PIPER JAFFRAY COMPANIES
Form 10-Q
July 31, 2013

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

R QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended June 30, 2013
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 No. 001-31720
PIPER JAFFRAY COMPANIES
(Exact Name of Registrant as specified in its Charter)

DELAWARE	30-0168701
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)
800 Nicollet Mall, Suite 1000 Minneapolis, Minnesota	55402
(Address of Principal Executive Offices)	(Zip Code)

(612) 303-6000
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes R 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 R 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer £ Accelerated filer R Non-accelerated filer £ Smaller reporting company £
(Do not check if a smaller reporting company)

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

As of July 26, 2013, the registrant had 16,138,831 shares of Common Stock outstanding.

Piper Jaffray Companies
Index to Quarterly Report on Form 10-Q

PART I. FINANCIAL INFORMATION

ITEM 1.	FINANCIAL STATEMENTS	3
	Consolidated Statements of Financial Condition as of June 30, 2013 (Unaudited) and December 31, 2012	3
	Consolidated Statements of Operations for the three and six months ended June 30, 2013 and June 30, 2012 (Unaudited)	4
	Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2013 and June 30, 2012 (Unaudited)	5
	Consolidated Statements of Cash Flows for the six months ended June 30, 2013 and June 30, 2012 (Unaudited)	6
	Notes to the Consolidated Financial Statements (Unaudited)	7
ITEM 2.	MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	38
ITEM 3.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	69
ITEM 4.	CONTROLS AND PROCEDURES	69

PART II. OTHER INFORMATION

ITEM 1.	LEGAL PROCEEDINGS	69
ITEM 1A.	RISK FACTORS	70
ITEM 2.	UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS	70
ITEM 6.	EXHIBITS	71
	SIGNATURES	72

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

Piper Jaffray Companies
Consolidated Statements of Financial Condition

(Amounts in thousands, except share data)	June 30, 2013 (Unaudited)	December 31, 2012
Assets		
Cash and cash equivalents	$69,274	$105,371
Cash and cash equivalents segregated for regulatory purposes	27,017	31,007
Receivables:		
Customers	20,355	13,795
Brokers, dealers and clearing organizations	122,437	148,117
Securities purchased under agreements to resell	117,311	145,433
Financial instruments and other inventory positions owned	327,082	384,789
Financial instruments and other inventory positions owned and pledged as collateral	1,154,271	826,806
Total financial instruments and other inventory positions owned	1,481,353	1,211,595
Fixed assets (net of accumulated depreciation and amortization of $63,770 and $61,032, respectively)	13,245	15,089
Goodwill	196,844	196,844
Intangible assets (net of accumulated amortization of $27,198 and $23,876, respectively)	37,936	41,258
Other receivables	45,913	44,874
Other assets	144,529	129,697
Assets held for sale	—	4,653
Total assets	$2,276,214	$2,087,733
Liabilities and Shareholders' Equity		
Short-term financing	$542,808	$477,014
Variable rate senior notes	125,000	125,000
Payables:		
Customers	32,686	42,007
Brokers, dealers and clearing organizations	129,479	60,155
Securities sold under agreements to repurchase	—	50,000
Financial instruments and other inventory positions sold, but not yet purchased	481,940	357,201
Accrued compensation	58,596	132,124
Other liabilities and accrued expenses	37,843	53,193
Liabilities held for sale	—	864
Total liabilities	1,408,352	1,297,558
Shareholders' equity:		
Common stock, $0.01 par value:		
Shares authorized: 100,000,000 at June 30, 2013 and December 31, 2012;		
Shares issued: 19,537,127 at June 30, 2013 and 19,530,359 at December 31, 2012;		
	195	195

Shares outstanding: 15,260,727 at June 30, 2013 and 15,213,796 at December 31, 2012		
Additional paid-in capital	739,565	754,566
Retained earnings	131,437	118,803
Less common stock held in treasury, at cost: 4,276,400 shares at June 30, 2013 and 4,316,563 shares at December 31, 2012	(141,863)	(140,939)
Accumulated other comprehensive income	546	667
Total common shareholders’ equity	729,880	733,292
Noncontrolling interests	137,982	56,883
Total shareholders’ equity	867,862	790,175
Total liabilities and shareholders’ equity	$2,276,214	$2,087,733

See Notes to the Consolidated Financial Statements

Table of Contents

Piper Jaffray Companies
Consolidated Statements of Operations
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
(Amounts in thousands, except per share data)	2013	2012	2013	2012
Revenues:				
Investment banking	$52,846	$49,368	$93,208	$97,453
Institutional brokerage	20,560	31,207	63,820	75,287
Asset management	18,031	16,030	36,242	32,563
Interest	14,360	12,139	27,723	23,285
Other income	3,310	979	6,263	1,007
Total revenues	109,107	109,723	227,256	229,595
Interest expense	9,335	6,625	17,951	13,059
Net revenues	99,772	103,098	209,305	216,536
Non-interest expenses:				
Compensation and benefits	65,000	62,601	131,105	131,397
Occupancy and equipment	6,543	6,752	12,360	13,614
Communications	5,030	4,939	10,262	10,836
Floor brokerage and clearance	2,247	2,002	4,397	4,109
Marketing and business development	5,957	5,845	10,937	10,723
Outside services	8,449	7,225	15,663	13,063
Restructuring-related expense	—	3,642	—	3,642
Intangible asset amortization expense	1,661	1,736	3,322	3,472
Other operating expenses	1,552	2,701	(242)	4,803
Total non-interest expenses	96,439	97,443	187,804	195,659
Income from continuing operations before income tax expense/(benefit)	3,333	5,655	21,501	20,877
Income tax expense/(benefit)	1,644	(5,699)	7,244	1,854
Income from continuing operations	1,689	11,354	14,257	19,023
Discontinued operations:				
Loss from discontinued operations, net of tax	(1,871)	(3,934)	(2,392)	(7,237)
Net income/(loss)	(182)	7,420	11,865	11,786
Net income/(loss) applicable to noncontrolling interests	(2,670)	569	(769)	2,006
Net income applicable to Piper Jaffray Companies	$2,488	$6,851	$12,634	$9,780

Net income applicable to Piper Jaffray Companies' common shareholders	$2,266	$5,890	$11,333	$8,344
Amounts applicable to Piper Jaffray Companies				
Net income from continuing operations	$4,359	$10,785	$15,026	$17,017
Net loss from discontinued operations	(1,871)	(3,934)	(2,392)	(7,237)
Net income applicable to Piper Jaffray Companies	$2,488	$6,851	$12,634	$9,780
Earnings/(loss) per basic common share				
Income from continuing operations	$0.25	$0.58	$0.86	$0.91
Loss from discontinued operations	(0.11)	(0.21)	(0.14)	(0.39)
Earnings per basic common share	$0.15	$0.37	$0.73	$0.52
Earnings/(loss) per diluted common share				
Income from continuing operations	$0.25	$0.58	$0.86	$0.91
Loss from discontinued operations	(0.11)	(0.21)	(0.14)	(0.39)
Earnings per diluted common share	$0.15	$0.37	$0.73	$0.52
Weighted average number of common shares outstanding				
Basic	15,621	15,932	15,602	16,002
Diluted	15,626	15,932	15,619	16,002

See Notes to the Consolidated Financial Statements

Table of Contents

Piper Jaffray Companies
Consolidated Statements of Comprehensive Income
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
(Amounts in thousands)	2013	2012	2013	2012
Net income/(loss)	$(182)	$7,420	$11,865	$11,786
Other comprehensive income/(loss), net of tax:				
Foreign currency translation adjustment	27	(79)	(121)	9
Comprehensive income/(loss)	(155)	7,341	11,744	11,795
Comprehensive income/(loss) applicable to noncontrolling interests	(2,670)	569	(769)	2,006
Comprehensive income applicable to Piper Jaffray Companies	$2,515	$6,772	$12,513	$9,789

See Notes to the Consolidated Financial Statements

Table of Contents

Piper Jaffray Companies
Consolidated Statements of Cash Flows
(Unaudited)

	Six Months Ended June 30,	
(Dollars in thousands)	2013	2012
Operating Activities:		
Net income	$11,865	$11,786
Adjustments to reconcile net income to net cash provided by/(used in) operating activities:		
Depreciation and amortization of fixed assets	2,852	3,689
Deferred income taxes	11,571	16,049
Loss on sale of FAMCO	1,876	—
Share-based and deferred compensation	4,890	5,485
Amortization of intangible assets	3,322	3,834
Amortization of forgivable loans	3,226	3,885
Decrease/(increase) in operating assets:		
Cash and cash equivalents segregated for regulatory purposes	3,990	7,999
Receivables:		
Customers	(6,560)	(27,989)
Brokers, dealers and clearing organizations	25,680	(30,479)
Securities purchased under agreements to resell	(2,639)	47,355
Net financial instruments and other inventory positions owned	(145,019)	(410,162)
Other receivables	(177)	(14,529)
Other assets	(26,508)	(9,454)
Increase/(decrease) in operating liabilities:		
Payables:		
Customers	(9,321)	6,427
Brokers, dealers and clearing organizations	69,324	137,358
Securities sold under agreements to repurchase	—	3,289
Accrued compensation	(53,781)	(34,831)
Other liabilities and accrued expenses	(17,876)	(5,354)
Decrease in assets held for sale	605	619
Decrease in liabilities held for sale	(465)	(524)
Net cash used in operating activities	(123,145)	(285,547)
Investing Activities:		
Sale of FAMCO	250	—
Purchases of fixed assets, net	(1,092)	(1,676)
Net cash used in investing activities	(842)	(1,676)
Financing Activities:		
Increase in short-term financing	65,794	259,962
Decrease in bank syndicated financing	—	(26,381)
Increase/(decrease) in securities sold under agreements to repurchase	(19,239)	45,196
Increase in noncontrolling interests	81,868	4,296
Repurchase of common stock	(40,496)	(42,291)

Excess tax benefit from share-based compensation	46	—
Net cash provided by financing activities	87,973	240,782
Currency adjustment:		
Effect of exchange rate changes on cash	(83)	(29)
Net decrease in cash and cash equivalents	(36,097)	(46,470)
Cash and cash equivalents at beginning of period	105,371	85,024
Cash and cash equivalents at end of period	$69,274	$38,554
Supplemental disclosure of cash flow information –		
Cash paid/(received) during the period for:		
Interest	$16,537	$13,636
Income taxes	$671	$(1,827)
Non-cash financing activities –		
Issuance of common stock for retirement plan obligations:		
96,049 shares and 165,241 shares for the six months ended June 30, 2013 and 2012, respectively	$3,939	$3,814
Issuance of restricted common stock for annual equity award:		
431,582 shares and 487,181 shares for the six months ended June 30, 2013 and 2012, respectively	$17,699	$11,244

