate in two business segments, Capital Markets and Asset Management. Capital Markets, which represents substantially our entire business, includes our securities, commodities, futures and foreign exchange trading and investment banking activities, which provides the research, sales, trading, origination and advisory effort for various equity, fixed income and advisory products and services. Asset Management provides investment management services to various private investment funds and separate accounts.

In addition, on April 1, 2013, we merged Jefferies High Yield Trading, LLC (our high yield trading broker-dealer) with Jefferies (a U.S. broker-dealer) and our high yield activities are now conducted by Jefferies. In addition, during the three months ended May 31, 2013, we redeemed the third party interests in our high yield joint venture.

Basis of Presentation

The accompanying Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) and should be read in conjunction with our Annual Report on Form 10-K for the year ended November 30, 2013.

As more fully described in Note 4, Leucadia and Related Transactions, the Leucadia Transaction is accounted for using the acquisition method of accounting, which requires that the assets, including identifiable intangible assets, and liabilities of Jefferies Group LLC be recorded at their fair values. The application of the acquisition method of accounting has been pushed down and reflected in the financial statements of Jefferies Group LLC as a wholly-owned subsidiary of Leucadia. The application of push down accounting represents the termination of the prior reporting entity and the creation of a new reporting entity, which do not have the same bases of accounting. As a result, our consolidated financial statements are presented for periods subsequent to March 1, 2013 for the new reporting entity

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(the Successor), and before March 1, 2013 for the prior reporting entity (the Predecessor.) The Predecessor and Successor periods are separated by a vertical line to highlight the fact that the financial information for such periods has been prepared under two different cost bases of accounting. We have made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with U.S. GAAP. The most important of these estimates and assumptions relate to fair value measurements, compensation and benefits, goodwill and intangible assets, the ability to realize deferred tax assets and the recognition and measurement of uncertain tax positions. Although these and other estimates and assumptions are based on the best available information, actual results could be materially different from these estimates.

Cash Flow Statement Presentation

Amounts relating to loans and investments in related parties are classified as components of investing activities on the Consolidated Statements of Cash Flows to conform to the presentation of our Parent company in connection with the establishment of a new accounting entity through the application of push down accounting. These amounts are classified by the Predecessor entity as operating activities for reporting periods prior to the Leucadia Transaction.

Consolidation

Our policy is to consolidate all entities in which we control by ownership a majority of the outstanding voting stock. In addition, we consolidate entities which meet the definition of a variable interest entity for which we are the primary beneficiary. The primary beneficiary is the party who has the power to direct the activities of a variable interest entity that most significantly impact the entity s economic performance and who has an obligation to absorb losses of the entity or a right to receive benefits from the entity that could potentially be significant to the entity. For consolidated entities that are less than wholly owned, the third-party s holding of equity interest is presented as Noncontrolling interests in the Consolidated Statements of Financial Condition and Consolidated Statements of Changes in Equity. The portion of net earnings attributable to the noncontrolling interests are presented as Net earnings to noncontrolling interests in the Consolidated Statements of Earnings.

In situations where we have significant influence, but not control, of an entity that does not qualify as a variable interest entity, we apply either the equity method of accounting or fair value accounting pursuant to the fair value option election under U.S. GAAP, with our portion of net earnings or gains and losses recorded within Other revenues or Principal transaction revenues, respectively. We also have formed nonconsolidated investment vehicles with third-party investors that are typically organized as partnerships or limited liability companies and are carried at fair value. We act as general partner or managing member for these investment vehicles and have generally provided the third-party investors with termination or kick-out rights.

Intercompany accounts and transactions are eliminated in consolidation.

Immaterial 2013 Adjustments

As indicated in our Quarterly Report on Form 10-Q for the three months ended August 31, 2013 and our Annual Report on Form 10-K for the year ended November 30, 2013, we have made correcting adjustments (referred to as adjustments) to our historical financial statements for the first and second quarter of 2013. We do not believe these adjustments are material to our financial statements for the quarterly periods ended May 31, 2013 and February 28, 2013. For additional information on these adjustments, see Note 1, Organization and Basis of Presentation, and Note 26, Selected Quarterly Financial Data (Unaudited), of the Consolidated Financial Statements of our Annual Report on Form 10-K for the year ended November 30, 2013.

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 2. Summary of Significant Accounting Policies

Revenue Recognition Policies

Commissions. All customer securities transactions are reported on the Consolidated Statements of Financial Condition on a settlement date basis with related income reported on a trade-date basis. We permit institutional customers to allocate a portion of their gross commissions to pay for research products and other services provided by third parties. The amounts allocated for those purposes are commonly referred to as soft dollar arrangements. These arrangements are accounted for on an accrual basis and, as we are not the primary obligor for these arrangements, netted against commission revenues in the Consolidated Statements of Earnings. The commissions and related expenses on client transactions executed by Jefferies Bache, LLC, a futures commission merchant, are recorded on a half-turn basis.

Principal Transactions. Financial instruments owned and Financial instruments sold, but not yet purchased (all of which are recorded on a trade-date basis) are carried at fair value with gains and losses reflected in Principal transactions in the Consolidated Statements of Earnings on a trade date basis. Fees received on loans carried at fair value are also recorded within Principal transactions.

Investment Banking. Underwriting revenues and fees from mergers and acquisitions, restructuring and other investment banking advisory assignments or engagements are recorded when the services related to the underlying transactions are completed under the terms of the assignment or engagement. Expenses associated with such assignments are deferred until reimbursed by the client, the related revenue is recognized or the engagement is otherwise concluded. Expenses are recorded net of client reimbursements and netted against revenues. Unreimbursed expenses with no related revenues are included in Business development and Professional services expenses in the Consolidated Statements of Earnings.

Asset Management Fees and Investment Income From Managed Funds. Asset management fees and investment income from managed funds include revenues we earn from management, administrative and performance fees from funds and accounts managed by us, revenues from management and performance fees we earn from related-party managed funds and investment income from our investments in these funds. We earn fees in connection with management and investment advisory services performed for various funds and managed accounts. These fees are based on assets under management or an agreed upon notional amount and may include performance fees based upon the performance of the funds. Management and administrative fees are generally recognized over the period that the related service is provided. Generally, performance fees are earned when the return on assets under management exceeds certain benchmark returns, high-water marks or other performance targets. Performance fees are accrued (or reversed) on a monthly basis based on measuring performance to date versus any relevant benchmark return hurdles stated in the investment management agreement. Performance fees are not subject to adjustment once the measurement period ends (generally annual periods) and the performance fees have been realized.

Interest Revenue and Expense. We recognize contractual interest on Financial instruments owned and Financial instruments sold, but not yet purchased, on an accrual basis as a component of interest revenue and expense. Interest flows on derivative trading transactions and dividends are included as part of the fair valuation of these contracts and recognized in Principal transactions in the Consolidated Statements of Earnings rather than as a component of interest revenue or expense. We account for our short- and long-term borrowings on an accrual basis with related interest recorded as Interest expense. Discounts/premiums arising on our long-term debt are accreted / amortized to Interest expense using the effective yield method over the remaining lives of the underlying debt obligations. In addition, we recognize interest revenue related to our securities borrowed and securities purchased under agreements to resell activities and interest expense related to our securities loaned and securities sold under agreements to repurchase activities on an accrual basis.

