

Jefferies Group LLC
Form 10-Q
October 05, 2016
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended August 31, 2016

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 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 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 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

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).

Table of Contents

JEFFERIES GROUP LLC
INDEX TO QUARTERLY REPORT ON FORM 10-Q
August 31, 2016

PART I. FINANCIAL INFORMATION

	Page
<u>Item 1. Financial Statements</u>	<u>2</u>
<u>Consolidated Statements of Financial Condition (Unaudited)- August 31, 2016 and November 30, 2015</u>	<u>2</u>
<u>Consolidated Statements of Earnings (Unaudited)- Three and Nine Months Ended August 31, 2016 and 2015</u>	<u>3</u>
<u>Consolidated Statements of Comprehensive Income (Unaudited)- Three and Nine Months Ended August 31, 2016 and 2015</u>	<u>4</u>
<u>Consolidated Statements of Changes in Equity (Unaudited)- Nine Months Ended August 31, 2016 and Year Ended November 30, 2015</u>	<u>5</u>
<u>Consolidated Statements of Cash Flows (Unaudited)- Nine Months Ended August 31, 2016 and 2015</u>	<u>6</u>
<u>Notes to Consolidated Financial Statements (Unaudited)</u>	<u>8</u>
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>64</u>
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>93</u>
<u>Item 4. Controls and Procedures</u>	<u>94</u>

PART II. OTHER INFORMATION

<u>Item 1. Legal Proceedings</u>	<u>95</u>
<u>Item 1A. Risk Factors</u>	<u>95</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>95</u>
<u>Item 6. Exhibits</u>	<u>95</u>

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (UNAUDITED)

(In thousands)

	August 31, 2016	November 30, 2015
ASSETS		
Cash and cash equivalents (\$10,442 and \$2,015 at August 31, 2016 and November 30, 2015, respectively, related to consolidated VIEs)	\$3,159,143	\$3,510,163
Cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations	1,026,865	751,084
Financial instruments owned, at fair value, (including securities pledged of \$10,458,629 and \$12,207,123 at August 31, 2016 and November 30, 2015, respectively; and \$91,146 and \$68,951 at August 31, 2016 and November 30, 2015, respectively, related to consolidated VIEs)	14,327,919	16,559,116
Investments in managed funds	191,692	85,775
Loans to and investments in related parties	657,074	825,908
Securities borrowed	8,460,736	6,975,136
Securities purchased under agreements to resell	4,038,194	3,857,306
Receivables:		
Brokers, dealers and clearing organizations	1,938,174	1,574,759
Customers	849,317	1,191,316
Fees, interest and other (\$549 and \$329 at August 31, 2016 and November 30, 2015, respectively, related to consolidated VIEs)	293,072	260,924
Premises and equipment	254,674	243,486
Goodwill	1,645,293	1,656,588
Other assets	1,285,524	1,072,411
Total assets	\$38,127,677	\$38,563,972
LIABILITIES AND EQUITY		
Short-term borrowings	\$432,235	\$310,659
Financial instruments sold, not yet purchased, at fair value	7,944,072	6,785,064
Collateralized financings:		
Securities loaned	2,930,376	2,979,300
Securities sold under agreements to repurchase	8,130,434	10,004,428
Other secured financings (includes \$53,586 and \$68,345 at fair value at August 31, 2016 and November 30, 2015, respectively; and \$606,307 and \$762,909 at August 31, 2016 and November 30, 2015, respectively, related to consolidated VIEs)	606,307	762,909
Payables:		
Brokers, dealers and clearing organizations	3,495,173	2,742,001
Customers	2,749,325	2,780,493
Accrued expenses and other liabilities (\$764 and \$893 at August 31, 2016 and November 30, 2015, respectively, related to consolidated VIEs)	1,030,425	1,049,019
Long-term debt (includes \$204,422 and \$0 at fair value at August 31, 2016 and November 30, 2015, respectively)	5,482,738	5,640,722
Total liabilities	32,801,085	33,054,595
EQUITY		
Member's paid-in capital	5,450,923	5,526,855
Accumulated other comprehensive loss:		

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Currency translation adjustments	(116,859)	(36,811)
Changes in instrument specific credit risk	(4,771)	—)
Additional minimum pension liability	(7,891)	(8,135)
Total accumulated other comprehensive loss	(129,521)	(44,946)
Total member's equity	5,321,402		5,481,909	
Noncontrolling interests	5,190		27,468	
Total equity	5,326,592		5,509,377	
Total liabilities and equity	\$38,127,677		\$38,563,972	

See accompanying notes to consolidated financial statements.

2

Table of ContentsJEFFERIES GROUP LLC AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS (UNAUDITED)

(In thousands)

	Three Months Ended August 31,		Nine Months Ended August 31,	
	2016	2015	2016	2015
Revenues:				
Commissions and other fees	\$152,044	\$172,284	\$454,025	\$512,714
Principal transactions	167,483	(50,297)	382,290	211,142
Investment banking	294,930	389,820	778,906	1,066,077
Asset management fees and investment income (loss) from managed funds	15,877	4,182	29,743	(5)
Interest	213,716	230,805	655,836	700,227
Other	19,791	34,329	(6,937)	82,810
Total revenues	863,841	781,123	2,293,863	2,572,965
Interest expense	209,391	202,195	621,018	610,811
Net revenues	654,450	578,928	1,672,845	1,962,154
Non-interest expenses:				
Compensation and benefits	376,438	336,499	1,141,497	1,182,484
Non-compensation expenses:				
Floor brokerage and clearing fees	40,189	45,307	124,259	159,100
Technology and communications	64,512	89,378	196,000	234,126
Occupancy and equipment rental	24,987	25,967	74,498	74,571
Business development	20,259	30,527	67,700	78,865
Professional services	29,761	24,684	82,799	76,359
Other	17,582	19,473	52,649	51,960
Total non-compensation expenses	197,290	235,336	597,905	674,981
Total non-interest expenses	573,728	571,835	1,739,402	1,857,465
Earnings (loss) before income taxes	80,722	7,093	(66,557)	104,689
Income tax expense	39,564	4,609	5,112	29,470
Net earnings (loss)	41,158	2,484	(71,669)	75,219
Net earnings (loss) attributable to noncontrolling interests	(11)	427	77	1,647
Net earnings (loss) attributable to Jefferies Group LLC	\$41,169	\$2,057	\$(71,746)	\$73,572
See accompanying notes to consolidated financial statements.				