See Notes to the Consolidated Financial Statements

6

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

Index

Note 1	Organization and Basis of Presentation	8
Note 2	Summary of Significant Accounting Policies	9
Note 3	Recent Accounting Pronouncements	9
Note 4	Discontinued Operations	10
Note 5	Financial Instruments and Other Inventory Positions Owned and Financial Instruments and Other Inventory Positions Sold, but Not Yet Purchased	11
Note 6	Fair Value of Financial Instruments	13
Note 7	Variable Interest Entities	22
Note 8	Receivables from and Payables to Brokers, Dealers and Clearing Organizations	23
Note 9	Collateralized Securities Transactions	23
Note 10	Other Assets	25
Note 11	Goodwill and Intangible Assets	25
Note 12	Short-Term Financing	26
Note 13	Variable Rate Senior Notes	26
Note 14	Bank Syndicated Financing	27
Note 15	Legal Contingencies	27
Note 16	Restructuring	28
Note 17	Shareholders' Equity	28
Note 18	Noncontrolling Interests	29
Note 19	Compensation Plans	30
Note 20	Earnings Per Share	34
Note 21	Segment Reporting	34
Note 22	Net Capital Requirements and Other Regulatory Matters	36
Note 23	Income Taxes	37
Note 24	Subsequent Events	37

Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

Note 1 Organization and Basis of Presentation

Organization

Piper Jaffray Companies is the parent company of Piper Jaffray & Co. (“Piper Jaffray”), a securities broker dealer and investment banking firm; Piper Jaffray Ltd., a firm providing securities brokerage and mergers and acquisitions services in Europe headquartered in London, England; Advisory Research, Inc. (“ARI”), which provides asset management services to separately managed accounts, closed-end and open-end funds and partnerships; Piper Jaffray Investment Group Inc., which consists of entities providing alternative asset management services; Piper Jaffray Financial Products Inc., Piper Jaffray Financial Products II Inc. and Piper Jaffray Financial Products III Inc., entities that facilitate derivative transactions; and other immaterial subsidiaries. Piper Jaffray Companies and its subsidiaries (collectively, the “Company”) operate in two reporting segments: Capital Markets and Asset Management. A summary of the activities of each of the Company’s business segments is as follows:

Capital Markets

The Capital Markets segment provides institutional sales, trading and research services and investment banking services. Institutional sales, trading and research services focus on the trading of equity and fixed income products with institutions, government and non-profit entities. Revenues are generated through commissions and sales credits earned on equity and fixed income institutional sales activities, net interest revenues on trading securities held in inventory, and profits and losses from trading these securities. Investment banking services include management of and participation in underwritings, merger and acquisition services and public finance activities. Revenues are generated through the receipt of advisory and financing fees. Also, the Company generates revenue through strategic trading activities, which focus on proprietary investments in municipal bond and non-agency mortgage-backed securities, and merchant banking activities, which involve equity or debt investments in late stage private companies. As certain of these efforts have matured and an investment process has been developed, the Company has created alternative asset management funds in merchant banking and municipal securities in order to invest firm capital as well as seek capital from outside investors. The Company receives management and performance fees for managing these funds.

As discussed in Note 4, the Company discontinued its Hong Kong capital markets business in 2012.

Asset Management

The Asset Management segment provides traditional asset management services with product offerings in equity securities and master limited partnerships to institutions and individuals. Revenues are generated in the form of management and performance fees. Revenues are also generated through investments in the partnerships and funds that the Company manages.

As discussed in Note 4, Fiduciary Asset Management, LLC (“FAMCO”) was sold on April 30, 2013.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”) and include the accounts of Piper Jaffray Companies, its wholly owned

subsidiaries, and all other entities in which the Company has a controlling financial interest. Noncontrolling interests represent equity interests in consolidated entities that are not attributable, either directly or indirectly, to Piper Jaffray Companies. Noncontrolling interests include the minority equity holders' proportionate share of the equity in a municipal bond fund, merchant banking fund and private equity investment vehicles. All material intercompany balances have been eliminated.

The preparation of financial statements and related disclosures in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates and assumptions are based on the best information available, actual results could differ from those estimates.

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

Note 2 Summary of Significant Accounting Policies

Refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2012 for a full description of the Company's significant accounting policies.

Note 3 Recent Accounting Pronouncements

Adoption of New Accounting Standards

Disclosures about Offsetting Assets and Liabilities

In December 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2011-11, "Disclosures about Offsetting Assets and Liabilities," ("ASU 2011-11") amending FASB Accounting Standards Codification Topic 210, "Balance Sheet." The amended guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. In January 2013, the FASB issued ASU No. 2013-01, "Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities," ("ASU 2013-01") to limit the scope of ASU 2011-11 to derivatives, repurchase agreements, and securities lending arrangements. ASU 2011-11 and ASU 2013-01 were effective for the Company as of January 1, 2013. The adoption of ASU 2011-11 and ASU 2013-01 did not impact the Company's results of operations or financial position, but did impact the Company's disclosures about the offsetting of certain assets and liabilities, and related arrangements.

Indefinite-Lived Intangible Assets

In July 2012, the FASB issued ASU No. 2012-02, "Testing Indefinite-Lived Intangible Assets for Impairment," ("ASU 2012-02") amending FASB Accounting Standards Codification Topic 350, "Intangibles - Goodwill and Other." The amended guidance permits companies to first assess qualitative factors in determining whether the fair value of an indefinite-lived intangible asset is less than its carrying amount. ASU 2012-02 was effective for annual and interim indefinite-lived intangible asset impairment tests performed by the Company for the fiscal year beginning as of January 1, 2013. The adoption of ASU 2012-02 did not impact the Company's results of operations or financial position.

Future Adoption of New Accounting Standards

Investment Companies

In June 2013, the FASB issued ASU No. 2013-08, "Financial Services - Investment Companies (Topic 946): Amendments to the Scope, Measurement, and Disclosure Requirements," ("ASU 2013-08") amending FASB Accounting Standards Codification Topic 946, "Financial Services - Investment Companies" ("ASC 946"). The amended guidance changes the approach to the investment company assessment in ASC 946, clarifies the characteristics of an investment company and requires new disclosures for investment company financial statements. ASU 2013-08 is effective for interim and annual periods beginning after December 15, 2013. The adoption of ASU 2013-08 is not expected to have a material impact on the Company's results of operations, financial position or disclosures.

Note 4 Discontinued Operations

The Company's Hong Kong capital markets business ceased operations as of September 30, 2012. In accordance with the provisions of FASB Accounting Standards Codification Topic 205-20, "Discontinued Operations," the results from this business, previously reported in the Capital Markets segment, have been classified as discontinued operations for all periods presented.

The components of discontinued operations for the Hong Kong capital markets business are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2013	2012	2013	2012
Net revenues	$—	$1,896	$—	$3,951
Total non-interest expenses	(38)	5,767	359	10,707
Income/(loss) from discontinued operations before income tax expense/(benefit)	38	(3,871)	(359)	(6,756)
Income tax expense/(benefit)	(17)	24	(90)	60
Income/(loss) from discontinued operations, net of tax	$55	$(3,895)	$(269)	$(6,816)

On April 30, 2013, the Company completed the sale of FAMCO for consideration of $4.0 million under a previously announced definitive agreement. The sale consideration of $4.0 million consisted of $0.3 million in cash and a $3.7 million note receivable from the buyer. FAMCO's results, previously reported in the Asset Management segment, have been presented as discontinued operations for all periods presented and the related assets and liabilities were classified as held for sale as of December 31, 2012. The disposal group primarily consisted of intangible assets, other receivables and accrued compensation. As part of the sale, the Company indemnified the buyer against certain costs and obligations associated with an administrative proceeding the SEC is pursuing against former FAMCO employees and any related matters stemming from this SEC investigation. The estimated fair value of this indemnification was included within the $1.9 million net loss recorded as part of this transaction. As of June 30, 2013, $3.0 million related to this indemnification was included within other liabilities and accrued expenses on the consolidated statements of financial condition. The potential amount of future payments that the Company could be required to make with respect to the administrative proceeding against the employees pursuant to the terms of the definitive sale agreement is not limited.

The components of discontinued operations for FAMCO are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2013	2012	2013	2012
Net revenues	$440	$1,403	$1,716	$2,775
Total non-interest expenses	538	1,534	2,121	2,872
Loss from discontinued operations before income tax expense/(benefit)	(98)	(131)	(405)	(97)

Income tax expense/(benefit)	(48)	(92)	(158)	324
Loss from discontinued operations	(50)	(39)	(247)	(421)
Loss on sale, net of tax	(1,876)	—	(1,876)	—
Loss from discontinued operations, net of tax	$(1,926)	$(39)	$(2,123)	$(421)

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

Note 5 Financial Instruments and Other Inventory Positions Owned and Financial Instruments and Other Inventory Positions Sold, but Not Yet Purchased

Financial instruments and other inventory positions owned and financial instruments and other inventory positions sold, but not yet purchased were as follows:

(Dollars in thousands)	June 30, 2013	December 31, 2012
Financial instruments and other inventory positions owned:		
Corporate securities:		
Equity securities	$9,228	$16,478
Convertible securities	71,604	44,978
Fixed income securities	29,194	33,668
Municipal securities:		
Taxable securities	319,037	164,059
Tax-exempt securities	479,884	418,189
Short-term securities	122,898	68,328
Asset-backed securities	152,034	116,195
U.S. government agency securities	249,988	304,259
U.S. government securities	13,369	4,966
Derivative contracts	34,117	40,475
Total financial instruments and other inventory positions owned	1,481,353	1,211,595
Less noncontrolling interests (1)	(224,700)	(103,480)
	$1,256,653	$1,108,115
Financial instruments and other inventory positions sold, but not yet purchased:		
Corporate securities:		
Equity securities	$54,345	$27,090
Convertible securities	899	1,015
Fixed income securities	15,815	19,314
Municipal securities:		
Short-term securities	—	60
U.S. government agency securities	102,104	73,724
U.S. government securities	304,668	231,043
Derivative contracts	4,109	4,955
Total financial instruments and other inventory positions sold, but not yet purchased	481,940	357,201
Less noncontrolling interests (2)	(67,322)	(27,308)
	$414,618	$329,893

(1) Noncontrolling interests consist of $122.7 million and $43.8 million of taxable municipal securities, $99.8 million and $58.0 million of tax-exempt municipal securities, and $2.2 million and $1.7 million of derivative contracts attributable to third party noncontrolling interests in a consolidated municipal bond fund as of June 30, 2013 and December 31, 2012, respectively.

(2)

Noncontrolling interests consist of $67.3 million and $27.3 million of U.S. government securities attributable to third party noncontrolling interests in a consolidated municipal bond fund at June 30, 2013 and December 31, 2012, respectively.

At June 30, 2013 and December 31, 2012, financial instruments and other inventory positions owned in the amount of $1.2 billion and $826.8 million, respectively, had been pledged as collateral for short-term financings and repurchase agreements.