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Cash Equivalents

Cash equivalents include highly liquid investments, including certificates of deposit and money market funds, not held for resale with original maturities of three months or less.

Cash and Securities Segregated and on Deposit for Regulatory Purposes or Deposited With Clearing and Depository Organizations

In accordance with Rule 15c3-3 of the Securities Exchange Act of 1934, Jefferies as a broker-dealer carrying client accounts, is subject to requirements related to maintaining cash or qualified securities in a segregated reserve account for the exclusive benefit of its clients. In addition, certain financial instruments used for initial and variation margin purposes with clearing and depository organizations are recorded in this caption. Jefferies Bache, LLC, as a futures commission merchant, is obligated by rules mandated by the Commodities Futures Trading Commission under the Commodities Exchange Act, to segregate or set aside cash or qualified securities to satisfy such regulations, which regulations have been promulgated to protect customer assets. Certain other entities are also obligated by rules mandated by their primary regulators to segregate or set aside cash or equivalent securities to satisfy regulations, promulgated to protect customer assets.

Financial Instruments

Financial instruments owned and Financial instruments sold, not yet purchased are recorded at fair value, either as required by accounting pronouncements or through the fair value option election. These instruments primarily represent our trading activities and include both cash and derivative products. Gains and losses are recognized in Principal transactions in our Consolidated Statements of Earnings. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (the exit price).

Fair Value Hierarchy

In determining fair value, we maximize the use of observable inputs and minimize the use of unobservable inputs by requiring that observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect our assumptions that market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. We apply a hierarchy to categorize our fair value measurements broken down into three levels based on the transparency of inputs as follows:

Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the reported date.

Level 2: Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these financial instruments include cash instruments for which quoted prices are available but traded less frequently, derivative instruments whose fair value have been derived using a model where inputs to the model are directly observable in the market, or can be derived principally from or corroborated by observable market data, and instruments that are fair valued using other financial instruments, the parameters of which can be directly observed.

Level 3: Instruments that have little to no pricing observability as of the reported date. These financial instruments are measured using management s best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation.

Financial instruments are valued at quoted market prices, if available. Certain financial instruments have bid and ask prices that can be observed in the marketplace. For financial instruments whose inputs are based on bid-ask prices, the financial instrument is valued at the point within the bid-ask range that meets our best estimate of fair value. We use

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prices and inputs that are current as of the measurement date. For financial instruments that do not have readily determinable fair values using quoted market prices, the determination of fair value is based upon consideration of available information, including types of financial instruments, current financial information, restrictions on dispositions, fair values of underlying financial instruments and quotations for similar instruments.

The valuation of financial instruments may include the use of valuation models and other techniques. Adjustments to valuations derived from valuation models may be made when, in management s judgment, features of the financial instrument such as its complexity, the market in which the financial instrument is traded and risk uncertainties about market conditions require that an adjustment be made to the value derived from the models. Adjustments from the price derived from a valuation model reflect management s judgment that other participants in the market for the financial instrument being measured at fair value would also consider in valuing that same financial instrument. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment.

The availability of observable inputs can vary and is affected by a wide variety of factors, including, for example, the type of financial instrument and market conditions. As the observability of prices and inputs may change for a financial instrument from period to period, this condition may cause a transfer of an instrument among the fair value hierarchy levels. Transfers among the levels are recognized at the beginning of each period. The degree of judgment exercised in determining fair value is greatest for instruments categorized in Level 3.

Valuation Process for Financial Instruments

Our Independent Price Verification (IPV) Group, which is part of our Finance department, in partnership with Risk Management, is responsible for establishing our valuation policies and procedures. The IPV Group and Risk Management, which are independent of our business functions, play an important role and serve as a control function in determining that our financial instruments are appropriately valued and that fair value measurements are reliable. This is particularly important where prices or valuations that require inputs are less observable. In the event that observable inputs are not available, the control processes are designed to assure that the valuation approach utilized is appropriate and consistently applied and that the assumptions are reasonable. The IPV Group reports to the Global Controller and is subject to the oversight of the IPV Committee, which is comprised of our Chief Financial Officer, Global Controller, Global Head of Product Control, Chief Risk Officer and Principal Accounting Officer, among other personnel. Our independent price verification policies and procedures are reviewed, at a minimum, annually and changes to the policies require the approval of the IPV Committee.

Price Testing Process. The business units are responsible for determining the fair value of our financial instruments using approved valuation models and methodologies. In order to ensure that the business unit valuations represent a fair value exit price, the IPV Group tests and validates the fair value of our financial instruments inventory. In the testing process, the IPV Group obtains prices and valuation inputs from sources independent of Jefferies, consistently adheres to established procedures set forth in our valuation policies for sourcing prices and valuation inputs and utilizing valuation methodologies. Sources used to validate fair value prices and inputs include, but are not limited to, exchange data, recently executed transactions, pricing data obtained from third party vendors, pricing and valuation services, broker quotes and observed comparable transactions.

To the extent discrepancies between the business unit valuations and the pricing or valuations resulting from the price testing process are identified, such discrepancies are investigated by the IPV Group and fair values are adjusted, as appropriate. The IPV Group maintains documentation of its testing, results, rationale and recommendations and prepares a monthly summary of its valuation results. This process also forms the basis for our classification of fair values within the fair value hierarchy (i.e., Level 1, Level 2 or Level 3). The IPV Group utilizes the additional expertise of Risk Management personnel in valuing more complex financial instruments and financial instruments with less or limited pricing observability. The results of the valuation testing are reported to the IPV Committee on a monthly basis, which discusses the results and is charged with the final conclusions as to the financial instrument fair values in the consolidated financial statements. This process specifically assists the Chief Financial Officer in

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asserting as to the fair presentation of our financial condition and results of operations as included within our Quarterly Reports on Form 10-Q and Annual Report on Form 10-K. At each quarter end, the overall valuation results, as concluded upon by the IPV Committee, are presented to the Audit Committee.

Judgment exercised in determining Level 3 fair value measurements is supplemented by daily analysis of profit and loss performed by the Product Control functions. Gains and losses, which result from changes in fair value, are evaluated and corroborated daily based on an understanding of each of the trading desks overall risk positions and developments in a particular market on the given day. Valuation techniques generally rely on recent transactions of suitably comparable financial instruments and use the observable inputs from those comparable transactions as a validation basis for Level 3 inputs. Level 3 fair value measurements are further validated through subsequent sales testing and market comparable sales, if such information is available. Level 3 fair value measurements require documentation of the valuation rationale applied, which is reviewed for consistency in application from period to period; and the documentation includes benchmarking the assumptions underlying the valuation rationale against relevant analytic data.