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

(In thousands)

	Three Months Ended August 31,		Nine Months Ended August 31,	
	2016	2015	2016	2015
Net earnings (loss)	\$41,158	\$2,484	\$(71,669)	\$75,219
Other comprehensive income (loss), net of tax:				
Currency translation and other adjustments	(55,945)	(319)	(79,804)	(11,376)
Changes in instrument specific credit risk (1)	(2,466)	—	(4,771)	—
Total other comprehensive income (loss), net of tax (2)	(58,411)	(319)	(84,575)	(11,376)
Comprehensive income (loss)	(17,253)	2,165	(156,244)	63,843
Net earnings attributable to noncontrolling interests	(11)	427	77	1,647
Comprehensive income (loss) attributable to Jefferies Group LLC	\$(17,242)	\$1,738	\$(156,321)	\$62,196

(1) Includes income tax benefit of approximately \$1.6 million and \$3.1 million for the three and nine months ended August 31, 2016, respectively.

(2) None of the components of other comprehensive income (loss) are attributable to noncontrolling interests. See accompanying notes to consolidated financial statements.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (UNAUDITED)
(In thousands)

	Nine Months Ended August 31, 2016	Year Ended November 30, 2015
Member's paid-in capital:		
Balance, beginning of period	\$5,526,855	\$5,439,256
Net earnings (loss) attributable to Jefferies Group LLC	(71,746)	93,534
Tax detriment for issuance of share-based awards	(4,186)	(5,935)
Balance, end of period	\$5,450,923	\$5,526,855
Accumulated other comprehensive income (loss) (1) (2):		
Balance, beginning of period	\$(44,946)	\$(14,673)
Currency adjustments	(80,048)	(27,157)
Changes in instrument specific credit risk, net of tax	(4,771)	—
Pension adjustment, net of tax	244	(3,116)
Balance, end of period	(129,521)	(44,946)
Total member's equity	\$5,321,402	\$5,481,909
Noncontrolling interests:		
Balance, beginning of period	\$27,468	\$38,848
Net earnings attributable to noncontrolling interests	77	1,795
Contributions	4,500	—
Distributions	(563)	(4,982)
Deconsolidation of asset management company	(26,292)	(8,193)
Balance, end of period	\$5,190	\$27,468
Total equity	\$5,326,592	\$5,509,377

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

(2) There were no material reclassifications out of Accumulated other comprehensive income (loss) during the nine months ended August 31, 2016 and the year ended November 30, 2015.

See accompanying notes to consolidated financial statements.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(In thousands)

	Nine Months Ended August 31,	
	2016	2015
Cash flows from operating activities:		
Net earnings (loss)	\$(71,669)	\$75,219
Adjustments to reconcile net earnings (loss) to net cash used in operating activities:		
Depreciation and amortization	(2,888)	10,784
Loss (income) on loans to and investments in related parties	15,862	(87,692)
Distributions received on investments in related parties	11,187	70,825
Other adjustments	13,359	(64,479)
Net change in assets and liabilities:		
Cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations	(277,019)	2,538,334
Receivables:		
Brokers, dealers and clearing organizations	(392,632)	100,690
Customers	341,930	(52,530)
Fees, interest and other	(35,514)	(41,759)
Securities borrowed	(1,510,588)	(852,183)
Financial instruments owned	2,079,134	(321,076)
Investments in managed funds	(132,941)	14,508
Securities purchased under agreements to resell	(248,931)	(351,875)
Other assets	(237,291)	(8,988)
Payables:		
Brokers, dealers and clearing organizations	781,782	192,867
Customers	(31,159)	(3,454,703)
Securities loaned	(22,326)	1,049,172
Financial instruments sold, not yet purchased	1,269,261	601,758
Securities sold under agreements to repurchase	(1,824,027)	176,960
Accrued expenses and other liabilities	68,024	(228,986)
Net cash used in operating activities	(206,446)	(633,154)
Cash flows from investing activities:		
Contributions to loans to and investments in related parties	(343,835)	(1,111,830)
Distributions from loans to and investments in related parties	485,620	1,119,775
Net payments on premises and equipment	(51,001)	(51,348)
Payment on purchase of aircraft	(27,500)	—
Proceeds from sale of aircraft	29,450	—
Deconsolidation of asset management entity	(39)	(16,512)
Cash received from contingent consideration	1,211	2,541
Net cash provided by (used in) investing activities	93,906	(57,374)
Continued on next page.		

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS – CONTINUED (UNAUDITED)
(In thousands)

	Nine Months Ended August 31,	
	2016	2015
Cash flows from financing activities:		
Excess tax benefits from the issuance of share-based awards	\$384	\$423
Proceeds from short-term borrowings	8,350,534	14,422,000
Payments on short-term borrowings	(8,229,669)	(14,422,000)
Proceeds from secured credit facility	—	903,000
Payments on secured credit facility	—	(1,073,000)
Net (payments on) proceeds from other secured financings	(156,602)	200,810
Net proceeds from issuance of long-term debt, net of issuance costs	239,779	—
Repayment of long-term debt	(373,246)	—
Net change in bank overdrafts	(56,126)	24,466
Net proceeds from noncontrolling interests	3,937	—
Net cash (used in) provided by financing activities	(221,009)	55,699
Effect of exchange rate changes on cash and cash equivalents	(17,471)	(3,354)
Net decrease in cash and cash equivalents	(351,020)	(638,183)
Cash and cash equivalents at beginning of period	3,510,163	4,079,968
Cash and cash equivalents at end of period	\$3,159,143	\$3,441,785
Supplemental disclosures of cash flow information:		
Cash paid (received) during the period for:		
Interest	\$675,896	\$621,279
Income taxes, net	(8,011)	1,574
See accompanying notes to consolidated financial statements.		