Financial instruments and other inventory positions sold, but not yet purchased represent obligations of the Company to deliver the specified security at the contracted price, thereby creating a liability to purchase the security in the market at prevailing prices. The Company is obligated to acquire the securities sold short at prevailing market prices, which may exceed the amount reflected on the consolidated statements of financial condition. The Company economically hedges changes in the market value of its financial instruments and other inventory positions owned using inventory positions sold, but not yet purchased, interest rate derivatives, credit default swap index contracts, futures and exchange-traded options.

Derivative Contract Financial Instruments

The Company uses interest rate swaps, interest rate locks and credit default swap index contracts to facilitate customer transactions and as a means to manage risk in certain inventory positions. The following describes the Company's derivatives by the type of transaction or security the instruments are economically hedging.

Customer matched-book derivatives: The Company enters into interest rate derivative contracts in a principal capacity as a dealer to satisfy the financial needs of its customers. The Company simultaneously enters into an interest rate derivative contract with a third party for the same notional amount to hedge the interest rate and credit risk of the initial client interest rate derivative contract. In certain limited instances, the Company has only hedged interest rate risk with a third party, and retains uncollateralized credit risk as described below. The instruments use interest rates based upon either the London Interbank Offer Rate ("LIBOR") index or the Securities Industry and Financial Markets Association ("SIFMA") index.

Trading securities derivatives: The Company enters into interest rate derivative contracts to hedge interest rate and market value risks associated with its fixed income securities. The instruments use interest rates based upon either the Municipal Market Data ("MMD") index, LIBOR or the SIFMA index. The Company also enters into credit default swap index contracts to hedge credit risk associated with its taxable fixed income securities.

The following table presents the total absolute notional contract amount associated with the Company's outstanding derivative instruments:

(Dollars in thousands) Transaction Type or Hedged Security	Derivative Category	June 30, 2013	December 31, 2012
Customer matched-book	Interest rate derivative contract	$5,380,431	$5,569,096
Trading securities	Interest rate derivative contract	254,000	244,250
Trading securities	Credit default swap index contract	344,233	230,650
		$5,978,664	$6,043,996

The Company's interest rate derivative contracts and credit default swap index contracts do not qualify for hedge accounting, therefore, unrealized gains and losses are recorded on the consolidated statements of operations. The following table presents the Company's unrealized gains/(losses) on derivative instruments:

(Dollars in thousands)		Three Months Ended June 30,		Six Months Ended June 30,	
Derivative Category	Operations Category	2013	2012	2013	2012
Interest rate derivative contract	Investment banking	$(111)	$(864)	$(649)	$(1,605)
Interest rate derivative contract	Institutional brokerage	15,527	(5,414)	21,462	(3,269)
Credit default swap index contract	Institutional brokerage	3,143	1,271	1,268	360
		$18,559	$(5,007)	$22,081	$(4,514)

The gross fair market value of all derivative instruments and their location on the Company's consolidated statements of financial condition prior to counterparty netting are shown below by asset or liability position (1):

(Dollars in thousands)		Asset Value at		Liability Value at
Derivative Category	Financial Condition Location	June 30, 2013	Financial Condition Location	June 30, 2013
Interest rate derivative contract	Financial instruments and other inventory positions owned	$439,707	Financial instruments and other inventory positions sold, but not yet purchased	$395,675
Credit default swap index contract	Financial instruments and other inventory positions owned	11,242	Financial instruments and other inventory positions sold, but not yet purchased	6,011
		$450,949		$401,686

(1) Amounts are disclosed at gross fair value in accordance with the requirements of FASB Accounting Standards Codification Topic 815, "Derivatives and Hedging" ("ASC 815").

Derivatives are reported on a net basis by counterparty (i.e., the net payable or receivable for derivative assets and liabilities for a given counterparty) when a legal right of offset exists and on a net basis by cross product when applicable provisions are stated in master netting agreements. Cash collateral received or paid is netted on a counterparty basis, provided a legal right of offset exists.

Credit risk associated with the Company's derivatives is the risk that a derivative counterparty will not perform in accordance with the terms of the applicable derivative contract. Credit exposure associated with the Company's derivatives is driven by uncollateralized market movements in the fair value of the contracts with counterparties and is monitored regularly by the Company's financial risk committee. The Company considers counterparty credit risk in determining derivative contract fair value. The majority of the Company's derivative contracts are substantially collateralized by its counterparties, who are major financial institutions. The Company has a limited number of counterparties who are not required to post collateral. Based on market movements, the uncollateralized amounts representing the fair value of the derivative contract can become material, exposing the Company to the credit risk of these counterparties. As of June 30, 2013, the Company had $24.3 million of uncollateralized credit exposure with these counterparties (notional contract amount of $202.0 million), including $12.4 million of uncollateralized credit exposure with one counterparty.

Note 6 Fair Value of Financial Instruments

Based on the nature of the Company's business and its role as a "dealer" in the securities industry or as a manager of alternative asset management funds, the fair values of its financial instruments are determined internally. The Company's processes are designed to ensure that the fair values used for financial reporting are based on observable inputs wherever possible. In the event that observable inputs are not available, unobservable inputs are developed based on an evaluation of all relevant empirical market data, including prices evidenced by market transactions, interest rates, credit spreads, volatilities and correlations and other security-specific information. Valuation adjustments related to illiquidity or counterparty credit risk are also considered. In estimating fair value, the Company may utilize information provided by third-party pricing vendors to corroborate internally-developed fair value estimates.

The Company employs specific control processes to determine the reasonableness of the fair value of its financial instruments. The Company's processes are designed to ensure that the internally estimated fair values are accurately recorded and that the data inputs and the valuation techniques used are appropriate, consistently applied, and that the assumptions are reasonable and consistent with the objective of determining fair value. Individuals outside of the trading departments perform independent pricing verification reviews as of each reporting date. The Company has established parameters which set forth when the fair value of securities are independently verified. The selection parameters are generally based upon the type of security, the level of estimation risk of a security, the materiality of the security to the Company's financial statements, changes in fair value from period to period, and other specific facts and circumstances of the Company's securities portfolio. In evaluating the initial internally-estimated fair values made by the Company's traders, the nature and complexity of securities involved (e.g., term, coupon, collateral, and other key drivers of value), level of market activity for securities, and availability of market data are considered. The independent price verification procedures include, but are not limited to, analysis of trade data (both internal and external where available), corroboration to the valuation of positions with similar characteristics, risks and components, or comparison to an alternative pricing source, such as a discounted cash flow model. The Company's valuation committee, comprised of members of senior management, provides oversight and overall responsibility for the internal control processes and procedures related to fair value measurements.

The following is a description of the valuation techniques used to measure fair value.

Cash Equivalents

Cash equivalents include highly liquid investments with original maturities of 90 days or less. Actively traded money market funds are measured at their net asset value and classified as Level I.

Financial Instruments and Other Inventory Positions Owned

The Company records financial instruments and other inventory positions owned and financial instruments and other inventory positions sold, but not yet purchased at fair value on the consolidated statements of financial condition with unrealized gains and losses reflected on the consolidated statements of operations.

Equity securities – Exchange traded equity securities are valued based on quoted prices from the exchange for identical assets or liabilities as of the period-end date. To the extent these securities are actively traded and valuation adjustments are not applied, they are categorized as Level I. Non-exchange traded equity securities (principally hybrid preferred securities) are measured primarily using broker quotations, prices observed for recently executed market transactions and internally-developed fair value estimates based on observable inputs and are categorized within Level II of the fair value hierarchy.

Convertible securities – Convertible securities are valued based on observable trades, when available. Accordingly, these convertible securities are categorized as Level II. When observable price quotations are not available, fair value is determined using model-based valuation techniques with observable market inputs, such as specific company stock price and volatility, and unobservable inputs such as option adjusted spreads over the U.S. treasury securities curve. These instruments are categorized as Level III.

Corporate fixed income securities – Fixed income securities include corporate bonds which are valued based on recently executed market transactions of comparable size, internally-developed fair value estimates based on observable inputs, or broker quotations. Accordingly, these corporate bonds are categorized as Level II. When observable price quotations or certain observable inputs are not available, fair value is determined using model-based valuation techniques with observable inputs such as specific security contractual terms and yield curves, and unobservable inputs such as credit spreads over U.S. treasury securities. Corporate bonds measured using model-based valuation techniques are categorized as Level III.

Taxable municipal securities – Taxable municipal securities are valued using recently executed observable trades or market price quotations and therefore are generally categorized as Level II.

Tax-exempt municipal securities – Tax-exempt municipal securities are valued using recently executed observable trades or market price quotations and therefore are generally categorized as Level II. Certain illiquid tax-exempt municipal securities are valued using market data for comparable securities (maturity and sector) and management judgment to infer an appropriate current yield or other model-based valuation techniques deemed appropriate by management based on the specific nature of the individual security and are therefore categorized as Level III.

Short-term municipal securities – Short-term municipal securities include auction rate securities, variable rate demand notes, and other short-term municipal securities. Variable rate demand notes and other short-term municipal securities are valued using recently executed observable trades or market price quotations and therefore are generally categorized as Level II. Auction rate securities with limited liquidity are categorized as Level III and are valued using discounted cash flow models with unobservable inputs such as the Company's expectations of recovery rate on the securities.

Asset-backed securities – Asset-backed securities are valued using observable trades, when available. Certain asset-backed securities are valued using models where inputs to the model are directly observable in the market, or can be derived principally from or corroborated by observable market data. These asset-backed securities are categorized as Level II. Other asset-backed securities, which are principally collateralized by residential mortgages, have experienced low volumes of executed transactions resulting in less observable transaction data. Certain asset-backed securities collateralized by residential mortgages are valued using cash flow models that utilize unobservable inputs including credit default rates, prepayment rates, loss severity and valuation yields. As judgment is used to determine the range of these inputs, these asset-backed securities are categorized as Level III.

U.S. government agency securities – U.S. government agency securities include agency debt bonds and mortgage bonds. Agency debt bonds are valued by using either direct price quotes or price quotes for comparable bond securities and are categorized as Level II. Mortgage bonds include bonds secured by mortgages, mortgage pass-through securities, agency collateralized mortgage-obligation ("CMO") securities and agency interest-only securities. Mortgage pass-through securities, CMO securities and interest-only securities are valued using recently executed observable trades or other observable inputs, such as prepayment speeds and therefore are generally categorized as Level II. Mortgage bonds are valued using observable market inputs, such as market yields ranging from 140-200 basis points ("bps") on spreads over U.S. treasury securities, or models based upon prepayment expectations ranging from 250-350 Public Securities Association ("PSA") prepayment levels. These securities are categorized as Level II.

U.S. government securities – U.S. government securities include highly liquid U.S. treasury securities which are generally valued using quoted market prices and therefore categorized as Level I. The Company does not transact in securities of countries other than the U.S. government.