Third Party Pricing Information. Pricing information obtained from external data providers (including independent pricing services and brokers) may incorporate a range of market quotes from dealers, recent market transactions and benchmarking model derived prices to quoted market prices and trade data for comparable securities. External pricing data is subject to evaluation for reasonableness by the IPV Group using a variety of means including comparisons of prices to those of similar product types, quality and maturities, consideration of the narrowness or wideness of the range of prices obtained, knowledge of recent market transactions and an assessment of the similarity in prices to comparable dealer offerings in a recent time period. We have a process whereby we challenge the appropriateness of pricing information obtained from external data providers (including independent pricing services and brokers) in order to validate the data for consistency with the definition of a fair value exit price. Our process includes understanding and evaluating the external data providers valuation methodologies. For corporate, U.S. government and agency and municipal debt securities, and loans, to the extent independent pricing services or broker quotes are utilized in our valuation process, the vendor service providers are collecting and aggregating observable market information as to recent trade activity and active bid-ask submissions. The composite pricing information received from the independent pricing service is thus not based on unobservable inputs or proprietary models. For mortgage- and other asset-backed securities and collateralized debt obligations, our independent pricing service uses a matrix evaluation approach incorporating both observable yield curves and market yields on comparable securities as well as implied inputs from observed trades for comparable securities in order to determine prepayment speeds, cumulative default rates and loss severity. Further, we consider pricing data from multiple service providers as available as well as compare pricing data to prices we have observed for recent transactions, if any, in order to corroborate our valuation inputs.

Model Review Process. Where a pricing model is to be used to determine fair value, the pricing model is reviewed for theoretical soundness and appropriateness by Risk Management, independent from the trading desks, and then approved by Risk Management to be used in the valuation process. Review and approval of a model for use may include benchmarking the model against relevant third party valuations, testing sample trades in the model, backtesting the results of the model against actual trades and stress-testing the sensitivity of the pricing model using varying inputs and assumptions. In addition, recently executed comparable transactions and other observable market data are considered for purposes of validating assumptions underlying the model. Models are independently reviewed and validated by Risk Management annually or more frequently if market conditions or use of the valuation model changes.

Investments in Managed Funds

Investments in managed funds include our investments in funds managed by us and our investments in related-party managed funds in which we are entitled to a portion of the management and/or performance fees. Investments in nonconsolidated managed funds are accounted for at fair value with gains or losses included in Asset management fees and investment income from managed funds in the Consolidated Statements of Earnings.

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Loans to and Investments in Related Parties

Loans to and investments in related parties include investments in private equity and other operating entities made in connection with our capital markets activities in which we exercise significant influence over operating and capital decisions and loans issued in connection with such activities. Loans to and investments in related parties are accounted for using the equity method or at cost, as appropriate. Revenues on Loans to and investments in related parties are included in Other revenues in the Consolidated Statements of Earnings. See Note 10, Investments, and Note 22, Related Party Transactions, for additional information regarding certain of these investments.

Receivable from and Payable to Customers

Receivable from and payable to customers includes amounts receivable and payable on cash and margin transactions. Securities owned by customers and held as collateral for these receivables are not reflected in the accompanying consolidated financial statements. Receivable from officers and directors included within this financial statement line item represents balances arising from their individual security transactions. These transactions are subject to the same regulations as customer transactions and are provided on substantially the same terms.

Securities Borrowed and Securities Loaned

Securities borrowed and securities loaned are carried at the amounts of cash collateral advanced and received in connection with the transactions and accounted for as collateralized financing transactions. In connection with both trading and brokerage activities, we borrow securities to cover short sales and to complete transactions in which customers have failed to deliver securities by the required settlement date, and lend securities to other brokers and dealers for similar purposes. We have an active securities borrowed and lending matched book business in which we borrow securities from one party and lend them to another party. When we borrow securities, we generally provide cash to the lender as collateral, which is reflected in our Consolidated Statements of Financial Condition as Securities borrowed. We earn interest revenues on this cash collateral. Similarly, when we lend securities to another party, that party provides cash to us as collateral, which is reflected in our Consolidated Statements of Financial Condition as Securities loaned. We pay interest expense on the cash collateral received from the party borrowing the securities. The initial collateral advanced or received approximates or is greater than the fair value of the securities borrowed or loaned. We monitor the fair value of the securities borrowed and loaned on a daily basis and request additional collateral or return excess collateral, as appropriate.

Securities Purchased Under Agreements to Resell and Securities Sold Under Agreements to Repurchase

Securities purchased under agreements to resell and Securities sold under agreements to repurchase (collectively repos) are accounted for as collateralized financing transactions and are recorded at their contracted resale or repurchase amount plus accrued interest. We earn and incur interest over the term of the repo, which is reflected in Interest income and Interest expense on our Consolidated Statements of Earnings on an accrual basis. Repos are presented in the Consolidated Statements of Financial Condition on a net-basis-by counterparty, where permitted by generally accepted accounting principles. We monitor the fair value of the underlying securities daily versus the related receivable or payable balances. Should the fair value of the underlying securities decline or increase, additional collateral is requested or excess collateral is returned, as appropriate.

Premises and Equipment

Premises and equipment are depreciated using the straight-line method over the estimated useful lives of the related assets (generally three to ten years). Leasehold improvements are amortized using the straight-line method over the term of the related leases or the estimated useful lives of the assets, whichever is shorter. Premises and equipment includes internally developed software, which was increased to its fair market value in the allocation of the purchase price on March 1, 2013. The revised carrying values of internally developed software ready for its intended use are depreciated over the remaining useful life. See Note 4, Leucadia and Related Transactions for more information regarding the allocation of the purchase price.

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Goodwill and Intangible Assets

Goodwill. Goodwill represents the excess acquisition cost over the fair value of net tangible and intangible assets acquired. Goodwill is not amortized and is subject to annual impairment testing on August 1 or between annual tests if an event or change in circumstance occurs that would more likely than not reduce the fair value of a reporting unit below its carrying value. In testing for goodwill impairment, we have the option to first assess qualitative factors to determine whether the existence of events or circumstances lead to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events and circumstances, we conclude that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is not required. If we conclude otherwise, we are required to perform the two-step impairment test. The goodwill impairment test is performed at the reporting unit level by comparing the estimated fair value of a reporting unit with its respective carrying value. If the estimated fair value exceeds the carrying value, goodwill at the reporting unit level is not impaired. If the estimated fair value is less than carrying value, further analysis is necessary to determine the amount of impairment, if any.

The fair value of reporting units are based on widely accepted valuation techniques that we believe market participants would use, although the valuation process requires significant judgment and often involves the use of significant estimates and assumptions. The methodologies we utilize in estimating the fair value of reporting units include market valuation methods that incorporate price-to-earnings and price-to-book multiples of comparable exchange traded companies and multiples of merger and acquisitions of similar businesses. The estimates and assumptions used in determining fair value could have a significant effect on whether or not an impairment charge is recorded and the magnitude of such a charge. Adverse market or economic events could result in impairment charges in future periods.

Intangible Assets. Intangible assets deemed to have finite lives are amortized on a straight line basis over their estimated useful lives, where the useful life is the period over which the asset is expected to contribute directly, or indirectly, to our future cash flows. Intangible assets are reviewed for impairment on an interim basis when certain events or circumstances exist. For amortizable intangible assets, impairment exists when the carrying amount of the intangible asset exceeds its fair value. At least annually, the remaining useful life is evaluated.