Table of ContentsJEFFERIES GROUP LLC AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Index	
Note	Page
<u>Note 1. Organization and Basis of Presentation</u>	<u>9</u>
<u>Note 2. Summary of Significant Accounting Policies</u>	<u>10</u>
<u>Note 3. Accounting Developments</u>	<u>16</u>
<u>Note 4. Fair Value Disclosures</u>	<u>18</u>
<u>Note 5. Derivative Financial Instruments</u>	<u>36</u>
<u>Note 6. Collateralized Transactions</u>	<u>40</u>
<u>Note 7. Securitization Activities</u>	<u>43</u>
<u>Note 8. Variable Interest Entities</u>	<u>44</u>
<u>Note 9. Investments</u>	<u>48</u>
<u>Note 10. Goodwill and Other Intangible Assets</u>	<u>50</u>
<u>Note 11. Short-Term Borrowings</u>	<u>52</u>
<u>Note 12. Long-Term Debt</u>	<u>53</u>
<u>Note 13. Noncontrolling Interests</u>	<u>54</u>
<u>Note 14. Benefit Plans</u>	<u>54</u>
<u>Note 15. Compensation Plans</u>	<u>55</u>
<u>Note 16. Income Taxes</u>	<u>56</u>
<u>Note 17. Commitments, Contingencies and Guarantees</u>	<u>57</u>
<u>Note 18. Net Capital Requirements</u>	<u>59</u>
<u>Note 19. Segment Reporting</u>	<u>60</u>
<u>Note 20. Related Party Transactions</u>	<u>61</u>
<u>Note 21. Exit Costs</u>	<u>62</u>

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(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. The accompanying Consolidated Financial Statements represent the accounts of Jefferies Group LLC 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 International Limited, Jefferies Hong Kong Limited, Jefferies Financial Services, Inc., Jefferies Funding LLC, Jefferies Financial Products, LLC, Jefferies Leveraged Credit Products, LLC and all other entities in which we have a controlling financial interest or are the primary beneficiary. On April 9, 2015, we entered into an agreement to transfer certain of the client activities of our Futures business to Société Générale S.A. and initiated a plan to substantially exit the remaining aspects of our futures business. During the second quarter of 2016, we completed the exit of the futures business. For further information on the exit of the Bache business, refer to Note 21, Exit Costs.

Jefferies Group LLC is an indirect wholly owned subsidiary of Leucadia National Corporation (“Leucadia”). Leucadia does not guarantee any of our outstanding debt securities. Our 3.875% Convertible Senior Debentures due 2029 are convertible into Leucadia common shares (see Note 12, Long-Term Debt, for further details). Jefferies Group LLC operates as a full-service investment banking firm and, as the holding company of its various regulated and unregulated operating subsidiaries, retains a credit rating separate from Leucadia and is a Securities and Exchange Commission (“SEC”) reporting company, filing annual, quarterly and periodic financial reports. Richard Handler, our Chief Executive Officer and Chairman, is the Chief Executive Officer of Leucadia, as well as a Director of Leucadia. Brian P. Friedman, our Chairman of the Executive Committee, is 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.

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, 2015.

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.

Consolidation

Our policy is to consolidate all entities that we control by ownership a majority of the outstanding voting stock. In addition, we consolidate entities that meet the definition of a variable interest entity (“VIE”) for which we are the primary beneficiary. The primary beneficiary is the party who has the power to direct the activities of a VIE 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 is presented as Net earnings to noncontrolling interests in the Consolidated Statements of Earnings.

In situations in which we have significant influence, but not control, of an entity that does not qualify as a VIE, 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.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

Immaterial Adjustments

We made immaterial correcting adjustments (referred to as “adjustments”) to our Consolidated Statement of Cash Flows for the nine months ended August 31, 2015. The adjustments had the impact of decreasing the Net change in accrued expenses and other liabilities by \$24.5 million (\$204.5 million as originally reported and \$228.9 million as revised), increasing the Net change in bank overdrafts by \$24.5 million (\$0.0 as originally reported and \$24.5 million as revised), decreasing the Net cash used in operating activities by \$24.5 million (\$608.7 million as originally reported and \$633.1 million as revised) and increasing the Net cash provided by financing activities by \$24.5 million (\$31.2 million as originally reported and \$55.7 million as revised) on the Consolidated Statements of Cash Flows for the nine months ended August 31, 2015. The adjustments relate to a classification error in the reporting of net change in bank overdrafts within our Consolidated Statements of Cash Flows. The adjustments have no effect on our Consolidated Statements of Financial Condition, the Consolidated Statements of Earnings, the Consolidated Statements of Changes in Equity or the Consolidated Statements of Comprehensive Income for the nine months ended August 31, 2015. We do not believe these adjustments are material to our financial statements for any previously reported period.

Note 2. Summary of Significant Accounting Policies

Revenue Recognition Policies

Commissions and Other Fees. 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. In addition, we earn asset-based fees associated with the management and supervision of assets, account services and administration related to customer accounts.

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 transaction revenues in the Consolidated Statements of Earnings on a trade date basis. Fees received on loans carried at fair value are also recorded within Principal transaction revenues.

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.

10

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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 transaction revenues 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.

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. 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. In addition, certain exchange and/or clearing organizations require cash and/or securities to be deposited by us to conduct day to day activities.

Financial Instruments and Fair Value

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 transaction revenues 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 at the reported date.

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

Level 2: prices are available but traded less frequently, derivative instruments that fair values for which have been derived using model inputs that 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.

Instruments that have little to no pricing observability at the reported date. These financial instruments are

Level 3: 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 prices and inputs that are current at 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.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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 reflected at fair value. 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 comprises our Chief Financial Officer, Global Controller, 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 independent sources, 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 determines the financial instrument fair values in the consolidated financial statements. This process specifically assists the Chief Financial Officer in 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 determined 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 trading desk's 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.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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. Our processes challenge the appropriateness of pricing information obtained from external data providers (including independent pricing services and brokers) 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 we use independent pricing services or broker quotes 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, collateralized debt obligations ("CDOs") and collateralized loan obligations ("CLOs"), our independent pricing services use 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. If a pricing model is 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 based on the net asset value ("NAV") of the funds provided by the fund managers with gains or losses included in Asset management fees and investment income (loss) from managed funds in the Consolidated Statements of Earnings.

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 9, Investments, and Note 20, Related Party Transactions, for additional information regarding certain of these investments.

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.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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 revenue 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 U.S. GAAP. 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. The carrying values of internally developed software ready for its intended use are depreciated over the remaining useful life.

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, by comparing the implied fair value of the reporting unit's goodwill to the carrying value of the reporting unit's goodwill.