Derivatives – Derivative contracts include interest rate and basis swaps, forward purchase agreements, interest rate locks, futures and credit default swap index contracts. These instruments derive their value from underlying assets, reference rates, indices or a combination of these factors. The majority of the Company's interest rate derivative contracts, including both interest rate swaps

and interest rate locks, are valued using market standard pricing models based on the net present value of estimated future cash flows. The valuation models used do not involve material subjectivity as the methodologies do not entail significant judgment and the pricing inputs are market observable, including contractual terms, yield curves and measures of volatility. These instruments are classified as Level II within the fair value hierarchy. Certain interest rate locks transact in less active markets and were valued using valuation models that used the previously mentioned observable inputs and certain unobservable inputs that required significant judgment, such as the premium over the MMD curve. These instruments are classified as Level III. The Company’s credit default swap index contracts are valued using market price quotations and are classified as Level II.

Investments

The Company’s investments valued at fair value include equity investments in private companies, investments in public companies and warrants of public or private companies. These investments are included in other assets on the consolidated statements of financial condition. Exchange traded direct equity investments in public companies and registered mutual funds are valued based on quoted prices on active markets and classified as Level I. Company-owned warrants, which have a cashless exercise option, are valued based upon the Black-Scholes option-pricing model and certain unobservable inputs. The Company applies a liquidity discount to the value of its warrants in public and private companies. For warrants in private companies, valuation adjustments, based upon management’s judgment, are made to account for differences between the measured security and the stock volatility factors of comparable companies. Company-owned warrants are reported as Level III assets. Equity securities in private companies are valued based on an assessment of each underlying security, considering rounds of financing and third-party transactions, discounted cash flow analyses and market-based information, including comparable company transactions, trading multiples and changes in market outlook, among other factors. These securities are generally categorized as Level III.

Fair Value Option – The fair value option permits the irrevocable fair value option election on an instrument-by-instrument basis at initial recognition of an asset or liability or upon an event that gives rise to a new basis of accounting for that instrument. The fair value option was elected for certain merchant banking and other investments at inception to reflect economic events in earnings on a timely basis. At June 30, 2013, $21.4 million in merchant banking and other equity investments, included within other assets on the consolidated statements of financial condition, are accounted for at fair value and are classified as Level III assets. The gains from fair value changes included in earnings as a result of electing to apply the fair value option to certain financial assets were $5.5 million and $1.1 million for the six months ended June 30, 2013 and 2012, respectively.

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

The following table summarizes quantitative information about the significant unobservable inputs used in the fair value measurement of the Company's Level III financial instruments as of June 30, 2013:

	Valuation Technique	Unobservable Input	Range	Weighted Average
Assets:				
Financial instruments and other inventory positions owned:				
Corporate securities:				
Convertible securities	Discounted cash flow	Option adjusted spreads over the U.S. treasury securities curve (1)	2,266 - 5,818 bps	2,946 bps
Municipal securities:				
Tax-exempt securities	Discounted cash flow	Debt service coverage ratio (2)	5 - 69%	24.7%
Short-term securities	Discounted cash flow	Expected recovery rate (% of par) (2)	77 - 80%	79.6%
Asset-backed securities:				
Collateralized by residential mortgages	Discounted cash flow	Credit default rates (3)	3 - 11%	6.1%
		Prepayment rates (4)	2 - 15%	5.1%
		Loss severity (3)	40 - 85%	68.4%
		Valuation yields (3)	4 - 7%	5.7%
Derivative contracts:				
Interest rate locks	Discounted cash flow	Premium over the MMD curve (1)	2 - 46 bps	21.1 bps
Investments:				
Warrants in public and private companies	Black-Scholes option pricing model	Liquidity discount rates (1)	30 - 40%	38.0%
Warrants in private companies	Black-Scholes option pricing model	Stock volatility factors of comparable companies (2)	38 - 135%	44.3%
Equity securities in private companies	Discounted cash flow/ Market approach	Revenue multiple (2)	2 - 5 times	3.1 times
Liabilities:				
Financial instruments and other inventory positions sold, but not yet purchased:				
Derivative contracts:				
Interest rate locks	Discounted cash flow	Premium over the MMD curve (1)	24.2 bps	24.2 bps

Sensitivity of the fair value to changes in unobservable inputs:

(1) Significant increase/(decrease) in the unobservable input in isolation would result in a significantly lower/(higher) fair value measurement.

(2) Significant increase/(decrease) in the unobservable input in isolation would result in a significantly higher/(lower) fair value measurement.

(3) Significant changes in any of these inputs in isolation could result in a significantly different fair value. Generally, a change in the assumption used for credit default rates is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally inverse change in the assumption for valuation yields.

(4)

The potential impact of changes in prepayment rates on fair value is dependent on other security-specific factors, such as the par value and structure. Changes in the prepayment rates may result in directionally similar or directionally inverse changes in fair value depending on whether the security trades at a premium or discount to the par value.

Table of Contents

Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

The following table summarizes the valuation of the Company's financial instruments by pricing observability levels defined in FASB Accounting Standards Codification Topic 820, "Fair Value Measurement" ("ASC 820") as of June 30, 2013:

(Dollars in thousands)	Level I	Level II	Level III	Counterparty and Cash Collateral Netting (1)	Total
Assets:					
Financial instruments and other inventory positions owned:					
Corporate securities:					
Equity securities	$7,996	$1,232	$—	$—	$9,228
Convertible securities	—	70,296	1,308	—	71,604
Fixed income securities	—	29,094	100	—	29,194
Municipal securities:					
Taxable securities	—	319,037	—	—	319,037
Tax-exempt securities	—	478,451	1,433	—	479,884
Short-term securities	—	122,242	656	—	122,898
Asset-backed securities	—	638	151,396	—	152,034
U.S. government agency securities	—	249,988	—	—	249,988
U.S. government securities	13,369	—	—	—	13,369
Derivative contracts	—	433,070	17,879	(416,832)	34,117
Total financial instruments and other inventory positions owned:	21,365	1,704,048	172,772	(416,832)	1,481,353
Cash equivalents	51,117	—	—	—	51,117
Investments	6,425	—	53,567	—	59,992
Total assets	$78,907	$1,704,048	$226,339	$(416,832)	$1,592,462
Liabilities:					
Financial instruments and other inventory positions sold, but not yet purchased:					
Corporate securities:					
Equity securities	$54,345	$—	$—	$—	$54,345
Convertible securities	—	899	—	—	899
Fixed income securities	—	15,815	—	—	15,815
U.S. government agency securities	—	102,104	—	—	102,104
U.S. government securities	304,668	—	—	—	304,668
Derivative contracts	—	401,432	254	(397,577)	4,109
Total financial instruments and other inventory positions sold, but not yet purchased:	$359,013	$520,250	$254	$(397,577)	$481,940

(1)

Represents cash collateral and the impact of netting on a counterparty basis. The Company had no securities posted as collateral to its counterparties.

17

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

The following table summarizes the valuation of the Company's financial instruments by pricing observability levels defined in ASC 820 as of December 31, 2012:

(Dollars in thousands)	Level I	Level II	Level III	Counterparty and Cash Collateral Netting (1)	Total
Assets:					
Financial instruments and other inventory positions owned:					
Corporate securities:					
Equity securities	$3,180	$13,298	$—	$—	$16,478
Convertible securities	—	44,978	—	—	44,978
Fixed income securities	—	33,668	—	—	33,668
Municipal securities:					
Taxable securities	—	164,059	—	—	164,059
Tax-exempt securities	—	416,760	1,429	—	418,189
Short-term securities	—	67,672	656	—	68,328
Asset-backed securities	—	24	116,171	—	116,195
U.S. government agency securities	—	304,259	—	—	304,259
U.S. government securities	4,966	—	—	—	4,966
Derivative contracts	—	595,486	827	(555,838)	40,475
Total financial instruments and other inventory positions owned:	8,146	1,640,204	119,083	(555,838)	1,211,595
Cash equivalents	51,346	—	—	—	51,346
Investments	5,810	—	33,245	—	39,055
Total assets	$65,302	$1,640,204	$152,328	$(555,838)	$1,301,996
Liabilities:					
Financial instruments and other inventory positions sold, but not yet purchased:					
Corporate securities:					
Equity securities	$25,362	$1,728	$—	$—	$27,090
Convertible securities	—	1,015	—	—	1,015
Fixed income securities	—	19,314	—	—	19,314
Municipal securities:					
Short-term securities	—	60	—	—	60
U.S. government agency securities	—	73,724	—	—	73,724
U.S. government securities	231,043	—	—	—	231,043
Derivative contracts	—	569,764	5,218	(570,027)	4,955
Total financial instruments and other inventory positions sold, but not yet purchased:	$256,405	$665,605	$5,218	$(570,027)	$357,201

(1) Represents cash collateral and the impact of netting on a counterparty basis. The Company had no securities posted as collateral to its counterparties.

The Company's Level III assets were $226.3 million and $152.3 million, or 14.2 percent and 11.7 percent of financial instruments measured at fair value at June 30, 2013 and December 31, 2012, respectively. The value of transfers between levels are recognized at the beginning of the reporting period. There were $0.9 million of transfers of financial assets from Level II to Level III during the three and six months ended June 30, 2013, respectively, related to convertible securities for which no recent trade activity was observed and valuation inputs became unobservable. There were no other transfers between Level I, Level II or Level III for the three and six months ended June 30, 2013, respectively.

Table of Contents

Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

The following tables summarize the changes in fair value associated with Level III financial instruments during the three months ended June 30, 2013 and 2012:

(Dollars in thousands)	Balance at March 31, 2013	Purchases	Sales	Transfers in	Transfers out	Realized gains/ (losses) (1)	Unrealized gains/ (losses) (1)	Balance at June 30, 2013
Assets:								
Financial instruments and other inventory positions owned:								
Corporate securities:								
Convertible securities	$—	$2,559	$(2,308)	$870	$—	$ 9	$ 178	$1,308
Fixed income securities	—	100	—	—	—	—	—	100
Municipal securities:								
Tax-exempt securities	1,431	—	—	—	—	—	2	1,433
Short-term securities	656	—	—	—	—	—	—	656
Asset-backed securities	107,654	162,754	(123,422)	—	—	5,573	(1,163)	151,396
Derivative contracts	2,372	710	(896)	—	—	186	15,507	17,879
Total financial instruments and other inventory positions owned:	112,113	166,123	(126,626)	870	—	5,768	14,524	172,772
Investments	41,653	10,000	—	—	—	—	1,914	53,567
Total assets	$153,766	$176,123	$(126,626)	$870	$—	$ 5,768	$ 16,438	$226,339
Liabilities:								
Financial instruments and other inventory positions sold, but not yet purchased:								
Derivative contracts	$399	$—	$745	$—	$—	$ (745)	$ (145)	$254
Total financial instruments and other inventory positions sold, but not yet purchased:	$399	$—	$745	$—	$—	$ (745)	$ (145)	$254

(1) Realized and unrealized gains/(losses) related to financial instruments, with the exception of customer matched-book derivatives, are reported in institutional brokerage on the consolidated statements of operations. Realized and unrealized gains/(losses) related to customer matched-book derivatives are reported in investment banking. Realized and unrealized gains/(losses) related to investments are reported in investment banking revenues or other income/(loss) on the consolidated statements of operations.