An intangible asset with an indefinite useful life is not amortized but assessed for impairment annually, or more frequently, when events or changes in circumstances occur indicating that it is more likely than not that the indefinite-lived asset is impaired. Impairment exists when the carrying amount exceeds its fair value. In testing for impairment, we have the option to first perform a qualitative assessment to determine whether it is more likely than not that an impairment exists. If it is determined that it is not more likely than not that an impairment exists, a quantitative impairment test is not necessary. If we conclude otherwise, we are required to perform a quantitative impairment test. Our annual indefinite-lived intangible asset impairment testing date is August 1.

To the extent an impairment loss is recognized, the loss establishes the new cost basis of the asset that is amortized over the remaining useful life of that asset, if any. Subsequent reversal of impairment losses is not permitted.

Income Taxes

Prior to the Leucadia Transaction, we filed a consolidated U.S. federal income tax return, which included all of our qualifying subsidiaries. Subsequently, our results of operations are included in the consolidated federal and applicable state income tax returns filed by Leucadia. In states that neither accept nor require combined or unitary tax returns, certain subsidiaries file separate state income tax returns. We also are subject to income tax in various foreign jurisdictions in which we operate. We account for our provision for income taxes using a separate return method. Amounts provided for income taxes are based on income reported for financial statement purposes and do not necessarily represent amounts currently payable.

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Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and for tax loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. Under acquisition accounting, the recognition of certain assets and liabilities at fair value created a change in the financial reporting basis for our assets and liabilities, while the tax basis of our assets and liabilities remained the same. As a result, deferred tax assets and liabilities were recognized for the change in the basis differences. Jefferies provides deferred taxes on its temporary differences and on any carryforwards that it could claim on its hypothetical tax return. The realization of deferred tax assets is assessed and a valuation allowance is recorded to the extent that it is more likely than not that any portion of the deferred tax asset will not be realized on the basis of its projected separate return results. The tax benefit related to Leucadia dividends and dividend equivalents paid on nonvested share-based payment awards are recognized as an increase to Additional paid-in capital. These amounts are included in tax benefits for issuance of share-based awards on the Consolidated Statements of Changes in Equity.

We record uncertain tax positions using a two-step process: (i) we determine whether it is more likely than not that each tax position will be sustained on the basis of the technical merits of the position; and (ii) for those tax positions that meet the more-likely-than-not recognition threshold, we recognize the largest amount of tax benefit that is more than 50 percent likely to be realized upon ultimate settlement with the related tax authority.

Legal Reserves

In the normal course of business, we have been named, from time to time, as a defendant in legal and regulatory proceedings. We are also involved, from time to time, in other exams, investigations and similar reviews (both formal and informal) by governmental and self-regulatory agencies regarding our businesses, certain of which may result in judgments, settlements, fines, penalties or other injunctions.

We recognize a liability for a contingency in Accrued expenses and other liabilities when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. If the reasonable estimate of a probable loss is a range, we accrue the most likely amount of such loss, and if such amount is not determinable, then we accrue the minimum in the range as the loss accrual. The determination of the outcome and loss estimates requires significant judgment on the part of management. As of May 31, 2014, we have reserved approximately $5.1 million for remaining payments under a non-prosecution agreement with the United States Attorney for the District of Connecticut and a settlement agreement with the Securities and Exchange Commission, both with respect to an investigation of certain purchases and sales of mortgage-backed securities. We believe that any other matters for which we have determined a loss to be probable and reasonably estimable are not material to the consolidated financial statements.

In many instances, it is not possible to determine whether any loss is probable or even possible or to estimate the amount of any loss or the size of any range of loss. We believe that, in the aggregate, the pending legal actions or regulatory proceedings and any other exams, investigations or similar reviews (both formal and informal) should not have a material adverse effect on our consolidated results of operations, cash flows or financial condition. In addition, we believe that any amount that could be reasonably estimated of potential loss or range of potential loss in excess of what has been provided in the consolidated financial statements is not material.

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Share-based Compensation

Share-based awards are measured based on the grant-date fair value of the award and recognized over the period from the service inception date through the date the employee is no longer required to provide service to earn the award. Expected forfeitures are included in determining share-based compensation expense.

Foreign Currency Translation

Assets and liabilities of foreign subsidiaries having non-U.S. dollar functional currencies are translated at exchange rates at the end of a period. Revenues and expenses are translated at average exchange rates during the period. The gains or losses resulting from translating foreign currency financial statements into U.S. dollars, net of hedging gains or losses and taxes, if any, are included in Other comprehensive income. Gains or losses resulting from foreign currency transactions are included in Principal transactions in the Consolidated Statements of Earnings.

Earnings per Common Share

As a single member limited liability company, earnings per share is not calculated for Jefferies Group LLC (the Successor company).

Prior to the Leucadia Transaction, Jefferies Group, Inc. (the Predecessor company) had common shares and other common share equivalents outstanding. For the Predecessor periods, basic earnings per share (EPS) is computed by dividing net earnings available to common shareholders by the weighted average number of common shares outstanding and certain other shares committed to be, but not yet issued. Net earnings available to common shareholders represent net earnings to common shareholders reduced by the allocation of earnings to participating securities. Losses are not allocated to participating securities. For Predecessor periods, diluted EPS is computed by dividing net earnings available to common shareholders plus dividends on dilutive mandatorily redeemable convertible preferred stock by the weighted average number of common shares outstanding and certain other shares committed to be, but not yet issued, plus all dilutive common stock equivalents outstanding during the period. Unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and, therefore, are included in the earnings allocation in computing earnings per share under the two-class method of earning per share.

Securitization Activities

We engage in securitization activities related to corporate loans, commercial mortgage loans and mortgage-backed and other asset-backed securities. Such transfers of financial assets are accounted for as sales when we have relinquished control over the transferred assets. The gain or loss on sale of such financial assets depends, in part, on the previous carrying amount of the assets involved in the transfer allocated between the assets sold and the retained interests, if any, based upon their respective fair values at the date of sale. We may retain interests in the securitized financial assets as one or more tranches of the securitization. These retained interests are included within Financial instruments owned in the Consolidated Statements of Financial Condition at fair value. Any changes in the fair value of such retained interests are recognized within Principal transactions revenues in the Consolidated Statements of Earnings.

When a transfer of assets does not meet the criteria of a sale, we account for the transfer as a secured borrowing and continue to recognize the assets of a secured borrowing in Financial instruments owned and recognize the associated financing in Other secured financings in the Consolidated Statements of Financial Condition.

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Note 3. Accounting Developments

Adopted Accounting Standards

Accumulated Other Comprehensive Income. In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. The guidance requires an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under U.S. GAAP to be reclassified in its entirety to net income. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety from accumulated other comprehensive income to net income in the same reporting period, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. We adopted the guidance effective March 1, 2013, presenting the additional disclosures within our Consolidated Statements of Changes in Equity. Adoption did not affect our results of operations, financial condition or cash flows.

Accounting Standards to be Adopted in Future Periods

Repurchase Agreements. In June 2014, the FASB issued ASU No. 2014-11, Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures. The accounting guidance changes the accounting for repurchase-to-maturity transactions and linked repurchase financings to secured borrowing accounting, which is consistent with the accounting for other repurchase agreements. The guidance also requires new disclosures about transfers that are accounted for as sales in transactions that are economically similar to repurchase agreements and increased transparency about the types of collateral pledged in repurchase agreements and similar transactions accounted for as secured borrowings. The guidance is effective prospectively in the second quarter of fiscal 2015. We are currently evaluating the impact of the new guidance on our consolidated financial statements.