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. Refer to Note 10, Goodwill and Other Intangible Assets, for further information.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

Income Taxes

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. Pursuant to a tax sharing agreement entered into between us and Leucadia, payments are made between us and Leucadia to settle current tax assets and liabilities.

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. We provide deferred taxes on our temporary differences and on any carryforwards that we could claim on our 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 benefits related to share-based awards are recognized as an increase to Additional paid-in capital. These amounts, and other windfall tax benefits/(detriment), are included in Tax benefit/(detriment) for issuance of share-based awards on the Consolidated Statements of Changes in Equity. In the event tax deductions associated with share-based awards are less than the cumulative compensation cost recognized for financial reporting purposes, we look to Leucadia's consolidated pool of windfall tax benefits in the calculation of our income tax provision. During the first quarter of fiscal 2016, the consolidated pool of windfall tax benefits had been exhausted. As a result, these tax detriments are now recognized in our Consolidated Statement of Earnings until such time the Leucadia consolidated cumulative compensation cost recognized for tax purposes exceeds the amount recognized for financial reporting purposes.

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. 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.

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.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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 transaction revenues in the Consolidated Statements of Earnings.

Securitization Activities

We engage in securitization activities related to corporate loans, consumer 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.

Note 3. Accounting Developments

Accounting Standards to be Adopted in Future Periods

Statement of Cash Flows. In August 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-15, Classification of Certain Cash Receipts and Cash Payments. The guidance adds or clarifies guidance on the classification of certain cash receipts and payments in the statement of cash flows. The guidance is effective in the first quarter of fiscal 2019 and early adoption is permitted. We are currently evaluating the impact of the new guidance on our consolidated statements of cash flows.

Financial Instruments-Credit Losses. In June 2016, the FASB issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments. The guidance provides for estimating credit losses on certain types of financial instruments by introducing an approach based on expected losses. The guidance is effective in the first quarter of fiscal 2021 and early adoption is permitted in the first quarter of fiscal 2020. We are currently evaluating the impact of the new guidance on our consolidated financial statements.

Employee Share-Based Payments. In March 2016, the FASB issued ASU No. 2016-09, Improvements to Employee Share-Based Payment Accounting. The guidance simplifies various aspects related to how share-based payments are accounted for and presented in the consolidated financial statements. The amendments include income tax consequences, the accounting for forfeitures, classification of awards as either equity or liabilities and classification on the statement of cash flows. The guidance is effective in the first quarter of fiscal 2018 and early adoption is permitted if all amendments are adopted in the same period. We are currently evaluating the impact of the new guidance on our consolidated financial statements.

Leases. In February 2016, the FASB issued ASU No. 2016-02, Leases. The guidance affects the accounting for leases and provides for a lessee model that brings substantially all leases onto the balance sheet. The guidance is effective in the first quarter of fiscal 2019 and early adoption is permitted. We are currently evaluating the impact of the new guidance on our consolidated financial statements.

Financial Instruments. In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments-Overall:

Recognition and Measurement of Financial Assets and Financial Liabilities. The guidance affects the accounting for equity investments, financial liabilities under the fair value option and the presentation and disclosure requirements of

financial instruments. The guidance is effective in the first quarter of fiscal 2019. We are currently evaluating the impact of the new guidance related to equity investments and the presentation and disclosure requirements of financial instruments on our consolidated financial statements. Early adoption is permitted for the accounting guidance on financial liabilities under the fair value option and we adopted this guidance in the first quarter of fiscal 2016. The adoption of this accounting guidance did not have a material effect on our consolidated financial statements.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

Revenue Recognition. In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers and in August 2015, the FASB issued ASU No. 2015-14, Revenue from Contracts with Customers - Deferral of Effective Date. The accounting guidance defines how companies report revenues from contracts with customers, and also requires enhanced disclosures. We intend to adopt the new guidance on December 1, 2017 and are currently evaluating the impact of the new guidance on our consolidated financial statements.

Adopted Accounting Standards

Debt Issuance Costs. In April 2015, the FASB issued ASU No. 2015-03, Simplifying the Presentation of Debt Issuance Costs. The accounting guidance requires that debt issuance costs related to a recognized debt liability be reported in the Consolidated Statements of Financial Condition as a direct deduction from the carrying amount of that debt liability. The guidance is effective retrospectively and we adopted this guidance in the first quarter of fiscal 2016. The adoption of this accounting guidance did not have a material impact on our Consolidated Statements of Financial Condition.

Consolidation. In February 2015, the FASB issued ASU No. 2015-02, Consolidation (Topic 810): Amendments to the Consolidation Analysis. The amendment eliminates the deferral of certain consolidation standards for entities considered to be investment companies and modifies the consolidation analysis performed on certain types of legal entities. The guidance is effective beginning in the first quarter of fiscal 2017 and we adopted it in the first quarter of fiscal 2016 using a modified retrospective approach. The adoption of this accounting guidance resulted in the deconsolidation of an asset management vehicle, which resulted in the following adjustment to the Consolidated Statement of Financial Condition on December 1, 2015: a decrease of \$27.0 million in Investments in managed funds, a decrease of \$0.7 million in Accrued expense and other liabilities and a decrease of \$26.3 million in Noncontrolling interests. For further information on the adoption of ASU No. 2015-02, refer to Note 8, Variable Interest Entities.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

Note 4. 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, excluding Investments at fair value based on NAV of \$29.5 million and \$36.7 million at August 31, 2016 and November 30, 2015, respectively, by level within the fair value hierarchy (in thousands):