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

(Dollars in thousands)	Balance at March 31, 2012	Purchases	Sales	Transfers in	Transfers out	Realized gains/ (losses) (1)	Unrealized gains/ (losses) (1)	Balance at June 30, 2012
Assets:								
Financial instruments and other inventory positions owned:								
Corporate securities:								
Convertible securities	$2,596	$3,130	$(2,152)	$710	$—	$ (40)	$ (563)	$3,681
Fixed income securities	4,275	—	(11)	—	(4,264)	—	—	—
Municipal securities:								
Tax-exempt securities	3,039	—	(556)	—	—	(190)	80	2,373
Short-term securities	1,930	375	(1,755)	—	—	(945)	789	394
Asset-backed securities	69,747	72,543	(55,499)	—	—	1,953	1,127	89,871
Derivative contracts	2,046	—	(2,289)	—	—	2,289	(1,830)	216
Total financial instruments and other inventory positions owned:	83,633	76,048	(62,262)	710	(4,264)	3,067	(397)	96,535
Investments	20,687	—	(7)	—	—	7	(823)	19,864
Total assets	$104,320	$76,048	$(62,269)	$710	$(4,264)	$ 3,074	$ (1,220)	$116,399
Liabilities:								
Financial instruments and other inventory positions sold, but not yet purchased:								
Derivative contracts	$3,495	$(6,509)	$1,380	$—	$—	$ 5,129	$ 3,584	$7,079
Total financial instruments and other inventory positions sold, but not yet purchased:	$3,495	$(6,509)	$1,380	$—	$—	$ 5,129	$ 3,584	$7,079

(1) Realized and unrealized gains/(losses) related to financial instruments, with the exception of customer matched-book derivatives, are reported in institutional brokerage on the consolidated statements of operations. Realized and unrealized gains/(losses) related to customer matched-book derivatives are reported in investment banking. Realized and unrealized gains/(losses) related to investments are reported in investment banking revenues or other income/(loss) on the consolidated statements of operations.

The following tables summarize the changes in fair value associated with Level III financial instruments during the six months ended June 30, 2013 and 2012:

(Dollars in thousands)	Balance at December 31, 2012	Purchases	Sales	Transfers in	Transfers out	Realized gains/ (losses) (1)	Unrealized gains/ (losses) (1)	Balance at June 30, 2013
Assets:								
Financial instruments and other inventory positions owned:								
Corporate securities:								
Convertible securities	$ —	$2,559	$(2,308)	$870	$—	$ 9	$ 178	$1,308
Fixed income securities	—	100	—	—	—	—	—	100
Municipal securities:								
Tax-exempt securities	1,429	1	—	—	—	(266)	269	1,433
Short-term securities	656	—	—	—	—	—	—	656
Asset-backed securities	116,171	348,412	(327,028)	—	—	20,838	(6,997)	151,396
Derivative contracts	827	710	(982)	—	—	186	17,138	17,879
Total financial instruments and other inventory positions owned:	119,083	351,782	(330,318)	870	—	20,767	10,588	172,772
Investments	33,245	15,362	—	—	—	4	4,956	53,567
Total assets	$ 152,328	$367,144	$(330,318)	$870	$—	$ 20,771	$ 15,544	$226,339
Liabilities:								
Financial instruments and other inventory positions sold, but not yet purchased:								
Derivative contracts	$ 5,218	$(5,650)	$745	$—	$—	$ 4,892	$ (4,951)	$254
Total financial instruments and other inventory positions sold, but not yet purchased:	$ 5,218	$(5,650)	$745	$—	$—	$ 4,892	$ (4,951)	$254

(1) Realized and unrealized gains/(losses) related to financial instruments, with the exception of customer matched-book derivatives, are reported in institutional brokerage on the consolidated statements of operations. Realized and unrealized gains/(losses) related to customer matched-book derivatives are reported in investment banking. Realized and unrealized gains/(losses) related to investments are reported in investment banking revenues or other income/(loss) on the consolidated statements of operations.

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

(Dollars in thousands)	Balance at December 31, 2011	Purchases	Sales	Transfers in	Transfers out	Realized gains/ (losses) (1)	Unrealized gains/ (losses) (1)	Balance at June 30, 2012
Assets:								
Financial instruments and other inventory positions owned:								
Corporate securities:								
Convertible securities	$ —	$3,130	$(2,152)	$2,960	$—	$ (40)	$ (217)	$3,681
Fixed income securities	2,815	38,433	(37,149)	226	(4,263)	49	(111)	—
Municipal securities:								
Tax-exempt securities	3,135	1,550	(1,896)	—	—	(571)	155	2,373
Short-term securities	175	3,075	(1,755)	—	—	(945)	(156)	394
Asset-backed securities	53,088	171,775	(139,440)	—	—	1,596	2,852	89,871
Derivative contracts	—	—	(2,289)	—	—	2,289	216	216
Total financial instruments and other inventory positions owned:	59,213	217,963	(184,681)	3,186	(4,263)	2,378	2,739	96,535
Investments	21,341	—	(10)	—	—	10	(1,477)	19,864
Total assets	$ 80,554	$217,963	$(184,691)	$3,186	$(4,263)	$ 2,388	$ 1,262	$116,399
Liabilities:								
Financial instruments and other inventory positions sold, but not yet purchased:								
Corporate securities:								
Convertible securities	$ 1,171	$—	$—	$—	$(1,171)	$ —	$ —	$—
Fixed income securities	900	(897)	—	—	—	(49)	46	—
Derivative contracts	3,594	(9,420)	1,380	—	—	8,040	3,485	7,079
Total financial instruments and other inventory positions sold, but not yet purchased:	$ 5,665	$(10,317)	$1,380	$—	$(1,171)	$ 7,991	$ 3,531	$7,079

(1) Realized and unrealized gains/(losses) related to financial instruments, with the exception of customer matched-book derivatives, are reported in institutional brokerage on the consolidated statements of operations. Realized and unrealized gains/(losses) related to customer matched-book derivatives are reported in investment banking. Realized and unrealized gains/(losses) related to investments are reported in investment banking revenues or other income/(loss) on the consolidated statements of operations.

The carrying values of some of the Company's financial instruments approximate fair value due to their liquid or short-term nature. Such financial assets and financial liabilities include cash, securities either purchased or sold under

agreements to resell, receivables and payables either from or to customers and brokers, dealers and clearing organizations and short-term financings.

Note 7 Variable Interest Entities

In the normal course of business, the Company periodically creates or transacts with entities that are investment vehicles organized as partnerships or limited liability companies. These entities were established for the purpose of investing in securities of public or private companies, or municipal debt obligations and were initially financed through the capital commitments of the members. The Company has investments in and/or acts as the managing partner of these entities. In certain instances, the Company provides management and investment advisory services for which it earns fees generally based upon the market value of assets under management and may include incentive fees based upon performance. The Company’s aggregate investments in these investment vehicles totaled $107.4 million and $96.9 million at June 30, 2013 and December 31, 2012, respectively, and are recorded in other assets on the consolidated statements of financial condition. The Company’s remaining capital commitments to these entities was $36.1 million at June 30, 2013.

Variable interest entities (“VIEs”) are entities in which equity investors lack the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities. The determination as to whether an entity is a VIE is based on the amount and nature of the members’ equity investment in the entity. The Company also considers other characteristics such as the power through voting rights or similar rights to direct the activities of an entity that most significantly impact the entity’s economic performance. For those entities that meet the deferral provisions defined by FASB ASU No. 2010-10, "Consolidation: Amendments for Certain Investment Funds," ("ASU 2010-10"), the Company considers characteristics such as the ability to influence the decision making about the entity’s activities and how the entity is financed. The Company has identified

certain of the entities described above as VIEs. These VIEs had net assets approximating $0.7 billion and $0.8 billion at June 30, 2013 and December 31, 2012, respectively. The Company's exposure to loss from these VIEs is $6.2 million, which is the carrying value of its capital contributions recorded in other assets on the consolidated statements of financial condition at June 30, 2013. The Company had no liabilities related to these VIEs at June 30, 2013 and December 31, 2012.

The Company is required to consolidate all VIEs for which it is considered to be the primary beneficiary. The determination as to whether the Company is considered to be the primary beneficiary is based on whether the Company has both the power to direct the activities of the VIE that most significantly impact the entity's economic performance and the obligation to absorb losses or the right to receive benefits of the VIE that could potentially be significant to the VIE. For those entities that meet the deferral provisions defined by ASU 2010-10, the determination as to whether the Company is considered to be the primary beneficiary differs in that it is based on whether the Company will absorb a majority of the VIE's expected losses, receive a majority of the VIE's expected residual returns, or both. The Company determined it is not the primary beneficiary of these VIEs and accordingly does not consolidate them. Furthermore, the Company has not provided financial or other support to these VIEs that it was not previously contractually required to provide as of June 30, 2013.

Note 8 Receivables from and Payables to Brokers, Dealers and Clearing Organizations

Amounts receivable from brokers, dealers and clearing organizations included:

(Dollars in thousands)	June 30, 2013	December 31, 2012
Receivable arising from unsettled securities transactions	$42,829	$66,426
Deposits paid for securities borrowed	25,368	32,163
Receivable from clearing organizations	5,188	17,655
Deposits with clearing organizations	37,812	24,717
Securities failed to deliver	3,261	5,440
Other	7,979	1,716
	$122,437	$148,117

Amounts payable to brokers, dealers and clearing organizations included:

(Dollars in thousands)	June 30, 2013	December 31, 2012
Payable arising from unsettled securities transactions	$106,403	$24,643
Payable to clearing organizations	10,352	5,763
Securities failed to receive	5,558	7,459
Other	7,166	22,290
	$129,479	$60,155

Deposits paid for securities borrowed approximate the market value of the securities. Securities failed to deliver and receive represent the contract value of securities that have not been delivered or received by the Company on settlement date.

Note 9 Collateralized Securities Transactions

The Company’s financing and customer securities activities involve the Company using securities as collateral. In the event that the counterparty does not meet its contractual obligation to return securities used as collateral (e.g., pursuant to the terms of a repurchase agreement), or customers do not deposit additional securities or cash for margin when required, the Company may be exposed to the risk of reacquiring the securities or selling the securities at unfavorable market prices in order to satisfy its obligations to its customers or counterparties. The Company seeks to control this risk by monitoring the market value of securities pledged or used as collateral on a daily basis and requiring adjustments in the event of excess market exposure. The Company will also use an unaffiliated third party custodian to administer the underlying collateral for certain of its repurchase agreements and short-term financing to mitigate risk.