Revenue Recognition. In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. The accounting guidance defines how companies report revenues from contracts with customers, and also requires enhanced disclosures. The guidance is effective beginning in the first quarter of fiscal 2017. We are currently evaluating the impact of the new guidance on our consolidated financial statements.

Discontinued Operations. In April 2014, the FASB issued ASU No. 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. The guidance changes the criteria for disposals to qualify as discontinued operations and requires new disclosures about disposals of both discontinued operations and certain other disposals that do not meet the new definition. The guidance is effective beginning in the first quarter of 2015. We do not expect the guidance to have a significant impact on our consolidated financial position or results of operations upon adoption.

Income Taxes. In July 2013, the FASB issued ASU No. 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. The guidance requires an entity to net their unrecognized tax benefit, or a portion of an unrecognized tax benefit, in the financial statements against a deferred tax asset for a net operating loss carryforward, a similar tax loss or tax credit carryforward, unless such tax loss or credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes resulting from the disallowance of a tax position. In the event that the tax position is disallowed or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit shall be presented in the financial statements as a liability and shall not be combined with deferred tax assets. The guidance is effective for fiscal years and interim periods within those years, beginning after December 15, 2013, and is to be applied prospectively to all unrecognized tax benefits that exist at the effective date. We do not expect that the adoption of this update will have a material effect on our consolidated financial statements.

Note 4. Leucadia and Related Transactions

Leucadia Transaction

On March 1, 2013, Jefferies Group LLC completed a business combination with Leucadia and became a wholly-owned subsidiary of Leucadia as described in Note 1, Organization and Basis of Presentation. Each share of Jefferies Group Inc. s common stock outstanding was converted into common shares of Leucadia at an Exchange Ratio of 0.81 of a Leucadia common share for each share of Jefferies Group, Inc. (the Exchange Ratio). Leucadia exchanged Jefferies Group, Inc. s $125.0 million 3.25% Series A-1 Convertible Cumulative Preferred Stock for a new series of

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Leucadia $125.0 million 3.25% Cumulative Convertible Preferred Shares. In addition, each restricted share and restricted stock unit of Jefferies Group, Inc. common stock was converted at the Exchange Ratio, into an equivalent award of shares of Leucadia, with all such awards for Leucadia shares subject to the same terms and conditions, including, without limitation, vesting and, in the case of performance-based restricted stock units, performance being measured at existing targets.

Leucadia did not assume or guarantee any of our outstanding debt securities, but our 3.875% Convertible senior Debentures due 2029 with an aggregate principal amount of $345.0 million became convertible into common shares of Leucadia. Other than the conversion into Leucadia common shares, the terms of the debenture remain the same.

The Leucadia Transaction resulted in a change in our ownership and was recorded under the acquisition method of accounting by Leucadia and pushed-down to us by allocating the total purchase consideration of $4.8 billion to the cost of the assets acquired, including intangible assets, and liabilities assumed based on their estimated fair values. The excess of the total purchase price over the fair value of assets acquired and the liabilities assumed is recorded as goodwill. The goodwill arising from the Leucadia Transaction consists largely of our commercial potential and the value of our assembled workforce.

In connection with the Leucadia Transaction, we recognized $9.0 million and $2.1 million in transaction costs during the three months ended May 31 and February 28, 2013, respectively.

The summary computation of the purchase price and the fair values assigned to the assets and liabilities are presented as follows (in thousands except share amounts):

Purchase Price		
Jefferies common stock outstanding		205,368,031
Less: Jefferies common stock owned by Leucadia		(58,006,024)
Jefferies common stock acquired by Leucadia		147,362,007
Exchange ratio		0.81
Leucadia s shares issued (excluding for Jefferies shares held by Leucadia)		119,363,226
Less: restricted shares issued for share-based payment awards (1)		(6,894,856)
Leucadia s shares issued, excluding share-based payment awards		112,468,370
Closing price of Leucadia s common stock (2)	$	26.90

Fair value of common shares acquired by Leucadia		3,025,399
Fair value of 3.25% cumulative convertible preferred shares (3)		125,000
Fair value of shares-based payment awards (4)		343,811
Fair value of Jefferies shares owned by Leucadia (5)		1,259,891
Total purchase price	**$**	**4,754,101**

(1) Represents shares of restricted stock included in Jefferies common stock outstanding that contained a future service requirement as of March 1, 2013.

(2) The value of the shares of common stock exchanged with Jefferies shareholders was based upon the closing price of Leucadia s common stock at February 28, 2013, the last trading day prior to the date of acquisition.

(3) Represents Leucadia s 3.25% Cumulative Convertible Preferred Shares issued in exchange for Jefferies Group, Inc. s 3.25% Series A-1 Convertible Cumulative Preferred Stock.

(4) The fair value of share-based payment awards is calculated in accordance with ASC 718, Compensation Stock Compensation. Share-based payment awards attributable to pre-combination service are included as part of the total purchase price. Share-based payment awards attributable to pre-combination service is estimated based on the ratio of the pre-combination service performed to the original service period of the award.

(5) The fair value of Jefferies shares owned by Leucadia was based upon a price of $21.72, the closing price of Jefferies common stock at February 28, 2013.

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Assets acquired:	
Cash and cash equivalents	$ 3,017,958
Cash and securities segregated	3,728,742
Financial instruments owned, at fair value	16,413,535
Investments in managed funds	59,976
Loans to and investments in related parties	766,893
Securities borrowed	5,315,488
Securities purchased under agreements to resell	3,578,366
Securities received as collateral	25,338
Receivables:	
Brokers, dealers and clearing organizations	2,444,085
Customers	1,045,251
Fees, interest and other	225,555
Premises and equipment	192,603
Indefinite-lived intangible exchange memberships and licenses (1)	15,551
Finite-lived intangible customer relationships (1)	136,002
Finite-lived trade name (1)	131,299
Other assets	939,600
Total assets	$ 38,036,242
Liabilities assumed:	
Short-term borrowings	$ 100,000
Financial instruments sold, not yet purchased, at fair value	9,766,876
Securities loaned	1,902,687
Securities sold under agreements to repurchase	7,976,492
Other secured financings	122,294
Obligation to return securities received as collateral	25,338
Payables:	
Brokers, dealers and clearing organizations	1,787,055
Customers	5,450,781
Accrued expenses and other liabilities	793,843
Long-term debt	6,362,024
Mandatorily redeemable preferred interests	358,951
Total liabilities	$ 34,646,341
Noncontrolling interests	356,180

Fair value of net assets acquired, excluding goodwill	$ 3,033,721
Goodwill	$ 1,720,380

(1) Intangible assets are recorded within Other assets on the Consolidated Statements of Financial Condition.
The goodwill of $1.7 billion is not deductible for tax purposes.