	August 31, 2016			Counterparty and	
	Level 1(1)	Level 2(1)	Level 3	Cash Collateral	Total
				Netting (2)	
Assets:					
Financial instruments owned:					
Corporate equity securities	\$2,019,490	\$108,194	\$22,195	\$ —	\$2,149,879
Corporate debt securities	—	2,494,303	35,007	—	2,529,310
CDOs and CLOs	—	99,794	44,070	—	143,864
U.S. government and federal agency securities	3,029,251	114,601	—	—	3,143,852
Municipal securities	—	550,210	27,257	—	577,467
Sovereign obligations	904,592	1,130,443	—	—	2,035,035
Residential mortgaged-backed securities	—	1,331,959	46,881	—	1,378,840
Commercial mortgage-backed securities	—	320,912	24,593	—	345,505
Other asset-backed securities	—	116,388	61,112	—	177,500
Loans and other receivables	—	1,323,092	78,457	—	1,401,549
Derivatives	2,530	6,206,366	9,560	(5,887,874)) 330,582
Investments at fair value	—	—	85,036	—	85,036
Total financial instruments owned, excluding	\$5,955,863	\$13,796,262	\$434,168	\$ (5,887,874)) \$14,298,419
Investments at fair value based on NAV					
Cash and cash equivalents	\$3,159,143	\$—	\$—	\$—	\$3,159,143
Cash and securities segregated and on deposit for					
regulatory purposes or deposited with clearing and	\$1,026,865	\$—	\$—	\$—	\$1,026,865
depository organizations (3)					
Liabilities:					
Financial instruments sold, not yet purchased:					
Corporate equity securities	\$1,682,196	\$58,834	\$38	\$—	\$1,741,068
Corporate debt securities	—	1,704,627	523	—	1,705,150
U.S. government and federal agency securities	1,213,672	—	—	—	1,213,672
Sovereign obligations	940,451	1,432,580	—	—	2,373,031
Loans	—	538,180	848	—	539,028
Derivatives	373	6,321,172	20,607	(5,970,029)) 372,123
Total financial instruments sold, not yet purchased	\$3,836,692	\$10,055,393	\$22,016	\$ (5,970,029)) \$7,944,072
Other secured financings	\$—	\$53,318	\$268	\$—	\$53,586
Long-term debt	\$—	\$204,422	\$—	\$—	\$204,422

(1) There were no material transfers between Level 1 and Level 2 for the nine months ended August 31, 2016.

(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 or deposited with clearing and depository organizations includes U.S. treasury securities with a fair value of \$99.9 million.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

	November 30, 2015			Counterparty and	
	Level 1 (1)	Level 2 (1)	Level 3	Cash Collateral Netting (2)	Total
Assets:					
Financial instruments owned:					
Corporate equity securities	\$ 1,853,351	\$ 133,732	\$ 40,906	\$ —	\$ 2,027,989
Corporate debt securities	—	2,867,165	25,876	—	2,893,041
CDOs and CLOs	—	89,144	85,092	—	174,236
U.S. government and federal agency securities	2,555,018	90,633	—	—	2,645,651
Municipal securities	—	487,141	—	—	487,141
Sovereign obligations	1,251,366	1,407,955	120	—	2,659,441
Residential mortgage-backed securities	—	2,731,070	70,263	—	2,801,333
Commercial mortgage-backed securities	—	1,014,913	14,326	—	1,029,239
Other asset-backed securities	—	118,629	42,925	—	161,554
Loans and other receivables	—	1,123,044	189,289	—	1,312,333
Derivatives	1,037	4,395,704	19,785	(4,165,446)	251,080
Investments at fair value	—	26,224	53,120	—	79,344
Total financial instruments owned, excluding Investments at fair value based on NAV	\$ 5,660,772	\$ 14,485,354	\$ 541,702	\$ (4,165,446)	\$ 16,522,382
Cash and cash equivalents	\$ 3,510,163	\$ —	\$ —	\$ —	\$ 3,510,163
Cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations	\$ 751,084	\$ —	\$ —	\$ —	\$ 751,084
Liabilities:					
Financial instruments sold, not yet purchased:					
Corporate equity securities	\$ 1,382,377	\$ 36,518	\$ 38	\$ —	\$ 1,418,933
Corporate debt securities	—	1,556,941	—	—	1,556,941
U.S. government and federal agency securities	1,488,121	—	—	—	1,488,121
Sovereign obligations	837,614	505,382	—	—	1,342,996
Residential mortgage-backed securities	—	117	—	—	117
Loans	—	758,939	10,469	—	769,408
Derivatives	364	4,446,639	19,543	(4,257,998)	208,548
Total financial instruments sold, not yet purchased	\$ 3,708,476	\$ 7,304,536	\$ 30,050	\$ (4,257,998)	\$ 6,785,064
Other secured financings (3)	\$ —	\$ 67,801	\$ 544	\$ —	\$ 68,345

(1) There were no material transfers between Level 1 and Level 2 for the year ended November 30, 2015.

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

(3) Level 2 liabilities include \$67.8 million of other secured financings that were previously not disclosed in our Annual Report on Form 10-K for the year ended November 30, 2015.

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:

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 of the fair value hierarchy.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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 are 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.

CDOs and CLOs

CDOs and CLOs are measured based on prices observed for recently executed market transactions of the same or similar security or based on valuations received from third party brokers or data providers and are categorized within Level 2 or Level 3 of the fair value hierarchy depending on the observability and significance of the pricing inputs. Valuation that is based on recently executed market transactions of similar securities incorporates additional review and analysis of pricing inputs and comparability criteria including but not limited to collateral type, tranche type, rating, origination year, prepayment rates, default rates, and severity.

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 and are generally categorized within Level 1 or 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.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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, Level 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 ("RMBS"): Agency RMBS 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 Interest-Only and 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 of the fair value hierarchy. We also use vendor data in developing our assumptions, as appropriate.

Non-Agency RMBS: 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.

Commercial Mortgage-Backed Securities

Agency Commercial Mortgage-Backed Securities ("CMBS"): Government National Mortgage Association ("GNMA") project loans are measured based on inputs corroborated from and benchmarked to observed prices of recent securitization transactions of similar securities with adjustments incorporating an evaluation for various factors, including prepayment speeds, default rates, and cash flow structures as well as the likelihood of pricing levels in the current market environment. Federal National Mortgage Association ("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 CMBS: Non-agency CMBS 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, student loans and other consumer loans and are categorized within Level 2 and Level 3 of the fair value hierarchy. Valuations are primarily determined using pricing data obtained from external pricing services and broker quotes and prices observed for recently executed market transactions.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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 transaction data. Corporate loans categorized within Level 3 of the fair value hierarchy are measured based on 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 Agency Residential Loans: Valuations of participation certificates in agency residential loans are based on observed market prices of recently executed purchases and sales of similar loans. The loan participation certificates are categorized within Level 2 of the fair value hierarchy given the observability and volume of recently executed transactions and availability of data provider pricing.