A reverse repurchase agreement is a transaction in which the Company purchases financial instruments from a seller, typically in exchange for cash, and simultaneously enters into an agreement to resell the same or substantially the same financial instruments to the seller at a stated price plus accrued interest at a future date. A repurchase agreement is a transaction in which the Company

sells financial instruments to a buyer, typically in exchange for cash, and simultaneously enters into an agreement to repurchase the same or substantially the same financial instruments from the buyer at a stated price plus accrued interest at a future date. Even though repurchase and reverse repurchase agreements involve the legal transfer of ownership of financial instruments, they are accounted for as financing arrangements because they require the financial instruments to be repurchased or resold at maturity of the agreement.

In a securities borrowed transaction, the Company borrows securities from a counterparty in exchange for cash. When the Company returns the securities, the counterparty returns the cash. Interest is generally paid periodically over the life of the transaction.

In the normal course of business, the Company obtains securities purchased under agreements to resell, securities borrowed and margin agreements on terms that permit it to repledge or resell the securities to others, typically pursuant to repurchase agreements. The Company obtained securities with a fair value of approximately $175.6 million and $186.1 million at June 30, 2013 and December 31, 2012, respectively, of which $169.7 million and $174.4 million, respectively, had been pledged or otherwise transferred to satisfy its commitments under financial instruments and other inventory positions sold, but not yet purchased.

The following is a summary of the Company's securities sold under agreements to repurchase ("Repurchase Liabilities"), the fair market value of related collateral pledged and the interest rate charged by the Company's counterparty, which is based on LIBOR plus an applicable margin, as of June 30, 2013:

(Dollars in thousands)	Repurchase Liabilities	Fair Market Value	Interest Rate
On demand maturities:			
U.S. government agency securities	$30,761	$30,103	0.25%

Reverse repurchase agreements, repurchase agreements and securities borrowed and loaned are reported on a net basis by counterparty when a legal right of offset exists. The following table provides information about the offsetting of these instruments and related collateral amounts at June 30, 2013:

(Dollars in thousands) Description	Gross Recognized Assets	Gross Amount Offset on the Consolidated Statements of Financial Condition	Net Amounts Presented on the Consolidated Statements of Financial Condition	Gross Amounts Not Offset on the Consolidated Statements of Financial Condition: Financial Instruments	Collateral Received (1)	Net Amount
Reverse repurchase agreements	$148,072	$(30,761)	$117,311	$—	$(117,311)	$—
Securities borrowed (3)	25,368	—	25,368	—	(25,368)	—

(Dollars in thousands) Description	Gross Recognized Liabilities	Gross Amount Offset on the Consolidated Statements of	Net Amount Presented on the Consolidated Statements of	Gross Amount Not Offset on the Consolidated Statements of Financial Condition: Financial Instruments	Collateral Pledged (2)	Net Amount

		Financial Condition	Financial Condition			
Repurchase agreements	$30,761	$(30,761)	$—	$—	$—	$—

(1) Includes securities received by the Company from the counterparty. These securities are not included on the consolidated statements of financial condition unless there is an event of default.

(2) Includes the fair value of securities pledged by the Company to the counterparty. These securities are included on the consolidated statements of financial condition unless the Company defaults.

(3) Deposits paid for securities borrowed are included in receivables from brokers, dealers and clearing organizations on the consolidated statements of financial condition. See Note 8 for additional information on receivables from brokers, dealers and clearing organizations.

There were no gross amounts offset on the consolidated statements of financial condition for reverse repurchase agreements, securities borrowed or repurchase agreements at December 31, 2012 as a legal right of offset did not exist. The Company had no outstanding securities lending arrangements as of June 30, 2013 or December 31, 2012. See Note 5 for information related to the Company's offsetting of derivative contracts.

Note 10 Other Assets

Other assets include net deferred income tax assets, proprietary investments, income tax receivables and prepaid expenses. The Company's investments include investments in private companies and partnerships, warrants of public and private companies and private company debt. Other assets included:

(Dollars in thousands)	June 30, 2013	December 31, 2012
Net deferred income tax assets	$22,051	$33,622
Investments at fair value	59,992	39,055
Investments at cost	25,464	26,364
Investments accounted for under the equity method	20,253	20,353
Income tax receivables	11,867	5,448
Prepaid expenses	3,947	3,840
Other	955	1,015
Total other assets	$144,529	$129,697

Management regularly reviews the Company's investments in private company debt and has concluded that no valuation allowance is needed as it is probable that all contractual principal and interest will be collected.

At June 30, 2013, investments carried on a cost basis had an estimated fair market value of $43.4 million. The estimated fair value of these investments was measured using discounted cash flow models that utilize market data for comparable companies (e.g., multiples of revenue and earnings before interest, taxes, depreciation and amortization ("EBITDA")). Because valuation adjustments, based upon management's judgment, were made to account for differences between the measured security and comparable securities, investments carried at cost would be categorized as Level III assets in the fair value hierarchy, if they were carried at fair value.

Investments accounted for under the equity method include general and limited partnership interests. The carrying value of these investments is based on the investment vehicle's net asset value. The net assets of investment partnerships consist of investments in both marketable and non-marketable securities. The underlying investments held by such partnerships are valued based on the estimated fair value ultimately determined by management in our capacity as general partner or investor and, in the case of investments in unaffiliated investment partnerships, are based on financial statements prepared by the unaffiliated general partners.

Note 11 Goodwill and Intangible Assets

The following table presents the changes in the carrying value of goodwill and intangible assets from continuing operations for the six months ended June 30, 2013:

(Dollars in thousands)	Asset Management
Goodwill	
Balance at December 31, 2012	$196,844
Goodwill acquired	—
Impairment charge	—
Balance at June 30, 2013	$196,844

Intangible assets	
Balance at December 31, 2012	$41,258
Amortization of intangible assets	(3,322)
Balance at June 30, 2013	$37,936

Note 12 Short-Term Financing

The following is a summary of short-term financing and the weighted average interest rate on borrowings:

	Outstanding Balance		Weighted Average Interest Rate	
(Dollars in thousands)	June 30, 2013	December 31, 2012	June 30, 2013	December 31, 2012
Commercial paper (secured)	$348,915	$304,439	1.58%	1.65%
Prime broker arrangement	141,893	172,575	0.94%	0.98%
Bank lines (secured)	52,000	—	1.50%	N/A
Total short-term financing	$542,808	$477,014		

The Company issues secured commercial paper to fund a portion of its securities inventory. The secured commercial paper notes (“CP Notes”) can be issued with maturities of 27 days to 270 days from the date of issuance. The CP Notes are issued under three separate programs, CP Series A, CP Series II A and CP Series III A, and are secured by different inventory classes. As of June 30, 2013, the weighted average maturity of CP Series A, CP Series II A and CP Series III A was 128 days , 104 days and 33 days , respectively. The CP Notes are interest bearing or sold at a discount to par with an interest rate based on LIBOR plus an applicable margin.

The Company has established an arrangement to obtain financing with a prime broker related to its municipal bond funds. Financing under this arrangement is secured by certain securities, primarily municipal securities, and collateral limitations could reduce the amount of funding available under this arrangement. The funding is at the discretion of the prime broker.

The Company has committed short-term bank line financing available on a secured basis and uncommitted short-term bank line financing available on both a secured and unsecured basis. The Company uses these credit facilities in the ordinary course of business to fund a portion of its daily operations and the amount borrowed under these credit facilities varies daily based on the Company’s funding needs.

The Company’s committed short-term bank line financing at June 30, 2013 consisted of a one-year $250 million committed revolving credit facility with U.S. Bank, N.A., which was renewed in December 2012. Advances under this facility are secured by certain marketable securities. The facility includes a covenant that requires the Company’s U.S. broker dealer subsidiary to maintain a minimum net capital of $120 million, and the unpaid principal amount of all advances under this facility will be due on December 28, 2013. The Company pays a nonrefundable commitment fee on the unused portion of the facility on a quarterly basis. At June 30, 2013, the Company had no advances against this line of credit.

The Company’s uncommitted secured lines at June 30, 2013 totaled $175 million with two banks and are dependent on having appropriate collateral, as determined by the bank agreement, to secure an advance under the line. The availability of the Company’s uncommitted lines are subject to approval by the individual banks each time an advance is requested and may be denied. At June 30, 2013, the Company had $52.0 million in advances against these lines of credit.

Note 13 Variable Rate Senior Notes

On November 30, 2012, the Company entered into a note purchase agreement (“Note Purchase Agreement”) under which the Company issued unsecured variable rate senior notes (“Notes”) in the amount of $125 million. The initial holders of the Notes are certain entities advised by PIMCO. The Notes consist of two classes, Class A Notes and Class B Notes, with principal amounts of $50 million and $75 million, respectively. The Class A Notes bear interest at a rate equal to three-month LIBOR plus 4.00 percent and mature on May 31, 2014. The Class B Notes bear interest at a rate equal to three-month LIBOR plus 4.50 percent and mature on November 30, 2015. Interest on the Notes is adjustable and payable quarterly. The unpaid principal amounts are due in full on the respective maturity dates and are not subject to prepayment at the Company's discretion. The proceeds from the Notes were used to repay the outstanding balance under the bank syndicated credit agreement (“Credit Agreement”) discussed in Note 14. The remaining proceeds are being used for general corporate purposes.

The Note Purchase Agreement includes customary events of default, including failure to pay principal when due or failure to pay interest within five business days of when due, any representation or warranty in the Note Purchase Agreement proving untrue in any material respect when made by the Company, failure to comply with the covenants in the Note Purchase Agreement, failure to pay or another event of default under other material indebtedness in an amount exceeding $10 million, bankruptcy or insolvency

of the Company or any of its subsidiaries or a change in control of the Company. If there is any event of default under the Note Purchase Agreement, the noteholders may declare the entire principal and any accrued interest on the Notes to be due and payable and exercise other customary remedies.

The Note Purchase Agreement includes covenants that, among other things, require the Company to maintain a minimum consolidated tangible net worth and regulatory net capital, limit the Company's leverage ratio and require the Company to maintain a minimum ratio of operating cash flow to fixed charges. With respect to the net capital covenant, the Company's U.S. broker dealer subsidiary is required to maintain minimum net capital of $120 million. At June 30, 2013, the Company was in compliance with all covenants.

The Notes are recorded at amortized cost. As of June 30, 2013, the carrying value of the Notes approximates fair value.