Reorganization of Jefferies High Yield Holdings, LLC

On March 1, 2013, we commenced a reorganization of our high yield joint venture with Leucadia, conducted through Jefferies High Yield Holdings, LLC (JHYH) (the parent of Jefferies High Yield Trading, LLC (our high yield trading broker-dealer)). On March 1, 2013, we redeemed the outstanding third party noncontrolling interests in JHYH of $347.6 million. On March 31, 2013, Leucadia contributed its mandatorily redeemable preferred interests in JHYH of $362.3 million to Jefferies Group LLC as member s equity. On April 1, 2013, we redeemed the mandatorily redeemable preferred interests in JHYH received from Leucadia. In addition, on April 1, 2013, our high yield trading broker-dealer was merged into Jefferies LLC (our U.S. securities broker-dealer).

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Note 5. Fair Value Disclosures

The following is a summary of our financial assets and liabilities that are accounted for at fair value on a recurring basis as of May 31, 2014 and November 30, 2013 by level within the fair value hierarchy (in thousands):

	May 31, 2014				
	Level 1	Level 2	Level 3	Counterparty and Cash Collateral Netting (1)	Total
Assets:					
Financial instruments owned:					
Corporate equity securities	$ 1,997,684	$ 345,139	$ 16,402	$	$ 2,359,225
Corporate debt securities		3,171,520	31,648		3,203,168
Collateralized debt obligations		290,292	42,313		332,605
U.S. government and federal agency securities	2,176,254	74,996			2,251,250
Municipal securities		690,649			690,649
Sovereign obligations	1,540,017	1,018,348			2,558,365
Residential mortgage-backed securities		3,024,940	71,962		3,096,902
Commercial mortgage-backed securities		579,591	24,246		603,837
Other asset-backed securities		13,603	45,444		59,047
Loans and other receivables		1,426,045	138,643		1,564,688
Derivatives	87,612	2,813,166	913	(2,648,507)	253,184
Investments at fair value		5,361	118,071		123,432
Physical commodities		47,166			47,166
Total financial instruments owned	$ 5,801,567	$ 13,500,816	$ 489,642	$ (2,648,507)	$ 17,143,518
Cash and cash equivalents	$ 3,958,288	$	$	$	$ 3,958,288
Investments in managed funds	$	$ 19,250	$ 56,119	$	$ 75,369
Cash and securities segregated and on deposit for regulatory purposes (2)	$ 3,288,517	$	$	$	$ 3,288,517
Securities received as collateral	$ 126,106	$	$	$	$ 126,106
Total Level 3 assets			$ 545,761		

Liabilities:

Financial instruments sold, not yet purchased:					
Corporate equity securities	$ 1,632,106	$ 52,160	$ 38	$	$ 1,684,304
Corporate debt securities		1,510,841	2,780		1,513,621
U.S. government and federal agency securities	1,554,835				1,554,835
Municipal securities					
Sovereign obligations	1,517,111	716,275			2,233,386
Residential mortgage-backed securities		16,837			16,837
Loans		872,322	31,534		903,856
Derivatives	75,585	2,881,585	16,195	(2,747,077)	226,288
Physical commodities		39,173			39,173
Total financial instruments sold, not yet purchased	$ 4,779,637	$ 6,089,193	$ 50,547	$ (2,747,077)	$ 8,172,300
Obligation to return securities received as collateral	$ 126,106	$	$	$	$ 126,106
Other secured financings	$	$	$ 20,288	$	$ 20,288
Embedded conversion option	$	$ 3,895	$	$	$ 3,895

(1) Represents counterparty and cash collateral netting across the levels of the fair value hierarchy for positions with the same counterparty.

(2) Cash and securities segregated and on deposit for regulatory purposes include U.S. government securities with a fair value of $564.7 million.

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	November 30, 2013				
	Level 1 (1)	Level 2 (1)	Level 3	Counterparty and Cash Collateral Netting (2)	Total
Assets:					
Financial instruments owned:					
Corporate equity securities	$ 1,913,220	$ 175,493	$ 9,884	$	$ 2,098,597
Corporate debt securities		2,957,102	25,666		2,982,768
Collateralized debt obligations		182,095	37,216		219,311
U.S. government and federal agency	2,293,221	40,389			2,333,610
Municipal securities		664,054			664,054
Sovereign obligations	1,458,803	889,685			2,348,488
Residential mortgage-backed securities		2,932,268	105,492		3,037,760
Commercial mortgage-backed securities		1,130,410	17,568		1,147,978
Other asset-backed securities		55,475	12,611		68,086
Loans and other receivables		1,203,238	145,890		1,349,128
Derivatives	40,952	2,472,237	1,493	(2,253,589)	261,093
Investments at fair value		40	101,242		101,282
Physical commodities		37,888			37,888
Total financial instruments owned	$ 5,706,196	$ 12,740,374	$ 457,062	$ (2,253,589)	$ 16,650,043
Cash and cash equivalents	$ 3,561,119	$	$	$	$ 3,561,119
Investments in managed funds	$	$	$ 57,285	$	$ 57,285
Cash and securities segregated and on deposit for regulatory purposes (3)	$ 3,616,602	$	$	$	$ 3,616,602
Securities received as collateral	$ 11,063	$	$	$	$ 11,063
Total Level 3 assets			$ 514,347		
Liabilities:					
Financial instruments sold,					
Corporate equity securities	$ 1,782,903	$ 40,358	$ 38	$	$ 1,823,299
Corporate debt securities		1,346,078			1,346,078
U.S. government and federal agency securities	1,324,326				1,324,326
Sovereign obligations	1,360,269	471,088			1,831,357
Residential mortgage-backed securities		34,691			34,691

Loans		672,838	22,462		695,300
Derivatives	43,829	2,480,463	8,398	(2,352,611)	180,079
Physical commodities		36,483			36,483
Total financial instruments sold, not yet purchased	$ 4,511,327	$ 5,081,999	$ 30,898	$ (2,352,611)	$ 7,271,613
Obligation to return securities received as collateral	$ 11,063	$	$	$	$ 11,063
Other secured financings	$	$ 31,000	$ 8,711	$	$ 39,711
Embedded conversion option	$	$ 9,574	$	$	$ 9,574

(1) During the nine months ended November 30, 2013, we transferred listed equity options with a fair value of $403.0 million within Financial instruments owned and $423.0 million within Financial instruments sold, not yet purchased from Level 1 to Level 2 as adjustments to the exchange closing price are necessary to best reflect the fair value of the population at its exit price.

(2) Represents counterparty and cash collateral netting across the levels of the fair value hierarchy for positions with the same counterparty.

(3) Cash and securities segregated and on deposit for regulatory purposes include U.S. government securities with a fair value of $304.2 million.

The following is a description of the valuation basis, including valuation techniques and inputs, used in measuring our financial assets and liabilities that are accounted for at fair value on a recurring basis:

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Corporate Equity Securities

Exchange Traded Equity Securities: Exchange-traded equity securities are measured based on quoted closing exchange prices, which are generally obtained from external pricing services, and are categorized within Level 1 of the fair value hierarchy, otherwise they are categorized within Level 2 or Level 3 of the fair value hierarchy.