Project Loans and Participation Certificates in GNMA Project and Construction Loans: Valuations of participation certificates in GNMA project and construction loans are based on inputs corroborated from and benchmarked to observed prices of recent securitizations of assets with similar underlying loan collateral to derive an implied spread. Securitization prices are adjusted to estimate the fair value of the loans incorporating an evaluation for various factors, including prepayment speeds, default rates, and cash flow structures as well as the likelihood of pricing levels in the current market environment. The measurements are categorized within Level 2 of the fair value hierarchy given the observability and volume of recently executed transactions.

Consumer Loans and Funding Facilities: Consumer and small business whole loans and related funding facilities are valued based on observed market transactions incorporating additional valuation inputs including, but not limited to, delinquency and default rates, prepayment rates, borrower characteristics, loan risk grades and loan age. These assets are categorized within Level 2 or Level 3 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.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

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 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, interest rate 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 and forwards, 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.

Investments at Fair Value and Investments in Managed Funds

Investments at fair value based on NAV 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 the NAV of the funds, provided by the fund managers and are excluded from 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.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

The following tables present information about our investments in entities that have the characteristics of an investment company (in thousands):

	August 31, 2016		
	Fair Value (1)	Unfunded Commitments	Redemption Frequency (if currently eligible)
Equity Long/Short Hedge Funds (2)	\$46,195	\$ —	Monthly, Quarterly
Fixed Income and High Yield Hedge Funds (3)	807	—	—
Fund of Funds (4)	226	—	—
Equity Funds (5)	41,716	20,295	—
Multi-asset Funds (6)	132,248	—	Monthly, Quarterly
Total	\$221,192	\$ 20,295	
	November 30, 2015 (7)		
	Fair Value (1)	Unfunded Commitments	Redemption Frequency (if currently eligible)
Equity Long/Short Hedge Funds (2)	\$54,725	\$ —	Monthly, Quarterly
Fixed Income and High Yield Hedge Funds (3)	1,703	—	—
Fund of Funds (4)	287	94	—
Equity Funds (5)	42,111	20,791	—
Multi-asset Funds (6)	23,358	—	Monthly, Quarterly
Convertible Bond Funds (8)	326	—	At Will
Total	\$122,510	\$ 20,885	

(1) Where fair value is calculated based on NAV, fair value has been derived from each of the funds' capital statements.

This category includes investments in hedge funds that invest, long and short, primarily in equity securities in domestic and international markets in both the public and private sectors. At August 31, 2016, approximately 2% of the fair value of investments in this category is classified as being in liquidation.

This category includes investments in funds that invest in loans secured by a first trust deed on property, 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. At November 30, 2015, the underlying assets of 8% of these funds are being liquidated and we are unable to estimate when the underlying assets will be fully liquidated.

This category includes investments in fund of funds that invest in various private equity funds. At August 31, 2016 and November 30, 2015, approximately 98% and 95%, respectively, of the fair value of investments in this category are managed by us and have no redemption provisions. The investments in this category are gradually being liquidated or we have requested redemption, however, we are unable to estimate when these funds will be received.

At August 31, 2016 and November 30, 2015, approximately 99% and 100%, 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.

This category includes investments in hedge funds that invest, long and short, primarily in multi-asset securities in domestic and international markets in both the public and private sectors. At August 31, 2016 and November 30, 2015, investments representing approximately 12% and 100%, respectively, of the fair value of investments in this category are redeemable with 30-90 days prior written notice.

(7)

Prior period amounts have been recast to conform to the current year's presentation due to the presentation of multi-asset funds. Previously, these investments had been classified within equity long/short hedge funds.

This category represents an investment in the Jefferies Umbrella Fund, an open-ended investment company (8) managed by us that invested primarily in convertible bonds. The underlying assets were fully liquidated during the nine months ended August 31, 2016.

Other Secured Financings

Other secured financings that are accounted for at fair value include notes issued by consolidated VIEs, which are classified as Level 2 or Level 3 within the fair value hierarchy. Fair value is based on recent transaction prices for similar assets.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

Long-term Debt-Structured Notes

Long-term debt includes variable rate and fixed to floating rate structured notes that contain various interest rate payment terms and are generally measured using valuation models for the derivative and debt portions of the notes. These models incorporate market price quotations from external pricing sources referencing the appropriate interest rate curves and are generally categorized within Level 2 of the fair value hierarchy. The impact of the Company's own credit spreads is also included based on observed secondary bond market spreads and asset-swap spreads.

Long-term Debt - Embedded Conversion Option

The embedded conversion option presented within long-term debt represents the fair value of the conversion option on Leucadia shares within our 3.875% Convertible Senior Debentures, due November 1, 2029 and categorized as Level 3 within the fair value hierarchy. The conversion option was valued using a convertible bond model using as inputs the price of Leucadia's common stock, the conversion strike price, 252-day historical volatility, a maturity date of November 1, 2017 (the first put date), dividend yield and the risk-free interest rate curve.

The following is a summary of changes in fair value of our financial assets and liabilities that have been categorized within Level 3 of the fair value hierarchy for the three months ended August 31, 2016 (in thousands):

Three Months Ended August 31, 2016

	Balance at May 31, 2016	Total gains/ losses (realized and unrealized) (1)	Purchases	Sales	Settlements	Issuances/ net transfers (out of) Level 3	Balance at August 31, 2016	Change in unrealized gains/ (losses) relating to instruments still held at August 31, 2016 (1)
Assets:								
Financial instruments owned:								
Corporate equity securities	\$48,816	\$(6,492)	\$ 291	\$(49)	\$ —	\$(20,371)	\$22,195	\$(892)
Corporate debt securities	24,113	(145)	10,696	(5,046)	—	5,389	35,007	405
CDOs and CLOs	52,710	(4,067)	4,205	(5,203)	—	(3,575)	44,070	(4,606)
Municipal securities	—	(7,074)	—	—	—	34,331	27,257	(7,074)
Sovereign obligations	120	5	—	(125)	—	—	—	—
RMBS	63,308	(2,343)	1,884	(10,874)	(463)	(4,631)	46,881	(183)
CMBS	24,983	(1,531)	—	—	—	1,141	24,593	(236)
Other asset-backed securities	43,033	(2,247)	3,416	(2,727)	(1,429)	21,066	61,112	(2,202)
Loans and other receivables	104,399	(23,445)	31,512	(10,140)	(16,804)	(7,065)	78,457	(16,044)
Investments at fair value	57,765	(966)	—	(485)	(278)	29,000	85,036	(1,113)
Liabilities:								
Financial instruments sold, not yet purchased:								
Corporate equity securities	\$—	\$—	\$—	\$—	\$—	-\$38	\$38	\$—
Corporate debt securities	—	(27)	—	550	—	—	523	(27)
Net derivatives (2)	4,424	(4,736)	—	11,101	32	601	11,047	(1,589)
Loans	1,896	(402)	—	170	—	(816)	848	(400)
Other secured financings	468	(200)	—	—	—	—	268	200

(1) Realized and unrealized gains/losses are reported in Principal transaction revenues in the Consolidated Statements of Earnings.