Note 14 Bank Syndicated Financing

On December 29, 2010, the Company entered into a three-year Credit Agreement comprised of a $100 million amortizing term loan and a $50 million revolving credit facility. SunTrust Bank was the administrative agent (“Agent”) for the lenders. The interest rate for borrowing under the Credit Agreement was, at the option of the Company, equal to LIBOR or a base rate, plus an applicable margin, adjustable and payable quarterly at a minimum. The base rate was defined as the highest of the Agent’s prime lending rate, the Federal Funds Rate plus 0.50 percent or one-month LIBOR plus 1.00 percent. The applicable margin varied from 1.50 percent to 3.00 percent and was based on the Company’s leverage ratio. In addition, the Company also paid a nonrefundable commitment fee of 0.50 percent on the unused portion of the revolving credit facility on a quarterly basis. The outstanding balance and unpaid interest on the Credit Agreement was repaid on November 30, 2012 from the proceeds of the Notes discussed in Note 13.

Note 15 Legal Contingencies

The Company has been named as a defendant in various legal actions, including complaints and litigation and arbitration claims, arising from its business activities. Such actions include claims related to securities brokerage and investment banking activities, and certain class actions that primarily allege violations of securities laws and seek unspecified damages, which could be substantial. Also, the Company is involved from time to time in investigations and proceedings by governmental agencies and self-regulatory organizations (“SROs”) which could result in adverse judgments, settlement, penalties, fines or other relief.

The Company has established reserves for potential losses that are probable and reasonably estimable that may result from pending and potential legal actions, investigations and regulatory proceedings. In many cases, however, it is inherently difficult to determine whether any loss is probable or even possible or to estimate the amount or range of any potential loss, particularly where proceedings may be in relatively early stages or where plaintiffs are seeking substantial or indeterminate damages. Matters frequently need to be more developed before a loss or range of loss can reasonably be estimated.

Given uncertainties regarding the timing, scope, volume and outcome of pending and potential legal actions, investigations and regulatory proceedings and other factors, the amounts of reserves and ranges of reasonably possible losses are difficult to determine and of necessity subject to future revision. Subject to the foregoing and except for the legal proceeding described below, as to which management believes a material loss is reasonably possible,

management of the Company believes, based on currently available information, after consultation with outside legal counsel and taking into account its established reserves, that pending legal actions, investigations and regulatory proceedings will be resolved with no material adverse effect on the consolidated statements of financial condition, results of operations or cash flows of the Company. However, if during any period a potential adverse contingency should become probable or resolved for an amount in excess of the established reserves, the results of operations and cash flows in that period and the financial condition as of the end of that period could be materially adversely affected. In addition, there can be no assurance that material losses will not be incurred from claims that have not yet been brought to the Company's attention or are not yet determined to be reasonably possible.

The Company has a contingency as to which management of the Company believes that a material loss is reasonably possible. The U.S. Department of Justice Antitrust Division, the SEC and various state attorneys general are conducting broad investigations of numerous firms, including the Company, for possible antitrust and securities violations in connection with the bidding or sale of guaranteed investment contracts and derivatives to municipal issuers from the early 1990s to date. These investigations commenced in November 2006. In addition, several class action complaints were brought on behalf of a proposed class of government entities that purchased municipal derivatives. The complaints, which have been consolidated into a single class action,

allege antitrust violations and are pending in the U.S. District Court for the Southern District of New York under the multi-district litigation rules. Several California municipalities also brought separate class action complaints in California federal court, and approximately 18 California municipalities and two New York municipalities filed individual lawsuits that are not part of class actions, all of which have been transferred to the Southern District of New York and consolidated for pretrial purposes. No loss contingency has been reflected in the Company's consolidated financial statements as this contingency is neither probable nor reasonably estimable at this time. Management is currently unable to estimate a range of reasonably possible loss for these matters because alleged damages have not been specified, the proceedings remain in the early stages, there is uncertainty as to the likelihood of a class or classes being certified or the ultimate size of any class if certified, and there are significant factual issues to be resolved.

Note 16 Restructuring

In the second quarter of 2012, the Company implemented certain expense reduction measures to better align its cost infrastructure with its revenues. For the three months ended June 30, 2012, the Company incurred a pre-tax restructuring-related charge of $3.6 million from continuing operations. The charge resulted from severance benefits of $2.4 million and from the reduction of leased office space of $1.2 million.

Note 17 Shareholders' Equity

Share Repurchases

In the third quarter of 2012, the Company's board of directors authorized the repurchase of up to $100.0 million in common shares through September 30, 2014. This share repurchase authorization became effective on October 1, 2012. During the six months ended June 30, 2013, the Company repurchased 797,673 shares of the Company's common stock at an average price of $32.23 per share for an aggregate purchase price of $25.7 million related to this authorization. The Company has $69.7 million remaining under this authorization. The Company also purchases shares of common stock from restricted stock award recipients upon the award vesting as recipients sell shares to meet their employment tax obligations. The Company purchased 364,952 shares or $14.8 million of the Company's common stock for this purpose during the six months ended June 30, 2013.

Issuance of Shares

During the six months ended June 30, 2013, the Company issued 96,049 common shares out of treasury stock in fulfillment of $3.9 million in obligations under the Piper Jaffray Companies Retirement Plan (the "Retirement Plan") and issued 741,972 common shares out of treasury stock as a result of employee vesting and exercise transactions. During the six months ended June 30, 2012, the Company issued 165,241 common shares out of treasury stock in fulfillment of $3.8 million in obligations under the Retirement Plan and issued 768,251 common shares out of treasury stock as a result of employee vesting.

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

Note 18 Noncontrolling Interests

The consolidated financial statements include the accounts of Piper Jaffray Companies, its wholly owned subsidiaries and other entities in which the Company has a controlling financial interest. Noncontrolling interests represent equity interests in consolidated entities that are not attributable, either directly or indirectly, to Piper Jaffray Companies. Noncontrolling interests include the minority equity holders’ proportionate share of the equity in a municipal bond fund of $116.0 million, a merchant banking fund of $13.3 million and private equity investment vehicles aggregating $8.7 million as of June 30, 2013. As of December 31, 2012, noncontrolling interests included the minority equity holders’ proportionate share of the equity in a municipal bond fund of $43.7 million, a merchant banking fund of $6.4 million and private equity investment vehicles aggregating $6.8 million.

Ownership interests in entities held by parties other than the Company’s common shareholders are presented as noncontrolling interests within shareholders’ equity, separate from the Company’s own equity. Revenues, expenses and net income or loss are reported on the consolidated statements of operations on a consolidated basis, which includes amounts attributable to both the Company’s common shareholders and noncontrolling interests. Net income or loss is then allocated between the Company and noncontrolling interests based upon their relative ownership interests. Net income applicable to noncontrolling interests is deducted from consolidated net income to determine net income applicable to the Company.

(Dollars in thousands)	Common Shareholders’ Equity	Noncontrolling Interests	Total Shareholders’ Equity
Balance at December 31, 2012	$733,292	$56,883	$790,175
Net income/(loss)	12,634	(769)	11,865
Amortization/issuance of restricted stock	20,572	—	20,572
Repurchase of common stock through share repurchase program	(25,708)	—	(25,708)
Repurchase of common stock for employee tax withholding	(14,788)	—	(14,788)
Issuance of treasury shares for 401k match	3,939	—	3,939
Shares reserved to meet deferred compensation obligations	60	—	60
Other comprehensive loss	(121)	—	(121)
Fund capital contributions, net	—	81,868	81,868
Balance at June 30, 2013	$729,880	$137,982	$867,862

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

Note 19 Compensation Plans

Stock-Based Compensation Plans

The Company maintains two stock-based compensation plans, the Piper Jaffray Companies Amended and Restated 2003 Annual and Long-Term Incentive Plan (the "Incentive Plan") and the 2010 Employment Inducement Award Plan (the "Inducement Plan"). The Company's equity awards are recognized on the consolidated statements of operations at grant date fair value over the service period of the award, net of estimated forfeitures.

The following table provides a summary of the Company's outstanding equity awards (in shares or units) as of June 30, 2013:

Incentive Plan	
Restricted Stock Shares	
Annual grants	888,530
Sign-on grants	246,989
Retention grants	—
Performance grants	—
	1,135,519
Inducement Plan	
Restricted Stock Shares	58,310
Total restricted stock shares related to compensation	1,193,829
ARI deal consideration (1)	220,456
Total restricted stock shares outstanding	1,414,285
Incentive Plan	
Restricted Stock Units	
Leadership grants	290,536
Incentive Plan	
Stock options outstanding	474,682

(1) The Company issued restricted stock as part of deal consideration in conjunction with the acquisition of ARI.

Incentive Plan

The Incentive Plan permits the grant of equity awards, including restricted stock, restricted stock units and non-qualified stock options, to the Company's employees and directors for up to 7.0 million shares of common stock (1.3 million shares remained available for future issuance under the Incentive Plan as of June 30, 2013). The Company believes that such awards help align the interests of employees and directors with those of shareholders and serve as an employee retention tool. The Incentive Plan provides for accelerated vesting of awards if there is a severance event, a change in control of the Company (as defined in the Incentive Plan), in the event of a participant's death, and at the discretion of the compensation committee of the Company's board of directors.

Restricted Stock Awards

Restricted stock grants are valued at the market price of the Company’s common stock on the date of grant and are amortized over the related requisite service period. The Company grants shares of restricted stock to current employees as part of year-end compensation (“Annual Grants”) and as a retention tool. Employees may receive restricted stock upon initial hiring or as a retention award (“Sign-on Grants”). The Company has also granted incremental restricted stock awards with service conditions to key employees (“Retention Grants”) and restricted stock with performance conditions to members of senior management ("Performance Grants").

The Company’s Annual Grants are made each year in February. Prior to 2011, Annual Grants had three-year cliff vesting periods. Beginning in 2011, Annual Grants vest ratably over three years in equal installments. The Annual Grants provide for continued vesting after termination of employment, so long as the employee does not violate certain post-termination restrictions set forth

in the award agreement or any agreements entered into upon termination. The Company determined the service inception date precedes the grant date for the Annual Grants, and that the post-termination restrictions do not meet the criteria for an in-substance service condition, as defined by FASB Accounting Standards Codification Topic 718, "Compensation – Stock Compensation" ("ASC 718"). Accordingly, restricted stock granted as part of the Annual Grants is expensed in the one-year period in which those awards are deemed to be earned, which is generally the calendar year preceding the February grant date. For example, the Company recognized compensation expense during fiscal 2012 for its February 2013 Annual Grant. If an equity award related to the Annual Grants is forfeited as a result of violating the post-termination restrictions, the lower of the fair value of the award at grant date or the fair value of the award at the date of forfeiture is recorded within the consolidated statements of operations as a reversal of compensation expense. The Company recorded $0.4 million of forfeitures through compensation and benefits expense within continuing operations for the three months ended June 30, 2013 and 2012, and $0.7 million and $1.2 million for the six months ended June 30, 2013 and 2012, respectively.

Sign-on Grants are used as a recruiting tool for new employees and are issued to current employees as a retention tool. The majority of these awards have three-year cliff vesting terms and employees must fulfill service requirements in exchange for rights to the awards. Compensation expense is amortized on a straight-line basis from the grant date over the requisite service period. Employees forfeit unvested shares upon termination of employment and a reversal of compensation expense is recorded.