Non-exchange Traded Equity Securities: Non-exchange traded equity securities are measured primarily using broker quotations, pricing data from external pricing services and prices observed for recently executed market transactions and are categorized within Level 2 of the fair value hierarchy. Where such information is not available, non-exchange traded equity securities are categorized within Level 3 of the fair value hierarchy and measured using valuation techniques involving quoted prices of or market data for comparable companies, similar company ratios and multiples (e.g., price/EBITDA, price/book value), discounted cash flow analyses and transaction prices observed for subsequent financing or capital issuance by the company. When using pricing data of comparable companies, judgment must be applied to adjust the pricing data to account for differences between the measured security and the comparable security (e.g., issuer market capitalization, yield, dividend rate, geographical concentration).

Equity warrants: Non-exchange traded equity warrants are generally categorized within Level 3 of the fair value hierarchy and are measured using the Black-Scholes model with key inputs impacting the valuation including the underlying security price, implied volatility, dividend yield, interest rate curve, strike price and maturity date.

Corporate Debt Securities

Corporate Bonds: Corporate bonds are measured primarily using pricing data from external pricing services and broker quotations, where available, prices observed for recently executed market transactions and bond spreads or credit default swap spreads of the issuer adjusted for basis differences between the swap curve and the bond curve. Corporate bonds measured using these valuation methods are categorized within Level 2 of the fair value hierarchy. If broker quotes, pricing data or spread data is not available, alternative valuation techniques are used including cash flow models incorporating interest rate curves, single name or index credit default swap curves for comparable issuers and recovery rate assumptions. Corporate bonds measured using alternative valuation techniques are categorized within Level 3 of the fair value hierarchy and comprise a limited portion of our corporate bonds.

High Yield Corporate and Convertible Bonds: A significant portion of our high yield corporate and convertible bonds are categorized within Level 2 of the fair value hierarchy and are measured primarily using broker quotations and pricing data from external pricing services, where available, and prices observed for recently executed market transactions of comparable size. Where pricing data is less observable, valuations are categorized within Level 3 and are based on pending transactions involving the issuer or comparable issuers, prices implied from an issuer s subsequent financings or recapitalizations, models incorporating financial ratios and projected cash flows of the issuer and market prices for comparable issuers.

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Collateralized Debt Obligations

Collateralized debt obligations are measured based on prices observed for recently executed market transactions or based on valuations received from third party brokers and are categorized within Level 2 or Level 3 of the fair value hierarchy depending on the observability and significance of the pricing inputs.

U.S. Government and Federal Agency Securities

U.S. Treasury Securities: U.S. Treasury securities are measured based on quoted market prices and categorized within Level 1 of the fair value hierarchy.

U.S. Agency Issued Debt Securities: Callable and non-callable U.S. agency issued debt securities are measured primarily based on quoted market prices obtained from external pricing services. Non-callable U.S. agency securities are generally categorized within Level 1 and callable U.S. agency securities are categorized within Level 2 of the fair value hierarchy.

Municipal Securities

Municipal securities are measured based on quoted prices obtained from external pricing services and are generally categorized within Level 2 of the fair value hierarchy.

Sovereign Obligations

Foreign sovereign government obligations are measured based on quoted market prices obtained from external pricing services, where available, or recently executed independent transactions of comparable size. To the extent external price quotations are not available or recent transactions have not been observed, valuation techniques incorporating interest rate yield curves and country spreads for bonds of similar issuers, seniority and maturity are used to determine fair value of sovereign bonds or obligations. Foreign sovereign government obligations are classified in Level 1, 2 or Level 3 of the fair value hierarchy, primarily based on the country of issuance.

Residential Mortgage-Backed Securities

Agency Residential Mortgage-Backed Securities: Agency residential mortgage-backed securities include mortgage pass-through securities (fixed and adjustable rate), collateralized mortgage obligations and interest-only and principal-only securities and are generally measured using market price quotations from external pricing services and categorized within Level 2 of the fair value hierarchy.

Agency Residential Inverse Interest-Only Securities (Agency Inverse IOs): The fair value of agency inverse IOs is estimated using expected future cash flow techniques that incorporate prepayment models and other prepayment assumptions to amortize the underlying mortgage loan collateral. We use prices observed for recently executed transactions to develop market-clearing spread and yield curve assumptions. Valuation inputs with regard to the underlying collateral incorporate weighted average coupon, loan-to-value, credit scores, geographic location, maximum and average loan size, originator, servicer, and weighted average loan age. Agency inverse IOs are categorized within Level 2 or Level 3 of the fair value hierarchy. We also use vendor data in developing our assumptions, as appropriate.

Non-Agency Residential Mortgage-Backed Securities: Fair values are determined primarily using discounted cash flow methodologies and securities are categorized within Level 2 or Level 3 of the fair value hierarchy based on the observability and significance of the pricing inputs used. Performance attributes of the underlying mortgage loans are evaluated to estimate pricing inputs, such as prepayment rates, default rates and the severity of credit losses. Attributes of the underlying mortgage loans that affect the pricing inputs include, but are not limited to, weighted average coupon; average and maximum loan size; loan-to-value; credit scores; documentation type; geographic location; weighted average loan age; originator; servicer; historical prepayment, default and loss severity experience of the mortgage loan pool; and delinquency rate. Yield curves used in the discounted cash flow models are based on observed market prices for comparable securities and published interest rate data to estimate market yields.

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Commercial Mortgage-Backed Securities

Agency Commercial Mortgage-Backed Securities: GNMA project loan bonds and FNMA Delegated Underwriting and Servicing (DUS) mortgage-backed securities are generally measured by using prices observed for recently executed market transactions to estimate market-clearing spread levels for purposes of estimating fair value. GNMA project loan bonds and FNMA DUS mortgage-backed securities are categorized within Level 2 of the fair value hierarchy.

Non-Agency Commercial Mortgage-Backed Securities: Non-agency commercial mortgage-backed securities are measured using pricing data obtained from external pricing services and prices observed for recently executed market transactions and are categorized within Level 2 and Level 3 of the fair value hierarchy.

Other Asset-Backed Securities

Other asset-backed securities include, but are not limited to, securities backed by auto loans, credit card receivables and student loans and are categorized within Level 2 and Level 3 of the fair value hierarchy. Valuations are determined using pricing data obtained from external pricing services and prices observed for recently executed market transactions.

Loans and Other Receivables

Corporate Loans: Corporate loans categorized within Level 2 of the fair value hierarchy are measured based on market price quotations where market price quotations from external pricing services are supported by market transaction data. Corporate loans categorized within Level 3 of the fair value hierarchy are measured based on market price quotations that are considered to be less transparent, market prices for debt securities of the same creditor, and estimates of future cash flow incorporating assumptions regarding creditor default and recovery rates and consideration of the issuer s capital structure.

Participation Certificates in GNMA Project and Construction Loans: Valuations of participation certificates in GNMA project and construction loans are based on observed market prices of recently executed purchases of similar loans which are then used to derive a market implied spread, which in turn is used as the primary input in estimating the fair value of loans at the measurement date. The loan participation certificates are categorized within Level 2 of the fair value hierarchy given the observability and volume of recently executed transactions.

Project Loans: Valuation of project loans are based on benchmarks of prices for recently executed transactions of related realized collateralized securities and are categorized within Level 2 of the fair value hierarchy.