(2) Net derivatives represent Financial instruments owned—Derivatives and Financial instruments sold, not yet purchased —Derivatives.

25

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

Analysis of Level 3 Assets and Liabilities for the Three Months Ended August 31, 2016

During the three months ended August 31, 2016, transfers of assets of \$147.0 million from Level 2 to Level 3 of the fair value hierarchy are primarily attributed to:

- Other asset-backed securities of \$27.3 million, CDOs and CLOs of \$23.7 million and RMBS of \$13.7 million, for which no recent trade activity was observed for purposes of determining observable inputs;

- Municipals securities of \$34.3 million and investments at fair value of \$29.0 million due to a lack of observable market transactions.

During the three months ended August 31, 2016, transfers of assets of \$91.8 million from Level 3 to Level 2 are primarily attributed to:

- CDOs and CLOs of \$27.3 million and RMBS of \$18.3 million, for which market trades were observed in the period for either identical or similar securities;

- Corporate equity securities of \$20.5 million due to an increase in observable market transactions;

- Loans and other receivables of \$15.8 million due to a greater number of contributors for certain vendor quotes to support classification within Level 2.

Net losses on Level 3 assets were \$48.3 million and net gains on Level 3 liabilities were \$5.4 million for the three months ended August 31, 2016. Net losses on Level 3 assets were primarily due to decreased valuations in loans and other receivables, municipal securities, corporate equity securities, CDOs and CLOs, RMBS, other asset-backed securities and CMBS. Net gains on level 3 liabilities were primarily due to decreased valuations of certain derivative liabilities.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

The following is a summary of changes in fair value of our financial assets and liabilities that have been categorized within Level 3 of the fair value hierarchy for the nine months ended August 31, 2016 (in thousands):

Nine Months Ended August 31, 2016

	Balance at November 30, 2015	Total gains/ losses (realized and unrealized) (1)	Purchases	Sales	Settlements	Issuances/ net transfers (out of) Level 3	Balance at August 31, 2016	Change in unrealized gains/ (losses) relating to instruments still held at August 31, 2016 (1)
Assets:								
Financial instruments owned:								
Corporate equity securities	\$40,906	\$(8,388)	\$5,225	\$(49)	\$—	\$(15,499)	\$22,195	\$(727)
Corporate debt securities	25,876	5,239	29,629	(20,331)	—	(5,406)	35,007	1,456
CDOs and CLOs	85,092	(24,356)	61,707	(69,397)	(605)	(8,371)	44,070	(13,196)
Municipal securities	—	(1,462)	—	—	—	28,719	27,257	(1,462)
Sovereign obligations	120	5	—	(125)	—	—	—	—
RMBS	70,263	(7,243)	1,948	(13,203)	(1,078)	(3,806)	46,881	228
CMBS	14,326	(4,606)	1,256	(2,023)	—	15,640	24,593	(3,337)
Other asset-backed securities	42,925	(2,420)	66,503	(60,525)	(6,678)	21,307	61,112	(9,993)
Loans and other receivables	189,289	(30,843)	305,920	(206,587)	(163,913)	(15,409)	78,457	(27,714)
Investments at fair value	53,120	(19,055)	26,227	(485)	(834)	26,063	85,036	(11,988)
Liabilities:								
Financial instruments sold, not yet purchased:								
Corporate equity securities	\$38	\$—	\$—	\$—	\$—	\$—	\$38	\$—
Corporate debt securities	—	(27)	—	550	—	—	523	—
Net derivatives (2)	(242)	3,104	—	11,101	(14)	1,606	(4,508)	(5,745)
Loans	10,469	7	—	681	(213)	(10,096)	848	45
Other secured financings	544	(276)	—	—	—	—	268	276

(1) Realized and unrealized gains/losses are reported in Principal transaction revenues in the Consolidated Statements of Earnings.

(2) Net derivatives represent Financial instruments owned—Derivatives and Financial instruments sold, not yet purchased—Derivatives.

Analysis of Level 3 Assets and Liabilities for the Nine Months Ended August 31, 2016

During the nine months ended August 31, 2016, transfers of assets of \$157.8 million from Level 2 to Level 3 of the fair value hierarchy are primarily attributed to:

- Other asset-backed securities of \$38.5 million, RMBS of \$21.7 million, CMBS of \$17.2 and CDOs and CLOs of \$16.9 million, for which no recent trade activity was observed for purposes of determining observable inputs;
- Municipals securities of \$28.7 million and investments at fair value of \$26.1 million due to a lack of observable market transactions;

During the nine months ended August 31, 2016, transfers of assets of \$114.5 million from Level 3 to Level 2 are primarily attributed to:

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CDOs and CLOs of \$25.3 million, RMBS of \$25.5 million and other asset-backed securities of \$17.0 million, for which market trades were observed in the period for either identical or similar securities;

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

Loans and other receivables of \$19.8 million due to a greater number of contributors for certain vendor quotes supporting classification into Level 2;

Corporate equity securities of \$19.2 million due to an increase in observable market transactions.

There were \$10.2 million transfers of loan liabilities from Level 3 to Level 2 due to an increase in observable inputs in the valuation.

Net losses on Level 3 assets were \$93.1 million and net losses on Level 3 liabilities were \$2.8 million for the nine months ended August 31, 2016. Net losses on Level 3 assets were primarily due to decreased valuations of loans and other receivables, CDOs and CLOs, investments at fair value, corporate equity securities, RMBS and municipal securities. Net losses on Level 3 liabilities were primarily due to increased valuations of certain derivative instruments.