Retention Grants were subject to ratable vesting based upon a five-year service requirement and were amortized as compensation expense on a straight-line basis from the 2008 grant date over the requisite service period, which ended in May 2013. Employees forfeited unvested retention shares upon termination of employment and a reversal of compensation expense was recorded.

Performance Grants awarded in 2008 and 2009 expired unvested in May 2013.

Annually, the Company grants stock to its non-employee directors. The stock-based compensation paid to non-employee directors is fully expensed on the grant date and included within outside services expense on the consolidated statements of operations.

Restricted Stock Units

The Company granted restricted stock units to its leadership team (“Leadership Grants”) in May 2012 and 2013, respectively. The units will vest and convert to shares of common stock at the end of each 36-month performance period only if the Company satisfies predetermined market conditions over the performance period. Under the terms of the grants, the number of units that will vest and convert to shares will be based on the Company achieving specified market conditions during each performance period as described below. Compensation expense is amortized on a straight-line basis over the three-year requisite service period based on the fair value of the award on the grant date. The market condition must be met for the awards to vest and compensation cost will be recognized regardless if the market condition is satisfied. Employees forfeit unvested share units upon termination of employment with a corresponding reversal of compensation expense.

Up to 50 percent of the award can be earned based on the Company’s total shareholder return relative to members of a predetermined peer group and up to 50 percent of the award can be earned based on the Company’s total shareholder return. The fair value of the awards on the grant date were determined using a Monte Carlo simulation with the

following assumptions:

Grant Year	Risk-free Interest Rate	Expected Stock Price Volatility
2013	0.40%	44.0%
2012	0.38%	47.6%

Because a portion of the award vesting depends on the Company's total shareholder return relative to a peer group, the valuation modeled the performance of the peer group as well as the correlation between the Company and the peer group. The expected stock price volatility assumptions were determined using historical volatility as correlation coefficients can only be developed through historical volatility. The risk-free interest rates were determined based on three-year U.S. Treasury bond yields.

Stock Options

The Company previously granted options to purchase Piper Jaffray Companies common stock to employees and non-employee directors in fiscal years 2004 through 2008. Employee and director options were expensed by the Company on a straight-line basis over the required service period, based on the estimated fair value of the award on the date of grant using a Black-Scholes option-pricing model. As described above pertaining to the Company's Annual Grants of restricted shares, stock options granted to employees were expensed in the calendar year preceding the annual February grant date. For example, the Company recognized compensation expense during fiscal 2007 for its February 2008 option grant. The maximum term of the stock options granted to employees and directors is ten years. The Company has not granted stock options since 2008.

Inducement Plan

In 2010, the Company established the Inducement Plan in conjunction with the acquisition of ARI. The Company granted $7.0 million in restricted stock (158,801 shares) under the Inducement Plan to ARI employees upon closing of the transaction. These shares vest ratably over five years in equal annual installments ending on March 1, 2015. Inducement Plan awards are amortized as compensation expense on a straight-line basis over the vesting period. Employees forfeit unvested Inducement Plan shares upon termination of employment and a reversal of compensation expense is recorded.

Stock-Based Compensation Activity

The Company recorded total compensation expense within continuing operations of $4.2 million and $5.5 million for the three months ended June 30, 2013 and 2012, respectively, and $5.1 million and $6.3 million for the six months ended June 30, 2013 and 2012, respectively, related to employee restricted stock and restricted stock unit awards. Total compensation cost includes year-end compensation for Annual Grants and the amortization of Sign-on, Retention and Leadership Grants, less forfeitures. The tax benefit related to stock-based compensation costs totaled $1.6 million and $2.1 million for the three months ended June 30, 2013 and 2012, respectively, and $2.0 million and $2.5 million for the six months ended June 30, 2013 and 2012, respectively.

The following table summarizes the changes in the Company's unvested restricted stock (including the unvested restricted stock issued as part of the deal consideration for ARI) under the Incentive Plan and Inducement Plan for the six months ended June 30, 2013:

	Unvested Restricted Stock (in Shares)	Weighted Average Grant Date Fair Value
December 31, 2012	2,322,438	$37.01
Granted	438,411	41.01
Vested	(1,099,548)	40.35
Cancelled	(247,016)	37.77
June 30, 2013	1,414,285	$35.35

The following summarizes the changes in the Company's unvested restricted stock units under the Incentive Plan for the six months ended June 30, 2013:

	Unvested	Weighted Average

	Restricted Stock Units	Grant Date Fair Value
December 31, 2012	173,271	$12.12
Granted	117,265	21.32
Vested	—	—
Cancelled	—	—
June 30, 2013	290,536	$15.83

As of June 30, 2013, there was $8.5 million of total unrecognized compensation cost related to restricted stock and restricted stock units expected to be recognized over a weighted average period of 1.96 years.

The following table summarizes the changes in the Company’s outstanding stock options for the six months ended June 30, 2013:

	Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in Years)	Aggregate Intrinsic Value
December 31, 2012	486,563	$ 44.76	2.9	$94,150
Granted	—	—		
Exercised	—	—		
Cancelled	(11,881)	42.99		
June 30, 2013	474,682	$ 44.80	2.4	$82,267
Options exercisable at June 30, 2013	474,682	$ 44.80	2.4	$82,267

As of June 30, 2013, there was no unrecognized compensation cost related to stock options expected to be recognized over future years.

The fair value of options exercised, cash received from option exercises and the resulting tax benefit realized for the tax deductions from option exercises were immaterial for the six months ended June 30, 2013 and 2012, respectively.

Deferred Compensation Plan

In 2012, the Company established the Piper Jaffray Companies Mutual Fund Restricted Share Investment Plan, a deferred compensation plan which allows eligible employees to elect to receive a portion of the incentive compensation they would otherwise receive in the form of restricted stock or other equity, instead in restricted mutual fund shares (“MFRS Awards”) of registered funds managed by the Company's asset management business. MFRS Awards are awarded to qualifying employees in February of each year, and represent a portion of their compensation for performance in the preceding year similar to the Company's Annual Grants. MFRS Awards vest ratably over three years in equal installments and provide for continued vesting after termination of employment so long as the employee does not violate certain post-termination restrictions set forth in the award agreement or any agreement entered into upon termination. Forfeitures are recorded as a reduction of compensation and benefits expense within the consolidated statements of operations.

Note 20 Earnings Per Share

The Company calculates earnings per share using the two-class method. Basic earnings per common share is computed by dividing net income applicable to Piper Jaffray Companies' common shareholders by the weighted average number of common shares outstanding for the period. Net income applicable to Piper Jaffray Companies' common shareholders represents net income applicable to Piper Jaffray Companies reduced by the allocation of earnings to participating securities. Losses are not allocated to participating securities. All of the Company's unvested restricted shares are deemed to be participating securities as they are eligible to share in the profits (e.g., receive dividends) of the Company. The Company's unvested restricted stock units are not participating securities as they are not eligible to share in the profits of the Company. Diluted earnings per common share is calculated by adjusting the weighted average outstanding shares to assume conversion of all potentially dilutive stock options. The computation of earnings per share is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Amounts in thousands, except per share data)	2013	2012	2013	2012
Net income from continuing operations applicable to Piper Jaffray Companies	$4,359	$10,785	$15,026	$17,017
Net loss from discontinued operations	(1,871)	(3,934)	(2,392)	(7,237)
Net income applicable to Piper Jaffray Companies	2,488	6,851	12,634	9,780
Earnings allocated to participating securities (1)	(222)	(961)	(1,301)	(1,436)
Net income applicable to Piper Jaffray Companies' common shareholders (2)	$2,266	$5,890	$11,333	$8,344
Shares for basic and diluted calculations:				
Average shares used in basic computation	15,621	15,932	15,602	16,002
Stock options	5	—	17	—
Average shares used in diluted computation	15,626	15,932	15,619	16,002
Earnings/(loss) per basic common share:				
Income from continuing operations	$0.25	$0.58	$0.86	$0.91
Loss from discontinued operations	(0.11)	(0.21)	(0.14)	(0.39)
Earnings per basic common share	$0.15	$0.37	$0.73	$0.52
Earnings/(loss) per diluted common share:				
Income from continuing operations	$0.25	$0.58	$0.86	$0.91
Loss from discontinued operations	(0.11)	(0.21)	(0.14)	(0.39)
Earnings per diluted common share	$0.15	$0.37	$0.73	$0.52

(1) Represents the allocation of earnings to participating securities. Losses are not allocated to participating securities. Participating securities include all of the Company's unvested restricted shares. The weighted average participating shares outstanding were 1,531,100 and 2,598,556 for the three months ended June 30, 2013 and 2012, respectively, and 1,791,940 and 2,754,682 for the six months ended June 30, 2013 and 2012, respectively.

(2) Net income applicable to Piper Jaffray Companies' common shareholders for diluted and basic EPS may differ under the two-class method as a result of adding the effect of the assumed exercise of stock options to dilutive shares outstanding, which alters the ratio used to allocate earnings to Piper Jaffray Companies' common shareholders and participating securities for purposes of calculating diluted and basic EPS.

The anti-dilutive effects from stock options were immaterial for the six months ended June 30, 2013 and 2012.

Note 21 Segment Reporting

Basis for Presentation

The Company structures its segments primarily based upon the nature of the financial products and services provided to customers and the Company's management organization. The Company evaluates performance and allocates resources based on segment pre-tax operating income or loss and segment pre-tax operating margin. Revenues and expenses directly associated with each respective segment are included in determining their operating results. Other revenues and expenses that are not directly attributable to a particular segment are allocated based upon the Company's allocation methodologies, including each segment's respective net revenues, use of shared resources, headcount or other relevant measures. The financial management of assets is performed on an enterprise-wide basis. As such, assets are not assigned to the business segments.

Table of Contents
Piper Jaffray Companies
Notes to the Consolidated Financial Statements
(Unaudited)

Segment pre-tax operating income/(loss) and segment pre-tax operating margin exclude the results of discontinued operations.

Reportable segment financial results from continuing operations are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2013	2012	2013	2012
Capital Markets				
Investment banking				
Financing				
Equities	$21,772	$13,132	$36,075	$36,360
Debt	22,131	22,256	39,163	37,025
Advisory services	9,409	14,631	18,965	25,353
Total investment banking	53,312	50,019	94,203	98,738
Institutional sales and trading				
Equities	21,392	16,682	42,127	37,662
Fixed income	4,959	20,620	33,002	49,083
Total institutional sales and trading	26,351	37,302	75,129	86,745
Other income/(loss)	2,146	265	3,686	(1,102)
Net revenues	81,809	87,586	173,018	184,381
Operating expenses	83,937	85,803	162,395	171,858
Segment pre-tax operating income/(loss)	$(2,128)	$1,783		