Escrow and Trade Claim Receivables: Escrow and trade claim receivables are categorized within Level 3 of the fair value hierarchy where fair value is estimated based on reference to market prices and implied yields of debt securities of the same or similar issuers. Escrow and trade claim receivables are categorized within Level 2 of the fair value hierarchy where fair value is based on recent trade activity in the same security.

Derivatives

Listed Derivative Contracts: Listed derivative contracts that are actively traded are measured based on quoted exchange prices, which are generally obtained from external pricing services, and are categorized within Level 1 of the fair value hierarchy. Listed derivatives for which there is limited trading activity are measured based on incorporating the closing auction price of the underlying equity security, use similar valuation approaches as those applied to over-the-counter derivative contracts and are categorized within Level 2 of the fair value hierarchy.

OTC Derivative Contracts: Over-the-counter (OTC) derivative contracts are generally valued using models, whose inputs reflect assumptions that we believe market participants would use in valuing the derivative in a current period transaction. Inputs to valuation models are appropriately calibrated to market data. For many OTC

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derivative contracts, the valuation models do not involve material subjectivity as the methodologies do not entail significant judgment and the inputs to valuation models do not involve a high degree of subjectivity as the valuation model inputs are readily observable or can be derived from actively quoted markets. OTC derivative contracts are primarily categorized within Level 2 of the fair value hierarchy given the observability and significance of the inputs to the valuation models. Where significant inputs to the valuation are unobservable, derivative instruments are categorized within Level 3 of the fair value hierarchy.

OTC options include OTC equity, foreign exchange and commodity options measured using various valuation models, such as the Black-Scholes, with key inputs impacting the valuation including the underlying security, foreign exchange spot rate or commodity price, implied volatility, dividend yield, interest rate curve, strike price and maturity date. Discounted cash flow models are utilized to measure certain OTC derivative contracts including the valuations of our interest rate swaps, which incorporate observable inputs related to interest rate curves, valuations of our foreign exchange forwards and swaps, which incorporate observable inputs related to foreign currency spot rates and forward curves and valuations of our commodity swaps, which incorporate observable inputs related to commodity spot prices and forward curves. Credit default swaps include both index and single-name credit default swaps. External prices are available as inputs in measuring index credit default swaps and single-name credit default swaps. For commodity and equity total return swaps, market prices are observable for the underlying asset and used as the basis for measuring the fair value of the derivative contracts. Total return swaps executed on other underlyings are measured based on valuations received from external pricing services.

Physical Commodities

Physical commodities include base and precious metals and are measured using observable inputs including spot prices and published indices. Physical commodities are categorized within Level 2 of the fair value hierarchy. To facilitate the trading in precious metals we undertake leasing of such precious metals. The fees earned or paid for such leases are recorded as Principal transaction revenues on the Consolidated Statements of Earnings.

Investments at Fair Value and Investments in Managed Funds

Investments at fair value and Investments in managed funds include investments in hedge funds, fund of funds, private equity funds, convertible bond funds and commodity funds, which are measured at fair value based on the net asset value of the funds provided by the fund managers and are categorized within Level 2 or Level 3 of the fair value hierarchy. Investments at fair value also include direct equity investments in private companies, which are measured at fair value using valuation techniques involving quoted prices of or market data for comparable companies, similar company ratios and multiples (e.g., price/EBITDA, price/book value), discounted cash flow analyses and transaction prices observed for subsequent financing or capital issuance by the company. Direct equity investments in private companies are categorized within Level 2 or Level 3 of the fair value hierarchy. Additionally, investments at fair value include investments in insurance contracts relating to our defined benefit plan in Germany. Fair value for the insurance contracts is determined using a third party and is categorized within Level 3 of the fair value hierarchy.

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The following tables present information about our investments in entities that have the characteristics of an investment company at May 31, 2014 and November 30, 2013 (in thousands):

	May 31, 2014		
	Fair Value (6)	Unfunded Commitments	Redemption Frequency (if currently eligible)
Equity Long/Short Hedge Funds (1)	$ 38,315	$	Monthly, Quarterly
High Yield Hedge Funds(2)	232		
Fund of Funds(3)	388	94	
Equity Funds(4)	69,047	27,409	
Convertible Bond Funds(5)	3,647		At Will
Total(7)	$ 111,629	$ 27,503	

	November 30, 2013		
	Fair Value (6)	Unfunded Commitments	Redemption Frequency (if currently eligible)
Equity Long/Short Hedge Funds (1)	$ 20,927	$	Monthly, Quarterly
High Yield Hedge Funds(2)	244		
Fund of Funds(3)	494	94	
Equity Funds(4)	66,495	40,816	
Convertible Bond Funds(5)	3,473		At Will
Total(7)	$ 91,633	$ 40,910	

(1) This category includes investments in hedge funds that invest, long and short, in equity securities in domestic and international markets in both the public and private sectors. At May 31, 2014 and November 30, 2013, investments representing approximately 99% and 98%, respectively, of the fair value of investments in this category are redeemable with 30 - 65 days prior written notice, and includes an investment in a private asset management fund managed by us with a fair value of $15.6 million at May 31, 2014. The remaining investments in this category cannot be redeemed as they are in liquidation and distributions will be received through the liquidation of the underlying assets of the funds. We are unable to estimate when the underlying assets will be liquidated.

(2)

Includes investments in funds that invest in domestic and international public high yield debt, private high yield investments, senior bank loans, public leveraged equities, distressed debt, and private equity investments. There are no redemption provisions. The underlying assets of the funds are being liquidated and we are unable to estimate when the underlying assets will be fully liquidated.

(3) Includes investments in fund of funds that invest in various private equity funds. At May 31, 2014 and November 30, 2013, approximately 96% and 98%, respectively, of the fair value of investments in this category are managed by us and have no redemption provisions, instead distributions are received through the liquidation of the underlying assets of the fund of funds, which are estimated to be liquidated in approximately two years. For the remaining investments we have requested redemption; however, we are unable to estimate when these funds will be received.

(4) At May 31, 2014 and November 30, 2013, investments representing approximately 99% and 99%, respectively of the fair value of investments in this category include investments in equity funds that invest in the equity of various U.S. and foreign private companies in the energy, technology, internet service and telecommunication service industries. These investments cannot be redeemed, instead distributions are received through the liquidation of the underlying assets of the funds which are expected to liquidate in one to eight years. The remaining investments are in liquidation and we are unable to estimate when the underlying assets will be fully liquidated. At May 31, 2014 and November 30, 2013, this category includes investments in equity funds managed by us with a fair value of $56.6 million and $54.4 million and unfunded commitments of $25.8 million and $39.2 million, respectively.

(5) Investment in the Jefferies Umbrella Fund, an open-ended investment company managed by us that invests primarily in convertible bonds. The investment is redeemable with 5 days prior written notice.

(6) Where fair value is calculated based on net asset value, fair value has been derived from each of the funds capital statements.

(7) Investments at fair value in the Consolidated Statements of Financial Condition at May 31, 2014 and November 30, 2013 include $87.2 million and $66.9 million, respectively, of direct investments which do not have the characteristics of investment companies and therefore not included within this table. We have unfunded commitments to such investments of $-0- and $3.3 million in aggregate at May 31