

Piper Jaffray Ltd

Pillar 3 Disclosure

As at 31<sup>st</sup> December 2009

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## **Pillar 3 Disclosure – Piper Jaffray Ltd**

### **Introduction**

The Capital Requirements Directive (“the Directive”) of the European Union establishes a regulatory capital framework across Europe governing the amount and nature of capital that must be maintained by credit institutions and investment firms. In the United Kingdom, the Directive has been implemented by the Financial Services Authority (FSA) in its regulations through the General Prudential Sourcebook (GENPRU) and the Prudential Sourcebook for Banks, Building Societies and Investment Firms (BIPRU).

The FSA framework consists of three ‘Pillars’:

1. Pillar 1 sets out the minimum capital amounts that meets the firm’s credit, market and operational risks;
2. Pillar 2 requires the firm to assess whether its Pillar 1 capital is adequate to meet its risks and is subject to annual review by the FSA; and
3. Pillar 3 requires disclosure of specified information about the underlying risk management, controls and capital position.

The rules in BIPRU 11 set out the provision for Pillar 3 disclosure. This document is designed to meet our Pillar 3 obligations. We are permitted to omit required disclosures if we believe that the information is immaterial such that omission would be unlikely to change or influence the decision of the reader relying on the information. In addition, we may omit required disclosures where we believe that the information is regarded as proprietary or confidential. In our view, proprietary information is that which, if it were shared, would undermine our competitive position. Information is considered to be confidential where there are obligations binding us to confidentiality with our customers, suppliers and counterparties.

We have made no omissions on the grounds that it is immaterial, proprietary or confidential.

### ***Frequency***

The company intends to publish Pillar 3 disclosures at least annually in accordance with FSA requirements

### ***Media and location***

The company’s Pillar 3 disclosures will be available on the company’s website [www.pjc.com/europe/](http://www.pjc.com/europe/).

## **Scope and application of the requirements**

Piper Jaffray Ltd (PJL) is authorised and regulated by the FSA and as such subject to minimum regulatory capital requirements. The company is categorised as a BIPRU full scope 730k firm.

The company's principal activity is providing securities brokerage and investment banking services. It makes markets in UK domestic securities, provides research coverage of UK and European domestic securities in support of its institutional sales activities and also provides a full range of investment banking services, including underwriting, to its corporate clients.

## **Risk Management**

The company is governed by its directors ('the Directors') who determine its business strategy and risk appetite. They are also responsible for establishing and maintaining the company's governance arrangements along with designing and implementing a risk management framework that recognises the risks that the business faces.

The Directors also determine how risks the company faces can be mitigated and assesses the arrangements to manage those risks on an on-going basis. The Directors meet both formally and informally on a regular basis to discuss current projections for profitability, cash flow, regulatory capital, business planning and risk management. The Directors manage the business and identify risks through a framework of policy and procedures taking account of risk appetite and relevant laws, rules and regulations. These policies and procedures are update as required.

The Directors have identified that, operational, market and credit risk are the main areas of risk to which the company is exposed. The Directors formally review their risks, controls and other risk mitigation arrangements and assess their effectiveness. Where material risk is identified the Directors consider the financial impact of such risk to the business and ensure that business planning and capital management recognise the significance of the risk and ensure that the level of regulatory capital is sufficient to cover such risk.

### ***Market risk***

Market risk represents the risk of financial volatility that may result from the change in value of a financial instrument due to fluctuations in its market price. The company's exposure to market risk is directly related to its role as a financial intermediary for its clients and to its market-making activities. The scope of the company's market risk management policies and procedures includes all market-sensitive financial instruments.

Market risk includes equity price risk which represents the potential loss in value due to adverse changes in the level or volatility of equity prices. The company attempts to reduce the risk of loss inherent in its market-making and in its inventory of equity securities by establishing limits on the notional level of its inventory and by managing net position levels with those limits.

Market risk can be exacerbated in times of trading illiquidity when market participants refrain from transacting in normal quantities and/or at normal bid-offer spreads. Depending on the specific security, the structure of the financial product, and/or overall market conditions, the company may be forced to hold onto a security for days or weeks longer than it had planned.

Market risk also includes currency risk which arises from the possibility that fluctuations in foreign exchange rates will impact the value of financial instruments. A portion of the company's business is conducted in currencies other than sterling, and changes in foreign exchange rates relative to sterling can therefore affect the value of non-sterling net assets, revenues and expenses. A change in the foreign currency rates creates a foreign currency transaction gain/loss recorded in the company's profit and loss account. Foreign exchange risk is mitigated by hedging strategies which reduce the impact of foreign exchange movements on balance sheet valuations and profit and loss. In addition, significant foreign exchange cash balances are sold into sterling where the retention of such balances has no business purpose or would increase foreign exchange risk.

***Credit risk***

Credit risk in the company's business arises from potential non-performance by counterparties and customers. The company is exposed to credit risk in its role as a trading counterparty to dealers and customers. The company's credit exposure to market counterparties is mitigated by those transactions which are traded electronically and taken on by the London Clearing House.

The company is subject to credit concentration risk if it holds large individual securities positions, executes large transactions with individual counterparties or groups of related counterparties, or makes substantial underwriting commitments. Concentration risk can occur by industry, geographic area or type of client. Potential credit concentration risk is carefully monitored by management and the Risk Management Department.

***Operational risk***

Operational risk refers to the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events. The company relies on the ability of its employees, its internal systems and processes and systems at computer centres operated by third parties to process transactions. In the event of a breakdown or improper operation of the company's systems or processes or improper action by its employees or third-party vendors, the company could suffer financial loss, regulatory sanctions and damage to its reputation. The company has business continuity plans in place that it believes will cover critical processes on a company-wide basis, and redundancies are built into our systems as deemed appropriate. These control mechanisms attempt to ensure that operations policies and procedures are being followed and that our various businesses are operating within established corporate policies and limits.

***Liquidity risk***

Normal activity could be affected should the company be short of liquid funds. The risk is reduced by the presence of third party banking facilities and the maintenance of a liquid asset buffer.

***Legal, regulatory and compliance risk***

Legal, regulatory and compliance risk includes the risk of non-compliance with applicable legal and regulatory requirements and the risk that a counterparty's performance obligations will be unenforceable.

The company has established internal policies relating to ethics and business conduct, and compliance with applicable legal and regulatory requirements, as well as training and other procedures designed to ensure that these policies are followed.

## Capital

### *Regulatory capital*

The company's capital position as at 31<sup>st</sup> December 2008 is summarised as follows:

<b>Capital item</b>	<b>£ '000</b>
Core tier 1 capital	10,000
Total tier 2 capital	0
<b>Total capital</b>	<b>10,000</b>
Total variable capital requirement	2,930
<b>Capital Surplus</b>	<b>7,070</b>

### *Internal assessment of capital adequacy*

Piper Jaffray Ltd defines capital as the resources necessary to cover unexpected losses arising from discretionary risks, being those which it accepts such as market risk and credit risk, or non-discretionary, being those which arise by virtue of its operations, such as operational risk and reputational risk. The Internal Capital Adequacy Assessment Process by which the Directors examine the company's risk profile from both regulatory and economic capital perspectives and ensures the level of capital:

- remains sufficient to support the company's risk profile and outstanding commitments;
- exceeds the company's formal minimum regulatory capital requirements;
- is capable of withstanding a severe economic downturn stress scenario; and
- remains consistent with the company's strategic and operational goals.