The following is a summary of changes in fair value of our financial assets and liabilities that have been categorized within Level 3 of the fair value hierarchy for the three months ended August 31, 2015 (in thousands):

Three Months Ended August 31, 2015

	Balance at May 31, 2015	Total gains/ losses (realized and unrealized) (1)	Purchases	Sales	Settlements	Issuances/ transfers/ to/ Level 3	Net transfers at August 31, 2015	Balance at August 31, 2015	Change in unrealized gains/ (losses) relating to instruments still held at August 31, 2015 (1)
Assets:									
Financial instruments owned:									
Corporate equity securities	\$20,547	\$3,901	\$21,162	\$(5,173)	\$—	\$(1,935)	\$38,502	\$3,803	
Corporate debt securities	31,917	(5,276)	10,395	(17,197)	(1)	4,493	24,331	(5,544)	
CDOs and CLOs	89,007	(12,560)	14,961	—	(13,230)	2,872	81,050	(12,561)	
RMBS	88,695	(3,009)	10,034	(8,424)	(195)	(679)	86,422	655	
CMBS	17,862	(510)	—	(680)	—	(1,525)	15,147	(545)	
Other asset-backed securities	11,857	870	21,913	—	(1,167)	(877)	32,596	813	
Loans and other receivables	108,756	(2,111)	31,269	(603)	(42,529)	617	95,399	(6,182)	
Investments, at fair value	131,343	83,580	—	(127,427)	(277)	(21,010)	66,209	19,675	
Liabilities:									
Financial instruments sold, not yet purchased:									
Corporate equity securities	\$38	\$—	\$—	\$—	\$—	\$(38)	\$—	\$—	
Corporate debt securities	452	(226)	—	—	—	—	226	226	
Net derivatives (2)	(1,586)	(1,020)	(1,432)	11,618	24	416	(857)	7,163	551
Loans	10,732	109	(3,012)	—	—	2,542	10,371	(110)	
Other secured financings	56,060	—	—	—	(3,914)	(51,572)	574	—	
Embedded conversion option	725	(611)	—	—	—	—	114	611	

(1) Realized and unrealized gains/losses are reported in Principal transaction revenues in the Consolidated Statements of Earnings.

(2)

Net derivatives represent Financial instruments owned—Derivatives and Financial instruments sold, not yet purchased —Derivatives.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

Analysis of Level 3 Assets and Liabilities for the Three Months Ended August 31, 2015

During the three months ended August 31, 2015, transfers of assets of \$73.4 million from Level 2 to Level 3 of the fair value hierarchy are primarily attributed to:

• CDOs and CLOs of \$42.8 million, non-agency RMBS of \$17.8 million and CMBS of \$3.7 million for which no recent trade activity was observed for purposes of determining observable inputs;

• Loans and other receivables of \$4.1 million due to a lower number of contributors comprising vendor quotes to support classification within Level 2;

• Corporate debt securities of \$5.0 million due to a lack of observable market transactions.

During the three months ended August 31, 2015, transfers of assets of \$91.4 million from Level 3 to Level 2 are primarily attributed to:

• Non-agency RMBS of \$18.5 million and CMBS of \$5.2 million for which market trades were observed in the period for either identical or similar securities;

• CDOs and CLOs of \$39.9 million due to a greater number of contributors for certain vendor quotes supporting classification into Level 2;

• Investments at fair value of \$21.0 million due to an increase in observable market transactions;

• Loans and other receivables of \$3.5 million due to a greater number of contributors for certain vendor quotes supporting classification into Level 2;

• Corporate equity securities of \$1.9 million due to an increase in observable market transactions.

There were \$2.5 million transfers of loan liabilities from Level 2 to Level 3 due to a decrease in observable inputs in the valuation and \$51.6 million transfers of other secured financings from Level 3 to Level 2 due to an increase in observable inputs in the valuation.

Net gains on Level 3 assets were \$64.9 million and net gains on Level 3 liabilities were \$1.7 million for the three months ended August 31, 2015. Net gains on Level 3 assets were primarily due to increased valuations of corporate equity securities and investments at fair value, partially offset by a decrease in valuation of CDOs and CLOs, corporate debt securities, RMBS and loans and other receivables. Net gains on Level 3 liabilities were primarily due to decreased valuations of certain derivative instruments.

Table of Contents

JEFFERIES GROUP LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(Unaudited)

The following is a summary of changes in fair value of our financial assets and liabilities that have been categorized within Level 3 of the fair value hierarchy for the nine months ended August 31, 2015 (in thousands):

Nine Months Ended August 31, 2015

	Balance at November 2014	Total gains/ losses (realized and unrealized) (1)	Purchases	Sales	Settlements	Issuances/ contracts	Net transfers (out of) Level 3	Balance at August 31, 2015	Change in unrealized gains/ (losses) relating to instruments still held at August 31, 2015 (1)
Assets:									
Financial instruments owned:									
Corporate equity securities	\$20,964	\$10,247	\$22,631	\$(5,176)	\$ —	\$ —	\$(10,164)	\$38,502	\$10,210
Corporate debt securities	22,766	(5,425)	83,613	(88,711)	(1)	—	12,089	24,331	(5,797)
CDOs and CLOs	124,650	(28,999)	63,038	(47,570)	(20,481)	—	(9,588)	81,050	(22,654)
RMBS	82,557	(6,776)	30,865	(25,222)	(358)	—	5,356	86,422	(2,507)
CMBS	26,655	(2,053)	3,366	(9,973)	(6,981)	—	4,133	15,147	(1,851)
Other asset-backed securities	2,294	666	69,892	(40,000)	(1,438)	—	1,182	32,596	607
Loans and other receivables	97,258	(7,331)	115,370	(40,978)	(82,100)	—	13,180	95,399	(8,850)
Investments, at fair value	53,224	88,195	—	(124,854)	(3,818)	—	53,462	66,209	24,372
Liabilities:									
Financial instruments sold, not yet purchased:									
Corporate equity securities	\$38	\$—	\$—	\$—	\$ —	\$ —	\$(38)	\$—	\$ —
Corporate debt securities	223	(1)	(6,677)	6,804	—	—	(123)	226	(226)
Net derivatives (2)	(4,638)	3,022	(4,527)	11,340	(30)	1,901	95	7,163	(5,211)
Loans	14,450	(102)	(3,487)						